

**ALASKA STATE LEGISLATURE**  
**SENATE SPECIAL COMMITTEE ON NATURAL GAS DEVELOPMENT**

August 4, 2006

10:18 a.m.

**MEMBERS PRESENT**

Senator Ralph Seekins, Chair  
Senator Lyda Green  
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  
Senator Albert Kookesh

**MEMBERS ABSENT**

All Members present

**OTHER LEGISLATORS PRESENT**

Senator Gary Stevens  
Representative Paul Seaton  
Representative Jay Ramras  
Representative Kurt Olson  
Representative Berta Gardner  
Representative Mark Neuman  
Representative Ralph Samuels

**COMMITTEE CALENDAR**

Alaska Gasline Port Authority Presentation

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."

MOVED CSSB 3002(NGD) OUT OF COMMITTEE

**PREVIOUS COMMITTEE ACTION**

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)
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)	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
08/01/06	(S)	Heard & Held
08/01/06	(S)	MINUTE(NGD)
08/02/06	(S)	NGD AT 1:30 PM SENATE FINANCE 532
08/02/06	(S)	-- Meeting Canceled --
08/03/06	(S)	NGD AT 9:00 AM SENATE FINANCE 532
08/03/06	(S)	Failed to Move Out of Committee
08/03/06	(S)	MINUTE(NGD)
08/04/06	(S)	NGD AT 10:00 AM SENATE FINANCE 532

**WITNESS REGISTER**

JIM WHITAKER, Chair  
Alaska Gasline Port Authority;  
Mayor, Fairbanks North Star Borough

PO Box 71267

Fairbanks AK 99707

**POSITION STATEMENT:** Gave Port Authority Presentation.

RADOSLAV SHIPKOFF, Director, Greengate LLC  
Financial Advisor, Alaska Gasline Port Authority  
2001 L Street NW, Suite 901  
Washington DC 20036

**POSITION STATEMENT:** Gave Port Authority Presentation.

BILL WALKER, General Counsel and Project Manager  
Alaska Gasline Port Authority  
411 4th Avenue, Suite 200  
Fairbanks AK 99701

**POSITION STATEMENT:** Commented on Port Authority Presentation.

DONALD SHEPLER

Greenberg Traurig, LLP

Consultant to the Legislative Budget and Audit Committee

Alaska State Capitol

Juneau AK 99801-1182

**POSITION STATEMENT:** Commented on the Port Authority's presentation.

RICK HARPER

Econ One Research, Inc.

Consultant to the Legislative Budget and Audit Committee

Three Allen Center, Suite 2825

333 Clay Street

Houston TX 77002

**POSITION STATEMENT:** Commented on the Port Authority's presentation.

EDWARD J. TWOMEY

Morrison & Foerster LLP

Counsel to the Governor

Washington DC

**POSITION STATEMENT:** Commented on Port Authority issues.

JIM CLARK, Chief Negotiator

Office of the Governor

PO Box 110001

Juneau AK 99811-0001

**POSITION STATEMENT:** Commented on Port Authority issues.

DR. PEDRO VAN MEURS

Consultant to the Governor

Office of the Governor  
PO Box 110001  
Juneau AK 00911-0001

**POSITION STATEMENT:** Commented on the gas pipeline and Port Authority issues.

BILL CORBUS, Commissioner  
Department of Revenue  
PO Box 110400  
Juneau, AK 99811-0400

**POSITION STATEMENT:** Commented on the gas pipeline and SB 3002.

DENNIS BAILEY, Attorney  
Legislative Legal Services  
Legislative Affairs Agency  
Alaska State Capitol  
Juneau AK 99801-1182

**POSITION STATEMENT:** Commented on SB 3002.

ROGER MARKS, Economist  
Department of Revenue  
PO Box 110400  
Juneau AK 99811-0400

**POSITION STATEMENT:** Commented on SB 3002.

#### **ACTION NARRATIVE**

**CHAIR RALPH SEEKINS** called the Senate Special Committee on Natural Gas Development meeting to order at [10:18:51 AM](#). Present at the call to order were Senators Fred Dyson, Bert Stedman, Gary Wilken, Lyda Green, Kim Elton, Donny Olson, Lyman Hoffman, Ben Stevens, Thomas Wagoner and Chair Ralph Seekins; Senators Con Bunde, Al Kookesh, and Thomas Wagoner arrived as the meeting was in progress. Also in attendance were Senator Gary Stevens and Representatives Paul Seaton, Jay Ramras, Kurt Olson, Ralph Samuels, Mark Neuman and Berta Gardner.

#### **Alaska Gasline Port Authority Presentation**

CHAIR SEEKINS announced that the committee would pick up where they left off yesterday with the Port Authority's presentation.

JIM WHITAKER, Chair, Alaska Gasline Port Authority (AGPA), said the overriding mission of the Port Authority was to keep as much of Alaska's natural resource wealth in Alaska as possible. He said that goal is consistent with Alaska's laws and with the legislative mandate that Alaska's constitution requires.

[10:21:43 AM](#)

RADOSLAV SHIPKOFF, Director, Greengate LLC, and Financial Advisor to the Alaska Gasline Port Authority, resumed his analysis contained in the "Presentation to Senate Special Committee on Natural Gas Development - AGPA Project Economics, August 3 - 4, 2006" and recapped that the LNG project was reviewed on a stand-alone basis. It has a net present value (NPV) of \$1.7 billion, an internal rate of return (IRR) of \$27.4 billion and rapidly achieved discounted payback. He reviewed sensitivities using current prices and what the break even Henry Hub price was, which is defined as the price necessary to achieve the minimum required return. He discussed that the LNG proposal offers an additional value to the producers that doesn't exist in the pipeline project and that is the ability to divert gas to the best market available - because it can be put on ships and delivered anywhere in the world.

[10:23:48 AM](#)

He explained that gas is diverted only when the opportunity arises to do so and the real question is how to quantify that possibility and that is what he would talk about next. He said slide 51 was heavy on statistical analysis and he would give them the overview of that analysis, which underpins the conclusion.

MR. SHIPKOFF explained his theory that options exist for values when there is lack of perfect correlation between two variables. Japanese gas prices tend to be very highly correlated with Japanese oil prices, which have to do with contractual formulas contained in their LNG purchase agreements. U.S. gas prices are not very well correlated with its oil prices. This low correlation increases the likelihood the U.S. will have periods when one price is high and the other is low. In Japan, there is no ability to choose between higher or lower. There have been periods when Japanese prices create greater value to a potential LNG supply from Valdez than what Alaska would receive from southern California.

He explained that he used both a straight algebraic approach and a Monte Carlo simulation, which used specialized statistical analysis software that created an expected average value from a large number of scenarios; the resulting graph was on slide 52. Both approaches calculated essentially the same number if the same assumptions are used.

[10:30:10 AM](#)

He said that California gas prices are not closely correlated with oil prices and that creates variability in price, which creates uncertainty. The graph shows that for any price below \$37 per barrel, one would expect to receive more value from Japan than from southern California and conversely for any price above \$37 per barrel, one would expect to receive more value from the U.S. than from Japan. This is only if southern California prices were perfectly correlated with oil, but that is not the case. The graph did not show how much more value the gas would have in Japan, just that it would be more and it would be different at each oil price (graph on slide 53).

[10:33:11 AM](#)

MR. SHIPKOFF reviewed the probability graphs on slides 53 - 58, which showed the higher the U.S. oil price, the lower the value of diverting to Japan is and explained, "So, if we were to have an LNG project today, you would not expect to be diverting to Japan very often." He said the probability distribution of oil prices can be plotted based on historical distribution and over the last five years it has been about \$40.

He said that slide 56 graphed historical observations using the Monte Carlo inputs. The results are almost the same using the straight algebraic approach. He said the intuitive concept behind these analyses is very simple and elaborated:

What we're saying is that the lower prices are, the lower the value is in the U.S. of the net back generated from selling the gas in the U.S. However, you would expect to generate higher value from Japan. The fact that you have the ability to go to Japan as opposed to the U.S., when going to the U.S. does not create much value, gives rise to this extra premium, which could be anywhere from \$0 to \$1.

[10:39:57 AM](#)

SENATOR STEDMAN asked him what kind of volumes he was talking about in playing this "arbitrage game" and how quick he proposed the project could respond in dealing with long-term contracts.

MR. SHIPKOFF replied that he didn't know how much volume would be diverted, but under the loan guarantee, 20 percent could be diverted and if the U.S. has extremely low oil prices, more than 20 percent could be diverted. How much is diverted does not change the analysis. The project is profitable without the ability to divert to Japan. Every project has that ability even

with long-term contracts. They always negotiate diverting cargo; that is why he is putting value on it.

SENATOR STEDMAN said he was struggling with the relevancy of the whole concept in the presentation versus just a casual comment that one might be able to play some pricing arbitrage between two different markets. The fundamental question he had to answer is what project is going to give the best value to the citizens of the State of Alaska - not so much weighing his project substantially heavier because he has the potential of an arbitrage play. He said, "To me, that's almost irrelevant." Showing analysis indicating his project is viable is just one step of many. He asked how that arbitrage information was supposed to help him make his decision.

MR. SHIPKOFF mentioned that first there is the ability to divert, which was ignored before - even though the project is very profitable without it. He said the producers frequently divert LNG. He said the LNG project is not an either/or project and takes nothing away from a potential highway project. "If the project becomes economic; then it becomes a no-brainer. You have to do it."

SENATOR STEDMAN replied:

Not necessarily. Without getting into an argument, clearly there is a decision being made on which project is going to be going forward and which ones aren't. Without recognizing that, clearly that's up to you. But clearly it looks to me like that's what's going on at the table for the last year and a half.

MR. SHIPKOFF replied that the decision should be that any project that creates value for the state and the producers should proceed. So, the highway project should proceed whenever it wants and so should the Port Authority project.

SENATOR BEN STEVENS said that Mr. Shipkoff offers so much, but his project has neither upstream fiscal agreements nor approval from the Federal Energy Regulatory Commission (FERC) - giving the appearance of trying to subvert the FERC. He also took offense at the "no-brainer" comment when everything Mr. Shipkoff presented is hypothetical discussion saying, "I don't think that it is even worthy of our consideration at this table at the point we are [at]."

CHAIR SEEKINS stepped in to say that he wanted an orderly debate and asked speakers to stick to the presentation.

[10:48:53 AM](#)

MAYOR WHITAKER disagreed with Senator Ben Stevens' basic precept that the producers, given a lease agreement and an obligation to produce, should determine what is in the state's best interests.

[10:49:24 AM](#)

MR. SHIPKOFF continued his presentation with slide 59, which shows what happens to upstream profitability if the optional arbitrage value is added. The IRR increases to about 31.9 percent; the NPV goes from \$0.5 billion up to \$2.2 billion. The breakeven prices are also reduced from \$4.30 Mmbtu to \$3.74 Mmbtu. He commented that he had seen comparative projects that were very good at \$3.74.

He then talked about the hypothetical of what happens if the highway project is added to the LNG project assuming it would come on line by 2016 at the earliest and that it is a 4.3 Bcf project. The incremental value of a Y-Line increases significantly for a total of \$13.1 billion, he said and, "The sum of the two is more than the sum of the parts," because both projects together save on the tariff of the shared line. Slide 61 indicated the highway project's netback improves if the LNG project goes first, because its transportation costs are reduced from Prudhoe Bay to Delta Junction. The value to the state increases from \$16.5 billion for a standalone highway project to a total of \$21.8 billion with the LNG project.

[10:52:02 AM](#)

MR. SHIPKOFF said that slides 63 - 71 look at what happens if only Point Thomson gas is used. He assumed the LNG project would get a combination of gas supply from Prudhoe Bay and Point Thomson of 1.2 Bcf for 30 years. Using just Point Thomson, there would be less overall supply and the decline would start sooner; therefore all of the costs would have to be amortized faster. His analyses did not take into account the economics of the liquids and condensates from Point Thomson. He said Slide 64 showed what the netback would look like at the pipeline inlets and spent a few minutes explaining that. He said the returns are very good, but the breakeven price is still somewhat high. He thought a Point Thomson project alone would end up looking very economic if the liquids and condensates were added.

[11:01:07 AM](#)

MR. SHIPKOFF concluded that AGPA's numbers show that an LNG project creates incremental substantial value both for the state and for the producers. He asked the committee if a project creates substantial incremental value for the state and the producers, why aren't the producers doing it. In a textbook financial scenario, a company should do every project that creates positive value, but in reality that is not the case. Companies have capital and resource constraints and regulatory and legal constraints. He explained that using the value maximization strategy, a company would make sure it has the opportunity to develop all the projects that create value. This means that all the projects with an expiration date will be developed first; and Alaska is one of the few jurisdictions that doesn't have an expiration date and that is why he thought it would be developed last.

[11:05:34 AM](#)

MAYOR WHITAKER remarked that it was unfortunate that some committee members weren't at the meeting.

CHAIR SEEKINS explained that some members had to attend a technical session and he said the committee would take a recess.

[11:06:02 AM](#) recess [11:25:03 AM](#)

CHAIR SEEKINS called the meeting back to order at 11:25 am.

MR. SHIPKOFF concluded his presentation saying that he didn't think the producers were serious about any of the projects yet, but they would do both if they could determine they had maximum value.

[11:29:11 AM](#)

BILL WALKER, General Counsel and Project Manager, Alaska Gasline Port Authority (AGPA), stated that it appears the Port Authority is adversarial to the producers, and in some instances they are, but that was not their first choice. He briefly recapped the history of the Port Authority saying was created to benefit the producers and the beginning idea came from an IRS finding on its tax-exempt status for financing an all-Alaska project. The project was presented to the producers and they declined to participate in it; then the Port Authority decided to continue on its own.

[11:30:29 AM](#)

MR. WALKER picked up his presentation saying that AGPA realized it needed assistance on the marketing side and entered into an

agreement with Semptra Energy. Semptra was very excited about the project and offered to participate by investing \$5 billion. However, it withdrew from the AGPA effort following the hostile attitude of the administration towards the all-Alaska gasline project and it is not in an agreement with the Port Authority at this point.

11:31:54 AM

MR. WALKER stated that AGPA submitted an application under the Stranded Gas Act and a few months after it was submitted, the Administration suggested that it withdraw. Since there was no need to negotiate concessions or amend existing tax structure, the Administration proposed that AGPA sign a protocol agreement, which was done [slides 19 - 31].

In the later part of March 2005, he said the Administration requested that AGPA resubmit its Stranded Gas Development Act (SGDA) application, which he did on the final day of the deadline. He was disappointed the next day when he saw the press release from the state saying it was disappointed to receive an application from the Port Authority and that it couldn't bring an application to the legislature this session. He said, "Well, that was most unfortunately - that was never part of the discussion." The president of Semptra was present at the meeting in which the Administration requested that AGPA resubmit its application and he was stunned.

11:34:42 AM

MR. WALKER said that slide 31 listed the eight sister ships owned by BGT that were built by General Dynamics in the late 70s. They are currently in the trade now. Two fleet life-expectancy studies were performed by Lloyd's Register, the most recent one in 2005, giving the ships a life expectancy up to at least 2020 with the older ships having some inefficiencies associated with them. He also said the U.S.-built ships would need to be reflagged, as discussed yesterday, but BGT's legal counsel in Washington, D.C. assured him that it was a congressional process with much fewer obstacles than receiving an exemption from the Jones Act. He said that the maritime unions had offered him their assistance in this process.

11:36:49 AM

SENATOR WAGONER asked how the capacity of ships built in 1978 or 1979 compared to more modern tankers and if there is a difference in the capacity, how would that affect transportation of the LNG.

MR. SHIPKOFF replied that all eight sister ships have identical capacity of 126,300 cubic meters (m<sub>3</sub>). The standard capacity for LNG tankers used to be between 125,000 m<sub>3</sub> and 138,000 m<sub>3</sub>. The Q-flex ships (Qatar-flex) are around 215,000 m<sub>3</sub> and Q-max ships are up to 260,000 m<sub>3</sub>. This trend is not general for all tankers, but rather project specific for Qatar that needs the extra capacity because it is so far away from the Gulf of Mexico - about 9,500 nautical miles. He said it's not a good idea to use Q-max sized tankers, because a reduced number of terminals can accommodate them. Most Japanese and European terminals cannot accommodate them. However, using smaller tankers means one must have more ships to accommodate capacity.

[11:39:49 AM](#)

MR. WALKER said the life expectancy study indicated that the BGT sister ships would go out to 2040 without much difficulty. The question is if the older ships should be used or be replaced with newer ones.

SENATOR STEDMAN asked if AGPA had the first right of refusal or some competitive advantage with BGT when its lease runs out with them.

MR. WALKER replied that they are currently negotiating that issue. BGT is anxious to have its ships in the Alaska trade.

MR. SHIPKOFF added that the charters expire in 2011; and many other suppliers could use them. AGPA does not have an exclusive arrangement with BGT, but they realize having U.S. built ships gives them an advantage. The rates he assumed in the graph take into account what he believes will be the range of values they could attract from other potential charterers and are set slightly above them for Alaska.

MR. WALKER noted that AGPA had received a proposal from Totem Ocean Trailer Express, as well, but it doesn't have any experience shipping LNG. Burma Gas Transport, 75 percent owned by Mitsui O.S.K. Lines, already ships LNG shippers and has experience worldwide.

MR. WALKER's slides 37 and 40 showed 16 North American LNG facilities on the West Coast that are in various stages of application that have the potential of receiving Alaska's gas. Most have contacted AGPA favorably about receiving Alaska gas and he is working with those that are closest to receiving their permits. The first one is Kitimat LNG Inc. in British Columbia, a 2.1-day sailing from Valdez. Sempra Energy has received its

permit and it is furthest south on the Baja Peninsula. He estimated that three of four facilities would be permitted on the West Coast.

[11:46:35 AM](#)

He said that slide 38 was from the California Energy Commission and listed the receiving terminals on the West Coast; slide 39 was a picture of the Sempra terminal 1.5 Bcfd expansion.

MR. WALKER said the initial LNG supply opportunity for Sempra was obtained by BP and Shell at 50 percent each.

MR. SHIPKOFF added that BP's 50 percent is held by Sempra.

MR. WALKER said that Kitimat just signed agreements with the First Nations and has received all, but one, of its environmental permits from British Columbia.

[11:51:22 AM](#)

SENATOR HOFFMAN asked how long it takes a ship to get from Valdez to Japan.

MR. SHIPKOFF replied about seven days for 3,500 nautical miles.

[11:52:06 AM](#)

MR. WALKER said when the \$18 billion loan guarantee was put in the 2004 energy bill, he found that the Port Authority was not part of it. He went to Washington, D.C. and with the help of Senator Ted Stevens, he got it added before it passed.

[11:53:50 AM](#)

CHAIR SEEKINS asked what hurdles one must get over to qualify for a loan guarantee.

MR. WALKER replied that one has to first go through the FERC process.

MR. SHIPKOFF added the specifics of obtaining the guarantee has not been set yet by the DOE, but essentially you would have to convince them to lend you the money.

CHAIR SEEKINS asked if one would have to go through an open season to get long-term shipping commitments to show a balance sheet to get a loan guarantee - in essence showing that you don't really need it.

MR. SHIPKOFF replied yes, that is what the process is all about.

CHAIR SEEKINS asked if he could get a guarantee without shipping commitments.

MR. SHIPKOFF replied no, a reasonable probability that supply is there must be present.

CHAIR SEEKINS asked if he could contractually arrange who would ship through AGPA's pipe.

MR. SHIPKOFF replied that was a possibility.

CHAIR SEEKINS asked how that would work.

MR. SHIPKOFF explained the rationale behind an open season was to ensure fairness that all possible producers would supply gas into it. The Port Authority could determine it wants to have an open season even though it's not required to.

CHAIR SEEKINS asked if he is actively negotiating with DOE to determine what the qualifications might be.

REPRESENTATIVE SAMUELS interrupted to say the Legislative Budget and Audit Committee, the Administration, the producers and Anadarko specifically petitioned the secretary of DOE to not set the rules up yet - until what mechanisms will be needed for what projects are known.

[12:01:33 PM](#)

MAYOR WHITAKER said that was consistent with the communication he has had with DOE, as well.

[12:01:37 PM](#)

SENATOR STEDMAN asked how he could was going to get certificates of public convenience and necessity if FERC is not going to regulate his project.

MR. WALKER replied that was the purpose of the meeting he had with the DOE's general counsel. Their response was if you're FERC exempt, you present your project to the DOE. He reasoned:

You know, we're not looking at picking a battle with any regulatory agency. We're looking at doing a project. Would we continue to have communications with FERC? Of course we would. We're not going to just ignore them. But our read of the law, and many of them agree, that under the definition and the description

that we have laid out, we are FERC exempt. And if that's going to save us a couple of years, that means a lot based on the way we see the marketplace.

SENATOR STEDMAN said that would be a good question for the FERC attorneys.

12:03:40 PM

MR. WALKER said next issue is YPC permits and data and there is an entire warehouse of data in Anchorage. AGPA became committed to it when it wired \$1 million for them in 2004 and since then AGPA has taken over the responsibility of maintaining them. To determine their value, he said that Bechtel Corporation looked at them and said there was significant value. Therefore, they proceeded to put in their 55,000 man-hours of work without payment from AGPA. The law firm of O'Melveny & Myers LLP did the same thing and was comfortable with the permits. Sempra Energy did a very significant due diligence on the permits before entering into an agreement with the Port Authority. The permits are current, but they need to be modified. He is comfortable that the package has great value.

12:06:52 PM

He said they have a 25-year export license that may or may not be of significant value depending on whether gas gets shipped to Japan [slide 44]. The Coastal Zone Contingency process took a year and it found TAGS Phase 1 was consistent with the standards of the Alaska Coastal Management Program and the North Slope Borough and City of Valdez coastal management programs. The EIS served as the National Environmental Policy Act compliance document on which all federal agencies based their permit application decisions. In it the agencies adopted a unique "tiered" permitting process.

12:07:44 PM

He said that the Ahtna Corporation [slide 45] right of way (ROW) agreement grants YPC the right to designate and acquire easements, rights of way and other similar agreements for access across lands for purposes that include gravel rights for a natural gas pipeline and associated facilities across Ahtna Native lands.

MR. WALKER said they have both federal and state rights of way for a gasline and related facilities. He reported that AGPA has a conditional ROW lease for 21 months that contains the text and stipulations of the final ROW lease that become effective when the conditional ROW lease requirements are met. It addresses the

pipeline on state lands from the North Slope to Anderson Bay within the TAPS corridor in a manner consistent with the federal ROW grant.

MR. WALKER said the DOE and OFE authorized YPC to export up to 14 million metric tons of LNG annually for 25 years to Japan, South Korea and Taiwan, and limited FERC's jurisdiction on the place of export sites to Anderson Bay. He said that FERC Order 350 is exempt. He report that the final EIS on the Anderson Bay site fulfilled the National Environmental Protection Act administrative review requirements and allowed FERC to issue place of export authorization.

MR. WALKER said the air quality permits go for eight years. Getting the data collected for it was critical because it was needed to amend the permit.

He reminded them that ANGDA recently received its conditional right-of-way lease from Glennallen to Palmer, but that the Port Authority has no rights to it. He applauded them for doing what they are doing saying it is very compatible with the Port Authority project. "Again, we sort of look at ANGDA as a related organization - not legally related, but similar goals and missions."

He said that slide 48 was a project timeline prepared by Bechtel, if the Port Authority had gas tomorrow, which it doesn't. It indicated a six-year process that was driven by a two-year modification of permits and financing phase followed by a four-year construction phase. He said an additional year might be needed for construction of the tanks in Valdez.

[12:13:06 PM](#)

MR. WALKER said that gas acquisition strategy is the core of the Port Authority's issues. He was relying on the fact that an Alaska gas project is reasonably profitable and that the producers have a duty to go forward with it. Furthermore, he stood by the beliefs stated by Spencer Hosie Esq., legal counsel to the LB&A Committee, that it is not the state's obligation to go head-to-head with international projects and give concessions until a project becomes economical. The law is clear that the producers cannot warehouse hydrocarbons merely because it makes sense from their perspective.

He related that he has had many meetings with ConocoPhillips, Exxon, and BP offering to move their gas through their tax-exempt structure. When those were not successful, AGPA filed an

anti-trust suit, which is on-going. He said that state administration's enforcement of the terms of the leases is really important and elaborated:

We follow closely the Point Thomson issue. We think that is a wonderful opportunity for Alaska to finally get its gas to market - 8 Tcf of proved reserves in Point Thomson, the largest undeveloped gas field in North America. So, we think that's in default currently and we think it's appropriate that that be made available to this project. What we've looked at is gas from Point Thomson and the state's royalty gas out of Prudhoe Bay combined is very close to what we need for this project. So, we're very interested in Point Thomson. We're not saying take Point Thomson back and make it available to us; that's not what we're saying - make it available to a project that's ready to go.

If the state terminated those leases and we should look at the legal steps necessary to do that - rather than giving up 87.5 percent of something that you know is there, the state may look at it a little differently and look at some of the other countries that have retained a greater role and have somebody else come in and be the operator of it without giving away significant amounts. So, there actually may be an upside on that.

MR. WALKER said he hadn't figured the upside on removal of the liquids from Point Thomson, which would be another significant amount. He said that bringing the liquids out without the gas is problematic as far as reinjecting the gas back in at Point Thomson, but the AGPA project would be happy to take the gases.

[12:14:36 PM](#)

He said that slide 50 showed competition around the world to bring gas into the United States. The point of the slide is to say that the hottest market on the planet right now is the Lower 48.

MR. WALKER remarked that, "We sort of describe our gas in Alaska as milk with no expiration date, because it never quite gets to the front of the counter, because there is really no downside to delay that." Development of other projects is why he is in a hurry - everybody is trying to their gas into the U.S.; approximately 15 sites are seeking permits. Other slides he

presented (from a Cheniere presentation) showed gas transmission systems in the United States as well as targeted gas demand projections.

SENATOR DYSON interrupted to ask if the committee was going to take a break because he had some questions.

CHAIR SEEKINS responded that the committee would break after a few more slides from Mr. Walker. He would take questions when it reconvenes at 1:30.

[12:20:03 PM](#)

MR. WALKER referenced an Anchorage Daily News article by Wesley Lori that supported AGPA's concern that the Lower 48 could be in LNG gas balance by 2012 and that Alaska's gas is projected to get there by 2016 to 2020. He said that BP, ExxonMobil and ConocoPhillips are all planning other projects in the Lower 48. He had a quote from Lee Raymond, CEO of Exxon, that said, "There isn't going to be an Alaskan gas pipeline before there is a Canadian gas pipeline." Another quote from Jim Mulva, CEO of ConocoPhillips, that said basically the same thing.

[12:21:38 PM](#)

MR. WALKER stated that AGPA believes that TransCanada's permits are good, but he thought that was somewhat ignored in the contract and litigation about how Canada would participate in the construction of a pipeline could be a potential delay. He opined that TransCanada holds valid property rights to build and own the Canadian section of the project and Alaska has no option but to defend those rights on behalf of Canadian shareholders.

[12:23:19 PM](#)

He said that AGPA was also concerned about the impact on the wellhead value if the liquids were taken off in Alberta. He also said that an off-take at Delta Junction does not work for their scenario.

[12:26:12 PM](#)

MR. WALKER summarized his presentation saying that AGPA is concerned about Alaska being shut out of North American markets. He is not sure what the impact of the Alberta tar sands would be; for one thing, some of the same companies own gas at Prudhoe Bay. Other concerns included: any concessions on the Canadian portion of the project (65 - 80 percent) will be deducted from the wellhead value, that the 30 - 40 year contract didn't actually guarantee a pipeline would get built, loss of the state's ability to manage its resources, and loss of state

sovereignty in the development of its gas and oil. He finished with a slide labeled "Comparative Benefits to Alaska of Proposed Projects" and reiterated that AGPA's biggest challenge is that it doesn't have gas commitments.

The committee took an at-ease from [12:30:27 PM](#) to [1:51:12 PM](#).

CHAIR SEEKINS called the meeting back to order at 1:51.

MAYOR WHITAKER said AGPA's presentation had been completed and they would answer questions. He pointed out that they consider themselves to be a collaborative and cooperative project along with the highway project.

[1:51:51 PM](#)

SENATOR WILKEN said one of the things that make the project unique is its tax exemption from the federal government. He asked Mr. Shipkoff to explain how that plays out in his calculations.

MR. SHIPKOFF answered that the economics he presented today don't include tax exemption benefits. The reason is because it is not a constant value and depends on a lot of assumptions. Whenever they have shown a project that includes the tax exemption benefit, they have been challenged - either the magnitude of it or whether they are tax exempt for real. They wanted to take the issue off the table; and the project works without it. He pointed out that the original objective of the Port Authority was to help improve producer economics.

[1:55:17 PM](#)

SENATOR WILKEN brought attention to a particularly good Anchorage Daily News article that challenged the Port Authority to come forward with five specific areas for the LNG project to respond to if it is truly a viable alternative to the Highway gas line; and opined if it isn't a viable alternative, "Let's end the distraction." He asked Mr. Walker to respond to the questions in a public manner.

[1:57:49 PM](#)

MR. WALKER replied that he didn't carry the ADN editorials with him and that he would answer the questions one at a time.

SENATOR WILKEN said the first is what the project is today, the second, is what AGPA's market is for West Coast gas, third, its financing design and commitments on ships, fourth what are all of its Memorandums of Understanding, both in place and being

negotiated, and fifth, the meaning of the IRS exemption to the project.

CHAIR SEEKINS asking if he wanted a response here or in the Anchorage Daily News.

SENATOR WILKEN replied if he were doing it, he would write a letter to the editor of the AND or as a compass piece.

[1:59:28 PM](#)

MAYOR WHITAKER responded that the questions are fair and reasonable and the Port Authority was prepared to respond. He thought all of the questions had already been addressed during the course of the committee's deliberations and considerations.

CHAIR SEEKINS said he also thought the presentation had addressed them.

[2:00:26 PM](#)

SENATOR DYSON said his packet doesn't have some of slides being discussed. One of his slides had the potential and plans to bring gas from the Gulf Coast to the Great Lakes, which he saw as a major challenge to the Highway project. He asked what the timeline was for that project and where they were on it.

MR. WALKER replied that AGPA hadn't seen an exact timeline, but it the project appears to be aggressively getting the permits for the re-gas terminals on the Gulf Coast to make that plan work.

MR. SHIPKOFF said that some information is not publicly available, but currently, at least six projects are going into the Gulf that will almost certainly start delivering gas between 2009 and 2012. Another 4 Bcf project could come in by 2012 or 2014 with something pretty close to certainty. You can count on 9 to 10 Bcf coming to the Gulf, which is well connected to the Midwest and Northeast. In addition, a new pipeline proposal will come in from the Colorado Rockies to the Midwest, an additional 2 Bcf. He said there is a lot of competition for the U.S. market.

SENATOR DYSON asked if it's right to assume that the existing pipelines from Gulf Coast to the Great Lakes don't have enough spare capacity to handle another 4 Bcf.

MR. SHIPKOFF answered that he didn't have the precise figures on spare capacity, but he could follow up on that adding that those projects have either obtained financing or are very close to it.

[2:04:59 PM](#)

SENATOR DYSON asked if they were thinking of bring AGPA's gas into Kitimat in Canada.

MR. SHIPKOFF replied that they also have the southern California option available, but if Alaska continues to wait, that option may go away. The reason their base case numbers assumed the gas would go to southern California is because it is of better value and that option is still available.

SENATOR DYSON asked him to explain why Kitimat might not be available.

MR. SHIPKOFF replied that it is available, but southern California is a better value today.

SENATOR DYSON said he was just in Edmonton and Calgary and talked to most of the Canadian players there. Those folks had no knowledge of the Port Authority making contact with the industry there. He asked if he just didn't talk to the right people.

MR. WALKER responded that they met with the chairman of the board, the president and all the officers of Kitimat LNG. He has an MOU with them.

SENATOR DYSON said that Kitimat has a 30-inch crude export line with a 20-inch dilutant import line and asked if there is no available gasline space between Kitimat and the Alberta Hub at this time.

MR. WALKER replied there is not sufficient room and they realize that. That is why Kitimat has entered into a joint venture with Pacific Northern Gas (PNG) to expand the existing line.

[2:08:15 PM](#)

SENATOR DYSON said he attended some seminars that talk about compressed natural gas (CNG) as opposed to LNG transport for short distances and asked if he took gas to Kitimat would it be short enough for him to consider doing CNG as opposed to LNG.

MR. WALKER replied that they looked into that and CNG makes a lot of sense for short runs, but it's right at the limit of what makes sense for the AGPA. The problem is that CNG is highly

compressed and it doesn't go through liquifaction and the cost of CNG vessels is significantly higher. Also, AGPA wanted the flexibility of going longer distances.

SENATOR DYSON asked if he said CNG vessels were more expensive than LNG.

MR. WALKER replied that was the estimate they gave. He elaborated they would need the larger size for coastal Alaska.

[2:09:45 PM](#)

SENATOR DYSON said his information on the cost of using CNG vessels was different than the information Mr. Walker has.

MR. SHIPKOFF clarified that his figures were based on per unit transported. The CNG boats are smaller, but they are a better option for smaller projects. So, the relative cost per unit transported is higher - even though in absolute terms they may be cheaper.

CHAIR SEEKINS noted there were no further questions and thanked the Port Authority presenters.

[2:10:51 PM](#)

CHAIR SEEKINS welcomed Mr. Shepler and Mr. Harper, legislative consultants, and asked if they had any comments at this point.

MR. SHEPLER, Greenberg & Traurig, and RICK HARPER, Econ One Research, Inc., introduced themselves as consultants to the legislature on gasline matters.

MR. SHEPLER began his comments by referring to a handout he'd provided and the FERC exemption issue. He summarized that the Port Authority was making this claim was under the Natural Gas Act (NGA). He said four different sections of the definitional terms apply to the NGA and stated, "It is my view that as a technical legal matter, the Port Authority's assertion of being exempt as a municipality finds support in the FERC case law and the statute."

Having said that, Mr. Shepler noted that only a handful of cases interpreting the municipality exception had been decided by the Commission and none of them were near the magnitude of the project that the Port Authority is talking about. Secondly, he said that while they have a credible legal claim, they do not have any official declaratory order from the FERC that would confirm that status - even though that is not a requirement. He

thought there might be some value in obtaining one to assure that standard is satisfied.

2:14:40 PM

MR. SHEPLER explained that the Natural Gas Act (NGA) applies to persons (page 1 of the handout). "Person" is defined to include a corporation; corporation is in turn defined to exclude municipalities. A "municipality" is defined by the statute to mean "a city, county or other political subdivision or agency of the State". He said the Port Authority is chartered under the Alaska Port Authority Act and it would appear to be a municipality or other political subdivision or agency of a state government.

He also cited 7(c)(1) of the NGA that talks about who needs to obtain a certificate of public convenience and necessity for any project that involves a transportation or sale of natural gas in interstate commerce.

MR. SHEPLER said the term "municipality" has been construed by the FERC in less than a dozen cases and for the first time in 1988 by a northwest Alabama gas district, which was basically a collection of communities that bought gas for resale to their citizens and engaged in some limited transportation of gas across their systems. The commission determined that because it was organized by several municipalities under a statute, there was a public purpose that was being served and that gas district would be exempt under the statute. In another case, the FERC was needed to regulate so-called regulatory gap. Another case involved one pipeline company bypassing another in order to serve the city of Decater, Alabama, utilities. FERC found that they had no discretion in the area and there was no need for them to try to infer what Congress intended.

2:17:28 PM

He said the last notable case is the most recent in 2004 and involved a piece of pipe connecting an LNG import terminal to the southern California Gas Company distribution system. It was significant between the FERC and the State of California over who had authority over the citing of import terminals. FERC originally said a 2 to 3-mile section of LNG pipe needed to file a certificate. That middle segment was owned by the City of Long Beach, California, and on rehearing, the Commission acknowledged that the City of Long Beach was a municipality and no certificate was required. The significance of this case is that it was a middle segment, a connector pipe between the import

facility and the further downstream activities as opposed to being on the delivery end of the transaction.

MR. SHEPLER said that based on those cases and a handful of others, he had to acknowledge that there is a credible legal claim, but 2.3 miles of pipeline at the end of an LNG terminal is not an 800-mile pipeline from the North Slope. There is a question of scale and scope as to whether the Decatur decision would be controlling on this project. He thought it was significant that the Port Authority did not have a declaratory order confirming its status and that it has said it doesn't intend to get one.

He said the Port Authority believes it has a FERC exemption, but it has a slightly different business model than the committee is used to in dealing with the FERC-regulated environment. For instance, FERC rules prohibit the owner of the pipeline from owning the gas in the pipeline and the Port Authority is initially proposing to actually buy the gas at the North Slope and then resell it as LNG as it comes out of the LNG terminal.

[2:22:09 PM](#)

MR. SHEPLER said that once the gas becomes LNG and is destined to leave the Port of Valdez, if it heads towards Canada in a highway route project, it is back in the realm of FERC jurisdiction. The entity that's buying the LNG and causing it to be delivered to a port in California or B.C. would need a certificate to either transport natural gas in interstate commerce between Alaska and California or to export natural gas either to Canada or Mexico. So, the downstream transaction away from the LNG terminal at Delta Junction, if it occurs, will be subject to normal FERC certificate requirements.

[2:23:45 PM](#)

MR. HARPER said that he didn't have a presentation, but he had been helping members to fully understand the presentation.

[2:24:13 PM](#)

REPRESENTATIVE RALPH SAMUELS asked Mr. Shepler to clarify that upstream from Delta Junction the pipeline is not regulated by FERC, but from Delta Junction south, it will be FERC regulated.

MR. SHEPLER responded that under the Port Authority proposal, the pipeline would be FERC-exempt, arguably because it is a municipality. The exempt line would be regulated by the Regulatory Commission of Alaska (RCA); a FERC-regulated line

would start from the exempt line under the Governor's proposed contract.

REPRESENTATIVE SAMUELS asked if the pipeline would be RCA-regulated before Delta Junction, FERC-regulated after Delta to the Alaska/Canadian border where it would become NEB-regulated and then wherever it crosses the border south of Alberta to Chicago it would become FERC-regulated again.

MR. SHEPLER replied that essentially he thought that was right. He said the issue has come up as to how far upstream would the FERC regulation extend - even in the context of the producer proposal. It's been said the parties certainly expect the FERC to regulate the gas treatment plant (GTP); however he said that would not be the case if the GTP is owned by the Port Authority. The upstream feeder lines to the GTP would appear to be FERC-regulated in the context of a producer-owned pipeline as well as a Port Authority context because it has not said it plans to own anything upstream from the GTP.

[2:26:27 PM](#)

SENATOR BEN STEVENS said confusion has recently come up over the mechanism to settle the basin control issue and who is regulating what entity.

MR. SHEPLER agreed, but thought that at some point it would become clear who would regulate what entity.

SENATOR BEN STEVENS asked if the Port Authority owned the GTP would it be FERC-regulated.

MR. SHEPLER clarified that anything the Port Authority owned wouldn't be FERC regulated - in its view - because of its status as a municipality.

[2:28:47 PM](#)

SENATOR BEN STEVENS asked if one can go from an interstate commerce FERC-regulated facility, into a state-regulated facility and then back out into an interstate-regulated facility.

MR. SHEPLER answered that that is unprecedented; but at least initially, based on statute, there appears to be a credible legal argument for it. "How that gets sorted out, I don't know and it would depend on how they structure all their commercial arrangements."

[2:30:04 PM](#)

CHAIR SEEKINS asked:

I got eight lanes, two of them are going to Valdez and six of them are going south across Canada. So because two of them are instate, the whole section that would be transporting all eight lanes might not be FERC-regulated?

MR. SHEPLER answered that it appears to turn on the issue of ownership. "If the Port Authority owns the eight lanes and the Port Authority is a municipality, then everything that they own would be exempt."

CHAIR SEEKINS summarized, "So, we just don't know."

MR. SHEPLER agreed with that.

CHAIR SEEKINS said by definition, the Port Authority is a municipality and so it appears it is exempt.

MR. SHEPLER agreed.

[2:31:17 PM](#) at ease [2:36:11 PM](#).

CHAIR SEEKINS called the committee back to order at 2:36.

EDWARD J. TWOMEY, Morrison & Foerster, Counsel to the Governor, came forward with Dr. Pedro van Meurs. He had worked closely with Bob Loeffler over the years and was a "long-term FERC aficionado." His legal career started with the TAPS rate case in 1977. He said it is interesting to hear the argument on the FERC jurisdictional matter, because he recalled vividly just before TAPS started up in June of 1977, when some of the eight oil companies that owned portions of the trans-Alaska pipeline floated a trial balloon jurisdictional issue saying that perhaps the Interstate Commerce Commission, which then regulated TAPS, did not have jurisdiction because it wasn't interstate commerce. The reason they said that was because when the oil left Valdez, it went into international waters and that broke the chain of interstate commerce. That argument was floated and dropped pretty quickly because of what was mentioned a few minutes ago - the size of the project and the idea that the biggest crude oil pipeline in the United States was not going to be federally regulated just didn't sit well.

MR. TWOMEY said he thought about that with regard to the Port Authority project. It seems that it would be very hard to take a line of that size and say that FERC doesn't have regulation over it. More particularly, he had some specific points. One is, as Mr. Shepler said, you could make an argument that a municipality isn't subject to the Natural Gas Act, but there are a few cases where FERC decided the other way and he thought it would ultimately find this project jurisdictional.

He explained that FERC would look at the overriding activity and what is being done as a municipality. He used an example of the California Energy crisis five years ago where both investor-owned utilities and municipality-owned utilities were selling into and buying out of the so-called California ISO and the PX markets. Those are short-term markets and the source of all the Enron discussions. FERC launched a major investigation into the sales into and buys out of the ISO and PX called the California Refund Proceeding and ultimately FERC found that a lot of utilities had overcharged and owed money. A lot of them were municipal utilities, but they said:

Hey wait a minute, you don't have jurisdiction over me. I'm a muni and under the Federal Power Act, just like the Natural Gas Act, 'munis' are exempt. And FERC says, 'No.' The ISO is a FERC jurisdictional facility and you chose, you voluntarily chose, to do business under the FERC rules. Therefore you are subject to our jurisdiction.

He said this case and several others related to it are on appeal and the jurisdiction issue is in front of the Ninth Circuit. He had just heard, however, that one of the cases just ruled that "munis" were subject to FERC jurisdiction.

MR. TWOMEY gave another example of a municipality in one of the southwest border-states that decided to take its line and extend it into the adjacent state, New Mexico. FERC came after it and said it was interstate commerce. They said no. FERC said they chose to build an interstate pipeline, therefore it was subject to FERC jurisdiction. He opined:

Now, I think there's a good chance what FERC will do is look at this Port Authority project as was described yesterday and today and say that is a continuous voyage, if you will, in interstate commerce, much like TAPS and the fact that you are a 'muni' you're still engaging in a voyage in interstate

commerce and the fact that you happen to be selling at Valdez, I would presume they're selling just north of the LNG terminal, the fact that you're selling there is no excuse for us not regulating this whole continuous journey. That, I think, is probably the argument you probably will see from FERC.

MR. TWOMEY read a quotation from Mr. Robert Cupina, one of the FERC officials who testified before the committee last week, taken from the September 2005 Petroleum News.

But the Alaska Gas Port Authority project is different - quote - and this is from Rob Cupina: 'Both the line and the terminal are for interstate commerce and therefore, they would both need a certificate.' - unquote.

He said the idea of no FERC regulation is going to be a slam-dunk for the Port Authority. FERC doesn't shy away from jurisdictional issues. He also cleared up a little confusion on Senator Seekins' six and eight-lane highway example assuming the highway project goes forward tomorrow and is an eight-lane highway - two lanes are reserved for intrastate service that gets off at Delta and goes all the way down. He stated:

There is no question under that fact circumstance, that the line from Prudhoe Bay down to Delta is FERC-regulated including the two lanes of the highway. I don't think anybody would question that. When there's co-mingling of inter and intra state, FERC is going to set the tariff from Prudhoe down to Delta. The RCA will set the tariff from Delta down to Valdez or wherever. There is no question that is a 100-percent certainty.

Now what we have here from the Port Authority is a little play on that - a reversal of it. That is, they're saying that they're going to own this eight-lane pipeline down to Delta. They're only going to use two of those lanes for X-number of years and the idea that after those X-number of years and the other six lanes get filled up, the idea that that would preclude FERC-jurisdiction, which is now the exact fact situation of the line initially being built by the producers, the idea that, the fact that, the Port Authority got there and reserved two lanes to begin with and happen to own an eight-lane highway that then

becomes used, six lanes of which for interstate commerce, I cannot conceive of FERC not coming in and taking control.

2:43:51 PM

CHAIR SEEKINS thanked Mr. Twomey for his testimony and invited Mr. Clark to testify.

2:44:06 PM

JIM CLARK, Chief Negotiator, Office of the Governor, said it was important for this dialogue to continue. In that regard, he sent the mayor of Fairbanks a letter suggesting a roundtable discussion next week with the Port Authority that the public could attend.

CHAIR SEEKINS offered to help facilitate it.

MR. CLARK thanked him and emphasized again how helpful he felt the roundtable discussions were.

2:46:39 PM

MR. CLARK said the Governor asked him to emphasize a point that he feels gets lost in the shuffle - that when the main line is built, there will be an open season and with that will come an opportunity for an off-take line to Valdez.

It's just a question of coming during the open season, bidding "ft" for a portion of the gas. Remember, we've said that for purposes of instate use, we are prepared to make Alaska's share, the 900 Mcf/d available for projects that we think are needed in-state. And obviously, our priority right now is looking at an off-take in Fairbanks to help gasify that community. We think that could really lower homeowners' costs in Fairbanks. With respect to getting gas to Kenai, that is a very, very high priority of the Governor's in order to find a way to keep the Agrium and LNG plant down there open. And an off-take to Valdez to allow this project to go forward on a smaller LNG project is something that is really open here and that we would assist.

But the place where we seem to not be able to connect with our friends from AGPA is on the notion of doing the line to Valdez to the exclusion of or first or instead of doing the project that we have in mind. I wanted to just preface the remarks from Roger and

Pedro to say we're not antagonistic to what they're trying to do; we just don't believe it can be done the way they want to do it. With that, Mr. Chairman, our presentation will come from Pedro and Roger who have spent quite a bit of time working on this. And thank you, again, for having these roundtables.

[2:48:55 PM](#)

DR. PEDRO VAN MEURS gave a slide presentation with accompanying handout. He said when he interacted with the Port Authority, the concept was precisely as he illustrated - to see whether there is some way, through beneficial taxation methods and through the help of the communities in Alaska, that maybe a producer project could be made more attractive. That was so important at that point in time when the Stranded Gas Act was passed in the hopes that the LNG project to Asia would succeed - and that project, then, fell apart. The project to Alberta by the producers didn't exist, yet.

He emphasized that in the year 2000, the Port Authority was the only project that Alaska had and it was important to realize that Alaskans kept the flame alive of trying to find innovative ways to make export of Alaska gas possible at that time. That is where his comments are coming from.

[2:51:22 PM](#)

DR. VAN MEURS said he would first comment on slides 2 - 5 on "Tax Comments". He explained that the source of the Port Authority's initial inspiration was finding out it had a tax exemption. The slide indicated that the U.S. federal government would receive almost \$50 billion in tax revenues on the upstream and \$2 billion in the mid-stream - federal taxation is a very big slice and therefore, trying to think creatively as to what can be done to minimize these taxes and maximize the possibility that the project goes forward is all very helpful. This is where he started working with the Port Authority six or seven years ago.

DR. VAN MEURS said the Stranded Gas contract took inspiration from the work that was done at that time and it includes a 20-percent participation by the State of Alaska, which results in a federal income tax savings of \$.5 billion. Hypothetically, if the state owned 100 percent of the pipeline system in Alaska, he estimated the total tax savings would be about \$2.5 billion. This doesn't make or break the project, but it demonstrates how important these tax matters are. For the Port Authority to come up with creative ideas on how its tax-exempt status could be

used to push an Alaskan project forward should be recognized as a good idea by Alaskans.

2:55:16 PM

DR. VAN MEURS said a reference was made to his "Aide Memoir" to the Port Authority in which he reiterated that he believed reducing taxes is very important in finding a commercial project along with finding a way of lowering the overall cost by finding a cooperative configuration with other parties so that the project can proceed. Conditions need to be created where this tax exemption can be effectively used for the project.

2:56:27 PM

DR. VAN MEURS said he enjoyed the Port Authority's analysis of the North American gas markets. It showed excellently something that he had been trying to impress on the legislature - the extreme volatility and risk of the North American gas market where gas price one day could be 60 percent of crude oil on a Btu equivalent basis and the next day it could be 100 percent. Just recently, there wasn't even a day when the gas prices were only 50 percent of the equivalent of crude prices. He showed his slide 6 labeled, "High Risk Nature of the Project." He also emphasized that the cost estimates made in 2001 have escalated enormously over the last five years. This is why the stranded gas contract and the related fiscal stability are so important.

2:58:38 PM

He said the Port Authority's presentation illustrated that the project to Alberta greatly benefits its project and he was somewhat surprised about its opposition to the stranded gas contract.

3:00:11 PM

SENATOR ELTON recalled that the Port Authority didn't say it opposed the other project, but that its project enhanced it.

DR. VAN MEURS supposed that perhaps he read about the Port Authority's opposition through the press, but he did think their remarks today were positive about the two projects. However, he wanted to comment on their timeline that claims their project can deliver first gas in 2012 if it starts by January 1, 2006. The sponsor plan provides for first gas in 2016 and has a starting date of January 1, 2007. If a correction is made for those two starting dates, it is fair to say that there seems to be only a three-year difference rather than four between the two timelines [slide 8].

[3:02:19 PM](#)

DR. VAN MEURS showed slides 9 - 10 where the Port Authority suggests that the gas treatment plant (GTP) would be constructed by the producers, but that they would be willing to do it themselves, if necessary. He said the main function of a GTP is to eliminate the carbon dioxide from the gas and it's important to realize that the CO<sub>2</sub> can't be released into the atmosphere; it must be reinjected. It can only be reinjected into existing oil and gas reservoirs. Consequently, it is imminently logical that the GTP would be a facility that would be operated and constructed by the producers, because it has to interact with the removal of the CO<sub>2</sub> and its re-injection. So, in his mind, the Port Authority project depends on the GTP being constructed by the producers. It also needs to be stated that it's not the same GTP they are talking about now but one that is more costly, because all the CO<sub>2</sub> would have to be removed in order to meet LNG specifications.

[3:04:14 PM](#)

DR. VAN MEURS said the producers provided a very detailed timeline (slides 11 -12). It indicated that the engineering and FERC permitting would take about four years. In their timeline they contemplate that the GTP certificate would actually be granted by January 2011. So, he found it difficult to see, if one assumes that the FERC certificate for the GTP would be granted in January 2011 and if the Port Authority contract illustrates that you need four years for construction, how there could be a startup date of 2013.

Alternatively, he said, the Port Authority said they could build the GTP themselves. But he found it difficult to believe it would be able to do all the project engineering, have the open season, do the regulatory processes, prepare somehow with the producers for the injection of CO<sub>2</sub> or acquire their own leases for the injection of CO<sub>2</sub> and then negotiate the financing in two years to meet the deadline - assuming it started in 2007. It is more likely that first gas would be achieved by 2015 or 2016.

[3:06:44 PM](#)

DR. VAN MEURS discussed slide 13 "Gas Sales in California" next and remarked that the Port Authority had very good information on the California market, various alternatives and competitors. However, he missed really conclusive evidence that they would be able to offer the lowest price in California compared to other LNG exporters. He saw good evidence that transportation distances from other sources were much longer, but he remained of the view that most of the LNG export facilities in the

Pacific are on tidewater, like Australia, Indonesia, Malaysia, and Brunei. Sakhalin's facility is connected to a short pipeline on Sakhalin Island. He said that all these countries have LNG expansion plants on their way and most of the projects relate to fields that have relatively low production costs. He agreed with Mr. Shipkoff, that if Alaska had its own LNG facility in Valdez and if there is more demand, it is not so difficult to put in another train, but it is also easy for all of our competitors, who are already in business [slides 14 - 15]. Just to get to tidewater, Alaska needs a \$5.3 billion pipeline, plus a GTP aimed at removing all the CO<sub>2</sub>. Given these conditions, it seems that it would extremely difficult for the Port Authority to undercut possible prices of their competitors.

[3:09:31 PM](#)

SENATOR DYSON said he raised the same question and the answer he got was that gas tankered to California wouldn't need to undercut. He got the impression it's not a spot market for every ship that pulls up to sell its gas.

DR. VAN MEURS agreed saying:

The situation is this. Gas is bought by buyers and buyers always want the best deal. Consequently, it is not automatic that a buyer has to pay, say, a so-called price. No, on large contracts buyers, whether they are electric facilities or if there are other gas distribution systems, always try to negotiate the best possible price. Consequently, if you have to go head to head with other suppliers, it is very important to have the latitude that if things get bad, that you can fight off your competitors.

So, consequently...there is no regulated price. There is a free market and in a free market, buyers have the right to acquire the lowest cost gas. And so, consequently, how the California market will evolve over the years is difficult to see. But we have a free market and marketers buy the lowest-cost gas. And therefore I have some concern if you make all these investments and if you have to pay all of these tariffs, that you will be in a somewhat difficult position to effectively compete.

[3:12:23 PM](#)

DR. VAN MEURS paraphrased slide 16 - Gas Sales in California - saying the Port Authority claimed one of the benefits of its

project is that it would diversify Alaska's access to the East Coast as well as the West Coast markets and he took some issue with that. He said the great advantage of bringing gas to the Alberta Hub is that it actually has access to both the East Coast and the West Coast. The benefit of trying to get the highest price for Alaska gas either in the West Coast or the East Coast markets is possible with the Alberta Hub, depending on pipeline constraints.

[3:13:32 PM](#)

DR. VAN MEURS showed slides 17 - 18 - Financing of the Project - saying that in his mind more fundamental issues relate with respect to the financing of the project. The Port Authority indicated it would initially use 1.2 Bcf in a 48-inch line. The Administration's FERC advisors indicate that if one builds a 48-inch line and uses far less gas to fill it, it is very unlikely those extra costs will be permitted in the rate base. Consequently, the pipeline tariff that would be approved by FERC, or maybe by the RCA, is unlikely to include the total cost of this huge pipeline. It is only likely to include the portion of it that seems really justified for the transportation of 1.2 Bcf.

DR. VAN MEURS said that guesstimating from the Port Authority's data, actually \$2.3 billion would have to be invested on pure speculation. There would be no income stream attached to it. It seems to him, if one does not receive an income stream from FERC or the RCA that allows one to recover the cost of the \$4.3 Bcf line, that somehow has to come out of your own pocket. You have to invest equity to build that large of a line - a 100-percent equity situation. While there could be other options, that seems to be the situation at first glance.

[3:16:26 PM](#)

DR. VAN MEURS showed slide 19 on federal loan guarantees. He said the deal at this point doesn't have specific obligations. A very important reason that the Department of Energy (DOE) is in charge of the federal loan guarantees is because the U.S. Congress wanted to express that this should not be just a normal treasury concept. It wanted this federal loan guarantee to consider wider interests of national importance.

He explained the way loan guarantees typically work is first of all it is not a loan to the borrowers of the project. It is a guarantee that if the lenders to the project have a default, then the federal loan guarantee would click in. But what is very important to realize is that a typical loan guarantee

arrangement doesn't get the Port Authority off the hook. The federal government would still try to recover the monies - say from the person that defaulted. Clearly, he agreed with Mr. Shipkoff that these loan guarantee negotiations could sometimes take a year and a very important point is precisely what happens if one defaults on a loan and what the assets are. It was difficult for him to envision that the federal government would come to the conclusion that there would be significant assets attached to the Port Authority that they could go to if it would default. However, that being said, the DOE has said it would bend over backwards to make a gas project work.

[3:19:33 PM](#)

DR. VAN MEURS showed slide 20 on completion risk and asserted:

What is absolutely certain is that the federal loan guarantee would not cover the completion risk and it is absolutely certain that the lenders to the Port Authority or to the project would not assume this completion risk.

DR. VAN MEURS explained that completion risk means that you have invested money, say \$7 billion, in a project and you have borrowed, say \$5 billion, from your lenders and now something occurs like an earthquake, a court case, a huge environmental problem, or something nobody thought about and the project cannot be completed. "What happens in that case?" Then the lenders will want their money back - that is a completion guarantee. So, the person financing the project from its own assets must be able to provide this guarantee; otherwise no lender will lend on a project-financing basis.

DR. VAN MEURS asked:

How is the Port Authority going to provide a \$7 billion or \$8 billion completion guarantee? Now, they can maybe go to their construction firms and go to Bechtel and say we'd like you to take a large part of this.... It is however, very unlikely that you can spread your completion guarantee completely around. So, consequently, somebody has to provide a completion guarantee. And the Port Authority has not explained to us how they are going to do that. And unless they explain that to us, nobody will lend them any money - not even with a federal loan guarantee.

[3:22:33 PM](#)

DR. VAN MEURS went on to slide 21 - Financing of the Project: Conclusion - and said:

So, it seems to me that the project is difficult to finance. Firstly, we may have \$2 billion or \$3 billion of excess capacity in a 48-inch line for which there is no revenue stream. Secondly, without a federal loan guarantee, although the federal government may provide that, but definitely not without a completion guarantee, it seems to me that the Port Authority will be unable to finance this project - even if they have ship or pay contracts from all the parties that have strong balance sheets. So, I think the capability of financing this project is very much in doubt.

[3:23:28 PM](#)

DR. VAN MEURS paraphrased slides 22-23 - Ship or Pay Commitment - saying no matter what you do, there have to be ship or pay commitments for the part between Prudhoe Bay and the LNG export point. So, the Port Authority needs contracts with a number of parties that want to ship their gas. This could be a producer interested in using the project or a buyer. A contract could be \$10 billion to \$20 billion over 20-years depending on the tariff.

"Who would be interested in concluding such a contract?" he asked. The information provided by the Port Authority indicates that it is likely that producers' netback through its project is lower than the netback from their own project. If that's the case, he asked why they would be interested in selling into this project. The Port Authority, by concluding such a ship or pay agreement, would actually be increasing the risk of their own project, because it would become more costly because it would have a higher reserve risk. It again seemed to him that it's highly unlikely that such a deal would actually come together.

[3:25:37 PM](#)

DR. VAN MEURS showed slide 24 - Stranded Gas Contract - and supposed what would happen if the Asian market conditions change. The Port Authority explained well how the Asian market and the North American market are two different markets and over the coming years Asian markets might become more attractive again compared to North American markets. "So, who knows," he asked.

He said under a stranded gas contract whether one sells through Valdez or directly to Canada is essential, particularly if on

average the producer would expect to have a lower netback. This makes the LNG project even higher risk.

[3:28:00 PM](#)

SENATOR DYSON thought he understood from Port Authority's presentation that it would buy gas from the producers rather than shipping gas that the producers own. He asked what difference it makes.

DR. VAN MEURS replied for the pipeline to be financed, someone must conclude a contract against which the financing can take place. The Port Authority talked about Sempra and it is theoretically possible to say that Sempra buys the gas right at the end of the pipeline and would take care of the ship-or-pay agreement - and the producers don't have to. This would be a very attractive arrangement for the producers.

SENATOR DYSON asked if that were the case, would the producers want a guarantee that the pipeline company would buy a specific or minimum amount and what if one producer says it didn't want to sell.

DR. VAN MEURS replied that in this society people are free to buy and sell as they wish. So, if a buyer makes an attractive proposal to buy gas at the Inlet of the Port Authority project and if that price is higher than the seller believes he can get himself, if there are less ship or pay commitments attached, yes, the producers have said they would look at it.

[3:31:01 PM](#)

SENATOR DYSON asked if a prospective financier of the project believes the producers will sell at either flange, would the risk of not having gas to put in the pipe be diminished.

DR. VAN MEURS clarified yes, the person constructing the line and the lenders like to see a commitment either from the producers or from a buyer to pay the tariffs on the line - so the lenders can see an income stream.

SENATOR DYSON asked if only one pipeline will be built from Prudhoe Bay and the Port Authority builds it, did he foresee any circumstances under which the producers wouldn't sell gas that day.

DR. VAN MEURS replied the problem is that before you even get to the point of putting up the sign, the line has to be financed

and you cannot do so without the contractual arrangements that are necessary to finance it.

[3:33:23 PM](#)

DR. VAN MEURS [slide 25 - Stranded Gas Contract] said it is important to realize no matter what happens, the first step, whether you have a Port Authority project or a gas line to Alberta or any combination, you always need to have a stranded gas contract first. Otherwise producers cannot even decide about the offers that would be made to them, because they don't know what the fiscal package is that would be attached to it.

SENATOR DYSON said he was tempted to say "phooey" because lots of gas lines get built without fiscal certainty. Others have represented to the legislature that this is a very attractive project with some risks, but a very good rate of return. He asked why he continues to say in today's market, a stranded gas contract has to provide fiscal certainty.

DR. VAN MEURS answered that Senator Dyson was right, a number of large projects around the world have been built without fiscal certainty and he had highlighted that fact in his Centennial Hall presentations. However, he said:

The reason that I believe fiscal certainty on this particular contract is important is because of the risk profile of this particular contract. In this risk profile we took into consideration that as of today we haven't seen a buyer come forward for the 4.3 Bcf that is willing to make the commitments that we just talked about - which means that the producers will be stuck with the commitments to make the ship or pay arrangements. If they are stuck with the commitments to make the ship or pay contracts, they take that into consideration in the risk assessment and consequently, because of that, this pipeline has an extreme risk profile that is quite different from your average pipeline, say, in the North Sea or in Southeast Asia or in some other parts of the world. This is a monster-mega project of a size that is well beyond all the projects in the world, as I mentioned, in total size except maybe the Kazhegam project. So, that is why under this particular case a stranded gas contract is justified.

[3:37:08 PM](#)

DR. VAN MEURS elaborated on slide 26:

It seems to me that from an economic perspective it doesn't seem sensible to consider the Alberta project incremental to the Port Authority project, because we believed such an option is very difficult to finance in reality. What seems rational is to consider the Port Authority project incremental to a project to Alberta. And this is precisely the option that is already included in the stranded gas contract. That is why the stranded gas contract contemplates that, yes, if during an open season a [1] Bcf can be taken from, say, Delta Junction, or another tie-in point to Valdez, then and if that is a viable situation and if because of changes in market conditions the producers are anxious to sell or maybe it proves that incremental explorationists believe that that option is viable to them, then that is immensely welcome - that there absolutely has never been any doubt about that.

[3:38:41 PM](#)

DR. VAN MEURS discussed slide 27 - Upstream Economics - and referenced the Port Authority slide showing a high rate of return. He said if there would be a buyer at the inlet of the pipeline, such rates of return cannot hurt. However, if the producers have to make the ship or pay commitments, then typically their capitalized value has to be taken into consideration in the economics, which makes their project not as attractive as presented.

He next commented on the revenues that the state would earn under various options - slide 71. It seemed to him that the Y-line plus the Port Authority option is a 5 Bcf case versus a 4 Bcf case. Offhand, it seemed to him that the difference between the highway project and the Y-line project is just the difference in the extra 1 Bcf. He took exception to the presentation where the revenues under the contract are much less than the revenues under the status quo. He said he had shown a very detailed presentation in Centennial Hall illustrating income from various sources item-by-item providing his model to all economists that were interested; and he had never heard any specific criticism about his assumptions or any errors noted. He therefore maintained that his own analysis is the correct one.

[3:42:03 PM](#)

CHAIR SEEKINS thanked Dr. Van Meurs for his comments and announced that the committee would take an at-ease from [3:42:42 PM](#) to [3:50:07 PM](#).

## SB 3002-STRANDED GAS AMENDMENTS

CHAIR SEEKINS called the meeting back to order at 3:50 and announced SB 3002 to be up for consideration. He reminded committee members that the proposed committee substitute (CS), Version F as amended, had failed to move from the committee yesterday. He emphasized the importance of allowing the commissioner enough time to prepare a summary of the public comments he received in response to the proposed contract and the preliminary findings and determinations and to accomplish the rest of the tasks in AS 43.82.430(a).

[3:53:00 PM](#)

CHAIR SEEKINS said he wanted to give the commissioner enough time to gather the aforementioned information and respond to the comments, prepare a list of amendments, and to make his final findings and determinations as to whether the proposed contract and any proposed amendments meet the requirements and purposes of the chapter. He then moved to adopt CSSB 3002(NGD), Version Y, as the working document. There being no objection, it was so ordered.

[3:53:28 PM](#)

SENATOR DYSON asked if his implication was that last night's bill failed because it gave the commissioner 60 days.

CHAIR SEEKINS answered no, that was just a part of the bill that failed.

SENATOR DYSON asked him to explain the rationale for using 120 days.

CHAIR SEEKINS replied that he didn't think there was a hurry and wanted an adequate job. This allows a maximum timeframe for the commissioner to do that. They know that 30 days isn't enough; 60 days is questionable and 120 days is a maximum.

[3:55:45 PM](#)

SENATOR DYSON expressed concern about getting the results back in time for the legislature to ratify it.

SENATOR BEN STEVENS asked Senator Dyson if he was ready to ratify a contract.

SENATOR DYSON responded that he was if he could see it.

SENATOR BEN STEVENS asked how they could complete a contract if they won't pass the amendments to enable it to be completed.

SENATOR DYSON replied, "I guess under the same regime that's allowed it to be negotiated over the last year and a half - not having the amendments hasn't stopped that process. "

SENATOR BEN STEVENS said he was encouraged to hear Senator Dyson was ready to ratify a contract when it was presented to the legislature.

SENATOR DYSON replied that it wouldn't be a rubber stamp and not being able to see it is part of what's holding it up. He was also interested in seeing the LLC and the fiscal interest finding.

SENATOR BEN STEVENS noted that they all are interested in seeing those.

[3:57:16 PM](#)

CHAIR SEEKINS said they had attempted to address other issues in terms of fiscal certainty, work commitments, and Alaska hire and had chosen not to give the Administration any direction on that in terms of the law. So, he wanted to give them the extra time to be able to work on those issues.

[3:57:38 PM](#)

BILL CORBUS, Commissioner, Department of Revenue, noted the public comment period had closed July 24 with a little over 2,000 comments; they were in the form of written comments, emails, verbal comments made at the public hearings. About 25 written comments were very scholarly and well-prepared, including a 50-page document. He received comments from legislators, public interest groups, and people with direct commercial association with the project other than producers. He was in the process of analyzing them and putting together a response. Certainly, he said 30 days is unrealistic to do justice to the public comments. He said the Administration supports the chairman's proposed amendment.

[4:00:13 PM](#)

SENATOR STEDMAN asked what direction the legislature is giving the Administration. Was it going to renegotiate anything it wanted and then come back and find it doesn't have support for some of it?

CHAIR SEEKINS replied he wasn't sure. He thought the committee did some good work last night and its only alternative now is to wait and see. "It's a trust me deal."

SENATOR STEDMAN asked if he was right to infer that this extension would put it in to the end of November so they would be dealing with this next January and February.

CHAIR SEEKINS replied that it wasn't his intent to do that, but he didn't want to give the Administration an artificial boundary that would hinder or delay or force it into a premature effort.

[4:03:11 PM](#)

SENATOR ELTON asked to hear what the commissioner considers his duties are under AS 43.82.430(a)(2) and (a)(3). He asked if this authorizes an extended period of time for the commissioner to work on proposed amendments to the contract and to the Stranded Gas Act, as well.

COMMISSIONER CORBUS replied yes; he would interpret it that way.

CHAIR SEEKINS added that in this timeframe, he and the other parties would be renegotiating changes to what he would propose as a final contract.

COMMISSIONER CORBUS replied that was correct. They have learned that negotiations always take longer than they expect. He said they badly need the extra time and commented that once negotiations are consummated, they must incorporate the changes in the fiscal interest finding.

CHAIR SEEKINS asked whether it is his opinion that negotiations that take place inside a tight timeframe might put one party or the other at a disadvantage.

COMMISSIONER CORBUS replied yes, particularly the state.

[4:06:12 PM](#) at ease [4:08:06 PM](#)

CHAIR SEEKINS asked if there was any objection to adopting work draft CSSB 3003(NGC), Version Y. There were no objections and it was so ordered.

[4:08:19 PM](#)

SENATOR BEN STEVENS moved to adopt Amendment 6 and objected for discussion purposes. He mentioned that it was drafted to Version

G, but he asked that members give the latitude to insert it in the new Version Y.

OFFERED IN THE SENATE BY: SENATOR BEN STEVENS  
TO: CSSB 3002(NGD) (24-GS2095\G)

Page 1, line 3, following "terms;":

Insert "providing for an advisory vote, treatment of certain laws, and approval and ratification regarding a stranded gas fiscal contract;"

Page 8, following line 8:

Insert new bill sections to read:

**\*\*Sec. 14.** AS 43.82.430(b) is amended to read:

(b) After considering the material described in (a) of this section and securing the agreement of the other parties to the proposed contract regarding any proposed amendments prepared under (a) of this section, if the commissioner determines that the contract is in the long-term fiscal interests of the state, the commissioner may execute [SHALL SUBMIT] the contract [TO THE GOVERNOR].

**Sec. 15.** AS 43.82.430(c) is amended to read:

(c) The commissioner's final findings and determination under (a) of this section and decision regarding whether to execute the contract under (b) of this section are final agency decisions under this chapter.

**Sec. 16.** AS 43.82.440 is amended to read:

**Sec. 43.82.330. Judicial review.** An [A PERSON MAY NOT BRING AN] action challenging the constitutionality of a law authorizing a contract developed under this chapter [ENACTED UNDER AS 43.82.435] or the enforceability of a contract executed under a process authorized by [A] law may not be brought [AUTHORIZING A CONTRACT ENACTED UNDER AS 43.82.435] unless the action is commenced within 120 days after the date that the contract was executed by the state and the other parties to the contract."

Renumber the following bill sections accordingly.

Page 11, line 30:

Delete all material and insert the following:

**\*\*Sec. 23.** (a) AS 43.82.435 is repealed.

(b) AS 43.82.445 is repealed. "

Page 11, following line 30:

Insert new bill sections to read:

**\*\*Sec. 24.** The uncodified law of the State of Alaska is amended by adding a new section to read:

APPROVAL AND RATIFICATION. Notwithstanding AS 43.82.435, repealed by sec.23(a) of this Act, the provisions of the Alaska Stranded Gas Fiscal Contract between the State of Alaska and BP Exploration (Alaska) Incorporated, ConocoPhillips Alaska, Incorporated, and ExxonMobil Alaska Production, Incorporated, as amended to conform to the provisions of the Act, are approved, and the process and procedures followed in formulating that contract are ratified.

**\*Sec. 25.** The uncodified law of the State of Alaska is amended by adding a new section to read:

SUSPENSION OF OTHER LAW. The provisions of the Alaska Stranded Gas Fiscal Contract between the State of Alaska and BP Exploration (Alaska) Incorporated, ConocoPhillips Alaska, Incorporated, and ExxonMobil Alaska Production, Incorporated, as amended to conform with the provisions of the Act, are effective notwithstanding the provisions of any other law, including AS 43.82.200-43.82.270. Any inconsistency between the Alaska Stranded Gas Development Act (AS 43.82) and the fiscal contract executed under AS 43.82 are cured and authorized by this section.

**\*Sec. 26.** The uncodified law of the State of Alaska is amended by adding a new section to read:

ADVISORY VOTE. At the 2006 general election to be held on November 7, 2006, in substantial compliance with the election laws of the state, the lieutenant governor shall place before the qualified voters of the state a question advisory to the governor and the commissioner of revenue. Notwithstanding other laws relating to preparation of the ballot proposition, the question shall appear on the ballot in the following form:

QUESTION

Shall the commissioner of revenue sign and make binding upon the State of Alaska the Alaska

Stranded Gas Fiscal Contract between the State of Alaska and BP Exploration (Alaska) Incorporated, ConocoPhillips Alaska, Incorporated, and ExxonMobil Alaska Production, Incorporated?

Yes [ ] No [ ]"

Renumber the following bill sections accordingly.

Page 12, line 7:

Delete "Sections 2-14 and 17-20"

Insert "Sections 2-13, 17, 20-22, and 23(b)"

Page 12, following line 9:

Insert new bill sections to read:

**\*\*Sec. 29.** CONDITIONAL EFFECT. Sections 14-16, 23(a), and 24 of this Act take effect only if a majority of the votes cast in the 2006 general election on the ballot proposition in sec. 26 of the Act favor execution by the commissioner of revenue and binding effect on the State of Alaska of the Stranded Gas Fiscal Contract between the State of Alaska and BP Exploration(Alaska) Incorporated, ConocoPhillips Alaska, Incorporated, and ExxonMobil Alaska Production, Incorporated.

**\*Sec. 30.** If secs. 14-16, 23(a), and 24 of this Act take effect under sec. 29 of this Act, they take effect on the date that the director of elections certifies the results of the 2006 general election."

Page 12, line 10:

Delete "This"

Insert "Except as provided in sec. 30 of the Act, this"

SENATOR BEN STEVENS said he agreed with the Chair's and Senator Stedman's comments about the work that was completed on the issues before the committee. He said he wouldn't reoffer the amendments they had already voted on, but if any other member offered those amendments, he would vote for them again. He was offering this amendment that hadn't been voted on. He explained:

It puts the ability to execute the contract at the discretion of the commissioner, it would remove legislative approval upon a vote of the general public, and the sections that have a meaningful change

to the Stranded Gas Act are all contingent on a conditional effect in Section 29.

Mr. Chairman, I think that the actions that we have taken previously on these subjects to address work commitments, to address fiscal certainty on oil, to address fiscal certainty on gas, to address public project labor agreements, to address sovereignty agreements, to address collateral and arbitration clauses, to address calculation of educational funding, to address payment in lieu of taxes to municipalities, all the issues that we've done for the last two special sessions are without any standing now. And so, from my position the only standing we have for those to be incorporated in the contract is to give the commissioner - empower the commissioner - to get those enacted.

We heard comment that there's concern that 120 days may be too long for the public period before the contract comes before us, but if we don't give the commissioner the authority to negotiate, we'll never get what we expect to see from the product of the negotiation. This is a simple amendment that says one thing: the legislature can't make a decision on changing the Stranded Gas Act to enable negotiation to go forward; let the public make the decision.

[4:11:29 PM](#)

SENATOR DYSON asked if this amendment passes and the people vote and the Governor executes the contract, what would be the provisions for modifying the Stranded Gas Act to come into conformity with the contract.

SENATOR BEN STEVENS replied that those provisions would be included in Section 25 of the amendment, the enabling legislation.

SENATOR DYSON asked if the contract would supercede state law on any difference between it and the conditions of the contract.

SENATOR BEN STEVENS replied that is correct.

[4:12:48 PM](#)

CHAIR SEEKINS said no matter what pathway they take, if the legislature ever authorizes the execution of the contract under the current law, the authorizing bill would more than likely

read "notwithstanding any other provision in law," which is often put in statute to keep lawsuits from happening.

[4:14:24 PM](#)

SENATOR BEN STEVENS responded that there had been a lot of discussion about the concept of whether the negotiators have been working within the bounds of the law and as a result the state has lost standing in the contract.

It's my opinion that the people that have been negotiating this contract, the commissioner of revenue, the members of the DNR staff, the members of the Administration staff, have one thing in common and that is to get a project that's in the best interest of the state. And we continually are saying to the Administration and saying to our lead negotiators, 'You're going outside of the law and you're giving away the state's assets.' And I have yet to see that come to reality. We in the legislature have done nothing but criticize the negotiation in terms of what they've produced and I think that the fact that a project is before us for ratification - granted it's not ready for ratification - we still haven't seen key components of it - but because of the fact that they have produced something that is to the benefit of the state, which is a project to move forward, is an example of the work that they've done. I've had it to the point where I can't listen to it anymore about the fact that the legislature or the Administration has given away state's rights. I just don't think it's justified any longer! And we can continue to sit as a legislature and say, 'We need more. Why did you give this away; why did you give that away.' And we're not making progress. So, the amendment does one thing. If we can't make progress, let the general public take the progress. By the way, this doesn't take away the fact that we can do it before the November 7 election. The other thing that this doesn't do - it's irregardless of who is in control after the elections. It lays all the responsibility on the general public to say if nothing is done by November 7, should we vote to ratify or not.

[4:17:13 PM](#)

SENATOR DYSON said the Administration has always been very clear with the legislature that if there were changes to be made to the Stranded Gas Act, they would deal with them at the

appropriate time after they negotiate the contract. "That's the process we've been in. At no point have I ever said that they were operating outside of the law and an intimation that I was saying so is unfathomable."

CHAIR SEEKINS said he didn't interpret it that way.

SENATOR BEN STEVENS said he could interpret his comments any way he wants, but that's not what he intended to say.

[4:18:51 PM](#)

CHAIR SEEKINS invited Dennis Bailey to sit with the committee.

SENATOR STEDMAN said he comes from a district that is as far from this gas line project as one can get, but the people there are very interested in monetizing the resource and moving the state forward. They are not afraid of deciphering complex issues and making the correct decision. He supported Amendment 6 and was glad it was before them today because the people he had talked to in his district about it didn't want to vote. "They want a gas contract and if there's inaction in the legislature, that can be taken care of in the ballot box."

[4:20:53 PM](#)

SENATOR ELTON diverted attention to Sections 23 and on and Sections 14, 15, and 16. He had asked for someone to be available from Legislative Affairs [Mr. Bailey] to see if his view of those sections is correct. He thought it read as follows: "Section 14 authorizes the commissioner to execute the contract." He asked if this bill passes with this amendment, would that authorize the commissioner to execute the contract the day it is signed.

SENATOR BEN STEVENS said that was not correct. Section 23(a), which removes legislative ratification until after a vote of the people, doesn't go into effect.

CHAIR SEEKINS said the entire process of Section AS 43.82.430 with fiscal findings and final determinations would become an agency decision, which are challengeable under the Administrative Procedures Act, as the Judiciary Committee discussed. Then it would not become effective until it was ratified by a vote of the people. He asked Senator Stevens if he was correct.

SENATOR BEN STEVENS responded it was most important to first understand Section 29 [Amendment 6] on page 3, which lay out the

dates the sections take effect. Sections 14, 15, 16, 23, and 24 are all conditional on a positive vote on a general ballot. Nothing is significantly altered until that point.

[4:23:52 PM](#)

SENATOR ELTON agreed with the sponsor that Section 29 provides a conditional effect, but that doesn't necessarily allay his concern. He asked, assuming SB 3002 is passed as amended in this manner, and that the commissioner recognizes that he can execute a contract, but it may not take effect because of the conditional dates in Section 29, what the need was for Sections 14, 15, and 16.

[4:25:57 PM](#)

CHAIR SEEKINS asked for an explanation of Section 43.82.440 - Judicial review.

SENATOR BEN STEVENS deferred to Mr. Dennis Bailey.

DENNIS BAILEY, Attorney, Legislative Legal Services, agreed with the understanding expressed by Senator Ben Stevens that Sections 14, 15, 16 don't take effect until after a public vote. In Section 30, after the director of elections certifies the results, the commissioner has the authority to sign the contract. The timing there is currently 30 days after the public comment period, which has already occurred. So, his reading is if there was a positive vote, Section 29 would make Sections 14, 15, and 16 effective; Sections 14 and 16 would become effective after the certification and then the commissioner could sign the contract. He thought the 120 days referred to after the date the contract was executed by the commissioner.

SENATOR ELTON asked if the commissioner could not sign the contract until after the certification of the election.

MR. BAILEY replied that was right - that is what Section 30 says.

CHAIR SEEKINS added that was 120 days after final execution by all parties.

MR. BAILEY replied yes.

[4:29:01 PM](#)

SENATOR BEN STEVENS removed his objection to the amendment.

SENATOR ELTON objected saying he was going to vote no, because he disagreed with any assertion that the legislature has been dilatory. He, personally, had started with a minimal amount of knowledge, and while he wouldn't say he is an expert in petroleum economics, he has greatly increased his knowledge from there. He was now prepared to make a decision on what is good for state after seeing the contract and the LLC and he wouldn't vote against the contract just because it contains some elements he didn't like.

[4:32:56 PM](#)

CHAIR SEEKINS recognized Senator Elton's attendance and participation as having been stellar.

SENATOR STEDMAN said he had no hesitation in taking the contract to the voters.

[4:33:57 PM](#)

SENATOR WAGONER said it's a matter of having the background and knowledge to be able to vote. His constituents have said they don't want to vote on this issue; it's a matter for the legislature to decide.

[4:34:37 PM](#)

SENATOR DYSON said he identified with Senator Elton's remarks. He said our founding fathers set up our government as a constitutional republic in which elders are elected to take care of the people's business and the time and resources were set up to allow them to do that. He was a "strong no vote on this."

[4:36:41 PM](#)

SENATOR HOFFMAN said Alaskans want a gas line; it's a financial key to our future and our children's future. He was sent to Juneau to make those decisions; that is why he supported the Stranded Gas amendments. They haven't done their job here and he doubted that they would this session. He still wanted to get the job done, but it seemed that they were being placed in a box and they would let the window of opportunity slip by. He was glad the Governor had kept legislature here to get its work done. He said this issue is critical to the financial well-being of the state and if this is the best chance to get a gasline built, if the legislature can't do the work in one regular session and three special sessions, maybe they should adopt the amendment and send it to the people to vote on. "I believe they will make the right decision and get the gasline built."

[4:40:50 PM](#)

SENATOR OLSON spoke against the amendment and in support of letting the legislature make the decisions.

[4:43:09 PM](#)

CHAIR SEEKINS said he didn't know if this was the right time to put it to a vote before the people and he would vote no on the amendment.

[4:45:58 PM](#)

SENATOR BEN STEVENS provided closing comments on Amendment 6 saying there are 89 days until November 7 and it doesn't remove the legislature's authority then. He stated that the project needed to move to the next phase.

[4:48:30 PM](#)

SENATOR ELTON maintained his objection.

A roll call vote was taken. Senators Hoffman, Senator Ben Stevens, and Stedman voted yea; Senators Kookesh, Olson, Wilken, Elton, Wagoner, and Seekins voted nay; so, Amendment 6 failed by a vote of 3 yeas and 7 nays.

SENATOR WILKEN moved to adopt Amendment 13.

### AMENDMENT 13

TO SB 3002  
BY SENATOR GARY WILKEN

"An Act amending the time allowed under the Alaska Stranded Gas Development Act, for the commissioner of revenue to summarize public comments, propose amendments, if any, and make findings; and providing for an effective date."

CHAIR SEEKINS objected for a discussion.

SENATOR WILKEN said he thought Version Y was good, but he was a little concerned that the title didn't define what the bill does, which could lead to delays over the next six days as this takes what could be a tortured path through the legislature.

[4:50:24 PM](#)

MR. BAILEY said he had no difficulty with this amendment since it was similar to the title on the original CS.

[4:51:17 PM](#)

CHAIR SEEKINS removed his objection and asked if there was further objection.

SENATOR STEDMAN objected and said he would prefer to leave the title the way it is.

CHAIR SEEKINS declared that as the introducer of this particular CS, he didn't intend it to have an open title nor was there any discussion with any other person in the other body about the title.

[4:52:35 PM](#)

SENATOR STEDMAN maintained his objection.

A roll call vote was taken. Senators Kookesh, Dyson, Wilken, Elton, and Wagoner voted yea; Senators Ben Stevens, Stedman, Hoffman and Seekins voted nay; so, by a vote of 5 yeas and 4 nays, Amendment 13 was adopted.

[4:53:32 PM](#)

SENATOR WILKEN asked Commissioner Corbus if this would allow him to collect and synthesize information for after the election. He asked if that was his intent.

COMMISSIONER CORBUS replied that it was their intent to get all this work done before the election.

[4:54:15 PM](#)

SENATOR BEN STEVENS moved to report CSSB 3002(NGD) Version Y as amended out of committee with individual recommendations. There were no objections and it was so ordered.

The committee took an at-ease from [4:54:55 PM](#) to [4:56:37 PM](#).

### **Alaska Gasline Port Authority Presentation**

CHAIR SEEKINS returned to the Alaska Gasline Port Authority presentation. He informed members that he would take rebuttal and continue the roundtable discussions in future meetings.

[4:58:40 PM](#)

MAYOR WHITAKER continued his Port Authority presentation. He said the legislature had cooperated with the Port Authority, but he couldn't say the same about the Administration. "We have found that the Administration has been anything but cooperative." And while they were willing to put up with that, other participants in the project were not. Sempra left saying,

"You've got the best economics that we can find, but you've got the worst politics." It was that kind of an attitude that it would be very difficult for the project to move forward. He stated:

I'm going to editorialize just a bit. Our results have been put on the board today and the commitments that we have made are clear. We're dedicated to moving a project forward. Are there roadblocks? Certainly. Can we overcome those roadblocks? We certainly think we can.

On the other hand, what you have in front of you is a contract that is essentially a hold harmless agreement; it's a hold harmless agreement for the producers given that if they choose not to build a project, there will be no penalty for it. And that hold harmless agreement is for 30 years and 45 years. I'll stop now. Those are the results that I see thus far.

[5:01:25 PM](#)

MR. SHIPKOFF said he disagreed with Dr. Van Meurs' slide 3 that listed the distribution of the take between the various state components and the producers. Mr. Shipkoff said that while he didn't disagree with any specifics, that according to his numbers there is a \$2 billion federal tax cost to the midstream, which the Port Authority's structure allows to be saved - a savings that can be shared between the state and the producers.

[5:03:01 PM](#) at ease [5:03:17 PM](#)

MR. SHIPKOFF referred to Dr. Van Meurs' slide 4 that discussed state ownership in the pipeline and indicated a certain portion of the federal tax cost could be alleviated, and he does not disagree; but what AGPA offers is that the entire amount of federal tax can be alleviated without the state having to take any ownership.

On Dr. Van Meurs' slide 5, Mr. Shipkoff said that likewise, there was nothing he disagreed with. The purpose of the Port Authority was to accomplish all of these goals. But the connection between the high-risk nature of the project and the need for fiscal stability is an area where he disagreed. AGPA doesn't see the need to give fiscal concessions. His concern with slide 7 was the same in that supporting the stranded gas

contract, the West Coast market and the LNG project might never happen.

MR. WALKER noted that the LNG may be lost to Alaska, but the producers have other projects elsewhere.

MR. SHIPKOFF agreed. He went on to slide 8 that discussed the timeline. He agreed that they were now past the startup date of January 1, 2006, but even if the LNG project started now, he believed that the benefits of having some engineering work already done and using existing permits would allow it to have first gas sometime late in 2012. He agreed with Dr. Van Meurs that every day waiting is a day lost.

MR. WALKER interjected that their offer to the producers included discussion on returning CO<sub>2</sub> back into the leases where it came from as miscible injectant (MI). In early meetings, the producers wanted to retain ethane as part of the MI stream; subsequently it appears that is not the case.

MR. SHIPKOFF added that they have never suggested that AGPA would do anything not in concert with the producers. "Obviously, everything has to be done in coordination with the producers. That's very clear."

[5:07:58 PM](#)

MR. SHIPKOFF went on to slide 10 and pointed out his argument that the LNG project is exempt from FERC regulation, thus compressing its timeframe for everyone including the producers.

[5:08:29 PM](#)

SENATOR ELTON said this point struck him during Dr. Van Meurs' presentation. He asked if he was suggesting that because the Port Authority already holds permits, that a GTP is possible in 2011 rather than in 2013.

MR. SHIPKOFF responded that his timeline takes into account work that has already been done on permits and, if the project is FERC-exempt, it does not have to go through the FERC process. The highway project that assumes first gas at 2016 includes the time needed to obtain permits and FERC approval, but he said, "We can eliminate that - for whoever and whichever project."

CHAIR SEEKINS asked if they anticipated owning the GTP.

MR. SHIPKOFF replied "We have said that we are prepared to own it if that benefits the state and the producers...."

CHAIR SEEKINS asked if the Port Authority didn't own it, would the producers still have to go through that process.

MR. SHIPKOFF replied no; he thought that would be a benefit the Port Authority could bring to them.

CHAIR SEEKINS asked if there was some indication that the downstream shippers out of Valdez would have to go through that process.

[5:10:30 PM](#)

MR. SHIPKOFF replied, of course; he did not dispute that for the downstream re-gas terminal and takeaway pipelines that bring the gas to market. As an example, Costa Azul in Mexico, regulated by the CRE, has already applied to FERC for a certificate of public convenience and necessity for its takeaway pipelines. He reasoned, "It's not us who has to obtain those permits."

CHAIR SEEKINS asked about the ships and the shippers.

MR. SHIPKOFF replied that he is not an expert on shipping regulations.

CHAIR SEEKINS said he thought Mr. Twomey said that the boats used downstream from the pipeline are FERC regulated.

An unidentified person in the audience indicated the he wouldn't say that.

[5:11:46 PM](#)

SENATOR ELTON asked if the Port Authority owned the GTP, 2011 is realistic for first gas, but if the producers own it, it could be as late as 2013.

MR. SHIPKOFF replied that 2011 may not be realistic, but 2012 may be; he thought AGPA could help compress the timeframe for everyone.

SENATOR ELTON said he thought Mr. Shipkoff said 2011 is when their project could start delivering gas.

MR. SHIPKOFF clarified that it was 2012. He went on to slide 13 on gas sales in California and countered that while he has not provided any evidence that the LNG project could offer the lowest price in California compared to other LNG exporters, he disagreed with Dr. Van Meurs that the LNG project had to provide

the lowest price. One must look at where the project fits on a cost-supply curve and compare oneself against all potential suppliers. The fact that Qatar is not the lowest cost supplier into the Gulf has not prevented them from having very successful projects. He said:

We do not expect to be the lowest cost supplier into the West Coast.... The lowest cost supplier into the West Coast is going to be indigenous California production that is non-conventional or something like that.

5:15:06 PM

DR. VAN MEURS commented that while there are things like supply and demand curves, one needs to always compare the strengths in a project relative to the strengths of other projects in the market.

MR. SHIPKOFF agreed with Dr. Van Meurs' comments that one needs to compare oneself against all the suppliers into the market one is selling into, not just LNG and stated, "We certainly are going to have a lower break-even price than many of the other suppliers who are going there...."

Mr. SHIPKOFF said slide 15 tied in to the same idea that their competitors are not just other LNG projects, but all suppliers into a market. He pointed out that the highway project faces the same situation going into the Midwest stating:

If all the projects that have break-even prices below the marginal cost and below the expected price in the market, it will proceed. We believe that both projects, the LNG project and the highway project, are well below the threshold and they both are economic.

Regarding slide 16, Mr. Shipkoff couldn't recall ever claiming that the LNG project brings the benefit of diversifying between the East and West Coast, but rather he talked about the benefit of diversifying between the West Coast and Japan. The highway project cannot bring the gas to Japan.

MR. WALKER added that regarding the last paragraph about the Alberta Hub and East Coast/West Coast markets, he has seen nothing in the contract that guarantees the gas leaves Alberta and stated, "We strongly believe that it will most likely stay in Alberta for the tar sands feed stock."

CHAIR SEEKINS commented that he was just in Alberta with the Pacific Northwest Economic Region (PNWER) and was told that by Alberta's oil and gas people that its tar sands were not a competitor for Alaska's gas. Their information is that by the time Alaska gas gets to Alberta there will be enough downstream capacity to accommodate all of it, because all the Mackenzie Delta gas would be used in the tar sands area.

MR. WALKER said the last report he saw indicated that the tar sands would require as much as 3.7 Bcf of gas and MacKenzie has about 1.2 Bcf. An official at ConocoPhillips said they're building their oil line out of the tar sands to St Louis for the refinery specifically because they plan to put the Alaska gas into the tar sands.

CHAIR SEEKINS admitted they could, but that is information he received within the last 30 days. It is a point for discussion.

[5:21:54 PM](#)

MR. SHIPKOFF went on to slides 17 and 18, the issue of over-sizing the pipeline. He has assumed they would have a negotiated rate and over sizing is for the benefit of the producers who also want to do the highway line. He saw no problem with that, putting aside the FERC-regulated issue.

He agreed, regarding slide 19, that you have to convince the provider of guarantee that a project is sound, but the Port Authority was confident that that case could be made.

CHAIR SEEKINS said his question was based on the fact that he's never gotten a loan guaranteed for him unless he already had enough capital that they didn't need to guarantee it for him.

MR. SHIPKOFF responded that went to the point of slide 20, which concerned whether the lenders (by extension the guarantors) would look at AGPA's assets as insurance that the loan would be repaid. If this was a full-recourse corporate type of financing, that would be the case, but most large capital projects aren't financed on that basis. They are financed on a limited-recourse basis - in which case the lender does not look to the assets of the borrower, but to the ability of a project to generate a specific revenue stream.

CHAIR SEEKINS asked if he didn't think the state would have to put up full faith and credit of people of Alaska as part of the guarantee.

MR. SHIPKOFF replied that he wouldn't recommend that and didn't expect it.

CHAIR SEEKINS commented that since there are no regulations yet, it is hard for him to form an opinion on it.

SENATOR BEN STEVENS commented that he disagreed with Mr. Shipkoff that his project wouldn't need the full faith and credit of the state behind it in a financial market. He related that last week, the Wyoming Port Authority's participation in the Rocky Mountain Express project was pulled by the FERC and reallocated amongst the remaining owners. The reason the Authority didn't get credit worthiness for the firm transportation commitment was because the Wyoming legislature would not exceed a \$3-billion backing for their 200-decatherm/day capacity. He exclaimed:

So, the comments that you don't have to have the full faith and credit of the state in the financial markets, I don't agree with that because there is an example that just happened last week.... You know, you continually put things in front of us that say it doesn't work, it doesn't work, we don't need that, we don't this, we don't need FERC, we don't need firm transportation commitments, we don't need upstream agreements, we don't firm financial agreements. I mean, what it's amazing to me that everything you say, you don't need it. Everything we've heard from every other project presenter that these are requirements that have to be in place for any project to be put forward; you say you don't need it. It's just a phenomenal presentation that you've given us in the last 24-hours.

MAYOR WHITAKER responded:

We've never said that we don't need a number of things that any other project would need. There are some things we do need, some things we don't need. Mr. Chairman, if it's okay with you, I would like Mr. Shipkoff also to reply.

CHAIR SEEKINS responded, "Absolutely."

[5:29:28 PM](#)

MR. SHIPKOFF responded that he couldn't speak to what the Wyoming Authority proposed, but what they offered was obviously

not sufficient to satisfy financial markets. Based on the Port Authority's experience, they believe they can put a structure in place with proper gas supply agreements, proper mitigation of risks through a combination of contractor guarantees to demonstrate that the project has robust viability to where the lenders will lend on a limited recourse basis. This is done all the time; it's not innovative or new.

[5:31:03 PM](#)

CHAIR SEEKINS directed that the discussion move on.

MR. SHIPKOFF said he didn't agree with slide 20 that said the Federal Loan Guarantee wouldn't cover completion risk. Nothing in the guarantee requires the secretary of DOE to ask for completion guaranties, but he could decide to. He agreed that non-guaranteed lenders generally don't take completion risk and that has been anticipated in his economic analysis. If Sempra invests in and operates the LNG plant, which it has proposed to do, that is their risk and it has the financial resources to back it. Completion guarantees can be provided for portions of the project that are not privately owned and he said financial instruments are available that can provide mitigation for completion risk and cover lenders.

CHAIR SEEKINS asked if he had any hard plan as to who will own what in the LNG project.

MR. SHIPKOFF replied that they are not in the position to negotiate final commercial agreements, but he pointed out the highway project is not in that position either.

CHAIR SEEKINS asked, "All we really can count on at this point would be that you would own the pipe?"

MR. SHIPKOFF replied, "It's very likely that we will, yes."

[5:35:04 PM](#)

DR. VAN MEURS remarked that Senator Elton had been requesting the LLC agreement and the reason it takes so long to negotiate it is precisely to deal with very complex questions like completion risk. In fact, the state has looked very hard at its ability to take on certain forms of completion risk as a partner. "So, I think the seriousness of completion risk at this point in time, I think is being understated by the Port Authority."

CHAIR SEEKINS said that was a point well taken.

MR. SHIPKOFF went on to slides 22 and 23 and said the point appears to be who is going to give you ship or pay commitments that are needed for financing if the netback the project provides is so low. He did not agree with this premise. He said the netback for the LNG project is low because it is using oversized pipe in preparation for a highway project. He said the only issue is whether the project can support itself or not, because it provides a netback greater than no netback at all.

[5:38:12 PM](#)

He said the stranded gas contract - slide 24 - goes back to his initial remarks about whether either project requires a stranded gas contract and whether the gas is stranded in the first place is a separate issue from whether the LNG project is viable. He stated, "We think that neither the LNG project nor the highway project are stranded gas and, therefore, neither of them require support...."

Relating this to the previous point he made that they will be successful in obtaining financing, Mr. Shipkoff said their tax-exempt financing and possible lower cost of capital is often rebutted by the idea that one can't evaluate projects on a post-financing basis, but purely on a pre-financed basis.

MR. WALKER said he had very significant concerns about slide 26 that said the LNG project could be the incremental piece of a highway project rather than adding the highway to the LNG project. They don't know when the line would come through Delta Junction because it's only a study at this point and he was concerned that they would lose the market by becoming an incremental addition a highway project.

MR. SHIPKOFF went to slide 27 that assumed a buyer would buy gas at the inlet of the pipeline. The Port Authority assumed the same thing, but it is also willing to act as transporter to a North Slope shipper. If producers have to assume ship or pay commitments, they are financial obligations of a sort and don't have to be capitalized on a balance sheet. He disagreed that capitalization of these commitments needs to be included in evaluating the upstream economics. There are many instances in which the upstream producer transports its gas via a third-party pipeline and clearly he said you evaluate upstream economics based on the value you get upstream.

MR. SHIPKOFF countered Dr. Van Meurs' slides that compared of state revenues making the point that the Y-line is a bigger

project. And Mr. Shipkoff said that was his point exactly; the Port Authority brings incremental value to the state by providing the opportunity for both the state and producers to capture a larger share of the Lower 48 market with Alaska gas, not with somebody else's gas.

[5:44:29 PM](#) at ease [5:46:11 PM](#)

CHAIR SEEKINS called the meeting back to order at 5:46 pm.

ROGER MARKS, Economist, Department of Revenue, informed members that he'd prepared a detailed presentation, but he would be brief. He referenced the Administration's perceived antagonism toward the LNG project. He stated this project is all about maximizing the benefits of the state's resources to the Alaskan people and the Administration takes that very seriously. "We believe maximizing the value means three things: the most gas at the highest price at the lowest cost."

MR. MARKS explained his view of the LNG project.

This is how we see LNG project. I'll talk about the West Coast market demand and supply real briefly and the price. The West Coast demand for gas is not growing very fast; this is from Wood McKenzie. Over between now and 2020, it's growing maybe 2 Bcf a day. It's just growing slowly with the population growth. The West Coast has large supplies of nuclear and hydropower, and oil, as well, to run power plants. In addition on supply side, what the West Coast has access to is, and what is going gangbusters is, the Rocky Mountains. You know, people talk about the North Slope has a lot of gas - 35 Tcf; the Rockies have over 300 Tcf of conventional and unconventional gas. It costs about \$.50 - the tariff from the Rocky Mountains to the West Coast about \$.50.

People have talked about the last couple of days, the Rockies Express Pipeline. There is so much gas in the Rockies that the producers in the Rockies cannot ship any more to the West Coast because the price would just crater. The Rockies Express Pipeline is something like 1,500 miles from the Rockies - you know the Powder River Basin, Wyoming, all the way to Ohio at a tariff of \$1. They're going to build a project that big and pay that much tariff because all the gas they

can get into the West Coast is there without crashing the market.

In addition, if you look at, you know, if is there room for LNG on the West Coast? Yeah, there is room for a little bit. This is a forecast from Wood Mackenzie. Their forecast, you know, by 2020 - and they have it all going into the Baja, which they believe is the only site that can be sited on the West Coast. This is the same opinion that PFC Energy had. They say that by 2020, there might be 1.8 Bcf of LNG coming into the Baja terminal.

Right now the Baja plant, the Sempra plant, is going to open in 2008; they have 1 Bcf a day committed. They recently had an open season to try to get another 1.5 Bs and more than that was subscribed. So, if you believe this forecast, there is about 2.8 Bcf a day already subscribed into the Baja plant. So, I think an argument can be made that there may not be any more room for any more LNG including our project, or if it does, it will suffer on the price side.

As Noel stated yesterday, West Coast prices are about \$.50 less than Chicago prices. So, on the price side, again if we believe we maximize the benefit of the project to the people by maximizing the value, just on the price side alone going to the West Coast, we lose \$.50.

Now on the cost side, LNG is an expensive process. In general, you know, people do LNG when they have no other options and the reason they do when they have no other is it's so expensive. You have to compress it about 600 times so it fits in a ship; it's 260 degrees below zero. It costs a lot!

In addition, this concept of the Y-line - you know, pipelines live and die by economies of scale. If you look at the option of shipping 4 Bcf a day to the upper Midwest and split that out between 3 and 1, you kill a lot of economies of scale. And so what happens is the costs go up a lot. You know, our estimate is just if you were to take the difference between 4 Bcf a day and 3 Bcf a day, it is an additional \$.40 per million Btu to get it to Chicago. So what you do by taking a Y-line is you dilute the economics on both

portions, because you just killed the economics of scale.

You know, you said yesterday that the Y-line option or the LNG option, the 1 B, doesn't take anything away from the Alcan project. Well, it certainly does; it takes gas away from the Alcan project. If it's economic to commercialize 4 Bcf a day, the state will realize more value doing all 4 Bcf to Chicago rather than 3 and 1. If it makes sense to commercialize 6 Bcf a day, it makes more sense to ship 6 Bcf a day to Chicago rather than 5 and 1.

Could the LNG project possibly pay for itself? Yes, it might but the issue is where do we get the most value. Well, Mr. Chairman, I just - what's been perceived again as the Administration's antagonism is really nothing but our reverence for the directive in the Constitution, the same directive that Mayor Whitaker stated yesterday. So, that's what I was going to say in half an hour down in about five minutes.

CHAIR SEEKINS called for questions.

REPRESENTATIVE SEATON asked Dr. Van Meurs or Mr. Marks if the Stranded Gas Act is needed for both projects and if it is needed for a 1.2 Bcf LNG project without over-sizing the pipeline.

DR. VAN MEURS answered that the Stranded Gas Act was actually created for an LNG project when the state was hopeful that the 2 Bcf Yukon Pacific project could be realized to the Asian market. Further he said:

Obviously, the same price volatility and the same cost overrun problems that face a project to Alberta face an LNG project. Consequently, if the producers, in the hypothetical case, that they would make a decision to sell gas to this LNG project, yes, they would like to know what the fiscal terms are; they would like to see some stability on the fiscal terms and consequently that is the same for either project.

REPRESENTATIVE SEATON asked if this is no longer a major project, was it his opinion that the Stranded Gas Act, concessions, credits, the fiscal certainty are necessary for this project to go forward as a stand-alone project.

DR. VAN MEURS answered that the situation is, as Roger Marks described, that the state has an obligation to maximize the benefits back to the state and he believed that this highway project did that. He sees the Port Authority project as a potentially valuable addition to the highway project. So, he can't see how they could have partial fiscal stability.

REPRESENTATIVE SEATON said in looking at the maximum value for the State of Alaska, he concluded that the Stranded Gas Act looked for the maximum value for the producers and concessions were needed for a stand-alone project.

[5:59:00 PM](#)

DR. VAN MEURS replied that he hadn't studied the details enough, but previous extensive analysis of the LNG project to Asia showed the clear need for fiscal stability, the Stranded Gas Act concessions, and at that time it authorized them to have far more extensive lowering of the fiscal terms than what has been agreed to currently. He disagreed with Representative Seaton that the stranded gas contract was done with the view of maximizing the benefits to the producers. He had hoped to explain over the last few months that there is an important balance between risk and reward. He elaborated:

Consequently, we believe that the reward to the investors can be lowered and it is important to lower the reward to the investors if you can lower the risk. And consequently, that is a concept that is true universally. The great advantage, the great innovation of the Stranded Gas Act was that for the conditions in Alaska where you are so far removed from markets, no matter what - and that was well-explained in the Port Authority presentation and I think in our presentation. No matter what you do, you are very far - or whether you go to Asia - you are very far from markets. Under those kinds of conditions it is very useful to consider the balance between risk and reward. And by reducing the risk through the Stranded Gas contract, we can reduce the reward and increase the benefits to the state. And that is precisely what Mr. Marks has also emphasized.

REPRESENTATIVE SEATON said that when the LNG analysis was made earlier, the highway project would have been uneconomic also. Economics have to be talked about as they exist on the two projects now. He thought they should be comparing the very large

supply of revenue the state would get from this LNG project and keep all the PPT oil money to subsidizing the gas project.

MAYOR WHITAKER said Representative Seaton was correct. When the YPC discussion was ongoing, there was an incredibly different price regime. With regard to the most gas, highest price, lowest cost comment, he has read the contract that is before the legislature and he didn't see anything that would take them there. He saw an indemnity for the producers to hold them harmless if they choose not to produce any gas. Therefore, he said if the state is looking for certainty, it should seriously look at the LNG project. He thanked the Chairman for the opportunity to come before the committee.

MR. WALKER suggested that if the goal of the Administration is to maximize the value of the wellhead at the lowest cost, they should look at the over the top option, which accomplishes that. The Port Authority thinks that Alaska can have as high a wellhead as any other project and keep gas in Alaska for the use of Alaskans as well. Perhaps, this is where they disagree.

CHAIR SEEKINS inserted that this legislature will not allow an over the top route under any circumstances; federal legislation won't allow it either.

[6:06:19 PM](#)

MR. WALKER said the PFC report, a slide that wasn't shown in the Administration's presentation, did the Port Authority a lot of damage because the people who did the analysis were instructed not to contact the Port Authority.

If they had contacted us, they would have had updated information. We would have gone to see them just like we went to see Econ One within six hours of our conversation the other day, Mr. Chairman, when you were going to utilize them to evaluate us. That was just a blindside that was indicative of driving the final stakes through the heart of the Port Authority project when you do an analysis. Then you do your best interest findings - all this stuff - based upon a study that we were never even contacted. So, we spent tons of money with Lukens, with Econ One, with anybody else doing an analysis and yet the Administration chose to go with PFC and that's just indicative of what we've lived with in this administration.

CHAIR SEEKINS noted that the legislature was doing its own independent analysis of the economics of the deal. When that comes out, it would be released even if it hadn't been discussed in public forum to the Port Authority.

We will do everything we can to make sure that our discussions are full, fair, and complete and balanced as we go forward in trying to make this determination for ourselves. We'll take everyone's input as you can see today.

MR. MARKS said he was the project director on the PFC study and the project description was absolutely consistent with the project description the Port Authority had on its website and continued to update even after the draft report was released. With regards some comments made yesterday about whether that study put the costs on an apples to apples basis with the Port Authority's estimates, he said PFC went to painstaking lengths to make them consistent in terms of inflation, steel costs, 2005 prices, profit margins, and contingencies, and the cost estimates, as well.

MAYOR WHITAKER said, "We absolutely disagree with those statements."

MR. WALKER said, "Not a single phone call to us."

[6:10:06 PM](#)

CHAIR SEEKINS found there were no further questions and commented that the conversation had been stimulating and he looked forward to continuing it as they go forward. There being no further business to come before the committee, he adjourned the meeting at [6:11:44 PM](#).