ALASKA STATE LEGISLATURE
SENATE SPECIAL COMMITTEE ON NATURAL GAS DEVELOPMENT
August 1, 2006
9:50 a.m.

MEMBERS PRESENT

Senator Ralph Seekins, Chair
Senator Gary Wilken
Senator Con Bunde
Senator Fred Dyson
Senator Bert Stedman
Senator Lyman Hoffman
Senator Donny Olson
Senator Thomas Wagoner
Senator Ben Stevens
Senator Kim Elton

MEMBERS ABSENT

Senator Lyda Green
Senator Albert Kookesh

OTHER LEGISLATORS PRESENT

Senator Gary Stevens
Senator Hollis French
Senator Charlie Huggins

COMMITTEE CALENDAR

SENATE BILL NO. 3001
"An Act relating to the production tax on oil and gas and to conservation surcharges on oil; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the production tax; amending the definition of 'gas' as that definition applies in the Alaska Stranded Gas Development Act; making conforming amendments; and providing for an effective date."
HEARD AND HELD

SENATE BILL NO. 3002
"An Act relating to the Alaska Stranded Gas Development Act; relating to municipal impact money received under the terms of a stranded gas fiscal contract; relating to determination of full and true value of property and required contributions for

education in municipalities affected by stranded gas fiscal contracts; and providing for an effective date."

HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: SB3001
SHORT TITLE: OIL/GAS PROD. TAX
SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

07/12/06	(S)	READ THE FIRST TIME - REFERRALS
07/12/06	(S)	NGD
07/13/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/13/06	(S)	Heard & Held
07/13/06	(S)	MINUTE(NGD)
07/14/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/14/06	(S)	Heard & Held
07/14/06	(S)	MINUTE(NGD)
07/24/06	(S)	NGD AT 1:30 PM SENATE FINANCE 532
07/24/06	(S)	Scheduled But Not Heard
07/25/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/25/06	(S)	Heard & Held
07/25/06	(S)	MINUTE(NGD)
07/26/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/26/06	(S)	Heard & Held
07/26/06	(S)	MINUTE(NGD)
07/27/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/27/06	(S)	Heard & Held
07/27/06	(S)	MINUTE(NGD)
07/28/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/28/06	(S)	Scheduled But Not Heard
07/31/06	(S)	NGD AT 1:30 PM SENATE FINANCE 532
07/31/06	(S)	Scheduled But Not Heard
08/01/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532

BILL: SB3002
SHORT TITLE: STRANDED GAS AMENDMENTS
SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

07/12/06	(S)	READ THE FIRST TIME - REFERRALS
07/12/06	(S)	NGD
07/13/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/13/06	(S)	Heard & Held
07/13/06	(S)	MINUTE(NGD)
07/14/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/14/06	(S)	Heard & Held
07/14/06	(S)	MINUTE(NGD)

07/24/06	(S)	NGD AT 1:30 PM SENATE FINANCE 532
07/24/06	(S)	Heard & Held
07/24/06	(S)	MINUTE(NGD)
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07/28/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
07/28/06	(S)	Heard & Held
07/28/06	(S)	MINUTE(NGD)
07/31/06	(S)	NGD AT 1:30 PM SENATE FINANCE 532
07/31/06	(S)	Heard & Held
07/31/06	(S)	MINUTE(NGD)
08/01/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532

WITNESS REGISTER

DAVID VAN TUYL, Commercial Manager
Alaska Gas Group
BP
Anchorage, AK
POSITION STATEMENT: Testified and answered questions during the hearing on SB 3001 and SB 3002.

WENDY KING, Director of External Strategies
ANS Gas Development Team
ConocoPhillips Alaska, Inc.
PO Box 100360
Anchorage, AK 99510
POSITION STATEMENT: Testified and answered questions during the hearing on SB 3001 and SB 3002.

BOB LOEFFLER
Morrison & Foerster LLP
Counsel to the Governor
Office of the Governor
PO Box 110001
Juneau, AK 99811-0001
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

JOE MARUSHACK, VP Gas Development

ConocoPhillips
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

MARK NELSON, Commercial Negotiator
ExxonMobil
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

BRADFORD G. KEITHLEY
Jones Day
Counsel to BP
Dallas, TX
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

JOSEPH K. DONOHUE
Preston Gates & Ellis
Counsel to the Governor
Office of the Governor
PO Box 110001
Juneau, AK 99811-0001
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

GREG O'CLARAY, Commissioner
Department of Labor & Workforce
Development
PO Box 21149
Juneau, AK 99802-1149
POSITION STATEMENT: Testified on Amendment 4 to SB 3002 during the hearing on SB 3001 and SB 3002.

JIM CLARK, Chief Negotiator
Office of the Governor
PO Box 110001
Juneau, AK 99811-0001
POSITION STATEMENT: Answered questions during the hearing on SB 3001 and SB 3002.

ACTION NARRATIVE

CHAIR RALPH SEEKINS called the Senate Special Committee on Natural Gas Development meeting to order at 9:50:47 AM. Present at the call to order were Senators Bert Stedman, Con Bunde, Fred Dyson, Gary Wilken, Kim Elton, Lyman Hoffman, Thomas Wagoner and Chair Ralph Seekins; Senator Donald Olson arrived soon

thereafter, and Senator Ben Stevens arrived as the meeting was in progress. Also in attendance were Senators Gary Stevens, Hollis French and Charlie Huggins.

SB 3001-OIL/GAS PROD. TAX
SB 3002-STRANDED GAS AMENDMENTS

CHAIR SEEKINS opened the hearing on SB 3001 and SB 3002. The version of SB 3002 before the committee was Version G, adopted as a work draft and amended on 7/28/06. He invited testifiers from BP, ConocoPhillips and ExxonMobil to address the committee.

9:51:21 AM
DAVID VAN TUYL, Commercial Manager, Alaska Gas Group, BP, noted he would give BP's perspective on issues raised yesterday. With respect to concern heard from Mr. Shepler and Mr. Harper about access to the pipeline, he clarified that no party - even a pipeline owner like BP - is guaranteed access. It is open access under the Federal Energy Regulatory Commission (FERC), which governs provisions for accessing space on the line.

He emphasized the importance of not taking actions that jeopardize building the pipeline in the first place. Only after it is built are things like expansion possible. Mr. Van Tuyl said BP wants to own the pipeline to manage costs; believes it can take on the associated risks; has the necessary experience; and wants a pipeline built to be able to monetize its gas resource. He cautioned that providing certain stipulations and limitations upfront with respect to terms relating to expansion and access could endanger building the base line.

He highlighted the example of rolled-in pricing. Mr. Van Tuyl explained that mandating rolled-in pricing for every expansion could penalize those who build the project to start with, who have a certain cost for their capacity, established in the open season and approved by FERC. If an expansion results in an increased rate and if rolled-in rates are mandated without a rebuttable presumption, the base shipper's rates could rise, but not because of anything that shipper had done.

He also cautioned against stipulating specific design issues in the contract, which BP believes would circumvent the whole open season process. Surmising BP has done more design work than the others, having spent over $100 million, Mr. Van Tuyl predicted spending perhaps $1 billion before even getting to the point of project sanction. In preparing for the open season, BP will

spend at least another $100 million for engineering and so forth.

MR. VAN TUYL emphasized the importance, with respect to the open season, of ensuring the pipeline system is designed right. For the FERC preapplication process, BP will do the engineering beforehand; it will be involved in the process and will consult with potential shippers - doing its best to get the design right beforehand so the service it offers is response to potential shippers.

He characterized the open season as the day of reckoning, when folks actually sign up for the service. There could be significantly more demand than designed for, or less. Only then does the company actually get that design right. If the ability to make changes has been preempted by a specific design, it doesn't allow learning as this proceeds. It could well result in a suboptimal system - a lesson Mr. Van Tuyl suggested may have been learned from the Alaska Natural Gas Transportation System (ANGTS) in the 1970s, when highly specific detail was included in the legislation, down to the actual vendor required for the turbine drivers. Mr. Van Tuyl remarked, "That's not the approach that we would recommend for this project."

9:57:43 AM
MR. VAN TUYL recalled discussion of the nature of expansions, how it seems logical that if the base amount is about 4.5 billion a day and it is expanded to 5.5 or 6, the rate for everybody should come down because of economies of scale. He said that's not necessarily the case. Rather, an efficient expansion would result in an equivalent cost or perhaps a slight increase for shippers, but hopefully wouldn't result in a big difference from the base rate.

He highlighted a tool used by engineers to design pipeline systems: a J-curve where one axis plots the cost per unit volume and the other might plot the capacity of the system. The ideal is as much capacity as possible for the least cost. There is a range over which the cost doesn't vary much. Mr. Van Tuyl said that is the goal with this project: a pretty good base rate, 4.5 a day. It's fairly flat at the bottom of the J-curve, and it might be expandable by a 1 or 1.5 a day without a significant increase in the cost of service.

He referred to a question raised by Senator Dyson and alluded to the proposed fiscal contract, noting it has a reference in Article 8.7 to 100-mile increments. Mr. Van Tuyl said it seems

an arbitrary number, but explained that it envisions a situation in which a compressor becomes bottlenecked and thus there might be a need to loop around it. The compressor spacing for the base design is about 100 miles or slightly more. It wouldn't mandate looping of the entire system, Mr. Van Tuyl noted.

10:01:05 AM
SENATOR DYSON asked whether the existing language prevents an expansion of more than 100 miles.

MR. VAN TUYL answered no. There are multiple avenues, some unique, that any shipper seeking an expansion can use for this project. The most prevalent is the voluntary process whereby a would-be shipper approaches the pipeline and seeks an expansion. In the Lower 58, the vast majority of pipelines are commercially motivated to increase volumes and thus to expand. One unique avenue is the Alaska Natural Gas Pipeline Act (ANGPA) of 2004: If the pipeline refused to expand, a shipper could go to FERC and, under Section 105 of ANGPA, to his recollection, could assert its rights to have a mandatory expansion imposed. He mentioned a further option, a mechanism in the contract.

SENATOR DYSON said he still didn't understand why the 100-mile limit is needed, either from an engineering or business perspective. He suggested there must be either something regulatory or protecting someone's interests.

10:04:00 AM
WENDY KING, Director of External Strategies, ANS Gas Development Team, ConocoPhillips Alaska, Inc., replied that the belief was that if somebody found that much gas and wanted to do a full line loop, the vehicle would be an economic voluntary expansion. The person would go to the pipeline and wouldn't rely on Article 8.7, the state-initiated expansion, for a full line loop of the system.

SENATOR DYSON surmised the 100-mile limit only applies to state-initiated expansions.

MR. VAN TUYL affirmed that.

SENATOR DYSON asked whether the state only has authority to work around a bottleneck at a particular place in the line, not for full line capacity.

MR. VAN TUYL explained that he'd mentioned the other two avenues because they would be available to the expander regardless. As

Ms. King had pointed out, a full line loop would more likely be covered by either of those. So it wouldn't foreclose full line looping.

SENATOR DYSON agreed, but suggested it precludes a state-initiated full line loop, a major expansion of capacity. If the other options don't work, the state cannot initiate a large-capacity expansion that requires looping or parallel lines.

MR. VAN TUYL replied that he cannot foresee a situation in which those other processes wouldn't work, given FERC's ability to impose an expansion - an unprecedented right that FERC wouldn't have absent the provisions in ANGPA.

10:06:00 AM
SENATOR DYSON recalled testimony yesterday that a provision says if FERC's decision isn't almost exactly what the unit operator or pipeline operator wants, the pipeline operator must reject it and not go along with FERC.

MR. VAN TUYL clarified that is only for a state-initiated expansion under Article 8.7.

CHAIR SEEKINS asked: If full line looping is inevitable, why retain, in the contract terms, that 100-mile restriction for state-initiated expansion through looping?

MS. KING answered that for a full line loop, the thought was that if somebody has found significant enough volume to have to "twin" a huge pipeline, the first vehicle likely would be a voluntary expansion: approaching the pipeline and asking whether the pipeline is prepared to expand under terms provided. If that potential shipper isn't satisfied, then Section 105, the mandatory expansion, is seen by ConocoPhillips as the primary vehicle at that point - with the FERC process - to use for that type of project.

She recalled discussion of Article 8.7 with the state. Inviting Mr. Loeffler to speak as well, Ms. King reported the predominant focus was this: What if the state wants to do an expansion for in-state needs? She emphasized concern about what happens if someone tries to force an uneconomic expansion. She gave an example in which someone had attempted a voluntary expansion, but the pipeline didn't see it as an economic benefit; there was dissatisfaction with the mandatory FERC expansion; and now there is the option of state-initiated expansion. Ms. King suggested

the aforementioned could be an expansion in trouble, with economic challenges.

She also recalled that the state had argued hard for an additional dispute resolution process, going to a tribunal with the question of whether the party had a full hearing. Noting the predominant focus for Article 8.7 relates to smaller expansions, Ms. King said the existing processes are there to help facilitate larger-type expansions.

10:09:09 AM
BOB LOEFFLER, Morrison & Foerster LLP, Counsel to the Governor, concurred with Ms. King's recollection. He said Article 8.7 was an effort to create a fairly circumscribed tool to deal with smaller expansions appropriate for in-state use. It received an inordinate amount of attention, and is being looked at from all directions. He reported there are two sets of comments in favor of Article 8.7. Mr. Loeffler added that if it creates more problems than it solves - despite its good intentions - that will be taken into consideration.

SENATOR DYSON highlighted the term "noneconomic" and said nobody wants to see a deal-killer. However, the legislature acts as a board of directors for Alaskans, whose interests might not coincide with the producers' economic interests. If in-state use, including gas liquids and value-added applications, requires expansion that causes a slight increase in the cost to all shippers, the producers could argue it isn't economic. It would cost more, and they'd lose a little from the bottom line.

He noted, however, the people's interests aren't just economic; Senator Dyson cited the cost and security of energy. He said it appears the state doesn't have the option of considering a public good that costs the state and the producers a little. Senator Dyson acknowledged the natural tension of such deals, expressing concern that this has been blocked out.

10:12:27 AM
MR. VAN TUYL suggested the reason BP would refer to something as a noneconomic or a suboptimal expansion is because a pipeline is naturally motivated commercially to do anything that is optimal or economically viable; those things will happen if nature is allowed to run its course. A pipeline could say it didn't want to do an expansion; that was recognized by FERC because of efforts by the state and others to make the points Senator Dyson was making about other potential needs that this particular pipeline would have to serve.

He said that is why the provisions in Section 105 of ANGPA exist. If the pipeline says no, the potential expander can request that FERC mandate expansion. Mr. Van Tuyl added that if the expander doesn't wish to use that process and has already gone through the voluntary process, there is a third tool, within the contract; as Ms. King and Mr. Loeffler said, it focuses on smaller expansions, which might tend to be more marginal. But it doesn't preclude the other avenues available to an expander, either under the voluntary process or under FERC-mandated expansion.

10:14:22 AM
MS. KING noted she was reading from FERC Order 2005-A and said the following:

> In adopting the presumption for rolled-in rate treatment, the commission balanced rate predictability for initial shippers with the objective of reducing barriers to future exploration, development and production of Alaska natural gas.
>
> Finally, to provide guidance to interested parties on the important subject of expansion rate treatment, the Final Rule establishes a presumption in favor of rolled-in pricing for expansions up to the point that it would cause there to be a subsidy of expansion shippers by initial shippers. We will determine whether a particular rate amounts to a subsidy when the issue is presented to us.

She summarized that FERC, in its order, acknowledged it would need to be addressed on a specific case when it was brought to FERC at that point. Noting FERC policy has been evolving on this issue, Ms. King asked that Mr. Keithley or Mr. Loeffler, as FERC experts, correct her if necessary.

She then explained that in 1995, FERC policy for Lower 48 pipelines was that if the expansion cost resulted in less than a 5 percent increase, it would be rolled in. In 1999, FERC changed that policy to say it would be incrementally priced. Furthermore, Ms. King told members, FERC established unique rules for the Alaska pipeline with the rebuttable presumption of rolled-in rates.

She posed a scenario in which a Fairbanks utility company pays $1.00 for shipping from the North Slope, with a total toll of

$3.00 to Alberta. Later someone wants an expansion. Suddenly, the Fairbanks utility is told its rate will rise to $1.50. Ms. King suggested the utility company would want to ask why, since there was a firm shipping commitment and an agreement that it would cost $1.00.

She surmised the pipeline and each shipper would want to look at such examples and ask why their rates had risen; FERC has already said it will look at these on a case-by-case basis and adjudicate whether or not that is a subsidy. Ms. King pointed out that this possibility of increased rates applies not only to the big producers, but also to any shipper with a firm transportation (FT) commitment. After giving another example, she said the contract has provisions so a party can protest a situation and initiate a proceeding with FERC. Ms. King concluded by highlighting the challenges in trying to describe a one-size-fits-all solution right now for this pipeline.

SENATOR DYSON indicated he didn't want to pursue this further, but was unconvinced as to why the 100-mile limit is needed. He remarked that nobody who wants to loop around a compressor station is going to build a line around it that is any bigger than necessary.

10:19:15 AM
SENATOR BUNDE requested confirmation that a rolled-in rate would be passed along to the customer, whereas an incremental rate would put one group at a competitive disadvantage because it would sell its gas at a higher price.

MR. VAN TUYL emphasized that the customers are the shippers, including the state. If the rolled-in basis resulted in a higher rate and it was passed on, the customers paying the additional cost would be BP, ExxonMobil, ConocoPhillips, the State of Alaska and other shippers who'd signed up for service on the line.

He added that the focus is on delivering the lowest-cost system possible, entering into long-term commitments of perhaps 20 or 30 years. The duration of the initial FT commitments isn't known, although the federal loan guarantees will be available for 30 years from commencement of commercial operations. With that size of an obligation for that length of time, a rate increase could significantly color the economics. A company makes choices based on an assumption of a certain price in year one, Mr. Van Tuyl said, but a later change creates significant risk relating to the project.

SENATOR BUNDE asked: Can't the producers pass on the cost of that increase to a utility in Chicago, for example?

MR. VAN TUYL answered that the "back end of the line" is the market. The companies cannot stipulate that costs for Alaska gas will be higher. They'll get the market rate for the gas, whether it is sold to a utility or another consumer. There is the market on one end, and the transportation cost in the middle, which is the cost they're trying to manage to ensure the highest possible netback at the front end.

10:22:53 AM
SENATOR ELTON recalled characterization of Article 8.7 of the contract as a sort of safety valve: if the other two expansion methods don't work, there could be state-initiated expansion. However, his interpretation of this morning's discussion is that there is more discrete reason for Article 8.7 - potential bottlenecks on part of the pipeline. He asked: If significant gas is found at Minto Flats, for example, and the other two expansion alternatives don't work, doesn't the 100-mile restriction for state-initiated expansion preclude using this as an alternative?

MS. KING replied for a future gas discovery at Minto Flats, for example, the gas owners likely would go to the pipeline for voluntary expansion from that point south. Before voluntary expansion, however, FERC requires a "reverse auction": the pipeline must ask its existing shippers whether there is capacity that someone is willing to give up. If adequate capacity is released, expansion isn't needed.

SENATOR ELTON posed a scenario in which someone doesn't want to give up its capacity, even though it isn't needed.

MS. KING questioned the economics of sitting on expensive capacity without a plan to fill it, a risky prospect. Returning to a situation involving full capacity, with nothing coming of the reverse auction, she opined that voluntary expansion would be the pipeline's first course of action to pursue; if a creditworthy party was willing to sign a shipping commitment, there'd be a normal FERC process for it. If that didn't work out, however, the federal Section 105 mandatory expansion could be applied. As for state-initiated expansion, if it involved a full line loop - which requires finding a significant quantify of gas - there'd be a limitation from that point south. She

suggested that risk would have to be looked at from an exploration perspective.

10:27:10 AM
MR. LOEFFLER offered clarification about the timing. He gave his understanding that the first step is voluntary expansion; the second is expansion under Article 8.7; and the third is mandatory expansion. He indicated it would be logical, if someone qualified, to try expansion under Article 8.7 after voluntary expansion, because it is designed to be a little quicker - although it may or may not work out that way.

SENATOR ELTON said he had some of the same reservations expressed by Senator Dyson. Even though it takes significant gas before line looping occurs, it is the whole issue of so-called basin control that the committee spent time on. Nobody anticipates that one find will suddenly fill the line for the cheap capacity; it is assumed this will be incremental. If North Slope gas is added incrementally, at some point explorers in the Nenana Basin or Minto Flats cannot do it; Senator Elton surmised Article 8.7 precludes alternatives with the 100-miles restriction. Recalling Mr. Van Tuyl's testimony that he cannot imagine getting to that point - given the other alternatives - Senator Elton questioned why the 100-mile limit exists.

10:29:18 AM
MR. VAN TUYL mentioned the idea of a viable expansion alternative in the commercial interest of a pipeline that is turned down for some reason. He recalled that Mr. Harper and Mr. Shepler had suggested yesterday that a pipeline might not expand specifically because it didn't benefit its producer affiliate; Mr. Van Tuyl said that smacks of violation of the affiliate rules which FERC adjudicates or other enforcement provisions under federal law. Entities will be commercially motivated to do what is in their best interest; a commercially viable expansion is something people will want to do, even if they decide not to for some reason, such as determining it isn't commercially viable. Even without Article 8.7, Mr. Van Tuyl said, that shipper would have access through ANGPA to seek a FERC mandatory expansion.

He recalled discussion a couple of weeks ago about challenges in structuring Article 8.7. Mr. Van Tuyl reported that BP had been concerned about not wanting to tell FERC how to do its business, which provisions of Article 8.7 seem to approach. Noting it is FERC's job to provide enforcement regulations for pipelines over which it has jurisdiction, Mr. Van Tuyl added, "Frankly, we

think FERC does a good job. They don't always rule in our favor when there's rate cases and whatnot. All of the provisions of Order 2004 and 2005 weren't necessarily the ones we would have preferred. But we think FERC works."

He highlighted a theme in testimony and documents from Mr. Shepler and Mr. Harper, which he interpreted to assert FERC cannot be trusted to do its job. Mr. Van Tuyl told members, "We disagree with that. We think FERC needs to be trusted to do its job." Agreeing with Ms. King that FERC policies have changed through time and as they relate to this project, Mr. Van Tuyl concluded by suggesting that process needs to be allowed to continue; he surmised FERC policy may change again over the duration of this contract.

10:32:06 AM
SENATOR WILKEN offered a different view: If the state and the producers say in a joint letter that they prefer rolled-in pricing for economic expansions, it isn't telling FERC what to do. Rather, it suggests preferences, which might help FERC do its job under this new provision in Section 105 for mandatory expansion, since there is no history of cases or decisions.

MR. VAN TUYL replied that the specific example of stipulating a preference for rolled-in pricing is a concern for BP because it is case-dependent. If rolled-in pricing results in the example given by Ms. King - with a long-term shipping contract made with one understanding, and then a sudden increase in BP's rate by 50 percent - that might not be the best outcome. Thus it might not be something BP wants to commit to at the outset. If the FERC process is allowed to occur, there will be hearings and so forth, and the process will result in an outcome; it might not be the outcome BP prefers, but there is already an avenue in place to allow people to be heard. "We know that the state's voice is an influential voice before the FERC," he added, citing recent legislation that was passed as a case in point.

SENATOR WILKEN responded that he was looking for the downside for the four parties expressing interest in rolled-in pricing; he called this a "class A problem with this contract." He voiced concern that if the groundwork isn't laid today for economic expansion of this pipeline, it will result in what exists today with respect to oil; saying one reason there isn't more exploration on the North Slope is because explorers cannot get into the pipeline, Senator Wilken gave two examples.

He also expressed concern about the producers having control of the pipeline, with the pipeline either inaccessible or too expensive. One hurdle seems to be incremental versus rolled-in pricing. Senator Wilken suggested for an explorer there'll be a double gamble: 1) whether gas will be struck and 2) whether it will get into the pipeline, even with the option of FERC-mandated expansion, which is new, takes time and money and has no track record.

10:37:38 AM
MR. LOEFFLER opined that the aforementioned Trans-Alaska Pipeline System (TAPS) example doesn't comport with reality, since TAPS is half empty, has plenty of capacity and takes bids every month. If the explorers have a problem, it must relate to something upstream. He suggested the need for more information in this regard.

SENATOR WILKEN thanked Mr. Loeffler, acknowledging he might not have all the details.

SENATOR DYSON announced he did have.

CHAIR SEEKINS first called upon Mr. Marushack.

10:38:36 AM
JOE MARUSHACK, VP Gas Development, ConocoPhillips, said he would offer the perspective of an explorer drilling wells in Alaska. Noting he could argue both sides but would explain why his company lands where it does, Mr. Marushack said an explorer needs access to the pipe; having ownership in the pipe doesn't guarantee any more influence than anyone else, as a producer. It is known that this pipe will be developed with expansion capabilities.

He referred to the J-curve described by Mr. Van Tuyl, reminding members that it shows the points at which theoretically it is most economic. Mr. Marushack emphasized the size of this project, with a base case of 4 billion cubic feet (Bcf) a day; perhaps a 48-inch or 52-inch pipe; and expansion capability to about 5.5 Bcf. The rate should be about the same for the extra 1.5 Bcf a day. However, 1 Bcf a day will require finding 8 to 10 trillion cubic feet (Tcf) of gas.

He posed a scenario in which an explorer makes a major discovery, 2 or 3 Tcf, and with its partners figures they can afford a 300-million-a-day expansion. They approach the pipeline, which says this is way off the J-curve and will

require doubling all compressors and so forth, as if it were a 1-Bcf-a-day expansion. It will cost a certain amount. Thus on an incremental basis, instead of the $3 per million everybody else might pay, it might cost $5 per million. Mr. Marushack said the question is whether it is fair to go to the other companies - those that made the base shipping requirement and made this project happen - and roll in all those costs.

He suggested the following ought to happen for volumes so huge: If the explorer is willing to pay $5 a million because gas prices are $10, then it pays the incremental cost. If not, it needs to work with others to find the 8 trillion required to get that incremental expansion, although it takes a little longer. While it would be great to have incremental costs rolled in and another company pay for it, Mr. Marushack emphasized he doesn't believe it's fair. Instead, the explorer should go to the pipeline, which would do its work and declare the cost; FERC would weigh in on whether it makes sense; and then the explorer might have to wait for other exploration successes in order to have an economic expansion.

10:42:22 AM
MARK NELSON, Commercial Negotiator, ExxonMobil, added that part of fiscal certainty is certainty about future rates. He told members, "All we're asking you to do is not mandate rolled-in rates in a contract, but allow FERC to do their job." He indicated when FERC develops its mandatory procedures, it recognizes the fairness issue: the rates don't require existing shippers to subsidize expansion shippers, which can adversely impact the economic viability of the project. Noting this is a risky project, he said those who'll underpin the project just want some certainty. Mr. Nelson closed by relating his belief that there is a fair FERC process, with unprecedented procedures built in, to allow that to happen.

SENATOR WILKEN responded, "We're not going to mandate anything." Recalling that the FERC order stated a preference for rolled-in pricing, he said it seems the four parties can align themselves with FERC and say they also prefer that, buttressing the FERC decision. Senator Wilken predicted FERC would probably say no for a 50 percent increase; for a 5 percent increase, however, FERC may look to the record, determine it aligns with its own goals and approve rolled-in pricing. He emphasized the desire to address it, to the fullest extent possible, in the proposed fiscal contract. Senator Wilken specified that he remains concerned about this particular contract provision.

10:44:31 AM
SENATOR DYSON referred to the oil-production bottleneck mentioned earlier by Senator Wilken. He recalled that a new producer had oil that needed to go through another producer's gathering center, which had limited capacity to handle water.

MR. LOEFFLER said that would make more sense.

SENATOR DYSON elaborated, recalling that the second company was unwilling to spend more money to produce more water for somebody that hadn't put money into building the plant and so forth. He surmised the new producer had been asked to pay for the cost of handling the increase, as a fairness issue. He predicted similar situations would arise with respect to gas when non-owners want to put gas into the line.

CHAIR SEEKINS continued with the fairness issue, saying he starts to have a problem with a requirement of subsidizing someone else in getting gas to market.

SENATOR BUNDE pointed out that Chair Seekins works in a subsidized business, since his transportation costs from Detroit are no more than for someone who lives in Minneapolis.

CHAIR SEEKINS agreed, calling it is rolled-in pricing and saying there is an economic reason related to Ford Motor Company, not the dealers. Returning to the gas pipeline, he raised the question of the length of time for which the ability to come into the market is preserved, and on what basis. Chair Seekins said it is a difficult issue and he doesn't know the answer.

10:47:54 AM
SENATOR WAGONER asked: What happens if 5 percent of the capacity is left over after the open season? Do those that bought capacity share the cost, or does the pipeline company absorb the lost revenue?

10:48:58 AM
BRADFORD G. KEITHLEY, Jones Day, Counsel to BP, answered in that situation FERC would consider whether that spare capacity had been developed reasonably; was prudently incurred; and was used and useful in the operation of the system. If FERC concluded it met this test, it would include those costs in the rates to existing shippers. If, however, FERC concluded the project was overbuilt and those costs were incurred unreasonably or imprudently, those would be excluded from the rate calculation. With respect to costs but not capacity, Mr. Keithley recalled

that a similar issue arose a couple of times for TAPS; it was flipped to FERC as to whether those costs were reasonably incurred, and FERC excluded some and included others.

MR. LOEFFLER added that if it is overbuilt and excluded from costs and rates, the pipeline pays for it and cannot pass it through. "We toyed around with this hypothetical when we were doing our open season comments," he recalled. Indicating the question had been why this pipeline shouldn't be overbuilt, since it is perhaps easier to add extra capacity to begin with, Mr. Loeffler noted that runs smack into the FERC policy that if the pipeline is overbuilt, the cost is paid out of the pipeline's own pocket. Even there, it could get into the subsidy question of whether it is in the public interest to overbuild this particular pipeline. "We couldn't reach that conclusion," Mr. Loeffler told members, saying it is another face of the subsidy issue and the expansion issue.

10:51:34 AM
SENATOR WAGONER said he doesn't see where there is a penalty for overbuilding the capacity of the line, to a certain extent, because there will be only four owners of the pipeline and probably only four that have the gas initially to buy capacity.

MR. LOEFFLER asked in response: How much overbuilding is enough?

SENATOR WAGONER replied that he didn't know and that it was a theoretical question.

MR. LOEFFLER made the point that this is the difficult question when dealing with contract terms. He alluded to Senator Wilken's earlier comments. He remarked that, assuming the desire is to overbuild by 5, 10, 18 or 33 percent over the open season amount, the aforementioned 5 percent and 50 percent examples are easy. But an independent company might put pressure on the pipeline to overbuild as much as possible; it would depreciate, and when the company was ready to use it, it would get an even better rate. Mr. Loeffler added that if he begins with the premise that building in some extra capacity is a good idea, he trips on the threshold of what is reasonable or unreasonable.

MR. VAN TUYL, in response to Chair Seekins, indicated the base design for the project was nominally 4.5 Bcf, with a delivered volume of 4.3 Bcf, to his belief, into the mainline process, through the gas treatment plant (GTP).

CHAIR SEEKINS asked whether there is approximately 40 percent expansion capability.

MR. VAN TUYL affirmed that as a ballpark figure.

10:54:07 AM
SENATOR DYSON observed that TransCanada's proposal appears to show a clear predisposition to rolled-in pricing for expansion. Asking what different business interests resulted in that, he surmised TransCanada might not have the same upstream interests as the major producers.

MR. VAN TUYL cited a key difference: The shippers that will likely participate in the first open season - BP, ConocoPhillips, ExxonMobil and others such as Chevron and Anadarko - have the motivation of signing those FT obligations, committing to ship under a service offered at the open season. When they see that the risk from terms they sign up for might change through no action of their own, it causes concern. Pipeline companies are on the opposite end of the spectrum, since they don't sign long-term FT obligations, and so their commercial motivation is different.

SENATOR DYSON highlighted a point from the producers today - the right to expect that the terms of a FT commitment will continue into the future. He said the threat that those will change is a legitimate concern. But a competing concern regarding basin control is the argument that the producers' upstream interests will shade their view of how to operate the pipeline. Stating appreciation for the producers' fiduciary responsibility to look after their interests and shareholders, Senator Dyson added, "What we don't want is the pipeline process to be distorted for anything except the pipeline's business."

MR. VAN TUYL replied that he can appreciate that. Also weighing heavily on his mind, as a producer who'll be a pipeline owner, is the bright line drawn between those two responsibilities by the affiliate rules and by the enforcement provisions. He recalled FERC's testimony about the $1-million-a-day-per-violation penalty if someone crosses that line, looking out for an affiliate shipper, for instance. He deferred to Mr. Keithley to expand on this, but said it is why FERC passed those regulations, to ensure that sanctity is maintained.

10:58:32 AM

MR. KEITHLEY added that as former general counsel for a pipeline operation, he could give one principal reason that TransCanada would make that statement: A pipeline looks for deep pockets, assurance of getting paid. Rolled-in rates spread the risk of recovering that cost over a much broader base or, in the case of this pipeline, over much deeper pockets. Incremental rates, by contrast, focus incremental costs on a single shipper that may or may not be solvent. It has nothing to do with expanding its business or being in a better position to serve customers, he opined. It has everything to do with cost recovery.

SENATOR DYSON indicated he hadn't thought of that, and expressed appreciation.

11:00:08 AM
MR. LOEFFLER offered two points. First, he agreed with Mr. Keithley, but indicated Canadian rate cases typically are settled on a rolled-in basis for expansion, according to his firm's Canadian counsel; thus TransCanada is used to it. Second, a possibly controversial point, Mr. Loeffler reported that he'd asked his firm's antitrust people to look at the argument that an independent pipeline wouldn't favor its affiliates, while a producer-owned pipeline might; an interesting analysis had resulted that Mr. Loeffler offered to provide in writing to the committee.

He relayed that the antitrust people said this doesn't make sense for the following reasons. Mr. Loeffler explained that if the owners of the pipeline had restricted access to keep the value of others' leases down, those leases would be available for bid because the lease owners wouldn't be able to get the production on the pipeline. At that point, however, the affiliates of the pipeline owners would be competitors in bidding for those leases, which naturally would drive up the lease prices to near market. They couldn't collude on the bidding for the supposedly depressed leases because that would be an agreement not to compete - violating the antitrust laws.

He observed that the other side is perhaps the desire to restrict supply to improve the downstream price in the U.S. However, the economic concept is market power. With respect to the numbers which apply to that, including the shares of what those companies will be in downstream markets in 2015, for example, Mr. Loeffler indicated Lukens Energy Group had provided estimates: BP's gas would be 7.3 percent, ExxonMobil's 7.9 percent and ConocoPhillips' 5.8 percent. Those are way under the threshold that the antitrust people apply in deciding

whether someone has market power, namely, the ability to benefit from withholding supply. Mr. Loeffler concluded that the analysis doesn't measure up under a set of antitrust laws.

He highlighted the assumption that an independent pipeline is only in the business of providing pipeline service. Mr. Loeffler countered that by saying an independent pipeline could have a marketing or production affiliate; some do and some don't. If it wanted to raise the tariff for a similar purpose of driving the value of leases down, it also could have or create a marketing or production affiliate to buy those leases. So the argument, from an antitrust viewpoint, falls apart on both sides.

11:04:35 AM
SENATOR DYSON voiced appreciation, but still expressed concern that bidders on leases couldn't get their product into the pipeline, and that those bidders with influence on access might have a significant advantage over other bidders. As for criticism in the media that nothing in the contract requires the producers to sell for in-state use, Senator Dyson characterized this as a cheap shot. He gave his understanding that the state's royalty share is more than enough to take care of any contemplated in-state use, except if it becomes economic to have in-state processing of liquids or other value-added products.

He suggested having the contract include that the producers must sell excess gas into the Alaska market as long as the price received is the same as in the Midwest. Senator Dyson indicated Article 9.4, on page 96 of the contract, says they aren't required to sell. He asked: Is there a way to protect the state's interests to have it for value-added needs and other in-state needs without hurting the producers financially?

MR. VAN TUYL acknowledged this as an interesting question that he wasn't specifically prepared to answer. He noted the language in Article 9.4 also says any party may sell its gas for in-state use. He averred that, all things being equal, BP would love to be able to sell its gas closer to home, rather than shipping it to Chicago. As for working out the details of requirements, matching prices and so forth, Mr. Van Tuyl relayed his initial reaction: being unsure how it would work without getting into a complicated system that could even be viewed as a restraint to free marketing. He suggested the need to look at it carefully.

SENATOR DYSON agreed it could be complicated, but indicated the legislature doesn't want the producers' other interests working against those of Alaskans. He also indicated it would give him more comfort if there were in-state use, but in such a way that the producers didn't get hurt.

11:09:02 AM
SENATOR STEDMAN asked whether the GTP will be regulated by FERC. He recalled earlier discussion of control and access to not only TAPS, but also the gas line and feeder lines.

MS. KING specified that the language in Article 8.1 has all the parties seeking and supporting FERC regulation of the gas transmission lines. From the National Petroleum Reserve-Alaska (NPR-A), that would be the line to take gas to the GTP, for example. Ms. King said she didn't recall hearing any potential shipper or the state disagree about seeking FERC jurisdiction for that. She surmised there is unity about seeking FERC jurisdiction over those facilities.

SENATOR STEDMAN pointed out that FERC's arm will reach further than on TAPS, to his understanding.

AN UNIDENTIFIED SPEAKER agreed.

SENATOR DYSON interpreted the language to say the state will have an interest in those gas transmission lines. He asked: Do any of those exist now?

MS. KING drew attention to two transmission lines that don't exist now: Point Thomson and NPR-A. With respect to state ownership in those, she pointed out that it's commensurate with how much throughput the state expects to ship. At Point Thomson, for example, the royalty rate is different than at Prudhoe Bay. At NPR-A, predominantly federal lands, the state's gas will be its tax-gas share, and so the state likely would prefer to own closer to the 6 percent net-after-royalty figure, instead of 20 percent. For the remaining transmission lines discussed in that section, Ms. King deferred to Mr. Van Tuyl.

MR. VAN TUYL noted one line that could theoretically exist is the Northstar line. However, that line would need to be looked at, and Mr. Van Tuyl said he wasn't familiar with the specifics of its design and whether it would be appropriate for gas transmission service in the advent of a sale. None of the other lines exist.

SENATOR DYSON asked: If it does apply to the Northstar line and because of the contract the state ends up owning a portion, does the state have to pay, to whoever built the line, part of the original cost or the depreciated cost of that line?

MR. VAN TUYL answered that the terms of ownership would be detailed in the entity agreement formed around the ownership of that piece, and would be detailed in the transmission-line limited liability company (LLC). Thus he didn't know what those specific terms of ownership would be.

11:13:13 AM
SENATOR WAGONER recalled recent discussion he'd had with Ms. King about taxes. He suggested the need to have tax experts address questions relating to how the state differs from the producers with respect to taxes that will or won't be paid, and the tax advantages and disadvantages of taking gas in kind or for royalty purposes.

He also quoted testimony from Mr. Massey of ExxonMobil yesterday as follows: "We are not going to own it forever, but we're going to own it until it's built." Noting Mr. Massey wasn't present today, Senator Wagoner expressed concern that the companies are asking the state for a lot of concessions. Once the pipe is built and costs are established for shipping gas, the producers can sell their interest in the pipeline corporation to TransCanada or others, and would have the best of both worlds without ownership of a pipeline where the return is controlled at about 14 percent or maybe higher. He requested a response.

11:15:10 AM
MR. VAN TUYL replied that the state has the same freedom once the pipeline is built.

SENATOR WAGONER said he understands that, but the state is kind of a minority partner.

MR. VAN TUYL referred to yesterday's discussion. As it relates to pipeline ownership, he said, the producers are uniquely motivated to ensure delivery of the pipeline system at the lowest cost. That enables transportation of the resource at the lowest cost, so it maximizes the value of the resource. Thus the producers, as resource owners, have a motivation that other third parties might not have. In fact, other third parties might have the opposite motivation. The only return a non-owner of gas gets is through the actual cost of the pipe that is

installed. Hence such a party might be motivated to deliver the highest-cost system.

He related the desire to own the pipeline initially to ensure it is delivered at the lowest cost. This is the business BP is in, and it does this around the world. Mr. Van Tuyl explained that once the pipeline is up and running, as discussed yesterday, it is a simple portfolio choice of whether to continue to be a pipeline owner or to divest that interest to another party. At that point, any party is free to buy or sell its assets as it sees fit. For example, North America's most recent gas line, the Alliance pipeline from central Alberta to the Chicago area, was owned initially by a group of producers, but shortly after first gas there was no producer ownership. Would that happen for the Alaska pipeline? Mr. Van Tuyl said he didn't know.

11:17:52 AM
MR. MARUSHACK added that the business is changing. Historically, ConocoPhillips found gas and wanted to sell it. But the world is evolving such that now the business requires taking ownership in the infrastructure and building it for all these mega-projects. If there isn't complete alignment in development of such a project and the resource pays for all the costs anyway, there is a need to protect interests by building that infrastructure.

He reported that ConocoPhillips has never said it would sell this after construction; it is a decision at the time. Mr. Marushack told members, "We pay for it anyway, so we prefer to own what we pay for." He explained that ConocoPhillips generally tries to match its ownership in the infrastructure with its ownership in the resource, though it is never a perfect fit. Mr. Marushack concluded, "It doesn't mean other folks can't ship on it. It's just our internal philosophy, and it keeps our balance sheet the cleanest."

11:19:27 AM
MR. NELSON noted ExxonMobil is in the same position. He recalled this is what Mr. Massey was trying to answer yesterday about why the company would want to build a pipeline, since it is normally a lower-return-type asset. Mr. Nelson told members ExxonMobil is getting more involved worldwide in construction of pipelines for these mega-projects, though in North America the only one he knows of is Mackenzie, with which his company's affiliate, Imperial, is involved.

He explained that because of the massive size of the Alaska project, there is a desire to be involved in the construction; while the three producers are involved in mega-projects and know how to do it, an independent company wouldn't necessarily be able to handle a project of this size. Recognizing that pipelines historically haven't been higher-performing returns, Mr. Nelson said a decision will be made in the future about whether to stay in the pipeline business. "We will be involved in operations as long as we think it's in our best interest to do that," he concluded.

11:21:05 AM
SENATOR WAGONER recalled hearing from the administration a willingness to give a credit for 35 percent of the construction - for example, the GTP and upstream gathering system - to improve the companies' internal rates of return. Referring to Mr. Massey's testimony yesterday, he asked: Why help improve these companies' internal rates of return if they're going to consider immediately turning around, once the gas pipeline is completed, and selling their portion of the pipeline?

MS. KING raised the issue of shipping commitments. Observing that the focus has been on the ownership decision, she pointed out the following: When ConocoPhillips signs up for a shipping commitment at the initial open season, it will be on the hook for it and the pipeline must be paid. This cannot just be sold. If somebody could be found to buy all the assets and obligations, that is one thing. But the shipping commitment will remain, and it is still the financial underpinning. Whoever owns the pipeline can go to the bank with the assertion of being paid day in and day out for it, regardless of whether market prices drop. Ms. King suggested factoring this into the equation.

SENATOR WAGONER reiterated concern that if the asset is sold after a credit is received, the company stands to gain a good profit at the expense of the state, and a credit wouldn't necessarily transfer to the next owner.

MS. KING clarified that under Article 20.3, the commitment allowance, the credit is actually applied to the holders of FT commitments. It isn't associated with ownership in the asset, but is directly tied to shipping commitments. It was set up for a shipper that makes a FT commitment to the pipeline or to the particular infrastructure. It isn't associated with the main line, but with the GTP and the gas transmission lines. As the language is drafted and under the upstream model contract,

it is whoever would show up to sign up for FT commitments on that particular infrastructure. For example, if Chevron shows up as a party, it would have a proportionate share if it chose to participate through an upstream model contract.

11:25:01 AM
SENATOR WAGONER asked whether his understanding was correct that it wouldn't matter who built the pipeline. If the state built 100 percent of it, the company would still show up during the open season for shipping commitments in order to get its gas to market.

MR. MARUSHACK highlighted this as a fundamental issue. Recalling arguments that there is no firm commitment to build the pipeline and so forth, he opined that the Alaska Stranded Gas Development Act ("Stranded Gas Act") was always intended to address resource issues; those relate to the tax, royalty and terms, and must be determined in order to make a FT commitment.

He focused on whether the FT commitment would be made no matter who built the pipeline. Mr. Marushack explained that this is a complicated issue because ConocoPhillips could make a FT commitment based on what it knows about its engineering and project-management capability; if it owns 25-30 percent, for example, it will fund perhaps $8-10 billion and have control so the cost hopefully won't run away. But would he feel as comfortable if somebody else built it? Mr. Marushack said no. Others won't be as interested in ensuring the project costs the least possible and is done efficiently, because they don't pay for it. "The state and the producers pay for this project through our shipping commitment," he added.

SENATOR WAGONER returned to his hypothetical scenario where the state builds it. He suggested it would be in the state's best interest to contract with someone who would keep costs low.

MR. MARUSHACK pointed out a huge difference in just turning it over to someone and asking that it be built as low-cost as possible, versus actually managing the project like a company does all around the world on these mega-projects. He added that the history of mega-projects is poor. Costs can escalate even under the best of circumstances, and the only chance of managing that is by controlling it, knowing at the end of the day "you're going to pay for it yourself."

11:27:20 AM

SENATOR STEDMAN said it seems pretty obvious it's an independent decision whether an entity would continue to own its interest in the gas pipeline. The state would negotiate its position from the point of view that the major leaseholders would divest themselves of that lower-rate-of-return project sooner rather than later after construction. Suggesting it might end up being a red herring, Senator Stedman indicated he'd be surprised if the administration didn't contemplate such divestiture. Turning to the credit and recalling discussion with respect to the oil-tax bill [SB 3001] and also the contract, Senator Stedman indicated the state has the ability to include its opinion on that in the contract if the desire is to modify it.

CHAIR SEEKINS asked: If a company decided to sell its portion of the asset, what options would the other members have to purchase it? Would they have first right of refusal?

MS. KING specified that the LLC, still being worked on, will dictate how individual members will relate to each other.

SENATOR STEDMAN asked whether there was previous testimony that if one of the initial four wanted out, the other three would have the first option to purchase that interest before it was put out for public bid.

SENATOR WAGONER recalled such discussion of a first right of refusal.

MR. VAN TUYL and MS. KING said they didn't recall it.

11:30:36 AM
MS. KING returned to Senator Wilken's question about rolled-in rates. Addressing whether "one size fits all" will work, she related a hypothetical example: The initial toll is $3.00 to get gas to market, with a market price of $5.00. Subtracting $3.00 from $5.00, the state's netback value for its royalty gas and tax gas is $2.00. If there is an expansion and suddenly that toll rises to $3.50, the netback for state gas declines from $2.00 to $1.50.

She asked: What if the source of that expansion was gas from Outer Continental Shelf federal lands, where there is no state gas? The state, as a shipper, would receive $0.50 less as a netback for its royalty gas and tax gas. Ms. King explained that the pipeline would recover its costs and thus the ownership in the pipeline would recover its costs. The state, however, as a shipper, might not view that particular application of rolled-

in rates as being in its best interests, since it would receive $0.50 less.

11:32:53 AM
SENATOR DYSON lauded this discussion, noting he'd been persuaded on some items. Recalling at least two epistles from federal folks noting a threat that the federal government would take over this project, he asked whether anyone had experience or knowledge about such a situation for other projects. He highlighted what might happen to the interests of Alaskans if the federal government took over this project and, for example, pushed the "over-the-top" route, which the state has determined not to be in its best interest.

MR. MARUSHACK answered that he had no idea what would happen if the federal government took over this project; there'd be questions about how to get shipping commitments and what project they were pursuing, for instance. With respect to the timeline, Mr. Marushack reported hearing his company's chairman say it is a concern; moving forward now makes sense because of a huge worldwide expansion in major energy projects, including those related to liquefied natural gas (LNG), pipelines and oil sands.

He cautioned that if all the engineering, open season work and permitting isn't done as quickly as possible, more projects can get ahead in line. Mr. Marushack said it makes no sense to specify what the project might look like. If steel prices go up, for instance, smaller pipe and more compression might result, and there has been a 50-80 percent price increase for steel, with huge projects committed for. Speaking against having delays simply because of inability to get the necessary materials, Mr. Marushack added, "We need more materials for this project than anybody else needs."

SENATOR DYSON again asked whether anyone knew of a project where the federal government took over, or how such a takeover might work to the detriment of Alaskans.

SENATOR BEN STEVENS suggested asking the following: Is there any other project where the federal government provided a loan guarantee to initiate it? Noting this is a unique project with respect to size and expense, he elaborated. As for the over-the-top route, he noted if the federal government took over the project under that scenario, it is written in [ANGPA, Sec. 103] that the pipeline won't enter Canada above a certain latitude.

SENATOR DYSON surmised the federal government realizes how important this project is to the national interest and, he'd argue, to national security.

11:38:30 AM
MR. KEITHLEY cited a precedent - although not a project - where the federal government had stepped in. In the 1970s, when the Lower 48 was having massive natural gas curtailments, the federal government - under Natural Gas Act powers that nobody thought existed before - took control of a large portion of natural gas supplies previously dedicated to intrastate markets in Texas, Louisiana, Arkansas and Mississippi. This was to get more gas to consumers in the Northeast. The Federal Power Commission (FPC), FERC's predecessor, took its powers to the limits, adopting regulations and orders that essentially nationalized a significant amount of the gas supplies. Thus there is precedent for the federal government to step in if the nation's natural gas supplies are believed to be at issue.

SENATOR DYSON asked how the interests of the producer states had fared under that federal takeover.

MR. KEITHLEY answered that the commission was balanced in the sense that it allocated supplies among the states, according to a set of criteria it established. For example, in Texas large amounts of gas had gone to power plants in the 1950s and 1960s, and the FPC's regulations gave power plants the lowest priority. Thus the gas formerly used for that purpose went to higher-value purposes, according to the FPC's rankings, in other states.

He further responded that the prices charged in the intrastate markets had been essentially unregulated. When the federal government took over regulation of those gas supplies, it subjected them to lower prices, consistent with what the FPC had established for gas supplies that previously were in the interstate market. As a result, Mr. Keithley said, there was a financial loss by the producers and producing states in terms of their tax and royalty interests.

MR. LOEFFLER recalled the aforementioned was in 1977 or 1978, during a cold winter when special federal legislation was passed to effectuate that.

SENATOR STEDMAN proposed getting some issues like the over-the-top route off the table, which could be answered by having staff find language that say where the line would enter Canada. He

pointed out that the over-the-top route isn't an issue unless Congress changes its opinion.

11:44:01 AM
CHAIR SEEKINS thanked participants and turned to amendments to SB 3002. He requested a motion to table Amendment 2 - moved and discussed 7/28/06 - until after the committee addressed shorter amendments.

11:44:27 AM
SENATOR BEN STEVENS moved to table Amendment 2 until a later date. There being no objection, it was so ordered.

11:44:39 AM
CHAIR SEEKINS brought before the committee Amendment 3:

A M E N D M E N T 3

OFFERED IN THE SENATE BY SENATOR STEDMAN
TO: CSSB 3002(NGD), Draft Version "G"

Page 4, lines 2 - 6:
Delete "and consent to entrance and enforcement of an arbitration award in any state court in the United States that has jurisdiction over the State of Alaska. The authority granted in this subsection is effective only after the arbitration award is entered and enforcement is sought in the superior court of the state"

SENATOR STEDMAN explained that Amendment 3 deals with giving up sovereignty. If a settlement takes away a longstanding practice that the legislature pays for a settlement demanded by the court if the state loses a particular disagreement, the bill as it stands allows another state to have jurisdiction over expenditures, basically forcing the legislature to make an expenditure.

He said there never has been a problem with the state paying its obligations. Rather, Senator Stedman suggested, payment practices most likely show the state to be more timely in payments than the producers with respect to past disagreements. Referring to previous testimony that no other state in the Union has given up this particular sovereignty, Senator Stedman closed by saying he doesn't believe Alaska should be the first.

11:46:32 AM

JOSEPH K. DONOHUE, Preston Gates & Ellis, Counsel to the Governor, pointed out that Amendment 3 would require renegotiation of Article 26 of the proposed fiscal contract.

SENATOR BUNDE surmised that would be the impact of many things the legislature would do in the next few days, including passage of a petroleum production tax (PPT) bill.

11:47:47 AM
CHAIR SEEKINS asked whether there was an objection to adopting Amendment 3. There being no objection, it was so ordered.

11:48:12 AM
CHAIR SEEKINS moved to adopt Amendment 4, which read:

A M E N D M E N T 4

OFFERED IN THE SENATE BY SENATOR RALPH SEEKINS
TO: SB 3002 24-GS2095\G

AS 43.82.230(a) is amended to read:

Sec. 43.82.230. Contract terms relating to hiring of Alaska residents and contracting with Alaska businesses. (a) The commissioner shall include in a contract under AS 43.82.020 a term requiring the qualified sponsor**,** [OR] qualified sponsor group**, or a related party,** and contractors of the qualified sponsor**,** [OR] qualified sponsor group**, or a related party,** to comply with all valid federal, state, and municipal laws relating to hiring Alaska residents and contracting with Alaska businesses to work in the state on the approved qualified project and not to discriminate against Alaska residents or Alaska businesses. Within the constraints of law**:**
(1)[,] the commissioner shall also include in a contract under AS 43.82.020 a term that requires the qualified sponsor**,** [OR] qualified sponsor group**, or a related party,** and contractors of the qualified sponsor**,** [OR] qualified sponsor group**, or a related party,** to employ Alaska residents and to contract with Alaska businesses to work in the state on the approved qualified project to the extent the residents and businesses are available, competitively priced, and qualified;[.] **and (2) should the state acquire an ownership interest in the qualified projects as part of a contract developed under this chapter, the**

parties shall agree to enter into negotiations for project labor agreements to facilitate the construction of the qualified project. To the extent lawful, the parties shall include provisions in any project labor agreement that would promote hiring of Alaska residents and the establishment of hiring halls in both rural and urban communities of the state.

SENATOR DYSON and SENATOR WAGONER objected for discussion purposes.

CHAIR SEEKINS opined that Amendment 4 is straightforward, making a couple of minor changes in talking about adding "a related party" and bringing in new text at the bottom, which he read to members. He requested that Commissioner O'Claray testify.

11:49:25 AM
GREG O'CLARAY, Commissioner, Department of Labor and Workforce Development (DOLWD), explained that because of the federal constitutional question regarding "Alaska hire," a preference for hiring Alaskans over residents of other states must not be the primary purpose for this particular amendment. However, the benefits of a project labor agreement (PLA) are many. He suggested this is a proper way to approach looking for identifiable costs and scheduling matters for a project of this magnitude - ensuring there is a qualified and trained workforce and that a unified labor policy covers all contractors and subcontractors. Commissioner O'Claray concluded by offering his belief that "to the extent lawful" in Amendment 4 is a good enough caveat to avoid a constitutional problem.

SENATOR DYSON requested time to think about Amendment 4 over the lunch break.

CHAIR SEEKINS concurred.

COMMISSIONER O'CLARAY, in response to Senator Elton, clarified that there is no problem with the PLA portion. Rather, his concern is that, if it is the primary purpose of a statute, a preferential Alaska-hire law will undoubtedly be challenged and possibly struck down in the courts. He related his understanding that attorneys for the producers, the state and the labor movement have looked at this issue.

CHAIR SEEKINS noted Amendment 4 doesn't say "require" but says "promote" with respect to hiring within Alaska. While urban residents can usually find a job, some rural areas have

extremely high unemployment. Mentioning finding a way to inform rural residents that jobs and training are available, he requested confirmation that training is available through the state's efforts.

COMMISSIONER O'CLARAY affirmed that. He specified that through a joint effort, one grantee - Alaska Works Partnership - primarily focuses on recruiting rural Alaskans for training within the construction field.

CHAIR SEEKINS recalled TAPS construction, suggesting if people can fly in from Oklahoma, they should be able to fly in from some rural Alaska communities. He proposed encouraging, to the extent lawful, promotion of these jobs and related training; for example, hiring halls could be located in Alaska. Chair Seekins added that care was taken in crafting Amendment 4 to ensure the constitutional line wasn't crossed in terms of an actual requirement for Alaska hire.

11:54:26 AM
SENATOR DYSON asked: Does the proposed contract call for promotion of the PLA?

COMMISSIONER O'CLARAY answered it doesn't exist now, although including some language has been discussed.

SENATOR DYSON recalled testimony from Jim Clark that some court case said nonunion workers couldn't be precluded from being hired. He asked what that decision means in practical terms. He also asked whether, in Amendment 4 or another, there should be language precluding a union's internal rules from superseding an intention that qualified Alaskans get the first shot. Senator Dyson related his understanding that at least one major construction union in Alaska has internal rules that say it cannot hire any Alaskans as long as there is somebody available on its books in the Northwest; he indicated someone from DOLWD at the Eagle River presentation last Friday had said there were efforts to address this.

11:56:38 AM
COMMISSIONER O'CLARAY specified that the decision with respect to a union-membership requirement to work under a PLA and others is the Beck decision, which he offered to obtain. It doesn't mandate compulsory union membership.

He turned to the second question, noting he wasn't aware which union Senator Dyson was referring to. Commissioner O'Claray

reported that all the union hiring procedures he has viewed in the building trades do show an Alaska residential preference of one year of residency for dispatch. He stated the desire to make certain, within the discussions of the PLA, that this is the case in terms of dispatch.

He cautioned against intruding too far into the purview of the federal government and federal law with respect to the National Labor Relations Act, which regulates how unions operate. Commissioner O'Claray said he believes Amendment 4 is covered by its wording with respect to the caveat, since it doesn't mandate hiring hall location - which isn't within the purview of states to dictate, under the aforementioned Act.

CHAIR SEEKINS agreed it doesn't mandate location, but says "we want to establish some of those."

COMMISSIONER O'CLARAY said he believes that is a clear statement of the desire that it not be a requirement.

CHAIR SEEKINS added that he just doesn't want it located so far away that Alaskans can't get there.

11:58:41 AM
SENATOR DYSON informed listeners that if a craftsman in Alaska is qualified by any standard but isn't a union member, it is his desire to have the local union extend membership to that person before hiring someone outside Alaska. He asked whether the National Labor Relations Act allows such a preference to be included in the contract.

COMMISSIONER O'CLARAY answered, "Yes, but very carefully worded." He explained that an attempt to mandate rules that are beyond the purview of the state's involvement would be in peril in terms of a court challenge with respect to constitutionality. He reported that Governor Murkowski has made it clear that he supports the PLA for this project, and is encouraging both labor and the producers to begin substantive discussions to get to that point so this project can be built.

SENATOR DYSON asked: Does Amendment 4 preclude a qualified nonunion contractor from being involved in this project?

COMMISSIONER O'CLARAY replied no. Mentioning that there are many cases under PLAs, he indicated he doesn't know of anyplace where unorganized employees are barred from participating.

12:00:37 PM
SENATOR BUNDE offered his assessment that a laborer who wanted to get hired would have to go through a union hall. He asked whether there would be a fee for the service of being hired.

COMMISSIONER O'CLARAY affirmed that likelihood.

SENATOR BUNDE characterized this as an agency shop, pointing out that for teachers the equivalent fee is substantial, almost what a union member would pay. Returning to Amendment 4, he suggested the last sentence provides intent without teeth because a hiring hall is created by a private agency, a union. The state cannot tell that union how to spend its money. Senator Bunde said he would be concerned if hiring halls were defined as state agencies, however, because of cost issues.

CHAIR SEEKINS agreed, noting the remainder of this Act talks about advertising through job services and so forth. That's why there is a caveat that the parties shall include provisions to the extent that is lawful. He concurred that the state cannot mandate it, but said as part of the PLA he believes there can be a request for hiring halls, facilities or some type of process in rural communities to be able to hit areas of high unemployment and promote hiring there. He cautioned against overlooking this in the rush to accomplish something.

12:04:40 PM
CHAIR SEEKINS called attention to a handout entitled "An Act of Congress, H.R. 4837-36" that contained the provisions of ANGPA. He read from Section 103(d), skipping over paragraph (1). It stated in its entirety:

> (d) PROHIBITION OF CERTAIN PIPELINE ROUTE - No license, permit, lease, right-of-way, authorization, or other approval required under Federal law for the construction of any pipeline to transport natural gas from land within the Prudhoe Bay oil and gas lease area may be granted for any pipeline that follows a route that--
>
> (1) traverses land beneath navigable waters (as defined in section 2 of the Submerged Lands Act (43 U.S.C. 1301)) beneath, or the adjacent shoreline of, the Beaufort Sea; and
>
> (2) enters Canada at any point north of 68 degrees north latitude.

CHAIR SEEKINS highlighted that this is the intent of Congress. He surmised there would be a big row within Alaska if someone tried to do otherwise.

SENATOR WILKEN pointed out that what Congress can do, it can undo. Saying he can envision a scenario in which this pipeline runs down the Mackenzie Valley, Senator Wilken suggested that might even benefit Alaskans. While taking some comfort in what is before the committee, he said it isn't cast in concrete.

12:06:25 PM
SENATOR BEN STEVENS advocated the position that Congress would only act to change this if Alaska failed to act under the criteria in ANGPA. He suggested the way to prevent an over-the-top route is to act on the route proposed now, the so-called highway route.

CHAIR SEEKINS announced he would offer an amendment on this question that might help to clear it up "in state as well."

The committee took an at-ease from 12:07:09 PM to 1:57:44 PM.

CHAIR SEEKINS returned attention to Amendment 4.

SENATOR DYSON noted he was having copies made of an article relating to a presentation made to the governor by the major bargaining units. He said, however, that the commissioner had answered most of his questions.

The committee took an at-ease from 2:00:14 PM to 2:01:50 PM.

SENATOR DYSON requested that members read the handout, an article from the Alaska Journal of Commerce entitled "Unions say labor agreement needed for gas line" by Melissa Campbell, dated 7/30/06. He then paraphrased a portion on page 2 that read:

> Depending on how it's written, a PLA could preclude nonunion workers from the project. That could mean that Alaskans would have to join a union.

He surmised nonunion contractors also could be precluded. Senator Dyson indicated he'd had discussion with the chair and the commissioner that there could be a PLA which doesn't say whether it has to be union or nonunion contractors or workers. If the intention is that Amendment 4 not be construed to make this an all-union contract or job, Senator Dyson encouraged stating it on the record.

CHAIR SEEKINS clarified that Amendment 4 doesn't specify there are union PLAs, but says to negotiate PLAs. He added, "I don't see how you could build the project without involvement of the union community, quite frankly. But it does not particularly specify that they must be union." He opined that this adequately protects the interests of Alaskans in this regard.

SENATOR DYSON specified that his request for clarification shouldn't be construed as anti-union in any way.

CHAIR SEEKINS observed that the union system has much to offer in providing labor and training, as well as trained and safe workers. However, he didn't want to specify that this has to be any particular "local" either. Rather, it has to be a PLA, and it should be carefully laid out ahead of time.

2:05:20 PM
SENATOR DYSON alluded to the Davis-Bacon Act with respect to wages. He asked whether all the work will be Davis-Bacon.

JIM CLARK, Chief Negotiator, Office of the Governor, asked whether Senator Dyson was referring to the federal Act. He indicated the administration had looked at the state Act, the "little Davis-Bacon," and it wasn't clear from the supreme court's five-part test whether it would be or not.

SENATOR DYSON surmised federal participation, including loan guarantees, wouldn't force it to be federal Davis-Bacon.

MR. CLARK indicated the administration didn't know.

SENATOR STEDMAN recalled for TAPS it was equivalent to Davis-Bacon.

CHAIR SEEKINS added those were union contracts, union PLAs.

SENATOR STEDMAN asked how the state would benefit if it weren't Davis-Bacon.

SENATOR BUNDE noted if there was "x" amount of money, it could be spread over twice as many jobs. He encouraged looking at the roots of Davis-Bacon, characterizing it as a racist law and questioning whether anything should be done to continue what he called race-based activities.

SENATOR STEDMAN said he didn't know how accurate or inaccurate Senator Bunde's comments were, but the communities he himself represents have been better off when operating under Davis-Bacon for capital projects. Even though it costs more, it provides livable-wage jobs in Alaska. If the effort is to employ as many Alaskans as possible, Senator Stedman said he'd like workers to have good wages and training so when construction ends they can continue working. Speaking against having contractors hire folks who'll work for the least money for this project, he opined that the state is better off if Davis-Bacon covers these types of projects.

CHAIR SEEKINS noted Canada is looking at immigration to get manpower for the Mackenzie pipeline, but also is negotiating with local unions on how that will work. He related his intention that immigration and "starvation wages" won't be used to put people to work on the Alaska natural gas pipeline. Rather, PLAs will stabilize those and set it out in clear terms before the project starts.

SENATOR ELTON agreed with Chair Seekins. He began discussion of Amendment 1 to Amendment 4. He highlighted the following language: "**the parties shall agree to enter into negotiations for project labor agreements**". He suggested this is no guarantee of a PLA because it only commits to talk about it. He asked why that limitation is included.

2:11:23 PM
CHAIR SEEKINS answered that there should be a clear intent, and he fully expects there will be PLAs. Chair Seekins said he doesn't have a problem with doing that, but wants to ensure they are negotiated PLAs, not necessarily mandated. He acknowledged the drafting might not have captured the intent clearly. If the owners must be put up against a wall and have PLAs regardless of how they are negotiated, Chair Seekins said he'd have a little problem with it. Recalling testimony in Fairbanks that TAPS wages were negotiated way too high, he specified the desire to have the terms negotiated, but to have PLAs.

2:12:42 PM
SENATOR ELTON moved to adopt Amendment 1 to Amendment 4, to change the aforementioned language to read: "**the parties shall negotiate and agree to project labor agreements**". He explained that unless he'd misunderstood what Chair Seekins just said, it provides that there will be a negotiation process of give-and-take, but also provides that it will lead to PLAs.

SENATOR DYSON objected. He voiced concern that if a non-owner organization was being outrageous in a demand for its terms on a PLA, the cost might be too high if it must come to an agreement, and it might destroy the negotiation process. He stated preference for the original language in Amendment 4.

SENATOR BUNDE agreed, suggesting it provides some serious veto power.

SENATOR ELTON referred to testimony in Fairbanks, Anchorage and Juneau, as well as comments outside of the committee process. He recalled that everybody had voiced commitment to a PLA as the best way to accomplish what needs to be done. He suggested it falls a bit short if all that is mandated is a commitment to talk about it, rather than a commitment to actually accomplish a PLA. He encouraged a "yes" vote.

SENATOR DYSON asked to hear from those who'll be at the table if this says they must come to an agreement - those representing the producers and the administration.

MR. CLARK opined that Senator Dyson was right, in part because of the context in which negotiations will take place. This is a fiscal contract, and negotiations will be done by contractors to be hired by the LLC that will manage affairs relating to pipeline construction. What is being directed with respect to the contract is that those discussions take place, but it will take place at the contractor level, and those terms will be worked out then. This gives legislative direction, and there will be constant communication with the legislature on this through appropriations and other matters, Mr. Clark asserted, noting legislators will be asking the administration about this as the event draws closer. He concluded that mandating it in this contract is the wrong place to do it.

2:17:34 PM
MR. MARUSHACK reminded members that ConocoPhillips has said it doesn't know where it will get all the people needed for this huge project. The company clearly is committed to Alaska hire, he said, just as it is for its current operations. Offering his personal belief that union labor will be needed on this project, Mr. Marushack predicted there also will be PLAs entered into.

He agreed with Senator Dyson, however. If the result must be a PLA, Mr. Marushack questioned how that is in Alaska's best interest. No matter what terms a party wanted to put forward, it would know the project wouldn't proceed unless those terms

were met. Since ConocoPhillips is reasonably good at negotiating, the company likely would want a PLA that works for its side as well. Mr. Marushack said he understands the intent of entering into good-faith negotiations, and he fully expects PLAs will result. However, mandating a PLA as the end result could cause completely unnecessary delays.

A roll call vote of 3 yeas and 6 nays proved Amendment 1 to Amendment 4 to SB 3002 failed, with Senators Olson, Elton and Hoffman voting yea, and Senators Ben Stevens, Stedman, Bunde, Dyson, Wilken and Seekins voting nay.

2:20:32 PM
CHAIR SEEKINS returned to the original Amendment 4. In response to a committee secretary, he opined that Senator Bunde and Senator Wagoner had objected previously. He noted Senator Wagoner wasn't present to remove his objection.

SENATOR BUNDE said he was removing his objection.

SENATOR BEN STEVENS announced he would vote no.

A roll call vote of 8 yeas and 1 nay proved Amendment 4 to SB 3002 passed, with Senators Stedman, Bunde, Olson, Dyson, Wilken, Elton, Hoffman and Seekins voting yea, and Senator Ben Stevens voting nay.

2:21:28 PM
CHAIR SEEKINS moved to adopt Amendment 5, which read:

A M E N D M E N T 5

OFFERED IN THE SENATE BY SENATOR RALPH SEEKINS
TO: SB 3002 24-GS2095\G

Sec. 43.82.100. Qualified project.

Based on information available to the commissioner, the commissioner may determine that a proposal for new investment is a qualified project under this chapter if the project
(1) principally involves
(A) the transportation of natural gas by pipeline to one or more markets, together with any associated processing or treatment;
(B) the export of liquefied natural gas from the state to one or more other states or countries; or

(C) any other technology that commercializes the shipment of natural gas within the state or from the state to one or more other states or countries;
(2) would produce at least 500,000,000,000 cubic feet of stranded gas within 20 years from the commencement of commercial operations; **[AND]**
(3) is capable, subject to applicable commercial regulation and technical and economic considerations, of making gas available to meet the reasonably foreseeable demand in this state for gas within the economic proximity of the project; **and**
(4) no project may be considered a qualified project under this chapter if the project enters Canada at any point north of 68 degrees latitude.

SENATOR BUNDE objected for discussion purposes. He related his understanding that Chair Seekins wanted a friendly amendment to change "68" to "64".

CHAIR SEEKINS asked whether there was any objection to Amendment 1 to Amendment 5, changing "68" to "64". He acknowledged there was no objection.

SENATOR OLSON moved to adopt Amendment 2 to Amendment 5. He alluded to Section 103(d)(1) of ANGPA, indicating his amendment would insert the following:

traverses land beneath navigable waters (as defined in section 2 of the Submerged Lands Act (43 U.S.C. 1301)) beneath, or the adjacent shoreline of, the Beaufort Sea; and

He read the above language. Noting he represents the people of the aforementioned area, Senator Olson said they are involved with marine mammal harvesting - whales in particular - and aren't interested in seeing development in that area.

CHAIR SEEKINS clarified that Amendment 5, with both the previous amendment to it and this one, if adopted, would have the following new language beginning with paragraph (4):

(4) no project may be considered a qualified project under this chapter if the project enters Canada at any point north of 64 degrees latitude if: the project traverses land beneath navigable waters (as defined in section 2 of the Submerged Lands Act (43 U.S.C. 1301)) beneath, or the adjacent shoreline of, the Beaufort

Sea; and if the project enters Canada at any point north of 64 degrees latitude.

SENATOR OLSON affirmed that.

SENATOR DYSON said he appreciated the effort, but thought it was redundant, since he didn't believe any part of the Beaufort Sea was south of 64 degrees.

CHAIR SEEKINS agreed Senator Dyson was probably correct, noting it just mirrors the federal language.

SENATOR BUNDE asked if this would impact any offshore exploration that requires a small feeder pipeline to connect to the Prudhoe Bay area.

CHAIR SEEKINS opined that it is only if it relates to a qualified project. He added, "If the project enters."

SENATOR BUNDE raised a concern about what precedent it would set for objections to other projects.

CHAIR SEEKINS clarified that it isn't the intent to affect any future feeder lines. It is specifically the qualified project, which to his belief would begin at the GTP. He asked whether that was correct and how far backwards it would go.

MS. KING replied that the defined project in the contract and the qualified project includes the gas transmission lines.

CHAIR SEEKINS asked whether it is anticipated that the gas transmission lines will be underneath the navigable waters.

MS. KING said it is possible over the course of time that some exploration could have gas transmission lines coming in.

MR. VAN TUYL added that he'd need to look at the specific language proposed for addition, but one concern BP might have - harkening back to an earlier discussion - is the Northstar line.

CHAIR SEEKINS indicated he was trying to resolve this. He noted it said "and ... Canada at any point" - not "or".

SENATOR BUNDE objected to Amendment 2 to Amendment 5, citing an abundance of caution.

SENATOR ELTON spoke in favor of it. He said he doesn't know what the possibility is that this will occur, but if the restriction just says the entry point into Canada is 68 degrees or further south, it doesn't preclude a pipeline starting along the Beaufort Sea and then entering Canada at some point less than 68 degrees latitude. Acknowledging that may or not be the case, Senator Elton also recalled concern raised about the upstream, and whether or not that would preclude feeder lines, for example. He suggested this is already a problem, given the federal language.

CHAIR SEEKINS said he wasn't so worried about it paralleling the Canadian line because there are no roads over there. He suggested someone trying to build a pipeline would certainly want a road and access. He further suggested it wouldn't save that much distance if it had to go down the line and then go across somewhere north of Dawson City.

SENATOR STEDMAN proposed it might be easier to rely on the federal language; if that were to be changed, there'd be ample warning to deal with it. While recognizing the attempt by Senator Olson, he agreed it seems redundant, since it is already prohibited by the federal Act.

CHAIR SEEKINS concurred with that possibility, suggesting it could read: "no project may be considered a qualified project under this chapter" - with a transition - "for any project that follows a route that transverses land beneath the navigable waters" and so forth.

SENATOR OLSON maintained that his amendment was appropriate. While acknowledging the aforementioned could allay some concerns at the outset, he highlighted the need for clear support from the people in that area, and therefore having specific language clarifying that lands traversing beneath the navigable waters will be excluded.

CHAIR SEEKINS asked Mr. Van Tuyl whether this is this talking about the midstream portion of the project.

2:29:46 PM
MR. VAN TUYL replied yes.

CHAIR SEEKINS asked whether it would be clearly defined by specifying it is the midstream portion of the project.

MR. VAN TUYL expressed concern because of the way the project is defined in the contract: it includes the main line, the GTP and the gas transmission pipelines. A portion of the project might traverse land beneath navigable waters, beneath or adjacent to the shoreline of the Beaufort Sea. It might already exist, and it might be the Northstar line, if indeed BP uses that for gas export. In that case, it would be excluded under this language, and it would cause a problem. Referring to the federal language quoted earlier, he noted subsection (d) says "of any pipeline to transport natural gas from land within the Prudhoe Bay oil and gas lease area". Mr. Van Tuyl said if this relates to the pipeline to transport gas away from the Prudhoe Bay oil and gas lease area, then he believes that context is clearer.

CHAIR SEEKINS asked whether the following would work: "No project may be considered a qualified project under this chapter if any pipeline to transport natural gas from land within the Prudhoe Bay oil and gas lease area may be granted that follows a route that" - followed by paragraphs (1) and (2).

SENATOR BEN STEVENS alluded to AS 43.82.100, Qualified project, noting it talks about a qualified project under this chapter. He indicated this chapter is designed to move gas from the North Slope to the market outside and inside Alaska. He mentioned including provisions (1) and (2), suggesting it takes away from the fact that the pipeline won't traverse the area and enter Canada. He opined there could potentially be submerged lines in the future if they don't enter Canada.

SENATOR WILKEN spoke against Amendment 2 to Amendment 5, opining that subsection (4) as originally proposed satisfies the intent and the statement of the people of Alaska. He reported having found out in the last 10 minutes that altering it opens different avenues that don't need to be pursued at this time.

2:33:23 PM
A roll call vote of 5 yeas and 4 nays proved Amendment 2 to Amendment 5 to SB 3002 passed, with Senators Olson, Elton, Hoffman, Ben Stevens and Seekins voting yea, and Senators Stedman, Bunde, Dyson and Wilken voting nay.

The committee took an at-ease from 2:36:10 PM to 2:40:09 PM.

SENATOR BUNDE moved to reconsider his vote on Amendment 2 to Amendment 5.

SENATOR ELTON objected in order to wait for the return of the amendment's sponsor, Senator Olson.

SENATOR BUNDE renewed his motion.

SENATOR OLSON objected, saying the vote had been taken and the committee should move on.

CHAIR SEEKINS requested a roll call vote on rescinding the previous action.

A roll call vote of 2 yeas and 7 nays proved the committee failed to rescind its action in adopting Amendment 2 to Amendment 5, with Senators Bunde and Wilken voting yea, and Senators Olson, Elton, Hoffman, Ben Stevens, Stedman, Wagoner and Seekins voting nay.

CHAIR SEEKINS opined that Amendment 5 as amended would read:

> ; **and**
> **(4) no project may be considered a qualified project under this chapter if the pipeline to transport natural gas from land within the Prudhoe Bay oil and gas lease area follows a route that (1) enters Canada at any point north of 68 degrees latitude and traverses land beneath navigable waters (as defined in section 2 of the Submerged Lands Act (43 U.S.C. 1301)) beneath, or the adjacent shoreline of, the Beaufort Sea**

He said it is only if the pipeline transverses from land within the Prudhoe Bay oil and gas lease area, and would not now affect feeder lines or transmission lines. Chair Seekins said this was the intent of the original amendment. He asked whether everyone understood the amendment to read that way.

SENATOR OLSON concurred.

CHAIR SEEKINS noted there'd been no objection stated.

The committee took an at-ease from 2:43:54 PM to 2:56:53 PM.

CHAIR SEEKINS began discussion of Amendment 3 to Amendment 5. He called attention to the federal legislation, pointing out that it says "north of 68 degrees", whereas the committee had made it "north of 64 degrees". He noted it should also say "north latitude" following that.

CHAIR SEEKINS moved to adopt Amendment 3 to Amendment 5, to insert "north" following "degrees" and before "latitude" in paragraph (1) as previously adopted.

SENATOR BEN STEVENS, following a procedural discussion, renewed the motion. There being no objection, it was so ordered.

CHAIR SEEKINS, in response to Senator Dyson, clarified that Amendment 5 as amended would read:

> ; **and**
> **(4) no project may be considered a qualified project under this chapter if the pipeline to transport natural gas from land within the Prudhoe Bay oil and gas lease area follows a route that (1) enters Canada at any point north of 64 degrees north latitude and (2) traverses land beneath navigable waters (as defined in section 2 of the Submerged Lands Act (43 U.S.C. 1301)) beneath, or the adjacent shoreline of, the Beaufort Sea**

SENATOR DYSON offered his understanding that this relates to what carries gas from the unit.

CHAIR SEEKINS replied that it is from land within the Prudhoe Bay oil and gas lease area.

SENATOR DYSON suggested "land" is redundant.

CHAIR SEEKINS said it is from the land within that unit. This duplicates the federal legislation.

SENATOR WILKEN expressed support for Amendment 5 as amended, but said it has been made unnecessarily complicated. He spoke in favor of having the people's voice, since there is another bite of the apple through the Qualified Project Plan to be published every year. As it is today, the state would have a 20 percent voice with respect to the route for the project.

He expressed hope that the people's voice would become the one that decides, in the future, whether this route takes a different direction from the highway route. The people could posit a scenario that keeps this project on the highway, and unfortunately could also set forth a scenario that makes a different route the only possibility. If and when it comes to that juncture, however, Senator Wilken said the people should

decide whether there will be in-state gas or whether the value will just be taken as the gas is shipped out of Alaska.

SENATOR BUNDE objected to Amendment 5 as amended, emphasizing he doesn't want to be a party to anything that "clever lawyering" could construe as opposition to having access to offshore gas.

A roll call vote of 8 yeas and 2 nays proved Amendment 5 as amended passed, with Senators Olson, Dyson, Wilken, Elton, Hoffman, Ben Stevens, Stedman and Seekins voting yea, and Senators Bunde and Wagoner voting nay.

3:04:43 PM
SENATOR WILKEN offered some issues relating to the presentation of SB 3002 last Friday, 7/28/06. He turned to page 2, line 11, of Version G. The language surrounding that line read:

> (2) allow the fiscal terms applicable to a qualified sponsor or the members of a qualified sponsor group**, or a related party**, with respect to a qualified project, to be tailored to the particular economic conditions of the project and to establish those fiscal terms in advance with as much certainty as the Constitution of the State of Alaska allows; and

He noted "related party" is defined on page 11 as follows:

> (14) "related party" means an entity, including a limited liability company or similar incorporated or unincorporated entity, that
>
> (A) is affiliated with a qualified sponsor or qualified sponsor group;
>
> (B) owns or operates a qualified project or any segment of a qualified project; and
>
> (C) is an intended beneficiary of the fiscal terms included in a contract developed under this chapter.

SENATOR WILKEN recalled discussion relating to subparagraphs (A), (B) and (C). He asked whether everyone was comfortable with the "related party" inclusion and the definition on page 11. He requested a response from the administration.

CHAIR SEEKINS asked Mr. Donohue for an example of such an entity.

MR. DONOHUE replied that the reason for including "related party" in .010, the purpose section, and several other places in the chapter is to clarify that some fiscal-stability terms relate to entities that aren't the qualified sponsors or the immediate parties to this proposed contract. It clarifies that project-owner entities such as the mainline LLC are eligible for the fiscal-stability terms set out in the contract, such as the payments in lieu of various property tax provisions.

SENATOR WILKEN recalled concern that "related party" could trickle down to a gas station or refinery, for instance. He alluded to the definition on page 11, asking whether the inclusion of "and" [following subparagraph (B)] on line 27 excludes that possibility.

MR. DONOHUE replied yes, in his view. He explained that the intended beneficiaries of the fiscal terms of the contract are the LLC entities that will own different segments.

SENATOR WILKEN turned to page 2 of Version G, lines 28-31, which read:

> (2) certain adjustments regarding **oil and gas lease agreements, unit agreements, and other agreements** [ROYALTY] under AS 43.82.220**; in this paragraph, "oil and gas lease agreements" includes royalty provisions of those agreements; and**

He noted this applies to what the commissioner may do. Senator Wilken recalled that when Pioneer wanted royalty relief, it negotiated with the commissioner for a deal brought to the Legislative Budget and Audit Committee for public review. He asked how this differs from current law, and whether this language eliminates public review of what amounts to a unilateral agreement between the commissioner and someone petitioning for royalty relief under paragraph (2).

3:10:55 PM
MR. DONOHUE replied that this is designed to conform this subsection to the more extensive changes to AS 43.82.220 in Sections 7-9 and so forth. Under current law, AS 43.82.220 only allows the administration to deal with various timing and notice provisions relating to royalty in kind (RIK) sales or royalty in value (RIV), meaning the administration could agree to take only RIV for the first 20 years under the purchase and sale agreements, or could take RIK or some allocation of both. In .220 there also are provisions for modification, establishing

and making more certain the RIV methodologies. That particular subsection isn't addressed in this "conforming amendments bill" because the state has agreed to take its royalty in kind. Thus there is no RIV methodology at issue.

He continued with paragraph (2). Mr. Donohue characterized the language **"'oil and gas least agreements' includes royalty provision"** as a drafting loop to clarify that the deletion of "royalty" doesn't exclude royalty provisions from that. Those are included in more comprehensive language in Sections 7-9.

SENATOR WILKEN asked: If the sponsor group or part of the sponsor group petitioned the commissioner for royalty relief somewhere, in some period of time, could the commissioner be able to do that, given the negotiations? And where is the public disclosure of that negotiation and result?

MR. DONOHUE answered as follows: To the extent that the leases are affected or included in this fiscal contract, the ability of the lessee to seek separate relief under separate statutes would be superseded. The remedies for those leases would be within the fiscal contract, and they would have to seek an amendment. If there are leases outside of this contract, then the statutory rights to seek review would remain in place.

CHAIR SEEKINS offered his understanding that none of those leases would be affected one way or the other.

MR. DONOHUE affirmed that.

3:12:52 PM
SENATOR WILKEN remarked that he would spend more time on that. He then turned to page 6, Section 11, new language beginning on line 28 in subsection (c) that read:

> However, the commissioner may develop a contract term that, in the event of a material change in the taxes enacted after the effective date of the contract, establishes a procedure for restoring the parties to substantially the same economic position they had as of the end of the period described in (b) of this section immediately before the change.

He alluded to discussion of SB 2004 at the end of the last special session. Senator Wilken recalled a suggestion that the commissioner in the above paragraph means the one in place today, whereas he and others believed the timeline implied it

would be the commissioner at the time when the issue of equilibrium came before the state for consideration. He asked: Are we clear that the commissioner on line 28 is the commissioner at the time of the need for equilibrium?

MR. DONOHUE gave his reading that it could be either. He said his initial reading is that the commissioner today could be developing terms relating to this fiscal-balancing test that would be put in place after the 14-year period.

SENATOR WILKEN suggested the need to revisit this.

SENATOR ELTON asked: If a future commissioner decided to change what the existing commissioner had done, would that action be challengeable through the dispute resolution process?

MR. DONOHUE indicated if there was a dispute about whether there was a material change under subsection (c), it would be in accordance with subsection (d) on the next page, the result under the dispute resolution process. Subsection (d) read:

> (d) Implementation of a contract provision authorized in (c) of this section may be made subject to the dispute resolution procedures of the contract.

SENATOR ELTON made the following point: Whether or not a future commissioner has the ability to change it, that action by a future commissioner could be taken through the dispute resolution process, and may or may not limit the latitude that a future commissioner has in making such a change.

MR. DONOHUE noted he was thinking through subsection (c). He said to the extent they are talking about contract terms, it relates to the fiscal contract everyone is working on now. He suggested a future change by a commissioner would have to be implemented by "amendment authorities" in the contract itself. He opined that subsection (c) is ambiguous on that point and would benefit from clarification.

SENATOR WILKEN alluded to previous discussion of time periods, saying he'd been thinking something would trigger it when the 11-year period started, and the commissioner at that time would deal with the question of equilibrium; he reiterated the need to revisit this issue. He turned to the retroactivity provisions on page 12:

RETROACTIVITY. (a) Sections 2 - 14 and 17 - 20 of this Act are retroactive to January 1, 2004.

(b) Section 1 of this Act is retroactive to January 1, 2005.

SENATOR WILKEN asked why Section 1, relating to arbitration, is retroactive to January 1, 2005.

MR. DONOHUE replied that Section 1 of the bill refers to the scope and application of the revised Uniform Arbitration Act, adopted and made effective as of January 1, 2005. It wasn't in effect as of January 1, 2004.

3:18:20 PM
SENATOR WILKEN noted the committee has worked on payments in lieu of taxes (PILTs) relating to municipalities. Recalling from the presentations that the PILTs would be essentially equal to the status quo, he asked if they are equal, since there appear to be differences, relating to gas and oil transmission lines and facilities. Senator Wilken indicated he was working with others, including Mr. Hoffbeck [petroleum property assessor with the Department of Revenue], on related data. Informing members that this may or may not lead to amendments, Senator Wilken suggested the need for further data and work with respect to balancing the benefits all across Alaska and ensuring that the PILTs equal the status quo. He added that these concerns stemmed from Friday's discussion.

CHAIR SEEKINS announced Amendment 2 to SB 3002 would be dealt with Thursday, 8/3/06; he acknowledged members might have other amendments as well. He held SB 3001 and SB 3002 over.

There being no further business to come before the committee, Chair Seekins adjourned the Senate Special Committee on Natural Gas Development meeting at 3:23:10 PM.