

HOUSE FINANCE COMMITTEE  
January 28, 2004  
1:45 PM

TAPE HFC 04 - 14, Side A  
TAPE HFC 04 - 14, Side B  
TAPE HFC 04 - 15, Side A

CALL TO ORDER

Co-Chair Harris called the House Finance Committee meeting to order at 1:45 PM.

MEMBERS PRESENT

Representative John Harris, Co-Chair  
Representative Bill Williams, Co-Chair  
Representative Kevin Meyer, Vice-Chair  
Representative Mike Chenault  
Representative Eric Croft  
Representative Hugh Fate  
Representative Richard Foster  
Representative Mike Hawker  
Representative Reggie Joule  
Representative Carl Moses  
Representative Bill Stoltze

MEMBERS ABSENT

None

ALSO PRESENT

Representative David Guttenberg; Representative Cheryl Heinze; Representative Norman Rokeberg; Representative Harry Crawford; Harold Heinze, Chief Executive Officer, Alaska Natural Gas Development Authority; Steven Porter, Deputy Commissioner and Liaison to the Alaska Natural Gas Development Authority, Department of Revenue; Dan Sullivan, Member, Board of Directors, Alaska Natural Gas Development Authority.

PRESENT VIA TELECONFERENCE

Bob Favretto, Member, Board of Directors, Alaska Natural Gas Development Authority.

GENERAL SUBJECT(S):

The following overview was taken in log note format. Tapes and handouts will be on file with the House Finance Committee through the 23rd Legislative Session, contact 465-

2156. After the 23rd Legislative Session they will be available through the Legislative Library at 465-3808.

**JOINT WITH MEMBERS OF THE HOUSE OIL AND GAS COMMITTEE**

**OVERVIEW: ALASKA NATURAL GAS DEVELOPMENT AUTHORITY  
Plans to Develop a Natural Gas Pipeline**

LOG	SPEAKER	DISCUSSION
	<b>TAPE HFC 04 - 14 SIDE A</b>	<b>ALASKA NATURAL GAS PIPELINE</b>
000	Co-Chair Harris	Convened the House Finance Committee meeting at 1:45 p.m.
0125	HAROLD HEINZE, CHIEF EXECUTIVE OFFICER, ALASKA NATURAL GAS DEVELOPMENT AUTHORITY	Reviewed his professional background in oil and gas, emphasizing his involvement with the gas issue for over 30 years.
256	Mr. Heinze	Explained that he would discuss the Alaska Natural Gas Development Authority (ANGDA) and its funding through the supplemental budget process. Ballot Measure 3 passed in the November 2003 election created ANGDA as a public corporation of the state. A 7-member board of directors was appointed in May 2003.
505	Mr. Heinze	Reviewed ANGDA's broad authorities that include the features of a public corporation. Explained that the Board of Directors is given decision-making control of the Authority and its corporate features.
549	Mr. Heinze	Explained that ANGDA will produce a report by June 2004 on the feasibility of an LNG project out of Valdez with a spur line from Glennallen to Cook Inlet. Initially looked at how to accommodate Alaska's needs for gas. The Authority found that the volume was quite low, with an inability to meet the state's needs. Attention shifted to a project to transport the gas to tidewater and connect with a spur line to Cook Inlet to provide benefits to Alaskans as well as export capability.
706	Mr. Heinze	Stated that the creation of other petrochemical or business industries in

		Alaska may be the single greatest benefit of North Slope gas development.
745	Mr. Heinze	Reviewed ANGDA's study of a project that would involve a gas treatment plant on the North Slope to remove the CO2, a pipeline running alongside the Trans-Alaska Pipeline to Valdez, an LNG plant in Valdez to cryogenically cool the gas, and a fleet of tankers to deliver the gas to the West Coast or across the Pacific Ocean to potential customers. Gave a price estimate of \$12 billion for the project.
834	Mr. Heinze	Explained that this would be a difficult commercial project because the high rate of return on \$12 billion when translated into pricing in the marketplace doesn't fit with the expected long-term conservative price of gas. When ANGDA recalculated those economics under other, more appropriate assumptions as an Authority with a unique tax status, it dramatically altered the economics into more competitive project.
942	Mr. Heinze	Discussed broader view of how the project would work. Referred to "ANGDA All-American LNG Project Conceptual Schedule" (copy on file) and explained the project involves three phases: a feasibility phase of determining the market, a business plan, and contracting to build the project. The feasibility decision will be made in June 2004 when ANGDA publishes its findings. Alaskans will make the decision whether or not to proceed with the project.
1147	Mr. Heinze	Asserted that the information ANGDA will provide by June 2004 will be extremely valuable to the legislature. Stressed that the \$2.5 million general fund contribution is ANGDA's total funding request from the state and that the Authority will privately finance the remainder of the project. The first \$200 million raised through venture capital will allow ANGDA to develop thorough information about the project's credibility that is essential in approaching lenders. The \$10 billion needed to build the project will be raised through revenue bonds.
1343	Mr. Heinze	Delineated legislature's role and said that \$2.5 million represents his estimate

		of what will be needed.
1525	Co-Chair Harris	Asked if ANGDA has obligated and spent the money it received from the state.
1540	Mr. Heinze	Responded that he's an employee of the Department of Revenue and he has obligated the funding, although not all of the work has been completed.
1633	Mr. Heinze	Summarized FY 04 Funding Plan (copy on file.) An essential component is marketing the project and North Slope gas.
1736	STEVE PORTER, DEPUTY COMMISSIONER AND LIAISON TO ALASKA NATURAL GAS DEVELOPMENT AUTHORITY, DEPARTMENT OF REVENUE	Explained that he has worked closely with ANGDA on the funding commitments, which cannot exceed \$350 thousand. Recently the money has been obligated and contracts have been signed. Currently the total amount is close to being fully committed to contracts.
1936	Mr. Heinze	Continued explaining the FY 04 Funding Plan. Money has been set aside to produce the findings in a report to the public.
2042	Mr. Heinze	Reviewed FY 04 Funding Plan, Business Contractors. Commented that ANGDA is awaiting good legal advice on the exact tax structure of the Authority. The Benefits Analysis will review economic and personal impacts to Alaska, including potential new jobs, rising property values, and lower heating bills.
2250	Mr. Heinze	Spoke to issues relating to market dynamics. Contracting for the best advice in these business analyses has been expensive.
2331	Mr. Heinze	Reviewed the third phase, Project Contractors, in which funds are set aside for engineering and technical project management issues to deliver gas to Valdez and liquefy it. The Authority has received invaluable information and assistance from several entities, and signed a Memorandum of Agreement with Mitsubishi for their expert advice relating to natural gas.
2557	Mr. Heinze	Stressed that there are four months to finish the remaining work of ANGDA and it is more than a statutory deadline because it also involves the market and the feasibility of the project.
2649	Mr. Heinze	Mentioned that this work by ANGDA will yield business structure information beneficial to the legislature in dealing

		with the Stranded Gas Act. Spoke to the other benefits of the work.
2920	Co-Chair Harris	Asked about the feasibility of supplying gas to Kenai Peninsula.
2953	Mr. Heinze	Replied that legislation will address the specific project. A requirement of Ballot Measure 3 was the inclusion in the project of a spur line from Glennallen to the Cook Inlet area because of a great need for gas in that area, with near depletion of the plentiful gas of 30 years ago.
3127	Mr. Heinze	He continued, current Cook Inlet wholesale price of gas is \$2.25, which also applies to power generation, driving the electrical cost as well. The price of gas in Anchorage is projected to double the current price in 5-7 years.
3219	Mr. Heinze	Asserted that once the gas is delivered to tidewater and Cook Inlet, it would be possible to deliver it to coastal communities and up the rivers to reach 99% of Alaskans.
2219	Vice-Chair Meyer	In relation to last week's announcement by the producers, asked the possibility of all three parties working together.
3425	Mr. Heinze	Replied that ANGDA doesn't need to build, own and operate all the benefits. ANGDA has had initial discussions with Pacific Star and would like to discuss the project with all the parties.
3606	Vice-Chair Meyer	Noted that Mr. Heinze referred to this as "The People's Pipeline," and asked if \$2.8 million is the total funding request.
3703	Mr. Heinze	The supplemental request for \$2.15 added to the \$350 thousand will total \$2.5 million. The project is benefit-driven, not investment-driven, making it belong to Alaskans. Individuals may invest in the project.
3903	Representative Fate	Inquired if one of the biggest challenges to the project relates to The Jones Act, and asked whether there has been resolution.
4035	Mr. Heinze	Explained that The Jones Act requires that any trade between U.S. ports be carried in U.S. built, crewed and flagged ships. One target market is the West Coast, requiring LNG vessels to supply the gas. Reviewed the issues.
4229	Mr. Heinze	Discussed LNG tanker cost estimates. The

		Jones Act explicitly requires that the tanker hull be of U.S. manufacture, but a tanker potentially could include Japanese ship interiors. The time involved in building a fleet is a potential problem. The State would contract out for the ships to be built, or for use of existing ships.
		<b>TAPE HFC 04 - 14, Side B</b>
4633	Mr. Heinze	Discussed the Stranded Gas Act in response to a question by Representative Fate.
4519	Representative Hawker	Asked if there is a mechanism to insulate the state from a risk of loss.
4437	Mr. Heinze	Responded that Ballot Measure 3 is explicit that the Authority cannot obligate the full faith and credit of the state. The project financing is non-recourse financing, and issuing a note, bond or certificate is high risk and high reward. At-risk investors will be brought in early.
4223	Representative Hawker	Asked if ANGDA has discussed with tax counsel the compatibility of issuing private investor bonds that will not put the state at risk and still retain tax exempt status.
4138	Mr. Heinze	Explained that he has sought the best legal advice because of potential conflicts. The Authority can't propose technical amendments to the law.
3945	Representative Hawker	Asked if ANGDA would have answers to the tax questions if the legislature approves the \$2.5 million funding request.
3921	Mr. Heinze	Replied, "Absolutely."
3835	Representative Stoltze	Asked what percentage the State would need in order to have a voice in the process.
3807	Mr. Heinze	ANGDA will help the state by keeping the cost of transporting the gas as low as possible, which will increase the wellhead value to benefit the producers and sponsors.
3632	Mr. Heinze	Continued, the ANGA is not directly involved in the Stranded Gas applications. The three major companies are submitting applications, and all discussions involving ANGDA, a public entity, are public.
3453	Representative Rokeberg	Commented in support of the spur line. Expressed concern regarding the \$200 million development phase to be financed

		through the high-yield junk bond market. Questioned the short four-month window to devise a plan for the Security Exchange Commission, to have the bonds in place and to sell them almost immediately. He asked if there aren't conflicts between the public authority having tax exempt status but a lack of equity position.
3227	Mr. Heinze	Responded with a discussion of debt financing.
2934	Representative Rokeberg	Asked if ANGDA will maintain its public status and not look for any private equity investment.
2914	Mr. Heinze	Replied affirmative, and discussed the tax code.
2805	Representative Rokeberg	Commented on the seed money and the turn-around coming up with the \$200 million dollars in bond proceeds. He expressed skepticism, stating that it will be difficult to demonstrate a profit.
2653	Mr. Heinze	Responded that current cash flows for this type of project are good. The bonding agencies have confidence in the project. Big projects can be financed and the market will support them.
2459	Representative Rokeberg	Asked if the \$12 billion project estimate is accurate in light of Yukon Pacific's figure of \$18-19 billion.
2435	PAUL FUHS, REPRESENTING BACKBONE	Clarified that Yukon Pacific's estimate was closer to \$12 billion dollars.
2409	Co-Chair Williams	Commented on the decline in oil production in the State and asked if some of the oil tankers could be used for this project.
2332	Mr. Heinze	Replied that's a good idea; however, an LNG has an expensive, cryogenic insulated tank. The oil tankers are not designed for this type of tank. An LNG tanker has a separate system and it is difficult to change the service.
2239	Mr. Heinze	Commented, could fill Jones Act barges successfully along the coast.
2220	Co-Chair Williams	Asked the source of funding for the building of the facility, and if it comes from the state, asked if it would reduce the production price of the gas.
2150	Mr. Heinze	Responded that because of the non-taxable status, the Authority's number is 30% lower than other funders. Servicing debt only would drop it further. He suggested that the issue of how the State

		will improve the marketability will eventually be addressed. It will be in some form of the State giving up revenue, but ANGDA offers cost of service by not paying federal income tax.
2015	Representative Hawker	Referenced the chart, FY 04 Funding Plan (copy on file.) He asked about the components that make up 60% of the costs: Plant Concepts, Engineering Design and Cost & Schedule. He recommended working on the confidence builders first.
1759	Mr. Heinze	Addressed Contractor Coordination that assists with managing the complex and watching the outflow. Under the business contractors are items underway. The project economics have not yet been launched.
1646	Mr. Heinze	Continued discussing contractor coordination and permit review. Spoke to the potential benefit of increasing Alaska hire.
1506	Mr. Heinze	Described issues in terms of the engineering design. Asserted that \$750 thousand dollars does not design very much. Discussed the idea of co-locating the compression stations with the Alyeska pump stations to facilitate construction and, later on, the operation and maintenance of the gas line. He was unsure if the producers have considered the idea.
1256	Mr. Heinze	Discussed the cost and schedule aspects. The work to be done is well defined, and how fast it can be accomplished may be crucial. Some of the factors are different than those with the oil line. If it could be finished in two construction seasons, he said the impact could be incredible.
1145	Mr. Heinze	Limiting choices for money requests.
1126	Mr. Heinze	Innovative thinking.
1105	Representative Hawker	Expressed his support for moving to the next level and diagnosing viability of the project.
1036	Mr. Heinze	Explained that he works with Mr. Porter to issue contracts through the State system. There are others who share concerns with spending public money. Asserted this will yield a good benefit for the State of Alaska.
924	Representative Croft	Asked when the Board was appointed.
914	Mr. Heinze	Responded, May 2003.

910	Representative Croft	Asked when ANGDA received the first installment of \$150 thousand.
902	Mr. Heinze	Replied, July 1, 2003.
855	Representative Croft	Asked when ANGDA received the \$200 thousand from Legislative Budget & Audit.
847	Mr. Heinze	He was unsure if it was October or early November, 2003.
841	Representative Croft	Asked his scheduled date for letting these contracts in order to complete the mandated report by June 2004.
833	Mr. Heinze	Replied, "Yesterday." He is willing to work with the Legislature to make things happen. Feeling pressure but he has a background of pulling together to get things done. Stressed that the timing of funding is crucial.
733	Representative Croft	Noted that the funding has been delayed. In a year and half schedule, a year has been wasted. The Authority needs the money soon, and he expressed hope that the legislature would fund the project over the next month.
623	Representative Heinze	Asked which petrochemical by-product of the LNG could be the most profitable.
546	Mr. Heinze	Explained that this project will deliver natural gas, which is mostly methane and some ethane, and also heavier hydrocarbons that have very high values compared to methane. The pipeline would be designed to carry the hydrocarbons to the LNG plant where they could be extracted. Suggested that once the private sector knows what is available, the ingredients can make it profitable to industry.
338	Representative Heinze	Spoke to the critical shortage of gas for the electrical grid of the state and emphasized the need for the state to provide the infrastructure for that.
243	Mr. Heinze	Offered to prepare a paper on the supply/demand issue.
138	Mr. Heinze	The ANGDA has limited ability to change the gas supply situation but it could make available gas at the current market price. For those projects that would require gas at a much lower price than the current price, the Authority "probably economically cannot do that." In the case of Agrium, he was unsure how much ANGDA could help them.
035	Representative Heinze	Asked if ANGDA could provide gas to Agrium at today's price, which they need

		to stay in business. Mr. Heinze responded that the Authority is the only hope for Agrium, which is on a slender pricing edge.
		<b>TAPE HFC 04 - 15, Side A</b>
0031	BOB FAVRETTO, MEMBER, BOARD OF DIRECTORS, ALASKA NATURAL GAS DEVELOPMENT AUTHORITY	Stated that ANGDA is tasked by the mandate of Ballot Measure 3 to answer questions by June 15. Expressed frustration with the workload over next four months and asked the committee to fund the project.
0237	Mr. Faveretto	Said that the Board is working with contractors to answer the question of whether or not it is a viable project.
0351	BOB SULLIVAN, MEMBER, BOARD OF DIRECTORS, ALASKA NATURAL GAS DEVELOPMENT AUTHORITY	Agreed with Mr. Heinze that the numbers show potential. Said that he himself is personally tight-fisted with public dollars. Spoke in support of the need to take the next step and further fund the project. The most important question is how to maximize the state's return from the development of a finite resource. By the end of June, the report will say if this project should proceed.
0544	Mr. Sullivan	Reviewed the meetings of the board with various entities that have included Yukon Pacific, Sempra, Mitsubishi, Pacific Star, and the Port Authority. Mentioned that Conoco Phillips analyzed the project as a corporate entity, not as a tax-free entity. Bechtel analyzed the costs of the LNG line a couple years ago. The board met with Enstar to discuss southcentral's gas needs and Enstar's interest in building a gas line.
0720	Mr. Sullivan	Stated that investors must be convinced that there is a market. The board has met once a month over the 8 months of its existence. He expressed hope that the legislature would concur that the project shows enough potential to move forward and that \$2.1 million is a reasonable request.
0809	Representative Kohring	Asked if a government-owned and operated gas pipeline is preferable to private sector ownership.
0832	Mr. Sullivan	Responded that the best interest of the state must be considered in developing a resource that will only last 30-70 years. Asked how the state can maximize its return to all the citizens if it owns the resource and leases it out. Sometimes the state is involved in infrastructure,

		or transporting energy from the source to the market.
0937	Representative Kohring	Commended the Board and the Authority for their work, but expressed concern over the government being involved in private sector projects that haven't succeeded. He cited as examples the Susitna Dam Project, the Pt. McKenzie Dairy, the Seward Grain Terminal, and Delta Barley. He frankly expressed skepticism and concern over establishing a bureaucracy on state payroll.
1051	Mr. Sullivan	Countered that Delta Barley wouldn't have been financed if it had gone out to market, whereas this project must prove there's a market to get funding from a bank. The infrastructure that the state owns will facilitate the project. The private sector will make a lot of money, with tremendous involvement.
1231	Representative Kohring	Asked if he could point to any world examples of government-owned facilities of this nature which are a success.
1249	Mr. Heinze	Replied that almost all of the foreign countries now developing LNG, including Cutter and Sakhalin, are government-owned facilities partnered with the private sector. If the ANGDA built the LNG plant, at a low cost of service infrastructure, it would be almost identical with the situation in Indonesia, with no tax and no interest. Stated that it might be positive for Alaska but those decisions haven't been made yet.
1352	Representative Kohring	Referred to legislation he sponsored last year authorizing the Alaska Railroad to issue tax exempt bonds, and asked if the Authority has the legal means to take advantage of the \$18 billion of cheap money that is available.
1426	Mr. Heinze	Replied that he's aware of the bill. The Authority would look at that vehicle as part of its total bonding consideration, and the limitations on the amount of the bonding.
1548	Representative Kohring	Reiterated his skepticism.
1609	Mr. Heinze	Responded that he respects Representative Kohring's position. If the private sector is unwilling, perhaps the state will take greater role..
1716	Co-Chair Harris	Asked if there is any assurance of the Administration's position on the funding

		request.
1756	Mr. Heinze	Reiterated that he is a state employee of the Department of Revenue, and he has arranged to delegate himself certain authorities. Since Senator Therriault introduced his bill, Mr. Heinze has not received any indication of the Governor's position on the funding request. There are concerns on spending the money.
1936	Co-Chair Harris	Asked for clarification that he is an employee of the state requesting \$2.1 million but he's unsure if the state supports this request.
2008	Mr. Heinze	Responded that he's unsure of the Administration's position on this specific request.
2022	Mr. Sullivan	Suggested that the Administration is neutral but recognizes the ANGDA needs funding to accomplish its mission by June 2004.
2044	Co-Chair Harris	Pointed out that \$150 thousand is earmarked for ANGDA in the FY 05 budget, and asked how the money will be utilized if the Authority is inactive after July 1.
2111	Mr. Sullivan	Replied that it's a good question. There is no overt opposition from the Administration to the appropriation. Co-Chair Harris countered that there is no overwhelming support for it, either.
	<u>ADJOURNMENT</u>	The meeting was adjourned at 3:34 PM