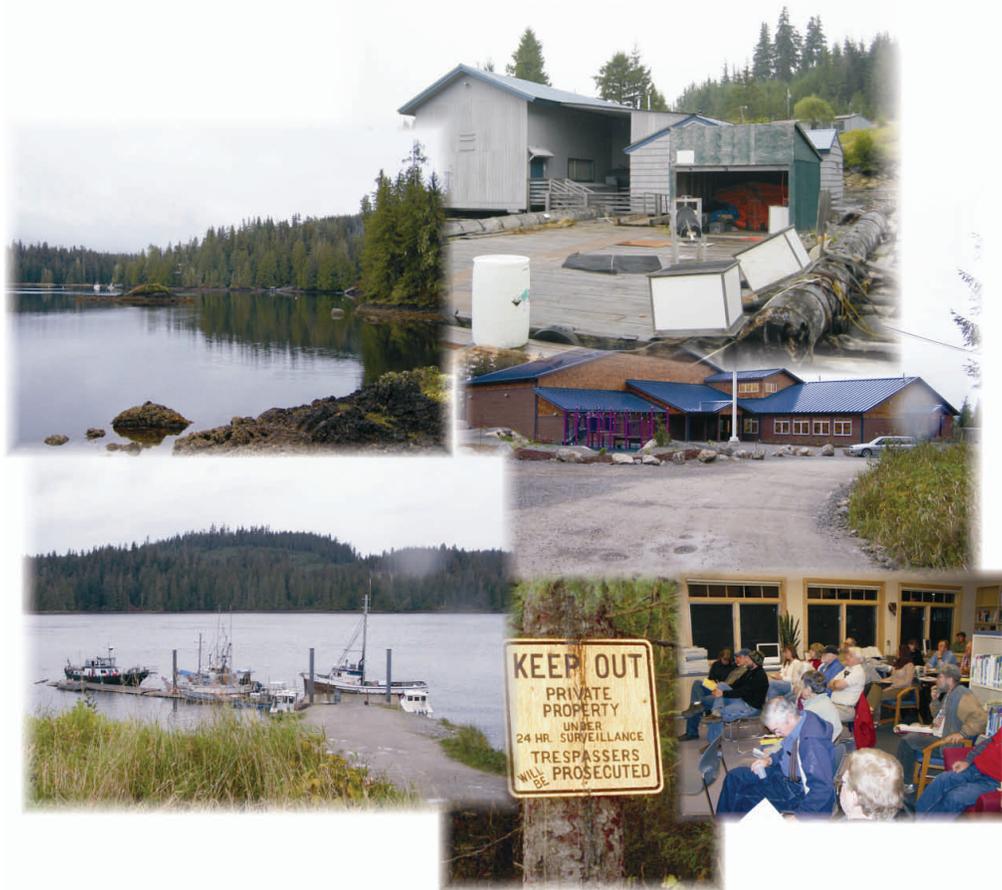




Final Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati



November 2005

Preface

State law requires the Alaska Department of Commerce, Community, and Economic Development (Commerce) to prepare both a preliminary report and a final report regarding petitions to incorporate local governments in Alaska.

Commerce's Preliminary Report on the pending Naukati city incorporation proposal was published in August 2005. The Preliminary Report examined details concerning the city incorporation proposal in the context of the relevant standards set out in law.

The principal focus of this Final Report is to examine any timely comments received regarding Commerce's preliminary report and address any relevant developments that have occurred since the Preliminary Report was published.

Documents relating to the city incorporation proposal have been made available for public review at the Naukati Store and Post Office. Materials have also been available on the Internet at:

http://www.commerce.state.ak.us/dca/lbc/naukati_bay.htm

Commerce complies with Title II of the Americans with Disabilities Act of 1990. Upon request, this report will be made available in large print or other accessible formats. Requests for such should be directed to the Local Boundary Commission staff at 907-269-4560.

TABLE OF CONTENTS

PART I BACKGROUND	1
PART II DEVELOPMENTS SINCE PUBLICATION OF COMMERCE’S PRELIMINARY REPORT	4
A. Introduction	4
B. Public Informational Meeting Regarding Proposed Incorporation	4
C. Comments on Preliminary Report	5
D. Scheduling and Notice of December 12, 2005, LBC Tour, Hearing, and Decisional Meeting	6
E. Notice to Petitioner and Respondent Regarding Preparation of Witness Lists	7
PART III SUMMARY OF INFORMATIONAL MEETING	8
A. Introduction	8
B. Summary of Informational Public Meeting	8
PART IV SUMMARY OF COMMENTS ON COMMERCE’S PRELIMINARY REPORT	12
A. Introduction	12
B. Summary of the Comments	12
1. Objection to inclusion of East Naukati within the proposed city boundaries.	12
2. Continued opposition to inclusion of Sarkar Cove in the boundaries of the proposed city	16
3. Support for an alternative boundary proposal that excludes only Sarkar Cove	18
4. Matters relating to the fiscal viability of the proposed city.	19
PART V FURTHER ANALYSIS OF BOUNDARY AND FISCAL ISSUES	24
A. Introduction	24
B. Further Examination of Boundary and Fiscal Issues	24
1. The most suitable boundaries of the proposed city.	24
2. The fiscal viability of the proposed city.	37
PART VI FINAL CONCLUSIONS AND RECOMMENDATIONS	57
A. Introduction	57
B. Final Conclusions	57
1. Final conclusions regarding boundaries of the territory petitioned for incorporation	57
2. Final conclusions regarding the fiscal viability of the proposed city.	58
3. Final conclusion regarding the size and stability of the territory recommended for incorporation.	59
4. Final conclusion regarding the need for city government.	59
5. Final conclusion regarding feasibility of services through annexation to an existing city.	59

Table of Contents continued on next page

Table of Contents (continued)

6. Final conclusion regarding the best interests of the State.....	59
7. Final conclusion regarding transition to city status.	60
8. Final conclusion regarding effect on civil and political rights.....	60
C. Final Recommendations	60
APPENDIX A TIMELY COMMENTSON COMMERCE’S PRELIMINARY REPORT	A-1
APPENDIX B COMMENTS FROM UNIVERSITY OF ALASKA OFFICE OF LAND MANAGEMENT	B-1
APPENDIX C ANALYSIS OF NAUKATI SHELLFISH NURSERY BY COMMERCE’S OFFICE OF ECONOMIC DEVELOPMENT	C-1
APPENDIX D PETITIONER’S FURTHER BUDGET REVISIONS (RECEIVED OCTOBER 31, 2005)	D-1
APPENDIX E COMMENTS FROM THE OWNER OF NAUKATI CONNECTION REGARDING 2004 GROSS SALES AND PROJECTED 2005 GROSS SALES.....	E-1

PART I

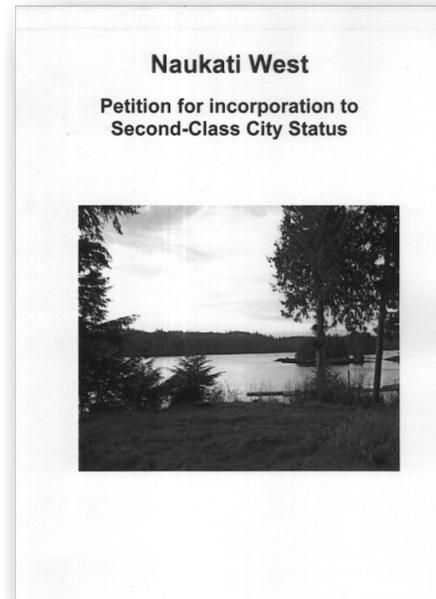
BACKGROUND

Thirty-six qualified voters in Naukati, a settlement on the northwest coast of Prince of Wales Island in southeast Alaska, collectively petitioned the Alaska Local Boundary Commission (hereinafter “Commission” or “LBC”) in 2004 to incorporate a general law, second-class city government. That group of voters is referred to in this report as the Petitioner. The Petitioner’s designated spokesperson is referred to as the Petitioner’s Representative. The terms “Petitioner” and “Petitioner’s Representative” are used interchangeably in this report.

The Petitioner and the Alaska Department of Commerce, Community, and Economic Development (hereinafter “Commerce”) provided extensive public notice of the filing of the incorporation proposal. The notice invited interested individuals, groups, and organizations to file responsive briefs and written comments regarding the Petition.

One individual, Scott Van Valin, filed a “Respondent’s Brief in Opposition to the Proposed Incorporation of Naukati as a Second Class City in the Unorganized Borough” (hereinafter “Responsive Brief”). By doing so, Mr. Van Valin became a formal Respondent in these proceedings. Mr. Van Valin and his wife are owners of the El Capitan Lodge at Sarkar Cove in the northern portion of the territory proposed for incorporation.

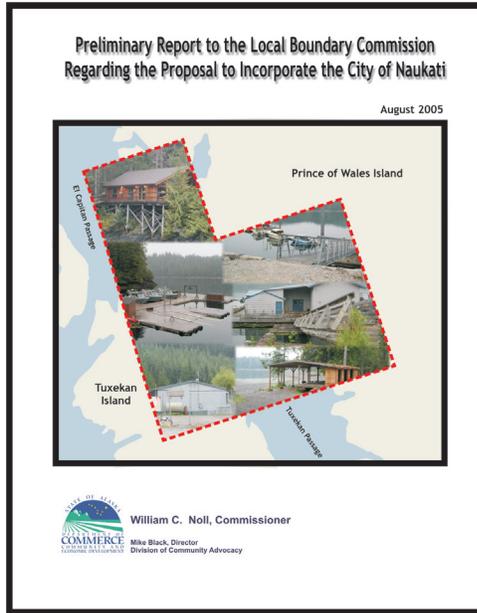
Additionally, Mr. Van Valin and several other Sarkar Cove property owners submitted written comments regarding the Petition. They are referred to in this report as “Commenters on the Petition,” and consist of the following: 1) A.L. and Dolores Donnelly; 2) Scott Van Valin; 3) Vern and Sue Bauer; 4) Roland Nehring; and 5) Morris and Verna Ververs.



Petition for Incorporation of the City of Naukati

The Petitioner's Representative subsequently prepared and submitted a Reply Brief to address the written comments and issues raised by the Respondent and Commenters on the Petition.

In its capacity as staff to the Local Boundary Commission, Commerce is required to prepare both a preliminary report and final report to the LBC regarding city incorporation proposals (AS 29.05.080(c) and 3 AAC 110.530). After reviewing the record in these proceedings (i.e., Petition, Responsive Brief, written comments on the Petition, and Reply Brief), and conducting independent research and analysis, Commerce prepared and published its *Preliminary Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati* (hereinafter "Preliminary Report"). The Preliminary Report, published in August 2005, consisted of 196 pages of background, analysis, supporting information, and recommendations.



Commerce's August 2005 Preliminary Report

Commerce concluded in its Preliminary Report that the 44-square mile area petitioned for incorporation included substantial territory that did not satisfy the boundary standards articulated in law. Consequently, Commerce recommended in its Preliminary Report that the proposed jurisdictional territory of the prospective city be reduced by roughly two-thirds.

Although Commerce's preliminary boundary recommendation encompassed Naukati Bay Subdivision East, Commerce expressed hesitation regarding that initial recommendation. Specifically, Commerce stressed on page 91 of its Preliminary Report that there is

. . . room for debate whether Naukati Bay Subdivision East can, in certain respects, be reasonably considered to be part of the community of Naukati as determined under the somewhat narrow legal standards set out in 3 AAC 110.920.

The Preliminary Report also raised significant concerns regarding the fiscal viability of the proposed city and concluded that a local tax may be necessary.

This *Final Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati* (hereinafter "Final Report") is intended to be read in conjunction with Commerce's Preliminary Report.

Within this Final Report, Commerce addresses developments regarding the Naukati proposal that have occurred since the Preliminary Report was issued. Included is a summary of the public informational meeting conducted in accordance with AS 29.05.080(a) and 3 AAC 110.520(a) by Commerce in Naukati on October 4, 2005. The Final Report also addresses timely comments regarding Commerce's Preliminary Report. Further analysis is also provided regarding fiscal and boundary issues related to the proposed city government. Lastly, the Final Report outlines Commerce's final written conclusions and recommendations to the LBC regarding the proposed incorporation of the City of Naukati.

PART II

DEVELOPMENTS SINCE PUBLICATION OF COMMERCE'S PRELIMINARY REPORT

A. Introduction

This section of the Final Report addresses significant developments regarding the Naukati city incorporation proposal since Commerce's Preliminary Report was issued in August 2005.

B. Public Informational Meeting Regarding Proposed Incorporation

State law (AS 29.05.080 and 3 AAC 110.520) requires Commerce to hold at least one public informational meeting in the area proposed for incorporation. In this case, the requisite meeting was scheduled to be held in the new Naukati School on October 4, 2005, beginning at 7 p.m.

Notice of the informational meeting was mailed by Commerce on September 8, 2005, to 58 individuals, groups, and organizations including the Petitioner's Representative, the Respondent, and the five Commenters on the Petition.

On September 10, as directed by Commerce, the Petitioner's Representative posted notice of the informational meeting at the following prominent locations readily accessible to the public within the territory proposed for incorporation:

1. Naukati Connection Store and Post Office bulletin board;
2. Naukati church bulletin board;
3. Naukati Cabins laundromat bulletin board; and
4. Naukati School bulletin board.

Commerce arranged for notice of the meeting to be published in the *Island News* on September 19 and 26, 2005, and in the *Ketchikan Daily News* on September 20 and 27, 2005.

Commerce convened the duly noticed public informational meeting at the scheduled time, date, and place. Commerce is required by law to include a summary of the informational meeting in this Final Report (3 AAC 110.520). That summary is provided in Part III.

C. Comments on Preliminary Report

The deadline for receipt of comments on Commerce’s Preliminary Report was 9 a.m., October 12, 2005. Eighteen individuals, groups, and organizations filed timely written comments. The correspondents are referred to in this report as “Commenters on the Preliminary Report” and are identified in Table 1.

Table 1. Listing of Written Comments on Commerce’s Preliminary Report

Commenter and Self-Described Affiliation	Date Received	Length of Comments
Ed and Chyral Berney, East Naukati landowners	October 12, 2005 ¹	one page
Larry Wilkinson, East Naukati landowner (handwritten letter)	October 12, 2005	one page
Larry Wilkinson, East Naukati landowner (typewritten letter)	October 12, 2005	one page
Art King, Petitioner’s Representative	October 11, 2005	seven pages
Art King, President, Naukati West, Inc.	October 11, 2005	one page
Claire King, Naukati community member and landowner	October 11, 2005	one page
Patrick and Leeann Thurston, East Naukati landowners	October 9, 2005	one page
Norman and Brenda Coon, East Naukati landowners	October 9, 2005	one page
Robert and Isabel Huestis, East Naukati landowners	October 8, 2005	three pages
Arlyn and Dolores Donnelly, Sarkar Cove residents	October 8, 2005	one page
Vern and Sue Bauer, Sarkar Cove residents	October 8, 2005	one page
Teresa Baskett, President and Agent of East Naukati Community Association	October 8, 2005	two pages
Morris and Verna Ververs, Sarkar Cove homeowners	October 7, 2005	one page
H. Clay Keene, Attorney representing Respondent Scott Van Valin	October 7, 2005	four pages
Robert Schmidt, East Naukati property owner	October 6, 2005	one page
Jerry Hermanson, East Naukati property owner	October 6, 2005	one page
Ruth Ann Albright, Sarkar Cove property owner	October 6, 2005	one page
Roland and Betsy Nehring, Sarkar Cove property owners	September 25, 2005	one page

¹ The comments are dated “10-11-05” and a heading appears on the comments indicating that they were faxed “OCT-13-2005 08:25 AM;” however, the comments were received on October 12, 2005 before the 9 a.m. deadline.

State law (3 AAC 110.530) provides, "In its final written report with recommendations, the department shall consider timely submitted written comments addressing the preliminary report with recommendations." Commerce addresses the written comments in Part IV of this report.

D. Scheduling and Notice of December 12, 2005, LBC Tour, Hearing, and Decisional Meeting

The LBC will conduct a public hearing in Naukati regarding the city incorporation proposal. The hearing is scheduled to be held in the Naukati School Library on Monday, December 12, 2005, beginning at 7 p.m.² Immediately following the hearing, the LBC may convene a decisional meeting under 3 AAC 110.570 to act on the Petition.

Circumstances permitting, the LBC will tour the territory proposed for incorporation before the hearing. The tour is scheduled to be conducted by automobile leaving Naukati Cabins at 8:00 a.m., December 12, 2005.

Formal notice of the tour, hearing, and decisional meeting has been given by Commerce under 3 AAC 110.550. Arrangements have been made for publication of the notice as a display advertisement in the *Island News* on October 31, November 7, and November 28, 2005. Publication of the notice in the *Ketchikan Daily News* has been arranged for October 28, November 9, and November 30, 2005.

Beginning October 26, 2005, the notice of the tour, hearing, and decisional meeting was posted on the Internet through the State's *Online Public Notice* system³ and on the LBC Web site.⁴

² 3 AAC 110.550(d) provides that the Commission may postpone the time or relocate the place of the hearing by conspicuously posting notice of the postponement or relocation at the original time and location of the public hearing, if the hearing is relocated within the same community or territory and is rescheduled no more than 72 hours after the originally scheduled time.

³ <http://notes3.state.ak.us/pn/pubnotic.nsf>

⁴ http://www.commerce.state.ak.us/dca/lbc/naukati_bay.htm

**State of Alaska
Local Boundary Commission (LBC)**

**Notice of Tour, Public Hearing, and Decisional Meeting
Regarding Naukati City Incorporation Proposal**

On the date and at the time and place noted below, the LBC will meet to conduct a public hearing under 3 AAC 110.560 regarding the Petition for incorporation of the City of Naukati as a second-class city:

**Monday, December 12, 2005 – 7:00 p.m.
Naukati School Library
Naukati, Alaska**

Immediately following the hearing, the LBC may convene a decisional meeting under 3 AAC 110.570 to act on the Petition.

Circumstances permitting, the LBC will tour the territory proposed for incorporation before the hearing. The tour is planned to be conducted by automobile leaving Naukati Cabins at 8:00 a.m., December 12, 2005.

Individuals with disabilities who need reasonable accommodations to participate at the hearing should contact LBC staff by December 1, 2005. Additional information concerning the tour, hearing, decisional meeting, and other aspects of the incorporation proposal may be obtained from:

LBC Staff
Department of Commerce, Community, and Economic Development
550 W. 7th Avenue, Suite 1770
Anchorage, Alaska 99501-3510
Telephone: (907) 269-4560
Fax: (907) 269-4539
E-mail: LBC@commerce.state.ak.us

A public hearing on the Naukati city incorporation proposal will be conducted by the LBC on December 12, 2005.

As required by 3 AAC 110.550, notice of the hearing was mailed to the Petitioner's Representative and the Respondent on October 25, 2005. In a letter dated October 25, 2005, the Petitioner's Representative was also directed by Commerce to post the notice in four designated public and prominent locations within the territory proposed for incorporation. The Petitioner's Representative was further directed to place a copy of the notice with the Petition materials available for public review at the Naukati Connection Store and Post Office.



The LBC hearing on the proposed incorporation will be held in the new Naukati School.”

On October 25, 2005, Commerce submitted to KRBD-FM, a Ketchikan-based radio station serving outlying areas including Naukati, a request to broadcast public service announcements of the hearing notice.

On October 26, 2005, Commerce mailed the hearing notice to 43 other individuals, groups, and organizations. All those who submitted written comments on the Petition and/or Commerce's Preliminary Report received the notice. Commerce also sent the hearing notice by e-mail to 129 individuals, groups, and entities that were subscribers at that time to the general LBC notice service available through the LBC's Web site.

E. Notice to Petitioner and Respondent Regarding Preparation of Witness Lists

On October 25, 2005, Commerce wrote to the Petitioner's Representative and the attorney for Respondent Scott Van Valin to remind those two parties that State law (3 AAC 110.550(e)) requires each to provide Commerce with a list of any witnesses that the party intends to call to provide sworn testimony at the December 12 hearing. The list must be received by Commerce no later than 4:30 p.m., Monday, November 28, 2005.

The witness list must include the name and qualifications of each witness, the subjects about which each witness will testify, and the estimated time anticipated for the testimony of each witness. On the same date the party submits its witness list to Commerce, that party must provide a copy of its witness list to the other party in this matter by hand-delivery or postage-prepaid mail.

PART III

SUMMARY OF INFORMATIONAL MEETING

A. Introduction

This section summarizes the informational public meeting conducted by Commerce in Naukati in accordance with AS 29.05.080(a) and 3 AAC 110.520(a).

B. Summary of Informational Public Meeting



The October 4, 2005 informational meeting was held in the Naukati School

On October 4, 2005, Commerce conducted a duly noticed public informational meeting concerning the Naukati city incorporation proposal. The meeting began at 7 p.m. in the Naukati School Library. Approximately 35 persons attended the meeting, which lasted approximately three hours.

The meeting commenced with Commerce's presentation of information regarding second-class cities in the unorganized borough, city incorporation standards, and city incorporation procedures. Commerce also presented an overview of its Preliminary Report. The presentation lasted approximately 45 minutes.

The presentation lasted approximately 45 minutes.

Commerce's presentation was followed by a lengthy period of public discussion. Opening questions related to photographs taken at the informational meeting and those used in Commerce's Preliminary Report. Specifically, residents inquired as to why photographs were taken of those in attendance at the informational meeting and about the source and purpose of photos used in the Preliminary Report. Commerce indicated that photographs serve as a graphic supplement within the reports. The photographs used in the Preliminary Report were obtained from various sources including the Petitioner's Representative, Commerce staff, and others.

Significant questions were raised regarding variations in population figures for Naukati. The local community, U.S. Census Bureau, and State of Alaska Demographer offer differing figures of the total number of local inhabitants. Commerce explained that discrepancies might be accounted for by differing boundaries, methods of counting residents, and resident qualifications. Naukati residents questioned why Commerce would not accept locally generated population counts. Commerce replied that it is obligated by State law (AS 29.05.080 and 3 AAC 110.530) to “investigate” every city incorporation proposal and that it is appropriate and best practice to use population figures that are established by an independent, professional, and objective source utilizing a pre-determined methodology if at all possible. Commerce recommended that if Naukati residents intend to dispute population figures used by Commerce in the Preliminary Report, they should first confer with the State Demographer.

Substantive questions were raised regarding future steps in the municipal incorporation process. Specifically, inquiries surfaced regarding the process by which the Petitioner may amend the Petition. Commerce noted that if amendments are made by the Petitioner under 3 AAC 110.540, certain additional steps must be taken. The Petitioner must prepare the formal amendments and circulate them for signature by at least the same number of qualified resident registered voters required by law to initiate a petition for incorporation of a second-class city. The amendments must include the dated signatures of at least a majority of the same voters who signed the original Petition.

Amendments by a Petitioner must be served on each person and entity designated to receive the original Petition and on the Respondent to the original Petition. The Petitioner must place a copy of the amended Petition with the original Petition documents, post public notice of the amended Petition, and submit an affidavit of service and notice in the same manner required for the original Petition.

The Chair of the LBC must then determine whether the amendments are significant enough to warrant an informational session, opportunity for further responsive briefing, an additional public meeting by Commerce, or a repeat of any other step or process in the incorporation proceedings.

Questions were also raised regarding the LBC’s decisional options. Those were described by Commerce as: 1) approval of Petition as submitted; 2) approval of the Petition with amendments and/or conditions; or 3) rejection of the Petition.

Extensive discussion occurred regarding the likely outcome of a ballot proposition that makes incorporation dependent upon voter approval of some form of local taxation. Of general concern to local residents is the assumption that voters will not approve city incorporation if it is conditioned upon voter approval of a proposition authorizing local taxation.

Responding to local taxation and other local revenue generation concerns, Commerce discussed the critical importance of evaluating the short-term and long-term financial viability of any proposed municipal government. In that context, Commerce referred to the Preliminary Report, which details contemporary accounts of the substantial number of Alaska city governments facing significant financial and managerial difficulties.

The recent elimination of State Revenue Sharing and Safe Communities funding programs and the corresponding negative impacts on local municipalities were also discussed.



Some of the estimated 35 individuals in attendance at the October 4, 2005 informational meeting

Questions were raised regarding the purpose of the State organization grant provided under AS 29.05.180 to newly incorporated cities. Specifically, residents questioned Commerce's assertion that it would be prudent to exclude consideration of the \$75,000 two-year grant from any analysis of the long-term financial viability of the proposed city. Commerce clarified its position by noting that the organization grant is a one-time funding source that is provided as a means to support a newly incorporated city during initial transition only. For example, the organization grant can provide needed revenue while a new city prepares to collect and administer local taxes. Therefore, Commerce stressed that the organization grant should not be included in any evaluation of a municipality's long-term financial viability.

There was also significant discussion regarding the future funding of National Forest Receipts and federal Payments in Lieu of Taxes. Commerce outlined contingencies in which the prospective City of Naukatu could receive substantially less funding under those programs than is currently projected. Commerce identified two plausible scenarios for significant funding reductions and one scenario in which the prospective city's funding would be eliminated altogether. One scenario involves the failure of Congress to reauthorize the current program funding level for the National Forest Receipts program. That funding level is scheduled to expire in the federal fiscal year ending September 30, 2006 and there is no guarantee that they will be renewed without cutbacks. Another scenario involves the prospect for annexation of nearly 5,000 square miles to the Ketchikan Gateway Borough. The final scenario involves incorporation of a Prince

of Wales region borough, which would render the City of Naukati and all other city governments within the borough ineligible for both National Forest Receipts and federal Payment in Lieu of Taxes funding.

One of the greatest concerns shared by many Naukati residents at the meeting was the potential for local taxation. As previously noted, local residents expressed reservations regarding any proposal that conditions incorporation upon voter approval of a proposition to authorize local taxes.

One approach presented and supported by multiple residents included levying a tax that burdens visitors rather than local residents (e.g., bed tax). Within the context of minimizing the need for locally generated revenue, one resident inquired about the plausibility of incorporating a second-class city that provides no services. Commerce replied that although State law does not require a second class city to offer any particular service, the legal standards for city incorporation require that a need for city government exist in the community. Commerce questioned how that particular standard could be satisfied if it were proposed that the prospective city would provide no local service.

El Capitan Lodge owner, Scott Van Valin, spoke directly to resident comments regarding the possibility of taxing “outsiders”. He described the lengthy history of the Lodge’s existence in Sarkar Cove and spoke about the lack of a common community between Sarkar residents and the greater Naukati community. Mr. Van Valin expressed discontent over being targeted as the lone major contributor of local operating revenue for the prospective city.

There were multiple inquiries regarding balancing and evaluating the current need for local government versus the probability of the city’s long-term financial viability. In response, Commerce referenced the need and legal obligation to evaluate the Naukati incorporation petition within the context of satisfying multiple pre-determined incorporation standards including provisions for community existence, boundaries, resources, population size and stability, need for city government, best interests of the state, transition resources, and non-discrimination.

PART IV

SUMMARY OF COMMENTS ON COMMERCE'S PRELIMINARY REPORT

A. Introduction

State law (3 AAC 110.530(d)) requires that, in the preparation of this Final Report, Commerce consider timely written comments on its Preliminary Report in the preparation of this Final Report. As noted in Table 1, Part II of this report, there were eighteen Commenters on the Preliminary Report. The comments are included in this Final Report as Appendix A. Those comments are summarized below.

B. Summary of the Comments

Comments on the Preliminary Report focused on the following four principal topics:

1. objection to inclusion of East Naukati within the boundaries of the proposed city;
2. continued opposition to inclusion of Sarkar Cove within the boundaries of the proposed city;
3. support for an alternative boundary proposal that excludes only the greater Sarkar Cove territory; and
4. matters relating to the fiscal viability of the proposed city.

Some of the eighteen Commenters offered remarks regarding more than one topic. The comments are organized and summarized below by topic. Analysis of specific issues raised in the comments is provided in Part V of this report.

1. Objection to inclusion of East Naukati within the proposed city boundaries.

Throughout the eight sets of remarks, Commenters expressed opposition to the inclusion of East Naukati (a/k/a Naukati Bay Subdivision East or Naukati East) within the boundaries of the proposed city. A summary of those remarks follows.

(a) Teresa Baskett, President and Agent of East Naukati Community Association.

The East Naukati Community Association President emphasized the fact that West Naukati and East Naukati bear different designations, reflecting that each is a discrete settlement. She notes that West Naukati and East Naukati are noncontiguous and, in fact, are eight miles apart.

Ms. Baskett emphasized that there are only five year-round East Naukati residents. She characterized East Naukati residents as being self-sufficient and having little, if any, interests in common with West Naukati residents. For example, she noted that her two daughters are educated at home and do not attend school at West Naukati. She also stated that East Naukati residents do not rely on West Naukati for services, shopping, or other fundamental needs.

She acknowledged that roads in East Naukati are in need of repair, but expressed doubt that West Naukati would or could serve that need.

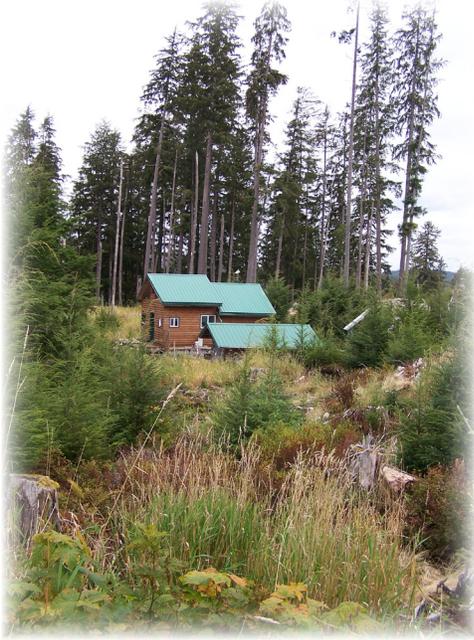
Ms. Baskett indicated that East Naukati residents share views similar to those of Sarkar Cove residents in terms of their separation from Naukati West. Specifically, she stated:

The residents of East Naukati enjoy the peace and quiet this place has to offer, the serenity of the area, the way we work together as a separate community to help each other here and also being able to live off the grid and enjoy the clear comfortable surrounding we work together to preserve.

Ms. Baskett emphasized that there is no need for city government in East Naukati. She concluded by urging the formal amendment of the Petition to exclude East Naukati from the proposed city boundaries.

(b) Ed and Chyral Berney.

Ed and Chyral Berney characterized the objectives of proponents for city government in Naukati as “honorable.” They noted that those objectives appear to include maintenance of roads and provision of other services in East Naukati. Notwithstanding, the Berneys concluded that the proposed city would lack the resources to accomplish its objectives. Consequently, they object to the inclusion of East Naukati in the proposed city boundaries.



Larry Wilkinson, whose East Naukati home is shown here, considers East Naukati to be as distinct from West Naukati as Sarkar Cove is distinct from West Naukati.

(c) Larry Wilkinson (handwritten letter).

Larry Wilkinson commented by handwritten letter that East Naukati should be excluded from the proposed city boundaries for the same reasons that Commerce recommended the exclusion of Sarkar Cove from the proposed city boundaries.

(d) Patrick and Leeann Thurston.

The Thurstons objected to the inclusion of East Naukati in the proposed city boundaries for several reasons. They cited a lack of common interests with West Naukati residents in terms of basic local services including road maintenance and utilities (i.e., electrical, water, sewer, and telephone services). They also indicated East Naukati and West Naukati are physically separated. In that regard,

the Thurstons stressed, “It takes over 30 minutes to drive to Naukati West and our boundaries don’t even touch.”

Moreover, the Thurstons indicated that they are aware of only two families who live in East Naukati year-round.

(e) Norman and Brenda Coon.

The Coons opposed inclusion of Naukati East in the proposed city boundaries for multiple reasons. Like the Thurstons, they stressed the lack of common interests between East Naukati and West Naukati in terms of basic local services. The Coons indicated that they shop in larger communities rather than at the limited facilities in West Naukati.

The Coons indicated that their greatest concern is the fear that the characteristics that make East Naukati distinct from West Naukati will be lost if the two settlements are included within the boundaries of a single city government. They further articulated that:

West Naukati should receive their city status if they qualify, but to reach out and use subdivisions miles and miles from them, to help in their qualifications, is wrong.

(f) Robert and Isabel Huestis.

Robert and Isabel Huestis offered seven distinct arguments to exclude East Naukati from the proposed city boundaries including the following assertions:

- East Naukati and West Naukati subdivisions are not contiguous;
- East Naukati is sparsely populated;
- East Naukati lacks resources that would benefit West Naukati;
- East Naukati lacks a need for city government;
- East Naukati homeowners' association will maintain roads in East Naukati;
- 95 percent of the permanent residents of East Naukati oppose incorporation; and
- East Naukati residents prefer that individual residents and property owners take responsibility for basic services.



Robert and Isabel Huestis, whose East Naukati home is shown here, contend that there are seven fundamental reasons to exclude East Naukati from the proposed city.

(g) Robert Schmidt.

Mr. Schmidt stressed that East Naukati and West Naukati are noncontiguous and it is unlikely that East Naukati would benefit from services proposed to be offered by the City of Naukati. Consequently, he urged that the boundaries of the proposed city be amended to exclude East Naukati.

(h) Jerry Hermanson.

Mr. Hermanson opposed the inclusion of East Naukati in the boundaries of the proposed city government for five particular reasons including:

- East Naukati and West Naukati are noncontiguous to one another;

- East Naukati and West Naukati are 9 miles and 25 minutes apart;
- the proposed city government would lack the capacity to provide effective fire protection to East Naukati;
- improvement of East Naukati roads by the prospective city is unlikely; and
- city incorporation will not bring about electrical utility service.

2. Continued opposition to inclusion of Sarkar Cove in the boundaries of the proposed city.

Six of the Commenters on the Preliminary Report supported Commerce’s analysis and recommendation to exclude Sarkar Cove from the boundaries of the proposed city government. A summary of those remarks follows.

(a) Respondent Scott Van Valin (by his attorney H. Clay Keene).

Mr. Van Valin endorsed the position taken by Commerce with respect to the proposed exclusion of Sarkar Cove. Specifically, he stated:

The Respondent concurs with Commerce’s conclusion that the boundaries for the proposed City of Naukati be reduced to those generally described in the Preliminary Report at page 96 in Figure 3-11, which boundaries would exclude the Sarkar Subdivision, and, in particular would exclude the El Capitan Lodge and the Sarkar Cove area from the boundaries of the proposed City of Naukati.



Respondent Scott Van Valin, whose Sarkar Cove property is shown here, concurred with Commerce that Sarkar Cove should not be included within the proposed city boundaries.

(b) Arlyn and Dolores Donnelly.

The Donnellys agreed with the analysis and conclusions in Commerce’s Preliminary Report that support the exclusion of Sarkar Cove from the proposed city boundaries. They urged the LBC to formally exclude that part of the territory proposed for incorporation when the Commission acts on the Petition.

(c) Morris and Verna Ververs.

Morris and Verna Ververs concurred with what they characterized as a “thorough and complete” Preliminary Report by Commerce regarding the proposed city incorporation. In particular, they emphasized full agreement with Commerce’s conclusion that Sarkar Cove should be excluded from the proposed city boundaries. They stressed, “the two locations are simply too far removed geographically and operationally to be a viable governance structure.”

(d) Roland and Betsy Nehring.

The Nehrings concurred with Commerce’s analysis and conclusion that Sarkar Cove should be excluded from the prospective city’s boundaries. Specifically, they stated:

. . . it is a legal, logical, and a sound financial conclusion due to our lack of community with Naukati, our separation from Naukati by uninhabited USFS lands, our seasonal occupancy, the lack of access from Naukati for emergency and other services due to distance and unimproved roads, and the potential cost for the proposed City to provide traditional facilities to our area.

(e) Vern and Sue Bauer.

The Bauers agreed with Commerce’s analysis and conclusions calling for the exclusion of Sarkar Cove from the proposed city boundaries. Specifically, they agreed with Commerce’s observations regarding the distance between Sarkar Cove and Naukati, the seasonal population at Sarkar Cove, and the lack of common interests between Sarkar Cove and Naukati.

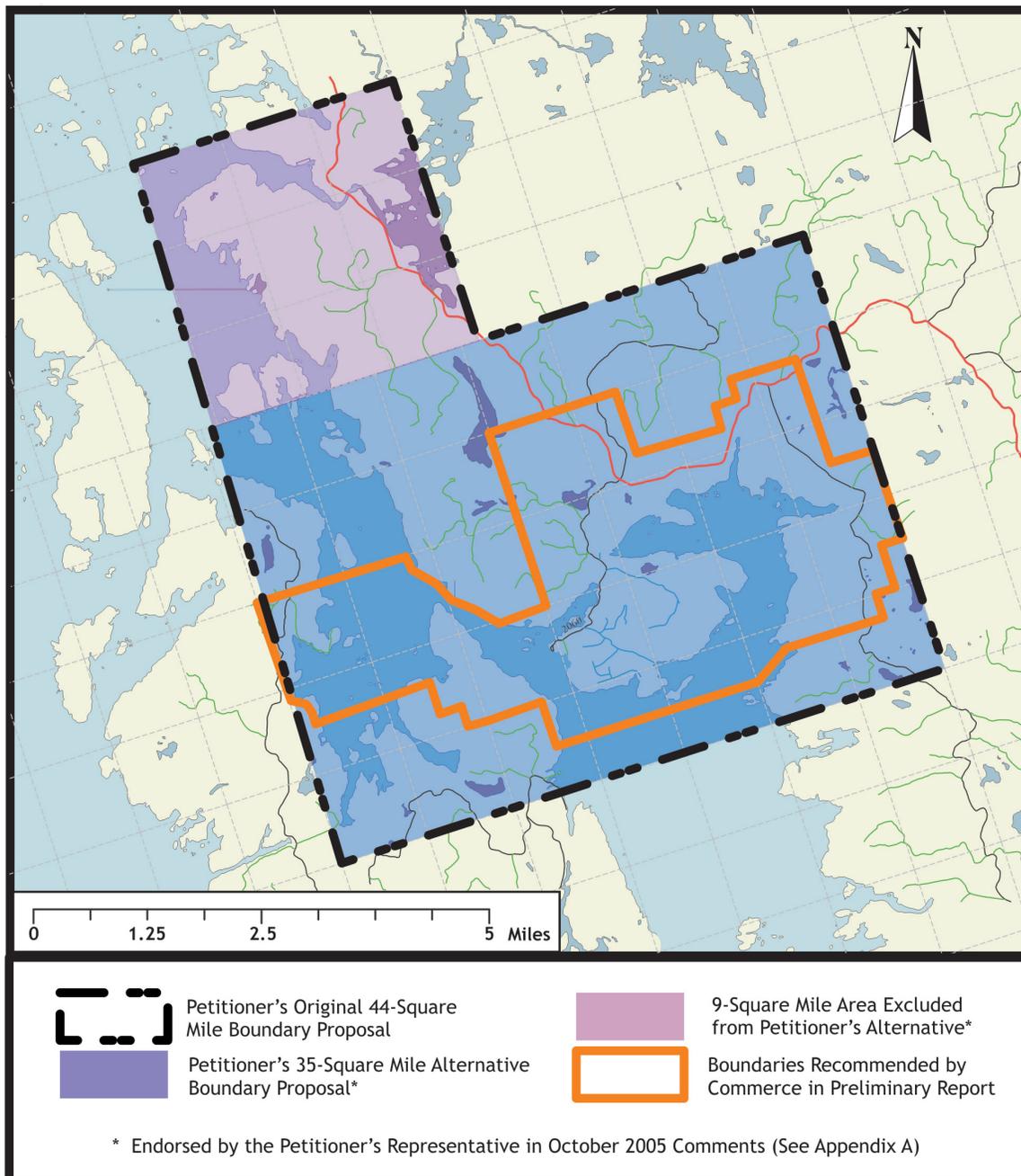
(f) Ruth Ann Albright.

Ms. Albright indicated that she perceives “no common goals or concerns between Naukati residents and Sarkar residents.” She also stated it is neither “convenient” nor “necessary” for Sarkar residents to patronize Naukati. For those reasons, she supported Commerce’s recommendation to exclude Sarkar Cove from the boundaries of the proposed city government.

3. Support for an alternative boundary proposal that excludes only Sarkar Cove.

Two Commenters advocated for more expansive city boundaries than those recommended by Commerce in its Preliminary Report. Both urged that only the nine-square mile greater Sarkar Cove territory be removed from the original 44-square mile boundary proposal. A summary of those comments follows:

Figure 1. Petitioner’s 35-Square Mile Alternative Boundary Proposal.



(a) Art King, writing as Petitioner’s Representative.

The Petitioner’s Representative offered the following three specific arguments in support of the boundary alternative encompassing 35 square miles:

The community of Naukati wishes to retain their original boundary with the exception of the portion that includes El Capitan and Sarkar (see attached map). The reasons Forest Service Lands are included are:

-The University stands to gain an equal match from the congress to match the lands conveyed from DNR. It is likely they will select near their existing entitlements.

-Sealaska still has nearly one million acres to select from the Tongass, and there is a Sealaska Heritage site near Naukati.

-The waters outside Naukati that are included in our original boundaries, but excluded from the boundary proposed by commerce, have several oyster farms. These oyster farms would be subject to a future sales tax and would contribute to the current fish tax.

(b) Claire King.

Ms. King expressed the same views as the Petitioner’s Representative in support of the alternative 35-square mile boundary alternative. Specifically, she stated:

I think that our boundary should stay the same with the exception of El Capitan/Sarkar. I would like to see that the waters we selected stay in our boundary for the shellfish farms that are here and the ones in the future.

Ms. King also provided commentary regarding the need for city government. Specifically, she stated, “As a community member and landowner of Naukati I would like to say that I think *Naukati West* needs to become a second-class city.” (Emphasis added.) It is unclear whether she meant that the need for city government in the alternative 35-square mile territory is limited to just that portion known as West Naukati.

4. Matters relating to the fiscal viability of the proposed city.

Six of the Commenters on the Preliminary Report expressed views about the fiscal viability of the proposed city. A summary of those remarks follows.

(a) Art King, writing as Petitioner's Representative.

The Petitioner's Representative emphasized that the State land grant to which the prospective city would be entitled would play a major role in assuring the fiscal viability of the proposed city.⁵ In that regard, Mr. King indicated:

Naukati will select all waterfront properties adjoining our waterfront master plan. The University of Alaska did not select any Commercial waterfront land, leaving Naukati the only owner of above-mentioned commercial land without a competitor.



To balance the budget of the proposed city, the Petitioner relies heavily on projected income from sales of land that would be granted by the State to the city.

To address fiscal concerns raised by Commerce in its Preliminary Report, on October 11, Mr. King submitted a "Revised and Amended Operating Budget."⁶ He also included certain financial records relating to the local shellfish nursery.⁷ The budget material and financial records concerning the shellfish nursery are addressed in Part V of this report.⁸

⁵ As outlined on pages 78 - 79 of Commerce's Preliminary Report, that entitlement is estimated to be 534 acres.

⁶ At the October 4, 2005 informational meeting and in correspondence dated October 7, 2005, Commerce outlined procedures for amendment of a petition by the Petitioner and, alternatively, by the LBC. The Petitioner chose not to formally amend the budget in the Petition to reflect the revised financial figures. Therefore, revised material submitted by the Petitioner's Representative is treated by Commerce strictly as suggestions from the Petitioner for revisions to the budget.

⁷ The records consisted of page one of five pages of a September 2005 bank statement for the Naukati West Shellfish Nursery and a typewritten list of accounts receivables for the nursery.

⁸ Following the October 11 submission of the "Revised and Amended Operating Budget" by the Petitioner's Representative, Commerce asked for clarification of revenue and expenditure projections relating to the shellfish nursery. In response, on October 31, the Petitioner further changed the revenue and expenditure projections relating to the shellfish nursery.

Mr. King, as Petitioner’s Representative, also argued against making incorporation conditioned upon voter approval of any tax. In that regard, he stated, “. . . we are absolutely against the tax issue and incorporation being tied together.” Mr. King stressed that profits from the shellfish nursery would provide “significant locally generated revenue.” He maintained that the question of local taxes is best left to the future city council.

(b) Art King, writing as President of the Naukati West Homeowners’ Association.

On behalf of Naukati West, Inc., Mr. King supplemented his arguments in opposition to local taxes that were expressed in his comments as Petitioner’s Representative. Specifically,

he again stressed the significance of the proposed allocation of all net income from the local non-profit shellfish nursery to support operations of the proposed city government. He indicated that nursery sales totaled one million spat in 2004 and that more than two million spat have been sold so far this year. Furthermore, Mr. King stated that the goal of the nursery is to sell four million spat by 2007. He reported that there are currently seven oyster farms in the Naukati area. Within this context, he concluded the following:



The Petitioner counts on shellfish nursery profits, in large part, to eliminate the need for local taxes.

Naukati has significant locally generated revenue in the form of the profits from the community owned shellfish nursery. Therefore at this time the tax question is not relevant to the fiscal viability of our community.

In apparent further reference to the importance of the anticipated State land grant in supporting local government operations, Mr. King stressed there has been a strong demand for real property in Naukati.

To further bolster the argument that city taxes are not necessary, Mr. King emphasized that Naukati lacks the financial burdens many city governments face with respect to supporting basic community facilities such as water and sewer utilities. Moreover, he also emphasized that no local public indebtedness exists with respect to current community facilities. Those facilities include a new \$4.1 million school⁹, a fast response vehicle, a refrigerated truck, and a new ambulance. Mr. King also noted that a new fire hall is presently under construction.

Mr. King concluded his letter on behalf of Naukati West, Inc., by stating:

I see no reason for our incorporation to be tied to any tax.

If that is a condition we have to meet I fear we will fail at the polls. Naukati is a strong community and I am confident it will become a good second-class city.

(c) Claire King.

Ms. King commented on the importance of the shellfish nursery in terms of the economic viability of the proposed city. She characterized it as a source of “great income for the community” and indicated that “it has done better than anyone hoped for in the first two years of operation.”

Ms. King also expressed the view that there is no need to require voter approval of any tax as a condition for incorporation. Specifically, she noted, “Looking at the revised budget of *Naukati West* it is apparent that the new City of Naukati would be able to prosper without a tax of any kind at this time.” (Emphasis added.) Here again, it is unclear whether her comment was intended to be an expression of views that the budget relates only to the West Naukati portion of the territory proposed for incorporation.

(d) Larry Wilkinson (typewritten letter).

Larry Wilkinson commended Art King for his leadership in West Naukati. He stressed that Mr. King’s efforts to establish an oyster nursery there have benefited that community well beyond what is reflected in the sale price of spat. In that regard, he stated that, “the wealth of the community should be measured by millions rather than pennies.” He encouraged Commerce to reflect the broader benefit to West Naukati from the nursery in its analysis of the city incorporation proposal.

⁹ The school is owned by the Southeast Island Regional Educational Attendance Area and was paid for by the State of Alaska.

(e) Ed and Chyral Berney.

The Berneys expressed the view that it appears that the proposed city will not be fiscally viable without a city property tax. They indicated there is universal local opposition to the prospect of such a tax.

(f) Respondent Scott Van Valin (by his attorney H. Clay Keene).

The Respondent agreed with Commerce that exclusion of Sarkar Cove necessitates significant revision of the Petitioner's original budget proposal. Specifically, he stated:

Respondent concurs with the proposed amendment to the Petitioner's operating budget that removes the "bed tax" revenue that would be generated by the El Capitan Lodge, located in Sarkar Cove. Removal of the El Capitan Lodge and other properties within the Sarkar Subdivision from the area proposed for inclusion within the boundaries of the proposed City of Naukati will correspondingly require revision to the operating budget of the City of Naukati that reflect those changes.

PART V

FURTHER ANALYSIS OF BOUNDARY AND FISCAL ISSUES

A. Introduction

Divergent viewpoints exist regarding two fundamental aspects of the Naukati city incorporation proposal: the most suitable boundaries and the fiscal viability of the proposed city. In Part V of this Final Report, Commerce offers its analysis of those two fundamental issues beyond the examination presented in the Preliminary Report.

B. Further Examination of Boundary and Fiscal Issues.

1. The most suitable boundaries of the proposed city.

(a) Sarkar Cove.

As reflected in Part IV-B-2 of this Final Report, Sarkar Cove property owners, including Respondent Scott Van Valin, have maintained from the beginning that the proper boundaries for the proposed city must exclude Sarkar Cove and the surrounding territory.

Moreover, as reflected in Part IV-B-3 of this Final Report, the October 2005 comments from the Petitioner's Representative and those of Claire King implicitly concur with the arguments calling for exclusion of a nine-square mile area encompassing greater Sarkar Cove.

No Commenter on the Preliminary Report argued that Sarkar Cove should remain within the



Sarkar Cove property owners remain adamantly opposed to the prospect of being included within Naukati city boundaries.

boundaries of the proposed city. Further, Commerce is unaware of any new evidence suggesting the recommendation in the Preliminary Report to detach Sarkar Cove from the territory petitioned for city incorporation should be altered.

Given the circumstances reflected above, Commerce affirms its conclusion in the Preliminary Report that Sarkar Cove should be excluded from the boundaries of the proposed city.

(b) Petitioner’s alternative thirty-five square mile territory.

As outlined in Part IV-B-3 of this report, the Petitioner’s Representative proposes an alternative to Commerce’s preliminary boundary proposal. The Petitioner’s alternative proposal excludes only the nine-square mile greater Sarkar Cove area from the territory originally proposed for incorporation. The map presented in this report as Figure 1 depicts the Petitioner’s original and alternative boundary proposals. It also shows Commerce’s preliminary boundary proposal.

In support of its alternative boundary scenario, the Petitioner offered three specific arguments. Those arguments are examined below.

(i) Anticipated federal land grant for the University of Alaska.

Federal legislation in 1915 and 1929 granted approximately 360,000 acres of federal land to the University of Alaska. The land had to be surveyed prior to conveyance.

When Alaska became a state in 1959, much of the University’s entitlement lands remained unsurveyed. The Alaska Statehood Act extinguished all existing designated claims on unsurveyed lands.

The University of Alaska ultimately received title to roughly 112,000 acres of federal land. However, the University’s remaining entitlement to roughly 250,000 acres was extinguished at the time of statehood.¹⁰

Although more than two-thirds of the University’s direct federal land entitlement was lost, the Alaska Statehood Act authorized the State of Alaska to select more than 103 million acres of federal land.

¹⁰ Statement of the University of Alaska President regarding H.R. 2958 before the Committee on Resources, United States House Of Representatives, October 27, 1999.



As indicated in the Preliminary Report, earlier this year the Alaska Legislature enacted a law granting 250,000 acres of State land to the University. That legislation was signed into law by Governor Murkowski on July 25, 2005, as Chapter 8 FSSLA 2005. Of the 250,000 acres in question, the law conveyed the University 937 acres within the territory proposed for incorporation.



The University of Alaska addressed the potential for selection of federal lands within the territory proposed for incorporation (see Appendix B).

In support of its alternative boundaries, the Petitioner asserts that the University of Alaska can be reasonably expected to receive a federal land grant equal to the recent 250,000 State grant. Moreover, the Petitioner argues that, under the anticipated additional federal land grant, the University will likely select federal lands within the territory proposed for incorporation.

To evaluate the Petitioner’s argument, Commerce conferred with Mari Montgomery, Director of the Office of Land Management for the University of Alaska. In brief, Ms. Montgomery advised Commerce that attempts have been made over the past nine years to gain an additional federal land grant for the University. None of those efforts has been successful thus far.

Moreover, the Director indicated that even if such federal legislative efforts were fruitful, “It is much too early to speculate as to what specific lands the University might reasonably be expected to select.” In that regard, she noted:

... the University would have to weigh the relative value of available lands and interests in land. However, it is likely that the University’s first preference would be to select lands that would provide long-term, high-value revenue streams such as those generated by oil and gas resources. National Forest lands, with the current climate of litigation and depressed world markets, would appear to be of fairly low interest at this time.

A copy of Ms. Montgomery's response to Commerce's inquiry is included in this report as Appendix B.

Given the federal legislative history relating to this matter, Commerce does not view the prospect that Congress *might* grant an additional land entitlement to the University as a compelling reason for the alternative boundaries endorsed by the Petitioner. Even if such legislative efforts are ultimately successful, the prospect that the University, in turn, *might* select National Forest lands and that those lands *might* be within the 35-square miles in question appears to be, at best, remote.

(ii) Anticipated Sealaska Corporation land selections.

The Petitioner's second argument in support of its alternative boundary proposal is that, "Sealaska still has nearly one million acres to select from the Tongass, and there is a Sealaska Heritage site near Naukati."

"Sealaska," of course, refers to Sealaska Corporation, the southeast Alaska regional Native corporation formed under the Alaska Native Claims Settlement Act (ANCSA). Sealaska's unfulfilled land entitlement is far less than the one million acres suggested by the Petitioner. According to the U.S. Forest Service,¹¹ Sealaska has a remaining ANCSA land entitlement of 22,250 acres, plus an anticipated additional entitlement of 40,000 acres or more from a statewide settlement of remaining ANCSA entitlement lands among all regional corporations.

In August 2002, Sealaska submitted a proposal to the U.S. Forest Service to exchange approximately 100,000 acres of National Forest lands for Sealaska lands and selection rights under ANCSA.

The proposed land exchange involved lands throughout the Tongass National Forest. Resolution of Sealaska's remaining ANCSA land entitlement would remove its selection rights in existing ANCSA withdrawal areas. The Sealaska land selections are an encumbrance that restricts Forest Service management on over 171,000 acres of the Tongass National Forest.

In 2003, the Forest Service drafted a feasibility report of the proposed land exchange. In that context, the Forest Service entered into discussions with Sealaska in an attempt to craft a mutually acceptable proposal. However, that effort failed to achieve its goal.

¹¹ See http://www.fs.fed.us/r10/tongass/forest_facts/faqs/sealaska.shtml. Additional information was obtained from Barbara Stanley of the U.S. Forest Service.



The Forest Service estimated that the Sealaska proposal would cause a net loss of old growth timber reserves of about 28,000 acres. The Forest Service concluded that there would also be a reduction of about 12% of the Tongass allowable timber sale quantity. In order to compensate for the loss of old growth reserve acres, the Forest Service concluded that areas of development land use designations would likely be further precluded from timber production. That would further reduce the allowable sale quantity of timber.

The Forest Service reasoned that impacts from the loss of available timber could have a significant adverse effect on the timber mills on Prince of Wales Island and surrounding areas. In addition, the Forest Service noted that the Sealaska proposal did not guarantee protection of heritage resources; nor were karst and cave resources necessarily protected. Moreover, there were no provisions in the Sealaska proposal that would allow for continued access to lands for subsistence and community recreation purposes.

In January 2005, the Forest Service indicated it was unwilling to agree to the Sealaska proposal because it would require a complete revision of the *Tongass National Forest Land and Resource Management Plan*. Forest Service officials indicated further that the proposal had little, if any, support from local communities and could result in further declines in the current timber industry dependence on the Tongass National Forest.

According to Forest Service officials, except for heritage sites, Sealaska has no prospective land selections around Naukatu. Sealaska was required to select land within the same area as the Native village corporations. Thus, Sealaska's closest selections to Naukatu are near Craig and Klawock.

Tongass National Forest Land And Resource Management Plan	
Table of Contents	
Chapter 1 - Introduction	1-1
Chapter 2 - Goals and Objectives	
Forest Desired Conditions	2-1
Forest-wide Multiple-use Goals and Objectives	2-2
Chapter 3 - Management Prescriptions	
Introduction	3-1
Land Use Designation Acreage	3-2
Special Designations or Classifications	3-2
Wilderness	3-7
Wilderness National Monument	3-23
Nonwilderness National Monument	3-40
Research Natural Area	3-49
Special Interest Area	3-55
Remote Recreation	3-62
Municipal Watershed	3-68
Old-growth Habitat	3-75
Semi-remote Recreation	3-82
Land Use Designation II	3-88
Wild River	3-94
Scenic River	3-102
Recreational River	3-110
Experimental Forest	3-118
Scenic Viewshed	3-124
Modified Landscape	3-133
Timber Production	3-141
Minerals	3-148
Transportation and Utility System	3-155
Chapter 4 - Forest-wide Standards and Guidelines	
Introduction	4-1
Air	4-3
Beach and Estuary	4-4
Facilities	4-6
Fire	4-7
Fish	4-8
Forest Health	4-13
Heritage Resources	4-14
Karst and Caves	4-18
Lands	4-21
Minerals and Geology	4-32

Forest Service officials opposed the Sealaska land transfer proposal, in part, because it would have required comprehensive revisions to the May 1997 *Tongass National Forest Land and Resource Management Plan*.

In Commerce's view, the arguments advanced by the Petitioner regarding prospective Sealaska selections do not offer a substantive basis for municipal boundary adjustments in these proceedings.

Another element of the Petitioner's second argument concerns the existence of a Sealaska heritage site within that territory included in the Petitioner's alternative boundary proposal but outside Commerce's preliminary proposal.

The Petitioner merely notes correctly that such a site exists. The Petitioner offers no explanation or justification of the need for municipal jurisdiction over that site.

The U.S. Forest Service has, in fact, identified six Sealaska heritage sites around the greater Naukati area. One of the sites is within the boundaries recommended by Commerce in the Preliminary Report. The 35-square mile territory currently proposed by the Petitioner contains another site. Four other sites are outside the Petitioner's proposed boundary.

If Commerce had perceived a particular need for city jurisdiction over the Sealaska heritage sites around Naukati, it would have recommended such.

(iii) Oyster farms.

The Petitioner's third argument in support of its alternative boundary proposal is that, "the waters outside Naukati that are included in our original boundaries, but excluded from the boundary proposed by commerce, have several oyster farms." The Petitioner reasons that those oyster farms "would be subject to a future sales tax and would contribute to the current fish tax."

There appear to be three shellfish farms within the original territory proposed for incorporation. All three are also within the Petitioner's alternative 35-square mile boundary proposal. Those three farms encompass a total of 10.28 acres.

Only one of the three farms is within the boundaries recommended by Commerce in the Preliminary Report. That farm encompasses 4.06 acres. Thus, there are two farms in the Petitioner's alternative boundary proposal that are not within Commerce's preliminary proposal.

With regard to the prospect for the levy of a future sales tax on oyster farms, Commerce notes that any business, including oyster farms, operating within the jurisdiction of a city that levies a sales tax is subject to that tax. However, Commerce has strong reservations over any suggestion that goods and services sold or delivered outside the boundaries of a taxing jurisdiction are subject to a sales tax levied by that jurisdiction. Commerce believes that, in order for a sales

transaction to be taxable, there must be a nexus between the taxing jurisdiction and the transaction. In that respect, McQuillin, a generally accepted treatise on municipal law, states as follows (Section 44.195.10):

Transactions in interstate or foreign commerce are not taxable, unless the tax is applied to an activity with a substantial nexus with the taxing state, and under some laws, a tax may not be imposed on sales for delivery to customers outside the city. However, sales of automobiles delivered to nonresident buyers across municipal boundary lines for the purpose of avoiding the municipality's sales tax are subject to such tax where all other details of the sale had been transacted within such municipality.

Most, if not all, sales of shellfish by the farms in Naukati would likely occur outside the boundaries of the proposed city (e.g., Craig, Ketchikan, Juneau, Anchorage, and other communities). Thus, the potential loss of future sales tax revenues that would result from the exclusion of the oyster farms in question is likely to be *de minimis*.



The Naukati shellfish nursery serves oyster farms in the Naukati area and beyond.

The Petitioner's comment in its third argument regarding the "current fish tax" refers to the State Fisheries Business Tax levied under AS 43.75.015. That tax is levied upon fisheries businesses and persons who *process or export fisheries resources from Alaska*. The tax is based on the fisheries value paid to commercial fishers or fair market value when there is not an arms length transaction. The Fisheries Business Tax is collected primarily from licensed processors and persons who export fish from Alaska.

In the case of shellfish, the amount of the State Fisheries Business Tax is 3 percent of the value of the fisheries resources. Under AS 43.75.130, the State pays each city government in the unorganized borough one-half of Fisheries Business Tax revenue collected within the boundaries of the city. Thus, the prospective City of Naukati would be entitled to a share of State Fisheries Business Tax revenue that would equal 1.5 percent of the value of any shellfish "processed" within the boundaries of the City of Naukati or exported from Naukati to areas outside the State of Alaska.

Commerce conferred with officials of the Alaska Department of Revenue, the agency that administers the State Fisheries Business Tax. According to Revenue officials, none of the shellfish farms in the territory proposed for incorporation report activities that are taxable under the State Fisheries Business Tax. In other words, those farms did not “process” oysters or export them from Alaska. The Naukati farms harvest the shellfish and ship them elsewhere for processing. Unless that changes, the prospective City of Naukati stands to gain no revenue from the shared State Fisheries Business Tax on shellfish.¹²

Based on the foregoing analysis, Commerce does not find merit in the Petitioner’s arguments for the 35-square mile boundary proposal. It is stressed here that municipal boundary determinations must be based on legal standards. If maximization of revenues were a standard, Commerce would have endorsed the original 44-square mile boundary proposal encompassing the El Capitan Lodge.

(c) East Naukati.

Commerce concluded in its Preliminary Report (page 91) that given the applicable legal standards for city incorporation,¹³ reasonable arguments could be made that East Naukati does not belong within the boundaries of the proposed city because it is not part of the West Naukati community. In that regard, Commerce stressed that Naukati Bay Subdivision East was “distant and removed” from West Naukati.

¹² The State Fisheries Business Tax program discussed here is distinct from the program administered by Commerce to share taxes collected from fishery resources with eligible municipalities. The money shared under the Commerce program is collected by Department of Revenue, but is then transferred in part to Commerce for distribution to eligible municipalities. The purpose of that program is to help municipalities impacted by the effects of the fish processing industry by sharing fish taxes. The Petitioner estimates that the prospective City of Naukati would receive \$2,928 annually under the program administered by Commerce. As noted in the Preliminary Report, Commerce considers that estimate to be reasonable.

¹³ In particular, 3 AAC 110.920(a) states:

In determining whether a settlement comprises a community, the commission may consider relevant factors, including whether the

- (1) settlement is inhabited by at least 25 individuals;
- (2) inhabitants reside permanently in a close geographical proximity that allows frequent personal contacts and comprise a population density that is characteristic of neighborhood living; and
- (3) inhabitants residing permanently at a location are a discrete and identifiable social unit, as indicated by such factors as school enrollment, number of sources of employment, voter registration, precinct boundaries, permanency of dwelling units, and the number of commercial establishments and other service centers.

Commerce further concluded in the Preliminary Report (page 51) that East Naukati was sparsely populated. It had no more than six inhabitants at the time of the 2000 Census. Since East Naukati is not a census designated place, a more contemporary official population figure for the settlement does not exist. Nonetheless, Commerce stressed in the Preliminary Report (page 91) that five years after the last federal census, the current population of East Naukati remained, at best, of moderate size.

Commerce noted further in the Preliminary Report that there was little or no commercial and industrial development in East Naukati. Additionally, that report indicated that separate incorporated homeowners associations represented East Naukati and West Naukati.

Notwithstanding the observations regarding East Naukati, the Preliminary Report stopped short of calling for detachment of East Naukati from the boundaries of the proposed city. The standards governing city boundaries allow flexibility in terms of including marginally connected areas within the boundaries of a city if such is justified in terms of other standards for incorporation. (See, in particular, 3 AAC 110.040(c)).



The President of the East Naukati homeowners association recently indicated that roads in the Naukati Bay Subdivision East are in "dire need of new ballast."

When the Preliminary Report was prepared and published, East Naukati residents and property owners had expressed no objection whatsoever to inclusion of East Naukati within the boundaries of the proposed city.¹⁴ Commerce hesitated to recommend detachment of East Naukati because it may have foreclosed what Commerce considered to be the best (perhaps only) opportunity in the foreseeable future to reasonably meet East Naukati's need for local public services.

¹⁴ Early in these proceedings, the Petitioner had notified East Naukati residents and property owners of the filing of the city incorporation proposal. Exhibit D of the Petition listed 17 individuals, groups, and entities that the Petitioner felt had sufficient interest in the proceeding to warrant receipt of notice of the filing of the Petition. Six of the 17 were affiliated with East Naukati. Those were the Naukati East Homeowners Association, Tom Bouy, Adam Baskett, Jerry Hermanson, Larry Wilkinson, and Mr. and Mrs. Mosenthin. The record reflects that on May 14, 2004, notice of the filing of the Petition was mailed to the 17 individuals, groups and entities.

Several of the comments summarized in Part IV-B-1 of this report acknowledged the need for some local services, particularly road maintenance, in East Naukati. In September of this year, the East Naukati Homeowners Association applied for a \$25,000 “Mini Grant” from Commerce to “add shotrock and culverts to the existing roadways in the East Naukati Subdivision.” The grant application indicated that the roads in question were in “dire need of new ballast.” Moreover, the application indicated, “There is no available cash for this project” as matching funds. Nor was there any in-kind match offered in the September 2005 grant application.



On October 5, 2005, Commerce’s LBC staff presented information regarding a prospective Prince of Wales borough to the Prince of Wales Community Advisory Council (commonly known as POWCAC).

Applications for FY 2006 Mini Grant funding far exceeded the monies available. The East Naukati application was denied, in large part, because grant application reviewers interpreted the project as “a maintenance/repair function of the local governing body, not an economic development activity, and is therefore not an appropriate use of Mini Grant Funds.” (Letter from Jo E. Grove, Grant Manager, Commerce, September 29, 2005.)

Difficulty in meeting East Naukati service needs is the result of (1) the absence of any local government structure and (2) the lack of local funding. Hypothetically, a local government structure and funding could come in the form of either a Prince of Wales region borough or a city government.

However, absent some significant alteration of the State’s *de facto* policy regarding borough formation that has been in place in Alaska since 1964, the prospects of creating a Prince of Wales Borough are, in Commerce’s view, unlikely.¹⁵

¹⁵ For a general discussion of issues relating to borough formation, see *Report of the Alaska Local Boundary Commission to the First Session of the Twenty-Fourth Alaska State Legislature*, January 2005. For a discussion of issues relating to the formation of a Prince of Wales borough, see materials provided by LBC staff to the Prince of Wales Community Advisory Council at a meeting in Coffman Cove on October 5, 2005. Although Commerce considers it unlikely that a Prince of Wales borough will form under existing State policy; it does not necessarily consider it unlikely that the policy will change. The Advisory Commission on Local Government, which was created by the 2005 Legislature, is currently exploring changes to the existing policy regarding boroughs.

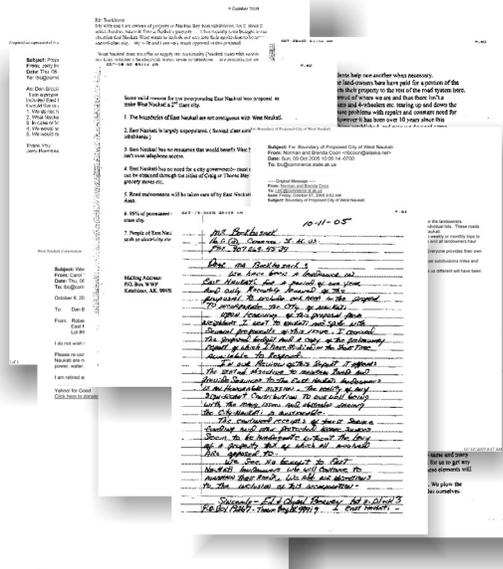


At this time, East Naukati cannot form its own city government because it clearly lacks the population, economy, and other fundamental characteristics necessary to do so. For example, a minimum of twenty-five resident registered voters is required to initiate a petition to incorporate a second-class city. Currently, East Naukati lacks the minimum number of resident voters needed to initiate a local action incorporation petition. Moreover, incorporation of a future East Naukati city government might be barred by AS 29.05.021, which prohibits formation of a new city if services can be provided by annexation to an existing city.

Thus, if East Naukati is excluded from the boundaries of the current city incorporation proposal, it is likely to remain beyond the jurisdiction of any local government in the foreseeable future. It is also likely to remain without local funding for services.

If East Naukati and its surroundings are excluded from the territory proposed for incorporation, a significant reduction in National Forest Receipts funding for the remnant city would result. Based on existing funding formulas, the loss would amount to approximately \$3,500 for each mile of road that would have otherwise been maintained by the city. Commerce does not attempt here to offer a specific estimate of such impact. However, it appears that at least one-quarter or more of the \$50,371 in National Forest Receipts funding projected for the proposed city in the Preliminary Report would be lost by such a boundary change.

Moreover, exclusion of the eastern territory proposed for incorporation would significantly reduce the prospective city's municipal land grant entitlement. As reflected in Figure 3-7 on page 78 of the Preliminary Report, nearly all of the State land in the eastern portion of the territory proposed for incorporation is classified as vacant, unappropriated, and unreserved (VUU). Since the proposed city would be entitled to a land grant of 10 percent of the State's VUU lands, removal of the eastern territory from the city's boundaries would reduce its municipal land entitlement. Again, Commerce does not attempt at this point



Comments from East Naukati residents and property owners opposing the proposed city boundary are included in Appendix A.

to offer a precise estimate of that impact. However, it appears that the City's entitlement - estimated in the Preliminary Report to be 534 acres - might be reduced on the order of at least one-third or more.

While East Naukati residents and property owners were initially silent regarding the city incorporation proposal, they have not remained quiet. Late in these proceedings, eight individuals, groups, and entities affiliated with East Naukati have expressed strong arguments on the record that East Naukati should be excluded from the boundaries of the proposed city.

Part IV-B-1 of this report summarizes the arguments of each of the eight individuals, groups, and entities now opposed to inclusion of East Naukati within the boundaries of the proposed city. Those arguments can be reasonably summarized as consisting of the following four significant points:

1. There is a lack of frequent personal contact between East Naukati and West Naukati residents, which is reflected by the fact that the only two students in East Naukati are educated at home rather than at the West Naukati school. Moreover, year-round and seasonal East Naukati residents do not rely upon West Naukati for shopping, leisure activities, or other needs.
2. The two settlements are remote from one another - by automobile they are eight or nine miles apart, a journey that takes 25 to 30 minutes over unpaved and poorly maintained roads.
3. With only five year-round residents in two households, East Naukati lacks a population density characteristic of neighborhood living.
4. While East Naukati needs certain fundamental public services including road maintenance and emergency services, there is a lack of confidence among East Naukati property owners and residents that the proposed city could or would satisfy those needs.

In conjunction with the October 2005 informational meeting, Commerce had an opportunity to extensively tour East Naukati, West Naukati, and other parts of the territory proposed for incorporation. During that tour and at the informational meeting, Commerce also had the opportunity to speak with residents and property owners of East Naukati and other parts of the territory proposed for incorporation.

Based on the tour and discussions, Commerce perceives that the claims of a lack of frequent personal contact between East Naukati and West Naukati residents are credible.

Further, as recorded in the Preliminary Report, the two settlements are remote from one another. Assertions by East Naukati residents and property owners that it takes 25 to 30 minutes to travel the eight to nine miles between the two settlements are accurate.

While no official contemporary population figure for East Naukati exists, the President of the East Naukati Homeowners Association, others from East Naukati, and the Petitioner's Representative have all indicated to Commerce that the settlement currently has only five year-round residents.¹⁶



Unlike East Naukati, no legal overland access to Sarkar Cove exists for the general public.

Some of the eight individuals, groups, and entities that have recently stepped forward to oppose the inclusion of East Naukati argue that it should be excluded from the proposed city boundaries for the same reasons that Commerce recommended the exclusion of Sarkar Cove. While Commerce perceives a number of fundamental similarities between East Naukati and Sarkar Cove in terms of their respective connections (or lack thereof) to West Naukati, there are also some important distinctions.

Perhaps the most significant distinctions concern the prospect for growth and development. There appear to be far more constraints on the opportunity for expansion of private development at Sarkar Cove than is the case for East Naukati. Limited privately owned lands in Sarkar Cove are in the hands of only a few individuals. Further, Sarkar Cove is surrounded by US Forest Service Lands desig-

¹⁶ The Petitioner's Representative advised Commerce of the population figure during a conversation on October 10, 2005. Also, regarding the above population figure cited by the East Naukati Homeowners Association President, Commerce notes that in the September 11, 2005, Mini Grant application to Commerce, the East Naukati Homeowners Association President indicated that East Naukati had a population of eight.

nated as old-growth forests for wildlife and fish habitat or as natural-appearing landscapes (see Preliminary Report, p. 91). It is inconceivable that those lands will be developed in the foreseeable future.

In contrast, the 32 lots and 3 tracts in Naukati Bay Subdivision East have many different owners. Many of the lots are presently undeveloped. Moreover, State land north of Naukati Bay Subdivision East is classified such that it could be selected under a municipal land grant entitlement (for a future borough or city) and sold for private development.

Another distinction between Sarkar Cove and East Naukati involves year-round population. Sarkar Cove has no year-round residents. Development at Sarkar Cove is limited to a seasonal lodge operation and a few seasonal home sites. While East Naukati currently has few year-round inhabitants, the number may grow in the future.

Overland transportation ties with West Naukati represent another significant distinction between Sarkar Cove and East Naukati. While both Sarkar Cove and East Naukati are eight or nine miles from West Naukati, the roads linking East Naukati and West Naukati are less rudimentary than those linking West Naukati and Sarkar Cove. It is certainly difficult for those unfamiliar with the area (and perhaps even for some local residents) to find the correct road to Sarkar Cove in the maze of old logging roads. That is not the case with East Naukati. Further, as noted in the Preliminary Report, legal access to Sarkar Cove by road does not exist for the general public. Again, that is not the case for East Naukati.

Nonetheless, given the strong views expressed on the record by East Naukati residents and property owners, the circumstances that constrained Commerce's preliminary boundary recommendation no longer exist. With the understanding that residents and property owners of East Naukati are prepared to remain self-sufficient in terms of local services for the foreseeable future, Commerce (hesitantly) formally urges the LBC in Part VI of this Final Report to exclude the eastern territory proposed for incorporation.

2. The fiscal viability of the proposed city.

(a) Budget changes suggested by the Petitioner.

To address concerns expressed by Commerce in its Preliminary Report, which were also discussed in detail at the October informational meeting, the Petitioner's Representative offered a significant number of revisions to the prospective city's three-year budget. The revisions were submitted in writing on October 11, 2005, prior to the deadline for comments on the Preliminary Report.

Appendix A of this Final Report includes that October 11 submission. As pointed out earlier in this report, the suggested changes were not submitted as formal amendments to the Petition. Accordingly, they are treated here as changes suggested by the Petitioner.

The scope of the Petitioner's suggested budget revisions was broad. On the income side, revisions were proposed with respect to six of the fourteen income components. Those related to the four percent bed tax, sales of land, shellfish nursery, capital projects matching grant, National Forest Receipts, and mobile home rental.

On the expense side, revisions were suggested regarding eleven of the sixteen expense components in the original budget. Those related to road maintenance, vehicle and equipment maintenance, municipal reserves, emergency services, capital projects surveying and engineering, planning and legal fees, land surveying, accounting fees, travel, harbor maintenance, and the shellfish nursery.

The suggested income and expense revisions also led to changes in the three surpluses listed in the original budget. Specifically, changes were proposed regarding the municipal reserve surplus (which is distinct from the "municipal reserves" contingency expense component noted in the preceding paragraph), shellfish nursery reserve surplus, and harbor reserve surplus.

In response to the previously noted inquiry from Commerce about the October 11 submission, the Petitioner submitted a second suggested revised budget on October 31.¹⁷ The changes in the second submission were limited to shellfish nursery income and expenses, including the addition of a \$12,000 "economic recovery grant" for the shellfish nursery. Subsequent inquiry by Commerce regarding the \$12,000 economic recovery grant led to further clarification of the figures by the Petitioner on November 8. That clarification is discussed in this part of the report dealing exclusively with a fiscal assessment of the shellfish nursery.

Commerce also noted that the Petitioner's October 31 submission erroneously listed the total of revised Year 1 expenses as \$148,621. The correct total is \$148,771. A copy of the October 31 submission is included here in the appendices. The analysis below reflects all of these revisions, clarifications, and corrections.

¹⁷ Although the second revision was received after the deadline for comment on the Preliminary Report, it was accepted by Commerce because it constituted a significant clarification of timely comments critical to the proper consideration of the proposal.

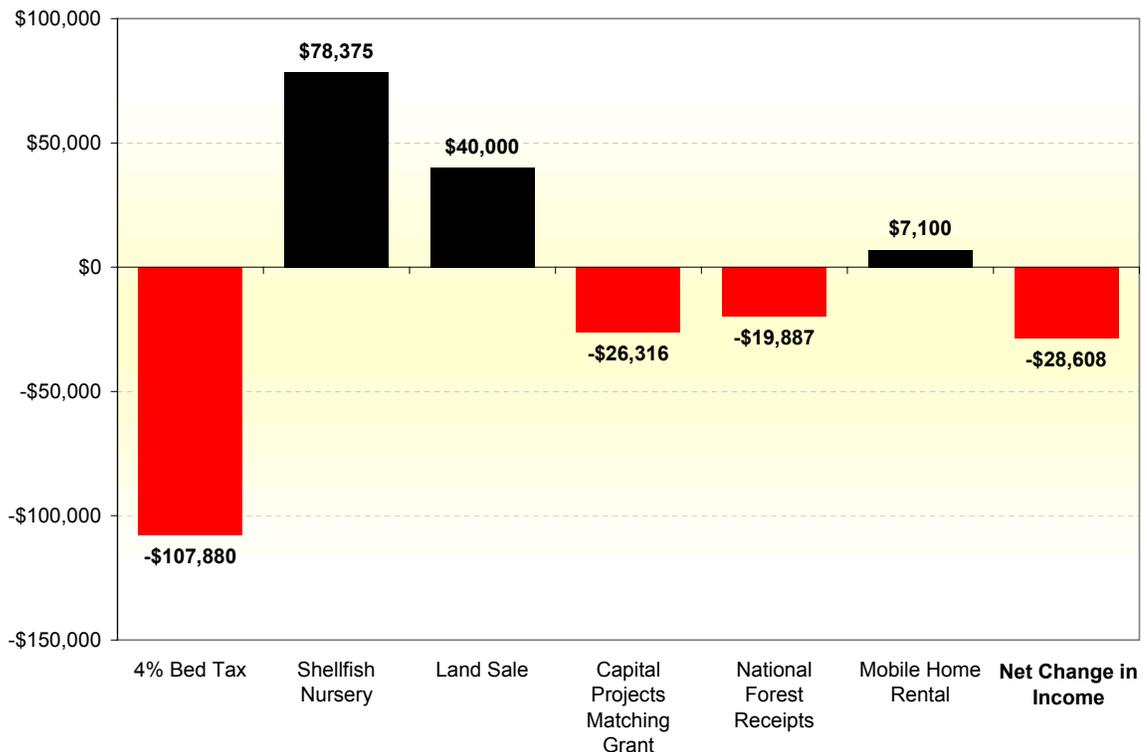
(i) Changes to projected income.

Three-year totals for each of the six income components changed by the Petitioner are shown in Figure 2.

The most significant change in projected income concerned the four percent bed tax. Originally projected to generate \$107,880 over three years within the Petitioner’s initial proposed boundaries, the bed tax was eliminated altogether in the October 2005 revisions.

Having conceded to the exclusion of Sarkar Cove from the proposed city boundaries, it was apparently reasoned by the Petitioner that the resulting loss of El Capitan Lodge as a source of bed tax revenue rendered the tax uncalled for in the remnant territory. As noted in the Preliminary Report, the El Capitan Lodge accounted for \$96,000 (89 percent) of the Petitioner’s original bed tax revenue projections over three years.

Figure 2 - Petitioner’s October and November 2005 Suggested Changes to Three Year Income Projections (Figures Represent Totals for Three Years).





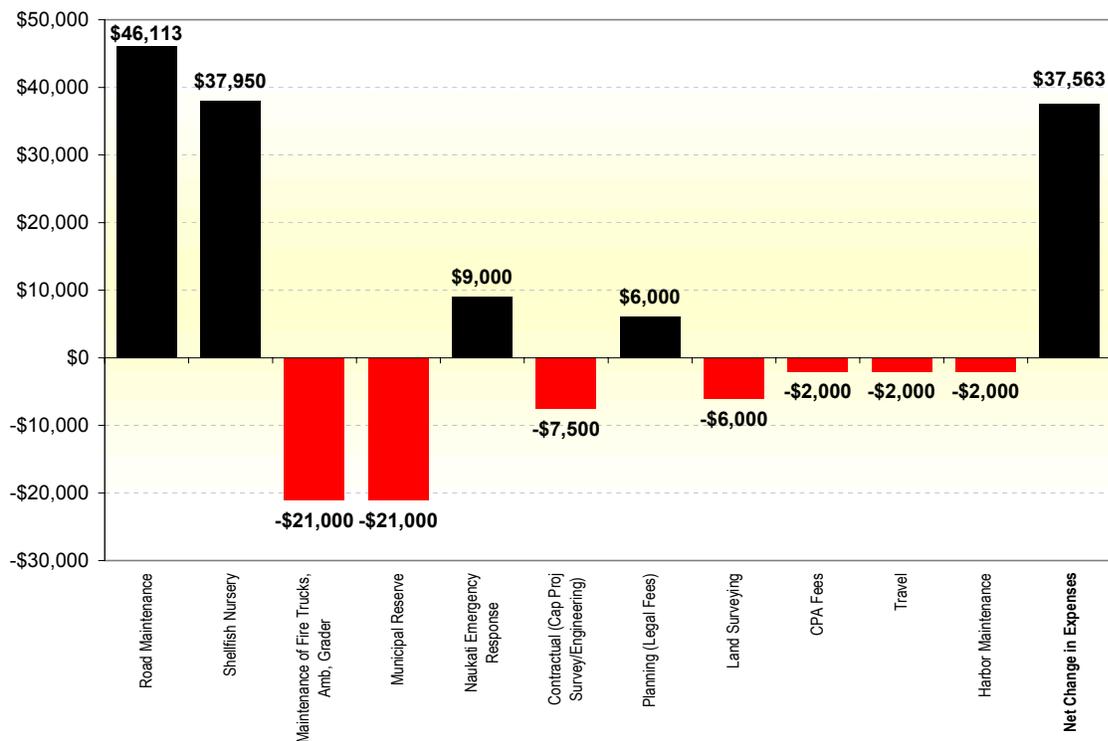
In large measure, the Petitioner offset the loss of bed tax income by projected increases in shellfish nursery income and land sales. The increase in gross income over three years from the nursery totaled \$78,375 (\$40,425 of which represented net income). Projected increases in income from land sales equaled \$40,000 over three years.

The total net effect of the various income changes suggested by the Petitioner was a \$28,608 reduction in income for the proposed city over three years.

(ii) Changes to projected expenses.

Three-year totals for each of the eleven expense components targeted by the Petitioner for change are shown in Figure 3. The greatest change is the \$46,113 increase in road maintenance expenses over three years. That change resolves the concern expressed by Commerce in its Preliminary Report that the Petitioner’s original budget had not allocated all National Forest Receipts for road maintenance as would be required under State and federal law.

Figure 3 - Petitioner’s October and November 2005 Suggested Changes to Three Year Expense Projections (Figures Represent Totals for Three Years).



The Petitioner proposed three other cost increases. One was a \$37,950 boost in projected expenses for the shellfish nursery over three years. Another was a \$9,000 increase in emergency services over three years, and the last was a \$6,000 increase in the allowance for planning and legal services.

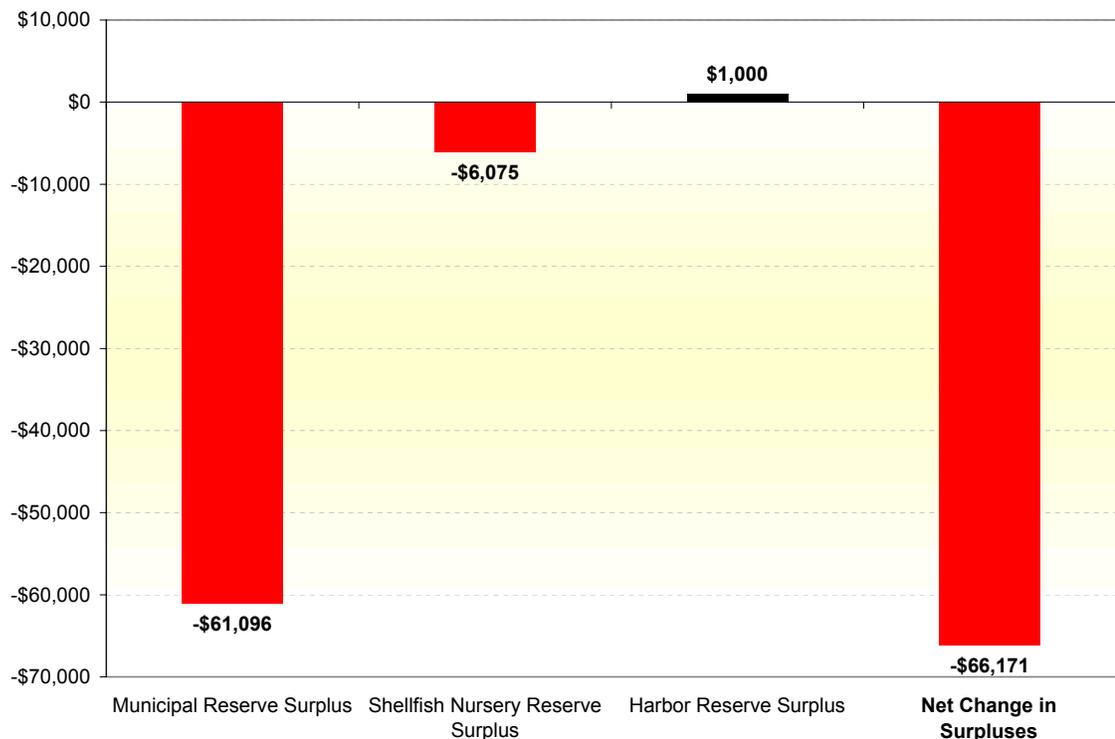
Changes to the remaining seven modified expenditure components projected lower costs than were reflected in the original budget. The Petitioner proposed to eliminate funding for maintenance of vehicles and equipment. A contingency fund, dubbed by the Petitioner as "Municipal Reserve," was also eliminated. The original budget had allocated \$21,000 for each of those two components over three years.

In sum, expenses over the three-year period were increased by \$37,563.

(iii) Changes to projected surpluses.

The proposed \$28,608 reduction in income and \$37,563 increase in expenditures resulted in a \$66,171 reduction over three years in surpluses projected in the original budget. Specifics are shown in Figure 4.

Figure 4 - Petitioner's October and November 2005 Suggested Changes to Three Year Projections of Surpluses (Figures Represent Totals for Three Years).



The surplus for “municipal reserve” was reduced by \$61,096 and the surplus for the “shellfish nursery reserve” dropped by \$6,075. The third surplus - for “harbor reserve” - was increased by \$1,000 over three years.

(b) Feasibility and plausibility of budget changes suggested by the Petitioner.

(i) Shellfish nursery net income.

As reflected in Figure 2, the Petitioner increased projected gross revenues from the shellfish nursery by \$78,375 over three years. As shown in Figure 3, projected nursery expenses increased by \$37,950, leaving a total projected \$40,425 increase in net income for the three years. If the one-time \$12,000 “economic recovery grant” listed in the October 31 submission were excluded from consideration, the projected net income from the nursery increased by \$28,425 over the three years.

The Petitioner’s latest figures suggest that in Year 3, following a transition period, annual gross revenues from the nursery will total \$76,000. Annual expenses for the same period are projected to be \$46,150. Those figures result in a projected annual net income of \$29,850.

The shellfish nursery in Naukati was established with assistance from a grant administered by Commerce’s Office of Economic Development (OED). OED’s Web site provides the following background information regarding shellfish mariculture in Alaska:¹⁸

Though Alaska’s mariculture industry has grown substantially since the Aquatic Farm Act passed [by the Alaska Legislature] in 1988, it remains in its infancy. In 2003, Alaska mariculturists sold only \$624,573 of product. The future aquatic farmer in Alaska inevitably faces many frustrating hurdles and financial risks when starting their business. Offsetting these hardships, however, is the potential for a healthy profit and great personal satisfaction.

The Pacific oyster, *Crassostrea gigas*, is the most common farmed shellfish in Alaska. Unlike traditional farms where oysters are cultivated on the beach, Alaska’s oysters are typically grown off the bottom on gear suspended in the water column. Though most

¹⁸ <http://www.dced.state.ak.us/oed/seafood/seafood.cfm>

available information focuses on these oysters, Alaskan farms also cultivate a number of other organisms including littleneck clams, mussels, scallops, sea cucumbers, and seaweed.

Given its role in establishing the Naukati nursery, OED staff was enlisted to evaluate that portion of the Petitioner’s October 11 budget revisions relating to the nursery. As reflected in the preceding summary, the changes regarding the nursery were limited to a \$10,000 (31 percent) increase in projected income



Naukati’s shellfish nursery was established with assistance from a grant administered by Commerce.

in each of the first three years. Notably, however, no increase in nursery expenses was projected in the October 11 revisions.

OED staff completed its analysis on October 25. A copy of that analysis is included here as Appendix C.

OED observed that, “the shellfish mariculture industry in Alaska is not a huge success story.” Statewide production for 2004 was reported to

be “over \$634,000.” That represented an increase of only about \$10,000 (1.6 percent) over the \$624,573 figure reported for 2003 on the OED Web site.

After conferring with the Aquatic Program Manager of the Alaska Department of Natural Resources (DNR), OED staff reported that only 21.63 acres were under lease for five oyster farming operations in the greater Naukati area.¹⁹ It was stressed that none of those farms operated at full capacity. One reportedly

¹⁹ LBC staff determined that three of the five farms in the greater Naukati area are within the original territory proposed for incorporation. Of those three, all are also within the Petitioner’s alternative 35-square mile boundary proposal. One of the three is within the boundaries recommended by Commerce in the Preliminary Report.

As indicated earlier in this report, the Petitioner states that there are seven oyster farms in the Naukati area. After conferring with officials of the Alaska Department of Natural Resources, two farms are located at Token Bay, well beyond the territory proposed for incorporation, and the other is in an unnamed bay on Tuxekan Island, west of the territory proposed for incorporation.

operated at just one-quarter of its potential. OED staff indicated that another farm - one encompassing 10 acres, or nearly half of the total acreage under lease in the Naukati area - was seeking to reduce the size of its operation.

OED indicated that the lease for one Naukati oyster farm was in jeopardy due to delinquent lease payments.²⁰ OED reported further that DNR was aware of no plans for new farms in the Naukati area. However, OED indicated that the prospect existed for sales to farms outside the immediate Naukati area, including the ones at Token Bay and others beyond the Prince of Wales region.

OED ultimately concluded that, "it is possible that [annual] revenues will reach \$40,000 and may increase." Thus, OED, in effect, determined that the Petitioner's October 11 projection of \$42,375 in gross annual income for the nursery was reasonable. However, OED expressed repeated concern that the projected increases in income were not accompanied by any increases (commensurate or otherwise) in projected nursery expenses.

On October 25, upon receipt of OED's assessment, Commerce's LBC staff asked the Petitioner's Representative to address the concern that the projected nursery income had increased without any increase in related expenses.

The Petitioner responded on October 31 by submitting a second suggested revised budget. A copy of the October 31 submission is included here as Appendix D.

The October 31 submission increased projected costs for the shellfish nursery. However, projected nursery income was also boosted further for Year 2 and Year 3. The Year 2 projected nursery income was increased to \$57,125, while Year 3 projected income was raised to \$76,000. The figure for Year 2 was \$24,750 (76.4 percent) higher than the original figure and \$14,750 (34.8 percent) more than the projection offered by the Petitioner less than three weeks earlier, on October 11. The boost in Year 3 nursery income amounted to \$43,625 (134.7 percent) over the original figure and \$33,625 (79.4 percent) more than the October 11 projection.

²⁰ In subsequent contacts with LBC staff, DNR officials indicated that it now appears as though the delinquent payments will be forthcoming and the lease will not be terminated.

Expenses, originally projected to be \$25,350 annually, were now anticipated by the Petitioner to be \$38,500 in Year 1, \$41,350 in Year 2, and \$46,150 in Year 3. Those increases amounted to, respectively, \$13,150 (51.9 percent), \$16,000 (63.1 percent), and \$20,800 (82.1 percent).

The October 31 submission also added \$12,000 to Year 1 income for an "Economic Recovery Grant." When questioned by LBC staff about that \$12,000 addition, the Petitioner insisted that the funds be counted. The Petitioner advised Commerce that the grant funds had already been spent to purchase oyster seed currently in the nursery. Given that circumstance, Commerce contended that the \$12,000 was being counted twice by the Petitioner - once as grant income and again in the context of income from the sale of spat.

Commerce noted, however, that since grant funds had been used to purchase Oyster seed not yet sold as spat, it would be legitimate to reflect that circumstance in the form of a \$12,000 reduction in nursery expenses for Year 1 (from \$38,500 to \$26,500). It is stressed here, however, that such consideration of grant income to reduce expenses overstates the fiscal strength of the nursery operation.

It is observed that nursery expenses in the original budget were estimated to be 78.3 percent of revenues. In the October 31 submission, projected nursery expenses (discounting the effect of the \$12,000 grant) were 71.8 percent of revenues.

Given OED's assessment, Commerce concludes that it is reasonable to project long-term gross annual income of \$40,000 from the nursery. Given the proportion of projected nursery expenses to income outlined above, Commerce further concludes that annual nursery expenses are reasonably estimated to be \$30,000. Thus, Commerce considers a reasonable projection of net income to be \$10,000 annually. The latest long-term figure offered by the Petitioner is nearly three times that figure ($\$76,000 - \$46,150 = \$29,850$).

Of course, as conceded by OED, annual nursery gross income may increase beyond \$40,000. However, even if such income were 25 percent higher (\$10,000), the increase in annual net income from the nursery operation would likely amount to about one-quarter of that, or \$2,500. Fittingly, OED ended its assessment with the reminder that State financial aid for shellfish nurseries was intended to promote economic development, not to create an income source for local government. Specifically, OED stated:

The State supported a number of shellfish mariculture economic development projects. Projects like the Naukati FLUPSY were intended to serve as economic development stimulators, not revenue generating engines for cash strapped local governments.

(ii) Income from sale of municipal entitlement lands.

As reflected above, the Petitioner increased projected Year 3 income from the sale of municipal land by \$40,000. In relative terms, the increase represented a 200 percent jump in the estimated revenue from that particular source.

In support of the increased projection, the Petitioner stated in its October 11 comments that:

Naukati will select all waterfront properties adjoining our waterfront master plan. The University of Alaska did not select any Commercial waterfront land, leaving Naukati the only owner of above-mentioned commercial land without a competitor.

The University of Alaska Land Management Staff has attended a meeting in Naukati, and assured us they would work with us on their land use plans. The City of Coffman Cove has worked with the University and has had great success and we feel comfortable that our relationship will be successful also.

As reflected above, the Petitioner is optimistic that the prospective city can select substantial valuable waterfront property under its municipal entitlement. However, only a small fraction of the coastline is available for municipal selection. Much of the waterfront is legislatively designated to be conveyed to the University. Substantial other waterfront lands are already in private ownership or are owned by the Mental Health Trust Authority and the U.S. Forest Service. Other waterfront lands are classified as crucial habitat or public facilities and are therefore not available for municipal selection.

As reflected in the Preliminary Report, the City of Naukati would be entitled to select ten percent of the vacant, unappropriated and unreserved (VUU) State lands within the boundaries of the city between the date of its incorporation and two years after that date (AS 29.65.030).

It is estimated that the Petitioner's original boundaries would result in an entitlement for the proposed city to 534 acres of State VUU land. A map of the VUU lands within the proposed city boundaries was included in the Preliminary Report as Figure 3-7 on page 78.

Given the Petitioner's three-fold increase in the projected proceeds from the sale of municipal entitlement lands to sustain local government operations, Commerce's LBC staff carefully examined the plausibility of the revised projection. That examination involved extensive consultation with several officials of the Alaska Department of Natural Resources (DNR).

VUU lands in the territory proposed for incorporation are subject to the land classifications under the State's *Prince of Wales Island Area Plan* (revised October 1998). VUU lands include those designated for general use, residential land disposal, commercial or industrial development or for public recreation. They also include lands classified as habitat, cultural resources, public facilities or water resources that would not be available for selection by the prospective city.

While all VUU lands within a newly incorporated municipality count toward the determination of its land entitlement (ten-percent of the total VUU area), all VUU lands are not eligible for selection by the prospective city. For example, VUU lands classified as habitat, cultural resources, public facilities, or water resources in a State area plan cannot be selected.

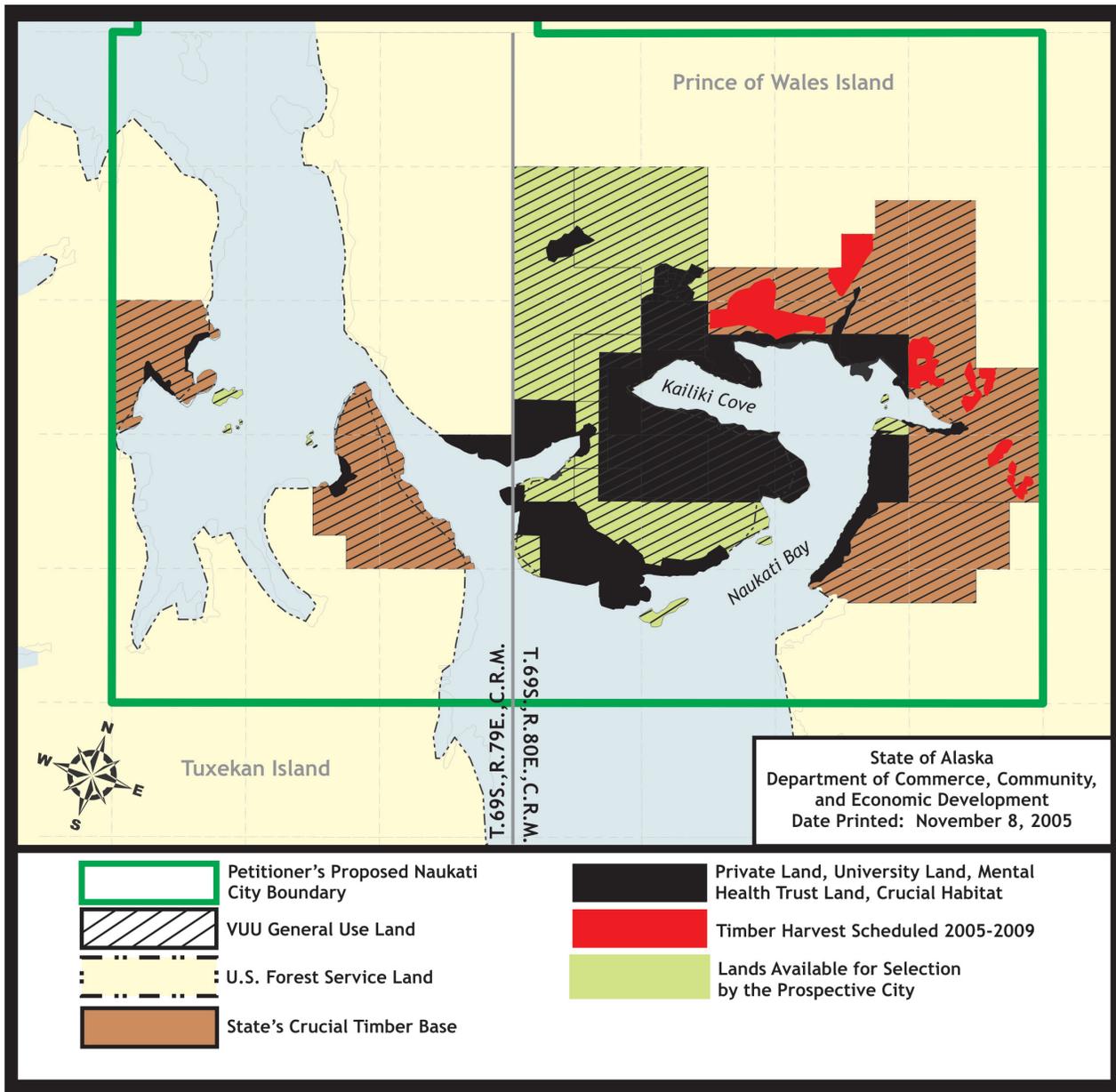
In addition, many of the VUU lands within the proposed City of Naukati cannot be selected by the prospective city because those lands have either been scheduled for timber harvest between 2005 and 2009 or because they are part of the State's crucial timber base.

DNR officials stressed that public policy does not favor municipal entitlement selections from the State's timber base because it would reduce the annual allowable cut. The crucial timber base consists of prime logging areas for old growth Sitka spruce, western hemlock, red cedar and yellow cedar with road access and nearby land transfer facilities so logs can be easily shipped out to sawmills.

DNR officials also pointed out that much of the valuable lands in the Naukati area, including waterfront land, has already been conveyed, subdivided, and sold by the State of Alaska. For example, Naukati East and Naukati West are subdivisions developed by the State of Alaska. Additionally, as noted in the Preliminary Report and earlier in this report, 937 acres in the Naukati area are to be conveyed to the University as part of its 250,000-acre land entitlement. Those 937 acres are specifically designated in the 2005 State law. The University may survey that land and sell it as subdivision lots to maximize revenue. The existing State subdivisions and any future University subdivisions may satisfy the desire for residential land in Naukati, thus driving down the demand for and price of city land sales.

Commerce prepared a map, included on the following page as Figure 5, showing State lands that would be available for selection by the prospective city. Those lands are shown on the map in green.

Figure 5 - Estimated Vacant, Unappropriated, Unreserved (VUU) Lands - City of Naukati - Total Estimated VUU Area: 5,340 Acres - Estimated Entitlement (10% of Total VUU Area): 534 Acres



Commerce stresses that the prospective city will not be allowed to pick and choose only the most valuable lands among the limited properties available for selection. The State does not allow "high grading" - the practice of choosing only the best lands - by cities selecting municipal entitlement lands. Municipal land selections must comprise compact, contiguous parcels that include desirable lands as well as less desirable lands. Under AS 29.65.070(c), a municipal selection must be compact and its length cannot exceed four times its width.

Another crucial issue regarding the Petitioner's revised budget involves the anticipated timing for the conveyance of municipal entitlement lands. The Petitioner expects that the lands will be conveyed in time to be sold during the third year following incorporation. Most of the lands in the municipal selection area are still owned by the federal government. Those lands have been "tentatively approved" for conveyance to the State under its entitlement to more than 103 million acres; however, the federal government has not yet surveyed those lands. That must be done before the lands are patented to the State and the prospective city. It will take extra time and cost for the city to subdivide the land to sell. City properties may not be ready for sale until the fifth or sixth year after incorporation.

Another issue to be considered here is the costs associated with survey, subdivision, and conveyance of municipal entitlement lands. The City of Naukati will be responsible for conducting a survey of the perimeter of the lands they will receive from the State. Waterfront surveys are more complex and expensive because of the meanders and additional monumentation required along the coastline. A DNR surveyor estimated that the cost of surveying the Naukati municipal entitlement lands would range from \$35,000 to \$45,000. In addition, the City of Naukati will have to bear the costs of subdividing and surveying the subdivisions. The Petitioner's revised budget allows only \$12,000 for survey costs; that figure is \$6,000 (33 percent) less than the cost projected in the original budget.

Moreover, as reflected in the preceding final analysis of boundaries, if East Naukati is detached from territory proposed for incorporation, it will significantly reduce the prospective city's municipal land entitlement and potential revenue from the sale of those lands.

Given the totality of the circumstances outlined here, Commerce has significant reservations about both the projected magnitude and timing of the Petitioner's revised income projections from land sales.

(iii) Road maintenance, emergency services, and vehicle and equipment maintenance and repair.

On the surface, it appears that the Petitioner's latest budget revisions eliminated altogether projected expenses relating to vehicle and equipment maintenance and repair. A budget component providing \$21,000 for such over three years appeared in the original budget. That component has been eliminated from the revised budget.

However, Commerce notes that Petitioner also increased projected expenses for road maintenance (\$46,113 over three years) and emergency response (\$9,000 over three years). After conferring with the Petitioner about the matter,

Commerce was advised that the increased road maintenance and emergency response figures include provision for repair and maintenance of vehicles and equipment.

In considering the feasibility of the figures in question, Commerce offers a reminder that detachment of East Naukati from the proposed city would significantly reduce the level of funding available for road maintenance.

(iv) Organization grant

Commerce continues to be concerned over the allocation of the \$75,000 organization grant to which the prospective city would be entitled. Two-thirds of organization grant is included as income in the Petitioner's Year 2 budget. The remainder is included in the budget as Year 3 income.

The grant is not a recurring source of funding. It is only intended to be used as a means to support a newly incorporated city during the initial transition period. However, the Petitioner relies on it for routine income.

(v) Prospect for new State revenue sharing program.

As noted in Commerce's Preliminary Report, State Revenue Sharing funding was discontinued in Fiscal Year 2004. However, on November 10, 2005, Governor Murkowski proposed an alternative long-term, sustainable approach to assist local governments.

The Governor's proposal would establish a "community dividend program" funded from the earnings of the Amerada Hess account that resides within the Permanent Fund for investment management purposes. By law, earnings from the Amerada Hess account cannot be used in calculating Permanent Fund dividends.

Estimated revenue from the account in Fiscal Year 2007 is \$27 million. The community dividend program outlined by the Governor would provide \$10 million in base payments to cities and boroughs. All boroughs would receive \$50,000 and cities would receive between \$25,000 and \$40,000, depending upon their population.

At the same time, Governor Murkowski encouraged Alaskans to consider the so called "Percent of Market Value" proposal for the Permanent Fund that passed the House of Representatives two years ago. That proposal would have provided some \$70 million for a community dividend program from a long-term funding source.

On the same day that the Governor announced his proposal, leaders of the Senate Majority indicated that they would give strong consideration in the upcoming legislative session to the proposal. Senate Majority Leader Gary Stevens said:

I think the governor is on the right track. The state does need to find a way to help local governments provide basic government services. The mechanics of how we achieve that will be one of our top priorities when we return to Juneau. We are examining several options on grant amounts to boroughs, municipalities and the unorganized communities.

If such proposals were enacted, it would serve as a source of revenue for the prospective city.

(vi) Prospect for sales tax.

As reflected in the Preliminary Report (p. 111 - 112), commercial sales in the territory proposed for incorporation that could be subject to a hypothetical sales tax were estimated in the Petition to be \$300,300 annually. However, following the October 2005 informational meeting, the Petitioner's Representative advised Commerce that the owner of Naukati Connection, a West Naukati store, projected that 2005 gross sales from that retail outlet alone would be \$950,000. The Petitioner confided that the original figure in the Petition - less than one-third of the projected sales from Naukati Connection alone - was an uninformed estimate.

Appendix E of this Final Report consists of a letter from the owner of Naukati Connection confirming the Petitioner's statement.

Given the new information about the volume of sales at Naukati Connection, plus the other potentially taxable business transactions in the community (e.g., the estimated \$99,000 in commercial room rentals in West Naukati addressed on page 112 of the Preliminary Report), it appears that a sales tax offers a feasible source of local revenue for the proposed city. With more than \$1 million in potentially taxable sales each year, a five-percent sales tax could raise more than \$50,000 in local revenues annually.

(c) Overview of the Petitioner's revised budget.

In its Preliminary Report, Commerce expressed significant concerns regarding aspects of the Petitioner's budget and the fiscal viability of the proposed city government.

The Petitioner's October 2005 revisions resolved certain of Commerce's earlier concerns. For example, the revised budget addressed the concern that National Forest Receipts could be used only to fund road maintenance. The Petitioner also eliminated State Capital Matching Grant funding from the budget because the funding is no longer available.

However, other fiscal concerns expressed by Commerce in the Preliminary Report were not resolved. Two such concerns are particularly significant. One is continued reliance on the one-time \$75,000 organization grant to support routine operations. The other is the continued keen aversion to any broad local tax measure such as a property tax or general sales tax.

Moreover, the October 2005 budget revisions generated five notable new concerns on the part of Commerce. The first is a substantially greater reliance on the part of the Petitioner regarding projected net income from the shellfish nursery. Originally, the Petitioner anticipated that the nursery would provide only \$7,025 in net proceeds to the proposed city each year. Now, the Petitioner projects that the nursery will provide \$29,850 in annual net revenues for the city (Year 3). That represents an increase of 325 percent over the original figure. The Petitioner's latest figure is roughly three times the level that Commerce's Office of Economic Development considers to be reasonable.

The second significant new concern to Commerce is the Petitioner's substantial escalation of projected revenue from the sale of land. The formal Petition anticipated that the proposed city would receive \$20,000 from land sales in Year 3. The October 2005 revisions increased that figure by \$40,000 (200 percent). The new figure reflects a level of optimism over the value of land to be conveyed to the city that may not be warranted.

As addressed earlier, the lands available for selection by the proposed city seem to be far more limited than is perceived in the community. Moreover, if the University of Alaska sells much or all of its 937-acre entitlement in the core of West Naukati, it can be reasonably expected to dampen the demand for land proposed to be sold by the city. The lands in Naukati to which the University is entitled appear to be among the best in the Naukati area and include substantial waterfront. Further, as explained earlier, the Petitioner's expectations regarding the schedule for conveyance of the city's municipal entitlement might not be realistic.

The third significant new concern to Commerce is the depletion of contingency funds and the diminution of surpluses that were part of the original budget. The budget submitted with the original Petition provided for a \$7,000 annual contingency (\$21,000 over three years). Additionally, the original budget

projected \$174,953 in various surpluses over the three-year period. In the revisions, projected surpluses over three years have dropped to \$87,782. The revised total for the surpluses is about half the original figure.

The fourth new concern is the Petitioner's insistence on including a one-time \$12,000 economic recovery grant in Year 1 of the revised budget. That creates the same type of concern expressed by Commerce with respect to including the one-time organization grant. If the \$75,000 one-time organization grant and the one-time \$12,000 economic recovery grant were excluded from the budget, the \$87,782 surpluses in the revised budget would be virtually wiped out (reduced to a mere \$782). Moreover, if the optimistic projections for income from the nursery and land sales prove to be unrealistic, the prospective city will experience significant deficits.

Lastly, a new fiscal concern arose as a result of Commerce's final boundary recommendation. Modification of the boundaries as recommended by Commerce in this report will reduce the funding available for road maintenance and will also reduce the city's municipal land entitlement.

This portion of the Final Report concludes with a graphic comparison of the Petitioner's original and revised budgets for each of the first three years following incorporation.

Figure 6 provides a comparison of the Petitioner's original budget and the proposed revised budget for all income components during each of the first three years.

Figure 7 provides a comparison of the original budget and the proposed revised budget for all expense components during each of the first three years.

Figure 8 provides a comparison of the original budget and the proposed revised budget for all surplus components during the first three years.



Figure 6 - Comparison of Original Budget Income Projections to Petitioner's October and November 2005 Suggested Changes.

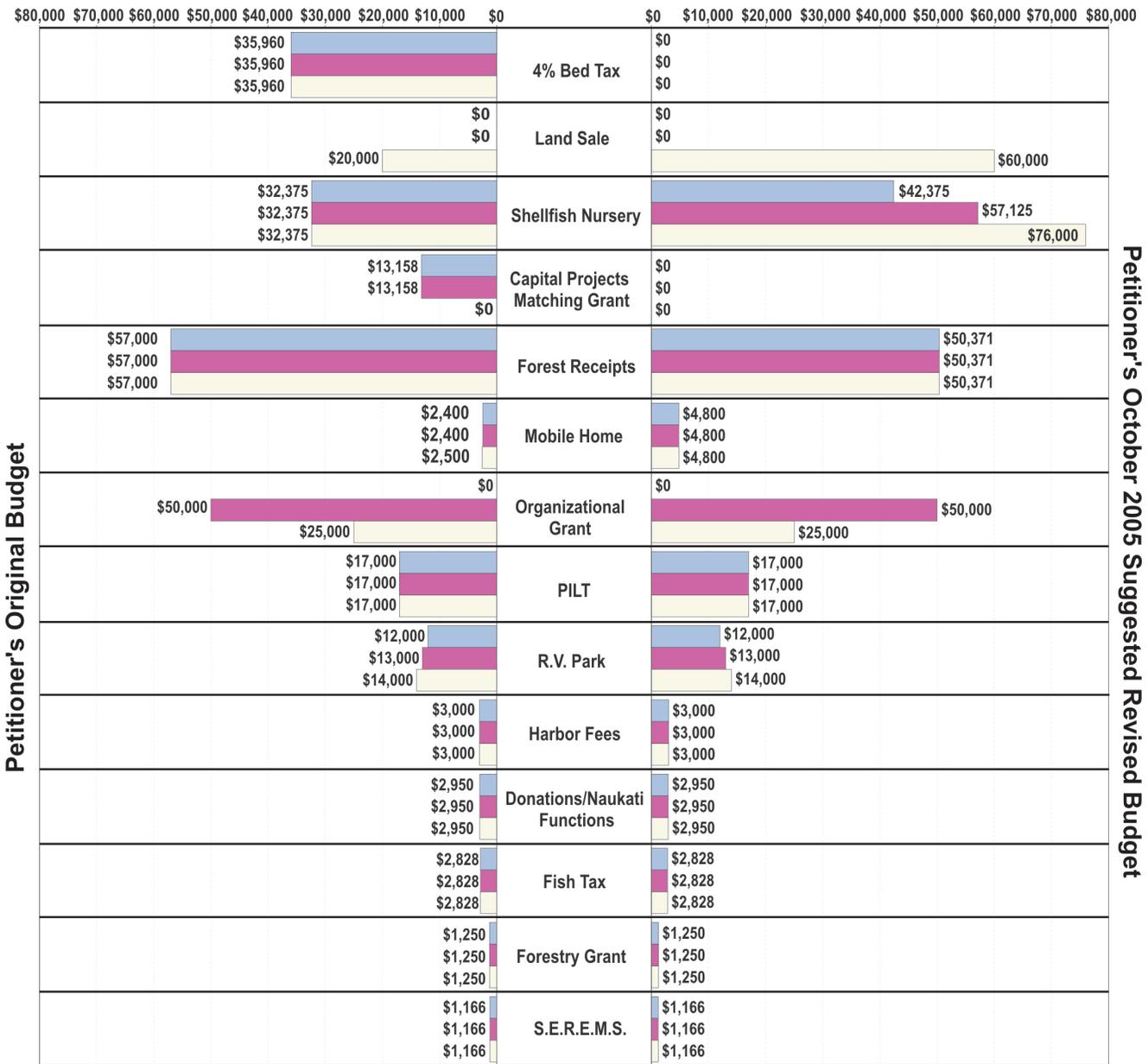
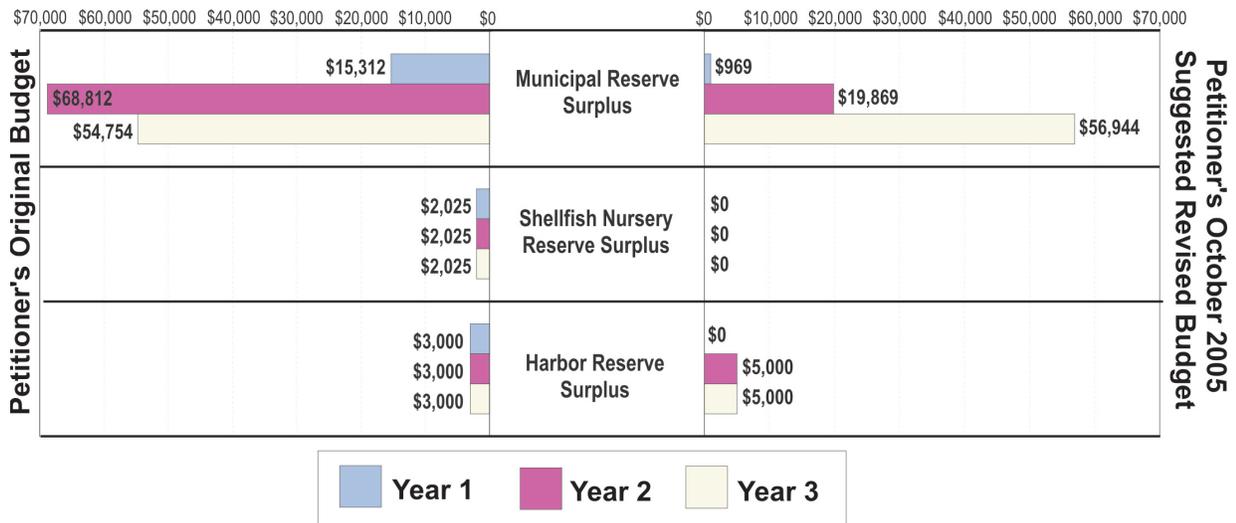




Figure 8 - Comparison of Original Budget Surplus Projections to Petitioner’s October and November 2005 Suggested Changes.



PART VI

FINAL CONCLUSIONS AND RECOMMENDATIONS

A. Introduction

Part VI-B of this Final Report presents the Commerce’s final conclusions in these proceedings. Part VI-C presents Commerce’s final written recommendations to the LBC regarding the pending petition to form the City of Naukati.

B. Final Conclusions

Based on the analyses in Preliminary Report and Final Report regarding the proposed incorporation of the City of Naukati, Commerce presents its final conclusions below.

1. Final conclusions regarding boundaries of the territory petitioned for incorporation.

The existence of a community is required under AS 29.05.011 and 3 AAC 110.005 for incorporation of a city in Alaska. The 44-square mile territory petitioned for incorporation includes West Naukati, a bona fide community as defined by LBC regulations (3 AAC 110.990). However, the territory petitioned for incorporation includes other settled and developed areas, notably Sarkar Cove and East Naukati. Sarkar Cove and East Naukati are distinct from West Naukati.

The legal standards that guide the Local Boundary Commission in setting boundaries of city governments are founded upon the “limitation-of-community doctrine.” That doctrine generally restricts the boundaries of a newly formed city to an existing community, plus territory reasonably anticipated for growth and development within ten years. It also generally prohibits the inclusion of large undeveloped and uninhabited territory within the boundaries of city governments.

The 44-square mile territory petitioned for incorporation includes areas beyond those which are necessary to provide municipal services on an efficient scale. That runs counter to the requirements set out in AS 29.05.011(a)(2) and 3 AAC 110.040(a).

The original boundaries of the proposed City of Naukati extend beyond the community of West Naukati and territory encompassing reasonably predictable growth, development, and public safety needs during the 10 years following the anticipated date of incorporation. Thus, the original boundaries exceed the limits under 3 AAC 110.040(b).

The originally proposed boundaries of the prospective City of Naukati include large unpopulated areas. Application of the incorporation standards under 3 AAC 110.040(c) do not justify those boundaries.

The boundaries of the proposed City of Naukati are contiguous and without enclaves. However, those boundaries include more territory than is necessary to allow for the full development of essential city services. Thus, under 3 AAC 110.040(d), the 44-square mile territory proposed for incorporation is excessive.

The boundaries of the proposed City of Naukati do not overlap the boundaries of an existing borough or city. Therefore, standards and procedures for annexation to or detachment from existing boroughs and cities need not be applied as would otherwise be required by 3 AAC 110.040(e).

2. Final conclusions regarding the fiscal viability of the proposed city.

As reflected in Part V-B-2, Commerce has serious concerns over the fiscal plan offered by the Petitioner. If anything, those concerns have increased as a result of the Petitioner's October 2005 revisions to the fiscal plan.

Commerce affirms the conclusion in its Preliminary Report that privately owned property in the proposed city may offer a property tax base that would render the prospective city government economically viable. As outlined in Part V of this Final Report, Commerce also concludes that sales taxes could help sustain local government operations.

The Petitioner has repeatedly stated that Naukati residents do not want property taxes or general sales taxes. Commerce notes, however, that nearly 90 percent of Alaskans currently live within municipal governments that rely upon municipal property taxes to support local services. Others live in municipal governments that, at a minimum, rely on sales taxes to fund local government.

In this era of demands by some State policy makers for greater local responsibility, Commerce concludes that a property tax or general sales tax is necessary if Naukati residents wish to pursue city incorporation.

As emphasized earlier by Commerce, contemporary reports by State and federal agencies suggest that more than half of Alaska's city governments are experiencing severe financial and managerial difficulties. Considering the current status of many municipalities, Commerce continues to be vigilant in terms of promoting municipal incorporation for only those prospective local governments that can demonstrate fiscal viability.

3. Final conclusion regarding the size and stability of the territory recommended for incorporation.

Commerce concluded in the Preliminary Report that the population of Naukati is marginally large and stable enough to support city government as required for city incorporation by AS 29.05.011(a)(4) and 3 AAC 110.030(a).

The determination in this Final Report that East Naukati should be excluded from the proposed city has minimal effect on the size and stability of the population of the proposed city. Therefore, Commerce concludes that the standard at issue is met with respect to its recommended boundaries.

4. Final conclusion regarding the need for city government.

Commerce affirms its conclusion in the Preliminary Report that there is a need for city government in Naukati, an unincorporated community in Alaska's unorganized borough. Thus, the standard in AS 29.05.011(a)(5) and 3 AAC 110.010(a) is met.

5. Final conclusion regarding feasibility of services through annexation to an existing city.

Commerce affirms its preliminary conclusion that the services to be provided by the proposed City of Naukati cannot be provided by annexation to an existing city. Thus, the limitations in AS 29.05.021(a) and 3 AAC 110.010(b) are not a barrier to incorporation of the City of Naukati.

6. Final conclusion regarding the best interests of the State.

As long as the fiscal viability of the prospective city government is reasonably assured, incorporation of the City of Naukati would serve the best interests of the State. The lack of such assurance, however, does not serve the State's best interest. With that stipulation that the proposed city is reasonably assured of fiscal viability, the requirement under AS 29.05.100 and as defined under 3 AAC 110.042 would be met.

7. Final conclusion regarding transition to city status.

The Petitioner has provided a transition plan properly addressing the proposed changes as required for city incorporation. Thus, the provisions of 3 AAC 110.900 are satisfied.

8. Final conclusion regarding effect on civil and political rights.

Incorporation of the City of Naukati will not deny any person the enjoyment of any civil or political rights, including voting rights, because of race, color, creed, sex, or national origin. This is a condition under 3 AAC 110.910 for city incorporation. Federal law, 42 U.S.C. § 1973, establishes similar requirements.

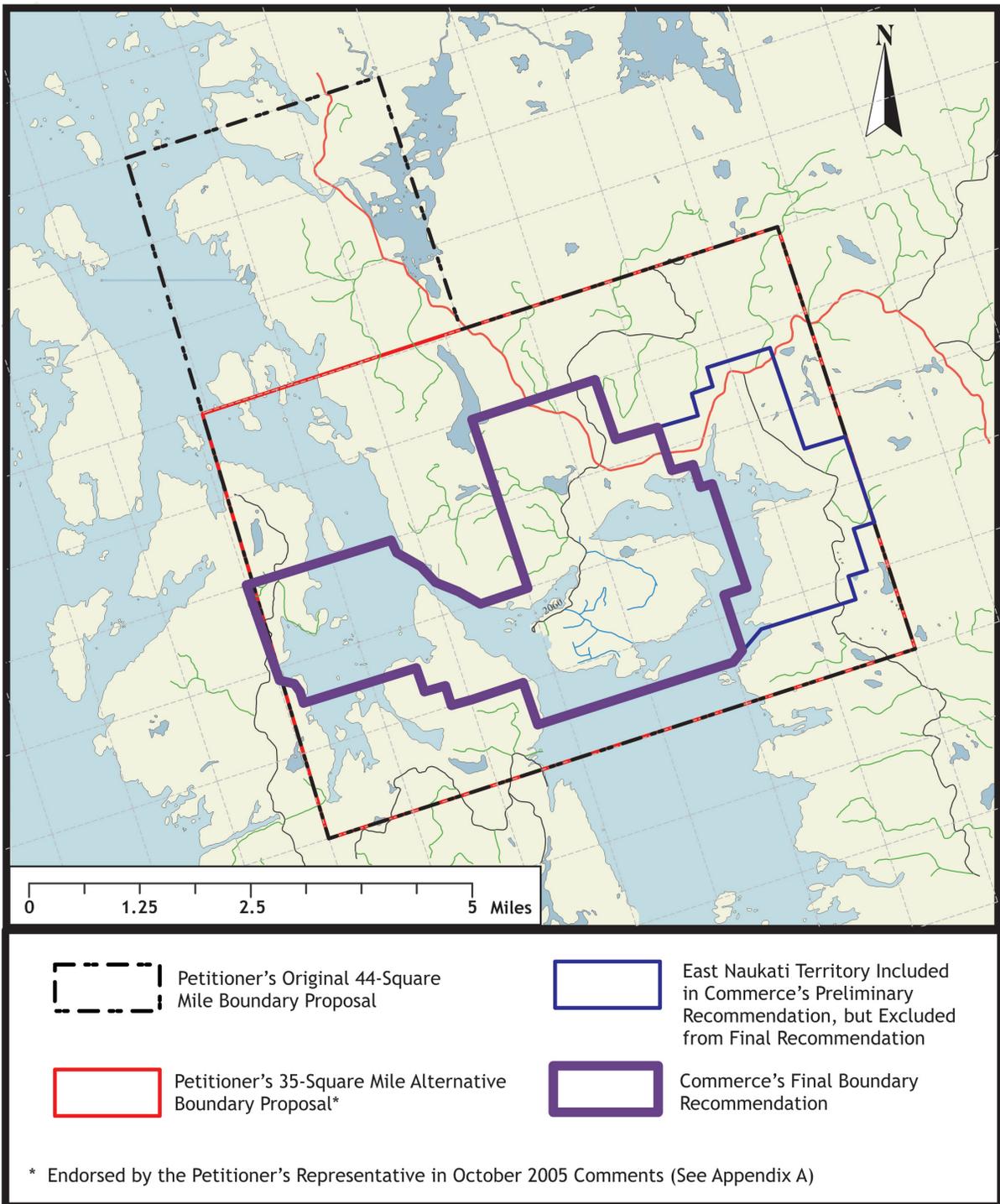
C. Final Recommendations

To address the boundary concerns raised by Commerce in its Preliminary Report and this Final Report, Commerce recommends that the Local Boundary Commission amend the boundaries set out in the Petition. Figure 9 reflects Commerce's final boundary recommendation.

To address concerns over the fiscal viability of the proposed city, Commerce recommends that the Commission condition incorporation upon voter approval of a proposition that authorizes the proposed city government to levy a general sales tax up to five-percent. Alternatively, Commerce recommends that incorporation be conditioned upon voter approval of a proposition that authorizes the proposed city government to levy a property tax, either alone or in conjunction with a sales tax.

Commerce stresses that either proposition would empower the city government to levy a tax; however, it would not require the city to do so. In the event, that Commerce's concerns over the fiscal viability of the proposed city ultimately prove to be well founded, the city government would have the tools to address its fiscal needs. Alternatively, if the Petitioner's optimism is borne out, the city would not have to exercise its authority to levy taxes.

Figure 9 - Commerce’s Final Boundary Recommendation





APPENDIX A

TIMELY COMMENTSON COMMERCE'S PRELIMINARY REPORT

OCT-13-2005 08:25 AM

P. 81

10-11-05

MR Backhausark

160 @ Commerce, S. AK. US.

FAX 907 269-4539

Dear MR Backhausark :

We have been a landowner in East Naukatu for a period of one year and only recently learned of the proposal to include our area in the proposal to incorporate the City of Naukatu.

Upon learning of this proposal from neighbors I went to Naukatu and spoke with several proponents of this issue. I received the proposed budget and a copy of the preliminary report of which I have studied in the short time available to respond.

In our review of this report it appears the stated objective to maintain roads and provide services to the East Naukatu landowners is an honorable mission. The reality of any significant contribution to our well being with the many issues and obstacles facing the City-Naukatu is questionable.

The continued receipts of fast source funding and other protected income sources seem to be inadequate without the levy of a property tax of which all involved are opposed to.

We see no benefit to East Naukatu landowners who will continue to maintain their roads. We add our objections to the inclusion of this incorporation.

Sincerely - Ed + Cheryl Berney lot 8-Block 3
P.O. Box 19267 - Thruway, AK 99719 I EAST NAUKATU -

RECEIVED

OCT 12 2005

Local Boundary Commission

10/6/05

LBC Staff
Department of Commerce, Community and Economic Development
550 West 7th Avenue, Suite 1770
Anchorage, AK 99501-3510

Gentlemen:

I own Lot 5 Block 3 in E. Naukati. If Sarkar is to be excluded from the Naukati petition for becoming a 2nd Class city then I believe that E. Naukati should be excluded for the same reasons.

Thank you,

Jerry Wilkinson

RECEIVED

Lawrence E. Wilkinson, P.E.

OCT 12 2005

Local Boundary Commission

Consulting Chemical Engineer
P.O. Box 19192 Thorne Bay, Alaska 99919
Phone (907) 723-4507
<Princewalesisland@Hotmail.com>

LBC Staff
Department of Commerce, Community and Economic Development
550 West 7th Avenue, Suite 1770
Anchorage, AK 99501-3510

Dear Mr Brockhurst:

Thank you for coming to East Naukati, Naukati and Coffman Cove. In Coffman Cove you heard how Art King had won a national USFS award for community development. Art was too modest to explain why.

I want to spell out one reason here. The Naukati balance sheet using your format was based on oysters cultured by the homeowners association as being worth between \$0.01 and \$0.03 each. Currently Art and one worker are nurturing 5 million oysters that will be worth \$0.50 each at market size.

Somewhere in your algebraic analysis the wealth of the community should be measured by millions rather than pennies when they are harvested due to the insight of Art and the Homeowner Association.

Sincerely,



Larry Wilkinson
East Naukati Landowner

Naukati West Inc.
NKI Box 1
Naukati, AK 99950
907-629-4266

Dan Bockhorst
Dept of Commerce
L.B.C. Staff

Thank you for the informational meeting in Naukati. The meeting was well attended and many questions about second-class city were answered.

Your letter to me October 7, 2005, you summarized commerce's concerns regarding fiscal viability. I will address each concern beginning with number one.

- 1a. Forest receipt funding can only be used for roads. If funding is reduced or terminated we would reduce road maintenance to that level. The community in the past two years has spent \$1,500.00 per year on road maintenance, most of that was fuel and repair of the community owned road grader.
- 1b. Annexation by Ketchikan Borough or formation of a Prince Of Wales Borough seem to be a ways down the road and we certainly are aware and preparing to deal with that issue.
2. Organizational Grant funds are extended to all Communities to help them form a Government that will succeed. Naukati feels this funding is a welcome aid in forming our Government to function properly. In years 2 and 3 we are posting a municipal reserve. These funds will be used for one-time capital expenses, which will come from the Organizational Grant.
3. Land sales in our budget for the third year are changed to reflect the true value of one commercial waterfront lot selling at \$60,000.00. That figure is reasonable in light of recent residential lots going for \$90,000.00 per lot in the last two sales in Naukati by Mental Health and D.N.R. These lots will most likely appreciate in value in the next two years. Naukati intends to sell three or more lots per year to help develop our waterfront plan in turn generating more income for the city. We have budgeted surveying the second and third year in preparation for the sales. We have budgeted sale of one lot in year three.

Naukati will select all waterfront properties adjoining our waterfront master plan. The University of Alaska did not select any Commercial waterfront land, leaving Naukati the only owner of above-mentioned commercial land without a competitor.

The University of Alaska Land Management Staff has attended a meeting in Naukati, and assured us they would work with us on their land use plans. The City of Coffman Cove has worked with the University and has had great success and we feel comfortable that our relationship will be successful also. They also informed us that DNR would convey the lands to the University in the third year. That is the same timeline DNR gave Naukati.

Naukati is presenting an operating budget that does not rely on any tax. We feel the tax question is very important but should be addressed by the city council once we are incorporated. The City of Naukati most likely would consider a sales tax if needed. Naukati has significant locally generated revenue in the form of the profits from the community owned shellfish nursery. Therefore at this time the tax question is not relevant to the fiscal viability of our community. If a tax issue was present we are absolutely against the tax issue and incorporation being tied together. Each issue has to be on a separate ballot.

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PAGE2

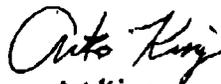
The community of Naukati wishes to retain their original boundary with the exception of the portion that includes El Capitan and Sarkar (see attached map.) The reasons Forest Service Lands are included are:

-The University stands to gain an equal match from the congress to match the lands conveyed from DNR. It is likely they will select near their existing entitlements.

-Sealaska still has nearly one million acres to select from the Tongass, and there is a Sealaska Heritage site near Naukati.

The waters outside Naukati that are included in our original boundaries, but excluded from the boundary proposed by commerce, have several oyster farms. These oyster farms would be subject to a future sales tax and would contribute to the current fish tax.

By amending the boundaries to NOT include El Capitan and Sarkar the community of Naukati accepts the withdrawal of the responsive brief from Mr. Van Valin.



Art King
Petitioners Representative



REVISED AND AMENDED OPERATING BUDGET - Exhibit E

A budget that does not include any form of tax revenue

Projections of city income and expenditures during the city's first three full years of Operation is included in this exhibit.

		Year 1	Year 2	Year 3
EXPENSES	City Clerk (1)	\$13,000.00	\$13,000.00	\$26,000.00
	Insurance (2)	\$10,000.00	\$10,000.00	\$10,000.00
	Elections costs	\$1,000.00	\$1,000.00	\$1,000.00
	Naukati Emergency Response	\$8,000.00	\$8,000.00	\$8,000.00
	Road Maintenance (3)	\$50,371.00	\$50,371.00	\$50,371.00
	Planning (Legal Fees) (4)	\$6,000.00	\$16,000.00	\$16,000.00
	Contractual (4)		\$7,500.00	\$7,500.00
	Land Surveying (4)		\$6,000.00	\$6,000.00
	Office Expenses	\$6,000.00	\$6,000.00	\$6,000.00
	Harbor Maintenance	\$5,000.00	\$7,000.00	\$7,000.00
	R.V. Park (5)	\$4,900.00	\$4,900.00	\$4,900.00
	Shellfish Nursery (13)	\$25,350.00	\$25,350.00	\$25,350.00
	Travel & Membership	\$4,000.00	\$6,000.00	\$6,000.00
CPA fees (6)	\$2,000.00	\$1,500.00	\$1,500.00	

Total Expenses \$135,621.00 \$162,621.00 \$176,621.00

INCOME	Organizational grant		\$50,000.00	\$25,000.00
	Forest Receipts	\$50,371.00	\$50,371.00	\$50,371.00
	PILT	\$17,000.00	\$17,000.00	\$17,000.00
	Shellfish Nursery (13)	\$42,375.00	\$42,375.00	\$42,375.00
	R.V. Park (7)	\$12,000.00	\$13,000.00	\$14,000.00
	Harbor fees (8)	\$3,000.00	\$3,000.00	\$3,000.00
	Land Sale (9)			\$60,000.00
	Trailer (10)	\$4,800.00	\$4,800.00	\$4,800.00
	Fish tax	\$2,828.00	\$2,828.00	\$2,828.00
	Donations, Naukati Functions	\$2,950.00	\$2,950.00	\$2,950.00
	S.E.R.E.M.S. (11)	\$1,166.00	\$1,166.00	\$1,166.00
	Forestry Grant. (12)	\$1,250.00	\$1,250.00	\$1,250.00

Total \$137,740.00 \$188,740.00 \$224,740.00

Difference \$2,119.00 \$26,119.00 \$49,119.00

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PAGE 4

Surplus			
Harbor Reserve Fund		\$5,000.00	\$5,000.00
Municipal Reserve Fund	\$2,119.00	\$21,119.00	\$44,119.00

- 1 This is a half time position. Third year will be a full time position.
- 2 Insurance for all buildings, dock, and all Naukati vehicles.
- 3 Paid for from Forest receipt funds. We plan to maintain all of public roads that are not State maintained. (As Funds allow.) City owned grader.
- 4 Fees to be paid for surveying, engineers etc. for planning & improvements. Some grants require projects to be plan ready
- 5 These figures reflect part time positions and other expenses. With the harbor master receiving free housing, elect, water etc for part of the payment for work.
- 6 First year expense includes audit to change from NCA to City of Naukati. Each proceeding year includes an amount for a certified financial statement, which will be done every year. Includes yearly income tax preparation.
- 7 City owned and operated businesses. R.V. Park @ 10 spaces, 50% occupancy of summer months.
- 8 Revenue from community moorage @ 25 boats x \$10.00 a month.
- 9 Land sale one waterfront commercial lot. Naukati intends to sell three to five lots per year on our commercial waterfront.
- 10 City owned rental unit.
- 11 HMS grant from the State.
- 12 D.N.R. grant for the Fire Department
- 13 These figures reflect a part time position during summer growing season, purchase of spat, and miscellaneous operating expenses, electric, power etc.

Revised Budget That does not include any tax revenue

- Naukati has taken out the tax of 4% from the operating budget.
- Naukati Shellfish Nursery is in the first year of operations and has been able to give Naukati West 20,000.00 in the first year of operation. See Budget for Naukati Shellfish Nursery. Our figures at the time was very conservative. We now have had two years of operations. All of the spat has been paid for, for the year 2006. We have been very successful in the first two years. Our year is not over as of now and we look for one more payment in this year.
- We have taken out the CPMG budget, as it does not apply at this time. We have to have road upgrades and will spend it within our budget of \$50,371.00 from forest receipts.
 - A. Naukati Emergency Response was changed from 5,000.00 to 8,000.00. As of Naukati Budget Report.
 - B. We have corrected the road maintenance.
 - C. Shellfish Nursery income has changed from 32,375.00 to 42,375.00. We feel that this is significantly locally generated revenue from the profits of the shellfish nursery.
 - D. Mobil Home income has increased from 2,400.00 to 4,800.00 a year.

We are saving a substantial amount each year out of our organizational grant; our substantial revenue source is the Shellfish nursery business. And will grow substantially each year.



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PAGE5



KEEP YOUR PIN AND PASSWORDS CONFIDENTIAL

*****AUTOCR**8900
 914 0.9330 AC 0.275 5 3 39
 NAUKATI WEST INC
 NAUKATI WEST SHELLFISH NURSERY
 PO BOX NKI
 KETCHIKAN AK 99950-0550

Account Number: 323710
 Start Date: 09-01-2005
 End Date: 09-30-2005

SAFEGUARD YOUR PERSONAL PIN NUMBERS AND PASSWORDS. IF YOU GIVE OUT ANY OF THIS INFORMATION BY MISTAKE, CALL YOUR LOCAL BRANCH IMMEDIATELY TO REDUCE YOUR RISK OF LOSS.

Account Summary for Business Checking -- 323710

\$ 25,516.21	\$ 11,177.95	\$ 25,011.31	\$ 11,682.85
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Deposit Summary for Business Checking -- 323710

09-06	8,371.29	09-13	1,055.12	09-16	862.50	09-21	889.04
-------	----------	-------	----------	-------	--------	-------	--------

Total Deposits: \$11,177.95

Transactions for Business Checking -- 323710

09-01	Starting Balance				25,516.21
09-01	305 Check - Item Processing	952.50			24,563.71
09-02	310 Check	26.12			24,537.59
09-02	307 Check	156.84			24,380.75
09-06	Deposit		8,371.29		32,752.04
09-06	309 Check	1,133.75			31,618.29
09-07	308 Check	2,519.48			29,098.81
09-08	311 Check	7.40			29,091.41
09-08	315 Check - Item Processing	9.98			29,081.43
09-12	316 Check	322.00			28,759.43
09-13	Descriptive Deposit Night drop		1,055.12		29,814.55
09-13	317 Check	5,723.50			24,091.05
09-14	313 Check - Item Processing	50.00			24,041.05
09-14	318 Check - Item Processing	300.35			23,740.70
09-14	312 Check - Item Processing	885.00			22,855.70
09-16	319 Check	13.65			22,842.05
09-16	Deposit		862.50		23,704.55
09-16	322 Check - Item Processing	68.55			23,636.00
09-16	321 Check - Item Processing	1,604.00			22,032.00
09-20	320 Check - Item Processing	25.20			22,006.80
09-20	314 Check - Item Processing	150.00			21,856.80
09-21	323 Check	909.50			20,947.30
09-21	Deposit		889.04		21,836.34
09-23	324 Check - Item Processing	10,000.00			11,836.34
09-27	325 Check - Item Processing	153.49			11,682.85



10-11-2005 12:52 ARTKING 9076294266

PAGE6

**Naukati Shellfish Accounts Receivable
From September To October 2005**

Seims Seafarms	8/30/05	10,000 20-25mm spat	\$419.38
Darian Seavey	8/23/05	59,000 12-15mm spat	\$1,130.10
Dave Chipman	9/15/05	150,000 20-25mm spat	\$5,379.17
Jeff Hetrick	8/1/05	65,500 18-20mm spat	\$1,732.25
		Total	\$8,660.90

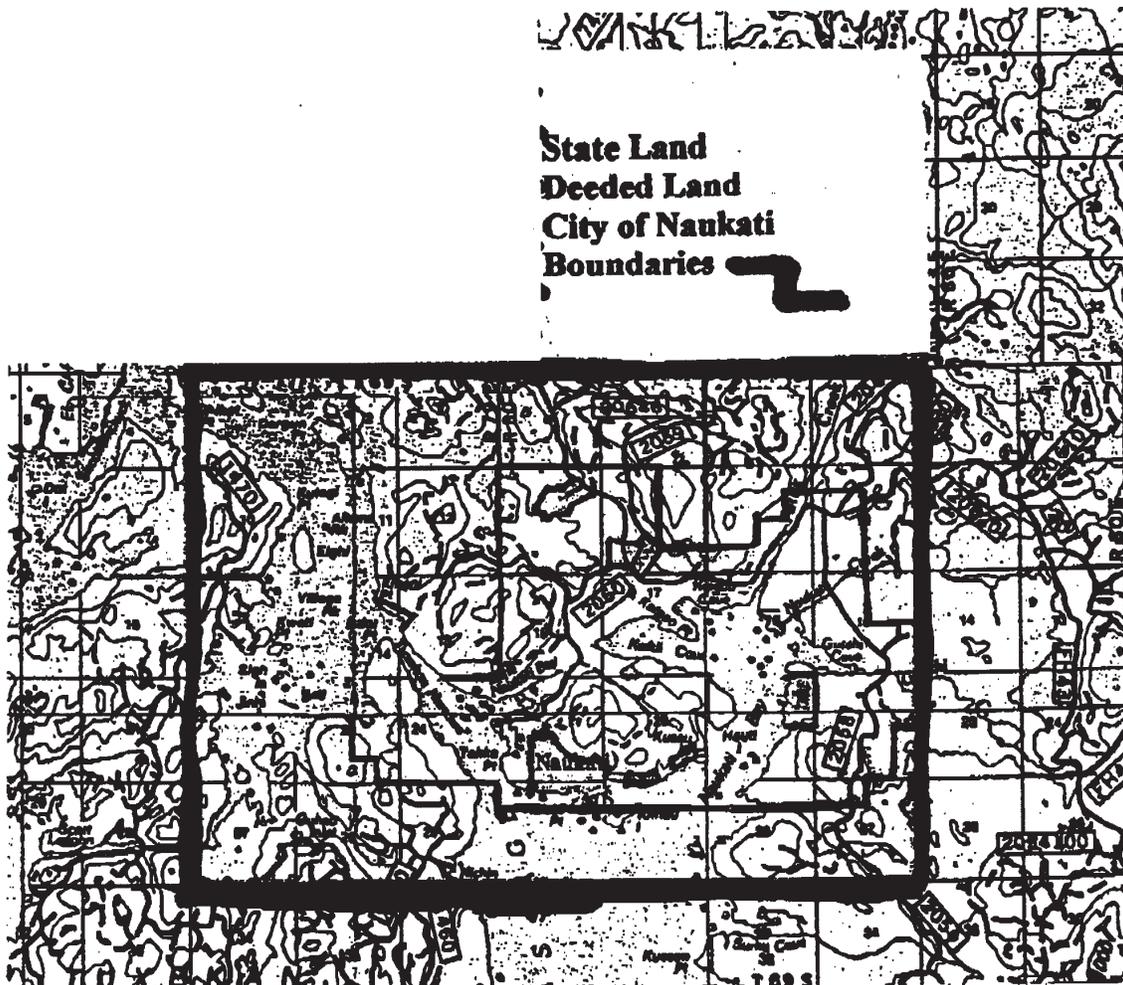
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PAGE 8

Exhibit B

MAP OF TERRITORY PROPOSED FOR INCORPORATION AND OTHER DOCUMENTS
A MAP SHOWING THE TERRITORY PROPOSED FOR INCORPORATION, ALONG WITH PLATS AND OTHER DOCUMENTS NECESSARY TO DEMONSTRATE THE ACCURACY OF THE WRITTEN LEGAL DESCRIPTION OF THE TERRITORY PROPOSED FOR INCORPORATION ARE PRESENTED AS Exhibit B.

A map of the area proposed for incorporation appears below.





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PAGE 7

Arthur King
NKI Box 431
Naukati, AK 99950
907-629-4266

Dan Bockhorst
Dept of Commerce
L.B.C. Staff

Our community is healthy and we are on the move. We also lost some of our population when our logging economy failed. Unlike many other communities we do not have sewer, water, and other services that the community has to financially support. We stepped up to the plate and looked for ways to change our economic base away from timber. Aquaculture came up on our radar screen. With the help of the Marine Advisory Program University of Alaska Fairbanks and Alaska Shellfish Growers Association we determined that a shellfish nursery was needed by the industry. We were successful in getting grants to build a nursery which is community owned. The nursery is operating and sold one million oysters in 2004 and two million so far in 2005. Our goal is production of four million oysters by 2007. Aquaculture is growing throughout Alaska and Naukati has two new farms starting this year. We now have seven oyster farms in the Naukati area which last year hired ten residences seasonally.

We have a brand new 4.1 million dollar school, a fast response vehicle, a refrigerated truck and a new ambulance. We received grants for the three vehicles and presently building a metal building for our new fire hall, which will house our emergency vehicles.

DNR offered 18 lots in Naukati in May 2005 and all sold within 60 days. We expect to offer another sale in 2006. The demand for real estate in Naukati is high.

Naukati has governed itself since 1988 and done a good job. We are responsible and have no debt but we do have an income. I see no reason for our incorporation to be tied to any tax.

If that is a condition we have to meet I fear we will fail at the polls. Naukati is a strong community and I am confident it will become a good second-class city.

Art King
President, Naukati West Inc.



10-11-2005 15:53 ARTKING 9076294266

PAGE1

Claire King
NKI Box 431
Naukati, AK 99950

Dan Bockhorst
Dept of Commerce
L.B.C. Staff

As a community member and landowner of Naukati I would like to say that I think Naukati West needs to become a second-class city. I have lived in the area for 14 years and became a landowner in 1999, I have worked hard to see that Naukati has a viable Volunteer EMS squad, (12 Volunteers) that Naukati has become involved with the Prince of Wales Island EMS, (which represents each community on P.O.W. Island) Local Emergency Planning Commission for Prince of Wales Island, Search and Rescue (12 Volunteers) and the Volunteer Fire Department. (14 Volunteers). There are many others who belong to different organizations that see that Naukati has representation. "POWCAC, Intertie, Southeast Conference, Village Safe Water, Alaska Shellfish Growers Association" etc.

I have seen the progress that Naukati has make in the past few years and everyone has worked very hard to become self supporting, and that Naukati has a say in their destiny. We have had many new landowners move into our community from the last few land sales, they are coming to monthly community meetings and seem to be interested in becoming involved with us.

Naukati has a Shellfish Nursery that has become a great income for the community, and has done better than anyone hoped for in the first two years of operations.

We have been able to purchase and build a Fire Department, (in progress) purchase a fast response unit to fight fires, and a new Transport Vehicle for EMS, these have been from the help of grants and the hard work of the people in the community.

I think that our original boundary should stay the same with the exception of Lil Capitan/Sarkar. I would like to see that the waters we selected stay in our boundary for the shellfish farms that are here and the ones in the future. We have a fast growing Mariculture Industry in Sea Otter Sound.

Looking at the revised budget of Naukati West it is apparent that the new City of Naukati would be able to prosper without a tax of any kind at this time.

Our community has very qualified people that are able to run a City Government. Naukati has had a Homeowners Association since 1988, and have done very well.

I am very proud of our community and it's people who have worked so hard to get to where we are.

Respectfully,
Claire King
Claire King

9 October 2005

Mr. Bockhorst,

My wife and I are owners of property in Naukati Bay East subdivision, lot 2, block 2, which borders Adam & Teresa Basket's property. . It has recently been brought to our attention that Naukati West wants to include our area into their application to become a second-class city. My wife and I are very much opposed to this proposal.

West Naukati does not offer or supply our community (Naukati East) with services of any kind. whether it be electrical, water, sewer or telephone. We maintain our own roads (Naukati West, as you probably noticed, can't even take care of their own roads), electricity is from our own generators and water is collected from the roof and there is no telephone service other than a DC repeater service. We have had our application in to AP&T for this service for over two years. Utilities of any kind, supplied by the state or local government are many, many years down the road. Our community is physically separated just to far away from Naukati West to be effectively part of their community. It takes over 30 minutes to drive Naukati West and our boundaries don't even touch.

The majority of the property owners in Naukati East are not full time residence. There are to my knowledge only two full time residence, Adam & Teresa Basket and Tom Bouy. All other property owners use their property for recreational use and are there only a small amount of time during the summer months.

Please give our request strong consideration. Naukati West offers the community in Naukati East Subdivision absolutely no advantages and they have well document issues in their community that we don't want in ours.

Yours truly,

Patrick & Leeann Thurston

Fw: Boundary of Proposed City of West Naukati

Subject: Fw: Boundary of Proposed City of West Naukati
From: Norman and Brenda Coon <nbcoon@alaska.net>
Date: Sun, 09 Oct 2005 10:05:14 -0700
To: lbc@commerce.state.ak.us

----- Original Message -----

From: Norman and Brenda Coon
To: LBC@commerce.st.ak.us
Sent: Friday, October 07, 2005 9:52 AM
Subject: Boundary of Proposed City of West Naukati

Dan Bockhosark:

The inclusion of East Naukati subdivision into the city of Naukati have no benefits for the landowners.

- We have built all of our roads in order to gain access to the subdivision and the individual lots. These roads are maintained by the landowners to a lot higher standard than the roads in West Naukati.
- No services are received from the town of Naukati. All supplies are obtained from weekly or monthly trips to other towns with more stores than a grocery. Garbage service is not available to us and all landowners haul their garbage to landfills to the south or east.
- We will not have phone and electric service until sometime in the distant future. Everyone provides their own and this is how we approach our needs. This is the way we want it.
- West Naukati should receive their city status if they qualify, but to reach out and use subdivisions miles and miles from them, to help in their qualifications, is wrong.
- Our biggest concern is that if we become part of Naukati, the standards that make us different will have been degraded. Look at subdivisions and you will see what we mean.

Please consider these facts in this boundary decision.

Norman and Brenda Coon
Lot 9, Block 3, East Naukati Subdivision

40815 Belnap Drive
Homer, AK 99603

OCT-10-05 09:14 AM

P. 02

Some valid reasons for not incorporating East Naukati into proposal to make West Naukati a 2nd class city.

- 1. The boundaries of East Naukati are not contiguous with West Naukati.**
- 2. East Naukati is largely unpopulated. (Second class cities have to have 25 inhabitants.)**
- 3. East Naukati has no resources that would benefit West Naukati. There isn't even telephone access.**
- 4. East Naukati has no need for a city government-- most needed services can be obtained through the cities of Craig or Thome Bay (Barge line) large grocery stores etc.**
- 5. Road maintenance will be taken care of by East Naukati Home Owners Assn.**
- 6. 95% of permanent residents of East Naukati do not want to become a 2nd class city.**
- 7. People of East Naukati do not desire to hook up to community facilities such as electricity etc-- They enjoy living off the grid.**

Robert Huestis

Isabel Huestis

**Lot 10, Block. 3
East Naukati**

Mailing Address:

P.O. Box WWP

Ketchikan, AK. 99950-0550

OCT-08-05 07:56 AM

P. 85

Some Valid Reasons for not incorporating East Naukati into proposed to make West Naukati a 2nd class city.

1. The boundaries of East Naukati are not contiguous with West Naukati.
2. East Naukati is largely unpopulated. (Second class cities have to have at least 25 inhabitants.)
3. East Naukati has no resources that would benefit West Naukati. There isn't even telephone access.
4. East Naukati has no need for a city government - Most needed services can be obtained through the cities of Craig or the net bay (large line) large grocery stores etc.
5. Road maintenance will be taken care of by East Naukati Home owners assoc.
6. 75% of permanent residents of East Naukati do not want to be governed by a city (Ovet)



OCT-08-05 07:56 AM

P.06

7. People of east Naukatu do not
desire to hook up to community
facilities such as electricity
& etc. They enjoy living
"off the grid."

Robert Heesters
Isabel Heesters

LOT 10, BLOCK 3
EAST NAUKATI



NAUKATI PROPOSAL

Subject: NAUKATI PROPOSAL
From: Dd7234@aol.com
Date: Sat, 08 Oct 2005 12:01:03 -0400 (EDT)
To: lbc@commerce.state.ak.us

We have received and read the copy of the "Preliminary Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati".

It is our belief, as residents of the Sarkar Cove area, that you have come to the right decision to exclude us from the proposed Naukati City boundary.

As explained in the report, "It was not reasonable and that there is no way Sarkar could remotely be considered part of Naukati".

We respectfully request that the LBC make a final decision to exclude the Sarkar Cove area from the boundaries originally proposed by the City of Naukati.

Sincerely,

ARLYN L. AND DOLORES L. DONNELLY



Exclusion of Sarkar Cove from the City of Naukati

Subject: Exclusion of Sarkar Cove from the City of Naukati
From: Sue&Vern Bauer <sbvb@3dnorth.com>
Date: Sat, 08 Oct 2005 23:06:35 -0700
To: lbc@commerce.state.ak.us

To: Local Boundary Commission,

Re: Department of Commerce's Preliminary Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati

Date: October 8, 2005

We would like to join our neighbors around Sarkar Cove and express our agreement with the Department of Commerce's Preliminary Report which excludes Sarkar Cove from the City of Naukati. We continue to believe, due to our distance from Naukati and the seasonal nature of our homes, that we are not a part of their community and we appreciate the fact that the preliminary report recognizes this.

Sincerely,

Vern and Sue Bauer
Property Owners at Sarkar Cove

OCT-08-05 07:53 AM

P. 02

October 7, 2005

Teresa Baskett
Pres. & Agent of E. Naukati
Community Association
P.O. Box 19549
Thorne Bay, AK. 99919

Mr. Dan Bockhorst
Local Boundary Commission Staff Supervisor
550 W. 7th Ave., Suite 1770
Anchorage, AK. 99501-3510

Dear Mr. Bockhorst:

First of all, I would like to thank you for stopping by and talking to me personally before the meeting on Tuesday the 4th of October. I am happy that you took the time to hear my opinions and concerns regarding this matter.

Secondly, our community of East Naukati was originally named so, as was West Naukati. This is similar to East and West Virginia, North and South Dakota, etc.. Our boundaries don't even touch. They are about 8 or so miles away. We believe that our boundaries should be kept separate as designated in the beginning.

We are a separate community with self-sufficient residents. There are 5 year round residents with our family being 4 of them. Most of the community members are retired and spend a portion of their summer here. We all have our own generators for electricity, we provide our own water, get fuel and propane delivered from Craig and Klawock. We get our groceries from the same and many of us get our mail in Thorne Bay. There is no need for us to get any services or use any from West Naukati. None of these elements will change if we were a part of the incorporation.

During the winter we take care of ourselves. We plow the snow from the road when needed and patch potholes ourselves.

OCT-08-05 07:54 AM

P. 03

The winter residents help one another when necessary.

Most of the land-owners here have paid for a portion of the road that connects their property to the rest of the road system here. This makes us proud of where we are and thus there isn't a problem with teens and 4-wheelers etc. tearing up and down the roads causing more problems with repairs and constant need for improvement. However it has been over 10 years since this community has been established, and now we do need some assistance with road repairs. We KNOW this won't come from the west side.

Our views are the same as the Sarkar area because we are separate and want to remain that way. The residents of East Naukati enjoy the peace and quiet this place has to offer, the serenity of the area, the way we work together as a separate community to help each other here and also being able to live off the grid and enjoy the clean comfortable surroundings we work together to preserve.

There is nothing in East Naukati that would benefit the west side financially or otherwise. There are no public services here to benefit the west side and we don't need a city government at this time.

Please reconsider the boundaries set forth and EXCLUDE the community of East Naukati because we were named as a separate community and would like to remain as such.

We have 2 girls that have been home-schooled since the start of their schooling with the exception of kindergarten for our oldest daughter. The only time they go there is for the testing required by the state. This also can be done in Thorne Bay and could possibly happen this year due to the school system in West Naukati.

In closing, I would like to invite you to call anytime if you have any questions about my cares and concerns regarding this matter of incorporation. (907) 629-4228 Lot 3 BK 2

Sincerely,

The Baskett Family

Alison Baskett
Debra Baskett
Allison Baskett *Faby Baskett*



Comment on Naukati City Incorporation

Subject: Comment on Naukati City Incorporation
From: Morris Ververs <vermor@bigsandytelco.com>
Date: Fri, 07 Oct 2005 10:24:21 -0600
To: lbc@commerce.state.ak.us

To Whom It May Concern:

We have reviewed the Preliminary Report to the Local Boundary Commission regarding the proposal to incorporate the City of Naukati. We are impressed with how thorough and complete the report dealt with the issue.

As homeowners in the Sarkar Cove, we very much agree with the conclusion to exclude Sarkar Cove in the proposed Naukati City boundary. The two locations are simply too far removed geographically and operationally to be a viable governance structure.

Please include these comments in the records of the proceedings of this issue.

Thank you for keeping all stakeholders informed of the deliberations.

Sincerely,

Morris and Verna Ververs
31550 CR 74
Simla, Colorado 80835



CT-07-2005 FRI 01:24 PM

FAX NO.

P. 02

H. CLAY KEENE
GEOFFREY G. CURRALL
HENRY C. KEENE, JR.
BLAKE M. CHUPKA
SHARON G. THOMPSON, PARALEGAL

KEENE & CURRALL
A PROFESSIONAL CORPORATION
ATTORNEYS AT LAW
CURRALL OFFICE BUILDING
540 WATER STREET, SUITE 302
KETCHIKAN, ALASKA 99901

AREA CODE (907)
TELEPHONE 225-4131
FACSIMILE 225-0540
E-MAIL: info@keenecurrall.com

October 7, 2005

~~Deliver to Dan~~

Dan Bockhorst
LBC Staff Supervisor
State of Alaska
Local Boundary Commission
Alaska Department of Community and Economic Development
550 West 7th Avenue, Suite 1770
Anchorage, Alaska 99501

Re: *Opposition to Proposed Incorporation of Naukati as a
Second Class City in the Unorganized Borough
Our File 14.097.B*

Dear Mr. Bockhorst

Scott Van Valin asked that we prepare the enclosed Notice of Intent of Respondent to Waive Objection to Amendments to the Petition of the Proposed Incorporation of Naukati as a Second Class City. The original will be mailed by express mail today.

If you have any questions, please do not hesitate to contact the undersigned.

Very truly yours,

KEENE & CURRALL
A Professional Corporation

H. Clay Keene

Enclosures:

Notice of Intent of Respondent to Waive Objection

cc: Client

(w/copy of enclosure)

OCT-07-2005 FRI 01:24 PM

FAX NO.

P. 03

BEFORE THE LOCAL BOUNDARY COMMISSION

**ALASKA DEPARTMENT OF COMMUNITY
AND ECONOMIC DEVELOPMENT**

In the Matter of the Proposed Incorporation of
Naukati as a Second Class City in the
Unorganized Borough

**NOTICE OF INTENT OF RESPONDENT TO WAIVE OBJECTION
TO AMENDMENTS TO THE PETITION OF THE PROPOSED
INCORPORATION OF NAUKATI AS A SECOND CLASS CITY**

Now comes the Respondent, Scott Van Valin, by and through H. Clay Keene, of the law firm of Keene & Currall, Ketchikan, Alaska, and James A. Van Altvorst, of Van Altvorst & Associates, Ketchikan, Alaska (herein collectively referred to as the "Respondent"), and gives notice of Respondent's intent to waive objection to the proposed amendments to the Petition for Incorporation of Naukati as a Second-Class City within the Unorganized Borough (herein "Petition"), as provided herein:

Respondent has reviewed the Preliminary Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati (herein "Preliminary Report"), issued August 2005, and prepared by the staff of the Alaska Department of Commerce, Community, and Economic Development (herein "Commerce"). Respondent, Scott Van Valin, attended the information meeting provided by the Commerce at the community of Naukati on October 4, 2005, during which Commerce's recommendations, as contained in the Preliminary Report, were discussed in an open forum with Petitioners, Commerce staff and interested persons.

OCT-07-2005 FRI 01:24 PM

FAX NO.

P. 04

Respondent concurs with the analysis, conclusions, and recommendations of Commerce as more particularly set forth in the Preliminary Report. In particular, and specific to the objections raised by Respondent in the Respondent's Brief in Opposition to the Proposed Incorporation of Naukati, dated July 15, 2004, which is incorporated herein by this reference, the Respondent concurs with the following:

a. **The applicable "standards regarding boundaries."** The Respondent concurs with the Commerce's conclusion that the boundaries for the proposed City of Naukati be reduced to those generally described in the Preliminary Report at page 96 in Figure 3-11, which boundaries would exclude the Sarkar Subdivision, and, in particular would exclude the El Capitan Lodge and the Sarkar Cove area from the boundaries of the proposed City of Naukati.

b. **The applicable "standard regarding resources" and in particular, that relating to "the ability of the proposed city to generate and collect local revenue, and the reasonably anticipated income of the proposed city."** Respondent concurs with the proposed amendment to the Petitioner's operating budget that removes the "bed tax" revenue that would be generated by the El Capitan Lodge, located in Sarkar Cove. Removal of the El Capitan Lodge and other properties within the Sarkar Subdivision from the area proposed for inclusion within the boundaries of the proposed City of Naukati will correspondingly require revision to the operating budgets of the City of Naukati that reflect those changes.

Respondent further represents and affirms that if the proposed amendments as summarized in paragraphs a. and b. above, are accepted by Petitioner, and adopted and made part of the Petition, Respondent agrees to withdraw objection to the Petition as



OCT-07-2005 FRI 01:24 PM

FAX NO.

P. 05

thereby amended, and to waive the opportunity for public comment to the amendments that may otherwise be provided. Respondent would ask that if the recommendations of Commerce are adopted and made part of the Petition, that Respondent continue to receive notification of scheduling and copies of all documents thereafter issued by Commerce to interested persons regarding this matter.

In the event either the Petitioners and/or the Local Boundary Commission do not accept the recommendations of Commerce to the Petition as provided in paragraphs a. and b., above, the Respondent reserves all rights to participate, object and appeal the decision of the Commission as otherwise provided in the applicable law and regulations.

Dated at Ketchikan, Alaska this 7th day of October 2005.

KEENE & CURRALL
Attorneys for Scott Van Valin

By H. Clay Keene
H. Clay Keene

VAN ALTVORST & ASSOCIATES
Consultant

By James A. Van Altvorst
James A. Van Altvorst

West Naukati Corporation

Subject: West Naukati Corporation
From: Carol Thompson <caroltstvd@yahoo.com>
Date: Thu, 06 Oct 2005 11:22:47 -0700 (PDT)
To: lbc@commerce.state.ak.us

October 6, 2005

To: Dan Bockhorst

From: Robert Schmidt
East Naukati
Lot #4 Block #2

I do not wish to part of the West Naukati Corporation!

Please re-consider the boundary proposal which would include East Naukati since East and West Naukati are non-continuous boundaries. With this corporation East Naukati would not benefit from power, water, sewer, TV hook-up or fire protection for many years.

I am retired and only use my property in summer.

Yahoo! for Good
[Click here to donate](#) to the Hurricane Katrina relief effort.



Proposed incorporation of Naukati

Subject: Proposed incorporation of Naukati
From: Jerry Hermanson <JHermanson@Hermanson.com>
Date: Thu, 06 Oct 2005 09:33:45 -0700
To: lbc@commerce.state.ak.us

Att: Dan Brockhorst

I am a property owner in East Naukati. I am aware of the proposed incorporation of Naukati which included East Naukati.

I would like to go on record of rejecting that East Naukati be included.

1. We do not have boundaries continuous with West Naukati.
2. West Naukati is 9 miles or 25 min. away
3. In case of fire, we are to far away.
4. We would see no benefits in road improvement
5. We would not be part of the power system

Thank You
Jerry Hermanson



Comments on Naukati City Incorporation

Subject: Comments on Naukati City Incorporation

From: Roland Nehring <rgnehring@earthlink.net>

Date: Sun, 25 Sep 2005 19:09:50 -0500

To: lbc@commerce.state.ak.us

CC: Al & Dolores Donnelly <Dd7234@aol.com>, Ruth Ann Albright <ruthanns@aptalaska.net>, Morris & Verna Ververs <vermor@bigsandytelco.com>, Lee & Leta Falk <letak4u@netzero.net>, Lodge Scott <scott@elcapitanlodge.com>, Vern & Sue Bauer <sbvb@3dnorth.com>

Dear Sirs/ Madams,

Thank you for a copy of your "Preliminary Report to the Local Boundary Commission Regarding the Proposal to Incorporate the City of Naukati" and your Public Notice of the upcoming Informational Meeting.

As homeowners in the Sarkar Cove area, we applaud and support the Department of Commerce's Preliminary Report's conclusion to exclude us from the area of the proposed Naukati City boundary.

For the reasons we outlined previously to the LBC, it is a legal, logical, and a sound financial conclusion due to our lack of community with Naukati, our separation from Naukati by uninhabited USFS lands, our seasonal occupancy, the lack of access from Naukati for emergency and other services due to distance and unimproved roads, and the potential cost for the proposed City to provide traditional facilities to our area. The Naukati core area simply will need to focus on other revenue sources.

We are in Northern Wisconsin for the next month and therefore will not be able to attend your informational meeting on October 4, 2005. Therefore, would you please include these comments in the file and / or record of that proceeding. Thank You.

Yours Truly,

/s/ R. G. NEHRING

Roland and Betsy Nehring

APPENDIX B

COMMENTS FROM UNIVERSITY OF ALASKA OFFICE OF LAND MANAGEMENT

10/20/2005 14:17 FAX 9077867733

LAND MANAGEMENT

002



UNIVERSITY
of ALASKA
Many Traditions One Alaska

October 20, 2005

Dan Bockhorst
Division of Community Advocacy
Alaska Department of Commerce,
Community & Economic Development
550 West 7th Avenue, Suite 1770
Anchorage, Alaska 99501-3510

Re: Naukati Second Class City Petition

Dear Dan:

This letter is in response to your request for information relating to 1) the status of a bill granting additional federal land to the University of Alaska; 2) whether any of the National Forest land within the 44 square mile territory proposed for incorporation as the City of Naukati might be reasonably expected to be conveyed to the University in the foreseeable future; and 3) the location of the State land granted under House Bill 130 in relation to the Naukati Waterfront Master Plan.

Since at least 1997, there have been on-going attempts to grant additional federal land to the University of Alaska. There are two main reasons. The first is a matter of equity. Only Delaware and Hawaii received smaller Federal land grants for higher education than Alaska. The second reason is that the University holds land either claimed by others or within Federal Conservation System Units, title to which the Federal government would like to recover.

The most recent federal legislation was introduced by Senator Lisa Murkowski as Senate Bill 293 on February 3, 2005. The bill provides that the University could select up to 250,000 acres of federal land or interests in land in or adjacent to Alaska, and an additional 250,000 acres as a matching grant, acre for acre, for the State land granted earlier this year by H.B. 130. Under the proposed legislation, it would be possible to select LUD III or LUD IV classifications within the Tongass National Forest, among other federal lands, possibly including interests in off-shore oil and gas leases. There is no requirement that the University select federal lands in the same vicinity as those conveyed by the recent state matching grant.

Much of the interest in S. 293 by federal agencies has been generated by their hopes to recover University land within the Wrangell-Saint Elias National Park and Preserve. House Bill 130 will convey an additional 12,500 acres in this same park to the University. The Letter of Intent accompanying the recent State land grant provides that;

The University may not convey the land to a not-for-profit corporation or to an entity that intends to set the land aside in trust for conservation purposes or non-economically productive uses.

Land Management

3890 University Lake Drive • Suite 103 • Anchorage • Alaska • 99508-4669
Phone: (907) 786-7766 • Fax: (907) 786-7733 • Web: ualand.com

10/20/2005 14:17 FAX 9077867733

LAND MANAGEMENT

003

Dan Bockhorst
Naukati Second Class City Petition
Page 2 of 2

It is not clear whether the conveyance of additional acreage within the Wrangell-Saint Elias National Park or the Letter of Intent will strengthen or dampen agency enthusiasm for the federal legislation. No Congressional action has taken place on S. 293 and it is unclear whether the bill will move anywhere in its present form.

It is much too early to speculate as to what specific lands the University might reasonably be expected to select under legislation similar to S. 293. In making such a decision, the University would have to weigh the relative value of available lands and interests in land. However, it is likely that the University's first preference would be to select lands that would provide long-term, high-value revenue streams such as those generated by oil and gas resources. National Forest lands, with the current climate of litigation and depressed world markets, would appear to be of fairly low interest at this time.

Finally, you asked about the location of the parcels to be conveyed under H.B. 130 in relation to the Naukati Waterfront Master Plan. The parcels to be conveyed by the State (and closest to Naukati West) are located on the north side of Little Naukati Bay (please see attached map). Although the highest and best use of the H.B. 130 grant lands is still to be determined, any development of the new University state grant lands is likely to complement the community's planned waterfront development, not compete with it.

The University plans to work closely with Naukati in designing and developing any subdivision or development of its new grant lands. New residents or commercial developments, either seasonal or year-round, would need services and goods, including those planned to be provided by the new City of Naukati, such as the harbor, boat launch, and emergency medical services. It may be worth mentioning that University land is managed as nontaxable trust land (AS 14.40.291(a)). It will not generate property tax revenues for a local government until it has been developed by or conveyed to private parties.

Thank you for this opportunity to clarify the status of legislation granting the University of Alaska additional federal land. Please do not hesitate to call should you have any additional questions.

Sincerely,



Mari E. Montgomery
Director

Attachment: Naukati Sound Map



APPENDIX C

ANALYSIS OF NAUKATI SHELLFISH NURSERY BY COMMERCE'S OFFICE OF ECONOMIC DEVELOPMENT



OFFICE OF ECONOMIC DEVELOPMENT

Frank H. Murkowski, Governor

DATE: October 25, 2005

TO: Dan Bockhorst, Local Boundary Commission
Nicole Grewe, Division of Community Advocacy

FROM: Glenn Haight, Office of Economic Development

SUBJECT: Naukati FLUPSY Viability

I had a chance to review the material relevant to Naukati West Inc.'s (petitioner) FLUPSY and its potential impact on the revenues for Naukati as an organized government. There is enough information to determine the FLUPSY has the potential to earn the kinds of revenues asserted in the revised budget. However, it is highly unlikely the FLUPSY, or any other business, can increase its revenues without increasing costs. In its revised budget, the petitioner expects to increase the FLUPSY's gross income 31% without increasing costs. I did not find information that indicates how this will be accomplished.

In my guarded speculation, increased revenues without increased costs might come from declines in product mortality or increases in spat price to the local farmers. This office assisted in the construction of the FLUPSY through an economic development grant intended to spur the development of the struggling shellfish farming industry. I hope the FLUPSY's main purpose is not changed to be one of supporting a local government at the burden of this industry sector.

What's a FLUPSY

FLUPSY stands for Floating Upwelling System. This simple, yet ingenious contraption allows baby shellfish seed (which grows into spat) to be kept in a safe environment and "force fed" nutrients in an effort to expedite growth and encourage a faster eating animal. The State funded upwards of four FLUPSYS through the Fisheries Revitalization Strategy, including Naukati's. The Naukati FLUPSY is operational and doing its job by all accounts.

Shellfish Mariculture in Alaska

The shellfish mariculture industry in Alaska is not a huge success story. Producing oysters, clams and mussels, the industry holds a farm value of over \$634,000 in 2004. This is a marked improvement over late 90's figures of around \$400,000. However, in comparison to other Alaska seafood this figure is very small. Salmon ex-vessel (price to fishermen) value is over \$250 million down from upwards of \$500 million in the early 90's. Halibut is moving beyond \$150 million. In comparison to these and other seafood sectors, mariculture is small. The industry is anticipating significant increases in value from the growth of the geoduck industry.

Haight Memo to Bockhorst/Grewe
Naukati FLUPSY Viability
October 25, 2005

While likely only a small up tick on the charts, it is anticipated Hurricane Katrina's destruction of significant Gulf of Mexico oyster production will put pressure on oyster supply around the world. Alaska is a very small player in this industry, but it is reasonable to expect some improvement in sales outside of Alaska, provided the farmers have adequate supply.

Shellfish Mariculture Around Naukati

Naukati is a positive force in the shellfish industry. The community fully appreciates the need to find alternative economies with the timber industry collapse. Naukati worked with the University of Fairbanks, Marine Advisory Program, community members, and shellfish farmers in determining appropriate shellfish farming sites in the area. This "public use" intervention by the community set a positive tone for shellfish farming in the area – not the case in other areas of Alaska.

In an October 11, 2005 fax from Art King to Dan Bockhorst, Mr. King states aquaculture is growing throughout Alaska. Mr. King reported Naukati has two new farms making seven farms total employing 10 residents seasonally.

In an October 11, 2005 email exchange with the Alaska Department of Natural Resource's Aquatic Manager, Guyla McGrady, Ms. McGrady indicated there were five farms currently operating in the Naukati areas with a total capacity of 21.63 acres. None were operating at full capacity. One lessee may be terminated if lease payments are not made, one is at 25% capacity and another lessee, with 10 acres total, is reporting he wants to reduce his overall footprint. Ms. McGrady also indicates that there are no new farms set to begin in the Naukati area, although there is one in Token Bay that might buy from the FLUPSY. Ms. McGrady also indicated Naukati could always sell to farms throughout the state and statewide farms may be interested in buying product.

The Nuts & Bolts

With the little financial information available it is possible to support some of the revised numbers by Mr. King. In a June 2005 field trip to the Naukati FLUPSY, Debbie McBride, OED Grants Administrator, reported Mr. King remarking that the FLUPSY's capacity was 4 million spat, and spat sold for \$25/1000. In Mr. King's October 11 fax, he entered the FLUPSY already sold 2 million spat in 2005. That puts revenues at \$50,000. If this is the case, it is possible that revenues will reach \$40,000 and may increase.

This increase in sales indicates the FLUPSY will most likely face higher costs. It appears unlikely they would improve on their dead loss enough to reduce their seed purchases. Further, it is counterintuitive to positive economic development for the community to increase the cost of spat to the very industry they are intending to boost. When Naukati considers increasing spat costs to the local farmers, I recommend they also consider the potential value of increased returns to the community through a simple local sales tax with a thriving farming industry nearby. The State supported a number of shellfish mariculture economic development projects. Projects like the Naukati FLUPSY were intended to serve as economic development stimulators, not revenue generating engines for cash strapped local governments.

APPENDIX D

PETITIONER'S FURTHER BUDGET REVISIONS (RECEIVED OCTOBER 31, 2005)

October 25, 2005

Dan Bockhorst,

These are the changes in our Shellfish Nursery Figures. We are working in year one on our budget and we calculated on the low side. Our gross for the nursery is presently \$38,000.00. Our fiscal year ends May 1, 2006 so \$42,375.00 certainly is not out of reach. We will increase our spat sales to 3 million in year 2 and four million in year three. The extra expense is for small spat purchase and increased labor. These figures are based on this years actual performance and clearly show the community has significant income. We received an Economic Development Grant for \$24,500.00 for initial start up spat, and due to short supply had \$12,000.00 left over. That \$12,000.00 was used to buy spat that is reflected in our income.

Art King
Naukati West President

RECEIVED
OCT 31 2005
Local Boundary Commission

REVISED AND AMENDED OPERATING BUDGET – Exhibit E

A budget that does not include any form of tax revenue

Projections of city income and expenditures during the city's first three full years of operation is included in this exhibit.

EXPENSES

	Year 1	Year 2	Year 3
City Clerk (1)	\$13,000.00	\$13,000.00	\$26,000.00
Insurance (2)	\$10,000.00	\$10,000.00	\$10,000.00
Elections costs	\$1,000.00	\$1,000.00	\$1,000.00
Naukati Emergency Response	\$8,000.00	\$8,000.00	\$8,000.00
Road Maintenance (3)	\$50,371.00	\$50,371.00	\$50,371.00
Planning (Legal Fees) (4)	\$6,000.00	\$16,000.00	\$16,000.00
Contractual (4)		\$7,500.00	\$7,500.00
Land Surveying (4)		\$6,000.00	\$6,000.00
Office Expenses	\$6,000.00	\$6,000.00	\$6,000.00
Harbor Maintenance	\$5,000.00	\$7,000.00	\$7,000.00
R.V. Park (5)	\$4,900.00	\$4,900.00	\$4,900.00
Shellfish Nursery (13)	\$38,500.00	\$41,350.00	\$46,150.00
Travel & Membership	\$4,000.00	\$6,000.00	\$6,000.00
CPA Fees (6)	\$2,000.00	\$1,500.00	\$1,500.00

TOTAL EXPENSES	\$148,621.00	\$178,621.00	\$196,421.00
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INCOME

Organizational grant		\$50,000.00	\$25,000.00
Forest Receipts	\$50,371.00	\$50,371.00\$	\$50,371.00
PILT	\$17,000.00	17,000.00	\$17,000.00
Shellfish Nursery (13)	\$42,375.00	\$57,125.00	\$76,000.00
R.V. Park (7)	\$12,000.00	\$13,000.00	\$14,000.00
Harbor Fees (8)	\$3,000.00	\$3,000.00	\$3,000.00
Land Sales (9)			\$60,000.00
Trailer (10)	\$4,800.00	\$4,800.00	\$4,800.00
Fish Tax	\$2,828.00	\$2,828.00	\$2,828.00
Donations, Naukati Functions	\$2,950.00	2,950.00	\$2,950.00
S.E.R.E.M.S. (11)	\$1,166.00	\$1,166.00	\$1,166.00
Forestry Grant (12)	\$1,250.00	\$1,250.00	\$1,250.00
Economic Recovery Grant	\$12,000.00		

TOTAL	\$149,740.00	\$203,490.00	\$258,365.00
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Surplus	Harbor Reserve Fund		\$5,000.00	\$5,000.00
	Municipal Reserve Fund	\$1,119.00	\$19,869.00	\$56,944.00

- 1 This is a half time positions. Third year will be a full time position.
- 2 Insurance for all buildings, dock, and all Naukati Vehicles.
- 3 Paid for from Forest receipt funds. We plan to maintain all of public roads that are not State maintained. (As Funds allow.) City owned grader.
- 4 Fees to be paid for surveying, engineers etc. for planning & improvements. Some grants require projects to be plan ready.
- 5 These figures reflect part time positions and other expenses. With the harbor master receiving free housing, elect, water etc for part of the payment for work.
- 6 First year expense includes audit to change from NCA to City of Naukati. Each proceeding year includes an amount for a certified financial statement, which will be done every year. Includes yearly income tax preparation.
- 7 City owned and operated businesses. R.V. Park @ 10 spaces, 50% occupancy of summer months.
- 8 Revenue from community moorage @ 25 boats x \$10.00 a month.
- 9 Land sale one waterfront commercial lot. Naukati intends to sell three to five lots per year on our commercial waterfront.
- 10 City owned rental unit.
- 11 EMS grant from the State.
- 12 D.N.R. grant for the Fire Department.
 - 13 These figures reflect a part time position during summer growing season, purchase of spat, and miscellaneous operating expenses, electric, power etc.

Revised Budget That does not include any tax revenue

- Naukati has taken out the tax of 4% from the operating budget.
- Naukati Shellfish Nursery is in the first year of operations and has been able to give Naukati West \$20,000.00 in the first year of operation. See Budget for Naukati Shellfish Nursery. Our figures at the time was very conservative. We now have had two years of operations. All of the spat has been paid for, for the year 2006. We have been very successful in the first two years. Our year is not over as of now and we look for one more payment in this year.
- We have taken out the CPMG budget, as it does apply at this time. We have to have to have road upgrades and will spend it within our budget of \$50,371.00 from Forest Receipts.
 - A. Naukati Emergency Response was changed from \$5,000.00 to \$8,000.00. As of Naukati Budget Report.
 - B. We corrected the road maintenance.
 - C. Shellfish Nursery income has changed from \$32,375.00 to \$42,375.00. We feel that this is significantly locally generated revenue from the profits of the shellfish nursery.
 - D. Mobil Home income has increased from \$2,400.00 to \$4,800.00 a year.

We are saving a substantial amount each year out of our organizational grant' our substantial revenue source is the Shellfish Nursery Business. And will grow each year.





APPENDIX E

COMMENTS FROM THE OWNER OF NAUKATI CONNECTION REGARDING 2004 GROSS SALES AND PROJECTED 2005 GROSS SALES

Oct 13 05 07:58a

Naukati Connection

19076294236

p. 1

NaukatiConnection
BoxNKI # 430
Naukati Ak.99950
907-629-4104

To: Don Bockhorst

10-13-05

The issue of potential sales tax revenue for the City of Naukati based on the Naukati Connection gross sales receipts for the year of "2004" was \$930,000.00 projected gross for "2005" is \$950,000.00. I'll be looking forward to the next meeting.

Respectfully Submitted

Andy Richter (Owner, Naukati Connection)

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OCT 13 2005

Local Boundary Commission

