

MUNICIPAL ADVISORY GAS PROJECT REVIEW BOARD

February 20, 2015

10:08 a.m.

Taken at:

Alaska Gasline Development Corporation Board Room
3201 C Street, Suite 604
Anchorage, Alaska

MUNICIPAL ADVISORY GAS PROJECT REVIEW BOARD:

Commissioner Randall Hoffbeck, Chair
Commissioner Mark Myers
Mayor Clay Walker
Mayor Larry DeVilbiss
Mayor Charlotte Brower
Mayor Mike Navarre (via telephone)
Mayor Reggie Joule
Robert Venables
Robert Bartholomew
Joe Hardenbrook

Others participating:

Stephanie Alexander, Department of Revenue
Rob Elkins, Department of Administration and Finance, North Slope Borough
Akis Gialopsos, Senator Giessel's Office (via telephone)
Steve Pratt, AGDC (via telephone)
Sharon Long, Senator Huggins' Office (via telephone)
Tom Williams, BP (via telephone)
Rena Delbridge, Representative Hawker's Office (via telephone)
Mike Fisher, Northern Economics
Rebecca Logan
Dan Seckers, Exxon Mobil
Cindy Bailey, BP
Joe Reese, BP
Paul Quesnet, BP
Dave Norton, Representative Hawker's Office
Drema Fitzhugh, Representative Hawker's Office
Shalon Harrington, Mayor Sullivan's Office
Andy Stemp, North Slope Borough
Ron Arvin, Mat-Su Borough
James Wilson, Mat-Su Borough
Chris Gates, Mat-Su Borough
John Tichotsky, DOR
Rocky Riley, Village of Minto (via telephone)

PROCEEDINGS

COMMISSIONER HOFFBECK calls the February 20, 2015, meeting of the Municipal Advisory Project Review Board. He asks Ms. Alexander to call the roll.

MS. ALEXANDER calls the roll.

COMMISSIONER HOFFBECK states that the first item on the agenda is the approval of the agenda.

MAYOR DEVILBISS makes a motion to approve the agenda.

MR. BARTHOLOMEW seconds.

There being no objection, the motion is approved.

COMMISSIONER HOFFBECK states that next on the agenda is the approval of the draft meeting minutes from November 12, 2014 and December 12, 2014.

MR. BARTHOLOMEW makes a motion to approve the minutes from the November 12, 2014 and the December 12, 2014 meetings.

MR. VENABLES seconds.

There being no objection, the motion is approved.

COMMISSIONER HOFFBECK states that next on the agenda is the review of the update to the report. He continues that at the December meeting there was some discussion on a particular phrase within the overarching principles that shape the government take methodology. The proposed language was: "While the MAG board may not share a common view on certain issues, nonetheless the board does agree that any recommendations for changes to the tax structure in AS 29.45 and/or AS 43.56 should be based on a set of principles," and then it goes into the principles. He asks Ms. Alexander for a review of what was found.

MS. ALEXANDER states that in reviewing the recording, the whole group agreed that this change would be adopted but did not actually vote on it.

COMMISSIONER HOFFBECK states that is why it did not show up in the original draft report, as it was never officially voted on, but was agreed upon. He continues that language is now included in the draft report.

MAYOR DEVILBISS thanks him for that.

COMMISSIONER HOFFBECK states that Ms. Alexander did all the hard work. He continues that the question going forward with the update of the report is whether to finalize this as the final initial report to the Governor or leave it as an interim report and then actually present the report with more meat as to the direction that the MAG board is intending to take.

A short discussion ensues.

COMMISSIONER HOFFBECK asks for a motion.

MR. VENABLES makes a motion to incorporate this language in the interim report, and then close out the interim report.

MR. BARTHOLOMEW seconds.

COMMISSIONER HOFFBECK calls the vote.

There being no objection, the motion is approved.

COMMISSIONER HOFFBECK states that this is an opportunity for general public comment.

GENERAL PUBLIC COMMENT

COMMISSIONER HOFFBECK states that the floor is open to anyone who would like to make any comments on the report, or anything generally.

MR. RILEY states that he is Rocky Riley from the Village of Minto. He continues that the proposed gasline runs right across the Minto Native people subsistence area. There are a lot of Native allotments which belong to the Minto people. He asks why no one from the Village of Minto was appointed to the board since it is going to be a big impact on the village. He believes that Minto should be included because of the impact to the village, even though it is not an organized borough.

COMMISSIONER HOFFBECK thanks Rocky.

MAYOR NAVARRE replies that Governor Parnell appointed the advisory board, and it is an advisory board. He states that the Legislature is going to put the final touches on whatever is developed around the parameters for a PILT. He continues that because the Governor tried to get broad representation in order to get to a recommendation, there will be plenty of opportunities, but the Legislature has the final determination.

COMMISSIONER HOFFBECK thanks Mayor Navarre.

MR. RILEY states that the alignment, the pipeline has a right-of-way all the way from Prudhoe to Livengood and then one almost to Anchorage. These areas are through virgin territory, and the Minto people should be considered.

COMMISSIONER HOFFBECK clarifies that the primary focus of the advisory board is to deal with issues associated with the taxation and how it would be handled under a gasline project. He continues that the board is primarily focused on organized boroughs, and those government entities that would be affected directly by the gasline. He states that there are issues with offtake and other impacts that will be dealt with, but there are also other avenues for dealing with the right-of-way issues that fall outside the purview of this particular board.

MR. RILEY, again, states that Minto should have a seat at the table.

COMMISSIONER HOFFBECK thanks him for his comments, and asks for any other comments on the phone or in the audience.

MAYOR DEVILBISS requests, as a motion of privilege, that the audience and people online identify themselves.

COMMISSIONER HOFFBECK asks Ms. Alexander to poll the people online.

MS. ALEXANDER polls the audience both online and in the room.

COMMISSIONER HOFFBECK thanks all, and if there are no more public comments, moves forward on the agenda to the timeline. He states that there was some expectation in the Legislature that if there was legislation that was going to be necessary to implement any PILT structure, that it could potentially be brought forward in this session. He continues that, if not, then it would be ready for a special session in the fall, if there is one. He adds that those timelines need to continue to move forward. He states that one of the biggest concerns expressed by the Legislature and by the parties within the negotiations is that this would be a drag on the process; the position that the Municipal Advisory Group takes would be one that would be hard to get resolved and therefore slow down the process. He thinks that this group can be one of the leaders in the process and can be diligent in that. There are three issues in front of the group that need to be dealt with: 1. Payments of both taxes during the operation portion of the pipeline; 2. Dealing with the issues of the construction time frame and those impact payments within that time period; 3. Identify the PILT structure. He states that the goal for today would be to try and lock in on the component of what would work as far as the PILT structure. That could then be loaded into the AK LNG process for looking at the total economic package for the pipeline. He suggests that the logical next meeting would be to deal with the impact payments. He states that the third is not really a process, and the AK LNG sponsor groups carry the weight on that which is an issue between the municipalities and the State, the distribution. He asks if everyone is comfortable with that kind of timeline moving forward.

MR. BARTHOLOMEW likes the structure.

A short discussion ensues.

MAYOR DEVILBISS asks if there is some time today to talk about the interaction of the two pipelines and the announcements that are playing into this.

COMMISSIONER HOFFBECK replies that the impact that has on this group is probably different than the overall impact it has. He continues that his preference is to stay focused on the impact it has with this group, and let the Governor's office talk about the overall impacts. He adds that it can be brought up before adjournment this afternoon. He states that next on the agenda is potential timelines for additional MAG board meetings. He suggests picking up the pace and meeting every couple of weeks instead of monthly to keep this process moving. He asks for any comments.

MR. VENABLES suggests talking about this at the end of the meeting.

MR. HARDENBROOK asks for clarification on the timeline of the three issues before us.

COMMISSIONER HOFFBECK replies that the direction from the administration is putting a structure around the PILT and working with how to deal with impact payments during construction are necessary to get into the economics of the project. He continues that it would be good to have it done before the legislative sessions are over, certainly before summer. He states that the third component on how the distribution is going to work probably needs to have more input on the economics of the project first. There are a lot of critical decisions that need to be made, and those may change the State's take and how it is distributed.

A discussion ensues.

COMMISSIONER HOFFBECK calls a five-minute break.

(Break taken.)

COMMISSIONER HOFFBECK calls the meeting back to order and begins the discussion on the PILT structure. He starts with a recap from the November 2014 meeting defining the principles for a property tax PILT mechanism. First, it needs to be fair to all stakeholders. The reality is that the State is a major stakeholder in the property tax and will probably be the largest stakeholder overall of any individual on the property tax. He continues that this is an important component within the economics of the project for the State, as well. He states that it needs to be clear and be easily understood. Next, it needs to be robust; something that will last and not be subject to changes in the future. He continues that it needs to be very clear and not subject to judgment and interpretation. He adds that it needs to be commercially sound and must be able to enable the project. He states that he read that the PILT structure should create a revenue stream similar to what would have been created under a standard taxing system. He continues his presentation, explaining as he goes along.

MR. VENABLE asks how 2B will play out both in time and in structure.

COMMISSIONER HOFFBECK replies that is a resolution on a PILT structure can be reached today, then a document could be formalized, have the MAG group concur, and then have the fiscal team present it in the LNG negotiations.

MR. VENABLE states that at previous meetings, the body discussed having members of this board be part of that fiscal team. He asks if that will happen.

COMMISSIONER HOFFBECK replies that is not likely to happen. He continues his presentation, explaining as he goes along. He talks about replacement costs and moves on, stating that another major component within the current tax system is measurements of obsolescence. He continues that the current tax structure has depreciation based on the economic life of proven reserves. He adds that it is very difficult to determine what the physical depreciation and obsolescence is associated with that.

COMMISSIONER MYERS states that the reserve is also challenged because a project may have dedicated reserves, but the basin has a vast resource out there.

A discussion on reserves ensues.

COMMISSIONER HOFFBECK continues his presentation, looking at the potential features of PILT that can be put into a PILT that would be the criteria that has been laid out. He states that the first is to work with the idea of actual costs, not replacement cost. Next is design throughput. He continues that instead of trying to chase throughputs up and down, simply lock in the design capacity in relationship to the actual cost at the time the pipeline goes into operation. That would give the anchor for the costs moving forward. He adds that design throughput is measurable. He continues to the actual gas flow, which is a measurable data point that will have little or no uncertainty on that. He states that annual inflation would be the component that would keep the values real rather than nominal. The final is the tax rate. He continues that the statutes make it clear that it is the 20-mill rate that is dictated in 43.56. He adds that the only place that becomes a difficult point is in Kenai or wherever the LNG plant is. He briefly explains how the 20-mill rate works.

MR. BARTHOLOMEW clarifies that the tax rate and the AS 43.56 plan, as proposed now, would cover the gas treatment plant and the pipeline.

The discussion continues.

COMMISSIONER HOFFBECK moves to the next slide, to begin talking about and building up a formula for the PILT. He talks about five components, beginning with the foundation of the actual cost. The second component would be the actual gas flow design divided by the design throughput. He explains that this would give a measure of obsolescence due to any kind of change of throughput in the pipeline. He adds that this will also allow dealing with expansions going forward, if there are expansions.

The discussion on this continues.

COMMISSIONER HOFFBECK states that the next component would be an inflation component, which he explains. He continues that the final component would be that in order to get to the PILT, there would be actual costs, times the gas flow provided by throughput, times the inflation index, times 20 mills. He states, that would be the PILT.

MAYOR DEVILBISS states that in seeing the formula, it seems that if there is a zero throughput there is zero tax.

COMMISSIONER HOFFBECK states that is correct. He moves on to talk about how to deal with unexpected interruptions that may not reflect the value of the reservoir or the asset. He continues that there needs to be some kind of protection put on those.

A discussion ensues.

COMMISSIONER MYERS states that the way the project is designed right now is fully integrated from upstream through all the assets to the marketplace. He continues that they are incentivized to fill their share of the pipeline. He explains this more fully.

A discussion ensues.

COMMISSIONER HOFFBECK moves on to inflation adjustment. He states that the question came up about these assets. He continues that the assets do have some physical life and are

going to be maintained in such a fashion that they will stay in use until no longer needed. He states that life becomes a very difficult thing to determine and has become a major issue with the value of TAPS and even some of the upstream assets in that it is tied to reserves. He continues that the idea was to put in an adjustment here that backs down the inflation component slightly in order to account for the depreciation of the asset. He would like to discuss this more after lunch. He states that the final component of the formula is the 20-mill levy and it seems pretty clear for the pipeline and the upstream assets, the GTP. He continues, that already falls under that 20-mill levy. He points that out on the slide; it reads “adjustment to inflation denominator” and should say “numerator.”

A discussion ensues on this and the depreciation formula.

MR. FULFORD states, in the context of Alaska oil and gas property tax and the way that works through statute, the circumstances here are relatively unique; but in terms of finding a long-term solution to a problem around some fiscal take, then look at production-sharing agreements. He continues that there would probably be a lot of evidence of mechanisms in there to address an equitable fiscal arrangement over a long period of time. He adds that it is kind of a risk-sharing mechanism. He states that what is being done here is slightly different because it involves providing finance for municipalities, social services, which is very different to a shareholder of a company who would take a very different view of it.

COMMISSIONER HOFFBECK states that the next issue is the 20 mills as it relates to the Kenai Peninsula Borough in Nikiski. He asks Mayor Navarre if he has any input to offer on this.

MAYOR NAVARRE states that in looking at how the project is structured and if a 20-mill assessment is being considered in order to determine the PILT, the Kenai LNG facility ought to be included in that. He continues that then it becomes just an issue of the sharing between the State and local government, which is what is being looked at for the rest of the project.

COMMISSIONER HOFFBECK asks if he sees any major pushback if that was recommended.

MAYOR NAVARRE replies that because of the value disparity, he does not know. He states that there are too many uncertainties and would ask ConocoPhillips.

COMMISSIONER HOFFBECK states that the other question would be that the Kenai Peninsula Borough would be locked in at some kind of fixed mill rate.

MAYOR NAVARRE replies that it would probably be a separately negotiated PILT under the Title 29 provisions, if that is where it stays. He adds that it all fits into the total government take.

MAYOR BROWER states concern about PILT and wants to make sure that a borough that has an opportunity to stay on this will.

COMMISSIONER HOFFBECK moves on to the next slide and reiterates that they would be well served to have three separate PILTs: One for the GTP; one for the pipeline; and one for the LNG plant.

A discussion ensues.

COMMISSIONER HOFFBECK moves on, asking Nick Fulford to go through the next slide.

MR. FULFORD moves on to the question of enabling a globally competitive LNG project. He continues that this is just a schematic which shows the kind of value flow between the markets on the one side of the equation and the wellhead value of the gas on the other side. He adds that included in the different bars is an example of the highest and lowest of each stage. He states that the objective here is to achieve a PILT mechanism which enables the value of that gas to be sufficiently attractive to justify the \$45 to \$65 billion of investment in the value chain. He continues that it was a precursor to returning to these original criteria for enabling a globally competitive LNG export.

COMMISSIONER HOFFBECK states that the next slide puts some numbers into perspective in this idea of wanting a commercially sound project, which he goes through. After a short discussion, he moves and introduces the idea of impact fees during construction, which he and Mr. Fulford explain. He continues that the next slide has the docket number which will enable the downloading of this report from the FERC website. He adds that it is about 140 pages and deals with a great deal of detailed information about the boroughs that are being represented.

A short discussion ensues.

COMMISSIONER HOFFBECK proposes that at the next meeting dealing with the impacts during construction and have someone from FERC present. He adds that the MAG report from Stranded Gas can be gotten. He calls a five-minute break.

(Break.)

COMMISSIONER HOFFBECK states that this last slide is of the next steps, which will be left up because it has the formula on it.

A discussion ensues on coming up with a consensus of putting together a document that can be presented to the Assemblies of the represented communities.

COMMISSIONER HOFFBECK steps through each of the factors to make sure that there is a consensus on how to deal with them, with a discussion following each factor.

MR. VENABLES states that it is his understanding that at the next meeting there will be more talk about direct and indirect impacts.

COMMISSIONER HOFFBECK asks for any further discussions.

A discussion ensues on a good time for the next meeting.

COMMISSIONER HOFFBECK states that the next meeting will be Friday, March 15, 2015, same time and same place. He asks for a motion to adjourn.

COMMISSIONER MYERS makes a motion to adjourn.

MAYOR WALKER seconds.

There being no objection, the motion is approved.

(Meeting adjourned at 3:20 p.m.)

DRAFT