

ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON ENERGY

February 2, 2010

3:05 p.m.

MEMBERS PRESENT

Representative Bryce Edgmon, Co-Chair
Representative Charisse Millett, Co-Chair
Representative Nancy Dahlstrom
Representative Kyle Johansen
Representative Jay Ramras
Representative Pete Petersen
Representative Chris Tuck

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 306

"An Act declaring a state energy policy."

- MOVED CSHB 306(ENE) OUT OF COMMITTEE

OVERVIEW(S) - TONY PALMER, TRANSCANADA: AGIA GAS PIPELINE
PROJECT & OPEN SEASON

- HEARD

PREVIOUS COMMITTEE ACTION

BILL: HB 306

SHORT TITLE: STATE ENERGY POLICY

SPONSOR(s): ENERGY

01/19/10	(H)	READ THE FIRST TIME - REFERRALS
01/19/10	(H)	ENE, RES
01/26/10	(H)	ENE AT 3:00 PM BARNES 124
01/26/10	(H)	Heard & Held
01/26/10	(H)	MINUTE(ENE)
01/28/10	(H)	ENE AT 3:00 PM BARNES 124
01/28/10	(H)	Heard & Held
01/28/10	(H)	MINUTE(ENE)
02/02/10	(H)	ENE AT 3:00 PM BARNES 124

WITNESS REGISTER

TONY PALMER, President, TransCanada Alaska, LLC; Vice President, Alaska Development TransCanada
Calgary, Alberta, Canada

POSITION STATEMENT: Presented an overview on the AGIA Gas Pipeline Project & Open Season.

ACTION NARRATIVE

[3:05:09 PM](#)

CO-CHAIR BRYCE EDGMON called the House Special Committee on Energy meeting to order at 3:05 p.m. Present at the call to order were Representatives, Petersen, Dahlstrom, Johansen, Millett, and Edgmon. Representatives Tuck and Ramras arrived as the meeting was in progress.

HB 306-STATE ENERGY POLICY

[3:05:36 PM](#)

CO-CHAIR EDGMON announced the first order of business would be HOUSE BILL NO. 306, "An Act declaring a state energy policy."

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REPRESENTATIVE JOHANSEN moved Amendment 5 which read:

Page 2, line 22, following "export":
Insert "of power that is surplus to the
needs of Alaska communities"

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CO-CHAIR EDGMON objected for the purpose of discussion.

REPRESENTATIVE JOHANSEN informed the committee that Amendment 5 follows page 2, line 19, which read "encourage economic development by (A) promoting the development of renewable energy resources, including geothermal, wind, solar, hydroelectric, hydrokinetic, tidal, and biomass energy for use by Alaskans and for export." He explained the amendment says, "as soon as we take care of ourselves ... then we can export."

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REPRESENTATIVE EDGMON removed his objection. Hearing no further objection, Amendment 5 was adopted.

CO-CHAIR MILLETT moved to report HB 306 [as amended] out of committee with individual recommendations and the accompanying fiscal notes. There being no objection, CSHB 306(ENE) was reported out of the House Special Committee on Energy.

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The committee took an at-ease from 3:07 p.m. to 3:10 p.m.

[3:10:12 PM](#)

OVERVIEW(S): BY TONY PALMER, TRANSCANADA: AGIA GAS PIPELINE PROJECT & OPEN SEASON

CO-CHAIR EDGMON announced that the final order of business would be a presentation by Mr. Tony Palmer of TransCanada regarding the AGIA gas pipeline project and the open season.

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TONY PALMER, President, TransCanada Alaska, LLC; Vice President, Alaska Development TransCanada, introduced his colleagues. Mr. Palmer prefaced his presentation by informing the committee that the materials that were submitted to the Federal Energy Regulatory Commission (FERC) on January 29, 2010, are available on TransCanada's Alaska Pipeline Project (APP) website. He began his presentation by saying that this is an historic moment for TransCanada and ExxonMobil, as this is the first open season to be conducted for the project. During open season, the pipeline company provides potential customers with engineering, commercial, tariff cost, and other information. He pointed out that FERC regulations-unique to this project-require that this information is also available to the public and to competitors. Also during open season, TransCanada will seek shipper's contractual commitments through executed agreements. He displayed slide 2, that was a map indicating the proposed route of the project with two options: (1) to the Lower 48 market via Alberta; (2) to the U.S. and international markets via Valdez.

MR. PALMER highlighted that major pipeline projects proceed through several stages, beginning with a lengthy development stage. This project is presently in the development stage and will be through 2014. The development stage is divided into three periods: "prior to" open season is the period through

April 2010; open season is scheduled from May to July 2010; and "post" open season is the period from August 2010 through 2014. He stressed that no single commercial party can guarantee the success of a project; in fact, its success will take the cooperation and action of the pipeline project, producers, shippers, and governments.

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MR. PALMER displayed slide 4 that indicated achievements prior to open season. Firstly, he credited producers and shippers for their past achievements such as the exploration and development of gas reserves, and the research of potential gas markets. Secondly, Alaska's administration and legislature defined their objectives and moved forward under the Alaska Gasline Inducement Act (AGIA). Mr. Palmer noted that a critical requirement for any project is the achievement of local and state support. Thirdly, the U. S. government and FERC established the regulatory structure needed for the project, including the federal loan guarantee. Lastly, the Canadian government established the Northern Pipeline Act that is the regulatory and legislative structure needed for the project. He described the difficulties other pipeline projects have faced and said, "In order for any project to succeed, the project needs customers and you need regulatory approval. One of those does not make a successful project."

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CO-CHAIR MILLETT asked whether there is a third element that must be in alignment-in addition to regulatory and commercial-for the open season process.

MR. PALMER stated that there are roles for all players; governments, shippers, and pipeline companies. He said this subject will be addressed later in the presentation.

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CO-CHAIR MILLETT suggested that there is no alignment without the third elements, which are fiscal terms. She questioned whether the pipeline company really has all it needs up to this point. Co-Chair Millett said, "You don't have a pipeline without ... shippers, and you don't have shippers without fiscal terms, so, I guess the equation in my terms ... the third leg is missing."

MR. PALMER observed that this subject is a fundamental part of his presentation to follow. He did point out, however, that TransCanada is not a party to fiscal matters.

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REPRESENTATIVE PETERSEN asked whether the project has moved ahead of the Mackenzie Delta pipeline.

MR. PALMER opined that the projects are in different stages; the Mackenzie project has customers, but not regulatory approval, and the Alaska project needs a FERC certificate and to attract customers. Thus, the success of both projects relies on regulatory and commercial breakthroughs. Mr. Palmer returned to his presentation and pointed out that TransCanada has held a project Right-of-Way (ROW) through the Yukon since 1983. He then displayed slide 5 that listed the project's achievements to this date. Mr. Palmer re-stated his belief that the best way to complete the project is to align five parties; three North Slope producers, TransCanada, and the State of Alaska. What has been achieved so far is that TransCanada and the state aligned in 2008, TransCanada and ExxonMobil aligned in 2009, and TransCanada and ExxonMobil continue to offer equity positions to major parties that significantly commit gas in the initial open season. As of this date, there are no negotiations in progress with BP or ConocoPhillips. Additional achievements by the project include the following: initiated the FERC pre-filing process and interface with the Northern Pipeline Agency (NPA); commenced negotiations with First Nations in Canada and with Alaska Native groups; resolved withdrawn partner claims on previous projects; developed comprehensive Alberta and LNG alternatives; filed open season plan with FERC; and completed an in-state gas study.

MR. PALMER displayed a timeline on slide 6 that indicated the FERC filing [January 29] began a 60-day FERC review for the U.S. section of the project. After the review, there will be a public comment period through February 24, and a decision on the plan is expected by the end of March 2010.

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REPRESENTATIVE RAMRAS asked when the state's reimbursement obligation shifts from 50:50 to 90:10.

MR. PALMER explained if open season is conducted from May through the end of July, prior to the end of July, the state

will reimburse TransCanada up to 50 percent for prudently incurred costs. After August 1, the state will reimburse 90 percent of prudent costs up to the cap of \$500 million.

REPRESENTATIVE RAMRAS asked whether TransCanada would move forward with the pipeline project if the state were to terminate AGIA and ask TransCanada to participate.

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MR. PALMER recalled that TransCanada was granted the AGIA license under established rules that included obligations and rights for TransCanada. He observed neither TransCanada, nor the state, possess the right to "unilaterally change the deal." If the state decides not to proceed, TransCanada would look at the process used to terminate any arrangement. He opined TransCanada has met all of its obligations to date and will continue to do so, and so has the state.

REPRESENTATIVE RAMRAS surmised the parties want the same thing: a large diameter gas pipeline and all five parties involved. He asked what TransCanada would do if the state set aside its obligations under AGIA in order to foster an opportunity for participation by all five parties. Representative Ramras opined the benefits to all of the parties would be numerous.

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MR. PALMER reminded the committee of the process, beginning with the 2007 statute, that was available to "all comers" who wished to participate in the project. TransCanada decided to participate, filed the required documents, and was subjected to extensive review by the administration and the legislature. In addition, TransCanada committed to a schedule and has presented massive amounts of information to the state for examination. Its competitors have not been subjected to this review. At the same time, TransCanada continues to offer equity participation to the sponsors of its competitor. Furthermore, the schedule of the project has allowed all of TransCanada's competitors to see "our entire proposal today, that's an unusual circumstance." He then remarked:

If the state makes a decision, to go a different direction, I presume they'll have discussions with TransCanada as to how they'll proceed.

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REPRESENTATIVE RAMRAS said:

What would TransCanada do if the state opted to terminate its relationship with AGIA? Would you walk away from the project or is it still appealing, given that you have peeled so many layers of the onion back and have expressed a great deal of confidence in the ability to build out a program ... My interest is in what posture would TransCanada take if the state withdrew from AGIA? Would TransCanada still be interested in this project if it was going forward with its own dough?

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MR. PALMER acknowledged that there are specific circumstances in AGIA that allow either party to withdraw, and some incur defined or undefined penalties; however, "TransCanada has not made any decision ... as to what it would do in that circumstance because, quite frankly, we have not contemplated it ..." he said.

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MR. PALMER returned to slide 6 and pointed out that the open season in Alaska will continue concurrently with the Canadian open season for service to the Alberta Hub. Subsequent to that, he expects to take the remainder of the year resolving conditioned bids. He assured the committee that the timeframe scheduled to resolve conditioned bids is not related to any political schedule; in fact, the original schedule for open season was delayed because the administration and legislature took longer to review TransCanada's application for the AGIA license. Conversely, if the bids have no conditions, or there are no bids, TransCanada will not need 100 days to review them.

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CO-CHAIR MILLETT asked whether TransCanada has a regulated, guaranteed rate of return under the AGIA agreement.

MR. PALMER clarified that there is a regulated rate of return, but not a guaranteed rate of return. In further response to Co-Chair Millett, he explained the AGIA application had a "formulated approach for return on equity, which when we filed would have yielded a 14 percent return on equity.... We're now

offering for customers that commit in the initial open season a 12 percent rate of return."

CO-CHAIR MILLETT then asked whether the reduction is based on the increase of natural gas from shale in the market.

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MR. PALMER agreed that since 2008 oil and gas prices have fallen, there is an epic financial crisis, and shale gas is a more significant player in the natural gas market. However, TransCanada has responded to these additional components of competition, and has put forward a more competitive proposal that shifts risk away from customers to the pipeline company. In fact, TransCanada is "stretching to make the project advance."

CO-CHAIR MILLETT inquired as to TransCanada's "threshold" and if the company could adjust its rate of return any more.

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MR. PALMER offered to respond to Co-Chair Millett's question very shortly. He returned attention to Slide 7 that indicated the project has a comprehensive, credible, and competitive open season plan. He stated that TransCanada's and ExxonMobil's expertise is well-known, and highlighted that both companies move interstate and inter-provincial natural gas, and can get the regulatory approvals necessary to advance the project. As a matter of fact, TransCanada moves 20 percent of North America's gas every day. He opined ExxonMobil's expertise in gas treatment plants is unmatched; moreover, ExxonMobil brings to the project, in addition to the producer study conducted in 2001, over one-quarter million hours of work done to complete the FERC application and to better understand the cost, complexity, and scope of the project.

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MR. PALMER then addressed the question, posed by Co-Chair Millett, about how the project has responded to competition; slide 8 displayed the improved commercial terms and access now offered to parties that commit gas during the initial season. He explained that this is a discount offered to advance the project on an expedited basis. Also, TransCanada has proposed both the comprehensive Alberta and Valdez options. In response to discussions with shippers, the project designed a 48-inch,

3.0 billion cubic feet per day (Bcf/d) pipeline to Valdez, is allowing customers to leave the pipeline upstream of the hub, shortened the minimum contract term to 20-years, offered short-term, interruptible, overrun, and park-and-loan services, and offered shared development costs in the event of the termination of the pipeline. In terms of the discount provided in the initial open season, TransCanada proposes to improve the tolls by \$500 million per year for 25 years. Referring to the formulated approach for return on equity in the AGIA application, Mr. Palmer said that TransCanada now proposes a fixed 12 percent rate. Further changes to AGIA terms include an 80 percent capital recovery over the initial contract term, and a 70:30 debt to equity ratio for expansions. He continued to point out the facets of the improved terms offered by TransCanada, and explained how these changes lower the toll and shift risk from the customers to the pipeline company.

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REPRESENTATIVE DAHLSTROM asked what the driving force was behind lowering TransCanada's capital recovery from 100 percent to 80 percent over initial contract term.

MR. PALMER answered that the driving forces were negotiations with customers and the competitive position of the project. He then displayed slide 9 that indicated the options for shippers to choose from in the open season: (1) a pipeline from the North Slope to Alberta, 4.5 Bcf/d, approximately 1,700 miles long, 48-inch diameter, with gas delivered to North American markets; (2) a pipeline from the North Slope to Valdez, 3.0 Bcf/d, approximately 800 miles long, 48-inch diameter, with gas converted to liquefied natural gas (LNG) and delivered by ship to U.S. and international markets. Both options include: opportunities for Alaskans to take gas off the pipeline at a minimum of five off-takes in Alaska; a world-class natural gas treatment plant; and a 58-mile transmission line connecting natural gas supplies from the Point Thomson field to the plant.

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MR. PALMER displayed slide 10 and pointed out that the estimates shown are "in 2009 dollars." The capital cost of the project ranges from \$32 to \$41 billion with a target in-service date of 2020. To address questions about the tariff he stated the tariff range, including fuel, to the Alberta Hub is from \$2.80 to \$3.50. Using the U. S. Department of Energy 2010 Annual Energy Outlook (DOE AEO) forecast, the net-back estimate is from

\$3 to \$4 per one million Btu (MMBtu) during the 2020 to 2030 timeframe. He opined this estimate makes the project technically and commercially viable based on current project cost estimates and price forecasts. To further clarify, he said net-back is simply the market price less the tariff, from which producers must "pay their own costs, take their profits, and share with governments."

REPRESENTATIVE RAMRAS suggested that Mr. Palmer's estimates are a best case scenario. He asked Mr. Palmer to "re-state that information for me, and give me the worst case scenario, so that I can get it like that. What happens if we do peg out at the highest price, what happens if we have one or two open seasons that fail, what becomes the in-service date, how much is it going to cost a leaseholder if they're looking for a market ... what is that margin if it's the Chicago market and we're on the lower range of the estimate...?"

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MR. PALMER responded that he is representing TransCanada's best estimate as to what it will take to advance the project and the cooperation that is needed from other parties, including the state, to succeed. What is presented is the best estimate, not the best case, of the cost range for the project. In fact, TransCanada does not have a worst case alternative, or a best case alternative. In further response to Representative Ramras, he said the capital cost range produces a tariff range of from \$2.80 to \$3.50. Taking the lower end of the Albert Hub gas price, \$6.25, and deducting the higher end of the tariff range, \$3.50, leaves \$2.75. The opposite, deducting \$2.80 from \$7.65, leaves \$4.75. This is still a fair range, between \$3 and \$4, with the numbers rounded at both ends. He opined it is not fair to take the DOE AEO forecast and arbitrarily deduct \$1 because this is an independent forecast that has been used consistently in front of this committee for four years.

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REPRESENTATIVE RAMRAS asked about the tariff to move the gas from Alberta to the Chicago market.

MR. PALMER said he provided a tariff range and gas price for gas at the Alberta Hub; there will be an additional tariff to take the gas to Chicago, although the price of the gas there is generally higher. Often the higher price is equal to the additional transportation cost, but it can be higher or lower.

Mr. Palmer called attention to slide 11 that displayed a comparison of DOE AEO forecasts for Alberta Hub natural gas prices. He noted that at the time of the AGIA application, the latest forecast available was dated December 2006. Based on forecasts through December 2009, the average estimated gas prices from 2020 to 2030 are: \$6.19, \$6.33, \$7.64, and \$6.79. Slide 12 displayed project cost estimates for the pipeline from the North Slope to Valdez. The capital cost range is from \$20 billion to \$26 billion with a targeted in-service date of 2020. The tariff range including fuel, is from \$2.45 to \$3.15, but does not include the cost of liquefaction or shipping to market. He said he used the Henry Hub index to estimate the gas price; however, if the gas is shipped to the Costa Azul LNG plant in Baja California, Mexico, and then back up to San Diego, or Los Angeles, the \$6.75 to \$8.15 price is too high. Secondly, in order to estimate the Asian market, he used DOE AEO estimates for oil prices. He reasoned that LNG prices in Asia are adjusted on an oil equivalency basis and provided DOE AEO forecasts for imported oil prices from December 2006, through December 2009, on slide 13.

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MR. PALMER displayed slide 14 and turned to the subject of the commercial and regulatory milestones that are needed to bring the project through the development stage to construction and in-service. Firstly, TransCanada expects that the bids received in open season will be conditioned bids; thus it will work with producers and shippers to resolve any conditions presented. Secondly, TransCanada needs to move forward with engineering, environmental, field work, and other work to prepare for major U.S. and Canadian permitting. In fact, contracts have been awarded to commence Alaska and Canada field work. TransCanada will meet its AGIA obligations, including the FERC application in 2012, and will advance the project in-step with commercial and regulatory breakthroughs while prudently managing expenses. Lastly, TransCanada and ExxonMobil will continue to seek alignment with BP and ConocoPhillips.

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CO-CHAIR MILLETT asked whether TransCanada normally adjusts commercial terms and risk ratios in order to entice producers to a pipeline project.

MR. PALMER pointed out that the normal procedure would be for negotiations to be in private-unlike this case-and commercial

terms often get adjusted, sometimes up, and sometimes down. He acknowledged that he has never seen a \$500 million reduction of the toll, however, this is a massive project, and "that's why you see such very large numbers on the table." In further response to Co-Chair Millet, he estimated that the return on equity on TransCanada's existing, in-the-ground, 50-year operational pipelines that are regulated by the (Canadian) National Energy Board, was 8 percent to 9 percent. He reminded the committee that the aforementioned percentage is a 40 percent equity ratio on a project that has been in the ground for 50 years, without the risks of completion, development, and construction. Moreover, if the calculation was "8 and a half on 40 percent, versus the 12 percent on 25, you would actually get a higher set of tolls."

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REPRESENTATIVE DAHLSTROM asked whether TransCanada has received any response from BP or ConocoPhillips.

MR. PALMER said there have been no negotiations on the project regarding the offer on equity. He recalled that negotiations with ExxonMobil began in the fall of 2008, and were not completed until June 2009. In further response to Representative Dahlstrom, he said, "To date, they have not been responsive to our offer."

MR. PALMER continued his presentation and spoke about the questions raised earlier by Co-Chair Millett. Slide 15 displayed the commercial and regulatory milestones that are required of other parties for the project to succeed: producers and shippers must resolve the conditional bids subsequent to the settlement of fiscal terms with the state as the "sovereign"; production levels must be resolved with the state and the Alaska Oil and Gas Conservation Commission (AOGCC). TransCanada was asked "to stay out of those issues" during the AGIA process.

CO-CHAIR MILLETT asked, "Doesn't that put your pipeline in a very interesting situation?"

MR. PALMER agreed, but advised that pipeline companies are never a party to upstream fiscal issues. He remarked:

Now, if that is a condition that customers require, in order to commit to the pipeline, clearly, we want to see it resolved. But we're not empowered to do

anything about it. We have to implore, ask, folks like yourselves to decide if you wish to engage.

MR. PALMER, in further response to a follow-up question by Co-Chair Millett, agreed that TransCanada is positioned between the state and the producers. Although not identical to the unique structure of AGIA, a similar situation occurred when there was a franchise to serve Alberta customers on TransCanada's pipeline system. At that time, TransCanada was aligned with governments; in fact, alignment with governments is critical in any basin-opening situation, like this one.

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CO-CHAIR MILLETT asked whether there were other government entities that had offered TransCanada inducements for pipeline projects.

MR. PALMER responded that when the original TransCanada pipeline across Canada was proposed, there was a decade of conflict; ultimately, the government of Canada invested money and had to guarantee debt for a portion of the project. Once the project succeeded, TransCanada repaid the debt, but the government acted as a financial backstop and made a contribution so that the pipeline went into service. He concluded that TransCanada has received inducements before to advance projects.

CO-CHAIR MILLETT remarked:

At a 90:10 sharing of costs, when do you determine that it's not profitable, and when do you stop? Do you stop when the \$50 million is gone, do you stop before? ... My fear is, have we now ... positioned you to a place where you, through the AGIA license, have to go ahead and continue with ... the project even if we can all look at it and wonder how anybody is going to ship gas....

MR. PALMER reflected that the terms are improved since the AGIA application. He acknowledged that there are provisions for both parties to withdraw from AGIA under certain circumstances, one of which is if the parties determine the project is uneconomic. However, TransCanada does not feel that is the case and has invested over \$60 million since the license was granted. To date, it has received \$1.1 million in reimbursement from the state. If TransCanada, or the state, sees that the project is no longer economic there is a vehicle to terminate. He opined

despite skepticism due to recent changes such as shale gas, the financial crisis, and increased costs, TransCanada and ExxonMobil believe the project makes sense. If there is no gas committed, "Then we'll all have to look at the circumstances at the time, but we're obligated, under AGIA to continue with the project, unless we feel it's uneconomic, and even if we feel that, we need your agreement to terminate...."

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REPRESENTATIVE RAMRAS expressed his belief that the most expedient way for Alaska to monetize its gas is for both sides to withdraw from AGIA, and after the election all five parties revisit the project. However, at this time he asked Mr. Palmer about allowable production by AOGCC, and to compare the nomination of gas to the Valdez or Alberta projects as to the size of the gas conditioning plant and on the Valdez side, the cost of the LNG facility and tankers.

MR. PALMER answered that the design option to Alberta is 4.5 Bcf/d and the design option to Valdez is 3.0 Bcf/d. Because there is insufficient volume for both, he opined the options are "either or" and customers will choose Alberta or Valdez. Regarding the gas treatment plant, he confirmed that there will be a larger volume at the inlet side of the plant for both options. The volumes going into the plants are higher because 11 percent to 12 percent of CO2 and other impurities are removed from the Prudhoe Bay gas.

MR. PALMER returned to slide 15. Additional commercial and regulatory milestones required for the success of the project are: customers must also arrange downstream transportation, secure final gas markets, and if needed, secure export permits; the state must resolve any upstream tax or production issues with producers and continue to facilitate project permitting; the U.S. government and FERC must establish the level, terms, and conditions of the federal loan guarantee and facilitate project permitting; and the Canadian government, Alaska Natives, and Canadian First Nations must facilitate project permitting and align with the project. Slide 16 was a summary of the presentation. Mr. Palmer reiterated that this is the time for all of the parties to come together and move the project forward to success for Alaskans, and for North American and international markets.

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REPRESENTATIVE PETERSEN shared information regarding problems with shale gas developments such as the amount of water needed and the subsequent contamination of drinking water. He cautioned that the future of shale gas is unknown.

MR. PALMER observed that the volumes of shale gas available are huge. Positive and negative "cards will be played out in the next few years."

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CO-CHAIR EDGMON adjourned the House Special Committee on Energy meeting at 4:[42] p.m.