TransCanada's AKLNG Participation

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Executive Summary

Background	▪ In June 2014, the State of Alaska (SOA) and TransCanada Alaska Midstream LP (TransCanada) entered into a key agreement authorizing TransCanada to pay the upfront capital costs and hold the State's 25 percent share of ownership in the midstream components of the Alaska LNG (AKLNG) Project. These midstream components are the Gas Treatment Plant (GTP) and pipeline portions of the overall project. ▪ The agreement, called the Precedent Agreement (PA), was based on terms of a Memorandum of Understanding (MOU) between the State and TransCanada signed in December 2013. While the Alaska Legislature was not a party to the PA, it reviewed and debated the terms of the MOU during the 2014 legislative session.
Decision at hand	▪ The State is now faced with a December 31, 2015 deadline to make a decision on whether to take back TransCanada's share and have direct equity participation in the AKLNG midstream. To do so would require termination of the PA. ▪ Under the PA's terms, by December 31, 2015, the State is obligated to either enter into a Firm Transportation Services Agreement (FTSA) with TransCanada or TC will be able to terminate the PA. Alternatively, if agreeable to TransCanada, the State can negotiate to extend the date for entering into an FTSA beyond December 2015.
Recomm-endation	▪ The State administration recommends termination of the TransCanada relationship by December 2015 and replacing it with the State's direct participation in the AKLNG midstream. ▪ The State administration expects this path to allow the State to better manage the obligation the State has for AKLNG midstream costs whether or not the project proceeds, increase the overall economics of the project to the State, and allow the State to have more direct voting rights on key AKLNG issues in return for its investment.

BACKGROUND OF STATE'S PRECEDENT AGREEMENT WITH TRANSCANADA

Context for State's 2014 decision to enter into a Precedent Agreement (PA) with TransCanada (TC)

- **AGIA framework:**
  - TransCanada was the State's licensee under AGIA
  - AGIA work product could not be transferred to AKLNG until after resolution of AGIA abandonment issues (including cost of the work product)
  - AGIA also contained a treble damages provision
  - It was in this context that the prior Administration negotiated an MOU with TC in 2013, and the AGIA Termination Agreement in 2014, to exit AGIA, transition to AKLNG, and sign the PA with TC
- **Entering into the PA with TC**
  - Gave the State a clean off ramp from the TC relationship, now, which it did not have when it entered into the PA for all the reasons discussed above
  - Gave the State time during pre-FEED to begin to develop its in-house capabilities in order to fully consider the option of participating directly in midstream at appropriate off-ramps
  - TC's work on AGIA and APP allowed smooth transition into pre-FEED
  - Entering into the PA with TC for pre-FEED also gave the State time to assess its ability to finance its share of investment in AKLNG without TC
- However, there was an **expectation that project enabling agreements would be defined** before Dec 2015 and enable SOA to evaluate TC role going forward

Key terms of the Precedent Agreement between State of Alaska & TransCanada

TC Owns the State's ~25% Entitlement to GTP + Pipeline

Funds up front midstream cash calls

Technical lead for pipeline during pre-FEED

State to Commit to 20-25 Year Transportation Agreement with TC by Dec 2015 to Pay for Using GTP+Pipe

SOA Ultimately pays TC for all its Costs (including a cost of capital of ~7%)

Both SOA and TC have Milestones & Off Ramps:

SOA Responsible for TC Costs, Regardless of Off Ramps

The Precedent Agreement has agreed upon off-ramps that allows the State to terminate before December 31, 2015

PROJECT STAGE:	PRE-FEED	FEED	FID	CONSTRUCTION
TIMELINE:	2014-2016	2016-2018		2019-2026
PERCENT SPEND:	~1%	~5-6%		~93-94%

OFF RAMPS:

Termination Dec. 31, 2015
Pay TC Dev. Costs of ~$70M[2]
(Incl. TC Internal Costs[3])
SOA also responsible for remaining GTP and Pipeline Pre-Feed costs from Jan-June 2016 of ~$61M[4]

Termination Dec. 31, 2018
Pay TC Dev. Costs of ~$490M
(Incl. TC Internal Costs[3])

[1] Assumes 25% State equity participation
[2] $70M estimate incorporates a $4M credit for an SOA payment to TC for AGIA reimbursement
[3] TC Internal costs include AFUDC and Internal Management Fees
[4] Provided by AGDC based on current approved WP&B for AKLNG and includes an additional 30% contingency

WHAT IS THE DECISION AT HAND?

The SOA is faced with the strategically important decision of whether to terminate the Precedent Agreement with TransCanada

The State has two main options:

1 Terminate the PA by December 31, 2015

State would have to reimburse TransCanada for its costs incurred to date (plus approximately 7% interest) – SOA increases overall equity and voting rights to 25%, which equals the SOA's share of gas

2 Or, assuming TC is willing, Execute an FTSA with TransCanada by December 31, 2015

TransCanada would continue to incur costs on behalf of the SOA unless there is a termination at a later date, at which point the SOA will have to reimburse TransCanada's costs (plus approximately 7% interest)[1]

[1] The State also has a third option, assuming TC is willing: exercise its option to acquire 40% of the equity of the TransCanada entity that will own the 25% of the AKLNG midstream. This option is not discussed in this primer but in general it has many of the same pros and cons associated with option 2 above.

The administration recommends Termination of the Precedent Agreement

Alignment

Currently, the SOA is estimated to receive 25% of the gas from Project; however, with TransCanada's equity participation in the midstream portion of the Project, the SOA only retains approximately 12.5% equity in the project

Voting Rights

Terminating the agreement and increasing the State's voting rights would allow the State to have a more direct say in the decision making process of the project

Economic Benefit

The SOA could realize up to $400 million of additional annual net cash flows from the Project, based on DOR's expectations of State being able to finance cheaper than TC by financing the midstream portion of the Project directly

WHY ARE EQUITY ALIGNMENT & VOTING RIGHTS IMPORTANT?

State does not have direct voting rights for GTP or pipeline

			EM	BP	CP	SOA	Total
UPSTREAM	Gas	PBU/PTU	32%	21%	22%	25%	100%
		=	=	=	=	=	=
MIDSTREAM/DOWNSTREAM	AKLNG Equity & Capacity					CURRENTLY HELD BY TC	
		GTP	32%	21%	22%	25%	100%
		Pipeline	32%	21%	22%	25%	100%
		LNG	32%	21%	22%	25%	100%

PRODUCER SHARE OF GAS IS EQUAL TO PRODUCER EQUITY SHARE IN AKLNG

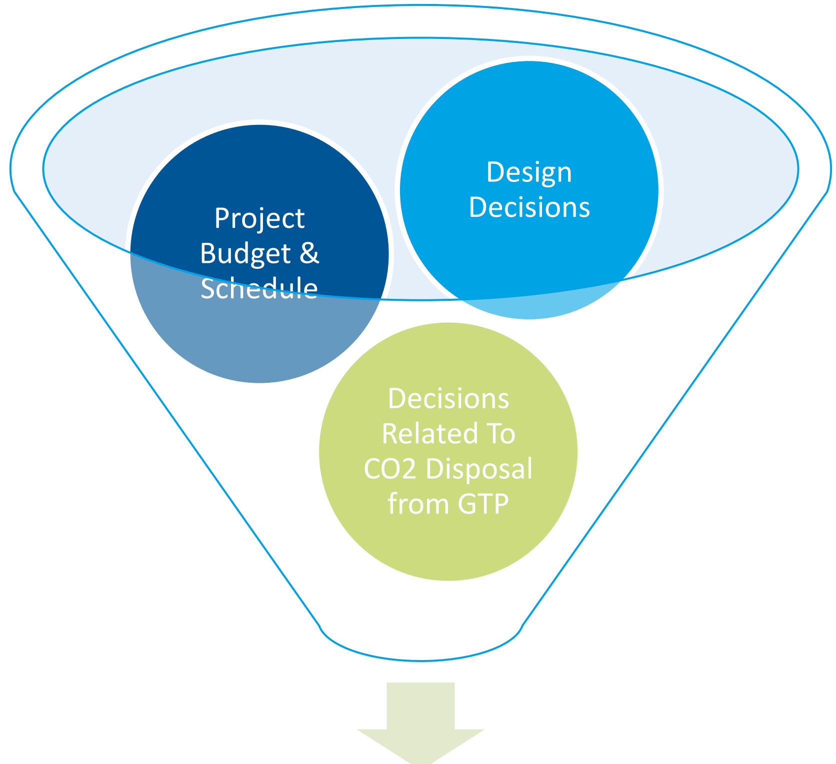
SOA SHARE OF GAS IS NOT EQUAL TO SOA EQUITY SHARE IN AKLNG

Note: All ownership shares shown are approximate and State equity participation is based on production mix from PBU and PTU and the State's royalty share from each field; State equity participation is currently expected to equal 24-25%

Alignment through direct participation will facilitate State influence equivalent to its investment

- TC's decisions driven by shareholder value; not always the same as SOA interests
- Governance and voting rights issues for State's share of project are more complex with TC:
  - **TC votes on GTP and pipeline issues and AGDC votes on LNG issues?**
  - **Share voting rights on issues that impact the whole project?**
  - **Who speaks for the State?**

KEY AREAS WHERE ALIGNMENT IS CRITICAL TO STATE INCLUDE:



STATE'S INTERESTS

WHAT IS THE ECONOMIC IMPACT OF THE TC DECISION FOR THE STATE?

Criteria for evaluating economic impact of TC Participation on SOA

CRITERIA FOR SOA IMPACTS

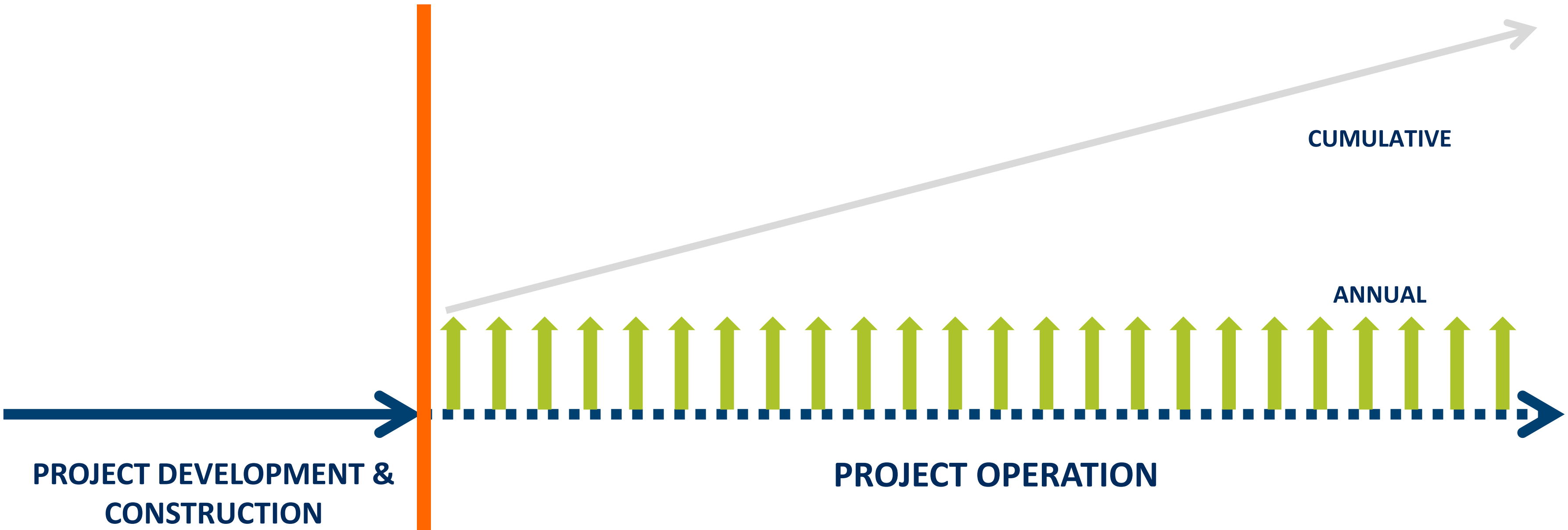
- **Cash flows**
  - Up front cash calls
  - Operational cash flows
- **Net present value**
  - Over a range of discount rates
- **Risk**
  - Incremental risk from TC participation

What are the State's up front cash calls required in the project for the State if the agreement is terminated?

$ Millions	SOA Current Up Front Cash Calls w/ TC	SOA Up Front Cash Calls w/o TC	Total
TC Termination Amount	-	~$70[1]	~$70
AGDC Pre-FEED[2]	~$66	~$61	~$127
FEED	~$365	~$310	~$675
Construction[3]	~$6,500 - $7,900	~$6,500 - $7,800	~$13,000 - $15,700

[1] TC Termination Amount includes TC Internal Costs (AFUDC + Management Fees) and a credit of ~$4M for SOA payment to TC for AGIA reimbursement
[2] Provided by AGDC based on current estimated WP&B for AKLNG. Includes prior AGDC pre-FEED appropriations.
[3] Range of costs is based on current estimates to 20% cost overrun
Note: Estimates do not include AGDC internal costs or agency fees

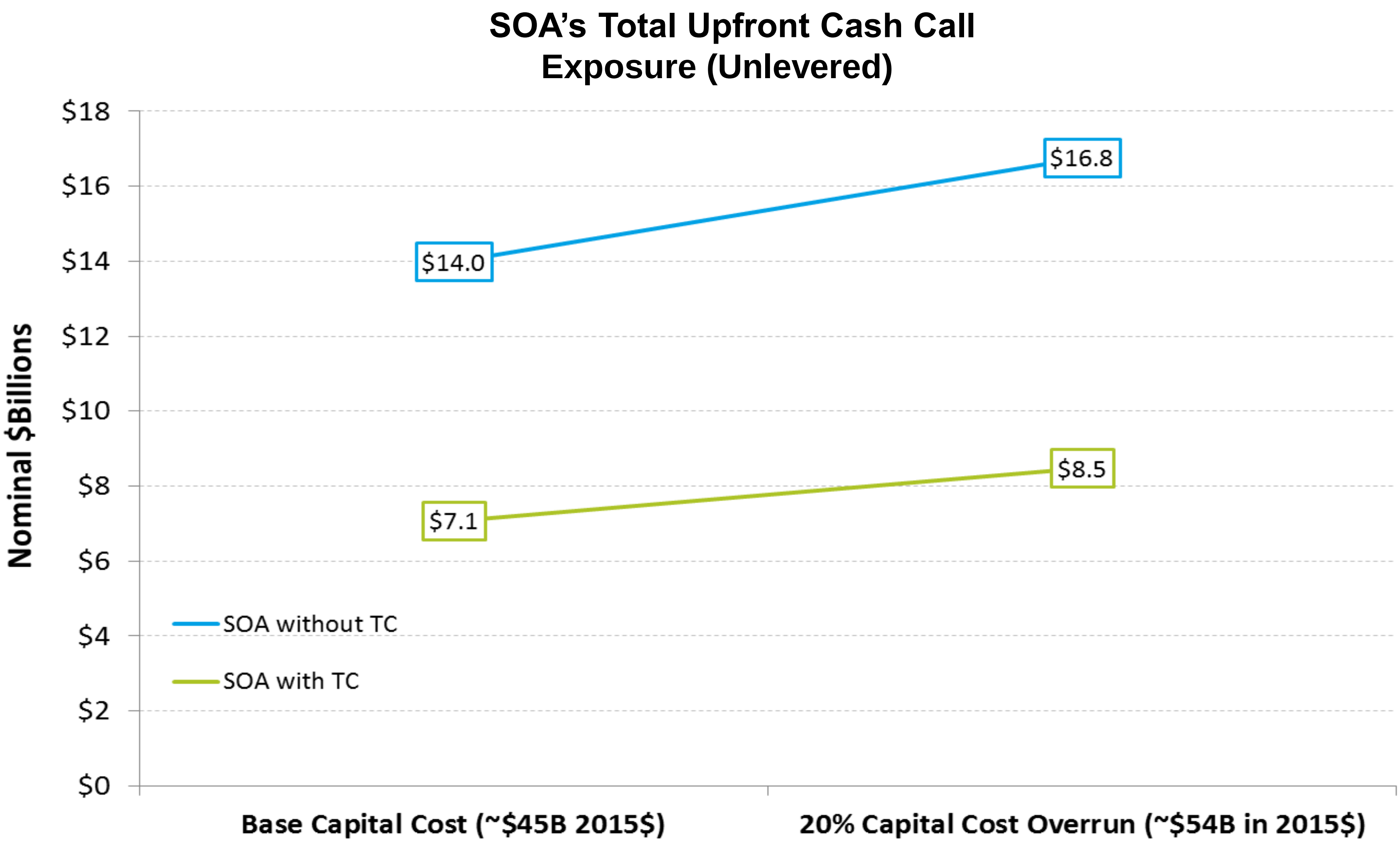
Economic impact to the State is driven by a trade-off between higher upfront investment and higher operational cash flows or lower up-front investment with lower operational cash flows



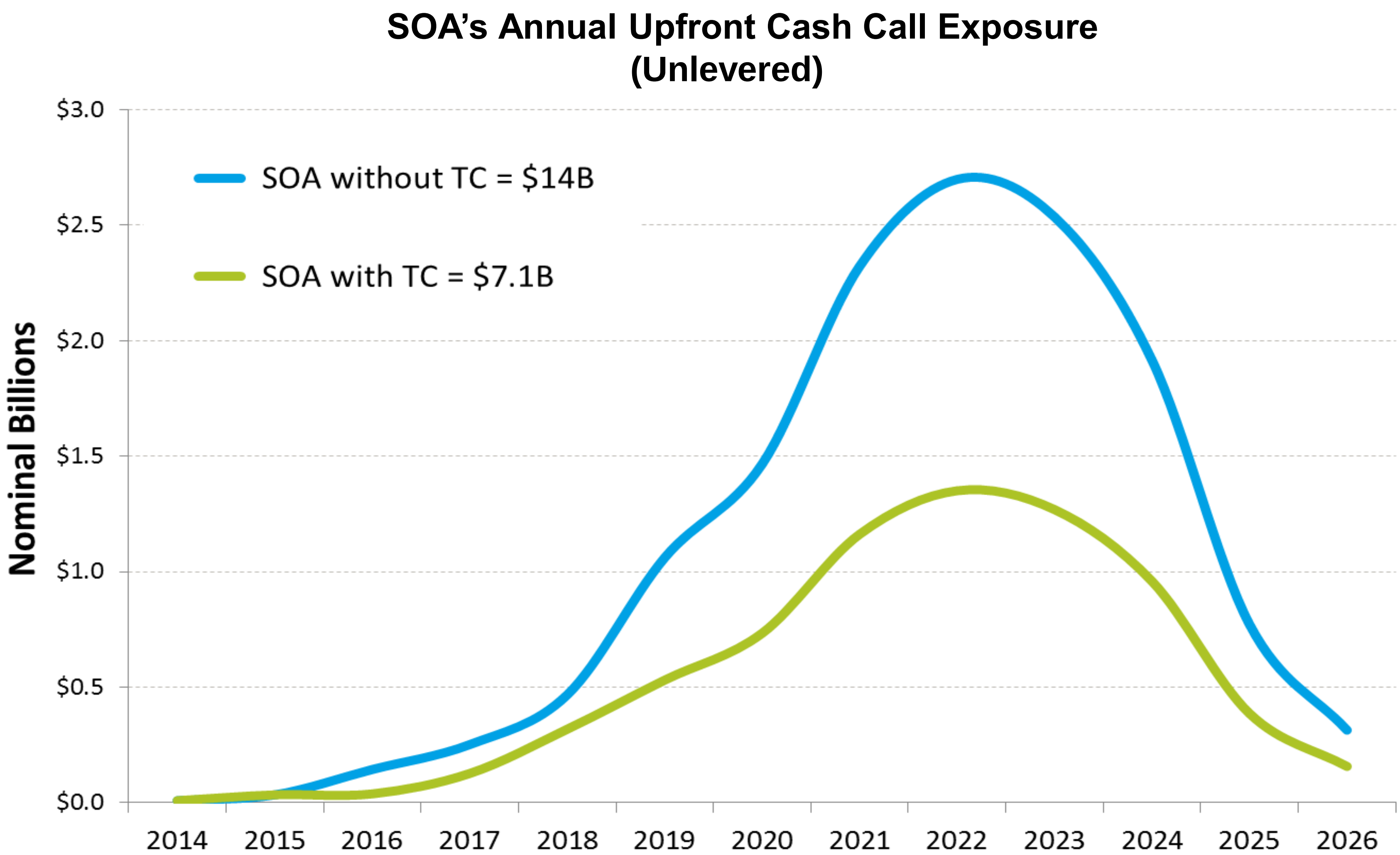
State's up front cash calls for GTP and pipeline would be higher without TC

Economic analysis examines the net impact of higher up front payments in exchange for higher cash flows (through lower tariff expenses) over the initial 20 year period of operation

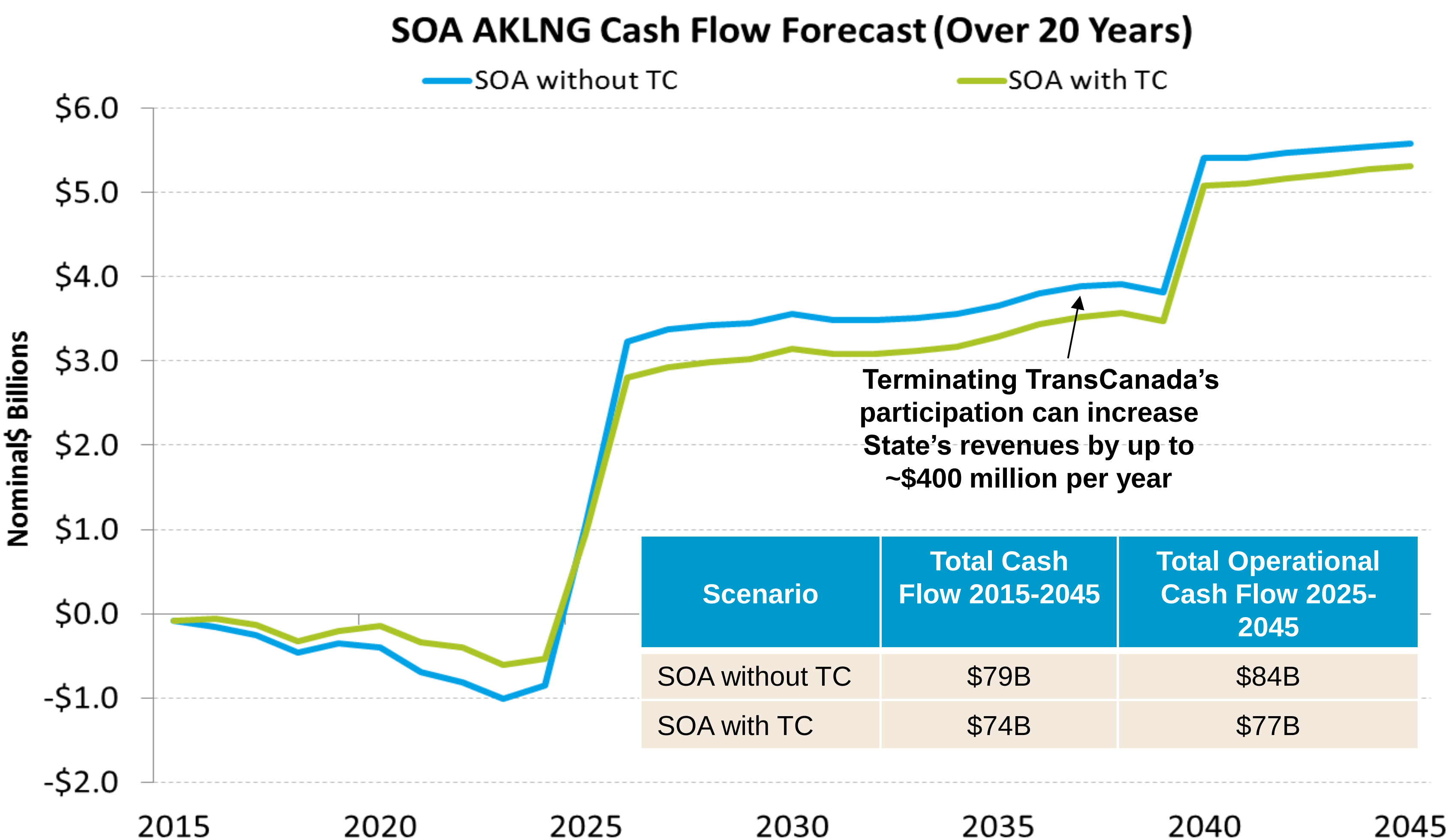
SOA's total upfront cash call exposure is $6.9-8.3B higher without TC participation



SOA's annual up front cash calls in the AKLNG project are expected to nearly double without TC



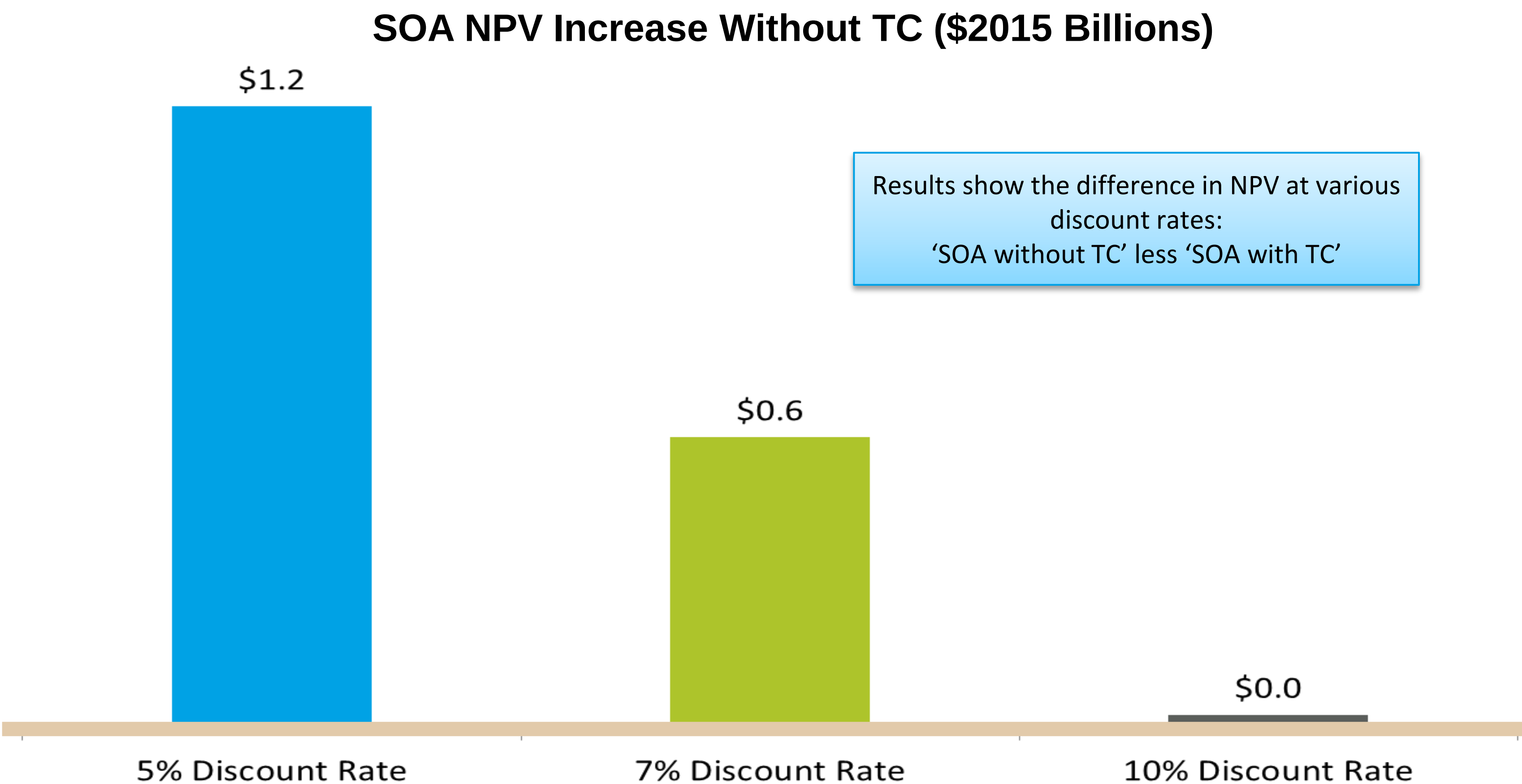
Once operational, SOA is expected to receive annual cash flows of up to ~$400 million higher without TC[1]



Scenario	Total Cash Flow 2015-2045	Total Operational Cash Flow 2025-2045
SOA without TC	$79B	$84B
SOA with TC	$74B	$77B

[1] Based on DOR's assumption that the State can finance it share cheaper than TC

NPV increase to the State without TC can be between $0-1.2B over 20 years



Results show the difference in NPV at various discount rates:
'SOA without TC' less 'SOA with TC'

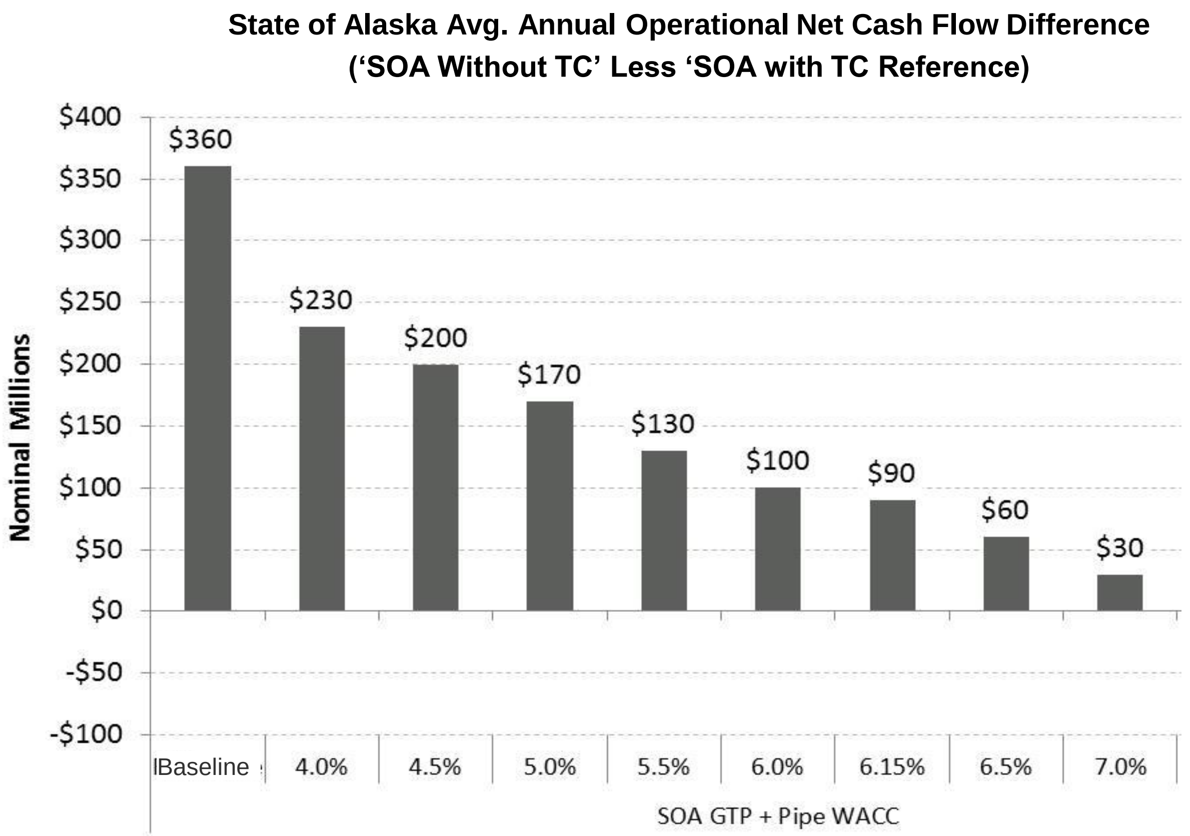
5% may be seen as a proxy for SOA's Cost of Borrowing

7% may be seen as a proxy for Permanent Fund returns

10% may be seen as a proxy return for a commercial investment

The economic benefit of replacing TC could vary based on the SOA's credit rating

- The State could potentially achieve up to ~**$400 million incremental annual cash flows,** based on the State's expected lower cost of capital
- The State's cost of capital would increase with any credit downgrades
- Even if the State's credit rating deteriorates and results in a higher cost of capital for the State, it is still expected that the State will achieve additional annual cash flows without TC



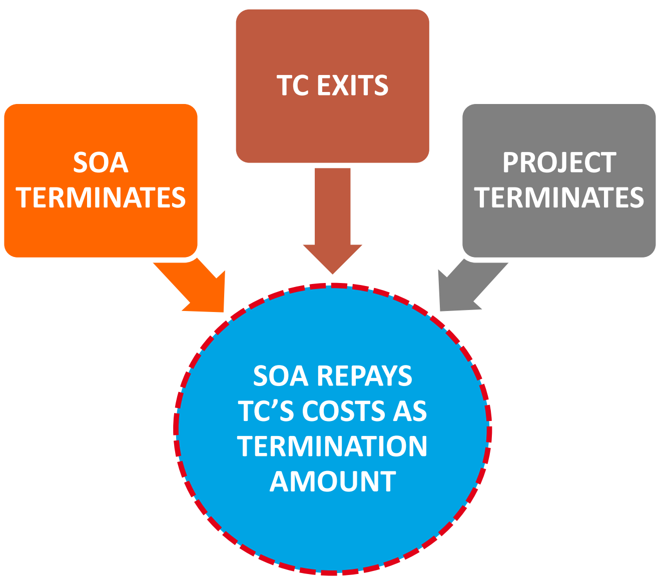
TIMING OF DECISION

Why terminate the agreement with TransCanada now?

Manage Financial Risk	▪ State owes TC its costs plus interests, regardless of project completion ▪ If project fails: Keeping TC in longer and terminating later means that State would need to make a bigger and more expensive payment later ▪ If project succeeds: State is expected to be able to finance cheaper than TC, potentially saving hundreds of millions a year
Avoid Back-in Rights	▪ Unlike the PA, the proposed FTSA is expected to include a commitment to give "back-in" rights for TransCanada, which states that within five years of exercising its termination option, if the State participates in a pipeline project substantially similar to the AKLNG project, the State would need to offer TransCanada an option to participate ▪ Terminating TC's participation now would give the State a clean off-ramp without needing to offer any back-in rights
Influence Project Decisions	▪ As the Project progresses towards the end of the Pre-FEED phase, certain key decisions are slated to be made in the next six months ▪ Due to fundamental difference between the SOA's primary design criteria and the producers', terminating the PA and increasing the SOA's voting rights may allow the SOA to have a more direct say in the decision making process immediately

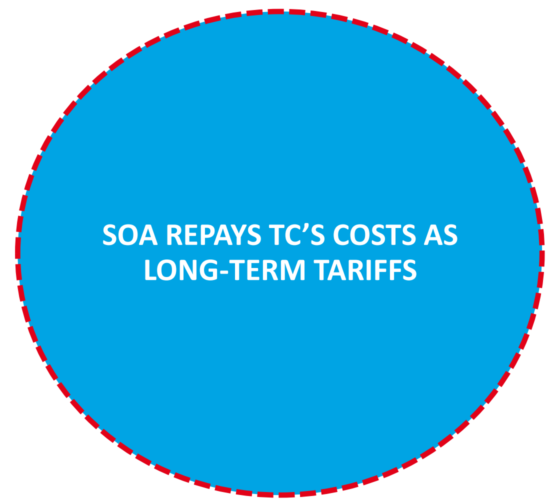
Per prior agreements, SOA is always obligated to repay TC's costs[1]

IF PROJECT DOES NOT MOVES FORWARD WITH TC



> Project development risk is borne by SOA

IF PROJECT MOVES FORWARD WITH TC



> SOA pays TC tariff regardless of price or volume risks

[1] TC costs to be repaid include its share of AKLNG work plan and budget, AFUDC, and internal management fees

Stakes get higher as Project proceeds through stage gates

2014-2016	2016-2018	2019-2025
PRE-FEED	FEED	FINAL INVESTMENT DECISION (FID) FOLLOWED BY CONSTRUCTION
Moving from "selecting concepts" towards more detailed engineering ~1% of total project spend Many LNG projects "die" during this stage	Substantially refine project design basis 5-6% of total project spend Few LNG projects get to FEED and then "die"	Turn dirt (!) 93-94% of project spend Long-term gas sales agreements in place Financing in place

Less Uncertainty And Increasing Commitments

Avoid Back-In Rights for TransCanada

- The proposed FTSA is expected to include a commitment to give “back-in” rights for TransCanada.

- The back-in right states that within five years of exercising its termination option, if the State participates in a pipeline project to commercialize North Slope gas that is substantially similar to the AKLNG project, the State would need to offer TransCanada an option to participate in the GTP and pipelines of that project under similar terms.

- Terminating TC’s participation now would give the State a clean off-ramp without needing to offer any back-in rights.

Influence Key Near-Term AKLNG Decisions

- There is a fundamental difference between the SOA's and the producers' (and potentially TransCanada's) primary decision criteria
  - Lowest cost vs. Most value for Alaskans
- Certain key decisions are slated to be made in the next six months
- By terminating the agreement with TransCanada, the SOA would gain voting rights equal to its gas share and have a more direct influence over key technical decisions related to the midstream such as:
  - By-product handling
  - Project budget
  - Schedule for the midstream portion
- In addition, terminating the PA with TransCanada is expected to facilitate simpler and more efficient resolution of voting rights in AKLNG governance agreements currently being negotiated

WHAT ARE OPTIONS FOR THE STATE TO FINANCE ITS SHARE OF MIDSTREAM AKLNG COSTS WITHOUT TRANSCANADA?

What are the options for the State to finance its share of AKLNG Midstream without TransCanada?

- The State will have the following options to pay the TC Termination Amount and finance its share of the Project during the remainder of Pre-FEED, FEED and the construction period[1]:
  - The Legislature could appropriate from existing State funds, e.g., the Constitutional Budget Reserve Fund (CBRF), Earnings Reserve Fund, etc.
  - The Legislature could authorize the issuance of State debt
  - The Legislature could authorize pursuit of project financing
  - The Legislature could authorize the pursuit of funding from other sources: LNG buyers and other potential equity investors

[1] These are the same funding options for the LNG Plant if TC remained in the Project

Will termination of the agreement affect the State's credit rating?

FirstSouthwest advises that a decision to terminate the TC's participation will not, in and of itself, result in a downgrade of the State's credit rating:

- No incremental commitments by the State
- As the State's overall costs related to the Project are projected to be reduced without TC (B&V estimates a reduction of up to $400 million per year), the termination should be viewed by the credit ratings agencies as a net positive for the State
- With or without TC, the State should anticipate a reduction in the State's credit rating during the construction period (when no gas sale revenues are being generated)
- Credit rating should recover once gas sale revenues become established
- TC's exit, by itself, should not result in a credit downgrade during the construction period that is greater than any downgrade if TC remained in AKLNG. The State's credit could instead be improved by the lower costs to the State as a result of TC's exit

HOW CAN THE STATE REPLACE TRANSCANADA'S TECHNICAL ROLE IN THE PROJECT?

What is TC's technical role in the AKLNG Project?

- TC is experienced in northern pipelines and leads the pipeline technical work for AKLNG

- TC in its current role performs or has performed several functions including the following:
  - Holds State of Alaska's midstream equity in AKLNG as signatory to the JVA
  - Contributes pipeline SMEs that were seconded to the JVA PMT
  - Coordinated FERC NEPA Process

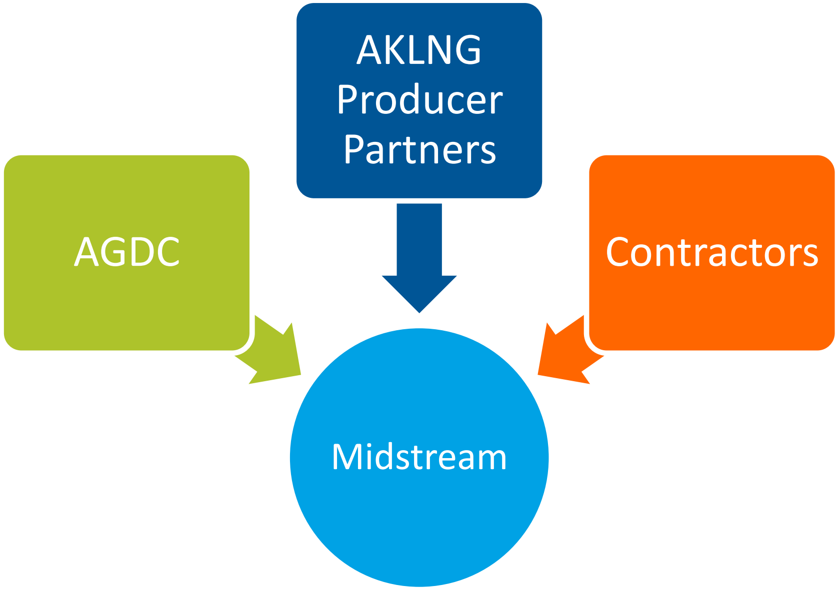
How will TransCanada's technical expertise be replaced?

- TransCanada is not anticipated to build the pipeline, that will be managed through the AKLNG Project Management Team (PMT) which leads and guides the AKLNG project
- PMT consists of Co-Venturer (CoV) employees seconded to project based on experience and skill sets
- PMT hires engineering and specialist contractors to advance design efforts
- Significant amount of work is done by contractors with oversight by PMT

How will TransCanada's technical expertise be replaced?

- AKLNG Project partners bring significant experience
- In addition, AGDC brings Alaska pipeline experience
  - Successfully completed Pre-FEED and FEED on ASAP
  - Key subject matter experts based in Alaska
  - AGDC has already taken over TC's role in coordinating NEPA process

The AKLNG Project partners have worldwide experience and resources to be able to step into the pipeline technical lead role played by TC



Conclusions & Recommendations

The current arrangement with TransCanada was designed to provide the State (and TransCanada) with several off-ramps as the AKLNG Project moved through its different development stages, including an important clean off-ramp for the State in December 2015

The State administration recommends termination of the TransCanada relationship by December 2015 and replacing it with the State's direct participation in the AKLNG midstream

The exercise of this off-ramp is expected to facilitate better alignment and control, lower risk and create additional value for the State in the AKLNG Project over the long-term