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MEMORANDUM April 6, 2011

SUBJECT: HB 142 and the terms of the Alaska Gasline Inducement Act (HB 142; Work Order No. 27-LS0451\B)

TO: Representative Mike Chenault
Speaker of the House of Representatives
Attn: Tom Wright

FROM: Donald M. Bullock Jr.
Legislative Counsel

You asked whether HB 142 constitutes a breach of contract between the state and TransCanada Alaska, LLC and Foothills Pipe Lines Ltd. (licensee).

In my opinion, HB 142 does not constitute a breach of the license terms that form the contract under the Alaska Gasline Inducement Act (AGIA). HB 142 questions whether the project licensed under AGIA has become uneconomic because of the failure to publish "the names of prospective shippers, amounts of capacity awarded, and the terms of the agreements" that were expected to be published on a date stated by the licensee in its Open Season Notice.

The issue of whether commitments to acquire firm transportation capacity were received during the open season that ended on July 30, 2010, is relevant both to the appropriation of money for the ongoing 90 percent reimbursement for qualified expenditures and to the economic viability of the licensed project. HB 142 does not amend AGIA and does not terminate the AGIA license. HB 142 does raise the presumption that if no commitments or insufficient commitments to acquire firm transportation were received during the 90-day open season, the project is uneconomic. HB 142 invites the commissioners to rebut the presumption.

AGIA clearly states that the reimbursement of qualified expenditures to the licensee is subject to annual appropriation.[1] During the consideration of a request for appropriation,

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[1] AS 43.90.110(a)(1):

> (1) subject to appropriation, state matching contributions in the form of reimbursements in a total amount not to exceed $500,000,000, paid to the licensee during the seven-year period immediately following the date the license is awarded; the payment period may be extended by the commissioners under an amendment or modification of the project

legislators may ask questions regarding the amount of the appropriation, what the appropriation will be used for, and the benefit to the state. The licensee could expect that the legislature would review the appropriation request under the Executive Budget Act (AS 37.07), specifically, under the statement of policy in AS 37.07.010 and within the responsibilities of the legislature in AS 37.07.014.

Because the reimbursement of qualified expenditures is subject to appropriation, within the budget process the licensee should expect that the AGIA project would be scrutinized in a manner similar to that in HB 142.

HB 142 creates a presumption based on the failure to disclose firm transportation commitments before July 15, 2011. Whether firm transportation commitments were entered into during or after the open season is a subject addressed by provisions within AGIA and under the federal regulations providing for the conduct of the open season.

Firm transportation commitments are referred to and the effect of making those commitments are addressed throughout AGIA, including, AS 43.90.110(a), 43.90.200, 43.90.240, 43.90.300, 43.90.310, 43.90.320, 43.90.330, and 43.90.450. In particular, firm transportation commitments are a factor to be considered by an arbitration panel

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plan under AS 43.90.210; a payment under this paragraph shall be made according to the following:

(A) on or before the close of the first binding open season, the state shall reimburse the licensee's qualified expenditures at the level specified in the license; however, the state's reimbursements may not exceed 50 percent of the qualified expenditures incurred before the close of the first binding open season;

(B) after the close of the first binding open season, the state shall reimburse the licensee's qualified expenditures at the level specified in the license; however, the state's reimbursements may not exceed 90 percent of the qualified expenditures incurred after the close of the first binding open season;

(C) a qualified expenditure is a cost that is incurred after the license is issued under this chapter by the licensee or the licensee's designated affiliate, and is directly and reasonably related to pursuing firm transportation commitments in a binding open season, to securing financing for the project, or to obtaining a certificate of public convenience and necessity from the Federal Energy Regulatory Commission or the Regulatory Commission of Alaska, as appropriate, or satisfying a requirement of an agency with jurisdiction over the project; in this subparagraph, "qualified expenditures" does not include overhead costs, lobbying costs, litigation costs, the cost of an asset or work product acquired or developed by the licensee before the license is issued, or civil or criminal penalties or fines; . . .

under AS 43.90.240(c) if the commissioners and the licensee do not agree that the project is uneconomic. AS 43.90.240 provides for the abandonment of an uneconomic project.

HB 142 was introduced on February 4, 2011; the open season for the project ended more than six months earlier. According to the "Open Season Notice" issued by the Alaska Pipeline Project (APP),[2] the open season was to begin at "8:00 a.m. CDT on Friday, April 30, 2010 and [end] on Friday, July 30, 2010 at 5:00 p.m. CDT."[3] "Open season" is defined in AS 43.90.900(17) as follows:

> (17) "open season" means the process that complies with 18 C.F.R. Part 157, Subpart B (Open Seasons for Alaska Natural Gas Transportation Projects) or a similar process for soliciting commitments for pipeline capacity under the regulations, policies, rules, or precedent of the Regulatory Commission of Alaska; . . . .

The licensee stated in the Open Season Notice:[4]

> This Open Season is being conducted in accordance with the Federal Energy Regulatory Commission ("FERC") Regulations governing Open Seasons for Alaska Natural Gas Transportation Projects, 18 C.F.R. §157.30 - §157.38, and will provide a non-discriminatory means of awarding capacity to bidders, provided APP receives bids that conform to its requirements and APP decides to proceed with the Project, pursuant to the terms of this Open Season.

The Open Season Notice was published after TransCanada Alaska Company, LLC filed the "Request for Commission Approval of a Detailed Plan for Conducting an Open Season" (Request) with FERC in Docket No. PF 09-11-001, dated January 20, 2010, and FERC issuing the "Order Approving Plan for Conducting an Open Season" (Approval), issued March 31, 2010, in Docket No. PF09-11-001. The Request, Approval, and Open Season Notice are significant because each stated the specific dates for making certain information public that related to commitments and precedent agreements. I have not found an amendment to the dates for certain relevant actions to occur that are stated in the

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[2] APP is the combined effort of the licensee and Exxon Mobil.

[3] Open Season Notice, at p. 1. The Open Season Notice (Notice) is included in volume I of the "Notice of Commencement of Alaska Pipeline Project Open Season under PF09-11," filed with FERC April 29, 2010, p. 6. The notice is published on the Internet at *http://elibrary-backup.ferc.gov/idmws/File_list.asp?document_id=13813012* (accessed April 5, 2011).

[4] Notice, p. 1.

Request, Approval, and Open Season Notice. Accordingly for the purposes of this memo, I presume the dates have not changed.

The specific requirements for the contents of the notice of the open season are in 18 C.F.R. 157.34. Of particular relevance to HB 142 and the conduct of the open season by the licensee is 18 C.F.R. 147.34(c)(13), which reads as follows:

> (c) Contents of notice. Notice of the open season required in paragraph (a) of this section, shall contain at least the following information; however, to the extent that any item of such information is not known or determined at the time the notice is issued, the prospective applicant shall make a good faith estimate based on the best information available of all such unknown or undetermined items of required information and further, must identify the source of information relied on, explain why such information is not presently known, and update the information when and if it is later determined during the open season period:
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> . . .
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> (13) ***The date, if any, by which potential shippers and the prospective applicant must execute precedent agreements***; . . . .

(Emphasis added.)

Given the significance of the commitments made during the open season that are formalized in precedent agreements, and the relevance of firm transportation commitments in the determination as to whether the project is uneconomic under AS 43.90.240(c)(1), the timely execution of precedent agreements is critical.

APP of which the licensee is a part, along with Exxon Mobil, stated in its Open Season Notice that it "will notify each bidder whether they have submitted a conforming bid and will provide a written explanation to those bidders whose bids have been rejected as non-conforming."[5] Provisions relating to final notification and the execution and approval of precedent agreements are included in the Open Season Notice, as follows:[6]

> **Final Notification**
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> On or before November 30, 2010, APP will provide conforming bidders with the final version of the Precedent Agreement.
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> **Execution and Approval of Precedent Agreement**

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[5] Notice, p. 6.

[6] Notice, pp. 7 - 8.

> Following the final notification and following APP Parties approval of each successful bidder's written evidence of creditworthiness, as stipulated in Exhibit B to the Precedent Agreement, *each bidder shall execute the final version of the binding Precedent Agreement and secure all board approvals and internal authorizations necessary to undertake the obligations required by the Precedent Agreement by no later than December 31, 2010.*
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> *Within 30 days of receiving notification of the last of the board approvals and other necessary internal authorizations, and confirmation of execution of the final version of the Precedent Agreement, from all successful bidders, the APP Parties shall secure all board approvals and internal authorizations necessary to undertake the obligations required by the Precedent Agreements and will execute Precedent Agreements.* Precedent Agreements shall not become binding until after the bidder, TC Alaska, and the APP Parties have secured all board approvals and internal authorizations necessary to undertake the obligations required by the Precedent Agreement, and the bidder and TC Alaska have executed the Precedent Agreement.
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> The Precedent Agreement will bind the bidder to execute a firm transportation service agreement ("FTSA") before Project construction commences, and will condition the provision of service on satisfaction or express waiver of the transporter conditions precedent stipulated in the Precedent Agreement.
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> *Within ten days after all Precedent Agreements have become binding, APP will make public the names of the prospective shippers, amounts of capacity awarded, and the terms of the agreements.* Within twenty days after all Precedent Agreements become binding, APP will submit copies of all such Precedent Agreements to the FERC, together with copies of any relevant correspondence with bidders who were not allocated capacity explaining why such bids were not accepted. APP reserves the right to submit such information to the FERC in confidence.

(Emphasis added.)

According to the excerpt above, bidders were required to execute the final versions of the precedent agreements and secure necessary board approval no later than December 31, 2010. I am unable to determine if a bidder executed a precedent agreement by the date specified in the Open Season Notice. There is no expectation of publication of that information in the Open Season Notice.

APP also stated in the Open Season Notice that it would take the necessary steps to execute its commitment in the precedent agreements within 30 days after receiving the bidders' executed and board approved precedent agreements. At the latest, assuming the bidders waited until December 31, 2010, to execute the precedent agreements, APP was to execute the precedent agreements within the first 30 days of January 2011. Furthermore, under the schedule in the Open Season Notice, APP was "to make public the names of the prospective shippers, amounts of capacity awarded, and the terms of the agreements" within 10 days after the precedent agreements become binding. APP was to also submit copies of the precedent agreement to FERC within 20 days after the precedent agreements become binding.

I am not aware of any publication by APP of the "names of the prospective shippers, amounts of capacity awarded, and the terms of the agreements." At the latest, that publication was expected approximately February 9, 2011 (thirty days after December 31, 2010 plus an additional 10 days).

Returning to HB 142, the bill does not amend AGIA. HB 142 does not require the licensee to do anything that it has not already done. The licensee has already conducted its first open season, apparently in compliance with the requirements in AGIA and 18 C.F.R. Subpart B. In compliance with federal requirements, the Open Season Notice set the date for executing precedent agreements. No names of prospective shippers have been published as anticipated in the Open Season Notice. Are there precedent agreements? Has the Open Season Notice been amended to set a new date for executing precedent agreements? Were commitments made during the open season to acquire firm transportation capacity? This information was expected to be published under the Open Season Notice as approved by FERC. It apparently has not been published.

HB 142 does not change the requirements in AGIA. HB 142 raises the question as to whether the project has become uneconomic because there were no commitments or insufficient commitments to acquire firm transportation capacity during the open season that ended on July 30, 2010. HB 142 does not constitute a breach of contract; HB 142 does raise the issue of whether a lack of commitments to acquire firm transportation capacity during the open season have made the project uneconomic under the criteria in AS 43.90.240.

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