

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS

March 28, 2001

3:10 p.m.

MEMBERS PRESENT

Representative Scott Ogan, Chair
Representative Hugh Fate, Vice Chair
Representative Fred Dyson
Representative Mike Chenault
Representative Vic Kohring
Representative Gretchen Guess
Representative Reggie Joule

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE CONCURRENT RESOLUTION NO. 8

Expressing the legislature's opposition to the proposed "northern" or "over-the-top" route for a natural gas pipeline to transport North Slope natural gas reserves to the domestic North American market, and expressing the legislature's support of commercialization of North Slope natural gas for the maximum benefit of the people of the state.

- MOVED CSHCR 8(O&G) OUT OF COMMITTEE

HOUSE BILL NO. 83

"An Act relating to natural gas pipelines, providing a statutory definition for the portion of the constitutional statement of policy on resource development as applicable to the development and transportation of the state's natural gas reserves, amending Acts relating to construction of natural gas pipelines to require conformance to the requirements of the statutory definition, and amending the standards applicable to determining whether a proposed new investment constitutes a qualified project for purposes of the Alaska Stranded Gas Development Act; and providing for an effective date."

- HEARD AND HELD

PREVIOUS ACTION

BILL: HCR 8

SHORT TITLE:NORTH SLOPE NATURAL GAS PIPELINE ROUTING

SPONSOR(S): REPRESENTATIVE(S)WHITAKER

Jrn-Date	Jrn-Page		Action
03/16/01	0625	(H)	READ THE FIRST TIME - REFERRALS
03/16/01	0625	(H)	O&G, RES
03/28/01		(H)	O&G AT 3:00 PM CAPITOL 124

BILL: HB 83

SHORT TITLE:NATURAL GAS RESOURCES DEVELOPMENT

SPONSOR(S): OIL & GAS

Jrn-Date	Jrn-Page		Action
01/19/01	0130	(H)	READ THE FIRST TIME - REFERRALS
01/19/01	0130	(H)	O&G, RES
01/19/01	0130	(H)	REFERRED TO O&G
01/30/01		(H)	O&G AT 10:00 AM CAPITOL 124
01/30/01		(H)	Heard & Held
01/30/01		(H)	MINUTE(O&G)
02/01/01		(H)	O&G AT 10:00 AM CAPITOL 124
02/01/01		(H)	Heard & Held
02/01/01		(H)	MINUTE(O&G)
03/28/01		(H)	O&G AT 3:00 PM CAPITOL 124

WITNESS REGISTER

REPRESENTATIVE JIM WHITAKER

Alaska State Legislature

Capitol Building, Room

Juneau, Alaska 99801

POSITION STATEMENT: As sponsor of HCR 8, gave a PowerPoint presentation and answered questions.

MICHAEL J. HURLEY

Government Relations

North American Natural Gas Pipeline Group

601 West 5th Avenue, Suite 500

Anchorage, Alaska 99501

POSITION STATEMENT: Testified on HCR 8.

MEAD TREADWELL

528 "N" Street

Anchorage, Alaska

POSITION STATEMENT: Testified on HCR 8 on behalf of former Governor Walter J. Hickel; read a letter from Governor Hickel to Chair Ogan and summarized points from an excerpt from E.L. Bartlett that was written at the Alaska Constitutional Convention; answered questions.

ACTION NARRATIVE

TAPE 01-21, SIDE A
Number 0001

CHAIR SCOTT OGAN called the House Special Committee on Oil and Gas meeting to order at 3:10 p.m. Members present at the call to order were Representatives Ogan, Fate, Dyson, Chenault, Kohring, Guess, and Joule.

HCR 8 - NORTH SLOPE NATURAL GAS PIPELINE ROUTING

Number 0072

CHAIR OGAN announced that the first order of business would be HOUSE CONCURRENT RESOLUTION NO. 8, Expressing the legislature's opposition to the proposed "northern" or "over-the-top" route for a natural gas pipeline to transport North Slope natural gas reserves to the domestic North American market, and expressing the legislature's support of commercialization of North Slope natural gas for the maximum benefit of the people of the state.

CHAIR OGAN informed members that in the new proposed committee substitute (CS), the sections were reordered and some redundant language was consolidated.

Number 0124

REPRESENTATIVE DYSON made a motion to adopt the proposed CS for HCR 8, version 22-LS0764\J, Chenoweth, 3/28/01, as a work draft. There being no objection, Version J was before the committee.

Number 0186

REPRESENTATIVE JIM WHITAKER, Alaska State Legislature, prime sponsor of HCR 8, came forward to give a PowerPoint presentation. [He provided a written copy later to the committee, the first page of which read, "Natural Gas in Alaska: What Does it Mean to the People of the State?"]

REPRESENTATIVE WHITAKER explained that information in the presentation had been garnered from the web site of the Energy Information [Administration] and from Tokyo Gas Company Ltd. The conclusions were his own, he emphasized, and were undergoing third-party review.

REPRESENTATIVE WHITAKER told members that to Alaskans, natural gas means \$680 million to \$4.2 billion a year to the state; significantly lower energy costs; and major direct and indirect employment opportunities, "if we demand that our resource be developed in our best interests."

REPRESENTATIVE WHITAKER referred to a chart showing national trends in home heating, furnished courtesy of BP; he said the trend for natural gas is increasing significantly when compared to electricity as a source of home-heating energy. He noted that for electricity, even though heating use has decreased, other uses have increased significantly. The "energy mix" is getting "lighter," and gas is becoming a larger component for the production of electricity.

REPRESENTATIVE WHITAKER called gas "clean and green"; the waste associated with its use is significantly less than that associated with coal, he said, and air pollutants are significantly less than from oil or coal. He noted that the related charts also were furnished by BP.

Number 0487

REPRESENTATIVE DYSON asked Representative Whitaker whether one could infer from the graph that coal and oil are not being used enough in America for heating.

REPRESENTATIVE WHITAKER said he didn't know whether that could be inferred, but one could infer that gas is being used more, in relationship to coal or oil, for home heating.

Number 0540

REPRESENTATIVE DYSON stated his understanding that in the United States most home heating [previously done] by coal or oil has been converted to electricity, with coal and oil going towards [electrical] generation. He suggested that may be a bit beyond the current discussion, however.

REPRESENTATIVE WHITAKER replied:

I think it is a bit beyond it, but I don't think that your assumptions - given that those are your assumptions - would be correct. I think you'd find that indeed gas has replaced coal and oil for home heating, and it is also replacing coal and oil for new electrical generation in the Lower 48.

REPRESENTATIVE WHITAKER noted that the demand for natural gas is soaring. He referred to a chart titled "Supply & Demand for North America" and said the numbers came from the Energy Information [Association]. He also noted that the chart referred to: current and expected supply from Canada and the Lower 48, including a depletion factor; expected additional supplies from Mexico and the Rockies; gas from an Alaskan pipeline project; and gas supplies from a Mackenzie delta project. Pointing out that the supply and demand curves on the chart don't come together, he offered his conclusion that it can be anticipated that higher prices will continue.

REPRESENTATIVE WHITAKER brought attention to a chart titled "Supply & Demand for the Pacific Rim," which mentioned "contract supply volume," "contract extension volume," and both an Alaskan LNG [liquefied natural gas] project - which he mentioned being online by 200 - and a Sakhalin LNG project. He commented, "Again, given that we probably don't have all supply sources included in this, I think it's fair to say that this line is more probably aligned with the mid-demand range; but, still, there is an upside, meaning to me that there is room in the marketplace."

Number 0767

REPRESENTATIVE WHITAKER mentioned the "world market dynamic reality." Referring to another "slide" in the presentation, he said:

Supply will restrict demand for the foreseeable future. That's an incredible statement to make for a commodity as important as natural gas. And given that Alaska's North Slope is the largest undeveloped reserve of natural gas in North America, we need to ask ourselves, "How can we take advantage of that situation?" It's very simple: We ... take our gas to market.

REPRESENTATIVE WHITAKER briefly addressed pipeline routing options shown on a series of maps, including the "over-the-top"

route, which he depicted as undesirable; the governor's preferred "highway" route; the TAGS [Trans-Alaska Gas System] route; and the so-called hub approach, "hubbing someplace in the Interior of Alaska, providing for a significant market access."

Number 0872

REPRESENTATIVE WHITAKER referred to a "slide" showing the state constitution, Article VIII, Section 2, which says the legislature shall provide for the utilization, development, and conservation of all natural resources belonging to the state, including land and waters, for the maximum benefit of its people. He emphasized that it is the legislature's responsibility.

Number 0913

REPRESENTATIVE WHITAKER turned to the question of how to obtain the maximum benefit. He highlighted the need for maximum market exposure, saying an overland route alone would exclude worldwide markets, especially in Asia and probably the West Coast of the United States. By contrast, connecting to multiple markets would stabilize market opportunities. He noted that the "over-the-top" and the Foothills "highway" routes exclude Asia, and the TAGS route excludes "middle America." Therefore, he said, the hub approach gives maximum market exposure.

Number 0995

REPRESENTATIVE WHITAKER turned to the issue of maximum dollars to the state. He said:

If we're to truly understand how the state can accrue the maximum dollars from a project of this nature, we have to discuss financing, because indeed there are dollars to the state associated with financing, or dollars from the state associated with financing.

And so, we look at our two options for financing: public financing, private financing. Public financing will exempt the financing component from federal taxes, which significantly improves the economics of an Alaskan gas project and increases the return to the state.

Additionally, the return on financing a project of this size will be 8 to 12 percent of capital costs per year for 30 years; that's a significant return.

Number 1069

REPRESENTATIVE WHITAKER addressed public ownership versus private ownership. He told members that under public ownership, besides being exempt from federal income taxes, the state-owned pipeline would give a greater netback to the state because no taxes would be charged back against the netback, and no tariff would be charged to the state. Under private ownership, on the other hand, taxes would be paid to the federal government, and a tariff would be paid to the producers. He continued:

So, in dollars to the state, what's the difference between public and private ownership? Given a six bcf [billion cubic feet] project, that's six billion cubic feet per day; the numbers are different, but the theories are the same whether it's a four-bcf-per-day project or a six-bcf-per-day project. We're using a six-bcf model.

By the way, these are Purvin & Gertz's assumptions. You can read it as well as I can: Under private ownership, the state would accrue \$680 million per year; under public ownership, \$1.3 billion per year. The difference is ... the tariff that would accrue to the state and the return, I'm assuming, to the permanent fund on the capital invested. ... We're assuming \$2.59 per million Btu[s] [British thermal units] sold in middle America; that is the assumption that Purvin & Gertz used in their study.

Number 1178

CHAIR OGAN asked about amortization under either public or private ownership.

REPRESENTATIVE WHITAKER replied:

As you can see, there is a return to the permanent fund; that is the amortization cost. And instead of that going to a third party, that would be returned to the state, to the permanent fund, assuming that was the [Alaska] Permanent Fund Corporation that invested in it.

CHAIR OGAN asked whether that would be the 8 to 12 percent [shown in the presentation].

REPRESENTATIVE WHITAKER affirmed that, saying it was assuming a 12 percent tariff.

Number 1238

CHAIR OGAN asked whether that is also with an assumption that 25 percent of the royalty would go to the permanent fund.

REPRESENTATIVE WHITAKER answered that the formulation would not change, given public ownership or private ownership.

CHAIR OGAN asked for confirmation that the assumption for the graph is 25 percent of the income.

REPRESENTATIVE WHITAKER affirmed that. He specified that it is assuming a per-million-Btu field price in middle America of \$2.59. He noted that the charts also addressed assumptions of gas prices at \$4.50 and \$8.00. Emphasizing that it is a 30-year project, and that gas prices are uncertain, he also noted that the current price is \$5.34. He concluded that assuming the \$2.59 price, under either private or state ownership, the producers would still get a substantial portion; in neither scenario would the state get more than its fair share.

Number 1360

CHAIR OGAN asked what Representative Whitaker's assumptions are regarding the state's purchase of the gas.

REPRESENTATIVE WHITAKER replied:

We're not buying the gas. The gas continues to be, once having left the unit, the property of the producers. We are collecting a royalty, a severance, a tariff, and a return on investment. The rest goes to the producers.

CHAIR OGAN asked whether the state wouldn't have the same problem that YP[C] [Yukon Pacific Corporation] has, for example: wanting to build a line, but having no gas. He said, "We've got 12.5 percent; [we could] take our gas in kind, ... but how do we get there with the producers, if the state decides to build the gas pipeline?"

REPRESENTATIVE WHITAKER replied that he had an answer [in other legislation], but it wasn't relevant to this particular presentation. His point is that there is a significant return to the producers and a reasonable return to the state.

Number 1453

REPRESENTATIVE WHITAKER addressed maximum in-state usage opportunity, saying those opportunities increase in relation to two factors: the number of population centers that the pipeline crosses, and the number of miles of pipe in the state. He indicated the "over-the-top" route [fails] in this regard; the "highway" route is "close"; the TAGS route is "closer"; and the hub concept works.

Number 1504

REPRESENTATIVE WHITAKER addressed maximum competition for gas production. He told members that a publicly owned pipeline would ensure that no producer on the North Slope would control access to the gas transportation system; he emphasized the importance of this component, noting that one problem in Alaska is too little competition and too few producers on the North Slope. Any producer of gas or oil should have an opportunity to produce and sell its product, he said. Public ownership ensures that access to the transportation system is available.

REPRESENTATIVE WHITAKER turned attention to maximum job opportunities for Alaskans. He said the state needs to ensure that both long-term and short-term jobs associated with the gas pipeline project are provided to Alaskans. Obviously, public ownership provides more opportunity for that.

Number 1563

REPRESENTATIVE WHITAKER concluded his PowerPoint presentation, summarizing the reasons that a hub project, publicly owned but privately operated, is in the best interests of Alaska. He said the hub approach gives maximum market exposure for Alaskan North Slope gas, and it allows maximum gas usage for Alaskans. Furthermore, public financing gives maximum dollars to the state, ensures maximum competition for North Slope gas production, and ensures both short-term and long-term jobs for Alaskans.

REPRESENTATIVE WHITAKER emphasized his willingness to have a third-party review. He said legislators have no choice but to follow the constitution, which is clear. He called HCR 8 a first step, highlighting the need for a northern (but not "over-the-top") route, as well as the legislature's role in ensuring that Alaska's gas goes to market. He pointed out that the debate regarding public-versus-private ownership and financing is for another day.

Number 1718

REPRESENTATIVE GUESS referred to the question of costs. She asked Representative Whitaker whether he had looked at which route would maximize a broader definition of profit, including not just money, but also jobs and "the greater profit."

REPRESENTATIVE WHITAKER answered:

Again, relating to the benefits, we've tried to list and define what is in the maximum best interest of the state. Included in that, of course, is employment and dollars to the state. And it was clear, under analysis, that the project that was adherent to maximum best interest of the state was the same in both cases.

REPRESENTATIVE GUESS stated her understanding that [the analysis] hadn't looked at whether one route was three times more costly, however.

REPRESENTATIVE WHITAKER replied:

We did, yes. Again, we used the "costing" assumptions association with the Purvin & Gertz study, which were very definitive with regard to the cost of a specific type of pipeline to a specific point. And, again, the program that we have here is available; we're happy to provide you with a copy of it. All of our analysis data is included.

CHAIR OGAN requested that the committee be provided hard copies of that material.

REPRESENTATIVE FATE also requested that Representative Whitaker provide an explanation of how the hub concept isn't just a physical concept, but is also a "pricing mechanism."

REPRESENTATIVE WHITAKER agreed to both requests.

Number 1878

REPRESENTATIVE GUESS turned attention to the ownership issue. She asked Representative Whitaker whether he had looked at both the cost of operating a pipeline - even if it's privately run - and what the risks of ownership are.

REPRESENTATIVE WHITAKER answered:

We certainly have. ... The cost-of-service and cost-of-fuel assumptions are the same whether it is a privately owned entity or a publicly owned entity. The risk, of course, is that the market is not adherent to the project, and we have to assure ourselves that the market is there. ... I'm very comfortable with the market dynamic. The market exists. ... And I've come to that conclusion as a result of years of analysis. I'm very, very comfortable making that assertion.

Number 1933

CHAIR OGAN noted that a memorandum of understanding (MOU) has been signed to deliver LNG from the Timor Sea, in Australia, to the West Coast of the U.S. He also noted that an LNG plant owned by Exxon has been shut down due to political unrest in Indonesia. He referred to testimony from previous overview hearings and to questions asked of Mr. Muraki [of Tokyo Gas Company Ltd., who had given a presentation before the committee]. Chair Ogan said:

I think maybe the shipment of LNG to the West Coast does indicate that one of the strongest markets, certainly for natural gas, in the world is the Lower 48, and it's unfortunate that it's not Alaska gas that's being shipped there - or at least the commitment for Alaska gas being shipped there.

Number 2078

MICHAEL J. HURLEY, Government Relations, North American Natural Gas Pipeline Group, came forward to testify as follows:

As you are aware, the three companies participating in the group (BP, ExxonMobil, and Phillips) are working

diligently to develop an economically viable project to commercialize North Slope natural gas by pipeline through Canada to the Lower 48 market. And in doing that, it is incumbent on us to fully consider the options that could help us accomplish that goal.

Indeed, the Federal Energy Regulatory Commission [FERC], before it will issue a certificate of public convenience and necessity, requires us to analyze alternative pipeline route options as part of the application process.

This project has the potential to be the largest energy project in North America, and will require capital investments in the billions of dollars. Indeed, investment decisions cannot be taken lightly, and must be made with the confidence that can only be gained by a thorough evaluation of the alternatives, and an understanding of their relative strengths, weaknesses, risks, and rewards. Such an approach is fundamental to good business decision making.

Our efforts are focused on creating and understanding opportunities, not prematurely discarding them. This resolution seems to suggest that we do the latter. We believe that legislative action which recommends shutting down options before they are fully understood limits dialog and interferes with the fundamental dynamics of a free-market economy.

It cannot be forgotten that any Alaskan gas project, whether it's LNG, GTL [gas-to-liquids] or pipeline technology, must be able to deliver products to the market at a competitive cost in order to succeed. There are many other competing sources of supply, and buyers will be going elsewhere if a project fails in this regard. If either Alaska project advances, the benefits to the state and its citizens and businesses will be substantial, and will make a significant contribution to Alaska's economic future.

Finally, the work we are undertaking this year will yield information we believe will be necessary for reasoned decision making. We have been listening to the views and concerns of the Alaska legislature ... and of Alaska's citizens, and we will be evaluating alternatives based on seven criteria: overall project

economics, Alaskan access to gas, jobs for Alaskans, revenues to the state, safety, environmental protection, and project timing.

Number 2271

MR. HURLEY, in response to a question by Representative Dyson, affirmed that "overall project economics" includes profit for the three companies involved. He continued:

We do not feel that we have enough information yet to make a route decision; indeed, that is the reason for our aggressive work program. Again, we think that the interests of commercializing North Slope gas are best served by creating choices, and not eliminating them. We expect that there will be many future opportunities for legislative guidance and action.

Number 2318

REPRESENTATIVE DYSON asked whether Mr. Hurley agreed that the only thing HCR 8 would preclude is the "over-the-top" route; that it could facilitate any of the other three options; and that it says nothing about hubs or ownership.

MR. HURLEY indicated that is his understanding as well.

Number 2375

CHAIR OGAN asked what Mr. Hurley would say "if we said we were trying to save you 75 million bucks."

MR. HURLEY replied:

What we're going to have to do in our program this year is, as yet, unclear. ... Part of these requirements are put on us by the Federal Energy Regulatory Commission. And even if the legislature were to appropriately express its desires to have one route or another, I'm not sure that that changes what we're required to do by the [federal government].

Number 2468

REPRESENTATIVE FATE asked whether the projected timeline for reporting at the end of the year on the findings of Mr. Hurley's group was still on target.

MR. HURLEY answered:

We are in the process of pulling together the contractors. And their first task, once we get contractors onboard, is going to be to look at the timeline we've given them and tell us whether they can do it or not. And we're waiting right now for them to get up and running, to be able to tell us that. We're still holding on to our goal to be finished and ready to apply by the end of this year, but we'll find out more once the contractors have reviewed the scopes of work that we've outlined and tell us whether or not we're being reasonable. ... We don't know yet.

Number 2476

CHAIR OGAN said he doesn't doubt the sincerity of Mr. Hurley's group and its efforts. Referring to the tight deadline, he said if it doesn't happen by the end of this year, and if the [legislature] must wait for several more months, legislators' hands will be tied unless there is a special legislative session. Chair Ogan said that is one reason he himself looks favorably upon HCR 8 and upon making this policy statement as a legislature.

CHAIR OGAN acknowledged that Mr. Hurley's group needs to use due diligence. However, he cautioned against saying that if the producers decide the southern route isn't economic, then there wouldn't be a project. He said the committee has to make an important policy call. He asked Mr. Hurley whether he cared to comment.

MR. HURLEY answered that the legislature, with the resolution, is expressing a preference, which it should do. He added:

What we're suggesting to you is not that you shouldn't have a preference, but that you should think about the implications of that preference, especially when you get into some of the language where it says that the legislature will use all efforts ... to make that occur.

Number 2625

CHAIR OGAN suggested that the language to which Mr. Hurley objected was on page 2, line 31 [continuing to page 3] of

Version J, where it says "the legislature will exercise every power within its authority [to prevent the routing of a North Slope natural gas pipeline that bypasses Alaska"]. He further noted that on [lines 26-28] it says "the legislature will exercise every power within its constitutionally required authority to guarantee commercialization of Alaska North Slope natural gas for the maximum benefit of the people of the state". He commented:

I remember one statement by a member of your group that said that the producers' interest is the same as the [state's]. And I disagree with that statement. ... I think that we have a lot of similar interests and a lot of interests that align, but it's not the same interest, because we each have our fiduciary responsibility. And there's nothing wrong with that; I think it's absolutely appropriate. ... You have a fiduciary responsibility to your stockholders, basically, and ours is to our "stockholders." We happen to be an owner state. ... We own the resources collectively. And so, I guess we're exercising our fiduciary responsibility by having this discussion.

MR. HURLEY said he understands that.

Number 2693

CHAIR OGAN asked whether this sends a discouraging message to Mr. Hurley's group or the companies behind it.

MR. HURLEY replied that he thinks it can. He clarified that he doesn't think the expression of a preference does [send a discouraging message] because everyone will have a preference. However, the language that Chair Ogan had quoted [on page 2, lines 23-25 and 28-29] may worry people, especially people who are "out trying to invest billions of dollars in assets."

Number 2731

REPRESENTATIVE DYSON said he appreciates that Mr. Hurley has a job to do, and that this may be disconcerting. He said, however, that it is hard to see how an across-the-top route can provide jobs for Alaskans; gas for Alaskan consumption, except to Kaktovik; or significant revenue from the gas transportation system. He said he appreciates Mr. Hurley's good-faith presentation but has to believe that the companies are, foremost, interested in their own bottom line. He suggested it

would be very difficult to convince the committee that leaving the "over-the-top" option on the table would be best for Alaskans.

MR. HURLEY said he agrees that it could be a tough road. He then stated:

We envision that this project is going to be large enough that it's not going to just challenge putting all the Alaskans to work, it's going to challenge getting enough people in North America to do it. So people who are going to want to work, no matter which direction it goes, are going to be able to get jobs. It's going to take a lot of people to build this.

With respect to gas for Alaskans, there have been discussions, and I believe the group is committed to evaluating a spur line down to Fairbanks, even ... when you're looking at the "over-the-top" route.

So anytime you're looking at multiple criteria, it's hard to say you can maximize one [criterion] at the expense of all others. ... You've got to try and optimize against a bunch of criteria. And what we tried to do here was lay out the criteria we're looking at. And they do include jobs; they do include gas to Alaskans. And our problem is, we don't yet have enough data to be able to fill in the matrix of ... what are the different attributes of the different routes in any detail or with any confidence.

Number 2889

REPRESENTATIVE FATE said he understands that the bottom line of the companies for which Mr. Hurley works is all-important, and that internal finances are important for any company to survive. On the other hand, to him this is more than just indicating a preference. The constitution mandates that the [legislature] maximize the resources for the benefit of Alaskans.

REPRESENTATIVE FATE asked whether the FERC had already issued certificates of convenience to another company close to 20 years ago, and now [Mr. Hurley's group] is reapplying for those. In the alternative, he asked whether the group is expecting a new issuance, and thus there would be two "layers" of certificates.

MR. HURLEY answered that at this point, they are pursuing it by doing the work necessary to file a new "green field." [This isn't on the tape, but was recorded in the log notes.]

TAPE 01-21, SIDE B
Number 2951

REPRESENTATIVE FATE further asked whether FERC has the power to negate the other issuances.

MR. HURLEY answered that the projects will be different and, to some extent, don't directly overlap; they have different "end-points," with different technology. He further stated:

The routing may mostly be the same, but it's not clear to us how different it is before the FERC gets to separate them in their own dockets, if you will. ... We have seen studies by the FERC that say that the ANGTA [Alaska Natural Gas Transportation Act] stuff does not preclude putting in a new "7C" application.
...

Quite frankly, we've seen and looked at several different legal opinions, and they all say different things, and that's something we're going to have to sort out, as part of this process. We don't know the answer yet. That is part of our work program.

Right now, we're assuming that, if you will, the worst case is, you have to go and file a brand new "green field," which means you have to do all the work necessary to have all the information for an application. That's the worst case in terms of the most work you have to do, so we're assuming that for the time being, as we move the process forward.

Number 2856

CHAIR OGAN asked Mr. Hurley whether his group opposes HCR 8.

MR. HURLEY answered that to the extent HCR 8 is expressing a preference, they don't oppose expressing a preference but suggest, if anything, that it may be premature, "given that there's not enough data out there to make a decision."

CHAIR OGAN asked whether his assumption is true that it wouldn't change what [the group] is doing, because they have to go

through an analysis, both to meet the federal requirements and to have "the holy water, if you will, sprinkled upon the project by the boards that want to invest the money."

MR. HURLEY replied that to the best of [the group's] knowledge right now, that is correct.

CHAIR OGAN reiterated, "Let the record reflect, we tried to save you 75 million bucks."

Number 2797

REPRESENTATIVE KOHRING referred to page 1, paragraph 5, of Mr. Hurley's written testimony, which read in part, "We believe that legislative action which recommends shutting down options before they are fully understood limits dialog and interferes with the fundamental dynamics of a free-market economy."

REPRESENTATIVE KOHRING mentioned his own concerns with regard to trying to force the eventual construction of a pipeline. He said he appreciates the efforts of committee members and other legislators, and surmised that his "no" vote may be the only one when something like this gets to the House floor. He explained:

We're supposed to be a government that's promoting a private-sector free-market economy, and I just don't see that this is consistent with that. And I know our constitution says one thing, and we all took an oath of office to uphold the principles of the constitution, but that doesn't necessarily mean the constitution is 100 percent right, either. ... It might have been God-inspired, but it's still written by men, and it's still subject to errors.

REPRESENTATIVE KOHRING suggested that supporting [every aspect of] the constitution may not always be in the best interests of Alaskans. He cautioned against acting prematurely, limiting options for the future, or doing something that discourages the oil and gas industry - which he believes has an excellent track record and which has added enormously to the state treasury - from acting in a "free-market way."

Number 2650

REPRESENTATIVE GUESS said she agreed in many ways. She observed that there is an oligopoly for oil and gas natural resources:

there are very few producers, which may cause natural market failures. It is not a free market.

REPRESENTATIVE DYSON compared it to a table-stakes poker game for which it takes \$3 billion or \$4 billion to buy into the game.

Number 2561

CHAIR OGAN thanked Mr. Hurley and stated that should HCR 8 pass, he and the committee, to his belief, "stand ready to assist you in whatever way possible to get this ... gas developed." He asked Mr. Hurley to "please convey the message to your colleagues and to your superiors" that this should be interpreted as positive, not negative.

Number 2520

MEAD TREADWELL testified via teleconference from Anchorage, noting that he would speak both on behalf of former Governor Walter Hickel, who was unable to testify that day, and as an individual.

MEAD TREADWELL, on behalf of former Governor Hickel, read into the record a letter [dated March 23, 2001, in packets], as follows:

Dear Representative Ogan,

While I'd hoped to visit you and the House Special Committee on Oil and Gas before the end of March, I'm not able to do so because I'm traveling to Moscow for a meeting of Northern forum leaders. Nevertheless, I want to compliment you and the committee on its efforts to understand where Alaska stands in world markets for natural gas.

Any successful gas project requires willing buyers, willing sellers, willing transporters, and financing. My work in this area has been to try to bring those elements together, and I hope your committee can do the same.

If I were there, I would make three points.

First, Alaska has to look out for its own interests. In the late 1970s, an overland project failed - but

not before Alaska's efforts helped Canadian reserves get to market. If overland was the best way to go, we would have an oil pipeline to Bellingham today. We don't. Tidewater gives us the most options, and while we can pursue an overland route, we can't allow the tidewater option to be ignored by the state or the producers. We must aggressively pursue Asian markets, and that means ensuring that a gas supply is independently offered for sale. So far, that has not been done. Instead, we're telling the Asian market we're not ready to sell.

Second, I've attached an excerpt from a talk the late Senator Bob Bartlett gave to Alaska's Constitutional Convention. He warned about companies with assets outside Alaska warehousing assets they acquire in Alaska. Of course, no oil company would admit that they are warehousing gas, or keeping it out of the market because it has other supplies available. But a state owner of such a large resource has to protect itself, because it could happen. It is clear to me that we have not protected ourselves.

What to do? We must be tough. Our options range from a reserve tax to taking back the resource for nonperformance. Neither of these options would be necessary if a sufficient gas supply to serve the LNG route were committed to an independent marketing effort.

Third, we must learn our lessons from the oil line: Unless structured correctly, a pipeline owned by producers is likely to result in tariff, royalty, and tax disputes because of a conflict in incentives between profits from transportation and profits from wellhead production. Since TAPS [Trans-Alaska Pipeline System] began, the state has had to collect close to \$10 billion in dispute because of the way the Trans-Alaska Pipeline was structured. Two options could help head off similar disputes on gas. First may be requiring an independent transportation company to carry the gas. Second may be having the state take an ownership interest in the pipeline at least equal to its royalty interest in the gas. Ken Thompson's trading hub idea also has merit in heading off this kind of conflict.

At least two transport companies have invested millions of dollars designing and permitting systems to deliver North Slope gas. The state is doing nothing I'm aware of to help bring these investors together with the producers.

I look forward to further discussion with you on my return. I'm doing what I can, as an individual, to urge producers, transporters, buyers, and financiers to get together. And the state must help to do the same.

If this letter is presented to your committee in my absence, Mead Treadwell - who works with me - can attempt to answer any questions you have.

With best regards.

Sincerely,

Walter J. Hickel

Number 2329

MR. TREADWELL referred to the attachment to the letter, pointing out that E.L. Bartlett [at the time of the Alaska Constitutional Convention in 1955] had noted that Alaska was becoming an owner state, and had said there are two dangers when a state owns a lot of natural resources: First, there can be exploitation under the thin disguise of development; second, taking Alaska's mineral resources without leaving some reasonable return for the support of Alaska's governmental services and the use of all the people will mean a betrayal in the administration of the state's wealth.

MR. TREADWELL highlighted the second danger discussed by Mr. Bartlett: Outside interests, determined to stifle development in Alaska that might compete with their activities elsewhere, will attempt to acquire great areas of public lands in order not to develop them until such time that "in their omnipotence and the pursuance of their own interests, they see fit." Mr. Treadwell concluded by noting that Mr. Bartlett had said the following: If large areas of "Alaska's patrimony" are turned over to such corporations, Alaskans may be even more the losers than if the lands had been exploited.

Number 2262

CHAIR OGAN remarked that he had found the statement by E.L. Bartlett, made in 1955, so prophetic that he had read a portion of it on the [House] floor.

CHAIR OGAN referred to the statement in Governor Hickel's letter, "Instead, we're telling the Asian market we're not ready to sell." He asked who "we" is.

MR. TREADWELL answered that in this instance, he thinks Governor Hickel is referring to what appears to be a policy "where they returned from a trip to Asia and kind of reported that there isn't a market." He suggested [Governor Hickel's] position is that if someone is trying to sell something, that person doesn't tell his or her customer there is no market there. He added:

We watched, very closely, the visit that you had from the representative of Tokyo Gas [Mr. Muraki], and we're also watching very closely what you reported to the committee at the beginning of this session, which is that there are now at least two projects announced to bring Australia gas to the West Coast of the United States or the West Coast of Mexico. ...

Take a look at the clear difference there. ... You've got oil producers in that case announcing projects. Those projects don't necessarily have market commitments as yet, but they announce an intent to sell and an intent to go out and try to sell. And we've never had that similar kind of intent announced on behalf of Alaska gas in the Asian marketplace that I'm aware of.

Number 2157

CHAIR OGAN referred to other markets and the Timor Sea. He asked Mr. Treadwell whether he was aware of any disincentive clause such as a reserves tax or a "use-it-or-lose-it-type of scenario built into their statutes" that might motivate these types of agreements.

MR. TREADWELL answered that he didn't have firsthand knowledge, although he had heard, in several cases, that most leases have performance clauses, which in some cases have a "short fuse." He added, "We have a performance clause, but our gas is mixed up with our oil, so that there is performance on the leases right now because the oil is being produced." He suggested it would

be a good issue for the committee to try to obtain more information about.

CHAIR OGAN replied, "We've been attempting to get that information, and it's difficult to obtain. But we have asked the producers if they're aware of any, and we're expecting responses."

Number 2080

CHAIR OGAN asked what former Governor Hickel meant when he talked about an independent marketing effort on the second page of his letter. Chair Ogan said he believes too much responsibility has been delegated by the legislature to the executive branch. He further asked, "What could we do better to market our gas?"

MR. TREADWELL responded that former Governor Hickel mentions, in the idea of an independent marketing effort, that options range from a reserves tax to "taking back for nonperformance." If, however, the legislature - through incentives, creating an authority, or working with the existing authority and "the existing permitted transporter for LNG" - were to see whether a commitment allowing the project to go forward could be put there, then it could live or die on its own merits in the marketplace - without a question of its being held back from the marketplace because of other competing projects owned by the same North Slope producers.

MR. MEAD went on to say that the gas doesn't necessarily have to be confiscated. The idea would be to get agreement to "put the marketing rights for that gas in a position where a group has the sole incentive to get that gas to market with a positive return to the state and ... the producers, as opposed to comparing the return from Alaska gas to any other kind of gas out there." If Alaska sells that gas, then Alaska makes the money. But if it doesn't sell and somebody sells gas out of Irian Jaya or the Northwest shelf of Australia, the state doesn't get any return at all.

Number 1920

CHAIR OGAN stated his understanding, then, that it would take a cooperative agreement between the producers and the state. Or perhaps the legislature would delegate an agent or designee to market the state's gas on its behalf. He mentioned that a big stumbling block with the Pacific Rim is that Yukon Pacific

[Corporation] doesn't own gas. He asked Mr. Mead how he envisions something like that would be done.

MR. TREADWELL replied that there are couple of options. He suggested reviewing Mr. Thompson's proposal that the state commit to, in essence, moving the wellhead to Fairbanks. If the state assessed the feasibility of that option - in return for providing help in the infrastructure that could potentially help both the overland project and the LNG project - then perhaps the quid pro quo is that there would be a commitment of gas to an independent marketing entity.

MR. TREADWELL pointed out a second option: to incorporate an independent marketing entity or to offer the state's royalty gas to a marketing entity that is able to get the other gas there. He explained that there are a number of disincentives for the state such as reserve stacks; however, it may be possible to get a positive finding.

MR. TREADWELL offered a third option: looking at "antitrust." If there is a competitive disincentive to sell, maybe there's an antitrust rule whereby a settlement could put an option [for] this gas into an independent marketing effort. He remarked that he thinks Governor Hickel is suspicious of ever having serious consideration of the Asian market unless all the incentives for Alaska are working together.

CHAIR OGAN remarked that he would prefer, philosophically, to do something in a positive light, rather than "holding guns to people's heads." He said he would like to discuss, with the committee, exploring and taking the lead on the hub issue, which probably needs to be developed in the interim. He remarked that it probably would be fairly complex to figure out how to move the wellhead to Fairbanks, for example, and it likely will take extensive statutory and policy changes.

Number 1731

CHAIR OGAN went on to say he thinks the "wellhead to Fairbanks" or hub idea probably addresses the third issue brought up by [former Governor Hickel], about structure and disputes. He noted that he says "requiring an independent transportation company to carry the gas." Chair Ogan said Representative Whitaker addressed that in his presentation. He asked if Mr. Treadwell could expand on this.

MR. TREADWELL offered some history in reply. When Alaska North Slope gas was discovered, there initially were at least three proposals to get it to market: an over-the-top route, the Alaska Highway route, and the El Paso LNG route. Congress stepped in and passed ANGTA, which said the President would make a choice and avoid a competitive choice by what was then the Federal Power Commission, which preceded FERC. There was never a question that gas would be brought to market by a transportation company, rather than the owners of the gas itself. Later, the owners of the gas became part owners of the Alaska Natural Gas Transportation System (ANGTS), which then-President Carter chose to have go down the highway. Even later, a "waiver of laws" package may have "increased that."

MR. TREADWELL continued, stating that since then, the country has gone through deregulation whereby the difference between transporter companies and producer companies has been erased in the law. There was a reason for that law in the first place; he suggested the state should look at its own reasons for whether or not it wants to have independent transportation companies. He explained that one argument for an independent transportation company is it provides good transparency regarding the cost of delivering the gas, in order to fully know what the wellhead [price] is, and to avoid disputes later on.

MR. MEAD explained that another advantage can be getting the gas to market if somebody wants to hold [gas] off the market, whereas now there is no "check" on that. He suggested it would be worthwhile for the committee to study that issue.

MR. MEAD further suggested that if the state is going to spend a lot of money permitting new projects - on routes that have already been permitted by independent transportation companies - it may be worthwhile to try to get the transportation companies and producers to work together. That hasn't been seen yet. In fact, he said, the unstated assumption of the administration appears to be that there must be a different transportation company. That assumption shouldn't go unquestioned.

Number 1480

CHAIR OGAN noted that in the same paragraph of the letter, former Governor Hickel talks about the state's having an ownership interest at least equal to its royalty interest in the gas, which is about 12.5 percent. Chair Ogan offered his perception of the advantage of that: at least [the state] would be at the table, and the information no longer would be

proprietary. He asked Mr. Treadwell whether [former Governor Hickel would agree].

MR. TREADWELL answered that he thinks [former Governor Hickel's] argument is this: "If you look how money has been made in the oil business since '77, when tax began flowing, there's certainly been money made at the wellhead, but there's also been money made in transportation." A question is how much money is made on transportation versus how much is made at the wellhead. If the state is an owner in the pipeline, then it is neutral, and there aren't conflicting incentives. He added that other arguments include the "information argument" brought up by Chair Ogan; the question of transparency, which Mr. Thompson had brought up; moving the gas; and Alaska's long-term position in the gas market. He added, "It doesn't come from any kind of socialist impulse. ... It comes from, basically, the state, as an owner, using a development tool to help make this happen."

CHAIR OGAN further noted that the letter says, "The state is doing nothing I'm aware of to help bring these investors together with the producers." He asked, "What can we do better?"

MR. TREADWELL replied that there are carrots and sticks. On the carrot side, if the legislature or the committee brought the people who got the permits for this project together, the state might save a lot of money in processing new permits.

Number 1284

CHAIR OGAN remarked that he would talk with the governor as to how the legislature can do its job better, by persuasion rather than coercion, if possible.

MR. TREADWELL stated that he thinks that's former Governor Hickel's point of view as well.

CHAIR OGAN asked Mr. Treadwell what he thinks former Governor Hickel's position is on [HCR 8].

MR. TREADWELL answered that [Governor Hickel] did not have the chance to specifically review the resolution; however, he stated in his letter that he is not crazy about the Alaska Highway pipeline. He remarked that he thinks [Governor Hickel] would support what is stated about the constitution and what the legislature's roll is in the policy of the state. He added that he doesn't think [Governor Hickel] has any objection with

expressing preferences. Finally, he said [Governor Hickel] would argue that a resolution could be passed against something, but would also argue to try to make something positive happen at the same time.

Number 1009

REPRESENTATIVE FATE made a motion to move the CS for HCR 8, version 22-LS0764\J, Chenoweth, 3/28/01, from committee with individual recommendations and the attached zero fiscal note.

Number 0974

REPRESENTATIVE KOHRING objected. He explained that he would be more amenable to the resolution if it did not have the word "guarantee" on page 2 [line 27]. He remarked that he has a problem: while the government is [advocating] a free-market economy, it is forcing the issue and the hand of industry in terms of attempting to guarantee a certain outcome.

CHAIR OGAN asked Representative Kohring if he would be more comfortable with the word "facilitate".

Number 0860

REPRESENTATIVE KOHRING said he would. He made a motion to adopt a conceptual amendment, "to substitute 'guarantee' with 'facilitate'." There being no objection, it was so ordered.

REPRESENTATIVE KOHRING withdrew his objection to moving the resolution from committee.

Number 0785

CHAIR OGAN announced that without further objection, CSHCR 8(O&G) was moved from the House Special Committee on Oil and Gas.

CHAIR OGAN called an at-ease at 4:37 p.m. He called the meeting back to order at 4:44 p.m.

HB 83 - NATURAL GAS RESOURCES DEVELOPMENT

[Contains discussion of SB 164]

Number 0765

CHAIR OGAN announced that the final order of business would be HOUSE BILL NO. 83, "An Act relating to natural gas pipelines, providing a statutory definition for the portion of the constitutional statement of policy on resource development as applicable to the development and transportation of the state's natural gas reserves, amending Acts relating to construction of natural gas pipelines to require conformance to the requirements of the statutory definition, and amending the standards applicable to determining whether a proposed new investment constitutes a qualified project for purposes of the Alaska Stranded Gas Development Act; and providing for an effective date."

CHAIR OGAN informed members that he had no intention of moving the bill that day, but wished to [adopt] a proposed committee substitute (CS), Version L [22-LS0322\L, Chenoweth, 3/28/01], as a work draft. Version L has language that would make it almost a companion bill to [SB 164]; however, it keeps the project language originally in HB 83, on page 2, lines 15 through 25, as well as the idea of designing enough capacity.

CHAIR OGAN indicated his desire to have a short meeting on [Version L] and to have members familiarize themselves with its new language. He stated his intention of eventually developing HB 83 into the hub concept, but acknowledged it may take longer than the current session to do so. He announced the intention of having meetings over the interim, therefore, in order to move rapidly at the beginning of the next session, should that be the wish of the committee.

Number 0380

CHAIR OGAN referred to a letter in committee packets [dated March 21, 2001] from Ken Thompson of Pacific Rim Leadership Development. He read from the attachment, which listed "Requirements for a Natural Gas Industry in Alaska." He noted that the first item, "Gas pipeline traversing Alaska," will probably be taken care of by the Senate bill. The second item needed discussion as to whether the state has at least a 12.5 percent share in the pipeline. The third item related to "in kind" use of gas [versus taking monthly royalty checks from producers selling the state's share]; he suggested in-kind gas could be on the Kenai Peninsula, for example, to keep the urea plants going there. The fourth item read:

- 4) State formulate clear policies and regulations for clarification of transparent netback pricing at the

"hub" or "spur line points" as a valuation basis for gas sales within the State and netback pricing at the North Slope wellhead for clear and transparent royalty and taxation purposes.

CHAIR OGAN commented that Mead Treadwell [who had testified on HCR 8 that day] had described that as moving the wellhead to wherever the hub is. Noting that Amerada Hess, in years past, had tracked every single drop of oil and every shipment in order to settle royalty disputes because the laws and policies were ambiguous, Chair Ogan emphasized the desire to avoid ambiguity and contentiousness with the producers by getting transparent royalty and taxation policies.

CHAIR OGAN suggested perhaps the hub to Fairbanks is a good idea. He restated his intention of working on the hub policy, if it is the will of the committee. In response to a question, he said the following Friday there would be testimony and lengthy discussion about [Version L].

Number 0025

REPRESENTATIVE DYSON expressed hope that the administration's representatives would be present.

CHAIR OGAN indicated his office would make that request.

TAPE 01-22, SIDE A
Number 0001

REPRESENTATIVE GUESS announced that she and Representative Joule would be in a House Special Committee on Education hearing on Friday and would, therefore, defer to the wisdom of the other members.

REPRESENTATIVE DYSON commended the chair for choosing to work on this during the interim, and for being proactive, rather than just responding to what is going on in the marketplace in that industry. He offered to use some of his office account to assist Representative Joule in attending interim meetings, should there be no funding for the committee during the interim.

CHAIR OGAN suggested the need to discuss with the leadership a bit of a budget to facilitate this. He said he would like to be that proactive facilitator.

REPRESENTATIVE DYSON proposed that the committee should put together what they foresee as being in the best interests of the state, and then say to the industry, "If you can top this, go for it." He characterized the industry as the goose that lays the golden egg for the state.

[HB 83 was held over.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 4:51 p.m.