

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS

March 14, 2002

10:44 a.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 BILL NO. 410

"An Act establishing the Alaska Natural Gas Development Authority, a public corporation, and providing for its structure, management, responsibilities, and operation, and requiring the development of a project plan for the construction and operation of a natural gas transmission pipeline project by the authority."

- HEARD AND HELD

HOUSE BILL NO. 423

"An Act relating to the Alaska Railroad; authorizing the Alaska Railroad Corporation to provide financing for the acquisition, construction, improvement, maintenance, equipping, or operation of facilities for the transportation of natural gas resources within and outside the state by others; authorizing the Alaska Railroad Corporation to issue bonds to finance such facilities; and providing for an effective date."

- HEARD AND HELD

HOUSE BILL NO. 394

"An Act relating to adjustments to royalty reserved to the state to encourage otherwise uneconomic production of oil and gas; and providing for an effective date."

- BILL HEARING POSTPONED

PREVIOUS ACTION

BILL: HB 410

SHORT TITLE:ALASKA NATURAL GAS DEVELOPMENT AUTHORITY

SPONSOR(S): OIL & GAS

Jrn-Date	Jrn-Page		Action
02/13/02	2233	(H)	READ THE FIRST TIME - REFERRALS
02/13/02	2233	(H)	O&G, RES, FIN
02/13/02	2233	(H)	REFERRED TO OIL & GAS
03/14/02		(H)	O&G AT 10:00 AM CAPITOL 124

BILL: HB 423

SHORT TITLE:NATURAL GAS TRANSPORTATION BY ALASKA RR

SPONSOR(S): RLS BY REQUEST OF THE GOVERNOR

Jrn-Date	Jrn-Page		Action
02/13/02	2244	(H)	READ THE FIRST TIME - REFERRALS
02/13/02	2244	(H)	O&G, FIN
02/13/02	2244	(H)	FN1: (CED)
02/13/02	2244	(H)	GOVERNOR'S TRANSMITTAL LETTER
02/13/02	2244	(H)	REFERRED TO OIL & GAS
03/14/02		(H)	O&G AT 10:00 AM CAPITOL 124

WITNESS REGISTER

SCOTT HEYWORTH

(No address provided)

POSITION STATEMENT: During hearing on HB 410, testified as one of the primary sponsors of Initiative 01GSLN, which the bill would supplant; suggested incorporating the nine-member Alaska Gasline Port Authority board.

WILSON L. CONDON, Commissioner

Department of Revenue

P.O. Box 110400

Juneau, Alaska 99811-0400

POSITION STATEMENT: Explained department's fiscal note for HB 410; cautioned about the large amount of upfront money required, no matter what size the project is.

NELS ANDERSON JR.

(No address provided)

Dillingham, Alaska

POSITION STATEMENT: Urged that HB 410 be moved forward, but suggested amendments.

DAVE DENGEL, City Manager
City of Valdez; and
Executive Director
Alaska Gasline Port Authority (AGPA)
P.O. Box 307
Valdez, Alaska 99686

POSITION STATEMENT: Testified in support of HB 410 and commercializing North Slope gas; requested amendment to include the AGPA.

ACTION NARRATIVE

TAPE 02-15, SIDE A
Number 0001

CHAIR SCOTT OGAN called the House Special Committee on Oil and Gas meeting back to order at 10:44 a.m. Representatives Ogan, Dyson, Fate, Kohring, Guess, and Joule were present at the call back to order; Representative Chenault arrived shortly thereafter. [For the overview presentation by Yukon Pacific Corporation (YPC), see the 10:08 a.m. minutes for this date.]

HB 410-ALASKA NATURAL GAS DEVELOPMENT AUTHORITY

[Contains testimony pertaining to SB 221]

Number 0040

CHAIR OGAN announced the first order of business, HOUSE BILL NO. 410, "An Act establishing the Alaska Natural Gas Development Authority, a public corporation, and providing for its structure, management, responsibilities, and operation, and requiring the development of a project plan for the construction and operation of a natural gas transmission pipeline project by the authority." [HB 410 was sponsored by the House Special Committee on Oil and Gas.]

CHAIR OGAN explained that he'd decided to introduce HB 410 because of his belief that [Initiative 01GSLN, "The All-Alaskan Gasline Initiative"] would be certified [to go on the November ballot], which had since happened. He offered his belief that the bill almost exactly mirrors the initiative, with a couple of minor changes; he referred members to the bill packet [which

contained two memorandums, dated February 8, 2002, and March 13, 2002, from Jack Chenoweth, drafting attorney, Division of Legal and Research Services] with regard to the changes.

CHAIR OGAN said this creates the Alaska Natural Gas Development Authority as a public corporation in the state; that authority would acquire and condition North Slope natural gas, and would construct a pipeline to transport that gas. The route would be from Prudhoe Bay to tidewater in Prince William Sound, with a spur line to Glennallen and the Southcentral gas distribution grid. The authority would operate and maintain the gas pipeline, and would ship and market the gas. He pointed out a five-page indeterminate fiscal note from the Department of Revenue, saying he wanted to have discussion about it. He also noted that the bill is silent with regard to how it interfaces with the proposed gas pipeline [that would parallel the Alaska Highway]. He said he believed there should at least be discussion of this issue, since it will be on the ballot; because it is a committee bill, however, he would defer to the will of the committee with regard to how to proceed.

Number 0230

CHAIR OGAN noted that the constitution allows the legislature to amend an initiative at any time, or to repeal it [after] two years. He suggested looking at whether there are flaws in the initiative. He also suggested this is a huge policy call, since he said it puts the State of Alaska in the business of building a pipeline and doing what usually the private sector does; the state would take the risks. In the alternative, legislators could let the initiative go forward, with what "our attorneys think are a couple of flaws in the bill, constitutionally and statutorily." Chair Ogan called on Scott Heyworth [one of the primary sponsors of the initiative that HB 410 would supplant].

Number 0393

SCOTT HEYWORTH testified via teleconference, as follows:

As guaranteed by our state constitution and state law, the citizens of Alaska have gathered more than ... enough signatures required to place this gas line initiative on the November ballot. I have seen or commissioned four statewide polls in the last year showing that the people of Alaska favor this Valdez route by over 65 percent. My poll done by Ivan Moore Research in just Anchorage alone shows a 70 percent

"favorability" in the town that controls 40 percent of the statewide votes. I've also polled the state with the exact ballot language ... you just read, Mr. Chairman, and it passes by 65 percent statewide today.

My petitioners told me it was the most popular petition that they've ever worked on in the state of Alaska. That is why we were able to gather so many signatures in the dead cold of winter, in so little time, and without the state fair.

The bottom, bottom line of this initiative is that the people of Alaska will now have a say in the development and commercialization of one of their resources, natural gas. But the legislature of our great state has an even more wonderful opportunity. You all can pass ... substantially similar legislation that we would agree on, that would speed this whole project up by one year and allow for a much earlier construction startup date. Representative Ogan has introduced HB 410, and Senator Taylor has introduced SB 221, which is in front of Senator Torgerson's Resources Committee. I have reviewed both of these bills, and, generally, I ... in most cases agree that they are substantially similar to our gas line initiative.

There are a few small things that might be added. As you know, the Alaska Gas Port Authority, or AGPA, made up of the three large boroughs of the North Slope, Fairbanks, and Valdez, have been working long and hard on their own port authority idea. In fact, I consciously stole many of their very good ideas and wrote them into this [initiative]. I would like to suggest that if a substantially similar bill does emerge, that you incorporate the seven-member board the initiative purports with the nine-member AGPA board's model. The reason for this is, it gives greater voice to all of Alaskans, including Juneau, Southeast, Bristol Bay, and/or the Southwest Alaska municipal conference.

Number 0653

MR. HEYWORTH told members he was extremely pleased to hear the numerous references to the phrase "in-state gas use" during the presentation by Mr. Fuhs earlier in the meeting [on behalf of

Yukon Pacific Corporation (YPC); see 10:08 a.m. minutes for this date]. Mr. Heyworth said the potential for in-state gas use is one of the most exciting aspects of the initiative. Alaska must develop an energy plan for all Alaska and bring down the high costs of rural energy as soon as possible. He reported that propane in Dillingham costs \$4.25 a gallon; in Anchorage, it costs only \$1.89. In Togiak in Bristol Bay, electricity costs 28 cents a kilowatt-hour; in Anchorage, it costs less than 9 cents. Developing a GTL [gas-to-liquids] and LPG [liquefied petroleum gas] or propane extraction plant in Valdez, he said, could result in three new energy sources to fuel all of Alaska: compressed gas, propane or LPG, and LNG [liquefied natural gas].

MR. HEYWORTH said each coastal, urban, or rural community might be unique in how its infrastructure should be built to receive this new "Alaska energy" from the North Slope; he said he looks forward to helping make this energy plan a reality for all Alaskans. He added:

I want to remind each and every Alaskan of one thing: neither Yukon Pacific nor I have ever purported that Yukon Pacific has any responsibility whatsoever to deliver in-state gas directly by them to any rural or urban area of Alaska. That is the sole responsibility of this new gas authority, and you as legislators, even, perhaps. It is an exciting task to look forward to creating the infrastructure and delivery systems from Valdez and along the pipeline corridor to get these new energy resources delivered. This will [most] likely be done by the private sector in contracts with this new gas authority.

This initiative gives you, as legislators, the potential to capture another revenue stream, possibly as early as 2007 or 2008, to help solve our fiscal gap and budget problems. This is not the Delta barley farms. It is not the milk farms or the hay farms over at Point MacKenzie. It is patterned off the permanent fund language. The permanent fund is something Alaskans trust and believe in. It has worked. So can the Alaska gas authority concept. It is a stand-alone project.

With the bonding capacities ... and/or in conjunction with the Alaska Railroad Corporation bond ideas that have emerged, the state would own 100 percent of this project. But this is very important to understand:

it would contract out all the work to the private sector. This is how an authority works. The State of Alaska is not building the gas pipeline.

Number 0867

MR. HEYWORTH suggested reading [proposed] Sec. 41.41.400, "Credit of state not pledged", in order to fully understand that this project doesn't put the permanent fund or the State of Alaska at risk. Once this initiative or [bill] becomes law, the newly appointed board is charged with putting a working plan together and presenting an economic model to Wall Street investors, he noted.

MR. HEYWORTH concluded by saying this model will offer a way to get "our stranded gas to the market, something that has never, ever happened before." He added:

If the model is sound - and I believe your confidence level should be a bit higher after you've just seen the model presented by Mr. Fuhs for Yukon Pacific - then Wall Street investors will buy our bonds, and we will begin to fully commercialize and finally commercialize our North Slope natural gas. I look forward to working with all of you to make this a reality.

Number 0928

CHAIR OGAN pointed out that the fiscal note prepared by the Department of Revenue asserts that there is some risk to the state; after confirming that Mr. Heyworth hadn't seen the fiscal note, he said the committee had just received it that morning. Referring to "Development Costs," beginning on the second of five pages of the fiscal note and analysis, he read, "First, it is important to point out there are no guarantees that this bill will result [in] a successful project [and,] under this legislation, the state would be exposed to taking commercial risks that no private firm has yet been willing to assume." Chair Ogan remarked that it seems to allude to putting the full faith and credit of the state at risk. He asked for Mr. Heyworth's take on it.

MR. HEYWORTH said he totally disagrees. He again referred to proposed Sec. 41.41.400 and said, "That's not the way the project's set up. The private sector will invest in the bonds. The project will sell itself. It doesn't put the state at any

risk." He acknowledged that he didn't have [the fiscal note]. He also emphasized his belief - from recent conversations with Mr. Obinata, general counsel from Japan, and from testimony from Mr. Muraki a year ago [at a joint hearing February 15, 2001, before the Senate Resources Standing Committee, the House Resources Standing Committee, and the House Special Committee on Oil and Gas] - that the Asian and Japanese markets are "hungry and would love to buy our gas from Valdez." He said in one year nothing has changed, and that it is economically feasible.

CHAIR OGAN indicated his own conversation with Mr. Obinata hadn't conveyed such a strong commitment.

MR. HEYWORTH offered his belief that the general counsel is very open to it, however.

Number 1163

REPRESENTATIVE GUESS questioned the wisdom of specifying a route in a bill or initiative, rather than having flexibility and allowing the market or business [to determine it]. She asked why the language specifies that it go to tidewater, instead of just saying it has to end in Alaska.

MR. HEYWORTH replied:

I think my answer would be simply, number one, [the] speed of the project, to get it going, and because, obviously, the permits are all in line with Yukon Pacific to go to Valdez. It was also, at one time, tried to get the permits to go down to Kenai, which ... passes through Denali State Park, the Minto Flats, and the Susitna wildlife refuge, and then under Cook [Inlet], over to Kenai. And that just wasn't found environmentally -- or a smart way to do it. And that's why Yukon Pacific got the permitted route.

MR. HEYWORTH also suggested that once it gets to Valdez, there are multiple markets, not only to Alaska but also to Asia, the West Coast, Mexico, and "everywhere." He said it is an economic, smart way to "bring our product to Valdez," and opens up all kinds of different markets, including that spur line down to Anchorage in order to hook into Southcentral Alaska.

Number 1270

CHAIR OGAN, noting that the bill mandates a spur line to Anchorage, said the Department of Natural Resources (DNR) believes there are significant gas reserves that haven't been exploited in Cook Inlet, where drilling is just now beginning. He asked what would happen if adequate supplies were found in Cook Inlet for the "near and maybe mid-term future." He said he has heard this spur line would be expensive, wouldn't pencil out as far as what it would cost to build versus what could be obtained for the gas, and wouldn't compete with what could be produced locally. He asked, "Have you done any analysis on what the spur line would cost?" If a law passes that says there must be a spur line, he asked what would happen if it doesn't pencil out and new gas sources are found. If the initiative passed by a vote of the people, he said, [the legislature] couldn't change it for two years.

MR. HEYWORTH said he understood and thought there were ways to get around it, if necessary. He said it is an intelligent question. He added:

There's a number of things. First of all, it's if anybody finds new reserves. The cost that I've seen on a paper napkin is about \$300 million; I could be high or low, in that I think it's only about 3 percent or 4 percent of the entire project if we added that one, so I think it's insignificant. I say, why don't we do things right the first time? ... We would wait to find a spur line because "if somebody finds some gas" - it's "if" and "ands" or "buts" - it's all I've heard ... for so many years.

I think it'd be smart to plan it and do it, and put it in. And if we need ... to amend it or change it, as you talked about, then the legislature can do that. And I'm not saying that I think it should be forced down our throats. If you can show me that it's not right or it's not economical - I'm a reasonable person - then maybe we can't do it that way. But at the time that we put this initiative together six, eight months ago -- every report that's out in front of you and everyone in the state of Alaska says we're going to be out of gas in Cook Inlet in ten years if we don't find anymore. Well, there's that word "if" again. Well, what if we don't find any more and we haven't put the pipeline in? Then where are we at? So I think we could work with it and look at different options, and

I think ... the wise people in the legislature can now work with us and help us figure that out.

Number 1470

CHAIR OGAN remarked:

One of the things that's happened since then is the Regulatory Commission [of Alaska (RCA)] has tied the price of gas that goes into the ENSTAR [Natural Gas Company] system to Henry Hub, or at least a formula based on Henry Hub, which has increased the interest in creating ... some more competition for looking for gas in Cook Inlet.

MR. HEYWORTH responded:

As you know, some company that I don't remember their name suddenly exposed themselves six or eight months ago and said they found all these reserves; that was the first report. And then when you got to the bottom of the whole newspaper article, the thing was, "Oh, actually we haven't found the gas; we're going to start looking for it next summer."

These are the kind of reports that keep coming out, so you and I and your committee and all of Alaska never know what the truth is. They didn't find any gas; they're going to look for gas next year, but the headline said they found 4 billion cubic feet of gas. It's misinformation. Nobody's found any gas recently. They may start drilling for it this summer; ... we'll have to take a look at that. Right now, we're going to run out of gas, and everyone knows that's the truth.

Number 1535

CHAIR OGAN pointed out that there has been some success in southern Cook Inlet.

MR. HEYWORTH replied in the affirmative, saying it is just a little bit, however, and that the talk is about sending it to Homer [and Kenai], to his belief, which doesn't solve problems in Anchorage and Southcentral Alaska. He suggested, "I think we can just all be reasonable and look at this." Emphasizing his

concern over the last 16 months that "our gas is stranded," he continued:

We're being told by the administration and the oil companies that our project doesn't work; no one provides any numbers. You just said you got a five-page [fiscal note and analysis] that says it's a \$16 billion project; we haven't seen it - I don't have it in front of me. We don't know what we're talking about at all. And yet, to make the Canadian highway route work, the one the administration purports, they want a \$10 billion loan from Congress; the oil companies need to have price-floor supports for some imagined \$1.25 wellhead price, all kinds of streamlined regulation, all kinds of federal corporate welfare to make the project work.

Our project in Alaska doesn't ask for any of those things. And the oil companies today, as you well know, ... don't even want to build the project, and they still haven't given you the studies that they promised to give you December 31; now they're telling you it's March 31. Why won't they give you the studies? We're giving you our studies - at least Yukon Pacific is; it's right there in front of you today.

Number 1624

CHAIR OGAN pointed out that the power of appropriation lies with the legislature. He asked what happens if there is a law on the books that the state doesn't have the money to [fund].

MR. HEYWORTH replied that he'd heard Senator Torgerson say that someone had guessed it would be \$3 million to \$3.5 million to start this. Mr. Heyworth said he himself believed it would be more like \$1 million to \$1.5 million, to bring a yearly revenue stream to Alaska of at least \$500 million a year, and possibly as high as \$750 million to \$1 billion. He pointed out that [the legislature] is being asked, meanwhile, to give money to the tourism industry and to Arctic Power, for example. He suggested [his proposal] is a small investment relative to the return. He said the state needs this huge new revenue source as well as in-state gas. He called it an "interesting project to look at, and soon, not later." He suggested perhaps HB 410 could be combined with Senator Taylor's bill in conference, and added, "I don't think I'd move to block it unless it was just tremendously not

substantially similar, because I think all of us in this room today and on these conference calls are working in the best interests of Alaskans, and that's what I'm trying to do."

Number 1729

REPRESENTATIVE KOHRING mentioned projects such as those at Point MacKenzie and Delta in which the state invested in the past; he voiced concern that this will be another government boondoggle and a colossal waste of money for which taxpayers will have to pick up the tab later. He asked Mr. Heyworth what makes him optimistic that this is viable and will provide some real benefit. He also asked why government should be involved in something that, in his opinion, the private sector should be doing. He suggested that if the private sector isn't stepping forward to do this, perhaps it isn't a viable project and doesn't pencil out.

MR. HEYWORTH replied that the private sector isn't stepping into the LNG project at Valdez or the "Canadian highway project" for many reasons. He said this isn't a state project whereby the state builds the pipeline, in contrast to the other projects that Representative Kohring had correctly mentioned. Mr. Heyworth explained:

This is an authority. And the way an authority works is, the state, yes, they do own the authority and the project. But everything is contracted and built by the private sector. And that's the difference between this project and the Delta barley farms and the Point MacKenzie milk farms and hay, and every other one that's never worked. It's a stand-alone project. The State of Alaska ..., through bonds or the railroad bonds or whatever, ... could invest some money if they wanted to. But that's not ... the way the project is financed, Representative Kohring. It's 100 percent - or should be or could be 100 percent - financed by bonds. That's not any investment by the State of Alaska. It doesn't take any money from the permanent fund or the State of Alaska.

I ... personally think the State of Alaska should try to own this whole project, but that's through the bonding process, not through investment. And, again, I've said it and I think Mr. Fuhs correctly said it, that if you put this economic model together and put the plan in front of Wall Street investors, if they

want to buy the bonds, that's what will determine the efficiency of the model of the project, is Wall Street investors themselves. And if they don't want to buy our bonds, then I'm wrong and we don't have a project; you're right. But if they do, we have a viable project that'll bring a tremendous amount of revenue to the State of Alaska, far more than any Delta barley farms [were] ever going to do.

Number 1912

REPRESENTATIVE KOHRING questioned whether government should get involved in a marketplace that "should be strictly a private-sector effort." If there are Asian markets, for example, he suggested oil companies will try to meet that demand and, if there is a profit to be made, will rise to the challenge and step forward with their own plans and financing, and will build the [pipelines]. He said he believes the private sector knows best and has the studies, for example. He concluded, "If they haven't stepped to the plate, then I'm really nervous about [the government's] getting involved."

MR. HEYWORTH reiterated that the state would own the authority and would contract with private-sector companies to do this whole project, including going to Asia to "make the offers to develop the infrastructure to build the pipeline." He likened it to how the John F. Kennedy (JFK) International Airport works, or the Houston Ship Channel; he further reported that most sports arenas are under an authority whereby the city owns it but the private sector builds it and then runs it. In response to Representative Kohring's suggestion that it should be left to the private sector, Mr. Heyworth said that is what has been for 25 years, which is why the gas is stranded.

Number 2050

REPRESENTATIVE FATE told Mr. Heyworth he may disagree a bit because the stranded gas has to do with the economics. Referring to Mr. Heyworth's mention of efforts at the federal level, he remarked:

They're doing this because of the tremendous risk involved. This is a huge, huge project. They're doing this to try to lessen that risk, and then doing this to raise the return on investments. You've implied here that this will be private people doing this work; now, they're going to have a return on

their investment also. So are we saying now that there's no risk in just going to tidewater, or that there is somehow an attenuated risk that is not comparable to the risk going down the southern route?

MR. HEYWORTH replied:

I think ... the last sentence you said is exactly correct, sir. Their project is a \$20 billion-plus project trying to move somewhere between 4 to 6 billion cubic feet of gas into a market in the Midwest that doesn't need the gas, has no gas shortages. And ... that gas, if it ever does get there in 2010, [2012, or 2015], will flood the market and drive the price of gas right down to the bottom, and then the federal price support will have to come in, and then the taxpayers are paying for the whole project. None of that happens with this state project.

REPRESENTATIVE FATE responded that it still doesn't attenuate the risk, and that supposition cannot be relied upon; whether the \$16 billion figure is valid or not, it will be a huge number, implying a huge risk.

Number 2170

MR. HEYWORTH replied that the risk would be taken not by the state, but by the market itself - Wall Street investors or companies that would invest in the bonds; it wouldn't indebt the state or the permanent fund. He suggested looking "happily" at these smaller numbers [put forth by Mr. Fuhs], which Mr. Heyworth said work because of a smaller project. He agreed that there would be risk, but suggested if the model were put to the market, Wall Street experts would decide whether the project is viable, and would give either a "thumbs up" or "thumbs down" to people to buy the bonds. He added:

We don't incur any debt until the bonds are bought and we start the project. That's when it happens. We don't accrue any risk to go forward with this and see what happens, to see if it is viable. Let the market decide. We're not going to go into debt. ... We're not investing in the project before it's been decided by Wall Street that it's a viable project. It doesn't work that way. And I really believe that it's just such an economy of scale of the Canadian highway route that makes it such a big project that you have to have

all those federal - what I call corporate welfare - to make sure that it all works, as opposed to this much smaller project that is much more sensible, deals with multiple markets, and has many, many places to spread that risk out that you talk about, sir.

Number 2245

CHAIR OGAN asked Mr. Heyworth whether he was willing to share the polling numbers.

MR. HEYWORTH answered in the affirmative, noting that he has given them out freely but hasn't had success in getting them published in newspapers.

CHAIR OGAN offered to fax Mr. Heyworth the five-page fiscal note and analysis.

Number 2359

WILSON L. CONDON, Commissioner, Department of Revenue, came forward to discuss the department's fiscal note for HB 410, expressing surprise at the controversy. He pointed out that the initiative - as well as the bill, to his belief - mentions getting a project up and running by 2007; he offered that it is too optimistic. He said that clearly the objective is to get the project done quickly, which will require upfront money. He acknowledged that the department could have put in a fiscal note that simply contemplated a board and support staff that would constitute the gas development authority; those could then "go around and talk to people and see what you might put together."

COMMISSIONER CONDON told members that in order to complete a project by 2007, 2008, or 2009, there is a need to start to spend real money now. He cited the need to make arrangements to buy the gas on the North Slope and to engineer the project. In addition, although YPC has done lots of work to get the permits necessary for part of the proposed project, it isn't known whether YPC would simply donate those permits to the project or if the project would have to pay YPC for them. Furthermore, a whole set of contracts would have to be negotiated with customers. All that work would have to be done by someone before there was the ability to go to Wall Street and sell bonds. Therefore, he said, the department doesn't know at this point how big the number is in terms of "front-end dollars" that have to be put into this project.

COMMISSIONER CONDON explained that even though it is contemplated that the work will be done by private-sector contractors, they will expect to be paid; the party responsible for paying them is this development corporation, which must have upfront money. Until it has the contracts in place and has a project engineered, it won't be able to borrow that money on Wall Street, and yet the cost to put this together will be substantial. "Great if it's done by the private sector," he added, "but nobody's going to donate the kind of commercial and engineering services that are going to be necessary to put this project together."

Number 2602

COMMISSIONER CONDON said the best indicator of the money needed is the kind of money spent by companies when looking at engineering a project and other upfront work before being able to turn to Wall Street for financing. He added, "So, if we're really serious about doing this, if we want to get underway and see whether or not the business model that's proposed in this legislation will work, then we've told you in the fiscal note that we think that the kind of upfront cash that's needed is something on the order, over a two-year period of time, of 175 to 250 million bucks." He said it might not turn out to be that much, but enough money ought to be appropriated to get it done; if it costs less, the money can be returned. "And if we're actually able to put the project together, we'll be able to convert part of what we spent into borrowed money, through bonds, on Wall Street," he added.

COMMISSIONER CONDON reiterated that [the state] won't be able to convert all this to bonds on Wall Street, or even borrow on Wall Street, unless it has spent the money upfront to put the project together; he said the only way he sees of getting money to do that is to appropriate the money "through the corporation from some source," which is the basis of the fiscal note. He added, "Now, the fiscal note then goes on and puts some big numbers on the table, because presumably ... the entity, the gas development authority, ... once it's got everything together, ... will go to Wall Street and borrow the money. ... And a projected stream of dollars is reflected in the fiscal note."

Number 2721

COMMISSIONER CONDON also cautioned that the state could appropriate and spend the \$250 million in the fiscal note through getting all the arrangements in place, and then Wall

Street could turn it down. Or most of the arrangements could be put in place, but not all of them, and the state would be unable to go to Wall Street and expect to borrow the money. He said, "In either of those eventualities, we're simply going to be out the money, and that's the risk we take if we're going to put this authority in place and seriously contemplate that they're going to put this project together."

COMMISSIONER CONDON indicated the fiscal note lists what the Department of Revenue staff see as the risks. He acknowledged that others evaluate these risks differently, but said, "Our job is to tell you what we think. And your job is to decide whether ... we have the capability to think better [than], or not as well as, Mr. Heyworth and others ... that see a little rosier picture with respect to this proposed project than we do." Drawing attention to the last couple of pages of the fiscal note, which list some points with respect to the general market around the Pacific Rim, he explained:

The way we see it is that there are lots of reserves at tidewater with easy access ... to the places around the [Pacific] Rim that need energy, and that with respect to all of those reserves, ... we believe they have about a \$1.50-per-million-Btu advantage over gas moving from the North Slope through a liquefaction plant in Prince William Sound and via LNG tanker either to the West Coast of North America or to Asia. And that relative disadvantage, we think, holds up at the small-sized project that the Yukon Pacific [Corporation] people propose, as well as the larger project that we mentioned in our fiscal note, which is a project that would be many times that size.

In the past, Alaska's had one advantage with respect to many of the places where LNG might be marketed, and that is that, in terms of the marine-shipping distance from south Alaska to Japan and the marine-shipping distance from south Alaska to Southern California and Northern Baja, we're closer. However, that advantage has shrunk over the last four or five years with the decline of the cost of LNG tankers, and, consequently, the one advantage that we had ... in the business has shrunk some.

Number 2917

COMMISSIONER CONDON continued:

With respect to focusing just on ... the Asian market, again, lots of gas chasing a limited market. And most of the gas that we're competing against doesn't have ... what we characterize here as the "pipeline disadvantage." And the market in Asia is changing. How quickly it will change, we're not sure. But in Japan the energy market for that country has changed with the introduction of deregulation in their ... electric power and distribution industry. And we do not know at this point what kind of pressure that's going to put on prices that you can get in Asia, and in Japan in particular. Historically, LNG has moved into the ... market in Japan at parity with crude oil. There has been some softening in those arrangements, and ... over the longer term, we may see a situation where the gas price becomes "delinked" [from the oil price]. [The bracketed portion isn't on tape, but was recorded in the committee secretary's log notes.]

TAPE 02-15, SIDE B
Number 2961

COMMISSIONER CONDON continued:

When you look at the California market, the way we've analyzed it, we believe that it's cheaper to bring gas from elsewhere around the Pacific Rim to California by LNG tanker than it would be to bring gas from Alaska. ... The lowest that ... our analysis has yielded is about a \$4 ... per-million-Btu cost into Southern California; if we're right there, obviously, it takes a \$4 price.

And, finally, in terms of the analysis we've done, we've concluded that it's cheaper to move gas to California by a pipeline to mid-North America, and then a redistribution of gas resources in the Lower 48, rather than a pipeline to Prince William Sound and an LNG tanker to Southern California.

Now, we may be wrong in all those assessments. Obviously, the ... possibility that we may be right is something we think you should evaluate before you undertake ... to set up this business and capitalize it with the kind of money that we think you'd need to capitalize the business with, in order to put things

together and go to Wall Street and buy bonds and so on.

Number 2879

REPRESENTATIVE GUESS asked whether, if the state wants to get into the gas pipeline business, an authority like this is needed.

COMMISSIONER CONDON answered, "There probably are other ways that ... you could structure the government's getting into the gas pipeline business. But if we are going to get into the business, in my judgment, this would be the best way to go."

Number 2841

CHAIR OGAN asked, "Where did you come up with the \$16 billion?"

COMMISSIONER CONDON said the analysis was done by one of [the department's] analysts. He added:

I don't know where he came up with that number. ... There are all kinds of different-sized projects that people have put on the table. You've got the port authority, which has proposed a big project, and you now have Yukon Pacific, which is proposing a smaller project. And if there is a specific-sized project and a specific-cost project that you would like us to model, we'd be glad to do that. We were not trying to find a project ... that was ... big that we could somehow "dis" this idea with. ...

The point we wanted to make is that ... if we're really serious about doing this, whatever size project it is, we've got to be prepared to come up with a lot of cash right now to get going.

Number 2758

NELS ANDERSON JR. testified via teleconference, emphasizing the need for gas. He commended the committee for putting HB 410 on the table, suggesting it is one way to "maybe shake up the oil and gas industry that's been stranding that gas on the North Slope." He said energy costs in the area [near Dillingham] are much higher than elsewhere than in the state, although cheaper in Dillingham than in nearby villages. Without something such as what HB 410 proposes, he said he doesn't know what will

happen in rural Alaska. He therefore urged that the bill be moved forward with dispatch. However, he expressed concerns about the bill as written, suggesting that there be amendments to clarify that "the State of Alaska, with its gas, would make sure that there is in-state, guaranteed use." He said there are in-state markets and that Anchorage has been depending on the Cook Inlet reserves, which are depleting rapidly; he mentioned the need there for long-term energy, and also mentioned the Lower 48 and the Pacific Rim.

MR. ANDERSON specified that he'd like HB 410 to be in compliance with Article VIII, Section 2, of the state constitution. Therefore, he requested the following amendments. First, he referred to Section 2 [page 3] under Sec. 41.41.010, "Establishment of the authority", [paragraph] (4) [which read, "the design, construction, and operation of other facilities necessary for delivering the gas to market and to Southcentral Alaska; and"]. He asked that it be amended to read, "the design, construction, and operation of other facilities necessary for delivering the gas to market and to communities throughout Alaska, including Anchorage and the Railbelt".

Number 2555

MR. ANDERSON, in response to Chair Ogan, agreed to provide suggestions in writing. Continuing with his amendments, he next referred to Section 5 [page 15], "DEVELOPMENT OF PROJECT PLAN," [paragraph] (6) [which read, "a plan for delivery and pricing of natural gas to communities along the pipeline route and to Southcentral Alaska through a spur line;"]. He suggested adding the phrase "including Anchorage and the Railbelt" after "spur line".

MR. ANDERSON then referred to Section 5 [paragraph] (7) [which read, "a plan for delivery and pricing of liquefied natural gas to Yukon River and coastal communities;"]. He suggested adding "throughout Alaska" after "communities".

MR. ANDERSON concluded by saying, "The sooner we get this thing going, the better. I would rather see substantially the same language passed as is found in the petition. I'm wondering if 42,000-plus registered voters of Alaska can be wrong, in that they want to use Alaska's gas for their use to bring down the cost of energy."

Number 2467

CHAIR OGAN mentioned polls indicating people support the initiative, but questioned how many really know what they are signing with regard to initiatives - what the costs are, for example, or whether the producers will be willing to sell the gas. He also inquired about the incentive to sell if there is a floor price of \$1.25.

MR. ANDERSON said this is the only game in town that has any prospect of providing long-term, low-cost energy for Alaska. He suggested the state should do everything possible to make something like this happen. He said the only time North Slope gas will be developed and moved is when the State of Alaska puts pressure on the oil and gas industry by taxing that gas in the ground and thus giving an incentive to move it. He said the signers of the petition, even if they don't know all the details, are making a demand or call on "our gas that's sitting stranded in the North Slope." He added, "And we need it." He said he sees this as a "hopeful, very positive move in the right direction to develop our gas for our use, and also provide for the markets that I think are out there in the Pacific Rim and the Lower 48."

CHAIR OGAN responded that he shares the desire to see the North Slope commercialized; he surmised that most Alaskans feel the same. He recalled countless hours of talking about it in committee.

Number 2234

DAVE DENGEL, City Manager, City of Valdez; and Executive Director, Alaska Gasline Port Authority (AGPA), came forward to testify. He told members:

I'm here today to offer Valdez's support to House Bill 410 and the idea of commercializing Alaska's North Slope gas. As you know, the City of Valdez, along with the Fairbanks North Star Borough and the North Slope Borough, formed the Alaska Gasline Port Authority [AGPA] ... in fall of 1999. The mission of that port authority is to develop Alaska's North Slope gas for the maximum benefit of all Alaskans, which ... is very similar to what HB 410 wants to do and what Mr. Heyworth's initiative wants to do.

Since the fall of 1999, when the port authority was approved by the voters of Valdez, Fairbanks, and the North Slope, over \$6 million has been expended by the

Bechtel Corporation, Taylor-DeJongh, and O'Melveny & Myers in helping the port authority to develop a cost estimate and an economic model for the development of North Slope gas. The economic model [that] has been developed for the port authority shows that our concept is economic. It also shows that it will have a return to the State of Alaska of between \$500 million and \$750 million a year.

The port authority economic model shows that a publicly owned project is economic and will provide [a] substantial return to the state and to the municipalities. [The] port authority model shows that using the port authority concept, ... the project can be 100 percent debt-financed. And this is a little bit different than what Mr. Fuhs indicated with their model, ... 75-25. We believe that our model and our project can be 100 percent financed ... by the investors so that there'd be no ... cash required by the port authority.

The City of Valdez has worked with Mr. [Heyworth] and his petitions, and we support his efforts. He along with members of the legislature have brought to the forefront the need to develop our natural gas resources. Valdez and the port authority have a very good working relationship with Yukon Pacific. Yukon Pacific brings the permits and their economic model; the port authority brings our economic model and our cost estimates and concept; and the initiative effort, and the legislature, brings the political will to do the right thing in developing our natural gas.

Valdez is supportive of a project that takes natural gas to tidewater, and manufactures LNG and LPG and transports it to markets within ... Alaska, within the United States, and within the Pacific Rim.

Number 2120

MR. DENGEL continued:

We support House Bill 410 and the initiative. Because of the work that has been completed to date by the port authority, Valdez would like to offer that the proposed legislation be amended slightly to incorporate the work that the Alaska Gasline Port

Authority has done, much like what Mr. Heyworth had indicated. By incorporating our existing board and our work into this, we can continue to move forward with this and not have to wait one year, two years, or three years in which to develop this project.

I want to applaud you, Mr. Chairman, and other legislators - Senator Taylor and Representative Whitaker - who have ... introduced legislation in the past ... to form a statewide authority to develop our Alaska North Slope gas. It's our belief that by using the port authority that is in place now and working with the legislature to amend the proposed legislation to include the port authority, ... Alaska can move forward with the development of our natural gas resources without delay. By using your political will, Yukon Pacific's permits and economic models, and the Alaska Gasline Port Authority's concept, I believe that we can achieve the goals of this legislation and of Mr. Heyworth's initiative to develop North Slope natural gas for the maximum benefit of all Alaskans in the very near future.

Number 2056

MR. DENGEL continued:

A couple of things that I've heard in the past about why we should wait for the private sector ... to do this project: I think when you look at what's driving the industry and the producers on the North Slope, ... I've been in YPC's offices a number of times, and they have a large map of the world on one of their walls; ... it shows where all the other LNG projects are throughout the world, and who owns them. And I think that that's what the North Slope gas project is competing against, ... all these other projects. ... Some of those countries have put requirements on those producers that they must develop those gas resources within a certain time. We don't have that on ours, and that's what we're competing against. And they're going to develop those projects before they develop our project.

And I think it's incumbent on us as Alaskans, and ... you as our legislative leaders, that we need to do something with that North Slope gas now. We need to

get that into production, and get it commercialized so that Alaskans can use it to reduce our electric costs, our high costs of living, and also to improve the economic picture for Alaska by providing petrochemical plants and whatever might come of that, as well as providing revenue back to the state from the sale of that ... North Slope natural gas.

MR. DENGEL concluded by offering to provide the committee with a presentation by the AGPA on its economic model and view of what is going on.

Number 1958

REPRESENTATIVE CHENAULT asked where the petrochemical plant is proposed to be situated.

MR. DENGEL replied that it hasn't been determined yet, although there would be a fractionation plant in Valdez. He offered his understanding that Williams is looking at putting a plant in Fairbanks, and said there may be other plants located in Valdez as well. He also mentioned the possibility of facilities in Southcentral Alaska if the spur line goes there.

REPRESENTATIVE CHENAULT conveyed interest not only in using the gas in-state, but also in having value-added products produced in Alaska, which he said interests him more than LNG, even though LNG will be a big portion of this project.

MR. DENGEL concurred but said LNG drives the project and helps to pay for it; if the value-added end can be pushed as well, that will be gravy to the State of Alaska. In response to Chair Ogan, he agreed to provide a copy of his written testimony. [HB 410 was held over.]

HB 423-NATURAL GAS TRANSPORTATION BY ALASKA RR

Number 1815

CHAIR OGAN briefly brought before the committee HOUSE BILL NO. 423, "An Act relating to the Alaska Railroad; authorizing the Alaska Railroad Corporation to provide financing for the acquisition, construction, improvement, maintenance, equipping, or operation of facilities for the transportation of natural gas resources within and outside the state by others; authorizing the Alaska Railroad Corporation to issue bonds to finance such facilities; and providing for an effective date."

CHAIR OGAN asked whether anyone wished to testify at the current hearing, rather than wait until the next meeting; there was no response. [HB 423 was held over.]

ADJOURNMENT

Number 1754

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 11:56 a.m. [For the overview presentation by Yukon Pacific Corporation (YPC), see the 10:08 a.m. minutes for this date.]