

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

February 28, 2007  
2:07 p.m.

**MEMBERS PRESENT**

Representative Carl Gatto, Co-Chair  
Representative Craig Johnson, Co-Chair  
Representative Vic Kohring  
Representative Bob Roses  
Representative Paul Seaton  
Representative Peggy Wilson  
Representative Bryce Edgmon  
Representative Scott Kawasaki

**MEMBERS ABSENT**

Representative David Guttenberg

**COMMITTEE CALENDAR**

PRESENTATION BY HAROLD HEINZE, ALASKA NATURAL GAS DEVELOPMENT  
AUTHORITY

**PREVIOUS COMMITTEE ACTION**

No previous action to report

**WITNESS REGISTER**

HAROLD HEINZE, Chief Executive Officer  
Alaska Natural Gas Development Authority (ANGDA)  
Anchorage, Alaska

POSITION STATEMENT: Presented a conceptual gas line project  
proposal for bringing North Slope gas to market.

**ACTION NARRATIVE**

**CO-CHAIR CARL GATTO** called the House Resources Standing  
Committee meeting to order at 2:07:00 PM. Representatives  
Gatto, Johnson, Kohring, Wilson, Seaton, and Edgmon were present  
at the call to order. Representatives Roses and Kawasaki  
arrived as the meeting was in progress.

PRESENTATION BY HAROLD HEINZE, ALASKA NATURAL GAS DEVELOPMENT  
AUTHORITY

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CO-CHAIR GATTO announced that the only order of business would be the presentation of a conceptual gas line proposal by Harold Heinze.

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HAROLD HEINZE, Chief Executive Officer, Alaska Natural Gas Development Authority (ANGDA), began his PowerPoint presentation by noting that ANGDA is a public corporation of the State of Alaska. At the committee's request, he outlined his personal background before commencing with his presentation: He came to Alaska in 1969 as a petroleum engineer with the Atlantic Richfield Company, eventually becoming an executive with the company and running the Alaska operations. He was appointed commissioner of the Department of Natural Resources during the Hickel Administration.

MR. HEINZE explained that ANGDA was formed by public initiative and that the statutes under which ANGDA exists are very broad as to the grant of power and direction. He said that in the last few years, ANGDA has focused on two things: 1) a liquefied natural gas (LNG) project out of Valdez, as required by the initiative, and 2) getting gas to southcentral Alaska because this is a significant emerging issue.

MR. HEINZE reported that he met with the new governor on December 5, 2006, and that Governor Palin challenged him to remember why ANGDA was established and asked whether ANGDA's role was being fulfilled. Thus, he decided that ANGDA had better come forward with something called the Alaska Gas Market System (AGMS) because it seems to fulfill the responsibility and challenge that ANGDA was given by the people of Alaska.

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REPRESENTATIVE WILSON inquired as to how this is different from the last time that Mr. Heinze was before the legislature. Has ANGDA changed direction, she asked.

MR. HEINZE explained that the intent is to present an entire system that links the North Slope to gas markets in Alaska. This is a bigger project in scope than what ANGDA has worked on before. However, it is a very small project in comparison to the other projects that are being proposed. He said that ANGDA

is trying to walk the line between being big enough for Alaska and yet small enough to be very doable. It is both a project and a process that will play out over the next one to one and one-half years.

MR. HEINZE noted that ANGDA is a small organization consisting of himself and an administrative officer, Connie Young, and that ANGDA basically operates through the use of consultants. He said that Shaw Alaska, Inc., compiled a lot of the project work behind his presentation of today. He explained that the concept of AGMS started first with the needs within Alaska which is about 250 million cubic feet (mcf) per day for power and heat. This does not provide for the current industrial uses in Cook Inlet, he said, but this may happen if those companies decide to join into this process.

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MR. HEINZE stated that when ANGDA first looked at bringing North Slope gas to the Cook Inlet area, it was found that the project would probably result in higher costs than homeowners would be willing to pay. Therefore, ANGDA looked at ways to lower those costs. One way is to run additional gas down the 700 miles to Glennallen in order to provide one billion cubic feet (bcf) of gas a day to Valdez for LNG. This significantly lowered the transportation cost to Cook Inlet and elsewhere along the pipeline.

MR. HEINZE referred to the map of the AGMS concept proposal in his PowerPoint presentation. He explained that a 24 inch pipe will run from the North Slope to Glennallen, with a capacity of slightly over 1.25 billion standard cubic feet per day (bscf/d). There will be no excess pipe capacity within this portion of the pipeline. However, he said, if someone comes forward with the inclination and commitment to want more gas, the pipe can be made bigger and other things can be done.

MR. HEINZE continued reviewing the map and information. He noted that the 16-inch pipeline coming into the Cook Inlet area is ample for 0.25 bscf/d and can carry the current Cook Inlet usage which is about 500 million standard cubic feet per day (mscf/d). He said that the Valdez pipeline component will transport 1 bscf/d and that the 20-inch pipe is sized according to feedback from major world LNG players who indicated that a volume of 7 million tons of LNG per annum would easily fit into the worldwide LNG trade. He noted that a North Slope

[conditioning] facility will be constructed to remove the carbon dioxide and re-blend the natural gas liquids (NGLs).

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MR. HEINZE pointed out the importance of remembering that the current gas in Alaska - Cook Inlet gas - is almost entirely methane which is very dry. However, he said, North Slope gas is very rich and contains large volumes of ethane, propane, and butane. Ethane is the basis of the petrochemical industry and propane is an excellent fuel for transport to the more rural and less densely [populated] areas of Alaska.

MR. HEINZE explained that the pipeline coming into Cook Inlet would terminate in one or two storage fields. This is because there is a tremendous variation in the use of gas between summer and winter in the Cook Inlet area. This is not the way to run a pipeline, he noted, so running the gas into storage allows for levelized flows and a levelized tariff that is much more favorable economically. Finally, there will be various take-off points at various locations along the pipeline such as Yukon River, Fairbanks, North Pole, and the military installations at Delta Junction.

MR. HEINZE stated that the cost of all the pipelines as shown on the chart will be about \$4 billion. The conditioning plant will be about \$1 billion and a Valdez LNG plant will be about \$3 billion. He said that ANGDA does not visualize building the LNG plant as part of the system because ANGDA believes it will be built by people in the LNG business. If these businesses do not come forward, he said, then there will not be a pipeline to Valdez. He reported that there are two or three major LNG companies in the world, all of whom have expressed some interest in having access to Alaska gas. The reason for their interest is because their other choices in the world are not good ones and Alaska offers a lot of advantages.

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MR. HEINZE predicted a tariff of anywhere from 50 cents to one dollar for transporting the gas to Cook Inlet as opposed to Chicago. He said that this will result in a somewhat lower price. However, the advantage of bringing North Slope gas to Cook Inlet is not that it is cheaper, but that it is a very plentiful supply which will provide stability of price. Given the impact of 30-40 percent price increases over the past few

years, he stressed, having stability may be one of the best assets that Alaska can achieve.

MR. HEINZE directed attention to the tariff numbers for Valdez shown in his PowerPoint presentation and advised that the people in the LNG business will decide whether this project is a commercial activity and whether they are prepared to invest based on these numbers. Preliminary feedback indicates that they continue to be interested, he said.

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MR. HEINZE declared that one of the unique characteristics of a smaller system like this one is that it does not require the huge reserve base that the committee is used to thinking of. He related that the large project carrying 4.5 bscf/d through Canada will require a reserve base of 50 trillion cubic feet (tcf). He said that 25 tcf is what is known to exist in Prudhoe Bay. There is another 10 tcf that has been identified but not developed on the North Slope. Additionally, the assumption being used on the large project is that another 15 tcf will be found. Mr. Heinze emphasized that the ANGDA project is on a whole different scale. He stated that 10 tcf will provide 1.25 bscf/d for over 20 years. That reserve basis, he said, is more than enough to finance and undertake this kind of a project.

MR. HEINZE referred to the "Reserves & Financing" chart in his PowerPoint presentation regarding ways to get to the 10 tcf. One way, he said, is to use the 3 tcf from the state's one-eighth ownership in Prudhoe Bay and add it to the 7 tcf of production from one of the three producers at Prudhoe Bay. Another way is to take the state's 3 tcf and add it to the Point Thomson production. A third way is to take the state's 3 tcf and add it to new discoveries in the Brooks Range.

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MR. HEINZE clarified that in terms of financing, the LNG plant will be built, owned, and operated by people in the LNG business. He related that they already have a fleet of ships, that they want to be able to call on the plant with whatever ships they want, and that they want to be able to sail those ships to whatever markets they already have. It will not be a dedicated trade under these kind of circumstances, he advised.

MR. HEINZE next described the "process" as opposed to his previous description of the "project". He stated that ANGDA has

no illusions of grandeur, it is not going to build this project. He said that he is not asking for billions of dollars, but rather a much smaller sum of money that will allow a process to move forward over the next year and a half. He acknowledged that the first steps of defining a system like this are the risky steps. The risk is that not enough is known to decide whether or not the project is feasible. Until it is determined that it is feasible most companies are going to have a lot of trouble committing tens of millions of dollars, he said, and that is what it takes at some point to advance the project to actual definition.

MR. HEINZE explained that this is a "Phase I" type of approach, and in this Phase I the doors are thrown open to anybody wanting to participate. He outlined the possible participants listed in his PowerPoint presentation under "Partners We Can Expect". These participants include oil and gas companies, pipeline companies, LNG plant and ship owners and operators, energy project investors, local Alaska utilities, the State of Alaska, and the federal government.

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MR. HEINZE predicted interest from the markets. He said this is because most of the people on the market side want to go back upstream. For instance, he contended, there is no doubt that the utilities in Alaska receiving the gas may look at the gas transmission system as a viable investment. He said that a large number of Alaskan entrepreneurs will become involved in distributing the propane. He said that he will not pick the entrepreneurs and does not know who they are, but that he is absolutely confident that people will come and they will come with all kinds of things to transport the propane in.

MR. HEINZE related that at least three companies have expressed interest in a Valdez LNG plant, including "BG Group, Mitsubishi, and Sempra". He said that each company serves a different market, has its own large fleet of LNG ships, and has very different re-gas facilities. He noted that a possibility might be for the three companies to build the LNG plant together. He pointed out that ANGDA is encouraging a cooperative rather than a competitive effort in order to get the strongest project possible. If the companies say that they need more than 1 bscf/d of LNG and they are prepared to make the commitment behind it, then making the project bigger should be looked at.

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MR. HEINZE reiterated that the two industrial facilities in Cook Inlet are not part of this system. He stated that neither the Kenai LNG plant nor the Agrium plant have expressed interest at this time. However, he said that he has every reason to believe that this will be revisited in the future as things move forward.

MR. HEINZE noted that because of the extreme richness of the [North Slope] gas, petrochemical companies have expressed interest in locating at the pipeline's terminus. He said that this is because the volume of ethane that will potentially be available is twice what it takes to have a world-scale industrial complex and that most of these companies do not have access in favorable settings to this volume of hydrocarbon.

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MR. HEINZE explained that because the pipeline is small, it will largely follow the Trans-Alaska Pipeline System (TAPS) right-of-way to Glennallen as this offers some regulatory advantages. He said that ANGDA believes the pipeline can be delivering gas to Cook Inlet in six years, based on three years of "front end" and three years of construction. During the construction phase the pipeline will require two crews of about 500 workers and this is well within Alaska's capability in terms of the skills and crafts that are needed. He said that a 24-inch, high pressure pipeline like this one is very suitable for welding machines and other techniques that lessen the requirement for highly skilled people because it is more of a craft type of setup.

MR. HEINZE stated that ANGDA believes there is a scenario where gas can be flowing into Cook Inlet ahead of finishing the North Slope conditioning facility and the finishing of the LNG plant in Valdez. He noted that this is very important when looking at the potential energy problems facing Cook Inlet where even two years might be significant.

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CO-CHAIR GATTO estimated a cost of \$5000 per home for the Glennallen to Cook Inlet portion of the pipeline to provide gas to the Matanuska-Susitna, Kenai, and Anchorage areas. He said that it will cost more than \$5000 per home to switch to heating oil, so having the ability to continue heating with natural gas would be a great advantage. Additionally, this figure does not include Agrium or the LNG plant. This section of the pipe will

be paid for completely and there will be no tariff because the consumers will all own it, so this is very valuable.

MR. HEINZE agreed with Co-Chair Gatto. He asserted that the pipeline is clearly a utility because it is servicing a number of households. The 20-30 year supply of gas to these households is an incredibly important thing, he said. Alternative investments for providing the same level of energy, coupled with energy security over time, are much more than a few hundred million dollars.

MR. HEINZE remarked that in addition to the spur line, continued exploration in Cook Inlet remains vital. However, he said, the cost of Cook Inlet gas will present major problems in the longer term when one considers that the rule of thumb is about \$1 billion for 1 tcf. He noted that LNG could be brought in, but that there are pricing and security issues associated with LNG. He said that he would be very uncomfortable with Alaska's communities having to rely on a tenuous foreign supply of LNG.

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MR. HEINZE directed attention to the schedule outlined in his presentation and noted that the intention is to allow for a negotiated open season early in the timeline. He explained that during the open season people must come forward and make commitments and that this is when you find out if you have a project, how big the project will be, and what the economics of the project really are. He predicted that the answers to the questions will be found quickly because this particular pipeline is a simple system. However, since this is a "Phase I" type of work level, the trick is to get there in a way that is comfortable information-wise to the potential participants. He noted that on the schedule, the trigger for this is pretty quick and that this is not inconsistent with the other things that need to happen to get gas to Cook Inlet in a timely way. Even though the open season begins early in the timeline, it will remain open for one year which is longer than the standard timeline of six months.

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MR. HEINZE explained that the joint-work process shown in his PowerPoint presentation will be a voluntary coming together of ANGDA, state resources, and individual company resources on a contributed, in-kind basis. It will be totally non-exclusive as well as voluntary. He said that if someone elects to

participate, it will not prevent them from also proceeding with their own efforts or other groupings of efforts. He noted that many of the issues are issues that are common to any project and any set of participants and that this will provide a vehicle for people to participate at a lower risk and, most importantly, to know that it is happening. Even though not every aspect of this will be public, he stated, the actual monthly progress reports will be a very public thing so that people can see what is going on and whether it is advancing. There will be an incentive for the participants in the process because only the summary information will be made public. Participating day-to-day at a technical level in a project like this is a way to learn the most.

MR. HEINZE stated that if he is given encouragement by the legislature, he will take the month of April to call on a number of people and offer them this opportunity. He said that a few will accept readily and the others will then also accept because one of the rules of the game is to never let a competitor have an advantage. There is no expense to these companies other than the talent and the expertise that they contribute.

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REPRESENTATIVE WILSON asked where would the State of Alaska gain in this project and will the project make it cheaper for people in Southeast Alaska.

MR. HEINZE replied that the answer to the second question is yes. He said that it is ANGDA's belief that everybody has a stake in North Slope gas. While it has not been the thrust of other sponsors, it is ANGDA's thrust that 99 percent of Alaska will participate in the actual molecules coming off the North Slope. That plentiful supply offers an opportunity for a modestly priced energy, he said, at a stable price from a large and secure supply. In Southeast Alaska there are a number of other alternatives that are different than the alternatives available in Cook Inlet or Fairbanks. There will be a very positive impact on the energy price by providing certain types of energy service, for example cooking and water heating for which propane and gas are very efficient. When the gas becomes present, Mr. Heinze said, it will put pressure on other parts of the energy system in a competitive sense. Once that competition starts, prices will respond. In the long run it offers an opportunity to the legislature to determine how it wishes to value the resources in Alaska. The 3 tscf/d that is the state's

one-eighth share of Prudhoe Bay is enough to provide Alaska with energy for 30 years.

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CO-CHAIR GATTO offered a further response to Representative Wilson's question by giving an example: If a person uses heating oil in the free market, it puts pressure on the heating oil stocks from which other people are also purchasing; but if that person does not use heating oil, then there is a bigger supply in the same market. Therefore, he explained, this is one way that other locations in the state are affected. Another way is that the state gets a royalty and this, in turn, affects every resident. He stated his opinion that if Southcentral Alaska prospers, it does not take away from any other area that prospers with it.

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MR. HEINZE directed attention to the map in his PowerPoint presentation depicting the transportation of propane with yellow highlights. He predicted that over 50,000 barrels a day of propane will come off the North Slope, but noted that the demand for propane in Alaska is only about 10,000 barrels per day. The trick, he said, is the logistics of distributing the propane and that is why the map shows the broad yellow arrows going around the coastal areas. He related that there are several studies available for review on ANGDA's website which show that every coastal community in Alaska will gain by having a plentiful propane supply. In areas of Alaska that are served by roads there is already competition between propane suppliers. He explained that in a similar way [to roads], the Yukon River system is a logical avenue for moving propane. The difference, however, is that there are no data points for moving this type of a commodity on a frozen river. He related that ANGDA is working with several entities to conduct a demonstration project based on trucking a small volume of propane out of Prudhoe Bay, putting it into a facility at the Yukon River, and then, in an experimental sense, letting the entrepreneurs act.

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MR. HEINZE subsequently displayed a PowerPoint picture of a propane tank. He noted that it is the same size and shape as an ISO or intermodal container. The tank ships just like an ISO container and can be stacked and handled together with and in the same manner as ISO containers. He explained that this

propane tank is the storage mechanism as well as the transport mechanism. Therefore it can be delivered to a destination, used until empty, and then exchanged for a full tank with the empty tank being returned, just like changing the propane tank on a barbecue grill. Additionally, he remarked, these tanks can be built in Alaska because they are modest pressure vessels, there is nothing hard about them, and there could be a standard Alaska design. He explained that ANGDA is trying to make this work for everybody and that ANGDA believes that over a period of a few decades there is an opportunity to influence energy prices everywhere in Alaska. For example, he said, the Yukon-Kuskokwim Demonstration Project is of great interest to the Denali Commission. They do not have a lot of opportunities to come into new energy models, he explained. Most of their money is being spent on perpetuating the system that exists and this offers a chance for a new paradigm.

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MR. HEINZE commenced explaining why he needs \$5 million dollars and why it is good for Alaska. He directed attention to the detailed matrix on the last page of the document in the committee packet. He stated that the 80 tasks listed in the matrix will be undertaken during the first one and one-half years in order to move the project forward. The total cost of the tasks is \$10 million, he said, but he is only asking for \$5 million because he can attract the other \$5 million as in-kind contributions. The actual task list will be worked out with the joint-work participants.

MR. HEINZE stated that at the end of the year or year and one-half, the project concept will be described to the point that the participants can make a decision - at their own cost and risk - on whether to proceed to a formal application to the State of Alaska as visualized under the Alaska Gas Inducement Act (AGIA). Participants can hold an open season and they can make the major financial commitments to design and permit applications. He pointed out that this is a \$100 million decision.

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MR. HEINZE argued that what Alaska gains is an alternative. The project has two significant virtues: 1) it is not vulnerable to what does or does not happen in Canada, and 2) it is of a size that meets Alaska's needs and it only requires one of the producers at Prudhoe Bay along with the State of Alaska to

commit their reserves. It does not require the unanimity of all the upstream reserve holders to make the project happen.

MR. HEINZE asserted that \$5 million is a cheap insurance for the legislature to know that there will be a backstop available if all else does not work out. He argued that the reality is that the biggest and best of these projects is still very challenged in terms of probability. The AGMS project is a highly doable project with a strong market pull and makes sense in many different ways, he said. He expressed his hope that legislators will choose to amend the supplemental appropriation to include the \$5 million for the AGMS project since there is no legislation to appropriate the money.

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CO-CHAIR GATTO inquired whether the \$1 billion figure for the gas conditioning plant is also the same figure that has been given for a 52-inch pipeline.

MR. HEINZE responded that the number shown on his chart may be toward the higher end because he has nothing to gain by understating the number. He said that he is unsure who would want to build and own the gas conditioning plant, but that it has so many virtues it is hard for him to visualize the producing operation not wanting to own the plant as a Prudhoe Bay unit facility. The carbon dioxide that could be recovered is very usable in enhanced oil recovery. Additionally, under federal legislation the facility would receive special tax treatment, such as enhanced oil recovery (EOR) tax credits. The plant would also be eligible for carbon sequestration credits if those are ever established.

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REPRESENTATIVE WILSON asked how much money the AGMS project will bring to the State of Alaska. A pipeline must be capable of carrying a large enough volume of gas to generate an income to the state, she opined. Otherwise, the state must find a different way to raise money, such as an income tax.

MR. HEINZE acknowledged that a project two or three times larger than AGMS will generate two or three times more revenue to the state. However, he cautioned, the probability of that project moving forward needs to be considered. The size of the AGMS project has a very high level of do-ability. If things are looking grim in another year and one-half, the state may be very

happy to have this size of a project available. While state revenues are important, the citizens of Alaska also value having a plentiful, modestly priced supply of gas. They value having construction jobs and the level of construction for the AGMS project is much more Alaska sized. He contended that the AGMS project will not create hyper-inflation or cause the in-migration of workers that other projects might. Lastly, Mr. Heinze opined, Alaska citizens are looking for something that pays attention to the economy here, for the short term as well as the long term. The creation of a petrochemical industry and other types of things are potentially more valuable here in Alaska than anything else. In moving AGMS forward as part of a Phase I activity, the virtues will be carefully defined in the sense of benefits to Alaskans on all those dimensions, not just state revenue.

MR. HEINZE related that past work by ANGDA indicates that this size of a project will have a significant impact here in Alaska far beyond the \$5 million. A project of this size does not in any way foreclose a bigger project in the future, he argued. In fact, it could be tacked onto any other project that is built. Additionally, a smaller project has the virtue of getting started because this is one of the biggest problems. "I have been here since 1969, and if I am worried about anything, it is not getting started," he said.

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CO-CHAIR GATTO remarked that Alaska's new governor wanted all proposals on the table, therefore this certainly is a legitimate proposal.

MR. HEINZE responded that he is describing a system. Once AGIA is brought forth, he said, this may turn out to be a proposal for three to five projects because there are different variations of AGMS. Right now it is unknown which variation is the best.

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REPRESENTATIVE SEATON commented that two to three times bigger does not necessarily mean two to three times more revenue. He pointed out that provisions in the previously proposed [Stranded Gas Development Act] canceled two-thirds of the state tax. He then noted that NGLs are currently put into TAPS and counted as oil under the production profits tax (PPT). He asked whether

Mr. Heinze is proposing to blend all the NGLs or only those that are not sold as oil and injected into TAPS.

MR. HEINZE stated that the current oil system has as much butane blended into it as the oil will hold and still meet the vapor pressure specifications; if more is added it gets too "fizzy" and causes air quality issues and other problems. There is some propane in the oil naturally, but more propane would not be added purposely to the pipeline. He said that what he is talking about is that along with moving methane molecules down the [gas line], the high pressure in the pipe allows the addition of large quantities of ethane, propane, and butane. He advised the committee to think of the gas line as a transport mechanism that is fundamentally unlimited as far as quantity. For instance, he said, approximately 80,000 barrels a day of NGLs are currently being re-injected into North Slope wells as part of enhanced oil recovery. Even a gas line as small as the one he is proposing has a high enough pressure to accept that amount of NGLs.

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REPRESENTATIVE SEATON related his understanding that a unique feature of Prudhoe Bay is that all three producers must agree before any one of them can do something. He asked whether this could legally limit one of those producers from taking out their third in order to participate in one of the proposed AGMS scenarios. Additionally, he asked whether Mr. Heinze saw a possibility of resolving the Point Thomson issue before the open season for that area closes in order to have a possibility of getting a commitment on that gas.

MR. HEINZE took the second question first. He said that he is not an expert on Point Thomson, but that it seems to him that the state and the owners of the Point Thomson unit have locked horns. The court's ruling that the owners have failed to live up to their lease is a significant ruling in the business. In his opinion, Point Thomson may actually be off the table and it is going to be very hard to have a 4.5 bscf/d pipeline. He argued they are in big trouble because pulling 4.5 bscf/d out of Prudhoe Bay will not be allowed. Much of the 4.5 bscf/d is premised on delivery from Point Thomson, he said.

MR. HEINZE then moved to Representative Seaton's first question regarding the agreements within the Prudhoe Bay unit that deal with how the owners relate to each other. He explained that one type of agreement is called a Balancing Agreement - it dictates

how things will be rebalanced if one company gets ahead of the others. Based on his anti-trust training when he was a corporate executive, Mr. Heinze surmised that the decisions to market are separate decisions of these companies and that a collective decision is not permissible. As a lease holder, each company has a responsibility to the State of Alaska to dispose of and market the state's royalty. It has a right to market the royalty, but it also has a responsibility and this is not a collective right. He said that in his opinion a representative of the State of Alaska could not talk to one company while the other companies were in the room without there being serious anti-trust implications. He said that he did not know exactly what the [Prudhoe Bay] agreements are, but that he could say that no agreement amongst companies can contravene law and that the companies are obligated to consider market conditions separately.

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CO-CHAIR GATTO turned the gavel over to Representative Seaton.

REPRESENTATIVE SEATON expressed his concern about going down a path that is based on scenarios that are not realistically possible. He noted that there might be other scenarios such as the National Petroleum Reserve-Alaska (NPR-A) and "Shell offshore", but that he wants to make sure whether a scenario is going to be useable during the proposed open season.

MR. HEINZE pointed out that in ANGDA's task list there is a proposal under the heading of "Risks and Rewards" to look at these scenario-type issues because there are very significant assumptions that are taken for granted when, in reality, they are not 100 percent deals.

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REPRESENTATIVE SEATON inquired whether open season would start in the fourth quarter of 2007 if ANGDA received the \$5 million.

MR. HEINZE responded affirmatively. He explained that he carefully defined that bar as a year because it is a negotiated type of open season rather than a bid type of open season. "All you have to do is be willing to negotiate evenhandedly, equally, offer the same terms to everybody and that may be a better way at this system," he said. He pointed out that if there are several participants, such as electric utilities in the Cook Inlet area and an LNG exporter, there must be a way for them not

to compete against each other because it is necessary for all of them to succeed. This is done through a negotiating process because then all of them will win, he contended. It is hard to know how each company will respond until a cycle is completed and there is a feel for what the commitments are. Then the numbers are revised and you go back out again, which is why ANGDA has allowed a year for the process. He explained that the information necessary to start this process is minimal and that is why he "pulls the trigger" so quickly on an open season. This would be difficult to do in a traditional FERC bid system, he said. However, completing a process that leads to some level of commitment by participants is a much easier thing to do on a negotiated basis.

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REPRESENTATIVE SEATON noted that a problem associated with the previous contract was a 35 percent tax credit on everything upstream, including the gas treatment plant, and that the state would lose two-thirds of its PPT rate to this. He asked whether he was correct in understanding that under ANGDA's proposal the open season will not be open to any of these kinds of negotiations and that participants will come to the table under the existing system.

MR. HEINZE said that there is nothing in this system that deals with the upstream issues. He noted that nothing he is talking about, in terms of the open season, involves a negotiation with the state. However, to lessen the front end risk ANGDA does need some sort of financial interaction with the state such as a line of credit, but not an investment. He said that some help through a completion guarantee is also needed because this lowers the interest rate for building this kind of a project. Coupled with utility financing, ANGDA thinks that this project - on a tariff basis - can do far better than what is shown by ANGDA's numbers.

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REPRESENTATIVE WILSON expressed her concern with not knowing how ANGDA arrived at its numbers. She inquired as to how many phases are envisioned and whether ANGDA would be coming back to the state for more money after Phase I.

MR. HEINZE answered the second question first. He explained that Phase I would be feasibility. The next steps would involve taking a further cut at design and developing information for

regulatory approvals, environmental permits, and those kinds of things. It still would not be a commitment of the major amount of money; at that point the state is still in for less than five percent of the total cost. The next phase would lead to the decision to commit to the big project and move forward and "that is when the big money hits the table." Mr. Heinze stated that it is not his intention to come back to the legislature. If this project does not work, he said, I will apologize to all of you for the \$5 million. If the project does work, there will be really big companies that will take over the ownership of this project. He promised that he will require the companies to reimburse the state for every nickel that it has put into the project. He said that he is asking for a "grubstake" and that he would rather ask the legislature for that grubstake than to go sell "grubstake bonds" which is his other available option. He explained that he needs enough money to be able to support a part of the process that will convince these other participants that the state is at least serious about taking care of itself by making sure that the gas gets to the state's own markets.

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MR. HEINZE explained that the numbers are cost estimates that are based on benchmark and that ANGDA has had three different cost estimates done by three different companies. He stated that he believes the numbers are conservative in that the actual numbers will be less than what ANGDA is presenting. He noted that the numbers calculated on ANGDA's chart are based on two different tariff levels. One is based on the utility model of financing that looks at an annual revenue requirement and has no equity investment because it is all debt or borrowed money. "That leads to a number that is about one-half of the number that we would scale off of, the \$2.50 producer tariff number you have heard many times before," he said. "We have calculated both numbers and said we do not know where exactly it will end up," he continued. "It is probably not higher than the number that is scaled off of \$2.50 to Chicago, but it could be starting to approach the lower utility end number." He said that it is a big range at this point and the purpose of the Phase I work is to get different participants comfortable. He pointed out that there has been a lot of input from financial people and that he expects many financial people will be involved as participants because they are very interested. A multi-billion dollar energy project in a place where there is this much gas on the Pacific Rim is a natural, he asserted.

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REPRESENTATIVE SEATON asked how ANGDA and the Alaska Gasline Port Authority (AGPA) would work together if AGPA were to come to the table with its design.

MR. HEINZE explained that ANGDA and AGPA are both political subdivisions of the state. One was created by a statewide vote and the other was created by more of a municipal type of vote. The two entities therefore have different histories and slightly different positions. However, he said, the missions and desires are shared and the boards are now working closer together and have recently signed a Memorandum of Understanding (MOU) to facilitate the exchange of confidential information. He said that he hopes that AGPA will be one of the first entities willing to work with ANGDA. At the same time, he said, he expects them to continue working on a proposal that is bigger and more suited to where they are in their process. He stated that ANGDA is not in competition with AGPA, but rather compatible with them.

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REPRESENTATIVE SEATON inquired whether ANGDA would need a federal loan guarantee.

MR. HEINZE stated that one of the chores on ANGDA's task list is to clearly understand the ins-and-outs of the federal system because ANGDA is obviously skating on the edge of that. He contended that federal law for the Alaska gas pipeline is written in a language where delivery to the market in Alaska is the same as delivering gas to Chicago. This is because the term used in the law is "continental" as opposed to "contiguous" United States. According to a legal opinion received by ANGDA, Alaska is part of the "continental" United States. Therefore, he said, some portion of the project might be eligible for a federal loan guarantee. He said that on projects like this there are a number of ways to lower the interest rate and ultimately lower the tariff in the long run. He acknowledged that the federal loan guarantee is an effective way to do that, but in ANGDA's case there may be more effective ways. Furthermore, he stated, having a state guarantee on the loan might lower the interest rate more than would a federal guarantee. It is ANGDA's intention to pursue all of the options, he said. There is also the issue of export which is a federal jurisdiction.

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MR. HEINZE, in response to a question from Representative Wilson, explained that he is a state employee, hired and fired by a seven member board of the Alaska Natural Gas Development Authority that was created by statute. He said that ANGDA is under the Department of Revenue, as required by the statute. He noted that in the previous administration there were times when a lot of the studies done by ANGDA were to answer questions that would be helpful to the whole process. He explained that the tone he is trying to set is to ensure that there is sufficient information available to the public during the process, not at the end of the process. In response to a further question, he explained that AGMS, the Alaska Gas Market System, is the name of a project.

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MR. HEINZE announced that all of the information he presented is publicly available at [angda.state.ak.us](http://angda.state.ak.us).

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:22 p.m.