

April 29, 2014

The Honorable Sean Parnell  
Governor  
State of Alaska  
P.O. Box 110001  
Juneau, Alaska 99811-0001

Re: HCS CSSB 138 (FIN) am H -- relating to  
gas pipeline, the Alaska Gasline  
Development Corporation, and the oil and  
gas production tax  
Our file: JU2014200362

Dear Governor Parnell:

At the request of your legislative director, we have reviewed HCS CSSB 138 (FIN) am H, relating to gas pipeline, the Alaska Gasline Development Corporation, and the oil and gas production tax.

The comprehensive bill would make changes to state law necessary to progress commercialization of Alaska's North Slope natural gas for the maximum benefit of the people of the state through delivery of natural gas in-state and to export markets. Through changes to the statutes related to the Alaska Gasline Development Corporation (AGDC), the Department of Natural Resources (DNR) and the Department of Revenue (DOR), the bill would establish a path for state participation in the development of North Slope natural gas through the state's royalty share of natural gas and gas subject to the oil and gas production tax, authorize the DNR to enter into project related contracts and lease modifications, provide for legislative consideration and approval of certain project contracts and public review of the same, and provide for state infrastructure and energy needs. The bill would add provisions to address the effects of commercialization of North Slope natural gas on municipalities, particularly those with oil and gas infrastructure within their jurisdiction. In addition, we have reviewed the letter of intent that accompanied the bill.

For organizational purposes, this review is arranged by topic rather than by bill section number. Our review of the bill's substantive provisions follows.

**I. Process for North Slope natural gas project agreements and contracts, lease modifications, and disposition of the state's royalty and tax gas.**

The bill would make changes to the Alaska Land Act (AS 38.05) provisions related to the

DNR commissioner's authority, oil and gas leasing provisions, and the sale of royalty.

To take the first steps necessary to enable state participation in a North Slope natural gas project, the DNR commissioner would be authorized (under proposed AS 38.05.020(b)(10)) to enter into commercial agreements of not more than two years for project services related to a North Slope natural gas project.<sup>1</sup> Project services mean services provided by a gas treatment plant, pipeline, liquefaction facility, marine terminal, marine transportation services, or other services necessary to transport natural gas to market.

Additionally, under proposed AS 38.05.020(b)(11), the DNR commissioner is authorized to negotiate agreements that include balancing, marketing, disposition of natural gas, offtake, and other contracts and agreements associated with a North Slope natural gas project, in consultation with the DOR commissioner. The legislature amended AS 38.05.020(b)(11) as introduced by the Administration, to include explicit direction that the agreements and contracts include balancing, marketing, disposition of natural gas, and offtake options related to a North Slope natural gas project. We believe that the more explicit direction is, however, consistent with the scope of agreements and contracts contemplated as necessary by the Administration. Under proposed AS 38.05.020(b)(13), the DNR commissioner may consult with the AGDC when developing agreements or contracts for specified project services.

In order to protect sensitive commercial information that must be considered in the negotiation of the agreements or contracts, proposed AS 38.05.020(b)(12) would allow the DNR commissioner to enter into confidentiality agreements related to the contract negotiations and implementation. Since information will be shared with the DOR commissioner, AS 40.25.100(a), related to disclosure of tax information, is amended to extend confidentiality provided for information under AS 38.05.020(b)(11). Legislators would be kept informed of the progress of negotiations through proposed AS 38.05.020(b)(12)(B), which would allow the DNR commissioner to share confidential information with legislators, their staff, and consultants. The amendments to AS 38.05.020 in sec. 24 of the bill would be effective immediately, if enacted into law.

With respect to negotiation of those agreements and contracts, proposed AS 38.05.023, (which would be effective January 1, 2015, if enacted into law) directs the DNR commissioner to ensure that terms in an agreement or contract negotiated under proposed AS 38.05.020(b)(11) would

- assure state access to data developed under the agreement if the state has directly participated financially in the contract and provide that access must be on the same or similar terms applicable to any other party in a North Slope natural gas project;

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<sup>1</sup> A North Slope natural gas project is defined in proposed AS 38.05.965(27) to mean a project to produce or transport natural gas from state oil or gas leases or gas only leases that include land north of 68 degrees North latitude in a gaseous state from the North Slope.

- not include a provision to change the property tax on property previously taxable under AS 43.56 (the oil and gas property and pipeline transportation property tax);
- provide a means for allocating infrastructure costs between the state and other parties in the project, considering project use and the state's share of participation in the project; and
- include principles based on commercially reasonable terms for delivering natural gas to public utilities in the state when utility demand for gas exceeds the amount of the state's royalty gas and natural gas delivered to the state as tax.

Some provisions of the bill are crafted to provide the legislature with a process to engage with the state in the development of the contracts and agreements to progress a North Slope natural gas project. In our view, the direction provided by the legislature in proposed AS 38.05.023 is aligned with the concept of legislative approval of the terms of contracts and agreements under proposed AS 38.05.020(b)(11) as included in the bill introduced by the Administration.

Under proposed AS 38.05.020(b)(11), the terms of a proposed contract that the DNR commissioner presents to the legislature must be made public at least 90 days before the proposed effective date for the terms and is not effective unless the legislature authorizes the governor to execute the agreement or contract. To the extent this provision may raise separation of powers questions under the Alaska Constitution, the Department of Law has previously advised that "the executive is free as a matter of comity to acquiesce in what amounts to the legislature's request for more active oversight."<sup>2</sup> Since the bill introduced by the Administration contained the provision for legislative approval, it is reasonable to conclude that the governor may choose in this instance to acquiesce to legislative review and approval. We believe this provision can reasonably be construed as not a violation of the separation of powers doctrine.

A core component of the bill relates to lease modifications. The bill proposes to give the DNR commissioner authority to modify leases, including modification of net profit share lease components, as set out in proposed AS 38.05.180(hh). The proposed new subsection would allow the DNR commissioner to propose (subject to making written determinations as discussed below) modifications to leases from which a lessee has committed gas from that lease to a North slope natural gas project; the modifications are to be in effect for the initial project term. The "initial project term" means the duration sufficient to support an investment decision by the sponsors of a North Slope natural gas project to permit realization of a competitive economic return, to enable necessary financing, and to support agreements for the sale of hydrocarbons transported on a North Slope natural gas project.<sup>3</sup>

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<sup>2</sup> 1998 Op. Alaska Att'y Gen. (May 29) 1999 WL 638618 (Alaska A.G.), reviewing SCS CSHB 393 (FIN), ch. 104, SLA 1998.

<sup>3</sup> Proposed AS 38.05.965(26).

The modifications under proposed AS 38.05.180(hh) would address the state's ability to switch between receiving royalty gas in value and royalty gas in-kind, provide a method to establish a fair market value for each component of the state's royalty gas, and establish fixed royalty rates in place of net profit shares for oil and gas and sliding scale royalty rates for gas. The legislature revised the third modification component (fixed royalty rates) to explicitly direct that any modification by the DNR commissioner must "yield a value to the state that the commissioner determines to be not less than the value the state would have received under the terms of the lease before a modification [.]"<sup>4</sup>

To approve a modification, the DNR commissioner must make a written determination, based on a clear and convincing showing by the lessee, that the modification is in the best interest of the state, that the project has a financial commitment for a work plan and sufficient commitment of gas, that the gas produced will be transported on a North Slope natural gas project, and that the lessee or an affiliate has offered to purchase, dispose of, or market the state's royalty in-kind gas and tax gas (proposed AS 43.55.014) on the same or substantially similar terms as the lessee or its affiliate sells, disposes of, or markets the lessee's gas. The provision would be effective January 1, 2015, if enacted into law.

Because this provision applies only to North Slope leases where the lessee has met certain conditions, the provision may implicate concern as an enactment of local or special legislation contrary to the Alaska Constitution. Special legislation is prohibited by art. II, sec. 19 of the Alaska Constitution that states: "The legislature shall pass no local or special act if a general act can be made applicable. Whether a general act can be made applicable shall be subject to judicial determination." We must first consider whether the proposed lease modification provision is of statewide application.<sup>5</sup> If the provision is not of statewide application, then we must consider whether the provision bears a "fair and substantial relationship" to legitimate purposes.<sup>6</sup> "Legislation need not operate evenly in all parts of the state to avoid being classified as local or special."<sup>7</sup> Legislation to encourage the development of state oil and gas resources has been considered a legitimate purpose.<sup>8</sup> Accordingly, since the lease modification provisions in the bill address an area of statewide concern – development of Alaska's North Slope natural gas through a gas pipeline and a liquefaction facility – and are fairly and substantially related to those goals, we believe that the bill would not be considered as local or special legislation.

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<sup>4</sup> Proposed AS 38.05.180(hh)(3). The modifications may be made only to *state* oil and gas and gas only leases. Since neither the DNR commissioner nor the legislature have oversight over the terms of federal or private leases, we see no basis for a lessee to challenge the application of this provision to state leases only.

<sup>5</sup> *Pebble Ltd. P'ship ex rel. Pebble Mines Corp. v. Parnell*, 215 P.3d 1064, 1078 (Alaska 2009).

<sup>6</sup> *Id.* at 1079.

<sup>7</sup> *Baxley v. State*, 958 P.2d 422, 430 (Alaska 1998) quoting *State v. Lewis*, 559 P.2d. 630, 643 (Alaska 1977).

<sup>8</sup> *Baxley*, 958 P.2d at 431.

Proposed AS 38.05.020(b)(14) would provide for the DNR commissioner to take custody of gas delivered to the state as payment of tax under proposed AS 43.55.014(b) and manage the project services and disposition and sale of that gas. Accordingly, amendments are proposed to AS 38.05.183, that the sale, exchange, or disposal of the state's mineral royalty share would include the sale, exchange, or disposal of gas delivered to the state under proposed AS 43.55.014 within the requirements of a competitive bid process, except that (consistent with current law), competitive bidding is not required if a determination is made that the best interest of the state does not require it, or no competition exists. Although the DNR commissioner would take custody of gas delivered to the state under proposed AS 43.55.014 for the purposes of sale, proposed AS 43.05.010(17) provides for the DOR commissioner to direct the disposition of revenue received from gas delivered to the state as payment of tax under proposed AS 43.55.014(b) and to enter into agreements with the DNR commissioner to manage the custody and disposition of that gas. As with other provisions that incorporate proposed AS 43.55.014, this section would be effective January 1, 2015, if enacted into law.

## **II. Provisions related to the Alaska Gasline Development Corporation.**

In 2013, the legislature made organizational and substantive changes to the AGDC, a public corporation and instrumentality of the state tasked to advance an in-state natural gas pipeline.<sup>9</sup> The bill would further amend the provisions of AS 31.25 to authorize the AGDC to participate in an Alaska liquefied natural gas project (AK LNG project) by acquiring an ownership or participation interest in an entity or joint venture that has an ownership interest in an AK LNG project, including gas treatment and liquefaction.<sup>10</sup> Although the bill provisions related to the AGDC differ somewhat from those in the bill proposed by the Administration, the end result appears consistent with statements made in the governor's transmittal letter accompanying the proposed legislation to expand the AGDC's purpose to include carrying the state's equity interest in the project's infrastructure, including treatment and liquefaction facilities, but not to impede the mission of the AGDC to advance an in-state natural gas pipeline.<sup>11</sup>

A number of provisions of the bill specifically relate to the AGDC's role in an AK LNG project.<sup>12</sup> Through proposed AS 31.25.005, the purpose of the AGDC, for the benefit of the state, would be expanded to include developing natural gas pipelines, including an AK LNG project to deliver gas in-state, provide economic benefits and revenue to the state through development of

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<sup>9</sup> Ch.11, SLA 2013, HB 4 (relating to the Alaska Gasline Development Corporation).

<sup>10</sup> If the state, through the AGDC or another state entity acquires an equity interest in the AK LNG project or an entity or joint venture that owns an equity interest in the project, the state will need to evaluate the federal tax implications of such a state entity receiving income from this investment. Final analysis of this issue will need to wait until the state has sufficient information to determine whether to acquire an equity interest. Generally, income earned by the state or an entity that is an integral part of the state is exempt from federal income tax under the doctrine of implied statutory immunity. *See* Rev. Rul. 87-2, 1987-1 C.B. 18 (1987).

<sup>11</sup> January 1, 2014, Senate Journal, page 1423 - 1426.

<sup>12</sup> An Alaska liquefied natural gas project is defined in proposed AS 31.25.390(7).

an AK LNG project and other transportation mechanisms. The AGDC is also tasked with assisting the DNR and DOR to maximize the value of the state's royalty natural gas, natural gas delivered to the state as payment of tax, or other natural gas received by the state. Specifically, the AGDC would be empowered to acquire an ownership or participation interest in an AK LNG project and associated facilities (proposed AS 31.25.080(a)(23)). But, AS 31.25.080(g) states that the power in proposed AS 31.25.080(a)(23) may not be exercised by an entity or subsidiary of the AGDC advancing the development of an in-state natural gas pipeline.

After consultation with the DNR commissioner and the DOR commissioner, the AGDC may enter into contracts related to an AK LNG project (proposed AS 31.25.080(a)(24)). For services related to transportation, liquefaction, marine terminals, marketing, and commercial support, the AGDC may not charge a service fee to the state or any state entity in an amount greater than the amount necessary to reimburse the AGDC for the cost of the service (proposed AS 31.25.005(5)).

Due to the addition of AK LNG project duties, the bill would create a new fund within the AGDC for the AK LNG project separate from the fund for the in-state natural gas pipeline. The Alaska liquefied natural gas project fund, proposed AS 31.25.110, would be created as a fund for monies appropriated to the AK LNG project, with direction to transfer net revenues received related to equity interest, contracts and other activities to the appropriate fund of the state as determined by the DOR commissioner in consultation with the DNR commissioner.

In order to maximize the efficient use of state resources, yet keep appropriate separation between the in-state natural gas pipeline and the AK LNG project due to confidential commercially sensitive information, proposed AS 31.25.040(c) would direct the AGDC board of directors to establish appropriate separation within the corporation when developing an in-state natural gas pipeline, an AK LNG project, and other transportation mechanisms in the state. Under proposed AS 31.25.040(d), the board may further implement this separation by appointing separate program directors for the in-state natural gas pipeline project and the AK LNG project. Under proposed AS 31.25.050(b), to further implement this separation, the attorney general is designated as legal counsel for the AGDC for legal services related to development of contracts and agreements for the AK LNG project, but no changes are made to the ability of the AGDC to retain legal counsel in other legal matters, including litigation.<sup>13</sup>

Currently, the DNR and DOR commissioners may not serve on the AGDC board of directors absent statutorily specified conditions related to the Alaska Gasline Inducement Act, AS 43.90. AS 31.25.020(a) would be amended to remove the possibility that the commissioner of natural resources and the commissioner of revenue may be appointed to the AGDC board. While typically the governor's power of appointment should not be limited, the governor may wish to acquiesce in the continued limitation in recognition of the extensive role those commissioners would have in the AK LNG project through consultation on contracts related to

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<sup>13</sup> The Department of Law is excepted from the state procurement code for legal services related to an AK LNG project (proposed AS 36.30.850(b)(48)). Similarly, the DNR is excepted in contracting for professional and technical services (proposed AS 36.30.850(b)(47)).

the AK LNG project under proposed AS 31.25.080(a)(24), and continued management of the state's royalty and gas tax share. Additionally, the AGDC is directed to provide the commissioners access to information related to contracts under AS 38.05.020(b)(10) and (11).<sup>14</sup>

AS 31.25.120 is amended to clarify that the AGDC may create subsidiary corporations and not be limited in the type of subsidiary that may be formed. In keeping with the goal of efficient operation and maximum use of state resources, the AGDC could transfer assets (technical studies, for example) to a subsidiary created by the AGDC subject to the limitation that funds may not be transferred between the in-state natural gas pipeline fund and the AK LNG project fund. Sections 7 - 21 of the bill related to AGDC would be effective immediately, if enacted into law.

### **III. Provisions related to the oil and gas production tax.**

The bill would make three major changes in core features of the oil and gas production tax statutes, as well as several definitional changes and numerous conforming amendments. Apart from the definitional changes, almost all of the bill's provisions affecting the production tax apply to oil and gas produced on or after January 1, 2022.

The first major change proposed is that gas produced on or after January 1, 2022, would be taxed at 13 percent of the gross value at the point of production of the gas.<sup>15</sup> This is in contrast to current law, under which both oil and gas are generally taxed at 35 percent of their *net* value (production tax value), i.e., net of upstream costs.<sup>16</sup> Under the bill, oil would continue to be taxed at 35 percent of its production tax value.

Second, for purposes of calculating the production tax value of oil produced on or after January 1, 2022, the bill would provide that lease expenditures - i.e., upstream costs of exploration, development, or production - would be deductible without regard to whether a lease expenditure might be considered attributable to oil or to gas.<sup>17</sup> In the interest of absolute clarity, it should be noted that current law is unchanged as to the potential deductibility of lease expenditures whether incurred with respect to oil or gas deposits. The change that would be made by the bill would be that the deduction of those lease expenditures would affect the taxable value of oil only, rather than affecting the taxable values of both oil and gas.

Proposed AS 43.55.160(h) also would identify more explicitly than under current law the applicable lease expenditures that would be deductible in calculating the production tax value for each of the several categories of oil for which a separate calculation is required. Moreover, as a result of other statutory changes described here and the expiration of several tax ceilings, fewer

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<sup>14</sup> Proposed AS 31.25.090(i).

<sup>15</sup> Proposed changes are in AS 43.55.011(e), levy of the oil and gas production tax.

<sup>16</sup> However, current law contains a number of exceptions to this general rule, such as special tax ceilings for various categories of oil and gas, which will continue. Some of those exceptions will expire by their own terms after 2021.

<sup>17</sup> Proposed AS 43.55.160(h).

production tax value categories would be required starting in 2022, and the remaining categories will be largely defined geographically.

The third major change proposed by the bill would be a provision that, for oil and gas leases that are modified under proposed AS 38.05.180(hh) and from which the DNR commissioner has determined to take royalty gas in kind under AS 38.05.182, producers would have the option to pay the producer's gas production tax in the form of physical gas, rather than money, on or after January 1, 2022. If a producer elects that option, the producer would be required to deliver to the state, at the point of production, 13 percent of the gas produced from each affected lease, instead of paying to the state 13 percent of the gross value of the gas produced.<sup>18</sup>

While payment of a tax in kind (in this case, in gas) rather than money is unusual, we have not found any constitutional or statutory impediment to this provision. The bill provision does not purport to bind future legislatures, so art. IX, sec. 1 of the Alaska Constitution regarding the "surrender of the taxing power" is not implicated.<sup>19</sup> Moreover, since payment in gas is optional under the bill at the producer's election, there should be no reason for a producer to protest about the availability of this option.

Proposed AS 43.55.014(c) would provide for the DNR to manage the custody and disposition of the gas, as previously discussed in this bill review. Proposed AS 43.55.014(d) would address underpayments and overpayments of tax in the form of gas. In addition to specifying how assessments of deficiencies and credits or refunds of overpayments will be calculated, this provision makes clear that an assessment, credit, or refund would not be triggered by an under-delivery or over-delivery of gas that is adjusted under a state-approved gas balancing agreement. Proposed AS 43.55.014(e) would provide that the in-kind tax payment option does not apply to gas that is flared beyond authorized amounts and considered produced under current AS 43.55.020(e).

The bill also would address several subsidiary issues particular to a tax paid in the form of gas under proposed AS 43.55.014. The bill proposes clarifying changes to the Alaska Net Income Tax Act. The changes proposed to AS 43.20.144(d) would provide that gas delivered to the state as payment for tax would not be construed as a sale for the purposes of the sales factor in the apportionment formula. In order to reflect activity in the state, gas subject to the election to pay gas as tax would be included in the extraction factor in the apportionment formula under the changes proposed in AS 43.20.144(f). Proposed AS 43.05.230(k) would exclude from taxpayer confidentiality provisions some information about a producer that makes an election to pay tax as gas under proposed AS 43.55.014(a) in recognition of the interest of the public in an AK LNG project.

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<sup>18</sup> Proposed AS 43.55.014.

<sup>19</sup> The AK LNG project may involve long term contracts, including for example contracts for sale of the state's share of royalty gas taken in-kind and tax as gas received under the proposed AS 43.55.014. An analysis of the possible constitutional impacts of those contracts may be appropriate if and when the state desires to enter into such contracts.

The definitions of "gas processing plant" and "point of production" would be amended, and a definition of "gas treatment plant" would be added.<sup>20</sup> These changes would ensure that the point of production for gas is always upstream of any pipeline transporting gas to a gas treatment plant and any pipeline system transporting gas to market, even if a producer for some reason were to postpone metering the gas until after the gas has been moved through the pipeline.<sup>21</sup>

Conforming amendments would be made to AS 43.55.011(f) (North Slope minimum tax); AS 43.55.019 (education tax credit)<sup>22</sup>; AS 43.55.020(a) (installment payments of estimated tax); AS 43.55.020(g) and (h) (interest on overpayments and underpayments); AS 43.55.020(l) (producers' tax settlement with private royalty owners); AS 43.55.030(a) (production tax returns); AS 43.55.160 (calculation of production tax values); and AS 43.55.165(e) (exclusions from lease expenditures). The majority of the substantive tax provisions would be effective January 1, 2015, if enacted into law; the provisions that clarify that credit would only be taken against the production tax levied under AS 43.55.011(e) would be effective immediately, if enacted into law (secs. 27, 48, 50, and 68 of the bill).

#### **IV. Provisions on the methods of municipal tax on oil and gas production and pipeline property.**

The legislature added provisions proposing changes in AS 29.45.080 to require a taxing municipality – with oil and gas production and pipeline property under AS 43.56 within the municipality's jurisdiction – to inform the DOR by May of each year the total value of the municipality's locally assessed property tax base and the payment amount for the principal and interest on bonds that the municipality intends to apply in its mill rate calculation the fiscal year corresponding to the tax year for which the assessment method selected by the municipality applies. This notice requirement would be in addition to the requirement in existing law to notify the DOR by February 1 each year of the method of taxation the municipality will use. A municipality may not collect property tax for taxable property within the municipality's jurisdiction in excess of the product of the percentage determined in proposed AS 29.45.080(f) of the average per capita assessed full and true value of the property in the state multiplied by the number of residents of the taxing municipality. The sliding scale percentage factor set in proposed new AS 29.45.080(f) would be based on the mill rate of a municipality. The current fixed percent factor of 225 percent is proposed to be removed by the legislature. A conforming change is proposed to be made to AS 43.56.010(c) to reference the new percentage factors in AS 29.45.080(f). Also, the sliding scale percentage factor, depending on the mill rate, would be incorporated into the tax limitation in AS 29.45.090 that provides a municipal ad valorem tax is not to exceed three percent of the assessed value of property in the municipality. A municipality

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<sup>20</sup> Proposed AS 43.55.900 (10), (20), and (25).

<sup>21</sup> Proposed changes to AS 43.55.900(20).

<sup>22</sup> The legislature added language that would clarify the scope of the education tax credit to include certain vocational, training, and apprenticeship equipment and programs. One of the changes has a delayed effective date of January 1, 2021, which is consistent with the delayed effective date for the education tax credit in current law.

that taxes at a mill rate above 19.0 would continue to have the same limitation in the percentage factor (225 percent) as current law. Municipalities with mill rates lower than 19.0 would see the percentage factor increase with a corresponding increase in tax they may levy before the tax limit applies.<sup>23</sup> These changes were not included in the Administration's proposal of the bill and are not limited to natural gas pipeline property and related facilities. However, the proposed changes to the tax cap address the recognition of the effects an AK LNG project would have on municipalities that could be addressed with property tax payments.

#### **V. Legislative intent, studies, reports, and briefings.**

The legislature proposes to reiterate in legislative intent that the AGDC when participating in an AK LNG project or a natural gas pipeline shall, to the maximum extent permitted by law, provide hiring and training opportunities in the state.<sup>24</sup> We have previously approved similar language intended to encourage, but not mandate, the training and hiring of Alaska residents. Accordingly, no constitutional infirmity would be associated with this aspect of the bill.<sup>25</sup>

Recognizing the importance of public infrastructure, and the likelihood that commercialization of North Slope gas would require expanded public infrastructure, the legislature proposes to direct the Department of Transportation and Public Facilities (DOTPF), in consultation with the AGDC, to evaluate the design and construction of a new separate bridge across the Yukon River that could accommodate vehicular traffic and a gas pipeline. Also, the DOTPF, in consultation with the AGDC and the DNR, would be required to evaluate existing infrastructure as well as infrastructure to be constructed to accommodate a gas pipeline in order to determine whether infrastructure could be constructed for vehicular traffic.

To assure consideration of statewide energy needs, the DNR commissioner, in consultation with the AGDC, would be required to make a report with recommendations to the legislature on a plan and alternatives to make North Slope natural gas available for delivery and use in the state, and the benefits and risks. The DNR commissioner would make the report and recommendations available to the legislature on or before the date a firm transportation services agreement for a North Slope natural gas project to which the state is a party is submitted to the legislature for approval.

Due to the effect on municipalities of new properties related to natural gas development, the legislature requests the governor to establish an advisory planning group to advise the governor on municipal involvement in a North Slope natural gas project, including property tax

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<sup>23</sup> The tax limitations in AS 29.45.080 - 29.45.090 apply to taxes that the municipalities use primarily for operating budgets as AS 29.45.100 renders the limits inapplicable to taxes levied to pay or secure bonds.

<sup>24</sup> This section would amend the legislative intent expressed in the legislation that established the AGDC. Section 1(b), ch. 11, SLA 2013.

<sup>25</sup> 2007 Op. Alaska Att'y Gen. (June 5), 2007 WL 2333365 (Alaska A.G.), reviewing SCS CSHB 177(FIN), ch. 22, SLA 2007, the Alaska Gasline Inducement Act (AGIA).

issues. The group would provide reports including recommendations to the governor. This request incorporates language from Administrative Order No. 269.<sup>26</sup> In our view, the governor has already met the legislature's request by issuing Administrative Order No. 269.

Several bill provisions would direct state entities and the commissioners of DNR and DOR to make studies and provide recommendations to the legislature.

The Alaska Energy Authority (AEA), in consultation with the AGDC, the DOR, and the Alaska Industrial Development and Export Authority (AIDEA), would be required to develop a plan for developing infrastructure to deliver more affordable energy to areas of the state not expected to have access to a North Slope natural gas pipeline. The plan would identify ownership options, different energy sources, and recommend the means for generating, delivering, and storing energy in the most cost-efficient manner. The AEA, in consultation with the DOR, would be directed to recommend funding possibilities. Also, the AEA would be required to provide the plan and suggested legislation to the legislature before January 1, 2017.

The DOR commissioner would report to the legislature on a range of financing options, including the respective risks and effect on the bonding capacity and bond rating of the state, for state participation in a North Slope natural gas project. An interim draft report would be available to the legislature on the first day of the First Regular Session of the Twenty-Ninth Alaska State Legislature. The final report would be submitted at the time the DNR commissioner submits the first agreement under proposed AS 38.05.020(b)(11) for legislative approval. Also at that time, the DOR commissioner would be required to submit a plan and *suggested* legislation to allow a municipality, regional corporation<sup>27</sup>, or resident of the state to participate as a co-owner in a North Slope natural gas pipeline.

In keeping with the bill's provisions designed to keep the legislature informed, the parties to a North Slope natural gas project would be required, at least once every four months before the first flow of gas, to provide progress briefings to interested legislators, legislative staff, and legislative consultants. The DNR would provide a written report, to accompany each briefing, on the amount of money that the state may be obligated to pay a third party under an agreement or contract for a North Slope natural gas project if the project is terminated before the first flow of gas.

## **VI. Letter of intent<sup>28</sup>**

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<sup>26</sup> Administrative Order 269 (Mar. 25, 2013), establishing the Municipal Advisory Gas Project Review Board to "develop a framework to evaluate the effects and issues that will arise in the future concerning development of the State's abundant North Slope natural gas resources and the newly created infrastructure to make those resources available to customers throughout the state and markets worldwide."

<sup>27</sup> Regional corporation is defined as a regional corporation organized under 43 U.S.C. 1606(a).

<sup>28</sup> April 20, 2014, Senate Journal, page 2643 - 2644.

Accompanying the bill was a letter of intent from the Alaska State Legislature expressing its intent that the AK LNG project honor commitments agreed to in the Heads of Agreement (HOA) through construction of the project.<sup>29</sup> Briefly, the letter incorporates Article 11 of the HOA related to the HOA parties' commitment to, *inter alia*, employ Alaska residents and contract with Alaska businesses and use, as far as practicable, job training centers operated by the Department of Labor and Workforce Development. While provisions that mandate "local hire" or preferential hiring raise constitutional concerns, statements of intent tempered with phrases such as "within the constraints of law" as used in Article 11 of the HOA do not impose specific hiring preferences, nor limit potential employment to qualified persons. We have found no constitutional problems with provisions encouraging local hire "to the maximum extent permitted by law" and similarly see no constitutional problems with the letter of intent.<sup>30</sup>

## VII. Conclusion

The bill is the legislature's substitute for the Administration's initial proposal. While there are changes from the document the Administration introduced, the bill substantially implements the policies of the original proposal. Other than as noted, we see no legal issues with the bill and believe the bill would withstand any legal or constitutional challenge.

Sincerely,

/ s /

Michael C. Geraghty  
Attorney General

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<sup>29</sup> The Heads of Agreement (HOA), January 14, 2014, was signed by the Administration of the State of Alaska, through the DNR and DOR commissioners, the AGDC, TransCanada Alaska Development Inc., ExxonMobil Alaska Production Inc., ConocoPhillips Alaska, Inc. and BP Exploration (Alaska) Inc. The HOA is a nonbinding agreement, and not part of codified or uncodified law. It is available on the Department of Revenue web site: <http://dor.alaska.gov/AKGasDocs.aspx>.

<sup>30</sup> 2007 Op. Alaska Att'y Gen. (June 5), 2007 WL 2333365 (Alaska A.G.), reviewing SCS CSHB 177(FIN), ch. 22, SLA 2007, the Alaska Gasline Inducement Act.