

MINUTES
SENATE FINANCE COMMITTEE
April 28, 2007
9:00 a.m.

CALL TO ORDER

Co-Chair Bert Stedman convened the meeting at approximately [9:00:53 AM](#).

PRESENT

Senator Bert Stedman, Co-Chair
Senator Lyman Hoffman, Co-Chair
Senator Charlie Huggins, Vice Chair
Senator Joe Thomas
Senator Fred Dyson
Senator Kim Elton
Senator Donny Olson

Also Attending: SENATOR GARY STEVENS; DAVID VAN TUYL, Gas Commercialization Team Lead, BP Exploration (Alaska) Inc.; PATRICK COUGHLIN, Senior Attorney, BP Legal Department;

Attending via Teleconference: There were no teleconference participants.

SUMMARY INFORMATION

SB 104-NATURAL GAS PIPELINE PROJECT

The Committee heard from a representative of BP. The bill was held in Committee.

#sb104
[9:00:57 AM](#)

CS FOR SENATE BILL NO. 104(JUD)
"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."

This was the tenth hearing for this bill in the Senate Finance Committee.

[9:04:47 AM](#)

DAVID VAN TUYL, Gas Commercialization Team Lead, BP Exploration (Alaska) Inc., introduced himself and began his presentation which was accompanied by a handout titled "Alaska Natural Gas Pipeline Project, Testimony on AGIA, Senate Finance Committee, April 28, 2007" [copy on file].

[9:05:54 AM](#)

Page 2

An Opportunity...and a Challenge

- BP wants and needs a successful gas pipeline

[Line graph showing BP Net Production (mboe/d) and projected production for the years 1975 through 2050 in the categories of Light Oil, Viscous, Heavy, and Gas. Overlaid is a line indicating Current decline with continued investment.]

- Project remains commercially challenged

Mr. Van Tuyl testified as follows.

BP wants and needs a successful gas pipeline project. And when I say successful, we want that pipeline to be built at a low capital cost and operated cost efficiently. We believe that is what is required to make the project happen and make it successful. Low costs are good for BP and they're good for the State because it results in lower tariffs, higher netbacks and more revenues for both the State and for BP. Also, a low cost project will help provide incentive to explore for more gas to keep the pipeline full into the future. That is also good for the both the State and for BP. The best way to ensure there is gas exploration in the future is to make sure we get a pipeline built in the first place, and to get it built for low cost. This is a hugely important project for BP, for

Alaska and for the nation as a whole. It represents the largest, known, but undeveloped gas resource in the United States, and in BP's world wide portfolio. The gas project itself is important in its own right, but it also extends the economic life of oil production on the North Slope for decades into the future. Extending oil production is good for the State, the nation and for BP. We share the governor's and the legislature's desire to get a successful gas pipeline project moving. But it's important to remember that the project remains commercially challenged. It requires massive capital investment. It requires even larger financial commitments to get the necessary financing in the capital markets to allow the project to advance. If it was easy, it would be advancing today. But it's not easy. It's incredibly challenging. The size of this project alone makes it incredibly challenging and risky.

[9:08:13 AM](#)

Page 3

BP Disagrees with Administration's Economics

- Project is nor "wildly profitable"
 - o Can't separate upstream economics from midstream commitments
 - o Economics must be based on the complete project
- Firm transportation commitments must be accounted for in project economics
 - o Upstream pays for the midstream
 - o Without FT there is no project
- Long-term cash generation is highly important
 - o Cash flow well beyond 10 years remains vital
- Need common understanding of project

Mr. Van Tuyl continued his testimony as follows.

I want to leave you with a point that we do fundamentally disagree with the way that the Alaska Gas pipeline project economics have been characterized recently by the Administration. We have concerns over a number of statements made by the Administration on the project

economics, but I'm going to limit my comments here to three key concerns. One relates to the underlying economic methodology in the assumption that you can somehow decouple the upstream from the midstream. We'll talk about that a little bit. There's the nature of firm shipping commitments, we heard a little bit about this from Fred Rich the other day and I'm going to talk a bit more about that. And the importance of not only near term but long term cash flow in investment decision making.

We are concerned that the economic analysis presented by the Administration to the legislature can be very misleading. First, on the topic of economics. Without the commitment of capital to the pipeline or the huge financial obligation required for Firm Transportation (FT) for the midstream facilities, there is no way to realize value from the sale of gas. It won't happen. Thus, any analysis of the project that excludes midstream capital and FT is incomplete. Because these commitments are just that, they're legally binding commitments, they need to be accounted for when evaluating project economics. Those commitments were ignored in the Administration's analysis of the economics when they split out the upstream returns. Because that method ignores the FT obligation, the resulting assertion that the upstream economics are so robust is patently incorrect. In fact, the upstream pays for the midstream. It does this through firm transportation commitments. And so those commitments cannot be ignored.

The second point I want to emphasize is to ensure we have a common understanding of the nature of these firm transportation commitments. FT is a binding commitment made by a shipper to a pipeline company in an open season to secure capacity on the pipeline for a specified duration of time at a specified cost. Again, we heard Fred Rich talk about this the other day. Now, there's a few important facts to be clear on about FT. Again, as I said, FT is binding legal obligation. It becomes binding once certain conditions are met, and one of those conditions is the pipeline coming into operation. We have heard the Administration claim that the producers say that FT is "exactly like debt". I'm not aware of any of us having said that in testimony. Long term commercial commitments like FT are often characterized as "debt-like", and therefore they have to be reported to the SEC, and we do report these long

term commercial commitments to the SEC. But that's not the core issue of how they're accounted for.

The core issue is whether those FT commitments require the producers to absorb the substantial majority of the risk associated with the project. FT is a financial obligation, and it is certain that the lenders would have recourse to the financial security provided by the producers' FT should the pipeline company fail to meet its obligations. Because of that, FT, again, can't be ignored if a project is to be evaluated properly. Generic statements about treatment of long term commercial commitments is dangerous. Commitments of the magnitude required to underpin this project are massive in both the dollar amount and the likely duration. These commitments will create their own weather in the financial markets just because of their size. They have to be considered.

The third and final point I wanted to emphasize is confidence in future cash flows is very important to investment decision making. That is particularly true for a commitment as large as the one that we're facing with the Alaska gas pipeline project. The Administration suggested that cash flows beyond 10 years are relatively unimportant in financial decision making on this project. That's just not true. Cash flows further out in time do have less effect on net present value due to discounting, I mean that is true. But cash impact years into the future will indeed be real. And in evaluating the economics of projects, BP looks at many different measures, including net present value, internal rate of return, productivity index, the things we heard the Administration talk about. Those are some of the measures which are considered. But the ability of a project to generate long-term cash flow is also an important consideration to investors. It's important to bear in mind that we expect the FT commitments we just talked about will be in effect well beyond 10 years. So those making those commitments want to make sure that they'll be able to make good on them. Lenders will want to know that, too. Getting this project right has enough challenges of its own, let alone when we have such fundamental disagreement with how the project is characterized.

[9:14:17 AM](#)

What is so important about FT?

- Firm Transportation commitments (FT) by the resource owners are needed for a gas pipeline company to get financing
 - "No customers, no credit, no pipeline" (TransCanada)
 - "No producers, no pipeline" (Enbridge)
- FT is a binding financial obligation
 - Not simply "committing gas to a pipeline"
- Requires multi-billion dollar commitments by resource owners
 - Assuming 4.5 bcfd, \$3.50/mcf, 25 year term.....\$144 billion
- Long term commitments represent real risk
 - Two risks:
 - Price risk (over time, market price will not cover FT cost and produce an acceptable return on the investment)
 - Supply risk (will not have sufficient gas to use the FT commitment over time)
 - Risk is borne by those making the commitments

Mr. Van Tuyl explained this page as follows.

FT commitments are typically obligations to "ship or pay" made by the resource owners or the "shippers", and they're needed by the pipeline company to get financing. Just to validate how important they really are, we've heard some very simple and straightforward comments from pipeline companies who have testified in the past few weeks, and they're shown here on the slide. TransCanada said "No customers, no credit, no pipeline". Enbridge put it perhaps even more simply: "No producers, no pipeline". I don't think those are "political" statements. They are simply statements about the simple financial truths of a gas pipeline project.

FT is a binding financial obligation. Sometimes I've sometimes heard FT described as "committing gas to a pipeline". Kind of a short hand reference. And I've heard that quote from industry as well as others, so I'm not

pointing fingers at anyone in particular here. But I wanted to make it clear that FT is a financial obligation. It's a commitment of dollars, not a commitment of gas. It's typically a "ship or pay" obligation, and that means that a shipper commits to pay the pipeline company for use of its service whether or not it actually ships gas. It's also important to note that a company doesn't have to have any gas resources to enter into a firm transportation commitment. Any company who meets the creditworthiness standards set by the pipeline company is free to bid for capacity in an open season. Gas pipelines are "open access", and anyone is free to obtain capacity if they make those requisite commitments.

The scale of the commitments is often oversimplified. It's not "just" the capital cost of the project, if that weren't enough on its own, being a twenty, thirty whatever billion dollar commitment it might be. The commitment is for the "demand charge" which is the cost of service the pipeline will charge through time. Capital is one major component of the demand charge. For illustration, I've shown on the slide some broad assumptions to put the scale of these commitments in perspective. If you assume you have a 4.5 billion cubic foot a day pipeline, that the charge is \$3.50 per thousand cubic foot, and you have a 25 year term for the commitment, and you do the sums it's a \$144 billion for the firm transportation commitments in total. That's a huge sum, even for a company the size of BP.

Again, these long term commitments are just that. They're commitments. Therefore, they represent real risk. That risk can manifest itself in a couple of ways. There's price risk. The price can drop in the future, the price of the commodity in the market, such that the costs of these commitments isn't covered. Does that relieve you of the commitment? No, it doesn't. The commitment exists. The gas supply on the upstream might be insufficient also to be able use the capacity that's been committed over time. That's another risk. The size of these commitments magnifies that risk. And again, the risk is borne by those that make those commitments.

[9:18:09 AM](#)

Page 5

Project Risk Resides with the Resource Owners

All risks are either borne directly by the resource owners or passed to them via the market or the toll.

[Flow chart depicting the Price Risk of Natural Gas Markets, market volatility; the Fiscal Risk of Government, Change in fiscal terms; the Production Risk of Reserves, Volume and deliverability risk; and the Toll Risk to the Pipeline Company, including the Fiscal/Schedule Risk of Governments/Regulators, Regulatory delay & fiscal terms; the Cost Risk of Materials and Construction, Material, labor, equipment costs; and the Finance Risk of Capital Markets, repayment risk.]

Those bearing a risk are commercially motivated to manage that risk

Mr. Van Tuyl spoke to the flow chart as follows.

What this slide attempts to show is that risk is ultimately allocated in a major resource development project like the Alaska Gas Pipeline Project, and how it all basically starts with the resource owners. And I'll walk through this one step at a time. First, we start with the resource owners, and that's of course folks like the State of Alaska, and it includes the lessees, like BP, Conoco-Philips, Exxon Mobile, Chevron and others. Now there's certain risks that are inherent with the resource itself. There's things like price risk, which we just talked about. We're in the business of selling a commodity like natural gas. There's always the risk that the price of gas will fall in the future, and it may even fall below the cost of the tariff to deliver it to the marketplace. But that's a risk we're in the business of managing. There's also production risk. We need to be able to deliver the volume of gas to the pipeline on a day-in and day-out basis, every day, and then over time we need to make sure we can keep the pipeline full over the life of the project. And again, those risks are important consideration when considering making these firm transportation commitments.

There's another risk for a lessee and that's fiscal risk. There's the risk that the fiscal terms on the upstream

business might change over time. On major infrastructure projects like the one we're talking about here, all around the world, it's not uncommon for host governments to address fiscal risk through a mutually agreed framework. There's a whole host of risks that we commonly think of as associated with the project itself. Those are things like regulatory risk, if the regulatory process changes it could result in delays, and schedule impacts and what not. There's cost risk associated with the materials required to build the project, and labor costs and project management and execution. And then there's finance risk. The ability to go out to the capital market and actually get financing for your project. Again that was a topic of discussion Fred Rich talked about at some length in that finance workshop.

I guess what is critical to appreciate here is that all these project-related risks that are taken by the pipeline company and then are ultimately passed through via the toll to the resource owners. The pipeline company receives a regulated rate of return. It gets a reasonable return on its investment that's commensurate with the risk that it takes. In exchange for being rewarded with that regulated rate of return, the regulators ensure that the pipeline company does not take on certain risks. And instead those are passed through to the resource owners. And that's how the risk/reward balance is struck by the pipeline regulators. So ultimately, virtually all risks are either borne directly by the resource owners, or passed through to the resource owners through the toll. To ensure a low cost project, we think it's important that those that bear a commercial risk are able to manage that risk. They are the ones that are commercially motivated to ensure that that risk gets managed downwards.

[9:21:51 AM](#)

Page 6

BP Messages on AGIA

- AGIA needs significant modification to result in a successful project

- As drafted, BP will not be able to submit a bid under AGIA
- As drafted, it is difficult to envision circumstances that would allow BP to make a firm transportation commitment to a licensed project under AGIA
- Why?...
 - Negotiated rate production unavailable upon expansion
 - Subsidization of competitors is commercially unreasonable
 - Resource terms insufficient to justify FT commitment
- BP intends to bid if AGIA is appropriately modified

Mr. Van Tuyl continued his testimony as follows.

I'd like to turn to some of our specific comments on AGIA. I guess to put it clearly and succinctly, AGIA needs substantial modification to result in a successful project. And I'll go into some detail as to the modifications we see as necessary. As we've said in previous testimony, we agree with the Governor's intent on using AGIA to advance a successful project. But the current version of AGIA won't get us there. I'll explain why again in a moment.

I want to be very clear with BP's evaluation of AGIA as it's currently drafted. Simply put, BP won't be able to submit a bid that conforms to the requirements of AGIA. It's not easy for me to say that. Because BP really does want to be able to compete in the AGIA process. BP wants to help deliver a successful Alaska gas pipeline project. We think we can add significantly to the success of the project. If AGIA is fixed, we intend to bid. We're happy to have our bid openly evaluated along with others. But the current terms of AGIA won't allow that to happen.

I also want to be very clear about the implications the current version of AGIA holds for BP participating in an open season. As currently drafted, it's difficult to envision the circumstances that would allow BP to make a firm transportation commitment to the licensed project under AGIA in an open season. And that's true even if a BP

affiliate was the licensee. Why is that? That's because BP believes the terms of AGIA put unreasonable commercial risk on initial shippers. AGIA removes negotiated rate protection. Those are protections from potential cost overruns, from subsidization of expansion shippers, and the ability to gain long term certainty of future rates. Now there is language in the bill that now references the term "negotiated rates" but it doesn't actually provide rate protection for initial shippers. AGIA doesn't provide the fiscal certainty also needed to justify the massive, long term firm transportation commitments necessary for a successful project.

I'm not trying to be dramatic, or issue any kind of a "threat". I'm just trying to be very open, and transparent. We owe that to you because there is so much at stake.

[9:24:37 AM](#)

Page 7

Key Concerns Preventing BP Bid Under AGIA
In the order they appear in SB-104

- .130(2)(B)/ .210 - "Detailed" description of design requires substantial customer consultation, engineering
 - FERC Order 2005 requires "god faith estimate"
- .130(2)(C-D) - Can't "demonstrate" economic viability
 - "nobody can say today whether this project is economic or not" (Mid-American Energy); need bottoms-up cost and revenue estimate
- .130(7) - Requires subsidization of competitors & eliminates negotiated rate protections
 - contrary to ANCPA & FERC rules
 - imposes unreasonable commercial risk
- .130(13) - Commitment to reserve capacity for in-state delivery points, regardless of open season outcome
 - imposes unreasonable commercial risk
 - not consistent with FERC Order 2005 [157.34(c)(8)]

- .150(a) - Release of proprietary information to competitors after license award creates huge exposure

Mr. Van Tuyl detailed how the provisions listed on this page would prevent BP from submitting a bid under the current version of AGIA.

While we have several concerns with AGIA as drafted, we've tried to hone this list only to the most significant concerns that we have that would prevent us from submitting a conforming bid. I'm not planning to walk through each of these in detail, but I'll explain a few of them to give you a sense of our concern. They are arranged in the order they appear in the bill, they're not in any sort of rank order.

For example, in section 130 paragraph 2 parts C and D, we think it's impossible, the bill calls us to "demonstrate" the economic viability of the project, and we think it's impossible to "demonstrate" the economic viability of this project within the AGIA timeframe. I mean we can make good faith estimates based on assumptions, but we don't have a detailed cost estimate. I mean, it took eighteen months and \$125 million to come up with the detailed cost estimate. It was actually a preliminary estimate, that we did back in the 2001, 2002 timeframe. In fact, Mid-American in their testimony about a month ago acknowledged that conundrum, saying that nobody can say for sure that the project's economic.

Another one, the next one down, we've provided substantial testimony in the past about section 130 part 7, paragraph 7 about AGIA as drafted requires subsidization of competitors. If we intended to be an initial shipper, upon expansion, this provision would require us to subsidize our competitors. It actually eliminates protections of negotiated rates. We think those provisions are in conflict with FERC policy, as we've talked about under Order 2005, and under the Alaska Natural Gas Pipeline Act, which talks about it does talk about rolled-in rates and again, our problem isn't with rolled-in rates. Our problem is with subsidization. There's a couple of important objectives that are highlighted in FERC Order 2005. One was providing incentive for future expansion, but it also says there's two of them. One of them is to provide rate predictability

for initial shippers. And this provision ignores that important objective.

Another one on down the list is section 150. AGIA as currently drafted would require the release of the successful licensee's proprietary information. We would hope to be able to make a very complete bid that included quite a bit of data so that the State could analyze that. Technical data, talk about new technologies that we've worked on, our strategies plans, rate making strategies, you name it. AGIA as drafted would require the State to release all that information to our competitors upon being awarded the license, which we think is commercially unreasonable. There's some more concerns on the next page.

[9:27:56 AM](#)

Page 8

Key Concerns Preventing BP Bid Under AGIA
In the order they appear in SB-104

- .200(a) - Must accept FERC certificate despite conditions
 - could add significantly to project cost
- .200(b) - Must sanction project within one year of FERC certification, regardless of cost
 - failure to sanction results in loss of all data to state (engineering, design, contracts, permits, etc.)
- .230(a)(2)/.210 - In breach if substantial deviation from plan set out in application
 - Unless it increases NPV, is ordered by AOGCC or isn't foreseeable
 - FERC, BLM, municipal agencies, Canada, etc. could require changes to project specs outside state control
- .240(c) - Effectively no way to abandon an uneconomic project; licensee subject to damages
- .310 - .320 - Fiscal terms insufficient; risk of no FT customers

- o "no customers, no credit, no pipeline"
(TransCanada)

Mr. Van Tuyl continued to address BP's concerns with AGIA as follows.

Under 200a, this would require the licensee to accept a FERC certificate despite potential conditions FERC might impose, which is commonly done by FERC on issuing a certificate. They'll issue a conditional certificate and say "you need to address certain things." We don't know what those conditions might be, we don't know what the disposition of FERC might be at the time. Those conditions could significantly add to the project cost, and if the FERC knows that we have to accept that certificate, what motivation will FERC have to, typically there's a consultation period where you can work that out. If FERC already knows that we have to accept that certificate, then that certainly impacts the bargaining position.

The next item then, once the FERC certificate's issued the project itself has to be sanctioned within one year, regardless of what the cost is. Again, we don't know what the cost of the project's going to be today. So, this would require up to go forward with the project potentially one that would lose money for the State and for the investors, and we don't think that's commercially reasonable. And if we didn't, then the breach would, that would be a breach. Failure to sanction would result in turning all of our data over to the State.

Another item that we've talked about quite a bit in testimony is the last one on the page about the fiscal terms. It is encouraging on one hand that AGIA does recognize certain of the resource risks to the lessees, things like RIV RIK switching, royalty valuation but the terms as they're addressed in AGIA just are not sufficient to justify those firm transportation commitments. We think there's a real risk as a result that potentially no FT commitments could be forthcoming, like I said. It's hard for us to envision BP making FT commitments under this current for of the bill.

[9:30:08 AM](#)

How AGIA can help deliver a successful project

- Address areas of key concern listed on prior slides
- Allow applicants to respond to State's objectives
 - Prescribing solutions up front will not result in the best project
- Avoid exclusivity to ensure a pipeline gets built
 - Even as amended, AGIA creates exclusivity
 - Federal model encourages competition in the marketplace
- Address fiscal terms to encourage FT commitments needed for a successful project
 - Allow resource owners to make offer in bid
- Allow due process of appeal, remove potential Order 2004 conflict, other clarifying edits

Mr. Van Tuyl testified as follows.

A number of modifications need to be made. Those ten areas of concern that we just highlighted would need to be addressed and fixed. And as we've discussed in every testimony on AGIA we've offered, there are three other key areas that we think also need to be fixed. First, we think the State should provide its list of objectives that prospective applicants must address. BP, and other applicants, should be allowed to tell the State how we would address the State's objectives. That's how the best solutions are developed - through creative thought, not by presupposed outcomes. Second, we think AGIA should remove elements of exclusivity. Now, an amendment was made in a prior committee to try and address that concern, but even with the amendment language, AGIA still creates exclusivity. And exclusivity prevents competition in the marketplace. The federal model that we have under federal law and FERC works well. It encourages open competition in the marketplace. It works everywhere else in America, and it will work for Alaska as well. Third, as I just spoke on the other slide, fiscal terms have to get solved in a way that will encourage firm transportation commitments from

shippers. We would like to have the opportunity to include fiscal terms in a bid under AGIA that the State can consider, and it can reject if it likes, but at least we'd have an opportunity to make a bid. We'd like the opportunity to submit a bid under AGIA. Finally, there are other edits, less fundamental than the ones I just mentioned that we think also should be addressed.

[9:32:13 AM](#)

Page 10

- BP's Vision for Alaska
- BP has a long history in Alaska...
- ...and we look forward to a 50-year future
- That future is only possible with a gas pipeline
- BP wants to bid under AGIA and hopes it will be modified appropriately

[Line graph showing BP Net Production (mboe/d) and projected production for the years 1975 through 2050 in the categories of Light Oil, Viscous, Heavy, and Gas. Overlaid is a line indicating Current decline with continued investment.]

Mr. Van Tuyl provided the following testimony.

To close, I'd like to spend a moment to look into the future and consider again the opportunities that we have before us. BP has a long history in Alaska. We've been actively involved in the exploration, development and production of Alaska's North Slope energy for decades. We see the opportunity for a bright future ahead. In fact, we talked about our 50-year future. And it's not just a slogan. If you look at this "green mountain chart", as I've heard it referred to, it shows the possibility of the future that BP sees for Alaska, this is just shown as BP's net share of production through time. A couple of things we can draw, of course, here we are in 2007. Those days of high plateau production are behind us. We still have a

significant amount of production today, but that production, too, will continue to decline with time. It's kind of hard to see on the graph, but there's a dotted red line that shows the current rate of decline at six percent, but that has the historic level of investment built into it. It requires a significant level of investment just to achieve that level of production. We can make up for that decline with new investment that would result in new production from things like heavy oil resources, that's shown in Viscous in yellow, the heavy oil in orange, huge resource on the Slope untapped. And then of course there's the known gas resource, which is shown in red. But none of this is a given. It's a vision of what's possible. That future is only made possible with a successful Alaska gas pipeline project.

[9:34:18 AM](#)

Page 11

What A Successful Gasline Means

- Jobs for Alaskans
- Additional revenue for future generations
- Increased economic activity
- New businesses created
- Long term gas supply opportunity for Alaskans
- A more diversified economy for decades

[Map of Alaska, Canada, and the Continental United States, with arrows indicating the path of the gasline traveling 2100 miles from the North Slope to the Alberta Hub, then 1500 miles to the Chicago Hub.]

Mr. Van Tuyl concluded his presentation as follows.

Again, it's not just any pipeline project that we need, we need a successful gas pipeline project. It's a project of tremendous scope and scale and that's what this picture in the lower left-hand part of the graph reminds us of. Because of that scope and scale, it presents tremendous risk. But if it's done right, it also presents a wonderful

opportunity for the State, for the industry and the people of Alaska. Because there is much at stake, we need to get it right. The project creates opportunity for jobs for Alaskans, and if we deliver that successful, low cost project, the opportunity for revenues to the State and to industry well into the future. In fact, we have an opportunity here to create a whole new industry of gas exploration with a successful, low cost project. Gas exploration and expansion are only possible if the pipeline gets built in the first place, and if it's built for a low capital and operating cost. That will make it attractive for bringing new volumes into the project, which benefits the State, gas explorers, and initial shippers as well. A successful gas pipeline project will provide the opportunity to bring a long term gas supply source for use by Alaskans right here at home. And finally, gas sales will diversify Alaska's economy for decades into the future. As I said, there's a lot at stake, so we need to get it right. BP wants to get it right. That's why we've tried to be very forthright and specific with our comments. We owe that to you as you finish your deliberations on AGIA.

AT EASE [9:36:23 AM](#)/[9:45:19 AM](#)

Co-Chair Stedman referred to the decrease in gas production depicted on the "mountain chart" on page 2, and asked if that graph was based only on known reserves.

Mr. Van Tuyl affirmed that the chart based all resource projections on known reserves without consideration of exploration potential.

Co-Chair Stedman referenced page 4, and asked if the \$3.50 figure in the third bullet on that page was related to the tariff rate.

[9:48:08 AM](#)

Mr. Van Tuyl responded that the tariff rate or the demand charge could not be predicted. The \$3.50 rate was provided to illustrate the FT commitment. The three major producers in Alaska conducted a cost study in 2001 through 2002 and arrived at an estimated \$20 billion total project cost, and a toll of \$2.39 per thousand cubic feet. Producers had not conducted another cost estimate, but project costs had undeniably

increased. The rate of \$3.50 was "half again as much" as the rate estimated in the 2001 study.

[9:49:32 AM](#)

Co-Chair Stedman assumed that the rates reflected nominal dollars and were not discounted to present value.

Mr. Van Tuyl understood that the \$2.39 figure incorporated nominal dollars, but would verify that. The \$20 billion cost estimate was calculated in constant dollars.

[9:50:11 AM](#)

Co-Chair Hoffman suggested that the same bullet point revealed "great potential". Price fluctuations from \$3.50 to \$6.50 demonstrated the potential for large revenues to the State, the pipeline owner, and the resource owners.

Mr. Van Tuyl admitted to the potential for profit in the gas market, but stressed that the project was not without risk due to unpredictable market fluctuations.

[9:52:00 AM](#)

Senator Huggins noted the reference Section ".200(a)" on page 8 of the presentation. BP testified that it objected to that provision of Section 43.90.200(a), and Senator Huggins asked how the provision could be "fixed" without putting the State at risk.

Mr. Van Tuyl would work on solutions to the concern regarding this subsection. The concern was the subsection's mandate that the licensee accept the "unknown".

[9:53:31 AM](#)

Co-Chair Stedman asked for an explanation of the subsection.

Senator Huggins cited Section 43.90.200. Certification by regulatory authority and project sanction on page 14, line 9 of the bill.

Mr. Van Tuyl clarified that BP was concerned that this section required the licensee to accept the FERC "conditioned

certificate" without knowledge of the conditions of the certificate or other factors, such as total project cost.

[9:54:53 AM](#)

Senator Huggins anticipated two or three recommended solutions to the issue. He next referenced Section 43.90.240(c) on page 18, and expressed his understanding that BP did not support the use of arbitration in determining that a project was uneconomic.

Mr. Van Tuyl affirmed.

Senator Huggins requested BP provide "fixes" to this perceived problem.

Mr. Van Tuyl described the concern associated with subsection (c) as the requirement for use of an arbitration panel to resolve differing opinions of whether the project was economically viable. The panel could determine a project was uneconomic only upon a finding of inadequate credit support and after the licensee had demonstrated that the project was uneconomic based on projected gas sales revenue and upstream investment. He asserted that neither of the requirements under this subsection were "provable".

[9:58:19 AM](#)

Co-Chair Stedman announced that a representative from the Palin Administration would be asked to address these issues at a later date. He reiterated the request that BP provide "reasonable solutions" to the Committee to attend to the company's identified trepidations.

Senator Huggins thanked BP and Mr. Van Tuyl for their "specificity and candor".

[9:59:41 AM](#)

Co-Chair Stedman indicated items of concern that the presentation had not specified, such as the five year extension for "no credit".

[10:00:08 AM](#)

Mr. Van Tuyl clarified that the list represented a sample of key concerns that would prevent a BP bid under AGIA. BP had other issues with the bill, including the five year extension. He pointed to page 9 for a listing of additional general concerns.

Co-Chair Stedman asked for more explanation of the items on page 8.

[10:01:25 AM](#)

Co-Chair Hoffman relayed "major concerns" of the previous legislature regarding the "freeze" on oil and gas taxes contained in the proposed contract negotiated between the Murkowski Administration and BP, Exxon Mobile and Conoco Philips. He asked BP's position on the rate structure contained in AGIA, and the location in the bill that the issue was delineated.

Mr. Van Tuyl expressed that the tax rate remained a key concern, and was addressed on page 8 in the presentation in the bullet labeled ".310/.320" generally as "fiscal terms insufficient". He recalled the debate by the legislature and in the public, and indicated BP's willingness to further explore the issue.

[10:03:26 AM](#)

Co-Chair Hoffman opined that the issue of FT commitments posed a "major stumbling block" in the negotiations between the State and producers. He asked if BP could prioritize its concerns with the AGIA legislation.

Mr. Van Tuyl answered that each item must be addressed, and that the list provided in the presentation was chronologically arranged in accordance with the bill.

Co-Chair Stedman informed that the "fiscal terms" of the bill referred to a ten-year period, but was contingent upon participation in the first binding open season. He asked if that provision was of concern to BP, or if it planned to participate in the first open season.

[10:04:52 AM](#)

Mr. Van Tuyl did not expect BP would participate in the first open season under the current proposal because of the fiscal

terms, the risk associated with the FT commitment, and the removal of negotiated rate protection through the employment of rolled-in rates. BP expected the FT commitments to extend 20 to 30 years, and would not likely commit to a long-term FT without a corresponding guarantee on the tax rate for the life of the FT.

Mr. Van Tuyl pointed out that AGIA addressed only the tax rate without regard to other elements of State take. He expressed approval that the proposed legislation indicated that "RIV/RIK switching" would need further attention and amendment.

[10:07:11 AM](#)

Co-Chair Stedman asked the definition of "RIV/RIK switching".

Mr. Van Tuyl defined RIV/RIK as "royalty in value royalty in kind". He informed that under the current proposal, the State had the option to take its royalty in the form of gas or as a monetary payment. This arrangement could cause problems of capacity and supply for the pipeline owner if the State "switched" between taking its royalty in value or royalty in kind.

[10:09:04 AM](#)

Co-Chair Stedman understood from previous comments that the issue had been resolved.

Mr. Van Tuyl disagreed. The bill recognized the issues created by RIV/RIK switching, and stated that they would be addressed via a regulation to be drafted before the first open season. The proposed legislation contained language that prohibited the forthcoming regulation from creating "unreasonable interference with marketing" or "unreasonably disproportionate costs," which Mr. Van Tuyl understood to mean that the regulation would be permitted to "create these problems" as long as they were not deemed "unreasonable".

[10:10:19 AM](#)

Senator Dyson asked for a comparable situation to demonstrate an instance when BP received the extent of fiscal certainty that was requested under AGIA.

Mr. Van Tuyl responded that comparable situations were uncommon due to the scope of the Alaska natural gasline project. However, he referenced the Baku-Tbilisi-Ceyhan (BTC) pipeline in Western Asia which was built under an agreement of fiscal stability for 60 years.

Senator Dyson assumed that all the sovereign countries involved had agreed not to change any of the tax structures relating to the BTC project.

[10:12:06 AM](#)

Mr. Van Tuyl replied that the tax agreement defined the tax on petroleum, oil or gas, and on the facilities and transportation. That tax was not subject to change.

Senator Dyson understood that the BTC pipeline crossed three national boundaries. He asked for affirmation that all three countries had agreed to the fiscal terms for a period of 60 years.

Mr. Van Tuyl answered, "I believe that is correct."

Senator Dyson asked if there existed a North American example of the fiscal stability BP had requested under AGIA.

Mr. Van Tuyl was aware of no North American pipeline example, as that infrastructure already existed. But he offered that oil and gas leases provided defined terms for the length of the lease.

[10:13:36 AM](#)

Senator Dyson surmised that none of the major North American projects had been built with the degree of fiscal stability BP was currently requesting.

Mr. Van Tuyl commented that there was no like project for comparison in North America.

[10:13:57 AM](#)

Senator Dyson acknowledged "constitutional public policy challenges" in negotiating a guarantee to the pipeline builder that it would recover the construction costs by freezing the tax rate for a fixed amount of time. He shared that a colleague had

suggested the tax rate remain fixed until the pipeline builder had recaptured its investment costs rather than fixing the tax rate for a period of time, thus reducing the monetary risk to the company and avoiding public policy litigation within the State. He asked if BP would be willing to examine such a possibility.

Mr. Van Tuyl replied that BP would welcome an opportunity to discuss options to resolve the issue.

[10:15:53 AM](#)

Co-Chair Stedman informed that he had requested that the Administration provide an estimate of the volume of gas necessary to equal the construction costs of a gasline.

[10:17:28 AM](#)

Senator Thomas understood that the pipeline project could be abandoned if the State and the licensee agreed that the project was uneconomic. He asked for clarification that BP's concern regarded an instance in which the State determined the project to be economic and BP disagreed with that determination.

Mr. Van Tuyl affirmed. Section 43.90.240 (c) would be applicable only in the event of a disagreement regarding the economic viability of the pipeline.

Senator Thomas asked what factors would cause a licensee to determine that the pipeline was uneconomic after expending the necessary resources to obtain the license.

[10:18:43 AM](#)

Mr. Van Tuyl responded that many factors could result in a project becoming uneconomic. For example, the project cost could become so high as to make transporting gas to market uneconomic for shippers, and the pipeline company would be unable to obtain FT commitments.

[10:19:33 AM](#)

Senator Thomas informed that the Committee heard an extensive presentation from Sullivan & Cromwell LLP addressing this issue, and assumed that those details had been researched. He inquired

whether, if BP found the terms of AGIA to be unacceptable, the company would pursue a FERC application outside of AGIA.

Mr. Van Tuyl replied that BP's "desire" was to work with the host government, as was its standard practice.

[10:20:12 AM](#)

Co-Chair Stedman invited questions regarding the provisions of Section 43.90.230(a)(2) and Section 43.90.210.

Mr. Van Tuyl shared that BP's concern was that the provisions presumed likelihood for a of breach of contract due to "substantial departure" from specifications set out in the application, as the licensee had only three opportunities to make changes to the plan under Section 43.90.210. Other events could occur which would compel a change in the initial plan not allowed under the proposed legislation, such as an order from FERC, the Bureau of Land Management (BLM), or a municipality.

[10:22:40 AM](#)

Senator Dyson asked the meaning of "loss of all data to state", which was included on page 8 of the presentation as a ramification of Section 43.90.200(b).

Mr. Van Tuyl assumed that BP would be determined to have credit support, resulting in a one-year "window" to sanction the pipeline project. If for any reason BP deemed the project uneconomical and failed to sanction the contract, it would be in breach of the agreement. Under the provisions of Section 43.90.230, a breach would be remedied by requiring the licensee to release to the State all data related to the pipeline project.

Senator Dyson discerned that BP would not "lose" the data it collected as the company would be allowed to retain copies which may be valuable for future projects.

Mr. Van Tuyl assumed that the records would also include proprietary data that BP could use in competing projects elsewhere. Revealing that valuable data would be of benefit to competitors.

[10:25:19 AM](#)

Senator Dyson reminded that the State could have paid up to \$500 million of the costs to gather that data. He hypothesized a situation in which the State would assure that the relinquished data would be kept confidential. He asked if that would be acceptable to BP.

Mr. Van Tuyl clarified that the "real concern" was the requirement that the licensee sanction the project within one year, as necessary information regarding project costs was not available.

Senator Dyson summarized that the loss of data was a concern, but the primary issue was the sanction requirement.

Mr. Van Tuyl affirmed. He also informed that BP would not seek State investment if it decided to participate in the application process and was selected as the licensee. Thus, the data would solely represent BP's investment.

[10:27:31 AM](#)

Senator Huggins perceived an "inoperability" in the provisions of Section 43.90.240(c) and Section 43.90.200(b) that would impede BP's willingness to participate in the application process. The latter Section allowed no avenue to abandon an uneconomic project, and the former required the acceptance of the FERC certificate and sanction of the project regardless of fiscal considerations.

Mr. Van Tuyl expressed that BP would prefer the flexibility to manage the project as it would any other project, by taking into consideration all relevant factors.

[10:28:26 AM](#)

Senator Huggins asked regarding administrative appeal rights under section 43.90.200.

Mr. Van Tuyl responded that the FERC process for certification allowed for review of a conditional certificate with FERC to determine the best way to proceed. He deferred to Mr. Coughlin for further explanation.

[10:29:38 AM](#)

PATRICK COUGHLIN, Senior Attorney, BP Legal Department, explained that under the normal FERC process, a certificate was often issued with several conditions. Those conditions instigated a "give-and-take" negotiation process. The applicant had the formal right to appeal the FERC decision through the administrative process, and if the applicant lost the initial appeal it could appeal the agency determination to the Washington, DC circuit court. AGIA would remove the right to appeal the FERC decision, thus weakening the applicant's negotiation leverage. This position would effectively force the applicant to accept the FERC determination.

[10:31:24 AM](#)

Co-Chair Stedman asked for additional information regarding FERC certificates issued to BP, and whether forfeiture of appeal rights was standard.

[10:31:41 AM](#)

Co-Chair Hoffman discerned that Section 43.90.200(b) required the project to go forward regardless of cost, which he found unreasonable. The economic viability of the project should be considered in the determination to proceed with a pipeline.

[10:32:25 AM](#)

Mr. Van Tuyl agreed that the provision would "tie the hands of the investor" and was unreasonable. He could not offer a specific language solution at this time, but would return to the Committee with recommendations.

[10:33:13 AM](#)

Co-Chair Stedman asked regarding Section 43.90.200(a).

Mr. Van Tuyl informed that the subsection was related to subsection (b), in that subsection (a) required the licensee to accept the FERC certificate and (b) mandated the licensee to advance the project regardless of cost.

[10:34:32 AM](#)

Senator Dyson reminded of the congressional act that stated that the Alaska natural gas pipeline was a necessary pipeline in the nation's best interest. The declaration that the pipeline was in the national interest included the "veiled threat" that the federal government would take over the construction process in the event that the State failed to secure a gasline. He asked if that fact would alter the current negotiations.

Mr. Van Tuyl shared both the federal and State governments' desire to complete a natural gas pipeline. He advised that the conditioned FERC certificate could, in the most extreme case, render the project completely uneconomical. It could also result in a major increase in the tariff. BP could devise a method to reduce the toll increases, but would need the ability to negotiate with FERC to achieve those results.

[10:36:49 AM](#)

Co-Chair Stedman returned to page 7 of the handout, and the bullet point labeled ".150(a)", for explanation.

Mr. Van Tuyl likened the release of proprietary information to a "winners curse", as the winning bidder would be required to provide all information relating to the project to its competitors after the license was awarded. This may cause a bidder to omit certain technological or other advantages in the application process.

[10:38:10 AM](#)

Co-Chair Hoffman opined that the requirement seemed reasonable. He asked if BP had discussed that concern with the Administration.

Mr. Van Tuyl recalled that the language was added during the legislative process, although had not been discussed with the Administration.

[10:38:55 AM](#)

Senator Thomas was unclear of how the licensee would be put at risk by the release of proprietary information after the license was awarded.

Mr. Van Tuyl exemplified "trenching" technology BP had developed and would include in a confidential application. That technology, however, was proprietary knowledge that would benefit BP's competitors worldwide if it was made public.

[10:40:09 AM](#)

Co-Chair Stedman next characterized Section 43.90.130 as the Administration's "must haves".

Mr. Van Tuyl set forth that paragraph (13) referenced FERC Order 2005 [157.34(c)(8)]. The FERC requirement was two-fold, first requiring that the licensee offer service to in-State delivery points, and secondly to offer distance-sensitive rates to those delivery points. BP did not object to the FERC requirements, but was wary of the implication in testimony by the Administration that the language in AGIA actually reserved capacity, which would exceed the FERC requirements and impose "unreasonable commercial risk".

[10:42:04 AM](#)

Co-Chair Stedman asked for confirmation that BP would not object to the requirement for distance-sensitive rates.

Mr. Van Tuyl affirmed.

[10:42:19 AM](#)

Co-Chair Hoffman allowed that the Administration may have claimed that capacity would be reserved for in-State distribution, but asked if that was specified in the language of the bill.

Mr. Van Tuyl was concerned with the potential interpretation of the language.

[10:43:03 AM](#)

Senator Thomas asked if the concern was with the provisions of Section 43.90.130(6)(B).

Mr. Van Tuyl explained that the issue was with the language that referenced "firm service", and BP was concerned that the mandate could be interpreted to go beyond the FERC requirement.

[10:43:59 AM](#)

Senator Huggins communicated that Mr. Van Tuyl was referencing language relating to the State's "royalty in value, royalty in kind" take contained in the House of Representatives' version of the bill. He read the language into the record as follows.

...eliminating the ability of the State to take its royalty in kind for gas in the quantity and volume committed to a firm transportation capacity acquired during the first binding open season.

Senator Huggins shared that the provision went on to state that in this case, the pipeline licensee would then be required to provide for the "in kind" requirements within the state. He asked if Mr. Van Tuyl was familiar with that language.

Mr. Van Tuyl recalled that an amendment to insert this provision was offered in the House Resources Committee.

Senator Huggins asked Mr. Van Tuyl's position on the amendment.

Mr. Van Tuyl would review the language and provide the Committee with a response at a later date.

Senator Huggins commented that it was "interesting language" that could address the RIV/RIK issue.

[10:45:29 AM](#)

Senator Thomas asked if Section 43.90.130(1)(B) on page 3 of the bill would speak to the concern.

[10:46:14 AM](#)

Mr. Van Tuyl understood that the provision in paragraph (1)(B) addressed a different issue than the in-state delivery points required by the FERC order. Paragraph (1)(B) did, however, represent another concern, as BP was unsure that it would have the required information prior to the application deadline.

[10:47:02 AM](#)

Senator Dyson surmised that FERC demonstrated a preference to rolled-in rates over negotiated rate increases in order to stimulate future exploration. Presentations to the Committee by various parties had indicated that pipeline expansions would not cause rates to increase over initial shipping tolls until "looping" was required, and then could increase no more than 15 percent over the original rate. He asked for Mr. Van Tuyl's position.

Mr. Van Tuyl explained that BP had "no problem" with rolled-in rates, as that was required by FERC for this project. FERC articulated its limited support of rolled-in rates, which extended to just before the point of creating a subsidy to expansion shippers by the original shipper. The language of Section 43.90.130(7) would not address the subsidization issue, and was contrary to FERC rules. That subsection would treat affiliates and non-affiliates differently, and create a subsidy for expansion shippers by eliminating negotiated rate protections. This was of "major concern" to BP.

[10:50:46 AM](#)

Senator Dyson judged that the intent of Congress, as reflected by the position of FERC, was to avoid the establishment of a "monopoly" pipeline. Due to the exorbitant costs of pipeline construction in Alaska, it was unreasonable to expect a competing pipeline to be built, as was a common occurrence elsewhere in the country. Therefore, the FERC regulations for the Alaska natural gas pipeline were created in an attempt to treat the gasline as a "common carrier", accessible for a fair price to new shippers. He asked why the State should manage the gasline differently, and whether the assurance that rates to the initial shipper would not increase more than 15 percent over initial rates was "any help".

[10:51:53 AM](#)

Mr. Van Tuyl responded that BP viewed the situation differently. He understood that FERC had the regulatory authority to promulgate different rules for the Alaska natural gas pipeline, as the circumstances in Alaska were unique. BP supported the FERC regulations. The company's concern was that the State was instituting additional regulations and rules on the construction of the pipeline. He favored FERC jurisdiction over regulation by the State of Alaska. He foresaw the 15 percent limit on the rate

increase as unpredictable and opined that it potentially represented an amount much greater than 15 percent.

[10:53:57 AM](#)

Senator Dyson asked if prior reference to AGIA's "exclusivity" was indicative of an assumption that only one natural gas pipeline would be built in the state.

Mr. Van Tuyl disagreed. The concern was that only one entity would be able to advance the pipeline project, as AGIA provided for the award of one license.

Senator Dyson commented that federal loan guarantees were available for more than one project, and assumed that the question was whether the State project coordinator could serve on multiple projects.

Mr. Van Tuyl allowed that this was a "fundamental difference" between AGIA and federal law.

[10:56:28 AM](#)

Senator Thomas recalled that the Canadian policy employed rolled-in rates.

Mr. Van Tuyl affirmed.

Senator Thomas calculated that the discussion of rolled-in versus incremental rates applied to approximately 22 percent of a 36,000 mile pipeline.

Mr. Van Tuyl set forth that the rate would apply to the Alaska section of the pipeline and any portion built in the continental United States.

[10:57:20 AM](#)

Co-Chair Stedman asked for more information regarding the Canadian rate structure and rates of return.

Mr. Van Tuyl was "not a FERC or an NEB expert" but understood that the Canadian NEB (National Energy Board) had adopted the use of rolled in rates for pipeline expansions.

10:58:18 AM

Mr. Van Tuyl stressed that the demonstration of a project's economic viability required under Section 43.90.130(2)(C-D) was "impossible".

Co-Chair Stedman asked Mr. Van Tuyl to speak to this provision in reference to mega-projects, and whether it would impede or enhance such a project.

Mr. Van Tuyl responded that as a project matured, it would provide a "better sense" of the technical and commercial viability. An investor might not initially understand the market, but would make a determination of reasonable probability of success, and expend the resources to mature the project and gain more specificity regarding the variables. The project would advance in steps, or pass through "gates" of maturity.

11:01:34 AM

Co-Chair Stedman asked if a consortium of companies that planned to develop a mega project would typically employ an outside consultant to conduct the analysis, or if that process was unique to BP.

Mr. Van Tuyl replied that other companies had similar "gated processes". One firm that provided consultation and analysis was IPA, or Independent Project Analysis. That company emphasized a disciplined, gated approach, especially for mega projects.

11:02:39 AM

Co-Chair Hoffman recalled learning about gated evaluation criteria for mega projects in a legislative seminar the previous summer.

Co-Chair Stedman was "trying to put these pieces together." He asked if the commitments required under AGIA would circumvent standard industry practice or compliment it.

Mr. Van Tuyl answered that the provisions of Section 43.90.130(2)(C) and (D) were inconsistent with the gated process. An applicant would be unable to demonstrate the economic viability of the project because the project had not

yet progressed to the "gate" at which viability could be determined.

[11:04:10 AM](#)

Senator Huggins asked the amount of time that would be required to produce a "bottoms up" cost analysis.

Mr. Van Tuyl informed that the 2001/2002 cost estimate required 18 months and \$125,000. That analysis required extensive field work and research, but was mandated to effectively "mature" a project.

Senator Huggins shared his concern that the legislature was operating on "blind faith" that the AGIA process would work. He was unsure that the current version of the bill was compatible with the expectations of the industry.

[11:06:52 AM](#)

Senator Thomas pointed out that the request for a design description and other basic application criteria was simply a method for the State to evaluate the different applicants' propositions. He understood that "proving" the economic merits of the project could be challenging, but was only one aspect of advancing the project. An applicant would be required to provide a project plan to the State before the State could find it reasonable to grant a license to any party. The application requirements were simply the beginning point of this process.

[11:08:40 AM](#)

Mr. Van Tuyl replied that BP would like to be a part of that application process, but would not be able to submit a bid under the current requirements.

[11:09:24 AM](#)

Senator Elton read the second bulleted point on page 6 as "BP will not submit a bid under AGIA". He asked if BP would submit an application for the AGIA license if the ten points addressed in this presentation were amended to be acceptable to BP.

Mr. Van Tuyl stressed that it would be the "intent" of BP to submit a bid if all concerns were addressed, including the three broad concerns listed on page 9.

[11:10:22 AM](#)

Senator Elton identified a difficulty in addressing the bulleted points to conform to BP's requests without a commitment from BP that the broad points would not be later cited as further reason to withhold a bid under AGIA.

Mr. Van Tuyl reported that the two bulleted pages were the explanation of why BP would not bid under AGIA. If those points were addressed, BP would reexamine the application process.

[11:12:41 AM](#)

Senator Elton advised that the assurances of FT commitments that BP stated would be required to allow the company to submit an application under AGIA were not included during the prior negotiations under the Stranded Gas Development Act (SGDA) either. He could identify no additional certainty for the construction of a pipeline under AGIA than under the previously negotiated SGDA.

Mr. Van Tuyl shared the same concern. That concern motivated BP to divulge what it identified as weaknesses in AGIA.

Senator Elton asked if BP was more comfortable with the SGDA application process than with that of AGIA.

Mr. Van Tuyl reminded that the SGDA application process was never completed.

[11:14:36 AM](#)

Co-Chair Hoffman pointed out that the stipulated 36 month time frame for the first open season in Section 43.90.130(3)(A) had not been mentioned. He asked if that the timeframe was reasonable and if the length of time could possibly be diminished.

Mr. Van Tuyl reiterated that BP had many concerns with AGIA that were not included on the list of "key concerns". The "time certain" components of AGIA were troublesome to BP. In the

2001/2002 cost study BP had declared its intent to hold the first open season within approximately two years. Thus, 36 months was a reasonable timeframe. He reiterated that date-specific commitments were a bad practice in advancing large projects.

[11:16:49 AM](#)

Co-Chair Hoffman assumed that aspects of Section 43.90.170 on page 11 of the bill would also need to be addressed.

Mr. Van Tuyl affirmed.

[11:17:23 AM](#)

Senator Dyson expounded on the importance of accelerating Alaskan gas production and asked if BP could provide a timeline of optimal gas "offtake" from Prudhoe Bay.

Mr. Van Tuyl was unsure.

Senator Dyson asked if he would be able to tell the Committee if he did know.

Mr. Van Tuyl was not sure that he would be permitted to share that information if he had it.

Senator Dyson cautioned that while the State was motivated by financial concerns to construct a natural gas pipeline as soon as possible, the producers were motivated by the dynamics of reservoir economics, and the two driving forces could be on different schedules.

[11:19:23 AM](#)

Mr. Van Tuyl stated that the concern regarding Section .130(2)(B) and Section 43.90.210 was that although the sections were patterned after the FERC regulation, they were markedly different from the FERC directives. Due to the fact that the applicant may not have the best information available at the time of application, the FERC regulations require a "good faith estimate" to describe the process, and allow for subsequent modifications. AGIA, however, required a detailed description, and would then prohibit deviation from that proposal as more complete information became available.

[11:20:59 AM](#)

Senator Dyson understood that BP participated with Conoco-Philips in the Rockies Express pipeline. That pipeline construction contract included a protection against cost-overruns. He asked how that protection operated.

Mr. Van Tuyl had "limited knowledge" of the project. BP was a participant and had committed to capacity on the pipeline. That project was comprised of three levels of negotiated rates to shippers.

Senator Dyson clarified that he was interested in the mechanism for managing construction cost overruns.

[11:22:39 AM](#)

Co-Chair Stedman asked Mr. Van Tuyl to provide that information to the Committee.

Mr. Van Tuyl agreed.

[11:23:10 AM](#)

Senator Thomas read Section 43.90.210. Amendment of or modification to the project plan., into the record as follows.

Subject to the approval of the commissioners, a licensee may amend or modify its project plan if the amendments or modifications improve the net present value of the project to the state, are necessary because of an order issued by the Alaska Oil and Gas Conservation Commission, or are necessary as a result of changed circumstances outside the licensee's control and are not reasonably foreseeable before the license was issued.

Senator Thomas judged that section to be reasonably accommodating, and asked BP's apprehension to the provision.

[11:24:22 AM](#)

Mr. Van Tuyl argued that the AGIA provision was "fundamentally different" from the FERC regulation, which recognized that the best information was not always available, and that market

demands are a reasonably foreseeable event that might result in a project change. AGIA would not permit such deviation from the original design.

[11:25:13 AM](#)

Senator Huggins asked the location of that stipulation in Section 43.90.130(2)(B).

Mr. Van Tuyl informed that Section 43.90.130(2)(B) required the provision of a detailed description of the project, including design capacity and receipt delivery points. He continued that BP would not know those specific details until the conclusion of the first open season.

Senator Huggins countered that assumptions must be made when compiling application data. He asked if Mr. Van Tuyl found this expectation unreasonable.

Mr. Van Tuyl characterized it as "absolutely reasonable", and told that FERC Order 2005 required a good faith estimate akin to Senator Huggins' comment.

[11:26:56 AM](#)

Senator Dyson observed that BP had not stated a need to control the construction of the pipeline, as other oil producing companies had. He understood that producers had been financial participants in pipelines, but that none of the major producers in the state had played a management role.

Mr. Van Tuyl assured that BP would like to build the Alaska natural gas pipeline. BP would contribute unique skills, such as experience in building mega-projects around the world, financial resources, and the "commercial motivation" to deliver a pipeline at the lowest possible cost. BP had experience in building and owning a pipeline in the Gulf of Mexico. Other North American examples may be available upon research.

[11:30:25 AM](#)

Senator Dyson asked the "dollar size" of the Gulf of Mexico project.

Mr. Van Tuyl did not have that information.

Senator Dyson judged that the Gulf of Mexico project did not compare to the proposed Alaska gasline project.

Mr. Van Tuyl agreed.

Senator Dyson perceived as common practice producers hiring an experienced pipeline company to build and manage a pipeline project.

Mr. Van Tuyl contended that it was more typical for the producing companies to participate in a pipeline project that would open a new basin, due to the risk associated with such endeavors. He characterized the Alaska gasline as a "basin opening" project.

[11:31:55 AM](#)

Senator Olson asked if BP was a participant in the Alliance Pipeline project.

Mr. Van Tuyl did not know.

[11:32:26 AM](#)

Senator Elton asked if BP would participate in building the pipeline if Exxon Mobil refused to take part in the project.

Mr. Van Tuyl was unsure of Exxon Mobil's position, but assumed that a successful project would require participation by the producers as well as the host government.

[11:33:25 AM](#)

Senator Elton relayed that Rex Tillerson, CEO of Exxon Mobil, had announced that the Alaska natural gas pipeline could not be completed without "fiscal durability".

Mr. Van Tuyl agreed that appropriate fiscal terms must be negotiated to encourage FT commitments and a successful open season. The current version of AGIA did not provide "appropriate" fiscal terms.

Senator Elton surmised that this concern should appear on the list of key issues provided in BP's presentation and handout.

[11:34:43 AM](#)

Mr. Van Tuyl clarified that fiscal terms would need to be defined to ensure FT commitments and a successful open season, and that concern was highlighted on pages 6 and 9. He suggested that the State allow the producers to propose fiscal terms for the State to review, and either accept or reject.

[11:36:04 AM](#)

Co-Chair Stedman reminded that the tax on gas was set at 22.5 percent under the Petroleum Profits Tax (PPT). The failed contract negotiated by the Murkowski Administration had proposed a different tax. "Progressivity" was applied to oil profits but not gas profits, as the gas was to be taken in kind. He understood Mr. Van Tuyl's comments to indicate a desire to revisit the issue of gas taxes and the period of tax certainty prior to the first open season.

Mr. Van Tuyl stated that BP would like to have that conversation "as soon as possible", as a resolution of those issues would provide for more informed decisions about the future. The duration of the tax guarantee was important, as BP expected the FT commitments to be much longer than the ten years currently proposed. Other elements of government take also needed to be addressed to provide fiscal certainty.

[11:38:18 AM](#)

Senator Elton asked if Mr. Van Tuyl was avoiding referencing "oil" in his comments on fiscal certainty.

Mr. Van Tuyl assumed that fiscal certainty would include oil, but would be willing to engage in negotiations.

Senator Elton asked if BP would require a fiscal certainty guarantee to be reached before participating in the application process.

Mr. Van Tuyl suggested that if fiscal certainty was not determined prior to the commencement of the application process the resource owners be allowed to include a tax structure proposal in their applications under AGIA.

[11:39:29 AM](#)

Co-Chair Stedman asked regarding the 70:30 debt to equity ratio. The State would support a lower equity position to reduce the tariff and enhance the value to the State. He asked BP's position on the 70:30 ratio.

Mr. Van Tuyl revealed that BP agreed with the State objective to achieve a low tariff, as well as a low construction cost for the project. The concern was that AGIA would prescribe the rate-making structure, which may deter lenders, thus affecting the financing of the project.

Mr. Van Tuyl continued that the rate-making requirements differed from the capital structure that a pipeline builder would arrange with its lender. A lender may require for a project to be comprised of greater than 30 percent equity, yet the toll imposed on shippers would be equal to a maximum of 30 percent equity. BP was unsure that that tax structure would allow the pipeline company to generate sufficient revenue to meet the lenders' long-term requirements.

[11:42:00 AM](#)

Co-Chair Stedman identified three components of the debt to equity issue: the State requirement under AGIA, the lender requirement, and the FERC tariff. He asked if FERC could set the rate regardless of the debt to equity ratio.

[11:42:37 AM](#)

Mr. Van Tuyl responded that the rate set by FERC may not reflect the structure agreed upon in the financial markets. BP preferred to allow the applicant to respond to the identified State need rather than setting inflexible requirements. The State would always have the option to reject an application that was insufficient at meeting the State's needs, and the applicants would have more latitude in crafting a proposal that would be acceptable to the potential financiers.

[11:43:45 AM](#)

Co-Chair Hoffman noted that the \$500 million matching contribution provided for in Section 43.90.130(18) on page 9 had

received significant attention. He asked BP's position on this provision.

[11:44:21 AM](#)

Mr. Van Tuyl replied that BP had not suggested the inclusion of the \$500 million match, and did not intend to pursue those dollars.

[11:44:35 AM](#)

Co-Chair Stedman asked why BP would not accept the \$500 million incentive.

[11:44:52 AM](#)

Mr. Van Tuyl answered that while the BP shareholders would likely approve of the incentive, it was not a requirement for BP to advance the project. The "establishment of resource terms with certainty" was the single largest enabling event to the construction of a natural gas pipeline.

[11:45:42 AM](#)

Co-Chair Hoffman summarized that BP had not asked for the \$500 million, but would accept it.

[11:45:44 AM](#)

Mr. Van Tuyl declared the intent of BP was to not require State money to further the project.

[11:46:03 AM](#)

Senator Dyson understood the assumption of Congress and FERC was that only one pipeline would be built. The possibility of a producer-owned pipeline had raised antitrust issues. He asked the State's possible exposure to antitrust actions.

[11:47:26 AM](#)

Mr. Van Tuyl deferred to Mr. Coughlin.

[11:47:36 AM](#)

Mr. Coughlin informed that BP's analysis of the issue revealed no antitrust concerns, due to the fact that the competition would exist in the downstream markets serviced by the pipeline. Additionally, FERC would regulate the monopoly of the pipeline by granting a license to an applicant. While this could in other cases create an antitrust issue, the concern was abated by the governmental agency involvement. FERC insured against antitrust claims by regulating both the downstream and upstream aspects of the pipeline functions to protect against a monopoly of services.

[11:49:22 AM](#)

Senator Dyson inferred that FERC was more concerned with the upstream access issues than with downstream competition. He asked for a "synopsis" of antitrust concerns that had emerged in other North American pipelines, particularly pertaining to upstream access issues.

[11:49:55 AM](#)

Mr. Coughlin was not aware of any antitrust actions relating to upstream activity. The regulation of pipelines had changed dramatically since 1984 when federal law was amended to allow producers to own pipelines.

[11:51:00 AM](#)

Senator Dyson assumed that FERC's "predisposition" for rolled-in rates was an indication that FERC endeavored to address access for new explorers, and prevent pipeline owners from discriminating against new explorers in an attempt to control production in the basin.

[11:51:43 AM](#)

Mr. Coughlin responded that FERC Order 2005 attempted to balance two contradictory goals. The first goal was to get a pipeline built. To finance the construction, rate certainty must be offered to initial shippers. The second goal was to ensure that new explorers would have access to the pipeline, especially because it would likely be the only pipeline in the basin. FERC Order 2005 was an attempt to balance the two goals. The balance was reached by including a rolled-in rate provision and by providing the initial shippers the guarantee that expansions to

accommodate new discoveries of gas would not result in initial shippers "subsidizing" expansion shippers.

[11:54:25 AM](#)

Co-Chair Stedman asked regarding the viability of loan guarantees.

[11:54:36 AM](#)

Mr. Van Tuyl stated that BP was interested in loan guarantees, as they would reduce the cost of the pipeline. There existed uncertainty as to the rules of access to the loan guarantees, which had not yet been established by the federal Department of Energy. Loan guarantees would be dependent upon other factors such as completion guarantees and negotiated FT commitments, stipulations he considered "entirely reasonable".

[11:55:55 AM](#)

Co-Chair Hoffman shared that the loan guarantees were established when pipeline cost was estimated to be \$20 billion. Current estimates for completion were approximately \$30 billion. He asked if the previous rates were still considered adequate.

Mr. Van Tuyl informed that the provisions of the loan guarantee program recognized the project cost escalations.

[11:56:47 AM](#)

Senator Thomas spoke of a presentation by the Alaska Oil and Gas Conservation Commission (AOGCC) that detailed the reported known reserves in the State. This presentation indicated that while BP had expended money to confirm reserves in other parts of the world, it had not done so in Alaska for several years. He asked what measures BP had taken to confirm reserves in this state.

[11:58:10 AM](#)

Mr. Van Tuyl answered that Alaska was a mature oil field. The majority of exploration and discovery was done in prior years. Basins typically declined in a pattern known as a "creaming curve", in which large reserves were identified first, and subsequent discoveries become smaller and smaller over time. The "green mountain" graph on pages 2 and 10 of the handout

illustrated this trend, as well as the potential for "significant future adds" to those reserves, such as heavy oil. This opportunity would not be displayed as a known reserve at this point. BP was also examining the possibility of opening new fields, but reminded that Alaska was a mature basin and the prospect for new adds was not significant.

[11:59:37 AM](#)

Senator Thomas clarified that his inquiry was to the measure BP had taken to confirm the volume of gas in the Prudhoe Bay area.

[12:00:07 PM](#)

Mr. Van Tuyl acknowledged 35 trillion cubic feet of known gas in that area, as well as additional volume in Endicott, North Star and other fields. United States Geologic Survey (USGS) estimates suggested that other large reserves may exist in the State. BP was not currently exploring for new volumes of gas, but construction of a gas pipeline would lead to further exploration.

#

ADJOURNMENT

Co-Chair Bert Stedman adjourned the meeting at [12:01:55 PM](#)