

MINUTES
SENATE FINANCE COMMITTEE
April 28, 2007
1:44 p.m.

CALL TO ORDER

Co-Chair Bert Stedman convened the meeting at approximately [1:44:43 PM](#).

PRESENT

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

Also Attending: TONY PALMER, Vice President, Alaska Business Development, TransCanada Corporation and Chief Executive Officer, Foothills Pipe Lines Limited; BILL WALKER, Project Manager & General Council, Alaska Gasline Port Authority; PAUL FULS, Legislative Liaison and Advisor, Alaska Gasline Port Authority; MILES BAKER, Staff to Senator Stedman; ANNETTE KRIETZER, Commissioner, Department of Administration

Attending via Teleconference: There were no teleconference participants

SUMMARY INFORMATION

SB 104-NATURAL GAS PIPELINE PROJECT

The Committee heard testimony from representatives of TransCanada Corporation and the Alaska Gasline Port Authority. The bill was held in Committee.

SB 125-PERS /TRS CONTRIBUT'NS; UNFUNDED LIABILITY

The Committee was provided an explanation of a new committee substitute by Co-Chair Stedman's staff and the Department of

Administration. The committee substitute was adopted and the bill was held in Committee.

#sb104

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."

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

Co-Chair Stedman stated that the first order of business today would be a presentation from TransCanada Corporation about the Alaska Gasline Inducement Act (AGIA). He asked that the testimony address "the interconnection between TransCanada and Foothills Pipe Lines Limited", one of its subsidiaries operating in the State.

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TONY PALMER, Vice President, Alaska Business Development, TransCanada Corporation [TransCanada] and the Chief Executive Officer, Foothills Pipe Lines Limited, explained that Foothills, which is owned by TransCanada, has been "the licensee in Canada for this project" for approximately 30 years.

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Mr. Palmer identified TransCanada as "the largest interstate natural gas company in North America". Its holdings include 36,500 miles of large inch interstate/inter-provincial pipelines. The 50 year old company transports 15 billion cubic feet (BCF) of gas each day.

Mr. Palmer informed the Committee that TransCanada was originally formed to construct a pipeline from the province of Alberta in western Canada to eastern Canada. That pipeline is longer than the pipeline that would be constructed from Prudhoe

Bay to Alberta. When the original pipeline began service in 1958, it initially transported 300 million cubic feet (MCF) or approximately one-third of a BCF, each day.

Mr. Palmer specified that the daily volume transported today is seven BCF. In order to handle this increased capacity, the original pipeline was "completely looped" by the addition of six parallel pipelines leaving Alberta. Product is now shipped to mid-west and north-east United States (U.S.) markets in addition to eastern Canada and Chicago. TransCanada moves two-thirds of western Canada's gas to market.

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Mr. Palmer noted that the original construction project included "a 'pre-build' for the Alaska Highway Pipeline System".

Mr. Palmer advised that TransCanada recently acquired a major U.S. pipeline interstate company, American Natural Resources (ANR). This has allowed TransCanada's system to transport gas north from the Gulf of Mexico to West Texas, Oklahoma, Michigan, Illinois, and Ohio markets.

Mr. Palmer stated that this history attests to TransCanada's "long-standing business of constructing and developing long distance pipelines as well as systems that are more gathering in nature" in that they move gas from gas processing and "conditioning plants to the borders of Alberta". "An independent pipeline model with rolled in tolls" was utilized to expand the original 250 mile long gathering system to one that will transport approximately 11 BCF each day via 15,000 miles of pipe.

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Mr. Palmer reiterated that the company has been involved in the effort to construct a gas pipeline to Alaska for approximately 30 years. The first section of the aforementioned pre-build was constructed in 1981. Another section was built in 1982 under the specifications of Canada's Northern Pipeline Act (NPA). Further expansions were made through 1998. Each section met NPA's standards that existed at the time of construction.

Mr. Palmer stated that, over the past 30 years, TransCanada has invested approximately two billion dollars in anticipation of

the project. The company holds "valid and exclusive certificates issued" under NPA for the Canadian section of the pipeline.

Mr. Palmer declared that these certificates were unusual in that they have no expiration date. In contrast, the terms issued by Canada's National Energy Board (NEB) propose a two year time period within which the proponents of the Canadian McKenzie project must begin construction or lose their license.

Mr. Palmer qualified that the open-ended certificate specific to the Alaska pipeline project is recognition of the national priority given it by both Canada and the U.S. The U.S. Federal Regulatory Commission (FERC) and the Canadian NEB approved project conditions "under their normal regulatory procedure". Both countries passed specific legislation for the project and both signed a treaty supporting the project. "Those terms and conditions are valid and effective today and are there for the benefit of the project in both countries."

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Mr. Palmer assured the Committee that "Alaskan gas arriving in Alberta we think will be attractive to the very liquid Alberta hub". The approximate 11 BCF of gas that moves each day through the Alberta hub attests to it being "the most liquid in North America". It is actively traded on the financial market and is significantly "more liquid than the Henry hub".

Mr. Palmer addressed the opportunities that would be available for Alaskan gas in the Alberta hub, including financial transaction accommodations. The expectation is that in ten years when the gasline was ready for service, "there would be sufficient spare capacity leaving Alberta" on TransCanada's and other's systems "to move the entire Alaska volume to market" in North America.

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Mr. Palmer stated that while TransCanada would welcome having long-term contracts for the use of its lines leaving Alberta, Alaska would have the option, as chosen by many of TransCanada's customers, to have short-term contracts. This option provides "significant flexibility" for customers "to choose markets day by day and optimize their systems and optimize their net backs year by year".

Mr. Palmer noted that during the 1990s, TransCanada invested \$14 billion into the construction of more than 7,000 miles of pipeline in Canada and the U.S. It was able to construct between 500 to 1,000 miles of line "each year on budget and on schedule". To put it in perspective, the length of the pipeline from Prudhoe Bay to Alberta would be approximately 1,750 miles.

Mr. Palmer stated that any Member desiring further information about the company's "cost and reliability record" could contact the Senate Resources Committee as this issue was thoroughly addressed during his testimony before that committee.

Mr. Palmer shared that TransCanada has paid for "a right-of-way through ... the entire Yukon for this project" since 1983. In 1993, TransCanada's rights were "recognized in the umbrella final agreement between each and every First Nation in the Yukon, the government of the Yukon, and Canada".

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Mr. Palmer qualified that this right-of-way easement is specifically identified "in each and every First Nation final land claim" that has been settled. It is expected to also be included in the two remaining First Nation settlement agreements. This matter was also thoroughly discussed in the Senate Judiciary Committee hearings.

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Mr. Palmer also advised that "the terms and conditions" of Canada's NPA agreement with TransCanada/Foothills as well as the terms and conditions of the treaty with Canadian First Nations and the benefits that would be provided to northern Canadians were also discussed during the Senate Judiciary Committee hearings. Examples of TransCanada's responsibilities include the "obligation to: consult with those parties", to provide training, entrepreneurial opportunities, and employment opportunities. They would also be required to provide gas "to certain communities with a financial contribution by TransCanada/Foothills".

Mr. Palmer also noted that the agreements specify that customers would be required to pay zonal tolls on sections of the pipe they use. A customer taking gas off the line in Whitehorse would

only be required to pay a toll on the pipe from Prudhoe Bay to Whitehorse. Property taxes and other things that must be paid are also specified in the First Nation treaties.

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Mr. Palmer finished the overview of the company and turned his attention to the AGIA legislation.

Mr. Palmer spoke of TransCanada's actions in recent years in support of an Alaska gasline project. They had not resist U.S. Congress' action on the Pipeline Act of 2004 legislation "despite, in our view, it being a clear work-around of our ANGTA [Alaska Natural Gas Transportation Act of 1976] rights and entitlements. TransCanada and our subsidiaries are the sole remaining partners in the original ANGTA partnership that was going to construct the pipeline in Alaska."

Mr. Palmer noted that TransCanada decided to take a position of compromise because they had "a significant position in the Canadian section of the project". The decision was made "not oppose that legislation when it was being considered by the U.S. Congress," even though it gave other parties the right to construct a pipeline through Alaska". It did not affect any pipeline in Canada. TransCanada concluded it would not resist the legislation if that's what "was needed to advance the project".

Mr. Palmer also noted that TransCanada "actively" responded two years prior to a request from former Alaska Governor Frank Murkowski's Administration, "to provide it with alternatives under the Stranded Gas Development Act (SGDA) framework".

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Mr. Palmer expressed that TransCanada had significant negotiations with the Murkowski Administration. While the discussions were productive, Governor Murkowski decided to "negotiate solely with the three producers and we stood aside".

Mr. Palmer advised that TransCanada began an effort to acquire State right of way status in June 2004. The application process was completed and submitted in February 2005. To date, the State has not made a determination on that application.

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Mr. Palmer reminded the Committee that TransCanada submitted written comments to the Legislature last year about the draft contract developed by Governor Murkowski and the three Alaska North Slope (ANS) producers. Those comments were limited to the Canadian section of the line only. While the remarks did not address the merit of the legislation, they did convey "a significant difficulty with that contract with regards to its treatment of Canada".

Mr. Palmer reiterated that TransCanada has "maintained and improved its rights to expedite the project in Canada" by its actions. For example, its 12 year effort to acquire 100 percent ownership of Foothills is beneficial because negotiations would only involve one party as opposed to numerous ones.

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Mr. Palmer also acknowledged "that the ANS producers control the majority of Alaska's proven gas reserves", under leases granted by the State decades earlier. Those parties have communicated "certain requirements before they will support a gas line arrangement". They have shared their requirements with the Legislature over the past several months.

Mr. Palmer pointed out, however, that "the State of Alaska has a sovereign responsibility to Alaskans and the State is also indicated certain objectives before the State will commit to a gasline arrangement". "To date, our observation is the producers and the State have not reached an acceptable agreement. There's in effect an impasse."

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Mr. Palmer concluded that Governor Sarah Palin has introduced the Alaska Pipeline Inducement Act (AGIA) in an effort "to advance the project. We support efforts to end the impasse and advance the project now." TransCanada continues to support getting a gas line project "in service expeditiously to serve North American markets because we believe that would be advantageous to Alaska, to America, and certainly to Canada and our company as well."

Mr. Palmer contended that gas consumers, the governments of both the U.S. and Canada, and the industry would be "best served by a large scale" trans-continental project that could transport approximately 4.5 BCF per day.

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Mr. Palmer reaffirmed TransCanada's preference for a five-party compromise to advance the project. This would include the three ANS producers, the State, and TransCanada. "Certain facts" must be considered: the producers do hold the gas under existing leases; TransCanada does hold the basis for expediting the project through Canada; and the State of Alaska is accountable for Alaska's long-run development and economic interests". TransCanada is prepared to compromise as evidenced by its willingness "to not insist on our past rights" in the State.

Mr. Palmer advocated for compromise amongst the five parties "in conjunction or parallel with the current AGIA process".

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Mr. Palmer directed his remarks specifically to AGIA. AGIA specifies that the State would provide "certain inducements to pipeline developers and gas producers". It also establishes specific application requirements under a request for applications (RFA) process. "TransCanada accepts the necessity of Alaska's initiative to implement a new process to meet its objectives".

Mr. Palmer shared TransCanada's concern to AGIA would require the licensee "to obtain a FERC certificate regardless of the outcome of initial open season". Independent pipeline developers might not participate in an AGIA RFA if this requirement was not amended.

Mr. Palmer continued. AGIA proposes a cost share between the State and the licensee: up to a 50/50 basis through initial open season and up to an 80/20 post-open season through the FERC certification. TransCanada supported the State's 50/50 cost sharing prior to an open season. However, private pipeline developers might be reluctant to commit monies to pursue a FERC certificate if the initial open season has not attracted enough gas commitments to make the project viable.

Mr. Palmer stated that while monies spent toward obtaining a FERC certificate could potentially save time if customers were ultimately found, the monies were at risk if the project did not proceed.

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Mr. Palmer pointed out that the State's circumstances differed from those of a pipeline proponent. "The pipeline proponent looks to the return it will receive on the capital it invests in the project. The State has many other avenues of revenue from this project other than simply royalties and tax collection." This would include the multiplier effect of employment and other development.

Mr. Palmer specified that as a pipeline developer, his focus was to "the money and the talent" required to invest in the project "and the risk that I take of committing that money and talent relative to return of that money over time, and a collection of an appropriate risk premium for the money that I commit". In TransCanada's experience, this would be the independent pipeline developer's only source of money.

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Mr. Palmer stressed that "the cost of pursuing the FERC certificate will be substantial". This activity "would not directly lead to customer commitments". Nonetheless, he assured the Committee that if the initial open season did "not secure sufficient volumes or credits", TransCanada "would continue to seek customers and credit for some reasonable period of time".

Mr. Palmer stressed, however, that they would prefer not to have our "talent and money committed to the dual efforts of a FERC certificate at the same times we're pursuing customers and credit".

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To that point, Mr. Palmer strongly recommended that consideration be given to amending language in the bill that required the licensee to work toward FERC certification "unless adequate shipper commitments or an alternate source of credit are in place".

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Mr. Palmer concluded his remarks by reiterating TransCanada's position "that the most expeditious and equitable path" through which to advance the gas pipeline project "is a collaborative arrangement" between the ANS producers, the State, and TransCanada. TransCanada also urges reconsideration of the FERC certification process. TransCanada's participation in AGIA would depend on the final form of the bill and the terms of the application process.

Mr. Palmer assured the Committee that TransCanada would continue to support the endeavor to reach "a five-party arrangement". If TransCanada was not the entity awarded the Alaska portion of the project, it would be willing "to vend" its substantial "rights and assets to the successful party that commercializes the project in Alaska ... under one condition and that is that they connect with us at the Canadian border".

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Co-Chair Stedman asked Mr. Palmer to affirm the company's ability to undertake this project.

Mr. Palmer responded that the company was capable of undertaking the project. However, the immensity of the project should be emphasized. While TransCanada has completed pipelines "much longer than this on time and within budget", a project of this magnitude would have "several forms of complexities". Capital costs, the 1,750 mile length of the project, and the fact that the project crosses two countries and numerous jurisdictions add to the complexity.

Mr. Palmer expressed that TransCanada's "long history of successfully developing complex projects and understanding and implementing the significant compromises that are needed between governments, customers, environmental issues, other stakeholders including First Nations and communities as well as commercial parties" speak to the company's ability to undertake the project.

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Mr. Palmer next addressed TransCanada's financial capacity. "With the U.S. federal loan guarantee for this project to cover

the debt", TransCanada's equity component specific to the Canadian portion of the gasline "is less than one year's cash flow". The company is "very well-positioned to construct this project" and would welcome having a role in the effort.

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Co-Chair Stedman asked Mr. Palmer to expand on TransCanada's position that "going to the FERC certificate through failed open seasons" might be "an impediment" to their applying for the AGIA license.

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Mr. Palmer considered the term "an impediment" to accurately portray TransCanada's position on this "significant issue". The application language in the final version of the bill would be carefully considered with specific attention to the likelihood of there being a successful open season.

Mr. Palmer stated that TransCanada's board of directors would thoroughly "examine the possibility of a successful open season" under the application language in the bill. Included in that discussion would be a review of "what further commitments" would be required of the corporation were insufficient volumes or credits attracted during the open season.

Mr. Palmer asserted that the company's 30 year history was indicative of its commitment to this project. "We intend to be there when this project is completed."

Mr. Palmer contended that if the open season's commitments were less than needed, the company would continue "to look for customers or credit". The Board would be interested in the level of talent and financial capacity that would be required of the company during the multi-year FERC certificate application period. This "would be a substantial commitment" of corporate funds. The State would also "have significant investment" during this time.

Mr. Palmer reminded the Committee that the State's perspective would differ from that of a pipeline proponent.

Mr. Palmer acknowledged that the bill's current FERC certificate language "was a significant hurdle" to the Corporation in respect to its "decision whether or not to apply".

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Co-Chair Stedman asked whether TransCanada had ever sought a FERC certificate after a failed open season or another similar scenario.

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Mr. Palmer was unaware of any such situation.

Mr. Palmer noted that 30 years ago when the original certificate for this project was granted, no open season had been conducted because it was deemed a national priority of both the U.S. and Canada.

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Senator Huggins acknowledged the consistency of TransCanada's concern "about a failed open season going to FERC certificate". He surmised that such a situation would be of concern to both the applicant and the State. He also agreed that "it's much more important to get gas in the pipeline than it is to go to a FERC certificate based on the parameters".

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Senator Huggins, a member of the Senate Resources and Senate Judiciary Committees, pointed out that the concern about the Federal loan guarantee was new since TransCanada's testimony on the bill before those committees.

Senator Huggins asked Mr. Palmer to comment on a hypothetical situation in which AGIA had been amended to address TransCanada's concerns about the FERC certificate and a failed open season. In this scenario, a company had acquired its FERC certificate but had not cemented its financing. In other words, the open season had not been successful.

Senator Huggins understood that the problem was that the five-year period provided in AGIA to acquire such financing did not mesh with the federal loan guarantee. It would expire two years

after the issuance of the FERC certificate if financing had not been acquired.

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Mr. Palmer appreciated the recognition of TransCanada's concern about the FERC certification. Regardless of whether new language was adopted, if TransCanada was successful in the effort to acquire the FERC certificate, but had not correspondingly secured project financing and the federal loan guarantee time period was about to expire, it and other stakeholders, including the State of Alaska, would seek a federal loan guarantee extension. "Any prudent party would be doing so".

Mr. Palmer declared that having the federal loan guarantee expire "would be a very significant event." Losing the federal debt support would require the company "to go solely to the public markets seeking debt support." Finding support to mirror that proposed by the federal government would be "a significant hurdle for any project of this scale".

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Mr. Palmer communicated it being unusual "that a project of this scale would be funded up to 80 percent debt". In addition, financing a project of this size typically "would require a higher coupon rate from just commercial parties than one that would be supported by the federal government".

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Senator Huggins stated that his remarks were intended to underscore TransCanada's position that acquiring the customer base was more important than getting the FERC certificate. For "the federal loan guarantee, as written today," would expire in two years regardless of "how good the FERC certificate is" if there were no customers. This strengthens "the importance of getting gas in the line".

Mr. Palmer affirmed that "attracting customers or credit is the most critical factor to make this project proceed".

Mr. Palmer referenced his earlier remarks about TransCanada's efforts to advance this project and the need for compromise among the parties involved. Even were compromises made, the

project "without customers and without credit" would not proceed. A pipeline applicant should not be required to acquire "a FERC certificate without having customers or credit".

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Senator Huggins asked how TransCanada might view the State's offer to provide \$500 million toward the project in return for some equity in the pipeline.

Mr. Palmer understood the intent of the State's \$500 million contribution toward the project was to, "in effect, reduce the capital costs of the project". Nonetheless, TransCanada would consider the proposal were the State's intent "instead to have that money included in the cost of the project and were seeking an equity position in the project for that contribution".

Mr. Palmer clarified however, that TransCanada would not be attracted to the State being a shareholder in the project if the money could not be applied toward project capital costs as currently specified in the bill.

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Senator Elton, who was hearing TransCanada's testimony for the first time, asked whether a copy of Mr. Palmer's remarks could be provided.

Co-Chair Stedman stated that the requested material would be made available.

Senator Elton asked whether TransCanada agreed with others that the construction phase of the project might take up to three years.

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Mr. Palmer concurred. Once all the required components, including customers and permits, were in place, the project could reasonably be constructed in two to three years. TransCanada estimates that one year of logistical pre-construction work and two years of construction work would be required.

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Senator Elton, in order to better understand the level of compromise that would be required, asked whether Mr. Palmer "suspected" that the State would be required "to compromise as much moving forward from this point as we did under Stranded Gas Development Act (SGDA)".

Mr. Palmer understood that the agreement reached on the SGDA worked for many of the involved entities, but not for the Legislature. TransCanada believes that the structure of this project "must work" for the people and government of Alaska, the three producers, TransCanada, and any involved stakeholder. "The degree of compromise the State needs to make has to be something" that the citizens and the State could support. The SGDA agreement did not garner such support.

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Senator Dyson asked for information about pipeline material strength; specifically the pound per square inch capacity that would be required to transport gas "in a super critical state". He also inquired to TransCanada's experience with such gas.

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Mr. Palmer stated that TransCanada's design plan for this project currently specifies "x80 pipe". This pipe would accommodate up to 80,000 lbs per square inch with "2,500 pounds of pressure on a daily basis". X80 was adopted as the company's pipe standard in 1995 and they have approximately 1,800 miles of it in use in North America.

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Mr. Palmer announced that TransCanada might decide to use x100 pipe on this project. It is also considering making this "next generation of pipe" its new standard. The company has been utilizing this Japanese or North American-manufactured pipe, since 2003 in Alberta and eastern Canada. It is lighter than x80 and therefore less costly to accommodate.

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Senator Dyson asked for assurance that these pipes could reliably transit Alaska's gas.

Mr. Palmer declared that x80 would be able "to manage that with no problem". The approximate 1,075 British Thermal Units (BTU) gas anticipated to leave Prudhoe Bay would be similar to the volume of gas transported in TransCanada's western Alberta pipelines today. He noted that Alberta currently has two gas processing facilities: one near the eastern edge of Alberta for gas heading to eastern regions and one near Calgary for gas headed toward western markets.

Mr. Palmer concluded that while x80 pipe would suffice, "x100 pipeline would simply mean a cheaper pipeline project."

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Senator Dyson asked whether TransCanada's "approach to this project" might change were "one of the State's off-take points" to remove gas liquids.

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Mr. Palmer responded that the owners and shippers of the gas would make the decision "as to where liquids would be removed".

Mr. Palmer specified that removing liquids at a terminus in Alaska "would be unlikely to change the pipe strength". It would however, reduce the number of "BTUs to spread the cost of the pipeline over" as costs are typically spread over the number of BTUs that "ultimately are going to the destination". For example, there would be a seven percent reduction in the number of BTUs over which to spread the cost were 75 BTUs removed from a 1,075 BTU gasline. He noted that stripping plants in Alberta typically remove 75 BTUs.

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Senator Thomas sought further discussion in regards to "the licensee and the loan guarantee"; specifically [unspecified] language that reads "the authority of the secretary to issue a federal guarantee in instruments under this section for a qualified infrastructure project shall expire on the date that is two years after the date on which the final certificate of public convenience and necessity including any Canadian certificates of public convenience and necessity is issued for the project".

Senator Thomas, referring to Senator Huggins's earlier hypothetical scenario on this issue, asked Mr. Palmer what he deemed to be the difference between an entity's holding "a license on one hand and the certificates of convenience in Canada and in Alaska".

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Mr. Palmer stated that TransCanada defined the term "license" as the license Alaska would grant under AGIA. TransCanada believes that approximately 12 months following the completion of a successful application process, "the State of Alaska would be granting a license under AGIA".

Mr. Palmer continued. The certificate of public convenience and necessity (CPN) is a FERC certificate. This is referred to as either a NEB" or "NPA" certificate in Canada. TransCanada currently holds an NEB for this project in Canada. It also possesses a FERC certificate under ANGTA. To that point, he noted that, as referenced earlier by Senator Huggins, TransCanada has requested a "technical amendment" that would allow TransCanada, if they chose to participate in AGIA, to acquire the certification needed to pursue the project in Alaska.

Mr. Palmer reviewed the process the successful licensee must conduct in order to obtain their certificate of public convenience and necessity. The process, which is anticipated to take approximately five years, includes conducting an open season, submitting a FERC application, and undertaking the associated multi-year FERC certificate process.

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Senator Huggins addressed the project timeline. AGIA currently specifies a 36 month open season. The licensee would be required to submit their FERC certificate application by year five. The ensuing FERC certificate process would take approximately two years. Thus, an entity could be granted a FERC certificate by year seven. The federal loan guarantee, as currently specified, would expire in year nine if financing had not been arranged.

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Co-Chair Stedman asked TransCanada's position on the legislation's "debt to equity ratio requirement of a maximum equity position of 30 percent".

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Mr. Palmer advised that TransCanada was comfortable with the maximum 30 percent project equity position under the current AGIA structure and the availability of the federal loan guarantee.

Co-Chair Stedman asked whether TransCanada "would be comfortable" with that maximum being lowered to a 20 percent equity position.

Mr. Palmer stated that the corporation would "be willing to look at something different than 30"; however, their opinion is that "20 percent is too low for the risk of this project".

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Co-Chair Stedman asked TransCanada to comment on the issue of "rolled in verses incremental rates". A rolled in rate structure is specified in Section 1, Sec. 43.90.130. Application requirements. subsection (7) on page 6 beginning on line 11 of the bill.

Mr. Palmer responded that TransCanada supports the utilization of a rolled in rate structure for AGIA. Rolled in rates are standard in Canada.

Mr. Palmer disclosed that TransCanada conducted an analysis of the pipeline system they designed for this project. That analysis indicates that, were the initial pipeline volume 4.5 BCF a day, "the rolled in tolls, up to 7 BCF, would not" exceed the initial 4.5 BCF a day rates. Their determination is that "this is not a significant issue for this project" in respect to a 50 percent expansion over the initial volume.

Senator Dyson understood the rolled in rate standard has worked well in Canada. If an original shipper determined they were subsidizing new shippers, they could appeal to the NEB. Historically, the determination has been that the rolled in rate process had "not been detrimental" to the original investors or inhibited the process.

Mr. Palmer considered Senator Dyson's summary of the rolled in rate process experience in Canada to be a "fair characterization".

Mr. Palmer again spoke in support of the ability to compromise. Compromise is often "required from parties that are shippers on the pipeline as well as the pipeline company". In his experience, the ability to compromise is important, especially for "the long run interest for a project that is going to be likely a single source pipeline for a very long time".

Mr. Palmer reviewed the success of the rolled in rate structure for TransCanada's pipeline in Canada, which is also a single source pipeline. Rather than precluding development, "it has encouraged" it.

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Nonetheless, Mr. Palmer acknowledged the concern of initial shippers. "They don't want to be in a position where it's all one-sided for future customers". Every pipeline company looking to the future wants to attract new customers while also "want[ing] to be fair to those initial customers".

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Mr. Palmer stated that initial shippers would be unfairly treated were a pipeline they had firm 25 year shipping commitments with at a particular tariff to "allow interruptible customers to get service on a daily basis at half that rate" two years later. This action would advantage the interruptible customers in the gas marketplace. A pipeline company should favor long term firm commitment customers as they would help get the pipeline built, would financially support the day to day operations of the pipeline, and would promote expansion and development over time.

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Senator Huggins asked whether pipeline companies were forced to negotiate rates with shippers.

Mr. Palmer deemed it "normal on a new project that negotiated rates", in many different forms, would be considered. This would

include such things as "a differing collection of depreciation over time" and even "fixed tolls". He noted however, that negotiating fixed tolls on this project, with its significant level of risk, would be unlikely. FERC also has toll requirements that must be adhered to.

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Senator Huggins was surprised to have recently heard an economist project a gas pipeline tariff rate, excluding the gas treatment plant, of \$1.65. He asked TransCanada whether that or any rate could be calculated at this stage of the project with certainty.

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Mr. Palmer communicated that TransCanada and likely any entity that has studied this project have estimates of what levels of tolls and tariffs would be required. However, at this stage, those estimates are simply "assumptions" based on such things as projected capital costs, operating costs, volumes, taxes, and expectations of when the project would begin service. The calculations would be updated prior to the open season process, and would be further refined as that process unfolded. The licensee would desire the most accurate toll and tariff estimates possible in order to "advance proposals to potential customers". Therefore, the fact that an economist had calculated a tariff rate was not unusual.

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Senator Huggins asked to the reliability of that \$1.65 tariff estimate.

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Mr. Palmer discussed actions that a project developer might be required to do to attract customers to a "binding open season. This would include such things as presenting "a fixed range" of tariff estimates. Oftentimes, negotiations include language specifying that the agreement would be binding on the customer if "the toll was not increased more than 25 percent". If the tariff exceeded that range, the customer could withdraw by a certain date.

Mr. Palmer noted however, that the project would not necessarily be considered "a failure" that if tariff costs increased beyond that 25 percent range. Customers might still consider the project "the best possible alternative in the marketplace and might reaffirm their commitment". Nonetheless, if they withdraw, the project manager would have "lost the money between the time where we committed, and the time where they've withdrawn". That is a risk for the project manager.

[2:50:42 PM](#)

Senator Thomas asked TransCanada to comment on "the concept that all risk is ultimately passed to the resource" providers.

Mr. Palmer did not support that concept. Shareholders as well as debt holders believe they take risks. The question is "who takes what risk in which projects". For example, the monies TransCanada has committed to this project to date "are at risk" as are the monies they might spend on the AGIA license as they "might not be the successful applicant".

Mr. Palmer argued that, even if they were successful, "there is a reason" that pipeline companies are required to have up to 50 percent equity. "It's because we have risks". Otherwise, projects would be funded with 100 percent debt or substantially lower financing costs. Unfortunately no bank is willing to do that. They always ask "pipeline shareholders to take the risk".

Mr. Palmer continued. Pipelines face regulatory, volume, and operating risks. "Rigorous debates" occur between pipeline and regulatory entities in regards to the "degree of risk they should take and what the appropriate return should be".

[2:53:20 PM](#)

Senator Dyson voiced that "some of the producers" think they should "control and build the pipeline because they only can manage the pipeline and not have cost overruns that would reflect on the tariff" against their company. To that point, he asked what pipeline constructors could do to protect shippers from construction cost overruns.

[2:54:11 PM](#)

Mr. Palmer opined that "potential" AGIA competitor could match TransCanada's track record for constructing and operating large regulated pipeline projects over long distances in a cold climate environment.

Mr. Palmer stated that the conditions surrounding the original North Slope gas pipeline project, 30 years ago, required the participating pipeline company to take "a portion of the capital cost risk". While TransCanada could commit to a maximum 30 percent equity, it could not commit to 100 percent of the capital cost risk because "of the likely return for a regulated pipeline" it would receive.

Mr. Palmer reminded the Committee that, unlike gas producers and the State, a pipeline owner does not benefit from increasing gas prices.

[2:56:33 PM](#)

Co-Chair Stedman thanked Mr. Palmer for his testimony.

AT EASE [2:56:46 PM](#) / [3:10:50 PM](#)

Co-Chair Hoffman called the meeting back to order.

Alaska Gasline Port Authority
Presentation

[3:11:17 PM](#)

BILL WALKER, Project Manager & General Counsel, Alaska Gasline Port Authority (AGPA) introduced himself and AGPA's legislative liaison advisor, Paul Fuhs. Mr. Fuhs had "a long history" with the endeavor to advance an Alaska gasline project.

Mr. Walker addressed information in a handout titled "Alaska Gasline Port Authority Presentation to the Senate Finance Committee April 28, 2007" [copy on file] as follows.

[3:11:59 PM](#)

Page 2

AGIA is Good for Alaska

- Open, transparent and competitive
- Identified clear evaluation criteria
- Inducements to project applicants in exchange for specific commitments
- Empowers selected applicant to build successful consortium, leading to open season

Mr. Walker characterized AGIA, with its "open, transparent, competitive process", "good" for the State. AGPA is "encouraged by the reaction" their project has received "from potential participants" from around the country because of AGIA.

Mr. Walker announced AGPA's intention to apply for the AGIA license. Their efforts to date align with those of AGIA in that they also support the creation of "a consortium ... as part of the application process".

Mr. Walker declared that AGIA "is working even before it is passed, because of the attention" the process has brought to the State. The interest in AGIA, in both the United States and Canada, has made it easier for AGPA to discuss the merits of its proposal with the industry.

Mr. Walker shared that some have asked what AGPA has been doing recently as it has been fairly quiet. His response is that "it's a lot quieter playing offense than defense". AGPA has "been playing offense since the AGIA process began".

Mr. Walker noted that AGPA representatives have been traveling quite a bit in their effort "to put a consortium together".

[3:13:35 PM](#)

Page 3

Indicative AGPA Project Structure

[Diagram depicting the variety of entities that would be involved in the consortium envisioned by AGPA to bring Alaska's gas to market. These entities would include the Gas Producer/Shipper, the Regas Terminal Owner, Gas Offtakers, the Gas Conditioning Plant (GCP) Pipeline Engineering Procurement (EPC) Contractor, the EPC Contractor, the Liquefied Nature Gas (LNG) Facility EPC Contractor, the GCP Operator, the Pipeline Operator, the

LNG Facility Operator, the LNG Ship Owner, and the Financing Institutions.]

Industry leaders will be involved in all components of AGPA's project

Mr. Walker described the role of AGPA as one of "a facilitator" or the entity putting together "the structure" of the project.

Mr. Walker stated that when the Trans Alaska Pipeline System (TAPS) was originally being considered, the producers asked then-Governor William Egan to provide State financing for the Alyeska Marine Terminal. Governor Egan was uncomfortable with "the closeness of that relationship" and suggested the City of Valdez undertake that responsibility. Consequently the City of Valdez passed a two billion dollar bond which financed that terminal.

Mr. Walker noted that a similar "conduit package" process was initially considered by AGPA. It would "put together a structure that provided economic benefit to a project; that would increase someone's revenues to the upstream by using a tax exempt structure".

Mr. Walker expressed AGPA's awareness of the fact that a specific "named" business must be in place for each of the generic entities depicted on the diagram. Some agreements have been made; others are in process.

Mr. Walker specified that in order for this to be a "viable project" there must be world class leaders in each of the areas depicted. "They cannot be start-up companies". This is the reason AGPA began negotiations with the large well-known company, Bechtel Corporation.

Mr. Walker noted that port authorities such as AGPA often become involved in a project when no one in the private sector thought the project would generate sufficient return. There is value in the structure a port authority brings to a project as evidenced by the hundreds of port authorities operating in the United States today.

Mr. Walker contended that it is often difficult to know a port authority was at the root of a successful project it since the

spokespersons for the project were "world-class recognized leaders in each of their areas of expertise".

[3:15:57 PM](#)

PAUL FUHS, Legislative Liaison and Advisor, Alaska Gasline Port Authority, informed the Committee that AGPA was established by legislation in 1993. Its organization resembles most port authorities in the country, particularly that of the "conservative state", Wyoming. The Wyoming Gasline Authority was successful in its endeavor to create an operating pipeline in the state when the private sector there was unable to.

Mr. Fuhs stated that like the port authority in Wyoming, Alaska's port authority is comprised of a small board. The private sector companies involved in the port authority project would actually operate it.

Mr. Fuhs also likened the port authority process to the Alaska Permanent Fund. "A small board runs it on behalf of the people of the State of Alaska to make sure that it meets State interests, but then you hire the best private people in the world that you can to actually operate it".

[3:17:12 PM](#)

Page 4

AGPA Project Description

- Gas Conditioning Plant in Prudhoe Bay
 - o removes impurities
 - o compresses and chills the gas to pipeline specifications

- Pipeline from Prudhoe Bay to Valdez
 - o parallel to TAPS (max. capacity: 6 Bcfd)
 - o pre-build to Delta Junction for later tie-in for the Alaska/Canada Highway Project
 - o tie-in at Glennallen for a spur line to Alaska South Central natural gas grid

- LNG Facility in Valdez
 - o integrated LNG liquefaction and LPG extraction facilities

- o includes storage and vessel loading facilities

[Map of State depicting route of proposed in-State pipeline from Prudhoe Bay to Valdez with spurline from Glennallen to Palmer.]

Mr. Walker described the project parameters. A 48 inch pipeline would run from Prudhoe Bay to Valdez. A pre-build would be placed at Delta Junction in anticipation of a future spurline to the Canada Highway. Another spurline would be located in Glennallen to provide gas to South Central Alaska. The gas liquefaction plant would be located in Valdez, which is 115 miles past Glennallen.

Mr. Walker informed the Committee that AGPA has signed a memorandum of understanding (MOU) with the Alaska Natural Gasline Development Authority (ANGDA) for the spurline to South Central.

Mr. Walker explained that a phased project is being proposed by AGPA. While the initial volume carried in the line would be small, the project could be expanded to accommodate market demands.

[3:18:26 PM](#)

Page 5

Project Status

1. Project Route Permitted
2. The 23 Senior Permits Acquired
 - Yukon Pacific Corporation
 - \$100 million expended
 - Right-of-way
 - Project FEIS
 - LNG terminal permit
3. Bechtel Cost Estimates
 - Complete & Updated
4. Marine Transportation / Jones Act
 - MOU with the largest LNG shipping company in the world - Mitsui OSK Lines
5. Access to Multiple Markets
 - West Coast receiving terminal under construction

- West Coast Alternatives
 - Hawaii
 - Pacific Rim
6. Anticipated Financing
- 80% debt (Federal loan guarantee available)
 - 20% private funding

Mr. Walker reviewed AGPA's accomplishments to date. The route is partially permitted and 65 percent of the right-of-ways are pre-staked. APGA acquired "the exclusive rights" to Yukon Pacific Corporation's (YPC) permits and data, the millions of dollars spent by YPC and the work they conducted in acquiring permits, environmental impact studies (EIS), permits associated with the liquefied natural gas (LNG) terminal in Valdez, export licenses and numerous other things have benefited APGA.

Mr. Walker noted that the Bechtel cost estimates are current to 2005. Efforts are underway to update that information to 2007. This cost estimate is very detail oriented and specifies such things as which gravel pits would be utilized and where workers' camps will be located.

Mr. Walker next addressed transportation issues pertinent to the gasline. AGPA has entered into an MOU with Mitsui OSK Lines, the largest LNG shipping company in the world with 645 ships. Eight of those were built in the United States. Meetings have been conducted with federal entities in Washington DC to ensure that re-flagging those ships would be permissible. Alaska's Congressional delegation has committed to assisting this effort.

Mr. Walker stated that Alaska's experience in exporting LNG from a Kenai facility has been a contributing factor in the interest this project is drawing from LNG receiving terminals on the west coast. Several of those terminals are either permitted or are in the process of obtaining permits to handle Alaska's LNG product. Opportunities to ship to Hawaii and Pacific Rim markets have also been presented.

[3:21:46 PM](#)

Mr. Walker advised that, after studying numerous projects around the world and consulting with international business firms such as Sullivan & Cromwell LLP, a firm which had recently testified about AGIA before this Committee, AGPA decided to continue their

original idea of financing pipeline construction on "a project finance basis".

Mr. Walker informed the Committee that AGPA also anticipates applying for the federal loan guarantee. Numerous meetings with the federal Department of Energy on this issue have occurred.

[3:22:40 PM](#)

Page 6

Phased Project = Better Cost Overrun Risk Management

- 800 mile pipeline is 100% adjacent to TAPS, 100% in Alaska
- Infrastructure in place for entire line - roads, bridges, camp pads, etc,
- LNG project" lower overall cost overrun risk:
 - Liquefaction facilities utilize proven technology and well-tested design, resulting in a relatively low level of uncertainty in cost estimate
 - Low level of cost uncertainty for LNG marine transportation and regasification
 - Pipeline component has the highest capital cost uncertainty - for LNG project the pipeline is only a portion of overall cost to market
- Phase approach with LNG project proceeding first: 2/3 less cost = 2/3 less risk

Mr. Walker reviewed the benefits of having a phased, all-Alaska pipeline project. The shorter 800 mile route would lower project risk factors. Other pipeline proposals range between 1,750 and 3,600 miles.

Mr. Walker also declared that utilizing existing infrastructure would save money. A route following the existing road from Prudhoe Bay to Valdez would lower environmental issues and reduce construction time.

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Mr. Walker attested that LNG liquefaction facilities are "proven technologies". Due to continuing improvements in technology, the cost of constructing these facilities continues to decrease. The pipeline should be built soon as LNG is increasingly becoming a

viable competitor to the oil industry: ships are becoming less expensive and liquefaction facilities are becoming more efficient.

Mr. Walker advised that transportation should not be considered a high risk factor as AGPA has already identified the ships it would utilize and the costs associated with transporting LNG from Valdez to market.

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Mr. Walker stated that the pipeline itself is presenting the highest risk; specifically the cost of steel; the shorter the pipeline, the better.

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Mr. Walker also emphasized that a phased project approach "would minimize the risk".

[3:25:07 PM](#)

Page 7

LNG Project is Economic

- Robust economics with projected strong return to upstream producers (with no tax concession by State)
- Favorable economics takes into consideration pre-build to Delta Junction for a future AlCan Highway
- Win-Win for Alaska with LNG:
 - o Capture West Coast market now *plus* enable a later AlCan Highway project to proceed when ready
 - o Earliest in-State gas availability

Mr. Walker stated that after AGPA received the construction cost estimate from Bechtel, they engaged the services of a Washington D.C. financial firm, Green Gate LLC, to develop "a financial model" of the project.

Mr. Walker noted that Green Gate "was pleased" with the project cost estimate" developed by Bechtel. Even though the initial financial model was developed in the years 1999 and 2000, economic changes have improved the project financing scenario.

Mr. Walker stated that the ability to pre-build to Delta Junction would also allow a gasline to be built at a later date along the Alcan Highway.

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Mr. Walker stressed that an all Alaska route would not negate the option of having a highway route. It was not "a neither/or" situation. The State "could have the benefit of both options at this point". The effort taken in this legislation to address the offtake issues should be commended. Any project that fits within the bill's parameters should be considered.

[3:26:19 PM](#)

Mr. Walker reiterated that AGPA's routing proposal was "a big plus" for the State as it would allow gas to be available in state sooner than other routes. A scenario in which the State could sell on the world market via shipping or via a highway line in the future would "be the best of both worlds".

Mr. Walker agreed with producers and industry entities that the construction of a gas pipeline would be "a basin opening opportunity". The basin in Alberta Canada opened in 1958 with a small single line and expanded over time.

[3:27:25 PM](#)

Co-Chair Stedman assumed his position as Committee chair.

[3:27:31 PM](#)

Mr. Walker advised that constructing a small line rather than a larger six BCF line would be "the way you get to a full optimum opening of the basin". The risk profile of the smaller pipe size line is measurably better. The smaller line could be expanded as market offtake demands increase.

[3:27:49 PM](#)

Page 8

Advantages of LNG from Alaska

- The Alaska LNG project will benefit from an efficient, low-cost liquefaction operation:
 - ambient conditions (low average temperatures) in Valdez result in significant unit cost savings in comparison with liquefaction facilities located in tropical climate
 - efficiency gains estimated in the range of 30 - 40 %
- Most other LNG projects have significantly higher marine transportation costs to market due to longer shipping distances
- Many other LNG projects involve higher upstream costs due to complex, expensive field development
 - Alaska benefits from substantial existing North Slope infrastructure and developed fields (Prudhoe Bay)

Mr. Walker reviewed the material and noted that Alaska's 30 to 40 degree temperature ranges increase "the efficiency of LNG out of Alaska" by approximately 30 to 40 percent more than global marketplaces such as Qatar with a mean temperature of 80 or 90 degrees.

[3:28:46 PM](#)

Mr. Walker also noted that a tidewater terminus in Valdez is only five or six days from market rather than 22 to 27 days associated with other pipeline projects. The overall merits of a project should be considered as opposed to focusing on one key aspect such as whether a project developer already had a pipeline.

Mr. Walker also stressed the benefits provided from having an existing upstream infrastructure on the North Slope. Other LNG pipeline projects have had to build "expensive upstream infrastructures" prior to building a pipeline. Surplus gas is currently being re-injected on the North Slope.

[3:29:20 PM](#)

Page 9

Advantage of LNG for Alaska - Phased Project

- Better mitigation of cost overrun risk
- Open North Slope to commercialization of gas; encourage further exploration

- Commercialize discovered gas resources, while allowing exploration for expansion to proceed
 - initial offtake for LNG project - within existing AOGCC Rule 9 limitation
- Better positioned to accommodate early in-State offtake:
 - Economics of project components downstream of Alaska do not suffer diseconomies of scale due to reduced export volume - offtake at Glennallen affects only 100 miles of pipeline to Valdez
- Pre-build for expansion affects only the pipeline in Alaska
 - Expansion either through addition of new LNG trains or by interconnection at Delta Junction with an AlCan Highway project
 - Availability of gas liquids in Alaska for value added processing

Mr. Walker reviewed the benefits of a phased project. Exploration would also be encouraged by the construction of a pipeline.

[3:29:59 PM](#)

Mr. Walker addressed the AGIA requirement that there be five off-take points in Alaska. An 800 mile all-Alaska line would "be in a much better position to accommodate large off-takes along the way". For example, an offtake point near Fairbanks would affect approximately 350 miles of pipe rather than thousands of miles of pipe associated with other pipeline proposals. Downstream volume adjustments for off-takes would be less impacting on a shorter pipe.

[3:31:09 PM](#)

Mr. Walker advised that AGPA was also willing to accommodate a pre-build to Delta in consideration of a future line down the Alcan Highway. The initial 48 inch line would accommodate approximately two BCF. It could be expanded to accommodate six BCF by use of compression. Looping would not be required.

[3:31:55 PM](#)

Mr. Fuhs interjected to note that a gas liquids market in Alaska should be further investigated as it is "a huge industry in Canada. Consideration should also be given to the significant

level of propane contained in Alaska's gas. A recent propane feasibility study indicated it would be "quite feasible to deliver propane to rural Alaska as a replacement for diesel fuel and to be able to save money". This is another reason in support "of bringing this gas to tidewater".

[3:32:36 PM](#)

Senator Elton asked for further information about the process through which a two BCF pipeline could be expanded to a six BCF capacity.

Mr. Walker reiterated that a 48 inch two BCF capacity pipeline could be expanded to accommodate six BCF through the use of compression. Looping would not be required.

[3:33:01 PM](#)

Senator Elton asked whether the compression technology being considered by AGPA differed from that being considered by highway pipeline proponents as he understood that compression alone would not suffice to proportionately increase capacity on that line.

[3:33:16 PM](#)

Mr. Walker communicated that AGPA's engineers have determined that the shorter pipeline being proposed by AGPA could be expanded to accommodate 5.9 BCF solely by the use of compression. Looping would not be required.

Mr. Fuhs pointed out that the highway route pipelines would be initially constructed to accommodate a 4.5 BCF capacity. Those lines could be expanded to six BCFs without compression. Looping would be required to achieve a 7.5 BCF capacity.

[3:34:06 PM](#)

Page 10

AGIA Suggested Project Evaluation Criteria

- If applicant's offtake amounts exceed AOGCC Rule 9 limitations (2.7 bcf/d less field use), must have already

filed an application with AOGCC for increased offtake limits

- Additional gas reserves needed? Budget and timeline for exploration program
- Analysis of liquids availability in Alaska for value added processing
- Current project cost estimate required with application

AGIC benefits towards advancing gas pipeline

- Rolled in rates - good for Alaska's future
- Allows for independently owned infrastructure
- Follows successful model used in other countries who also use rolled in rates and independently owned pipelines.
- \$500 million skin in the game - sends very positive message about Alaska's desire to commercialize Alaska's gas
- Supports lowest tariff

[3:35:10 PM](#)

Mr. Walker suggested that further attention be given to AGIA's offtake and timing provisions. In addition, a review of when additional gas, beyond the current 35 trillion cubic feet (TCF) of proved gas reserves on the North Slope, might become available should be conducted. AGPA would need approximately 15 TCF for the first phase of their project. An analysis of the availability of liquids is a "critical point".

Mr. Walker shared that one country "has held up development of gas ... because they want to have a certain amount of liquids dedicated to remain" in that part of their country. Alaska should follow this example. Having a dedicated supply of liquids to support Alaska industry is important.

Mr. Walker also stressed the importance of having project cost estimates accompany each proposal.

[3:37:29 PM](#)

Mr. Walker next spoke in support of rolled in rates. Canada, which has rolled in rates, has "a very robust infrastructure of

gas pipelines". This approach would benefit the State and assist in furthering the opening of the basin.

Mr. Walker supported independently owned infrastructure. In response to the argument that AGPA's lack of pipeline ownership experience was a negative, he countered that AGPA has benefited from the experience of the Trans Alaska Pipeline System (TAPS); specifically in regards to such things as cost overruns, construction experiences, and interactions with the Federal Energy Regulatory Commissions (FERC) and the Regulatory Commission of Alaska.

Mr. Walker concluded that the TAPS "model should not be replicated on the gas" pipeline. The gasline should be independently owned and have the goal of moving as much gas as possible.

Mr. Walker stressed that the experiences of other projects would assist in containing cost overruns. The builder should absorb the majority of cost overruns with only a portion of the cost overruns being included in the tariffs. This and other issues should be addressed during contractual discussions.

[3:38:55 PM](#)

Mr. Walker informed the Committee that numerous financial advisors have commended the concept of the State's \$500 million "skin in the game" investment. "It sends a good message that Alaska's ready for this to happen".

Mr. Walker contended that the AGIA process will support a low tariff and attract more companies.

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Mr. Walker concluded his formal presentation.

[3:40:24 PM](#)

Senator Dyson asked AGPA to comment on the open season process.

[3:40:48 PM](#)

Mr. Walker reminded the Committee that the open season capacity of AGPA's project would be smaller than other projects as its

initial line would transport two BCF rather than the 4.5 or 6 BCF of the highway route projects. The entities meeting with AGPA are not interested in larger volumes as that would require a substantial level of exploration.

[3:41:32 PM](#)

Mr. Walker communicated that producers have said they would sell gas to a project that minimized risk and provide them a good return. That is the goal of AGPA.

[3:41:46 PM](#)

Mr. Walker stated that an open season goal of 1.7 BCF would be within the capacity of AGPA's project. The fact that producers are currently paying to re-inject that gas would attract them to the open season. Producers are in the business of commercializing gas and AGPA is "in the business of bringing together a consortium that does just that".

AT EASE [3:42:28 PM](#) / [3:43:04 PM](#)

Mr. Fuhs addressed the commonly stated position "that only the producers can take the risk and that it'll be just firm transportation commitments on their part to make the project work". Numerous LNG projects have been successfully developed with "market commitments" to buy the gas. "Other people could agree to buy the gas from the producers and make the commitments for this project."

Mr. Fuhs contended that this project would work even without the participation of "all three producers". As it appears right now, "even one reluctant party" could "leverage the entire rest of the system. Not only the State in terms of its taxes and returns and benefits to the State, but all the other participants as we saw with the holdout on the LLC and that's the reason why a contract could never be brought before you under the past administration. One party was able to hold out for ultimate leverage."

Mr. Fuhs suggested that this same scenario might occur with the open season process. Nonetheless, "there might be companies that are willing to commit to this where it does not require all three companies to make the project work".

Senator Dyson asked whether AGPA was contemplating purchasing gas from the producers at the wellhead or at a gas conditioning plant. He was also curious as to who would be responsible for building the gas conditioning plant.

[3:44:56 PM](#)

Mr. Walker expressed that AGPA could "do it either way". Whichever method was acceptable to the producers would be fine.

Mr. Walker communicated that AGPA's economic model "assumes" that the producers would construct and own the gas conditioning plant as it would provide them tax benefits. AGPA would "pay a toll for that work".

[3:45:26 PM](#)

Senator Thomas understood that AGPA considered a smaller project more economical in terms of being able to generate gas commitments. This in turn might allow the project to proceed at a faster pace than a larger one.

Mr. Walker expressed that AGPA did not view its project as a smaller project but rather a phased expandable project that would accommodate market demands. This approach would minimize risk and have a sooner start-up date. The field efforts to date could allow the project to begin operation in six years. The work that has been conducted over the past 20 plus years would "shave off three or four years".

[3:47:12 PM](#)

Senator Thomas asked for further details about the pipe sizes that might be used along the route.

[3:47:19 PM](#)

Mr. Walker advised that a 48 inch pipe would be utilized from the North Slope to Delta Junction. Discussion is continuing in regards to the size of the pipe from that point south. Using a smaller size pipe out of Delta Junction might restrict the line's ability to be expanded to six BCF. A decision in this regard would be made prior to project financing. Other considerations include the prospect of having a line extend through Canada.

[3:47:59 PM](#)

Senator Huggins hypothesized a situation in which the State looked at AGPA's application and concluded that a two BCF pipeline would not generate adequate levels of revenue for the State. The question was whether AGPA could accommodate a pipe with a minimum 3.5 BCF capacity if the State requested that.

Mr. Walker replied that AGPA could accommodate that request because of the project's ability to expand to 5.9 BCF. Market conditions and infrastructure are factors in AGPA's project design. A two BCF project was proposed because "it was the smallest base case that would make good money for the State, and gave a sufficient return to the producers on the wellhead". It also significantly reduced risk and provided a significant time advantage on project start-up.

Mr. Walker advised that some have questioned whether a smaller project might negate the opportunity for a larger project. His response was that most basins have opened with smaller pipe and then expanded as influenced by market conditions. This project should be viewed as the first phase of a big project.

[3:50:49 PM](#)

Mr. Fuhs acknowledged the thought that a bigger pipe would provide more revenue to State. However, gas availability and commitments must substantiate that pipe and make it "a practical project" which would not "collapse oil production in Prudhoe Bay". That is "a legitimate question" that must be addressed by the Alaska Oil and Gas Conservation Commission during the application process.

[3:51:55 PM](#)

Mr. Fuhs declared that the risks associated with starting with a smaller project should be weighed against such things as "the likelihood of the project going forward". State departments are charged under AGIA with those evaluations.

[3:52:26 PM](#)

Co-Chair Stedman thanked Mr. Fuhs and Mr. Walker for their presentation.

The bill was HELD in Committee.

AT EASE [3:52:32 PM](#) / [4:42:52 PM](#)

#sb125

SENATE BILL NO. 125

"An Act relating to the accounting and payment of contributions under the defined benefit plan of the Public Employees' Retirement System of Alaska, to calculations of contributions under that defined benefit plan, and to participation in, and termination of and amendments to participation in, that defined benefit plan; making conforming amendments; and providing for an effective date."

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

Co-Chair Hoffman moved to adopt committee substitute Version 25-GS1074\K as the working document.

There being no objection, the Version "K" committee substitute was ADOPTED.

[4:43:47 PM](#)

Co-Chair Stedman announced that several spreadsheets and a new Department of Administration fiscal note dated April 20th, 2007 pertinent to Version "K" [copies on file] would be addressed during today's discussion. A side-by-side comparison of Version "K" to the original version of the bill was being developed.

MILES BAKER, Staff to Co-Chair Stedman, communicated that his remarks would highlight areas of change in this committee substitute relative to the original version of the bill. As noted, a side-by-side comparison was currently unavailable but would be provided once completed.

Mr. Baker identified the first change as being the elimination of a section in the bill pertaining "to the duties and responsibilities" of the Alaska Retirement Management Board (ARMB). The reference to ARMB in the bill's title was also

removed. The provisions pertinent to ARMB had not been included in the original version of the bill, but were incorporated by a previous committee substitute adopted by the Committee.

Mr. Baker informed the Committee that "some slight drafting differences" resulted in there being minor language changes in Section 1. The substance of the Section had not been changed. In addition, definitions incorporated into Section 1 in the previous committee substitute, Version 25-GS1074\E, had been moved to "the broad definition section" of the Teachers Retirement System (TRS) Statute.

[4:45:49 PM](#)

Senator Olson asked for confirmation that the Senate's proposed TRS employer contribution rate of 12.56 percent had not been affected by these changes.

Mr. Baker affirmed the rate was unchanged.

[4:45:58 PM](#)

To that point, Mr. Baker directed attention to Section 1 subsection (d) page 2 line 9. In essence, this section specified that "regardless" of that 12.56 rate, "if the normal cost goes above that in the future", then that higher rate would become the normal cost.

[4:46:24 PM](#)

Mr. Baker indicated that, other than minor "wording differences" resulting from "editorial" changes, no substantial changes were made in Sec. 2. The working differences also resulted in a change in the title of the section: instead of reading "Determination and payment of state contributions", the title now read "Additional state contributions".

[4:46:50 PM](#)

Mr. Baker stated that the TRS definition removed from Section 1 has been incorporated into Sec. 3, page 3 lines 3 through 5.

[4:47:16 PM](#)

Mr. Baker specified there being were "no real changes to Sections 4, 5, 6, or 7.

[4:47:34 PM](#)

Mr. Baker expressed that the first substantial change made by Version "K" is in Sec. 8. The effort being furthered in this bill is to transition entities to a cost-share system. In the case of the Public Employee Retirement System (PERS), all PERS employers would contribute 22 percent of "their active payroll" base.

Mr. Baker reminded the Committee of the concern raised in previous hearings on this bill that employers might endeavor to reduce their payroll base by selling off, "for example, their local utility or to decide to outsource something that previously was done by the municipality". While such action would lower that municipality's contribution, other municipalities "would be required to share in the loss of that revenue".

Mr. Baker specified that language in Sec. 8 subsection (a) page 5 lines 4 through 11 was reworked to address this concern. Each year, an employer would be required to pay 22 percent of the greater of either their current total payroll base or "the salary base as it was for the fiscal year ending June 30, 2007". This would prevent an employer from contributing less were their payroll to decrease as well as ensure their contribution adequately reflected any increase in their payroll base in the future.

[4:49:41 PM](#)

Senator Dyson asked whether the municipality would still be held to this obligation if the buyer of one of its political subdivisions "agreed to assume the benefits liability for the employees".

[4:50:35 PM](#)

Mr. Baker clarified that that issue could be addressed during the negotiations with the buyer. However, the reason for requiring the municipality to pay 22 percent of the "higher payroll base is because built into that 22 percent is the money

that this employer currently is putting forward into this new pooled pot to pay off the unfunded liability".

Senator Dyson characterized this obligation as "legacy costs"

Mr. Baker affirmed.

Senator Dyson accepted the explanation.

[4:51:21 PM](#)

Mr. Baker noted that language in Sec. 9 was slightly reworked. This section clarified the State's additional obligation to the retirement systems. In addition to paying 22 percent on its payroll base, the State, as specified in Sec. 9 line 5 page 6, "shall contribute to the plan each July 1" or as soon after that date as possible, "the amount of money required between the 22 percent and the Board adopted rate to fund the payment for the whole system for the unfunded liability for that year". The date for the payment was allowed some flexibility in consideration of the State's cash flow situation in July, as numerous payment obligations are specified for July first.

[4:52:55 PM](#)

Mr. Baker communicated that no changes were made in Sec. 10.

[4:53:29 PM](#)

Mr. Baker deferred to the Department of Administration to discuss Sec. 11.

[4:53:53 PM](#)

ANNETTE KRIETZER, Commissioner, Department of Administration, informed the Committee that Sec. 11 would allow the Department "to claim monies that's owed to it under the system". The language in this section was rewritten in consideration of concerns of the Alaska Municipal League (AML). The revised language is located on page 7, lines 5 through 8 and reads as follows.

After the agency submits this amount to the administrator, the employer may appeal the administrator's claim to the Office of administrative hearings (AS 44.64). If an appeal

is timely filed, the administrator shall hold the submitted funds in an escrow account pending a final decision on the appeal.

Commissioner Kreitzer stated that this compromised language would assist in addressing some of AML's concerns.

[4:55:23 PM](#)

Senator Elton inquired to the cost of conducting an administrative hearing; specifically to a small community.

Commissioner Kreitzer responded that this information would be provided.

[4:56:08 PM](#)

Mr. Baker addressed Sections 12, 13, 14, and 15. They dealt with two sections of statute regarding an employer's termination from the plan or amending their participation agreement. Both the original bill and the previous committee substitute "envisioned that" once the system transitioned to a cost share plan, employers would have a 90 day period in which "to make changes to their participation agreement": they could opt in or out classes of employees. No such changes would be allowed after that. The only recourse after that would be for an employer to exit the system completely.

Mr. Baker advised that Version "K" would eliminate that 90 day window. An employer's ability to amend their participation agreement would continue to be allowed as in current Statute. However, language in Sec. 15, page 8 was required to address costs associated with an employer's decision to opt in or opt out a group of employees or sell off a portion of the business which would in effect reduce the employer's payroll base. For instance, a community could decide not to cover their municipal waste people or their fire chief or city administrator.

[4:58:47 PM](#)

Mr. Baker stated that while an employer could continue to amend their participation agreement, language in Sec. 15 specified that an employer who terminates a class of employees or completely terminates from the system would be required to pay termination costs. He reviewed how the termination costs would

be calculated. For instance, an employer terminating a class of employees would be required to pay that groups' past service costs.

[5:00:20 PM](#)

Senator Thomas expressed concern that, as has happened in the past, the State might not have an accurate unfunded liability figure. Were that the case, an entity terminating groups of people or completely terminating from the plan, might be told their obligation was satisfied, but then might un-expectantly get a "huge bill" later" when the system's unfunded liability was reevaluated.

[5:01:43 PM](#)

Commissioner Kreitzer pointed out that "no plan is foolproof". The Department, Committee members and staff, and other entities and individuals working on this bill have worked diligently "to identify areas where we think that there could be some loophole and could allow for a situation where you might not have the unfunded liability taken care of". The bill before you "is our best effort to deal with that and to not come into a situation in the future where we would have someone getting a big bill because the Division of Retirement and Benefits made a mistake". She could not envision where at this point, a mistake might be made.

Senator Thomas also acknowledged being unable to identify any specific weakness. Nonetheless, despite professional action in the past, the State is facing a substantial unfunded liability.

[5:02:47 PM](#)

Mr. Baker pointed out that "liabilities by individual employers" are tracked under the current retirement system. Each year, the actuary conducts an extensive process to determine "the new liability of the system is and allocating it as appropriate to all the individual employers".

Mr. Baker directed his remarks to Senator Thomas's concern. An employer might have been fine at one time, but, as each new valuation was determined, their unfunded liability grew. This was the experience of most employers.

Mr. Baker expressed that the same valuation process would continue under this bill. However, under the cost share system being proposed, the unfunded liability would be "shared amongst everybody".

[5:03:44 PM](#)

Mr. Baker stated that, under the current system, each entity was combating "a different number".

Mr. Baker agreed with Commissioner Kreitzer that "this is a best attempt to address the fact that everyone will be sharing the load and" appropriately allocating it going forward.

[5:04:15 PM](#)

Mr. Baker informed the Committee there was no change in Sec. 16.

Mr. Baker noted that it was decided to move definitions from individual areas of the bill to a more appropriate place in the Statute section. Thus, definitions were added to Sec. 17.

[5:04:31 PM](#)

Mr. Baker deemed Sec. 19 to be a significant component of the committee substitute. The spreadsheets earlier referenced by Co-Chair Stedman were pertinent to this section.

Mr. Baker stated that Sec. 19 subsection (a) of Version "K" contained a listing of employers who had contributed excess funds to their retirement plans during the prior three years and their contribution rates, as adjusted, for the first year of program implementation. This information had been re-verified by the Department.

Mr. Baker directed attention to a spreadsheet titled "FY 08 Rate Adjustments Required to Recoup Excess Muni PERS Contributions from Prior 3 Years (Revised 4/28/07) Prior to application of Hold Harmless Provision" [copy on file], which pertained to this section.

[5:05:40 PM](#)

Mr. Baker addressed Column "9" of the spreadsheet. Changes on this spreadsheet, as compared to the previous version, are

highlighted. For instance the City of Barrow and the City of Klawock have been added to the list.

5:06:26 PM

Mr. Baker next addressed the spreadsheet titled "Impact of a 22% Employer PERS Rate on Municipalities, with CSSB 125 Hold Harmless Provision" [copy on file]. In addition to the desire to assist the "Heroes" communities, those entities which had contributed excess funds toward their retirement plans, an effort was made "to be equitable. As we set a rate of 22 percent, many municipalities are going to see quite a windfall or credit to what they previously thought they were going to have to pay if their rates were substantially higher than 22".

Mr. Baker also pointed out that there were also a few communities that had rates significantly lower than 22 percent. They would be experiencing a substantial increase in their payments.

Mr. Baker signified that the "Impact" spreadsheet reflected communities' estimated FY 08 payroll; their FY 07 employer contribution rate; and the FY 08 Board recommended rate they would have been required to pay absent this legislation. For example, the City of Fairbanks would have paid \$13,271,641 under the FY 08 Board Requested Rate. Under this legislation, they would pay \$1,578,676 for a savings of \$11,692,965 or an 88 percent "credit gain".

Mr. Baker stated that the City of Fairbanks would not be subject to the hold-harmless provision in the bill because, under this bill, they would be experiencing a tremendous decrease in the contribution level as compared to the status quo system.

5:08:33 PM

Mr. Baker stated that the City of Fairbanks situation was opposite to that of the City of Seldovia in that the proposed cost share system would require them to contribute more than they would under the status quo system. Therefore, hold harmless provisions were incorporated into the bill in an attempt to provide equality.

Mr. Baker explained that the hold harmless provision would apply to those entities whose FY 07 rate or FY 08 Board Recommended

Rate was less than 22 percent. They would be subject to the lower of those two years' contribution rates.

Mr. Baker informed the Committee that the total fiscal impact of the hold harmless provision was then calculated. The State, in addition to its 22 percent contribution, would be required to contribute an additional \$1.3 million as specified at the bottom of Column (7).

[5:10:21 PM](#)

Senator Elton asked whether there were school districts with employees in the PERS system which might require similar hold harmless considerations.

[5:11:00 PM](#)

Mr. Baker stated that this issue is under review. Until recently, only municipalities and cities had been considered. In addition to considering whether any school districts with PERS employees should be included, attention is being expanded to the category referred to as "PERS Others". This would include entities such as a housing authority or Bartlett Regional Hospital in Juneau.

Mr. Baker calculated that an additional one million dollars could be added to the hold harmless total were school districts considered. "PERS Others" might add an additional three million dollars.

Mr. Baker concluded that applying the hold harmless clause to these entities would be doable; it would be a policy call matter.

Senator Elton appreciated the foresight given to this issue.

[5:12:23 PM](#)

Mr. Baker referred the Committee to the spreadsheet titled "CSSB 125 Sec (19) Rate Adjustments" [copy on file]. This spreadsheet reflects communities "recoup" rates as affected by the hold harmless provisions. For instance, the Aleutian East Borough's recoup rate for FY 08 would have been 10.01 percent. Once the hold harmless rate is factored in, their rate for FY 08 would be 3.24 percent.

[5:14:16 PM](#)

Mr. Baker stated that communities who qualified for both the recoup and hold harmless provisions would contribute at the adjusted rate for FY 08. The hold harmless provision adjustment would continue to apply to qualifying communities for an additional four years.

Mr. Baker specified that all communities would be subject to the 22 percent contribution rate beginning in FY 13.

[5:15:20 PM](#)

Mr. Baker noted that the communities depicted at the top of the spreadsheet were those that qualified for the recoup and/or the hold harmless rate provisions specified in Sec. 19(a) for FY 08.

Mr. Baker stated that 19(b) contains the hold harmless provisions specific to the additional four years. Communities subject to that provision are depicted at the bottom of the spreadsheet.

[5:15:45 PM](#)

Commissioner Kreitzer "commended" Co-Chair Stedman's staff for their efforts in developing the Version "K" committee substitute.

Co-Chair Stedman asked Members to review Version "K" thoroughly and advise his office of any concerns or suggestions.

The bill was HELD in Committee.

#

[5:16:59 PM](#)

Co-Chair Stedman conducted housekeeping of the Committee's upcoming hearing schedule.

ADJOURNMENT

Co-Chair Bert Stedman adjourned the meeting at [5:17:06 PM](#).