

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

April 11, 2007

1:05 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 David Guttenberg  
Representative Scott Kawasaki

**MEMBERS ABSENT**

All members present

**OTHER LEGISLATORS PRESENT**

Representative Anna Fairclough

**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) Heard & Held  
03/28/07 (H) MINUTE(O&G)  
03/28/07 (H) O&G AT 8:30 AM CAPITOL 106  
03/28/07 (H) Heard & Held  
03/28/07 (H) MINUTE(O&G)  
03/29/07 (H) O&G AT 3:00 PM BARNES 124  
03/29/07 (H) Heard & Held  
03/29/07 (H) MINUTE(O&G)  
03/30/07 (H) O&G AT 8:30 AM CAPITOL 106  
03/30/07 (H) Heard & Held  
03/30/07 (H) MINUTE(O&G)  
03/31/07 (H) O&G AT 1:00 PM BARNES 124  
03/31/07 (H) -- MEETING CANCELED --  
04/02/07 (H) O&G AT 8:30 AM CAPITOL 106  
04/02/07 (H) Heard & Held  
04/02/07 (H) MINUTE(O&G)  
04/03/07 (H) O&G AT 3:00 PM BARNES 124  
04/03/07 (H) Moved CSHB 177(O&G) Out of Committee

04/03/07 (H) MINUTE(O&G)  
 04/04/07 (H) O&G RPT CS(O&G) NT 3DP 2NR 2AM  
 04/04/07 (H) DP: RAMRAS, DOOGAN, OLSON  
 04/04/07 (H) NR: SAMUELS, KAWASAKI  
 04/04/07 (H) AM: DAHLSTROM, KOHRING  
 04/04/07 (H) O&G AT 8:30 AM CAPITOL 106  
 04/04/07 (H) -- MEETING CANCELED --  
 04/05/07 (H) O&G AT 3:00 PM BARNES 124  
 04/05/07 (H) -- MEETING CANCELED --  
 04/10/07 (H) RES AT 1:00 PM BARNES 124  
 04/10/07 (H) Heard & Held  
 04/10/07 (H) MINUTE(RES)  
 04/11/07 (H) RES AT 1:00 PM BARNES 124

**WITNESS REGISTER**

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

**POSITION STATEMENT:** Provided an overview of the Alaska Gasline Inducement Act (AGIA) as proposed in HB 177.

DONALD SHEPLER, Attorney at Law  
 Greenberg Traurig, LLP  
 Alaska State Legislature  
 Juneau, Alaska

**POSITION STATEMENT:** During hearing of HB 177, answered questions.

KEVIN BANKS, Acting Director  
 Division of Oil & Gas  
 Department of Natural Resources  
 Anchorage, Alaska

**POSITION STATEMENT:** During hearing of HB 177, answered questions.

**ACTION NARRATIVE**

**CO-CHAIR CARL GATTO** called the House Resources Standing Committee meeting to order at 1:05:34 PM. Representatives Gatto, Johnson, Seaton, Roses, Guttenberg, Kohring, and Wilson were present at the call to order. Representatives Edgmon and Kawasaki arrived as the meeting was in progress. Also in attendance was Representative Fairclough.

HB 177-NATURAL GAS PIPELINE PROJECT

1:06:12 PM

CO-CHAIR GATTO announced that the only order of business would be HOUSE BILL NO. 177, "An Act relating to the Alaska Gasline Inducement Act; establishing the Alaska Gasline Inducement Act matching contribution fund; providing for an Alaska Gasline Inducement Act coordinator; making conforming amendments; and providing for an effective date." [Before the committee is CSHB 177(O&G).]

1:11:49 PM

PAT GALVIN, Commissioner, Department of Revenue (DOR), drew attention to the PowerPoint presentation dated 4/11/2007 from the Palin-Parnell Administration. As specified on slide 1, Commissioner Galvin said that the administration would like the committee to recognize that the Alaska Gasline Inducement Act (AGIA) is designed to be a commercial vehicle for the opportunity to create a competitive environment in which the commercial players can make their own independent decisions regarding how to participate and develop solutions to the issues that will arise with this project. Furthermore, AGIA is focused on moving the project ahead because it's in Alaska's interest to [construct] the pipeline sooner and have certain terms imbedded in the contract. In order to do the aforementioned as a government, it must be done in as transparent a manner as possible. Therefore, the decision-making process is focused on transparency. There is also the desire for the inducements that Alaska puts forward to be transparent as well. The aforementioned results in knowledge of what the state is offering as well as the price for those inducements. The aforementioned further provides knowledge of the risks and the costs the state will face.

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COMMISSIONER GALVIN, referring to slide 2, emphasized that it's important to note that AGIA is not a negotiation. The AGIA model is to create a bidding opportunity through the request for application process that allows all competing proposals to come forward. The aforementioned will provide the state with an idea of the opportunities it has among competing interests. The legislation includes inducements that attempt to generate interest in this project such that it results in the commercial players moving ahead with the project per a specified timeline and committing to certain terms and requirements. In order to

achieve the aforementioned there is a midstream inducement of potentially \$500 million capital contribution. He clarified that although the amount of the contribution isn't necessarily known at this point, it won't exceed \$500 million. The aforementioned is an important aspect of AGIA as it specifies that the state has a limit on its exposure for this venture. He pointed out that AGIA includes upstream tax and royalty inducements that are geared toward obtaining a commitment to the licensed project at the initial open season. Again, those are being designed to be clear and transparent.

[1:16:39 PM](#)

COMMISSIONER GALVIN acknowledged that sometimes AGIA is compared to the stranded gas contract. However, there was a lot of concern that the stranded gas contract was developed out of public view. The legislation attempts to address that concern. There were also concerns with regard to the hidden costs [of the stranded gas] contract. Therefore, AGIA is trying to eliminate the aforementioned level of uncertainty with regard to the cost to the state by ensuring that the inducements are quantifiable and known at the onset.

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REPRESENTATIVE SEATON expressed concern that there is uncertainty with regard to the tax rate. One of the big components of this process is to get partners to the table, get gas in the open season, and have bids made. If the tax rate is unknown until the open season, it will be difficult for entities to come forward and work with other partners. Representative Seaton opined, "We basically have the most expertise we're ever going to have on what [petroleum production profits tax] PPT was and how the tax program was put together and what it means at this time in the legislature." He questioned why some certainty isn't given by specifying what tax rate is going to apply.

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COMMISSIONER GALVIN explained that the concept behind the current structure of HB 177 is that the tax rate in place at the time an interested party makes the decision will drive the decision whether to commit or not. Under this concept, there is no need to know the tax rate years in advance because the decision won't be made until the commitment is made. Commissioner Galvin said he understands the logic of the argument of setting the tax rate before the applications are

due. However, one concern is the constitutionality of locking in the tax rate [before the applications are due]. He opined that the strongest argument for locking in the tax rate is based upon the exchange of making the gas commitment for locking in the tax rate at that time. The mechanism by which the tax rate would be locked at the time the applications are due isn't necessarily present because the gas isn't being committed at the time of application. Therefore, there isn't the same immediate exchange that would lock in that contractual relationship. If the application doesn't lock in the tax rate, then it could easily be changed by the legislature between [the submittal of the application] and the open season.

COMMISSIONER GALVIN related his disagreement that there is a lot of expertise at this point. He pointed out that the first returns on PPT have only recently been received and are being assessed. There was a gap in what was expected and what was received. Some time will have to be taken to determine why that occurred and whether the current PPT structure will deliver what it was expected to deliver. He noted that the aforementioned relates only to the oil side. With regard to the gas side, much more information is necessary. The PPT discussions primarily focused on oil, and therefore the gas tax rate now needs to be more the focus. More information, he opined, is necessary to have that discussion and be able to set a rate that can be locked in for many years. Still, it's worthwhile to discuss whether it's necessary to have a discussion on the PPT between now and the current target date for applications being due, October 1st. For the purposes of AGIA, Commissioner Galvin stressed that [the administration] feels very strongly that this legislation needs to be passed prior to addressing the complication associated with setting the gas tax rate in HB 177.

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CO-CHAIR GATTO related his understanding that the real return was less than the anticipated return by \$813 million over 8 months. He calculated that \$813 million over 8 months amounts to about \$100 million a month. Over 12 months, it would amount to \$1.2 billion, which is closer to what the PPT has produced.

COMMISSIONER GALVIN clarified that the expectation for what PPT was going to produce for that [8-month] period of time was approximately \$950 million. The aforementioned was used as the model for the evaluation of what the appropriate rate should be. Therefore, there is a disconnect between what was expected and what was received. Commissioner Galvin further clarified that

he is merely suggesting that more must be known about why that happened prior to locking in some of these things for an extended period of time.

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REPRESENTATIVE WILSON inquired as to how much of an adjustment was made due to the oil spill that caused the shutdown.

COMMISSIONER GALVIN said that is part of the analysis. He pointed out that the \$950 million was the expectation after the spill had occurred and the shortfall had occurred, and therefore it was factored in the expectation. Commissioner Galvin characterized it as an additional complication that requires review.

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REPRESENTATIVE SEATON said he could appreciate those comments. However, he pointed out that the state will never have experience with gas until it is flowing. He recalled that what he has heard continuously is that to achieve something that works, people have to at least know what the tax rate is. He then related his understanding from other committee hearings that there has been testimony that the players anticipated to be at the table as pipeline companies aren't going to proceed unless they have some confidence that there's a source of gas. Therefore, the lack of knowledge of the tax rate "may not get us there," he said. Representative Seaton said he wasn't sure that [a specific tax rate] isn't one of the components that should be reviewed. He then related his understanding from analysis that the PPT will be high because there are very few expenses since the development costs of Prudhoe Bay have already occurred. Furthermore, he opined that the economics are that the gas is going to be more profitable. Still, knowing the tax rate may be more important to obtain successful applications through AGIA versus waiting to work on the upstream if no applications are received.

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COMMISSIONER GALVIN turned to the characterization that participants have expressed a reluctance to participate unless they receive assurance that they get the gas if they participate. He opined that the testimony was a reflection of TransCanada's comments that it wasn't comfortable participating given that the state was requiring a commitment to submit a

certificate. That's different than an entity not submitting an application unless it knows that it's going to get the gas. Commissioner Galvin opined that ultimately the state needs to have a vehicle that is shown to be economic and provides the lessees with a reason to place their gas in the line. He said, "You have moved from a question of whether the producers need to have this level of certainty that they keep talking about at the time they submit the application or whether it's at the time that they are being asked to commit their gas." The legislation has structured a level of certainty that is believed to be appropriate at the time the applicant commits the gas.

COMMISSIONER GALVIN opined that when one views the economics from a Prudhoe Bay lessees' perspective, the economics are so positive when \$6 gas is factored in. That view results in a potential rate of return of 50 percent due to the limited level of investment required. The question becomes: what level of tax change is needed to affect that decision. Upon review of the history of Alaska's tax take, Alaska has never even come close to the international norms. Therefore, Commissioner Galvin said that he personally takes offense to the notion that the state needs to provide certainty [to potential lessees]. The state is trying to be responsive by providing a 10-year window to commit the gas to the line and whether that window should be expanded is a different discussion.

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REPRESENTATIVE GUTTENBERG opined that the producers' major role is to obscure the issue. He asked if this is the appropriate time to provide the certainty or can it be compared to other projects on the world market to determine when the certainty is necessary. He also asked if the producers are in need of certainty in the form of specific numbers.

COMMISSIONER GALVIN highlighted that no jurisdiction provides the certainty the producers are requesting. "So, you don't have a comparable to say when is this necessary along this timeline because you don't have an example of where it was actually ever provided," he pointed out. He reiterated that the legislation attempts to provide an opportunity for participants to make decisions regarding how and when they'll participate in this process. When one talks about certainty it's really a response to uncertainty. From a resource development company standpoint, there are uncertainties that are dealt with daily. The question before the state is regarding the point at which the state, prior to other uncertainties, does Alaska need to lock in the

perceived uncertainties of the state fiscal system. He related the belief that once the range of potential economics on the pipeline has been defined and demonstrated through an open season, the issues associated with the need for more certainty on the state fiscal system will fall to the side. The aforementioned is the point of AGIA. Commissioner Galvin then commented that the issue raised by Representative Seaton is a legitimate matter on which to hear from the industry. He emphasized that the tax lock in is clearly trying to induce the commitment of gas to the project. The [administration's] feeling today is that it isn't necessary to lock in the tax rate in AGIA.

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CO-CHAIR JOHNSON said that part of [the purpose] of AGIA is to get people to bid on the pipeline. He questioned what would be wrong, from the standpoint of AGIA, if taxes are locked in and more people are brought to the table.

COMMISSIONER GALVIN answered, "Nothing." He said he would agree if the producers say that they need to know the tax rate for the 10-year period prior to considering submitting an application. Clearly, AGIA has been designed so that the producers will decide to participate. "And, if that's one of the drivers, then we need to address that," he said.

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CO-CHAIR JOHNSON asked then if a provision is included in HB 177 that locks in taxes now would impact other parts of the legislation.

COMMISSIONER GALVIN opined that the question of locking in the tax rate in AGIA is more a question of what is the tax rate [an applicant] is willing to lock in. He reiterated his early comment that his level of confidence in the current tax rate is relatively low. Commissioner Galvin said he would be uncomfortable saying that the state should lock in the current tax rate for the [10-year] period of time. Furthermore, he didn't believe the producers would view the current tax rate as much of an inducement. Therefore, the question becomes whether the state will somewhat arbitrarily pick a lower number for the tax rate. The [administration] wouldn't support such action, he said.

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REPRESENTATIVE WILSON, recalling the debate last year, related her observation that it takes the producers a long time to make decisions. Therefore, she surmised that the producers would need some certainty as soon as possible, before they would even [be interested].

COMMISSIONER GALVIN opined that he doesn't believe anyone is suggesting that the rate be set weeks before an interested party is asked to make the decision. This is a matter of when in the sequence of events [the tax rate should be set]. There is potentially up to three years between when the license is issued and when the open season would take place.

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COMMISSIONER GALVIN, returning to his PowerPoint presentation, directed the committee's attention to slide 3 regarding the state's terms. He pointed out that the state's "must haves" are located in the section of the legislation that addresses the requirements placed on the licensee. The "must haves" are geared toward achieving a competitive and vibrant oil and gas industry on the North Slope in the future. In order to achieve the aforementioned, there needs to be a pipeline that begins with a low tariff and a pipeline that can and will be expanded when new gas is found. That expansion must be something that the explorers can rely upon, he said. He opined that the "must haves" were developed after much thought and research into what is commercially reasonable as well as where the state's true interests lie in this pipeline. Additionally, the state wants to ensure that there will be opportunities for in-state use and that there are opportunities for Alaskans to enjoy job opportunities due to the construction of the pipeline and the expanding oil and gas sector in the North Slope. He characterized the "must haves" as the state's bottom line. He then opined that it's for the state, through this process, to tell the industry and the nation what the state's "must haves" are. Furthermore, the state should receive something in return for its \$500 million, a pipeline that meets the state's needs.

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CO-CHAIR GATTO asked if the producers have voiced any objection to the "must haves."

COMMISSIONER GALVIN noted that there is a slight variation in the message from the producers. For example, ExxonMobil

Corporation (ExxonMobil) has opined that the state shouldn't establish "must haves" but rather should have broad objectives and allow the applicants to suggest the "must haves." However, other participants have suggested moving some of the items from the "must have" list into a valuation criteria. When the latter suggestion is made, one must consider why it was suggested. Commissioner Galvin opined that the must have list includes those things the state truly must have and shouldn't negotiate away. He mentioned that another aspect to consider is whether the change desired by the applicant is a change to the competitive field that would provide that applicant with a competitive advantage.

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REPRESENTATIVE ROSES related his understanding that during the application process, the applicant must specify its project, the route, size, design, timelines, budget, and its capacity. However, he questioned how an entity can develop a comprehensive plan for the capacity if there haven't been discussions with those who have the gas regarding how much they're willing to provide. An integral part of how much gas they're willing to provide, he surmised, is probably directly proportional to the tax they have to pay and whether it's profitable to distribute the gas. Therefore, he questioned how the plan is put together without having such a commitment from the producers. Furthermore, if the state has a list of "must haves" it's likely that all other companies that have to generate a profit do as well. Representative Roses inquired as to how an entity reaches a point in the application process to provide a somewhat realistic expectation of capacity without having some commitment from the producers as to what they're willing to provide. He further inquired as to how the producers will know the aforementioned if they don't know what their costs will be.

COMMISSIONER GALVIN explained that the sequence of events is that [an applicant] is going to provide the state with the plans for a pipeline that has a certain capacity. That capacity will be based upon the expectation of what will be committed once an open season occurs. The open season will confirm or deny whether it's a reasonable expectation.

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REPRESENTATIVE ROSES posed a scenario in which an applicant has preliminary conversations with the producers who say they will provide a certain amount of gas or a certain amount of time and

the applicant says a pipe of a certain size is necessary. During the open season the tax rate is determined and the producers change the amount, although it was designed based on what the applicant thought he/she would have. Representative Roses then related his understanding that part of the design is how to expand the capacity. In that regard, he questioned whether the design would include expansion of the capacity due to new exploration or the underestimation of the [amount of gas] because of the lack of knowledge with regard to fixed costs.

COMMISSIONER GALVIN deferred to Mr. Shepler. He suggested that there is some confusion with regard to how the uncertainties fit into the level of gas that would be committed. If the tax rate changes, there isn't suddenly more gas to flow.

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DONALD SHEPLER, Attorney at Law, Greenberg Traurig, LLP, informed the committee that in the Lower 48 the open season process evolved as a way for Federal Energy Regulatory Commission (FERC) to assure that pipeline capacity, new projects, and new expansions are offered to anyone who desired such access. He characterized the open season as an interactive process that involves communication with the potential shippers and even perhaps nonbinding open seasons to test the waters. Mr. Shepler said that it isn't unheard of for a pipeline to put out an open season and determine that the demand was inadequate for what it had in mind. He recalled an instance in which there were at least four open seasons for a project that ultimately resulted in a major pipeline interconnecting system. Another aspect is that FERC is going to review this open season proposal before it becomes official in order to ensure that it's not a discriminatory open season.

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REPRESENTATIVE ROSES surmised then that an entity comes in with a design in which a certain size [pipe] with a certain size capacity is proposed, then an open season occurs. Based on the results of that open season and the commitment of the producers with regard to providing gas to the line, the [project] would be resized based on the need.

MR. SHEPLER replied, "Generally, yes." In that context it's important to note that the pipeline is talking to its future customers, shippers, which can be producers or nonproducers. In

Alaska, for the most part, there is a known size of the resource base on the North Slope.

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REPRESENTATIVE ROSES asked if the application process is required to occur prior to the open season, or should the open season occur first and then design a pipe to fit the capacity that's guaranteed. He questioned why there should be multiple open seasons to achieve the right size of the pipe.

MR. SHEPLER reminded the committee that the unique situation in Alaska is that it's known that there is 8 billion cubic feet (bcf), more or less, that's going around in circles. Furthermore, the state also has the experience of negotiations under the Stranded Gas Act a couple of years ago. Those negotiations centered around a reasonably narrow range of sizes. He opined that the real issue is whether the producers will commit their gas to a project in the open season. The process of the open season starts the FERC proceedings, which eventually lead to a FERC certificate application. He characterized the aforementioned as a funnel narrowing the level of uncertainties. By the time FERC has approved a certificate, the size of the pipe, the route, and the projected costs are known. The open season starts the aforementioned process going and culminates under AGIA with the commitment by the licensee or applicant to process a FERC certificate.

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REPRESENTATIVE ROSES related his view that there is an application process that uses theoretical concepts in terms of the design. If the open season exceeds the expectation, then a larger pipe may be needed. Representative Roses opined that [under AGIA] it seems that the decision of who to grant the license will be based on the size of the pipe, the route, and the capacity. The open season occurs and after an applicant is determined, that applicant's design work is modified based on the open season. He asked if there is a law preventing an open season from occurring prior to designing the size of the pipe and awarding a license to move forward with the pipe.

COMMISSIONER GALVIN noted his agreement that the natural progression of the project is what Representative Roses described. However, it's not happening. He opined that it's not happening because the market isn't working in that direction since there are three companies that hold all the rights to all

the gas. Those three companies, the producers, aren't willing to move ahead with any decision making until they receive something more than they received last year.

[2:07:08 PM](#)

REPRESENTATIVE ROSES related his understanding then that by doing AGIA and now having someone apply for a theoretical construct for a pipe, the producers now have more than before.

COMMISSIONER GALVIN clarified that the producers have a project that defines the economics of the line. The [producers] will make their decision based on a known pipe and a known cost. The producers will then explain to the state why they aren't committing their gas to the line based on a real project. Therefore, AGIA is intended to force the issue through the state putting up the money to induce someone to move the project to the open season. The project would then be on the table and the costs, tariffs, and risks to the producers would be known. The producers would then have to decide whether they are going to do the project.

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REPRESENTATIVE ROSES inquired as to what happens if the producers still aren't willing to cooperate.

COMMISSIONER GALVIN answered, "Because then we will have a project that has an economic base." The state can then ask the producers why they aren't putting their gas in the line. If the producers, as suggested by Representative Roses, say it's because they don't want to put their gas in the line, then they'll have to explain that to Congress, consumers, the state, and the Federal Trade Commission (FTC). If the project proves to be economic and the producers choose not to participate, they will have a lot of answers to provide.

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REPRESENTATIVE ROSES, returning to Representative Seaton's earlier comment, opined that unless the producers see something different that will entice them to sell what they aren't willing to now, it sounds like the project is back at the point of the Stranded Gas Act. However, much more time, 15-20 years, will have passed at the time litigation is decided.

COMMISSIONER GALVIN stated that he and Representative Roses are concerned about the same thing; the risk that as more time passes, Alaska teeters closer to the financial edge. The question is whether to have the discussion about what is necessary to make this project happen today with all the uncertainties or to have the project move ahead to the point at which the cost of the project is known. He opined that when the discussion occurs in that context, it's a completely different discussion than what is occurring now. Furthermore, AGIA provides an opportunity for the producers to decide now whether they want to participate and take the state's terms in order to ensure the opportunity isn't lost. The aforementioned is a much better position for the state than the current situation.

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CO-CHAIR GATTO highlighted that the producers are not without risk. In fact, at this moment it isn't their gas, they only have a lease to produce it. However, if, in a few years, there is a plan and a builder, the producers would be at risk because there is a requirement. If the requirement isn't met, the producers have to give up the gas. He characterized [AGIA] as an opportunity for the producers to be the builder.

[2:15:44 PM](#)

REPRESENTATIVE WILSON, referring to page 4, lines 7-14 of CSHB 177(O&G), recalled that last year that [the producers] couldn't make a decision on the size of the pipe until after the open season. At that point, FERC would get involved. She further recalled that [the producers] were contemplating 48-inch pipe, which is the largest built thus far. However, a 52-inch pipe would be cheaper in the long run due to the price of gas. As more gas is found, it's cheaper to have the larger pipe than to have feeder lines. Still, the 52-inch pipe hasn't yet been invented nor has the machinery required to put it in place, and therefore she questioned how such could be said to be economically viable.

COMMISSIONER GALVIN said that any project based on materials still in the laboratory will have to be seriously questioned in regard to whether it will be delivered. The aforementioned is why the analysis is both economic and technical. He reminded the committee that when a proposal is made, it will be based on the known resource and an expectation about what may be committed at an open season. The pipe will be designed based on the range of possible commitment that they'll receive.

Therefore, the state, in its analysis, will have to factor in the likelihood of actually obtaining that level of commitment and the plan's flexibility in regard to the various levels of commitment. Commissioner Galvin stressed that everyone should realize that what the producers propose now is before an open season and before the actual commitments are received or there is a sense of the initial shipping capacity. The producers, he pointed out, will have to be responsive to the state's interests and their interests in having a line that is expandable and would be cost effective for some time. This means that the producers' proposal will have to address those different scenarios, which will also be reflective of both the design of the pipe or the other steps to commit more gas or a particular capacity.

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REPRESENTATIVE WILSON surmised then that the state is asking the producers to put down on paper "imaginary" numbers they believe will work. The state will then have to review those numbers and decide whether they're possible.

COMMISSIONER GALVIN noted that all the numbers from the producers will be based on the level of analysis done to that point. The level of confidence that the state will have in the producers' numbers will be based upon the level of detail provided in the analysis. There will have to be [analysis/data] to support the numbers proposed by the producers.

[2:22:28 PM](#)

COMMISSIONER GALVIN, in further response to Representative Wilson, said that there is a certain amount of flexibility in regard to what the producers choose to do at a certain point in the process.

[2:23:46 PM](#)

CO-CHAIR JOHNSON inquired as to the location of the five delivery points that are required in the legislation.

COMMISSIONER GALVIN clarified that the applicant has to commit to five delivery points once the demand is present to require them. In further response to Co-Chair Johnson, Commissioner Galvin said that five isn't a magic number.

CO-CHAIR JOHNSON surmised then that [if there is flexibility with regard to the number of delivery points required], then five delivery points must not be a "must have." Therefore, he questioned why it's a "must have."

COMMISSIONER GALVIN explained that the "must have" is that the producers have to agree to meet in-state demand. One aspect of that is having a commitment that the producers will provide for five offtake points.

[2:25:04 PM](#)

CO-CHAIR JOHNSON inquired again as to why there are five delivery points and the location of them. He pointed out that the legislation calls for [applicants/producers] to come forward with certainty that will be evaluated by the state. Therefore, he questioned why the same can't be expected from the state.

COMMISSIONER GALVIN related that from the administration's perspective if the delivery points were eliminated, [the contract] isn't as valuable. From Commissioner Galvin's perspective the question would be whether the state should consider a proposal that doesn't include delivery points. By placing the delivery points in the "must haves" section, it means that the state doesn't want to consider an application that doesn't have five delivery points. He clarified that the application doesn't have to specify the five delivery points, the applicant merely has to commit that when the opportunity arises and there is a demand for in-state use, they will allow the delivery point to take place. Whether there are three, five, or seven delivery points is open to discussion. The five delivery points was what [the department] anticipated within the state.

CO-CHAIR JOHNSON said that he wants to know what are really "must haves." He inquired as to what would happen if the committee reduces the number of "must haves." He specifically inquired as to what are the deal breakers.

COMMISSIONER GALVIN clarified that the items labeled as "must haves" in the legislation are telling the world that these are the state's "must haves." He related that "we" are open to discuss what should or shouldn't be on the list of "must haves." He further clarified that whether these are the administration's "must haves" is a different question.

[2:29:07 PM](#)

CO-CHAIR JOHNSON inquired then as to why what is currently referred to as "must haves" aren't set as guidelines/criteria, such that the applicant that reaches or exceeds the guidelines is awarded the contract. He questioned why an applicant that meets all the requirements, but only has three delivery points would be considered noncompliant.

COMMISSIONER GALVIN opined that since the state is willing to put up \$500 million and match [the applicant] in its costs, the state has the right to ask for things in return. He further opined that [the department] believes it's appropriate for the state to establish at least a floor for what is expected and allow the interested parties to compete on that basis. [The administration], he related, believes that it's appropriate for the state to tell applicants that five delivery points are a "must have." [The administration], he further related, would prefer that the five delivery points remain a requirement for an application to be considered.

[2:32:17 PM](#)

CO-CHAIR JOHNSON said that he is looking at what is imperative to the legislation. He again inquired as to what is a true "must have" that's absolutely nonnegotiable. He then inquired as to what can be included in HB 177 to broaden it [such that it obtains many applicants].

COMMISSIONER GALVIN commented that it's a bit disconcerting to have a discussion about the legislation in regard to what can be stripped out and remain something the administration is willing to endorse. Commissioner Galvin related that the administration believes HB 177 is in great shape as it is now and doesn't need to be changed much at all. He said that the administration is interested in hearing what areas the committee finds to be problematic.

[2:34:48 PM](#)

CO-CHAIR GATTO mentioned that in 2000 the producers invested \$125 million on a feasibility study, so there has been work done [on this project].

COMMISSIONER GALVIN interjected that TransCanada will probably comment on how much it has invested in the project also.

[2:35:22 PM](#)

COMMISSIONER GALVIN, returning to his PowerPoint presentation, directed attention to slide 4. He related that the decision-making process is intended to be transparent and competitive, not a negotiated process. The process affords the opportunity of the bids being reviewed in a public setting during which the public can comment. The decision [as to who is awarded the contract] is made and returned to the legislature for approval. The entire process is intended to be as transparent as possible so that the public can have confidence in the outcome.

[2:36:26 PM](#)

REPRESENTATIVE GUTTENBERG related his understanding that the public is going to have 60 days for review. He then asked if the administration is going to place the contract proposals without analysis before the public or is there going to be some process in which there are comparisons and data that a lay person can understand.

COMMISSIONER GALVIN answered that at this point the administration doesn't have a preconceived idea how the information will be presented and thus the legislation doesn't include such. However, in keeping with the intent of having public involvement, it's incumbent upon the administration to make information available to the public in a way that's understandable. He then turned the presentation over to Mr. Shepler.

[2:38:12 PM](#)

MR. SHEPLER, referring to slide 5, opined that expansion of the pipeline is vital to the ultimate goal of establishing a vibrant, competitive oil and gas driven economy on the North Slope. The FERC, in its orders, have recognized the unique situation of Alaska and that there will almost certainly be only one pipeline built out of Alaska. The aforementioned has led FERC to adopt a rebuttable presumption in favor of rolled-in pricing, which means that as the costs are accumulated they are divided amongst all the volumes under contract. The FERC orders recognized that there are some governmental subsidies that are included in the initial project in the form of federal loan guarantees that will reduce the borrowing costs of the sponsor of the pipeline project. Another subsidy is the seven-year depreciation for income tax purposes, which reduces rates for initial shippers. Mr. Shepler clarified that ultimately the rates for all initial shippers will be reduced by the

aforementioned factors, and therefore reduce the real-world impact of rolling in pricing when expansion becomes more expensive. He informed the committee that initial expansions will typically be based on adding new compressor units, which are relatively low cost and produce a substantial bang for the buck. However, in order to maximize the value of the pipeline itself the expensive looping and expansions will increase the rates for all shippers.

[2:41:22 PM](#)

REPRESENTATIVE GUTTENBERG requested clarification with regard to the looping.

MR. SHEPLER explained that looping is a pipeline industry term for putting in a parallel pipe, a welded in integrated piece of the original pipe. Once the gas has been compressed and no more expansion from compression exists, the size of the pipe can be doubled by putting in another run of pipe. The aforementioned is expensive because miles of pipe are being purchased. Mr. Shepler related his understanding that the pipe would be installed a few miles downstream of a compressor initially. As more volumes come on, a few more miles would be put in downstream of the compressor, ultimately resulting in a dual line. He pointed out that looping is more expensive than simply purchasing another compressor unit or station. At some point during the looping, the rolled-in rates increase. Mr. Shepler highlighted that AGIA specifies that the obligation for the pipeline company to file for and support rolled-in rates is capped. The pipeline company has to commit that it will file for and propose rolled-in rates so long as that doesn't increase the rate for shippers by more than 15 percent over initial tariff rates.

[2:43:40 PM](#)

REPRESENTATIVE SEATON asked if that 15 percent over initial tariff rates is in nominal dollars.

MR. SHEPLER reminded the committee that he is an attorney not an economist. However, he offered that the target here is the initial regulated rate that the FERC approved when the pipeline went into service. The legislation, AGIA, contemplates the initial rate increase of up to 15 percent through roll-ins and the pipeline company would have the obligation to file for that, subject to FERC approval.

[2:44:44 PM](#)

REPRESENTATIVE SEATON asked if this is a meaningless number 10 years later after inflation. He asked if it's the actual dollar value at the time FERC decided the rate.

[2:45:27 PM](#)

KEVIN BANKS, Acting Director, Division of Oil & Gas, Department of Natural Resources, posed a scenario in which the initial rate is \$2.00 and 10 years from now expansion is occurring that will increase the cost of shipping to about \$2.30 on a rolled-in basis. Inflation isn't taken into account. He informed the committee that the fact that it's based off of the rate in the initial open season works in the favor of the initial shipper because the 15 percent uptake is still measured against a \$2.30 cap. If the expansion is more that \$2.30, the amount above \$2.30 will be determined using an incremental basis and thus the cost will shift to the new shippers. Mr. Banks, in response to Co-Chair Gatto, said [the cost] is nominal and works to the favor of the initial shipper if inflation has occurred during the intervening period. The cap means that 15 percent over the initial rate will be borne by the expansion shippers.

[2:48:09 PM](#)

REPRESENTATIVE ROSES questioned what occurs if there is another roll-in later. He asked if since the 15 percent cap has been reached, there would be no new increase and everything would be passed on to the new guy. Or, would \$2.30 become the initial rate for the next roll-in, he asked.

MR. BANKS answered that the \$2.30 will remain and thus the next expansion will be incremental.

COMMISSIONER GALVIN clarified that it won't necessarily be incremental. He explained that AGIA is set up to obligate the licensee to support rolled-in rates up to this limit. Therefore, the licensee may propose rolled-in rates for its own purposes. This provision is included with the understanding that the licensee may prefer not to roll-in rates beyond this level.

[2:50:17 PM](#)

REPRESENTATIVE ROSES surmised then that this rate is the tariff being paid to ship gas down the line.

COMMISSIONER GALVIN replied yes.

REPRESENTATIVE ROSES further surmised, "So, the initial commitment by the producers to put 'X' volume of gas into the line - they're going to start off with this initial rate. We now expand the line because somebody else has come on with a new field. They can be brought up to 15 percent more than what they originally paid, still based on the volume that they had agreed to pay."

COMMISSIONER GALVIN interjected that at each expansion, when the rate changes, [the licensee] will have the opportunity to opt-out of the commitment.

REPRESENTATIVE ROSES asked if the opportunity to opt-out is in the legislation.

[2:51:17 PM](#)

MR. SHEPLER said that the opportunity to opt-out is part of FERC's policy. He explained that FERC requires that for a pipeline company that expands, there has to be an offer to let parties "turn back" capacity. There might not need to be an expansion at all if those holding the capacity are willing to return it to the pipeline to sell it to those wanting the new capacity.

[2:51:49 PM](#)

REPRESENTATIVE ROSES posed a scenario in which one of the three producers agrees to sell the gas. However, five years after gas flows down the line a new well is brought on and the three original entities are offered the ability to opt-out. In such a scenario, he questioned what would stop them from all opting out unless there are new negotiations that result in a different tariff rate.

[2:52:33 PM](#)

CO-CHAIR GATTO pointed out that just because there is expansion doesn't mean that the price increases. He reminded the committee that the price of a compressor is little compared to the price of the pipeline. He opined that the initial expansion probably lowers the price for everyone.

MR. SHEPLER confirmed the aforementioned.

CO-CHAIR GATTO said that part of expansion is beneficial.

[2:53:19 PM](#)

REPRESENTATIVE ROSES said he understood that, but pointed out the potential in the legislation for a 15 percent increase. He related his agreement that no one would opt-out if the price is lowered. However, any increase in price could result in one opting out since it would become a leverage point. He suggested that the concern would be that once costs are increased there is no mechanism or guarantee that all three major producers can't pull out unless the state renegotiates.

[2:53:51 PM](#)

MR. SHEPLER stated that the turn back is limited to the amount of the new demand. He then pointed out that the FERC policy in the Lower 48 from 1960-1999 was for rolled-in treatment for all expansions, even when it increased existing shippers' rates. In 1995, the aforementioned was somewhat limited such that if the expansion had any system benefits to all users and increased shippers' rates by 5 percent, rolled-in pricing was required. In 1999 FERC changed its policy saying that it created an unlevel playing field for competing pipelines. Therefore, the policy in the Lower 48 switched over to incremental pricing and thus it isn't a foreign concept in the Lower 48 for an existing shipper to face increasing rates as a result of expansions. Mr. Shepler then pointed out that rolled-in rates are the standard operating practice for expansions in Canada.

[2:55:54 PM](#)

MR. BANKS highlighted that Canada, at the outset of its oil and gas industry in Alberta, was much the same as Alaska today. Initially, rolled-in rates made it possible for the market within Alberta to expand dramatically. At the same time, very long pipelines were built across Canada. Furthermore, the development of the gas line system within Alberta has resulted in thousands of producing fields and thousands of miles of pipeline serving those fields. As a consequence of that development, one sees the same access to the marketplace that is present in the Lower 48 where a fairly competitive market for transportation exists as a consequence of Canada's rate-setting policies.

[2:57:39 PM](#)

MR. BANKS, referring to slide 7 regarding resource risk, explained that resource risk pertains to what exploration and production companies as well as the state have to review in terms of their expectations. Mr. Banks then related the following quote from Rex Talston (ph), ExxonMobil Corporation, which read: "We're willing to take geological risk, we're willing to take cost risk, we're willing to take price risk. But we can't take fiscal terms changing on us risk because then I can't calculate the basis on which to decide whether it's a good investment or not." Mr. Banks indicated that the state is similarly involved in each of those types of risk. With regard to geological risk, the state has its own geological risk to address. The state is more involved than ever in the cost of developing those risks because the state has assumed a net profit tax system through the PPT. Furthermore, the state shares in the transportation cost risk. He noted that companies will be allowed to deduct transportation costs, including the potential "that they may have to pay for a 'take-for-pay' situation." In the leases the state is proposing to make under AGIA, the state would assume that the actual and reasonable costs, including empty capacity, should be an allowable deduction on the royalties and taxes. The state will assume the same sort of market risk as the companies and will evaluate the royalties and taxes based on the prices the market will deliver at any given time.

MR. BANKS highlighted that the state faces other risks as well, such as the risk of nonperformance by the lessee. He emphasized that the state doesn't control the timing of production from the leases. The aforementioned is a decision made by the lessee as it works through its economics. Point Thomson is an extreme example of how the state doesn't have control over inducing production on the state's leases. Furthermore, the oil and gas business is generally risky and is a business in which large corporations participate daily. The reason these large corporations can manage the risk is because they have a portfolio of activities around the world. Mr. Banks said that the primary reason the oil and gas industry is an integrated industry is because it's a way of managing price risk and geology due to the opportunity to develop high risk:high reward prospects balanced against low risk:low reward prospects. The state doesn't have that kind of broad portfolio. Therefore, in a sense the state is faced with a different risk profile.

MR. BANKS then turned to price risk. He informed the committee that the price risk has recently increased from \$4 to \$14 for

gas in the Lower 48. The aforementioned is a much greater swing than the state thought it could possibly impose, in terms of changing the state's fiscal terms. He acknowledged that the lessees have raised this issue as they are accustomed to dealing with much greater risk in their business. He opined that the state is a fairly stable and patient regime with which the lessees can work.

[3:02:47 PM](#)

REPRESENTATIVE GUTTENBERG returned to the PPT credits in relation to oil versus gas, and requested further explanation.

COMMISSIONER GALVIN clarified that the PPT system is an integrated oil and gas system. Therefore, deductible costs due to gas production are deducted against the PPT payment, which is either for oil and gas tax. To the extent that the lessee has an allowable deduction, gas costs could be deducted against the oil production tax or be a credit if there's no production tax. With regard to what constitutes a deductible gas expense, Commissioner Galvin pointed out that per the PPT it must be a lease-hold expense. A lease-hold expense is based on what is upstream of the point of production, which is where the gas moves out of the control of the lessee to a more common system. With oil, the aforementioned takes place either when the product moves into a common carrier line or at TAPS. With gas, it would take place at the entrance of the gas treatment plant (GTP). The gas treatment plant would be downstream of the point of production and thus wouldn't be a deductible expense under the PPT. However, everything from [the gas treatment plant] upstream would be deductible under the PPT, both as a capitol expense, the 20 percent, and as part of the ongoing expenses, the 22 percent deduction from the [lessees'] revenue.

[Co-Chair Gatto passed the gavel to Co-Chair Johnson.]

[3:06:11 PM](#)

REPRESENTATIVE GUTTENBERG surmised then that all of the distribution lines would be able to be written off.

COMMISSIONER GALVIN answered that is a potential so long as the distribution lines are part of a system short of that point of production. In further response to Representative Guttenberg, Commissioner Galvin said he wasn't sure if there is a way to build in some pre-treatment on lease. Potentially, [the lessee]

could add additional costs in that sector of development that could be deducted under the PPT.

[3:07:11 PM](#)

REPRESENTATIVE GUTTENBERG asked if the regulations on the PPT have been completed.

COMMISSIONER GALVIN replied no.

[3:07:18 PM](#)

REPRESENTATIVE GUTTENBERG inquired as to how the deductions would be written into the tariff.

MR. SHEPLER, noting his limited knowledge of how the PPT actually works, said that he can't provide an answer.

COMMISSIONER GALVIN offered to review the question and provide the committee with an answer.

[3:08:39 PM](#)

MR. BANKS, continuing with slide 9, explained that a system is being created that is a prescription or a definition of a set of terms for the state and the applicants in the form of a contract. [The legislation] lays out a set of relatively general requirements such that the marketplace is allowed to generate the most creative solutions to these issues. For example, overrun risk will be balanced and shared between the pipeline and the upstream shippers. The "must haves" provide a framework in AGIA between the state and the pipeline owner, the lessees and resource owners, as well as between the pipeline itself and the resource owners and those competing for the application. Mr. Banks highlighted the importance of recognizing that [AGIA] is establishing a mechanism that levels the playing field while creating a setting in which all the players come on the field. The "must haves" accomplish the aforementioned and allow the state to achieve some critical values out of the pipeline in terms of expansion, in-state use of gas, jobs, low tariffs, et cetera by bringing all parties together in a competitive setting. The evaluative criteria, he said, is intended to establish the aforementioned by setting out a mechanism in which the state specifies what it means in terms of potential revenue for the state and balance that against whether the pipeline applicant can really deliver.

[Co-Chair Johnson returned the gavel to Co-Chair Gatto.]

[3:11:32 PM](#)

COMMISSIONER GALVIN turned the committee's attention to slide 10 regarding the FERC process and requested that Mr. Shepler focus on some aspects of the FERC process particular to Alaska. He further requested discussion of the risk associated with the initial open season and how it can be shared between the pipeline company and the initial shippers.

[3:12:06 PM](#)

MR. SHEPLER said that the FERC process basically narrows the range of uncertainty. The process begins with the open season that has to be pre-approved by FERC and which results in binding solicitation of capacity interest and precedent agreements that define termination conditions. From there [an applicant] would move through the FERC certification process, which involves a detailed project description with environmental research. Furthermore, FERC must make a finding on the project, as required by the present public convenience and necessity. Unique to Alaska is that Congress has already codified that the pipeline is required by the public convenience and necessity. In fact, two weeks ago FERC representatives before the House Special Committee on Oil and Gas confirmed that from that standpoint, it's a unique pipe.

[3:13:43 PM](#)

MR. SHEPLER, referring to slide 11, explained that the rates for pipelines in the Lower 48 are divided into the following two categories: recourse rates and negotiated rates. The recourse rate is the default rate, the cost-based conventional rate the [Regulatory Commission of Alaska] RCA would establish. The FERC also allows for negotiated rates in which a willing buyer of capacity and a willing seller of capacity meet and agree on price terms that are agreeable to both parties so long as the shipper has access to the default rate. The FERC encourages parties in new projects and expansions to negotiate between themselves the risks of cost overruns. For example, on the Rockies Express Pipeline Project the company offered fixed rates for the full 10-year term of the contract as a negotiated rate option that was subject to change in future rate cases. Under the negotiated rate if the pipeline company overruns its cost estimate, the pipeline company and its shareholders will have to

bear the risks of that cost overrun. He noted that ultimately FERC has to approve the negotiated rates.

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MR. SHEPLER, in response to Representative Seaton, said that AGIA contemplates commercial activity structured around commercially reasonable terms. There is no state veto, although he suggested that the state, as a participant, could exercise its right to comment on the setting of the recourse rates and the negotiated rates. In the context of a project like this most of the initial shippers will move forward under negotiated rates as opposed to recourse rates, he opined.

[3:17:06 PM](#)

REPRESENTATIVE SEATON posed a scenario in which there is an open season and the producers wait it out. In the meantime, Shell comes forward and bids for the gas. In such a situation, what is the state's position, he asked.

COMMISSIONER GALVIN, referring to slide 12, said that AGIA provides applicants multiple opportunities to participate. He opined that a scenario in which a pipeline is proposed and a company is willing to commit its gas to the line even in the face of incurring significant development costs in order to get the gas into the line begs the question as to why the state's lessee wouldn't be willing to put gas in the line when they wouldn't have to incur the same development costs. The aforementioned doesn't seem to be a realistic scenario, he opined. He highlighted that the explorers would have a much higher hurdle to commercialize the producers' gas than would the producers. Therefore, it doesn't seem likely that a line would be filled with OCS [outer continental shelf] gas as the initial product. He reiterated that AGIA provides multiple opportunities for the producers, in particular, to participate as well as to the third party pipeline companies and other entities during the initial inducement. At the point of the open season, there is again an opportunity for the producers to participate by committing their gas to the line. Explorers and gas purchasers may decide to participate at this time as well. He said that AGIA is structured so that the various participants see opportunities at various stages and make a decision to move the project ahead.

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COMMISSIONER GALVIN opined that as the state moves through this process and the unknowns are eliminated and the actual project is identified, the project will be clearer than it is today. However, he acknowledged that there may still be some level of uncertainty with some aspects of the project. Through the negotiated ratemaking some of that uncertainty can be mitigated between the pipeline and the shippers, although it may not be at the point of obtaining the necessary commitment. Therefore, the administration feels strongly that the state should obtain from the licensee a commitment from the outset that it won't use that as a sign of failure and that the licensee will move forward if it's an economic project. Otherwise under the terms of AGIA it would have been dropped along the process. With a significant amount of confidence, Commissioner Galvin opined that the producers in this process will recognize the opportunity at each step of the process and determine it's in their interest to participate.

[3:24:26 PM](#)

REPRESENTATIVE GUTTENBERG recalled that the 2005 FERC ruling includes a section for an in-state demand study and a section regarding methodology of determining value of bids for deliveries in the state. He asked if those sections would be appropriate in AGIA.

MR. SHEPLER clarified that the 2005 FERC ruling requires that a "FERC-compliant open season" must have been preceded by the in-state study and requires distance-sensitive rates for deliveries in Alaska, as does AGIA. The aforementioned is already part of the federal requirements. He said he didn't know whether the aforementioned should be part of the AGIA "must haves." However, the AGIA requirement for distance sensitive rates for in-state deliveries is the real concern for Alaskans as well as the instant delivery points.

[3:26:18 PM](#)

REPRESENTATIVE GUTTENBERG opined that it would be advantageous to Alaska to do so sooner through AGIA rather than during the FERC process.

COMMISSIONER GALVIN related his belief that the in-state demands study has to be done prior to the open season under the FERC rules. Therefore, it wouldn't be at the very end of the process. Commissioner Galvin opined that [the administration] clearly recognizes that meeting in-state demand is an important

part of the natural gas pipeline policy as a state. [The administration] further recognizes that the pipeline needs to move forward as quickly as possible and have the opportunity for in-state demand to catch up to the initial open season. More significantly, in-state demand is likely to be met through the expansion and opportunities for future expansion and open seasons for in-state use, he said. He opined that when [the administration] reviewed how to meet in-state demand in AGIA the focus was on long-term issues. He mentioned that the Alaska Natural Gas Development Authority (ANGDA) has done in-state studies and have expressed concern with regard to the level to which the state will be ready to participate in an initial open season. He mentioned that the House version of AGIA includes a gasification revolving loan program. At some point, one must decide where the initial priorities lay in order to get the project moving and an initial open season. "We don't want to necessarily have that slow down because of a need for an additional study ... that's not going to actually meet in-state demand in a timely manner," he opined. However, he opined that it's worth reviewing in terms of where the state stands regarding how to meet both goals.

[3:29:46 PM](#)

REPRESENTATIVE GUTTENBERG reminded members that he lives in a town that has an oil pipeline, a refinery, and where he pays high national averages for petroleum products. He then commented that it's in the state's best interest to plan to have optimal use of a gas pipeline throughout the state.

CO-CHAIR GATTO interjected that once a gas pipeline is in place several things will follow, such as serving villages and propane availability.

[3:30:33 PM](#)

REPRESENTATIVE SEATON recalled that yesterday there was discussion about carbon dioxide as an evaluation criteria, although there has been no mention of it today.

COMMISSIONER GALVIN confirmed that the state is interested in working with the committee to address that issue. Therefore, a number of different ways to address it are being reviewed in terms of what language may or may not be necessary to include in the legislation. The desire, he opined, is to achieve an environmentally friendly project.

[3:31:43 PM](#)

REPRESENTATIVE SEATON, referring to Chevron's annual report regarding its management of energy, directed attention to page 10, which relates that Chevron has installed California's first mega-watt class hydrogen fuel cell co-generation plant.

MR. BANKS related his understanding that the aforementioned plant uses methane.

REPRESENTATIVE SEATON confirmed that it does. He said, "As long as you're not releasing methane or fugitive CO<sub>2</sub>, that's what we're trying to get at is so that we're not looking at a cap and trade or something that could impact negatively the pipeline. So, it's an interesting thing if we have fuel cell technology that doesn't release methane, that actually uses methane for the hydrogen source. But as long as we're not releasing CO<sub>2</sub> that's ... the whole purpose of getting around addressing this somehow in a criteria."

CO-CHAIR GATTO pointed out that there is CO<sub>2</sub> that is a raw material and there's CO<sub>2</sub> that is created.

[3:33:51 PM](#)

COMMISSIONER GALVIN, drawing the committee's attention to slide 13, reiterated that AGIA sets up a commercial vehicle geared toward leveling the playing field and having competition along with a transparent process. Furthermore, AGIA meets the state's needs, which are geared toward expansion and low costs. The commercial interests in the project are used to try to resolve some of the issues the state faces with this project. Commissioner Galvin restated his earlier comments that AGIA provides an opportunity for participants to enter the process and receive state inducements for something in return. He highlighted that any project can move forward without any state participation and AGIA doesn't preclude the aforementioned. Still, the administration believes that AGIA provides the best mechanism for the state to participate in the project so that ultimately there is the greatest likelihood of the project moving forward in a timely manner with terms that are favorable to the state's long-term future.

[3:35:33 PM](#)

CO-CHAIR JOHNSON asked if there can be a rolled-in and an incremental rate request. He clarified that he was thinking of

Shell from which no tariffs or oil taxes are received. He questioned whether the state can treat companies differently during an expansion based on whether there's a rolled-in rate or an incremental rate.

MR. SHEPLER said that technically a partial rolled-in rate and an incremental rate can be used. However, he pointed out that it's a policy call. He noted that ultimately FERC will review the project in terms of consumers in the Lower 48 and the other shippers on the system. Therefore, he surmised that FERC will follow its policy of favoring rolled-in pricing for any expansion, regardless of whether it benefits the state directly or not.

[HB 177 was held over.]

[3:38:40 PM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:30 p.m.