

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON OIL AND GAS

March 28, 2007

7:34 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 Carl Gatto
Representative John Coghill

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
03/19/07	(H)	Heard & Held
03/19/07	(H)	MINUTE(O&G)
03/20/07	(H)	O&G AT 3:00 PM BARNES 124
03/20/07	(H)	Heard & Held
03/20/07	(H)	MINUTE(O&G)
03/21/07	(H)	O&G AT 5:30 PM SENATE FINANCE 532
03/21/07	(H)	Heard & Held
03/21/07	(H)	MINUTE(O&G)
03/22/07	(H)	O&G AT 3:00 PM BARNES 124
03/22/07	(H)	Heard & Held
03/22/07	(H)	MINUTE(O&G)
03/23/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/23/07	(H)	Heard & Held
03/23/07	(H)	MINUTE(O&G)
03/24/07	(H)	O&G AT 1:00 PM SENATE FINANCE 532
03/24/07	(H)	-- Public Testimony --
03/26/07	(H)	O&G AT 8:30 AM CAPITOL 106
03/26/07	(H)	Heard & Held
03/26/07	(H)	MINUTE(O&G)
03/27/07	(H)	O&G AT 3:00 PM BARNES 124
03/28/07	(H)	O&G AT 7:30 AM CAPITOL 106
03/28/07	(H)	O&G AT 8:30 AM CAPITOL 106

WITNESS REGISTER

RON BRINTNELL, Director
Gas Development
Enbridge, Inc.
Calgary, Alberta
Canada

POSITION STATEMENT: Testified at the hearing on HB 177.

WENDY D. KING, Manager
Alaska North Slope Gas Development
ConocoPhillips Alaska, Inc.
Anchorage, Alaska

POSITION STATEMENT: Testified at the hearing on HB 177.

MARK HANLEY, Manager
Alaska Public Affairs

Anadarko Petroleum Corporation
Anchorage, Alaska

POSITION STATEMENT: Testified at the hearing on HB 177.

ACTION NARRATIVE

CHAIR VIC KOHRING called the House Special Committee on Oil and Gas meeting, which recessed on 3/27/07 at 5:51 p.m., back to order at [7:34:42 AM](#). Representatives Ramras, Doogan, Kawasaki, Dahlstrom, Samuels, and Kohring were present at the call back to order. Representative Olson arrived as the meeting was in progress.

HB 177-NATURAL GAS PIPELINE PROJECT

[7:35:08 AM](#)

CHAIR KOHRING announced that the first 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."

[7:35:45 AM](#)

RON BRINTNELL, Manager, Alaska Gas Project, Enbridge Inc. (Enbridge), informed the committee that he will present Enbridge's candid views on the Alaska gas pipeline project. Enbridge, he said, wants to see the project go ahead because the gas supply is desperately needed. He continued to say that Enbridge maintains a network of pipelines supplying oil and gas throughout North America and abroad, including the Alliance line, which is very similar to the proposed Alaska gas pipeline. Enbridge also owns Canada's largest utility company, is knowledgeable regarding the supply of natural gas, and is experienced regarding the construction and maintenance of facilities in northern climates.

[7:39:38 AM](#)

REPRESENTATIVE RAMRAS asked for Enbridge's market capitalization value.

MR. BRINTNELL answered that Enbridge's value is approximately US\$15 billion and its stock is traded on the U. S. and Toronto stock exchanges.

REPRESENTATIVE RAMRAS further asked for Enbridge's balance sheet debt level.

[7:40:41 AM](#)

MR. BRINTNELL responded that its debt equity ratio is 65 percent to 35 percent.

REPRESENTATIVE RAMRAS then asked how Enbridge would bond the gas pipeline project.

MR. BRINTNELL explained that the project would be financed by shipping commitments.

[7:41:32 AM](#)

REPRESENTATIVE RAMRAS observed that Enbridge would leverage financing back from the customer to the project source.

[7:41:42 AM](#)

MR. BRINTNELL explained that, directly or indirectly, it is the strength of the shipping commitments, the producers, and the state that will be the basis of obtaining credit. Mr. Brintnell continued his presentation by noting that during previous projects Enbridge has gained significant experience in terms of ordering steel and dealing with the tight labor market. He added that Enbridge is ready to train Alaskan workers who are interested in working on Canadian projects now; however, Enbridge's current projects will be near completion by the time construction begins on the Alaska gas pipeline.

[7:42:51 AM](#)

MR. BRINTNELL told the committee that Enbridge believes that the pipeline can not be built without the producers as shippers. The North Slope producers and the state are in the best position to make shipping commitments. His concern, he said, is that delay in the construction of the gas pipeline will cause other sources of energy to be developed because the market for energy is high. Mr. Brintnell encouraged the state and the producers to re-establish negotiations. He said Enbridge feels that gas pipeline development through the Federal Energy Regulatory Commission (FERC) process is a well defined and sound process for Alaska.

[7:46:38 AM](#)

MR. BRINTNELL said that Enbridge is encouraged to see that the state has placed a priority on the gas pipeline; however, the Alaska Gasline Inducement Act (AGIA) is insufficient due to its focus on the pipeline and not on the producers and shipping commitments.

[7:47:30 AM](#)

CHAIR KOHRING asked for suggestions on how to accomplish the goal of obtaining commitments from the producers and the shippers.

[7:47:45 AM](#)

MR. BRINTNELL suggested that the state and the producers begin a flexible and open dialog. He said that he believes that the producers want the gas pipeline to be constructed.

REPRESENTATIVE DOOGAN asked for confirmation that Enbridge believes that the economics are such that a commitment for gas will result in viable project.

[7:49:50 AM](#)

MR. BRINTNELL assured the committee that the project is commercially viable, but not without risk, due to the cost of the project and the unstable market price of gas.

[7:50:36 AM](#)

REPRESENTATIVE RAMRAS commented that the price of gas today is \$7.20 according to the Henry Hub natural gas index.

[7:50:50 AM](#)

MR. BRINTNELL pointed out that gas prices have ranged from \$15 million cubic feet (Mmcf) to \$4 Mmcf, due to storms, warmer winter temperatures, and the availability of gas reserves.

[7:51:31 AM](#)

REPRESENTATIVE DOOGAN asked what the state could do to lower the project risk and gain commitments from the producers.

MR. BRINTNELL responded that the risk is not just the pipeline cost but also the future market price and, most importantly, the uncertainty of tax rates.

[7:54:31 AM](#)

REPRESENTATIVE DOOGAN asked whether Enbridge has built a pipeline that, after construction, became uneconomic by changes in the tax regime.

[7:55:16 AM](#)

MR. BRINTNELL recalled that, typically, pipeline companies will pass increases in tax rates to the shippers. He explained that the pipeline company takes its risk in controlling operating and construction costs.

[7:56:40 AM](#)

REPRESENTATIVE DOOGAN re-stated his question by asking whether Enbridge is aware of a project that became uneconomic due to a tax rate change assessed to the producers.

[7:57:31 AM](#)

MR. BRINTNELL answered no; however, as a shipper, the pipeline company would not be impacted unless the tax rate is so high the producers can not ship their product.

[7:59:32 AM](#)

REPRESENTATIVE SAMUELS requested clarification on Enbridge's need to be part of a consortium in order to participate in the gas pipeline project.

[8:00:16 AM](#)

MR. BRINTNELL explained that, to participate, his company will require shipping commitments prior to developing the project. Enbridge will not hold an open season unless it is confident of a successful outcome. Typically, non-binding open seasons can be held at a lower cost and garner many responses. Enbridge's job, he said, is to develop pipeline concepts, look at the fundamentals, and propose a project through a non-binding open season or through direct dialog with producers. Before proceeding to a binding open season, Enbridge will have shipping commitments in place.

[8:02:29 AM](#)

CHAIR KOHRING asked whether rights of way and permitting in Canada will pose problems.

[8:03:08 AM](#)

MR. BRINTNELL replied that permits on the Canadian side will fall in place in a timely fashion. The Canadian government, he said, knows the importance of this project. He assured the committee that TransCanada Corporation (TransCanada) does not have exclusive rights to build the pipeline. In fact, the Canadian government has announced that its priorities for a northern gas pipeline are to let the market decide on the builders, to establish a regulatory regime, to support Aboriginal economic development, and to retain benefits for Canadians. Mr. Brintnell continued to say that creating alignment with the producers is important due to their experience, financial resources, and the fact that the producers will bear the largest risk during the development of the project.

[8:10:36 AM](#)

REPRESENTATIVE DOOGAN requested a description of the project Enbridge is proposing.

[8:10:57 AM](#)

MR. BRINTNELL replied that his company anticipates the construction of a gas pipeline to Alberta, Canada. After reaching Alberta, there is sufficient capacity in existing pipelines to reach the U. S. markets. Mr. Brintnell cautioned that the existing pipelines, however, may not be the best choice for shipping the gas. He also warned the committee that they should be concerned about the possibility of a failed open season due to the high cost of the project and the unbalance of the risks involved.

[8:14:24 AM](#)

CHAIR KOHRING asked whether the \$500 million is a sufficient inducement to prospective applicants.

[8:14:43 AM](#)

MR. BRINTNELL, replied that the grant is a favorable factor, but it is unnecessary.

CHAIR KOHRING asked for Enbridge's opinion of the evaluation criteria established in AGIA.

[8:15:56 AM](#)

MR. BRINTNELL informed the committee that the AGIA process is unnecessary. He expressed his belief that negotiations with the producers are most important for the project to proceed.

[8:17:11 AM](#)

REPRESENTATIVE DOOGAN asked for more information regarding the value of the \$500 million grant.

MR. BRINTNELL answered that the real issue is the longer risk, not the initial cost. He pointed out that during the construction of the first gas pipeline in Alberta, the future growth of the market was unknown.

[8:20:36 AM](#)

MR. BRINTNELL observed that at this time it is unrealistic to expect builders to make an unconditional commitment to the project due to uncertainties related to permitting, regulations, market price, and the labor market. Mr. Brintnell added that completing FERC and [Canadian] Northern Economic Development (NED) applications requires spending hundreds of millions of dollars that Enbridge cannot spend without commitments from shippers. He concluded his presentation by saying that AGIA does not address the tax concerns of the producers. He expressed his belief that the terms of AGIA are weighted in favor of the pipeline companies and do not resolve the producer's issues; therefore, AGIA will not attract their support. In addition, government financial assistance is not essential, and the additional regulatory process outlined by AGIA is unnecessary. Finally, Mr. Brintnell emphasized that Enbridge believes in the future demand for natural gas and desires a role in the construction and operation of the pipeline.

[8:28:33 AM](#)

REPRESENTATIVE SAMUELS asked how long it would take for Enbridge to develop a consortium in order to participate in the project.

[8:29:23 AM](#)

MR. BRINTNELL opined that the first step would be to complete fiscal arrangements with the producers. After that, agreements between partners will be completed within months.

[8:29:51 AM](#)

REPRESENTATIVE SAMUELS then asked how long it would take for the consortium to prepare for open season.

[8:30:08 AM](#)

MR. BRINTNELL told the committee that a reasonable estimated timeline is two to three years.

[8:30:54 AM](#)

REPRESENTATIVE SAMUELS asked for Mr. Brintnell's opinion of the 15 percent limit [on a tariff increase].

[8:31:27 AM](#)

MR. BRINTNELL replied that rolled-in rates (RIR) are a concern for Enbridge for the reason that, as a potential shipper, it is required to get permission for its shipping rates from a regulatory body. Thus, subsequent rate increases are undesirable.

[8:34:17 AM](#)

REPRESENTATIVE SAMUELS remarked:

What percentage of the gas that you haul in Canada, where they have the presumption of rolled-in rates, is negotiated? And what part of it is just rolled-in, that's because the government says that that's the policy of the country?

[8:34:45 AM](#)

MR. BRINTNELL replied that the Alliance pipeline has rates that were negotiated with the shippers prior to construction; recently constructed pipelines in Canada and the U. S. tend to have negotiated rates.

[8:37:03 AM](#)

MR. BRINTNELL, responding to a question, informed the committee that Canada's energy regulatory body is the National Energy Board (NEB).

[8:37:50 AM](#)

CHAIR KOHRING announced that the next order of business would be testimony by ConocoPhillips Alaska, Inc.

[8:39:18 AM](#)

WENDY D. KING, Manager, Alaska North Slope Gas Development, ConocoPhillips Alaska, Inc., informed the committee that ConocoPhillips Alaska, Inc., (ConocoPhillips), is the state's largest producer of oil and gas and has completed 1,200 uninterrupted liquefied natural gas (LNG) shipments since 1969. Ms. King continued to say that ConocoPhillips is the largest acreage holder on federal and state lands on the North Slope, has drilled 60 exploration wells since 1969, and that 13 percent of its production is based in Alaska. The construction timeline of the natural gas pipeline is critical, and ConocoPhillips is committed to development of the North Slope gas resource. She noted that the midstream part of the project includes the transmission lines to transport the gas to the gas treatment plant (GTP) and the large pipeline to take gas to Alberta, Canada. Ms. King explained that the resource terms of the project are related to the gas itself or to the holders of the firm transportation (FT) commitments. She compared the Alaska gas pipeline to previous North American projects and pointed out its large size and estimated cost.

[8:47:15 AM](#)

REPRESENTATIVE DOOGAN confirmed that ConocoPhillips's project cost estimate is for a gas pipeline to Alberta.

[8:48:02 AM](#)

MS. KING clarified that the 2001 cost estimate of \$20 billion is for a pipeline terminating in Chicago. She added that questions concerning the costs of the Alberta to Chicago portion of the pipeline depend on the future capacity, cost of fuel, and tariffs on existing pipelines. Ms. King continued to say that another key unknown to the cost of the project is the instability of the market price for natural gas. There is no

question, she said, that U. S. markets need a long term source of gas; however, industry market predictions of prices are unreliable. She affirmed that ConocoPhillips wants to work with the administration and the legislature on a balanced framework that will advance the project. Ms. King informed the committee that ConocoPhillips has artic experience and financial strength to bring to the project.

[8:51:03 AM](#)

REPRESENTATIVE RAMRAS commented that the "Predicting Natural Gas Prices" chart provided to the committee by ConocoPhillips is a distortion and asked for the source of the information.

[8:54:19 AM](#)

MS. KING assured the committee that she would be happy to provide the details and specifics that support the data presented.

[8:55:11 AM](#)

REPRESENTATIVE RAMRAS reiterated his concern that the data presented not an accurate presentation of the movement in the price of natural gas.

[8:55:47 AM](#)

MS. KING continued her testimony by saying that ConocoPhillips has already spent millions of dollars to advance the Alaska gas pipeline project. She said that her company is in the process of reviewing the terms of AGIA, and is interested in working with the legislature to address the resources needed to support the long term shipping commitments. Ms. King pointed out the imbalance of the risk factors regarding the midstream and upstream portions of the project. ConocoPhillips's review of AGIA reveals that the initial, and greater, risk is borne by the producers. The first area of ConocoPhillips's is concern is exclusivity, and it asks why the state would block alternative projects and discourage the free market process.

[8:59:04 AM](#)

MS. KING referred to AS 43.90.340 and remarked:

I'll read from these sections here, except as otherwise provided in this chapter, I'm on line 23

now, "The state grants a licensee assurances that the licensee has exclusive enjoyment of the inducements provided under this chapter. If the state extends to another person preferential royalty, tax, or monetary treatment for the purpose of facilitating the construction of a competing natural gas pipeline project in this state, and if the licensee is in compliance with the requirements of the license and with the requirements of state and federal statutes and regulations relevant to the project, the licensee is entitled to payment from the state of an amount equal to three times the total of the reasonable costs that the licensee has incurred in developing the licensee's project as of the date that the state first extended preferential treatment to another person." ... Why wouldn't state offer the benefits of streamlined coordination to any project? That was how the federal process was set up.

MS. KING further noted that the inducements provided in section 340(b) will only apply to the licensed project and could be interpreted to mean that state agencies have the authority to burden competing projects by withholding permits and authorizations.

[9:01:15 AM](#)

REPRESENTATIVE DOOGAN urged Ms. King to explain the existence of a competing project.

[9:01:32 AM](#)

MS. KING expressed her belief that one project will be developed but that there may be spur lines and complimentary projects. What is important, she said, is that multiple projects should advance to licensing.

[9:03:03 AM](#)

REPRESENTATIVE DOOGAN said:

I don't understand how we get a competing pipeline project. ... I'm having a hard time with the practical problem that this represents.

MS. KING remarked:

If somebody has some good ideas, we think it's important that they could be able to advance their project. ... What if a winner is chosen and it's the wrong winner?

[9:04:49 AM](#)

REPRESENTATIVE RAMRAS noted that, after an election, it is incumbent on everyone to work with the successful candidate. For this reason, he suggested, it is also incumbent on ConocoPhillips to participate in the legislation that passes and to work with the state for the success of the project.

[9:06:42 AM](#)

MS. KING highlighted that ConocoPhillips is making efforts to assess the bill and make improvements.

[9:07:32 AM](#)

REPRESENTATIVE RAMRAS repeated his belief that the producers can suggest improvements, but ultimately they need to work within the framework of AGIA.

[9:08:13 AM](#)

REPRESENTATIVE DOOGAN stressed that the inducements are an integral part of AGIA and asked what progress can be made without them.

[9:10:17 AM](#)

MS. KING advised the committee that ConocoPhillips is not proposing removing inducements, but allowing them to apply to other projects.

[9:11:14 AM](#)

REPRESENTATIVE DOOGAN reminded Ms. King that inducements must be exclusive to be meaningful.

[9:12:11 AM](#)

MS. KING pointed out that three of the four inducements are exclusive and those are of concern to ConocoPhillips. The \$500 million grant is acceptable, she said.

[9:14:16 AM](#)

REPRESENTATIVE DAHLSTROM requested clarification of ConocoPhillips objections to AS 43.90.330.

[9:15:30 AM](#)

MS. KING responded that the company is concerned that the language will allow roadblocks to be put in the way of a competing project.

[9:16:45 AM](#)

REPRESENTATIVE DAHLSTROM expressed her understanding that the position of an Alaska Gasline Inducement Act coordinator is meant to be a help, not a roadblock. She said she will research the intent of the creation of this position.

[9:17:33 AM](#)

MS. KING continued her testimony by calling the committee's attention to the 16 application requirements described in AS 43.90.140. She surmised that rejection of one item on the application would result in a non-conforming bid.

REPRESENTATIVE RAMRAS assumed that the committee will be addressing this situation through an amendment.

[9:19:32 AM](#)

REPRESENTATIVE DAHLSTROM agreed with Representative Ramras, and she then added that the bill also allows an opportunity for the applicant to complete an incomplete application.

[9:20:33 AM](#)

MS. KING offered an example to illustrate ConocoPhillips objections. She told the committee that AGIA requires a number of fixed deadlines, and that the industry's experience is that with a project this size, flexible and alternative work commitments are vital.

[9:22:11 AM](#)

REPRESENTATIVE RAMRAS requested the location in the bill of the dates to which she was referring.

[9:22:19 AM](#)

MS. KING answered:

Conclude by a date certain, it's ... page 5, line 17 through 30, there's three dates in there. There's the [indisc.] pre filing, the applying for the FERC certificate and for concluding an open season. ... And page 4, ... line 19, receipt and delivery points, and the size and design capacity of the proposed natural gas pipeline at the proposed receipt and delivery points. That is what an open season is for.

[9:24:04 AM](#)

REPRESENTATIVE RAMRAS expressed his desire to remind the producers that AGIA'S timeline is its best feature. The bill requires only the outline of a project and an expedited open season will accelerate the process.

[9:26:44 AM](#)

MS. KING assured the committee that ConocoPhillips understands work commitments. However, she noted that conceptually million of dollars can be saved by proper planning in the early stages of a project. ConocoPhillips wants to find creative solutions to the challenge of building the best project at the lowest price.

[9:28:21 AM](#)

REPRESENTATIVE RAMRAS remarked that the administration is sensitive to the need to keep tariffs low.

[9:28:54 AM](#)

MS. KING explained that tariff prices are determined by the capital cost of project. ConocoPhillips is focused on maintaining a low capital cost project. She then returned to the subject of bid requirements and said that ConocoPhillips estimates a cost of \$400 million to \$500 million to conclude an open season. Bid requirements specify that the successful applicant would take a portion of the \$500 million grant prior to the open season. In fact, ConocoPhillips feels this should be a variable and should be determined by the company. Unfortunately, another concern resulting from the exclusivity of

the state's evaluation process is the possibility of an applicant submitting empty promises and phony estimates.

[9:31:46 AM](#)

MS. KING further said that ConocoPhillips believes it has creative solutions to these questions. Granted, the state wants must-haves included in this project, and the applicants, she noted, can include those items in the context of bid variables. She returned to her analysis of AGIA and said that Article 3 relates to the resource owners and that section 310 of Article 3 creates the greatest obstacle: the state's taxes and royalty terms. The importance of fiscal stability is noted by the administration, but the bill is designed to make changes to the tax structure not by negotiation, but by regulation. ConocoPhillips will be asked to sign up for 15 year to 25 year shipping commitments, even though royalty in-kind (RIK) and royalty in-value (RIV) terms can change. In addition, the Production Profits Tax is stable, but other taxes may change. ConocoPhillips needs to know what the resource package looks like, and suggests that the resource package be converted to a variable bid package.

[9:36:31 AM](#)

REPRESENTATIVE RAMRAS asked:

If you had a choice, ... and you could either change one of these two variables, either the time increments that are prescribed in the bill, or the resource package. Which of those two would be the more important variable change to you?

[9:36:59 AM](#)

MS. KING said:

We put those both in the context of bid requirements to bid variables, so we think by that solution we can address both of those issues.

[9:37:31 AM](#)

REPRESENTATIVE RAMRAS asked:

If we opened it up so that it can be a much more interpretive resource package, if you will, if we

leave the prescribed time requirements in there is that something that is accommodative to Conoco? ... Would you rather keep the time increment and be able to innovate your own resource package design?

9:39:30 AM

MS. KING replied that ConocoPhillips requires the flexibility to provide suggestions regarding a resource package and the ability to offer alternatives to time management of the project. Both of these choices are critical, she said.

9:40:06 AM

REPRESENTATIVE RAMRAS requested an answer to his question as soon as possible.

9:41:52 AM

MS. KING told the committee that she will be submitting recommendations for amendments to HB 177.

9:44:00 AM

REPRESENTATIVE SAMUELS expressed his belief that the competition to build the pipeline is the race for the gas. Thus, ConocoPhillips has an advantage because they have the gas. He then said:

If you make everything a bid variable, if you don't have gas, are you even going to come to play? ... How do you find that middle ground there, ... I believe true competition is ... is to let everybody come back with their best proposal. ... But automatically you get to attach gas to yours so you have this huge advantage and then nobody else plays, and we're right back to where we started. ... Going completely the other way, making everything a bid variable, might exclude all other players other than the producers.

9:46:51 AM

MS. KING commented that ConocoPhillips doesn't want litigation. She also reminded the committee that the producers are independent of each other. The prescriptive lists of requirements in the bill remain a problem for ConocoPhillips.

[9:49:25 AM](#)

REPRESENTATIVE SAMUELS asked if ConocoPhillips is authorized by its operating agreements to ship gas independently of its partners.

[9:50:25 AM](#)

MS. KING responded that the operating agreements vary from field to field. This issue, she added, will need to be addressed on a case by case basis.

[9:51:00 AM](#)

REPRESENTATIVE SAMUELS asked if internal operating agreements are a matter of public record.

[9:51:28 AM](#)

MS. KING expressed her understanding that the administration has access to the operating agreements for Prudhoe Bay. She noted that overall oil production in Prudhoe Bay may be affected by one party taking off gas.

[9:52:33 AM](#)

REPRESENTATIVE SAMUELS further asked whether ConocoPhillips, if in a partnership with a pipeline company, would be in a position to spend \$400 million in preparation for open season.

[9:53:41 AM](#)

MS. KING replied that ConocoPhillips would participate in parallel work activities during the preparation for the open season. The concern is that if open season is held and the technical work is not done to update the cost estimate, customers will not trust the cost estimates and will be reluctant to bid. The three producer's previous cost estimate, she noted, cost \$125 million to complete and she estimated an update would take six months at an unknown cost.

[9:55:55 AM](#)

CHAIR KOHRING recessed the meeting until after the House floor session.

[11:21:30 AM](#)

CHAIR KOHRING adjourned the House Special Committee on Oil and Gas meeting of Tuesday, March 27, 2007, and called to order the meeting of Wednesday, March 28, 2007. Representatives Doogan, Kawasaki, Dahlstrom, Samuels, and Kohring were present at the call to order. Representatives Olson and Ramras arrived while the meeting was in progress.

CHAIR KOHRING announced that Wendy King of ConocoPhillips Alaska, Inc. will complete her testimony.

[11:21:32 AM](#)

MS. KING answered a question Representative Samuels asked prior to the meeting's recess. She said that the mandated RIR operating agreements on state approved units are a matter of public record.

[11:23:07 AM](#)

MS. KING continued by saying that ConocoPhillips's testimony on HB 177 is focused on eliminating exclusivity and changing bid requirements to bid variables. The final item to be addressed regarding bid variables is the question of mandating expansions and rolled-in rates (RIR). ConocoPhillips operations include acreage in the National Petroleum Reserve - Alaska (NPRA) which is known to be gas prone. Mandated expansions and RIR's mean that the initial shippers will be required to make firm shipping commitments, thereby taking on more risk than required by existing statutes and regulations. She pointed out that parties can wait until after the project is built with the knowledge that expansion will occur and the tariffs will be mitigated through RIR subsidies. ConocoPhillips has been working since 2001 to advance the pipeline project and has already spent millions of dollars. She asked why a company would drill now when the state will provide guaranteed subsidized rates to those who defer drilling.

[11:24:41 AM](#)

MS. KING asked the committee to consider ConocoPhillips's prospective of AGIA's project risk allocation. Initial shippers are asked to take risks, beginning early in the development of the project and with uncertainties regarding the future tolls. In addition, the initial shippers must prepare for the delivery of gas at the same time as they are involved in the construction of the pipeline. In contrast, late shippers can come in at the

time of expansion, without the previous costs, and with shorter shipping commitments. Ms. King explained that this shorter time commitment also results in less state take. Size, duration, scope, and project delays are additional risks for initial shippers. Obtaining shipping commitments from creditworthy parties and project delays are risks faced by the pipeline company; however, the actual project cost will be passed along to the initial shipper through the toll.

[11:28:10 AM](#)

MS. KING estimated that a toll of \$3.50 at 1Bcf per day for a 20 year initial shipping commitment will total \$25 billion. The financial strength needed to back a commitment of this size, with the possibility of low gas prices or field deliverability problems, is enormous. Ms. King turned to the subject of the ability of the non-owners to access producers' facilities. She emphasized that the U. S. Congress created mandated expansion provisions effective only in Alaska, and the real question is not access, but the cost of the access. ConocoPhillips encourages the formation of partnerships to control costs and it feels access should not be part of AGIA's requirements.

[11:32:46 AM](#)

MS. KING stressed that ConocoPhillips does not oppose the application of RIR's for some, not all, expansions and that it supports FERC regulations that allow RIR's for some expansions. However, one reason mandating potential expansions is not acceptable is due to the effect of disparate shared royalty on lands. If new gas developments are discovered on lands without royalty, the state may benefit from toll increases by FERC regulation. Moreover, later expansions may result in higher tolls that act as a subsidy for other and perhaps less well-managed producers.

[11:37:23 AM](#)

REPRESENTATIVE SAMUELS recalled that TransCanada provided estimates on the capacity of the gas pipeline that did not exceed the original maximum rate.

[11:38:08 AM](#)

MR. KING explained that some expansions will not be full in-fill compression. The cost of these expansions for lower capacities will be greater than estimated and will bring engineering

challenges. Looping expansions are impacted by the need to predict the costs of steel and fuel. She warned that expansion costs are difficult to estimate and there may be situations where incremental rate increases are desirable.

[11:40:45 AM](#)

REPRESENTATIVE SAMUELS asked for the reason that ConocoPhillips and TransCanada have such different estimates and concerns.

[11:41:26 AM](#)

MS. KING expressed her belief that ConocoPhillips sees the benefit of RIR's in some potential scenarios, but not all, and it encourages the state to allow FERC regulations to prevail.

[11:42:52 AM](#)

REPRESENTATIVE SAMUELS asked whether ConocoPhillips assumed RIRs in its Canadian operations. Some pipelines, he noted, cross borders and may be subject to varying regulations.

MS. KING responded that she is unfamiliar with ConocoPhillips's Canadian agreements; in fact, the NEB has a bias for RIRs. However, the Alaska gas pipeline, she added, travels a long distance before reaching the Canadian border and continues afterward into the Lower 48 to markets.

[11:46:33 AM](#)

REPRESENTATIVE SAMUELS surmised that one-third of the gas pipeline will be regulated by the Canadian authority and that the RIR issue covers the distance between the North Slope and the Canadian border.

[11:47:29 AM](#)

MS. KING expressed some doubt about the jurisdiction over the Alberta portion of the pipeline if new, rather than existing, pipeline is used.

REPRESENTATIVE SAMUELS further asked whether differing rates will impact expansions and tariffs.

MS. KING assured the committee that the FERC and the NEB have previously regulated pipelines that cross national borders. She said that regardless of who owns the pipeline, there will be a

different entity in Canada that will offer a toll and that will have an open season. The Alaska entity will conform to FERC regulation, she added.

[11:48:48 AM](#)

MS. KING continued her testimony by describing an example of a pipeline with an expansion to allow a short haul service to Fairbanks at a certain cost. Then, 10 to 20 years later, an expansion of the other part of the pipeline could raise consumer prices even though the gas was initially committed at a lower price.

[11:50:46 AM](#)

REPRESENTATIVE DAHLSTROM volunteered to provide a copy of FERC order 5(a) to committee members for their reference. She then observed that rate increases can be compared to discounts used to attract new customers.

[11:51:47 AM](#)

MS. KING clarified that ConocoPhillips does not want to pay costs that are the result of someone else's action.

[11:52:08 AM](#)

REPRESENTATIVE DAHLSTROM further noted that ConocoPhillips is requesting the opportunity to negotiate for prices.

[11:52:28 AM](#)

MS. KING reiterated that ConocoPhillips wants the right to debate its case before the FERC.

[11:52:57 AM](#)

REPRESENTATIVE DAHLSTROM questioned whether ConocoPhillips wants that right written in the bill.

[11:53:21 AM](#)

MS. KING stated that this provision does not have to be included in the bill.

[11:54:41 AM](#)

MS. KING summarized that the state has many inducements to offer to pipeline construction applicants. ConocoPhillips does not want unknown gas prospects that are ten years away from development to determine the success of the pipeline project. She encouraged the committee to consider that ConocoPhillips is ready to solve problems and that efforts to resolve the resource issues will begin to move the project to completion. She said that the Alaska gas pipeline is a difficult project and compromise is necessary to achieve the goals of a new source of revenue for the state, jobs for Alaskans, and new development for the industry.

[11:56:28 AM](#)

REPRESENTATIVE SAMUELS asked how long would it take for ConocoPhillips to enter into a partnership and apply for a license.

[11:57:14 AM](#)

MS. KING replied that the timely formation of a partnership would depend on the parties. She added that the challenge of the project is to balance the partnership between the two distinct parts of upstream and midstream development.

[11:58:09 AM](#)

REPRESENTATIVE SAMUELS asked how long ConocoPhillips, without partners, would need to prepare for a successful open season.

[11:59:16 AM](#)

MS. KING responded that ConocoPhillips has estimated 18 months to 24 months to get to open season.

[12:02:49 PM](#)

REPRESENTATIVE SAMUELS remarked:

Does ConocoPhillips think that the tax debate should happen now, before the application process moves forward or do you think that it would be okay to have the tax discussion, as long as you have it ... before the open season. ... Do you think having it now ... would be beneficial, realizing all the of the political ups and downs. ...

12:03:52 PM

MS. KING suggested that the committee amend the bill to make the resource package variable, due to its complexity. Then, the parties will be able to work together.

12:05:24 PM

The committee took an at-ease from 12:06 p.m. to 12:11 p.m.

CHAIR KOHRING announced that the committee will hear testimony by Anadarko Petroleum Corporation.

12:12:15 PM

MARK HANLEY, Manager, Alaska Public Affairs, Anadarko Petroleum Corporation (Anadarko), informed the committee that Anadarko is an independent company that explores for and produces oil and gas without downstream operations. Anadarko has partnered with the major oil companies and has maintained operations in Alaska for 10 years. Mr. Hanley said that Anadarko maintains good relations with ConocoPhillips and Atlantic Richfield Company (ARCO). At this time, Anadarko's biggest interest is in beginning construction of the Alaska gas pipeline project, and it is significantly aligned with its partners on some of the issues involved.

12:15:42 PM

MR. HANLEY continued to explain that Anadarko holds about 5.4 million acres of gross exploration acreage and 1.8 million acres of net exploration acreage. Anadarko's partners include ConocoPhillips, BG Group (BG), Artic Slope Regional Corporation (ASRC), Petro-Canada. He noted that the Foothills region is ready for exploration and Anadarko has four prospects there that are ready to drill. Exploration, given that the gas pipeline is still uncertain, is done to meet the lease requirements to the state, and to prepare for participation in the initial open season. However, the challenge is to continue to prepare for the production of gas while controlling costs. Mr. Hanley explained that even if exploration drilling in 2008 is promising, Anadarko will not be in a position to go to an open season until after delineation of the field and additional wells are drilled. In any case, it will take three to four years to determine if the economics will support a gas commitment to the gas pipeline. Furthermore, Anadarko, he said, does not think its prospects will be sufficient to underpin the gas pipeline.

[12:21:59 PM](#)

REPRESENTATIVE SAMUELS observed that the time delay in AGIA is designed to give the explorers time to prepare for gas production. He then remarked:

To me, shortening the timeline up to as soon as you can have a real open season with real information ... [so] the people who do have gas can decide whether they want to come or not, makes more sense than waiting a little bit longer if you're not ... if you can't be reasonably certain that you can come to us ... [and] participate.

[12:23:28 PM](#)

MR. HANLEY expressed his belief that Anadarko's policy decisions will be based on the earliest available information. Anadarko will begin planning before the open season, in fact, if the pipeline is designed for expansions that lower the tariff, Anadarko will want to participate in the inexpensive expansion. Anadarko may be in a position to participate one or two years after the initial open season and request an expansion before the pipeline is in service. Mr. Hanley said that additions during construction can be a part of the design of the pipeline.

[12:25:57 PM](#)

REPRESENTATIVE SAMUELS asked whether Anadarko considers the benefit of the tax freeze associated with the first open season to be unfair.

[12:26:57 PM](#)

MR. HANLEY replied that the tax freeze will be a competitive advantage. Anadarko will not be at the open season, but feels that any company that makes commitments to the pipeline should qualify for tax certainty. He stressed that the more that the state can do to improve fiscal stability will also improve the economics of the project and reduce the risk. Anadarko would not like to see competitive disadvantages for the companies that do not participate in the initial process.

[12:29:01 PM](#)

MR. HANLEY continued his testimony on AGIA by pointing out that Anadarko appreciates the opportunities to comment on the legislation now, during the public comment period after the applications are revealed, and during the review of the successful application by the legislature. He agreed that the earliest development of the project is a benefit for all parties. Mr. Hanley called the committee's attention to AS 43.90.110 and stated that Anadarko is not a pipeline company and will not be submitting an application for the license. Therefore, it feels that the \$500 million inducement will reduce the tariff and that it is a benefit. Regarding the criteria for the application, Mr. Hanley stated that Anadarko has concerns about the sub-subparagraph (ii) on marine transportation of liquefied natural gas (LNG). This item requires a description of transportation services and a detailed description of all access and tariff terms on a marine route only. Anadarko feels that this language should apply to any proposed pipeline route.

[12:34:16 PM](#)

MR. HANLEY suggested that the AGIA application should also require stating the operating pressure of the pipeline as part of the design standards and gas quality requirements. Additionally, Anadarko supports section 140, paragraph (5), that requires the applicant to assess the market demand for additional pipeline capacity at least every two years through non-binding solicitations, and paragraph (6), that requires expansions to encourage exploration. Mr. Hanley expressed Anadarko's concern about the motivation of parties in the industry who would influence the process representing either the owner of the pipeline, or the producers. He recalled earlier testimony that the bigger risk is borne by the shippers and the bigger return will be on the resource, not on the regulated pipeline. The large producers, he noted, will represent both roles, that of a competitor and that of a partner in the pipeline. In fact, a pipeline company may propose a RIR, or, when its interest as a shipper dominates, may request an incremental rate. The incentive for a producer owned pipeline is often to request a high rate.

[12:39:52 PM](#)

MR. HANLEY added that Anadarko feels that a producer owned pipeline should be held under the close scrutiny that AGIA requires.

[12:40:35 PM](#)

REPRESENTATIVE SAMUELS requested Anadarko's opinion of the producer's argument that the scale of the project and the fact that they will provide the gas should put the pipeline under the producer's control. He asked:

What would you tell the three people with the [gas reserves] that say, "If I'm wrong about building the pipeline I'm paying the higher tariff and my gas is not as competitive. If I'm right, then my costs are less." ... How do you find the middle ground there?

[12:42:26 PM](#)

MR. HANLEY answered that Anadarko feels that the access and expansion provisions in AIGA address some of these issues in a reasonable manner.

[12:43:03 PM](#)

REPRESENTATIVE SAMUELS opined that, in this case, Congressional and FERC regulations are insufficient.

MR. HANLEY stated that some of the issues, for example, the design of the pipeline, are critical, and have yet to be decided. He called the committee's attention to a graph of Indicative Expansion Tariffs, that compares the incremental tariff of \$1.07 to a rolled-in rate tariff of \$1.47 at the first expansion to 5.5 billion cubic feet (Bcf) per day. Anadarko, he said, is concerned that a 42-inch pipe would need to be looped at the first expansion. In that case, incremental tariffs would make would make any expansions uneconomic. Mr. Hanley pointed out that the producers are appealing FERC regulations over pipeline design. If FERC regulations are overruled, he said, the pipeline could be designed to effectively eliminate the possibility of future low cost expansions. Mr. Hanley read the FERC regulations that are under appeal.

[12:49:13 PM](#)

REPRESENTATIVE DAHLSTROM requested clarification on the FERC regulations under appeal.

[12:50:02 PM](#)

REPRESENTATIVE SAMUELS said that his reference was to the rebuttable presumption of rolled-in tariffs. Congress and the

FERC, he said, recognize the presumption that the producer-owner of the pipeline has an inherent conflict.

[12:50:17 PM](#)

MR. HANLEY expressed his understanding that the presumption of rolled-in rates applies to voluntary expansions only. A producer who owns the pipeline may refuse an expansion request and that would force the issue to litigation. In fact AGIA, he said, merely instructs shippers to ask FERC for rolled-rates. Mr. Hanley returned to the tariff graph and pointed out that a second expansion to 6.5 Bcf per day results in an incremental tariff of \$1.73 and a rolled-in rate of \$1.51. These rates are less than the initial tariffs, but higher than the first expansion. If Anadarko is participating in the first expansion, it assumes the risk of paying a higher rate for a rolled-in tariff. Mr. Hanley explained that this is an acceptable risk in order to proceed with the project. However, designing a pipeline for expansion and setting a limit on the expansion rate are critical factors.

[12:56:12 PM](#)

REPRESENTATIVE RAMRAS asked for the origin of the tariff rates reflected in the graph.

[12:56:43 PM](#)

MR. HANLEY expressed his belief that the rates were provided by the Department of Revenue.

[12:56:59 PM](#)

REPRESENTATIVE RAMRAS concluded that the rates are "stylized" numbers.

[12:57:27 PM](#)

REPRESENTATIVE SAMUELS remarked:

Realizing the example [on the graph] in the United States does simply the marketplace take care of your example in expansion number four, eventually, nobody is going to bid \$3.25 while somebody is paying \$1.50. Or is that the way in the United States it works, ... you've got various way to ship your gas.

[12:58:14 PM](#)

MR. HANLEY reminded the committee that the Alaska gas pipeline is a monopoly and in the Lower 48 a shipper would have other options such as building a new pipeline. Again, the initial design of the pipeline is a critical factor in the economics of expansion.

REPRESENTATIVE SAMUELS observed that Trans-Canada's estimations remained under the 15 percent limit throughout the life of the project.

[12:59:25 PM](#)

REPRESENTATIVE DOOGAN referred to the Indicative Expansion Tariffs graph and asked whether expansions 1 and 2 are compression expansions, and whether expansion 3 is a looping, or new construction, expansion.

[12:59:43 PM](#)

MR. HANLEY answered yes.

[1:00:04 PM](#)

REPRESENTATIVE SAMUELS asked whether tariffs are normally increased to match the rate of inflation.

[1:00:48 PM](#)

MR. HANLEY said he is unsure and will provide an answer to that question. He continued his testimony by saying that Anadarko is supportive of AGIA's requirements regarding the debt ratio and the evaluation criteria. Anadarko would suggest the comment and review period in AS 43.90.180 be amended to say "a minimum 60-day period." Again, Anadarko supports offering inducements to all parties rather than creating competitive advantages for the successful applicant.

[1:02:45 PM](#)

MR. HANLEY told the committee that Anadarko's risk during upstream development is equal to or greater than that of the North Slope producers. In fact, the risk of gas reserves and deliverability is higher due to the uncertainty of gas discovery. This bill, he said, creates benefits for the initial shipper that are not available to the late shipper, such as the

certainty on taxes. Again, Anadarko will bear the risk of increased tariffs and the producers have the ability to manage costs. In addition, for Anadarko to participate in the pipeline, it will need to ship one-half Bcf per day in production.

[1:08:31 PM](#)

MR. HANLEY concluded by saying that Anadarko appreciates the opportunity to discuss the bill with the committee. He repeated that the issue of RIRs and whether they can be negotiated with FERC remains to be resolved. In addition, he recommended that the state include its must-haves in the statute. Anadarko, he said is also supportive of the process established by AGIA and of the fact that AGIA addresses many issues for the explorers.

REPRESENTATIVE DAHLSTROM recalled an issue regarding a previous cross-border pipeline wherein the exact transition point was in question. She asked if this type of situation can occur again.

[1:13:58 PM](#)

MR. HANLEY assured the committee that many pipelines have successfully crossed the U. S. and Canada border.

[1:14:14 PM](#)

REPRESENTATIVE OLSON recalled Mr. Hanley's past legislative experience and asked for guidance.

[1:14:52 PM](#)

MR. HANLEY advised that committee members should not rush to judgment, but need to keep the process moving forward. He noted that the legislature has the final review after the license is issued.

[HB 177 was held over.]

[1:16:37 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Oil and Gas meeting was adjourned at 1:16 p.m.