

Introductory Remark

Good evening Madame Chair and Senators and Representatives. For the record my name is Dan Fauske and I am the President of your gas-line company, the Alaska Gasline Development Corporation. We are here tonight to present the quarterly Legislative update mandated by Senate Bill 138.

You just heard the technical update from Steve Butt and I think you will agree that the AKLNG Technical Team is doing well progressing the design, engineering, and permitting on the AKLNG Project.

However, the State team is very concerned about the lack of progress on many of the key commercial and fiscal issues. The process we are currently involved in assumes that all parties are equally motivated to getting a project built as soon as possible within reasonable engineering and design constraints. That may have been an unreasonable assumption given the different alternatives and economic considerations of each party. In the State Gas Team's opinion, the progression of the following key agreements will not allow them to be completed in time for a special session this fall:

- Gas balancing negotiations are at a virtual standstill with little progress amongst all parties having been made in the last several months. This is a critical issue that needs to be resolved for the process to move forward;
- Commercial agreements including governance and operating agreements are being negotiated but are not on schedule for a review by the Legislature in this calendar year;
- A Tax Stability Agreement, historically referred to as a fiscal agreement, has yet to be agreed, and there is little common ground between the Parties;
- Provisions for withdrawal by a party which would allow the State to proceed without interruption or delay if a party wanted to withdraw have yet to be agreed. In addition there is no agreement on milestones to insure that the parties are reasonably progressing the project. The failure to meet the milestones with out good cause would result in a loss of the fiscal stability provisions.

Without these foundation agreements, it will not be possible for the State Gas Team to present a project to the Legislature for review this fall. The State Gas Team does not intend to bring an incomplete package to the Legislature and expect a decision from you on a change to the Constitution to give the Producers the tax certainty they desire.

However, there are policy decisions including issues related to the State's participation and interim funding necessary for continuing the State's participation that may need to be resolved by a special session before the end of this calendar year.

On behalf of the State Gas Team, I thank you for your continued support of AGDC and the State's participation in the AKLNG Project.

1. AGDC views the conditions / milestones required to make a decision to proceed to FEED are primarily technical in nature and must include successful delivery of key Pre-FEED work products and deliverables. Those work products are now targeted for completion in early to mid 2016.

2. The deliverables for Pre-FEED are all necessary for a positive FEED decision, and those are clearly addressed by the Pre-FEED Joint Venture Agreement. While those are mostly technical deliverables, there are also commercial agreements that will need to be completed to ensure there is a commercial foundation in place for FEED.

Anticipating that there may be a concern by one or more Producers to make any commitment to enter FEED until the constitutional amendment authorizing the Fiscal Agreement has been passed during the November 2016 General Election, the SOA has offered that if the Producers make a conditional commitment to enter FEED in advance of the general election, the State will fund its share of FEED expenditures, estimated to be \$400-500M, to meet all FEED cash calls through the election, which will be the condition precedent for all Parties to enter FEED officially without further conditions.

3. The State has achieved tentative alignment on a property tax structure subject to MAGPR review that includes:

- Impact payments during construction
- Flow-related property tax mechanism after startup
- MAGPR meeting scheduled Sept 23 in Fairbanks to review property tax proposal
- To discuss alternative legislation to implement property tax structure

4. A decision on TC's role in the equity of the project must be made quickly. The failure to make that decision will substantially impair the ability of the parties to move the Process forward. TC's participation in the project is very expensive for the State of Alaska and reduces alignment between the SOA and the Producers. If TC is in the project, the SOA cannot act as a full partner with the producers, and its information and control over the entire project is reduced. While AGDC currently owns 25% of the LNG facilities, if the SOA terminates the TC relationship, AGDC will own 25% of the entire project. Uncertainty over the status of TC is holding up governance and LLC agreements. DNR retained B&V to do an extensive study of the pros and cons of terminating TC's status in the project. That project has been completed and has concluded that it may be advantageous to the SOA for the relationship to be terminated. If this decision is made, it will be brought before the Legislature and the report and analysis will be provided at that time.

5. No. As stated in my introductory statement, we are very concerned with the lack of agreement on Fiscal Terms. The Governor and his administration firmly believe that inadequate progress has been made in advancing and completing a fiscal agreement for the AKLNG Process.

6. We support bringing a resolution on a Constitutional Amendment to the Legislature only if it is accompanied by key fiscal and commercial agreements that fully describe the State's participation in the Project.

7. Rigdon Boykin is leading the State's Gas Team and is briefing the Governor and me daily. Questions about the team's day-to-day activities and engagement can be directed to me or Joe Dubler.

8. The costs for AGDC for the FEED segment of the AKLNG Process will need to be funded through Legislative Appropriations. It is anticipated that amount could approach \$1 billion. Appropriation authority lies with the Legislature, but it is likely that those appropriations will need to be made from either the Earnings Reserve of the Permanent Fund or the Constitutional Budget Reserve. Once the parties have made a positive Final Investment Decision, a project financing will likely provide the majority of the remaining investment by the State.

9. The process we are currently involved in allows the pace of the project to be dictated by any party. Because of this the State needs to ensure that if the process fails for any reason, the State will be able to continue progressing a project to commercialize North Slope gas. The only way for it to commercialize North Slope gas is if it has access to that gas, which is an underlying principle of the withdrawal process.

Specifically, the State will require the following from each withdrawing party:

- (i) such party's equity in the project company and in the LLC Members' Agreement;
- (ii) Each Producer must agree to sell gas or ship gas through the project; and
- (iii) All rights to receive project data/assets (technical or otherwise) produced during the Pre-FEED process up to the point of withdrawal.

10. In the State Gas Team's opinion a gas balancing agreement among all producers will not occur in time to meet a special session deadline for this fall.

11. DNR to answer.

Concluding Remark

I once again thank you for your continued support of the AKLNG Project. I believe that all of us share the goal of commercializing North Slope gas through a large-scale LNG export project. The timing of large infrastructure projects is critical to their

success, particularly when competing in the global LNG market. We therefore must move a Project expeditiously to completion. I assure you that, even though we are disappointed with the lack of progress in the current process, the State Gas Team continues to effectively represent Alaska's best interests.