

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

CALL TO ORDER

Co-Chair Bert Stedman convened the meeting at approximately [1:44:02 PM](#).

PRESENT

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

Also Attending: MARTIN MASSEY, Joint Interest Manager, ExxonMobil Corporation;

Attending via Teleconference: From offnet locations: DAVID HILL, General Counsel, U.S. Department of Energy; JAMES SLUTZ, Deputy Assistant Secretary, Office of Fossil Energy, U.S. Department of Energy.

SUMMARY INFORMATION

SB 104-NATURAL GAS PIPELINE PROJECT

The Committee heard from the U.S. Department of Energy and Exxon Mobile Corporation. The bill was held in Committee.

#SB104
[1:44:19 PM](#)

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 fifteenth hearing for this bill in the Senate Finance Committee.

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DAVID HILL, General Counsel, U.S. Department of Energy, testified via teleconference from an offnet location in Washington D.C. giving his history at the Department of Energy and prior to that as a private attorney.

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Co-Chair Stedman expressed interest in federal loan guarantees and asked the current status.

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Mr. Hill told of the Alaska Natural Gas Transportation Act of 2005, which authorized the Department of Energy to issue loan guarantees for the construction of an Alaska natural gas pipeline. Public comment was taken on how the Department should proceed. No other action had been taken on the matter.

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Co-Chair Stedman understood regulations had not been written and asked when this would be done.

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Mr. Hill replied that the Act authorized the Department to issue regulations, but did not require that regulations be issued. A "number" of public comments recommended against the issuance of regulations due to the unique nature of the project. Those providing this recommendation argued that regulations could "tie" developers "down too much", given that the financing method was unknown. Mr. Hill was unsure whether regulations would be written.

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Co-Chair Stedman asked the loan underwriting procedures that would be employed.

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Mr. Hill qualified that the Department had not issued loan guarantees for "a long time". The 2005 Act also provided authorization for the issuance of loan guarantees for other types of projects.

Mr. Hill anticipated that in the case of the Alaska natural gas pipeline project, the Department would investigate the credit worthiness of the project and any commercial commitments made, in addition to conduction of due diligence.

Mr. Hill furthered that the Federal Energy Regulatory Commission (FERC), as part of the issuance of a certificate, would also undertake a technical review from which the Department would benefit. Any technical financial factors relevant to establishing the cost of the federal loan guarantee would also be considered.

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Co-Chair Stedman asked if the loan underwriting debt would be similar to the process employed by financial institutions or banks issuing bonds.

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Mr. Hill answered the process would be similar. Because the Department would issue loan guarantees but not debt itself, it would collaborate with the financial institution that actually issued the debt. The financial institution could be a commercial lender.

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Co-Chair Stedman clarified that the federal government would not issue government backed bonds, but rather a guarantee to another lending institution.

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Mr. Hill affirmed and reiterated that Section 116 of the Act authorized the Department to enter into agreements to issue federal loan guarantees. It also partially defined eligible lender as "non-federal qualified institutional buyer."

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Co-Chair Stedman asked if the lender and the federal government would each conduct underwriting reviews.

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Mr. Hill stated that the Department would collaborate with the lender in the underwriting process.

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Senator Elton asked if the due diligence would be undertaken within the "bureaucracy" or contracted out.

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Mr. Hill qualified that it had been a "long time" since the Department had issued loan guarantees. He anticipated that the underwriting would be overseen by the Department with collaboration with the federal Office of Management and Budget and that the actual underwriting activities would be contracted out.

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Co-Chair Stedman requested an explanation of the process "through construction to first gas".

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Mr. Hill replied that the guarantee assured repayment of debt in the event of default on the debt obligations by the project. As the guarantor, the Department was not the project owner or operator. The provisions of Section 116 prohibit the issuance of the guarantee until the project received FERC certification. The point at which the loan guarantees would be issued, disbursement of funds and other terms and conditions would be subject to negotiation with the project developer.

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JAMES SLUTZ, Deputy Assistant Secretary, Office of Fossil Energy, U.S. Department of Energy, testified via teleconference from Houston, Texas. The Office had been assigned to administer the issuance of this loan guarantee.

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Co-Chair Stedman asked if the loan guarantees would expire at some point after the FERC certificate was obtained.

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Mr. Hill explained the "normal FERC process" was outlined in Section 7 of the Natural Gas Act. The ability of the sponsor to finance its project would be considered in the FERC evaluation of the project. The FERC would review any agreements reached to date. In the case of the Alaska natural gas pipeline, FERC would investigate whether the sponsor would utilize the federal loan guarantees, for which debt they would be used and the point in which the guarantees would be activated. The loan guarantee could not be issued until the project was certificated by FERC.

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Co-Chair Stedman understood the loan guarantees had a two year timeline.

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Mr. Hill affirmed. The provision of Section 116(a)(3) stipulated that "the authority of the Secretary to issue federal guarantee 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 is issued for the project." The subsection further defined the final certificate.

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Co-Chair Stedman asked if the loan guarantee functioned in a similar manner to other guarantees issued for bonds.

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Mr. Hill affirmed.

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Co-Chair Stedman asked the different recourse procedures on a defaulted loan that occurred during the construction phase versus post construction and production.

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Mr. Hill explained the recourse would depend on how the terms were structured. The federal statute did stipulate that "the Secretary shall not require as a condition of issuing a federal guarantee instrument under this section, any contractual commitment or other form of credit support of the sponsors other than equity contribution commitments and completion guarantees or any throughput other guarantees from prospective shippers greater than such guarantees that shall be required by the project owners." The details of this provision would be negotiated with the project owners.

Mr. Hill surmised that the structure of the project would determine whether recourse would be allowed "beyond the project sponsor and the project assets."

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Co-Chair Stedman restated his question asking if the recourse procedure would be different during the construction phase and after completion of the project. He wanted to know if "the corporate balance sheet" of the project owner would be required to "back up" the loan guarantee; and if the loan were defaulted, whether the corporate entity would be "at risk and at what magnitude".

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Mr. Hill reiterated that this would depend on how the sponsor structured its project. He noted that the Credit Reform Act of 1990 required the Department to have appropriated funds to pay the cost of the loan guarantee prior to issuance. The elements that would increase risk to the government would have the potential for increasing the amount of the appropriation needed.

Efforts must be undertaken to determine the amount of the risk and to identify the assets available for recourse.

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Co-Chair Stedman asked if a limited liability corporation or other entity was formed to undertake the pipeline project whether its assets would be subject to recourse.

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Mr. Hill answered that the Department and the project sponsor could negotiate terms to allow ultimate recourse to the parent companies, but this would "not necessarily" be the case.

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Co-Chair Stedman requested the witness address "completion risk" and its impact to the loan guarantee in the event the project encountered substantial cost overruns during the construction phase or if the "entity fails".

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Mr. Hill reported that the Department had not yet decided on the method in which completion risks would be addressed. This would be resolved later in the process.

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Co-Chair Stedman asked the time limit on the loan guarantees.

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Mr. Hill replied that federal statute provides that the term of any loan guarantee could not exceed 30 years. The term for this project could be less, but could not be longer.

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Senator Dyson asked the stage of the project in which the two year time limit to secure the loan guarantee would be in effect.

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Mr. Hill reiterated that the Department had the authority to issue the guarantees up to two years after FERC certification was completed. He cited from Section 116 that "a final certificate would be considered to have been issued when all certificates of public convenience and necessity have been issued that are required for the initial transportation of commercially economic quantities of natural gas from Alaska to the continental United States." The Department had not "taken any authoritative position as to exactly how it would construe that section." He predicted that the Department would attempt to "construe it in a flexible way" to "not unduly bind a particular project sponsor in a way that was commercially unrealistic."

Mr. Hill informed that FERC "often" would issue a certificate that had various conditions. A period of time could be required after the issuance before the conditions were satisfied and before work authorization could be granted. The Department would construe the two year limitation flexibly, to allow for the congressional intent of the loan guarantee.

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Senator Dyson clarified that the final FERC certificate would be issued at the point all permits were secured and had no relevance to construction startup or commencement of operation.

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Mr. Hill agreed the term "construction" was not referenced in the statutory language. Neither was production from the completed facility mentioned. The Department would interpret Section 116 in a manner that would allow a project developer to satisfy FERC conditions and to undertake activities required by its lenders. The intent was to not bind the project developer in such a manner that it could not comply with the section.

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Senator Elton pointed out that the project would also require certification from the Canadian government, which could be issued after the FERC certificate. Therefore the two-year timeline would not begin until after both certificates were issued.

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Mr. Hill affirmed that the Canadian certificate was included as a certificate or permit needed before the FERC certification would be considered final. The Department had not taken a position on whether the flexibility would be extended to allow for compliance with any conditions attached to the Canadian certificate.

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Senator Elton surmised that completion of financing would be difficult for any sponsor without Canadian certification.

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Mr. Hill agreed and assured that the Department was considering its implementation of the subsection to allow the project to proceed in a "commercially reasonable" manner.

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Co-Chair Stedman asked the structure of government loan guarantees and whether it would be possible or practical to structure the financing of the Alaska natural gas pipeline project in which the federal government "would issue the \$18 billion and then the debt service would just be paid through an intermediary to retire that debt."

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Mr. Hill repeated that the federal statute granted the Department the authority to issue loan guarantees; it did not authorize the Department to issue affirmative debt obligations. The statute stipulated the definition of an eligible lender and a nonqualified lender, which included pension plans and government entities.

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Senator Olson asked the number of instances in which loan guarantees were utilized to "bail out" a larger petroleum transportation system.

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Mr. Hill did not know. The federal government issued loan guarantees for a variety of projects, including agricultural projects, export and import banking, airlines and student loans. Most programs experienced low default rates; other programs had high default rates.

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Senator Olson asked specifically about energy related projects.

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Mr. Hill recounted that the Department of Energy had issued loan guarantees during the 1980s and experienced "a number" of defaults. Several factors were likely the cause. As a result the Federal Credit Reform Act of 1990 was passed to govern the manner in which federal agencies administered loan guarantee programs and included the requirement that funds in the amount of the guarantee must be appropriated in advance.

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Senator Huggins referenced subsection 116(a)(3), pertaining to the two year time limit for a project sponsor to obtain the loan guarantee following final FERC certification. Mr. Hill commented to the intent that the Department would interpret this provision to allow for "maximum flexibility". However, previous testimony warned the Committee to "look for what could go wrong." Senator Huggins asked that if the two year period was not "operative" why it existed.

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Mr. Hill assured that the two year time limit would be "operative" and must be complied with. The issue would be determining the date in which the time period commenced. He did not intend to imply that the provision would be ignored, but rather that it would be administered in a reasonable manner.

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Senator Huggins, citing a proposed timeline of the Alaska natural gas pipeline project, estimated the project would have been underway for approximately nine years at the time the loan guarantee deadline was reached. Construction would not yet have

commenced. At this point, it could be argued that the State was in jeopardy.

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Senator Huggins next spoke to recourse. He asked if lending institutions would be required to seek payment from the parent companies or holding companies of the project developer before collecting on the federal loan guarantees.

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Mr. Hill answered that the point at which the lender could call upon the loan guarantee would be subject to negotiation of the loan guarantee commitment. He anticipated that project sponsors would chose to not have a requirement to seek payment from their parent companies before the federal guarantee was activated. However, that would affect the "credit subsidy score", the cost of the loan guarantee, and subsequently the amount of funding that must be appropriated.

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Mr. Hill offered his assistance and that of the Department of Energy. The Department supported the project and its process.

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MARTIN MASSEY, US Joint Interest Manager, ExxonMobil Corporation, read his testimony into the record as follows.

I am the US Joint Interest Manager for ExxonMobil, a position I have held since November 2001, and I am responsible for the commercialization of ExxonMobil's gas resources in Alaska.

ExxonMobil has been in Alaska for over 50 years and has been a key player in Alaska's oil industry development. We hold the largest working interest at Prudhoe Bay (36.4%) and our current net production in Alaska is approximately 150,000 barrels per day. We have benefited from our involvement in the State of Alaska, and we believe that Alaska has benefited from this long-term relationship as well. Commercializing Alaska's North Slope gas will allow

us to continue this mutually beneficial relationship for another 50 years or more.

EXXONMOBIL READY TO PROGRESS PROJECT

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

As an illustration of our commitment, ExxonMobil has spent more than \$180 million studying ways to commercialize Alaska gas. Since the 1970's we have evaluated LNG, gas to liquids and gas pipeline alternatives. Based on these studies we have determined that a Producer Gas Pipeline Project will result in the best value for the State, the Producers and the nation.

GENERAL FEEDBACK ON AGIA

I would now like to provide you with some feedback on AGIA. ExxonMobil embraces the concept of competition all over the world and is ready to participate in a competitive and market-based environment. AGIA, as it is written today, does not encourage market-based competition due to its prescriptive nature. In addition, AGIA does not adequately address the significant upstream issues and risks associated with the scale and magnitude of the Alaska Gas Pipeline Project. We have consistently advised the Legislature and the Administration that AGIA, in its current form, will not encourage competitive proposals and will not result in a commercially viable project. We strongly believe AGIA will not create an acceptable framework for this world-scale mega-project unless it allows the parties taking the risks to make a proposal that properly manages the risks.

After listening to the testimony over the past several weeks, it has become clear to me that one of the reasons the Administration's view of the project is so different from ours is due to flawed assumptions in the State's economic model. The Administration's model fails to recognize the integrated nature of this basin-opening project. The upstream pays for the midstream and you cannot split them apart when evaluating commercial viability. Any attempt to do so will deliver erroneous results. This issue is critically important, because if you put in place a process based on a flawed analysis, it will most likely fail. For this reason it is important that the State's economic model be corrected. The Administration's approach is not consistent with how project economics are evaluated, and I'll expand on this later in my testimony.

To ensure the best result, the logical way forward in our opinion is for AGIA to establish the State's broad key objectives, then allow applicants flexibility so that they can compete to meet those objectives and define the parameters that are necessary to make the project commercially viable. As an illustration of what I am proposing, AGIA could allow the applicant to demonstrate how their proposal encourages exploration and development in Alaska rather than specifying the method of project access and expansion.

If you were to amend AGIA to make it objective driven, it would allow open competition, maximize the number of applicants and allow those applicants to propose innovative solutions to meet the State's needs and open the basin. The State could then evaluate the proposals and select the one that best serves Alaska's needs and assures Alaskans realize the maximum value for their resource. That process would allow ExxonMobil, the largest leaseholder of gas on the North Slope, to compete under the AGIA process while providing the State complete flexibility on who is chosen to move the Alaska Gas Pipeline Project forward.

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

PROJECT RISK / PRODUCER CAPABILITIES

The tendency exists for many to underestimate the size, magnitude and risks associated with this project. The Alaska Gas Pipeline Project is a world-scale undertaking with significant risks. In fact, the project would be the largest private investment in North America - significantly larger than most "model" worldwide oil and gas "mega" projects. Let me be clear, this will be a precedent setting global mega-project. As you heard last week from Mr. Fred Rich of Sullivan and Cromwell (Head of Global Project Development and Finance), this project's financing could be many times greater than the largest North American project financing to date (the Alliance pipeline). There is not really another project that compares.

Because of this size, many factors impact commercial viability, including cost and the potential for cost overruns, gas price, schedule delays, construction conditions, and regulatory and State fiscal uncertainties. Our previous cost estimate of \$20 billion (which is in \$2001) will be substantially higher due, in part, to increasing steel prices, which have nearly doubled since 2001, and because we are experiencing hyperinflation on industry and construction labor costs. World-wide mega-projects are also placing pressure on pricing and availability of global materials, and skilled manpower. In addition, as we have observed over many years, natural gas prices remain highly volatile.

The State of Alaska cannot anticipate how individual applicants will view the various risks I have discussed or how applicants may choose to address them. Establishing a set of rigid, prescribed terms in AGIA will not allow the flexibility needed by individual applicants to weigh and manage those risks in a way that maximizes value to the State and the applicant.

HOW PIPELINES ARE FINANCED

The way projects are financed gives some insight into who bears the risks for projects of this type and how these risks are managed. Last week you heard how pipelines are financed from Mr. Rich. Commercially-sound oil, gas, and pipeline projects traditionally have been able to obtain financing if they have strong sponsors with proven track

records and the financial strength to both provide upfront lender required sponsor equity and to backstop key project commitments. For the Alaska Gas Pipeline Project, key project commitments take the form of completion support (either a full debt guarantee or additional equity overrun commitments) and firm, long-term gas transportation commitments. Firm transportation commitments are binding obligations made by companies to pay for the cost of reserving long term gas capacity as shippers on a pipeline. These commitments are made during an "open season", which is a period during which any and all prospective gas shippers can make binding commitments for a specific volume of transportation capacity.

As you may recall, Mr. Rich indicated that for a project of this scale and magnitude, financial institutions will require substantial, long-term, firm transportation commitments to provide funding. These commitments must be provided by creditworthy shippers because this tariff stream underpins the debt repayment. Furthermore, lenders not only look at the contractual commitments, but place equal importance on the underlying economics of the project. Any potential reduction in the Producer's netback is a concern to the lender since it increases the likelihood that the integrated project may not be economic, that the transportation charges are not paid, and that as a result the lenders are not repaid. Looking at this another way, the lenders are assessing how effectively the parties taking the risks are managing these risks. They will also want these risks reduced to a minimum to make sure they will get paid back. For this reason they would prefer stable fiscal regimes, project sponsors who have a proven track record of delivering mega projects on time and on budget, project sponsors with ownership in the upstream, and shippers who can support and will honor multi-billion dollar firm transportation agreements.

WHO BEARS PROJECT RISKS

That is why it is so important to understand who bears the project risks. Through the firm transportation commitments, the project development costs and the associated cost overrun risks are ultimately borne by the shippers. For this project, the shippers will be the Producers, and, directly or indirectly, the State or the State's shipper. These firm transportation commitments are valued in the tens of

billions of dollars for our company alone, and could be over \$100 billion for all the shippers. Shippers must make long-term ship or pay transportation commitments and agree to pay transportation and treating rates that are ultimately based on the final cost of the pipeline and treating facilities. The only information the shippers will know in advance of making these multi-billion dollar commitments will be a projection of the transportation charges based on the project sponsor's initial estimate of costs. The firm transportation commitments must be paid regardless of whether the shipper making those commitments actually transports gas through its reserved capacity and irrespective of the actual transportation charges. The shipper is also required to pay this reserved capacity commitment even if the market price for the gas is less than the cost of transportation.

For these reasons, the parties taking the risks for a project of this magnitude need to be able to manage those risks. The Producers, as shippers, cannot make firm transportation commitments during an open season unless they are confident the gas pipeline project can be built and operated cost effectively so that producing and shipping gas over the long-term is commercially viable.

INTEGRATED GAS PIPELINE PROJECT ECONOMICS

For this reason, AGIA needs to bring together the upstream and the midstream and provide for an integrated proposal. Any approach that evaluates them separately is flawed. Let me expand on this point. You heard last week that lenders evaluate the upstream very carefully when financing the midstream. The reason is simple - the upstream pays for the midstream. When I say upstream, I'm talking about the revenue generated from production and sale of the gas and liquids through the pipeline project. Without the commitment of capital to the pipeline by a producer-affiliate or the huge financial obligation required for firm transportation commitments to a third-party pipeline, there is no way the transportation system will be built. Thus, any analysis of the project which excludes midstream capital or the firm transportation commitments is not correct. Lenders and project sponsors do not make that mistake because they recognize that major gas pipeline projects are built on the back of direct capital commitments or, long-term, firm transportation commitments.

Since firm transportation commitments are legally binding commitments that are the backbone of any financing and essential to funding a pipeline, it only makes sense to account for these commitments when evaluating project economics. Surprisingly, the Administration's analysis of the economics fails to incorporate these financial obligations associated with underpinning the pipeline. Let me expand on this point by asking you to think about the economics from a shipper perspective. The shipper can either make the investment in the midstream through one of its pipeline affiliates or make a commitment to a third party to build the pipeline. In the case of making the commitment to a third party, the shipper must pay the third party for the cost of the pipeline plus a return to the pipeline builder for the investment he ultimately made, not what he projected the costs to be when the commitment was made. So in this case the shipper is paying for the ultimate cost of the pipeline plus the profit the pipeline builder requires. When you think about it this way, the economics have to be worse for the shipper when he makes a transportation commitment versus directly investing in the pipeline.

Because the Administration's economic analysis is flawed, the resulting assertion that the producer's stand-alone upstream economics are robust and improved without ownership of the pipeline is absolutely incorrect. Again, the upstream pays for the midstream and it is no more complicated than that.

Since it appears AGIA is based on this flawed economic analysis, it is critical the legislature address this issue and AGIA be modified to recognize who is taking the risk, the shipper. For ExxonMobil any decision to invest will be based on integrated project economics. It only makes sense for the State to evaluate the proposal on an integrated basis as well because the State is in the same position as the producers receiving the bulk of its revenue from the sale of gas. Because we both receive our revenue from the sale of gas, we should be aligned on the best approach for minimizing transportation costs and maximizing netback value.

IMPORTANCE OF STATE / PRODUCER ALIGNMENT AND BENEFITS OF

THE PRODUCER PROJECT

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

Maximizing the value to the State of Alaska and the resource holders means selecting the right design concept for this mega-project and then executing the Project to deliver the lowest possible cost and fastest possible completion. On a project of this size and magnitude, project construction and operating experience should be a significant consideration. Only a limited number of companies have demonstrated the capabilities, financial strength and arctic experience to effectively participate in and manage world-scale mega-projects.

The Producers have mega-project experience on numerous projects world-wide and have demonstrated success in meeting project objectives. A critical component of that experience is the Producers' Arctic experience in Alaska and throughout the world. ExxonMobil's arctic experience is extensive - over 40 years - with developments in multiple types of arctic environments. Large projects with significant complexity in harsh environments are what we do and we are extremely qualified to take on this work. ExxonMobil's global project development company is unique within industry and leads the industry in project cost and schedule performance.

ExxonMobil has also demonstrated world-class leadership in safety, health and environmental performance. ExxonMobil is a leader in operating efficiency and a pacesetter in operating safety.

In addition to our project and operational excellence, ExxonMobil has the financial strength to make this mega-project a reality. ExxonMobil has consistently maintained one of the strongest financial positions of any company in the world. We are one of just a few public companies to maintain the highest credit rating from Standard and Poor's (AAA) and Moody's (AAA), and we have done so for each of the last 88 years. Our financial strength minimizes the likelihood that external financing requirements will significantly delay the project timeline, even in times of financial market turmoil.

It is important to remember that the Alaska Gas Pipeline Project is a basin-opening project that will benefit the State and the oil and gas industry in Alaska for decades into the future. Basin-opening projects throughout the world have progressed and been successful when there is alignment between the host government and the leaseholders. The Producers and the State both want a pipeline project to commercialize the known ANS gas resources and open the basin to gas exploration.

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

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

Based on the demand for workers that this Project will generate, Alaskans are obviously key to successful project execution. Both the State and the Producers want Alaskans to benefit from the many job opportunities that will exist.

We believe that financial strength, experience and the ability to get the job done should be critical components of any evaluation of proposals. When you consider carefully the options available, a Producer pipeline will provide maximum value to the State of Alaska.

IMPORTANCE OF PREDICTABLE AND DURABLE FISCAL TERMS

I would now like to talk about fiscal predictability and its importance for a mega-project such as the Alaska Gas Pipeline Project. For ExxonMobil to progress this mega-project and mitigate its inherent risks, we will need to work together with the State on some very important fiscal issues. Because of the nature and magnitude of the risks associated with this Project, fiscal terms that are

predictable and durable are necessary. This is a common thread for any mega-project investments. In all such cases, we are willing to take geologic risks, we are willing to take cost risks, and we are willing to take commodity price risks, but we cannot take the risk of fiscal terms changing. Let me expand on this further. The first two risks, geologic and cost risk are risks for which we have developed an industry leading expertise to manage. This is what we do day after day at ExxonMobil. Market risk is inevitable in a commodity business such as oil and gas and we manage that by attempting to ensure that we deliver those products into the highest value market at the lowest cost. However, the risk of a change in fiscal terms is of a completely different nature and completely outside our control. We must have agreements that will allow us to develop this mega-project under predictable and durable terms, so that we can make an investment decision with an adequate degree of certainty. This does not mean that taxes cannot change over the life of the project. Predictability means that the State's tax and take terms are sufficiently understood that they can be defined and predictably modeled over time for purposes of evaluating the overall project economics. If fiscal terms can be changed in unpredictable ways in the future, then we are not able to make a well founded investment decision on behalf of our shareholders, nor will lenders be as confident in providing financing for a project of this size.

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

It is important for the State to recognize that for mega-project developments, governments do grant long term fiscal stability. These contracts include fiscal stability

protection that in some cases runs for the length of the contract and in other cases runs for 40 years or more.

AGIA should allow applicants to put forward their best proposal on what is required to make the project commercially viable, which will allow the State the opportunity to consider those proposals that have the best chance of actually delivering an Alaska gas pipeline.

ADDITIONAL FEEDBACK ON AGIA

I would like to now give some specific feedback on AGIA which is based on the conclusions and principles I've mentioned. I will also outline some additional thoughts on how AGIA should be modified to ensure the best chance of a successful result and allow the State to maximize value. As I previously stated, alignment between the State and the leaseholders is essential to a basin opening project of this magnitude. Therefore, establishing the right approach going forward is the most important activity for the project at this time. To be able to calculate the revenue from the upstream we must have clarity on the taxes and royalty from our oil and gas operations and the taxes and royalties must be set at a level that makes the project viable. In order to ensure a viable project from the outset, we believe this must be done at the beginning.

ExxonMobil recognizes the importance to the State, explorers and others of having access to the project so their gas can be treated and transported to markets. To ensure that a project is constructed, it must be commercially attractive to shippers at the time they make their initial firm transportation commitments. Shippers, particularly those who must invest substantially to explore for, develop and produce gas resources, will not be willing to enter into long-term financial commitments for the transportation of gas if they believe there is a substantial likelihood that their initial rates will be significantly increased in the future in order to accommodate expansions.

Under the Alaska Natural Gas Pipeline Act, Congress struck what it determined was the proper balance between encouraging investment by those willing to commit to pay for initial capacity and encouraging exploration by providing an opportunity for future access to the pipeline.

Because of the unique nature of the Alaska gas pipeline project, FERC approved unprecedented policies to enable a FERC-mandated expansion to benefit explorers. The issue of how potential future shippers may access initial capacity and future expansion capacity, if needed, should be administered by the FERC for all elements of the project in the United States.

In addition, the pipeline entity should not be required to accept a FERC certificate irrespective of FERC imposed conditions.

Under AGIA, the proposed upstream inducements would require significant modification to ensure a commercially viable project is obtained. In fact, we do not believe it is practical to address these terms in legislation. Therefore, it would be better for AGIA to not prescribe specific upstream terms and allow applicants to make proposals to address those terms.

AGIA also prescribes activities that must be completed within a specific timeframe or date certain. Setting arbitrary target dates is not consistent with good project management practices. Further, milestones are not necessary if the project is commercially viable. The Producers will progress the project at the maximum prudent pace, consistent with the industry proven "stage-gate" process for project development - there is no reason to do otherwise.

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

Finally, because of the complexity and risk associated with this project, the parties must have an efficient and impartial means of handling disagreements when they arise. We believe project related agreements should provide for binding neutral arbitration as the mechanism for resolving disputes. Binding neutral arbitration is widely utilized in U.S. and international commercial agreements and is not a new concept with the State of Alaska. Arbitration is the

method used to resolve disputes under the State's Royalty Settlement Agreements.

CONCLUSION

In closing, I would like to reiterate that ExxonMobil is committed to moving the Alaska Gas Pipeline Project forward. However, we cannot move the project forward if it is not commercially viable. AGIA as written does not provide for a commercially viable project. The Administration's stated goal for AGIA is to increase competition through an open and transparent process. However, in its current form, AGIA will result in less competition because it fails to adequately address the issues raised by those parties who will ultimately pay for the project. It also appears AGIA is based on flawed economic assumptions. It is critical that the legislature and administration address these problems in AGIA or we will end up with a process that sets unrealistic expectations and results in disappointment and failure. In addition, the existing prescriptive terms in AGIA will preclude ExxonMobil from being able to make an open, competitive and conforming proposal; thus, the State will be denied the opportunity to even consider terms from the party holding the largest discovered gas resource and has the capability to deliver a successful project.

ExxonMobil possesses the financial strength and project experience required to make this project a success. We are ready to work with the Administration and the Legislature to establish a process that recognizes the integrated nature of the project and mitigates the risks I've discussed to allow the project to progress. We suggest AGIA be amended to provide for a broad objective driven process that sets out what the State wants to achieve and allows each applicant to propose how best to meet those objectives and identify what is required from the State to advance the project. This process will secure more viable applications, create more competition, afford the State the opportunity to secure the most value and actually get the pipeline built. We are ready to participate in a competitive, open and transparent process as I've described, but unless AGIA is modified we will not be able to participate.

What we are struggling to understand is why the State is insisting on such a prescriptive way forward. AGIA should allow all interested parties to submit a conforming bid so that the people of the State of Alaska have the opportunity to see and compare all of the bids put forward to build the Alaska gas pipeline.

[2:49:34 PM](#)

Co-Chair Stedman remarked that AGIA should be constructive to the interests of both ExxonMobil and the State.

[2:50:12 PM](#)

Co-Chair Stedman requested the witness identify concerns with the bill and provide recommendations at a later date.

[2:51:25 PM](#)

Co-Chair Stedman spoke to the \$500 million reimbursement incentive intended to demonstrate the State's commitment to the natural gas pipeline project. He asked ExxonMobil's position on this proposal.

[2:52:01 PM](#)

Mr. Massey acknowledged that the Palin Administration needed to take action to "kick start" the project. However, the incentive would apply only to the pipeline itself and would not address the "critical" upstream issues, which would determine whether the project was undertaken. These issues had not been adequately or "appropriately" addressed in AGIA. If the State intended to invest in the project, it should "get return from it moving forward" and be a participant in the project. This would provide more leverage to the State and the AGIA applicant.

[2:53:36 PM](#)

Co-Chair Hoffman shared questions asked of him that he had committed to learning the answers. He asked if ExxonMobil was currently exploring for natural gas on the North Slope or had plans to explore in the future.

[2:54:03 PM](#)

Mr. Massey provided the following response.

We have ongoing work that is competitive in nature in terms of assessing the basin and where might be the most attractive exploration opportunities. The key will be [whether] we get a gas pipeline going. Right now we have discovered resources that are in a 35 tcf [trillion cubic feet] to keep this thing full for thirty-something years, we're going to need 50 tcf. So there's going to be plenty of opportunity to put gas into this pipe. And that's not even considering the fact that we should be able to expand the pipe.

The way I'd answer your question is: we're doing studies preparing for that. Those are competitive in nature. Our activities primarily on the Slope right now are focused on the oil side; maximizing the recovery of the discovered oil resource. Plus looking at oil opportunities that are around existing infrastructure that haven't been fully developed, need to be further explored. A lot of this activity is occurring at the western side of the Prudhoe Bay field right now where the partners are bringing on a significant field called the Orion [unverified] field. It wasn't thought to be attractive in significant resource and we're working to bring that on production.

[2:55:41 PM](#)

Co-Chair Hoffman listed facts considered in the questions posed to him, which he was relaying to the witness. Other companies were actively exploring for natural gas and the more identifiable reserves held by a company would provide a more accurate prediction of that company's actions during an open season. This legislation contained projections on the open season. Only 35 tcf of gas was currently identified and the amount must be at least doubled to allow for a viable pipeline project. ExxonMobil had the financial resources available for exploration activities and Mr. Massey asserted the company's commitment.

Co-Chair Hoffman considered a validation of a company's commitment was whether that company was actively pursuing "gas in Alaska". He asked if the witness agreed with this measurement of commitment to the Alaska natural gas pipeline.

[2:57:10 PM](#)

Mr. Massey answered that an adequate discovered gas resource existed to "back this firm commitment". However, it would be likely that the firm commitment could extend "beyond the plateau of this discovered resource", thus providing a strong incentive if ExxonMobil made the commitment, to identify additional resources.

Mr. Massey explained that the discovery process to "put any sort of sizable development on place" required ten years and included planning, conducting and evaluation of seismic surveys, drilling and ultimately development.

Mr. Massey considered this time period satisfactory, given that the pipeline project would last ten years. He opined, "Everyone will have a running start to build gas for the first expansion as well as build gas for the fill this gap back in the end."

Mr. Massey disagreed with Co-Chair Hoffman's characterization that a company that was not actively exploring demonstrated a lack of commitment. The commitment would "actually come from the discovered resource." Once the pipeline project was underway, "we won't have any trouble finding folks [to] go out and explore for gas" due to the ample opportunity for expansion.

Mr. Massey anticipated ExxonMobil would be one of those "folks". He stated, "We're quietly preparing ourselves for that ... opportunity, once we realize that gas on the North Slope is viable." Currently, the company did not have this assurance.

[2:59:29 PM](#)

Senator Thomas shared Co-Chair Hoffman's concerns. Discussion on this legislation had repeatedly focused on upstream risk. Lack of known resource was a major issue contributing to that risk. Efforts should be undertaken to reach the approximately 50 tcf capacity and while he appreciated ExxonMobil's stated commitment to the pipeline project, he questioned why the company was not "working toward confirming" the known resource to mitigate the risk.

[3:00:22 PM](#)

Mr. Massey understood the perception. Discovered gas reserves equaled 35 tcf but that amount was not currently commercially

viable. Therefore, the time and expense of exploration efforts would not be commercially viable either. Making the 35 tcf reserves commercially viable would mitigate the upstream risk. Sufficient discovered gas resources existed to make the "the initial commitment" and to "get the initial pipeline going." However, if not commercially viable, the commitment could not be made.

[3:01:31 PM](#)

Senator Thomas reported that the financiers share the concerns about the upstream risk, specifically the uncertainty of the known resources. While financiers could be willing to accept ExxonMobil's explanation and agree to finance the project, he surmised that more confirmation was necessary.

[3:02:08 PM](#)

Mr. Massey pointed out that the credit worthiness of the shipper that made the firm transportation commitment would also be evaluated. If ExxonMobil, ConocoPhillips and BP made the shipping commitment, and "the gas wasn't there" the financiers would have greater assurance of getting paid.

[3:03:11 PM](#)

Senator Huggins asked the optimum consortium of the pipeline sponsor, if it were to include ExxonMobil.

[3:03:41 PM](#)

Mr. Massey responded that the entities assuming the risk must have the capability to manage that risk. At present, ExxonMobil, Conoco Phillips and BP would comprise the optimum consortium. The State would assume a portion of the risk as well.

[3:05:00 PM](#)

Senator Elton furthered Co-Chair Hoffman and Senator Thomas' questioning. ExxonMobil's "2005 10k filing" with the Federal Trade Commission capitalized its wells located at Point Thomson. To do this, the company must make a determination that the field was commercially viable given the market conditions and technology.

[3:06:14 PM](#)

Mr. Massey responded that the Point Thomson wells "have been on the books for many years." ExxonMobil considered itself to be partaking in active discussion with the State to achieve a commercially viable project at that location. As a result, those wells could be capitalized.

[3:06:41 PM](#)

Senator Elton clarified that the determination was made by ExxonMobil in 2005 that given the current market conditions and current technology, the project was commercially viable.

[3:06:55 PM](#)

Mr. Massey answered, "I'd say we're in discussions with the State as to how to achieve a commercially viable project."

[3:07:06 PM](#)

Senator Elton contended that capitalization must be based on "what you think is true not what you think could be true given certain future events."

[3:07:23 PM](#)

Mr. Massey admitted he was not an expert in filing requirements and he repeated his previous response.

Co-Chair Stedman ended the discussion on this item.

[3:07:36 PM](#)

Senator Elton asked if the competition attested as necessary by ExxonMobil and other producers, could be achieved if the producers did not apply for the AGIA license. He asked if the producers could create a proposal to coincide with the timing of the public hearing process and legislative review process of the AGIA applications. This would allow the legislature to judge the producer's proposal in comparison to the AGIA application proposals.

[3:08:54 PM](#)

Mr. Massey deemed this possible. However, ExxonMobil would rather operate "in a full and conforming way" within the process established by the Administration so that its proposal would receive "the scrutiny, the debate, the comparisons with every other project that's been proposed". The Palin Administration had determined that AGIA would be the process.

[3:09:35 PM](#)

Co-Chair Stedman directed the discussion "away from the historic practices" and to "get down into the actual language". He intended to learn which sections of the bill were considered "positive" or "negative" to ExxonMobil. He requested the company submit suggested language. Concern was expressed about "some of the flawed analysis" that was not addressed in the bill.

[3:10:17 PM](#)

Co-Chair Stedman asked the witness to comment on the provision of subsection (3)(a) of Section 43.90.130. Application requirements, on page 5, lines 5 through 8, which required the AGIA licensee to conclude a binding open season no later than 36 months after the date the license was issued.

[3:10:54 PM](#)

Mr. Massey relayed the position of ExxonMobil that AGIA should not establish any date certain. ExxonMobil would intent to meet this timeframe, but it should not be a requirement.

[3:11:31 PM](#)

Co-Chair Stedman asked if this provision would be a "show stopper" that would prevent the company from submitting an AGIA application.

[3:11:43 PM](#)

Mr. Massey affirmed that ExxonMobil would not undertake a project that included an arbitrary deadline.

[3:12:06 PM](#)

Co-Chair Stedman noted the provision of subsection (5), on page 5 lines 25 through 27, which stipulated that the application

"commit that after the first binding open season, the applicant will assess the market demand for additional pipeline capacity at least every two years through public nonbinding solicitations or similar means." He asked if the witness considered this common practice.

[3:12:43 PM](#)

Mr. Massey responded as follows.

There's a number of must haves in here relating to expansion, open season requirements. Our suggestion would be that you turn those into a broad objective that the State wants to make sure that the project can be expanded and that there would be availability to access the pipe and allow each applicant to come forward and determine how best - how they would propose to achieve that overall objective.

Mr. Massey assured, "This stuff works its way out." If a party wanted the pipe expanded because of a discovery, it would approach the owner of the pipeline. The market would not have to be assessed every two years because "this is business, people know how to do these sort of things."

Mr. Massey qualified that compliance with the provision would not be overly cumbersome; however, it focused on "a detail that ought to be left to the applicant's proposal".

Mr. Massey reiterated that the provisions of this section pertained to the pipeline and did not address the upstream "critical issues" that would determine whether the pipeline project would be undertaken.

[3:14:13 PM](#)

Co-Chair Stedman understood the witness' concern with the upstream issues, but intended to review each section of the bill to "have a logical flow" to the discussion.

[3:14:35 PM](#)

Co-Chair Stedman next addressed subsection (7) on page 6, line 11, pertaining to rolled-in rates. The presumption of the FERC was that all parties preferred rolled-in rates.

[3:15:17 PM](#)

Mr. Massey understood the importance to the State that explorers had access to the pipeline. FERC had addressed this matter in "the proper way" and ruled that because of the unique nature of the project, it would approve "unprecedented policies to enable a FERC mandated expansion to benefit explorers." FERC was positioned to determine the proper rate for the expansion. FERC determined a presumption for rolled-in rates, but also announced that a subsidy would be considered in determining whether the rolled-in rate was appropriate. ExxonMobil did not oppose this. However, the provisions of AGIA included a "proposed 15 percent increase in the rate," which was too great of a risk. That increase could increase the cost of the tariff for the initial shippers by \$500 to \$800 million annually.

Mr. Massey suggested that the incentive that the State would be required to offset this tariff increase could be detrimental to the State. If the 15 percent rate increase was approved, ExxonMobil would factor the affect into its "economics" and would need "some sort of reduction on the upstream side to compensate for that." He did not consider such compensation by the State to be in the State's best interest.

[3:17:15 PM](#)

Co-Chair Stedman requested ExxonMobil conduct an analysis of the fiscal impact of this provision.

Mr. Massey agreed to do so.

[3:17:44 PM](#)

Co-Chair Stedman asked if the witness had comments on the provision of subsection (8) on page 7, line 29, relating to a North Slope gas treatment plant.

[3:17:57 PM](#)

Mr. Massey acknowledged that the applicant would have to address the gas treatment plant. This provision should be "broadened" to allow the applicant to "provide more description of how they intent to deal with the gas treatment plant." The requirement of "net book value" for "rate-making purposes" should instead be

"left up to the applicant" because "that particular approach" might not be in the best interest of the State or the applicant. The applicant should be allowed to propose how it would address the issue.

[3:18:41 PM](#)

Co-Chair Stedman next spoke to subsection (10) on page 8, lines 14, through 17, which would commit the applicant to a 70 percent debt to equity ratio. He relayed discussions about lowering the "equity position, all else being equal of course" because "the lower the tariff, the higher the net back, the better value to the State". A lower equity position would be in the interest of the State, "ruling out the impacts of the financing." He asked ExxonMobil's position on the ratio and whether it should be changed.

[3:19:26 PM](#)

Mr. Massey characterized this as another issue that should be "left to the applicant to come forward" and propose the ratio that would "drive their particular needs". The debt to equity ratio was only one portion of the tariff structure. The cost to construct the project would have the largest impact on the tariff.

[3:20:46 PM](#)

Co-Chair Stedman requested comment on subsection (12) on lines 21 and 22 that would "commit the applicant to provide for a minimum of five delivery points of natural gas in this state".

[3:20:54 PM](#)

Mr. Massey remarked "We're not talking about a lot of money here for a delivery point" and that the requirement should therefore be "left open for the applicant to describe".

[3:21:25 PM](#)

Co-Chair Stedman next asked the witness' position on the provision of subparagraph (16), on page 9, lines 9 through 11, which would require the applicant to waive the right to appeal the final FERC certificate ruling.

[3:21:43 PM](#)

Mr. Massey noted the advantages and disadvantages of this provision. It would be favored by unsuccessful AGIA applicants, but not favored by the successful applicant. Given the importance of this project, he surmised that participants would want the opportunity to appeal. This provision could "limit some folks from bidding."

[3:22:29 PM](#)

Senator Olson, returning to the provision of subsection (8), relayed a comment that the North Slope might not be the best location for the gas treatment plant due to the complexity of separating individual components of natural gas. He asked whether Mr. Massey agreed.

[3:22:58 PM](#)

Mr. Massey reported ExxonMobil's contention that the North Slope would be the best location for the gas treatment plant. This would allow for all the CO₂ to be removed and thus not shipped through the pipeline, which would subsequently create room in the pipeline for more gas.

[3:23:38 PM](#)

Co-Chair Hoffman requested the witness comment on the provision of subsection (15) on page 8 line 30, which would require "Alaska hire", to the extent permitted by law.

[3:24:02 PM](#)

Mr. Massey referred to his testimony, emphasizing that Alaskans would "play a very important role" in the project and should benefit from "the many job opportunities". He suggested this provision should be "broadened" to request that the applicant describe its "total Alaska hire plan".

[3:24:44 PM](#)

Co-Chair Stedman directed the witness to submit alternative language.

[3:24:56 PM](#)

Co-Chair Stedman continued to subsection (17) on page 9, lines 12 through 16, that would require the applicant to commit to negotiate a project labor agreement before construction.

[3:25:04 PM](#)

Mr. Massey deemed such a requirement as "premature at this time". Job opportunities would be available for union and nonunion workers. Project labor agreements should be negotiated by the major contractor of the project, if the contractor decided to enter into an agreement.

[3:26:08 PM](#)

Co-Chair Stedman spoke to subsection (20) on lines 28 through 30, which provided that the applicant must "otherwise demonstrate that the applicant is ready and able to perform the activities specified in the application, including the detailed work plan, timeline, and associated budget. He remarked that ExxonMobil had the financial means to undertake the project with or without external financing. He asked about availability of a workforce and materials such as steel, and the impact of competing projects elsewhere in the world.

[3:27:07 PM](#)

Mr. Massey advised that the applicant's ability to secure labor and materials should be considered. ExxonMobil expends \$20 billion per year for capital expenditures. Therefore, the company had "the muscle" to "move projects in and out of the cue" with various service providers. The Alaska natural gas pipeline project would be a "huge undertaking" that would "stretch the resources" and therefore, the successful applicant should have had access and continue to have access to the necessary resources to complete the project. ExxonMobil met this criterion.

[3:28:21 PM](#)

Co-Chair Stedman recalled testimony from a previous hearing in which Enbridge informed that the Alaska project would be too large for that company to undertake alone and would require it to change its capital structure. He asked if the project,

estimated to cost between \$20 and \$30 billion, would require ExxonMobil to change its capital structure.

[3:29:01 PM](#)

Mr. Massey answered it would not.

Mr. Massey further commented.

There's a lot of other things that you could build into this one, you know, experience in executing projects of similar scope. You're [going to] want to see that a person has the experience, that they've done something of this scale and magnitude. You know, can they provide the project management resources. You're [going to] want them to demonstrate that they have the project management resources that they can come to bear: what's their safety, health, environmental record; how do they go about quality management and assurance capabilities. One of the key things in a project is project control - how do you control the project, how do you know that the cost that you're getting is correct and your future projection of cost is right, you're [going to] want to make sure that an applicant has the capability and the processes to make sure that's done very well. Then it's just the overall integrity, business ethics - how comfortable are you from that standpoint with the company that you're picking; you're [going to] get the right deal.

Co-Chair Stedman suggested that ExxonMobil could recommend these factors as requirements of the AGIA applicants.

[3:30:28 PM](#)

Senator Olson responded to Mr. Massey's statement, "with all due respect", declaring that the integrity and business ethics record of ExxonMobil was likely the worst in the state. The Exxon Valdez oil spill was a "disaster" and 20 years after it occurred, "conflicts" remained unresolved. He therefore challenged the assertion that ExxonMobil's demonstrated experience would be a benefit to the State.

[3:31:05 PM](#)

Mr. Massey responded that the company had "learned from that particular incident" and had "improved our work processes and as a result, have become a much better company in terms of how we go about doing our business."

[3:31:37 PM](#)

Senator Dyson noted that testimony given by representatives of BP and ConocoPhillips opined that this project would not be "wildly or even profoundly profitable". He asked if ExxonMobil shared this position and if so, requested an analysis.

[3:32:18 PM](#)

Mr. Massey replied that the current provisions of AGIA did not provide him with sufficient information to determine whether the project would be commercially viable because he did not know which terms to utilize to calculate the project's economics. If the current provisions remained unchanged, the project would not be commercially viable and that he "would have to assume today that what's on the books will only get worse and that the taxes and so forth will go up over time."

[3:32:58 PM](#)

Senator Dyson asked the projects ExxonMobil had undertaken in North America that provided the fiscal certainty requested of this project.

[3:33:07 PM](#)

Mr. Massey set forth the following as a response.

I wish we had another project that we could be talking to somebody else on this continent that has this magnitude and potential impact. It has to do with the project and where this project is located; this project is in Alaska. Alaska gets 80, 90 percent of its revenue from the oil and gas business. Everywhere around the world where there are mega-projects, we get the sort of fiscal stability that I've described - predictability in terms of understanding what the taxes are. So mega-projects - that's what we get. That's the norm it's not the exception. And in many of those places around the world, they're in the same position as Alaska in that the bulk of their revenue comes from

their oil and gas operations as well. So when you take that context, the fact that Alaska, if they need some money in the future, where are they [going to] come - they're [going to] come to the oil and gas business. And that's why we have to understand what the taxes are and understand for a very long period that those taxes are not going to change and ultimately impact the commercial viability.

[3:34:22 PM](#)

Senator Elton stated that fiscal stability was a "big issue". He questioned the implication that Alaska operated such a "predatory tax regime" as to pose a greater risk than price fluctuation for the product or action taken by Hugo Chavez the leader of Venezuela in taking possession of an oil field in which ExxonMobil held partial ownership.

[3:35:46 PM](#)

Co-Chair Stedman noted that fiscal stability was addressed elsewhere in the legislation.

[3:36:11 PM](#)

Mr. Massey responded to Senator Elton's comment, saying that fiscal stability pertaining to mega projects was necessary to "encourage that investment". The Alaska natural gas pipeline would be a major project, a "basin opening" project. The developers must therefore know what the tax rates and royalty terms would be "such that we can make an adequate investment decision". Whether "Alaska is less risky or not" was irrelevant because "the risk does exist" and the State could change the taxes to an extent that it would "undermine" the fiscal stability.

[3:37:30 PM](#)

Senator Dyson requested a list of mega projects in which ExxonMobil was the project manager, not just part owner, as well as the size of those projects and the fiscal stability terms received from the sovereigns governing the locations of the projects.

[3:38:20 PM](#)

Mr. Massey cited "confidentiality protections" as the reason he would not provide the information. He directed Senator Dyson to review the "Interim Fiscal Interest Finding" compiled the previous year, which included a summary of all "major deals that had been put together and had been made public." It was not uncommon for major basin opening big projects "much, much smaller scale than this" to have 35 to 40 years of fiscal stability.

[3:38:58 PM](#)

Senator Dyson clarified that the witness could not state the projects in which ExxonMobil was the project manager.

[3:39:12 PM](#)

Mr. Massey answered, "Those agreements are signed between us and the country and they are confidential so we can not..."

[3:39:31 PM](#)

Senator Dyson interrupted to specify he was not requesting confidential agreement information, but rather inquired as to "the construction, management, project management that Exxon managed the project" to demonstrate Mr. Massey's claim that the company possessed the experience necessary to undertake the Alaska pipeline project.

[3:39:55 PM](#)

Mr. Massey agreed to provide "a couple of those".

Co-Chair Stedman requested the witness submit the information in writing and detail the date of construction, the consortium and entities involved, the management partner, the "dollar amounts" the geographic location, and "whatever terms that you can give the Committee that's not confidential". He indicated that the Committee had access to some of the confidential data.

Co-Chair Stedman pointed out the 22.5 percent tax structure "for ten years" currently in statute. Therefore, the tax was not "totally unknown".

[3:40:53 PM](#)

Co-Chair Stedman proceeded to Sec. 43.90.140. Initial application review; additional information requests; complete applications, on page 9 line 31 through page 10 line 14, asking the recommendations of ExxonMobil.

[3:41:17 PM](#)

Mr. Massey suggested this language be amended to allow for a "more efficient process" and that he would provide an example.

[3:42:14 PM](#)

Co-Chair Stedman asked the witness' position on the provisions of Sec. 43.90.160. Notice, review, and comment, on page 11 line 1.

[3:42:40 PM](#)

Mr. Massey expressed that the legislature should have access to "all the information". He stated that "from a constitutional test standpoint," the legislature "should be involved through enabling legislation like AGIA or the [former] Alaska Stranded Gas Act; then they should look at the applicants and approve the final selection of the applicant." This would "help the constitutionality of whatever deal we end up cutting." This provision was therefore, the "proper approach".

[3:43:18 PM](#)

Mr. Massey noted that Section 43.90.150. Proprietary information and trade secrets., on page 10 line 15, had been bypassed. He perceived this provision would require that an applicant's proprietary information and trade secrets be made public. ExxonMobil would not support this requirement. He predicted the State would receive no "quality bid" because "no one is going to give their trade secrets or proprietary information out to a competitor." In place of this language, the provision should stipulate that "if an applicant believes they have proprietary information that is a trade secret that they note that in their [application] when it's given and that not be made public."

[3:44:24 PM](#)

Co-Chair Stedman directed Mr. Massey to provide suggested language that would "allow access to information but still protect the corporate entities".

Mr. Massey did not oppose providing the proprietary information to the State but did oppose allowing access to that information by competitors.

[3:44:52 PM](#)

Co-Chair Stedman asked if ExxonMobil had concerns with the ranking of proposed projects with the net present value as provided for in Section 43.90.170. Application evaluation and ranking., on page 11 line 19.

[3:45:29 PM](#)

Mr. Massey identified the "overriding objective of the ranking" should be whether the proposal would "maximize the benefits to the State. Net present value (NPV) was only one factor of a multiple that should be considered. Other factors would include some that would be "qualitative rather than quantitative" such as "undiscounted cash flow".

[3:46:05 PM](#)

Co-Chair Stedman requested the witness provide suggested language.

[3:46:14 PM](#)

Co-Chair Stedman directed attention to Section 43.90.200. Certification by regulatory authority and project sanction., on page 14 line 9, and asked for comment.

[3:46:38 PM](#)

Mr. Massey remarked that this language was unnecessary, and should instead be "referred to as an objective of the State" and the applicant be allowed to propose how it would address expansions, open seasons, and access to the gas.

[3:47:21 PM](#)

Co-Chair Stedman next addressed Article 3. Resource Inducement., on page 19 line 25.

[3:47:26 PM](#)

Mr. Massey proposed that although the inducements listed in this portion of the bill reflected the State's "view ... of what they should be", the applicants should instead present the resource inducements that would make the project viable. The provisions of Section 43.90.300. Qualification for resource inducement., on page 19 line 26, would not allow for a commercially viable project. As a result, "significant modification" would be required, and should not be stipulated in legislation.

[3:48:56 PM](#)

Co-Chair Stedman spoke to Section 43.90.320. Gas production tax exemption., on page 22 line 12, which pertains to upstream fiscal stability. This provision would offer fiscal stability for entities that participate in the first binding open season and would offer that stability for ten years. He requested the witness' "feedback".

[3:49:08 PM](#)

Mr. Massey asserted that this provision would not provide adequate fiscal stability. The Palin Administration's recognition of the need for such stability was "important"; but this provision would address only "one aspect of the government take". Subsequently, no fiscal stability would exist, as all aspects must be addressed, including "where revenue comes from". He again recommended that the applicant be allowed to propose fiscal stability terms.

[3:49:51 PM](#)

Co-Chair Stedman announced preference to "operate under AGIA". However, numerous concerns were expressed, and therefore a "radical departure" could occur.

[3:50:43 PM](#)

Mr. Massey agreed and made the following statement.

What is necessary for us to be able to submit a conforming bid, will require significant change to AGIA [in its] current form. However, we would say that that should be in the State's best interest. ExxonMobil is the largest leaseholder of discovered gas resources. I believe you would want to see what we would propose in the way of an applicant that will allow this project to go forward. I think we bring a lot to the project itself in terms of our financial strength, our ability to execute, our ability to make the project a reality, and it would be a shame if we weren't allowed to participate in the AGIA process.

[3:51:42 PM](#)

Senator Elton understood ExxonMobil's desire to participate in the AGIA process, as well as the company's position that this bill was likely to not be "fixable". If ExxonMobil determined it could not participate in the AGIA application process, he encouraged it to participate in "an alternative way", which he defined as "putting what you think you need to build a gas pipeline on the table so that it can be part of the public discussion when the Governor goes to public hearings with hopefully a potential licensee; so that it can be part of the Legislature's deliberations during the 60-day permit" process.

[3:52:31 PM](#)

Senator Huggins pointed out some predictions of success of a natural gas pipeline project undertaken outside the AGIA process, as well other predictions that such a project would not be successful. He asked if ExxonMobil could envision a scenario in which it could collaborate with other entities and successfully construct a pipeline.

[3:53:04 PM](#)

Mr. Massey responded that the company must have a contract with the State that "describes how we're [going to] share the revenue on the upstream side of this project between the State and ourselves before we can go forward." He surmised such a contract could be entered into outside of the AGIA process under the provisions of the Alaska Stranded Gas Act, or "outside of legislation". Ultimately the contract would require legislative endorsement.

Mr. Massey, addressing Senator Elton's comments, assured that ExxonMobil would never "give up" on changing the provisions of AGIA. The project was "too important" and the company must participate in the AGIA process to "fix" the legislation.

[3:54:13 PM](#)

Co-Chair Stedman opined to Mr. Massey, "Hopefully the next time you show up here, we'll have a contract and be going forward under AGIA."

The bill was HELD in Committee.

#

ADJOURNMENT

Co-Chair Bert Stedman adjourned the meeting at [3:54:28 PM](#)