BUILDING A WORLD OF DIFFERENCE

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RISK OF MISALIGNMENT IN AKLNG PROJECT

EXTRACT FROM ALASKA NORTH SLOPE ROYALTY STUDY

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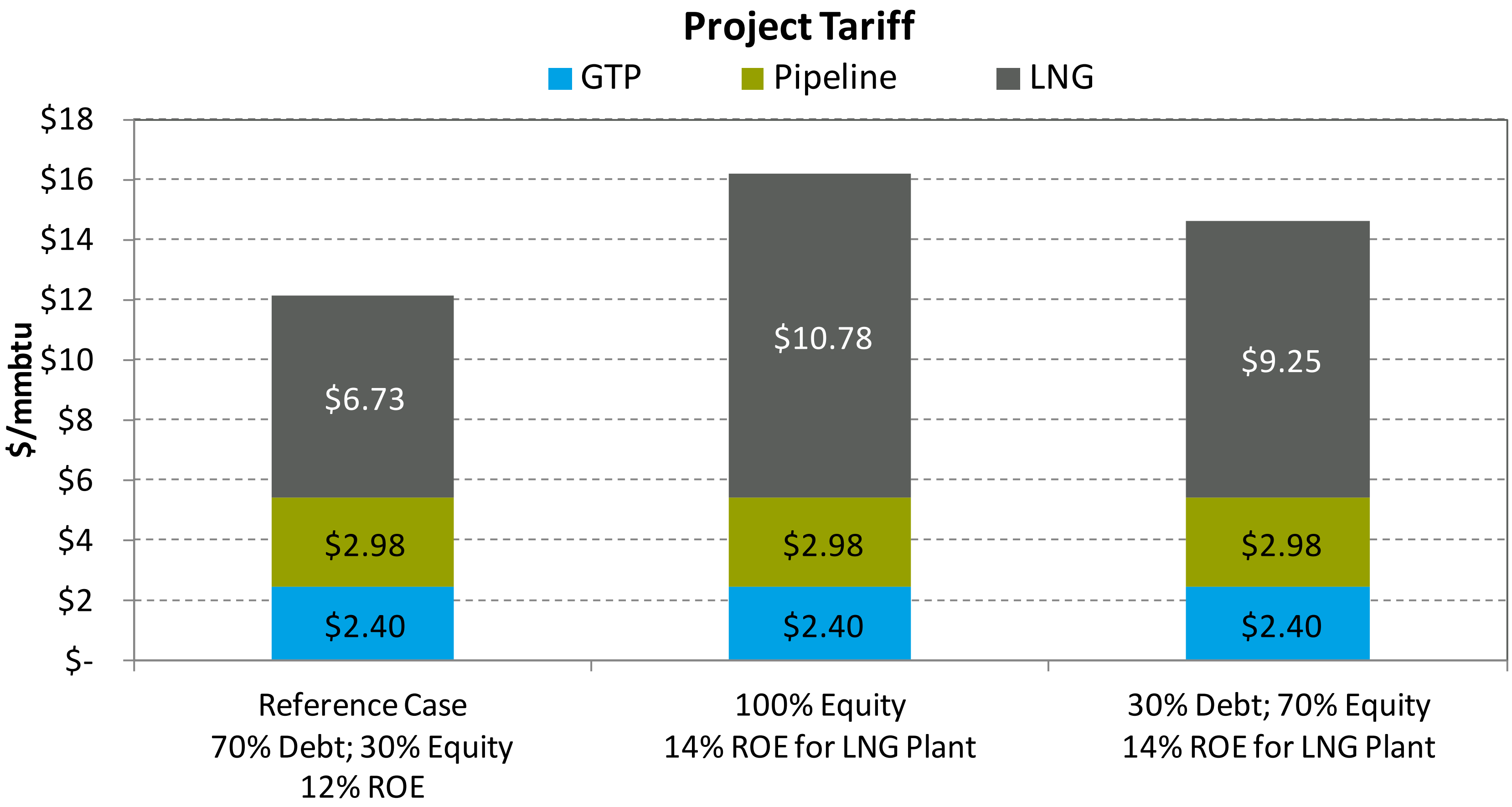
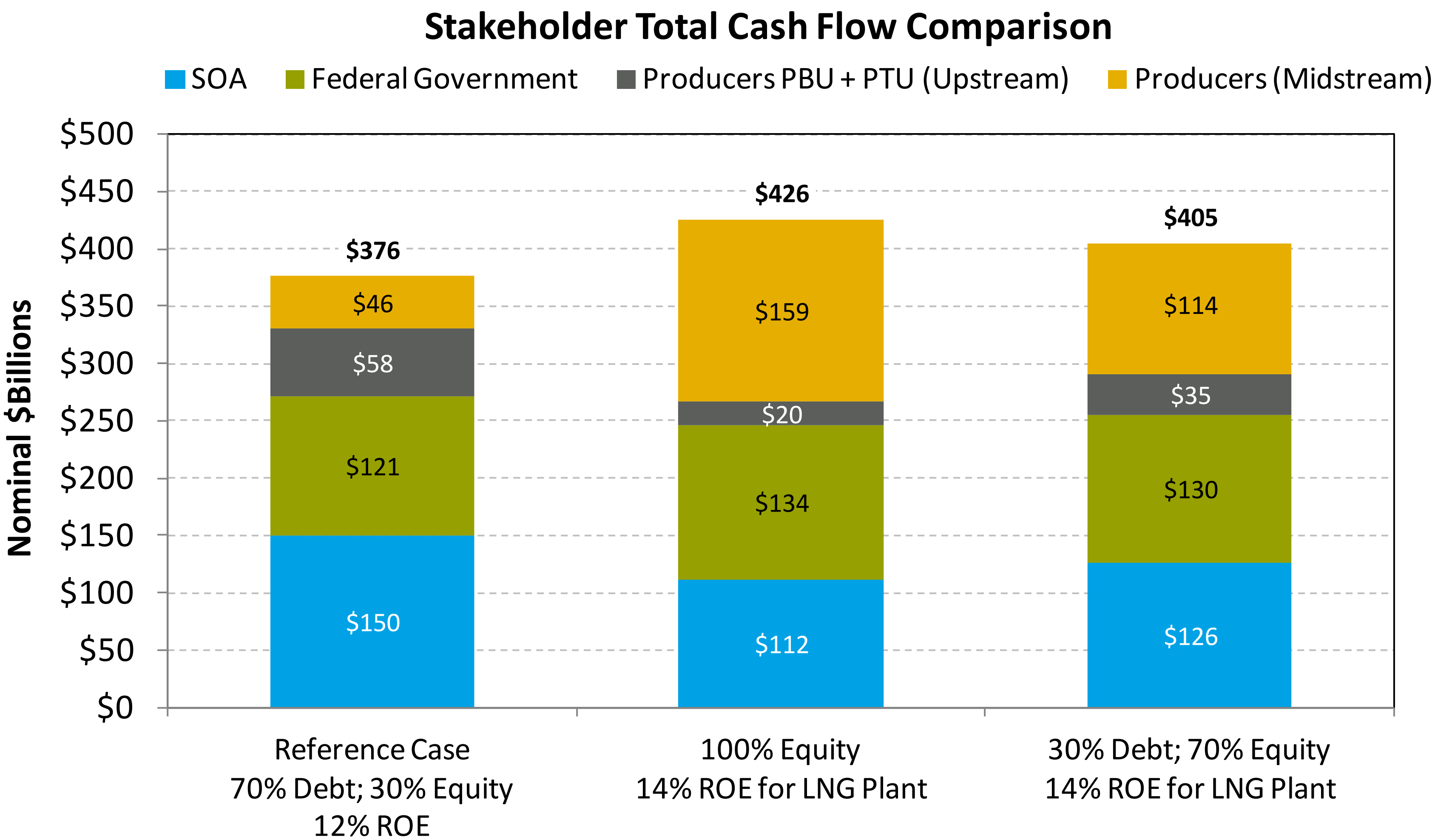
COMMERCIAL STRUCTURE OF AKLNG PROJECT COULD DRIVE MISALIGNMENT BETWEEN THE STATE AND PRODUCERS

- **A Producer-owned project creates risk for the State related to its fiscal revenues due to potential misalignment of interests between the Producers and the State**
- **Under various alternate project structures contemplated, there could be incentive for Producers to shift revenues between the upstream and the midstream segment of the project, as a way of increasing Producer take (and thereby reducing the State's take) from the project**
- **This analysis examines a scenario where the LNG plant's service rates are established using an equity-rich financing structure and with a relatively high return on equity**

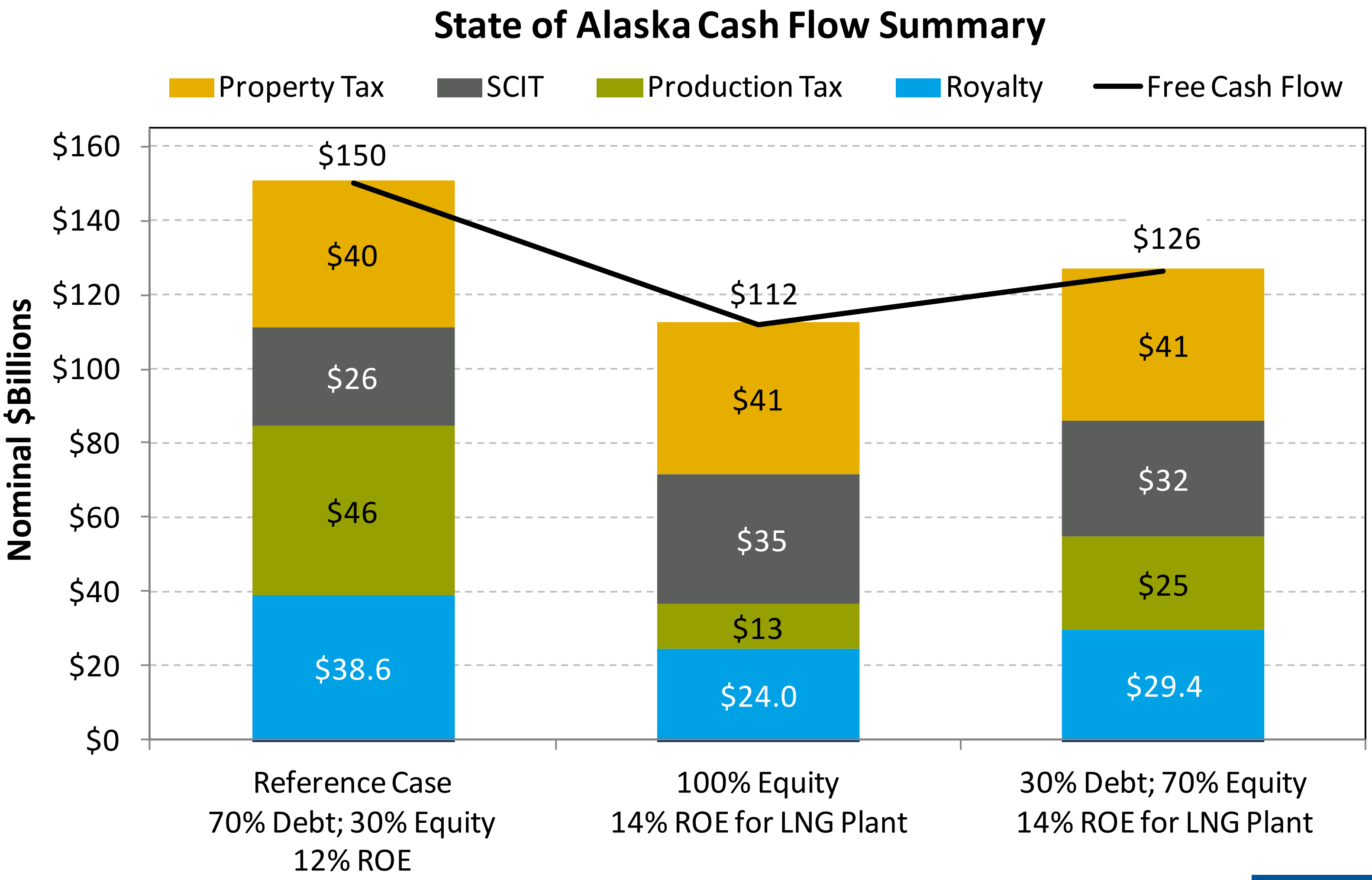
EQUITY-RICH FINANCING STRUCTURE DRIVES A HIGH TARIFF FOR LNG PLANT



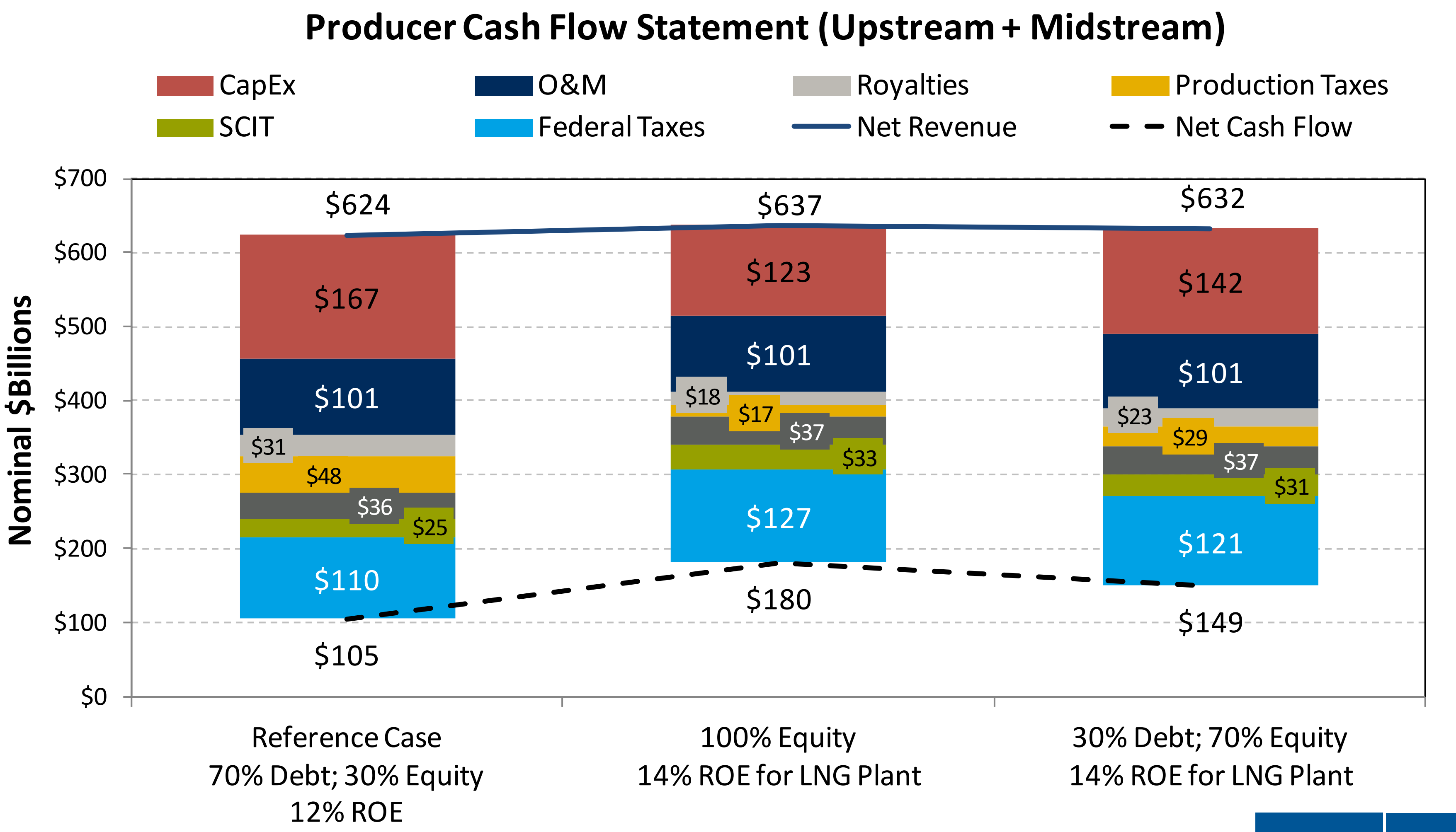
PRODUCERS GAIN NET CASH FLOWS THROUGH THEIR MIDSTREAM COMPONENTS AT THE EXPENSE OF THE STATE



STATE COULD POTENTIALLY LOSE BILLIONS OF DOLLARS OF VALUE FROM AKLNG PROJECT THROUGH MISALIGNMENT



PRODUCERS COULD GAIN TOTAL CASH FLOWS WITH MORE EQUITY AND HIGHER ROE FOR THE LNG PLANT



IT IS CRITICAL TO CREATE ALIGNMENT BETWEEN STATE AND PRODUCER INTERESTS TO ENABLE STATE RECEIVING ITS FULL SHARE OF VALUE FROM THE AKLNG PROJECT

- **Although the State could use regulations as potential safeguards, there is potential for misalignment of interests between the Producers and the State in a producer owned project**
  - Areas of potential misalignment include need for transparency, open access and low tariffs
- **Transparency within a producer-owned project into costs and cost allocation is likely to be an ongoing challenge for the State**
- **The risk of misalignment is higher with an LNG project than with a pipeline project driven by the absence of regulation of the LNG plant's commercial structure or rate setting mechanism by FERC and other pertinent authorities**
- **Creating alignment between the State and Producers is critical for the State to receive the full value of the AKLNG project**

EXECUTIVE SUMMARY – CONCLUSIONS

- Direct state equity participation in the project can provide key benefits to the State including :
  - Create alignment of interests;
  - Create transparency through the midstream portion of the supply chain;
  - Facilitate third-party access to the mid-stream;
  - Potentially increase State cash flows, and improve producer economics.