

ALASKA STATE LEGISLATURE
SENATE RESOURCES COMMITTEE

January 31, 2001
3:37 p.m.

MEMBERS PRESENT

Senator John Torgerson
Senator Drue Pearce
Senator Robin Taylor
Senator Pete Kelly
Senator Rick Halford
Senator Georgianna Lincoln
Senator Kim Elton

MEMEBERS ABSENT

All members present

COMMITTEE CALENDAR

Alaska Soil and Water Conservation Briefing by:

Mr. Art Weiner, Executive Director
Natural Resource Conservation and Development Board
Department of Natural Resources
550 West 7th Ave., Ste 1400
Anchorage AK 99501

Mr. Van Oss, Member
Alaska Natural Resources Conservation Development Board
Homer AK

Ms. Rachel Morse, District Coordinator
Alaska Soil and Water Conservation District
Homer AK

Overview of Natural Gas Pipeline by:

Commissioner Pat Pourchot
Department of Natural Resources
400 Willoughby Ave.
Juneau, AK 99801-1724

Commissioner Wilson Condon
Department of Revenue
PO Box 110400

Juneau, AK 99811-0400

Mr. Kevin Banks
Petroleum Analyst
Division of Oil and Gas
550 W 7th Ave, Ste. 800
Anchorage AK 99501

ACTION NARRATIVE

TAPE 01-5, SIDE A

Number 001

CHAIRMAN TORGERSON called the Senate Resources Committee meeting to order at 3:37 p.m. and announced that the committee would now hear a short overview by the Alaska Soil and Water Conservation Service.

MR. ART WEINER, Alaska Soil and Water Conservation Districts, said he also represented the Alaska Natural Resources Conservation Development Board (ANRCDB) and that the State of Alaska has 12 conservation districts that are directed in part by an appointed board. He explained that the board and districts are funded in part by the state and part by the federal government. Most recently, the districts have received \$2 million from the federal government which has allowed the districts to hire staff people. This has allowed districts to grow their capacity so they have brought in approximately \$10 million worth of project money from the federal government. Projects that have been accomplished by the Soil and Water Conservation Districts have included very large flood control projects in the Salcha Delta area, a shoreline erosion protection project in Unalakleet, a stored water protection program in McCarthy, a number of water quality monitoring projects throughout the state (funded by 319 funds from the Department of Environmental Conservation), smaller education programs, and small farm based programs.

MR. JIM VAN OSS, Homer District Board member, gave the committee a power point presentation from the local Soil and Water Conservation District. He explained that the Natural Resources Conservation Service got started after the Soil Conservation Act of 1935 during the dust bowl days of the Roosevelt Administration. The first conservation district was started in 1938 in the state of North Carolina. Alaska came on with AK 41.10 in 1947. Since that time, 12 conservation districts have been established in Alaska.

MS. RACHEL MORSE, Alaska Soil and Water Conservation District, said this district is the largest in the nation, 331 million acres, and encompasses everything that has yet to be incorporated into a local

conservation district so that every resident of Alaska has a district. She used a power point presentation to illustrate her points.

Her Board of Directors serves a dual function; they are also the Natural Resource Conservation and Development Board which works with the commissioner of Department of Natural Resources. For her, this means that rather than having a locally elected board of directors, she has one appointed by the governor. They come from all regions of the state and their qualifications are that they are a land user and cooperator in the local districts. They bring a lot of experience as far as agriculture and natural resource use.

The focal point of her district that spans such a great area is outreach to the communities to let them know of available services and to provide a pipeline to NRCS. The Board also contributes to professional conservation activities that are going on around the state and tries to function as a local conservation district wherever they can. They have standard outreach between conferences and fairs, but those really don't get out to the people they represent. So, they do the site visits which were in the presentation. They work with non-timber forest products and there is a conference in November 2001 in Anchorage to bring together all the users and producers to talk about wise use development, market niches, making sure they have all the cultural and traditional uses. She related how one woman sells all of her product, a birch syrup, overseas before she ever touches a tree. They work with the Alaska delegation for conservation and reinvestment legislation so the conservation districts can be supported in that manner. They are working with conservation districts nation-wide on this. They also work with other groups that promote the wise use of natural resources in Alaska and lend their expertise wherever they can.

MS. MORSE said they function as a traditional district and work with the inter-tribal watershed council, a group of villages along the Kobuk that is interested in collecting base-line water quality data. The data is very useful as the watershed resources are developed, Cooperative agreements with NRCS are maintained so that the projects not mentioned here take place.

CHAIRMAN TORGERSON announced an at ease from 3:50 to 3:52.

COMMISSIONER PAT POURCHOT, Department of Natural Resources, said he wasn't prepared to break down line-by-line budget items, but he could walk through some areas where work could be started now and proceed through permitting and actual construction of a gas pipeline. He explained:

In the 1970's the oil line hadn't been completed when the prospect of gas development on the North Slope was being discussed in earnest. In 1976 Congress passed the Alaska Natural Gas Transportation Act (ANGTA), which set the process in motion for a presidential finding and decision on what route and actually what company would be granted a right-of-way for bringing to market of a gas line. In 1977, President Carter issued presidential findings and found the proposal by - at that time - Northwest Pipeline Co. and the ANGTA route, which followed the existing TAPS route and then the Alcan Highway down through Canada to lower 48 markets, was the preferred route and should be the subject for a right-of-way and the necessary EIS work.

In 1978 Congress ratified that decision, essentially declaring that company and that route should be granted a right-of-way. In 1980 BLM followed through and issued federal permits through federal lands and some state lands that had not been transferred to the state. They issued the right-of-way to the Northwest Pipeline Company for a gas line following that route. Almost concurrently, the United States entered into an agreement with Canada to cooperate on that right-of-way. Canada, during that same period, issued similar permits and rights-of-way and fully permitted and granted a right-of-way through Canadian lands for that same project - matching up with both ends in the United States.

The project never got financing and events changed in the national oil and gas world. By 1984 the project was dormant - dormant in terms of the state was relevant in that they had filed for a right-of-way for that same permit across state lands from the state and that application was never acted on by the state nor was it requested to be finished by the company at the time.

By 1988 there was a lot of interest in the liquefied natural gas route. Yukon Pacific pursued permits and rights-of-way with both the state and the federal government. In 1988 they received a federal right-of-way following, basically, the TAPS route to the Valdez area and they received a conditional right-of-way from the state. The conditional right-of-way needed and still needs lots of work to make it 'unconditional.' There's a whole series of permits we could supply you, but it's a ways from a final right-of-way. It was also not an

exclusive right-of-way nor did it convey any title or rights to land per se.

COMMISSIONER POURCHOT displayed some large DNR maps with the proposed routes on them. One of the tasks that is needed, he said, for any kind of detailed work that could involve variances from the original rights-of-way because of advance geologic determinations, is that the state needs to bring its land status completely up-to-date in a corridor fashion, a couple of townships wide, down the whole length of the pipeline. This would not only fully identify land status within that, but it would develop a system where that information is readily available to any companies and applicants by the web, so that people who are working on very small areas can have instant land status.

COMMISSIONER POURCHOT said the state renewed the conditional right-of-way and BLM renewed the TAGS line permit in 1998 for another 10-year period. There is no state ANGTA right-of-way, but the federal right-of-way still exists. He added that all the companies and attorneys are now rereading and evaluating the status of all the events that took place in the late 70's and they don't yet know the answers to the following questions:

- Is the EIS still good?
- Can the right-of-way be moved?
- Can pump stations be relocated?
- Is it only Northwest or their successors, which is now Foothills owned by TransCanada and West Coast Transmission, Canadian Companies.
- Are they the only ones?
- What is their ownership right?
- What are their pay back responsibilities for the work that they did?

CHAIRMAN TORGERSON asked if he thought Congress would take up the issue.

COMMISSIONER POURCHOT said he read in the paper that an energy bill might address some aspects of the gas line or clarifications. He said that through the early gas process, the Federal Inspector's Office was designated as the central point of contact for the feds.

That was merged with the Department of Energy and over the years when nothing happened on the pipeline, it gradually faded away, but it still exists as a statutory designation within the Department of Energy. He said it needs to be revisited and that the Department of Interior and the Federal Energy Regulatory Commission (FERC) are involved already.

The State Pipeline Coordinator's Office parallels the federal

counterpart agencies in the Joint Pipeline Office (JPO). Their mission under state law is to "permit any and all pipelines in Alaska and to monitor on-going operations of those pipelines." Oversight of the TAPS is the bulk of their work. The federal side of the JPO reports through the Department of Interior now. The governor issued an administrative order several weeks ago designating the State Pipeline Coordinator's Office, under DNR, as the lead state agency under which we would coordinate the state right-of-way and permitting functions for a gas line (like the TAPS). This has been working well and hopefully the permitting function would move into construction and there would be teams of people working in unison to every extent possible so that each agency isn't independently going to each contractor or project sponsor.

He touched on some of the Governor's budget items for advancing the gas line commercialization. In addition to the creation and staffing of the State Pipeline Coordinator's Office, the state is coordinating with its federal agency and Canadian counterparts. The department has found that identifying requirements and explaining the process up-front to their applicants and people wanting permits makes the whole process move faster.

There are some resource needs and research work that are going to be required in any permitting scenario, COMMISSIONER POURCHOT said, like hydrology work, identifying and updating geologic hazards, fishery information and land status. He wants to get a jump start on this required work. He explained that there is a reimbursable fee for some work done by the applicants.

He is recommending some studies of Alaskan gas supplies and demand and an analysis of the national gas market that are absolutely necessary. One study is to determine the possibility of instate uses and instate needs. Another would be to assess the outside market and its economic and financial impacts on the actual feasibility of a gas line construction. They also have a component that references some of his earlier questions dealing with study of some legal and legislative or congressional legislation issues that may surround gas line development. He is recommending studies of some fiscal regimes like what the state can expect for a return on state resources and various aspects of that. Skilled labor needs to be identified and how it might be provided when and if construction starts. One of the objectives is to put as many Alaskans to work as possible.

CHAIRMAN TORGERSON asked how many of these studies are currently under way.

COMMISSIONER POURCHOT answered that Commissioner Condon has let one contract for some of the national market information. Outside of some of the broadest land work, DNR hasn't initiated any of the

studies for resource information as DNR did not have the funding before legislative appropriation. They have started on one of the tasks by sharing what permitting information they have with applicants. The JPO, which is getting hit with a lot of the work, is largely funded by RSAs.

SENATOR TAYLOR said he had read the original pipeline bills and Congress actually said one couldn't sue to enjoin the work, that all of the provisions of federal labor law were suspended as concerned the ability of a labor union to strike during construction of that project. Many other federal laws were suspended concerning that project. He asked if such legislation wouldn't be necessary in the construction of a gas pipeline, too. He asked how they intend to get around the litigation obstacles, no matter where the pipeline is built.

COMMISSIONER POURCHOT replied that the most significant exemption in the TAPS law was the declaration that it had indeed complied with the National Energy Policy Act (NEPA) and that the Environmental Impact Statement (EIS) was valid. He recommended reading the Alaska Natural Gas Transportation Act (ANGTA) of 1976 and the presidential findings in 1977. He was surprised to find it contained the EIS, the right-of-way, and other things that were fairly straight-forward, he said. Some, all, or most of that may still apply today.

SENATOR LINCOLN said she heard a presentation by Yukon Pacific that emphasized that is the only project that doesn't need permits and that is to go; and if the state goes with the Alcan project, 860 permits are still needed. She asked him to respond to that. Also, she said, it was reported that if there was an Alcan route going to Calgary, the prebuilt pipeline it would connect with is already full. She asked him to respond to that, too.

COMMISSIONER POURCHOT distinguished between state and federal rights-of-way and permits. Many, if not most, of the federal permits and the federal right-of-way for the TAGS route has been granted. On the state side, there are a number of studies and further information, as well as many non-right-of-way permits that are needed for the TAGS line. A conditional right-of-way exists which is a piece of the total state permitting picture. Many times getting information from applicants is what takes a lot of time, so an efficient process would speed it up. He estimated it would take at least 18 months for the necessary state rights-of-way and permits.

Regarding capacity, he explained, gas pipelines aren't as rigid as oil pipelines. Pressure and compression can be increased, so more gas can be put through the recently completed pipeline from Calgary to Chicago.

SENATOR ELTON asked if the Administration had considered how information would be collected and how they would work with other decision makers, including the Legislature so everyone is asking the same questions and getting all the answers at the same time.

COMMISSIONER POURCHOT replied that is already a challenge within the state agencies and DNR is in the process of submitting a supplemental budget to the Legislature for those very concerns.

TAPE 01-5, SIDE B
Number 2230

COMMISSIONER POURCHOT said the Governor signed an Executive Order last week that called for an advisory council and one of the core functions of that council is to have a citizen group act as a sounding board.

SENATOR ELTON said he wasn't sure it was entirely the Administration's responsibility to make sure there is a loop that includes the Legislature. However, he thought it is important to be in that loop early so legislators can ask appropriate questions throughout the process and review what the Administration is doing.

CHAIRMAN TORGERSON asked if there are any provisions for in-state processing or any benefits from it.

COMMISSIONER POURCHOT replied that they didn't identify a separate study for that, but they expected to hear of those possibilities as applicants come to the department.

Another charge of the natural gas policy council is to solicit, analyze, and make recommendations on in-state industrial development through the use of limited royalty gas.

CHAIRMAN TORGERSON asked if he thought the state could commit royalty gas to any project it felt like.

COMMISSIONER POURCHOT replied the same statute applies to royalty gas that applies to royalty oil, which requires best interest findings. He thought the state needs to receive the same value or better, as if we would take the oil in value.

MR. KEVIN BANKS, Division of Oil and Gas, testified that was correct and is in statute.

CHAIRMAN TORGERSON asked if the state still gets 12.5 percent royalty.

COMMISSIONER POURCHOT replied yes.

CHAIRMAN TORGERSON asked how we got a royalty share from gas or gas liquids.

COMMISSIONER CONDON answered that he was involved in litigation on behalf of the state addressing gas issues. Some of the liquids that are recovered on the North Slope today and sent through the pipeline and off to market are classified as gas, principally the butane. It is recovered at the central gas facility and blended with crude oil and sent down the pipeline. Under the state's oil and gas lease and the applicable state tax statutes, both for royalty and production tax, that substance is classified as gas. "Miscible injectant in the Prudhoe Bay field - and that same substance that is sent over to the Kuparuk field - all of those substances are technically gas. What finally gets produced and sent to wherever, the state will own one eighth of that."

CHAIRMAN TORGERSON said he hoped we would have the opportunity of taking our eighth for something in state, not something that goes to Chicago.

COMMISSIONER CONDON replied that we obviously have that option. "It doesn't have to go to Chicago and it doesn't have to go to Asia, if we want to take it and do something else with it."

SENATOR PEARCE asked if the governor's council is charged to look at just a natural gas pipeline and just one route.

COMMISSIONER POURCHOT answered that they are not charged with looking at routings. They're charged with soliciting views of Alaskans on a variety of issues concerning the use of gas, needs and desires of Alaskans in terms of labor, returns to the state, and best uses of in-state gas, particularly royalty gas.

SENATOR PEARCE said she would like to see an Alaskan Highway route natural gas pipeline built. It seemed to her that this group is going to go out and raise expectations and have conversations on just one route and the Legislature doesn't really know what proposal they are going to get from the owners. She said our one - eighth is not enough to build any of these projects and she is trying to understand why the state is so far out front.

COMMISSIONER POURCHOT explained that it was always envisioned that a gas line following the Alcan Highway through Canada doesn't mean you wouldn't have other options also, like spurs to Valdez or Cook Inlet. The charge also addresses use of NGL, LNG, and other uses that are not viewed as alternates to an Alaskan Highway route. They

could be adjuncts which also serve valuable purposes for Alaska.

COMMISSIONER POURCHOT said:

The Council shall deliberate and make recommendations on topics related to natural gas commercialization, including benefits of gas development to Alaskan communities, best uses of state's royalty share of gas, promotion or attraction of investment for in-state or value-added processing, the costs and benefits of the state taking delivery of its royalty share of gas in Alaska versus allowing a project developer to include the gas in delivery to lower 48 states, options for projects utilizing gas to liquids, liquefied natural gas, and natural gas liquids, demand for in-state natural gas consumption and its effect on a gas project, environmental impacts, necessary protection measures, training and readiness for Alaskans for jobs on a gas project, use of Alaska labor pool by contractors and subcontractors and use of Alaskan businesses, and state promotion and facilitation of project financing including potential ownership by the state of some or all of the project.

SENATOR ELTON said he sees two reasons for a public process. One would be to decide, after talking to Alaskans, what questions need to be asked as DNR proceeds with the studies, and the other would be to go back to Alaskans and say, "This is what we found out. Help us make a good decision on what some of these options would be."

COMMISSIONER POURCHOT said the administrative order calls for a report to the gas cabinet and to the Governor and the Legislature on November 30, 2001. The idea was to have a long enough time to solicit the views of Alaskans knowing that we're probably not going to make decisions during that time frame. He would not call the work items he laid out policy decisions; he would consider them as the foundation for making decisions, doing some nitty gritty permitting and right-of-way work, and for preparing legislation for the next session.

Number 1690

SENATOR PEARCE said they are running the risk of doing work that, if not useless, would be put on the shelf for a few years, like hydrology work, fisheries, or fiscal regimes, until they know what projects are on the table.

COMMISSIONER POURCHOT said he is optimistic. He reviewed the contents of the meeting for Senator Halford, who arrived late.

SENATOR HALFORD asked if the federal legislation is still on the books.

COMMISSIONER POURCHOT answered yes.

SENATOR HALFORD asked if it is exclusive in both cases.

COMMISSIONER POURCHOT said it named a specific company and granted a specific right-of-way, but lawyers are trying to answer that.

SENATOR LINCOLN said she understood that the report from the governor was just on that Alcan route and not the alternatives.

COMMISSIONER POURCHOT answered that it could very well speak to branches from the route and some other kinds of use of gas.

SENATOR LINCOLN wanted clarification if they were just looking at that one route.

COMMISSIONER POURCHOT answered that to their knowledge, the only other alternative to the major marketing of gas would be the so-called over-the-top route off-shore of ANWR and down through the Mackenzie River delta.

SENATOR LINCOLN asked about following the existing line to Valdez and shipping out of there (TAGS).

COMMISSIONER POURCHOT explained that there is an application for that route and some rights-of-way had been granted, but he thought it was more a function of the market rather than public policy decisions.

SENATOR LINCOLN said it was also a fact that spurs are a responsibility of the community. They can tap in, but they have to pay for that spur from that point to the community.

COMMISSIONER POURCHOT said there could be a private project like Enstar in the Cook Inlet area.

CHAIRMAN TORGERSON asked if he had an opportunity to figure out how not reinjecting gas and repressurizing the fields would impact the production of oil.

COMMISSIONER POURCHOT said that the last item on his list was study of the impacts of gas commercialization on North Slope oil

resources. He said there were two separate studies, done by the AOGCC and by the Division of Oil and Gas.

SENATOR TAYLOR said throughout Administrative Order 188, the Alaska Highway Gas Pipeline cabinet will work with the Governor and with the council. He asked who the Gas Pipeline cabinet is.

COMMISSIONER POURCHOT replied that it is a subgroup of the governor's cabinet, chaired by DNR. It includes all the departments that have a permitting function or an interest in gas line development. It includes DNR, ADF&G, DEC, DOTPF, DOL, DOR, and DGC. He said it's a large group, but it's indicative of why there needs to be a forum in which to discuss the gas line.

SENATOR TAYLOR asked why right-of-way would be a problem in the state since it has the right of eminent domain.

Number 1147

COMMISSIONER POURCHOT answered that pipelines, highways, and utilities do have eminent domain. In Alaska there traditionally has been little private land ownership and, unlike other states, when we exercise eminent domain, we do it very cautiously.

CHAIRMAN TORGERSON asked if the state had been paid royalty on gas that has been used on the North Slope.

COMMISSIONER POURCHOT replied yes.

SENATOR PEARCE asked if the group could discuss the possibility of Alaskan ownership of an equity interest in whatever projects come to the table eventually. She thought that is the place right now for public discussion. She also noted that there was no discussion of possible financing schemes in terms of using alternative methods such as a port authority. She asked if the council was charged with looking at some of the opportunities that might be available to some of our communities.

CHAIRMAN TORGERSON said he just received an e-mail saying that the department had suspended all the applications on shallow gas and frontier leasing and he wanted to know if that is true and why.

COMMISSIONER POURCHOT answered that it is true and explained that the department issued one shallow gas lease to Cominco in the Nome area to develop some alternative energy sources. DNR has 250 pending applications. To grant the leases, the same DNR staff has to search all the titles. Meanwhile, on the North Slope, to issue the leases the department granted last fall, the same people have

to do the same process. The shallow gas leases are worth thousands of dollars, but the North Slope leases are worth millions in state revenue. He said DNR is not suspending the program; it is shifting resources temporarily until it gets caught up on the North Slope leases. DNR is committed to the program, but the reality is has to slow down on the actual granting of the shallow gas leases. The applications are still valid and the program is still on-going.

Number 730

COMMISSIONER CONDON said he would run through his notes and talk about the dollars:

They are important with respect to the economic viability of a gas commercialization project. They're important for public revenue from a gas commercialization project and they're important to financing, which links back to the economic viability. In terms of thinking about the dollars for any one of the proposed projects, whether it's the project that we've been more or less focused on here today, which is to take the gas pipeline down the Alcan or whether it's over the top which we're not talking too much about, but I want to talk a little bit about the variables [which] are: what's the gas worth in the market you take it to, whether it's central North America or North America in the largest sense or whether it's Asia.

The second variable is project cost - how much does it cost to build a project to get it there. The third variable is the volume you're shipping through the facilities you build to the market you're accessing. Thinking about those three variables, you can think about it in a simplified term. You don't need to think a lot about operating costs, but you do need to think about what is the market going to be like when you get there, what kind of capital investment do you have to make to get there and how much do you send - because you're going to spread the capital costs over the volume that you send.

As folks have focused on pipelining gas to mid-North America, they've really talked about a lot of different combinations of projects. To keep the discussion here simple, I want to just focus on three. Two of them are variations on sending gas down the highway. One is a 2.5 billion cubic foot per day (bcfd) project that would send gas to Alberta. Another version of the same idea is a 4

bcfd project following the same route. A third project, just to talk about these variable, I want to hypothetically put out before you, is over the top where folks have talked about taking 2.5 bcfd from Prudhoe Bay moving it under the Beaufort Sea over to the Mackenzie Delta and there picking up 1.5 bcfd and thus moving 4 bcfd into the North American market.

As you think about those projects, if you're moving 2.5 bcfd of Alaska gas, either down the Alcan or over the top into the North American market a \$1 change in the destination market is going to make a difference in state revenue of about \$180 - \$200 million. That's the sensitivity for Alaskan public revenue to a dollar change in the market price in the lower 48.

With the 4 bcfd project taking Alaska gas into the market place, a \$1 change results in a \$360 - \$400 million in state revenue. If you look at the sensitivity of state revenue, just sort of a proxy of what happens to the economics of the project of changes in the project costs and if you're looking at a project that takes 2.5 bcfd of Alaska gas to market and you have a \$1 billion change in the project costs, that results in either an increase or decrease of Alaska's wellhead value by about 20 cents per mcf. For a project that takes 4 bcfd, a \$1 billion change in project costs results in about a 12 cent change in revenue for the state.

As people think about what the over the top route might be worth to Alaska as opposed to the Alaska Highway, if you believed that the over the top project would cost \$2 billion less than the Highway route - and we don't know how much less it cost or whether it would cost more - but if you thought how much less it would cost, and each of those projects would deliver 4 bcfd to the market, we have another set of comparative revenue numbers that we ought to look at. The wellhead value per unit, if you assume the over the top project costs less, would result in a wellhead value for Alaska gas that would be 15 cents [per mcf] higher than it would if you went down the Alcan. But the total revenue to the state would be about \$160 million per year greater - if you went down the Alcan with a 4 bcfd project than if you went over to the Mackenzie with 2.5 bcfd and then went to market with 4 bcfd there. It's obvious why. You are taking more Alaska gas to market earlier [with the Alcan project].

In terms of thinking about public revenue, while what the state would receive per unit would be 15 cents/mcf less, lots more Alaskan gas would be moving into the marketplace and, Alaska's revenue, as a consequence, would be considerably greater. There are lots and lots and lots of variations that you can then continue with in terms of volumes - making assumptions about whether or not and when Alaska gas gets to market. You can add on LNG plants, spurs, and possible GTL plants. I'll close out this discussion by saying that all of these variables are modelable. Our staff has put together models that can look at any of them.

COMMISSIONER CONDON said there are other variables that complicate it. There is the question of gas liquids and it may be important to a project's economics in terms of an industrial base here in Alaska. Models aren't available for those at this point in his department. They have talked with Cambridge Energy Research Associates (CERA) about helping to lay out a path for doing this kind of analysis.

TAPE 6, SIDE A
Number 001

COMMISSIONER CONDON said:

There are issues related to royalty in-kind gas and to the extent you are talking about using royalty in-kind gas not just as fuel in communities, but as possible industrial feed stock, the same kind of analysis really ought to be done.

In terms of looking at the variables we talked about - markets, costs, and volumes, we commend to you the analysis that we'll make available to you from CERA on the North American gas market. They're certainly prepared to share with us their analysis of the Asian Pacific Rim LNG market, as well.

With respect to construction costs and that variable, that is not something which we've undertaken to look at ourselves. We're rather not qualified to do that in terms of the staff at the Department of Revenue. There are folks who've done some quick and not so expensive studies and there are people who claim to have devoted thousands of hours to studying alternative costs. Some of that is available in the public domain and some of it has been held proprietary by the companies that have done it. We have not had access, yet, to that information -

the Purvin and Gertz study which some of you have seen was a quickly done study. They certainly have qualified people, but it was not an expensive or extremely thorough cost study. They certainly have qualified people. The mayor's group had an extensive study which was in effect - donated may not be quite the right verb, but it certainly hasn't been paid for yet - that was done for them. Bechtel, one of the major pipeline companies had done a study that has not been shared with us nor discussed in a public forum. Yukon Pacific had redone its own cost studies and again that's information they might choose to share with you.

Of course, we can't know for sure what kind of projects people are finally going to propose in terms of the volume of gas that's likely to move. All we can do is model the economics of as many different kinds of projects as seem plausible and that's what we have done and what we are prepared to continue to do to the extent that you or anyone else wants our assistance or wants to look at our analyses.

I should say something about the fiscal system. Senator Pearce is correct that until we know what someone proposes to do quite specifically, it's not going to be possible to make a judgment about whether or not the state's fiscal system needs to be modified or tailored in some way to accommodate the project. In tailoring the fiscal system, it seems to me there are two questions that we would ask ourselves. The first one is, do we need to change it to get a project? We need to make a judgment about whether that's the case. If we are going to change it, obviously the way we would want to change it is how do we maximize the public interest in the development. That may mean modifying the way we tax, but certainly I hate to see us talk about it as I read stories in the various publications - tax concessions. That's really not the lens we should be looking through. We're not trying to do the taxpayers a favor. We're trying to figure out what it's going to take for us to have a project and what fiscal system makes the most sense for the project in terms of our analysis of what the public interest is.

Let me return to CERA for just a moment. There's been a lot of discussion about markets and what we can expect in the market. As the person who has the responsibility for coordinating the contract that we've entered into to deal

with the gas issues, I would commend their market analysis to you and will certainly work to try to make them available at a time that would be useful to you to hear what they have to say about the North American gas market - where is it today, where do they think it's going to go and you can form your own conclusions about what that means for commercializing this resource for Alaskans.

Those are my notes, Mr. Chair.

Number 413

CHAIRMAN TORGERSON asked if he discussed the possible state investment.

COMMISSIONER CONDON replied he hadn't, but added that was certainly a possibility. He didn't know what more he should say about it now. "If you're going to make an equity investment, you've got to have some equity to invest." There may be things the state could do even if it were not an equity investor to facilitate the financing of the pipeline, he said and those are obviously things the state should explore and we intend to do so. "That's an area where our department has responsibility. We will study the options and give you our judgment about what might be available."

CHAIRMAN TORGERSON asked for any help he could give him in understanding the difference in West Texas Intermediate (WTI) and West Coast (WCI) oil prices.

COMMISSIONER CONDON passed copies of a graph to the committee and referred to it with his explanation. He said this is how his chief petroleum economist likes to present information.

When OPEC announced its October 1 increase, the increase it put into the market at that point was largely sour crude. As a result, we saw a worldwide decline in value of sour crudes relative to West Texas Intermediate which we all know is a very sweet crude. ANS values held up relatively better than other sour crudes. ANS fell after the first few days of September. Dated Brent did not, but it is not a sour crude.

You can pretty much explain what we've seen with respect to the differential between ANS and WCI by looking at the price behavior of sour crudes worldwide. There are also some specific issues with respect to the west coast in terms of refinery shutdowns, other crudes being imported into the west coast by some refiners which may put

further pressure on ANS relative to WCI. We've actually seen a little bit of a recovery on all ANS since this chart was prepared, but I think there is still some possibility that what we see in the market place will again widen the differential with respect to WCI. What has happened now, of course, is that OPEC has announced that it is taking crude off the market. I believe we will see a price response for sour crude and the question is whether ANS will track that. It is something we are watching on a daily basis.

CHAIRMAN TORGERSON said he heard something about other states (Washington, Oregon, and California) investigating something like price fixing and asked if the Commissioner was in contact with these states.

COMMISSIONER CONDON answered yes. One of the things he foresaw was Senator Widen, who got access to some of the documents that were produced in connection with the merger, focused specifically on BP's pricing behavior, and sought to reposition the export ban. If BP was behaving as Senator Widen alleges it was, of course, we were the beneficiaries of that, and it is not in our interest for there to be a reimposed export ban.

CHAIRMAN TORGERSON asked how much we are exporting now.

Number 1000

COMMISSIONER CONDON answered that we are not exporting any right now.

SENATOR HALFORD said they just agreed to reduce the quota out of Saudi Arabia and asked, "If they have reduced the component of their export oil from which they are getting the lowest price, we would assume the glut of low grade oil on the West Coast declines and the differential would decline, too. Is that wishful thinking?"

COMMISSIONER CONDON said he didn't think it was wishful thinking and he could find out the answer, but he didn't know it right now. One has to assume they would take the sour crude off the market first.

SENATOR HALFORD asked if he knew what portion of the OPEC decline the Saudis agreed to take.

COMMISSIONER CONDON answered that he would find out.

CHAIRMAN TORGERSON thanked everyone for joining the committee and adjourned the meeting at 5:30 p.m.