

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

February 12, 2014

1:06 p.m.

**MEMBERS PRESENT**

Representative Eric Feige, Co-Chair  
Representative Dan Saddler, Co-Chair  
Representative Peggy Wilson, Vice Chair  
Representative Mike Hawker  
Representative Kurt Olson  
Representative Paul Seaton  
Representative Scott Kawasaki  
Representative Geran Tarr

**MEMBERS ABSENT**

Representative Craig Johnson

**OTHER LEGISLATORS PRESENT**

Representative Andrew Josephson

**COMMITTEE CALENDAR**

OVERVIEW(S): ALASKA LNG PROJECT - MEMORANDUM OF UNDERSTANDING

- HEARD

**PREVIOUS COMMITTEE ACTION**

No previous action to record

**WITNESS REGISTER**

MICHAEL PAWLOWSKI, Deputy Commissioner  
Office of the Commissioner  
Department of Revenue (DOR)  
Anchorage, Alaska

**POSITION STATEMENT:** On behalf of the administration, provided a presentation regarding the Memorandum of Understanding (MOU) between the State of Alaska and TransCanada for the Alaska LNG Project.

JOE BALASH, Commissioner  
Department of Natural Resources (DNR)

Anchorage, Alaska

**POSITION STATEMENT:** Answered questions and provided information on the Memorandum of Understanding between the State of Alaska and TransCanada.

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

**POSITION STATEMENT:** Answered questions regarding the Memorandum of Understanding between the State of Alaska and TransCanada.

#### **ACTION NARRATIVE**

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**CO-CHAIR ERIC FEIGE** called the House Resources Standing Committee meeting to order at 1:06 p.m. Representatives Seaton, P. Wilson, Tarr, Kawasaki, Hawker, Saddler, and Feige were present at the call to order. Representative Olson arrived as the meeting was in progress. Representative Josephson was also present.

**OVERVIEW(S): Alaska LNG Project - Memorandum of Understanding**

[Contains discussion of HB 277]

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**CO-CHAIR FEIGE** announced that the only order of business is the administration's overview of the Memorandum of Understanding (MOU) between the State of Alaska and TransCanada for the Alaska Liquefied Natural Gas (LNG) Project.

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**MICHAEL PAWLOWSKI**, Deputy Commissioner, Office of the Commissioner, Department of Revenue (DOR), on behalf of the administration, began a PowerPoint presentation by drawing attention to slide 2, titled "Guidance Documents & HB 277." He said his focus today will be on the Memorandum of Understanding, but the Heads of Agreement (HOA) is the umbrella document that provides the roadmap of how the administration and the producer parties intend to advance the Alaska LNG Project (AKLNG) through a phased process. The HOA describes key understandings and

consensus on certain terms. The MOU is a separate piece which describes a specific agreement between the State of Alaska and TransCanada to transition away from the license of the Alaska Gasline Inducement Act (AGIA) to a more traditional commercial relationship. The MOU also describes key commercial terms for that relationship. Both the HOA and the MOU provide the guidance for how the administration would use the powers enabled in HB 277. He recognized that HB 277 is not before the committee, but said those powers in the proposed legislation are participation, percentage, and process. The legislature and the public will always be in the position of deciding whether to advance through the certain gates.

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MR. PAWLOWSKI moved to slide 3, titled "Where We Are Today?" He said the settlement of Pt. Thomson [litigation] and the joint work agreements, and the confidence in investment in the oil industry in Alaska, has created the opportunity for the commercialization of gas. Since 2011 when the governor called for alignment, the parties have been working on concept selection, which is deciding what the project itself looks like. To date the parties have been operating through TransCanada, the state's licensee under AGIA. However, the parties to the agreements have been doing other work. ConocoPhillips and BP have advanced a significant amount of work under the "Denali pipeline project." Under the AGIA process the state will have reimbursed about \$330 million [to TransCanada and ExxonMobil] by April 2014 for the Alaska Pipeline Project (APP). TransCanada and ExxonMobil will have spent roughly \$130 million in unreimbursed funds for APP. The MOU specifies how that information is contributed, and then not counted, as data going forward as the Alaska LNG Project advances. Similarly in the HOA, all of the parties are contributing their information, which includes the work done by ConocoPhillips and BP on the Denali project. The green star at the top of slide 3 recognizes that HB 277 is the decision point that decides whether the state proceeds on this path or stops. If the state decides to stop, there is an opportunity under AGIA to buy the \$100-\$130 million-worth of data generated under APP. He reminded members that AGIA has a process through which the state can reimburse for TransCanada's work and then has an option to purchase the data. Should enabling legislation pass, the MOU articulates what the commercial relationship between the State of Alaska and TransCanada will look like beginning in the Pre-Front-End Engineering and Design (Pre-FEED) stage.

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CO-CHAIR SADDLER inquired whether the Denali work would be contributed without compensation.

MR. PAWLOWSKI responded that the administration's understanding is that it would.

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REPRESENTATIVE KAWASAKI asked how proprietary information from the prior work of AGIA and the Denali project will be handled and whether that is outlined within the MOU.

JOE BALASH, Commissioner, Department of Natural Resources, replied the information itself is being contributed by the parties to the Alaska LNG Project venture. As far as the state's relationship with TransCanada, it is not going to be considered part of the development costs or, later on, part of the rate base. The proprietary information is definitely not considered to be part of the development costs; development costs are defined as those costs incurred by TransCanada after January 1, 2014 that are not reimbursed.

MR. PAWLOWSKI added that the definition of development costs is found in Exhibit C of the MOU, page 8.

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REPRESENTATIVE SEATON observed slide 3 states [that the Alaska Stand-Alone Pipeline (ASAP)] being done by [the Alaska Gasline Development Corporation (AGDC)] is going forward at the same time and is using shared data with the Alaska LNG Project. He inquired what the situation will be with AGDC's use of the data for developing the smaller diameter pipeline [ASAP] if the Alaska LNG Project does not go forward.

MR. PAWLOWSKI answered the reference to this is in the bullet titled "Conveyance of Transporter Alaska LNG Project Interest to Shipper" in Exhibit C of the MOU, page 9. If the project is to terminate, the idea is that the information and the assets developed by TransCanada during the process come back to the state upon the payment of TransCanada's development cost. A financing charge for that, called Allowance for Funds Used During Construction (AFUDC), is incurred if the state is the one that terminates the project. If TransCanada is the one terminating the project, the AFUDC charge does not come into

play. How it is then directed by the state to AGDC depends ultimately on how the House and Senate bodies talk about the way AGDC itself is structured within the partnership. The current thought is that an AGDC subsidiary will carry that role in the project and will have the access to the information. The MOU specifies that the information has a direct conveyance at a basic development cost price so [the state] gets the information back, unlike AGIA where [the state] has a right to negotiate for purchase.

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REPRESENTATIVE SEATON posed a scenario in which the Alaska LNG Project analysis goes forward and then one of the parties determines the project to not be economic. He asked where that leaves the information that AGDC is using for going forward to open season; for example, whether that information is still available or is a basis for the open season.

MR. PAWLOWSKI apologized for misunderstanding the premise of Representative Seaton's previous question. He pointed out that shown below the schematic on slide 3 is the concept that AGDC is advancing the Alaska Stand-Alone Pipeline on its own through open season. If in that time period the Alaska LNG Project ceases to go forward, the information developed under the Alaska LNG Project would be available for the state to then contribute to AGDC to continue work to the degree it is relevant. There are very big differences between the projects and part of the importance of maintaining that parallel path at this stage is that each is investing in the information that is relevant. There is intent, broadly, by all the parties to cooperate where they can to share information. In a failure case the state does have access to information, although the degree to which it is actually relevant to AGDC in advancing ASAP he is not equipped to say, but other parties may be able to answer that question.

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REPRESENTATIVE HAWKER pointed out that the stoplight depicted in the schematic on slide 3 is a major decision gate. He noted that if the state and TransCanada mutually abandon the AGIA license, AGIA is still the law today. The hammer in AGIA has been the treble damages clause that says the state shall not get involved in a competing pipeline project. When looking at the work done over the recent past, it seems it might be construed as a competing pipeline project that the state has been actively involved in. He asked what the state has done to give him

assurance that the committee is not violating that provision and triggering the treble damages by the very investment of all this time, effort, and state monies in this process.

MR. PAWLOWSKI responded it is a good foundational question that either DOR, DNR, or the Department of Law (DOL) could answer. At a high level, the state agencies have approved project plan amendments under AGIA, which are included in the committee packet. As the governor called for in 2011, the work to date has been through the AGIA license and is therefore not a competing project.

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CO-CHAIR SADDLER how much money is likely to be spent for development costs between January 1, 2014 and June 30, 2014.

COMMISSIONER BALASH replied the budgets associated with the planning activity in the first quarter will continue to be eligible for AGIA reimbursement under "PPA-1B" and are measured in the tens of millions of dollars -- about \$30 million. Once in the second quarter, specifically past June, things start to ramp up. If another field season takes place from points south of Livengood, then it will be in the dozens of millions of dollars in calendar year 2014. He noted that slide 4 identifies the projected costs and budget for the Pre-FEED stage.

CO-CHAIR SADDLER said he will hold his remaining questions as they may be answered by the remainder of the presentation.

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MR. PAWLOWSKI turned to slide 4, titled "What Happens if HB 277 Passes?" He said the Pre-FEED period is the stage that the project, the parties, and the state are looking at moving into. Pre-FEED is expected to last 12-18 months and cost roughly \$435 million. The HOA describes a state share of roughly 20-25 percent of the cost, and the MOU says how the state will fund that 20-25 percent cost. The MOU contemplates the state bringing TransCanada as a partner to the table to represent a specific interest in support of the state's 20-25 percent share for this period. The state's share, through the AGDC subsidiary, is contemplated at roughly \$35-\$43 million, which is roughly 20-25 percent of the LNG plant-related costs of that \$435 million, he explained. During that time period, TransCanada, under the MOU, will be carrying the state's share of the midstream, the pipeline, and the gas treatment plant.

TransCanada will be spending roughly \$53-\$67 million, depending on whether the state share is 20 or 25 percent. He said that the separation here is that the starting obligation of the state taking 20-25 percent is the combination of the state/AGDC subsidiary share plus the TransCanada share. That is 20-25 percent of the \$435 million. This is not total cost of the project, as will be seen in the fiscal notes for the legislation he added. The state needs to bring on important work and experts, both at the agency level and at AGDC, and there is an important request for contingency because costs sometimes do not end up where it was thought they would. So, the fiscal notes do not reflect the exact number; rather, they reflect what is necessary to advance the project and fund the state's share as well as the associated agency costs. For example, DOR is asking for roughly \$500,000 for work related to the change of the gas tax and repurposing its tax systems, plus \$250,000 for regulations. Both are one-time costs. Either directly within DNR or within a transfer to AGDC, DNR is looking to retain expertise related to marketing and supporting the negotiation of marketing contracts, a cost that is above and beyond [the \$35-\$43 million]. TransCanada is shouldering a portion of what would be the state's share, he stated.

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REPRESENTATIVE HAWKER drew attention to slide 3, saying Mr. Pawlowski's answer regarding the risk the state is exposed to under the treble damages clause [of AGIA] seems like a probability game, "like [the state's] people think this way ... we've got our law people that could take a position in defining it." He asked whether the state is gambling that it is not afoul of something that somebody else might take another position were this whole thing to come apart and the other party says the state did not pass adequate or appropriate enabling legislation.

MR. PAWLOWSKI answered that people other than himself can give a much more definitive answer, but he does not believe the state is gambling. He is convinced that the work the state has done with the AGIA licensee through the project plan amendments has protected the state through this period where the state and TransCanada are working together under the AGIA license. In and of itself, that keeps it from being a competing project because the licensee is in the room. He deferred to Commissioner Balash or others for a more detailed analysis of what happens after a "stop decision."

REPRESENTATIVE HAWKER related that another member of the committee has raised the question of whether TransCanada agrees with Mr. Pawlowski, but said the question can be answered later.

MR. PAWLOWSKI noted that TransCanada is in attendance and could come before the committee now or later.

CO-CHAIR FEIGE requested it be later when TransCanada gives its presentation.

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MR. PAWLOWSKI resumed his discussion of slide 4 and the Pre-FEED period, noting that AGDC's ASAP project is continuing its work around its open season. He drew attention to the orange box on slide 4 which states, "Savings with TransCanada include cash commitments by TransCanada for Pre-FEED costs which reduce State of Alaska appropriations by \$53-\$67 million and seamless transition into Pre-FEED with personnel and data continuing to be committed to the project." At the end of Pre-FEED, he said, contracts and legislative approval will be taken up again since this is a staged process. So, at the end of Pre-FEED there is a stop opportunity if it is determined that the project is no longer in the interest of the state or all of the parties. If work stops, the state under the MOU would repay the development costs that TransCanada has expended on behalf of the state during that time period. If the state is the one that terminates, it would pay TransCanada the development costs, estimated to be \$53-\$67 million, plus 7.1 percent in AFUDC. If TransCanada is the one that terminates, the state would pay TransCanada the \$53-\$67 million with no AFUDC. He noted that for purposes of slide 4, he assumed the state is the one terminating the project.

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REPRESENTATIVE P. WILSON said she sees on slide 4 where the \$53-\$67 million comes in, but asked where "the other" comes in.

MR. PAWLOWSKI responded "the other" is the \$35-\$43 million that the state has put in to fund AGDC holding the share of the liquefaction plant. The balance share of \$348-\$327 million comes under the Heads of Agreement. That is where, in this project, the other parties are handling 80-75 percent of the cost of the project instead of the state; that is part of the state gas share being 20-25 percent. Under AGIA the state was reimbursing 90 percent. The policy call under the HOA is to let

each party pay for its share, so now the state is paying 20-25 percent minus what TransCanada is carrying, and the other parties are carrying 75-80 percent of the cost.

REPRESENTATIVE P. WILSON asked what that amount is.

MR. PAWLOWSKI replied it is \$348-\$327 million, shown on slide 4 as the producer share of the total amount of \$435 million.

REPRESENTATIVE P. WILSON understood the total amount is \$435 million, producers are going to be paying \$348-\$327 million, and AGDC is currently spending \$35-\$43 million.

MR. PAWLOWSKI corrected that AGDC is not spending until it is given an appropriation; AGDC's work is focused on ASAP and the \$35-\$43 million cannot be spent until there is legislative authorization.

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REPRESENTATIVE SEATON understood the \$35-\$43 million for AGDC is not on "the pipeline project." He inquired whether that money is to maintain access to capacity in the LNG plant or is actual development and planning costs.

MR. PAWLOWSKI answered the \$35-\$43 million is the estimated development cost for the state's share of Pre-FEED at the LNG plant itself, including the environmental, regulatory, and land work associated directly with the LNG plant. "So," he continued, "it's LNG plant down in the project and TransCanada would be handling LNG plant up to the producing fields."

REPRESENTATIVE SEATON surmised "AGDC's current budget money that was already allocated is proceeding with the development of the pipeline and that is totally independent from AGDC's role in this amount of money."

MR. PAWLOWSKI responded the HOA contemplates AGDC continuing the work on ASAP, which is why on slide 4 it is included in the green arrow located underneath [the schematic for the Alaska LNG Project]. In the HOA the administration commits to seeking an appropriation to fund the additional work asked of AGDC to step into the LNG plant.

REPRESENTATIVE SEATON, noting AGDC has been doing a lot of pipeline work and incurred a lot of expenses, inquired whether

that work rolls into the Alaska LNG Project or is useless information for the Alaska LNG Project.

MR. PAWLOWSKI replied it is likely to be useful information for the Alaska LNG Project because some things will be able to be shared. Statutory direction was given under HB 4 for AGDC to cooperate with a large project, so AGDC and the Alaska LNG Project will need to enter into a cooperation agreement to design how that information is shared. It is incumbent on the committee to be clear about how that is going to work when the committee takes up legislation for the Alaska LNG Project.

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REPRESENTATIVE SEATON noted he does not see where "all of that money that is being spent on that" is represented. He can see the numbers for the producer parties, TransCanada, and the state's share of AGIA, but he does not see anything as a state contribution "in that."

MR. PAWLOWSKI apologized for missing Representative Seaton's question at the beginning and said the quantification of how much of AGDC's work is directly relevant to the Alaska LNG Project is work that will need to be done once the state decides to move the Alaska LNG Project. While there is potential for synergies, he cannot provide a number today that this work is directly relevant. To his knowledge, the agreement has not been developed or executed between the two projects to identify some of that work, but he knows they are working together on that.

REPRESENTATIVE SEATON understood the idea is that there is a balloon out there someplace for whatever portion of that state investment is applicable to the project and goes in as a state contribution share.

MR. PAWLOWSKI said the HOA describes the intent of that cooperation. He confirmed it is a balloon but said it is difficult to quantify at this stage.

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CO-CHAIR SADDLER posed a scenario where the project comes to a stop [after passage of HB 277]. He inquired whether there would be a use for the Pre-FEED work product that was done to that point in time and, if so, how it would be apportioned, split, and sold at that time.

COMMISSIONER BALASH responded the governance of that information will be contained separately in a joint venture agreement that will be applicable to the Pre-FEED phase of the project. That agreement will need to be executed after enabling legislation passes. Who retains what information and what ability the parties have to use that publically will be a product of the negotiations to close out that agreement. It will be [the administration's] intent to maximize the opportunity.

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REPRESENTATIVE KAWASAKI returned to slide 3, which shows that for AGIA the state is roughly in for \$330 million, the Alaska Pipeline Project is in for \$130 million, and Denali is in for \$200 million. He inquired whether those figures are included in slide 4 or whether slide 4 depicts new dollars for the producer, AGDC, and TransCanada shares.

MR. PAWLOWSKI specified slide 3 does not add to slide 4; slide 4 is a fresh start. Also not included is the money appropriated for AGDC to do ASAP work. Those are other things that are being looked at point forward from action on HB 277.

REPRESENTATIVE KAWASAKI presumed the AGIA licensee and APP and Denali have not yet shared information. He asked what will happen once they do share information if, for example, the same route studies have been done by the parties.

MR. PAWLOWSKI encouraged that this question be asked of the other parties out doing the work, but said when people start working together with all of the information available they find synergies and those ultimately reduce cost. From the state perspective of knowing about these types of projects, he said he is hesitant to estimate that these costs are going to go down. While there is an opportunity for that when people start working that data and sharing that work, which they have done a lot of since 2011, he hesitates to say it is likely to result in less estimated cost rather than the other way where it is found that more engineering needs to be done.

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REPRESENTATIVE P. WILSON understood HB 277 must be passed before the Pre-FEED stage can occur.

MR. PAWLOWSKI said she is correct; the Heads of Agreement describes that enabling legislation leads to a ramp-up of the Pre-FEED work and the acceleration of all the parties.

REPRESENTATIVE P. WILSON further understood that if HB 277 is passed, then a joint venture agreement would be needed first to lay out exactly how the parties will work together.

MR. PAWLOWSKI answered in the affirmative but explained it is important to remember there is a distance between what the state does as a resource owner and what happens between the parties that are actually doing the business side of the operations. As [the administration] contemplates things in the HOA, the business-side agreements will be done by AGDC, AGDC's subsidiary, and TransCanada. The MOU says how that information flows back to the resource owners to evaluate and have the transparency that [the state] needs; the HOA also contains principles of how that information is shared. Day-to-day agreements like the joint venture agreement are not something that the agencies see themselves in the middle of. The agencies will be watching and be informed, but those are agreements that happen between business parties. It is an important distinction of what is actually getting worked on by whom.

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REPRESENTATIVE P. WILSON, in regard to TransCanada and AGDC working together at this time, surmised that legislators "have to assume that they are saying 'okay, we're doing this stand-alone pipeline, AGDC, but we kinda need to know what you need to know if the stand-[alone] pipeline does not go so that while we're doing this work that work is being taken care of at the same time, so that ... if this goes then, TransCanada would feel comfortable about taking over that part of ... the 20-25 percent cost of the state because they feel they've gotten ... their money's worth from what AGDC has done alongside it.'"

MR. PAWLOWSKI responded a cleaner way to think about it is that the progress on the Alaska LNG Project - the big project that has the state, TransCanada, BP, ExxonMobil - is really a separate progress than the work that goes on at AGDC for the Alaska Stand-Alone Pipeline. Those are two horses, parallel paths. There are very good potentials for complementary work to go on and part of an important policy call by the state is maintaining those parallel tracks, but they have to work together to figure out what can be shared. At the decision point to move into the Front-End Engineering and Design (FEED)

stage, in late 2015 or early 2016, the state will know whether one or the other is going to advance. After that stage, the decision of what is valuable for whom and how that gets reconciled is seen as an opportunity that has yet to be worked out. That is part of what gets developed during Pre-FEED while AGDC continues on ASAP and the state moves forward on the Alaska LNG Project. The administration and the legislative bodies have work to do in the discussion around the legislation because the state is asking AGDC to take on a large additional role. Managing exactly how that is structured is a key part of the dialogue between the state, the committees, the administration, and AGDC while actually digging into the legislation.

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REPRESENTATIVE P. WILSON remarked that [legislators] are working in a vacuum at the same time that they are thinking about this because they do not know for sure what is ahead.

MR. PAWLOWSKI replied that that challenges what really is the fundamental driver for the state decision to recognize that the Alaska LNG process is a staged process. Long-term commitments are not being made on the Alaska LNG Project because the project is not ready for long-term commitments. At the same time, the need to get gas to Alaskans and advance the ASAP project means the state needs to maintain the parallel path on both projects because the future outcome is unknown. Thus, Representative P. Wilson is right. The HOA, MOU, and HB 277 are asking for the ability to take a step forward to see what the opportunity is.

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REPRESENTATIVE HAWKER surmised the dollar amounts displayed on slide 4 represent the money to get to the stage gate of starting the FEED process.

MR. PAWLOWSKI answered correct.

REPRESENTATIVE HAWKER noted the equity option agreement in the MOU must be executed within 90 days of the enabling legislation, making the equity option agreement a necessary part of the process forward. The equity option agreement is the ability for the state, via whatever mechanism, to purchase up to 40 percent of TransCanada's interest in this process. That option expires the earlier of 12/31/15 or the date of execution of the commercial agreements to commence FEED. Therefore, the state needs to have that money as the very last thing on deck prior to

those expiration dates in order to cross the line from Pre-FEED to FEED, if the state wants to exercise that option. He inquired whether that money is included in any of the monies [depicted on slide 4].

MR. PAWLOWSKI responded it is not at this point. He explained that on slide 4 he put the equity option in the "Go arrow" that is located to the right of the box for legislative approval of the contracts. The decision of when to appropriate that money and put it into place is a very valid consideration as [the administration and legislature] work through these questions.

REPRESENTATIVE HAWKER surmised the red stop box on slide 4 depicts the legislature failing to appropriate that money.

MR. PAWLOWSKI replied no, the exercising of the equity option is depicted in the "go arrow" for 40 percent of FEED; \$21-\$27 million is 40 percent of the \$53-\$67 million.

REPRESENTATIVE HAWKER apologized for mishearing what Mr. Pawlowski had said earlier.

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REPRESENTATIVE HAWKER surmised that if money is needed on deck, it would need to be appropriated in HB 277. He said his understanding of the legislation and its fiscal notes is that that money is not provided.

MR. PAWLOWSKI answered the fiscal notes include a significant amount of contingency money, which is prudent in any project in an appropriation for a fiscal note.

REPRESENTATIVE HAWKER asked whether the contingency money is \$27 million.

MR. PAWLOWSKI responded the current fiscal note has a \$75 million capitalization of the fund.

REPRESENTATIVE HAWKER inquired about the \$83 million.

MR. PAWLOWSKI replied the \$83 million includes the costs for AGDC and potential transfers through. In the notes on the fiscal note, the actual appropriation for the cost is roughly \$75 million, so there is some contingency built into that and for good reason. That would provide an opportunity for some of that, though the contingency is to recognize what happens during

FEED. When looking at the issue, it was recognized that the decision to go to FEED and the exercise of that equity option happens sometime during the 2015 year and that decision to proceed is going to be accompanied by appropriations for the next stage. It is a strategic question as to whether to appropriate now or during the 2015 legislature.

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CO-CHAIR SADDLER inquired from what basis the treble damages to TransCanada would be determined; for example would it be based on the \$130 million in expenses that are yet to be reimbursed.

MR. PAWLOWSKI answered he is unprepared to provide an estimate or an opinion on the treble damages because he has not done work on this. He deferred to the Department of Law or commissioner of DNR to provide an answer.

CO-CHAIR FEIGE requested the committee be provided an answer at some point.

MR. PAWLOWSKI agreed to do so.

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REPRESENTATIVE SEATON surmised the legislative approval of contracts depicted on slide 4 is actually the "go decision." Another decision the legislature could exercise, but does not have to do for the project to still go, is exercise of the option for up to 40 percent.

MR. PAWLOWSKI responded correct.

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REPRESENTATIVE TARR understood that if TransCanada was the one to terminate, then TransCanada would be responsible for paying back the \$53-\$67 million. She asked where in the timeline of events would be the termination of the AGIA license.

MR. PAWLOWSKI replied the termination of the AGIA license is in the MOU and would not happen immediately with enactment of enabling legislation because there would be a little bit of transition period, windup, and finalization of some of the audit work. So, almost commensurate with enactment of enabling legislation will be a lag and then the license would be abandoned by both parties.

REPRESENTATIVE TARR understood, then, that if that stop point [depicted on slide 4] was reached by moving forward and the AGIA licensed expired, the state, even if it was the responsible party in the stop point, would not be subject to paying treble damages. The state would only be subject to paying the [\$53-\$67 million] plus the 7.1 percent AFUDC fee.

MR. PAWLOWSKI answered yes, that is his understanding.

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REPRESENTATIVE HAWKER said the enabling legislation, as he sees it, does not address the state extracting itself from the parameters of AGIA. He offered his belief that the MOU is the only place this is referenced. Language in the MOU seems soft, he argued, because it simply says the commitment is to initiate the process of making a determination. It does not say [the state] will make a determination or conclude a determination. The MOU says that upon the occurrence of the trigger event and the execution of the transition agreement, the licensee will agree that the project licensed under AGIA is uneconomic. He said he does not see any real formal commitment for the state to extricate itself and move into a new post-AGIA world. He inquired whether it is too late to add some firmness to that commitment to both the legislature and the people of Alaska.

MR. PAWLOWSKI responded the administration is open to discussing with the committee and other members any additional firmament surrounding that concept. It is an open item that is worthwhile to discuss, especially when getting to the legislation.

REPRESENTATIVE HAWKER commented that the aforementioned is just academic business conversation, it is not any comment on the quality or the commitment or service of any party involved. It is just looking for what is the right and best business deal that is possible for the state to achieve.

MR. PAWLOWSKI appreciated the comment and allowed there is room for providing clarity.

[1:57:46 PM](#)

MR. PAWLOWSKI turned to slide 5, titled "What Happens after FEED?" He noted there has been talk about the state exercising the option of 40 percent, the reinvesting of up to 40 percent of the cost of the midstream, \$21-\$27 million, where the state can

then stand on both sides of the transaction in the midstream. Exercise of this option happens as the FEED stage is stepped into. He stressed the depicted FEED costs are very rough estimates and that they are rounded and therefore do not add up. The costs are based on the advice of [the administration's] technical experts [Black & Veatch] using 4 percent of \$45 billion, portending that 60 percent is midstream and 40 percent is downstream. This is an illustrative idea of what a reasonable FEED spend would be like. The actual costs will get refined through this next stage; for example, two years after the Pre-FEED stage, these numbers are very likely to change, but they provide a scale of what can be expected. Cost of the FEED stage is estimated to be in the neighborhood of \$1.8 billion. Under the concept of the state taking between 20 and 25 percent, the producers would carry roughly \$1.44-\$1.35 billion of the cost of the FEED stage. The state's AGDC subsidiary share would be \$145-\$180 million, excluding contingency and actual staff and agency support. If the state exercises the equity option and is carrying an additional 40 percent of the midstream, the state's cost would increase to \$230-\$290 million. If the state does not exercise its option, TransCanada would carry \$215-\$270 million; if the option is exercised, TransCanada would carry \$130-\$160 million. When the decision point is reached, all of the parties will look at the project and decide whether it is appropriate to go to Final Investment Decision (FID) at which construction commences. If the decision is to stop, under the MOU the development costs will come into play. Mr. Pawlowski pointed out that he has made the assumption on slide 5 that the Alaska LNG Project is moving forward. In the arrow under the schematic on slide 5 it can be seen that AGDC's mission is broad and AGDC will continue working on getting gas to Alaskans through interconnections to the Alaska LNG Project. Thus, it recognizes that the Alaska LNG Project is not the totality of the work that needs to be done in a success-case scenario.

[2:01:26 PM](#)

CO-CHAIR SADDLER, regarding slide 4, asked whether the blue go arrow about the exercise option for 40 percent is for 40 percent of FEED or for 40 percent equity purchase.

MR. PAWLOWSKI apologized, replying the go arrow should say Pre-FEED because it is truing up the Pre-FEED costs and then [the state] assumes 40 percent of the midstream FEED costs going forward.

CO-CHAIR SADDLER understood, then, that it is 40 percent of the midstream FEED cost.

MR. PAWLOWSKI answered it should be 40 percent of Pre-FEED.

CO-CHAIR SADDLER inquired whether it is 40 percent of all the Pre-FEED costs.

MR. PAWLOWSKI responded it is actually 40 percent of TransCanada's \$53-\$67 million depicted on slide 4.

CO-CHAIR SADDLER asked whether the green box on slide 4, regarding yes or no for legislative approval of contracts, is the same thing as go/stop.

MR. PAWLOWSKI nodded yes.

CO-CHAIR SADDLER, regarding the blue box on slide 5, inquired whether the State/AGDC subsidiary share without equity option, and the State/AGDC subsidiary share with equity option, are alternative options and therefore are not additive.

MR. PAWLOWSKI replied they are intended as one or the other as options.

CO-CHAIR SADDLER complemented the charts, saying he wants to understand what the protocols of the colored boxes mean.

[2:03:15 PM](#)

REPRESENTATIVE HAWKER remarked that exercise or non-exercise of the [40 percent] option is an absolutely essential and major component of the MOU. He understood that the equity option term sheet [in the MOU] provides that the state can take 40 percent ownership in the one-quarter of the project carved out for the state/AGDC. Thus, the state is not really buying into the project itself, but rather into a TransCanada subsidiary that has 25 percent actual ownership equity in the pipe project. However, the state is the sovereign, a tax-exempt entity, and the state wants to maximize its benefit. He said he does not know what the consequences are for the state to be buying into the subsidiary of a corporate entity, as opposed to the state actually holding directly a component of the overall project, and whether that is the right and best decision or whether the state is compromising its rights and privileges as a sovereign and its financial advantage by not owning directly a chunk of that pipe project within the Alaska LNG Project.

MR. PAWLOWSKI noted the equity option term sheet is Exhibit B in the MOU. Offering to get back to the committee, he said it is structured in a way to maximize the tax advantages to the state. Through several of its funds, either directly or indirectly overseen by DOR, the state currently invests in these types of partnerships and the state maintains the tax advantages on the income; it is actually one of the benefits of the master limited partnership or limited partnership model. He agreed with Representative Hawker that how it is structured is a key point.

CO-CHAIR FEIGE advised the aforementioned is in Exhibit B of the MOU, page 3, bullet 10.

[2:07:07 PM](#)

REPRESENTATIVE HAWKER said he is looking at Exhibit B of the MOU, page 2, item 7, which outlines the conditions on the state transferring its interest in the limited partnership. He added this would be after the state has acquired the limited partnership. He observed this section talks about being able to transfer the state's interest to any government fund owned by the state, such as the "State Department of Revenue Constitutional Budget Reserve Fund." Because the state would be holding a part of a corporate entity, it seems it would be fraught with questions on which he would like to see legal analysis. He further questioned what others in the project think about this ability to move that around and not knowing who might be their partner at the end of the day.

MR. PAWLOWSKI responded that Commissioner Rodell played a large role in this as a fiduciary looking at how the state invests through different funds and these types of structures. He said will get information back to the committee about this.

REPRESENTATIVE HAWKER remarked that this is an area he does not quite understand.

[2:08:43 PM](#)

CO-CHAIR FEIGE said he thinks the concern being expressed by Representative Hawker is that as the project progresses and gets to the point where project partners have to be voting on particular aspects or particular directions that the project is going to take, the question is who will be at the table representing the State of Alaska's share in the overall project -- Commissioner Balash, Commissioner Rodell, a representative of

AGDC, or TransCanada. This needs to be made clear so everybody has the same understanding.

MR. PAWLOWSKI thanked Co-Chair Feige for the direction, saying he views it as one of the key moving pieces in HB 277 that is ripe for legislative engagement, just as how the legislature will participate in the development of the contracts that enable each of these stop and go decisions. Drawing attention to slide 2, he said those are the three big pieces that are up for discussion in HB 277. Clarity is key in how the state will play a role in this project going forward. Some of those assumptions are articulated in the HOA. The MOU describes one specific arrangement of the state transferring and working with TransCanada for the midstream portion of the project.

[2:10:30 PM](#)

REPRESENTATIVE SEATON noted that one alignment issue was about having the percentage of all the pieces. He asked what the alignment is if AGDC is 20 or 30 percent of the LNG and 0-40 percent of the midstream pipe. He further asked whether it is a fixed percentage of all components because it really only works if there is an equal amount through the entire process.

MR. PAWLOWSKI brought attention to slide 2, saying the HOA at a broad high level describes that alignment concept and that alignment concept starts with the gas. The state's share of the gas feed will drive what the state share of the project is. For example, if the state's share is 20 percent of the gas, the state will have 20 percent of the infrastructure. Looking back to the [November 18, 2013, Alaska North Slope Royalty Study by Black & Veatch (royalty study)], that decision is the real alignment. The MOU is a separate step away from that. Each party, each owner of the gas resource, will determine how it will finance or support its particular share. The MOU says the state is going to support its share through AGDC subsidiary participation. That does not upset the fundamental alignment of the gas in the infrastructure because the alignment is as much about what is happening to the other partners. One alternative to moving the project forward was to reduce royalty rates to reduce the burden of investment in infrastructure to carry the value. However, the policy call was made that reducing the royalty was not in the best interest of the state; rather, the state co-investing along with its share of the gas was the way to maximize the value to the people of Alaska. How the state finances that participation is a state question. He encouraged committee members to ask the companies their perceptions of that

and whether it up-ends the alignment. From the state's perspective it does not. What matters is that the state's share of the gas matches the state share of the infrastructure. Who the state brings in to work with, within reason, is the state's choice, not the choice of the other parties.

REPRESENTATIVE SEATON posed a scenario of 25 percent, meaning the alignment would be that TransCanada has one-fourth of the amount. He surmised the option would then be whether the state wants to purchase part of that, but TransCanada would have one-fourth of the capacity in the pipe. One-fourth of the liquefaction capacity would belong to AGDC, which would allow that alignment to be set up.

MR. PAWLOWSKI replied correct.

[2:14:49 PM](#)

REPRESENTATIVE HAWKER noted that overall the operating agreement would be very large. As currently conceived, three producers would own about 75 percent of the project and another entity would own about 25 percent. He understood Mr. Pawlowski to have said that the producers would be completely indifferent to what the state did with the state's quarter of the project. He remarked it seems odd to him that a party putting up \$45-\$65 billion in an aggregate project would not want to know who its partner was going to be. He expressed amazement that industry would be ambivalent toward the terms of the MOU, who the state's partners are, and what the state's intent is. He asked what the administration did to get that concurrence from the producers and whether the producers had a chance to review the MOU so they knew what they were getting into before they signed the HOA.

MR. PAWLOWSKI apologized, acknowledging he stretched the boundaries of language when he said that "within reason" the partners the state brings in and he should have been more careful. Of course, the partners care about the credibility and capability of the partners that the state brings to the table; that is a fundamental issue. The state was working with TransCanada throughout the process of the development of the Heads of Agreement, he reported. As called for by the governor in 2011, all of the parties were working together. Saying [the administration] is comfortable, he urged the committee to ask the other parties about their relationship to TransCanada. The other parties were not in a position, or asked, to review the agreement between the state and TransCanada, he noted. The HOA references the agreement between the state and TransCanada being

released concurrently. So the MOU and HOA were released at the same time. The MOU is a separate agreement between the state and TransCanada, but comfortable within the boundaries of the HOA as signed by all the parties.

[2:18:11 PM](#)

REPRESENTATIVE HAWKER appreciated Mr. Pawlowski's apology. However, he said he is hearing within Mr. Pawlowski's response that it would be judicious for the committee to get put on the record the comfort level that the proposed participants to this project have with the terms of the MOU, given they were not consulted in its construction.

MR. PAWLOWSKI answered the administration, regarding the MOU, will continue to work with the committee to talk about the interest that is seen as a state. What committee members ask the companies is something for which he would not presume to offer guidance. He will continue to talk about the policy reasons the state is offering in advancing the MOU.

[2:19:01 PM](#)

REPRESENTATIVE P. WILSON understood that the agreement between TransCanada and Alaska that was released at the same time [as the HOA] was the MOU.

MR. PAWLOWSKI responded correct.

REPRESENTATIVE P. WILSON presumed that the other parties do not really care about how Alaska does, the other parties only care about whether the deal works for them. She asked how legislators will be able to determine whether the State of Alaska is getting the best deal.

COMMISSIONER BALASH replied a number of things were considered when [the administration] examined the specific terms and whether they were acceptable and in Alaska's interest. The terms were benchmarked against a variety of other work, other decisions made by this body, and a positive conclusion was reached. [The administration] examined the Federal Energy Regulatory Commission (FERC) approved rates of return and capital structure for new-build projects under Section 7 of the Natural Gas Act. While not exactly analogous here because this is expected to be a Section 3 governed project, it is a starting point. Also looked at was the capital structure for other LNG projects around the world, some that include pipelines. Also

taken into account were the specific actions by the legislature in 2008 on the AGIA license. The license contains terms that are very similar to this, but [the administration] thinks this package represents an improvement over that set of terms. The royalty study included information that looked at these kinds of metrics, such as what the typical returns are for a project like this. [The administration] was satisfied that it was a positive package and that it was going to allow retention of momentum through calendar year 2014 and keep the project on a positive trajectory. When getting down to the final sets of terms and whether, for example, it was worth it to hold out for another half point on the return on equity (ROE), [the administration] looked at what that would mean to the state's net present value and compared that to what a delay of a year might cost. It turns out that a half point difference is worth about \$100-\$200 million in net present value to the state; a year's delay is worth \$800 million. That choice was weighed in regard to whether to shop around for a better deal somewhere else, but it was thought to not be in the state's collective interest. [The administration] thought things were close enough with the package of terms as they sat before the body in the MOU to meet the state's long-term interests.

MR. PAWLOWSKI added that Representative P. Wilson's question is a key question. He said the administration's consultants will be available to work with committees to talk about the analytics and look at these questions. Additionally, [the administration] has confidence in the ability of the legislature's consultants to look at the metrics and to do a financial analysis that is independent of the administration.

[2:24:34 PM](#)

REPRESENTATIVE TARR, regarding how much the legislature needs to appropriate and in what time frame, observed from slide 4 that upwards of \$43 million would be needed, plus another \$27 million to exercise the state's 40 percent option. She inquired whether only those two costs will be what the legislature is looking at next year. She further asked whether the costs depicted on slide 5 also need to be looked at next year so things can move in a seamless way.

MR. PAWLOWSKI answered he presumes the most efficient way to advance the project is in the 2015 timeframe -- to be looking at the totality of the appropriations necessary to move through that stage gate, which would be FEED plus all of the other work. That is what is meant by commensurate steps. The step

contemplated at this stage when looking at the fiscal note is somewhere between \$70 and \$90 million. The next step is a much bigger step and the step after that is in the tens of billions of dollars by all parties to move into the construction stage.

[2:26:07 PM](#)

CO-CHAIR SADDLER, referring to the earlier statements made by Commissioner Balash, said the extent to which the administration can give more information to the committee about the analysis, and the weighing and balancing done by the administration, might forestall a number of probing questions because members must exercise their independent judgments. The more members can be helped in understanding the process that the administration went through, the more comfort members will have with the administration's calculations and conclusions.

COMMISSIONER BALASH responded he will be happy to do so.

[2:26:36 PM](#)

REPRESENTATIVE P. WILSON understood there are five fiscal notes all from different departments. She requested the committee be provided on one sheet of paper the amount of money needed for 2014 and the amount needed in 2015 for the project to proceed to the next stage.

MR. PAWLOWSKI replied he would be happy to do that, but with the caveat that he earlier put on the FEED stage, which is that at this point there is a danger in being too precise. However, those numbers will get better through the Pre-FEED stage.

COMMISSIONER BALASH added that those numbers will be prepared as the governor's legislation contemplates the state take - 22.2 percent total - rather than the ranges seen on today's slides.

[2:28:07 PM](#)

REPRESENTATIVE HAWKER said the committee received some degree of answers to the questions it submitted [after the committee's January 29, 2014 hearing on the MOU]. He noted he is trying to use [the 6-page response from commissioners Balash and Rodell, dated February 11, 2014, and in the committee packet] as a roadmap for things he wants to see discussed in committee; that he had not planned on the answers just being written responses that are never referred to again. He inquired as to whether the administration pursued or considered other avenues besides this

one for extricating the state from the existing AGIA contract. He further asked whether this was the only route considered and, if so, why other viable options are not out there. He maintained the [written] response to this question, question 4, is a "nonresponsive response."

COMMISSIONER BALASH answered that the guidance taken from the "org chart" is instructive here. In 2011 the governor called on the parties to work within the AGIA framework, including with the state's AGIA partner. As things have matured and picked up speed in 2013, he would not say that alternatives were not contemplated, but a need was not seen to break the partnership. TransCanada has been a good partner, has worked well with state agencies helping solve problems, and has worked hard to understand the state's interests. As the state's participation was considered in this project overall, the question was considered as to what role TransCanada would play here, if any. A spectrum of zero to fully representing the state's interest in the midstream was considered and it can be seen where it ended up. In the course of conversations with TransCanada it was learned that the smaller TransCanada's interest the less likely TransCanada was going to devote significant personnel to the effort. What a pipe company really brings to the table is the expertise -- the understanding that can be brought to bear here. In the longer run, TransCanada's commercial motivations and fiduciary interests are ones that [the administration] thinks align fairly well with the state in the broader scheme of things and provides a fine counterbalance overall and this ultimately weighed in [the administration's] "decision making to end up at the point we did in the end."

[2:32:08 PM](#)

MR. PAWLOWSKI interjected, saying an additional consideration contemplated by the administration was that the MOU was not drafted in isolation. While the MOU is a separate document and agreement, at the time the MOU was being worked the administration was also working with all of the parties on the alignment document in the HOA. The comfort of all the parties with TransCanada, the working relationship for years, and the momentum was an issue in the development of the HOA. [The administration] saw the benefits that TransCanada brought from the state's side within the HOA in resolving key issues and also saw the working relationship that the companies have with TransCanada. At the same time [the administration] was working the MOU, it was also conscious on momentum of the HOA. All through last summer the governor was calling for a commercial

agreement. It took quite a long time to work both concurrently to be able to get to a place where the state was comfortable advancing them to the legislature and the public for consideration. He stressed that [the administration] does not view the [written] responses to the committee's questions as the last response and looks forward to the give and take as more questions are generated.

REPRESENTATIVE HAWKER offered his appreciation for the responses of Commissioner Balash and Mr. Pawlowski. He said the responses give him a great deal of personal comfort about the process that was gone through and that it was a well-thought, deliberate process that considered other alternatives. The route chosen is sincerely thought by Commissioner Balash and Mr. Pawlowski to be the best route forward and the aforementioned responses give him much greater comfort than the written answer.

[2:34:56 PM](#)

CO-CHAIR SADDLER brought attention to question 9 in the administration's February 11, 2014, response letter, which asks where in the MOU or other related documents is TransCanada required to build the pipeline. The administration's answer, he related, says it is not required but that the state's preference is TransCanada be selected. He asked who is saying this is the state's preference and how was that expressed.

COMMISSIONER BALASH directed attention to the last page of the February 11, 2014, response which shows a breakout of the respective owner interest for each of the other three parties when the state's equity is at 20 percent and at 25 percent. [At 20 percent state equity, ExxonMobil would be 34.6 percent, BP 22.5 percent, and Conoco Phillips 22.9 percent; at 25 percent state equity, ExxonMobil would be 32.5 percent, BP 21.1 percent, and Conoco Phillips 21.5 percent.] TransCanada's interest could be the second largest among the parties by virtue of the state's interest. That may weigh in the decision making as to who is the actual lead to manage the construction of the project. Once at operation, each of "the four pipes in a pipe" will be operated relatively independently in terms of being able to pursue additional opportunities or additional customers, which is what the expansion policy in Appendix A of the HOA really achieves. Whether or not a party is the actual Operator, that party will be able to pursue additional opportunities to transport more gas for more customers, including the state and potentially others; that is one of the things that keeps [the administration] attracted to TransCanada in this regard.

2:37:33 PM

MR. PAWLOWSKI interjected, bringing attention to the schematic on page 30 of the Heads of Agreements [titled "Attachment 1, Southcentral Alaska LNG - Integrated Team"]. He explained the schematic shows how the parties will work together in the concept selection agreements. TransCanada will be the lead for pipelines, BP the lead in producing fields, and ConocoPhillips the lead in the LNG plant. ExxonMobil will lead the integration team and BP will lead the commercial team. Responding further, he clarified the schematic is under Exhibit I-B of attachments to the HOA and outlines the project team during the concept selection period. Drawing attention to slide 3 of his presentation, he explained that the Alaska Pipeline Project (APP), in which TransCanada was the lead, plays a large role in the midstream, just as BP as the operator of Prudhoe Bay is bringing expertise as the lead in the producing fields. Each company brings a particular expertise that complements the differing expertise of the others. This gives confidence to the people looking at the project that credible companies are involved in pushing this project forward; each company has much expertise around the different pieces of the project. [The administration] also looked at the opportunities created by the share that each party would own.

2:40:35 PM

CO-CHAIR SADDLER noted the answer to question 24 in the administration's response says a flowchart will be presented today. The flowchart is good, but it is high level, he said, and he was hoping for a more detailed flowchart that talks about the enabling legislation, equity agreements, and so forth. He said he will be glad to work with the administration to identify specifically what he would like to have. He presumed Commissioner Balash and Mr. Pawlowski must have used some type of schematic to find the path forward through all these things and said he would like to have a copy of that.

MR. PAWLOWSKI responded a schematic is being working on and [the administration] will work with the committee to continue that work. A dilemma is translating from engineers through lawyers. The designs get really impossible to read, so that issue is still being worked through internally.

CO-CHAIR FEIGE quipped he is envisioning a wall full of sticky notes that get moved around a lot.

[2:41:49 PM](#)

REPRESENTATIVE SEATON observed from the last page of the administration's response that, regardless of the state having a 20 or 25 percent equity, BP and ConocoPhillips are basically at equal percentages and ExxonMobil is at a slightly higher percentage. He inquired whether those percentages are based on the reserves of gas in the current fields.

COMMISSIONER BALASH replied yes, it is the working interest owner percentage of each of the three parties in the combined resources of Prudhoe Bay and Point Thomson.

REPRESENTATIVE SEATON asked whether all of the interests had by each party have the same royalty rates on all of those fields.

COMMISSIONER BALASH answered no and said Point Thomson generally has higher royalty rates than Prudhoe Bay.

[2:42:59 PM](#)

REPRESENTATIVE SEATON inquired how each party's combination of royalty percentage, amount of gas, and tax rate are being looked at to come up with the specific percentage of share equity per party.

COMMISSIONER BALASH responded that it will require lots of work on the gas balancing agreements referenced in the HOA. The presumption is that there will be a 75/25 mix of Prudhoe Bay/Point Thomson gas for the vast majority of the life of this project. As long as that is the case, it can be counted on that the numbers will be relatively stable. But, in the early years, there may be a concentration of one or the other field, in which case it must be ensured that all of the parties are kept whole commercially; that a consistent amount and volume of gas for each party can be provided that matches up with the presumptions for throughput and volumes produced at the LNG plant that will go into the Sale and Purchase Agreements (SPAs) that will be marketed and completed.

[2:44:46 PM](#)

REPRESENTATIVE SEATON expressed his concern that as a representative of Alaska he wants to ensure that what happened with the administration's bill on oil taxes will not happen in this agreement, which was that everyone pays at 12.5 percent

even though some had bids at 16 percent. For people putting through the same amount of gas, he said he wants to ensure that if there is a difference in royalty between different fields there will not be varying tax rates to compensate for the different royalty rates. This is a long-term project and now the state is taking tax in-kind and it could become "mushy" and expensive unless all of the aforementioned is figured out ahead of time.

MR. PAWLOWSKI replied there are two key points in HB 277, the first being that the bill contemplates the "opportunity" for in-kind. All tax being paid in-kind at all times is not being allowed. Rather, the in-kind option for tax exists for very specific instances, which is consistent with the Heads of Agreement when a party's royalty has been taken in-kind. Second, HB 277 does not contemplate changes, offsets, or differences in the tax rate for gas. The combination of these two things drives the state's share in the project. Offsetting incentives are not being looked at to offset different royalty rates. A simple flat tax system of 10.5 is being proposed, which will be discussed when the bill is before the committee.

[2:47:57 PM](#)

CO-CHAIR SADDLER drew attention to question 1 on the first page of the administration's February 11, 2014, response, which asks whether there is a termination contract [related to the AGIA license]. He related that the answer states there is no termination contract and that there are two different mechanisms for terminating the AGIA license. One is an uncontested abandonment under a certain section and the other is a mutual agreement that the original project contemplated is uneconomic. Maintaining that those two mechanisms are parallel and duplicative, he asked the reason for having both.

COMMISSIONER BALASH answered the AGIA statute provides two paths, with both paths starting the same way. He posed a scenario in which the State of Alaska, through the DNR and DOR commissioners, says the project is uneconomic. That triggers one of two outcomes. One is that TransCanada agrees and it is mutually agreed to abandon with no contest. The other is "not so fast, you gotta approve ... that the project is uneconomic." There is a skeleton of a process laid out in the statute that would govern that contested determination involving an arbitrator and certain economic assumptions. If at the end of that process the arbitrator says the state is correct and it is uneconomic, then everything wraps up. If the arbitrator goes in

TransCanada's favor, then the license stays in effect and there potentially are rights to make up for any lost time or value.

[2:50:12 PM](#)

CO-CHAIR SADDLER asked whether he is correct in assuming there are two different mechanisms and it will be the state's decision to pursue both of them or just one of them.

COMMISSIONER BALASH responded the path outlined in the MOU is the first one that he described. The process is outlined in statute and the state would initiate and TransCanada would agree that the "Alberta project" is uneconomic. Responding further, he confirmed this would be called the uncontested abandonment.

CO-CHAIR SADDLER understood that is separate and distinct from TransCanada's agreement that the AGIA project is uneconomic. One is uncontested and the other is going through the transition agreements. He said he does not understand why because both seem to be the same end, but two different paths.

COMMISSIONER BALASH replied the intent if the enabling legislation is adopted is to draft and execute the transition agreements identified in the MOU, specifically the Precedent Agreement and the Equity Option Agreement. That would then trigger the process for abandonment of the license. It would be at that point that [the state] would raise its hand, initiate the process on the state's side, and TransCanada would then agree that the "Alberta project" is uneconomic.

CO-CHAIR SADDLER understood that is the mutual agreement that is uneconomic.

COMMISSIONER BALASH answered yes.

CO-CHAIR SADDLER said that is distinct from the uncontested abandonment of the AGIA license.

COMMISSIONER BALASH responded "uncontested" and "mutual" are the same thing.

[2:52:07 PM](#)

CO-CHAIR SADDLER said he still does not understand whether it is one process or two.

MR. PAWLOWSKI offered his belief that part of the confusion here is that the pathway for the uncontested abandonment stated in sentence two of the response [for question 1] is based on the determination that the project is uneconomic. They are not actually separate processes; the way the word "uneconomic" is used here implies a separate process, but actually the abandonment process itself depends on the decision to be uneconomic. It really is one process. How the process is executed, whether it is uncontested or mutual, changes how that one process is gone through.

[2:53:19 PM](#)

CO-CHAIR FEIGE said the whole arrangement with the MOU and how it fits into the HOA is fine. The business deal that is the MOU asks that the State of Alaska essentially cede a share of its potential ownership in the overall project to TransCanada; a value is assigned to that. [The administration] has demonstrated there is value that TransCanada brings to this. The question for the committee is whether the values offset whether it is a good deal for the state or a slightly better deal for TransCanada. Slide 4 depicts the numbers being talked about for the next two years. If the state executes "the divorce option," which is the red box on slide 3, the state pays \$130 million for the information and the state walks down the road without bringing somebody else into the overall project. If the state did that, the state would be on the hook for a lot of these costs. Not having to put up cash initially has a value to the state. The state may exercise an option to buy back 40 percent of that overall share in just the pipeline and the gas treatment plant (GTP). He inquired what those values are and whether the value of the equity share is offset by that. He further inquired whether the state has to go further down the road into the FEED process and the billions of dollars that have to be spent to get through FEED. He asked at what point the value works out to be an equitable arrangement for the state.

[2:55:58 PM](#)

MR. PAWLOWSKI replied that one of the two issues is the upfront cash. Today, the equity option from a net present value perspective does not look like a good deal to the state because of the time that elapses when the state is putting cash on the table. The revenues the state is receiving when the project is in operation must be carefully looked at because the time between today and the time of operation in the mid-2020s is a long time to be putting cash out before there is revenue coming

back in. When looking at it from a purely net present value basis, the state actually comes out ahead by having TransCanada as a partner. Exercising the equity option so that the state is paying money during that time period actually reduces some of the net present value benefit to the state of not having to spend that money. The carry cost must be analyzed. When looked at broadly, the state's opportunity cost of capital is about 6 percent -- the state earns 6 percent when its money is sitting in the Constitutional Budget Reserve Fund (CBR). Taking that money out of the CBR, or out of another reserve account, and putting it into this project comes at a cost. The state's debt capacity must also be carefully looked at for that financing period of 2018-2024. There is a certain limit to the amount of debt that the state can prudently take and analysis of that is ongoing. The offset of the money in the near term versus the revenue difference in the long term shows little difference in the revenue in the long term to compensate for the cash out in the near term. [The administration] looks forward to the legislature's consultants getting up to speed on those numbers and providing an independent analysis around that. The state has some of that information available online in the royalty study. He cautioned members about the lens through which this is looked at in regard to determining whether this business deal, this offset, makes sense because it could be looked at purely from a net present value standpoint that would under-appreciate some of the cash benefits in the outer years that the equity option provides.

[3:00:19 PM](#)

REPRESENTATIVE P. WILSON emphasized she wants to ensure the legislature does not do anything that would jeopardize [the state's] position. She said she would like to hear from TransCanada that going ahead with ASAP, as is being done by AGDC, will not trigger the triple damages [under AGIA].

TONY PALMER, President, TransCanada Alaska, LLC and Vice President, Alaska Development, TransCanada, replied the process underway today, in which TransCanada has participated with the state administration, the three major producers, and AGDC, and which is before the committee for its consideration, has not been in contravention of the AGIA process during the course of that timeframe.

[3:01:54 PM](#)

REPRESENTATIVE P. WILSON understood [HB 277] is what is before the committee. Since no one knows what the next step is, she presumed that Mr. Palmer cannot speak in regard to that area.

MR. PALMER responded yes, TransCanada has agreed with the other parties, including the administration, on a structure to go forward to transition out of AGIA into a new structure. He said he cannot predict what will happen in the event the legislature says no to that structure and then wishes to go forward on a different basis. TransCanada has agreed that during the course of this process the state is not in contravention of the treble damages issue. In the event the legislature decides to say no to this proposal, TransCanada will see what the situation is at that time.

REPRESENTATIVE P. WILSON surmised the aforementioned means that maybe TransCanada would go back to where things are at now and change its mind.

MR. PALMER said that going forward he cannot look to respond to a hypothetical circumstance if the state turns down the legislation. TransCanada has agreed to a structure today that it thinks is a smooth and amicable transition with the administration - subject to sanction by the legislature - that would move out of AGIA and into a new structure.

[3:03:38 PM](#)

#### **ADJOURNMENT**

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 3:04 p.m.