

**ALASKA STATE LEGISLATURE**  
**HOUSE SPECIAL COMMITTEE ON OIL AND GAS**

March 19, 2007

8:33 a.m.

**MEMBERS PRESENT**

Representative Vic Kohring, Chair  
Representative Kurt Olson, Vice Chair  
Representative Nancy Dahlstrom  
Representative Jay Ramras  
Representative Ralph Samuels  
Representative Mike Doogan  
Representative Scott Kawasaki

**MEMBERS ABSENT**

All members present

**OTHER LEGISLATORS PRESENT**

Representative Bob Roses  
Representative Berta Gardner

**COMMITTEE CALENDAR**

HOUSE BILL NO. 177

"An Act relating to the Alaska Gasline Inducement Act; establishing the Alaska Gasline Inducement Act matching contribution fund; providing for an Alaska Gasline Inducement Act coordinator; making conforming amendments; and providing for an effective date."

- HEARD AND HELD

**PREVIOUS COMMITTEE ACTION**

BILL: HB 177

SHORT TITLE: NATURAL GAS PIPELINE PROJECT

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

03/05/07	(H)	READ THE FIRST TIME - REFERRALS
03/05/07	(H)	O&G, RES, FIN
03/06/07	(H)	O&G AT 3:00 PM BARNES 124
03/06/07	(H)	-- MEETING CANCELED --
03/08/07	(H)	O&G AT 3:00 PM BARNES 124
03/08/07	(H)	-- MEETING CANCELED --

03/13/07 (H) O&G AT 3:30 PM HOUSE FINANCE 519  
03/13/07 (H) Heard & Held  
03/13/07 (H) MINUTE(O&G)  
03/15/07 (H) O&G AT 3:00 PM BARNES 124  
03/15/07 (H) Heard & Held  
03/15/07 (H) MINUTE(O&G)  
03/19/07 (H) O&G AT 8:30 AM CAPITOL 106

#### **WITNESS REGISTER**

MARCIA DAVIS, Deputy Commissioner  
Commissioner's Office  
Department of Revenue (DOR)  
Juneau, Alaska

POSITION STATEMENT: Provided sectional analysis of HB 177.

PAT GALVIN, Commissioner  
Department of Revenue (DOR)  
Juneau, Alaska

POSITION STATEMENT: Answered questions on HB 177.

#### **ACTION NARRATIVE**

**CHAIR VIC KOHRING** called the House Special Committee on Oil and Gas meeting to order at [8:33:49 AM](#). Representatives Samuels, Ramras, Doogan, Kawasaki, and Kohring were present at the call to order. Representatives Dahlstrom and Olson arrived as the meeting was in progress.

#### HB 177-NATURAL GAS PIPELINE PROJECT

[8:34:25 AM](#)

CHAIR KOHRING announced that the only order of business would be HOUSE BILL NO. 177, "An Act relating to the Alaska Gasline Inducement Act; establishing the Alaska Gasline Inducement Act matching contribution fund; providing for an Alaska Gasline Inducement Act coordinator; making conforming amendments; and providing for an effective date."

[8:36:12 AM](#)

MARCIA DAVIS, Deputy Commissioner, Commissioner's Office, Department of Revenue (DOR), began her sectional analysis of the Alaska Gasline Inducement Act (AGIA). This act amends AS 43 by the addition of Chapter 90, which is known as AGIA. The Alaska Gasline Inducement Act begins with Article 1, she said, entitled

"Inducement to Construction of a Natural Gas Pipeline in this State." Section 43.90.010 states that the purpose of this act is to encourage expedited construction of a natural gas pipeline with the following goals: facilitate North Slope gas commercialization, promote exploration on the North Slope, maximize benefits for the people of the state, and encourage the commitment of natural gas to the North Slope pipeline. Article 2, is entitled "Alaska Gasline Inducement Act License." Ms. Davis informed the committee that Section 43.90.100 essentially outlines that the commissioners of Department of Natural Resources (DNR) and Department of Revenue (DOR) will award the AGIA license and inducements.

[8:38:15 AM](#)

REPRESENTATIVE SAMUELS observed that an applicant applies for [one] license, not multiple licenses.

MS. DAVIS confirmed that one license would be awarded to one applicant. She continued to say that Section 43.90.110 lists the inducements that are awarded to the licensee. Paragraph (1) is the state matching contribution, which is not to exceed \$500 million, paid out over a five year period, and the period commences on the date of the issuance of the license. The terms for matching the matching contribution are: subparagraph (A), on or before the close of the first binding open season, the match will be an equal match; subparagraph (B), after the close of the open season the match is not specified, but left as an item to be resolved in the bidding process with a limit on the state's match of 80 percent; subparagraph (C), qualified expenditures are costs that occur after the license is issued, that are directly related to obtaining a Federal Energy Regulatory Commission (FERC) or Alaska Regulatory Commission (RCA) certificate, and are not overhead costs, litigation costs, assets or work product predating the issuance of the license, or civil or criminal penalties or fines. The second inducement provided to the licensee is the benefit of the AGIA coordinator, whose duties are more fully specified in AS 43.90.330. The licensee also receives the benefit of a state program that provides training for the employment workforce needed for the construction of a pipeline.

[8:40:40 AM](#)

REPRESENTATIVE SAMUELS asked what amount of the state's money will be spent prior to the open season and what amount will be spent between the open season and certification.

MS. DAVIS said that total estimates are as low as \$50 million and as high as \$200 million, and the state's portion would be one-half.

REPRESENTATIVE DOOGAN asked for details about the state training program described in Section 43.90.110(3).

MS. DAVIS responded that this is the sole reference to the program.

PAT GALVIN, Commissioner, Department of Revenue, informed the committee that the training program is not established yet, and that the intent is to work with Department of Education, the University of Alaska, Department of Labor, and the licensee, to develop a program geared toward jobs for pipeline development and construction. The bill provides assurance to the licensee that a training program will be developed with its project in mind and it will be in place at the beginning of the project.

REPRESENTATIVE DOOGAN surmised that the Palin Administration intends to develop a training program that will train Alaskans to build the gas pipeline. He asked if there was a timeline for this training.

COMMISSIONER GALVIN responded that the details and timeframe of the training program will be available soon, and confirmed Representative Doogan's statement of the intent of the program. He noted that the schedule of the training program will be dependent on the licensee.

REPRESENTATIVE DOOGAN asked if the training program would require additional legislation.

[8:44:58 AM](#)

COMMISSIONER GALVIN said, at this point, the need for additional legislation is not known.

REPRESENTATIVE DOOGAN asked if funding would be needed.

COMMISSIONER GALVIN answered yes.

REPRESENTATIVE SAMUELS asked if the open season is successful, financing is obtained, and the state has already paid \$25 million to \$100 million, why would the state spend more money after the open season?

COMMISSIONER GALVIN responded that the state anticipates receiving proposals that denote spending a certain amount of money to get to open season and that will also specify the cost split with the state for either a successful or unsuccessful open season. The proposals will be evaluated based on their value to the state. He said that the applicants will want to limit the state's cost.

REPRESENTATIVE SAMUELS noted that there is the possibility that there will not be enough gas committed to obtain financing and build the pipeline. If the proposal denotes that the state gives to the licensee 80 percent [of \$500 million] for design and permitting, and the open season is unsuccessful, the state may be in a better position to keep 100 percent of the inducement and develop the project without the licensee.

COMMISSIONER GALVIN responded that the failure of an initial open season is not necessarily the fault of the licensee. There will be many hurdles that the state and the producers need to identify and overcome. To proceed from the open season to obtaining a FERC certificate requires a tremendous amount of expertise and the licensee is needed to get the certificate.

[8:48:18 AM](#)

REPRESENTATIVE SAMUELS remarked, "You are spending 80 percent of the money on the highest risk part, you don't have a customer. You're designing it ...."

COMMISSIONER GALVIN noted that 80 percent is the maximum that the state may be requested to spend at that point.

REPRESENTATIVE SAMUELS said:

But assuming that you allow them to get up to 80 percent, going to 100 percent, and just hiring somebody, because then when you get to the end of the day ... you have something of value ... that you can sell it to the producers in exchange for the gas, you could sell it back to Mid America, you could certainly make your money back. ... You've now paid for something and you're not going to get your money back.

COMMISSIONER GALVIN assured the committee that the state will get its money back, the question is whether the state has the

opportunity to further maximize that return. He explained that the state needs to encourage applicants. Commissioner Galvin then said:

If [the applicants] look [at] this process and they say if we get to an open season and it's unsuccessful, then the state is going to kick us out the door and bring in somebody else and drive the rest of the way under some other scenario, then it's going to be less likely that we're going to get somebody in initially. We're locking in a relationship at the time the proposal is made, that's going to carry us all the way through to that FERC certificate. ... What we recognized, in designing this, is sort of risk sharing between the state and the companies, is we need to provide them with the opportunity to see a successful end product and if we cut them off at open season then their attractiveness of engaging in this at the initial phase becomes much lower.

REPRESENTATIVE SAMUELS observed that [the applicants] would be enthused about a successful open season.

COMMISSIONER GALVIN responded yes, but they also would be taking a risk that if they have an unsuccessful open season they would lose their investment.

REPRESENTATIVE SAMUELS asked about the ramifications of a second unsuccessful open season.

COMMISSIONER GALVIN noted that the state can not predict when the commitments and financing for the project will happen, but AGIA will begin a process with the best chance to succeed. If there is a time when the FERC certificate is issued, but the open season has not been successful, the state will look at alternatives. Commissioner Galvin said that he believes AGIA is the clearest path for success.

[8:54:16 AM](#)

REPRESENTATIVE RAMRAS said that his conception is that the legislature must address the two valuable commodities of time and money. The AGIA program spends money to obtain a set outcome in a certain period of time. He said that AGIA sets a finish line, but the uncertainty is, whether the producers will cross the finish line and will transport the gas to market. Representative Ramras remarked:

It strikes me that the whole philosophical approach to AGIA is that we swap the unknown of time for a finite amount of time. We seed that with our money, a non-specified amount, up to and not to exceed \$500 million, dollar-for-dollar, and then we have to wait and see whether the producers are good faith partners or whether the state has a, a deeper problem. ... Is that a pretty accurate read of what we are discussing this morning?

COMMISSIONER GALVIN agreed. However, he added, within one year the legislature will see the schedule for the expenditures and will have an opportunity to reject the proposal.

REPRESENTATIVE DOOGAN asked at what point the legislature will approve the expenditure of the \$500 million.

COMMISSIONER GALVIN explained that the intent of AGIA is to re-designate \$300 million held by Alaska Housing Finance Corporation (AHFC). These funds will be sufficient to proceed through the initial process and through open season. Within one year, there will be an expenditure timeline from the successful applicant, and more funds may or may not be needed.

[9:01:18 AM](#)

REPRESENTATIVE DOOGAN clarified that \$300 million is needed this legislative session.

COMMISSIONER GALVIN said yes.

REPRESENTATIVE DOOGAN observed that potential bidders will ask for funds within a range of zero to 80 percent of the \$500 million.

COMMISSIONER GALVIN reiterated that the maximum the bidders will ask for is \$500 million; the determination of 80 percent develops as the project progresses, and becomes 80 percent of the expenditures.

REPRESENTATIVE DOOGAN noted that one of the evaluation criterion listed in Section 43.90.170 requests the percentage of the state's matching contribution. How important, he asked, is that criterion compared to the other criteria?

COMMISSIONER GALVIN responded that the primary factors important to the state are the value to the state, and the likelihood of success. Net Present Value (NPV) to the state will be part of the evaluation and how much money the state will have to spend is a significant factor in determining NPV. If a lesser amount is required of the state, and the applicant is proposing a greater investment on its part, that will be a factor to be evaluated. Commissioner Galvin said that a lesser amount required from the state will also be considered to contribute to the likelihood of success.

9:04:33 AM

REPRESENTATIVE DOOGAN pointed out that the bidder needs to know how much each criterion is worth. Accordingly, if a legislator is evaluating the award, he/she must also know how much a criterion is worth in order to assess the award.

COMMISSIONER GALVIN agreed that DOR and DNR need to provide more detail and information on the objectivity of the economic evaluation. More information is also needed on how the commissioners will judge how the money will be split and the provisions related to the likelihood of success.

REPRESENTATIVE DAHLSTROM also requested clarification of the evaluation criteria. She then recalled her conversations with oil industry representatives who are encouraged to see a true commitment of money from the state. The state's matching contribution, she said, has garnered positive reactions from the industry.

9:07:48 AM

REPRESENTATIVE OLSON asked about a contingency plan in the event that the \$300 million held by AHFC is not re-designated.

COMMISSIONER GALVIN advised the committee that AGIA, if enacted, requires funds to be authorized by the legislature. The \$300 million will not come from the current budget, but was previously set aside for the development of the gas pipeline.

REPRESENTATIVE OLSON noted that the money was put in AHFC so it could not be spent last year.

REPRESENTATIVE SAMUELS asked how the commissioners will answer questions from the potential bidders on the \$500 million, and if the evaluation be open to the public.

COMMISSIONER GALVIN said that the commissioners will balance a desire to provide a level of expectation, in terms of what type of proposal is going to win favor versus another, but they will not create weighted, specified, percentages to score the applications.

[9:11:03 AM](#)

REPRESENTATIVE SAMUELS questioned how each of the applicants can get exactly the same answer to questions posed over a period of time and during different conversations.

COMMISSIONER GALVIN relayed that Representative Samuels' concern is shared by the commissioners. At this time, discussions with potential applicants are focused on the language in the bill. After its passage, the interaction with the applicants and the evaluation of the applications will be closely regulated. The Request for Application (RFA) will have clarifying language regarding the evaluation criteria and there will not be an informal exchange of information between the commissioners and the applicants.

REPRESENTATIVE SAMUELS recalled that the past administration maintained that the gas is not stranded. He also suggested that because the state is taking more than half the risk of developing the gas pipeline, and the producers will not have to pay the state's money back or provide equity in the project, AGIA is very appealing to the producers. Representative Samuels reminded the committee that an amendment to last year's gas pipeline bill required each builder to deposit \$300 million in escrow until a successful open season occurred. There was also the potential of a penalty for not meeting a certain deadline.

REPRESENTATIVE DAHLSTROM stressed that the successful applicant may not request any state money.

[9:15:23 AM](#)

COMMISSIONER GALVIN emphasized that the state is granting up to \$500 million as an inducement to the applicants. The applicants may forego requesting state funds to strengthen their proposals. In any event, AGIA's purpose is to encourage the producers to submit proposals to build the pipeline, or to participate as shippers. The state has a vested interest in seeing the Alaska gas pipeline project proceed, unlike producers and pipeline companies who can use their assets for other projects around the

world. Commissioner Galvin said that the bill is designed to create a robust competition for construction of the pipeline and increase the opportunities for the ultimate success of the project. In addition, AGIA responds to the oil industry's wish to see a financial commitment on the part of the state.

[9:18:32 AM](#)

MS. DAVIS added that the competitive process between the oil companies for construction of the gas pipeline has already begun. At the same time, the state wants to keep the process open to all applicants, and not begin eliminating potential applicants for any reason. After the Request for Proposal (RFP) process and open season, the state will invite competition for the most favorable terms for the state. Applicants, she said, will be cognizant of the competition for post-open season state funds.

REPRESENTATIVE SAMUELS reiterated that legislators do not know how the criteria will be weighted so they will be unable to determine the impact of the requested funds on the application. He remarked:

If the 80 percent match is equally as important as just having a headquarters here ... there is a huge discrepancy but the bill doesn't say ... where the 80 percent match comes in. So if somebody comes in and says "I don't want your money, I'll spend my own money and I'll beat my competitors that way" and then they don't beat their competitors....

[9:21:15 AM](#)

COMMISSIONER GALVIN confirmed that more information will be provided on how the commissioners will apply the evaluation criteria and how the impact of a successful, or unsuccessful, open season will be weighted.

REPRESENTATIVE DOOGAN posed three situations to Commissioner Galvin for his analysis: The legislature does not fund the \$500 million grant; the legislature gives a lesser amount than requested; or the legislature requires some return of ownership.

COMMISSIONER GALVIN answered that in not funding, or reducing the amount of funding, the state would be limiting the number of potential applicants. The state, he said, must demonstrate its commitment to the ultimate success of the project. Commissioner

Galvin explained that \$500 million is about one-half of the cost of acquiring a FERC certificate and an amount that recognizes the potential risk of this project. The application process also provides the licensee an opportunity to propose how to put this money toward the process. Regarding state ownership of the pipeline, he said that a guaranteed return on the state's investment will eliminate the state's risk. In order to demonstrate the state's interest in the project, and to encourage participation in the application process, the state needs to accept some risk in the initial phase. The state, he noted, receives significant value back for its investment through more participation, lower tariffs, expansion, and other provisions.

[9:26:08 AM](#)

REPRESENTATIVE DOOGAN acknowledged that each of these situations will result in less participation.

COMMISSIONER GALVIN said yes.

REPRESENTATIVE DOOGAN said:

If the most important element of getting a gas ... pipeline built is to get the producers to commit gas at the open season, so that the project can be financed, why aren't we paying the producers \$500 million to make that commitment? Wouldn't that be a better investment of that money?

COMMISSIONER GALVIN said:

It would, if that would be enough. But, ... one aspect of the previous contract that I think is illustrative to that point is that they put tremendous value, much more than \$500 million, onto that contract and we didn't get a commitment to do much of anything ... What we're trying to do is use that \$500 million to get us something that may get them to commit...

REPRESENTATIVE DAHLSTROM asked if Commissioner Galvin is willing to work with legislators on amending the evaluation criteria.

COMMISSIONER GALVIN said yes.

[9:28:50 AM](#)

REPRESENTATIVE RAMRAS remarked:

The fact is that the two commodities that are on the table are time and money. That's what I hear throughout this committee. ... One of the greatest failings, apart from fiscal certainty on oil and gas, on the Governor Murkowski's proposal, the other one was the uncertainty of the benefit of time spent and so what I appreciate about this proposal is that, although I have my own reservations about spending so much money, if it narrows down and makes the scope more finite for the time component, that to me is the most helpful element. .... I like that fact that this thing is time triggered. And that we are ... accelerating or expediting this process because the loss to the state for each year of delay are so significant. We certainly studied this. ... The cost component in there, that's the trade-off for the certainty of time, is the expenditure, and I think that that's something that those of us in the private sector are very accustomed to.

REPRESENTATIVE SAMUELS said:

Failed open season, we actually design a pipeline, get a FERC certificate. Second failed open season, now I have a five year contract with my partner to get financing. Now I'm at 11 years right now, if you add a second failed open season ... Second failed open season ... Time is of the essence. ... I understand this process, you're right, it gets to an open season 36 months, somebody's going to win the license, you're going to get to an open season, but, at the end of day, if you have a failed open season the first time and now ... the worst case scenario, we've spent 80 percent of the money, we're halfway in so we have a partner to the open season and we had 80 percent of the money to the certificate, and now we have a failed open season. Now we are \$500 million into it and we now have a partner that we're tied to for another five years, we have no gas. ... What the plan is ... other than suing to take Prudhoe Bay away....

COMMISSIONER GALVIN relayed that different factors will come into play after the passage of time. He pointed out that AGIA provides the opportunity for a mutual, or unilateral, decision to abandon the project. If sometime during the process it is

recognized that a licensee or project is not going to succeed, the state will have the authority to terminate the contract.

[9:36:26 AM](#)

CHAIR KOHRING announced the formation of a subcommittee chaired by Representative Dahlstrom, and consisting of Representatives Ramras, Doogan, and Samuels.

MS. DAVIS continued her analysis by noting that Section 43.90.120 is titled "Abandonment of project." Subsection(a) relates that if the commissioners and licensee agree that the project is uneconomic, then the inducements end, and there are no further obligations except on the part of the licensee to complete an audit. If the commissioners and licensee do not agree that the project is uneconomic, then an impartial third party will make the final determination.

REPRESENTATIVE SAMUELS stated that the terms of abandonment only address the "uneconomics" of the project. If the licensee has decided to abandon the project, and the arbitrator rules in favor of the state, can the licensee be forced to continue the project, he asked.

MS. DAVIS responded that in this instance, the licensee will be in violation of the license. Section 43.90.240 gives the state authority to revoke the license, recoup state money, and release the licensee.

COMMISSIONER GALVIN added that AGIA also allows the commissioners to seek remedies and damages allowable by law and that may be due after the breach of the terms of the license.

[9:41:51 AM](#)

MS. DAVIS continued to say that the abandonment provision establishes that if the state makes a payment in violation of the licensed project assurances, this would also result in abandonment of the project.

REPRESENTATIVE DOOGAN requested the definition of "uneconomic" as used in AGIA.

MS. DAVIS said that she believes that commercial parties will have their own definitions to use during negotiations. An impartial third party would bring to bear commercial or industry standards.

REPRESENTATIVE DOOGAN observed that the lack of a definition may cause problems in the future.

MS. DAVIS cautioned that uneconomic needs to be defined from the state's perspective.

REPRESENTATIVE DOOGAN urged Ms Davis to prepare a definition of uneconomic for the committee's review.

REPRESENTATIVE RAMRAS remarked:

A 12 percent or 14 percent return on a pipe is terribly uneconomic for Conoco, BP, or Exxon. But it's remarkably economic for Mid America or Trans-Canada. ... It means different things to different companies that have different capital structures and require different returns on investment. ... Presumably, every potential licensee ... is going to be a publicly traded company, and that's, I think, a critical piece of this to bear in mind....

[9:46:44 AM](#)

COMMISSIONER GALVIN agreed that clarification on this issue is needed. He advised that the question of whether the bill sets up the economic standards, or whether the companies should establish economic standards in their proposals, has not been answered.

REPRESENTATIVE SAMUELS warned that defining uneconomic will be difficult. He added that, after an unsuccessful second open season, the project will be uneconomic for everyone. He then asked:

What are you going to do when Trans-Canada comes up and says it's uneconomic because I think we're not going to get the gas? And you're going to go, well you can get out, but I'm going to sue you for all of the monies. Or you can get out and I'm going to sue you for damages, or you must continue with me on this partnership. ... Your partner wants out ....

[9:48:54 AM](#)

MS. DAVIS assured the committee that a definition of uneconomic can be stated from the perspective of the state, and a company

will then base its policy decisions on the definition included in the bill. She added that, an open season can be unsuccessful for legitimate commercial reasons, or perhaps, not. The state's perspective is what will provide the greatest certainty and security for investment in the project, from the applicant's point of view.

COMMISSIONER GALVIN explained that the proposals for the project will include contingency plans for certain events like an unsuccessful open season. The state will expect a commitment for action dependent upon anticipated variables and the companies are expected to have made plans as a part of the application. However, the state will need to decide what its reaction will be if a FERC certificate is issued and there is an unsuccessful open season.

[9:53:14 AM](#)

REPRESENTATIVE DOOGAN agreed that drawing a definition of uneconomic is difficult, but during the project it is possible for the licensee to require a change in the previously arranged terms. He recommended further discussion to decide whether the bill is better with or without the definition.

REPRESENTATIVE DAHLSTROM suggested that some questions may need to be discussed in executive session.

MS. DAVIS continued her analysis of Section 43.90.130, titled "Request for applications for the license." Subsection (a) requires the commissioners of DNR and DOR to issue the request for application within three months of the effective date of this chapter. Subsection (c) declares that the requests for application are exempt from the state's procurement code in order to accelerate the application process. Section 43.90.140 relates to the application requirements, which details the request for application (RFA) process. Information that the commissioners, the legislature, and the public will need from the applicant includes filing deadlines, a detailed description of the gas pipeline route, the design of the receiving and delivery points, analysis of the economic and technical viability of the project, an economic and technical work plan, and the timeline and budget for developing the project. In addition, if the proposed route passes through Canada, information must be included regarding international rights-of-way and licensing. Ms. Davis noted that if the proposed project includes the transportation, storage, and liquefaction of natural gas (LNG), details of the additional components

necessary for a LNG plant are required. The application must also include a schedule for holding the initial open season that confirms to FERC regulations.

[9:58:39 AM](#)

REPRESENTATIVE RAMRAS asked: "Why wouldn't the producers come to an open season?"

MS. DAVIS responded that uncertainty over the proposed shipping tariffs is one factor that may contribute to a failed open season. Shippers must negotiate for the conditions attached to their commitments to buy shipping capacities. Favorable shipping rates will enable a shipper to allocate the risk of cost overruns between itself and the pipeline companies. If a shipper does not want to ship gas, it may be because it has not been able to negotiate favorable tariff rates. Ms. Davis noted that the second factor may be the shippers' concern about the future market price for the sale of the gas.

REPRESENTATIVE RAMRAS suggested that the subcommittee look at tariffs in addition to the evaluation criteria.

MS. DAVIS expressed her belief that private enterprise can often solve its own problems. In addition, in AGIA, there is the opportunity for a shipper to realize benefits from participating in the initial open season. Therefore, the pipeline company will benefit from timing the open season to the advantage of both entities. A level of coordination and cooperation between the producers and the selected pipeline company is expected, she said.

[10:02:27 AM](#)

REPRESENTATIVE SAMUELS remarked:

I don't think the state, on a project this size, is, Trans-Canada or Enbridge or Mid America big enough to essentially backstop the tariff? ... Are they big enough, as a corporate entity, to backstop large tariff increases? And when the original legislation was going through Congress, there was talk by various players, you know, and industry disagrees on what they need or don't need, but the only one actually big enough would be the United States government. ... So instead of having the tariff subsidy they put in the loan guarantees. ... Are some of these relatively

small companies, which are huge corporations, big enough to take on that additional risk?

COMMISSIONER GALVIN informed the committee that the \$35 million to \$45 million estimate described earlier in the presentation represents value to the state, not the cost to a pipeline company. The ultimate question is whether the risk-sharing is a legitimate expectation, or whether the costs will be borne by the producers. He suggested that more information on this subject will be coming from testimony on AGIA by the industry. Commissioner Galvin also noted that the potential problems associated with a failed open season, after the FERC certificate is issued, may lead to intervention by Congress.

10:07:20 AM

MS. DAVIS continued her analysis of Section 43.90.140 subparagraph (B), regarding the FERC certification process. The applicants are required to use FERC pre-filing procedures and apply for the certificate of public convenience and necessity. If the project requires certification from the Regulatory Commission of Alaska (RCA), the time commitments remain the same. The applicant is required, after the first binding open season, to commit to soliciting applications to expand the pipeline every two years. Expanding the project will be based on reasonable engineering increments and by commercially reasonable terms. Expansion will also occur with the commitment of rolled-in rates that are not to exceed 15 percent of the initial tariff rates.

REPRESENTATIVE DOOGAN asked: "How did we get to the 15 percent figure?"

MS. DAVIS replied that the 15 percent was derived from analyst's determination of the typical costs of expansion. According to the scope of the expansion on the North Slope, this rate delivers the majority of the value.

MS. DAVIS returned to the application requirements of AGIA, and said that the applicant is prohibited from entering into negotiated rate agreements that by-pass the rolled-in rate requirements. In addition, the applicant, if its proposal includes using an existing gas treatment plant, must also agree to include the value of the gas treatment plant in the calculation of the tariff at the net book value. The applicant must specify the percentage of the state's matching contribution after the open season, must ensure financing does not exceed 70

percent debt, and demonstrate how to handle cost overruns. This section of AGIA also requires that the applicant commit to designate five delivery points with distance sensitive rates to delivery points within the state, establish a local headquarters for the project in the state, and hire qualified local residents to work on the project.

MS. DAVIS said that Section 43.90.150 relates to the process of the application review. The commissioners will receive the applications and reject any incomplete applications. They may request additional information, if desired.

[10:12:41 AM](#)

REPRESENTATIVE DOOGAN asked if all applicants will be requested to supply the same information.

MS. DAVIS confirmed that, even though the projects may differ and the types of information may be irrelevant, the state's intent is that all applicants will be treated equally.

REPRESENTATIVE DOOGAN stated that two comparable applications would be required to provide identical information.

COMMISSIONER GALVIN said that the intent is that the commissioners can request details about a specific proposal when necessary. He added that earlier in the process, the timeframe will allow for full competition with no competitive advantage. Later, the questions and additional information will be made public at the same time as the original application.

MS. DAVIS added that additional pieces of information can be requested from all of the applicants during the review process.

MS. DAVIS relayed that Section 43.90.160 is titled "Proprietary information and trade secrets." An applicant is required to identify and demonstrate that information on the application is proprietary or a trade secret, and not subject to public disclosure.

[10:16:24 AM](#)

REPRESENTATIVE DOOGAN asked how an applicant can demonstrate that information is proprietary.

MS. DAVIS explained that the company would need to demonstrate that the information is non-public, unavailable, protected by

other laws, or will, if disclosed, put the company at a material disadvantage.

MS. DAVIS informed the committee that Section 43.90.170 identifies the application evaluation criteria. The evaluation criteria includes: timing, the management of cost overruns, transportation rates, the initial design capacity, the percentage of the state's matching contribution, the reasonableness, specificity and feasibility of the work plan, the timeline and budget, and the applicant's financial records. Section 43.990.180, she said, relates to the application notice, review, and comments. After the applications are complete, they will be open for public comment for a 60-day period.

REPRESENTATIVE DOOGAN returned the committee's attention to the application criteria paragraph (7) and asked how an unpaid federal judgment would affect an applicant's record of performance.

COMMISSIONER GALVIN indicated that this provision is a standard clause to ensure that the commissioners are able to use information to approve or reject an application.

REPRESENTATIVE DOOGAN said: "So this is a term of art someplace. And there's either a definition or history to tell us the specifics of how we would be defining, say, business ethics in this?"

MS. DAVIS said that is correct.

REPRESENTATIVE DAHLSTROM recommended that application criteria paragraph (7) also be discussed by the subcommittee.

[10:21:10 AM](#)

MS. DAVIS continued her analysis of Section 43.90.190, "Notice to the legislature of intent to issue license; denial of license." She said that, once the commissioners decide that an application meets AGIA's criteria and requirements, they will issue a determination of findings and publish a notice of intent to issue a license with the written findings. This notice will be forwarded to the legislature for action. The commissioners also have the right to issue a written finding that none of the applications meet the criteria of the bill. Section 43.90.200 relates to legislative action regarding the issuance of the license. Ms. Davis noted that within 30 days of the receipt of

the commissioners finding, the legislature can disapprove of the issuance of the license by a joint resolution.

CHAIR KOHRING asked if the disapproval is by resolution of the legislature.

MS. DAVIS answered that the notice of intent to disapprove would be a joint resolution of the legislature.

CHAIR KOHRING asked whether the joint resolution would prevail if the administration did not accept the decision of the legislature.

COMMISSIONER GALVIN said that the intent is that the resolution by the legislature can not be overturned by the governor. However, he recommended that this question be referred to the Department of Law.

REPRESENTATIVE OLSON asked: "What happens if we receive it in the middle of the first or second special session?"

[10:23:36 AM](#)

MS. DAVIS assured the committee that the 30 day time limit could be accommodated within a special session.

CHAIR KOHRING asked what would happen if the receipt of the finding occurs at the end of a regular session.

MS. DAVIS indicated that that situation will require a special session.

COMMISSIONER GALVIN added that the resolution is not required, and would only be necessary if the legislature decides to act and overrule the decision of the commissioners.

MS. DAVIS noted that Section 43.90.210 relates to certification by regulatory authority and project sanction. A licensee is required to accept the FERC or RCA certificate if awarded, and to proceed with the project within one year, if financing is approved, or obtain financing within five years. If the licensee does not sanction the project at this time, it must abandon the project and transfer the certificates, project data, etc., to the state, at no cost to the state.

[10:25:54 AM](#)

REPRESENTATIVE DOOGAN asked: "Can you explain to me why the bill imagines that the license might be awarded to somebody who doesn't have the financing?"

MS. DAVIS answered that FERC has the authority to issue the license notwithstanding the credit worthiness of the applicant.

COMMISSIONER GALVIN urged the committee to recognize that the only entities that can initially guarantee financing are the large producers. Through AGIA, at some point the state must look to the licensee for proof of specific credit support. The state is not obligated to wait for the entire five years. This provision, he said, will alert the applicant to the time limit for obtaining the financing and commitments of gas from the producers.

CHAIR KOHRING recalled that the Alaska Railroad Corporation has tax exempt, low interest bonds available to companies.

COMMISSIONER GALVIN said he was unfamiliar with the Alaska Railroad Corporation bonds, but that there are opportunities for state, federal, consumer groups, utilities, and others, to participate in financing the project.

[10:30:50 AM](#)

MS. DAVIS informed the committee that Section 43.90.220 relates to the amendment or modification of project plans. Changes to the plan can be approved through the commissioners if they are the result of circumstances outside the licensee's control and were not reasonably foreseeable. However, these changes can not diminish the value to the state of the project. Section 43.90.230 is relevant to records, reports, conditions, and audit provisions. Subsection (a) requires the licensee to maintain records for audit purposes. In addition, the commissioners will have a representative present at all meetings of the licensee's governing body and equity holders that relate to the project. In addition the representative will have access to all information given to equity holders. Section 43.90.240 defines license violations and damages. Ms. Davis said that a licensee is in violation of its license if it uses state money for other purposes, departs from the approved plan, or violates any terms of AGIA, or violates the terms of the license. Commissioners will give written notice of the violation and allow 90 days to resolve the violation. If the violation is confirmed the state has rights to recover.

10:33:30 AM

REPRESENTATIVE DOOGAN asked whether the state will take over all the work that had been done on the existing project, in addition to the license.

MS. DAVIS answered yes.

REPRESENTATIVE DOOGAN further asked whether the license and project could then be transferred to another licensee.

MS. DAVIS answered yes. She then continued her analysis of Article 3, that focuses on shippers and the inducement portion of AGIA. Section 43.90.300 outlines the qualifications for receiving resource inducements. Ms. Davis noted that inducements are acquired by obtaining a firm transportation capacity at the first binding open season. Royalty inducements will be based on regulations written by the commissioner of DNR and will establish the fair market value for the state's royalty gas and to exercise the state's right to switch between royalty gas in-value and in-kind. As a condition to receiving the royalty inducements the shipper must agree not to contest rolled-in rates. The commissioner of DNR will review the regulations every two years. A shipper has the right to opt into these benefits if desired. Section 43.90.320 outlines the gas production tax exemption. The intent of this exemption is that by contract, a shipper can exempt the amount that is equal to the difference between its gas production tax obligation and the tax that was in effect at the first binding open season. This benefit continues for the first ten years of the commercial operation of the pipeline.

10:36:21 AM

REPRESENTATIVE DOOGAN asked what the value of this tax exemption will be to the producers.

MS. DAVIS explained that if there is no change in the tax structure, the value is zero. However, if the tax rate is increased in the future, the value will increase also.

REPRESENTATIVE DOOGAN questioned whether the value to the producers can be calculated at different tax rates.

COMMISSIONER GALVIN offered to provide the committee estimates of tax rate changes. He said that the models will give a perception of risk on the part of the producers by limiting the

uncertainty of the state's future tax rate. The intent is to be responsive to requests from the producers. Commissioner Galvin opined that Alaska is a stable tax regime, and reminded the committee that the tax freeze will need to survive a constitutional challenge.

REPRESENTATIVE DOOGAN asked:

If the tax rate right now, is, I think it's 22.5 percent on gas, if, how much, making the assumptions that you have already made in your presentation on AGIA, for the kind of pipeline you're building and the ... rate at which gas can be passed through it and all the rest of that, how much would one percent ... increase or decrease, in that tax be worth?

COMMISSIONER GALVIN indicated that that information would be provided to the committee.

MS. DAVIS advised the committee that Section 43.90.330 creates the position of the AGIA coordinator, which is an inducement for both the pipeline construction company and the shippers. This position will coordinate the activities of the state agencies, assist with the compliance of the requirements of AGIA, and coordinate with the federal coordinator. The coordinator will focus on actions taken by state agencies relating to the project.

[10:41:41 AM](#)

CHAIR KOHRING asked whether the coordinator will be authorized to hire additional individuals to support this position.

MS. DAVIS, responding to questions, stated that the AGIA coordinator will be a single position, serving until one year after the operation of the pipeline begins, and at the discretion of the governor.

[HB 177 was held in committee]

[10:45:00 AM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 10:45 p.m.

