

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS

March 27, 2003

3:20 p.m.

MEMBERS PRESENT

Representative Vic Kohring, Chair
Representative Hugh Fate
Representative Jim Holm
Representative Lesil McGuire
Representative Norman Rokeberg
Representative Harry Crawford
Representative Beth Kerttula

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE JOINT RESOLUTION NO. 17

Strongly encouraging the Secretary of the Interior to conduct additional competitive oil and gas lease sales within the National Petroleum Reserve in Alaska.

- MOVED HJR 17 OUT OF COMMITTEE

HOUSE BILL NO. 204

"An Act relating to the regulation of natural gas pipelines under the Pipeline Act."

- MOVED CSHB 204(O&G) OUT OF COMMITTEE

PREVIOUS ACTION

BILL: HJR 17

SHORT TITLE:LEASES IN NATL PETROLEUM RESERVE

SPONSOR(S): REPRESENTATIVE(S) KOHRING

Jrn-Date	Jrn-Page		Action
03/14/03	0540	(H)	READ THE FIRST TIME - REFERRALS
03/14/03	0540	(H)	O&G, RES
03/27/03		(H)	O&G AT 3:15 PM CAPITOL 124

BILL: HB 204

SHORT TITLE:REGULATION OF NATURAL GAS PIPELINES
SPONSOR(S): REPRESENTATIVE(S)CHENAULT

Jrn-Date	Jrn-Page		Action
03/19/03	0586	(H)	READ THE FIRST TIME - REFERRALS
03/19/03	0586	(H)	O&G, RES
03/27/03		(H)	O&G AT 3:15 PM CAPITOL 124

WITNESS REGISTER

RANDAL G. BUCKENDORF, Counsel
Anchorage Legal Department
ConocoPhillips Alaska, Inc.
Anchorage, Alaska

POSITION STATEMENT: During hearing on HJR 17, testified in support of Alternative A of the Bureau of Land Management's draft environmental impact statement; said BLM should proceed with the lease sale as soon as possible.

JAMES COWAN, Geologist
Division of Oil & Gas
Department of Natural Resources
Anchorage, Alaska

POSITION STATEMENT: Testified in support of HJR 17; answered questions.

REPRESENTATIVE MIKE CHENAULT

Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Testified as sponsor of HB 204.

KEVIN TABLER, Manager of Land and Government Affairs
Union Oil Company of California (Unocal)
Anchorage, Alaska

POSITION STATEMENT: Testified in support of HB 204, which he called necessary legislation; answered questions.

A. BEN SCHOFFMANN, Project Manager

Alaska Business Unit
Domestic Production
Marathon Oil Company;
Vice-President, Kenai Kachemak Pipeline, LLC
Anchorage, Alaska

POSITION STATEMENT: Offered presentation in support of HB 204 and SB 151, the companion bill; answered questions.

DAVE HARBOUR, Commissioner, Chair
Regulatory Commission of Alaska (RCA)
Anchorage, Alaska

POSITION STATEMENT: Offered perceptions with regard to HB 204 and how the situation differs in the Lower 48.

JIM STRANDBERG, Commissioner
Regulatory Commission of Alaska
Anchorage, Alaska

POSITION STATEMENT: During hearing on HB 204, answered questions about RCA's role in consumer protection, the existing Pipeline Act, and other issues; suggested the need for RCA to maintain jurisdiction.

ANTONY SCOTT, Commercial Analyst
Division of Oil & Gas
Department of Natural Resources
Anchorage, Alaska

POSITION STATEMENT: During hearing on HB 204, answered questions pertaining to DNR's fiscal note analysis.

ACTION NARRATIVE

TAPE 03-16, SIDE A

Number 0001

CHAIR VIC KOHRING called the House Special Committee on Oil and Gas meeting to order at 3:20 p.m. Representatives Kohring, Holm, Fate, Crawford, and Kerttula were present at the call to order. Representatives Rokeberg and McGuire arrived as the meeting was in progress.

CHAIR KOHRING introduced Representative Holm as the new committee member who was replacing Representative Chenault because of revised committee assignments.

HJR 17-LEASES IN NATL PETROLEUM RESERVE

Number 0104

CHAIR KOHRING announced that the first order of business would be HOUSE JOINT RESOLUTION NO. 17, Strongly encouraging the Secretary of the Interior to conduct additional competitive oil and gas lease sales within the National Petroleum Reserve in Alaska.

CHAIR KOHRING, sponsor, informed members that the National Petroleum Reserve in Alaska [known on its Bureau of Land Management (BLM) web site as National Petroleum Reserve-Alaska (NPR-A)] was established in 1923 by President Harding as a 23-million-acre area from which to acquire oil in the event of a national emergency. Then called Naval Petroleum Reserve [No. 4], NPR-A is the largest block of federal land in Alaska. In 1976, Congress transferred management to the Department of the Interior, with a provision that oil development would be prohibited except by Act of Congress; in 1980, the reserve was opened with a further provision that 50 percent of the royalties from any oil extracted would go to the State of Alaska, despite the fact that the reserve is federal land.

CHAIR KOHRING said Alaska stands to benefit from additional oil exploration there. He suggested this is timely: because of Congress's recent vote against opening the Arctic National Wildlife Refuge (ANWR) [to exploration and development], it is prudent to aggressively look at other areas in Alaska. He noted that Drue Pearce, former state Senate president and now a special assistant for the U.S. Department of the Interior, recently recommended submitting a resolution of this nature.

Number 0375

REPRESENTATIVE HOLM offered his understanding that the state's 50 percent doesn't necessarily go into the general fund. He asked about that.

CHAIR KOHRING observed that nobody from the Department of Revenue was at the meeting or on teleconference. He asked Mr. Buckendorf to respond.

Number 0528

RANDAL G. BUCKENDORF, Counsel, Anchorage Legal Department, ConocoPhillips Alaska, Inc. ("ConocoPhillips"), presented his own testimony first. Mr. Buckendorf informed members that he does both environmental and pipeline-related legal work; he has been participating in the NPR-A environmental impact statement (EIS) analysis, beginning in 1998 with the northeast planning area, and continuing now with the northwest planning area. He told members:

ConocoPhillips believes it is possible for environmentally sound and culturally responsible oil and gas exploration and development to occur in the

National Petroleum Reserve-Alaska. As I mentioned, in 1998 the Bureau of Land Management, the BLM, conducted a similar environmental impact statement process and, as a result of that, held two lease sales, in 1999 and again in 2002; this is for the northeast planning area. As a result of that, ConocoPhillips and our partner, Anadarko Petroleum Corporation, participated in those lease sales and are the number-one acreage holders in the northeast planning area.

We have also been fortunate to be successful in our exploration process, and just this January have proposed the first development in [NPR-A]. We're currently conducting the environmental impact statement process for three satellite development projects that will be produced back to our Alpine project. That process is currently underway.

Number 0672

MR. BUCKENDORF addressed the northwest planning area. Explaining why ConocoPhillips supports "Alternative A" in the draft EIS, he said it is the only option that makes the entire "high-prospectivity area" available for lease in a manner that provides meaningful access to the northernmost part of the reserve, the "Barrow arch," without imposing unnecessary restrictions upon surface occupancy. Contending that Alternative A will fully protect sensitive wildlife and traditional lifestyles, he said it doesn't "prematurely and categorically exclude leasing from certain lands without first understanding the potential negative impacts of the proposed development, if any, and whether such potential impacts can be mitigated or eliminated." Saying Alternative A appropriately identifies sensitive areas while reserving the application of specific protective measures until the future, when site-specific evaluations and determinations can be made, Mr. Buckendorf suggested BLM should proceed with this lease sale as quickly as possible.

Number 0850

MR. BUCKENDORF returned attention to Representative Holm's question and said:

The 50-50 split, ... as part of the revenue-impact process, is split between the federal and state and local governments. As part of the 1998 analysis, the

1999 lease sale and 2002 lease sale resulted in - I don't have the specific numbers here in front of me - well over a hundred million dollars in lease sales, bonuses. 50 percent does go to the state; the state then shares that with local impacted governments, the North Slope Borough ... particularly.

That money goes into what is termed an "impact assistance fund." I believe in the '99 lease sale about ... 60 to 70 percent ultimately went to the North Slope Borough. ... The latest data was not available ... as of last week for the 2002 lease sale. The way I understand the process is that if there are any funds left that do not go into the impact assistance fund, then that can be utilized and goes into the general fund.

Number 0970

REPRESENTATIVE HOLM asked whether possibly there could be nothing left for the state, then.

MR. BUCKENDORF suggested the Department of Revenue could answer better, but said monies always go to the state and that what ends up going to the local boroughs - the North Slope Borough, in this instance - is for the impact assistance fund.

CHAIR KOHRING offered to explore with the Department of Revenue different hypothetical scenarios and what kinds of monies could be expected. He mentioned potential gain in terms of general economic growth and jobs, as well as money to local communities such as Barrow.

MR. BUCKENDORF offered to provide data that he'd prepared to submit in testimony in two weeks.

Number 1073

REPRESENTATIVE FATE remarked that how much of the state's 50 percent will be used for impact funds and so forth won't be known ahead of time. It depends on "what is turned in" to a committee that determines the impact to villages and whether to grant the money. Furthermore, this money could be put into the permanent fund or PCE [power cost equalization], for example, and thus there might not be any money put into the state's general fund.

Number 1240

JAMES COWAN, Geologist, Division of Oil & Gas, Department of Natural Resources, in response to Chair Kohring, said he supports the resolution. He said the revenue sharing is a big aspect and that Representative Fate had painted a pretty accurate picture of how it works. He noted that a specific statute establishes how those funds will be distributed, and agreed that the general fund might not receive a lot. He added that the funds are unpredictable and depend on the sale results, development results, and production.

CHAIR KOHRING asked whether Mr. Cowan thinks the timing is appropriate because of the recent [congressional vote against opening] ANWR.

MR. COWAN answered in the affirmative.

Number 1308

REPRESENTATIVE FATE asked whether Mr. Cowan believes this will redirect the federal efforts away from continuing efforts to open ANWR.

MR. COWAN said this has been a concern for several years within the state administration and DNR. He added that he believes it is important for the state to have a benchmark for revenue-planning purposes.

Number 1393

CHAIR KOHRING offered his assessment that the industry is quite supportive of this resolution. He said the state should pursue all significant opportunities for oil development in the state.

CHAIR KOHRING noted that everyone who'd signed up had testified already. He turned attention to members' comments.

Number 1423

REPRESENTATIVE FATE expressed concern about the timing, saying the focus on NPR-A has been used repeatedly in the past to refocus away from ANWR. He emphasized his desire to keep the focus on ANWR instead.

CHAIR KOHRING respectfully disagreed. He said he'd prefer drilling in ANWR, but doesn't see this resolution as refocusing.

Rather, it is an addition for expanding oil and gas development. Even if few dollars go into the general fund, it will help the economy in a substantial way.

Number 1621

REPRESENTATIVE MCGUIRE suggested adding a section that encourages a shift in the percentage Alaska will receive.

CHAIR KOHRING said he'd be receptive to such a conceptual amendment.

Number 1720

REPRESENTATIVE FATE pointed out that the 50-50 split has been adjudicated through litigation brought by the recipients of the impact funds; the State of Alaska lost. He questioned the propriety of requesting in a resolution a different set of figures.

REPRESENTATIVE HOLM asked Representative Fate whether there is some vehicle by which the state could change how the state's 50 percent is applied with regard to the general fund.

REPRESENTATIVE FATE answered that the 50 percent is already affected by the "impact money." He surmised that changing it such that the federal government receives 40 percent would require an Act of Congress. If the state then got 60 percent, he asked, would the state get 10 percent more or would that 60 percent be split up through "the impact funds"? He said he wasn't sure.

Number 1945

REPRESENTATIVE MCGUIRE said she envisioned a "WHEREAS" clause that would encourage the congressional delegation to explore an Act of Congress to change the percentage to 60-40. She added that she wasn't sure whether it was worth pursuing.

REPRESENTATIVE FATE said he'd be amenable after looking into whether it would be proper and could be done. He pointed out that it is federal property that goes back to the Teapot Dome scandal, and suggested the chance of success would be remote.

Number 2070

CHAIR KOHRING reiterated that he is amenable to Representative McGuire's suggestion, and said he'd like to lobby for the highest percentage possible for Alaska. He proposed that he and his staff research the issue, however, with an eye toward bringing it to the House Resources Standing Committee.

Number 2114

REPRESENTATIVE CRAWFORD spoke in favor of the resolution. He remarked that Representative Fate's comments gave him pause, and that he didn't want anything to take away from the chances of success with ANWR. He said he believes there is a better chance of getting the jobs sooner through NPR-A, however, and that he doesn't believe this resolution would be detrimental to the efforts towards ANWR.

Number 2215

REPRESENTATIVE ROKEBERG stated support for the resolution, but highlighted a national move to focus on NPR-A [instead of ANWR]. He questioned the economic benefit to the state because of current constraints.

Number 2324

REPRESENTATIVE HOLM moved to report HJR 17 out of committee [with individual recommendations and the accompanying fiscal notes].

REPRESENTATIVE FATE objected.

A roll call vote was taken. Representatives Holm, Rokeberg, McGuire, Crawford, Kerttula, and Kohring voted in favor of reporting HJR 17 from committee. Representative Fate voted against it. Therefore, HJR 17 was reported from the House Special Committee on Oil and Gas by a vote of 6-1.

HB 204-REGULATION OF NATURAL GAS PIPELINES

[Contains discussion of SB 151, the companion bill]

CHAIR KOHRING announced that the final order of business would be HOUSE BILL NO. 204, "An Act relating to the regulation of natural gas pipelines under the Pipeline Act."

Number 2396

REPRESENTATIVE MIKE CHENAULT, Alaska State Legislature, sponsor of HB 204, informed members that in 2000 the legislature amended Alaska's Pipeline Act to make provisions for the operation of a North Slope gas pipeline. One provision allowed two classes of transportation services: firm and interruptible. At the time, the North Slope gas pipeline was the only gas pipeline in Alaska proposing to provide such a service. Currently, however, a pipeline under construction on the Kenai Peninsula [by Kenai Kachemak Pipeline, LLC (KKPL)], proposes to provide transportation to the Cook Inlet service area. He offered his belief that this the first pipeline to be built in Alaska since the oil pipeline [the Trans-Alaska Pipeline System (TAPS)].

REPRESENTATIVE CHENAULT reported that recently KKPL requested authorization from the Regulatory Commission of Alaska (RCA) to provide firm and interruptible service. Although RCA hasn't issued a final ruling on this portion of the case, it has raised questions of whether contract carriage for gas pipelines elsewhere in Alaska was permissible, given the 2000 amendment to the Pipeline Act that apparently was exclusive to transportation of gas on the North Slope. He said HB 204 is intended to resolve that question raised by RCA. It makes firm and interruptible service available to any natural gas pipeline carrier operating in Alaska. It also adds the definitions of "natural gas pipeline" and "natural gas pipeline carrier".

Number 2659

KEVIN TABLER, Manager of Land and Government Affairs, Union Oil Company of California (Unocal), voiced support for HB 204, calling it necessary legislation. Noting that Unocal has extensive operations throughout Cook Inlet, he indicated this bill provides for transportation throughout Alaska for other areas [besides the North Slope] where transportation systems will be used and needed. Mr. Tabler opined that it wasn't intended in 2000, when the Pipeline Act was amended, to preclude other areas, and that there just weren't other projects then. He said this sort of activity will come up repeatedly, and commended Representative Chenault for introducing the bill.

Number 2719

REPRESENTATIVE ROKEBERG asked whether Unocal has any gas pipelines affected by this bill.

MR. TABLER answered that [Unocal] has an 40-percent working-interest ownership in the KKPL.

REPRESENTATIVE ROKEBERG asked whether other pipelines would be affected.

MR. TABLER said not to his knowledge at this time.

Number 2768

A. BEN SCHOFFMANN, Project Manager, Alaska Business Unit, Domestic Production, Marathon Oil Company; Vice-President, Kenai Kachemak Pipeline, LLC, gave a presentation and provided a 12-page handout. He referred to page 2 of the handout and mentioned the Senate companion bill, SB 151, indicating he'd addressed many of the same issues in the Senate Labor and Commerce Standing Committee. Suggesting this "cleanup" bill just gives RCA another tool, he said it allows RCA to approve the offering of firm and interruptible service - sometimes known as contract carriage - for any gas pipeline in Alaska, that it doesn't remove RCA's authority in any way, and that it clarifies that RCA has authority to rule on tariffs for such pipelines.

MR. SCHOFFMANN suggested this is considered sound policy in most realms; it aligns with what has been happening in the Lower 48 since deregulation of natural gas over the past two decades, and is something the Federal Energy Regulatory Commission (FERC) is accustomed to seeing there. However, there haven't been many pipelines in Alaska, and thus there hasn't been a need to deal with the evolution elsewhere in the natural gas business.

Number 2885

MR. SCHOFFMANN referred to page 3 of the handout and explained that firm service is common to many things like public utilities; electrical service often is offered on a firm or interruptible basis, for example. [Firm service] is a way of reserving capacity or promising delivery in exchange for a reservation fee paid in advance, regardless of whether the service is used. By contrast, interruptible service is paid for on an as-used basis, but is subject to interruption - or, more likely, curtailment - if there is a capacity restriction or conflict at any point in time.

MR. SCHOFFMANN addressed page 4 of the handout, indicating the bill is important to both pipeline investors and shippers. For pipelines, he mentioned setting a benchmark for the minimum capacity that people are willing to promise and pay for, whether or not they utilize it. Without such a tool, there is a risk of

putting in an unnecessary pipeline or one that is too large or small. The pipeline investor wants minimal risk, as well as and assurance of some return on the investment, he added. Turning to page 5, he noted that a pipeline's customers - shippers who generally are producers of the gas - would like [to be able to choose between] firm and interruptible service for two reasons.

TAPE 03-16, SIDE B

Number 2995

MR. SCHOFFMANN explained that, first, this allows the shipper to align its gas-transportation services to its gas sales. The interruptible [sales contracts] may have a lesser priority sometimes, but may be subject to curtailment if there is some problem. If a producer has interruptible contracts, the customer may not be willing or consider it worthwhile to pay to reserve capacity. And people with firm gas-sales contracts ideally would like firm transportation service. It does no good to promise to produce the gas but then not be able to ship it to the customer. If the pipeline doesn't have the capability to offer firm and interruptible service, he said, there can be a conflict in the relationship of the producer and the customer because the pipeline cannot adhere to the very thing required.

MR. SCHOFFMANN said, second, that some shippers/producers haven't yet fully explored for their natural gas. It would be inappropriate for them to commit to paying for capacity they may never need or capacity of the wrong volume. This [bill] allows them time to look at that. This offers the shipper a choice: firm service if the shipper needs to deliver gas in a certain amount to a certain place, which requires paying a reservation fee for which the pipeline will promise to deliver the gas, or interruptible service for those unwilling to pay that reservation fee. He emphasized that the key element is alignment.

MR. SCHOFFMANN, addressing page 6 of the handout, told members the bill won't change the open-access provisions in AS 42.06; the intent isn't to exclude potential shippers, but to give them a choice as to the type of service. He opined that the bill won't have an adverse fiscal impact on the state.

Number 2865

MR. SCHOFFMANN brought attention to the fiscal note [from DNR, dated 3/26/03, the analysis for which says it is difficult to predict what effects this bill might have on revenues because it

is difficult to predict the effects of contract-carriage pipelines on gas exploration and development]. Agreeing with the fact that the fiscal note [shows zero cost under the categories "Operating Expenditures" and "Fund Source"], he referred to the second page of the analysis, which read:

For pipelines that are owned by non-affiliated pipeline companies, contract carriage could reduce uncertainty of future throughput. This would reduce capital costs, which in turn could encourage pipeline construction and facilitate gas exploration and development. However, for pipelines that are owned by affiliated producers, contract carriage may not provide greater assurance of throughput; the pipeline company may know the volumes that its affiliated producer wants to ship. Meanwhile, contract carriage on a pipeline owned by an affiliated producer could potentially be used to impede pipeline access for non-affiliated producers. This could hinder natural gas exploration and development and ultimately result in a negative fiscal impact for the State.

Number 2840

MR. SCHOFFMANN disagreed with the foregoing analysis, asserting that this gives the smaller producers or "nonfirm" producers an opportunity to develop their resources "prior to that happening." Emphasizing that RCA will be regulating any lines under this statute and has the authority to approve or disapprove the tariffs offered for these services, he said:

It is their job to ensure that these are fair and equitable and are nondiscriminatory, ... regardless of what the affiliation of the shippers and the pipeline owners is. So, first of all, we believe that. Second of all, the RCA has the opportunity to fully take a look at those capacities ... that are being offered, and to make sure that there are services available for others who have yet to firm up their gas supplies.

And specifically in the case of KKPL, I'll be able to demonstrate that there is quite a bit of extra capacity available for the people who have yet to do their exploring at this point in time. So, again, we would disagree. We believe it's going to be an incentive because it allows pipelines to be built to

areas that ... currently are isolated from the infrastructure.

Getting a pipeline in is going to encourage investment. That's the first and foremost thing. And if we can't encourage the investment to be made, if we can't assure shippers that they're going to be able to move the gas that they have committed to sales, those are impediments. Building pipelines [is an incentive].

Number 2762

MR. SCHOFFMANN returned to the handout, page 8, explaining that KKPL is a limited liability company (LLC) "arranged in Alaska" and is a "Marathon-Unocal joint project" with Marathon Oil Company at 60 percent and Unocal at 40 percent. He told members:

KKPL will be a 33-mile pipeline 12 inches in diameter and cost about \$25 million. Its purpose is to ... connect new gas discovered by Marathon and Unocal around Ninilchik to the infrastructure of the pipeline network in the Cook Inlet, thereby allowing that gas to go wherever the Cook Inlet pipeline's infrastructure goes.

Number 2731

MR. SCHOFFMANN continued, expanding on information on page 9 of the handout, as follows:

In June 2002, we held an open season for prospective shippers; that includes leaseholders throughout the Kenai Peninsula - potential shippers and customers. Two shippers, Marathon and Unocal, made firm commitments - so, in other words, they'd like this firm gas - for about 300 Bcf [billion cubic feet] in total over 15 years.

The total peak committed rate is 90 million cubic feet a day. That is not flat. ... It is basically a profile that peaks at 90 and then drops off, so it ramps up to that and drops off. That dictated a 12-inch pipeline; the next smaller pipeline would have not necessarily been adequate for that. But this

pipeline has a capacity of about 130 million, so it's only about 75 percent full at its peak.

Before and after that, there is even more room available, so there is room for other shippers in that line. Expansion of that line is also possible if that comes about, if there's a justified need. So that's not the limit at that point in time; it could be larger.

Number 2690

CHAIR KOHRING asked, if the gas pipeline began in Ninilchik, where it would go.

MR. SCHOFFMANN answered that it would go to just south of Kenai, running up the Sterling Highway and then along Kalifonsky Beach ("K-Beach") Road to the Kenai gas field. Returning to the handout, pages 10 and 11, he offered the expectation of being in service two months ahead of the scheduled date of November this year. He indicated this legislation is important [to KKPL] because it will soon submit a request back to RCA for its tariff case; in order that RCA has clarity that it can rule on a two-part service, firm and interruptible; and to be able to do that as [KKPL] makes this filing, which it plans for probably sometime in April. He added, "For us, we believe it's key. It's pro-development without giving a handout. It gives people the opportunity to select two different types of service. We believe it's a positive thing for the State of Alaska."

The committee took an at-ease from 4:13 p.m. to 4:14 p.m.

Number 2636

MR. SCHOFFMANN turned attention to page 12 of the handout and offered the following in conclusion:

We really view this as providing a tool to the RCA. It means that the request for a pipeline to offer firm and interruptible service will be decided on the merits of that service, as opposed to a limitation in the statutes. It has a purpose in encouraging investment, both for pipeline owners and for prospective shippers, because it gives them more choices. And then finally, again, ... this is going to be before the RCA shortly. We would just like them

to have the clarification that this indeed [is] something they can rule on, based on its merits.

Number 2604

REPRESENTATIVE HOLM observed that page 9 of the handout shows that Marathon Oil Company and Unocal have committed to 300 Bcf of gas in 15 years. He asked what the capacity is of that 12-inch pipeline in that period of time.

MR. SCHOFFMANN noted that page 9 also shows that the 12-inch pipeline would have a nominal operating capacity of 130 million cubic feet per day. Calculating an answer, he said the peak rate of the 300 Bcf required by Marathon Oil Company and Unocal is 90 million cubic (Mmcf) feet a day. However, the expectation is to start at about 40 and ramp up to 90 Mmcf a day in about 5 years, and then taper off at about a 10 percent decline over 15 years. He added that more than half of the volume of the pipeline over that 15 years is still available on that basis.

Number 2518

REPRESENTATIVE CRAWFORD pointed out that other pipelines might not have excess capacity for common-carrier [shippers]. He asked whether that might be the reason the fiscal note says this could hinder natural gas exploration and development and ultimately have a negative fiscal impact for the state. He also asked what the reason was for wanting to change the law for the whole state and for any pipeline.

MR. SCHOFFMANN, expressing interest in keeping the bill as simple as possible, said offering these two classes of service isn't unusual policy and is very similar to what's being done by FERC in the Lower 48. He also said it isn't in the interest of pipeline owners to turn away business or in the interest of KKPL to ship only its affiliates' gas. He continued:

We would love to ship other people's volumes through that. Why? That's going to result in efficiency and cost savings for everybody involved. It was not our intent to find language that purely benefited ourselves, but rather to basically look at ... an incentive across the state. Again, this is in alignment with the way business has been done over the past decade and a half, ... as regulated by FERC in the Lower 48.

It's also an important issue for just attracting investment, both on the pipeline investors' side to this state - how ... are we going to incentive people to build pipelines if they cannot firmly line up the business in advance - and, secondly, we're going to incentivize the smaller producers and ones who haven't done that, because they will have a pipeline coming past them. So once the pipeline gets built, that's one of the biggest incentives to investment ... that I think you could see.

Number 2392

MR. SCHOFFMANN continued:

There are other regulations within the state. For example, we could choose to build gas-gathering lines, which are purely for the benefit of those investors. ... Those opportunities, if people wanted to do that, I believe are potentially there. So this is really just an alignment issue. And I ... understand your concern, but I believe this is expressed in this fiscal note as a hypothetical and is not necessarily well defined. And at this in point in time I would disagree with it because I just don't see that the incentive is for people to build assets that are only partly utilized or utilized for one specific purpose, as opposed to serving all the available gas that may be found.

Number 2350

REPRESENTATIVE CRAWFORD recalled that there has been some experience in Alaska of some smaller, independent companies being "frozen out" of pipeline capacity or overcharged for transportation costs. He suggested it behooves legislators to pay attention and not make that same mistake twice.

MR. SCHOFFMANN emphasized that it is RCA's mission to make sure that fair, nondiscriminatory tariffs are charged. He added:

All we're asking ... is to give them the approval to rule on this type of service. It's still under their purview to approve or disapprove the tariffs that would result and understand what access is available for others. We don't have models in place of this type. Most of the models the state has had have been

oil pipelines that have been even-divided-interest or common carriers [where] that's been a concern This is a different mechanism. I think it is tried and true, to some extent, with the experience in the Lower 48.

Number 2271

REPRESENTATIVE FATE told members he is for the bill, but suggested it might need to be clarified that it is intrastate. He said he'd requested FERC to get an opinion on future conflicts because of concern about possible conflicts among FERC, RCA, and the new pipeline authority [proposed by an initiative approved by voters in the 2002 election]. Since this deals with gas and not oil, he suggested making it clear that it is for in-state [transportation] and that there is no question RCA has that responsibility for in-state gas.

Number 2160

MR. SCHOFFMANN, in response to questions from Representative Rokeberg about the KKPL line, said:

Initially, when the first project was conceived, it was to run to Anchor Point, ... very near Homer. That was based on drilling activity that was planned or in progress at the time by ... our partner in this project, Unocal. Unfortunately, they didn't see the success they were hoping for. As a result, when we finished the open-season process in June 2002, the only firm capacity commitments we had were ... for delivering gas from [the] Ninilchik field, which is only about halfway that far.

There are certainly possibilities, again, that this ... line or some other line could be built to extend service farther south. Again, this is a transmission line, ... not a distribution line. But we are in conversation with ENSTAR [Natural Gas Company], for example, who's a partner in this project, who is very interested ... in serving the community down that direction. I believe our partner Unocal still has leases that direction, ... and other producers do too. If, at some point in time, more gas is discovered down that direction and there are firm commitments, again, to undergird any additional investment for an extension, that would certainly be considered and

possible. Other pipelines, likewise, could be built and tied in to KKPL.

Number 2063

REPRESENTATIVE McGUIRE mentioned discussions that day in her office and said she shared some concerns raised by Representative Crawford. She emphasized that smaller, independent companies - perhaps not even formed yet - will want to come into the marketplace; she suggested the need to encourage that, saying she believes it is healthy for the market and for Alaskans to have that kind of competition in the state. She continued:

One of the discussions that we had involved RCA, and ... we're in the process of looking at RCA as a whole right now. ... And I advocated ... and told you today that I think we really do need to have a specialist in this area. But ... you mentioned, too, that RCA, even right now, has the power to order expansion of the pipeline, even if there are more offers that are out there. Is that correct?

Number 1999

MR. SCHOFFMANN answered that under AS 42.06, if there are compelling reasons to do that because of the open-access concepts therein, he believes RCA has some authority in that respect. He indicated the hope and need to ensure that any investments KKPL makes are able to be recovered. He added that if there is a compelling reason and it can be done economically, there will be a significant incentive and other ways of ensuring that expansion can happen. He continued:

For instance, this pipeline doesn't necessarily have a hard line at 130 million cubic feet a day. ... There are several things that dictate pipeline capacity. One is the diameter; the other is the operating pressures. There are numerous ways to expand capacity; installing compression ... is a great one, changing the inlet-outlet pressure conditions.

So we're not necessarily talking about huge investments to lay a second piece of pipe down there. And, again, I believe under compelling reasons, undergirded by sound investment policies, that ...

expansion, at least of the capacity, ... is something that RCA has the ability ... to approve.

Number 1919

REPRESENTATIVE McGUIRE again suggested the need to ensure good staffing and well-trained people for RCA. Offering that RCA also has the ability to make decisions regarding modification, she asked whether it is correct that if a person isn't sure how big a discovery is or whether it warrants a firm commitment, that person could get an interruptible contract and then later go through RCA to change it to a firm contract.

MR. SCHOFFMANN affirmed that. He said the selection of the type of service one wants will be available for people throughout the life of the pipeline, although there might be a question of how much firm capacity remains 10 years from now; at that point, there might be a capacity restriction, and until the pipeline could be expanded, if that is justifiable, there might not be as much firm service as desired at that point. He added, "However, they still can select firm service contracts or interruptible contracts; those ... will be designed to be fair to all parties."

Number 1838

REPRESENTATIVE McGUIRE, referring back to concerns mentioned by Representative Crawford, explained that the notion of producer-owned pipelines creates discomfort sometimes for legislators whose charge is to uphold the constitution and ensure maximum yield from [the state's] resources. She cautioned against setting up a network across Alaska of producer-owned pipelines for which the firm offers are already in the bag for capacity by the same producers, such that no independent companies have an opportunity to get a fair shake and be part of the competitive marketplace. She emphasized the need to remember that principle, and mentioned jobs and so forth.

MR. SCHOFFMANN responded that a pipeline affiliate that found more gas five years later, for example, would be in exactly the same situation as others discovering gas then, and couldn't displace people from the line who were there before. He suggested it is nondiscriminatory in that sense, and that [the bill] just gives RCA the tool to make its own rulings to ensure that the two-tiered system - firm and interruptible, rather than the current common carriage - is fair and equitable.

CHAIR KOHRING invited Mr. Harbour to comment.

Number 1637

DAVE HARBOUR, Commissioner, Chair, Regulatory Commission of Alaska (RCA), told members Mr. Strandberg, RCA commissioner, was more capable of addressing technical aspects. He offered the following, however:

We appreciate the wisdom and the handicraft of the people who are proposing ... this statute. I believe that everything that has been stated so far has been technically on point and very well done. The legislature should realize, in making decisions like this, where it may be going. Representative McGuire made some good points about where the legislature may be going, as did Representative Crawford.

This is neither right nor wrong. It's just a decision. In the Lower 48, as distinguished from Alaska, there is a great deal of contract carriage in gas pipelines. Those gas pipelines are connected to enormous grids, providing the opportunity for massive competition. Those pipelines are typically owned by gas pipeline companies, not by producers. The gas pipeline company incentive is to maintain as complete capacity for the best price that they can - that's the business - and to expand, to loop, wherever possible to increase business.

Number 1543

MR. HARBOUR continued:

In Alaska, we're not connected to that grid. ... I appreciate the candor of the witnesses when they address the affiliated-interest issue, because it is a consideration. It is in the far realm of possibility that a company could own reserves and could own a ... gas pipeline and could have contract carriage and could obtain reserve capacity on that pipeline, bought and paid for by an affiliate of the company that owns the pipeline, when in fact the gas was not ready to move in the pipeline and other volumes from a competing company perhaps were.

That having been said, I hear the legislature, through its questions, appreciate the fact that he who makes the investment has certain rights and is taking a certain amount of ... initiative, and that that spurs additional investment by those companies. That's right too.

In short, ... I haven't heard anything today, myself, that seems right nor wrong. I have heard things that suggest that the legislature makes a decision that's greater simply than supporting the construction of one pipeline.

Number 1438

REPRESENTATIVE McGUIRE reported that in her discussions that day with Marathon Oil Company, her questions with regard to RCA were asked for one purpose: to understand how contract negotiations occur and how so-called openers are dealt with - changes in discoveries of fields or capacity, and how a company would get in or out of a particular pipeline. But she said she also wanted to understand RCA's role in the area of consumer protection. She offered that there is a high degree of merit in saying Marathon Oil Company and Unocal took the initiative and risk, and that Alaskans should support that investment in the state. However, she emphasized the importance, when looking at infrastructure development, to provide an opportunity for competition. She asked:

Do you believe that RCA, through its rule-making power in [AS] 42.06, has the ability to effectively advocate for consumer rights ... in that way, to be able to force expansion of pipelines, when it's clear that a case that you just mentioned is present, where you can see that there are independents who are trying to get in the line; they have ... proven gas; they want to get in there. ... Do you feel that you have the tools right now, through regulating interruptible and firm contracts and being able to exchange between the two, and - as the testimony indicated - potentially force the expansion of a pipeline? Are those adequate tools? Do they work?

MR. HARBOUR answered that these are important and perceptive questions. The RCA has the capability, through contract or common carriage, to assure the consumers of just and reasonable

treatment, he said, but deferred to Mr. Strandberg, who was on teleconference, to answer more fully.

Number 1238

JIM STRANDBERG, Commissioner, Regulatory Commission of Alaska, told members he believes the proposal by Mr. Schoffmann is a "mainline proposal." He concurred that this is commonly applied in the Lower 48. He said Alaska's statute was well put together to protect the rights of both ratepayers and shippers under the common-carrier rules, and that he believes the current statute does that very well for a common-carrier pipeline. He continued:

What we will need to work together on, I believe, to carry something like this forward, would be to make sure that the statute is modified so that those same protections continue. In short, ... under the current statute, yes, we have adequate powers for consumer protection. ... Consumer protection in pipelines is considerably different, often, than under our regulation of public utilities such as electric utilities, where we have many, many ... residential customers. Under the Pipeline Act, typically, we have shippers and producers. ... Especially for a circumstance such as the Kenai pipeline, we will have shippers that ... we have to protect their rights on, but in protecting those rights, that also must extend to the individual ratepayers who might be using that gas.

Number 1102

REPRESENTATIVE ROKEBERG expressed concern about why the 2000 legislature specifically added this for the North Slope. He asked Mr. Strandberg to address the regulatory theory behind the existing common-carrier law, whether interruptible service was allowed previously under RCA's jurisdiction, and whether he sees negative impacts from this bill to existing pipelines.

MR. STRANDBERG answered:

The Pipeline Act was passed in 1972. And during that time ... the legislature, I believe, wished to establish a policy of equal and unfettered access to oil and gas pipelines. And the common-carrier concepts at that time ... were widely employed, and

indeed they ... have worked quite well. The principal concept, of course, under common carriers is that a pipeline must take oil and gas from all shippers equally. And we have the ability to allocate the capacity of the pipeline to stop any discrimination. We can also, of course, order the pipeline to be larger.

I believe those basic concepts ... still apply. And the stranded gas pipeline Act, ... I have not looked at that for several months. ... But I will state that a lot of that was built ... to really harmonize our statute with ... federal statutes that would improve the chances of actually getting the project through, and also to ... protect the rights of in-state ratepayers. There was a massive amount of negotiations that went on ... under that stranded Act - again, that was two and a half years ago. Is that getting at your question, sir?

Number 0864

REPRESENTATIVE ROKEBERG said it did in part, but asked what the economic impact to existing common carriers would be from this legislation. He also asked whether [RCA] currently allows interruptible service to the common carriers.

MR. STRANDBERG replied:

Currently, we have two gas pipelines, which are regulated under [AS] 42.05; ... these pipelines are really regarded as public utilities. We don't have ... any gas pipelines that we ... currently regulate under this statute. And there are a couple of reasons for that; I'd be happy to go into that. But under ... [AS] 42.05, treating these pipelines as utilities gives us a lot of flexibility to make sure that all ratepayers are served. ...

And so when we look at this particular bill language, ... this would really be a fundamental change, and it may well ... see a different brand of regulation that we really haven't done in this state for a gas pipeline yet. ...

The devil will be in the detail here. I believe that ... certainly we can create a statutory change that

would allow effective contract carriage. But there are a number ... of interrelationships between ... the common-carrier language that are currently in this statute and contract-carriage language that is included in the current changes, which we would have to work out to make sure that the RCA maintains its powers, its jurisdiction ... to really fully regulate the pipeline.

Number 0653

REPRESENTATIVE ROKEBERG asked Mr. Strandberg to identify the two carriers it regulates now and explain why the other lines aren't regulated.

MR. STRANDBERG responded that they are Beluga Pipe Line Company and Alaska Pipeline Company; the latter conveys gas from a number of fields through two lines up either side of [Cook] Inlet, basically in a loop, using a 20-inch line, to his belief, that goes up the north side of the inlet. He said this is tied in not only with the ENSTAR [Natural Gas Company] residential customers on the Kenai Peninsula, in the Matanuska-Susitna area, and in Anchorage, but also with the Beluga power plant. Therefore, the pipelines that [RCA] regulates under [AS] 42.05 are basically in the Cook Inlet basin, stretching on both sides of the inlet.

Number 0533

REPRESENTATIVE ROKEBERG alluded to Mr. Schoffmann's testimony and a Kenai gas hub with a [KKPL] line running north. He asked whether that is a regulated line.

MR. STRANDBERG answered that basically the KKPL project hub, to his belief, is somewhere near Kalifonsky Beach or in the Soldotna area and goes south from there. He said it is designed to interconnect with the existing "Alaska Pipeline network."

REPRESENTATIVE ROKEBERG asked whether passage of this bill to allow interruptible transportation services would have any impact on the Alaska Pipeline Company with regard to RCA's jurisdiction.

MR. STRANDBERG replied, "As currently written, I do not believe so, because there is no retroactive conversion of regulation included in the current language. Unless you put that in there, it would not apply ... to these other pipelines."

Number 0428

REPRESENTATIVE ROKEBERG offered his understanding that if the legislature enacted a change that affected RCA's ability to regulate, there would need to be a retroactive clause in order to affect previous contracts or dockets and decisions by RCA.

MR. STRANDBERG answered, "That's correct. It would be important ... in any statute change to really define the breakpoint and whether this only applies to new pipelines."

REPRESENTATIVE ROKEBERG suggested that the bill's sponsor check into it.

MR. STRANDBERG added:

These other pipeline companies hold their own certificates, and indeed they are certificated as public utilities. So unless you reached in through your statute and threw them back here to say, "Well, you have the option," ... they would stay put where they're at.

REPRESENTATIVE ROKEBERG again requested that the sponsor look into it to ensure that is the case legally. He added that if so, this shouldn't affect existing lines, only future lines, "and therefore they would know what they are getting into." Suggesting that is consistent with practice in the Lower 48, he acknowledged the deregulated gas market there.

Number 0233

REPRESENTATIVE CRAWFORD asked whether there would be an advantage to being regulated as a utility, rather than a transportation pipeline. He also inquired about the reason for treating the two differently.

MR. STRANDBERG opined that it is generally beneficial to the ratepayer when a gas pipeline company "comes in under [AS] 42.05." He said there are other ramifications, such as whether or not a pipeline company would come under PUHCA - the Public Utility Holding Company Act [of 1935] - conditions; that relates to "the vertical integration of the company," he added. He continued:

Under the current statute, I believe that ... a gas pipeline company with specific delivery requirements on a long term ... would look at our common-carrier requirements. And ... if the pipeline were to get completely filled, under that statute we would really be obligated ... to require that pipeline company to put that additional customer on, and then everybody's pro-rata share of the capacity would be reduced. Now, we don't have that situation here, with a full pipeline. But I believe those sorts of considerations certainly pipeline companies look at these days, and especially if you have a gas pipeline where you have specific demands that you have to fulfill over the long term. Those are ... of concern.

Number 0016

CHAIR KOHRING asked whether anyone else wished to testify. [He closed public testimony.]

TAPE 03-17, SIDE A

Number 0030

REPRESENTATIVE ROKEBERG asked Mr. Schoffmann to comment on the questions just discussed. He offered his belief that the only concern is whether there would be any negative impact from the bill to existing lines or access to lines.

MR. SCHOFFMANN responded:

My understanding of what Mr. Strandberg said was exactly true. ... These other lines have a certificate that is under a different statute. Unless they ... had the freedom to refile and again go through RCA for a different statutes, I don't see how that would affect existing lines ... in their status. ...

I believe, personally, that one of the reasons we're seeing Alaska have a lot of producer-affiliate lines being installed is exactly ... the inability ... of an independent investor to come in and line up business in advance. ... It's very difficult ... for people who don't have ... a vested interest elsewhere in the state to make these type of investments. So I think this type of legislation is exactly why we're seeing primarily producer affiliates step forward to make pipeline proposals, as opposed to independent

investors. So, with that clarification, I think that that kind of speaks to, potentially, another reason to see some legislation of this type go through.

Number 0186

REPRESENTATIVE McGUIRE offered her understanding from Mr. Strandberg's testimony that he believes there may need to be statutory modifications to incorporate consumer rights similar to those granted under common-carrier status today, now that there will be contract-carrier status [if the bill passes]. She asked what those changes are, requesting that Mr. Strandberg provide them to the committee if he wasn't prepared to address them at this meeting.

MR. STRANDBERG agreed to respond in writing.

CHAIR KOHRING stated his desire for an immediate effective date.

Number 0343

REPRESENTATIVE McGUIRE moved to adopt an amendment to provide for an effective date. There being no objection, it was so ordered.

Number 0404

REPRESENTATIVE CRAWFORD expressed concern about whether this bill potentially could be used to impede pipeline access for nonaffiliated producers. He asked why DNR put the analysis in the fiscal note [text provided previously] if there wasn't a concern.

Number 0503

ANTONY SCOTT, Commercial Analyst, Division of Oil & Gas, Department of Natural Resources, answered that there are two possible ways contract carriage could be used to impede access. He offered his understanding that the open-season process - wherein a pipeline company solicits binding commitments for capacity on a pipeline - isn't actively regulated on the federal side, for example, by FERC, in the Lower 48. He added, "That goes to when open seasons occur; there are certain sort of baseline requirements of conduct in terms of posting notice ... and making sure that there's adequate notice and so on."

MR. SCOTT said he sees no provision in this bill that gives RCA authority to regulate the open-season process either. Thus he noted some concern about a North Slope gas pipeline: an open season could be timed to facilitate the sizing of a pipeline to meet producer-affiliate needs, and would not be particularly responsive to the needs of independent explorers. He continued:

While it is certainly true that the RCA has authority to order capacity expansion - and it would be awfully nice if, on the federal side, that authority existed, say, with regard to a North Slope pipeline - for smaller pipelines and basins, which would potentially involve much smaller quantities of gas for ... an independent explorer, the prospect of needing to first discover gas - you haven't discovered it yet - before you can then go to the RCA and try to get an order for capacity expansion, which would then subsequently allow you to market your gas, that ... delay there could, in some cases, be enough to prevent the explorer from ever making the exploration investment. And ... the RCA would never hear from an explorer who failed to get into the exploration business because of concerns that the payback on their project might not be favorable.

Number 0720

MR. SCOTT emphasized that, as Mr. Schoffmann said, permitting contract-carriage provisions could be useful for facilitating development of independent pipeline companies in the state. For nonaffiliated pipeline companies, he said, there's clearly no conflict; in fact, an independent pipeline company makes all its money by moving gas on a pipeline and attracting carriage to do so. He highlighted the possibility, however, that a producer-affiliated pipeline could have competing incentives to want to create barriers to entry, or at least might profit from barriers to entry that reserve potential exploration basins to itself.

Number 0831

REPRESENTATIVE McGUIRE requested confirmation that Mr. Scott's position is that RCA currently has no authority to regulate open-season requirements for a contract carrier.

MR. SCOTT said that is correct. Offering what he called a minor point, he conveyed his view that beyond giving RCA the tool to permit contract carriage, the language possibly gives a pipeline

company the right to offer contract-carriage service. He suggested there would be much less concern about potential problems with a producer-affiliated pipeline if it were within RCA's discretion whether or not to provide that. Mr. Scott emphasized that none of his comments go specifically to KKPL or imply anything nefarious; rather, this is a question of future policy and how this could affect the state's resources, since the state is a property owner in these gas resources.

Number 0997

REPRESENTATIVE ROKEBERG suggested the Division of Oil & Gas was looking for something that isn't there, since, to his belief, the bill doesn't speak to that. He suggested that if there is a defect regarding open seasons, additional legislation should be introduced. He offered his belief that RCA "can move." He asked, if neither FERC nor RCA regulates open seasons, how it can be commented on in the fiscal note.

Number 1047

REPRESENTATIVE ROKEBERG moved to report HB 204, as amended, out of committee with individual recommendations and the indeterminate fiscal note; he related his belief that it should be a zero fiscal note. There being no objection, CSHB 204(O&G) was reported from the House Special Committee on Oil and Gas.

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 5:08 p.m.