

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

April 12, 2007

1:02 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  
04/11/07 (H) Heard & Held  
04/11/07 (H) MINUTE(RES)  
04/12/07 (H) RES AT 1:00 PM BARNES 124

#### **WITNESS REGISTER**

MARTY MASSEY, U.S. Joint Interest Manager  
Exxon Mobil Corporation ("ExxonMobil")  
Houston, Texas

POSITION STATEMENT: Presented testimony and answered questions regarding CSHB 177(O&G).

#### **ACTION NARRATIVE**

**CO-CHAIR CARL GATTO** called the House Resources Standing Committee meeting to order at [1:02:58 PM](#). Representatives Gatto, Edgmon, Kohring, Wilson, Seaton, and Roses were present at the call to order. Representatives Johnson, Guttenberg, and Kawasaki arrived as the meeting was in progress. Representative Fairclough was also in attendance.

#### HB 177-NATURAL GAS PIPELINE PROJECT

[1:03:12 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 was CSHB 177(O&G).]

[1:04:03 PM](#)

CO-CHAIR GATTO stated for the record that Mr. Massey is able to personally sign an agreement should one be reached between Exxon Mobil Corporation and the state.

MARTY MASSEY, U.S. Joint Interest Manager, Exxon Mobil Corporation ("ExxonMobil"), said that this is correct.

[1:04:52 PM](#)

MR. MASSEY stated that he has held his position as U.S. Joint Interest Manager for ExxonMobil since November 2001 and that he is responsible for the commercialization of ExxonMobil's gas resources in Alaska. He presented his testimony from a written statement [original punctuation provided]:

ExxonMobil has been in Alaska for over 50 years and has been a key player in Alaska's oil industry development. We hold the largest working interest at Prudhoe Bay (36.4%) and our current net production in Alaska is approximately 150,000 barrels per day.

We have benefited from our involvement in the State of Alaska, and we believe that Alaska has benefited from this long-term relationship as well.

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Commercializing Alaska's North Slope gas will allow us to continue this mutually beneficial relationship for another 50 years or more. Let me emphasize that ExxonMobil wants a successful gas pipeline project and we want to move it forward.

The Alaska Gas Pipeline project is important to Alaska, to our nation, and to ExxonMobil. The Project has the potential to generate billions of dollars in revenues for the State of Alaska, the U.S. federal government, and Canada, and could provide a stable and secure source of clean energy for Alaska and North America for decades to come. For ExxonMobil, the project has the potential to add over 1 billion cubic feet per day (EM share) of gas sales, which would be more than a 10% increase to our current worldwide daily gas production. Given the significant impact this project could have on our business, we strongly support efforts to advance a pipeline project and we

are ready to work with Governor Palin and her cabinet and with the Legislature to move the project forward.

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As an illustration of our commitment, EM has spent more than \$180 million studying ways to commercialize Alaska gas. Since the 1970's we have evaluated LNG, gas to liquids and gas pipeline alternatives. Based on these studies we have determined that a Producer gas pipeline project will result in the best value for the State, the Producers and the nation. It is important for me to say ExxonMobil is aligned with the Governor, the legislature and the people of Alaska regarding the overall objective—we are committed to moving the Alaska Gas pipeline project forward.

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ExxonMobil embraces the concept of competition all over the world and is ready to participate in a fair market based competition. We understand the overarching goal of [the Alaska Gasline Inducement Act (AGIA)] is to create open competition but due to the prescribed conditions included in AGIA it will not achieve this goal. A prescriptive bidding process will not allow the flexibility needed for individual applicants to weigh the risks associated with this basin opening mega-project and propose what is necessary to manage these risks.

It is important that AGIA allow applicants to define how they could achieve the State's objectives rather than prescribing specific requirements that must be met. To ensure the best result, AGIA should establish broad key objectives and allow applicants flexibility in meeting those objectives and in defining the requirements that are necessary to make the project commercially viable. If you were to amend AGIA to make it objective driven, it would result in an open competition, maximizing the number of applicants and allowing those applicants to propose innovative solutions.

As such, we suggest AGIA be modified to establish an objective driven process - define the state's broad objectives, request proposals as to how applicants

intend to meet or not meet those objectives, evaluate the proposals and then select the one that best serves Alaska's needs. If none meet the State's overall objectives then you can always reject them or opt to negotiate with the party that most closely meets your needs.

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CO-CHAIR GATTO asked what is the issue that ExxonMobil has with the 20 objectives that are included in AGIA.

MR. MASSEY advised that the broad, key objectives described by AGIA should relate to: making sure that the project delivers the most value for the state; making sure that gas is provided for Alaskans; making sure that people can access the pipe so that explorers can get their gas down the pipeline; and making sure that Alaskans will have the opportunity for the jobs that the pipeline creates. Then, he continued, the state should allow the applicants to lay out how they intend to meet those objectives.

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CO-CHAIR GATTO surmised that ExxonMobil would like to see the remaining 15 objectives deleted and that then it would submit a proposal.

MR. MASSEY said yes.

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REPRESENTATIVE SEATON stated his understanding that there is nothing that prevents ExxonMobil from coming forward right now with a proposal to build a pipeline under those conditions. He asked why this has not happened.

MR. MASSEY responded that ExxonMobil has been asked to participate in an open, competitive process which has been laid out in AGIA and that ExxonMobil has not been asked to provide a proposal that meets its needs. He said that ExxonMobil did do that once before in what is referred to as the old fiscal contract. The process that the administration has laid out is an open, transparent, competitive process which ExxonMobil is ready to participate in as long as it is allowed to participate in such a way that the company can describe what is necessary to make the project commercially viable, and to meet the state's

objectives. Mr. Massey stated that it would not be in ExxonMobil's best interest to participate outside of the open competitive process when that is the direction that the state is trying to go.

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CO-CHAIR GATTO commented that the AGIA bill was introduced on April 4, 2007, and that prior to that date anyone could have come forth with a plan for moving gas. He inquired whether the introduction of new gas is somehow detrimental to ExxonMobil's ability to sell existing gas in the open market at a higher price. Is it an advantage or disadvantage for ExxonMobil to move forward at this time, he queried.

MR. MASSEY responded that it is an advantage for ExxonMobil to move the project forward when it is commercially viable.

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CO-CHAIR GATTO asked at what point would ExxonMobil determine whether it is commercially viable.

MR. MASSEY stated that commercial viability is determined by looking at a combination of different factors: the ability to execute the project, the ability to mitigate the risk associated with the execution, and the range of project costs versus the anticipated range of future gas prices. If the project is judged to be viable, then the company would move forward.

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CO-CHAIR GATTO inquired as to who gathers the information and makes the decision on whether or not to move forward - the corporation's board of directors, a group of other people, or one person.

MR. MASSEY responded that a set of people within the company would make the decision together after weighing and discussing the information provided by all of the experts in each of the different aforementioned categories.

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CO-CHAIR GATTO acknowledged the difficulty in making such a decision.

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MR. MASSEY continued with his presentation:

To understand why it is important to use broad objectives as opposed to prescribing specific requirements it is helpful to review project risks and issues surrounding its development that will have to be addressed by an applicant.

Because there is a perception this is "simply" a gas treating / gas pipeline project, the tendency exists for many to underestimate the size, magnitude, and risks associated with this undertaking. The Alaska Gas Pipeline Project is a world-scale undertaking with significant risks. In fact, the Project would be the largest private investment in North America - significantly larger than most "model" worldwide oil and gas "mega" projects. There is not really another project that compares.

Because of this size, many factors impact commercial viability.

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First there is cost: Our previous estimate of \$20 billion [in 2001 dollars] is now substantially higher. Since 2001, steel prices have nearly doubled. Industry and construction labor costs are experiencing hyperinflation. In addition, world-wide mega-projects are placing pressure on pricing and availability of global materials, and skilled manpower.

Next there is gas price: Despite recent increases, natural gas prices remain highly volatile. The price of natural gas before 2000 was less than currently estimated gas treating and transportation costs.

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Finally, there are many other risks: These include cost overruns, schedule delays, construction conditions, and regulatory and State fiscal uncertainties. It is also important to note that project investments would have to be made over a

period of 10 or more years before gas flows down the pipeline and is sold at the marketplace.

With size comes complexity, and an even greater premium on getting the design concept, contracting and marketing plans right...and then executing these plans efficiently and effectively. Most importantly, size also amplifies the consequences of poor execution. If a mistake is made on this project it would cost us all dearly.

The State of Alaska cannot anticipate how individual applicants will view these risks or how they may address them. Establishing a set of rigid prescribed terms will not allow the flexibility needed for individual applicants to weigh and manage those risks.

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It is also important to understand how pipelines are financed which is a key reason why AGIA should allow flexibility in proposing upstream terms. Commercially-sound oil, gas, and pipeline projects traditionally have been able to obtain financing if they have strong sponsors with proven track records and the financial strength to both provide sponsor equity and to backstop key project commitments. For the Alaska gas pipeline project, key project commitments take the form of firm, long-term gas transportation commitments. Firm transportation commitments are binding obligations made by companies to pay for the cost of reserving a quantity of gas capacity as shippers on a pipeline over a specified period of time, typically many years. These commitments are made during an "open season", which, according to FERC Order 2005 for the Alaska gas pipeline, is a period of at least 90 days during which any and all prospective gas shippers can make binding commitments for a specific volume of transportation capacity.

Financial institutions generally require substantial, long-term, firm transportation commitments to provide funding for a gas pipeline project. These commitments must be provided by creditworthy shippers. In this case, the shippers will be the Producers, and, directly or indirectly, the State or the State's

shipper. These firm transportation commitments are substantial, in the tens of billions of dollars and must be paid whether the shipper making those commitments actually transports gas through its reserved capacity. The shipper is also required to pay this commitment regardless of the price of gas in the market place.

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Pipeline investors use these firm transportation commitments from shippers to show creditors they have capacity confirmed over a sufficient duration to secure financing and must rely on the financial strength of the companies backing the transportation commitments to secure project financing. Thus, the development costs and the associated over-run risk are ultimately borne by the shipper via this commitment. In other words, shippers must make long-term ship or pay transportation commitments and agree to pay transportation and treating rates that are based on the ultimate cost of the pipeline and treating facilities. The only information known in advance of making these commitments will be a projection based on each project entity's initial estimate of costs.

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For that reason, the parties taking the risks need to be able to manage those risks. The Producers, as shippers, cannot make firm transportation commitments during an open season unless they are confident the gas pipeline project can be built cost effectively and operated on a long-term, commercially viable basis, including being competitive with other sources of gas supply. This is especially true for a project of this magnitude.

The existing prescriptive terms will preclude leaseholders from being able to make a conforming proposal which would deny the state the opportunity to even consider terms from the parties who hold the largest stake in the project's successful development.

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Let me now talk about the importance of alignment between the State and the Producers and the benefits of a Producer project.

Maximizing the value to the State of Alaska and the resource holders means selecting the right design concept for this mega-project and then executing the project to deliver the lowest possible cost.

On a mega-project of this size and magnitude, project construction and operating experience should be a significant consideration. Only a limited number of companies have demonstrated the capabilities and financial strength to effectively participate in and manage world-scale mega-projects.

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CO-CHAIR GATTO inquired whether Mr. Massey believed that ExxonMobil is the only one in Alaska that can do this.

MR. MASSEY noted that ExxonMobil is a large resource owner and also holds the largest discovered gas resource. He said that he thinks the State of Alaska is very fortunate because it is ExxonMobil that will put up the necessary firm transportation commitment (FT) along with the other large stakeholders, "BP and ConocoPhillips". He said that ExxonMobil cannot do the project by itself, that it will take all three companies.

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CO-CHAIR GATTO asked whether ExxonMobil would or could do the project independently.

MR. MASSEY stated that it will take ExxonMobil, BP, ConocoPhillips, and the State of Alaska. "Until we are all aligned on the project it just is not going to happen," he said.

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MR. MASSEY continued with his presentation:

The Producers have mega-project experience on numerous projects world-wide and have demonstrated success in meeting project objectives. For example, ExxonMobil operates in nearly 200 countries and territories and on every continent except Antarctica. We are the

world's largest non-government producer of both oil and natural gas. ExxonMobil's global project development company is unique within industry. This global development company leads the industry in project cost and schedule performance. Nearly 90% of ExxonMobil projects with costs greater than \$1 billion are delivered within 15% of estimated costs at the time of project funding and nearly 80% of those were delivered within 15% of the funding schedule. ExxonMobil's superior performance was independently validated in a report (dated September 21, 2005) published by Sanford C. Bernstein and Co. On the topic of project delays, the report stated "ExxonMobil came out on top of this analysis, with the lowest slippage rates, despite undertaking some of the largest projects. We believe this to be a direct result of its highly competent internal development company, which assumes full responsibility for monitoring a new project from idea to profit." Combining our capability with BP and ConocoPhillips will provide the best chance of delivering a successful project.

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The Producers also have Arctic experience in Alaska and throughout the world. ExxonMobil's arctic experience is extensive - over 40 years - with developments in multiple types of arctic environments. Our Arctic offshore activity started in 1966 with the installation of the ice resistant Granite Point platform in Alaska's Cook Inlet, which is still producing oil. In the 1970's we provided a significant amount of research and engineering for the Prudhoe Bay project, where our completion designs for permafrost were of key importance to the project. We also developed the combined hydraulic flow model and thermal simulator on which the design of TAPS was based. In 1984, we installed the Concrete Island Drilling System (CIDS) to drill exploration wells in the Alaska Beaufort Sea. This was the first mobile drilling platform to operate in the ice covered waters of the Beaufort. In addition to our Arctic experience in Alaska, ExxonMobil also has extensive Arctic experience in Canada, developing the Norman Wells Field in the Mackenzie River area near the Arctic Circle. Offshore Newfoundland, we completed the

Hibernia platform, the first and only iceberg resistant offshore structure in the world. In Russia, we recently started up the Sakhalin 1 development which involved an offshore drilling platform where CIDS was reused and renamed Orlan, an onshore drill site where we have set new industry limits for extended reach drilling, an onshore oil, and gas plant with a capacity of 250,000 barrels per day, and purpose built tankers which are used year-round. All of this work is being done in an arctic and seismically-active area. At Sakhalin we are currently producing 250,000 barrels of oil per day. I hope you see from these examples that large projects with significant complexity are what we do and we are extremely qualified to take on this work.

These successful efforts were the result of a long-term commitment to technology development which has played an important role in the advancement of oil and gas development in Alaska. ExxonMobil believes innovation is the key to meeting the world's energy challenges. Technology is the lifeblood of our industry, and it always has been. We are the leader in our industry in technology development. In 2006, we spent \$730 million on technology development and we have spent more than \$3 billion since 2002.

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In addition, ExxonMobil has demonstrated world-class leadership in safety, health, and environmental performance. ExxonMobil is a leader in operating efficiency and a pacesetter in operating safety. Our total recordable incident rates for employees and contractors are substantially below the average of US Petroleum Industry benchmark of participating American Petroleum Institute companies. We believe a company's commitment to the highest standards of safety, health and environmental care manifests itself in superior performance in all aspects of its operations.

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In addition to our operational excellence, ExxonMobil has the financial strength to make this mega-project a reality. ExxonMobil has consistently maintained one of the strongest financial positions of any company in

the world. We are one of just a few public companies to maintain the highest credit rating from Standard and Poor's (AAA) and Moody's (Aaa), and we have done so for each of the last 88 years. Our unparalleled access to financial resources gives us the flexibility to pursue opportunities worldwide throughout the economic cycle with the knowledge that they can be financed. Host governments recognize this strength and its importance as they look to develop their resources and economies. As an example of that strength, ExxonMobil's project financing experience exceeds \$30 billion in value for recently completed and ongoing activities. Our efficient management of large scale project financings is a critical piece in the overall success of ExxonMobil's project implementation record.

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It is important to remember that the Alaska gas pipeline project is a basin-opening project that will benefit the State and the oil and gas industry in Alaska. Basin-opening projects throughout the world have progressed and been successful when there is alignment between the host government and the leaseholders. The Producers and the State both want a pipeline project to commercialize the known ANS gas resources and open the basin to gas exploration. So, at a very high level we are aligned.

We believe a Producer gas pipeline project will result in maximum value to the State and the Producers. The reason is the Producers and the State have maximum incentive to control costs. Low capital and operating costs, which result in lower treating and transportation costs, and access to premium market price, result in higher netback value on gas. It should be noted that the State will receive the majority of its revenue from the value of gas sales via revenue received under its lease royalty agreements and from production taxes, which are valued based on the netback received from the gas.

Third-party owners do not share the same incentives in that they actually benefit from increased capital costs.

Based on the demand for workers that this project will generate, Alaskans are obviously key to successful project execution. Both the State and the Producers want Alaskans to benefit from the many job opportunities that will exist. When you consider carefully the options available, a Producer pipeline will provide maximum value to the State of Alaska.

We believe that financial strength, experience and the ability to get the job done should be critical components of any evaluation of proposals.

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For us to progress the project and mitigate its inherent risks, we will need some things from the State. Let me discuss the importance of predictable and durable fiscal terms for the upstream participants. Because of the nature and magnitude of the risks associated with this project - tens of billions of dollars of financial commitments, unprecedented cost and scope, potential for construction delays, as well as the inevitable risks associated with the commodity price of gas - fiscal terms that are predictable and durable are necessary. This is a common thread for all of our mega-project investments in basin opening developments. In all such cases, we are willing to take geologic risks, we are willing to take cost risks, and we are willing to take commodity price risks, but we cannot take the risk of fiscal terms changing. Let me expand on this important concept further. The first two risks, geologic and cost risk are risks for which we have developed an industry leading expertise to manage. This is what we do day after day at EM. Market risk is inevitable in a commodity business such as oil and gas and we manage that by attempting to ensure that we deliver those products into the highest value market. Fiscal risk, however, is of a completely different nature and wholly outside of our control. We must have agreements that will allow us to develop this mega-project under predictable and durable terms, so that we can make an adequate investment decision. If fiscal terms can be changed in the future, then we are not able to make a well founded investment decision on behalf of our shareholders.

The Alaska Gas Pipeline Project will require massive investments to be made over a period of many years before any revenue is generated from those investments. As a result, increases in taxes on oil and gas related activities during the life of the project could significantly impact the commercial viability of the project and offset the benefits of taking on a project of this magnitude. Because fiscal terms could be modified under the proposed AGIA legislation, it does not provide the fiscal stability necessary to ensure a commercially viable project.

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CO-CHAIR GATTO inquired whether a legislated 10 year certainty on tax rates is sufficient for ExxonMobil, provided that it is ruled legally permissible.

MR. MASSEY said that his understanding of AGIA is that the proposed 10 years is on the gas production tax. However, he said, there are more forms of "take" within the State of Alaska than just the gas production tax. Locking in one piece of the take while leaving open all the other pieces of take still does not provide any fiscal stability because it can just be changed in another form of the take. There needs to be an agreement between the state and the producers as to how the revenue generated from the project will be shared over the life of the project. Until that is known, ExxonMobil cannot make a good investment decision. Mr. Massey said that he does not know how to run the economics if he does not know what the terms are going to be, and that he will have to assume that they will go up. On a mega-project of \$20-30 billion in magnitude, this is too big of a risk to take, he said.

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CO-CHAIR GATTO requested Mr. Massey to give some examples of other jurisdictions where the certainty that ExxonMobil is asking for - longer than 10 years and maybe the life of the project - already exists.

MR. MASSEY referred Co-Chair Gatto to ExxonMobil's interim fiscal finding that was done for the previous effort. The finding includes an analysis of approximately 50 projects across the world where these types of arrangements have been made. Especially on mega-projects of this magnitude, he stressed, it

is not unusual to see terms much longer than 35 years and none of those projects really compare to this project.

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CO-CHAIR GATTO stated that he has seen the document and reviewed the names of the places where terms of certainty were provided. However, he noted, many of these places are politically unstable so that any [contractual] certainty will only last until the next military coup, in which case the project is jeopardized in its entirety. He requested examples of long-term tax stability agreements in Europe and places that are considered politically stable.

MR. MASSEY responded that whether this project was in the United Kingdom (UK) or Texas, ExxonMobil would still require this same sort of understanding because it is a \$20-\$30 billion mega-project, not one well. Additionally, he remarked, there is no project that is even comparable in the UK.

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CO-CHAIR GATTO commented that there would seem to be a benefit to knowing that the reserves are proven.

MR. MASSEY acknowledged that this obviously helps a lot. However, he argued, the estimated 35 trillion cubic feet (tcf) of discovered resource is not enough. He said that 50 tcf is needed because of the 35-year period of the project. While this is not of too much concern based on the estimates of North Slope gas, finding more gas to keep the pipeline full is still an issue.

1:42:15 PM

REPRESENTATIVE SEATON asked if the concern about the gas production tax exemption, as written on page 21 of CSHB 177(O&G), is that the tax will be increased between the time the license is issued and the open season. He inquired whether ExxonMobil would be more comfortable with fixing the rate at the time of licensing and having this rate continue until 10 years after the open season. Is it this certainty that you want, he asked, or is it a negotiation on rate that you are wanting.

MR. MASSEY acknowledged that the words "lock in the rate" make some people nervous. Whether it is income tax, production tax, or property tax, he said, the rate can change over time as long

as ExxonMobil knows what the rate will be at the start of the project. The rate can be flat, declining, or increasing as long as the agreed-upon rate results in a commercially viable project. He reiterated that he cannot run the economics and make a sound decision today because the rates on all of the taxes can change.

[1:44:56 PM](#)

REPRESENTATIVE SEATON inquired if he is correct in understanding that Mr. Massey's answer means that ExxonMobil's needs would be satisfied if the tax section on page 21 were to provide the certainty of a tax rate that will continue from the time of licensing, the 3 years between licensing and open season, and then for 10 years after the close of the open season.

MR. MASSEY replied that 10 years is inadequate for a project of this magnitude, that the term must be for the life of the project so that ExxonMobil can run the economics. He reiterated that the production tax rate is only one form of take. If this is the model for the system that is to be used, then the take for income, property, and other taxes must also be defined under this model so that he can run the economics.

[1:47:13 PM](#)

REPRESENTATIVE SEATON asked if what Mr. Massey is saying is that ExxonMobil will not participate in building the pipeline as a producer if locking in the tax rates for the life of the project is ruled unconstitutional.

MR. MASSEY offered his opinion that there is little question that the constitutionality issue will ultimately be resolved in court. He pointed out that the Stranded Gas Development Act (SGDA) had a 35-year term in the belief that it was constitutional based upon legal opinions received by two administrations. He said that ExxonMobil's view is that it will be ruled constitutional to agree on what the revenue share is going to be over the term of the project. However, if it is ruled unconstitutional the court can be asked to provide advice in its ruling as to what needs to be done to make it work and adjustments can be made that are based upon the advice.

[1:49:08 PM](#)

REPRESENTATIVE ROSES voiced his concern about going to court over the constitutionality issue because it will cause a

substantial time delay during which nothing moves forward. He suggested that a way around the tax rate issue might be for the state to receive a percentage share in the volume of product instead of charging a tax. He asked whether this could be used as a measurable quantity for determining the financial viability of the project.

MR. MASSEY pointed out that in its contract [under the previously proposed SGDA] ExxonMobil had committed to continue the project up to a certain level of spending even if there was a judicial challenge, although he could not recall the amount. He stressed that ExxonMobil was ready to risk a significant sum of money while that judicial challenge was going on because of its belief that the tax rate would be ruled constitutional. He said that in his view, Representative Roses is right in terms of a way to share the risk because if the state takes its revenue in a share of the gas, then that eliminates a lot of the other issues.

[1:52:01 PM](#)

REPRESENTATIVE GUTTENBERG asked whether ExxonMobil would withdraw from the contract should the 10 year production tax exemption be found unconstitutional.

MR. MASSEY replied that if the courts decide that the tax structure of AGIA is not constitutional, ExxonMobil would have to re-visit the issue to determine if it would be possible to craft a constitutional tax provision. "We would not be able to go forward until we understand what the deal is," he said.

[1:53:28 PM](#)

REPRESENTATIVE GUTTENBERG asked if these were conditions that ExxonMobil would like built into the contract.

MR. MASSEY answered yes.

[1:53:39 PM](#)

REPRESENTATIVE GUTTENBERG asked what would happen if the state was unable to provide a level of fiscal certainty satisfactory to ExxonMobil.

MR. MASSEY responded that he believes the court would provide guidance as to how to make it constitutional. He reiterated

that he believes the tax exemption provision is constitutional and that ExxonMobil will be ready to spend funds and go forward during any constitutional challenge.

[1:54:12 PM](#)

CO-CHAIR GATTO read, in response to a prior comment, the names of countries, and noted that he did not see any European countries on the list. He opined that no countries on the list were equivalent to a United States or Alaskan operation.

[1:55:13 PM](#)

REPRESENTATIVE ROSES requested further detail on the need for fiscal certainty, noting that in business lenders may require that a lease exceed the life of a loan.

MR. MASSEY responded that lenders will closely examine any deal, but noted that in a "deal of this magnitude" lenders will require the full backing of ExxonMobil, whether the gas flows or not. He opined that a consideration should be whether the company has the financial strength to provide that backing.

[1:57:21 PM](#)

REPRESENTATIVE ROSES asked whether there had been any prior discussion of an equity split based on the volume of the gas.

MR. MASSEY replied that is "exactly what we did for the majority of the take." The prior approach had the state take and be responsible for its share of the royalty and tax gas. The state would then receive the benefits from the sale of that gas, he explained.

[1:58:07 PM](#)

CO-CHAIR GATTO asked if "you inked your name on that agreement."

MR. MASSEY answered that ExxonMobil had been ready to do so.

[1:58:15 PM](#)

CO-CHAIR GATTO put forth for consideration:

If we looked today at the value of the gas, almost \$8 and the tax at 22 and one-half percent, and the royalty, and figured out that that equaled 25

percent of the value of the gas and said tell you what -- Why don't we become a one-quarter, three quarter partner. That's as simple a contract as anyone could come up with. It would end taxes, it would end all the uncertainty except for the price, but then we would all suffer equally or be blessed equally.

He asked whether the aforementioned scenario was something ExxonMobil would consider.

MR. MASSEY said "where do we sign?" He went on to say that the actual percentage share in any partnership arrangement would need to be considered. He opined that the aforementioned concept is one that would allow the state and ExxonMobil to work together to minimize the risk associated with the project.

[1:59:35 PM](#)

REPRESENTATIVE ROSES clarified that he does not support the state owning a part of the pipeline. Instead, he suggested that it might be possible to establish fiscal certainty downstream if the state took its share of the gas in-kind. He did not suggest that the state share the expense of building the pipeline.

[2:00:22 PM](#)

CO-CHAIR GATTO commented that the tariff is an extremely important part of the value of the gas. He opined that the state may want to own a piece of the pipeline. He offered his belief that the tariff provides consistent income, whereas the income from the gas varies depending on the price of gas.

[2:01:15 PM](#)

MR. MASSEY responded to a question about the \$500 million state contribution proposed in AGIA by stating that he approves of the amendments made to allow individual applicants to propose how they would propose to use the \$500 million. He described that change as consistent with his belief that AGIA should be made less prescriptive so that the applicants have more leeway to describe how they propose to address different aspects of commercial viability. He said that the \$500 million "is not a big deal" to ExxonMobil and offered that if the state is going to put money into the project, it should be a participant. He advocated that joint ownership may align the partners to execute the project.

2:04:54 PM

MR. MASSEY continued with his presentation:

Development of a predictable and durable fiscal framework means that the terms agreed between the Producers and the State recognize the magnitude and risks associated with the project; balance State and Producer needs; and provide for the calculation of total State take in a transparent and predictable manner.

2:05:42 PM

AGIA should allow market participants to put forward their best proposal on what is required to make the project viable, thereby creating a competitive process that will allow the State the opportunity to consider those proposals that have the best chance of actually delivering on the promise of an Alaska gas pipeline.

I would like to now give some specific feedback on AGIA which is based on the conclusions and principles I've mentioned. I will also outline some additional thoughts on how AGIA should be modified to provide the best chance of a successful result. For example, alignment between the State and the leaseholders is essential to a basin opening project of this magnitude. Therefore, establishing the right approach going forward is the most important activity for the project at this time. It is important that AGIA bring together the upstream and the midstream and provide for an integrated proposal. Let me expand on this point. The upstream and midstream at some point in time will have to come together. The reason is simple - the upstream pays for the midstream. When I say upstream I mean the revenue generated from sale of the gas and liquids from the pipeline project. To be able to calculate the revenue from the upstream we must have clarity on the taxes and royalty from our oil and gas operations and the taxes and royalties must be set at a level that makes the project viable. In order to ensure a viable project from the outset, we believe this must be done at the beginning. At a minimum, any proposal should demonstrate how a successful open season would be achieved.

2:06:58 PM

As I discussed previously, with regard to upstream terms, the proposed upstream inducements would require significant modification to ensure a commercially viable project is obtained. It would be better to leave that issue open for now and allow an applicant to make a proposal to address those terms.

AGIA also prescribes activities that must be completed within a specific timeframe or date certain. Setting arbitrary target dates is not consistent with good project management practices. Further, milestones are not necessary if the project is commercially viable. The Producers' builder will progress the project at the maximum prudent pace, consistent with the industry proven "gate" process for project development.

2:07:39 PM

In general, AGIA lacks specifics on key fiscal terms and other requirements. To address these gaps, AGIA gives commissioners broad authority to adopt additional requirements and establish regulations. Not knowing the requirements now creates significant uncertainty.

Finally, because of the complexity and risk associated with this project, the parties must have an efficient and impartial means of handling disagreements when they arise. We believe project related agreements should provide for binding neutral arbitration as the mechanism for resolving disputes. Binding neutral arbitration is widely utilized in U.S. and international commercial agreements and is not a new concept with the State of Alaska. Arbitration is the method used to resolve disputes under the State's Royalty Settlement Agreements. In addition, Alaska courts have recognized a strong public policy in favor of arbitration.

2:08:34 PM

CO-CHAIR GATTO said that in his experience, arbitration can be a slow process. He asked whether binding arbitration would apply to project labor agreements.

MR. MASSEY replied that ExxonMobil proposes that binding neutral arbitration apply to the relationship between the producers and the state. In response to a question, he agreed that the arbitration proposed by ExxonMobil would follow commonly accepted procedures whereby each side picks an arbitrator, and the two arbitrators pick a third arbitrator.

[2:09:23 PM](#)

REPRESENTATIVE GUTTENBERG asked if the producers use binding arbitration for disputes between themselves.

MR. MASSEY replied that the "our agreements govern how we make decisions," such as voting. He said the producers have not had a dispute which has required legal or other proceedings. He put forth that the parties have agreed that they need to work towards arbitration should there be a major disagreement among themselves. He responded to a question by stating that in the past 30 years, the producers have been able to work out disputes.

[2:10:28 PM](#)

CO-CHAIR GATTO asked what type of arbitration was in existence at the time of the Exxon Valdez tanker incident [1989].

MR. MASSEY opined the issues there were handled through the courts.

CO-CHAIR GATTO noted that the aforementioned litigation has "taken a lifetime," and opined that binding arbitration may be a much quicker dispute resolution procedure.

MR. MASSEY agreed that binding arbitration is a more efficient process for handling disputes.

[2:11:23 PM](#)

MR. MASSEY continued with his presentation:

We also note that the House Oil & Gas Committee and the Senate Resources Committee made a number of amendments to AGIA. While substantial work needs to be done to make AGIA truly objective, several of the proposed changes moved in the right direction,

including making the state's entire capital contribution a bid variable, beefing up evaluation criteria, recognizing the need to include terms in a contract and requiring legislative approval of any license award. Unfortunately, steps were also taken that will likely limit the number of potential bidders by eliminating any confidentiality protection for a licensee's proprietary and trade secret data and imposing new prescriptive terms such as requiring any bidder to forego its legal rights to challenge an improper award. What we have at this stage is an AGIA bill that remains too prescriptive to solicit the quality market based bids necessary to move the project forward.

[2:12:28 PM](#)

In closing, I would like to reiterate that ExxonMobil is committed to moving the gas pipeline project forward. Our company possesses the financial strength and project experience required to make this project a success. We are ready to work with the Administration and the Legislature to establish a framework that recognizes the integrated nature of the project and mitigates the risks I've discussed to allow the project to progress. We would suggest AGIA be amended to include a broad objective driven framework that sets out what the State wants to achieve. AGIA should allow each applicant to propose how best to meet those objectives and to identify what is required from the State to advance the project. This process will secure more viable applications, create more competition and afford the State the opportunity to secure the most value. We are ready to participate in a competitive, open, and transparent process under the approach I've outlined.

Thank you for your attention and for the opportunity to address this important topic today. I look forward to addressing your questions.

[2:13:34 PM](#)

REPRESENTATIVE ROSES asked for more clarification of the "objective driven" concepts referred to above, noting that many issues discussed appeared to be objective. He asked whether

compliance with Regulatory Commission of Alaska (RCA) requirements is an objective issue.

MR. MASSEY replied that ExxonMobil believes the project will be regulated by FERC and RCA will not have a role.

[2:14:28 PM](#)

REPRESENTATIVE ROSES asked whether "access to market capacity" is an issue in terms of the desire for an "objective driven document."

MR. MASSEY suggested that the applicant should be allowed to decide how it will assess market capacity. He suggested that the applicant may be able to come up with an approach preferable to a mandated biennial review of market issues.

[2:15:47 PM](#)

CO-CHAIR GATTO asked whether ExxonMobil would object to review of market factors such as cost and demand every two years to possibly make adjustments so that as much gas can be produced as is reasonable under the circumstances.

MR. MASSEY responded that pipelines are expanded frequently, and that pipeline companies work with suppliers and shippers regarding expansion mechanics and funding. He reminded the committee that FERC oversight applies in these situations, and that any parties can go to FERC. He opined that the issue of expansion should be left to the applicant to provide in its proposal. The state could then review that aspect of the proposal just like other terms.

[2:18:48 PM](#)

REPRESENTATIVE SEATON said he is trying to ascertain the answer -- Is ExxonMobil willing to have an assessment every two years of whether there are other parties who want to ship gas down the pipeline?

MR. MASSEY asked that his comment not be misinterpreted. His suggestion is that the applicant be allowed to make its proposal in this area. He noted that an applicant may propose that market factors are reviewed far more frequently than every two years.

REPRESENTATIVE SEATON noted that currently AGIA proposes a review "at least" every two years" [AS 43.90.130(5)].

[2:20:14 PM](#)

REPRESENTATIVE ROSES reiterated his desire to determine which application factors are objective driven and which are not. He offered his belief that a requirement for review every two years is objective driven, regardless of whether two years is the appropriate number or not.

MR. MASSEY replied that the objective for the state is to ensure that the pipeline could be expanded. It should be left to the applicants to describe the process they propose to ensure expansion, he suggested.

[2:21:37 PM](#)

REPRESENTATIVE ROSES noted that requirement number six [AS 43.90.130(6)] requires the applicant to commit to expand the proposed project in reasonable engineering increments with commercially reasonable terms. He asked whether it is in the best interests of the pipeline owner to always build in an expansion capability, therefore that term does not need to be legislated.

MR. MASSEY stated he believes that the aforementioned characterization is correct.

[2:22:29 PM](#)

REPRESENTATIVE ROSES asked whether the witness considered the terms [regarding pipeline expansion] to be objective driven.

MR. MASSEY replied no.

[2:22:3 PM](#)

REPRESENTATIVE ROSES asked about AS 43.90.130(7) which requires an applicant to commit to "propose and support recovery of mainline capacity expansion costs," which he characterized as limiting the roll-in costs to not exceed 15 percent "above the initial maximum recourse rates from the North Slope to the project's downstream terminus ..." He asked whether the witness considered this "an objective driven statement."

MR. MASSEY replied that he does not.

2:23:04 PM

REPRESENTATIVE ROSES asked whether this requirement could be re-structured to be "objective driven."

MR. MASSEY responded that obviously it is very important for the state to understand how each applicant would propose to deal with pipeline expansion. However, he stated his confidence that the business community "knows how to do these things." He said that given the state's interest in this area, every applicant should be required to describe in detail how it proposes to treat issues related to future expansion.

2:24:34 PM

REPRESENTATIVE GUTTENBERG asked whether it is a reasonable choice for the state to require applicants to describe their plans for future expansion and exploration.

MR. MASSEY said he did not intend to imply that the state's interest in this area was unreasonable. However he reiterated his preference that the applicant be allowed to describe its approach to future expansion and exploration. He went on to opine that under the Alaska Natural Gas Pipeline Act ("ANGPA"), the United States Congress struck what it determined was the proper balance between encouraging initial investment and encouraging exploration and future expansion. He emphasized that basin opening projects require alignment between the state and the producers. He opined it most likely that the producers will build the project because that approach will provide maximum benefit to the state. He said that Congress gave FERC unprecedented abilities to mandate a FERC-mandated expansion to benefit explorers. Therefore, to some extent this issue has been dealt with and delegated to the right agency, he opined.

2:2707 PM

CO-CHAIR GATTO noted that exploration for gas may allow for the discovery of additional oil resources, which would benefit the state. He sought clarification as to whether FERC mandates future expansion, or whether it is simply the decision maker in this area.

MR. MASSEY replied that "you will not have any trouble" attracting additional explorers once the gas pipeline is in operation, and indicated ExxonMobil would "be a part of that

effort." He emphasized that under federal law, FERC has the unprecedented right to "mandate an expansion to benefit explorers."

[2:28:34 PM](#)

REPRESENTATIVE GUTTENBERG asked whether ExxonMobil was currently in litigation with FERC regarding provisions which would mandate design changes to meet open seasons.

MR. MASSEY reminded the committee that ANCPA was effective in 2004. The issue of FERC's ability to mandate a design change after the pipeline builder has planned and invested substantial sums is currently in litigation, he explained. He said ExxonMobil has no problem with FERC mandated expansion, but would like some clarity on the design change issue.

[2:30:58 PM](#)

REPRESENTATIVE WILSON asked for clarification as to why ExxonMobil objects to the inclusion of items in the application that the witness has indicated will be covered by the applicants, such as the commitment to expand the pipeline.

MR. MASSEY suggested that applicants be allowed to propose how they intend to deal with expansion rather than describing it in legislation. He indicated that some items should be in legislation, but others should be left to the applicant to propose. He suggested that the state simply describe its requirement that explorers need access to the pipeline, and let the applicants propose how they would meet that requirement.

REPRESENTATIVE WILSON expressed some uncertainty regarding the aforementioned answer.

[2:33:22 PM](#)

REPRESENTATIVE ROSES sought to clarify matters by summarizing the witness' point as stating it would be in the state's best interest if AGIA was not as prescriptive regarding issues of expansion, but rather allowed the applicants more flexibility to describe their plans for pipeline expansion.

MR. MASSEY agreed with the aforementioned summarization.

[2:35:06 PM](#)

REPRESENTATIVE WILSON noted her question concerned the requirements in proposed AS 43.90.130(5) and (6).

[2:35:18 PM](#)

REPRESENTATIVE ROSES referred to AS 43.90.130(7) and asked whether requirements regarding the limitation of expansion costs to no more than 15 percent above the initial maximum recourse rates is an encumbrance to applicants.

MR. MASSEY replied yes. The issue of how potential future shippers may access initial capacity and future expansion capacity should be administered by FERC for all elements of the project in the United States. He offered his belief that shippers, being the producers, should not be required to subsidize other expansion gas-holders at 115 percent of initial maximum rates. He described this as potentially costing the initial shippers an additional \$500 to \$800 million a year. He characterized this as a subsidy to the expansion shipper, and claimed that ExxonMobil "is not in the business of subsidizing our creditors." He suggested that the applicants be allowed to suggest what is necessary to achieve an acceptable expansion.

[2:37:16 PM](#)

CO-CHAIR GATTO referenced the possibility that ExxonMobil could be the primary beneficiary of a rolled-in rate in some situations. Additionally, rolled-in rates initially "drop everybody's rates," he said. He asked whether it was to ExxonMobil's advantage to incorporate "these rules that say rolled-in rates are really good things."

MR. MASSEY replied that ExxonMobil proposes removing any sort of mandates regarding expansion costs and suggested that the businesses resolve these issues at the time. He characterized incremental rates as rolled-in rates. He cautioned that mandates could harm the future economic benefits to the parties. He emphasized that the parties should be allowed to come to a business arrangement, and that one party not have more leverage than another. He offered that FERC would be able to resolve disputes should the parties not come to an agreement.

The committee took an at ease from [2:40:55 PM](#) to [2:49:48 PM](#).

[2:50:25 PM](#)

REPRESENTATIVE SEATON questioned how the state's setting forth minimum requirements regarding certain aspects of the pipeline constrains applicants from putting forth a better offer to be evaluated by the state under the six different criteria in AGIA.

MR. MASSEY responded that what ExxonMobil is proposing that AGIA be amended to remove prescriptive provisions, and to instead describe the state's broad objectives. The applicants will then propose how they will meet the broad objectives.

REPRESENTATIVE SEATON noted that the state may have certain minimum requirements, and suggested it is important to set forth minimum requirements so applicants have some notice and clarity regarding what must be addressed.

[2:54:30 PM](#)

MR. MASSEY said that the "must-haves" set forth in AGIA give potential applicants an indication of what the state would like addressed. He opined that it is difficult to discuss these requirements in isolation, but offered that a preferable approach would allow more flexibility as applicants may want to propose terms more beneficial in one area, but will be penalized or rejected if they do not meet the requirements in another area. An overly prescriptive approach may foreclose the state from considering options that actually have more value to the state, he opined. He offered that AGIA has provided helpful information to potential applicants regarding the state's objectives, but that a more flexible approach will allow the state to receive maximum benefits.

[2:56:18 PM](#)

REPRESENTATIVE SEATON noted that applicants could propose more generous terms. He asked whether the state should make clear that there may be certain minimum requirements, such as a review of market capacity and queried as to whether the applicants would like knowledge of those minimums.

MR. MASSEY noted that it can be difficult to assess hypothetical situations, but agreed that they offer some guidance for purpose of discussion. He offered that they can be used to describe the difficulties of a prescriptive approach.

[2:57:42 PM](#)

CO-CHAIR GATTO reminded members that AGIA is currently just a proposal, and the stakeholders may have the ability to influence its final provisions.

MR. MASSEY responded that if the administration was willing to seriously consider and discuss what is necessary to go forward, ExxonMobil would be willing to do so. He stated that as of now the administration has set forth a particular process that requires amendments before ExxonMobil could make a conforming bid. He said that as currently written AGIA does not result in a commercially viable project, therefore ExxonMobil could not make a conforming bid.

[2:59:10 PM](#)

CO-CHAIR GATTO opined that committee members are interested in determining possible necessary amendments. He suggested that ExxonMobil has the ability to put forth suggestions to the administration.

MR. MASSEY replied that if the administration was willing to consider a proposal, ExxonMobil would provide one. However, he said that it "is not the approach they have taken."

[3:00:45 PM](#)

REPRESENTATIVE ROSES asked about whether AS 43.90.130(8) regarding a North Slope gas treatment plant (GTP) sets forth an objective driven criteria.

MR. MASSEY replied that a gas treatment plant has to be dealt with and should be part of an applicant's proposal. He suggested that provisions regarding valuation of existing facilities should be left to the applicant to describe. He responded to further inquiry by indicating that although the GTP could be considered an integral part of the project, he has concerns about the provisions establishing the rate and net book value of the GTP.

[3:02:39 PM](#)

REPRESENTATIVE ROSES asked about possible changes to this part of AGIA.

MR. MASSEY replied the applicant should be allowed to describe how it intends to roll-in assets to determine net book value of the GTP.

3:03:30 PM

REPRESENTATIVE ROSES asked whether AS 43.90.130(9) regarding the percentage and dollar amount that will define the level of the state's contribution is an objective driven criteria.

MR. MASSEY responded that the state contribution provision should be left entirely up to the applicant to propose, noting that the applicant may not even want a contribution, or may like to see some state ownership.

CO-CHAIR GATTO asked if amending the language to read "the applicant shall determine the extent to which the state may contribute a percentage of the project cost" would be preferable.

MR. MASSEY responded that such a change would be reasonable.

3:05:06 PM

REPRESENTATIVE ROSES asked whether AS 43.90.130(10) regarding rates for the project and the GTP is an objective driven criteria.

MR. MASSEY replied that the applicant should propose how it proposes to structure the tariff, but he expressed disagreement with AGIA's mandate of not less than 70 percent debt. He said that the applicant should be able to determine how it wants to propose the rate structure. He indicated he understands that as proposed the capital structure must be "not less than 70 percent debt," but suggested that although an applicant could "not do it unless it is 60, but they give you something else that you value, therefore you ... would want to hear that."

3:06:12 PM

CO-CHAIR GATTO suggested that the administration put that provision in to help control the cost of the pipeline and to keep the tariff at a rate where everyone is "making good money." He suggested that the 70 to 30 ratio is designed to meet that goal, and that the administration may be unwilling to alter this proportion. He asked whether the witness would characterize this requirement as a "deal killer."

MR. MASSEY responded that in its last proposal, ExxonMobil hoped to achieve an 80 percent debt ratio. He reiterated that

applicants should have flexibility to determine how they propose to meet the state's objectives. He suggested that by picking 70 percent, the state may miss an opportunity to "get something that works better for you."

[3:07:38 PM](#)

CO-CHAIR GATTO referred to a chart and offered that the three North Slope producers have a higher rate of return in activities that do not involve pipeline construction. Based on this history, he asked why the producers would want to hold more than 30 percent of a pipeline as it may reduce their rate of return.

MR. MASSEY responded that ExxonMobil would like to own the percent of the project that matches its percent of the throughput so that "the amount of gas we have going through equals the amount of pipe." He went on to say that in a basin opening project, the resource owner and the lease holders must be aligned before the project goes forward. He said that worldwide, the lease holders take the lead in basin opening projects because the leaseholder is the main beneficiary.

[3:10:20 PM](#)

REPRESENTATIVE ROSES asked whether AS 43.90.130(11) regarding the management of cost overruns is an objective driven criteria.

MR. MASSEY responded yes.

[3:10:38 PM](#)

REPRESENTATIVE ROSES asked whether AS 43.90.130(12) requiring a minimum of five delivery points is an objective driven criteria.

MR. MASSEY suggested the applicant be allowed to propose how it plans to propose access to the pipeline for in-state deliveries.

CO-CHAIR GATTO suggested that this requirement is a political problem, not a monetary problem, as state residents desire natural gas for in-state delivery.

MR. MASSEY reiterated that this requirement should be left to the applicant to describe how it intends to handle in-state gas access.

[3:12:24 PM](#)

REPRESENTATIVE ROSES suggested it is important for the state to specify some minimums to avoid costly change orders.

MR. MASSEY said that off-take points do not cost a lot of money, but if the state absolutely has to have five, it should so state.

[3:14:17 PM](#)

REPRESENTATIVE ROSES asked for the witness' opinion as to AS 43.90.130(13) regarding in-state transportation services.

MR. MASSEY opined that how to manage in-state transportation services should be part of the applicant's proposal.

[3:14:42 PM](#)

REPRESENTATIVE ROSES asked about AS 43.90.130(14) regarding local headquarters.

MR. MASSEY replied that the applicant should be allowed to explain how it will manage the project, and opined that obviously there will be Alaska offices to manage the project.

[3:15:16 PM](#)

REPRESENTATIVE ROSES asked whether AS 43.90.130(15) regarding local hire would be considered an objective driven criteria.

MR. MASSEY suggested that the state should propose a broad objective to allow an applicant to explain how it intends to use Alaskans on the pipeline project. He suggested that state would like to see more than a commitment to local hire, and would benefit from a fuller explanation of employment issues.

[3:16:26 PM](#)

REPRESENTATIVE ROSES asked whether there was concern over the possibility that AS 43.90.130(15) could limit the applicant's ability to hire workers if it could not find in-state workers at a reasonable cost.

MR. MASSEY replied that obviously the project is going to have to be cost competitive. Furthermore, employees must be qualified to meet the needs of the project. He noted that this project will provide excellent opportunities for Alaskans, and

that the language should be broadened so that the applicant provides more details as to how it intends to hire Alaskans.

REPRESENTATIVE ROSES summarized that the witness is suggesting the applicants be required to provide a general statement regarding local hire qualifications and implementation.

MR. MASSEY agreed with the aforementioned summarization.

[3:19:42 PM](#)

REPRESENTATIVE ROSES asked about AS 43.90.130(16) regarding the waiver of the right to appeal.

[3:19:55 PM](#)

MR. MASSEY said that section 16 removes an applicant's ability to challenge whether the award was done correctly. He opined that would limit the number of applicants rather than open the process up to great competition.

CO-CHAIR GATTO asked whether the limitation on the ability to appeal would keep ExxonMobil from submitting an application.

[3:20:53 PM](#)

MR. MASSEY replied that ExxonMobil will consider the total AGIA bill once it is "all put together" to determine how to proceed. For this particular item, he indicated he would prefer it not be in the bill. He went on to say that ExxonMobil will likely be able to put a competitive bid forward, and is supportive of the competitive process. He offered his opinion that AGIA in its current form "does not deliver a commercially viable project, so I can't play today the way it is written."

[3:21:34 PM](#)

REPRESENTATIVE ROSES stated that if the open season was held first, the state would know how much gas the producers would be willing to commit to the project so that the pipeline could be sized to the project. He expressed concern that if the appeal process was closed out, the state would lose the ability to go back and review applications should the pipeline have to be re-designed depending on the result of open season. He also noted that there is a benefit to the winner to not have its bid challenged.

[3:24:43 PM](#)

MR. MASSEY responded to a question by explaining that as he understands the appeal provision, there is no administrative appeal available to an aggrieved applicant since the commissioners are making the decision. As a result, an applicant would have to appeal to the court system, he opined. He went on to explain that one appeals a decision to the person above the decision maker so that person can review the decision and review new information.

REPRESENTATIVE SEATON referenced the delay of litigation and asked whether there was any benefit to constraining the ability of an applicant to go to court to protest the bid award.

MR. MASSEY replied that he "would make that available," noting that an applicant could continue with the project during litigation and could describe how it intends to proceed in such a situation.

[3:28:56 PM](#)

REPRESENTATIVE SEATON noted that under AGIA a single license will be issued and asked whether the licensee would proceed despite a possible restraining order limiting the ability to proceed with the project.

MR. MASSEY reminded the committee that "we're talking hypotheticals," and that a restraining order would be a problem.

[3:30:23 PM](#)

REPRESENTATIVE ROSES asked about AS 43.90.130 (17) requiring an applicant to commit to a project labor agreement.

MR. MASSEY said the applicant should be required to describe how it intends to require labor for the pipeline and described a requirement for a project labor agreement as too specific and premature.

CO-CHAIR GATTO referenced the costly nature of a strike. He asked about the significance of the labor costs for a project like this.

MR. MASSEY responded that labor will be a big part, but he cannot recall the actual amount of predicted labor costs. He

suggested that the labor environment could be flexible and include union and non-union labor.

CO-CHAIR GATTO opined that project labor agreements are valuable to avoid delays due to labor issues.

[3:33:56 PM](#)

REPRESENTATIVE ROSES asked whether AS 43.90.130(18) requiring exclusion of the state's contribution from an applicant's rate base is an objective driven criteria.

MR. MASSEY replied that in his opinion it is not, and expanded by stating that the applicant should be allowed to describe how it would characterize any state contribution amounts.

[3:34:40 PM](#)

REPRESENTATIVE SEATON relayed that a major goal is to keep the tariff low, and that section 18 provides that any state contribution amount will not be considered in raising the tariff. He characterized the witness's position as potentially allowing the state's contribution amount to be considered in the tariff calculation, therefore potentially raising the tariffs, and violating one of the state's main objectives - low tariff rates.

MR. MASSEY replied that an applicant may actually propose that the state's \$500 million contribution be rolled into the rate base. Another applicant may propose a lower tariff without having taken any state contribution amount, or suggest some other arrangement that would still result in a lower tariff rate. He suggested that if the objective is to get the lowest tariff, the state should allow the applicant to propose how it intends to structure the tariff.

[3:36:43 PM](#)

REPRESENTATIVE SEATON noted that the aforementioned possibility is in the evaluation criteria, and asked whether consideration of this issue is objectionable as part of the evaluation.

MR. MASSEY indicated that it is not objectionable.

REPRESENTATIVE ROSES characterized AS 43.90.130(19) regarding applicant information as requesting fairly specific criteria.

MR. MASSEY agreed with the above characterization.

3:37:30 PM

REPRESENTATIVE ROSES characterized AS 43.90.130(20) regarding the applicant's readiness and ability as requesting fairly specific criteria.

MR. MASSEY agreed section 20 was objective.

3:38:01 PM

REPRESENTATIVE SEATON referred to page 6 of HB 177 and asked whether the original pipe size should be included in the application.

3:39:24 PM

MR. MASSEY reiterated that ExxonMobil position is that the requirements set forth in AGIA would be set forth in the applicant's proposal. He did note that Representative Seaton's query put the interpretation of AS 43.90.130(6)(B) somewhat at issue, as it could be interpreted to mean one would have to build a "whole new pipe."

REPRESENTATIVE SEATON indicated agreement with the aforementioned interpretation.

CO-CHAIR GATTO noted that section (6)(B) uses the word "or", allowing for compression or new construction to accommodate additional capacity.

3:40:30 PM

REPRESENTATIVE SEATON asked whether the 15 percent cap on rolled-in rates was really a substantial issue since it applies to initial maximum recourse rates not adjusted for inflation. He noted that initial expansion would likely be through compression, and that it would only be later that expansion would be through looping. Based on those assumptions, he queried as to the significance of the 15 percent limitation.

3:41:18 PM

MR. MASSEY responded that 15 percent is huge and is too big of a risk to take at any time.

REPRESENTATIVE SEATON sought confirmation that the witness also meant 15 percent of the original rate structure.

MR. MASSEY replied "at any time."

[3:41:37 PM](#)

REPRESENTATIVE SEATON asked whether there is a rate increase limitation figure which his company would not object to.

MR. MASSEY answered that ExxonMobil would prefer that the applicant be allowed to propose how it would deal with expansion, rolled-in rates, and incremental rates. He said he understands what the state has suggested, and opined that if ExxonMobil wants to win the bid it will need to deal with the issue in a very positive way for the state.

[3:42:31 PM](#)

CO-CHAIR GATTO asked whether it would be fair to establish a tariff whereby ExxonMobil would not receive the benefits of lowered rates, yet would also not bear the cost of increased rates.

MR. MASSEY said he has not really considered this and is not able to answer that question at this time. He did say that the items reviewed with Representative Roses were the "pipeline side" which he characterized as the easy part of this project. However, it is the upstream side which will determine whether the project is commercially viable. He emphasized that the applicants should be allowed to propose the upstream terms required to make the project viable.

[3:44:11 PM](#)

REPRESENTATIVE GUTTENBERG asked whether ExxonMobil has the ability to put forward to FERC a pipeline project plan regardless of AGIA.

MR. MASSEY responded that if ExxonMobil thought the project was commercially viable under the current terms, it could go to FERC and apply for a certificate. However, he opined that with respect to the upstream portions, the project at present is not commercially viable. He stated that uncertainty over future terms does not allow ExxonMobil to determine whether the project is viable over the long-term. In response to further questioning, he relayed that a determination of commercial

viability regarding a project of this size is not so much a matter of trust as of "understanding what the deal is." This requires a determination of the terms between the state and the pipeline developer, he explained. He agreed that the state and the producers have a long history, but reiterated that for this "mega-project" the terms and conditions must be fully understood. He opined that worldwide, projects that go forward are those where the resource owner and the developer have come to an arrangement regarding how the revenue will be shared. The project will not progress until that point is reached, he concluded.

REPRESENTATIVE GUTTENBERG noted that Alaska provides a stable political environment and it is looking for an open competitive process. He implied that the state's position may not be in alignment with that of ExxonMobil's.

[3:49:34 PM](#)

REPRESENTATIVE SEATON characterized AGIA as a "mid-stream" proposal, while the witness was referring to upstream issues which are of interest only to the producers. He suggested that the witness was referring to a closed process with the producers receiving upstream concessions to make the project viable. He opined that "we tried that route and it didn't work." However, the approach of AGIA is to focus on a competitive process to develop a pipeline. He asked whether the producers would sell their gas regardless of ownership in the pipeline.

[3:51:19 PM](#)

MR. MASSEY again emphasized that the upstream pays for the "cost of the pipe" he said. He expressed his opinion that in a basin opening project, the gas will pay for the infrastructure. Therefore, there will not be a project until the upstream terms are dealt with to the satisfaction of the producers. He suggested that the upstream applicants be allowed to propose their needs for the project to proceed. He once again emphasized that in his opinion AGIA as proposed does not make a commercially viable project, therefore his company cannot make a conforming bid. He reminded the committee the state can accept ExxonMobil's terms, reject them, or enter negotiations. He opined it is difficult to do this through legislation.

[3:53:22 PM](#)

CO-CHAIR JOHNSON asked whether ExxonMobil would bid on the project if AGIA were to pass today.

MR. MASSEY answered that the way AGIA is written today, the project is not viable, so ExxonMobil cannot make a bid.

CO-CHAIR JOHNSON asked about the process of examining AGIA to develop a bid.

MR. MASSEY said ExxonMobil is going to try to win the bid, and the items set forth in AGIA give a good indication of what the state wants in the project. He explained that ExxonMobil would look at the state's objectives, and could come up with something more favorable to the state than is proposed in AGIA.

[3:55:23 PM](#)

CO-CHAIR GATTO indicated that the above comment is why the state has proposed that applicants not be allowed to appeal the award.

MR. MASSEY responded that appeal concerns are a reason to not put so many prescriptive criteria in AGIA, but to instead put forth broad objectives. He suggested this broad approach would make it less likely for an unsuccessful applicant to appeal.

CO-CHAIR GATTO opined there will likely be an appeal.

MR. MASSEY agreed, and pointed out that he believes that AGIA as written does not set forth a competitive process. He said that ExxonMobil, despite being a major player on the North Slope, "can't play." He suggested that the legislature should consider whether it wants ExxonMobil to participate. He clarified that the state owns the resource, but ExxonMobil is a lease holder.

[3:57:18 PM](#)

REPRESENTATIVE ROSES asked whether ExxonMobil has participated in competitive requests for proposals (RFPs).

MR. MASSEY explained that normally RFPs are done when one is trying to access land or a resource. He noted that here Alaska already has much of the gas leased, which makes RFP in this situation more complicated. He opined that once the land is leased, the resource owner needs to work with the lessee to make the project go forward.

[3:59:18 PM](#)

REPRESENTATIVE ROSES summarized that typically RFPs include lease negotiations. However, since in this instance the leases have already been issued, the applicants have nothing to trade off except the value of the product and would therefore prefer a more flexible process.

MR. MASSEY characterized the aforementioned summary as fair.

[4:00:22 PM](#)

REPRESENTATIVE SEATON asked about the effect on the tariff should ExxonMobil be required to purchase carbon dioxide emissions credits.

MR. MASSEY said that issue has not yet been considered.

REPRESENTATIVE SEATON asked about the possible effect of federal law regarding carbon dioxide emissions and the possible effect on tariffs should a portion of the carbon dioxide be able to be monetized by the pipeline operator.

MR. MASSEY replied that the policy should be that the pipeline owner receives a fair return on its investment. If they are able to lower their expenses, it should carry through to the tariff, he said.

REPRESENTATIVE SEATON opined that this is a significant issue as there may be federal legislation to pre-allow certain carbon dioxide emissions and that this may be a significant factor.

MR. MASSEY answered he has not looked at this issue yet.

[4:03:59 PM](#)

MR. MASSEY responded to a question regarding possible negotiations with the administration by explaining that he would like total flexibility in that regard and is not wedded to any prior agreement. He suggested that the parties could first agree on common objectives, then could consider how to assign responsibility to accomplish those objectives.

[4:05:28 PM](#)

CO-CHAIR JOHNSON asked about how more fiscal certainty regarding taxation would affect the likelihood that ExxonMobil would participate in the process.

MR. MASSEY stated that "we're going to have to deal with predictable and durable fiscal terms" for all aspects of the project. He said he "does not know how we can deal with that in a piece of legislation," noting that prior negotiations resulted in a 400 page document. Due to the difficulty of establishing fiscal certainty, he suggested that the better approach is to allow the applicants to describe what they need. The state can then determine whether it wants to accept the proposals.

[4:07:24 PM](#)

REPRESENTATIVE ROSES observed that "you've made it ... abundantly clear that as this bill currently exists" ExxonMobil may not bid on this project. He asked whether this was true of other producers as well.

MR. MASSEY said he could not speak for the other producers.

[4:08:49 PM](#)

MR. MASSEY responded to a question as to how he would present the status of this project to his company by stating that he would indicate "we gotta keep working at it." He reminded the committee that his company is committed to finding a way to make this important project go forward. He indicated that if the state and the producers can agree on how to structure the upstream, this project will go forward.

[4:10:26 PM](#)

CO-CHAIR GATTO suggested that the long-term forecast supports development of this project. He asked about communication with the administration.

MR. MASSEY said the governor has made herself available for conversation with ExxonMobil management. He offered his belief that the commissioners have decided on their approach and "they don't want to negotiate with us."

[4:12:56 PM](#)

REPRESENTATIVE ROSES asked whether the open season should be held before or after the issuance of the license.

MR. MASSEY replied that he has not pondered that question, although he understands the point. He restated that his concern is "what the deal is" prior to proceeding with the project.

CO-CHAIR GATTO reminded the committee that previous pipeline negotiations had very little public discussion.

[4:15:59 PM](#)

REPRESENTATIVE GUTTENBERG read from a letter by a consultant who worked on prior pipeline negotiations which concluded that the state has never developed fiscal terms that are unreasonable compared to international practices. The letter put forth that the state has "been a reliable business partner," and there is no need to "treat Alaska as banana republic in order to secure the gas line."

[HB 177 was held in committee.]

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 4:17 p.m.