

HOUSE FINANCE COMMITTEE  
April 4, 2011  
8:39 a.m.

8:39:02 AM

CALL TO ORDER

Co-Chair Thomas called the House Finance Committee meeting to order at 8:39 a.m.

MEMBERS PRESENT

Representative Bill Thomas Jr., Co-Chair  
Representative Anna Fairclough, Vice-Chair  
Representative Mia Costello  
Representative Mike Doogan  
Representative Bryce Edgmon  
Representative Les Gara  
Representative David Guttenberg  
Representative Reggie Joule  
Representative Mike Hawker (Alternate)  
Representative Tammie Wilson

MEMBERS ABSENT

Representative Bill Stoltze, Co-Chair

ALSO PRESENT

Representative Kurt Olson; Representative Mike Chenault, Sponsor; Tom Wright, Staff, Representative Mike Chenault; Donald Bullock, Attorney, Legislative Legal Services; Roger Marks, Legislative Consultant, Legislative Budget and Audit Committee.

SUMMARY

HB 142      PRESUMPTION AGIA PROJECT IS UNECONOMICAL

HB 142 was HEARD and HELD in committee for further consideration.

#hb142

HOUSE BILL NO. 142

"An Act relating to the creation of a rebuttable presumption that the project licensed under the Alaska Gasline Inducement Act is uneconomic because of insufficient firm transportation commitments during the first open season."

[8:39:26 AM](#)

REPRESENTATIVE MIKE CHENAULT, SPONSOR, introduced HB 142. He provided history; just over three years ago, Alaska Gasline Inducement Act (AGIA) was passed and TransCanada was authorized to pursue the project. He reported that TransCanada conducted an open season for the duration of April 30, 2010 through July 2010 and announced bids from multiple parties with a significant interest. TransCanada expected the negotiation of precedence agreements by the end of 2010. He informed the committee that three months later, the self-imposed deadline remained unmet. He stated that the unmet deadline was not an indication of a failure on the part of TransCanada.

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Representative Chenault explained that the state and legislature had no knowledge of the bids, the conditions attached, or negotiations toward the precedent agreements. Under AGIA, the state promised up to \$500 million in reimbursements to TransCanada. Alaska paid up to 50 percent of the qualified expenses up to the end of the first open season, \$36 million. After open season, the state would pay 90 percent. TransCanada had not submitted all requests, but the governor included \$160 million dollars in the FY12 budget request. The state paid a great share despite all of the unknowns, while world economic conditions changed dramatically. Gas prices remained at extremely low levels. Major gas discoveries came into production rapidly to serve potential markets for Alaska gas.

Representative Chenault questioned whether AGIA was still economical for Alaska. He asserted that the administration must prove that the investment was sound. He stated that he did not want Alaska to waste time and opportunity to develop the resource.

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Representative Gara believed the worst thing that could happen was a breach of contract on the largest future

project for the state. He opined that walking away from a contract where a party met obligations would prove detrimental for the state.

Representative Chenault opined that the bill would not breach the contract but would force the administration to revisit the legislature and prove the economic viability of the project.

Representative Doogan clarified that the state paid a certain amount of money and the governor requested an increase of funding to \$300 million.

Representative Chenault agreed.

Representative Doogan continued that HB 142 presented an opportunity to the legislature to intervene in the process.

Representative Chenault clarified the intention that the administration would communicate with TransCanada and return with a determination whether the project was economical allowing for a decision to be made.

Representative Doogan asked who would make the decision.

Representative Chenault responded that the administration would make the decision.

Representative Doogan asked if a valid contract between state and TransCanada existed to go to Federal Energy Regulatory Commission (FERC) license.

Representative Chenault pointed out a clause in the contract that would allow either or both parties to determine that the project was uneconomical and would be able to back out of the contract.

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Representative Doogan understood the contract differently.

Representative Gara inferred that the project was dead and uneconomical if TransCanada failed to disclose firm transportation commitments by July 15, 2011. He asked if the date of July 15, 2011 existed as a firm transportation commitment in either the license or the statute.

TOM WRIGHT, STAFF, REPRESENTATIVE MIKE CHENAULT, replied that the language in the bill should be changed to state "precedent agreement. He explained that the intent stated by TransCanada and filed with FERC included precedent agreements by December 31st 2011. He clarified that the bill ought to state "precedent agreement" rather than "firm transportation commitments."

Representative Gara noted that the July 15, 2011 did not exist in either the license or the statute.

Mr. Wright responded correct.

Representative Guttenberg asked whether the Department of Law had provided an opinion regarding the contract.

Representative Chenault replied that he had not solicited the information from the Department of Law. He believed that the administration had asked the questions of the attorney general, but he was not aware of an answer. He suggested that Representative Guttenberg ask the administration.

Vice-chair Fairclough admitted that her statement was anecdotal. She continued that when AGIA was passed and a contract was awarded, an expectation from general public was established that Alaskans would know whether a viable project existed. She asked if the expectations were reasonable.

Representative Chenault agreed with the vice-chair's stated expectation of Alaskans regarding a viable project. He asserted that the AGIA process was sold to Alaskans through previous administrations as the only viable way to bring a gas pipeline forward in the state. The process did not outlaw the producers from bidding on the project. TransCanada bid on the project and he opined that TransCanada was a world class pipeline corporation. He respected the organization of TransCanada. The idea was proposed to get Alaska out from underneath the "thumbs" of the big three producers. However, within a week of the issuance of the license, the chairman of TransCanada was asked when go forward and his response was "When Exxon says we are ready to go." He described that as the first "eye-opener" for Alaskans and the legislature.

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Representative Chenault believed that the contract had to be met, although he did not personally agree with the projects. He thought a crossroads had been reached and decisions must be made. He stressed that the issue was the economical nature of the project. He feared that \$500 million could be spent, without the finality of gas production and export.

Vice-chair Fairclough recalled concern by the general public about spending \$500 million. She pointed out that \$136 million had been spent without a clear understanding of the benefits gained by the expense.

Representative Chenault agreed.

Vice-chair Fairclough understood that tax structure was a key component of the argument. She noted that the legislature was fighting internally. She read in the newspaper that tax certainty was essential and the tax structure was failing. She suggested that those seeking economic certainty were in opposition to the bill. She asked if the terms of the tax structure were sufficient for the producers to commit gas to the AGIA or Denali projects.

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Representative Chenault responded that gas certainty would eventually become part of any gas project. TransCanada would not negotiate the tax certainty issue. Alaska would negotiate with potential shippers. The AGIA process would address the cost of the project and negotiate without third-party involvement.

Representative Wilson asked about a requirement to inform the public about the outcome of the open season.

Representative Chenault replied that TransCanada would have to disclose the information. He believed that disclosure must occur within ten days of filing for the FERC license. The deadline regarding results was self-imposed by TransCanada.

Representative Wilson recalled hearing that the public would receive information about the open season soon after the election in November. She asked whether the bill would allow disclosure sooner.

Representative Chenault believed not since the deadline was self-imposed.

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Mr. Wright provided an overview of HB 142. He urged the committee to adopt the words "precedent agreement" rather than "firm transportation commitment." The bill required the administration to prove to the legislature that the project was economic. If the bill was not deemed economic, then the administration was required to submit a report to the legislature rebutting the presumption before August 15, 2011. The legislature might also state that there was insufficient evidence to rebut the presumption in conjunction with a request for an appropriation for the reimbursement of qualified expenditures for FY 2013 and provide testimony and evidence that the project had credit sufficient to finance construction. The administration shall notify the legislature before August 1, 2011 whether the commitments are disclosed to the commissioners before July 15th and report whether the disclosed commitments were sufficient to support development of the project. The report should be submitted by August 15, 2011. Should the administration state that they were unable to rebut the evidence, they would be requested to initiate abandonment per AGIA Section 43.90.240. The abandonment clause was complicated and could be initiated by either one or both parties.

Representative Gara asked if the legislation presented a bridge of contract. He maintained that a contract was signed and a bill passed.

Mr. Wright retorted that the statement existed already in law in AS 43.90.240 as abandonment of project.

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Representative Gara argued that the bill changed the rules constituting the presumption that the project was not economic. He pointed out that the new bill was not in the license or in the original statute as a basis for exiting the contract. He expressed concern that the bill might be viewed as a breach of contract and may potentially expose the state to a large amount of damages rather than moving ahead toward a gas pipeline.

Mr. Wright responded that changing economic conditions occurred throughout the country and the world. He stressed that the legislation did not intend to violate a contract. He stated that if the project was deemed uneconomic, and the precedent agreements or firm transportation commitments were not reached, then the administration was to inform the legislature.

Representative Guttenberg recalled that the legislature had access to reports, records, and requirements for TransCanada. He asked whether the records had been investigated.

Mr. Wright responded that the Alaska Gasline Project website provided information. He understood that TransCanada expected to have precedent agreements in place by December 31, 2011. He stated that his office did not have access to internal information as much of it was confidential and proprietary.

Representative Guttenberg stated that AS 43.92.20 allowed commissioners access to records. He expected some arbitrary dates and commitments.

Mr. Wright stated that he did not have the answer. He believed the administration had more information as well as TransCanada

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DONALD BULLOCK, ATTORNEY, LEGISLATIVE LEGAL SERVICES, reported that he participated in the drafting of AGIA. He opined that the proposed legislation did not breach the contract but instead raised questions of legitimate legislative concern. He cited the reimbursement in 43.90.110, which stated "subject to appropriation, state matching contributions in the form of reimbursements." He noted that the appropriation comes up every year. He asserted that the bill did not take action; there was clear division of authority between the legislative branch and the executive branch. The executive branch was responsible for carrying out the license: auditing, reviewing TransCanada's expenditures, access to on-going information. House Bill 142 raised the question of the viability of the project. He stated that AGIA provided the "out," AS 43.92.40 if the project was uneconomic. The bill did not

deem the project uneconomic conclusively because of the response that commissioners can make after August 1st or August 15th when they were required to respond and provide information to the state.

Mr. Bullock pointed out the discussed dates addressing the agreement between the state and TransCanada. He referred to other relevant documents including the open season notice published by TransCanada last summer. He pointed out that the notice included past dates. Some of the dates referred to public information regarding the open season response including notices to the bidders. He stated that AGIA required the open season dates. He mentioned the importance of the increase in shared contributions and questions about the open season. He mentioned a provision regarding the inducements offered to producers who committed during the first binding open season. He pointed out royalty provisions for commitments made during the first open season. The provisions related to the fiscal future of the state. He maintained that HB 142 did not change the contract, but provided a request for information regarding AGIA and commitments.

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Representative Hawker spoke to concerns about HB 142 interfering with the contractual agreement between the state, TransCanada, and Exxon Mobil. He clarified the date of the self-imposed deadline for completion of the precedent agreement as December 3, 2010 rather than 2011. He opined that the bill paid careful attention to avoid a conflict or interference in the existing contractual relationship. He requested confirmation from Mr. Bullock that the language in the bill did not involve the contractual relationship.

Representative Hawker pointed to Page 1, Line 12, and the action item stating that the commissioners shall notify the legislature. He pointed out Page 1, Line 14, which stated that communication shall report whether firm commitments were disclosed and sufficient to support the project. He cited Page 2, Line 3, which was under the conditional, if the presumption in Item 1 is raised. The only mandate was for the administration to submit a report to the legislature as stated in Line 3. The other requirement stated was that the administration provided testimony and evidence implicitly to the legislature. He stated that

these action items do not address the operation of the contract.

Representative Hawker pointed out Page 2, Lines 18 - 20, Section C, which state that nothing in the legislation proposed, precluded the agreement between the commissioners and the licensee. The bill clearly stated that it did not have any effect on the obligations, roles, responsibilities or possible execution under that provision. He maintained that the bill created a relationship between the legislature and the administration.

Mr. Bullock agreed.

[9:17:41 AM](#)

Representative Costello asked whether AGIA was a traditional contract.

Mr. Bullock responded that AGIA was a license issued by the state including commitments stated in 43.91.10. He stated that the commitments included that the state share in the costs of developing the pipeline project and provide the services of the AGIA coordinator. The consideration offered by TransCanada included the "must haves" in 41.91.30 or the commitments required to qualify for the license and receive the money; contractual aspects and procurement aspects. The procurement aspects included in advance of the license, the state advertised it and explained the expectations of the state in return for a response to the commitments.

Representative Costello asked if when the assertion was made that the contract or agreement was breached, then a timeline requiring communication by a specific date was established by the proposed legislation. She supposed that the legislation required the communication by a specific date.

Mr. Bullock agreed, but added that the language was not limited to the communication between TransCanada and the state. He opined that the statement made by TransCanada that they would like to inform the state in December the extent in which they had enjoyed success during the open season, was an informal comment. He mentioned other dates established in TransCanada's open season notes. The dates were incorporated in the order approving a plan for open season. Some of the dates had come and gone. House Bill 142

was simply requesting information regarding AGIA. He highlighted that AGIA stated the commitments and promises of the state and interest in sharing the contributions, which were relevant issues of legislative concern. The bill asked the administration whether the money was spent on an appropriate project.

Representative Costello understood that the state was without a project until they heard the words "precedent agreement." She asked whether project could be economic based on the existence of bids or was a resolution of conditions required in the precedent agreement before the project was determined to be economic.

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Mr. Bullock opined that the ideal method of establishing the viability of the project would include a review of the standards for abandonment. Timing was a different issue. The commissioners agreed that additional time was necessary. The arbitration panel would consider whether the project was uneconomic. The panel only gets involved in the events of disagreements between the commissioners and TransCanada. The arbitration panel would then make a determination that the project was uneconomic only if the panel finds that the party claiming the project was uneconomic as proven by a preponderance of the evidence. He quoted the statute "the project does not have credit support sufficient to finance construction of the project through firm transportation commitments, government assistance, or other external sources of financing." "The predicted cost of transportation at a 100 percent load factor when deducted from a predicted gas sales revenue using publicly available predictions of future gas prices, but result in a producer rate of return that is below the rate typically accepted by a prudent oil and gas exploration and production company for incremental upstream investment that is required to produce and deliver gas to the project." He asked if enough commitment existed to fill the pipeline and whether the tariff was low enough so that people putting gas into the pipeline at the Alaska end could profit.

Representative Gara never thought he would see the legislature try to kill a project that Alaskans have been working toward for 30 years. He reported that he once practiced law as an assistant attorney general on oil and

gas issues. He argued the statement that the proposed legislation did not breach the contract.

Representative Gara referred to Page 1, which stated that "by July 15th 2011, transportation commitments have to be put forward and if they are not, there is a brand new rebuttable presumption that the project is uneconomic, which gives the state greater power than to back out of the contract." He asked if the rebuttable assumption that the project is uneconomic existed in license, contract, or statute.

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Mr. Bullock questioned the premise of the question. He stated that TransCanada would not rebut the presumption. He maintained that there was no additional burden on TransCanada. He informed the committee that the administration would rebut the presumption.

Representative Gara asked whether the provision that a rebuttable presumption existed in license and in statute. He believed that the language was new and did not exist in the license and the statute.

Mr. Bullock agreed. He stressed that the legislation did not amend AGIA, but instead asked questions regarding the provision included in AGIA. The ongoing issue was whether the project continued to prove uneconomic.

Representative Gara countered that the rebuttable presumption provided the state a greater power to back out of the contract.

Mr. Bullock responded no, the rebuttable presumption did not provide the state a greater authority to back out of the contract. The ultimate issue, whether the contract would be abandoned were within the terms of AS 43.90.240, a provision enacted before the license was issued. The bill did not change the provision.

Representative Gara asked if the bill accomplished anything.

Mr. Bullock replied no.

Representative Gara asked why the bill the bill was necessary.

Mr. Bullock responded that the legislature required the information mandated by the legislation. He believed that the legislature should know how and where the money was spent. The information would enable the legislature to determine whether the money was well spent.

Representative Gara found Mr. Bullock's testimony inconsistent. He asserted that if the existing bill carried the required contracts then HB 142 was unnecessary. The existing law created no rebuttable presumption language, nor did it advise the state to back out in the event of a rebuttable presumption. The existing law did not create any July 15th, 2011 language. He argued the need for the bill unless there was a desire to change AGIA.

Mr. Bullock wondered what questions the committee might ask the administration and TransCanada following the request of an appropriation of \$160 million.

[9:27:44 AM](#)

Representative Gara contended that existing legislation contained no rebuttable presumption and the bill would create one. He expressed interest in the attorney general's opinion of the proposed legislation.

Mr. Wright agreed. He maintained that the bill did not provide a breach of contract, but he instead viewed the bill as a means to determine whether the project remains economic.

Representative Hawker referred to statements that the "bill kills the gasline" and that "the bill requires transportation commitments to be put forward by a date certain." He asked Mr. Bullock if the bill required firm transportation commitments to be put forward by a certain date.

Mr. Bullock responded no.

Representative Hawker asked about the statement that the bill was "attempting to change AGIA law." He asked if any language included in HB 142 changed the AGIA law.

Mr. Bullock stated that the bill made no amendments to AGIA.

Representative Hawker asked if the proposed legislation accomplished any action other than posing the question to the administration from the legislature.

Mr. Bullock responded no. The bill only requested information for the legislature for the purpose of their decision making regarding ongoing appropriations.

Representative Doogan asked who the contract existed between.

Mr. Bullock responded the commissioners of Department of Revenue (DOR) and Department of Natural Resources (DNR) and TransCanada and Foothills Ltd. who represented the licensee.

Representative Doogan asked if "we" were a party to the contract.

Mr. Bullock responded that if "we" was the state then yes, but "we" was the executive branch then no. He furthered that the executive branch was responsible for implementing the contract and ensuring that terms were met. He stated that the legislature was initially responsible for enacting the terms of AGIA including the required commitments and the annual appropriation of money toward the contract or to reimburse the contributions.

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Representative Doogan commented on expectations regarding the passage of HB 142. He understood that AGIA maintained that TransCanada would do everything it could to get a pipeline financed and built. He understood that the real obligation was to go as far as FERC to obtain a license. The expectation was a \$500 million cost, which would be paid in segments. He asked if his recollection of the AGIA agreement was accurate.

Mr. Bullock replied that Representative Doogan was correct. He added that proposed licensees were obligated to disclose the amount of reimbursement they planned to seek. He noted that TransCanada's application requested the statutory

maximum, which was 50 percent initially and then 90 percent after the close of the first open season.

Representative Doogan asked about the \$500 million figure.

Mr. Bullock agreed with \$500 million as the stated figure.

Representative Doogan clarified that the state was in the middle of that process authorized by law, yet Mr. Bullock advised the legislature that they could legally back out of the deal.

Mr. Bullock corrected that he did not advise backing out of the deal. He mentioned the provision AS 43.90.240 in AGIA, which stated the standard for AGIA to continue.

Mr. Bullocks stressed that the legislature could not void the contract established in AGIA, but they could refuse to appropriate money for the reimbursement.

Representative Doogan asked if refusal to appropriate the money for the reimbursement would void the contract.

Mr. Bullock responded that the courts would decide the issue. He recalled that the legislature had encountered similar issues in the past. An appropriation remained necessary for money to be spent. He stated that the issue may raise contractual questions, but the contract did not require the legislature to vote for an appropriation.

Representative Doogan opined that if the contract was voided the state would end up contributing the money without the benefits of the gasline. He asked if there was any reason not to suspect that would happen.

Mr. Bullock agreed that the risk existed. He noted that 43.90.240 would apply in the event that the contract ended because if the project was deemed uneconomic then it would be ripe for abandonment.

[9:35:23 AM](#)

Representative Costello believed that the project created a compelling interest for the public. The public wished to understand where the state stood in the instate gasline process. She stated that the AGIA bill existed without a fiscal note and HB 142 allowed the legislature access to

information. She requested comments from Mr. Wright regarding the public's influence on the creation of the bill.

Mr. Wright responded in the affirmative. He added that the aspect of appropriation was also a catalyst for the bill. He corrected an earlier date to December 31st 2010. He stated that the bill wished to achieve the information about precedent agreements and TransCanada. He found the lack of information regarding the success of the open season disturbing. He discussed concerns regarding timelines. He wished to know whether AGIA would prove economic or not. If the project was not deemed economic then the legislature must explore other options for Alaskans. The public was considered heavily with the introduction of the bill.

Representative Costello pointed out that the bill jumpstarted a conversation regarding confidential information. She understood that the legislature did not intend to seek any detailed information. She asked what the state anticipated that the legislature would achieve in terms of the status of the project.

Mr. Bullock replied that the question regarding the viability of the project was in the jurisdiction of the commissioners. The commissioners were also aware that the information was confidential, which required a certain amount of trust. He was sure that confidential information would not be provided and he did not know what the legislature would be told. He knew that the bill would direct the commissioners to consider the questions raised and they would make decisions about how the answers to the questions affected the license.

Representative Costello understood that one legislature could not bind another. She heard the feelings of uneasiness about changing AGIA and wondered about the response if one legislature cannot bind another.

[9:40:29 AM](#)

Mr. Bullock replied that binding contracts existed, hence the caution "subject to appropriation." The person that bid on a contract or responded to a quest for proposal would understand and determine the appropriate risk.

Representative Costello asked if a project was not funded, would it succeed.

Mr. Bullock replied that he was unsure about past instances where the issue had arisen. He explained that if the legislature did not pay a bill, the state might be sued for breach of contract. He mentioned timing issues. He reiterated that the bill was directed to the appropriation process. He believed it inappropriate to amend AGIA. He stated that HB 142 approached the issue from the standpoint of ongoing appropriations and the provision within AGIA.

Representative Guttenberg recalled repeated discussion regarding the bill and its inability to change the contract between the state and TransCanada. He asked if the bill changed the relationship between TransCanada and those seeking firm commitments. He wondered if the bill would create a new deadline for those entities seeking a firm commitment with TransCanada.

Mr. Wright responded that he viewed the legislation as a benchmark to inform the legislature about the economic viability of the project. He explained that if the project was not economic, steps outlined in the AGIA process would be taken.

Vice-chair Fairclough mentioned AS 43.90.240 and the abandonment of a project. She read "if the commissioner or licensee determines that the project is uneconomical" and added that a dispute would then proceed to the American Arbitration Association. She concluded that the current statute addressed the process under consideration.

[9:45:33 AM](#)

Representative Hawker asked about the abandonment clauses and whether they were in the existing statute. He wondered whether the proposed legislation modified existing statute.

Mr. Bullock replied that the statute was enacted as part of AGIA and provided for the abandonment of a project should that project become uneconomic.

Representative Hawker wondered that if the abandonment clauses were invoked would they trigger any economic damages located in other provisions in AGIA.

Mr. Bullock answered no. He explained that the damage provision existed as AS 43.90.440. The damage provision would arise if the state provides similar inducements to a competing pipeline that they provided to the licensee.

Representative Hawker wondered who had the authority to invoke the abandonment provisions, within the context of AGIA. He asked if the legislature had the authority to invoke the abandonment provisions.

Mr. Bullock replied that the legislature did not have the power to initiate the abandonment provision in AS 43.90.240. TransCanada or the commissioners had the authority to initiate the provision. Upon disagreement, arbitration would be the next step. If both parties agreed that the project was uneconomic, the project would be abandoned.

Representative Hawker asked if the proposed legislation imposed a duty on the legislature with regard to the power to appropriate.

Mr. Bullock replied no, the bill made no change in the legislature's ability to make an appropriation for the project.

Representative Gara requested testimony from Larry Persily prior to the passage of the proposed legislation from committee.

Vice-chair Fairclough responded that she would pass the request on to the co-chair.

Representative Gara agreed that the price of gas had fallen. He asked if the state would have the ability to become a part owner of the pipeline, if the project were deemed uneconomic. He recalled testimony that the state could become part owner of the pipeline for a 7 percent rate of return, which could substantially reduce the tariff. By reducing the transportation cost or the tariff, the price of gas might become more competitive. He encouraged creative solutions. He wondered if the proposed legislation might prevent the opportunity for a creative solution.

[9:49:26 AM](#)

Mr. Wright replied that the proposed legislation would not prohibit the potential solutions expressed by Representative Gara. He noted that the bill did not address negotiations between TransCanada and the commissioners or the administration.

Representative Gara pointed out the two proposed gas lines that were discussed throughout the Capitol building. One option, the instate line, included testimony stating that the tariff cost would be four times larger than the other proposed option. He assumed that the instate line would require a subsidy to enable affordable gas for Alaskans. He added that the downside for the instate line was the lack of taxation, which limits state revenue. He added that the other proposed project would produce revenue for the state, which led to his support of the larger gasline. He wondered whether HB 142 contained language that might prevent the state from taking the necessary subsidy.

Mr. Wright believed that Representative Gara's statements amounted to a presumption, and he felt unqualified to state whether the instate gas line would or would not produce revenue for the state. He stated that he could not comment about the necessity of a state subsidy for the instate gasline.

Mr. Bullock commented that AGIA allowed both a gasline and an AGIA licensed gasline. The AGIA licensed gasline was a result of issuing a solicitation under certain requirements that commitments be made in return for that offered by the state. If the terms of AGIA were changed, then the project would no longer be termed an AGIA project.

Representative Gara understood. He pointed out that the law stated that the gas sold in state was not taxed under the production tax regime. The advantage of the proposed export gasline was the revenue produced. He mentioned a study performed by the Alaska Gasline Development Corporation (AGDC) showed that the inefficiencies of an instate gasline would require the balance of a tariff in the 17 dollar range, compared to a 3 or 4 dollar tariff for the export gas line.

Mr. Wright admitted that he was unaware of the AGDC study. He discussed Representative Gara's request for testimony from Mr. Persily. He noted that Mr. Persily's area of expertise included regulating and permitting for any Alaska

natural gas transportation project in the Lower 48. He stated that Mr. Persily might not be qualified to discuss the economics of the project.

Vice-chair Fairclough asked Representative Gara about the documents that he was quoting.

Representative Gara stated that he was happy to distribute the document through the committee aide. The AGDC distributed an estimation of the cost of an instate gasline, which was \$17 in MCF. He added that Anchorage paid \$8 for gas, which included transportation, lifting, and production. He commented on the change in prices of gas products in the Lower 48. He believed that Mr. Persily made a good case that while shale gas produced a low price, the downside was groundwater pollution. He understood from Mr. Persily that the price of gas would increase due to increased regulation and he wished to hear testimony from Mr. Persily on the issue.

[9:56:07 AM](#)

Vice-chair Fairclough asked for proof that shale gas contaminated water. She cautioned the statement of absolutes without the accompanying proof.

Representative Gara agreed that all fracking and all shale gas were not the same, but some states are proposing substantial and expensive regulations for the development of shale gas. He mentioned reports from the Lower 48 that asserted contamination of water leading to legislation proposed that will increase the production of shale gas.

Representative Wilson stressed that the responsibility lies with TransCanada to prove that AGIA is economical.

Mr. Wright clarified that it was the state's responsibility through the commissioners of DNR and DOR to determine whether the project was economic.

Representative Wilson commented on Representative Gara's argument that the state must contribute financial resources to enable economic viability of the project. She disagreed with Representative Gara's argument.

Mr. Wright agreed.

Representative Wilson added that the best action for the state may mean an increase in economical fuel oil rather than revenue.

Mr. Wright wished to avoid a debate about revenues. He maintained that an instate gasline would provide opportunities for Alaska. He stressed that HB 142 addressed the AGIA process rather than the instate gasline.

Representative Wilson asked about the potential to spend a large quantity of state money without acquiring a gasline.

Mr. Wright responded yes, the potential did exist. He added that the question would be better addressed by the administration.

[10:00:03 AM](#)

Representative Wilson noted that the administration might deem the project uneconomical, since the commissioners are privy to information that was not available to the legislature. She stated that the legislature wished to have access to the same information.

Mr. Wright opined that the legislature's interest included the viability of the project and the wisdom of the expenditures.

Representative Doogan echoed the request of Representative Gara regarding the testimony of Larry Persily. He believed that the opinion of the federal coordinator was valid. He asked Mr. Bullock's opinion regarding a potential dispute between the administration and TransCanada.

Mr. Bullock explained that any agreement carried risk that might result in a court battle and damages paid. He opined that one potential was that the project might be deemed economic, yet the state decides not to go forward, which would raise the issue that the state was no longer acting in good faith and could lead to litigation.

Representative Doogan recalled the phrase "treble damages." He asked to know the value of the legislature intervening in the operation.

[10:04:35 AM](#)

Mr. Bullock likened the situation to buying a car and having it evaluated for proper function.

Representative Doogan expressed that the value of a car was far less than the value of the proposed pipeline.

Representative Hawker stated concerns that the latitude allowed in the committee was mischaracterizing HB 142. He asked whether the discussion was remotely relevant to the bill.

Mr. Wright stated that the discussions were not totally relevant; but indirectly.

Representative Hawker asked whether the bill contemplated competing projects.

Mr. Wright responded no.

[10:06:42 AM](#)

ROGER MARKS, LEGISLATIVE CONSULTANT, LEGISLATIVE BUDGET AND AUDIT COMMITTEE, delivered the PowerPoint presentation "Changes in North America Natural Gas Market Outlook Between 2008 & 2011" (copy on file). He noted his background working for DOR tax division for 25 years beginning in 1983. His prime responsibilities for DOR were to analyze commerciality of North Slope gas from 1983 to 2008; for 15 years he was the only state employee doing that. He stated that he built Alaska's first comprehensive economic model of North Slope gas commerciality. He participated in crafting stranded act negotiations under Governor Tony Knowles and Governor Frank Murkowski.

Mr. Marks discussed the optimistic outlook which had changed between 2008 and current time period. He provided a brief history, pointing to graph "Henry Hub Spot Prices" (Slide 2). Until the year 2000, gas prices were too low for commercial consideration. Beginning in the year 2000, the Lower 48 saw declining "low priced gas" and more expensive gas entered the market, which increased the price. The trend continued through 2008 gas prices and the opinion was that the high gas prices were permanent. He explained that the current outlook was different and a North Slope gas project, if it existed, would lose money.

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Mr. Marks referred to Slide 3: "2008 DOE/EIA Henry Hub Forecast" graph for Department of Energy/Energy Information Administration (DOE/EIA). The forecast was used by the administration to determine findings for awarding the license in 2008. He noted that the forecast displayed were representative of the consensus. The prices shown were in 2009 dollars.

Mr. Marks displayed Slide 4: "2008 Wood Mackenzie Henry Hub Forecast" and Slide 5: "2008 Black & Veatch Henry Hub Forecast."

Mr. Marks referred to Slide 6: "U.S. Shale Gas Reserves." He stated that shale changed the outlook. Shale is sedimentary rock that was rich in gas. The graph illustrated the increase in shale gas reserves between 2008 and 2011. Shale gas did not require a \$30 to \$40 billion pipeline to bring it to market.

Representative Gara noted that the least expensive shale gas was currently produced and the more expensive shale gas will be produced in the future.

Mr. Marks explained that one of the key unknowns regarding Representative Gara's comment would be discussed later in the presentation.

Mr. Marks continued that hard data between 2008 and now illustrated that shale gas had increased eight billion cubic feet per day (equivalent of two North Slopes). He reported working extraordinary technological advances in 3D seismic horizontal drilling and fracturing technology. The technology was still very new. Similar reserves discovered in Canada as well. The technological revolution was remarkable.

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Mr. Marks detailed Slide 7: "2008 vs. 2011 DOE/EIA Unconventional Gas Production Outlook" referring to shale, tight gas, coal bed methane. He explained that the forecast in 2008 was for 25 Billion Cubic Feet (BCF) per day to be produced by 2030.

Mr. Marks explained Slide 9: "DOE/EIA Forecasted U.S. Natural Gas Supply 2008 vs. 2011." He pointed out that the

outlook in 2008 was that the gas supply would be 53 BCF/day in 2030. Current outlook was 68 BCF/day, which was an increase of approximately 15 BCF/day. The 2008 forecast included Alaska North Slope coming on in 2020. In the current forecast the Department of Energy did not include Alaska gas in their forecast.

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Mr. Marks described Slide 10: "DOE/EIA Forecast of U.S. Supply & Demand." He explained that a combination of the supply and demand was illustrated in the slide. The current situation for the United States involved importing approximately seven BCF per day.

Mr. Marks detailed Slide 11: "U.S. Natural Gas Supplies." He explained that the additional production from shale was not envisioned in 2008.

Mr. Marks explained Slide 14: "Growth in World Natural Gas Reserves (excl. new shale)(tcf)." The slide illustrated the total domestic gas production predicted from shale, which increases approximately 45 percent in 2030.

Mr. Marks discussed "New/Sanctioned LNG Plants," (Slide 15):

- Sakhalin, Russia; opened 2009; Shell/Mitsui/Mitsubishi; 1.5 bcf/d
- Tangguh, Indonesia; 2009; BP/Mitsubishi/Nippon Oil/LNG Japan/CNOOC/Korea Gas; 1 bcf/d (short subsea pipes to shore)
- Yemen LNG, Yemen; 2009-2010; Total/Hunt Oil/Korea Gas/Hyundai/Yemen government; 900 mmcf/d (tidewater)
- Qatargas II, Qatar; 2009; Exxon/Total/Qatar Petroleum; 2 bcf/d (tidewater)
- Ras Laffan III, Qatar; 2009 and 2010; Exxon/Qatar Petroleum; 2 bcf/d (tidewater)
- Qatargas III, Qatar; 2010; ConocoPhillips/Mitsui/Qatar Petroleum; 1 bcf/d (tidewater)
- Melchorita LNG, Peru; 2010; Hunt Oil/Marubeni/Repsol; 600 mmcf/d (260 miles of overland pipe)
- Pluto LNG, Australia; under construction, 2011; Woodside/Tokyo Gas/Kansai Electric; 1.7 bcf/d by 2014 (includes planned expansions) (17 miles of subsea pipe)

- Soyo LNG, Angola; under construction, 2012; Chevron/Eni/Total/BP/national oil company; 700 mmcf/d
- Qatargas IV, Qatar; 2011; Shell/Qatar Petroleum; 1 bcf/d (tidewater)
- Gorgon LNG, Australia; under construction, 2014; Chevron/Shell/Exxon/ Tokyo Gas/Osaka Gas/Chubu Electric; 2 bcf/d (expansion contemplated) (subsea pipe, measured in the dozens of miles)
- Port Moresby, Papua New Guinea; under construction, 2014; Exxon/Nippon Oil/several other partners; 850 mmcf/d (450 miles of pipe, mostly subsea)
- Queensland Curtis, Australia; under construction, 2014; BG/Tokyo Gas/CNOOC (China); 1.1 bcf/d
- Gladstone, Australia; under construction, 2015; Santos/Petronas/Total; 1 bcf/d (260 miles of overland pipe)

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Mr. Marks continued with Slide 16, "Key Price Variables:"

- How much of shale reserves are economic
- Environmental fracking issues
- Controls on greenhouse gas and air emissions
  - Affects coal demand, which competes with natural gas

Mr. Marks detailed Slide 17, "Cost to Produce Shale Reserves?"

- Still too new to tell. Unknowns :
  - How do shale wells perform long term?
  - Ultimate recoveries and production potential for wells?
- Costs will go up?
  - Production tends to drop off quickly
  - More rigs will be needed: cost pressure
  - Land access
  - Water availability
- Costs will go down?
  - Exploration continues
  - Cost cutting technologies possible
  - Reserves and production of new energy resources tend to increase over time

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Mr. Marks discussed "Hydraulic Fracturing Issues," (Slide 18):

- Can fracking fluid migrate from deep underground to contaminate shallow aquifers?
- Sloppy drilling practices have occurred
- Currently under state oversight
  - Updated standards for well design, drilling, waste disposal
  - Federal possible
- Compliance and environmental costs will increase
  - Not overwhelming (5%-20% per well?)
- New technologies for water treatment are emerging

Mr. Marks detailed the process of fracturing or "fracking." He noted that problems with pollution might be avoided if the fracturing was done properly. He added that the "mainstream" would believe that fracking was unlikely to be banned, but regulatory costs might increase.

Representative Gara asked about Slide 18. He asked about the increase in costs of 5 to 20 percent. He asked about reported estimates of increased environmental regulations.

Mr. Marks responded that general consensus regarding estimates of the potential state and Environmental Protection Agency (EPA) oversight were those included in his presentation. He agreed that various other estimates could be found.

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Representative Gara asked about potential credible estimates showing that the cost of shale fracture would be greater than 20 percent.

Mr. Marks stated that most estimates were in the range provided in the presentation, but many different estimates existed. He reiterated that the recent advent of shale fracture was the reason for the unknowns.

Vice-chair Fairclough asked if the intent of the estimates was to provide an understanding that increased costs may be incurred with fracking.

Mr. Marks responded correct.

Vice-chair Fairclough concluded that a large supply of gas existed and shale fracture included a great deal of unknowns.

Mr. Marks discussed the issue of greenhouse gas and air emissions with Slide 19, "U.S. Electricity Generation by Fuel (billion kilowatt-hours). He stated the Department of Energy's forecast showed that 48 percent of the fuel for power generation was derived from coal. He added that one quarter of natural gas was used for electricity. Insofar as regulations increase the cost of coal, gas could become a more popular supply for power plants.

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Representative Doogan asked about the nuclear line. He wondered whether the increase represented a new plant.

Mr. Marks replied that there had not been a new nuclear plant licensed in the United States since before 1979.

Representative Doogan questioned the graph on Slide 19 and its referral to nuclear energy.

Mr. Marks replied that in 2010 there were approximately 3200 billion kilowatt-hours.

Vice-chair Fairclough noted that the graph provided a layered approach.

Representative Doogan stated that he understood that nuclear energy was rising according to Slide 19.

Mr. Marks explained that nuclear energy contributed approximately 800 billion kilowatt hours in 2010 and 2030. He explained that the top line of the graph represented the total of all of the different sources of energy.

Representative Doogan understood.

Mr. Marks discussed Page 20, "Regulation of Greenhouse Gas."

- Near term -insufficient support for comprehensive climate change legislation coming out of Congress
- 2009 -EPA begins regulating GHG under the Clean Air Act
- Subject to judicial challenge
- Congress may try to limit regulatory action under CAA

Mr. Marks deemed it unlikely that there would be any greenhouse gas legislation coming out of Congress in the near future. In 2009, the Environmental Protection Agency began regulating greenhouse gas under the Clean Air Act. He moved on to address "Regulation of Air Emissions" on Slide 21. The EPA would soon issue tougher air emission standards for nitrogen dioxide, sulfur dioxide, and mercury.

- EPA will soon issue tougher air emission standards for nitrogen dioxide, sulfur dioxide, mercury
- Large compliance costs for old coal plants:
  - Upgrading plant vs.
  - New natural gas plant
- Decision depends on severity of regs and coal/gas price spread
  - At low gas prices coal plants will be shut down
- Do not underestimate coal and railroad lobby

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Mr. Marks discussed the graph on Slide 22, " 2008 vs 2011 DOE/EIA Henry Hub Forecast (\$/mmbtu) (2009 dollars). He reiterated that alternative forecasts could be found.

Mr. Marks detailed Slide 23, "2008 vs. 2011 Wood Mackenzie Henry Hub Forecast (\$/mmbtu) (2009 dollars).

Representative Gara opined that the EIA and Wood Mackenzie oil forecasts were typically wrong. He asked if the natural gas forecasts were more accurate.

Mr. Marks replied that "everyone's forecast is always wrong." He believed that the opinion of the producers was of greater importance.

Representative Doogan asked why each forecast graph began with the year 2015.

Mr. Marks replied that DOE's forecast was released in five year increments making the 2015 forecast the most relevant in 2011.

Representative Doogan asked if a substantial difference existed between the 2010 and the 2015 forecast.

Mr. Marks replied no.

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Mr. Marks clarified that both DOE and Wood Mackenzie forecasted prices declining from \$10 to \$6.50 in 2030.

Mr. Marks continued with Slide 24, "2008 vs. 2011 Black & Veatch Henry Hub Forecast." He noted that Black and Veatch predicted a drop of \$2.50. He reiterated the importance of the opinion of the investors. He noted that every forecast decreased since 2008 due to the increase in shale supply.

Mr. Marks detailed Slide 25, "Alaska North Slope Gas Pipeline Rate of Return." He stated that every drop in price of one dollar was approximately one and one half percent drop in the rate of return. He added that one and one half percent on a \$30 billion project was substantial.

Mr. Marks finished with Slide 26, "Conclusion: What has Changed between 2008 and Now?" (Slide 26):

- Short-medium term:
  - Grim market outlook
  - Imprudent for investors to proceed while uncertainties playing themselves out
  - Outlook for North Slope gas commercialization has been deferred
- Longer-term
  - Depending on how certainties play out
  - Possible alternative opportunities

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Mr. Marks added that Russia had a fleet of Liquefied Natural Gas (LNG) ice-breaking tankers. He thought that the tankers might gain popularity in Alaska.

Representative Doogan asked how the information presented informed the discussion about HB 142.

Mr. Marks responded that a clause existed in AGIA regarding the term "uneconomic." He believed that great ambiguity existed in the clause, which could lead to long-term litigation.

Vice-chair Fairclough requested the specific citation quoted.

Mr. Marks stated that he referred to AS 43.90.240(c)(1) and (c)(2), which attempts to define that which makes a project uneconomic.

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Representative Doogan asked if the situation changed sufficiently in the last three years to call into question the project's economics.

Mr. Marks responded that a significant change in market outlook occurred between the time that the license was granted and the present. He opined that ambiguities in the statute could result in various interpretations based on forecasts.

Representative Doogan wondered if forecasts might appear substantially different three years in the future as well. The future could not be accurately predicted.

Mr. Marks agreed that forecasted numbers could change in three years. If the clause in the statute had meaning, then it must include a time dimension.

Representative Gara opined that the larger export driven gasline was most important to Alaska's future. He was concerned that the bill created deadline that did not exist before, and might potentially compromise the project. He pointed to the uncertainty about shale oil prices. Mr. Persily testified that natural gas would be more stable. He asked whether Mr. Marks shared any of the concerns.

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Mr. Marks responded that the consensus outlooks were low. He believed that investors would wait to see how those outlooks evolved. He understood that TransCanada would apply for their certificate in 2014; if project was not

built for ten years, what was achieved for the money spent. If the project was delayed, new open season markets could change.

Mr. Marks discussed the potential for a future supplemental EIS, which could be as expensive as the original depending on changes such as new species on the endangered species list. He questioned the value of what the state was putting in currently if the data and technology became obsolete.

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Representative Gara asked about Slide 25. He understood that the rate of return was lower on natural gas.

Mr. Marks replied that the rate of return represented the fact that projects require money from equity and debt. He stated that the project had great risk. If the project was built five years ago, producers would be losing money. He did not know rate of return required.

Representative Costello stated that HB 142 would provide additional information as opposed to invoking the uneconomic clause of AGIA.

Vice-chair Fairclough concurred.

Representative Guttenberg asked whether there was value in Alaskan gas in the future.

Mr. Marks responded that the North American natural gas market outlook was less optimistic than it was during the time that AGIA was passed. As a result, the timeframe for the commercialization of North Slope gas was deferred.

Representative Guttenberg clarified that TransCanada was spending money on projects that could be 90 percent reimbursed. He asked why moving forward.

Mr. Marks thought the questions should be asked of TransCanada, who believed that the project was eminent.

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Representative Hawker clarified the committee statement that HB 142 "moves up deadline that did not exist before." He argued that the statement contradicted the statement of

Mr. Bullock. He challenged the statement that ConocoPhillips received a higher rate of return in Alaska. He stated that the concept of rate of return was specific based on various calculations and interpretations. He noted the difference between profitability and rates of return.

HB 142 was HEARD and HELD in committee for further consideration.

[11:01:35 AM](#)

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ADJOURNMENT

The meeting was adjourned at 11:01 AM.