

**PRESENT-  
ATION:  
STRANDED  
GAS ACT  
PROPOSALS  
4/27/05**

## **GOVERNOR FRANK H MURKOWSKI**

### **NONCONFIDENTIAL STATUS REPORT ON STRANDED GAS APPLICATIONS**

**April 27, 2005**

- I feel it is appropriate that we meet with you today and provide you with a status report on where we stand in our ongoing efforts to build a North Slope gas delivery system.
- As most of you know, we are currently evaluating three proposals to construct and operate a North Slope gas delivery system.
- One from the North Slope oil producers (Conoco/Phillips, ExxonMobil, and BP), one from TransCanada Pipeline Company, and one from the Port Authority. Also, I want to recognize the Alaska Natural Gas Development Authority (ANGDA).
- I am joined today in this effort by the members of my Gas Cabinet ---- Bill Corbus, Commissioner of Revenue; Dave Marquez, our Attorney General; and Tom Irwin, Commissioner of the Department of Natural Resources and others on the team.
- Because of the confidentiality requirements mandated in our ongoing commercial negotiations, I am only able to speak in general terms about the status of the discussions.
- I hope all of you will understand and appreciate the sensitive nature of these talks and the reasons a high degree of confidentiality must be maintained.
- We stand on the brink of making the most important decision in our state's history ---- actions we soon will be taking are going to

have a profound effect on Alaska's economy for generations to come.

- As you can imagine a decision of this scope and magnitude is surrounded with a great deal of emotion, enthusiasm and deeply held opinions ---- some are founded on fact ---- some are not.
- As Governor, I am charged with the solemn responsibility of evaluating all of the gasline development proposals and determining which is in the best interest of all the people of Alaska.
- We are guided in this effort by the Stranded Gas Development Act ---- Passed by the Legislature and signed into law in 2003.
- That Act sets forth a process whereby the Governor is authorized to negotiate fiscal certainty for an extended period of time regarding taxation and other applicable issues with qualified applicants who propose to build a North Slope gas delivery system.

#### GOALS:

- My goals in negotiating a contract under the Stranded Gas Act is to achieve:
  1. A fair share of the revenues for Alaska.
  2. Provisions for in-state use of the gas.
  3. Access to the pipeline for others who explore for gas.
  4. A pipeline that may be expanded.
  5. A state equity ownership in the pipeline.
  6. Jobs for Alaskans and job training.
- In addition the SGA specifies that any negotiated contract that I deem appropriate for consideration by the legislature go out for a 30-day public review.
- Upon completion of that review, the contract will be provided to the legislature for ratification.

- Once received, the contract must be voted either up or down ---- there is no opportunity provided for amendment.
  - This places a great burden on the Administration to “get it right the first time”.
  - Out of necessity, the scope and complexity of these contracts will be staggering ---- running into the hundreds of pages.
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- Because of the complexity inherent in a contract that embraces hundreds of billions of dollars in commercial content, I am mindful of the need to provide the legislature with the time and information necessary to adequately weigh the value of the contract I forward to them.
  - To address this need my Administration has been working closely with the joint Senate/House Legislative Budget and Audit Committee.
  - Members selected by the leadership in both bodies are being provided with access to all the confidential information being collected and analyzed in our negotiating efforts.
  - They are currently in the middle of this process ---- they are afforded the opportunity to observe the so called good, the bad, and the ugly associated with these complex commercial discussions.
  - I have provided this unprecedented access because I believe it is the right thing to do.
  - As I have my responsibilities under the SGA, so too does the legislature ---- and their duties are no less solemn or difficult than mine.

- They must either accept or reject the contract I present to them - --- to be able to do that they absolutely need to understand all of the complexity and nuance of the information used to make our decisions.
- As you can imagine it is not always pretty watching sausage being made ---- but at the end of the day, they “will” understand how we arrived at our decisions and the information we used in the process.
- As I stated we are currently evaluating three separate North Slope gas commercialization efforts.
- The good news is that we have “three” proposals ---- for the gasline veterans in this room this is extremely good news and suggests that our gas may soon no longer be stranded.
- Unlike previous efforts that ran 60 miles per hour into a market reality of \$2.00/mcf ---- these “new” proposals reflect a tide change in the market.
- With current gas prices close to \$7.00/mcf and strong demand/price projections stretching well into the foreseeable future I believe that now is the time to deliver our gas to the nation’s consumers.
- The first big step in making this a reality occurred late last year when Alaska’s Congressional Delegation under the leadership of Ted Stevens, Don Young, and Lisa Murkowski successfully passed federal enabling legislation for the Alaska Gas Pipeline Project.
- This legislation contains a number of provisions critical to the construction of the Alaska gas pipeline.
  - Expedited judicial review;
  - Priority permit processing by FERC and other federal agencies;

- Loan guarantees;
  - Accelerated depreciation for the pipeline;
  - Conditioning plant benefits;
- In mid February of this year another big step was taken when the U.S. Federal Energy Regulatory Commission proposed regulations governing “open seasons” for the Alaska gas pipeline.
  - I am pleased to report that those regulations embraced my main policy goals;
    - Providing access for new explorers;
    - Providing off-take points for instate usage;
    - Requiring serious consideration be given to in-state needs during open seasons and expansions.
  - Now the ball is in the State’s court.

## **PRODUCERS**

- The first application we received under the SGA arrived on January 20, 2004 from a consortium of North Slope oil and gas producers Conoco/Phillips, ExxonMobile, and BP.
- They propose a 52” pipeline will be constructed along the existing highway system from Prudhoe Bay through Alaska and Canada to existing North American pipeline infrastructure.
- This project would begin with an initial capacity of 4.5 bcf/day expandable through compression up to 5.6 bcf/day.
- Receipt of that first application triggered an enormous effort by my Departments of Revenue, Natural Resources, and Law.
- We found ourselves right in the middle of a multi-multi billion-dollar negotiation ---- and frankly in those first days we were challenged.

- I am tremendously proud of the men and women in my administration and how they rose to meet this daunting challenge.
- Through the employment of their own talents and the acquisition of world-class consultants ---- we have developed a formidable analytical capability.
- Because of their efforts I can say with confidence the State of Alaska's interests "will" be protected.
- This would not have been possible without the budgetary support provided by the legislature and I appreciate their understanding the need to build this critical skill set.
- I would also note for the record that a similar same skill set developed for the producer negotiations is also being used for the TransCanada and Port Authority effort.
- The Producer application is by far the most complex of the three.
- That complexity stems from the fact that it embraces every aspect of gas transportation beginning at the bottom of the production well ---- through the gathering system and the gas conditioning facility ---- into the proposed pipeline across Alaska, the Yukon, British Columbia, Alberta and back into the United States ---- through the marketing process ---- ending up at the gas consumer's front door.
- Every step along the way has its own set of opportunities, complexities, and risks.
- Contemplation of this departure from a state's normal royalty and taxation process is based on two reasons.
  - The project may be accelerated if the state provides contract provisions beyond the status quo;

- The opportunity to significantly increase the financial benefit of the project to the state.
- This could be accomplished through three specific actions.
  - Converting royalty and taxes into outright ownership of a significant portion of the in-place gas reserve.
  - Taking an equity position in the gasline and processing facility proportionate to our gas ownership share;
  - Marketing our gas and taking firm transportation capacity in the pipeline to deliver that gas to purchasers.
- I am pleased to report that the state has made tremendous progress in putting this very complex concept into the form of a contract.
- I am convinced that the Producers are fully committed to successfully concluding these negotiations and are providing all the supporting resources necessary to support our discussions.
- While there is a solid financial and technical underpinning for the producer proposal, it is not without its challenges.
  - Because this pipeline will run through Canada, they must deal with regulatory uncertainty in that country;
  - They must also deal with procuring enough steel to construct over 2000 miles of 52" pipeline

## **TRANSCANADA**

- The second application we received under the SGA arrived on June 1, 2004 from TransCanada Pipeline Company.

- Under this proposal a 48" pipeline will be constructed along the existing highway system from Prudhoe Bay through Alaska and Canada to existing pipeline infrastructure in Alberta.
- It does however contemplate state equity ownership in the gas conditioning facility and the pipeline ---- it also envisions the possibility of the state taking the responsibility for the transportation and marketing of its own gas if the Producers choose to sell their reserves rather than ship on an independent pipeline.
- Under this proposal the state and TransCanada would attempt to strike a business deal with the North Slope gas owners to either sell their gas at the wellhead or make a firm commitment to move their gas down the pipeline to market.
- I would also characterize these negotiations as well advanced with all parties committed to finalizing discussions in the very near future.
- I have been impressed with the willingness of TransCanada to work with the state team to create a tariff framework that embraces both my gas development policies and the FERC regulations.
- As in the Producer discussions, I believe TransCanada is fully committed to successfully completing all the negotiations as quickly as possible.
- TransCanada's proposal also has its challenges.
  - This proposal presumes the Producers will be commercially reasonable and either ship their gas on an independent pipeline or sell their gas at a commercially reasonable rate;
  - As with the producers, they must deal with regulatory uncertainty in Canada;
  - They must also deal with procuring enough steel to construct 1800 miles of 48" pipeline.

## ALASKA PORT AUTHORITY

- The third, and most recent, gas development proposal we are evaluating was submitted by the Alaska Port Authority on March 30th of this year.
- The Port Authority was formed in 1999 and is made up of the North Slope Borough, Fairbanks North Star Borough and the City of Valdez.
- The Port Authority proposes to build a gas delivery system consisting of a 56" pipe from the North Slope to Delta Junction and a 48" pipe from there to tidewater in Valdez.
- In Valdez the gas would be converted to liquefied natural gas and transported by tanker to West Coast markets or other markets in addition, natural gas liquids such as propane, ethane, and butane would be extracted and sold in the markets of the world.
- Under this proposal the Port Authority would make a business deal with the North Slope Producers and the State to purchase gas at the wellhead, transport it through a tax exempt entity, and sell the gas to a marketer for sales into the consumer market.
- This project envisions no direct state participation but does recognize that the North Slope Producers may need a degree of fiscal certainty on gas production taxation.
- Our analytical team is just beginning to evaluate the Port Authority's submission and it is too early to make any risk or value judgments pertaining to the proposal.
- As in the other two proposals, the Port Authority effort is not without its challenges.
  - Since they do not control the gas supply they must make a commercial proposal to the owners sufficient to obtain sales contracts;

- They must get formal approval from the Internal Revenue Service to retain their tax-free status;
  - They must get long-term sales contracts;
  - They must obtain a permanent exemption from the Jones Act;
  - And they must deal with difficult siting issues on the West Coast.
- I will say that this project is radically different than the Alaska Highway proposals submitted by the North Slope Producers and TransCanada ---- as a result it will have a significantly different risk/reward profile.
  - Before I will be in a position to make any recommendation on this project we will need to be able to do an "apples-to-apples" comparison on the risk/reward profiles of all three proposals.
  - Not covered under the Stranded Gas Development Act is the Alaska Natural Gas Development Authority created by Proposition 3 in the November 2002 election. ANGDA has been working on a spur line which will bring gas to Cook Inlet.
  - I am not certain at this time how long this is going to take, but we will keep you apprised as we move down the analytical trail.
  - Regardless of what happens with any of the proposals already discussed, I assure you that we enshrine in any agreement an opportunity to construct a pipeline to the Cook Inlet ---- I have asked the Alaska Natural Gas Development Authority to lead in that effort.
  - It is common knowledge by now that I made a recent trip to Ottawa to discuss the gasline with Prime Minister Martin.
  - This was in recognition of the fact that no matter how quickly we act here in Alaska, the highway routes all will travel through Canada.

- While Alaska would not presume to recommend what regulatory framework is appropriate for Canada, we do believe the time is right to create a process by which a gas pipeline project can be constructed in the most expeditious manner possible.
- I know all of you are making plans for the summer and would like to hear from me that a specific date had been chosen for a "special session" to act on a stranded gas contract.
- While I can say that we are getting close, I can not give you that date today.
- Once we have closed on general terms, there is a lot of detail work for the attorneys to do before we have a contract ready for public and legislative review.
- I will tell you that I am personally involved in the negotiations and will continue to be involved until I am satisfied that I have a contract worthy of your consideration.
- I will send you a contract containing what I believe it takes to get our gasline built and it "will" be what is best for Alaskans today and what will be best for Alaskans tomorrow.
- It will have the earliest "in-service" date possible, contain the best fiscal benefit package possible, and afford new explorers and Alaskans the best access possible.
- What is best will be a product of raw economic reality ---- it will not be based on emotions. .
- And you should also know that my decision will not be without criticism ---- no matter which way we go.
- And I promise you my decision ---- the contract I send to you for your approval ---- **will be based on what I believe is right.**

- So, enjoy your summer (at least the first month or so) and I will see you back here soon ---- and when I do, we will really have something to celebrate.