

HOUSE FINANCE COMMITTEE
THIRD SPECIAL SESSION
October 31, 2015
10:06 a.m.

10:06:15 AM

CALL TO ORDER

Co-Chair Neuman called the House Finance Committee meeting to order at 10:06 a.m.

MEMBERS PRESENT

Representative Mark Neuman, Co-Chair
Representative Steve Thompson, Co-Chair
Representative Dan Saddler, Vice-Chair
Representative Bryce Edgmon
Representative Les Gara
Representative Lynn Gattis
Representative David Guttenberg
Representative Scott Kawasaki
Representative Cathy Munoz
Representative Lance Pruitt
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Pat Pitney, Director, Office of Management and Budget, Office of the Governor; Marty Rutherford, Deputy Commissioner, Department of Natural Resources; Mark Myers, Commissioner, Department of Natural Resources; Representative Dave Talerico; Representative Shelley Hughes; Representative Paul Seaton; Representative Andy Josephson; Representative Dan Ortiz; Representative Geran Tarr.

SUMMARY

HB 3001 APPROP: LNG PROJECT & FUND/AGDC/SUPP.

HB 3001 was HEARD and HELD in committee for further consideration.

TRANSCANADA AND PRE-FEED SUPPLEMENTAL APPROPRIATIONS
SUMMARY

Co-Chair Neuman reviewed the agenda for the day.

#hb3001

HOUSE BILL NO. 3001

An Act making supplemental appropriations; making appropriations to capitalize funds; making appropriations to the general fund from the budget reserve fund (art. IX, sec. 17, Constitution of the State of Alaska) in accordance with sec. 12(c), ch. 1, SSSLA 2015; and providing for an effective date.

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^TRANSCANADA AND PRE-FEED SUPPLEMENTAL APPROPRIATIONS
SUMMARY

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PAT PITNEY, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, OFFICE OF THE GOVERNOR, provided a PowerPoint presentation titled "TransCanada and Pre-FEED Supplemental Appropriations Summary" dated October 2015 (copy on file). She explained that the presentation covered five major topics (slide 2):

- How much funding for AKLNG has the state provided to date?
- What is included in the supplemental appropriation request?
- Why is the supplemental request \$157.6M versus \$108M?
- What changes have occurred in the Pre-FEED phase resulting in cost increases?
- How much will it cost to complete the future gasline phases?

Ms. Pitney advanced to slide 3: "SOA AKLNG Appropriations to Date."

Funding to Date \$90.5 M

SB 138 General Fund to LNG Fund (FY14-FY15) \$69,835.0

- Capitalized the LNG Fund
- AGDC, AKLNG downstream cash calls, contractual service with agencies

Ms. Pitney noted that some of the SB 138 [legislation passed in 2014 related to a gas pipeline, AGDC, and oil and gas production tax] general funds were allocated to different departments via RSA [reimbursable services agreement] for service to Alaska Gasline Development Corporation (AGDC). She continued to address slide 3:

General Fund Appropriations (FY15) \$11,762.0

- AEA in-state affordable energy study
- DNR North Slope Gas Commercialization
- DOR Tax Division

Ms. Pitney expounded that the Alaska Energy Authority (AEA) energy study was conducted to look at energy requirements and needs outside of the area that would be available on the gasline (i.e. rural and other areas within Alaska that would not be directly serviced by the pipeline). She continued to address slide 3:

Appropriations (FY16) \$8,987.0

- DNR North Slope Gas Commercialization (in-state gas line fund)

Ms. Pitney elaborated that the funding request had been just over \$13 million, but only \$9 million had been funded. The current request was to fund the additional amount. She concluded with the final points on slide 3:

Authorization from LNG Fund (FY16)

- Within original \$69,835.0 capitalization
- AGDC, DNR, DOTPF \$3,023.0

Ms. Pitney explained that because of available capacity within the original \$69 million, authorization of \$3 million from the LNG Fund had been given to cover the operating costs primarily of AGDC. She noted that the cost was within the original \$69 million capitalization. Of the \$3 million increment, \$150,000 would go to the Department of Natural Resources (DNR) and \$71,000 would go to the Department of Transportation and Public Facilities (DOT).

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Ms. Pitney moved to slide 4 titled "State Gas Team FY2016 Supplemental Summary":

Supplemental Request \$157.6 million plus \$5 million AGDC Statutorily Designated Program Receipts (SDPR):

Agency Operating Budgets \$13,607.0

DNR: \$2,126.0

DOR: \$1,381.0

DOL: \$10,100.0

AGDC: Capital Budget \$144,045.0

Reimburse TransCanada: \$68,445.0

Fund State's remaining Pre-FEED share: \$75,600.0

AGDC: Receipt Authority \$5,000.0

AKLNG reimbursement for work performed

Ms. Pitney elaborated on the \$5 million in receipt authority to AGDC. She explained that AGDC had done work on behalf of all of the partners within the AKLNG project; the funds provided the corporation the ability to receive the money and to essentially reimburse itself for the work.

Ms. Pitney addressed why the supplemental request had increased from \$108 million to \$157 million (slide 5). She explained that the \$108 million had been limited to the AGDC portion of the request, which meant the request had really only increased from \$108 million to \$144 million. She furthered that the number had changed because there had been a pre-FEED [Front End Engineering and Design] scope and schedule increase of \$182 million for all of the AKLNG partners; the overall cost had increased from \$511 million to \$694 million. She furthered that the state's share of the new total was \$173 million (\$66 million for the liquefaction plant and \$107 million for the gas treatment plant (GTP) and pipe). She noted that the difference between the \$173 million and the \$182 million was based on the number of months.

Representative Gattis asked Ms. Pitney to repeat the information.

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Ms. Pitney addressed the question by turning to slide 6 titled "Pre-FEED Scope and Budget Changes." Prior to the pre-FEED increase the administration had estimated the supplemental request at \$108 million. She noted that the actual cost if no increase had occurred would have been \$106.8 million. The figure included funds TransCanada had already spent, the remaining cash calls for the midstream area the state would pick up. She addressed the increase from \$511 million to \$694 million. There had been no change to the following figures: \$68.4 million for the buyout of TransCanada's portion of the project and \$29.6 million on the midstream cash calls. Under the budget change the allowance for midstream scope changes had increased to \$31 million [from \$8.8 million] and another \$15 million for downstream costs (liquefaction plant).

Ms. Pitney returned to slide 5 and explained that the state's share of the \$66 million for the liquefaction plant was \$15 million and its share of the \$107 million for the GTP and pipe was \$31 million.

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Co-Chair Neuman asked if the increase in the request was because the gasline development team moved some of the projects from FEED into the pre-FEED stage. He asked for the reason of the increase.

Ms. Pitney agreed. She directed attention to the bottom of slide 5 and relayed that there were four pieces of the change. The first piece was related to component level optimization to lower costs and increase efficiencies, which had been moved from FEED back to pre-FEED. The second component was related to accelerating regulatory and pre-bid work on FEED contracting. She elaborated that the intent was to be ready to put contracts "on the street" in a very short timeframe if a FEED decision was made.

Co-Chair Neuman asked who made the change to the scope.

MARTY RUTHERFORD, DEPUTY COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES, replied that it was the AKLNG project scope change, which was managed by a team comprised of representatives from the three producers, TransCanada, and AGDC. The scope change had added additional costs to complete the pre-FEED work.

Co-Chair Neuman asked for verification that the changes had been requested by the project development team. Ms. Rutherford replied in the affirmative.

Ms. Pitney continued to explain the scope changes on slide 5. The third and fourth components were to increase the scope of geohazard work and to bring the 48-inch pipe concept design up to the 42-inch pipe level of development. She relayed that DNR would address the agency operating requests.

Ms. Rutherford advanced to slide 7 titled "Department of Natural Resources State Gas Team." Relayed that there were certain aspects of SB 138 that were DNR's responsibility. The most important were the negotiating of the upstream commercial agreements associated with gas supply and gas balancing, upstream cost allowance, and disposal costs. The issues were important to ensure that there was a reasonable sharing of cost among all of the project interest owners. The department also had a role in negotiating the midstream issues to ensure that expansion and third-party access was accommodated by the project. She communicated that it would have a huge effect on the state's future lease sales, in addition to existing and future exploration and development companies with interest in exploring for and monetizing gas supplies. The department had an incredibly important role associated with marketing the gas, which was also part of the commercial negotiations. She furthered that joint venture marketing and equity marketing were both under consideration. Additionally, SB 138 specified that each of the three producers were to provide the DNR commissioner with an offer to purchase and market the state's gas. She noted that all of those alternatives were under consideration by DNR.

Ms. Rutherford relayed that there were three pieces of the department's request. She noted that for FY 15 DNR had requested approximately \$13 million and received just under \$9 million, which represented a \$4 million shortfall of DNR's expected expenditures. The department had been told that if the shortfall became a problem it could submit a supplemental request; therefore, it had decided to take advantage of the special session to make the request. She explained that DNR would be expending money fairly intensively between the present day and the second quarter of 2016 as it worked to finalize the commercial agreements.

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Co-Chair Neuman asked Ms. Rutherford to provide the costs associated with each item she discussed. For example, there was \$70 million to cover the costs that TransCanada had incurred on behalf of the state within the AKLNG project management team. He asked her to specify whether a request was for supplemental funds or for additional work to be required due to the change in scope.

Ms. Rutherford clarified that she was currently only speaking to the DNR supplemental request for the remainder of FY 16.

Representative Gara remarked that under the current structure each of the project partners were looking to obtain their own gas marketer. He referred to a provision in SB 138 that provided the option to let the producers sell the gas for themselves and the state at the best terms they could achieve. He asked why there had to be more than one gas marketing person. He wondered if it was not possible for all of the partners to rely on one another to only have one marketer.

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MARK MYERS, COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES, replied that one of the challenges with marketing natural gas to overseas markets was the lack of transparency in the structure combined with the warranting required to deliver the gas, and the coordination it took because it was not sold on the spot market. He elaborated that very little was sold on the spot; therefore it was necessary to make long-term commitments and guarantees. He explained that a seller had to assure supply and needed a trusting relationship with the buyers. Additionally, the prices and contracts were indexed. A project the size of AKLNG would have many contracts; there was no single party that would purchase all of the state's gas unless it was sold to an aggregator in which case the price would be heavily discounted. He continued that the scenario described by Representative Gara where producers sold the gas was fundamentally what would be done under the royalty in value (RIV) methodology - where the producer would be the seller and the state would receive the higher value in the field of any of the producers. Throughout the process one of the known challenges was transparency. He detailed that when selling

multiple contracts gas moved very complexly; tracking the molecules and ensuring a seller received their actual price was difficult. He explained that most of the time when producers offered to sell gas for an entity to market, they offered a specific price. He furthered that it was the producers' job to make money on all aspects of the business, including the sales piece. Under the scenario, the state would be guaranteed a price for its gas, but he believed the producers would try to exceed the price in the market. He relayed that producers could not go that route under an RIV scenario, but the state would have to be able to trace the molecules or have some mechanism to its reopener processes.

Commissioner Myers explained that realistically a joint venture marketing process was preferable if the state was going to market with the producers; that way the state would have employees seconded into the project and it would be an equal partner with equal information flow. He stressed that joint venture marketing was an important mechanism to market. He relayed that some producers preferred joint venture marketing whereas others preferred equity marketing; it varied by region and by partner. He expounded that it was a complex deal that had to be negotiated. For example, one company may advocate for joint venture marketing in the AKLNG project, which was DNR's choice as the cleanest, easiest, lowest cost, and highest fidelity option. However, all of the producers would have to agree on the option, which they may or may not choose to do. He noted the issue was under negotiation.

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Ms. Rutherford expounded on Commissioner Myers's answer to the question posed by Representative Gara. She explained that there was one particularly good reason why it was not possible for more than one party to work on marketing gas; there were serious antitrust issues. She detailed that the negotiations had to be conducted in a bilateral way.

Co-Chair Neuman interjected that he believed each owner of the gas pipeline would be responsible for selling their own gas.

Ms. Rutherford agreed and added that there were legal limitations to the project partners marketing gas together. There were commercial negotiations underway that would

determine what the state's recommendations would be on the marketing structure. She continued that if the state recommended a joint venture marketing structure with one or more of the parties, the structure would have to be set up very specifically in order to avoid triggering antitrust issues. She relayed that joint venture marketing, equity marketing, and selling the gas directly to each company were all under discussion. The reason the state currently needed a gas marketer was because the structure had not been determined and the state was limited to bilateral conversations with potential purchasers. Additionally, the state needed advice on the appropriate structure or combination of structures it should begin to develop internally in order to present a full package to the legislature when it came forward with the commercial agreements.

Co-Chair Neuman asked committee members to keep their questions to the budget and presentation before the committee.

Representative Kawasaki asked if the agency budget requests were specifically due to the change in scope that AGDC made. Ms. Pitney replied that the costs would exist without the scope change; the costs were related to the state's representation in the project. She furthered that had the scope not changed, the acceleration of the project and the state's role in moving the project more urgently required the costs.

Ms. Rutherford elaborated that the funding requests associated with the Department of Revenue (DOR), DNR, and the Department of Law (DOL) were all related to the project's commercial negotiations. The project piece would be held by AGDC going forward [instead of TransCanada] and the work plan and budget numbers, which was where the accelerated pre-FEED impact resided.

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Representative Kawasaki asked if there was a need to move the commercialization forward faster because of the new pre-FEED and scope changes.

Ms. Rutherford responded that in order to keep the project on schedule with the intended operational timeframe of the end of 2024 to 2025, it was necessary to backup to finish

pre-FEED in 2016/early 2017. In order to complete the commercial agreements the state needed the ability to have a constitutional vote by the next general election on November 8, 2016. The timeline required that the administration would have the commercial agreements to the legislature in the late second quarter of 2016. She stressed that the end of 2015 and the following two calendar quarters would be incredibly intense negotiations on all of the commercial agreements, which was driving the additional appropriations to the agencies.

Representative Gattis remarked on the \$840,000 gas marketing position. She did not know what the industry pay standards were for the position. She inquired about the going rate and wondered if the state knew other companies that paid the going rate.

Commissioner Myers responded that the state had looked at and benchmarked the costs; it had used Human Capital Management for Oil and Gas and Black and Veatch. Additionally, the department had conferred with its colleague Audie Setters who had retired from Chevron as a gas marketer. The prices hopefully represented the upper end of the range. He stressed that it was critical for the state to hire the best marketer due to the swing in value associated with how the state marketed, how it negotiated the markets, and how it assured that the state was effective and credible during negotiations (both internally and with the markets). He stressed that the contracts had to be aligned by the end of FEED otherwise the project would not be financed. He continued that the presented cost represented the appropriate cost for the career field. One of the challenges was that typically gas marketer positions were paid a large bonus, which could be equal to or greater than their salary. He elaborated that the base salaries were not that high, but with bonuses and factoring in incentivizing a person to move to Alaska for the job added cost. He reiterated that the cost represented a benchmarked range. He believed analytica had testified to the range as well.

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Representative Gattis summarized that the \$850 million was the going rate and a bonus was paid if the marketer produced results. She asked if the position would have a long-term contract for the next 20-plus years.

Commissioner Myers responded that that the department foresaw the need for a larger marketing group. The single marketer was to help the state structure, build, and negotiate the early contracts. Depending on the style of marketing it would be more or less labor intensive.

Representative Wilson recapped some fiscal numbers. She asked for verification that the [pre-FEED] cost had increased from \$511 million to \$694 million. Ms. Pitney replied in the affirmative.

Representative Wilson remarked that it was a difference of \$183 million. She asked if the state was required to pay 25 percent of the amount. Ms. Pitney answered in the affirmative.

Representative Wilson surmised that the state's portion would include a \$48 million difference. Ms. Pitney answered in the affirmative.

Representative Wilson thought that based on the administration's numbers, the difference was \$37 million instead of \$48 million.

Ms. Pitney referred to slide 6. She explained that the funding estimated by the administration had included an allowance for midstream scope changes of \$8.8 million, which was available to cover the additional costs. The increase was \$31 million. There had been a contingency built in for scope changes. The past spring/summer, the \$108 had included an allowance for scope changes in the midstream area. She furthered that because the scope changes for the midstream had been determined, the \$8.8 million could be applied and came off of the \$48 million.

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Representative Wilson had used the numbers on slide 6 in her calculation. She explained that she had subtracted \$8.8 million from the \$31 million (under the new pre-FEED scope column), which equaled \$22.2 million. She had added the \$15 million allowance for AGDC [downstream scope changes}, which brought the amount to \$37.2 million. She had multiplied the figure by 4 to account for the four partners, which brought the total to a change of \$148.8

million. She thought the figure should match the \$183 million, but it did not.

Ms. Pitney explained that the reason the \$8.8 million Representative Wilson had subtracted from her calculation actually counted towards the scope change.

Representative Wilson asked for verification that the state had not yet paid the \$8.8 million. Ms. Pitney replied in the affirmative. The figure could be applied to the scope change. Representative Wilson asked for verification that it was only the \$8.8 million that had not been paid. Ms. Pitney replied in the affirmative.

Ms. Rutherford continued to address the most important responsibilities DNR had under SB 138. She moved to the bottom of slide 7. She explained that the department was requesting funds to cover personal services in the amount of \$646,000 and additional contractual money in the amount of \$1.5 million. She elaborated on the personal services request, which included funds to hire the high-level marketing lead that would begin to represent the state as it moved into a gas marketer in whatever structure the state determined was appropriate. She furthered that the state would need a lead marketing person even if it became an equity marketer. The state would also need a lead marketing person if the state became a member of a joint venture market structure in order to ensure that the state had an equal representative at the table when gas purchase agreements were developed. She relayed that it was the beginning of developing the structure that ultimately would be in place for the state. The position would also help the state analyze the appropriate structure or combination of structures the administration would recommend to the legislature in the spring of 2016.

Ms. Rutherford continued to address the personal services increment on slide 7. The administration was requesting an additional \$480,000 added to an existing \$360,000 to hire the existing gas marketing lead position; the additional money was for the remainder of the current fiscal year. The administration would include a total request as part of the regular budget request in the coming year. The administration was also requesting a new marketing analyst position to assist with negotiations and pre-marketing work.

Ms. Rutherford addressed the contractual request on slide 7. She communicated that DNR had been requesting \$580,000 to reimburse the department for supporting the AKLNG commercial negotiations going forward; it had revised the request to \$303,500 because it had eliminated some of the backfill positions that supported the project at a level of 50 percent or less. However, there were two positions the department needed to replace within the Division of Oil and Gas. The positions were commercial analyst positions within the division; to date the positions had provided 80 to 90 percent of their work in the past year to the AKLNG commercial negotiations on issues associated with RIK, upstream reservoir information to protect the state's interest as a gas transporter and marketer. She explained that the individuals were no longer available to provide their regular work to the division. She expounded that the division was engaged in commercial negotiations on a daily basis. There were six positions within the division: two had not been filled due to budget cuts, two were available, and two had been committed to AKLNG work. The \$303,500 request would enable the division to hire two additional commercial analysts for the remainder of the current fiscal year to prevent it from sliding further behind on its ongoing oil and gas commercial management responsibilities.

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Ms. Rutherford continued with slide 7 and explained that DNR was requesting \$900,000 for its contractual services related to the additional time spent by subject matter experts who were mostly under contract and were assisting with every aspect of the commercial negotiations and the package that would be brought to the legislature in the spring of 2016. The total \$1.8 million request had been reduced from the original request of \$2.125 million [note: the slide showed a total contractual request of \$1.48 million].

Vice-Chair Saddler asked for verification that DNR was requesting AKLNG funds for AKLNG work done by two of its Division of Oil and Gas employees. Ms. Rutherford replied in the affirmative.

Vice-Chair Saddler believed there should be a corresponding reduction in the General Fund money that had already been appropriated to pay for the services as regular departmental employees.

Ms. Rutherford answered in the negative. She explained that the department was asking to be reimbursed by AKLNG funds for AKLNG work performed by two Division of Oil and Gas employees. Thereby freeing up the General Fund money within the division to backfill the two positions in order to do the original oil and gas work.

Commissioner Myers added that the commercial analysts are worth their weight in gold. He elaborated that the analysts were responsible for the state's RIK sales. There were currently three proposals for RIK oil sales, which would be delayed without commercial analysts. The analysts also developed the department's lease sale terms and evaluated commercial terms on the state's unitization issues. He noted that there were many new units coming in.

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Co-Chair Neuman spoke to the issue of who would vote on the work plan and budget on the state's behalf on December 4. He shared that the committee had received an email the previous day from the governor related to the topic. He asked which state organization would be casting the state's vote on the work plan and budget assuming an appropriation was made and TransCanada was no longer involved.

Commissioner Myers responded that if the buyout [of TransCanada's portion of the project] happened AGDC would vote on behalf of the state.

Co-Chair Neuman asked who would direct the way AGDC employees should vote (i.e. the AGCD Board of Directors or other). Commissioner Myers replied that the AGDC vote would be the vote of the state. He relayed that the state would advise in the process from the perspective of the necessary commercial terms. The vote would be to move an established work plan and budget forward; therefore, he did not foresee any issues with the vote. He explained that the only options would be to vote for or against the work plan and budget; if the state voted against the items the project would be terminated. He believed the process was straight forward.

Ms. Rutherford clarified that the state had been working with AGDC on many of the commercial agreements that affect the project (i.e. on the GTP, pipeline, and the

liquefaction plant). She explained that if the legislature made the appropriation to terminate the Precedent Agreement with TransCanada, the interest that TransCanada currently holds in the pipeline and GTP would be transferred to AGDC. She continued that AGDC would continue to work with the state agencies for input on the work plan and budget; however, the AGDC board would direct the vote by the representative to the project management team.

Co-Chair Neuman referred to Ms. Rutherford's testimony that AGDC would work with DNR on the work plan. He asked if it would only work with DNR on requests made by AGDC related to project permitting.

Ms. Rutherford responded that as the state moved through the phase of developing commercial agreements that affect the state's interest, there were portions of the agreements that were led by AGDC, such as the governance of the project. The governance of the project would be the actual interest owners of the project. Assuming AGDC would hold all of the state's interest in all three elements of the project, the parties would be AGDC, ExxonMobil, BP, and ConocoPhillips. She furthered that AGDC had representatives on the management team and would be the ones to vote; however, the commercial agreements had elements that were of great importance to the sovereign, such as expansion, third-party access, withdrawal, to what degree the state received information and had a vote, and whether a vote required all four parties to agree or a majority vote. She explained that all of those questions would be embedded in some of the various agreements. She elaborated that the various state entities all had input and had been discussing what the state's interests were and what the agreements would look like. She stressed that the input from the state would continue before the project structure and governance became fully solidified. She stated that at the end of the day AGDC would hold the state's interest and its vote and the board of directors would direct the vote.

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Co-Chair Neuman remarked that according to the state's AKLNG gas team organizational chart, Commissioner Myers was listed as the decision maker for DNR. He asked Commissioner Myers if he had signed a confidentiality agreement that allowed him to see information considered confidential by the AKLNG project.

Commissioner Myers replied in the negative.

Co-Chair Neuman asked how the commissioner could make key decisions to negotiate agreements concerning the project [without having access to the confidential documents]. He referred to a hypothetical scenario where someone developed a compressor and specific information about their components was confidential. He stated that the committee had been told that members of Alaska's team had to leave the room in order to have certain discussions and that it had been disruptive. He wondered if the fact that Commissioner Myers was not privy to some of the confidential information had slowed the process down.

Commissioner Myers replied that Attorney General Richards and the governor had produced a letter stating that the attorney general believed that commissioners were not required as senior decision makers to sign confidentiality agreements to see the data (similar to a CEO or senior and vice president at a corporation). Additionally, the state had been working with the producers on an agreement that was clear and concise. He continued that when he went to a sponsors meeting he would email the group to let them know he would hold the information confidential; the process allowed them to successfully move information back and forth. Additionally, there were data sets that were critical to the project and were held confidential under other means in state government. For instance, the upstream data and supply issues and balancing lease equity related to net profit sharing was all done under DNR's existing authority and confidentiality. The subset of data specific to AKLNG was not as large as one may think; however, certain issues were. The state had worked with the producers and had seen adequate confidential data.

Ms. Rutherford added that the provided confidential AKLNG information had been provided by the producers to administration executives. She furthered that there had been sponsors meetings that included that attorney general and commissioners where the producers had rolled out confidential information. The producers had accepted to some degree, the ability of the executives to participate in the discussion without having signed confidentiality agreements.

Co-Chair Neuman asked if Ms. Rutherford had stated that there had been faux meetings. Ms. Rutherford answered in the negative. She explained that the sponsors group was made up of the highest level representatives of the parties with interest in the project. When the sponsors met there had been times when the state's attorney general or commissioners had been invited to the meetings where the producers had shared confidential AKLNG information. She added that it was the primary method by which the commissioners had been receiving confidential information from AKLNG

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Co-Chair Thompson stated he was confused about the by DNR's statements that AGDC would make decisions and vote on the state's behalf at the management team level, but it had not been allowed to sign a confidentiality agreement. He surmised that when confidential information was discussed at meetings, AGDC would be required to leave and the attorney general or department commissioners would step in for the state. He stressed that the situation would leave AGDC out of the loop. He was unclear on why there was a problem with confidentiality agreements. He furthered that confidentiality agreements were common in every industry especially in the oil and gas industry. He wondered how the state was supposed to make an informed decision. He emphasized that HB 4 [legislation passed in 2013 related to AGDC and the Regulatory Commission of Alaska] and SB 138 provided specific authority for AGDC to sign robust confidentiality agreements. He asked why it was an issue.

Ms. Rutherford clarified that there was a huge distinction between the AKLNG project management team and the commercial discussions. The project management committee currently represented the state's interests through Joe Dubler [AGDC vice president and chief financial officer] with AGDC and TransCanada. She elaborated that if the TransCanada Precedent Agreement was terminated AGDC (probably through Mr. Dubler) would continue to make the project decisions. She relayed that Mr. Dubler had signed an AKLNG confidentiality agreement. The only people involved in the AKLNG commercial discussions who had not signed confidentiality agreements were at the highest levels (i.e. the governor, DNR and DOR commissioners, and attorney general). She relayed that it had been the opinion of the administration that just like producer executives,

the aforementioned individuals were not required to sign the confidentiality agreement. She stated that functionally it had been working. She emphasized the importance of making the distinction between the project and the commercial discussions clear. She believed that all of the staff at AGDC working on the AKLNG project had signed the confidentiality agreement, as had the agency staff.

Co-Chair Thompson referred to proposed regulations related to changing the confidentiality requirements by AGDC. He noted that some individuals within AGDC had signed confidentiality agreements; however, he wondered if the proposed regulation would change confidentiality agreement requirements for future people.

Ms. Rutherford answered that she had heard there were new confidentiality regulations that had been proposed by AGDC, but she was not familiar with them. She stated that questions about the regulations would best be directed to AGDC.

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Commissioner Myers echoed the response given by Ms. Rutherford. He stated that the discussion about regulations and AGDC did not pertain to DNR, DOR, or DOL (which was not working directly with AGDC). He could not speak to the internal matter related to AGDC because he was not privy to the information. He understood the need for confidentiality within a project and it was his hope that AGDC would second people into the project in the future. The corporation did not currently have anyone seconded into the project. He believed having people fully seconded into the project at all levels was critical to represent the state's 25 percent ownership.

Co-Chair Thompson asked if secondees would be required to sign a confidentiality agreement. Commissioner Myers responded that that an agreement was needed, but he did not know what the agreement would look like because the issue was between AGDC and its attorneys.

Co-Chair Neuman believed that SB 138 gave AGDC the ability to "have a blanket over them" as far as the Freedom of Information Act or the Public Information Act in order to enter into discussions with companies that had proprietary information. He also understood that the request for a

change in regulation by AGDC to alter the specific scope required in SB 138 was causing the entire project to slow. He stated that it had been an issue with numerous parties if a regulation change allowed AGDC to enter into the negotiations and have discussions without being covered under a confidentiality authority. He asked who had requested the regulation change that AGDC had proposed.

Commissioner Myers replied that the department did not know. He stated that AGDC reported to an independent board and did not report to "our structure." He noted that Dan Fauske [AGDC president] was on lateral line to the commissioner of DNR and reported to a board and governor.

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Co-Chair Neuman noted that AGDC would speak to the committee during a meeting the following day. He asserted that the confidentiality agreement question was key to the commercial negotiations that were currently underway. He stated that the DNR commissioner was responsible for the negotiations. He asked if the partners were reluctant to enter into commercial agreements unless they were confident.

Commissioner Myers replied he had not seen that occur. The department had recognized the challenges early on associated with the DNR commissioner not signing a confidentiality agreement. He believed the information he was receiving from the companies was adequate. He elaborated that there was a long history of working with DNR and confidential data and to his knowledge DNR had never breached a confidential agreement in the 30 years he had been involved. He stated that there was a fair amount of trust in the relationship and he would not divulge confidential information.

Co-Chair Neuman asked if Commissioner Myers had requested to see the confidentiality agreement in order to start reviewing it.

Commissioner Myers answered that he had spoken with the governor and the attorney general about whether they should sign the agreement; the conclusion had been that they should not sign them. He respected his boss and the decision. They had found a way to work through the solution, which was based on the advice that senior

executives were not required to be under the confidentiality in order to receive the information.

Co-Chair Neuman believed Commissioner Myers had stated that the governor and attorney general suggested that the DNR commissioner not sign confidentiality agreements.

Ms. Rutherford disagreed with Co-Chair Neuman's assessment.

Commissioner Myers clarified that he had not asked to sign or not sign a confidential agreement. He had been aware that if he could not see confidential information there was an issue with the responsibility he had as the commissioner of DNR and as a decision maker. He relayed that the governor's statement and a memorandum to the producers specifying that senior executives (who were not under the agreements) needed to see confidential data, had been adequate and had worked. He noted that it had made some individuals uncomfortable, but it had been working. He stated that he had worked with a significant amount of industry and confidential data and had not seen a blockage of information. He had also been very respectful of keeping information confidential.

Co-Chair Neuman did not see how the issue would not slow the project down. He remarked that the state's organizational chart specified Commissioner Myers as a key decision maker. Additionally, the other department commissioners had not signed a confidentiality agreement. He commented on the December 4th deadline.

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Co-Chair Neuman stated that he had asked if the issue would slow down the project and that Commissioner Myers had answered that it would not. He was concerned about the issue and intended to address it further at a subsequent meeting. He discussed that the committee was scheduled to have a hearing about SB 138 and AKLNG project specifications in the bill. He elaborated that under the legislation, DNR with consultation with DOR, was to negotiate commercial agreements, market royalty in kind and tax as gas, and modify leases. He referred to a letter from the governor from the previous day affirming that AS 38.05.02 gave DNR and DOR the authorities and obligations to negotiate the associated commercial agreements and dispose of the gas from the AKLNG export project. He wanted

to discuss who was negotiating the commercial agreements for the state. He remarked on the \$10 million supplemental request from DOL for drafting, negotiating, and reviewing LNG contracts. He asked if the \$10 million worth of attorneys would be negotiating commercial agreements.

Commissioner Myers answered that DOL's direct support to its attorneys and the contracted attorneys (Millbank, Tweed, Hadley, and McCloy and Greenberg Traurig LLP) were critical to the negotiating success because the assistant attorney generals really understood Alaska law and the external lawyers had a long history of working on complex LNG projects. He explained that the organizational chart was not the chart of the operational organization, but the chart of the structure to negotiate on commercial agreements. The chart showed the various functions and positions and what the attorneys were working on. He stated that the fund was crucial. He elaborated that it was the third version of a gasline he had participated in; he remarked that the companies would be spending significantly more than that [\$10 million] on negotiations. The funds were to create a parity in the negotiations of the team; the specified experts on LNG were very important to calibrate the agreement versus others they had negotiated worldwide. There were many complex issues, a short time period, and multiple teams working on multiple issues in order to make things work. The legal support was absolutely necessary to the negotiating teams and commercial people. Ultimately, his responsibility to sign the agreements - he had to be sure the state had done all of its due diligence and had negotiated an acceptable deal; without that the department could not come to the legislature for approval of the structure and agreement in good faith. He reiterated that the attorneys were core to having a professional team in an LNG project, where the state was not experienced. He remarked that the state was experienced in oil and gas, but not LNG.

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Ms. Rutherford emphasized that the legal team was assisting with the commercial discussions (at the bottom of the organizational chart). She detailed that it was a team approach; the legal team was not making the decisions, but were participating in the discussion as part of the team.

Co-Chair Neuman requested a list of individuals on the organizational chart who had signed confidentiality agreements.

Co-Chair Neuman stated that according to the State of Alaska AKLNG gas team organizational chart, Audie Setters was the gas marketing lead. He remarked that DNR had requested an additional \$480,000 for [a total of] over \$800,000 to add to the existing vacant marketing position. He furthered that the committee had requested additional details on the roles and responsibilities envisioned for the position and how it compared with industry standards. He noted that the committee was awaiting the answer.

Ms. Rutherford responded that she had believed the information had been provided to the committee the prior evening or before the meeting. She relayed that it should be to the committee shortly. She clarified that Mr. Setters was a contractor and had been assisting the state to date. The department firmly believed it was time to begin to institutionalize the state's capacity on gas marketing in order to get up to speed and be a full participant as it moved into the actual project.

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Co-Chair Neuman asked why a marketing position was needed at the present time. He remarked that the state did not know how much gas it would have, no RIK or tax as gas decisions had been made yet, the transportation costs of the state's gas or whether the state would market its gas independently was not yet known.

Commissioner Myers replied that SB 138 had established a structure for commercial negotiations on the broadest scale. The legislature had given the department and commissioner strict instructions that the state had to receive RIK value that was equal to or higher than RIV. There were many ways to achieve a project, but limited ways to achieve a project that would maximize value at the wellhead for the state. He furthered that the state's work on the project - with assumptions on value to the state - assumed a certain wellhead value. The wellhead value was determined by the cost the state paid upstream, the surety of gas supply, transportation costs, and what the state would get in the market.

Commissioner Myers continued that it was all about selling a commodity at a price that maximized the benefit to Alaska in addition to other advantages of jobs, in-state gas, and the construction of infrastructure. The legislature had charged the department with analyzing all of the elements he had listed, which the agreements summarized. He detailed that a surety of gas supply and balancing meant it would be necessary to get gas out of two fields in predictable quantities and when one field went down a bit, the other field could make it up (balancing). He elaborated that the state would lose a substantial amount of money if the pipeline was not full for the first 15 years of operations. He furthered that if the state marketed to customers and could not guarantee supply, the state would have to sell the supply at a heavy discount. He stressed that if the state paid too much for transportation fees it would lose money. In order to preserve the upstream value, the state had to negotiate agreements that were fair. He stated that it was necessary to be able to calculate the fees for comparison against an RIV structure (as required in the finding he had to deliver for approval by the legislature), which was very different. He explained that it meant the state had to know how it would market going into the discussions early.

Commissioner Myers continued to address Co-Chair Neuman's questions. He explained that the state would have to know how it was going to market and had to negotiate agreements with the other producers. He spoke to a joint venture marketing scenario where the state would be a partner with the producers, which would require the state to have people of equal caliber embedded in the structure. Under equity marketing, the state would need a whole team of people, (independent of the producers) that could preserve value in the markets where the gas was sold (e.g. Korea, Japan, and etcetera). He stressed that the state would be one of the largest gas marketers in the world under the project. He stated that under SB 138, the legislature had changed the game from being passive to being an active investor. Being an active investor meant that the state had to build to technical capacity in the organization in all phases moving forward. He stated that each one of the phases involved commercial negotiations at a more finite level where more value is exchanged. He spoke to the importance of having a lead that was a state employee and accountable to the state and could build the capacity. He remarked that consultants were skilled, but they only lasted with the organization

for a period of time and could be hired away. He explained that the knowledge base needed to be institutionalized and the team needed to be trained. He reiterated the need for a leader who would build the structure. He stated that the position was currently needed because the state was actively negotiating the marketing structure with the producers and the RIK finding determining what the approximate values would be as the project moved towards FEED. Once the project entered FEED the state would have to be marketing and making the contracts necessary to finance post-FEED into the final investment decision (FID).

Commissioner Myers further explained that the state would have to sell its gas before getting to FEED. He remarked that three or four years was not a very long time. He relayed that there was one contractor currently in place with expertise in the subject matter. He added that the contractor was very good, but was building a retirement home out of state. He furthered that the reality was building the continuity required the investment in people at present. He stated that the issue had been established by SB 138, which the department was trying to honor. Professionalizing and building a corporate structure for marketing was a large piece of the value stream for the project. The department wanted to do things professionally, which meant bringing in the right people at the right time. The department also wanted to minimize the number of people the department had in the structure. He remarked that AGDC would have many more individuals in the structure than DNR would have, even though DNR was doing the upstream and marketing. The department would need fewer than 6 people; the number of individuals seconded and embedded into the pipeline structure would be much higher. He clarified that most of the department's boxes on organizational chart would go away once the project entered the construction and operational phase. He reiterated that the negotiations were complex and took full teams of people to negotiate; it was necessary for the state to have the people in place. He stated that the project was one of the largest in the world; the state had signed on in an active role as part of the business structure. He added that if the state could not honor the business structure with the right people and budget, it would fail.

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Co-Chair Neuman referred to page one of the supplemental backup detail and referenced a sentence: "a gas marketing organization within DNR is an important step in preparing the state for successful gas under the Alaska AKLNG or alternative project." He asked if an alternative project was being considered.

Commissioner Myers answered that he was not aware of an alternative project. He believed that the governor had stated that if AKLNG failed he would still make efforts to monetize the gas on the North Slope; it would depend on why the failure occurred. Ultimately, the state was building a specific marketing structure for AKLNG, but the structure would depend on equity versus venture marketing; if venture marketing was chosen it would depend how many partners were involved. The state had created a flexible environment where the first people would be hired and as the project evolved, DNR may or may not request another position here or there; the situation was evolutionary.

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Co-Chair Neuman asked if it was the intent of the administration to terminate the contract with TransCanada prior to December 4 [2015].

Ms. Rutherford answered that the administration was intent upon purchasing TransCanada's interest in order to vote at the December 4, 2015 meeting (assuming legislative appropriation by the legislature). The administration was committed to having AGDC in place to cast the state's vote. She relayed that Commissioner Myers would provide a presentation at the next committee meeting that would provide additional detail. There would be a document the administration hoped to have ready for execution by the last week in November in order for everything to transition smoothly (with interest transferred to AGDC, a check cut to TransCanada, and the state moving forward as equity owner on all three elements of the project).

Co-Chair Neuman asked for verification that it would be the document that ensured legislators that AGDC would have a voting seat.

Ms. Rutherford answered that there may end up being three documents, which the administration was in the process of determining. She relayed that they did not know whether one

document could accommodate terminating the Precedent Agreement between TransCanada and DNR or whether it could terminate the relationship between TransCanada and DNR and convey the assets simultaneously to AGDC. She affirmed that the department would be executing all of the necessary documents to accomplish both.

Commissioner Myers added that in the House Resources Committee there had been concern about DNR's intent, given that the transfer could be to DNR prior to going to AGDC. He assured the committee that it had always been his intent that the facilities should be owned and integrated by the state's interest in AGDC. He stated that it was necessary to have a vehicle because he wanted to see smooth operations between the treating plant on the North Slope, the pipeline, and the liquefaction plant; they all had to operate together in unity. He elaborated that it would be problematic if each of the components became a competed against each other as separate profit centers. He furthered that there would not be a smooth, integrated organization. He stated that it had always been his belief that it was the best answer and the department had never contemplated any other structure. He remarked that if the committee was hearing rumors he did not know their origin. He stated that the rumors were not coming from the intent; the letter he had written to the committee verified that. He reiterated that it was the only logical structure for the state to be in; it was structured similar to the rest of the project. He expounded that creating an integrated infrastructure and smoother communications was one of the reasons that had been discussed structurally for buying out TransCanada. He saw DNR as the customer for AGDC. The department's ability to work with AGDC to ensure the customer's happiness was important. He would be a tough customer and wanted low tariffs and inexpensive transportation, which would increase wellhead value and revenue going into the General and Permanent Funds.

Commissioner Myers continued that pipeline companies did not always want the lowest tariff structure. He pointed to the history of Trans-Alaska Pipeline System (TAPS) and remarked that the companies clearly had not preferred it [the lowest tariff structure]. He wanted expansion in the pipeline because the department managed a lot of other gas on the North Slope. The department also wanted opportunities for its partners in the Arctic Slope Regional Corporation and Doyon to put their gas in the system. He

emphasized that the department was very insistent on expansion, which could be achieved commercially or with a larger pipe. He explained that as AGDC communicated back to the project it was important to have good communications and for AGDC to understand that its customer really wanted these things. There was a natural tension that existed, but communicating the need of the customer to the pipeline needed to be crucial. He stressed that the customer wanted a high quality product at a cheap price because it raised the wellhead value and the ultimate profitability to the state. The state would make very little money on the pipeline; the money would be made by selling its gas.

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Co-Chair Neuman expressed concern about the autonomy of the AGDC board and its ability to make decisions. He elaborated on the concern that the board would receive pressure from the administration on how to vote and conduct its work. For example, the Board of Fish was also supposed to be an autonomous entity, absent of political decisions; however, he believed that Governor Walker had contacted members of the board to ask them for a venue change for next year's meetings. He believed it was unheard of for boards that were supposed to be completely autonomous of politics. He continued that the boards were not supposed to have legislators or members of the administration putting pressure on them to make decisions. He asked what assurances Commissioner Myers could provide that AGDC would be completely autonomous in its decisions.

Commissioner Myers replied that he could not warranty what administration influences had affected AGDC and what had not. He stated that it was an awkward situation whereby he provided formal information requests to AGDC, which made requests to the management committee; information then flowed from the management committee to AGDC and back to DNR. He respected that AGDC had an independent board and he believed it was import that the board talk to the legislature if it had challenges. He detailed that the board needed to have the discussion with the legislature to explain how it was or was not working. He stated that he had never been invited to a board meeting and could not tell the committee what was happening within AGDC (he believed Ms. Rutherford had attended one meeting, but he had never had a conversation with Chairman Mike Burns or the board) other than from information received at a

sponsors meeting or in other meetings where there was a process for AGDC to get project information.

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Co-Chair Neuman stated that Commissioner Myers had told the committee that he had been instructed by the attorney general and governor's office not to sign confidentiality agreements. He had spoken with producers and other members of the gas negotiating team who were concerned that they could not enter into some of the confidential agreements because of proprietary information that may be provided by producers or others. He stated that it slowed down the process and he was concerned.

Commissioner Myers replied that any discussion of confidentiality agreements within AGDC were between the attorneys of AGDC and their client. He relayed that there was a relationship between DOL and AGDC, which DNR was not and should not be a party to because DNR was not the client. He did not know what the issues were between AGDC and its internal confidentiality agreement to work with the project.

Vice-Chair Saddler remarked that many of the committee's questions had been answered with conditions and were difficult to follow. He believed both testifiers were "straight shooters," but did not know if he could rely on the answers unless he took very careful notes. He heard a desire for things to happen and that a mechanism was in place, but he did not hear a clear yes or no or commitment. He asked if it was the administration's intent to terminate the structure going forward (to vote no on the work plan and budget).

Ms. Rutherford answered that the administration had every intention to move the project forward, which would be done in the form of commercial agreements as part of the work plan and budget. She stressed that it was not possible to ever be sure if commercial agreements would materialize in an agreement that was acceptable to all parties. She reiterated that it was absolutely the intent of the administration to move the project forward under the SB 138 framework.

Vice-Chair Saddler asked for verification that the administration did not intend to terminate the project. He had heard references to an alternative project. Ms. Rutherford responded that the administration had absolutely no intention of terminating the project.

Vice-Chair Saddler asked for verification that the department had stated that Joe Dubler [vice president and chief financial officer, AGDC] would cast AGDC's vote on the work plan and budget on December 4.

Ms. Rutherford replied that to the best of her knowledge Mr. Dubler would cast the vote for AGDC. She detailed that Mr. Dubler was the current AGDC representative on the AKLNG project management team. She communicated that she did not know whether Mr. Dubler would continue to be AGDC's choice once all three elements of the project were integrated; however, she assumed AGDC would choose him. She stressed that it would be AGDC voting the management committee decision on behalf of the state.

Commissioner Myers added that DNR had read about the subsidiary corporation in the AGDC minutes; the department had not been a party to any discussions about how internally AGDC would structure its pipeline organization or the gas treatment plant component. He hoped from the outside as a customer that it would be an integrated organization because the desire was to see a smooth flow of gas through a balanced and efficient system. He was not aware of how AGDC actually planned to do it; it had been an assumption on his part. He continued that AGDC's "structure would be determined by their board, not by me as their customer." As a customer, he would want to make sure he was receiving the lowest possible tariff structure and an efficient pipeline that was operational and expandable to take the other gas managed by DNR.

Vice-Chair Saddler stated that the silos were surprising to the committee - that Commissioner Myers was surprised by the development of some of the potentially very significant developments in the structure.

Commissioner Myers reiterated that it was a separate board structure. He reported directly to the governor; the processes in DNR including its confidentiality standards and its requirement to report findings to the legislature were clearly spelled out within SB 138. He furthered that

DNR had a very established public structure in the project and traditionally with its oil and gas management. For example, the department could not do a long-term royalty oil contract without coming back to the legislature for approval. He stated that the legislature had included the checks and balances in SB 138 for a reason. Similar checks and balances were not included in the AGDC structure - the legislature had designed the agency as a separate corporation with a separate board of directors; because the structures were very different, the level of internal and external information flow was also very different.

11:34:55 AM

Vice-Chair Saddler referred to an earlier question about the following language on page 1 of the supplemental request ["FY2016 Supplemental Request for State Agencies - \$13.6 Million" from Governor Bill Walker (copy on file)]:

The need for a marketing organization within DNR is an important step in preparing for successful sale of gas under the Alaska LNG Project or an alternative project.

Vice-Chair Saddler remarked that Commissioner Myers had stated he did not know of any plans for an alternative project. He stated that the document had come from the Office of Management and Budget. He asked Ms. Pitney if an alternative project was being considered in any way, shape, or form and to what degree.

Ms. Pitney answered that there was no other project currently being considered. There was intent to still move the state's gas to market if the current project did not succeed. She communicated that the administration wanted the project to succeed; they were as far down the road as possible and were on the cusp of making things work. Absent of that she questioned whether the state did not want to move its gas to market. She did not believe it was a good alternative for the state.

Vice-Chair Saddler agreed. He wondered to what degree the administration was looking past the potential termination to any alternative. He asked for verification that Ms. Pitney was saying there was no such consideration.

Ms. Pitney responded affirmatively.

Vice-Chair Saddler asked why it was not premature to be working on marketing currently. He pointed to the first page of the supplemental request document that included a bulleted list of projects including commercial agreements, marketing plan, lease modification, payment in lieu of taxes (PILT), and other. He thought the schedule had envisioned that the legislature would look at and approve the negotiated agreements sometime during the fall (2015). He wondered why that was not the case.

Ms. Rutherford stated that the parties had not reached agreement at present. The issues were not only between the state and the producer parties; some of the issues were between the producers themselves. Agreements on some key issues had not yet been obtained - once they were agreed to it would open up negotiations on other issues. It was the intention to have commercial agreements to the legislature by the second quarter of 2016. It was something that could only be attained if all four parties were equally committed to finding middle ground and acceptable arrangements.

Vice-Chair Saddler stated that his comfort in proceeding with TransCanada's involvement was that the information would be available to the legislature in order to make the decision to terminate TransCanada's involvement. He stated that the information in the document in front of the committee was going to be what he would have relied on to make the decision. He would have more comfort if he knew the status of the agreements and the likely outcome of the processes prior to committing the state to pursuing an alternative.

Ms. Rutherford replied that the administration had hoped that the commercial arrangements would have been completed as well. However, she disagreed with Vice-Chair Saddler about why the commercial agreements were absolutely necessary. She referred to a presentation given to the committee by Deepa Poduval (principal consultant, Black and Veatch) and stated that at the end of the day the issue was primarily a financial analysis on where the state should wear its risk and where it should make its payments. The state would pay TransCanada no matter what, but the choice was whether the state would pay the costs up front to become the complete equity holder or to bear the costs as part of the tariff structure. She remarked that there had been a pretty exhaustive discussion on the topic. She was

not sure what tremendous additional value the commercial agreements provided to the decision on terminating TransCanada's Precedent Agreement.

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Commissioner Myers elaborated on Ms. Rutherford's answer to Vice-Chair Saddler. He noted that TransCanada had testified before the committee; he discussed that there were multiple reasons for the company to support the buyout. He explained that under the agreement structure any of the five parties could terminate at any time all the way up to the FID decision at a certain cost. He furthered that TransCanada could opt to exit the project and the state would have to pay the costs. He continued that if the state bought out TransCanada's portion of the project there would only be four parties remaining; the state wanted to move the project forward and the administration hoped and believed that the producers also wanted to move the project forward. Parties that were fully aligned and commercially advantaged would help to move the project forward. He stated that TransCanada is a great company but it had serious commercial challenges with the governance pieces if they were not operators of the project - it would be difficult for the company to stay in given its business model.

Commissioner Myers communicated that buying out TransCanada's portion of the project would provide much more assurance of the project moving forward. Also, it would move forward in a way where the economics of the project were shown to the legislature including the voting rights to AGDC. He believed that buying out TransCanada's portion pointed to advantaging the state and moving the project forward. The fact that the other framework agreements had not been done was a challenge of the immensity of the agreements and the lack of alignment and commercial differences between the companies. He noted that the state was not a producer and had to effectively be like a producer in order for the deal to work. The supply assurance agreements would be number one; if the state could not assure supply, it had no business being in the project. He furthered that under that scenario the state would be better off staying in an RIV world and would

hopefully gain equity and the producers would ship on the state's pipeline; it was the alternative model that had been proposed in SB 138. For the project to work the state had to have the fundamental agreements to secure its supply to match its capacity in the project. He stated that without the fundamental agreements the other agreements were not "worth the paper they were written on." There was a critical sequencing to the agreements.

[11:42:13 AM](#)

Vice-Chair Saddler asked why it was not premature to go to marketing if the necessary commercial agreements had not been negotiated.

Commissioner Myers answered that the necessary team could not be built overnight; it took years to build a competent team. He stated that the contracts would have to be in place to market at the FID decision, which was not many years down the road based on the project timeframe. Additionally, the state has to negotiate a marketing position with the producers as a part of the RIK process; they needed to decide whether to go with equity of venture marketing. The state wanted the best professionals available in the field to help it make the best decision. He continued that each step of the way there were important marketing decisions the state needed to make; some of the positions were negotiated positions with the producers in each step along the way. The negotiations were part of the whole process of getting the baseline information the legislature wanted to have by December 31 [2015]. He furthered that it accelerated after that time and putting people in place at present was critical.

Vice-Chair Saddler understood there had been \$360,000 in the budget for marketing positions and the request had been made for an additional \$480,000 for a total of \$840,000. He asked if there had been recruitment efforts to fill the position at the \$360,000 level and what the results had been.

Commissioner Myers replied that the state had not yet begun recruiting because it did not currently have funding for the position. He did not want to do any recruiting without some assurance the funding would be available. He furthered that the state would hire a highly qualified person for less if possible.

Vice-Chair Saddler had heard someone say that the \$360,000 was already available, but the state had not tried to fill the position at that amount.

Ms. Rutherford explained that the department had received the \$360,000 on July 1. The state had been in the midst of determining what it could buy as a marketing lead and everyone involved had been shocked at the price tag associated with marketing leads in the industry both nationally and internationally. The department had realized quickly that the amount provided [\$360,000] would not suffice. How the state would deal with the issue had been part of the discussions; as the discussions evolved around the special session, the state hoped it would be an opportunity to adequately fund the position to ensure successful recruiting.

[11:45:26 AM](#)

Vice-Chair Saddler thought he had heard that there was not really recruitment or an open post and that Audie Setters had just communicated that he did not believe the amount [\$360,000] would be enough.

Commissioner Myers replied that they had gone to Human Capital and Black and Veatch to get further input. He explained that when he had heard the prices discussed by the state's team he had requested much more due diligence on the cost. He knew it would be an issue and had stressed the importance to the team about the need to benchmark the cost. Human Capital had looked at the market costs and the legislature's consultant analytica had also testified that the figures were in the ballpark.

Ms. Rutherford elaborated that Black and Veatch had not only relied on its own expertise; it had done outreach to multiple parties before providing feedback to the administration. She detailed that it had been a relatively broad effort, which included soliciting information from parties. She furthered that the consultant had not always received the information, but they had obtained sufficient consistent information to reach its determination. She had been relieved to hear that analytica believed the figures were consistent with its analysis as well.

Representative Gattis believed the state should want access to all of the information possible in order to make the best decision. She was concerned as an Alaskan citizen that the state would not do its best to obtain all of the information possible. She believed the department was remiss in not getting all of the information possible.

Co-Chair Neuman believed that the entire committee shared the concern.

11:48:16 AM

Representative Munoz noted that the previous day Mr. Butt had spoken to the importance of alignment. She detailed that a key element of the goal was the ability to have protection of intellectual property through confidentiality agreements. She wondered why Attorney General Richards - who was involved in commercial aspects of the project and was chief counsel to AGDC - was unwilling to enter confidentiality agreements related to the project.

Commissioner Myers deferred the question to Attorney General Richards. One of the concerns was that it would be necessary to revisit the issue if the confidentiality prevented providing enough information to the public. He referred to federal issues that percolated up over actions and the inability to explain. For example, military confidentiality created doubts in people's minds. He stated that on a commercial side there was concern about having confidentiality overly broad. He fully respected and agreed with the need to have the best information. He noted that he was a scientist by background and he believed in getting all of the information. He noted that the state needed to find a way to get all of the information, while having the ability to explain to the public with adequate granularity why the decisions were being made. He understood that balance was an issue, but for a further explanation he deferred to the Attorney General Richards or his designee.

11:50:13 AM

Representative Munoz asked if Attorney General Richards would be available for questions.

Co-Chair Neuman believed Attorney General Richards would be available for questions the following Monday.

Representative Munoz thanked the department for providing clarity on where the TransCanada shares would go if the state decided to buy them. She relayed that earlier in the day the legislature had received a letter from the commissioner and governor clarifying the intent.

Representative Wilson referred to slide 6 titled "Pre-FEED Scope and Budget Changes." She asked about the term "allowance for" and asked if it was the amount the administration thought the state would have to pay. She wondered why the \$8.8 million was in the left column instead of the right column.

Ms. Pitney responded that in the spring and summer when the state had the estimate of \$108 million it had assumed roughly \$70 million in the TransCanada buyout plus the \$38.4 million for remaining cash calls for the midstream through the end of the year. Had the scope not changed, the remaining cash calls would have only been \$29.6 million. The actual was the original estimate plus the \$31 million for the scope changes and \$15 million [allowance for AGDC downstream scope changes]. She explained that when the administration had initially estimated the cost of buying out TransCanada's portion of the project and taking over the cash calls at \$38.4 million (the combination of the \$29.6 million and the \$8.4 million). She furthered that without the changes the amount would have been \$29.6 million, which made the administration's original estimate a little off. She reiterated the costs including the scope changes.

Representative Wilson asked for verification that the figures on slide 6 represented actual amounts owed by the state that would make it current through the end of the year. Ms. Pitney responded in the affirmative.

Representative Wilson stated that the previous day the committee had learned that the state would be required to pay an additional \$60 million at the December 4th meeting. She asked for verification that the administration was asking for \$204 million.

Ms. Pitney responded that the \$29.6 million plus the \$31 million was the \$60 million that would be required.

Representative Wilson asked for verification that the total was \$144 million and the \$60 million did not need to be

added. Ms. Pitney agreed. She detailed that \$144 million was the total amount required for the state's full participation on midstream and downstream through the pre-FEED cash calls.

[11:54:41 AM](#)

Representative Wilson thought the administration may have the money in a part of its budget that was not accessible because the funds had been designated to come out of oil and gas but not permitting. She wondered whether the money could be adjusted within the existing budget versus allocating new funds.

Ms. Rutherford responded that the state did not have the money. She detailed that the request that was just under \$2 million included \$300,000 that would go to the Division of Oil and Gas to backfill two commercial analysts. She explained that everything else money that was money that was unavailable. If the department did not receive the additional \$1.8 million it would not have the ability to backfill the two positions and the people assisting the department with commercial contract negotiations would not be able to continue forward at the rate to achieve the contracts by April 2016.

Representative Wilson requested the amount of the total DNR budget for the current year.

[11:57:06 AM](#)

Ms. Pitney replied that she did not have the figure on hand; however, the department's budget had been reduced by 18 percent the previous year (one of the largest reductions to a department). She expounded that the Oil and Gas Division had received a reduction and had not received a requested increase associated with the AKLNG project. She stated that there was tremendous stress on the department's overall budget. She could follow up with the total FY 15 and FY 16 budgets. She explained that new money was required to allow the division to progress on the project.

Representative Wilson understood that the department may not have the funds within the Division of Oil and Gas. She was not convinced that other funds could not be shifted within the department's overall budget to meet the AKLNG needs. She requested to hear from the DNR subcommittee

chair on the budgetary decisions that had been made. She remarked that the following year would bring more budget decreases.

Co-Chair Neuman stated that Representative Wilson was correct. He relayed that at the end the last legislative session there had been an unallocated \$30 million cut to the departments in order to work out a compromise. He believed DNR's portion of the cut had been about \$480,000. He wondered if the administration was just trying to backfill reductions within departments that the legislature had requested.

Mark Myers answered that DNR generated \$35.00 of General Fund revenue for every \$1.00 allocated by the legislature. He stressed that cuts to the department would have severe consequences on the revenue generation side or could result in closing a major agriculture or forestry operation. He relayed that the economy started and finished with the 160 million acres of state land. He stated the decision could be made to not manage the lands in order to maximize economic benefit for the state's citizens. He relayed that he had run many organizations and had run an organization that was eight times larger than DNR; he had individuals internally and externally review the department and the consensus was that the department was very strapped. For example, in the past ten years DNR had a General Fund budget increase of 8 percent; inflation had been 16 percent. He asked the committee to consider revenue generation and loss of revenue generation as a result of cuts versus the ability to take funds from someplace else.

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Representative Wilson remarked that Ms. Rutherford had testified that because special session was taking place the administration had chosen to make the funding request at present instead of waiting until regular session. The statement lead her to believe that the funds would not have been requested until February [2016] if special session had not taken place. She reiterated her request to hear from the House Finance Committee member who chaired the DNR budget.

Co-Chair Neuman replied that Representative Pruitt had the DNR budget.

Representative Edgmon pointed out that Ms. Rutherford had made statements that the buyout of TransCanada's portion of the project would occur if the legislature approved the transaction. He clarified that the administration had already made the decision to buyout TransCanada's portion of the project. He stated that the legislature was merely approving the funds for the transaction. He wanted the record to be clear that the legislature was not making the decision to terminate the contract with TransCanada; it was making the decision to approve the funds. He stressed that the distinction between the two was significant.

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Commissioner Myers replied that the decision was his to make as the DNR commissioner; however, he would not make the decision [to terminate the contract with TransCanada] unless the legislature allocated the funds. He stated that it was possible - albeit unlikely - that the project would continue without the buyout. He detailed that he had the ability to negotiate a contract with TransCanada and that the company may stay. He furthered that the state would not have the ability to vote positively on the work plan and budget and the project would stop if he terminated the contract early without funds. In order to avoid the situation he wanted to wait to make sure the funding had been allocated.

Co-Chair Neuman noted that the legislature had heard from TransCanada that its intention was to terminate with the state.

Representative Edgmon stated that TransCanada was exiting the project. He continued that it was technically correct to say that a formal decision was yet to be made, but it was a matter of semantics. He furthered that "we know that they are exiting the stage" and that they would not be present to vote on December 4. He believed the legislature would approve the buyout provision. He remarked that in fairness it was important to keep in mind that there was a new administration in place and a governor with some beliefs that differed dramatically from those of the previous administration. He expounded that with a new governor and team in place there were alignment issues by virtue of just organizational challenges. He continued that there would be some wrinkles that maybe over time the Walker Administration would smooth out and that some of the

challenges would be met as the project moved forward. He stated that in the meantime he had the right to uphold the [Ronald] Reagan mantra of "trust but verify." He asked why Audie Setters was listed as Alaska Gas Team general manager in the governor's September 18 press statement and as the marketing lead in the organizational chart provided by the administration. He stated that it added to the blurriness about who was really in charge. He remarked that the presentation the previous day by Mr. Butt left no doubt about who was in charge of the project. However, he heard in the news that Mr. Butt's counterpart on the state side was the governor (instead of someone in a similar position). He surmised that it was the governor who could provide the equivalent of the perspective provided by Mr. Butt. He stated that he certainly would not presume to demand that the committee hear from the governor. He did not believe they were going to receive full organizational clarity. He asked for a description of Mr. Setters' true role.

Ms. Rutherford replied that Mr. Setters had been hired by DNR as a marketing consultant. She furthered that he was still under contract with DNR as a marketing contractor and was considered a subject matter expert by the department. There had been a period in May and June when the administration chose to have Mr. Setters leading the commercial negotiations, but it had not continued for any significant length in time. She stated that Mr. Setters was the marketing contractor for DNR, but was working as part of the teams that were discussed as part of the bottom of the organizational chart. She detailed that the teams were matched by company representatives at approximately the same levels in each company. There was not any one particular head for BP, ConocoPhillips, or ExxonMobil across all commercial negotiations. There were teams that functioned for each issue and agreement that would eventually roll up into commercial agreements that were hopefully finalized. She stated that the BP teams answered up to Janet Weiss, the ConocoPhillips teams answered up to Joe Marushack, and the ExxonMobil teams answered up to Jim Flood. She stated that the project was different than and not part of the commercial negotiations. She expounded that the state's equity holder in the liquefaction - in the form of TransCanada - had been part of the commercial negotiation. She explained that Mr. Butt was not part of the commercial negotiations. She contended that the state's executive officer was equal to the positions held by Ms.

Weiss, Mr. Marushack, and Mr. Flood. She stressed that the teams that were supported by legal, commercial, and subject matter experts that answered up to the head structure, were not dissimilar to the other equity owners in the project.

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Representative Edgmon restated his question about Mr. Setters' role in the project.

Commissioner Myers answered that the governor had made some changes. He elaborated that when the governor had placed Mr. Setters in charge he had replaced Ms. Rutherford who had been serving as the state's chief negotiator and coordinator of the structure. He elaborated that as the state's chief executive, the governor had the prerogative. He noted that the governor had replaced Mr. Setters with Rigdon Boykin at a later date. He continued that as the chief executive, the governor was simply exercising his prerogative to change leadership over time.

Representative Edgmon stated he still had questions about AGDC's true authority, the role envisioned by SB 138, and the command structure that had been developed. He was not saying that it was wrong and was not trying to impugn anyone's motives, but the information had not been demonstrated to him. He saw overlapping responsibilities and policy decisions being made in different entities. He did not see the organizational clarity that he believed was necessary.

Co-Chair Neuman believed it had been the overwhelming theme of the committee meeting.

12:11:30 PM

Representative Guttenberg stated that he had been around the building for a long time and had never seen an issue generate so much conflicting outside buzz from all different parties and he was unclear about their motives. He stated that the administration had done a good job answering questions and trying to delineate its role in a shifting project. He noted that the project was changing and evolving and Mr. Butt had indicated that things in the organizational chart were changing too. He spoke about SB 138, which had passed the legislature before the new administration had come into office. He recalled that

Commissioner Myers had communicated that the state had gone from a passive to an active player. He asked how the shift had changed the state's role in the process.

Commissioner Myers replied that it was a very significant change - the state had traded security for commercial viability in terms of its role. He had been told by consultants to the prior administration that when the previous administration and legislature had approved SB 138, it had been designed to bring in approximately the same revenue as the passive role would bring (assuming an SB 21 structure [legislation passed in 2013 related to oil and gas production tax legislation]). The state became less of a sovereign and more as a commercial party to the agreement. He furthered that the shift in roles meant that the state went from a passive RIV structure. He noted that the state always had the ability to do RIK, but practically that would not happen in an LNG project because the gas would be locked up in long-term contracts. He continued that the commercial structure the state had used would not have worked for the current project. He furthered that stability had been needed from the Stranded Gas Development Act, AGIA, and other - the tax systems had all contemplated the need to fix some of the structural issues for long-term gas sales contracts and maximizing the use of capacities. He stressed that the state had to make direct investment. He discussed that the state would not normally directly invest billions of dollars into a project and would not take out loans to purchase infrastructure.

Commissioner Myers emphasized that the state would not typically take project failure risk like it was in the current project. He detailed that if the project failed the state would lose its money; it represented a significant change. In the current scenario the state would receive a project that would unlock the gas that had not been unlocked by previous structures. He reiterated that the state was taking more risk, a larger commercial role, was surrendering sovereignty in terms of severance tax for a set amount of gas, and flattening royalty rates. The state was doing numerous things to look like an oil company; however, in the end the state was not quite an oil company because it could not get a drill rig and go explore for more gas. He detailed that the state did not have its own drilling company, exploration agency, and did not drill its own leases; the state was passive; therefore, the complex commercial agreements were necessary. The upfront costs of

converting to an active investor meant the state had to create a new commercial structure, had to do a huge amount of direct investment, and had to accept a huge amount of project risk. He furthered that it had been done on one of the biggest projects in the world, with numerous partners, and with a requirement to make commitments that would last for more than two decades. He remarked that they were locking it down. He continued that it was change in the way the state had operated - the model could not be found anywhere else in North America and Alaska was blazing new territories. He remarked that other companies had state oil companies including Norway and Nigeria. He noted that it was not an easy decision, particularly for a state without a huge surplus. He explained it was the reason commercial expertise was paramount.

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Representative Guttenberg thought the state should have been more active for a long time, but he also believed it should be more passive in some areas. He reasoned that to play both sides was very difficult. He discussed that the previous day Mr. Butt had testified that it could be problematic that the DNR commissioner had not signed a confidentiality agreement. He asked if Commissioner Myers had ever felt that he had not had the information necessary to make a decision. He asked what would happen if that point arrived.

Commissioner Myers replied that he had told the governor that if that point arrived he would sign a confidentiality agreement, but that point had not yet arrived. He was comfortable with the working relationships and respective data flow. He explained that it was not necessary to have all of the details to know where the issues stood on the concepts under negotiation. He noted that getting the data back from producers contained the granularity he needed. He furthered that as a key decision maker his primary job was to run a department with very broad interests including managing 160 million acres of land, forestry, agriculture, oil, and gas. He stressed that the project was very important, but there was no way a commissioner should be the project lead. He stated that he would drill down on specific issues and relied on the team, which was the reason he wanted the very best team of people and the necessary resources. He relayed that it would be foolish to believe that he could manage all of the components on his

own. He furthered that the information flowed very effectively within the team because everyone else was under the confidentiality issues and the department had been able to work to provide the information the commissioner needed. He was comfortable with the structure and he would sign the confidentiality agreement if a point arrived where he was not comfortable.

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Representative Gara was trying to determine if there was as much disagreement on the issues under discussion as it sounded like. He had heard some concern about AGDC creating a new entity for the AKLNG project. He stressed that statute specified that there had to be one entity within AGDC for the in-state line and one entity for the large line. He asked for verification that his understanding was accurate.

Commissioner Myers replied that the entities needed to be separated, but he was unsure about the requirement related to the precise corporate structure. He stated that there were limited liability issues, but he did not know the details. He deferred to DOL for further information.

Representative Gara stated that the statute was clear that separate entities were required for the in-state and large lines.

Co-Chair Neuman indicated that there would be a review of SB 138 the following Monday.

Representative Gara remarked that the confidentiality issue had taken up a significant portion of the meeting. He asked for verification that the commissioner would sign a confidentiality agreement if there was something he needed to know. He believed the commissioner was allowed to speak with the governor about the issue even though the governor had not signed a confidentiality agreement. He asked if his understanding was accurate.

Commissioner Myers answered that the administration believed that as senior executives he and the governor really had access to all of the confidential information, similar to that of corporations; they were assuming they had full access in the current structure. He stated that because of concerns he had specified in a sponsors meeting

that he would keep the information confidential, which he would have done no matter what.

Representative Gara commented that AGDC had signed a confidentiality agreement. He spoke to whether the confidentiality agreement issues were slowing down the project. Based on testimony he surmised that the administration believed everything was on schedule. He remarked that unfortunately there was not yet a binding commitment from the three major oil companies to sell their gas. He asked if the project was on or behind schedule.

Commissioner Myers replied that the project was behind where the administration wanted to be, which was largely because some of the framework commercial agreements had not yet been fully secured. He stated that the project work was on time, but the commercial negotiations were lagging. He noted that the lag could not be attributed to any single party. He added that the next negotiations needed to be completed in time to have the ability to do a constitutional amendment. There was a framework to make everything work, but it would be aggressive.

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Representative Gara mentioned the high salary slated for the marketing position. He remarked that the committee had heard from analytica on the issue - the consultants had advised against being penny wise and pound foolish. He noted that the state was acting like a private company - it was a 25 percent owner of one of the largest projects in the world if it chose the RIK method. He asked if ExxonMobil or the other companies had a similar position on their teams.

Commissioner Myers responded that ExxonMobil had an entire marketing structure and very sophisticated teams of people - they operated worldwide and were one of the top gas marketers. He relayed that BP was very sophisticated in its gas marketing and ConocoPhillips had started in the 1960s out of Cook Inlet. He postulated that the state was a bit behind and was clearly significantly under capacity compared to the companies.

Ms. Rutherford agreed. She relayed that the department was meeting with each of the companies' marketing teams - as

established in SB 138. She affirmed that the state was lagging behind the companies.

Representative Gara remarked that the commissioner had not signed the overall confidentiality agreement and sometimes he signed an agreement to be in on a particular meeting. He asked if Commissioner Myers believed that as a consequence of not signing the overall confidentiality agreement he had missed out on any information that he needed to do his job.

Commissioner Myers replied in the negative. He relayed that he would have signed the agreement if he believed he had not received the necessary information. He felt that he had and continued to receive the necessary information through a collaborative process.

12:25:52 PM

Co-Chair Neuman referred to the \$10 million request for outside legal counsel under DOL. He asked if the outside counsel worked under the direction of the attorney general or the DNR commissioner. He asked if Commissioner Myers made legal requests.

Commissioner Myers answered that there had been good discussions between DNR and the Attorney General Richards on the issue. He detailed that the outside counsel would work for the attorney general, but at the request of DNR. The department had laid out its needed capacity and the attorney general had made some suggestions. He communicated that there was total alignment in the decision making. He stated that they were world-class LNG attorneys and had been critical to the department to date.

Ms. Rutherford further explained that the genesis of the bulk of the work provided by Greenberg Traurig LLP and Millbank, Tweed, Hadley, and McCloy was at the team level. She elaborated that the work evolved as the negotiations occurred; it was not driven externally, but from the team working on particular issues or agreements.

12:27:09 PM

Vice-Chair Saddler remarked on Commissioner Myers' testimony about when he would sign a confidentiality agreement. He stated that the committee had been told multiple times that DNR did not receive its total FY 16

budget request. He remarked that there had been budget cuts due to the deficit; part of the cuts to DNR were associated with the unallocated reduction. He asked how much FY 17 funding the department would require for marketing, the geologist, and half of Ms. Rutherford's salary.

Ms. Pitney stated that the information was in the last slide of the presentation but would have to get to that at another time. The administration was estimating between \$25 million and \$35 million of capacity, which took into account that DNR had \$8 million; therefore, it may not be entirely additional funding. In order for the state to act as a project owner, it would need the capacity across DNR, DOR, and DOL to take on the scale of the project. The final schedule included \$100 million through the FEED stage of the project, which was a three to four-year process. Additionally, there was an estimated \$100 million for AGDC. She explained that the state was essentially becoming a producer company to move its gas to market. It was a significant investment - the costs would be narrowed down by the time it submitted its FY 17 request.

Commissioner Myers added that there was a construction period. For example, he remarked on the huge number of employees involved in building the oil pipeline - the number had decreased to a much smaller operational staff. He spoke to DNR's role in the current project including the early stages of building up the commercial capacity and getting the marketing agency underway. He explained that the role would decrease down to that of a marketing agency - the department envisioned that the marketing agency would fall under a separate organization similar to the Alaska Permanent Fund Corporation board structure. He elaborated that it would be a relatively small operation if the joint venture marketing plan was utilized. At that point the consultants would no longer be required.

Co-Chair Neuman encouraged members to provide any additional questions to his office. He asked if the commissioners would be available for further questions.

Commissioner Myers replied that he would be available at least through the coming Wednesday.

Co-Chair reviewed the agenda for the following day.

HB 3001 was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

12:32:01 PM

The meeting was adjourned at 12:32 p.m.