

MEMORANDUM

State of Alaska
Department of Law

To: William Corbus, Commissioner
Department of Revenue

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Subject: Effect of Article IX, Sections
1 and 4 of the Alaska
Constitution on Proposed
Stranded Gas Development
Act Contract Terms

I. INTRODUCTION

The purpose of this opinion is to provide analysis and advice on the question of whether sections 1 and 4 of article IX of Alaska's Constitution permit the state to enter into a long-term fiscal contract under the Stranded Gas Development Act ("SGDA"), AS 43.82.010 *et seq.* The proposed contract would exempt the sponsors of the Gas Pipeline Project from paying certain taxes associated with oil and gas production and transportation, and would replace those taxes with specified payments in lieu of those taxes. The provisions in the contract that would incorporate a Petroleum Production Tax ("PPT") similar to that considered by the legislature (HCS CSSB 305 FIN AM H, S Fld CONCUR H(AM)) have not been finalized at this time. However, it is expected that the contract will generally provide for 30 years of fiscal certainty for payments in lieu of certain taxes on oil and up to 45 years for payments in lieu of all other taxes. Other key provisions of the proposed contract include state commitments to finance and own 20 percent of the Gas Pipeline Project and to take in-kind and market the royalty and production tax shares of the gas.

II. SUMMARY OF ADVICE

Article IX, section 1 of Alaska's constitution prohibits the legislature from surrendering the power of taxation, but permits the legislature to suspend or contract

away the tax power as provided in article IX.¹ Section 4 of article IX provides the permissive authority for the legislature to grant tax exemptions by general law.² Thus, while Alaska's constitution restricts the legislature's authority from surrendering its power of taxation, it does not prohibit the legislature from suspending or contracting away its power to tax by granting tax exemptions.

The SGDA authorizes the Commissioner of Revenue ("Commissioner") to negotiate fiscal terms for inclusion in a proposed SGDA contract, including periodic payments in lieu of taxes that otherwise would be imposed by the state or a municipality on the sponsor of a gas pipeline project.³ The fiscal terms may be "tailored to the particular economic conditions of the project and . . . [established] in advance with as much certainty as the Constitution of the State of Alaska allows."⁴ The term of the proposed contract "may be for no longer than is necessary to develop the stranded gas that is subject to the contract . . . ; however, the term of the contract may not exceed 35 years from the commencement of commercial operations of the approved qualified project."⁵ The proposed SGDA contract must be approved by the legislature before it is binding on the state.⁶

While the SGDA is not the first time the state has authorized contractual tax incentives to encourage development of Alaska's resources, the Alaska Supreme Court

¹ Alaska Const. art. IX, § 1: "[t]he power of taxation shall never be surrendered. This power shall not be suspended or contracted away, except as provided in this article."

² Alaska Const. art. IX, § 4:

Exemptions. The real and personal property of the State or its political subdivisions shall be exempt from taxation under conditions and exceptions which may be provided by law. All, or any portion of, property used exclusively for non-profit religious, charitable, cemetery, or educational purposes, as defined by law, shall be exempt from taxation. Other exemptions of like or different kind may be granted by general law. All valid existing exemptions shall be retained until otherwise provided by law.

³ AS 43.82.020(1).

⁴ AS 43.82.010(2).

⁵ AS 43.82.250. The administration proposes to amend this and other provisions of the SGDA. In this memorandum, we assume there is statutory authority for the contract terms.

⁶ AS 43.82.435.

has not addressed the extent of the state's authority under section 1 of article IX to enter into such agreements or whether a future legislature may amend or repeal the terms of such a fiscal certainty contract. However, the United States Supreme Court has held that state legislatures may agree to long-term, binding tax arrangements to the extent permitted under individual state constitutions.

In accordance with the SGDA, the Commissioner has issued comprehensive preliminary findings which conclude that the proposed fiscal certainty terms are necessary to encourage investment in the Project. The fiscal certainty provided is also expected to slow the decline in oil production by encouraging further investment in Alaska's oil fields, particularly its marginal fields.

We believe that a reviewing court will defer to the findings of the Commissioner and the legislature. The provision of tax incentives to develop Alaska's resources to benefit all Alaskans was expressly contemplated by the delegates to the constitutional convention and deliberately embodied in sections 1 and 4 of article IX as well as sections 1 and 2 of article VIII. Additionally, Congress provided unprecedented amounts of land to Alaska under the Statehood Act so that the state could support itself through development of its resources. Therefore, we believe that the proposed SGDA Contract is constitutional under sections 1 and 4 of article IX. The next sections of this memorandum explore this conclusion in greater detail.⁷

III. SUMMARY OF THE FISCAL CERTAINTY TERMS IN THE PROPOSED CONTRACT

The state legislature has enacted the SGDA and has considered legislation providing for a new PPT. In accordance with the authority provided to it in the SGDA, the state administration has negotiated the proposed SGDA Contract with Exxon, ConocoPhillips and BP (collectively, the "Sponsor Group"). The proposed terms would exempt the Sponsor Group, as well as any other producers that enter into an upstream fiscal certainty contract and commit to ship North Slope gas on the Project (collectively, "Participants"), from certain state and municipal taxes that would otherwise be imposed as a consequence of the commercialization of North Slope gas (e.g., oil and gas production, property and corporate income taxes, as well as other state and local taxes).

⁷ This memorandum addresses only the effects of sections 1 and 4 of article IX on the proposed contract terms; it does not address other sections of article IX or other provisions of the constitution that do not directly relate to sections 1 and 4. Similarly, we have analyzed the question of whether the state may contract away certain aspects of the power of taxation, thus requiring a federal Contract Clause analysis, but we have not considered the impact of other provisions of the federal constitution on the proposed contract.

In lieu of exemption from certain taxes, Participants would make specified payments to the state and affected municipalities.

Generally speaking, total state oil and gas revenues under the SGDA Contract are comparable to those the state would receive if the 2005 fiscal regime remained in place.⁸ The Commissioner has also determined that oil and gas revenues could increase under the proposed SGDA Contract.⁹ In the words of the Commissioner, “the contract provides inducement through stability, not by materially reducing the present day tax burden on the project.”¹⁰ The state will receive its tax payments in gas instead of cash and commit to ship the gas on the pipeline.¹¹

The Commissioner’s Findings indicate that North Slope gas could be one of the most expensive resources in the world to bring to market, and that building the gas line may turn out to be one of the most expensive private construction projects ever undertaken.¹² Fiscal certainty improves the Project’s internal rate of return, making it more likely that it will go forward.¹³ Moreover, the combination of fiscal stability, state equity participation, and the state agreeing to take its gas in-kind and ship it on the pipeline, “provide[s] commercially reasonable inducements to influence a timely and favorable decision to commence the feasibility and regulatory work obligations . . . and create a higher probability that the required investment in the project will be made on the

⁸ Commissioner’s Preliminary Findings and Determination as required by the Stranded Gas Development Act (May 10, 2006) (hereafter “Commissioner’s Findings”) at FIF-246. Revenues under the SGDA Contract are expected to approximate or be higher than total state oil and gas revenues that would have been received under the fiscal system as it existed in 2005. *Id.* at ES-2 (\$35 billion under the proposed Contract versus \$34 billion under the 2005 fiscal structure); FIF-73 (Table 6, Comparison of Total State Oil and Gas Revenues).

⁹ Commissioner’s Findings at ES-2. The Commissioner expects a gain in gas-related revenues of \$12 billion in net present value and an increase of oil-related revenues of \$2 billion in net present value, for a total gain of \$14 billion. *Id.* Additionally, Table 6 at FIF-73 indicates higher revenues than those expected under the 2005 fiscal system for \$5.50/MMBtu (million British thermal units) of gas and higher and \$35 per barrel of WTI (West Texas Intermediate) oil.

¹⁰ *Id.* at FIF-246.

¹¹ *Id.* at ES-11, FIF-47, FIF-50-51.

¹² *Id.* at FIF-48, FIF-115.

¹³ *Id.* at FIF 142-43; FIF-165.

project sanction date.”¹⁴ Therefore, the Commissioner has found that the fiscal stability the SGDA Contract would bring is intended to raise the Project higher on the investment priority list for projects in the producers’ portfolio of potential projects worldwide.¹⁵

Furthermore, the provision of fiscal certainty for gas developed in the future under other state leases will encourage all North Slope producers to provide additional gas to the Project needed to completely fill the pipeline to capacity for the term of the contract.¹⁶ In short, the Commissioner has determined that fiscal certainty is necessary to establish a significant long-term gas industry in Alaska.¹⁷ Additionally, he has found that the fiscal certainty arrangement is also expected to have the added benefit of encouraging investment in smaller oil fields in Alaska, which may slow the otherwise predicted decline in oil production.¹⁸ Providing fiscal certainty for oil as well as gas will make the Project more attractive since the Participants’ overall oil and gas business in Alaska will benefit from fiscal stability under the Contract.¹⁹

With respect to the proposed terms of fiscal certainty, the Commissioner has determined that the long-term fiscal interests of the state will be served by providing fiscal certainty for up to 45 years for gas.²⁰ This term is required to allow the pipeline owners (including the state) to recover pipeline investment costs as well as provide assurance to Project lenders that a stable fiscal environment will prevail.²¹ Additionally, the Commissioner’s Findings state that such certainty is required to locate the additional reserves that will be needed to fill the gas line to capacity for its useful life.²² In other

¹⁴ *Id.* at FIF-243. *See also* ES-9, ES-12, FIF-107.

¹⁵ *Id.* at FIF-103, FIF-244.

¹⁶ *Id.* at ES-11, FIF-48, FIF-115. Legislation will be proposed to provide fiscal certainty to all ANS state leases, as well as to any party that makes firm transportation commitments. *Id.* at ES-5, ES 8-9, FIF-98, FIF-115.

¹⁷ *Id.* at ES-1.

¹⁸ *Id.* at ES-1, FIF-118, FIF-246.

¹⁹ *Id.* at FIF-117-18.

²⁰ *Id.* at ES-2, FIF-115-17.

²¹ *Id.* at ES-5, FIF-115-17, FIF-245.

²² *Id.* at ES-5, FIF-115-17, FIF-246. Alaska’s 35 trillion cubic feet of known proven reserves of gas is likely not enough to fill the line for the entire 35-year useful life and therefore, (continued)

words, because the state, as an equity owner in the Project, will receive revenues from the sale of gas shipped through the pipeline, fiscal certainty not only provides the state with a steady flow of tax revenues, but also encourages maximum Project success, thus further enhancing the state's revenue sources from monetizing its gas in this fashion.²³

It is expected that the Contract will generally provide for 30 years of fiscal certainty for oil taxes, which will enhance the likelihood of Project success.²⁴ First, gas exploration expenses are deductible from the proposed PPT, thereby encouraging exploration for the gas needed to fill the gas line to capacity.²⁵ Since this gas will be needed in the midpoint of the 35-year useful life, providing fiscal certainty for oil up until that time instead of for up to 45 years is appropriate.²⁶ As noted above, the PPT will encourage investment in smaller oil fields as well. Additionally, the Project is less likely to be built unless oil fiscal certainty is provided since the Sponsor Group has indicated that it will not enter into an SGDA contract without oil fiscal certainty.²⁷ Without certainty on both oil and gas taxes, the state could increase oil taxes to capture additional value and thus change the fiscal stability of the gas tax structure.²⁸

Finally, to assure the terms of fiscal stability, the proposed SGDA Contract requires the state to reimburse Participants for tax payments they might be required to make under any subsequently enacted tax that is the same or similar to a tax from which they are exempt under the Contract. The Sponsor Group maintains that the reimbursement provisions are required to insulate them from future legislation or ordinances providing for new or additional taxes after they have undertaken the investment necessary to develop the Project.

the Project's success will depend in part on providing the proper investment climate to find that gas. *Id.* at FIF-117.

²³ *Id.* at FIF-105.

²⁴ *Id.* at FIF-246.

²⁵ *Id.* at FIF-118.

²⁶ *Id.* at FIF-118, FIF-246.

²⁷ *Id.* at FIF-117.

²⁸ *Id.* at FIF-117-18.

IV. LEGAL ANALYSIS

The question of whether the proposed SGDA Contract is enforceable raises questions of federal and state law. First, may a state, which is sovereign, enter into a fiscal contract that is enforceable? Second, even if a state may enter into a fiscal contract that would be enforceable under the U.S. Constitution, does the Alaska Constitution provide the legislature with the authority to do that?

A. States May Enter into Fiscal Contracts Subject to Limitations Contained in Individual State Constitutions

The Supreme Court of the United States has determined that a state legislature may alienate its taxing powers, at least to some degree, if not prohibited by the state's constitution and if done in an unmistakable manner. Once the tax power is properly alienated, a state's contractual promise is binding through application of the Contract Clause of the Constitution of the United States.

The legal maxim that one legislature has the ability to overrule its predecessors was firmly embedded in English common law.²⁹ However, in American jurisprudence the doctrine underwent significant limitation with the adoption of the federal Contract Clause, which establishes that, “[n]o State shall . . . pass any . . . Law impairing the Obligation of Contracts.”³⁰ In 1810, the Supreme Court began defining the contours of the Contract Clause in *Fletcher v. Peck*.³¹ The Court recognized that the clause imposes limitations on the states, established requirements for its enforcement, and developed an analytical framework for alleged violations.

The Contract Clause was adopted by the federal framers for several reasons. First, they were aware of the abuses of the English Parliament, especially during the reign of Charles II, when lands were blatantly confiscated and contractual rights extinguished by

²⁹ “Acts of parliament derogatory from the power of subsequent parliaments bind not Because the legislature, being in truth the sovereign power, is always of equal, always of absolute authority: it acknowledges no superior upon earth, which the prior legislature must have been, if its ordinances could bind the present parliament.” 1 W. Blackstone, *Commentaries on the Laws of England* 90 (1765).

³⁰ U.S. Const. art. I, § 10.

³¹ 10 U.S. 87 (1810).

parliamentary enactments.³² Second, they were aware of the abuses of local legislatures in interfering with debtor-creditor relationships.³³ They wished to prevent this from happening in the republic. Third, after the American Revolution, the newly emerging country was in substantial economic crisis and the federal framers felt that fiscal instability that did not promote economic investment would hamper the success of the new republic.³⁴ They hoped that a constitutional provision enshrining contractual rights and limiting state rights would promote economic growth in the nation.³⁵

The fundamental and governing principles established by the United States Supreme Court can be stated as follows: a state's power of taxation is not a police or regulatory power, but is a power fully capable of alienation by a sovereign; it can be bargained away by the sovereign for consideration; once it is bargained away, the promise concerning it is fully protected by the Contract Clause, which is binding on states through application of the Supremacy Clause.³⁶ For the Contract Clause to have any meaning, the promise of the state has to be binding on the state's future legislatures.³⁷ If it were not binding on the legislatures, states would be free to void contractual obligations by enacting nullifying laws.

³² See *Trustees of Dartmouth College v. Woodward*, 17 U.S. 518, 559 (1819) (argument of Daniel Webster).

³³ The Contract Clause “was made part of the Constitution to remedy a particular social evil — the state legislative practice of enacting laws to relieve individuals of their obligations under certain contracts” *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 256 (1978). James Madison explained that the people were “weary of the fluctuating policy” of state legislatures and wanted it made clear that under the new government men could safely rely on states to keep faith with those who justifiably relied on their promises. *The Federalist No. 44*, at 301 (J. Cooke ed. 1961).

³⁴ *The Federalist No. 7*, at 42-43 (A. Hamilton) (J. Cooke ed. 1961).

³⁵ B. Wright, *The Contract Clause of the Constitution* 4-5, 15 (1938).

³⁶ U.S. Const. art. VI, cl. 2 (“This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.”).

³⁷ See Eule, *Temporal Limits on the Legislative Mandate: Entrenchment and Retroactivity*, 1987 Am. B. Found. Res. J. 379, 392-93 (observing that the English rationale for precluding a legislature from binding its successors does not apply in America).

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With respect to certain state rights, however, sweeping application of the Contract Clause is undesirable, and limited by three principles. First, the states still retain some authority to define what is a legal contract under their state laws, and therefore enforceable under the Contract Clause. The states may enact constitutional provisions defining what contracts are enforceable that will be recognized as a threshold matter by the Supreme Court in Contract Clause analysis.

Second, there are certain essential attributes of state sovereign authority that are incapable of alienation. They are called the “reserved powers.” A state can never alienate those powers so that the alienation will be binding on future legislatures and enforceable under the Contract Clause. The reserved power is the residuum of state sovereignty that inheres in all of the state’s contracts. Under United States Supreme Court precedent, taxation power is not a reserved power.

Third, before a promise of alienation of sovereign power will be enforceable under the Contract Clause, the promise must be so clearly expressed, and unmistakably detailed, that it is capable of no other interpretation but of the sovereign’s unequivocal intent to alienate the power. This is called the “unmistakability doctrine” of Contract Clause law.

The purpose of the federal Contract Clause is to promote economic certainty through the enforcement of contractual obligations. The purpose of the reserved powers doctrine is to prevent a sovereign from selling off critical powers essential to governance. The purpose of the unmistakability doctrine is to avoid unnecessarily trammeling on state sovereign rights unless it is clear beyond any debate that the state meant to give up that right.

As recognized by the Supreme Court many times, there is an inescapable tension between, on the one hand, the Contract Clause, and, on the other hand, the three limitations. From nearly the birth of this country to present day, the Court has struggled to develop its framework balancing all principles. The question of whether the proposed SGDA Contract violates article IX, section 1 or is enforceable under the Contract Clause calls into play all these complex principles.

In *Fletcher v. Peck*, the U.S. Supreme Court considered whether the federal Contract Clause precluded the Georgia legislature from enacting a law voiding an earlier sale of certain lands conveyed by Peck to Fletcher in 1803.³⁸ The seller argued the

³⁸ 10 U.S. 87 (1810).

familiar English maxim that one legislature was always competent to repeal any act which a former legislature had passed.³⁹ In interpreting the meaning of the federal guarantee against impairment of contract in the context of the Georgia legislature's attempt to void the sale, the Court invalidated the Georgia act.

In a similar case, in 1845 the Ohio legislature granted a corporate charter to a bank that provided for a six-percent tax on the profits of the bank. In 1851, the legislature passed another law imposing a different tax structure on the bank. The U.S. Supreme Court considered whether a promise to maintain a certain tax structure was enforceable under the Contract Clause.⁴⁰ The county treasurer seeking to uphold the 1851 Act argued that the state could not have alienated its taxation powers in the 1845 charter. The Court held that the state could have alienated such power.

Again, in *Ohio Life Ins. & Trust Co. v. Debolt*,⁴¹ the U.S. Supreme Court upheld the right of an Ohio life insurance company to enforce an 1834 corporate charter stating it would pay no more than five percent of its dividends on net profits as tax to the state notwithstanding the fact that, in 1851, the Ohio legislature enacted a law modifying the arrangement. The Court held the taxation agreement in the 1834 charter enforceable under the Contract Clause:

[I]f the contract was within the scope of the authority conferred by the constitution of the State, it is like any other contract made by competent authority, binding upon the parties. Nor can the people or their representatives, by any act of theirs afterwards, impair its obligation. When the contract is made, the Constitution of the United States acts upon it, and declares that it shall not be impaired, and makes it the duty of this court to carry it into execution.⁴²

The Court made clear that a threshold inquiry must be made to determine if the alienation of taxation power was authorized under a state constitution: “[N]o one legislature can, by its own act, disarm their successors of any of the powers or rights of sovereignty confided by the people to the legislative body, unless they are authorized to do so by the constitution under which they are elected.”⁴³

³⁹ *Id.* at 135.

⁴⁰ *Piqua Branch v. Knoop*, 57 U.S. 369 (1853).

⁴¹ 57 U.S. 416 (1853).

⁴² *Id.* at 429.

⁴³ *Id.* at 431.

Because the Court concluded the Ohio constitution had no such prohibition, the Ohio legislature had power to enter into such a tax contract. Therefore, the 1834 agreement was enforceable under the Contract Clause.

In *Stone v. Mississippi*, the Court delivered its clearest explanation of the limits on the alienability of powers of taxation and the reserved powers doctrine up to that point.⁴⁴ In 1867 the State of Mississippi granted a corporation a charter to conduct a lottery for 25 years. An 1868 constitutional provision prohibited all lotteries.

The Court found that, while the legislature could not bargain away the public morals with regard to lotteries, no such prohibition existed with respect to taxing power:

While taxation is in general necessary for the support of government, it is not part of the government itself. Government was not organized for the purposes of taxation, but taxation may be necessary for the purposes of government. As such, taxation becomes an incident to the exercise of the legitimate functions of government, but nothing more. No government dependent on taxation for support can bargain away its whole power of taxation, for that would be substantially abdication. All that has been determined thus far is, that for a consideration it may, in the exercise of a reasonable discretion, and for the public good, surrender a part of its powers in this particular.⁴⁵

In *United States Trust Co. of New York v. New Jersey*, the United States Supreme Court held that the New Jersey legislature could not enact legislation modifying an earlier enacted bondholder covenant, and that limited deference would be given to the sovereign's stated need for the later legislation since the state was perceived to have a self-interest in repudiating its debt.⁴⁶ The Court concluded that when a state entered into a debt contract that included terms upon which investors rely, the state cannot avoid its financial obligations by seeking refuge in the reserved powers doctrine. One legislature can bind another with regard to such obligations. The Court did state, however, that the Contract Clause "is not an absolute bar to subsequent modification of a State's own

⁴⁴ 101 U.S. 814 (1879).

⁴⁵ *Id.* at 820.

⁴⁶ 431 U.S. 1 (1977).

financial obligations.”⁴⁷

In *United States v. Winstar Corp.*, the Court’s most recent pronouncement on the enforceability of a sovereign’s contractual promises to adhere to financial obligations, the Court embraced Contract Clause analysis in considering the binding nature of a contractual promise by two federal agencies.⁴⁸ The Court concluded that the agreement by federal agencies to hold harmless a private party against future regulatory changes did not impede the exercise of any sovereign power.⁴⁹

In *Simpson v. Murkowski*, a case in which the Alaska Supreme Court was evaluating, not a tax exemption issue, but rather the discontinuance of the longevity bonus, the court applied a two-part test to determine whether the law violated the federal Contract Clause.⁵⁰ First, the court examines whether the law operates as a substantial impairment of a contractual relationship. To make that determination, the court considers (1) whether there is a contractual relationship; (2) whether the law impairs that relationship; and (3) whether the impairment is substantial. Second, if the court finds that the law substantially impairs a contractual relationship, the court examines whether the impairment is “reasonable and necessary to serve an important public purpose.”⁵¹

To determine whether a statute creates a contractual relationship, the court looks primarily to the statute’s language. “In general, [the court] will look for language specifically creating a contract or expressly prohibiting future amendments that would reduce benefits.”⁵² By using “language evincing a clear and unequivocal intent to create a binding contract,” the legislature may create a contract entitled to Contract Clause protection.⁵³

⁴⁷ *Id.* at 25 (citing *City of El Paso v. Simmons*, 379 U.S. 497 (1965)). In *El Paso*, the Court held that a statute that put a limit on the amount of time that buyers of public land had to pay off delinquent interest in order to get their land back was not an unconstitutional impairment of contract. It stated further that a state’s “economic interest” could justify contract impairment. 379 U.S. at 508.

⁴⁸ 518 U.S. 839 (1996).

⁴⁹ *Id.* at 883.

⁵⁰ 129 P.3d 435, 444 (Alaska 2006).

⁵¹ *Id.* (quoting *U.S. Trust Co.*, 431 U.S. 1, 25 (1977)).

⁵² *Id.* at 445.

⁵³ *Id.* at 446.

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The cases cited above suggest that, if permitted by their individual constitutions, states may, in the exercise of reasonable discretion, surrender a portion of their taxing powers. They must, however, do so unmistakably and unequivocally. Courts will not infer a contracting away of taxing power.⁵⁴

We believe that the proposed SGDA Contract and the act of the legislature in authorizing the governor to sign it constitute a contract under applicable Contract Clause analysis. The Contract Clause analysis asks if the fiscal certainty guarantee requires the alienation of a reserved power. As discussed, the United States Supreme Court has found taxation powers to be fully alienable in various contexts. We believe that a reviewing court is likely to find that the power of taxation provided for in section 1 of article IX is fully alienable.

The next question will be whether the SGDA Contract and the act of the legislature in authorizing the governor to enter into it are unequivocally clear and capable of no other interpretation but that Alaska intended to alienate its taxation powers for the terms established in the SGDA Contract. We believe that the SGDA Contract does unequivocally indicate that the state intends to alienate its power to change taxes from the terms established in the Contract.⁵⁵ Therefore, assuming the legislature authorizes the governor to enter into the Contract, the federal Contract Clause is likely to permit Participants who have relied on the fiscal certainty guarantee to bring a successful constitutional claim if a future legislature alters the fiscal certainty terms in a manner that substantially impairs the Contract and is not otherwise justified as reasonable and necessary to serve an important public purpose.

B. The Alaska Constitution Provides Authority for the Legislature to Contract Away or Suspend Taxing Authority Through General Law

1. In response to the United States Supreme Court's interpretation of a state's power of taxation, many states restricted their inherent power to contract away taxes through state constitutional taxation clauses -- but not Alaska

In the nineteenth century many states, in order to attract certain businesses such as

⁵⁴ See *Covington v. Kentucky* 173 U.S. 231 (1899) (The Court established that a sovereign's intent to enact an irrevocable law must be unmistakable).

⁵⁵ See Art. 11.1 of the proposed SGDA Contract.

railroads to their states, began conferring permanent, total tax exemptions to those corporations in their charters.⁵⁶ When the fiscal uncertainties of later times rendered the continuing grant of permanent tax exemptions ill-advised, many states attempted to impose taxes on the corporations.⁵⁷ However, the Supreme Court refused to impose the taxes and instead upheld the corporations' permanent tax exemptions under the federal Contract Clause.⁵⁸ As far back as 1810, in *Fletcher v. Peck*, the United States Supreme Court determined that a state could alienate the power to tax if done in a clear and unmistakable way.⁵⁹

Several states were displeased with the Supreme Court's construction of the federal Contract Clause.⁶⁰ Some states therefore enacted state constitutional prohibitions against the surrender of taxation power.⁶¹ The National Municipal League (NML) Model State Constitution included a power of taxation clause which stated that "[t]he power of taxation shall never be surrendered, suspended or contracted away."⁶² The wording of these provisions varies slightly among states, but the most common language is that used by the NML.⁶³ As we discuss in further detail in a subsequent section of this memorandum, Alaska did not adopt the language used by the NML. Instead, its representatives at the constitutional convention considered the wording of the model provision, and adopted instead the unique clause in article IX giving the Alaska legislature authority to suspend or contract away taxing power by providing tax exemptions by general law.

⁵⁶ See generally Sterk & Goldman, *Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations*, 1991 Wis. L. Rev. 1301, 1319 (1991).

⁵⁷ E.g., *Home of the Friendless v. Rouse*, 75 U.S. 430 (1869).

⁵⁸ See generally *id.*; *Ohio Life Ins. & Trust Co. v. Debolt*, 57 U.S. 416 (1853); *Piqua Branch v. Knoop*, 57 U.S. 369 (1853).

⁵⁹ *Fletcher v. Peck*, 10 U.S. 87 (1810).

⁶⁰ *Gulf & S.I.R. Co. v. Hewes*, 183 U.S. 66 (1901); *Williams v. Mayor of Baltimore*, 289 U.S. 36 (1933); *Home of the Friendless v. Rouse*, 75 U.S. 430 (1869).

⁶¹ See generally Sterk & Goldman, *Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations*, 1991 Wis. L. Rev. 1301, 1319 (1991). Such provisions are known as "power of taxation clauses" or "alienation clauses."

⁶² Model State Constitution art. VII, § 700 (Nat'l Mun. League, 5th ed. 1948).

⁶³ See, e.g., Ariz. Const. art. IX, § 1.

It is well established that state legislatures possess plenary powers, except as the powers are limited by federal or state constitutions. A state legislature's plenary powers extend to everything within the sphere of the legislature's power, except as restricted by the federal or state constitutions.⁶⁴ In other words, "the [state] Legislature possesses every power not delegated to some other department or to the federal government, or not denied to it by the Constitution of the state or of the United States."⁶⁵ In contrast, the power of the federal government is one of only "delegated powers."⁶⁶

It is also well established that a state legislature may not contract away certain reserved powers, such as its police power. Some light is shed on Alaska's reserved powers by considering how the Alaska Supreme Court has defined "police powers," since police powers are regarded as inalienable.⁶⁷ The court has described Alaska's police powers as "broad and comprehensive."⁶⁸ The court has previously found many challenged state actions to be legitimate exercises of the police powers.⁶⁹ But the court

⁶⁴ *Pine Grove v. Talcott*, 86 U.S. 666 (1873).

⁶⁵ *People ex rel. Chicago v. Barrett*, 26 N.E.2d 478, 482 (Ill. 1940). See also *Smith v. Penta*, 405 A.2d 350 (N.J. 1979) (as the repository for the reserved powers of the government, the state legislature is free to act except in respect of the powers delegated to the federal government by the Constitution of the United States and except as such exercise may be limited by the state constitution; there are no other restraints on state legislative power); *Com v. Henry*, 65 S.E. 570 (Va. 1909) (the power of the legislature of the state is supreme except so far as it is restrained by the state or federal constitution, and even in case of doubt as to the power, all doubts are to be resolved in favor of the existence of the power).

⁶⁶ *Carter v. Carter Coal Co.*, 298 U.S. 238, 291 (1936) ("the powers which the general government may exercise are only those specifically enumerated in the Constitution, and such implied powers as are necessary and proper to carry into effect the enumerated powers.").

⁶⁷ See *Stepanov v. Homer Elec. Ass'n*, 814 P.2d 731 (Alaska 1991) (public utility contract between developer and public authority was subject to the reserved authority of the state, under the police power, to modify the contract in the interest of the public welfare).

⁶⁸ *State v. Enserch*, 787 P.2d 624 (Alaska 1990) (resident hiring preference not within police power).

⁶⁹ The following exercises of power have been found to be within the state's police powers: regulation of a food distribution center, *O'Callaghan v. Anchorage*, 2002 WL 1293001 (Alaska 2002); utility regulation, *Tlingit-Haida Reg'l Elec. Auth. v. State*, 15 P.3d 754 (Alaska 2001); hazardous substances releases, *Kodiak v. Exxon*, 991 P.2d 757 (Alaska 1999); regulation of hunting, *Totemoff v. State*, 905 P.2d 954 (Alaska 1995); tariff ratemaking for intrastate oil shipments, *Cook Inlet Pipeline Co. v. Alaska Pub. Util. Comm'n*, 836 P.2d 343 (Alaska 1992); and use of confidential well data by the state in order to maximize state revenues from leased (continued)

has also indicated, in dicta, in one case that it views “taxation power” as separate and apart from Alaska’s “police powers.”⁷⁰ A review of United States Supreme Court cases indicates that state taxation powers are not generally considered police powers and may be subject to being contracted away if permitted under individual state constitutions.

The determination of whether the Alaska legislature has authority to alienate its taxing powers begins by analysis of article IX, section 1, the “power of taxation clause,” to ascertain whether Alaska’s constitutional framers deprived the legislature of all authority to alienate its power of taxation. Based on the text of article IX, section 1 and section 4, and the constitutional history of the provisions, the framers of Alaska’s constitution chose to limit, but not preclude, the state’s legislature from alienating its power of taxation through tax exemptions to provide incentives for economic development of Alaska’s resources.⁷¹

Based on the debate that occurred among the delegates at the Alaska Constitutional Convention, and on the familiar principle that constitutional and legislative provisions should be harmonized so that none of the words are rendered superfluous, we believe that the framers intended to leave the legislature with the authority to suspend or contract away the power to tax as part of its power to grant tax exemptions by general law.⁷² Indeed, immediately before and after the constitutional convention, both the Alaska territorial and state legislatures adopted industrial incentive acts providing tax

lands, *Dep’t of Natural Res. v. Arctic Slope Reg’l Corp.*, 834 P.2d 134 (Alaska 1992). Cf. *Matthews v. Quinton*, 362 P.2d 932 (Alaska 1961) (transportation of schoolchildren to nonpublic schools not within police powers).

⁷⁰ In *Waiste v. State*, 10 P.3d 1141 (Alaska 2000) (Takings Clause challenge to seizure of boat for suspected fishing law violations), the court in enumerating different sources and types of state power, listed “taxation power” separately from “police power” and separately from “the power to purchase property.” *Id.* at 1155. Arguably, if taxation power were already subsumed within “police power,” there would have been no need for the court to separately identify the power.

⁷¹ Very little case law directly interprets the pertinent article IX provisions. The Alaska Supreme Court has considered other issues arising out of tax contracts without addressing the constitutionality of the underlying contracts. Case law from other states is mixed, and is highly dependent on the particular language of other states’ constitutions and the particular facts. It is difficult to draw firm conclusions from these cases that are applicable to Alaska in view of the framers’ discussions concerning the unique language of Alaska’s power of taxation clause.

⁷² *Park v. State*, 528 P.2d 785 (Alaska 1974). This reading of the taxation clause is enhanced by article VIII of the state constitution, which provides for development of the state’s resources “for the maximum benefit of the people.” See Section IV-B-3, *infra*.

exemptions and other incentives to businesses investing in Alaska that were considered contractual in nature. Several delegates to the convention were members of the legislature when these acts were enacted.⁷³

Much direct archival evidence exists of the intent of the framers of Alaska's constitution to permit legislators to alienate a portion of taxation powers through tax incentives to encourage development of Alaska's resources. When members of the Committee on Finance and Taxation met to begin crafting article IX, they had already reviewed a paper concerning the NML Model State Constitution provisions that was prepared by consultants from the Public Administration Service (PAS).⁷⁴ Committee minutes reflect the discussion.⁷⁵

The PAS paper considered the origins of the Model State Constitution power of taxation clause, the ability of a sovereign to alienate its taxation powers through exemptions and incentives, and the negative view of tax incentives held by some economists.⁷⁶ The paper expressly cautioned delegates that tax exemptions could result in binding contractual obligations:

Whatever may be the merits of [the tax exemptions'] use, business and industrial tax exemptions have occasionally given rise to a significant constitutional problem. By granting such inducements in legislation, states have been held on occasion to have contracted away the taxing power. It is a settled principle of public law that one legislature cannot bind another and that the government of a state cannot contract away its police powers. The power to tax is not considered inalienable, however. *In granting exemptions, one legislature may bind another and thereby lose for the state its power*

⁷³ These acts are discussed in greater detail in section IV-B-3, *infra*.

⁷⁴ 3 Constitutional Studies, PAS Staff Paper 9, Vol. 3, State Finances (1955). The Alaska Supreme Court has recognized the importance of PAS papers in interpreting the framers' intent. See *State v. Alex*, 646 P.2d 203, 209 n.5 (Alaska 1982).

⁷⁵ "There followed a general discussion of the material PAS Paper #9 -Finance- and finance provisions in the Model State Constitution, Hawaii and Puerto Rico Constitutions, and those of various states. The discussion included . . . alienation clauses as they may affect tax incentives and other matters . . ." Minutes of the Finance Committee, Alaska Constitutional Convention (Nov. 16, 1955). In fact, the Finance Committee unanimously decided that the outline of PAS Paper No. IX be followed in committee deliberations.

⁷⁶ PAS Staff Paper, State Finance, at 15-16 ("tax specialists frown darkly on such devices").

to tax. The exemption may, under certain conditions, result in a contract relationship that legislatures may not abrogate without violating the federal constitutional guarantee against state legislation impairing the obligation of contracts.⁷⁷

Another PAS paper studied by all delegates advised that state constitutional limitations on legislative power, such as a power of taxation clause, could retard growth.⁷⁸ Nonetheless, it is clear from the convention history that the delegates consciously rejected the PAS' advice.

2. Alaska's constitutional delegates carved out an exception for suspending or contracting away the power to tax, as provided in section 1 of article IX

It is evident from the minutes of committee meetings and the transcripts of convention debate that the framers had a unique design and purpose for Alaska's taxation clause. They modified the NML Model State Constitution taxation clause into a preliminary draft of article IX, section 1 that read: "[t]he power of taxation shall never be surrendered; and shall never be suspended or contracted away, except as provided herein."

In committee meetings, when delegates asked if incentives might be viewed differently by experts in light of Alaska's unusual position, the committee's financial consultant, Dr. Weldon Cooper, replied, "yes, but that it should be part of an overall picture."⁷⁹

The committee's summary progress report noted that, "[t]he Finance and Taxation Committee is still considering tax incentive measures, which may be affected by classification, and related problems, *including a time limit on any incentive program.* The Committee has tentatively adopted certain secs. of the preliminary draft, and is preparing a Proposed article for submission soon."⁸⁰ At the first reading, Delegate White

⁷⁷ *Id.* (emphasis added).

⁷⁸ PAS Constitutional Studies, Vol. 2, "The Legislative Department," at 5-6 stated: "if, on the one hand, the restrictions [on legislative power in state constitutions] are highly specific and well-defined, there is always the danger that they may rapidly become out-moded and develop into barriers to necessary reform. This is well illustrated, for example, by state constitutional restrictions upon the power to tax."

⁷⁹ Minutes of Finance Committee (Dec. 5, 1955).

indicated that the semicolon and division of thought, and the addition of the words, “except as provided herein,” were to remove doubt as to what the framers meant in the exemptions provision of article IX, the proposed section 4.⁸¹ White described section 4 as allowing for the “granting of tax incentives to new industries.”⁸²

Delegate Nerland, chairman of the committee, explained this modified version of the section 1 taxation clause at second reading. He stated that the proposal “has been altered slightly from the usual wording of a number of state constitutions”⁸³ He continued, “[b]ut we did feel that there would possibly be occasion and good justification in the future for such things as allowing an industry-wide exemption to encourage new industry to come in and that is the reason for the particular wording there.”⁸⁴ As to the section 4 exemptions, he continued: “this is the provision that allows for some exemption or inducement to industries or similar things.”⁸⁵ The committee’s official commentary to section 1 explained that “[t]he power to tax is never to be surrendered, but under terms that may be established by the legislature, it may be suspended or temporarily contracted away. This could include industrial incentives, for example.”⁸⁶

Section 4 delineated a number of tax exemptions, and then followed with, “other exemptions of like or different kind may be granted by general law”⁸⁷ Official commentary to section 4 explained that “the legislature is authorized to make further tax

⁸⁰ Convention Committee’s Summary Progress Report No. 3, at 5 (Dec. 10, 1955) (emphasis added).

⁸¹ *Proceedings of the Alaska Constitutional Convention* (Dec. 19, 1955).

⁸² *Id.*

⁸³ *Id.* (Jan. 16, 1956).

⁸⁴ *Id.*

⁸⁵ *Id.* This evidence demonstrates that framers considered industrial exemptions to be one type of tax incentive, and authorized under section 4. The phrase “inducement to industries” is arguably broader than the term “exemption,” and allows for inducement schemes like the SGDA Contract that involve exemptions and other inducements.

⁸⁶ Commentary on the Article on Finance and Taxation (Dec. 16, 1955).

⁸⁷ Alaska Const. art. IX, § 4. Section 4 contains express tax exemptions for nonprofit, religious, charitable, cemetery, or educational purposes, but permits “other exemptions of like or different kind.”

exemptions to encourage, among other purposes, new industry”⁸⁸

Such archival history demonstrates that although the prohibition against surrendering taxation power may be absolute, the prohibition against suspending or contracting away taxing power is not absolute, but is qualified by the permissible exemption provisions in section 4. Thus, in Alaska the language governing suspending or contracting away taxing authority is permissive under certain conditions, whereas in other state constitutions the language is absolutely prohibitory. In Alaska, the framers deliberately rejected putting parameters around what would constitute a temporary tax incentive and specifying exactly what kinds of incentives could be provided.

The convention made no alterations to the committee’s final proposed language. The Committee on Style and Drafting, however, made nonsubstantive grammatical changes, adopting the current article IX, section 1: “[T]he power of taxation shall never be surrendered. This power shall not be suspended or contracted away, except as provided in this article.”

The final version of section 4’s tax exemption provision stated, in relevant part, “other exemptions of like or different kind may be granted by general law.” Chairman Nerland explained to the delegates that one purpose of the power of taxation clause was to prohibit forgiveness of already-delinquent or back taxes.⁸⁹ No floor debate on sections 1 and 4 voiced the framers’ concern with potential corporate overreaching, the impetus behind other states’ adoption of taxation clauses, although in discussions of other sections of the constitution the delegates were generally interested in making sure that Outside industries (the focus at the time was on the salmon industry) did not control Alaska’s resources or commandeer Alaska’s resource wealth.

With respect to the “like or different” language, Mr. Smith asked: “Isn’t that, in effect, saying that exemptions of any kind may be granted?” Mr. Nerland responded: “Yes, that was the purpose of it.”⁹⁰

Dr. Cooper repeatedly reminded the committee members that tax exemptions were highly disfavored.⁹¹ Nevertheless, the committee and entire convention manifested their

⁸⁸ Commentary on the Article on Finance and Taxation (Dec. 16, 1955).

⁸⁹ *Proceedings of the Alaska Constitutional Convention* (Jan. 11, 1956).

⁹⁰ *Id.* (Jan. 16, 1956).

(continued)

strong belief that in Alaska tax incentives should be encouraged under section 4. As Delegate Marston explained with regard to incentives, “to get outside capital coming here we’ve got to be liberal.”⁹² In spite of Dr. Cooper’s urging, the committee chose not to adopt a specific durational limit for tax exemptions for the express purpose of avoiding constitutional questions.⁹³

Of additional significance is “A Report to the People of Alaska from the Alaska Constitutional Convention, February 1956.”⁹⁴ This report simply stated: “Save for exempted property used for non-profit, religious, charitable, cemetery or education purposes, the legislature may determine the kinds and subjects of taxation and prescribe standards for appraisal of property for state or local purposes.”⁹⁵ This language informed the voters that the legislature had broad powers to determine the specifics of any tax regime. Moreover, the court expressly held in *DeArmond v. Alaska State Dev. Corp.* (which is discussed in greater detail in a subsequent section of this memorandum) that exemptions different from the charitable and other exemptions could be provided.⁹⁶

The broad authority over tax exemptions conferred in the constitution and described to Alaska voters at ratification continued historical precedent. As discussed below, the framers and their contemporaries in the territorial and first state legislatures were well aware of — and approved of — industrial incentives in the nature of tax contracts.

3. Constitutional history and principles of constitutional construction link together sections 1 and 4 of article IX

⁹¹ Minutes of Finance Committee (Dec. 5, 1955) (“Mr. Cooper also pointed out that experts generally viewed tax exemptions, beyond those traditionally granted, as a poor practice.”).

⁹² *Proceedings of the Alaska Constitutional Convention* (Jan. 18, 1956).

⁹³ Minutes of Finance Committee (Dec. 5, 1955).

⁹⁴ *See, e.g., State v. Lewis*, 559 P.2d 630, 637-38 (Alaska 1977) (footnote omitted) (citing directly to this report, the court stated: “While voters were probably not privy to the comments of the delegates in adopting the provision, they were made aware of its purpose in unambiguous language by A Report to the People of Alaska from the Alaskan Constitutional Convention which was widely distributed.”).

⁹⁵ Proposed Constitution of the State of Alaska, A Report to the People of Alaska from the Alaska Constitutional Convention, February 1956, at 1.

⁹⁶ 376 P.2d 717 (Alaska 1983).

Even before statehood, the legislature of the Territory of Alaska had enacted the Alaska Property Tax Act of 1949.⁹⁷ This Act authorized the tax commissioner to exempt “new industry” and “new industrial enterprises” from “license fees, excises or other taxes levied by the state or a political subdivision of the state” for up to ten years.⁹⁸ Factors influencing eligibility for the exemption included: permanence of the industry, amount of capital invested, whether the operation was seasonal or continuous, whether the operation was likely to be marginal because of the distance from principal markets, and the number of Alaskan workmen employed.⁹⁹ The Act constituted “a contract between the [local] taxing unit, and the owner of the property.”¹⁰⁰ It provided that the “exemptions shall remain in full force and effect for the periods granted and are binding.”¹⁰¹ Several of the delegates had been legislators when this Act was passed, bringing their experience to the convention. Thus, at the time the framers met in 1955, Alaska had a tax exemption act in place that by its own terms was considered contractual in nature.

The Alaska Industrial Incentive Act of 1957, a territorial statute enacted shortly after the convention but before ratification, established a graduated taxation exemption related to the amount of investment.¹⁰² Businesses could apply for a ten-year tax exemption certificate which, if granted, was deemed to be binding and in full force and effect upon the terms set forth for the period granted.¹⁰³ It provided for exemptions and

⁹⁷ Ch. 10, SLA 1949.

⁹⁸ *Id.* sec. 6(h)(1).

⁹⁹ *Id.* sec. 6(h)(2).

¹⁰⁰ H.B. 43, § 2, approved March 16, 1953.

¹⁰¹ *Id.* § 3.

¹⁰² See former AS 43.25.010 *et seq.*

¹⁰³ *Id.* The Alaska Supreme Court has considered provisions of this Act several times. In *Union Oil Co. of Cal. v. State*, 677 P.2d 1256 (Alaska 1984) (*Union I*), the court held that under the Act the incentives operated to reduce the state income tax liability of a subsidiary only, and not of an entire consolidated group. In *Union Oil Co. of Cal. v. State*, 804 P.2d 62 (Alaska 1990) (*Union II*), the court found the Department of Revenue’s interpretation of a tax exemption certificate reasonable. In *K & L Distribs., Inc. v. Murkowski*, 486 P.2d 351 (Alaska 1971), the court found that an industrial incentive tax credit of up to 75 percent of the value of an investment for seven years could be applied against a tax liability due under an excise tax. In none of these cases did the court opine, even in dicta, that the existence of such a tax incentive contract under the Act violated Alaska’s power of taxation clause. In fact, in *K&L Distribs.*, the (continued)

credits from a wide array of taxes, including income and property taxes as well as “license fees, excises or other taxes levied by the Territory or any political subdivision thereof.”¹⁰⁴ Moreover, an individual exemption could be tailored with terms and conditions needed to further the industrial development in question.¹⁰⁵ At least one major project on the Kenai Peninsula benefited directly from the provisions of the Industrial Incentive Act, and might never have come to fruition without its contractual terms.¹⁰⁶ Several members of the 1957 legislature had been convention delegates, and presumably brought their understanding of article IX’s provisions to the 1957 Act.

Following statehood, in 1968 the legislature enacted the Alaska Industrial Incentive Tax Credits Act.¹⁰⁷ Under this Act the grant of a tax credit was “effective for a period . . . not to exceed 10 years from the date of grant”¹⁰⁸ It offered tax credits rather than the exemption available in the 1957 Act.¹⁰⁹

In sum, the convention record indicates that the delegates were familiar with tax exemptions and credits, and the Acts discussed above suggest that they considered such incentives to be contractual in nature. Significantly, several members of the constitutional convention, including members of the Committee on Finance and Taxation, were also members of the 1949, 1957 or 1968 legislature. None of these members questioned the constitutionality of such Acts under article IX. In our view then, it is reasonable to conclude that the delegates did not view the Acts as violating article IX and intended that the “other exemptions” in section 4 relate to section 1.¹¹⁰

court found that the grant of tax relief provided for in the Act was “in the broadest possible form and that the legislature intended that a credit could be provided for almost any tax within the State of Alaska.” *Id.* at 358.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.*

¹⁰⁶ The liquefied gas plant, gas pipeline, and related facilities project on the Kenai Peninsula provided substantial development to the young state and utilized the benefits of the Act. 1998 Inf. Op. Att’y. Gen. (May 29; 883-98-0083), 1999 WL 638618, at * 4.

¹⁰⁷ Former AS 43.26 et seq., repealed in 1986.

¹⁰⁸ Former AS 43.26.010(a). Another provision, AS 43.26.050, set forth a few limited grounds for revoking the tax credit, but included no provision for allowing revocation based on a change in the law.

¹⁰⁹ Former AS 43.26.010(a).

(continued)

Moreover, unlike the earlier Incentive Acts, the proposed SGDA Contract requires continuous payments in lieu of taxes, not a complete exemption from payment of taxes. Additionally, as previously noted, taken as a whole, the payments are not expected to materially reduce the present-day tax burden on the project.

The length of fiscal certainty provided for in the SGDA Contract is much longer than the period of exemption provided for under the earlier Incentive Acts. However, as noted above, the framers rejected time limits for complete exemptions under section 4. If complete exemptions for taxes could be provided for any amount of time, it follows that continuous payments for a long period of time are not prohibited by sections 1 and 4. As previously noted, the Commissioner has found that the periods of fiscal certainty that will be provided for in the proposed SGDA Contract are necessary to convince the Sponsor Group to (1) build one of the largest and most expensive projects ever built; (2) invest in the Project in Alaska now as opposed to investing in numerous other gas projects around the world; (3) ensure that the vast amounts of gas needed to fill the pipeline to capacity are both discovered and committed to the Project; (4) allow recovery of the cost of building the pipeline; and (5) provide assurance to the parties' potential lenders. The Commissioner has also found that the fiscal certainty provided for in the Contract will encourage investment in oil fields to combat declining oil production. In short, it is reasonable to conclude that the proposed SGDA Contract is within the parameters established by the framers in sections 1 and 4 to use the state's tax structure to encourage development for the maximum benefit of the people.

¹¹⁰ With respect to the weight that the earlier Incentive Acts may have in interpreting these constitutional provisions, the court in *Juneau v. Hixson*, 373 P.2d 743 (Alaska 1962), considered post-constitutional legislation affecting "capital improvements" in determining that a home rule city's bond issue was not an unauthorized "capital improvement" within the meaning of article IX, section 9. On the other hand, the court held more recently in *Hickel v. Cowper*, 874 P.2d 922, 936 n.7 (Alaska 1994), that "the applicable degree of deference is lessened by the fact that at issue is the meaning of a constitutional amendment for which the legislature is not the ultimate adopting authority." The people are the ultimate adopting authority. *See, e.g., State v. Lewis*, 559 P.2d 630, 637-38 (footnote omitted) ("While we believe there can be no serious question as to the intent of the delegates in drafting Art. VIII, Sec. 9, we are cognizant [of the fact that a] constitutional provision . . . must be ratified by the voters, and it is therefore also necessary to look to the meaning that the voters would have placed on its provisions. While voters were probably not privy to the comments of the delegates in adopting the provision, they were made aware of its purpose in unambiguous language by A Report to the People of Alaska from the Alaskan Constitutional Convention which was widely distributed.") As noted above, the people were made aware of sections 1 and 4 in the Report to the People.

Article VIII, section 1 of the Alaska Constitution provides that it is “the policy of the State to encourage . . . development of its resources by making them available for maximum use consistent with public interest.” Further, article VIII, section 2 states that the “legislature shall provide for the . . . development . . . of all natural resources . . . for the maximum benefit of the people.” The constitution thus provides the legislature with broad powers to take actions to utilize and develop the natural resources of the state.

The proposed SGDA Contract is consistent with article VIII’s mandate to develop the state’s gas for the maximum benefit of Alaska citizens and fits within the parameters of sections 1 and 4 of article IX. Commentary by the delegates regarding article VIII makes it clear that all saw it as allowing for development of the state’s vast resources to benefit future Alaskans. For example, Delegate Rivers stated: “It seems to me that here we have the foundation and the framework for a real orderly development and utilization of our resources, and I, for one, feel we have laid the foundation here for the future success and well-being of all of our citizens [and for] the great success of the future state.”¹¹¹ The framers recognized that developing Alaska’s resources according to the mandate of article VIII might require an innovative tax regime, and this is reflected in their rejection of the highly restrictive NML model for article IX, the finance and taxation clause.

The need to develop natural resources for the people’s benefit was a continuing concern expressed not only at the convention but also in the Statehood Act debates that occurred simultaneously with the adoption of Alaska’s constitution. As the Alaska Supreme Court has noted, “[t]he primary purpose of the statehood land grants contained in section 6(a) and (b) of the Statehood Act was to ensure the economic and social well-being of the new state.”¹¹² The court explained in *Trustees* that even congressmen who supported statehood conceded that there would be difficult financial burdens without some special consideration of Alaska’s unique circumstances. To address the need for an economic base, Congress granted 103 million acres of federal land to Alaska as an endowment that would yield income for Alaska to meet the costs of statehood. The statehood land grant was considered “the foundation upon which Alaska can and will build to the enormous benefit of the national economy shared by her sister States.”¹¹³

The Supreme Court of Alaska first considered the section 4 exemptions clause in *DeArmond v. Alaska State Dev. Corp.*, a declaratory judgment action challenging

¹¹¹ *Proceedings of the Alaska Constitutional Convention* (Jan. 31, 1956).

¹¹² *Trustees for Alaska v. State*, 736 P.2d 324, 335 (Alaska 1987) (citations omitted).

¹¹³ *Id.* at 336 (citations omitted).

creation of the Alaska State Development Corporation.¹¹⁴ Taxpayers contended that the act creating the corporation, which exempted the Alaska State Development Corporation from all taxes and assessments, violated article IX, section 4, the exemptions clause.

The taxpayers argued that the phrase “other exemptions of like or different kind” limited the exemptions to only those types of exemptions previously named, and therefore, no residual exemption should be recognized for a state development corporation. The court rejected such a narrow construction of section 4. It concluded that the legislature may grant exemptions beyond those specifically listed in section 4:

We believe the word ‘like’ refers to the named exemptions in the preceding sentence and that ‘different’ was intended to clearly indicate that the legislature was not to be bound by the rule of *ejusdem generis* and was free to grant other exemptions even though they may not be of the same kind or character as those named.¹¹⁵

In *Alascom, Inc. v. North Slope Borough*, the court held that the prohibition against surrender or suspension of taxation power did not preclude application of a six-year statute of limitations to tax collections.¹¹⁶ The court stated:

We believe that the response to the Borough’s contention is provided by Article 9, section 4, of the Alaska Constitution, the provision addressing exemptions from taxation. After setting forth specific exemptions this provision states that “[o]ther exemptions of like *or different* kind may be granted by general law.” In our view this constitutional grant of power to except encompasses the power to require that taxes be assessed and collected within a certain period of time or be forever barred.¹¹⁷

The court in *Alascom* thus viewed a statute of limitations as a “different kind” of “exemption” under section 4. *Alascom* illustrates that the court will not consider sections 1 and 4 of article IX in isolation, but will attempt to harmonize their reading.

¹¹⁴ 376 P.2d 717 (Alaska 1962).

¹¹⁵ *Id.* at 725.

¹¹⁶ 659 P.2d 1175 (Alaska 1983).

¹¹⁷ *Id.* at 1179 (emphasis in original).

Additionally, although sections 1 and 4 of article IX were not discussed, the court held in *K&L Distribs., Inc. v. Murkowski* that the grant of tax relief provided for in the Industrial Incentive Tax Credits Act was “in the broadest possible form and that the legislature intended that a credit could be provided for almost any tax within the State of Alaska.”¹¹⁸

In *Atlantic Richfield Co. v. State*, oil and gas production companies raised numerous challenges to the constitutionality of the oil and gas corporate income tax.¹¹⁹ They claimed the tax deprived them of due process and equal protection, and violated the Commerce Clause. In addition, the companies contended that the income tax increased the state’s share under various leases, and thus violated the federal Contract Clause.

The court noted in dicta that, in entering into leases, the state could not contract away its power as a sovereign to tax income earned in the state, and the court then specifically observed that a government’s power to tax remains unless it has been specifically surrendered.¹²⁰ In *Atlantic Richfield*, the state’s power of taxation had not been specifically and unambiguously altered by the legislature and thus, *in entering the leases*, the state had no authority to contract away its taxing powers. The holding does not deal with a fact situation similar to the proposed contract at issue here in which the state unequivocally states its intent to alienate its power to change taxes for the terms established in the contract.

Finally, given the significant number of state constitutions with taxation clauses, it is surprising that relatively few cases exist that challenge tax incentives under power of taxation clauses. Even fewer cases address the precise points at issue in the proposed SGDA Contract.¹²¹

¹¹⁸ 486 P.2d 351, 358 (Alaska 1971).

¹¹⁹ 705 P.2d 418 (Alaska 1985).

¹²⁰ *Id.* at 438 (emphasis added) (citing *St. Louis v. United R. Co.*, 210 U.S. 266 (1908)); *See also Exxon v. Eagerton*, 462 U.S. 176, 187-94 (1983).

¹²¹ Relevant cases significant in upholding a fiscal certainty guarantee under a power of taxation clause include: *Valencia Energy Co. v. Arizona Dep’t of Revenue*, 959 P.2d 1256 (Ariz. 1998) (power of taxation clauses do not preclude some contracting away of taxing authority); *Gruen v. Tax Comm’n*, 211 P.2d 651 (Wash. 1949) (power of taxation clauses do not prohibit a legislature from contracting for a term longer than the life of the current legislature), *overruled in part on other grounds*, 384 P.2d 833 (Wash. 1963); *In re Opinion of the Justices (Mass.)*, 168 N.E.2d 858 (Mass. 1960) (a 40-year tax contract for urban renewal purposes is not a surrender of (continued)

In summary, the words of article IX, section 1, “except as provided in this article” would be superfluous and meaningless if there were no other provision in article IX allowing a suspension or contracting away of taxing power. Because sections 1 and 4 were adopted simultaneously and the convention history links them together, section 1 can reasonably be read to refer to the legislature’s power to authorize tax exemptions and other incentives by general law.¹²²

Further, the Alaska Supreme Court recognizes that the state constitution must be considered a “living document adaptable to a change in the conditions and circumstances unanticipated at the time it was written.”¹²³ Framers 50 years ago could hardly foresee the dramatically increased international competitiveness in energy development arising from the commercialization of former East Bloc nations, China, and other relatively undeveloped nations. Nevertheless, the framers’ intent to maintain an attractive industrial climate in Alaska is abundantly clear in the archival history, as is their intent to refrain from imposing arbitrary time limits for tax incentives.¹²⁴

Based on the significant constitutional and legislative histories discussed above, it is our conclusion that the framers intended to leave relatively unfettered the legislature’s authority to approve tax incentive contracts. Moreover, this conclusion is enhanced with respect to the current proposed SGDA Contract because of article VIII’s mandate to develop state resources and the Statehood Act’s provision of vast acreage to Alaska to develop an economic base to support all Alaskans.

V. CONCLUSION

As noted above, the words of article IX, section 1, “except as provided in this article” would be superfluous and meaningless if there was no other provision in article IX allowing a suspension or contracting away of taxing power. Because sections 1 and 4 were adopted simultaneously and the convention history links them together,

a sovereign’s taxing power); and *Bailey v. State*, 500 S.E.2d 54 (N.C. 1998) (irrevocable tax exemption did not violate North Carolina’s power of taxation clause).

¹²² *Proceedings of the Alaska Constitutional Convention* (Dec. 19, 1955) (comments of Delegate White regarding sections 1 and 4); *id.* (Jan. 16, 1956) (comments of Chairman Nerland regarding sections 1 and 4).

¹²³ *Warwick v. State ex rel. Chance*, 548 P.2d 384 (Alaska 1976).

¹²⁴ Industrial tax incentives in the oil and gas industry in the United States are widespread.

section 1 refers to the legislature's power to authorize tax exemptions and other incentives by general law.

Further, it is reasonable to conclude that the state will receive adequate consideration for the fiscal certainty provided for in the SGDA Contract in the form of the various benefits that will result to the state from building the Project. To summarize, in order to develop the state's vast gas resources now when oil production is declining rapidly, the Commissioner has determined that the fiscal certainty provided for in the proposed SGDA Contract is necessary. The Commissioner has found that certainty will encourage the Sponsor Group to (1) build one of the largest and most expensive gas lines ever built; (2) invest in the Project in Alaska now as opposed to investing in numerous other gas projects around the world; (3) ensure that the vast amounts of gas needed to fill the pipeline to capacity are both discovered and committed to the Project; (4) allow recovery of the cost of building the pipeline; and (5) provide assurance to the parties' potential lenders. The Commissioner has also found that the fiscal certainty provided for in the Contract will encourage new investment in oil fields to combat declining oil production.

Finally, if the proposed SGDA Contract is approved by the legislature, the Contract Clause of the U.S. Constitution may well prohibit future legislatures from changing its fiscal terms. For the reasons discussed above, we believe that the powers of taxation set forth in the Alaska Constitution are alienable. Therefore a fiscal contract of the type contemplated in the SGDA will likely be enforceable by the parties to the contract.