

SENATE FINANCE COMMITTEE
THIRD SPECIAL SESSION
October 26, 2015
9:03 a.m.

9:03:07 AM

CALL TO ORDER

Co-Chair MacKinnon called the Senate Finance Committee meeting to order at 9:03 a.m.

MEMBERS PRESENT

Senator Anna MacKinnon, Co-Chair
Senator Pete Kelly, Co-Chair
Senator Peter Micciche, Vice-Chair
Senator Click Bishop
Senator Mike Dunleavy
Senator Lyman Hoffman
Senator Donny Olson

MEMBERS ABSENT

None

ALSO PRESENT

Marty Rutherford, Deputy Commissioner, Department of Natural Resources; Deepa Poduval, Director, Black and Veatch; Senator Cathy Giessel; Senator Kevin Meyer; Senator Gary Stevens; Representative Andy Josephson; Representative Geran Tarr; Senator Mia Costello; Senator John Coghill; Representative Sam Kito III; Senator Charlie Huggins; Representative Liz Vasquez.

SUMMARY

SB 3001 APPROP: LNG PROJECT and FUND/AGDC/SUPP.

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

#sb3001

SENATE 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."

[9:04:14 AM](#)

Co-Chair MacKinnon discussed the meeting agenda. She relayed that SB 3001 was an appropriation bill that would buy out Alaska's partner TransCanada and commit funds to complete pre-FEED [Front End Engineering and Design] for the Alaska Liquid Natural Gas pipeline project [AKLNG]. She asked presenters to address why the administration believed the state should buy out TransCanada.

MARTY RUTHERFORD, DEPUTY COMMISSIONER, DEPARTMENT OF NATURAL RESOURCES, introduced herself.

DEEPA PODUVAL, DIRECTOR, BLACK AND VEATCH, introduced herself. She relayed that the company had worked with the State of Alaska for the past 10 years. She detailed that Black and Veatch worked on large infrastructure projects worldwide.

Ms. Rutherford explained the items included in the day's packets. She discussed the presentation titled "TransCanada's AKLNG Participation" dated October 24, 2015 (copy on file). She explained that in June 2014, the state and TransCanada-Alaska had entered into a key agreement authorizing TransCanada to pay the upfront capital costs and hold the state's 25 percent equity share of ownership in the midstream components.

[9:07:29 AM](#)

AT EASE

[9:09:20 AM](#)

RECONVENED

Co-Chair MacKinnon reiterated that the committee was addressing a presentation from Department of Natural Resources (DNR) and Black and Veatch titled "TransCanada's AKLNG Participation."

Ms. Rutherford restated that the presentation addressed whether or not to terminate TransCanada's Precedent Agreement (PA) with the State of Alaska. She addressed slide 2, "Executive Summary":

Background:

In June 2014, the State of Alaska (SOA) and TransCanada Alaska Midstream LP (TransCanada) entered into a key agreement authorizing TransCanada to pay the upfront capital costs and hold the State's 25 percent share of ownership in the midstream components of the Alaska LNG (AKLNG) Project. These midstream components are the Gas Treatment Plant (GTP) and pipeline portions of the overall project.

The agreement, called the Precedent Agreement (PA), was based on terms of a Memorandum of Understanding (MOU) between the State and TransCanada signed in December 2013. While the Alaska Legislature was not a party to the PA, it reviewed and debated the terms of the MOU during the 2014 legislative session.

Decision at hand:

The State is now faced with a December 31, 2015 deadline to make a decision on whether to take back TransCanada's share and have direct equity participation in the AKLNG midstream. To do so would require termination of the PA.

Under the PA's terms, by December 31, 2015, the State is obligated to either enter into a Firm Transportation Services Agreement (FTSA) with TransCanada or TC will be able to terminate the PA. Alternatively, if agreeable to TransCanada, the State can negotiate to extend the date for entering into an FTSA beyond December 2015.

Recommendation

The State administration recommends termination of the TransCanada relationship by December 2015 and replacing it with the State's direct participation in the AKLNG midstream.

The State administration expects this path to allow the State to better manage the obligation the State has for AKLNG midstream costs whether or not the project proceeds, increase the overall economics of the project to the State, and allow the State to have more direct voting rights on key AKLNG issues in return for its investment.

[9:12:50 AM](#)

Ms. Rutherford highlighted slide 4: "Context for State's 2014 decision to enter into a Precedent Agreement (PA) with TransCanada (TC)":

AGIA [Alaska Gasline Inducement Act] framework:

- TransCanada was the State's licensee under AGIA
- AGIA work product could not be transferred to AKLNG until after resolution of AGIA abandonment issues (including cost of the work product)
- AGIA also contained a treble damages provision
- It was in this context that the prior Administration negotiated an MOU with TC in 2013, and the AGIA Termination Agreement in 2014, to exit AGIA, transition to AKLNG, and sign the PA with TC

Entering into the PA with TC:

- Gave the State a clean off-ramp from the TC relationship, now, which it did not have when it entered into the PA for all the reasons discussed above
- Gave the State time during pre-FEED to begin to develop its in-house capabilities in order to fully consider the option of participating directly in midstream at appropriate off-ramps
- TC's work on AGIA and APP allowed smooth transition into pre-FEED
- Entering into the PA with TC for pre-FEED also gave the State time to assess its ability to finance its share of investment in AKLNG without TC

However, there was an expectation that project enabling agreements would be defined before Dec 2015 and enable SOA to evaluate TC role going forward

9:15:18 AM

Ms. Rutherford moved to slide 5 titled "Key terms of the Precedent Agreement between State of Alaska and TransCanada":

TC Owns the State's 25 percent Entitlement to GTP plus Pipeline
Funds up front midstream cash calls
Technical lead for pipeline during pre-FEED

State to Commit to 20-25 Year Transportation Agreement with TC by Dec 2015 to Pay for Using GTP plus Pipe

SOA Ultimately pays TC for all its Costs (including a cost of capital of 7 percent)

Both SOA and TC have Milestones and Off-ramps: SOA Responsible for TC Costs, Regardless of Off-ramps

Co-Chair MacKinnon queried the value of the technical expertise TransCanada had brought to the table thus far. Ms. Rutherford replied that the presentation would address the question in detail later on.

Co-Chair MacKinnon wondered if the cost in the delay in the off-ramp had been considered. She asked if there were models showing how waiting until a later date would impact the project from a financial and technical perspective. Ms. Rutherford affirmed that the presentation would address the topics.

9:17:25 AM

Ms. Rutherford discussed slide 6, "The Precedent Agreement has agreed upon off-ramps that allows the State to terminate before December 31, 2015." She elaborated that the project was currently in the pre-FEED stage and the first of the off-ramps was the termination by the end of 2015. She detailed that at that time the state would be responsible for paying TransCanada's total development costs including internal costs and 7 percent interest. The second off-ramp would occur at the end of FEED (estimated

to by December 31, 2018), but prior to making a final investment decision (FID); the state would be responsible for paying all of TransCanada's costs, which were currently estimated at about \$490 million (including internal costs and 7 percent interest).

Co-Chair MacKinnon asked if the presentation would address a footnote related to a \$4 million credit on slide 6. Ms. Poduval explained that the \$70 million estimate incorporated a \$4 million credit for a payment the state had made to TransCanada for AGIA reimbursement.

Co-Chair MacKinnon had been concerned that the state may lose the credit in the future if it was not taken at present. She surmised that it was a credit that was owed to the State of Alaska. Ms. Poduval replied in the affirmative.

Ms. Rutherford highlighted slide 8, "The SOA is faced with the strategically important decision of whether to terminate the Precedent Agreement with TransCanada":

The State has two main options:

1. Terminate the PA by December 31, 2015

State would have to reimburse TransCanada for its costs incurred to date (plus approximately 7 percent interest) - SOA increases overall equity and voting rights to 25 percent, which equals the SOA's share of gas

2. Or, assuming TC is willing, Execute an FTSA with TransCanada by December 31, 2015

TransCanada would continue to incur costs on behalf of the SOA unless there is a termination at a later date, at which point the SOA will have to reimburse TransCanada's costs (plus approximately 7 percent interest)

[9:20:54 AM](#)

Vice-Chair Micciche referenced footnote 3 on slide 6 and asked for an additional explanation on TransCanada's internal costs. He specifically wondered what portion of the \$490 million was included in the internal costs. Ms.

Rutherford agreed to provide the information. Ms. Poduval explained that of the \$70 million pre-FEED costs, about \$50 million was associated with the AKLNG work plan and budget, \$15 million was for TransCanada's internal costs, and \$3 million was associated with the interest cost.

Vice-Chair Micciche surmised that approximately 25 percent of the total was associated with TransCanada's internal costs. Ms. Poduval stated that of the approximate \$500 million at the end of FEED, about \$100 million would be associated with TransCanada's internal cost plus interest.

Co-Chair MacKinnon requested the information in writing for dissemination to other legislators.

Senator Bishop wondered whether the costs were reasonable and how the analysis compared to other pipeline companies. Ms. Rutherford agreed to include the information as part of the written response to the committee.

[9:23:28 AM](#)

Co-Chair MacKinnon looked at slide 8, and wondered who would be in charge of Alaska's voting shares. She noted that TransCanada was currently voting on behalf of the state.

Ms. Rutherford replied that the discussion would address the issue of moving forward in the commercial negotiations on the governance. She explained that the question on who would have the state vote remained if there was a split between the Alaska Gasline Development Corporation (AGDC), which holds the liquefaction; and TransCanada, which holds the pipeline and gas treatment plant [GTP]. She questioned whether the vote would come from AGDC if it only pertained to liquefaction; whether a vote would come from TransCanada if it was specific to the pipeline or GTP; or who the vote would come from if it pertained to the entire project. She stated that the issue was confusing. She relayed that AGDC would become the holder of the state's full equity position in the project and would be responsible for voting on the state's behalf if the state chose to terminate the PA with TransCanada.

Co-Chair MacKinnon wondered if the administration had designated a party within AGDC who would be responsible for casting the state's vote. Ms. Rutherford replied that Joe

Dubler [Vice President and Chief Financial Officer, AGDC] had been identified by Daniel Fauske [President, AGDC] as the person responsible for carrying the state's vote for AKLNG.

Co-Chair MacKinnon remarked that the administration had named Rigdon Boykin as the person responsible for voting on the state's behalf at a meeting in Wasilla. She wondered if the switch to Mr. Dubler was a recent development.

Ms. Rutherford replied that Mr. Dubler would carry the state's vote with the AKLNG project. Mr. Boykin had been the lead negotiator for the commercial negotiations, which were handled primarily by the executive branch. She detailed that Mr. Boykin was currently under contract with AGDC. She elaborated that AGDC had roles in the commercial negotiations, but not throughout the entire set of commercial negotiations. For example, AGDC would not be involved in the decision on the recommendations the administration would bring to the legislature on fiscal terms and were not as involved in the upstream gas balancing and supply.

Co-Chair MacKinnon wondered how long it would take to obtain an organizational chart for the project. Ms. Rutherford stated that the department could provide an organizational chart by the end of the day. She added that the House Finance Committee had also requested an organizational chart the previous day.

Co-Chair MacKinnon noted that the Senate Resources Committee had made a request for an organizational chart six months earlier. She asked if the committee should take a break to wait for the chart, or if it should continue on.

Ms. Rutherford recommended continuing on and committed to providing an organizational chart by the end of the day.

9:27:32 AM

AT EASE

9:28:39 AM

RECONVENED

Co-Chair MacKinnon relayed that the committee had been waiting for some time to understand the organization of the management team, which had been a sticking point for the

committee. She emphasized that the committee wanted an Alaska gas pipeline, but it also wanted to understand the organization moving the project forward. She explained that the organizational chart would be foundational for the committee to decide on whether to fund the buyout or not. She asked for verification that Mr. Boykin had been hired from out of state as the lead negotiator on establishing commercial agreements for the project. She surmised that Mr. Boykin was working with a team and the administration had selected a member of team to cast the state's vote.

Ms. Rutherford explained that AGDC was responsible the infrastructure only. The agency was also responsible for supplying domestic gas, which would include some of the infrastructure associated with offtakes. She explained DNR and AGDC had a responsibility to provide the legislature with a report on domestic gas supply and offtakes. She stated that in AGDC's role as infrastructure owner of the liquefaction it had named Mr. Dubler as its management team voting representative for the AKLNG project. She detailed that Mr. Dubler and other AGDC representatives had been part of the overall gas team dealing with commercial issues. She elaborated that AGDC's role in the commercial discussion was very limited to the areas that included infrastructure decisions. She affirmed that Mr. Boykin had been leading the commercial negotiations. Additionally, there were a few representatives from AGDC, DNR, the Department of Law, and the Department of Revenue (DOR). Many of the representatives were subject matter experts, including David De Gruyter for pipelines, Steve Wright for project management and upstream issues, and Deepa Poduval for fiscal issues. The team tried to assist the lead at the negotiating table. The contract was currently held by AGDC, but Mr. Boykin's responsibilities were broader than the infrastructure piece.

Co-Chair MacKinnon believed the organizational chart would outline something the legislature could count on for a structure.

[9:31:53 AM](#)

Senator Dunleavy wondered if Mr. Boykin was replacing Mr. Fauske in terms of roles and decision making capability. He asked what role Mr. Fauske currently had. Ms. Rutherford replied that Mr. Fauske was still the CEO of AGDC and answerable to the board; whereas Mr. Boykin was currently a

contractor with AGDC working solely on the commercial aspects of the project. She relayed that Mr. Boykin had not replaced Mr. Fauske in the role of leading AGDC's efforts.

Co-Chair MacKinnon remarked that the state hired contractors from around the world in order to work to make the best decisions possible. She asked if the administration had provided the legislature an opportunity to review the PA. Ms. Rutherford replied that the department had received approval the previous day to provide a slightly redacted version of the PA, which was a confidential document between the state and TransCanada. She relayed that the committee would receive the document shortly.

Co-Chair MacKinnon asked if the legislature would sign a confidential agreement to view the document or if the document would become open. Ms. Rutherford replied that it would become a public document with a couple of slight redactions.

[9:33:49 AM](#)

Senator Olson opined that the state focused on hiring the most experienced individuals. He did not believe Mr. Dubler and Mr. Fauske had any extensive experience in dealing with megaprojects such as AKLNG. He hoped to see that Mr. Dubler did have experience, given his role in voting on behalf of the state. He asked Ms. Rutherford to comment on the issue.

Ms. Rutherford answered that she did not know what Mr. Dubler's and Mr. Fauske's resumes looked like. She believed that TransCanada was an outstanding northern pipeline company; for that reason the project chose the company as the pipeline lead on the pre-FEED stage. However, there was a large difference between holding the state's equity interest and being a lead on any particular segment of the project. She elaborated that AGDC already held the state's equity position in the liquefaction project. The administration was proposing that AGDC would also hold the state's equity position in the pipeline and GTP if TransCanada's role in the project was terminated. She furthered that who would handle the pipeline component for the AKLNG project would be decided by the project and not the state or producers. The management committee would be making recommendations for approval by the entire structure of AKLNG on who would continue to be the lead for the

remainder of pre-FEED and continuing forward; none of the decisions had yet been made. TransCanada had agreed to allow the AKLNG project to hire any of its top employees during the process of closing out pre-FEED, which was currently in its final stages. The project would then decide if it would include another third-party or one of the current companies with pipeline experience.

[9:36:45 AM](#)

Senator Olson expressed concern that there would be exposed people as AGDC took on more and more responsibility. He did not believe some of the personnel had all of the needed experience. Additionally, he recalled that in the past Mr. Boykin had remarked that he tended to get his way at the negotiating table. He stated that the forcefulness of the comment almost reminded him of Donald Trump. He asked for comment on Mr. Boykin's expertise related to getting fair representation for the state's 25 percent share of the project.

Ms. Rutherford replied that Mr. Boykin was a very experienced attorney. He did not have LNG experience, but had energy project experience. She believed the experience had primarily been in the financing aspect of projects. She noted that her comments reflected what she had heard at a September meeting. She did not have further knowledge regarding Mr. Boykin's experience.

Co-Chair MacKinnon relayed that she had made a note that the committee may want to hear from Mr. Boykin.

Senator Olson asked if there were reservations about Mr. Boykin's lack of LNG experience. He opined that LNG experience was very different than being a financier. Ms. Rutherford replied that given the complexity of the project no one had the breadth of experience to fill all of the gaps, which made it important to have a fully functional team with broad experience. She relayed that there were some vastly knowledgeable people involved. She believed that good decisions would be made if the team used the knowledge of the various participants to its advantage.

[9:39:24 AM](#)

Vice-Chair Micciche believed most of those involved understood the benefits and liabilities of buying out

TransCanada. He observed that there may be a relatively sophisticated team, but he believed there was a lack of an institutional process. He noted that the state would be making the decisions that TransCanada was currently helping with at present. He believed it was the only gap in the deal. He referred to the organizational chart and remarked that the organization had changed substantially over the months. He stressed that there should be stability in the organization. Additionally, he wanted to know that the administration understood the positions that were necessary to manage the decision making process and he wanted to see names associated with positions. He felt that there should be a set of qualifications for individuals who may fill the positions. He believed the request was reasonable. He believed the process was stalled until the information was made available. He added that he was largely in support of the deal.

Ms. Rutherford agreed to provide the information.

Senator Dunleavy agreed that the organizational chart was essential to the decision. He believed a meeting in Mat-Su made it harder to understand who was in charge of what. He remarked that alignment with the administration should lead to alignment with the legislature. He wanted to ensure that there was some concurrence within the administration on what to do. He hoped there was consensus within the administration that there was a particular course of action DNR would recommend at meetings with the legislature. Ms. Rutherford agreed.

[9:42:58 AM](#)

Ms. Rutherford addressed slide 9 titled "The administration recommends Termination of the Precedent Agreement":

Alignment: Currently, the SOA is estimated to receive 25 percent of the gas from Project; however, with TransCanada's equity participation in the midstream portion of the Project, the SOA only retains approximately 12.5 percent equity in the project

Ms. Rutherford elaborated that with the termination of the PA, the state would have an equal share of the gas and project infrastructure. She continued to address slide 9:

Voting Rights: Terminating the agreement and increasing the State's voting rights would allow the State to have a more direct say in the decision making process of the project

Ms. Rutherford expounded that a termination of the PA would allow the state to have a much more clear say in the project decision making process during the completion of pre-FEED and moving into the FEED stage. She remarked that having a portion of the project held by TransCanada and another portion held by AGDC made things complicated. She finished addressing slide 9:

Economic Benefit: The SOA could realize up to \$400 million of additional annual net cash flows from the Project, based on DOR's expectations of State being able to finance cheaper than TC by financing the midstream portion of the Project directly

Ms. Rutherford added that DOR finance staff would speak to the economic benefits at a later time.

Senator Bishop referred to voting rights on slide 9. He wanted to ensure that votes would be made in the state's best economic interest, and not on politics.

[9:45:47 AM](#)

Senator Dunleavy believed the first two items on slide 9 were clear, but asked for verification that the third point was a guesstimate. Ms. Rutherford replied that the estimate was based on the best analysis the state's outside financial advisors (Lazard, FirstSouthwest, and Greengate) could provide.

Senator Dunleavy observed that "up to" \$400 million was the best case scenario. Ms. Rutherford agreed. Senator Dunleavy surmised that the figure could be anywhere from zero to \$400 million. Ms. Rutherford agreed that the figure could be as low as zero. Senator Dunleavy asked for verification that the number represented a net figure. Ms. Rutherford confirmed that the \$400 million was a net figure.

Senator Olson wondered what would happen if the gas market crashed. He asked if there was a chance the state would lose money. Ms. Rutherford replied that there was a chance the state could go negative once it took an equity position

in a complex LNG project, which was market and cost-driven. She detailed that the long-term contracts the state would need to negotiate to underpin the project financing would be indexed. Often times financing was indexed to oil prices, which were currently very low. She agreed that inherently the state could go negative by taking an equity position in the project, which was a very different situation than the one at present with royalties and gas and no equity positions because production tax and royalties could go to zero, but could not go negative. However, once the elements were turned into gas ownership positions, it was possible to go negative, hopefully only for short periods of time. She relayed that it was part of the analysis the administration would bring to the legislature as part of the final commercial proposal.

[9:48:19 AM](#)

Senator Olson clarified that he was not asking whether the state would lose or win; he understood that the issue was market driven. He wondered if a market upset would change the state's financial liability under a scenario that included partnership with TransCanada versus a scenario without TransCanada. Ms. Rutherford replied in the negative. She added that the issue would be discussed further.

Vice-Chair Micciche referred to voting rights on slide 9. He queried the details of the consultation currently taking place between the state and TransCanada before a vote occurred. He wondered what kind of a quantifiable voice the state currently had when voting occurred. Ms. Poduval replied that the presentation would address the issue in more detail later on.

Vice-Chair Micciche surmised that the \$400 million on slide 9 was related to the difference in the cost of capital. Ms. Rutherford replied in the affirmative.

Vice-Chair Micciche remarked that there were only three times in the state's history where it had paid an interest rate higher than the one in the deal with TransCanada. He asked for verification that the \$400 million was around just over 3 percent for the cost of capital. Ms. Poduval agreed. She noted that it was 3.5 percent.

Co-Chair MacKinnon asked if DNR had made a determination that the state would take gas as tax. Ms. Rutherford replied that the determination had not yet been made, but DNR was following SB 138 [legislation passed in 2014 related to a gas pipeline, AGDC, and oil and gas production tax]. The commercial agreements were a necessary element, which had been recognized by the legislature in its Heads of Agreement (HOA) discussed in 2013. An informed decision could be made once the commercial agreements were in place that would affect things like the disposal of carbon dioxide, the upstream cost allowance on the various fields, what rate would flatten the Point Thomson net profit share leases, supply agreements for receiving gas, and surety the gas could be delivered to the state's buyers.

Senator Bishop addressed economic benefit and noted the importance of ensuring the state maintained its credit rating. He wondered if the state would run up against a limit on future borrowing if it bonded for the full amount on the project. Ms. Poduval answered that the finance team was prepared to provide detailed information.

[9:52:08 AM](#)

Senator Dunleavy queried the goal of the pipeline from the administration's perspective. He wondered if the goal was to maximize revenue for the state or to provide the lowest cost energy for Alaskan's. He asked which option was the priority.

Ms. Rutherford replied that DNR's role and responsibility was to maximize the revenue value to the state. The project was a transportation system and the intent was to keep those costs to a minimum in order to maximize the upstream values. She stated that the legislature would get to make a decision on whether it wanted to subsidize particular energy projects in the state. She furthered that AGDC's role was to provide gas for domestic use. She believed the agency was anxious to speak to the legislature about how domestic gas could provide a way to lower energy costs to local communities; however, it was not something DNR was allowed to do. She referred to a legal decision that it was DNR's constitutional responsibility to maximize the upstream values for the Permanent Fund and General Fund.

Co-Chair MacKinnon queried if Senator Dunleavy was interested in hearing from the Alaska Energy Authority

(AEA), which had been charged with the responsibility of looking at instate gas under SB 138.

Senator Dunleavy replied in the affirmative. He remarked that his question pertained to alignment. He believed that if the state's goal was to maximize revenue the pipeline should be as big as possible with as few offtakes as possible and gas would be taken directly from the slope to a ship in a route as direct as possible in order to lower costs. Alternatively, some people believed the purpose of the gasline was to lower the cost of energy for Alaskans, which had been the reason for discussions on a 36-inch pipeline with offtakes and the impetus for HB 4 [legislation passed in 2013 related to AGDC and the Regulatory Commission of Alaska]; however, these items increased the project cost. He wanted to better understand the goal of the state and reasoned that various departments may have differing views on the subject.

Ms. Rutherford replied that DNR's responsibilities were constitutionally based as directed by the courts. She relayed that the situation was very similar to what occurred with oil under Trans-Alaska Pipeline System (TAPS); values were maximized and the legislature determined how those revenues were utilized for Power Cost Equalization or other methods to provide lower energy costs to the state's citizens and communities. There would be opportunities to include offtakes to try to keep the cost of domestic supplies as low as possible, but DNR's responsibility to maximize the resource value was fairly clear. She concluded that it was up to the legislature to decide how to use the revenues and how to use revenues to lower costs. For example, the legislature could look at subsidizing some of the offtake kits that AGDC was looking at or at other methods.

Co-Chair MacKinnon recognized Senator Charlie Huggins and Representative Liz Vasquez in the committee room.

[9:57:43 AM](#)

Senator Olson believed that one of the main goals of a 48-inch line was to allow other gas fields to tap into the line. Ms. Rutherford agreed. She furthered that the state was working to ensure that there were adequate offtakes and intakes along the entire route. She provided the Nenana Basin as an example, where there would be the opportunity

to put additional gas into the pipe. Additionally, the goal was to ensure that the pipeline was expandable to the maximum degree possible at the lowest possible cost in order for third-party, new found gas to access the line. She explained that the situation was very different than subsidizing the offtake value of the gas. She confirmed that the state wanted to encourage new exploration, new found gas, and to facilitate gas developed somewhere along the route of the pipeline such as the Nenana Basin. She elaborated that the state was very involved in commercial discussions about trying to ensure expansion and third-party access provisions that made good sense for the state as a sovereign.

Senator Olson queried the difference between the 42-inch and the 48-inch pipeline options. He wondered if each option could accept extra capacity or if one would require more compressors.

Ms. Rutherford replied that the state believed that the value of increasing the pipe size from 42 inches to 48 inches was in the state's best interest. She explained that the larger pipe could be expanded much more cheaply, that it would not be as "pipe constrained" from bringing in third-party gas somewhere along the routes, and would require less compressor stations for the initial and additional throughput. She stressed that with a larger pipe the capital costs could probably be repaid within 12 years, because fewer fuel and compressor stations would be required. However, the project had only developed the 42-inch pipe to the current pre-FEED level. Therefore, as part of the state's efforts and in response to SB 138 requirements that asked for the consideration of a 48-inch pipe, the state had asked the project to bring a 48-inch analysis up to the same stage of pre-FEED as the 42-inch pipe. The analysis would enable the legislature to make comparable decision on whether the state's assumptions on a 48-inch pipe were correct and what the costs would be for capital investment and operations.

Co-Chair MacKinnon stressed that SB 138 specifically asked DNR (not the project) to develop the criteria. She wondered if there was information the legislature could be privy to from the state's perspective to evaluate on its assertion and to ask the state's partners for the expansion. She asked if a legislative resource committee should have a meeting on a 42-inch versus a 48-inch pipe. She reasoned

that it seemed to be a resource issue related to maximizing the resource and a criteria that had been asked for of DNR by SB 138.

Ms. Rutherford agreed to provide that information.

[10:02:30 AM](#)

Senator Dunleavy believed that Ms. Rutherford had indicated that going from a 42-inch pipe to a 48-inch pipe would be advantageous to Alaska. He wondered if there were any pipe sizes exceeding 48 inches. He reasoned that the state would increase the pipe size even more if it believed a larger pipe would be more beneficial.

Ms. Rutherford replied that generally, 42-inch and 48-inch pipes were the most traditional and pipeline companies had the most experience with those sizes. She stated that a 44-inch pipe had been under consideration but the state had heard that all of the replacement parts and compressors would have to be newly created, which would have greatly increased the cost. She believed that a 48-inch pipe was the most traditional and largest pipe available.

Co-Chair MacKinnon asked if DNR would share with the resources committee how the weight on the pipe would physically handle the selected corridor. She had heard that the weight on the pipe caused some technical difficulties for the project that would increase costs exponentially.

Ms. Rutherford agreed that the weight would be greater and there would be an associated reduction in the number of pipes that could be trucked (from 4 down to 3). She confirmed that there would be an additional cost, which would be part of the full analysis the project had agreed to undertake on the difference between a 42-inch and 48-inch pipeline. She explained that DNR had made some assumptions that it would discuss with the legislature.

[10:05:06 AM](#)

AT EASE

[10:18:20 AM](#)

RECONVENED

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Senator Dunleavy wondered whether it would be a reason to keep TransCanada for its expertise if the state was considering a 48-inch pipe. Alternatively, he wondered if the state could locate the expertise on its own. Ms. Rutherford replied that the administration believed the project could replace the capacity that TransCanada brought to the project. She detailed that the project could utilize the expertise of the producers or could bring in another third-party into the project (not into the state's equity position). She explained that the state was replacing TransCanada as its agent, not as the project piece. She elaborated that because of TransCanada's pipeline expertise the project had elected to put the company in charge of the pipeline for pre-FEED.

Senator Hoffman wondered if the project would automatically go from a 42-inch pipe to a 48-inch pipe if it was determined that the larger pipe was more economically beneficial. He asked about the process and timeline associated with making the decision.

Ms. Rutherford replied that given that the project had agreed to bring the analysis of a 48-inch pipe up to the same level of information as the 42-inch pipe, the analysis would be completed at the same time as the remainder of the pre-FEED product completion. She relayed that there had been some slippage in the timing; the project had hoped to have all of the pre-FEED products completed by the first part of 2016. However, the project had identified product areas that would require additional effort. She noted that the topic would be addressed further during the budget discussion. Assuming pre-FEED would be completed by the end of 2016, the 48-inch analysis would be done at the same time. She believed that if the 48-inch pipe was shown to be more economic there would be some impetus by the project to agree to the change. She stressed that all parties would have to agree to make the change as part of the project agreement. She added that hopefully the state would have the ability to influence the decision, given the importance of some of the values it brought to the project (such as fiscal certainty).

[10:23:41 AM](#)

Senator Hoffman surmised that each member had veto power in determining the size of the pipe. Ms. Rutherford replied that she was getting into some confidential areas.

Co-Chair MacKinnon remarked that the size of the pipe may be a conversation more appropriate for the resources committee. She added that certainly the committee wanted to understand the associated costs from a financial perspective.

Co-Chair Kelly remarked on the importance of keeping in mind that the purpose of the special session was for the TC buyout. He noted that the session had initially included discussion on a tax reserves tax. He remarked that he had voted to include TransCanada in the project two years earlier based on testimony by the department. He wanted to understand why Black and Veatch believed the state should buy out TransCanada from the project. He opined that two years earlier many legislators put significant value on the consultant's reasoning as to why TransCanada should be included in the project.

Ms. Poduval appreciated the remarks.

Senator Dunleavy asked for verification that Ms. Rutherford had been part of the AGIA process. Ms. Rutherford responded in the affirmative. Senator Dunleavy asked for confirmation that TransCanada had been brought into a state conversation at that time. Ms. Rutherford replied in the affirmative.

Co-Chair MacKinnon encouraged the presenters to identify themselves.

[10:26:29 AM](#)

Ms. Poduval responded to an earlier question from Co-Chair Kelly about what had changed in the time since she had presented on why bringing TransCanada into the AKLNG project was a good idea. She spoke to the importance of the background of when the decision was made, which was at the time of the AGIA termination. She elaborated that the work product TransCanada had access had been instrumental for the state's transition to the AKLNG process and the AGIA treble damages provision had created some concerns. She furthered that it had also been the very beginning of the state's participation as an equity investor in the project. She explained that there were various things that had not yet been understood at the time of the decision. For example, whether the state would be able to finance its full share of the project, which had been a very important

concern at the time. She relayed that the pre-FEED time had given the state the opportunity to study the question and to get more comfortable with what it could and could not do. The finance team had determined that terminating the TransCanada relationship would bring more value for the state. Additionally, the pre-FEED period with TransCanada was always recognized as a sort of courtship. By design, several off-ramps had been built into the PA that had enabled the current discussion. She stated that the legislature had made the current off-ramp a clean and advantageous option for the state. She relayed that the presentation would address the reasoning for terminating the agreement at present versus at a later date. She saw the option as a part of the plan and not a deviation; the PA included the decision points. She stated that based on the current information, the recommendation was for the state to continue forward on its own.

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Co-Chair Kelly believed that government tended to not be efficient. He stated that there had been a private sector personality embedded in the project through TransCanada. He wondered how private sector thinking would be institutionalized in the project going forward without TransCanada. He did not need an answer to the question at present but he believed the issue was important.

Vice-Chair Micciche opined that the legislature should be very proud of the deal made in SB 138. He stated that for roughly the price of 7 percent of the work effort put forward by TransCanada, SB 138 brought TransCanada's work product to state ownership and relieved the state from the \$500 million liability and potential treble damages. He believed it had been a bargain. He stated that it had been clearly the right thing to do in order to relieve the state from the liability and potential liability associated with AGIA. He queried how to replace the value. He did not want the state to take all of the advantages of an efficient partnership and turn its 25 percent of the project into something inefficient. He wondered whether the state had realized the full value of the relief of liability and whether it was or was not time to go on independently. He disputed the idea that the state was moving outside of the SB 138 framework. He believed it was quite clear that it had been the correct decision to involve TransCanada in the

project thus far and that perhaps the full value of the agreement had been reached.

Co-Chair MacKinnon asked for verification that key TransCanada employees would be kept through pre-FEED in order to maintain the technical expertise needed to finish out the current stage of the project. Ms. Rutherford replied in the affirmative.

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Co-Chair MacKinnon queried the number of individuals that would be retained. Ms. Rutherford replied that there were approximately 15 TransCanada employees involved in the AKLNG project. She did not know how many the project would want to retain to finish off the pre-FEED stage. She believed it was probably a subset of the 15 employees.

Co-Chair MacKinnon communicated that the committee was interested in continuity and seeing an organizational chart. She wanted to know how many individuals the project would retain and if the state would need to go out to contract, which would be a financial implication and loss of continuity depending on how the team leadership made recommendations. Ms. Rutherford answered that she would try to get the information for the committee. She qualified that the determination would be made by the project. She detailed that the state would have people involved in the discussion. Additionally, AGDC and the project would discuss what capacities could be provided in-house and deltas that needed to be provided externally such as from TransCanada.

Co-Chair MacKinnon asked if Mr. Dubler would be voting on the state's behalf. Ms. Rutherford replied in the affirmative. She elaborated that the project management team (comprised of each party's representative) made the ultimate decisions on the best interests of the project. TransCanada was the project lead for pre-FEED on the pipeline because it was a good pipeline company and not intrinsically because it was the state's agent. She continued that TC may have become the lead if it was retained as the state's agent and may or may not have been the lead going into FEED, construction, and operations. She discussed that the project was primarily a private sector project (the state would have a 25 percent equity stake) and the structure of governance would be decided by the

project. The state would have one vote or possibly a split vote depending upon TransCanada's continuation as the state's agent.

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Senator Dunleavy asked for verification that 25 percent was the upper limit of the state's risk. He referred to talk about state ownership of 51 percent. Ms. Rutherford replied in the affirmative, assuming that no other parties withdrew from the project. She detailed that currently there were no withdrawal agreements in place, so she could not describe what one would look like. One of the fears the administration had discussed was that it would not want to see the project halted by the withdrawal of one party; it wanted some withdrawal agreements in place that would provide the opportunity for someone committed to the project to continue the project forward.

Senator Dunleavy surmised that the door remained open for the state to assume a greater involvement in the project [if a party withdrew]. Ms. Rutherford replied that increased ownership was not part of the state's plan. She believed the plan would be to make provision for the project to continue forward and to make room for another party to fill the vacancy. For example, if one producer withdrew and wanted to sell its gas, another party could step into the equity position. She stressed that there had been no discussion specifying that it had to be the State of Alaska. The state wanted the project to move forward and did not want to see a delay in the event that a party decided to withdraw its participation.

Senator Dunleavy wondered if the presenters were convinced that the benefits [of the termination of the agreement with TransCanada] outweighed the risks for the state. Ms. Poduval replied that the benefits outweighed the risks. She would elaborate during her portion of the presentation. Ms. Rutherford stated that she also believed the buyout was in the state's best interest. She stressed that the additional value (between zero and \$400 million per year) was a good cushion, should the price of oil continue to decline.

Senator Bishop asked if TransCanada provided value in the HOA in ensuring expansion principles and offtake options for the state. Ms. Poduval replied that TransCanada helped in the commercial negotiations related to expansion issues

and access for third parties. The negotiations had been led by the state's gas team supported by legal and subject matter experts that brought significant regulatory and pipeline expansion experience.

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Senator Bishop wanted to feel comfortable that he was making the right decision. He remarked that the legislature had followed Black and Veatch recommendations two years earlier and he did not want to change decisions every two or three years. He believed continuity was important. He observed that there were some milestones that were supposedly needed to have been met in order to make the decision at hand, which had not been met. He specified the firm transportation services agreement (FTSA) and the RIK [royalty in kind] decision as examples. He believed it was difficult to make a decision and emphasized that he would need to be convinced going forward.

Senator Dunleavy wondered if there was a benefit to waiting to exit the deal with TransCanada until a later off-ramp. Ms. Poduval replied that Black and Veatch believed it was appropriate to take the current off-ramp. One reason was due to the back-in rights, which the legislature had built into the PA that allowed the state to take the option at the current point in time.

Ms. Poduval discussed slide 11 titled "State does not have direct voting rights for GTP or pipeline." The slide showed the project structure as currently envisioned. She pointed out that each of the three producer parties (ExxonMobil, BP, and ConocoPhillips) have a certain share of gas (shown in boxes at the top of the slide) and their equity ownership in the project was set up to be equal to their gas share. She explained that the producers had a straight path through the infrastructure to get their gas to market. Additionally, the producers' voting rights were aligned with their share of gas. The state was expected to have about 25 percent of the gas from the project (shown on the right side of the slide) and its 25 percent equity was only in the LNG plant. Currently the state's 25 percent share in the GTP and pipeline was held by TransCanada. She explained that the state effectively held 12.5 percent equity in the project (which also translated into voting rights) compared to its 25 percent of the gas because the GTP and pipeline accounted for roughly half of the project's size.

[10:45:21 AM](#)

Ms. Poduval highlighted slide 12: "Alignment through direct participation will facilitate State influence equivalent to its investment." She explained that the state effectively shared voting rights with TransCanada and TransCanada's decisions were driven by maximizing its shareholder value. She detailed that the TransCanada's decisions were sometimes aligned with the state's interests, but not always. She elaborated that TransCanada's perspective was that of a pipeline company and the state's perspective was that of a resource owner with the goal of maximizing the resource value for all Alaskans. Fundamentally, the two perspectives created differences in opinion on what constituted the best decision. She relayed that pre-FEED experience had shown that TransCanada was not simply an agent of the state. The PA specified that the state could direct TransCanada's vote related to the work plan and budget only; the company could vote independently of the state in all other areas. She expounded that TransCanada was essentially another commercial party the state had to negotiate with on any given issue and that it hoped to achieve alignment with.

Ms. Poduval remarked that it had become clear that it may be much better for the state to have a direct seat at the table where it could control its own vote. She relayed that the current structure also created complexity. For example, she questioned whether TransCanada would vote on all issues pertaining to the GTP and pipeline, while AGDC would vote on issues pertaining to the LNG plant. She asked how the vote would get made when an issue pertained to the entire project. Additionally, she questioned who would represent and speak for the state in the AKLNG project. She explained that all of the implementation issues were lessons the state had learned during the pre-FEED process. She elaborated that there were various upcoming key decisions where the state's interest would be better protected with a seat directly at the table. She discussed the importance of decisions related to byproduct handling, which would be influenced by whomever was watching over the GTP on behalf of the state.

Ms. Poduval communicated that due to the high percentage of carbon dioxide that would be extracted from the Prudhoe Bay gas, the plan was to reinject the carbon dioxide in the

Prudhoe Bay unit. She explained that the negotiation and the related costs could happen in one of two ways: there could be bilateral negotiations between each of the parties liable for the byproduct with the Prudhoe Bay unit owners; or the negotiation could occur on behalf of the AKLNG project and it could be added as a service provided by the GTP. She relayed that there were billions of dollars at stake in the decision. For example, from TransCanada's perspective it would be a pass-through cost that would ultimately be paid for with the state's tariffs related to the GTP. However, for the state, it would be actual money leaving the state's pockets. Another challenge had been access to information. She explained that there was significant information passing through the AKLNG project and the state's ability to obtain the quality and quantity of information it desired in a timely manner was diluted given that it had to pass through TransCanada.

[10:50:14 AM](#)

Vice-Chair Micciche remarked that the state had handicapped itself on access to information due to its unwillingness to require AGDC professionals to sign confidentiality agreements. He wondered if the state would acknowledge that it was unable to have conversations with key vendors (that had no commercial interest in the project) without signing confidentiality agreements. He wondered if the state would accept and acknowledge that transparency of a project and basic commercial professionalism were two different things. He believed the state could be as transparent as possible yet privy to key information.

Ms. Rutherford replied that the AGDC staff involved in AKLNG had signed the AKLNG confidentiality agreement; however, the AGDC board had not. She believed the administration had worked to find the balance between the necessary commercial confidential information and a transparent representative government. She understood that the balance was not easy to find and could be very specific to the particulars of the agreement or documents at hand. She reiterated that AGDC's personnel working on AKLNG had signed the confidentiality agreement, with the exception of staff who had been assigned to the instate Alaska Stand Alone Pipeline project.

Vice-Chair Micciche disagreed with the summation by Ms. Rutherford. He wanted to make certain that the state was

not creating its own handicap related to access of information. He asked if the partnership voting process required a simple majority vote. Ms. Poduval replied that the information was confidential because it was part of the governance terms still under negotiation.

Vice-Chair Micciche reasoned that there was only one company (ExxonMobil) needing to bring in another entity if the voting requirement was a simple majority, while every other party had to bring in two votes. He wondered if that was the focus on future commercial agreements. Ms. Rutherford replied that voting prerogatives for the state were critically important as it negotiated the governance terms of the project. She remarked that a simple majority was one thing, but if all parties were required to agree the situation would be more difficult on many votes. She relayed that the state was working to maximize its position on the issue.

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Co-Chair MacKinnon wondered if the negotiations were different (a consensus versus a majority vote) in pre-FEED versus the construction stage. Ms. Poduval replied in the affirmative. She detailed that the negotiations were also likely to be different based on different issues; certain issues would require unanimous votes, others would require a simple majority, and others would need a super majority.

Co-Chair MacKinnon noted that in past presentations looking at AGIA and SB 138 there had been a Memorandum of Understanding and agreements with partners. She asked for verification that it was public information that the state was working on consensus that all parties had off-ramps until the FEED decision was reached. Ms. Poduval replied in the affirmative.

Co-Chair MacKinnon asked for confirmation that the new terms currently under negotiations would apply once the final investment decision (FID) was reached or sooner if the partners agreed to a structure. Ms. Poduval stated that the current structure would take the project through pre-FEED. Anything past pre-FEED (FEED, construction, and operation) was yet to be developed.

Co-Chair MacKinnon asked when the voting decision would be finalized. Ms. Rutherford replied that once the joint

venture agreement on the pre-FEED was complete, everything subsequent to that would be decided. She detailed that it was not yet clear whether there would be a joint venture agreement that went all the way to governance on a project or to FEED and FID. She stated that there could be multiple agreements.

Co-Chair MacKinnon queried a specific calendar date for the agreements (summer or winter 2016). Ms. Poduval replied that there were two specific points in time when layers of clarity would be added: 1) before the parties would make a FEED decision (pre-FEED was expected to end mid-2017); 2) remaining details would occur prior to FID.

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Vice-Chair Micciche passed around a document prepared by DNR and DOR on April 3, 2014 (copy not on file). He asked the department to update the document with current information on what had been executed, what had yet to be executed, dates that would be adjusted, a list of all services and contracts including dollar amounts, and a brief summary of the work product. Ms. Rutherford agreed.

Ms. Poduval looked at slide 14 titled "Criteria for evaluating economic impact of TC Participation on SOA." There were three criteria to evaluate the economic benefit for the state. The first was cash flows, which included upfront cash calls the state would be obligated to make and the operational cash flows the state would achieve once the project was completed. The second and third criteria were related to net present value (NPV) and risk.

Ms. Poduval discussed slide 15 titled "What are the State's upfront cash calls required in the project for the State if the agreement is terminated?" She detailed that the immediate cash call obligations came from the TransCanada termination amount (the estimated \$70 million the state would pay back to TransCanada for its development and internal costs plus interest) and the cost for AGDC to continue and complete the pre-FEED work in the AKLNG midstream (approximately \$60 million). She added that as the state went through pre-FEED and construction it would pick up an additional 12.5 percent of the project of associated costs.

Senator Bishop pointed to footnote 3 on slide 15 and asked the "higher of" was the 20 percent estimate for cost overrun. Ms. Poduval replied in the affirmative.

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Co-Chair MacKinnon wondered if the administration had done an evaluation of the cash calls, given the state's current fiscal information. Ms. Poduval replied in the affirmative. She relayed that the finance team would share the information with the committee.

Ms. Poduval highlighted slide 16, which included an illustration demonstrating the fundamental tradeoff between higher upfront investment and higher operational cash flows or lower upfront investment with lower operational cash flows. She noted that the tradeoff had also been discussed during the legislative session of 2014 when Black and Veatch had recommended the TransCanada decision. She explained that the fundamental question had not changed.

Ms. Poduval discussed slide 17 and detailed that the additional upfront cash call the state would have without TC was between \$6.9 billion and \$8.3 billion. The \$6.9 billion figure related to the base capital cost estimate of approximately \$45 billion; whereas the \$8.3 billion was based on a 20 percent capital overrun scenario, which would increase project costs up to \$55 billion.

Vice-Chair Micciche did not believe most people agreed that the state was on the hook for the cost either way. He addressed that the conversation was about the difference in the cost of capital, which was the benefit of the deal under discussion. He asked to hear Ms. Poduval's take on the issue.

Ms. Poduval replied with slide 24, "Per prior agreements, SOA is always obligated to repay TC's costs." She agreed with Vice-Chair Micciche's statement. She detailed that the state was always obligated to repay TransCanada's cost; therefore, the question was not whether the state should or should not pay TransCanada, but whether the state should pay TransCanada a lower amount at present or a higher amount later. She looked at the development side of the project (through pre-FEED, FEED, and construction) and relayed that the state would be obligated to pay back TransCanada's costs plus 7 percent interest under a project

failure scenario; all of the development risks were borne by the state in that relationship. She explained that under a successful project scenario the state was obligated to pay back all of TransCanada's costs plus 7 percent interest in the form of tariffs.

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Co-Chair MacKinnon pointed to slide 24 and reasoned that the state could have chosen to exercise an off-ramp in a different way by buying back 40 percent, which had originally been part of the deal. Under the scenario the state would have maintained a risk level and opportunity equal to approximately 12.5 percent. She wondered what kind of comparative analysis the state had done between the two choices. Ms. Poduval agreed. She elaborated that the state had an equity option with TransCanada to purchase a 40 percent stake in the TransCanada entity participating in the AKLNG project. There was an associated analysis that was part of the Black and Veatch package pertaining to TransCanada. She stated that it was effectively "splitting the baby." She concluded that the decision appeared clear in terms of whether to lose or keep TransCanada as part of the project and she believed the finance team's information would help the legislature understand it better. She relayed that the option to buy back 40 percent did not make as much sense, given that there would be voting rights issues and lost value to the state through the 7 percent interest rate.

Co-Chair MacKinnon stressed that there were some Alaskans that believed the government had no business owning any portion of the pipeline.

Co-Chair MacKinnon looked at slide 17, and wondered if the upfront costs included cash calls for construction or only for the pipe itself. Ms. Poduval replied that the upfront cost shown was primarily for project construction; the figures on slide 17 represented the state's 25 percent share in the GTP and pipeline.

Co-Chair MacKinnon remarked that the analysis (on slide 17) represented the best case scenario and the first numbers the state had received at \$45 billion. She noted that the discussion had always been about a case ranging from \$45 billion to \$65 billion. She thought a 20 percent cost overrun seemed to be probable and possibly highly probable.

She wondered if the slide was a low-ball figure. She noted that the project cost estimate had increased and the state had been asked for additional money. She wondered why the slide used only a 20 percent capital cost overrun and the low base of \$45 billion. She asked if it was possible to see a range between the \$45 billion and the \$65 billion.

Ms. Poduval replied that the \$45 billion to \$65 billion range included the investment that was needed in the Point Thomson unit. She explained that the range reflected how the producers were thinking about their entire investment in the project. The cost estimate for the GTP, pipe, and LNG was closer to \$40 billion and \$55 billion. She clarified that \$45 billion was the mid-estimate (and not the low estimate) used on slide 17. The \$54 billion on slide 17 corresponded to the \$65 billion overall project range. She summarized that the slide showed a mid to high range.

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Co-Chair Kelly believed that the project cost had been arrived at during a time of "estimation madness." He recalled working for the University of Alaska at the time and relayed that the cost of large maintenance projects and other had kept increasing due to high petroleum costs. He wondered if there was hope that there were a lot of contingencies built into the estimate. Ms. Poduval replied that there had been a very inflationary environment (especially for LNG projects), which had caused various projects to exceed their capital cost estimates. Additionally, the cost for personnel and materials had been very high. She remarked that there had been a slowdown in the market and the availability of some scarce resources was expected to increase. She believed there was a likelihood that the project could benefit from more rationalization of the costs. She stressed that the estimates were extremely preliminary; it was necessary to get through pre-FEED and a large portion of the FEED stage in order to really scope the project.

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Senator Bishop remarked on the percentage of capital cost overrun. He explained that the committee had requested a slide during the debate on SB 138 (two years earlier). He recalled requesting a list of the top 20 LNG projects worldwide in order to show Alaskans the potential of cost overrun, which ranged from 20 to 45 percent.

Co-Chair MacKinnon asked if the cost overrun range mentioned by Senator Bishop was a risk. She wondered if it was beneficial for equity owners to take a 25 to 30-year look at a project and recovering the costs over a much longer period of time.

Ms. Poduval replied in the affirmative. She agreed that LNG projects were capital intensive upfront and acted as "cash cows" over a very long period of time, which was how investors earned back their significant upfront investment.

Co-Chair MacKinnon noted that she did not mean to diminish Senator Bishop's comments. She elaborated that the committee was very cognizant of huge cost overruns. She wanted to confirm that the \$45 billion base capital cost included the GTP on the North Slope, the pipeline from the North Slope to tidewater (Nikiski), and the LNG plant in the Nikiski area.

Ms. Poduval replied in the affirmative.

Co-Chair MacKinnon referenced the \$65 billion and concluded that the portion related to Point Thomson and the state's partners was \$20 billion. Ms. Poduval responded that there was no fixed Point Thomson number to add to the low, mid, and high cost scenarios (the number varied). For example, the Point Thomson figure could range from \$5 billion to \$10 billion (added to the low, mid, and high numbers in order to capture the \$45 billion to \$65 billion range).

Ms. Rutherford furthered that an incremental inflation was added to the base, which was how one got from the \$45 billion up to the potential \$65 billion. She explained that each had a spread that went from a base price to an inflated price; the figures were then added together to obtain the \$45 billion to \$65 billion.

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Co-Chair MacKinnon asked if the Point Thomson development would be part of the project and all project owners would share. Alternatively, she asked if a portion of the incremental cost (referred to in the \$45 billion to \$65 billion span) was held at a greater degree by the lease owner at Point Thomson. Ms. Poduval responded that the Point Thomson costs would be borne by the owner of the leases in Point Thomson. She explained that the figures discussed included the project "kit" [GTP, pipe, and LNG] and the anticipated upstream costs.

Ms. Poduval highlighted slide 18, "SOA's annual upfront cash calls in the AKLNG project are expected to nearly double without TC." For example, at the peak of construction, the state's cash call obligation would have been about \$1.5 billion with TransCanada and \$2.5 billion without TransCanada. She explained that pre-FEED and FEED were typically equity financed (each of the project participants provided direct funding); however, the bulk of the funds associated with the project would be spent at FID. She elaborated that 1 percent of the total project costs were spent during pre-FEED, 5 percent of the project costs were spent during FEED, and 95 percent of the funds were spent during construction. She furthered that before a significant portion of the funds were spent on the project, the boards of all participants took a final investment decision. She noted that the legislature would act as the state's board at that time.

Ms. Poduval explained that several things had to line up to get to FID. First, FEED estimates including detailed engineering and cost estimates would be completed, which provided significant clarity on the project from a technical and cost perspective. Second, firm long-term (over a 20 to 25-year period) commitments from buyers and an associated price structure would be required. Third, the financing for the project had to come together. She detailed that each of the parties would choose its optimal way to finance the project and the state would have lined up the debt it needed for financing. She elaborated that determining how to come up with the cost would occur on an annual basis; the financing plan had to be made before the state took FID in the project and before a commitment was made to spending 95 percent of the costs.

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Ms. Poduval addressed slide 19, "Once operational, SOA is expected to receive annual cash flows of up to \$400 million higher without TC." The analysis on slide 19 illustrated that terminating TransCanada's participation could increase the state's revenues by up to \$400 million per year. She noted that the bulk of that value would come from the expected lower cost of debt the state would incur (as opposed to the 7 percent interest on TransCanada's cost of capital). The state would also save some money because it was not a taxable entity like TransCanada. She elaborated that TransCanada would pass its tax obligation on to the state in any tariff the state paid.

Co-Chair MacKinnon remarked that the administration currently had a very good advocate representing financing. Additionally, the legislature's advisor analytica had conducted a review and analysis of the information currently under discussion. She furthered that analytica asked whether the administration's analysis had considered the implication to local municipalities if the state took over full ownership and a loss of taxable income to communities occurred (i.e. through property tax, income tax, and corporate income tax). She believed the effect could be around \$800 million over the life of the project. She wondered whether the issue had or had not been included in slide 19. She asked about the impact to the PILT [payments in lieu of taxes] process. Additionally, she wondered how the state would work with its partners at local communities to affect the consequences of the change if the buyout was successful.

Ms. Poduval answered that the Black and Veatch economic benefit analysis for the state did not break out the different state entities. For example, the analysis did not consider what DOR received from production tax or state corporate income tax, royalties received by DNR, or how the property tax was shared between the state and municipalities. The analysis considered the economic benefits coming to the state as a whole. She continued that the increase of state revenues up to \$400 million (slide 19) looked at the holistic state coffers; it was additional value the state would truly receive because it was paying less to third-parties such as lenders. She detailed that the state was expected to have a lower cost of debt than the 7 percent interest it would pay to TransCanada. She acknowledged that there may be an impact on how much of the

funds were in the state's coffers versus municipal coffers, but the analysis did not make the distinction.

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Co-Chair MacKinnon wondered if the state had calculated how PILT would be affected. Ms. Rutherford replied that the question may be better answered by another party. She stated that the amounts would be fixed, both the impact funds and the property tax driven by throughput. Whether or not one party would or would not continue to be a taxable entity would not negatively impact the municipalities' income stream if TransCanada was no longer involved (the state would not be a property tax payer). Ms. Poduval deferred to DOR to provide a more detailed response. She clarified that state plus municipality was \$400 million more without TransCanada than it would be with TransCanada. There was truly additional value for the combination of all state entities without TransCanada.

Co-Chair MacKinnon clarified that there was the potential for the upside. Ms. Poduval agreed, assuming that the state could finance cheaper than the 7 percent cost of debt. Co-Chair MacKinnon asked for verification that the savings would be on an annual basis. Ms. Poduval replied in the affirmative.

Senator Bishop surmised that the \$400 million increase was a dollar for dollar increase and did not account for a multiplier effect of spreading the dollars around the state through other projects. Ms. Poduval answered in the affirmative.

Co-Chair MacKinnon wondered if there was a scenario Black and Veatch could run that showed where TransCanada protected the state. She referred to Ms. Poduval's testimony citing a zero to \$400 million annual potential upswing [without TransCanada], which was contingent on Alaska's credit rating and its ability to acquire lower cost credit. She noted in the current low borrowing market, if the project was at FID at present, the state would have a significantly lower interest rate [without TransCanada]. She wondered how the state would achieve that with TransCanada.

Ms. Poduval replied that slide 21 addressed some of the analysis. She addressed slide 20 first. The slide showed

the NPV for the project with three different discount rates, recognizing that people had differing views. A 10 percent discount rate used a commercial hurdle rate for the project recognizing the project was an investment the state was making. A 7 percent discount rate could be viewed as a proxy for Permanent Fund returns and a 5 percent discount rate could be viewed as a proxy for the state's cost of borrowing. She had heard arguments that the state's discount rate was actually negative because the state liked having its cash flows grow over time in contrast to companies that liked front-ending their cash flows because they did not want to cut the budget with a declining cash flow. The analysis showed that without TransCanada the NPV increase could be zero in the worst case scenario and up to \$1.2 billion in the best case scenario.

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Ms. Poduval turned to slide 21 and addressed Co-Chair MacKinnon's prior question. The Black and Veatch analysis made the assumption that the state could finance cheaper than TransCanada. She addressed the idea that the scenario was incorrect. She believed there were two pieces to the answer. First, she considered how the projection of up to \$400 million in savings would be impacted if the state's cost of debt was more than Black and Veatch's estimation. Second, she questioned how high the state's cost of capital could actually be. She relayed that the second question would be answered by the finance team. She addressed what the impact would be if the state's cost of debt was higher than expected. She noted that the \$400 million figure was a rounding of the \$360 million shown on the left of the chart on slide 21. She explained that the \$400 million figure assumed a standard 70 percent debt/30 percent equity structure, with a financing rate of approximately 5 percent. However, the chart illustrated an incremental net cash flow benefit to the state at varying interest rates if the state financed all of its investment (without investing 30 percent equity, which would be approximately \$2 billion). She detailed that at 5.5 percent cost of debt there was still an additional \$130 million in value the state would receive each year of the project's operation. The finance team had looked at what would occur if the state's credit rating was downgraded to various levels from its current AAA rating. She noted that in the current market the state would receive an interest rate of about

5.5 percent if its credit rating was A-, which would be a significant credit downgrade.

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Co-Chair MacKinnon restated her interest in knowing whether there was a scenario where TransCanada would benefit the state. She surmised that if the interest rate was above 7 percent, the agreement with TransCanada would protect the state. Ms. Poduval agreed. She detailed that TransCanada's interest rate for the state was 7 percent; therefore, if the state ended up with an interest rate above that number, it should not terminate the agreement with TransCanada. She explained that it was necessary to consider what would increase the state's interest rate above 7 percent. She noted that it was one of two factors. First, a downgrading of the state's credit rating would impact the state alone. She reiterated that the finance team had assumed varying credit rating downgrades as low as A-, where the state's cost of debt would be 5.5 percent. The consideration was how much the state would have to be downgraded to get to an interest rate that was higher than 7 percent. The second driver that could increase the state's interest rate was a general inflationary environment; under that circumstance the agreement with TransCanada had floating rates. She explained that if the Treasuries went up and the state's costs increased, TransCanada's costs would go up as well. Unless it was a credit downgrade that would increase the state's interest rates, the advantage without TransCanada would remain.

Vice-Chair Micciche commented that Ms. Poduval's initial answer made it sound like TransCanada's interest rate in the project was static; however, it was actually a floating rate.

Senator Dunleavy asked if the concern about cost overruns was greater than concern about the interest rate the state could secure. Ms. Poduval replied that the state bore the cost overrun risk, regardless of the TransCanada buyout. She explained that the state would be responsible for paying all of the costs back to TransCanada through a tariff and cost overrun risk was not shared by TransCanada.

Senator Dunleavy surmised that the state should be more concerned about cost overruns than the interest rate it could secure on borrowed money. Ms. Poduval summarized her

understanding of the question. She believed he was asking if the state's risk associated with the cost overrun was higher than its risk associated with interest rates (regardless of TransCanada's involvement).

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Senator Dunleavy provided an example to clarify his question. He stated that a person may think they were building a home for \$250,000 at 4 percent interest, but when change orders occurred the price could increase to \$350,000. He noted that the wide project cost estimate of \$45 billion to \$65 billion was kind of low. He reasoned that the state had to be keeping on top of all of the components; however, he wondered if an overemphasis was being placed on the interest rate, while it should be keeping an eye on potential cost overruns.

Ms. Poduval agreed that the state should be considering all of the components. She relayed that the biggest value driver for the state would come from the price, which was something the state should be very concerned with, given that "price is king." She detailed that if prices did not support the project, everything else (capital costs, interest rates, and other) would be overwhelmed by the impact. She explained that the reason for emphasizing the interest rate was to highlight the incremental elements in the TransCanada decision. The state would bear the cost overrun obligation with or without TransCanada. She added that the exposure did not directly affect the decision on whether to terminate TransCanada; whereas, the expectation that the state could finance the project at a lower interest rate than TransCanada did have a direct impact. She agreed that cost overruns and interest rate were risk exposures to the state.

Senator Dunleavy believed it was one of the issues central to the point of terminating the relationship with TransCanada. Specifically, he questioned whether TransCanada's expertise was of such value that it would be able to recognize and help minimize potential cost overruns. He wondered if the cost of retaining TransCanada was a benefit to the state regardless of the potential upside of \$400 million per year [that may result if the relationship with TransCanada was terminated]. Ms. Poduval believed the question was important. She replied that her answer would have been different if the state had different

partners in the AKLNG project. She expounded that ExxonMobil, BP, and ConocoPhillips were some of the biggest and most sophisticated oil and gas companies in the world, with very well-developed project management science. The project had communicated to Black and Veatch that it did not have a preference one way or the other [if TransCanada was involved or not]; they believed it was the state's decision and the project could work either way. The lead on the GTP was currently ExxonMobil and the "number two" for the pipeline was also an ExxonMobil person. She highlighted that there was significant technical and project management expertise residing with the AKLNG partners that should help manage the risk.

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Vice-Chair Micciche was uncertain about his agreement with the exposure on cost overruns. He stated that TC was essentially serving as a bank for the state. He reasoned that if buying out TransCanada would lower the state's interest rate that financing cost overruns would also be at a significantly lower rate than TransCanada's pass through rate. He believed savings to the state would be increased overall if financing cost overruns was cheaper without TransCanada.

Ms. Rutherford believed that TransCanada was an excellent commercial company and was highly motivated to keep costs down; however, in the particular situation there was no negative effect to them unless the project cost became so high that the project did not move forward and gas sales were no longer economic. She explained that the state was required to reimburse TransCanada for all of its costs plus interest. However, the parties with the responsibility for the gas and its ultimate sale (the three producers and the state) were the most motivated to keep the costs down because at the end of the day the cost would impact the netback cost to the gas and how much money the state would make. She noted that the transportation system was just a means to monetize the gas.

Vice-Chair Micciche restated his question. He surmised that savings to the state would be increased overall if financing cost overruns was cheaper without TransCanada. Ms. Rutherford agreed.

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Ms. Poduval addressed slide 23 titled "Why terminate the agreement with TransCanada now?" The answer was broken into three parts: 1) to better manage the state's risk; 2) to avoid back-in rights; and 3) to influence project decisions. She moved to slide 24 and addressed that per prior agreements, the state would always be obligated to repay TransCanada's costs. She reiterated her earlier statements that the state had all of the development and cost risk in the project, whether the project moved forward or not. She explained that it would be less expensive for the state to directly own the equity in the project and make investments at a lower interest rate than to incur "failure leg" costs at a higher interest rate. Ultimately, if the project did not succeed, the loss to the state was lowered by lowering the cost. She remarked that the project was currently in the pre-FEED stage where a significant portion of the money had not yet been spent. She noted that at present the check due to TransCanada was approximately \$70 million.

Vice-Chair Micciche remarked that the repayment mechanism during operation was the long-term tariffs to TransCanada for its 6.85 percent. He wondered if the tariff would be lowered where the state would not enjoy the benefits of lower interest rates or if the tariffs were the same, thereby creating value for the state.

Ms. Poduval replied that the state's tariffs would be lower than a payment to TransCanada. She detailed that the state's midstream cost basis would be lower alone because its debt payments to a third-party would be lower than the rate built into TransCanada's tariff. She noted that the lower cost would result in \$200 million to \$400 million in extra value to the state.

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Vice-Chair Micciche asked if the mechanics of the lower tariff resulted in lower cost energy to in-state users. Ms. Poduval replied in the affirmative.

Co-Chair MacKinnon wondered if the statement was contingent on the debt to equity ratio the state used to finance the project. She surmised that the state could drive the tariff even lower if it used all equity for its share of the project. Ms. Poduval answered in the affirmative; if the

state had \$14 billion to contribute, there would be no tariff to pay, given that it would have paid for the state's share of the infrastructure upfront.

Ms. Rutherford furthered that each partner would have its own tariff costs based on its own portion of the pipe. The state would only pay its own tariff costs, either through TransCanada or AGDC.

Senator Bishop stated that the goal was to lower costs of energy to drive other forms of economic activity in the state. Ms. Rutherford agreed. She added that the goal was also to maximize wellhead values.

Co-Chair MacKinnon wondered if there had been discussion about how parties that did not currently own a percentage of the pipe would have access. She remarked that the state wanted as much gas in the pipeline as possible, which meant creating access to other parties. Additionally, one of TransCanada's stated goals was that it wanted as many molecules moving through the pipe as possible in order to obtain a return on its equity. She asked if the state would only be incentivizing its 25 percent share of the pipe.

Co-Chair Kelly asked Ms. Poduval to restate the question prior to answering.

Ms. Poduval understood that the question was about whether the state would be incentivizing third-party access to the project by creating a lower tariff through a reduction in the state's midstream costs as a result of direct investment by the state.

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Co-Chair MacKinnon agreed. Ms. Poduval answered that TransCanada, as a pipeline company, would always be incentivized to increase the volumes transported in the line; which naturally supported alignment for an expansion and bringing in another third-party to transport gas in the project. She relayed that the state had been negotiating commercial terms under which third parties could enter the project and under which expansions could be effectuated within the AKLNG structure. She referred to the earlier discussion about voting rights, which was an area that was important to the state. The hope was that the commercial terms would help the state create some rules about how

expansions would be considered by the AKLNG project and the power of the different parties to veto the action or not. From a commercial perspective, she believed it would be up to the state whether its lower cost basis would somehow benefit a third-party entering the project. She stated that a third-party entering the project would have the opportunity to negotiate with each of the project parties to expand the project. The expectation was that the state would probably offer the most favorable terms to bring a competing producer into the project. She elaborated that the state would have significant discretion that would depend on the specifics of the value that would come from the development of a field. For example, if the new gas came from federal offshore lands, the state's motivations for providing cheap service through the project may be different than if the new gas was derived from state lands. The commercial arrangements that were anticipated at present, would give the state the leeway to evaluate the benefit to the state across a range of scenarios.

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Co-Chair MacKinnon remarked that whether the project used a 42-inch or 48-inch pipe, the available space that may be the most attractive to new producers somewhere along the corridor would be the state's 25 percent. She stated that what may support the administration's position was that there would be reduced flexibility in allowing third-parties to enter the project because the state would only have 12.5 percent ownership (under the 40 percent buyback option) or less if TransCanada carried everything. She asked if her statements were accurate.

Ms. Rutherford could not speak to the difference in the state buying back all of TransCanada's interest versus 40 percent. She relayed that the cost of third-party access would be lower if the state had its own tariff structure. She elaborated that the state would have significant discretion about determining how third parties would pay to use the pipeline. She stated that all participants would have more capacity to provide to third parties if the participants all agreed and paid for an expansion. She expounded that if the state had 25 percent of the full expansion capacity (5 billion cubic feet) there would be more throughput available through the state's lower tariff structure than it would under a maximum expansion capacity of 3.5 trillion cubic feet. She relayed that the state

would provide an advantage with a lower tariff structure regardless of the size of pipe, but there would be more capacity to provide more molecules with a top-end expansion capacity. Part of the discussion with producers related to access and expansion was about who had the expansion capacity and under what circumstances it could be provided. She relayed that the information would eventually be shared with the legislature, given that the legislature would ultimately have to approve the contracts. The administration believed that lower tariffs were better as a sovereign. The state would receive more cash value on an annual basis if TransCanada was out of the project. The state would be advantaged because it could provide third-party new gas with a lower tariff structure. Additionally, a 48-inch pipe was superior because it would provide more room for third-party gas even at the beginning of the project when there would be the most gas coming out of Point Thomson and Prudhoe Bay.

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Co-Chair MacKinnon mentioned an interplay in the buyout agreement which affected the expansion note that was dependent on whether the state and the legislature fully appropriated 100 percent of the costs. She furthered that there was an interplay between totally buying TransCanada out and the molecules that were available for third-party expansion. She referenced Ms. Rutherford's comments on the difference between the 42-inch and 48-inch pipe. She stated that no matter what, dependent on the state's debt to equity ratio, if TransCanada were in the project the state would see less value. She believed the maximum future benefit from the project to the state would occur if it went for 100 percent equity by meeting cash calls as they came in (versus going out into the market). Under the provided scenario, she queried how the state would be paid back if a third-party entered in. She reasoned that the party would be benefitting from a deal put on the table by the state to incentivize third-party participation. She referred to the administration's current request for \$70 million and an increase to the overall budget at present. She noted that the state was currently paying its bills as they were accrued and if that continued, the issue would become more relevant.

Ms. Rutherford replied that the administration would provide the committee with information associated with a 40

percent buyout versus a 100 percent buyout and what it may look like in terms of expansion and access provisions for third parties. Additionally, the administration would provide information on a 100 percent equity option versus a 70/30 debt to equity ratio and what it may look like for third-party access and tariff structure.

Co-Chair MacKinnon clarified that she was not saying the state had \$7 billion to \$11 billion it was willing to dedicate as 100 percent equity in the project, but it did make a difference if the state was incentivizing the lower tariffs.

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Ms. Poduval believed slide 25 had been sufficiently addressed. The slide indicated that the stakes increased as the project continued forward. Additionally, it was better for the state exit the agreement with TransCanada earlier if TransCanada was accumulating costs on the state's behalf at a higher rate of interest than what the state would pay on its own.

Ms. Poduval turned to slide 26 and relayed that terminating the PA by December 2015 was important in order to avoid back-in rights for TransCanada. She explained that the option had been built in to the PA. She furthered that originally the PA was meant to include the back-in rights that would allow TransCanada to come back into the project even if the state terminated the PA; however, the provision had been removed by the legislature in order to facilitate the clean off-ramp at the end of December 2015. The back-in right specified that if the state terminated TransCanada and pursued a substantially similar project over the next five years, the state would need to offer TransCanada an option to participate in the project under similar terms. She continued that if December 2015 passed and the state entered into an FTSA, the state would have to give TransCanada the right to come back into the project. She noted that the December 2015 off-ramp was the one clean option that had been designed into the PA by the legislature.

Co-Chair MacKinnon asked if the back-in rights were automatically triggered on December 31, 2015. Alternatively, she asked if the rights were triggered only with an FTSA. Ms. Poduval replied that the back-in rights

would be triggered if the state did not terminate the PA by December 31, 2015 and instead entered into an FTSA with TransCanada. The terms of the FTSA were expected to include the back-in right.

Senator Bishop asked if Ms. Poduval had sufficiently answered the question.

Co-Chair MacKinnon affirmed that the answer had specified that the state had an off-ramp prior to December 31, 2015 that was provided, but the state was also supposed to have an FTSA in effect by that date. She believed the current off-ramp was clean. She wondered if there was a back-in right if the state chose to make no changes or partially fund up to 40 percent and there was no FTSA on January 1, 2016.

Ms. Poduval replied that according to the terms of the PA one of two things had to happen by December 31, 2015: 1) the termination of the PA; or 2) the state executed an FTSA with TransCanada. She detailed that if the legislature did not support terminating the PA, it would have to execute an FTSA with TransCanada by December 31, 2015 and the terms would include back-in rights for the company.

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Co-Chair MacKinnon wondered what would happen if the legislature chose not to act, since it was the administration's decision (specifically the DNR commissioner). She asked about a scenario where the state decided not to proceed with TransCanada. She wondered if there would be litigation because the state had not executed an FTSA and had not paid the bills it owed the partner.

Ms. Poduval replied that TransCanada had the right to terminate the PA if the state did not execute the FTSA by December 2015. At that point it was likely that TransCanada could deliver the termination notice, meaning the state's obligation to pay back TransCanada for its development costs would begin.

Co-Chair MacKinnon asked how many days' notice were required to terminate the PA. She asked if it was 45 or 90 days. Ms. Poduval believed the number was closer to 30, but it would be provided in writing to the committee.

Co-Chair MacKinnon believed it was 90 days. Ms. Rutherford answered that there were distinctions between a termination initiated by the state or by TransCanada and even under the circumstances TransCanada opted for termination. The department was compiling a chart outlining the distinctions that it would provide to the committee the following day.

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Ms. Poduval turned to slide 27 and relayed that the third factor influencing the timing of the TransCanada termination decision was the need to influence key AKLNG decisions. In relation to alignment and voting rights there were some fundamental differences between the partners on different issues. For example, the lowest cost for the project versus the highest value for Alaskans. She continued that as the project was going through pre-FEED, there were key decisions slated to be made. She explained that Black and Veatch believed it was important for the state to have a direct say in decisions on issues such as by-product handling, project budget, and schedule for the midstream portion of the pipeline. She spoke to the importance of the governance agreement currently under negotiation. She detailed that trying to divide the voting rights between TransCanada and AGDC that would accrue to the state's 25 percent was adding complexity to the negotiations and agreements. She addressed the importance of providing clarity on the state's position in order to bring the agreements to completion.

Ms. Poduval addressed options for the state to finance its share of AKLNG midstream without TransCanada (slide 29). She qualified that slides 29 and 30 were high-level summary slides that had been extracted from the finance team's presentation; the slides had been included for the sake of completeness. She recommended addressing any questions on the slides to the finance team. She read options from slide 29:

- The Legislature could appropriate from existing State funds, e.g., the Constitutional Budget Reserve Fund (CBRF), Earnings Reserve Fund, etc.
- The Legislature could authorize the issuance of State debt

- The Legislature could authorize pursuit of project financing
- The Legislature could authorize the pursuit of funding from other sources: LNG buyers and other potential equity investors

Ms. Poduval noted that given the magnitude of the amounts involved there was concern that there would be an impact on the state's credit rating, which would impact the state's ability to borrow for other purposes.

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Ms. Poduval turned to slide 30 and relayed that FirstSouthwest was the financial advisor responsible for analyzing whether the termination of the agreement with TransCanada would impact the state's credit rating. The company had concluded that the TransCanada termination on its own was not expected to result in a credit downgrade. She furthered that the state's commitment to pay TransCanada's costs regardless of project success or failure would be seen as state debt. She explained that if the state could finance the debt directly at a lower cost, the overall net effect could be positive on the state's credit rating. The company had concluded that given the magnitude the state was expected to borrow, the state's credit rating was likely to deteriorate, especially during the construction phase; however, the company believed that the state's credit rating should recover once the project became operational and revenues began coming in.

Senator Dunleavy surmised that the downgrade, in combination with another potential downgrade the state was facing as a result of getting its fiscal house in order, could result in an increase in the cost of borrowing money. He wondered if any models had been run on the scenario. Ms. Poduval replied that the finance team had looked at the scenario and could answer the question.

Ms. Poduval addressed how TransCanada's technical role in AKLNG could be replaced. She noted that TransCanada was experienced in northern pipelines and had brought the wealth of its experience to the AKLNG project. She read from slide 32:

TC in its current role performs or has performed several functions including the following:

- Holds State of Alaska's midstream equity in AKLNG as signatory to the JVA
- Contributes pipeline SMEs that were seconded to the JVA PMT
- Coordinated FERC NEPA Process

Senator Dunleavy wondered if the state was on the verge of missing deadlines in the project. Ms. Rutherford responded that there were some reports due, but the state was not in danger of missing any of the deadlines. She believed the state was completely on schedule. She stated that there had always been a hope that the commercial agreements would be completed more quickly, but there was not a deadline specified by SB 138 or in any other documents. She stated that commercial agreements evolved at their own pace (especially with four or more parties negotiating) and an outcome could not be forced. She noted that a couple of reports were coming due, one was when the first commercial agreement came to the state and another was associated with instate domestic gas.

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Senator Dunleavy wondered if the termination of the agreement with TransCanada would be seamless or if it would result in a potential setback that could cause cost overruns or delays. Ms. Rutherford replied that the AKLNG project and TransCanada had been very helpful in trying to ensure that no delay would occur. She detailed that TransCanada's willingness to provide some of its staff to complete the pre-FEED stage would ensure that the transition was seamless.

Vice-Chair Micciche referenced slide 32 and asked for verification that TransCanada had been involved in the pipeline technical work and the pre-FEED stage only. He asked if TransCanada was expected to lead the work moving into the next stage. Ms. Poduval agreed that TransCanada was the pipeline technical lead during pre-FEED. The lead subsequent to pre-FEED had yet to be determined (especially related to the construction stage).

Vice-Chair Micciche asked if the maximum value TransCanada had to offer to the project had already been realized. Alternatively, was it expected that TransCanada would lead the technical pipeline design team in the FEED stage. Ms. Rutherford replied that she did not believe enough was known to answer the question because there had been no finalization of the structure of the joint venture agreement for FEED, construction, or operation; therefore, there had been no expectation that TransCanada would necessarily be the lead on any of those elements. She opined that if TransCanada remained an agent for the state in the project that it would advocate for its own role in FEED; however, she could not foresee whether the outcome would be sustained or what it would be.

Senator Dunleavy wondered if there were any circumstance where the administration or consultant would advocate that TransCanada remain in the partnership.

Co-Chair MacKinnon replied that the committee could ask Governor Walker the question.

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Senator Dunleavy asked if there was anything the state would lose without TransCanada's involvement in the project. Ms. Poduval replied that there were two main risks. The first was the financial aspect and whether the state could finance the project without TransCanada. She believed the finance team's assessment had determined that the state would be better off without TransCanada because of the state's "no conditions attached" commitment to TransCanada. The second aspect was the technical expertise that TransCanada brought to the project and whether there would be inefficiency in continuing the project without the expertise. She relayed that the AKLNG project felt comfortable that the project could proceed. Additionally, TransCanada's offer to allow its employees to continue in their roles to avoid a disruption had helped to mitigate the concern.

Ms. Rutherford communicated that she had also been concerned about the financing aspects of the project; however, information that had been shared with the House Finance Committee and that would be shared with the Senate Finance Committee had been comforting. Additionally, she did not believe TransCanada should be taken out before pre-

FEED and that there should be adequate provision for pre-FEED to continue smoothly. She relayed that the issue had been worked out in discussions between the project and TransCanada.

Co-Chair Kelly queried the role of the royalty in value (RIV) versus RIK determination. He asked if it was all academic if it was determined that it was not in the state's best interest to take the gas in kind.

Ms. Rutherford did not believe it was academic. She believed the issue was very important from various perspectives. She detailed that SB 138 presumed that the commissioner of DNR would provide an RIK decision and required a full analysis on the implications in to make an informed decision. For this reason, having the commercial agreements that affect the value of the upstream gas was critical prior to making an RIK decision. She relayed that the administration's goal was to get to an RIK decision, which was the reason for its hard work on some of the upstream and gas-balancing supply issues. She believed that if the state decided that its ability to take gas in kind (which triggered the tax as gas option for producers under SB 138) was too risky, there would be a significant discussion about whether or not the structure laid out in SB 138 would still work because the producers were very interested in the state carrying its own throughput.

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Co-Chair Kelly reasoned that the issue was all academic if there was no RIK decision. He wondered if it was all hinging on the decision. Ms. Rutherford confirmed that the administration would certainly want to reach an RIK decision because it was a facilitator for the project. On the other hand, it was critical to bear the importance of the RIK decision to the state during negotiation on the upstream agreements. She explained that it was necessary to know beforehand if the cost of handling carbon dioxide and upstream costs associated with field cost allowances at Point Thomson and Prudhoe Bay were both so high that they would diminish the state returns. She stressed that prior to electing RIK, state had to ensure that it had reasonable costs, that supply was available (the state would receive its gas as a derivative of the producers' production and it would never be at the table deciding that it could get

another drill in the ground in another location if gas was unavailable), and upstream costs.

Co-Chair Kelly understood. However, he surmised that if it was not the outcome, he agreed that the structure of SB 138 would have to be questioned. He had assumed that the decision would have been made already. He believed it was "almost the elephant in the room." Ms. Rutherford replied in the negative. She detailed that in the HOA it had always been presumed that the commercial agreements would be completed prior to making an RIK decision. She emphasized that just like fiscal certainty, the decision was one of the most significant leverage points for the state. The presumption was that the elements effecting the state's value by taking RIK would be negotiated first. Only at that point would it be possible to make an informed decision about whether RIK would be in the state's best interest.

Co-Chair Kelly did not believe the RIK decision necessarily impacted the decision on TransCanada. Ms. Poduval added that there would be no gas to transport without understanding the suite of commercial agreements and terms the state would be part of and what the value would be to support the RIK decision. She elaborated that without gas to transport the state could not enter into an FTSA.

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Co-Chair Kelly asked Ms. Rutherford to walk through the sequencing at a later time. Ms. Rutherford agreed to provide the information.

Ms. Poduval addressed how will TransCanada's technical expertise would be replaced (slide 33). She reiterated earlier testimony that TransCanada was leading the pipeline work for the pre-FEED portion of the project. She read from the slide:

TransCanada is not anticipated to build the pipeline. It will be managed through the AKLNG Project Management Team (PMT) which leads and guides the AKLNG project

PMT consists of Co-Venturer (CoV) employees seconded to project based on experience and skill sets

PMT hires engineering and specialist contractors to advance design efforts

Significant amount of work is done by contractors with oversight by PMT

Ms. Poduval elaborated that even through pre-FEED contractors (engineering and other experts) that had been brought in did a significant amount of the work under supervision by the project management team. She moved to slide 34 and stated that the AKLNG project partners (ExxonMobil, BP, and ConocoPhillips) brought significant expertise and experience to the project. She elaborated that the partners all brought worldwide experience and resources to staff the management team with experts. She continued to address slide 34:

In addition, AGDC brings Alaska pipeline experience

- Successfully completed Pre-FEED and FEED on ASAP
- Key subject matter experts based in Alaska
- AGDC has already taken over TC's role in coordinating NEPA process

Ms. Poduval elaborated it was a combination of the structure where AGDC, AKLNG producer partners, and contractors worked on the management team that would continue the work needed to execute the midstream in TransCanada's absence.

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Ms. Poduval addressed conclusions and recommendations on slide 35:

The current arrangement with TransCanada was designed to provide the State (and TransCanada) with several off-ramps as the AKLNG Project moved through its different development stages, including an important clean off-ramp for the State in December 2015

The State administration recommends termination of the TransCanada relationship by December 2015 and replacing it with the State's direct participation in the AKLNG midstream

The exercise of this off-ramp is expected to facilitate better alignment and control, lower risk and create additional value for the State in the AKLNG Project over the long-term

Senator Olson was convinced that TransCanada had done its job and that the sunset had been reached. He believed that whenever government got involved, things became murky. He stressed that he and others wanted the state to have more voting rights. He wondered what kind of safeguards were in place to ensure that the bureaucrats were competent in their voting. He remarked that with a company like TransCanada it was clear that voting always came from its bottom line. He did not know if the bureaucrats had the expertise to vote on the state's behalf. He had not been impressed with people who were going to be voting.

Ms. Rutherford replied that when the presenters had addressed voting rights they had spoken about alignment of the state's 25 percent interest because it was currently complicated with multiple parties sharing one party's voting right. She elaborated that AGDC had a role in the liquefaction and TransCanada had a role on the pipeline and GTP. At the end of the day, the state had world-class private sector partners in the project that would also bring their voting rights to the discussion. She expounded that it was the partners' expertise that brought the state comfort that the partners would always work for the bottom line and to optimize the value of the product. She explained that the state would not get more voting rights, but it would have a more aligned and clear voting right in the joint venture.

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Senator Bishop addressed voting rights. He remarked that Mr. Dubler carried the voting right for AGDC. He wondered if AGDC commissioners would make a voting decision and communicate it to Mr. Dubler to carry out. Ms. Rutherford replied that she did not know the exact structure for AGDC. However, typically in corporations the CEO and director would make decisions about what level of detail would be taken to the board of directors for approval. She could not speak to the AGDC bylaws, but she was certain that the people participating in the project from AGDC had been

reporting directly to AGDC leadership and that information would go to the board subsequent to that.

Co-Chair MacKinnon believed that the question should be directed to AGDC.

Co-Chair MacKinnon thanked the presenters. She discussed the agenda for the week.

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

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ADJOURNMENT

12:43:09 PM

The meeting was adjourned at 12:43 p.m.