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natural gas. The three producers will also influence the criteria used to award and allocate capacity in any open season as well as the timing of any open season. These facts make the situation far different than in the lower 48, where producers and pipeline owners for a project are typically or largely unaffiliated. Also, while in the lower 48 there are often competing pipelines, it is generally accepted that the North Slope most likely will be served by only one large diameter gas pipeline.

The State takes no position on the propriety of the NOPR's proposed approach with regard to lower 48 gas pipelines. Nor does the State object to that proposed approach being applied to Alaska gas pipelines not originating on the North Slope, *e.g.*, those in Cook Inlet. However, the State submits that the Commission-found unique competitive conditions surrounding the North Slope gas project do indeed "warrant special consideration and oversight." *See* Order No. 2005 at ¶ 9. The past concerns over various aspects of North Slope gas competition, discussed *supra*, and the continuing concentration of reserves ownership in three companies sets Alaska apart from the lower 48 and justifies the continued application of the more sweeping standards of conduct contained in Order No. 2004. The State submits that it is better to put safeguards in place now in the form of the Order No. 2004 requirements than to try later to unscramble abuses after the fact.

The State does recognize that *National Fuel* evidenced skepticism in the Commission's being able to justify Order No. 2004 solely on a theoretical abuse basis. While that skepticism may be well founded for the lower 48, where there are many existing pipelines and thus plenty of opportunity to show actual (as opposed to theoretical) abuse, that is not the situation in Alaska. Order No. 2004 had no reason to, and did not, discuss Alaska separately, and thus the court was unlikely to have considered or even been aware of the unique situation on the North Slope. If

there is any situation where the theoretical threat alone would be sufficient to justify an order extending the standards of conduct to Energy Affiliates, it is for this yet-to-be-built North Slope project. Because the North Slope project has yet to be certificated much less built, there literally can be no factual evidence of abuse between unknown marketing/non-marketing affiliates and an unknown pipeline company. However, Congress and the Executive Branch have repeatedly voiced their concerns about competition in the exploration, development, and production of Alaska natural gas and the potential for abuse. This justifies the Commission taking the action the State requests.

To accomplish this exception, the State recommends that the following italicized words be added to § 358.1(e):

*“The Standards of Conduct in this part do not govern the relationship between a natural gas Transmission Provider as defined in § 358.3(a)(2) and its Energy Affiliates, except for a Transmission Provider carrying natural gas from Alaska’s North Slope to destinations in the lower 48 states, and its Energy Affiliates.*

The Commission Should Confirm that Order Nos. 2005 and 2005-A Remain Intact

As noted above, Order No. 2005 incorporated relevant portions of the Order No. 2004 standards of conduct and made them applicable to the open season process. See Order No. 2005 at ¶ 74. The incorporation included prohibited dealings between a North Slope gas pipeline and its Energy Affiliates. Also as noted, no challenge was made to the Commission’s holding on the applicability of Order No. 2004. However, in light of the D.C. Circuit’s action in *National Fuel*, an argument could be fashioned that the vacated portions of the standards of conduct incorporated into Order No. 2005 are no longer binding unless the Commission addresses Order No. 2005 in its final rule in this proceeding.

This argument fails for at least two reasons. First, the Order No. 2004 standards of conduct apply only to a certificated pipeline. See Order No. 2005 at ¶ 74 n.24. Order No. 2005 takes portions of Order No. 2004 and applies it to an entirely new and different situation -- an open season that will take place well before the certificate stage. Order No. 2005 also has an independent foundation, Section 103(e) of the ANGPA. The Commission found based on the record in the Order No. 2005 proceeding that North Slope competition concerns justified its action. No one has appealed that aspect of Order No. 2005 and it is thus final and non-appealable.

Second, even though the same standards applied to all Transmission Providers, the court vacated the standards of conduct only for natural gas Transmission Providers and thus did not treat all Transmission Providers the same. The court left the standards intact for electric Transmission Providers because no one appealed their applicability to electric services. Just as the court implicitly viewed electric Transmission Providers as performing a different service than natural gas Transmission Providers, the Commission should view the open season "service" as being different than that provided by natural gas Transmission Providers -- one unaffected by the holding in *National Fuel*.

Nonetheless, the State recommends that the Commission err on the side of caution and presume that *National Fuel* does have an impact. The Commission can negate this presumed impact by simply confirming that Order Nos. 2005 and 2005-A remain intact because those orders are necessary to address the unique competitive concerns surrounding an open season for the North Slope project.

Respectfully submitted,

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Dated: March 30, 2007

CERTIFICATE OF SERVICE

I, Edward J. Twomey, hereby certify that on March 30, 2007, copies of the foregoing COMMENTS OF THE STATE OF ALASKA ON PROPOSED RULEMAKING in the above-captioned proceedings were served upon each person designated on the service list compiled by the Secretary in these proceedings.

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UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION

Standards of Conduct for  
Transmission Providers

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Docket No. RM07-1-000

REPLY COMMENTS OF  
ANADARKO PETROLEUM CORPORATION

INTRODUCTION

On January 18, 2007, the Federal Energy Regulatory Commission ("FERC" or "Commission") issued a Notice of Proposed Rulemaking proposing revisions to the Standards of Conduct for transmission providers ("Standards of Conduct NOPR").<sup>1</sup> On March 30, 2007, the State of Alaska submitted timely Comments on the proposed rule, directed solely at the relationship between this rulemaking proceeding and federal regulation of an Alaska natural gas transportation project. Anadarko Petroleum Corporation ("Anadarko"), an oil and gas exploration company with significant gas-prone acreage in the State of Alaska, hereby submits Reply Comments supporting the Comments filed by the State of Alaska.

Anadarko joins the State of Alaska in its request that the Commission (1) make it clear that the Standards of Conduct for an Alaska natural gas transportation project apply to the relationship between the project sponsor's and the ultimate pipeline's relationship with *both* its "Marketing Affiliates" and "Energy Affiliates", and (2) confirm that the requirements of Order Nos. 2005 and 2005-A, relating to the conduct of open seasons for an Alaska natural gas

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<sup>1</sup> *Standards of Conduct for Transmission Providers*, Notice of Proposed Rulemaking, 118 FERC ¶ 61,031 (2007).

transportation project,<sup>2</sup> remain unaltered by this Commission's actions on remand of *National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831 (D. C. Cir. 2006) ("*National Fuel*").

## BACKGROUND

### 1. Competitive Concerns Affecting The Alaska Natural Gas Pipeline

In Order Nos. 2005 and 2005-A, the Commission promulgated its first rules relating specifically to an Alaska natural gas transportation project. The rules were promulgated to satisfy a Congressional directive in the Alaska Natural Gas Pipeline Act, 15 U.S.C. § 720, *et seq.* ("ANGPA") that the Commission promulgate specific rules formalizing for an Alaska pipeline the Commission's policy that all new pipeline construction be preceded by a non-discriminatory "open season." The open season is the process through which potential shippers bid on capacity on the pipeline, as designed by the project sponsor. It culminates in a final project design and the execution of precedent agreements between the project sponsor and the prospective shippers for some or all of the design capacity of the project.

In enacting the ANGPA Congress was cognizant of the fact that virtually all of the natural gas that would be available for commitment to an Alaska pipeline in the initial open season would be the Prudhoe Bay/Point Thomson reserves, identified as a result of the development of the Prudhoe Bay/Point Thomson oil and gas fields. Over 90% of these reserves are owned by three producers – ExxonMobil Corporation, ConocoPhillips Company, and BP Exploration (Alaska) Inc. ("North Slope Producers") – the self-declared Alaska pipeline project sponsors. Therefore, to ensure that potential competitors of the North Slope Producers will have access to the pipeline, and, thereby, be positioned to move forward in their exploration programs, Congress required that the Commission's open season regulations "promote competition in the

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<sup>2</sup> *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, Order No. 2005, 110 FERC ¶ 61,095 (2005), *order on reh'g*, Order No. 2005-A, 111 FERC ¶ 61,332 (2005).

exploration, development, and production of Alaska natural gas" and, as to open seasons for capacity exceeding the initial capacity, that the regulations provide the opportunity for gas other than that from Prudhoe Bay and Point Thomson to be transported through the pipeline.

To develop the rules, the Commission compiled a substantial record, receiving both written comments and oral testimony from many parties, including the State of Alaska, certain Alaskan elected officials, Alaskan Natives, representatives of potential project sponsors – both the North Slope Producers and independent pipeline companies, potential shippers – including the North Slope Producers and explorers, representatives of state and federal agencies, and the general public.

A primary concern expressed by the State of Alaska, explorers, independent pipeline companies, and federal and state agency representatives, was the fact that the North Slope Producers intend to own and/or control the pipeline, and, were they to succeed in doing so, would have every incentive to enhance and solidify their dominance in the Alaska natural gas production market through their control over the Alaska natural gas pipeline. This expressed concern related not only to the open season process but also to the on-going operating conditions of the pipeline. As to open seasons, the primary concern expressed by these parties is the pipeline's ability to hold open seasons for expansion capacity under conditions that could tilt the balance toward their own production – either through timing, rates, or terms and conditions of service. If the North Slope Producers controlled the pipeline, the Commission was told, the risk would be significant that the North Slope Producers would give themselves preferential access to the pipeline and preferential terms and conditions of service in order to enhance their already dominant market position in Alaska.

These competitive concerns are not new, as noted in the Comments filed by the State of Alaska. Rather, they date back to the Alaska Natural Gas Transportation Act of 1976 (“ANGTA”),<sup>3</sup> in the very early stages of the effort to develop a natural gas pipeline to transport Alaska’s North Slope gas to markets in the lower 48 states. That the concerns remain today is clear from the record in Docket No. RM05-1, and ANGPA itself, where Congress directed the Commission to ensure that the rules governing access to the pipeline will “promote competition in the exploration, development, and production of Alaska natural gas.”<sup>4</sup>

The need to establish a level playing field for explorers, both in terms of obtaining capacity and in terms of receiving service, was a fundamental objective of the Commission’s rulemaking proceeding in Docket No. RM05-1. To address the competitive concerns, the Commission found it necessary to impose “strict requirements on all proposals, and *particularly on affiliate-owned projects*, with respect to the public disclosure of information.”<sup>5</sup> Concerned that even with the informational disclosure requirements there would still be an unacceptable risk that the producer and/or marketing affiliates of a project applicant would have an advantage over non-affiliates, the Commission specifically incorporated into its Order No. 2005 rules certain of the Standards of Conduct promulgated in Order Nos. 2004 *et seq.* to govern the relationship between the project sponsor and any of its marketing or energy affiliates. Moreover, faced with the prospect that the North Slope Producers, themselves, will be the project sponsors conducting the open seasons for capacity on the Alaska pipeline, the Commission required that any project applicant create a unit or division to conduct the open season, which unit or division “will be required to function independent of the *other non-regulated divisions* of the project applicant *as*

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<sup>3</sup> Pub. L. No. 94-586, 90 Stat. 2903 (1976).

<sup>4</sup> ANGPA § 103(e)(2)(B).

<sup>5</sup> *Id.*

well as the project applicant's Marketing and Energy Affiliates."<sup>6</sup> Through this rule, the Commission independently adopted and made applicable to project applicants conducting an open season for an Alaska natural gas transportation project the following regulations, initially promulgated in Order Nos. 2004 *et seq.*: separation of functions (18 C.F.R. §§ 358.4(a)(1), (3), (4), (5) and (6) and (b)(e)(3), (5) and (6) (2004)); information access (18 C.F.R. § 358.5(b) (2004)); prohibitions against discrimination (18 C.F.R. § 358.5(c)(5) (2004)) and discounts (18 C.F.R. § 358.4(d) (2004)).<sup>7</sup> The Commission's application of these regulations to an Alaska natural gas transportation project was not the subject of a rehearing request in Docket No. RM05-1 and was not the subject of the court appeal filed in that rulemaking docket.

## 2. The Standards of Conduct As They Relate To An Alaska Natural Gas Pipeline

The Commission's rulemaking adopting Standards of Conduct for transmission providers in Order Nos. 2004 *et seq.*, as it relates to interstate pipelines, had its genesis in the Standards of Conduct developed in Order No. 497, *et seq.*<sup>8</sup> These rules were intended to address the propensity of interstate natural gas pipelines to grant special preferences to their marketing or brokering affiliates over non-affiliate<sup>9</sup> The Alaska pipeline was not a focus of the rule. The Commission subsequently promulgated similar Standards of Conduct for electric transmission providers.<sup>10</sup> In an effort to develop one rule applicable to all transmission providers, gas or electric, the Commission synthesized and expanded the application of its Standards of Conduct

<sup>6</sup> Order No. 2005 at P 74.

<sup>7</sup> See Order No. 2005 at P 74.

<sup>8</sup> *Inquiry Into Alleged Anticompetitive Practices Related to Marketing Affiliates of Interstate Pipelines*, Order No. 497, FERC Stats. & Regs. Regulations Preambles 1986-1990 ¶ 30,820 (1988); *order on reh'g*, Order No. 497-A, FERC Stats. & Regs. Regulations Preambles 1986-1990 ¶ 30,868 (1989); *order extending sunset date*, Order No. 497-B, FERC Stats. & Regs. Regulations Preambles 1986-1990 ¶ 30,908 (1990); *order extending sunset date*, Order No. 487-C, FERC Stats. & Regs. Regulations Preambles 1991-1996 ¶ 30,934 (1991), *reh'g denied*, 58 FERC ¶ 61,139 (1992); *aff'd in part and remanded in part sub nom. Tenneco Gas v. FERC*, 969 F.2d 1187 (D.C. Cir. 1992).

<sup>9</sup> See Order No. 497 at ¶ 31,127; *Tenneco Gas*, 969 F.2d at 1194 (D.C. Cir. 1992)

<sup>10</sup> See *Open Access Same-Time Information System and Standards of Conduct*, Order 889, FERC Stats. & Regs. Regulations Preambles Jan. 1991- Jan. 1996 ¶ 31,035 (1996).

rules in Order Nos. 2004, *et seq.* to govern not only the relationship between transmission providers and their “Marketing Affiliates,” but also the relationship between transmission providers and their “Energy Affiliates.”<sup>11</sup> As relevant here, a “Marketing Affiliate” excludes sellers that sell gas solely from their own production or solely from their own gathering or processing facilities.<sup>12</sup> Therefore, with respect to an Alaska pipeline, the Standards of Conduct would not apply to the relationship between the pipeline and its producer affiliates if the rule were restricted to “Marketing” rather than “Energy” affiliates of the pipeline.

In *National Fuel*, the United States Court of Appeals District of Columbia Circuit vacated Order Nos. 2004, *et seq.* as applied to interstate pipelines, noting that while the court had affirmed the rules developed in Order Nos. 497, *et seq.* governing the relationship between interstate pipelines and their “Marketing Affiliates”<sup>13</sup> there was no record evidence in the Order No. 2004 proceeding supporting the extension of the restrictions to the pipeline’s “Energy Affiliates.”

As a result of the court’s decision in *National Fuel*, the Commission is proposing in this rulemaking to eliminate the restrictions that Order Nos. 2004 *et seq.* placed on the relationships between an interstate pipeline and its “Energy Affiliates” and to reinstate the Order Nos. 497, *et seq.* “Marketing Affiliate” rules. The proposed rule in this proceeding makes no distinction between the application of the “Marketing Affiliate” rules to interstate pipelines, in general, and the application of those rules to an Alaska natural gas transportation project, despite the Commission’s action in Order Nos. 2005 and 2005-A. As explained in greater detail below, it is

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<sup>11</sup> See *Standards of Conduct for Transmission Providers*, Order No. 2004, FERC Stats. & Regs., Regulations Preambles, 2001-2005 ¶ 31,155 (2003); *order on reh’g*, Order No. 2004-A, FERC Stats. & Regs., Regulations Preambles, 2001-2005 ¶ 31,161 (2004); *order on reh’g*, Order No. 2004-B, FERC Stats. & Regs., Regulations Preambles, 2001-2005 ¶ 31,166 (2003); *order on reh’g*, Order No. 2004-C, FERC Stats. & Regs., Regulations Preambles, 2001-2005 ¶ 31,172 (2004); *order on reh’g*, Order No. 2004-D, 110 FERC ¶ 61,320 (2005).

<sup>12</sup> See, proposed §§ 358.3(e)(3)(i) and (ii).

<sup>13</sup> *Tenneco Gas v. FERC*, 969 F.2d 1187 (D.C. Cir. 1992).

important that the Commission clarify that its proposed rulemaking in this docket does not impact the adoption of the specific regulations implementing the Standards of Conduct governing the relationship between an Alaska natural gas transportation project, its sponsors, and their Marketing and Energy Affiliates under Order Nos. 2005 and 2005-A.

### DISCUSSION

Anadarko fully agrees with and supports the State of Alaska's request that the Commission confirm that the regulations promulgated by Order Nos. 2005 and 2005-A remain intact, including the application of § 157.34(c)(18)-(21), §157.35(c) – (d) to an Alaska natural gas transportation project and its sponsors. Further, Anadarko supports the request by the State of Alaska that the Commission modify its regulations at § 158.1(e) to confirm that the Standards of Conduct govern the not only the relationship between an Alaska natural gas transportation project, its sponsors, and their Marketing Affiliates, but also the relationship between an Alaska natural gas transportation project, its sponsors, and their Energy Affiliates. It is also important that the Commission confirm that as to an Alaska natural gas pipeline, the Standards of Conduct apply in the pre-certification open season process, as provided in Order Nos. 2005 and 2005-A. In this regard, Anadarko respectfully submits that the *National Fuel* decision does not affect the Commission's regulations promulgated in Order Nos. 2005 and 2005-A.

At the heart of the court's decision in *National Fuel* is the proposition that vertical integration creates efficiencies and benefits for consumers, and, therefore, the Commission "cannot impede vertical integration between a pipeline and its affiliates without adequate justification."<sup>14</sup> This proposition derives from the D.C. Circuit's earlier analysis in *Tenneco*, where it found that "in a competitive market, the efficiencies of the pipeline-affiliate relationship

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<sup>14</sup> See *National Fuel Gas Supply Corp.*, 468 F.3d at 840 (citing *Tenneco Gas v. FERC*, 969 F.2d 1187, 1199 (D.C. Cir. 1992)).

should produce benefits for consumers.” The *National Fuel* court further commented that “advantages a pipeline gives its affiliate are improper only to the extent that they flow from the pipeline’s anti-competitive market power; otherwise, vertical integration produces permissible efficiencies that cannot by themselves be considered uses of monopoly power.”<sup>15</sup> Because the Commission did not have specific findings of affiliate abuse between a pipeline and its Energy Affiliates, the *National Fuel* court vacated Order No. 2004’s application of the Standards of Conduct to the relationship between a pipeline and its Energy Affiliates.

But, the rationale of *National Fuel* does not apply to an Alaska natural gas transportation project. Firstly, an Alaska natural gas transportation project will be a monopoly. Secondly, the North Slope Producers own over 90% of the natural gas reserves initially available for transportation through the pipeline. Thirdly, the North Slope Producers may well own or control, either themselves or through affiliates, the Alaska natural gas transportation project. Finally, Congress has recognized the unique competitive issues applicable to the development of Alaska natural gas and access to the pipeline by directing the Commission to promulgate regulations governing access to that pipeline that promote competition in the exploration, development and production of Alaska natural gas.

It can safely be said that the market for interstate pipeline capacity in Alaska is *not competitive*. It can also safely be said that the North Slope Producers’ control over the gas reserves that will anchor the project, and their resultant ability to influence the terms and conditions of access to the pipeline, create serious competitive concerns for explorers. These concerns take on added significance in the likely circumstance that the North Slope Producers will own or control the pipeline, either directly or through affiliates. The Commission

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<sup>15</sup> See *National Fuel Gas*, 468 F.3d at 840 (citing *Tenneco*, 969 F.2d at 1205)

recognized as much in Order No. 2005 when it stated: “the competitive conditions that are unique to such a project warrant special consideration and oversight.”<sup>16</sup>

This is not the natural gas market addressed by the D.C. Circuit in *National Fuel*. This is the Alaska natural gas market – a market with respect to which the Commission received considerable evidence during the rulemaking proceeding in Docket No. RM05-1, and which has been the subject of substantial competitive analyses since the 1970’s, during which time the United States Department of Justice (“DOJ”) conducted an extensive study into the anticompetitive issues related to an Alaska natural gas pipeline.<sup>17</sup> Even then, DOJ identified serious anticompetitive concerns associated with a producer-sponsored Alaska natural gas pipeline, concluding that “an ownership interest, or participation in any form in the transportation system, by producers of significant amounts of natural gas, or their subsidiaries or affiliates, should be prohibited.”<sup>18</sup> The DOJ Report discusses not only competition concerns at the very outset of the pipeline planning process, but also competition concerns after the initial construction, noting: “[W]e cannot say that the problem has been solved just because initial pipeline capacity seems adequate (indeed, even if initial capacity strains technical construction and operating capabilities). For the case we are concerned with includes future efforts by other producers to enter the Alaskan field and consequential needs for expanded pipeline capacity . . . . Producer-ownership of the pipeline creates incentives to deny or impede such future capacity expansion.”<sup>19</sup>

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<sup>16</sup> See Order No. 2005 at P 3.

<sup>17</sup> See Report of the Attorney General Pursuant to the Alaska Natural Gas Transportation Act of 1976 (July 1977) (“Attorney General Report”).

<sup>18</sup> *Id.* at p. 80; see also *id.* at pp. v, 29, 30.

<sup>19</sup> *Id.* at p. 39.

The competitive environment in Alaska has not improved since the time of the DOJ Report. In fact, if anything, it has worsened, with the North Slope Producers now owning or controlling over 90% of the discovered natural gas reserves on the North Slope. Faced with these competition concerns and Congressional directives, as well as the extensive record in the RM05-1 rulemaking proceeding, the Commission's decision to apply the Standards of Conduct to the Energy Affiliates, as well as the Marketing Affiliates, of an Alaska natural gas transportation project, and to do so from the outset, is fully justified. Thus, even if the Commission were to have to justify its application of those rules to an Alaska natural gas pipeline project, it could clearly do so.

But, *National Fuel* is simply inapposite. The risk of anti-competitive conduct relating to access to an Alaska natural gas pipeline controlled by the North Slope Producers has been fully recognized by Congress and by the Commission. Here, the threat of a producer-owned or controlled pipeline enabling its producer affiliates to secure capacity under terms and conditions not generally available to their non-affiliated competitors or otherwise to benefit from non-public information or knowledge about the operations and plans of the transmission system is readily apparent. The threat, here, like in *Tennaco*, stems directly from the pipeline's monopoly position and the North Slope Producers' control over Alaska's immediately available reserves. The facts are clearly different from those in *National Fuel*.

Finally, as explained by the State of Alaska, and as noted above, the Commission's regulations applying the Energy Affiliate rules to an Alaska natural gas transportation project were not challenged by any party to the proceeding and, therefore, are final and non-appealable. Accordingly, the Commission should confirm that these regulations remain in full force and effect, notwithstanding *National Fuel*.

CONCLUSION

For the reasons set forth above, Anadarko supports the Comments filed by the State of Alaska and urges the Commission to clarify that its open season regulations promulgated in Order Nos. 2005 and 2005-A remain in full force and effect and are not in any way affected by the Commission's actions in this rulemaking proceeding. In addition, Anadarko supports Commission adoption of the suggested clarification to its regulations, as requested by the State of Alaska.

Respectfully submitted,

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Paper on Alaska Gas Line Issues

Relative To the Alaska Natural Gas Pipeline Act of 2001

August 2001

Note: This paper was prepared before Congress enacted legislation relative to the Alaska Gas Line and before FERC adopted its open season regulations. Some issues raised in this paper have been addressed. It is being distributed because much of the background is still relevant in June of 2006.

Rationale for Modifications to  
Alaska Natural Gas Pipeline Act of 2001

**BACKGROUND**

The natural gas pipeline required to deliver Alaskan North Slope ("ANS") natural gas reserves to Western Canada and the U.S. Lower 48 States is a massive undertaking. It is anticipated that an 1,800 mile-large diameter pipeline will need to be constructed to Alberta, Canada. This ANS gas pipeline is expected to have an initial capacity of about 4 Bcfd.

In addition, it is assumed that the existing pipelines emanating out of Western Canada to market centers in Eastern Canada, the U.S. Midwest, and U.S. Pacific Coast will not have sufficient excess capacity to transport all of this new Arctic gas supply to market centers. Therefore, it is anticipated that another 1,800 miles of new pipeline, of somewhat smaller diameter will have to be installed to transport ANS gas to markets. Including the cost of a gas conditioning plant and the anticipated need for new pipeline facilities all the way to U.S. market centers (e.g. Chicago), the project sponsors (Exxon, BP, and Phillips) have been quoting total costs for this ANS gas pipeline project in the \$15 - \$20 billion range.

The 1,800-mile ANS to Alberta portion of the pipeline alone will be the largest, most expensive pipeline project ever undertaken. Cost estimates for this portion of the project, excluding ancillary services such as gas conditioning, run in the \$7 - \$10 billion range.

The ANS reserves anchoring the proposed pipeline are predominately held by three multinational oil companies, BP, Exxon-Mobil, and Phillips. These three majors, own more than 98% of the gas reserves in the giant Prudhoe Bay Unit and nearly 80% of the gas reserves in the second largest North Slope gas accumulation, Point Thomson Unit. Together, these two fields represent more than 30 Tcf of the 35 Tcf of proved ANS gas reserves. In addition, BP, Exxon-Mobil, and Phillips own the overwhelming majority of the remaining ~ 5 Tcf of proven gas reserves attributable to the other North Slope oil and gas fields. On a volume-weighted basis, these three companies control more than 90% of the proven North Slope gas reserves.

This dominant market position and power held BP, Exxon-Mobil, and Phillips is a competitive concern and threat to other natural gas explorers in northern Alaska. By holding practically all of the ANS gas reserves, these three companies also control all of the critical facets of the pipeline required to monetize the vast North Slope natural gas reserves and even far greater gas resources. The proven natural gas reserves on the North Slope are equivalent to nearly 25% of the proven natural gas reserves in the U.S. Lower 48 states.

Exxon-Mobil, BP, and Phillips have undertaken a detailed, \$100 million feasibility study to determine the economic feasibility and routing for the required ANS gas pipeline. The feasibility study is scheduled to be completed by years' end.

## CONCERNS

### Anti-Competitive / Market Concentration Issues

With more than 90% of the natural gas reserves concentrated among three companies, these companies wield unnatural and de facto monopolistic market powers. These three companies will control all of the commercial issues surrounding an ANS gas pipeline and are poised to exercise their market powers to the detriment of all competing ANS gas explorers.

Access to the ANS gas pipeline is of paramount importance. Without access to the pipeline, natural gas explorers' gas discoveries will be of no value. There is a very real fear that Exxon-Mobil, BP, and Phillips will secure all of the pipeline capacity. Those shut-out of the pipeline initially will have to either (1) await spare capacity after initial fields have declined; (2) seek release capacity from the shippers that secured the initial capacity; or (3) sell their discoveries at distressed prices to the holders of the pipeline capacity.

Each of these options is either unrealistic or extremely onerous to the explorers. In the first case, gas reserves and expected production rates from the Prudhoe Bay and Point Thomson Units will likely keep a 4 Bcf/d pipeline at capacity for nearly twenty (20) years. In addition, BP and Phillips each hold huge acreage positions from which they are expected to be able to replace Prudhoe Bay and Point Thomson production declines. Therefore, if the three dominate gas reserve holders secure all of the initial pipeline capacity, it is likely that they will be able to keep the pipeline full with their own equity production for decades.

Relying upon released capacity from the shippers securing capacity on the pipeline is also an onerous option due to the provisions of FERC Order 637. Under Order 637, the shippers releasing capacity to other are not bound by the maximum tariff imposed by the FERC at the outset of the pipeline capacity contractual process. Therefore, holders of the capacity can either release capacity to the explorers at whatever tariffs the market will bear, or similarly offer to buy the explorers' gas at distressed prices.

Explorers need look no further than the recent past in Western Canada for an example of how holders of transportation capacity can drive wellhead prices to severely low levels during periods that transportation capacity is in short supply. During the year 1996, Western Canadian gas prices averaged \$1.03 per MMBtu, while U.S. gas prices averaged \$2.51 per MMBtu (Henry Hub, Louisiana). The Western Canada prices should have averaged more like \$1.80 per MMBtu, based solely upon transportation cost differentials. However, pipeline capacity out of Western Canada was constrained and as a result,

Western Canadian gas prices were more than 40% lower than they should have been. Parties holding the scarce pipeline capacity were the segment of the industry that reaped the nearly \$0.75 per MMBtu windfall. This windfall represents 70 – 75% of the wellhead prices realized to find, develop, and produce the natural gas.

Lastly, if Exxon-Mobil, Phillips, and BP hold all or nearly all of the capacity on the pipeline, other petroleum companies will be at their mercy in order to secure transportation of all new natural gas discoveries. The big three producers could deny the purchase or transport of their competitors' natural gas with the intention of driving them out of business and/or forcing the distressed sale of their properties.

Manipulation of the pipeline access and tariffs in Alaska by the major players to the detriment of the second tier companies has a storied history in Alaska. Companies that exited Alaskan North Slope exploration and production in the 1980's and 1990's, such as Conoco, have been very open and vocal that they were squeezed out of their North Slope properties due to unfair manipulation of the Trans-Alaskan Oil Pipeline (TAPS).

Just last week (August 9, 2001), the *Calgary Herald* carried a story about the Arctic gas pipeline situation in which Conoco's CEO Archie Dunham cited anti-competitive operation of TAPS for his vehement insistence that Conoco have an ownership in any Arctic gas pipeline serving the Canadian Mackenzie Delta region. The article stated in part, "Dunham defended his hard-line position by citing Conoco's woes in Alaska in the early 1990's when it felt it couldn't get full value for its resources because it did not own a stake in the Trans-Alaska pipeline. 'The owners of the pipeline, by adjusting tariffs on the pipeline, could really diminish the value of producing properties and that's not going to happen again,' pledged the CEO of the Houston-based company."

The remote location of the Alaskan North Slope, for all intents and purposes, creates a natural monopoly for the pipeline owners and capacity holders. The 1,800 miles of pipeline and \$7 - \$10 billion of capital outlays to build the pipeline's initial pipeline leg to Alberta, Canada represent very real barriers to entry. In all likelihood, there will never be another gas pipeline built from the North Slope to Western Canada and the Lower 48 states. In order to build another pipeline, another 30 Tcf of natural gas reserves will have to be discovered and shut-in awaiting pipeline outlet. It is extremely unlikely that petroleum companies will spend the money to prove-up another 30 Tcf to justify a second, competing pipeline. It has taken more than 20 years for there to be sufficient economic inertia to drive the probable construction of the first such pipeline.

In all probability, the ANS gas pipeline project that is currently being controlled by BP, Phillips, and Exxon-Mobil, will be the only gas pipeline built to the Lower 48 states from the ANS. Therefore, the dominant producers, BP, Exxon-Mobil, and Phillips, are poised to control construction of the pipeline, as well as the throughput capacity. BP, Exxon-Mobil, and Phillips will enjoy monopolistic power over the North Slope gas pipeline and by extension hold a monopoly over the exploration and production of Alaskan North Slope natural gas.

### Non-Discriminatory, Open-Access Is a Misnomer

There is a common misconception that, as an interstate natural gas pipeline that falls under the jurisdiction of the Federal Energy Regulatory Commission ("FERC"), access to the pipeline by all comers will not be an issue. The FERC regulates interstate pipelines under a non-discriminatory, open-access mandate. However, under the circumstances of this pipeline, non-discriminatory, open-access statutes are of dubious value and comfort to the exploration and production companies other than Phillips, Exxon-Mobil, and BP.

FERC regulated natural gas pipelines are generally known as "contract carriage" pipelines. Under such a regime, the parties desiring transportation service ("shippers") contract for capacity to the pipeline. In areas with little or no direct competition, most, if not all of the capacity is contracted for on a firm basis for extended periods, such as 10 or 20 years. Once the capacity has been fully subscribed, only interruptible or capacity released, or sublet, by such firm shippers is available to parties unable to secure firm transportation services at the outset. As discussed above, if the holders of the firm capacity are direct competitors of the parties desiring new pipeline capacity, the firm capacity holders are likely to take economic advantage by charging excessive tariffs for its released capacity. In other words, potential shippers that fail to secure capacity on the pipeline under firm contracts at the outset, face having no access to capacity, or access at unattractive and even detrimental tariffs.

This "contract carriage" system of capacity allocation differs greatly from the standard for allocation of capacity on oil pipelines. Oil pipelines are generally structured as "common carriers". Capacity on a common carrier pipeline is always allocated on a pro rata basis. If shippers, both existing and new, tender more oil to the pipeline than there is capacity, then all shippers, both existing and new, are prorated such that each shipper is allocated a proportionate share of the pipeline capacity. Therefore, failure to secure transportation capacity at the outset of an oil pipeline's operation is not nearly as onerous as the situation related to securing capacity on a natural gas pipeline. New comers are afforded a pro rata share of the pipeline capacity regardless whether they had achieved capacity at any prior point.

With respect to the allocation of capacity on a "contract carriage" natural gas pipeline, the capacity is generally bid for during an "open season" process. The open season is a relatively short, typically 30-day, period for which bids are taken. If all of the capacity is subscribed for on a firm basis during the open season, no capacity may be available on the pipeline for a very long period, up to 20 years or more.

Therefore, the "non-discriminatory, open access" process is not synonymous with free access to the pipeline at any point in time. In fact, in a pipeline such as the Alaskan natural gas pipeline, access to the pipeline will likely be limited to those companies that successfully bid for capacity during the 30-day open season. Thereafter, for up to 20 years or longer, all other interested shippers will be either at the mercy of those securing capacity in the open season, or potentially completely shutout.

### Open Season Process and Oversight

Generally, the open season process is either lightly regulated or not regulated at all. One of our concerns is that the pipeline sponsors will keep all potential shippers and other stakeholders in the dark as to the operational and commercial characteristics for the pipeline until announcing the open season. By controlling the information disclosed and the timing thereof, the project sponsors can limit the number and effectiveness of those shippers interested in bidding for pipeline capacity in the open season. This concern is exacerbated by the fact that the project sponsors are the major reserves holders on the Alaskan North Slope and can use this "control" of information to their competitive advantage over competing exploration and production companies.

Our proposed resolution of this potential anti-competitive situation is to require at least a 90-day notice period prior to the start of the open season and further require disclosure of critical information needed to make an informed and competitive bid for capacity. The type of information that we seek in our "pre-open season disclosure" includes: specifications of the proposed pipeline such as route, diameter of pipe, operating pressures, pipeline capacity and the amount available for transportation, gas quality specifications, anticipated tariff rates, delivery and receipt points, tariff structure, bidding procedures in the open season, methodology utilized in determining capacity awards, allocation procedures for capacity in the event of receiving bids of equal value and the inclusion of the precedent agreement. This detailed document should provide sufficient information to allow an interested party to make an informed, competitive bid for capacity on the proposed pipeline.

Another major concern regarding the securing of pipeline capacity is the potential for the project sponsors to "hold-back" capacity from the open season process. A number of recent FERC regulated natural gas pipelines have been implemented allowing sponsor holdbacks of up to 50% of the ultimate capacity. Under such a scenario, not only will non-owners desiring capacity be at a major knowledge disadvantage in competing for capacity at the open season, as much as one-half of the pipeline capacity may be withheld for the project sponsors prior to the advent of the open season. Again, given the fact that this pipeline is likely to be the only gas pipeline constructed from the Alaskan North Slope to the Lower 48 states, none of the capacity should be permitted to be withheld from the open season.

Lastly, the determination process for awarding of winning bids during the open season should be set out in the pre-open season announcement. Potential shippers that are not pipeline owners must be afforded an even playing field in the competition for finite transportation capacity. All bids submitted for the maximum allowable tariff and for the full contract term should be allocated a full pro rata share of the pipeline capacity, up to the capacity bid for by such shippers. For this purpose, the maximum contract term used in assessing the bids should be capped at some reasonable term, such as 10 or 20 years. Again, producer owners of the pipeline will have an unfair economic advantage in bidding longer terms, if a reasonable truncation is not imposed.

## Tariff Issues

There are a number of components within the tariff structure that could be crafted by the pipeline sponsors that we would favor themselves at the expense of their competitors. One of the major concerns is the amortization period used in the tariff calculation for the recovery and return on capital investments. If a relatively short amortization period were permitted, the resultant tariff would be excessively high. If high pipeline tariff would reduce the netback gas price received by the gas producers. Given the remote location and seasonal drilling limitations associated with the Alaskan North Slope, it is expected that new natural gas developments will be quite expensive. If the pipeline tariff is too high, the wellhead price could be driven to unattractive or even uneconomic levels.

If the major North Slope producers are also major equity owners in the pipeline, they will be insulated from the adverse impact of such high tariffs and will have preferentially better project economics than non-pipeline owner petroleum companies. This is precisely the anti-competitive situation that Conoco's Mr. Dunham referred to with respect to the operation of the TAPS oil pipeline and what he stridently intends to avoid in the Canadian Mckenzie Delta region.

Another major issue is to ensure that the pipeline tariff is "unbundled" as to ancillary services. Such unbundling has been FERC policy for the past decade. However, there is concern that the producer sponsors intend to include the costs of a gas conditioning plant in the pipeline tariff. The subject treating plant would be used to extract CO<sub>2</sub> from the Prudhoe Bay Unit gas prior to injection into the pipeline. CO<sub>2</sub> is a corrosive gas that must be reduced to minimal levels prior to delivery into the pipeline. Cost estimates for the CO<sub>2</sub> plant have been estimated at \$1 billion or more. On a per unit basis, the cost of CO<sub>2</sub> conditioning can exceed \$0.50 per MMBtu.

It would be inequitable and anti-competitive to include the CO<sub>2</sub> conditioning plant, or any other ancillary services in the pipeline tariff. By including such costs in the tariff, the producer pipeline sponsors would effectively have the largest natural gas field in North America be subsidized by the producers of other smaller, less profitable gas fields. Many new ANS gas fields are expected to be of pipeline quality as produced and therefore not require CO<sub>2</sub> conditioning.

While others, such as those expected to be found south of Prudhoe Bay in the Brooks Range, will likely interconnect with the pipeline downstream of the Prudhoe Bay area CO<sub>2</sub> conditioning plant and will not derive any benefit from such a Prudhoe Bay sited plant. To exacerbate the situation, fields connected downstream may have to install their own CO<sub>2</sub> conditioning plants at their sole cost and expense, while subsidizing the Prudhoe Bay CO<sub>2</sub> conditioning plant.

There are a number of other aspects, of the tariff process that could be structured to the benefit of the producer pipeline owners. Even fairly innocuous provisions such as quality specifications could be structured in an anti-competitive manner in an attempt to manipulate and monopolize the limited pipeline capacity.

For instance, the sponsors could set the minimum Btu content at higher than normal levels in order to deny capacity to leaner natural gas sources.

Another concern along the same vein is the potential for the sponsors to require shippers to forfeit their rights to natural gas liquids (NGLs) entrained in their gas stream. This is purported to be the case on the recently completed Alliance Pipeline. Under such a scenario, the pipeline sponsors would reap a windfall processing the shippers gas for the profitable extraction of NGLs.

In addition, there is concern that the sponsors may compute the tariff rates on a volumetric (Mcf) basis rather than on a heating value (MMBtu) basis. Natural gas is now bought and sold on an MMBtu basis, computing the tariff on an Mcf basis would result in leaner gas subsidizing richer gas streams.

One final concern is to ensure that new receipt and delivery points are afforded unfettered connection to the pipeline. If new natural gas fields are discovered along the pipeline route, they should be afforded interconnection to the pipeline so long as capacity on the pipeline exists. Conversely, if new markets develop along the pipeline route, parties should be afforded new delivery points to serve these markets. Again, under the assumption of a single Alaskan gas pipeline to the Lower 48 states, this pipeline will enjoy a natural monopoly and as such should be required to accommodate all new receipt and delivery point requests.

Along these same lines, the tariffs assessed these intermediate receipt and delivery points should be computed on a mileage based manner taking into consideration the fact that these new points do not require use of the full pipeline distance and should therefore pay commensurately lower tariff rates.

### Pipeline Expansions

The FERC does not currently hold the regulatory authority to order pipeline expansions. The modifications we have made to the proposed Senate Bill provide that the FERC be afforded the authority to require expansion of the pipeline when credible shippers are willing to enter into long-term transportation arrangements needed to underpin such an expansion.

We are concerned that the producer pipeline sponsors could deny or delay pipeline expansions to serve their competitive aspirations rather than operating the pipeline as a prudent pipeline owner. That is, a prudent pipeline owner would expand its pipeline if viable economic opportunity presented its self. However, the pipeline sponsors in this case may intentionally delay or withhold expansion in order to be better postured to secure the expansion capacity for its own use.

A case in point, would be a scenario where a third-party exploration company makes a major discovery and petitions the pipeline for an expansion and is willing to commit to long-term transportation contracts to justify the expansion costs. If this situation were to occur a few years before the Prudhoe Bay Unit owners, BP, Exxon-Mobil, and Phillips, intended to maximize gas production from their field, they may delay the requested expansion so that they could be better positioned to secure the pipeline capacity for themselves at expansion.

This access to and timing of pipeline expansions is a critical issue inasmuch as there are physical limitations to how much the pipeline can be expanded. Current thinking is that the maximum the pipeline can be expanded beyond the expected initial capacity is only an incremental 50%.

**Conoco dismisses native demands: CEO insists on pipeline ownership**

Calgary Herald  
Thursday, August 9, 2001  
Page: D1 / FRONT  
Section: Business  
Byline: Stephen Ewart  
Column: The Politics of Energy  
Source: Calgary Herald

Archie Dunham, the chief executive of Conoco Inc., has a message for aboriginal groups demanding 100 per cent ownership of a proposed Mackenzie Valley natural gas pipeline: No.

Dunham, who gained control of 1.2 trillion cubic feet of gas in the Canadian Arctic with Conoco's blockbuster takeover of Gulf Canada Resources Ltd., said his company must have a stake in the pipeline.

"We're going to have an ownership of the pipeline . . . we have to have it," he said Wednesday.

Dunham, who was in Calgary for the first time since signing the \$9.8-billion takeover of Gulf Canada in May, spelled out the position while asserting that Conoco will be a much more active proponent of speedy development of Canadian Arctic gas than Gulf had been.

"We need to bring Mackenzie Delta gas to market a lot quicker than what we were originally thinking," he said, listing it as the top priority for new Conoco Canada Ltd. president Henry Sykes.

"If we could do it in four to six years, that would be good."

Dunham was here to welcome Gulf's 1,200 employees to Conoco with the completion of the largest takeover in Canadian oilpatch history. He was also able to report second quarter earnings had jumped 37 per cent from last year to \$119 million.

But Arctic gas was the primary topic of his meeting with the media. The Mackenzie Delta producers' group, led by Imperial Oil Ltd., proposes taking a two-thirds ownership stake in the line, but is facing twin problems -- demanding unanimous aboriginal support before proceeding with the \$3-billion project although some native groups are insisting on 100 per cent ownership.

Winter Lennie, a member of the Sahtu First Nation seeking complete native ownership for the pipeline, wasn't alarmed by the comments from the newest player in the renewed effort to develop the massive northern resource.

"It's a only a bargaining position," said Lennie, president of Western Arctic Energy Corp. in Norman Wells, N.W.T.

\* Dunham defended his hard-line position by citing Conoco's woes in Alaska in the early 1990s when it felt it couldn't get full value for its resources because it did not own a stake in the Trans-Alaska pipeline.

\* "The owners of the pipeline, by adjusting the tariffs on the pipeline, could really diminish the value of the producing properties and that's not going to happen again," pledged the CEO of the Houston-based company.

Intense demand for gas has renewed interest in developing the Mackenzie Delta after a two-decade moratorium was imposed by a federal commission amid aboriginal land claim battles in the 1970s.

Another gas megaproject has been proposed for Alaska's Prudhoe Bay and there are concerns from the likes of N.W.T. Premier Stephen Kakul that development of the larger U.S. resource could strand Mackenzie Delta gas for a decade or more.

Dunham said the companies behind the two Arctic projects -- including ExxonMobil Corp. BP PLC and the Canadian affiliate of the Royal Dutch/Shell Group -- must work together to develop the massive strategic resources.

He was also adamant the Mackenzie gas must be part of the plan.

"I can not imagine a politician in Canada agreeing to a pipeline route that did not include Mackenzie Delta gas," said Dunham, who urged Ottawa to throw its support to the Canadian development.

Alaskan producers are studying a pipeline route through the state that would cross into Canada en route to markets in the lower 48 states.

He also cited the potential conflict of interest of some resource owners in Canada who have resources in Alaska -- most notably ExxonMobil, which is the majority owner of Imperial -- to "chase in" one project over another.

Spokesman for Imperial and ExxonMobil dismissed the suggestion and noted the merits of both projects and any "synergies" are being studied.

Imperial spokesman Plus Roliholser also warned it would be difficult to push ahead the timetable for Mackenzie Delta development noting "the political and social-economic challenges are just as complicated or more as the technical side."

SHELL

Testimony on April 27, 2007, to the Sen. Finance Committee, Alaska  
State Legislature on SB 104, AK Gas Inducement Act, 'AGIA'.

Mr. Chairman, and members of the committee, my name is Cam Toohey, Alaska Manager of Communications and Government Relations with Shell Exploration and Production Company.

I appreciate the opportunity to provide Shell comments in support of SB 104, Governor Palin's Alaska Gas Inducement Act "AGIA" legislation.

Last year, Shell submitted formal comments on the North Slope gas pipeline proposal developed by the Murkowski Administration. That letter has been provided to the committee. I am going to highlight a couple of points discussed in that letter that I believe are relevant as you consider this legislation.

Shell supports development of a North Slope gas pipeline and believes it is important to the continued economic health of the State of Alaska and the Nation.

While Shell currently does not have material proven gas reserves to commit to a North Slope pipeline Project, Shell has made a significant investment in the State with the specific objective of aggressively exploring for and, where economically feasible, developing oil and gas reserves.

The certainty of construction of a North Slope gas pipeline is an important factor in Shell's planning and future investment decisions in the State.

Of importance to Shell is capacity access and expansion and as we stated last year,.....

### Capacity Access and Expansion

Any North Slope gas pipeline Project should be structured to ensure reasonable access to pipeline capacity by new explorers and non-owner shippers.

In addition, it would be prudent to design and permit the Project in anticipation of the future expansion of the pipeline, especially with respect to establishing adequate right-of-way width and environmental assessment that paves the way for future incremental compression facilities, pipeline looping, and/or a second parallel pipeline.

The Project structure should provide reasonable terms for accomplishing future expansion of the line, including a presumption for rolled-in rates and mechanisms for requiring and advancing the timely completion of expansions.

Given the vast reserve potential within the State, the pipeline should be designed to provide a minimum expansion capacity of 6 bcf/d.

*Shell believes AGIA addresses these aspects very well.*

Another important element of a North Slope pipeline identified in 2006 was that .....

### Terms of Service

The Project should provide fair and reasonable terms of service for new explorers and non-owner shippers.

The terms of service, particularly transportation rates, have a critical bearing on whether North Slope development Projects are economic and competitive with other global opportunities.

Project construction costs will be the principal driver of the future rate for shipping gas on the pipeline system, and it is important that the State take steps to ensure that construction is completed in the most cost-effective and timely manner to ensure the lowest possible rate.

These concerns are not simply a matter of Shell's economic interest. For the State, as the royalty owner, the terms of service are vitally important because increases in pipeline project costs will be passed on to shippers in the form of higher transportation rates, and higher transportation rates will be detrimental to the development of new reserves and will decrease the netback value of the State's royalty gas.

*Shell believes that these issues are well incorporated in AGIA.*

#### FERC Regulation

*Shell also believes it is important that* All sections of the pipeline traversing the United States should be subject to the regulatory oversight of the Federal Energy Regulatory Commission ("FERC").

FERC oversight is necessary to ensure open access, fair and reasonable terms of service, and non-discriminatory behavior.

FERC oversight will also provide all parties an impartial forum to seek redress of grievances.

Should FERC decline regulatory oversight of certain components of the Project, then those facilities should be regulated under the jurisdiction of the Regulatory Commission of Alaska.

In closing;

- Shell applauds the effort of the Palin Administration to advance the gas line project.
- Shell fully supports the Administration in their efforts to include all interested parties in the gas line discussions as this will impact the future of all involved for generations to come.
- Shell believes development of a North Slope gas pipeline is critical to the continued economic health of the State of Alaska and the Nation.
- The certainty of construction of a North Slope gas pipeline is an important factor in Shell's planning for its current holdings in the State, as well as its decision-making regarding Shell's future investment.
- Shell believes it is critically important to future explorers that they have access to the gas pipeline and the line must be expandable.
- The project should provide fair and reasonable terms of service for new explorers and non-owner shippers, which will benefit the State of Alaska.

Thank you for the opportunity to present this morning in support of AGIA.

I would be happy to take any questions from the committee and provide written responses.



# Shell Exploration & Production

## Shell Energy Resources Company

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July 24, 2006

The Honorable William Corbus  
Commissioner, Alaska Department of Revenue  
P.O. Box 110430  
Juneau, Alaska 99811-0430

RE: Alaska Stranded Gas Fiscal Contract Between the State of Alaska and BP Exploration (Alaska) Inc., ConocoPhillips Alaska, Inc., and ExxonMobil Alaska Production Inc. ("Fiscal Contract") / Preliminary Findings and Determination ("Preliminary Findings")

Dear Commissioner Corbus:

Shell supports development of a North Slope gas pipeline as important to the continued economic health of the State of Alaska and the Nation. While Shell currently does not have material proven gas reserves to commit to a North Slope pipeline Project, Shell has made a significant investment in the State with the specific objective of aggressively exploring for and, where economically feasible, developing oil and gas reserves. The certainty of construction of a North Slope gas pipeline is an important factor in Shell's planning and decisions regarding future investment in the State, and Shell applauds the effort of the Administration to advance this important Project.

Several months ago, the Governor outlined six principles guiding the Administration's negotiation of an agreement for the construction of a North Slope gas pipeline with the current North Slope producers. Shell's comments with respect to the proposed Fiscal Contract and Preliminary Findings are primarily focused on two of those six principles: Principle No. 3, "Future explorers must have access to the gas pipeline"; and Principle No. 4, "The gas pipeline must be expandable."

Given the monopoly nature of the proposed North Slope pipeline system, certain modifications to the proposed Fiscal Contract and Preliminary Findings are needed to bolster the principles articulated by the Administration, particularly with respect to access and expansion. Below are Shell's preliminary comments on these and several other important aspects of this Project. At this time, Shell's comments are necessarily general in nature as critical components of the Project are, as yet, not available for public review, including, for example, the LLC agreement, the construction management agreement, the pipeline operating agreement and, most importantly, the pipeline Tariff General Terms & Conditions of Service. We assume that these documents are currently being negotiated and may not be available for public review for some time.

### Capacity Access and Expansion

Any North Slope gas pipeline Project should be structured to ensure reasonable access to pipeline capacity by new explorers and non-owner shippers. In addition, it would be prudent to design and permit the Project in anticipation of the future expansion of the pipeline, especially with respect to establishing adequate right-of-way width and environmental assessment that paves the way for future incremental compression facilities, pipeline looping, and/or a second parallel pipeline. The Project structure should provide reasonable terms for accomplishing future expansion of the line, including a presumption for rolled-in rates and mechanisms for requiring and advancing the timely completion of expansions. Given the vast reserve potential within the State, the pipeline should be designed to provide a minimum expansion capacity of 6 bcf/d.

### FERC Regulation

All sections of the pipeline traversing the territory of the United States should be subject to the regulatory oversight of the Federal Energy Regulatory Commission ("FERC"), including the Point Thomson transmission line. FERC oversight is necessary to ensure open access, fair and reasonable terms of service, and non-discriminatory behavior. FERC oversight will also provide all parties an impartial forum to seek redress of grievances. FERC regulation should not be prospectively limited or conditioned in any contract or other agreement with the State of Alaska. Should FERC decline regulatory oversight of certain components of the Project, then those facilities should be regulated under the jurisdiction of the Regulatory Commission of Alaska ("RCA").

### Terms of Service

The Project should provide fair and reasonable terms of service for new explorers and non-owner shippers. The terms of service, particularly transportation rates, have a critical bearing on whether North Slope development Projects are economic and competitive with other global opportunities. Project construction costs will be the principal driver of the future rate for shipping gas on the pipeline system, and it is important that the State take steps to ensure that construction is completed in the most cost-effective and timely manner to ensure the lowest possible rate. This will require prudent construction management by an entity that has the capabilities and resources to manage a project of this magnitude and an incentive to manage costs.

These concerns are not simply a matter of Shell's economic interest. For the State, as the royalty owner, the terms of service are vitally important because increases in pipeline project costs will be passed on to shippers in the form of higher transportation rates, and higher transportation rates will be detrimental to the development of new reserves and will decrease the netback value of the State's royalty gas.

### Upstream Facilities

For the Project to succeed in stimulating new investment, new explorers need access to existing and newly constructed upstream facilities that serve to deliver gas to the Project. Mechanisms must exist for new explorers to access these facilities on reasonable and fair terms preventing duplication of facilities to minimize the impact on the environment, local communities and future development costs.

In addition, the Project description should clearly include the transmission line from Point Thomson to the gas treatment plant. Similarly, future upstream transmission lines that might be developed, such as any NPRA feeder lines, should be deemed part of the Project and subject to FERC regulation.

State Capacity

If the State assumes an ownership interest in the Project, the State should have the power and discretion to broker its capacity to third-party shippers. Such authority should extend to both the gas treatment plant and pipeline capacity. Brokering of capacity is a very successful and active program on US pipelines ever since FERC established capacity release rules as part of Order 436 in 1992.

Shell applauds the Administration's efforts to date to advance a North Slope gas pipeline Project. However, Shell believes that the proposed Fiscal Contract can be improved to protect the interests of new explorers and, at the same time, better promote the interests of the State of Alaska in encouraging new development. Shell looks forward to working with the State of Alaska as this Project becomes more fully developed and as remaining Project components are introduced. Shell representatives are available to discuss Shell's views with you, or others in the Administration or Legislature, upon request.

If you have any questions or followup, please contact Cam Toohey with our Alaska office at 907-770-3700.

Sincerely,



BP

4/28/07

bp



David Van Tuyl

Gas Commercialization Team Lead  
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# **Alaska Natural Gas Pipeline Project**

## **Testimony on AGIA**

### **Senate Finance Committee**

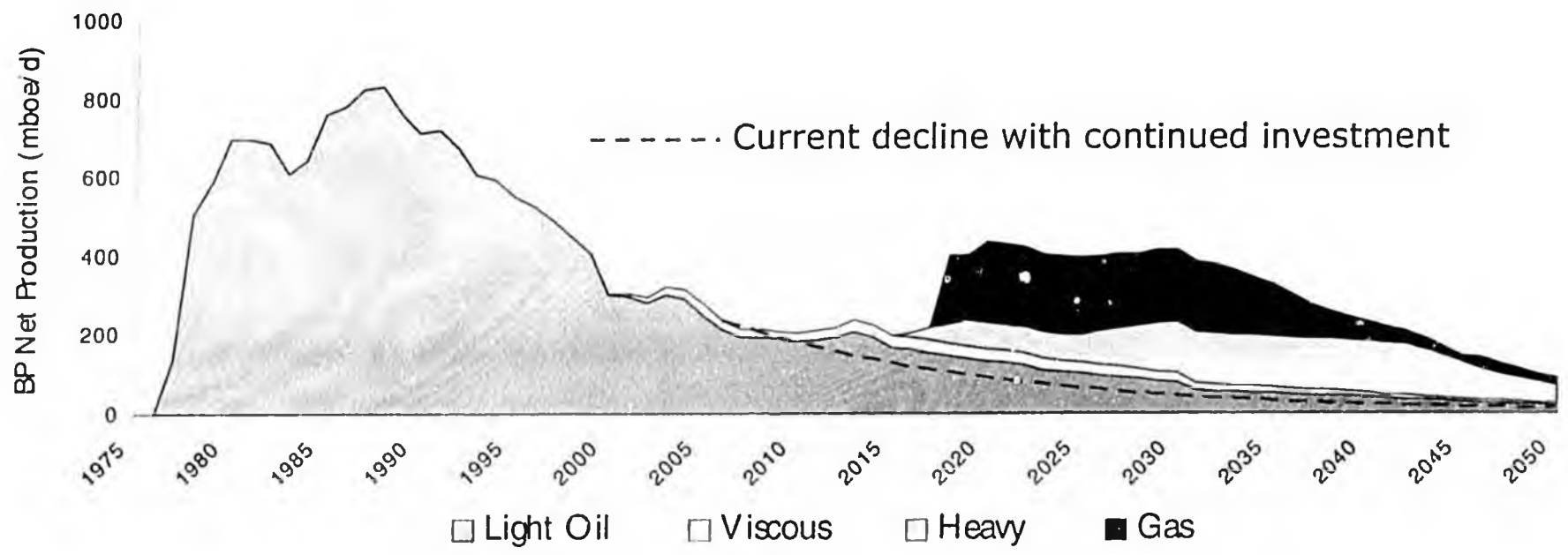
April 28, 2007





# An Opportunity...and a Challenge

- BP wants and needs a successful gas pipeline



- Project remains commercially challenged

# BP Disagrees with Administration's Economics



- Project is not "wildly profitable"
  - Can't separate upstream economics from midstream commitments
  - Economics must be based on the complete project
  
- Firm transportation commitments must be accounted for in project economics
  - Upstream pays for the midstream
  - Without FT there is no project
  
- Long-term cash generation is highly important
  - Cash flow well beyond 10 years remains vital
  
- Need common understanding of project to determine best way forward

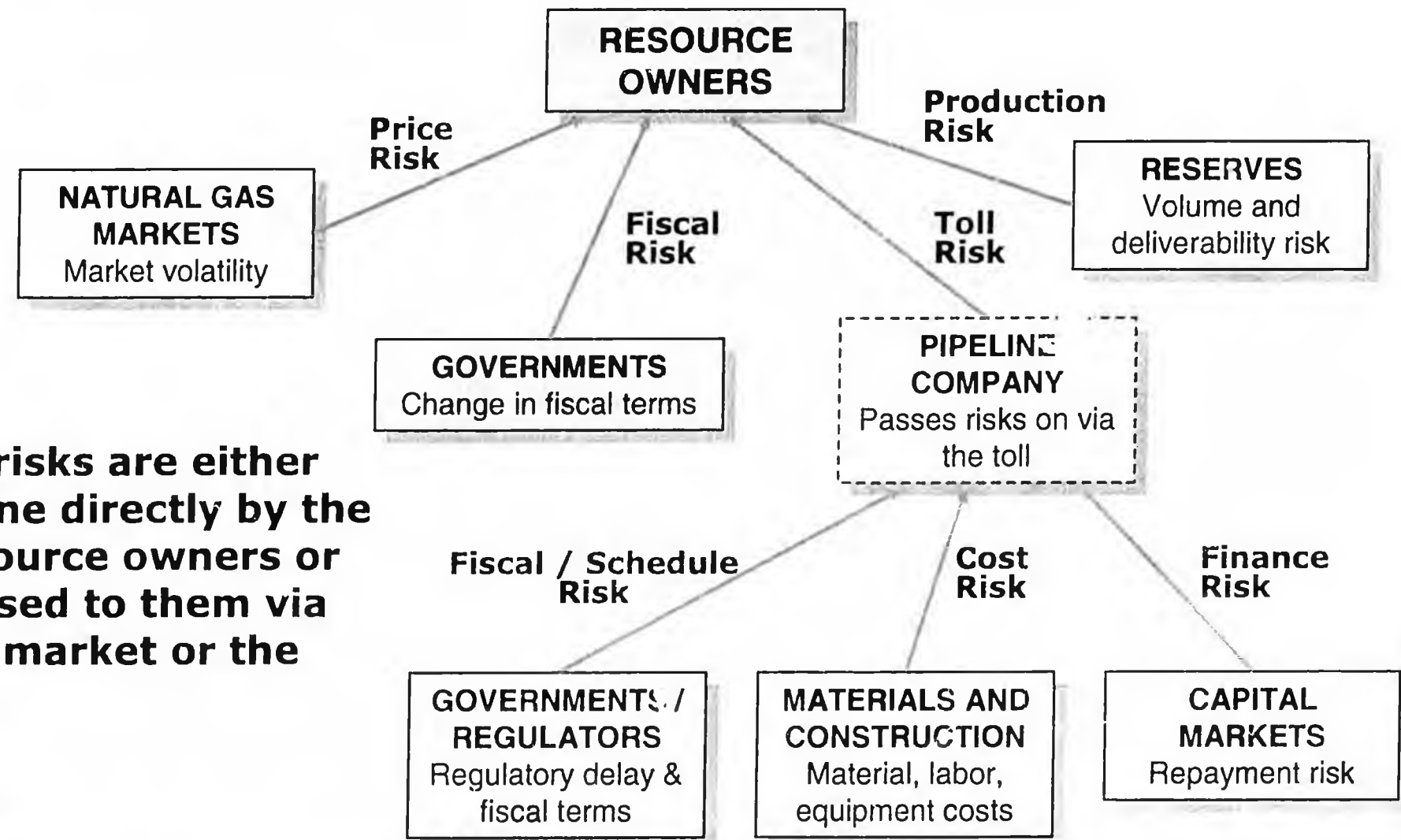
## What is so important about FT?



- Firm Transportation commitments (FT) by the resource owners are needed for a gas pipeline company to get financing
  - "No customers, no credit, no pipeline" (TransCanada)
  - "No producers, no pipeline" (Enbridge)
- FT is a binding financial obligation
  - not simply "committing gas to a pipeline"
- Requires multi-billion dollar commitments by resource owners
  - Assuming 4.5 bcfd, \$3.50/mcf, 25 year term.....**\$144 billion**
- Long term commitments represent real risk
  - Two risks:
    - Price risk (over time, market price will not cover FT cost *and* produce an acceptable return on the investment)
    - Supply risk (will not have sufficient gas to use the FT commitment over time)
  - Risk is borne by those making the commitments



# Project Risk Resides with the Resource Owners



**All risks are either borne directly by the resource owners or passed to them via the market or the toll.**

**➔ Those bearing a risk are commercially motivated to manage that risk**

## BP Messages on AGIA



- AGIA needs significant modification to result in a successful project
- As drafted, BP will not be able to submit a bid under AGIA
- As drafted, it is difficult to envision circumstances that would allow BP to make a firm transportation commitment to a licensed project under AGIA

Why?...

- Negotiated rate protection unavailable upon expansion
  - Subsidization of competitors is commercially unreasonable
  - Resource terms insufficient to justify FT commitment
- BP intends to bid if AGIA is appropriately modified

## Key Concerns Preventing BP Bid Under AGIA

In the order they appear in SB-104



- .130(2)(B) / .210 – “Detailed” description of design requires substantial customer consultation, engineering
  - FERC Order 2005 requires “good faith estimate”
- .130(2)(C-D) – Can’t “demonstrate” economic viability
  - “nobody can say today whether this project is economic or not” (Mid-American Energy); need bottoms-up cost and revenue estimate
- .130(7) - Requires subsidization of competitors & eliminates negotiated rate protections
  - contrary to ANGPA & FERC rules
  - imposes unreasonable commercial risk
- .130(13) - Commitment to reserve capacity for in-state delivery points, regardless of open season outcome
  - imposes unreasonable commercial risk
  - not consistent with FERC Order 2005 [157.34(c)(8)]
- .150(a) - Release of proprietary information to competitors after license award creates huge exposure

## Key Concerns Preventing BP Bid Under AGIA

In the order they appear in SB-104



- .200(a) - Must accept FERC certificate despite conditions
  - could add significantly to project cost
- .200(b) - Must sanction project within one year of FERC certification, regardless of cost
  - failure to sanction results in loss of all data to state (engineering, design, contracts, permits, etc.)
- .230(a)(2) / .210 - In breach if substantial deviation from plan set out in application
  - Unless it increases NPV, is ordered by AOGCC or isn't foreseeable
  - FERC, BLM, municipal agencies, Canada, etc. could require changes to project specs outside state control
- .240(c) - Effectively no way to abandon an uneconomic project; licensee subject to damages
- .310 - .320 - Fiscal terms insufficient; risk of no FT customers
  - "no customers, no credit, no pipeline" (TransCanada)

# How AGIA can help deliver a successful project

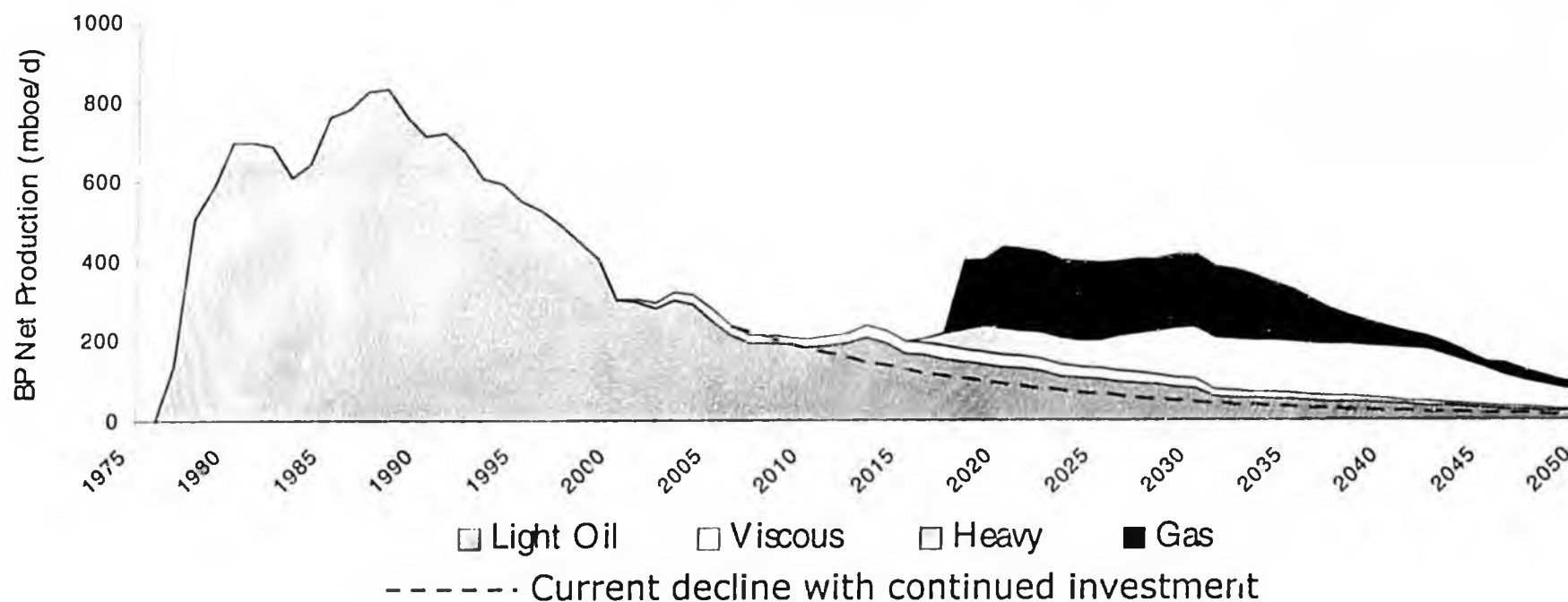


- Address areas of key concern listed on prior slides
- Allow applicants to respond to State's objectives
  - Prescribing solutions up front will not result in the best project
- Avoid exclusivity to ensure a pipeline gets built
  - Even as amended, AGIA creates exclusivity
  - Federal model encourages competition in the marketplace
- Address fiscal terms to encourage FT commitments needed for a successful project
  - Allow resource owners to make offer in bid
- Allow due process of appeal, remove potential Order 2004 conflict, other clarifying edits



# BP's Vision for Alaska

- BP has a long history in Alaska....
- .....and we look forward to a 50-year future
- That future is only possible with a gas pipeline
- BP wants to bid under AGIA and hopes it will be modified appropriately

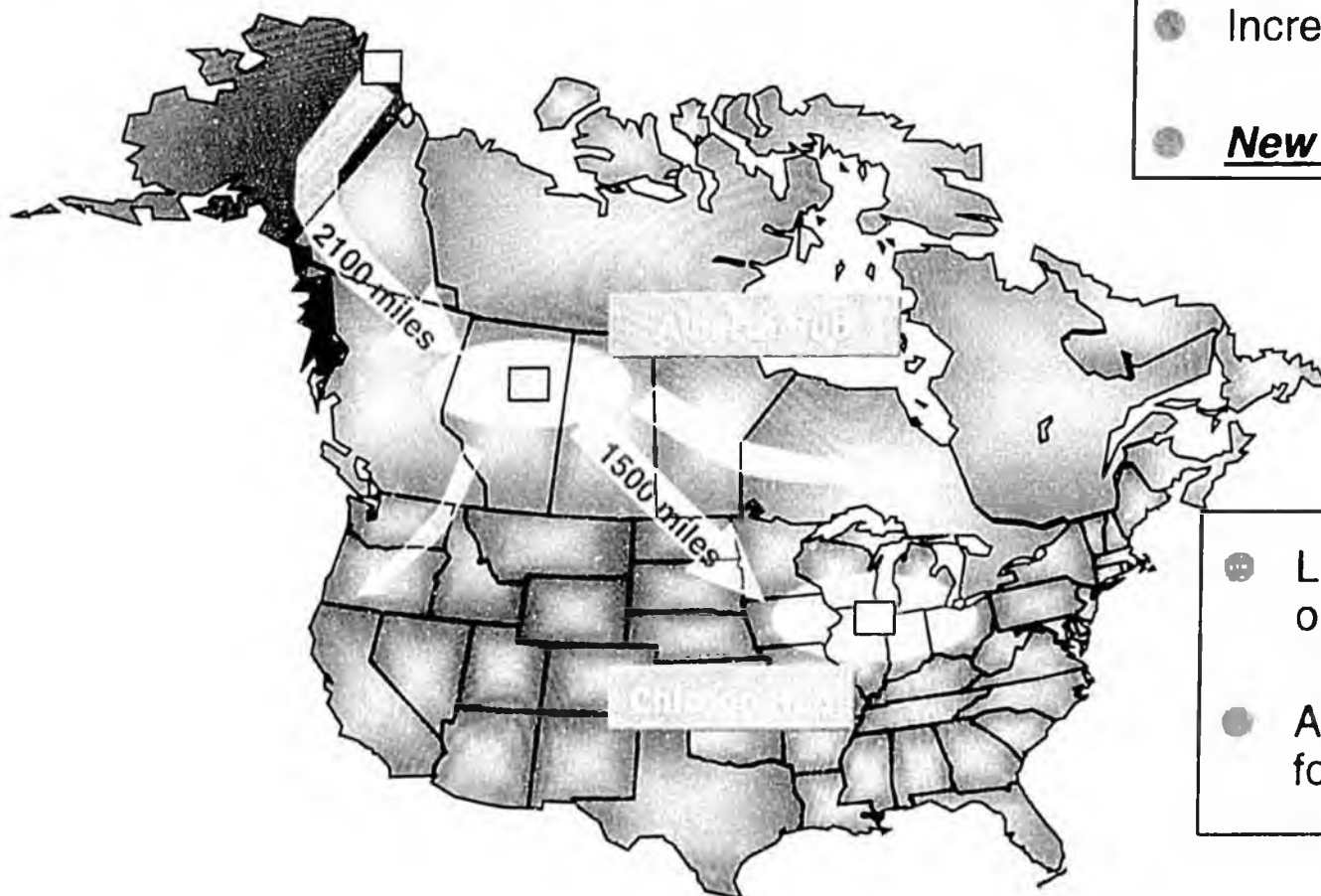




# What A Successful Gasline Means

- Jobs for Alaskans
- Additional revenue for future generations

- Increased economic activity
- New businesses created



- Long term gas supply opportunity for Alaskans
- A more diversified economy for decades

**BP Testimony on AGIA (SB104)**  
**Senate Finance Committee**  
**April 28, 2007**

- Mr. Chairman, members of the committee, for the record my name is Dave Van Tuyl. I am the Gas Commercialization Manager for BP Alaska. Thank you for the opportunity to testify before you this morning.
- My testimony will start with a reminder of the opportunity and challenge before us, and a brief discussion of the project economics and risk. Then I'll provide our specific concerns on AGIA, and end with a vision of a successful outcome which I think we are all trying to achieve.

**An Opportunity...and a Challenge**

- **BP wants and needs a gas pipeline.** And we need that pipeline to be built for a low capital cost and then operated cost efficiently. We believe that is what is required to make the project happen and be successful. Low costs are good for both BP and the State because it results in lower tariffs, higher netbacks and more revenues for the State and BP.
- Also, a low cost project will provide incentive to explore for more gas to keep the pipeline full into the future. That is also good for the State and for BP
- The best way to ensure there is gas exploration in the future is to get a gas pipeline built in the first place, and to get it built for a low cost.
- **This is a hugely important project to BP, to Alaska and to the nation.** It represents the largest, known, undeveloped gas resource in the United States, and in BP's global portfolio. The gas project is important in its own right – but it also extends the economic life of Alaska's oil production for decades. Extending oil production is good for the State, the nation and for BP.

- We share the governor's and the legislature's desire to get a successful gas project moving.
- But the project remains commercially challenged. It requires massive capital investment. It requires even larger financial commitments to get the necessary financing to allow the project to advance.
- If it was easy, it would be advancing today. But it's not easy. It's incredibly challenging. The size of this project alone makes it incredibly challenging and risky.

#### **BP Disagrees with the Administration's Economics**

An important point I want to leave with you is that we fundamentally disagree with the characterization of the Alaska Gas project economics as recently presented by the Administration.

We have concerns over many different statements made by the Administration, but I'll limit my comments to addressing three key concerns.

1. Underlying economic methodology – Decoupling the Upstream from the Midstream
2. Nature of firm shipping commitments
3. The importance of long term cash flow in investment decision making

We are very concerned that the economic analysis presented by the Administration to the legislature is very misleading.

### Economics

- Without the commitment of capital to the pipeline or the huge financial obligation required for Firm Transportation (FT) for the midstream facilities, there is no way to realize value from the sale of gas. Thus, any analysis of the project that excludes midstream capital and FT is incomplete.
- And because these commitments are just that, legally binding commitments, they need to be accounted for when evaluating project economics. These commitments were ignored in the Administration's analysis of the economics.
- Because that method ignores the FT obligation, the resulting assertion that our upstream economics are so robust is patently incorrect. In fact, the upstream pays for the midstream. It does this through firm transportation commitments. These commitments cannot be ignored.

The second point we want to emphasize is to ensure we have a common understanding of the nature of these firm transportation commitments we've just talked about.

### Nature of Firm Transportation Commitments

- FT is a binding commitment made by a shipper to a pipeline company in an open season to secure capacity on the pipeline for a specified duration at a specified cost. We heard Fred Rich talk about this the other day.
- There are a few important facts to be clear on about FT
- FT is binding legal obligation. It becomes binding once the necessary conditions are met, including the pipeline coming into operation.
- The Administration has claimed that the Producers say that FT is "exactly like debt". I'm not aware of any of us having said that in testimony. Long

term commercial commitments like FT are often characterized as "debt-like", and must be reported to the SEC.

- The core issue is whether the FT commitments require the producers to absorb the substantial majority of the risk associated with the project.
- FT is a financial obligation, and it is certain that the lenders would have recourse to the financial security provided by the producers' FT, should the pipeline company fail to meet its obligations.
- Therefore, FT cannot be ignored if a project is to be evaluated properly.
- And generic statements about treatment of long term commercial commitments is dangerous. Commitments of the magnitude required to underpin this project are massive in both the dollar amount and the likely duration.
- These commitments will create their own weather in the financial markets – they must be considered.

The third and final point I wanted to emphasize is that confidence in future cash flows is very important in evaluating the commercial viability of any investment decision. That is particularly true for a commitment as large as the Alaska gas pipeline project.

#### Importance of Long Term Cash Flow

- The Administration suggested that cash flows beyond 10 years are relatively unimportant in financial decision making on this project
- That's not true.

- Cash flows further out in time tend to have less effect on NPV – this is true
  - But cash impact years into the future will indeed be real
  - In evaluating the economics of projects, we look at many different measures. NPV, IRR and PI are just some of the measures which are considered.
  - The ability of a project to generate long-term cash flow is also an important consideration to investors.
  - It's important to bear in mind that we expect the FT commitments we just talked about will be in effect well beyond 10 years.
  - So those making long terms commitments want to know that they'll be able to make good on them. Lenders will want to know this, too.

Getting this project right has enough challenges of its own, let alone when we have such fundamental disagreement with how the project is characterized.

#### What Is So Important about FT?

- FT commitments, typically obligations to "ship or pay" made by the resource owners or "shippers", are needed by the pipeline company to get financing
  - validating just how important they are, we've heard some very simple and straightforward comments from pipeline companies who have testified in the past couple of weeks
  - TransCanada has said "No customers, no credit, no pipeline" (and in this context customers means shippers)
  - Enbridge put it even more simply by saying "No producers, no pipeline"
- Those aren't "political" statements. They are statements about the simple financial truths of gas pipeline projects
- FT is a binding FINANCIAL obligation. I've sometimes heard FT described as "committing gas to a pipeline". I've heard that quote from industry as well as

others, so I'm not pointing any fingers here. But I just wanted to make it clear that FT is an actual financial obligation

- Typically, FT is known as a "ship or pay" obligation
  - That means that a shipper commits to pay the pipeline company for use of its service whether or not the shipper actually delivers gas to the line
  - And it's also important to note that a company does not need to have ANY gas resources to enter into a firm transportation commitment. Any company who meets the creditworthiness standards set by the pipeline company is free to bid for capacity. Gas pipelines are "open access". Anyone is free to obtain capacity if they make the requisite commitments.
- The scale of these commitments is often oversimplified. It's not "just" the capital cost of the project, if that weren't in itself a large enough commitment.
    - the commitment is for what is known as the "demand charge" which is the cost of service the pipeline will charge through time
    - Capital is one major component
    - But for illustration, I've provided some broad assumptions to put the scale of these commitments in perspective.
      - assuming a 4.5 bcf/d project, at a unit cost of \$3.50/mcf for 25 years results in a total FT commitment of \$144 billion
      - That's a huge sum, even for a company the size of BP
  - These long term commitments are just that – commitments. Therefore, they represent real risk. The risk can manifest itself in two key ways:
    - the PRICE can drop such that the costs of these commitments isn't covered; and
    - the GAS SUPPLY may be insufficient to use the capacity that has been committed over time.

- And the size of these commitments magnifies the risk. And that risk is borne by those making the commitments,

### Project Risk Resides with the Resource Owners

- This next slide attempts to show how risk is ultimately allocated in a major resource development project like the Alaska Gas Pipeline Project
- I'm going to **step through it one bit at a time.**
- First, we start with the **Resource Owners** – that's of course the State of Alaska, and it includes the lessees, like BP, CP, EM, Chevron and others.
- There are certain risks that are inherent to the resource itself.
  - There is always price risk associated with selling a commodity like gas
    - that's the risk that the price of gas will fall in the future, possibly below the tariff
  - There's also production risk
    - Keeping the pipeline full for project life
    - Being able to deliver the full volume every day
    - These risks are important considerations when a resource owner has to make the firm transportation commitments necessary to underpin the project
- Next, there's fiscal risk for a lessee; that's the risk that the fiscal terms on the upstream business might change. On major infrastructure projects like this around the world, it's not uncommon for host governments to address fiscal risk with a mutually agreed framework.
- There are also a whole host of risks associated with constructing the pipeline itself
  - Regulatory process could change → schedule risk

- Material, labor and equipment costs → cost risk, which includes project management and execution
- Need for finances from the capital markets → finance risk (Again, Fred Rich talked at some length about this risk at his project finance workshop earlier this week)
  
- **What is critical to appreciate** is that all these project-related risks that are taken by the pipeline company are ultimately passed through to the resource owners through the toll
  - The Pipeline company receives a regulated rate of return
  - Gets a reasonable return on investment commensurate with the risks
  - That's the pipeline's reward
  - In exchange for this regulated rate of return, the regulators ensure that the pipeline does not take on certain risks
  - These instead are passed through to the resource owners, provided that the pipeline owner delivers the project on time and operated efficiently
  - That's how the risk / reward balance is struck by the pipeline regulators
  
- So ultimately, virtually **ALL RISKS** are either borne directly by the resource owners, or are passed through to the resource owners through the toll
  
- To ensure a low cost project, it's important that those that are bearing a risk are able to manage that risk
  - They are commercially motivated to manage that risk downwards

#### **BP Messages on AGIA**

- I'd like to turn to our specific comments on the current version of SB-104.

- To put it clearly and succinctly, AGIA needs substantial modification to result in a successful project. And I'll go into some detail as to the modifications we see as necessary.
- As we've said in previous testimony, we agree with the Governor's intent on using AGIA to advance a successful project. But the current version of AGIA won't get us there. I'll explain why in a moment.
- I want to be very clear with BP's evaluation of AGIA as it's currently drafted. Simply put, BP won't be able to submit a bid that conforms to the requirements of AGIA.
- It's not easy for me to say that. BP really does want to be able to compete in the AGIA process. BP wants to help deliver a successful Alaska gas pipeline project. We think we can add significantly to the success of the project.
- If AGIA is fixed, we intend to bid. We're happy to have our bid openly evaluated along with others. But the current terms of AGIA won't allow that to happen.
- I also want to be very clear about the implications the current version of AGIA holds for BP participating in an open season. As currently drafted, it's difficult to envision the circumstances that would allow BP to make a firm transportation commitment to the licensed project under AGIA in an initial open season.
- And that's true even if a BP affiliate was the licensee.
- That's because BP believes the terms of AGIA put unreasonable commercial risk on initial shippers.

- AGIA removes negotiated rate protection (protections from potential cost overruns, protections from subsidization of expansion shippers, and the ability to gain long term certainty of future rates).
  - There is language in the bill that now references negotiated rates, but it doesn't actually provide rate protection for initial shippers
- AGIA doesn't provide the fiscal certainty needed to justify the massive, long term firm transportation commitments necessary for a successful project.
- I'm not trying to be dramatic, or issue any sort of a "threat". I'm trying to be very open, and transparent. We owe that to you because there is so much at stake.
- Next I'll explain what provisions prevent us from making a bid under AGIA as it's currently drafted.

#### Key Concerns Preventing BP Bid Under AGIA

- While we have several concerns with AGIA as drafted, we've tried to hone this list only to the most significant concerns we have that would prevent us from submitting a conforming bid.
- I'm not planning to walk through each of these in detail, but I'll explain a few of them to give you a sense of our concern. They are arranged in the order they appear in the bill and not in any sort of ranking.
- 130(2)(B) / .210 – currently requires a "detailed" description of size and offtake, and the way we understand section .210, we wouldn't be able to change our plan as better information becomes available

- 130(2)(C-D) – We think it's impossible to "demonstrate" economic viability of the project within the AGIA timeframe.
- 130(7) – We've already testified in some detail regarding our concerns with this section.
  - these provisions are in conflict with FERC policy and the ANGPA
  - it ignores one key objective of FERC Order 2005 – rate predictability for initial shippers!
- 130(13) – Implies a commitment to reserve capacity for in-state delivery points, whether or not that service is committed in an open season
- 150(a) – requires release of the successful licensee's proprietary information.

#### Key Concerns Preventing BP Bid Under AGIA (cont.)

- 200(a) – requires the licensee to accept a FERC certificate despite of potential conditions FERC may impose.
- 200(b) – the licensee effectively turns over sanction authority to the State
- 230(a)(2) – This provision says that the licensee is in breach if there is a substantial deviation from the terms set out in the application
- 240(c) – The way we understand this section, there is effectively no way to prove the project uneconomic, therefore there is no "off-ramp"
- 310 – 320 – Finally, as we've consistently testified, the resource terms under AGIA are inadequate.

#### How Can AGIA Help to Deliver a Successful Project?

- For BP to be able to submit a bid under AGIA, a number of modifications need to be made
- The 10 areas of concern I just walked through need to be fixed
- As we've discussed in every testimony on AGIA we've offered, there are three other key areas that need to be fixed
- First, the State should provide its list of objectives that prospective applicants must address
  - BP, and other applicants, should be allowed to tell the State how we would address the State's objectives
  - that's how the best solutions are developed – through creative thought, not by presupposed outcomes
- Second, AGIA should remove elements of exclusivity.
  - An amendment was made in a prior committee to try and address this concern [in .100(b)], but even with this amendment, AGIA creates exclusivity
  - Exclusivity prevents competition in the marketplace.
  - The Federal model works well, and encourages open competition in the marketplace. It works everywhere else in America. It will work for Alaska as well.
- Third, fiscal terms have to get solved in a way that will encourage firm transportation commitments from shippers
  - we would like the opportunity to include fiscal terms in an bid under AGIA that the State can consider (and reject if it likes)
  - BP wants to be able to submit a bid under AGIA

- Finally, there are other edits, less fundamental than the ones I just mentioned that we think also should be addressed.

### BP's Vision for Alaska

- To close, I'd like to spend a moment to look into the future and consider again the opportunities we have before us.
- BP has a long history in Alaska. BP has been actively involved in the exploration, development and production of Alaska's North Slope energy resources for decades.
- And we see the opportunity for a bright future ahead. In fact, we envision our 50-year future in Alaska. It's not just a slogan.
- I'd like to turn your attention to the graph at the bottom the slide, which shows the possibility of the future that BP sees in Alaska, depicting BP's share of production through time.
- There are a few key points to draw from the graph.
- The days of high plateau production are behind us.
- We still have a significant level of production today, but that production will continue to decline with time. That's what the dotted red line depicts.
- That shows production declining at historic levels, which already would require significant investment.
- We can make up that decline in production with new investment that would result in new production from heavy oil resources and from gas.

- But it's not a given. It's a view of what's **POSSIBLE**.
- That future is only made possible with an Alaska gas pipeline project.

#### **What A Successful Gasline Means**

- Finally, it's worth a reminder of the importance of a successful project. And I'd like to emphasize that what we need is a **SUCCESSFUL** gas pipeline, not just ANY gasline.
- As we've said, this is a project of tremendous scope and scale and that's what the picture reminds us of. Because of this it presents tremendous risk. But if it's done right, it presents a wonderful opportunity for the State, Industry and the people of Alaska.
- Because there is much at stake, we need to get it right.
- The project creates the opportunity for jobs for Alaskans, and if we deliver a successful, low cost project, for revenues to the State and to Industry well into the future.
- We can create a whole new industry of gas exploration with a successful, low cost project. Gas exploration and expansion are only possible if the pipeline gets built in the first place, and if it's built for a low capital and operating cost. That will make it attractive for bringing new volumes into the project, which benefits the State, gas explorers, and initial shippers as well.
- A successful gas pipeline project will provide the opportunity to bring a long term gas supply source for use by Alaskans.

- And finally, gas sales will diversify Alaska's economy for decades into the future.
  
- As I said, there's a lot at stake, so we need to get it right.
  
- BP wants to get it right. That's why we've tried to be very forthright and specific with our comments. We owe that to you as you finish your deliberations on AGIA.
  
- Thank you for the opportunity to testify today. I'd be happy to answer any questions you might have.

TRANS CANADA

4/28/07 PM



## Tony Palmer

Vice-President, Alaska Business Development

As Vice-President, Alaska Business Development, Tony Palmer leads TransCanada Corporation's efforts on the Alaska Highway pipeline project. Tony is also CEO of Foothills Pipe Lines Limited, a subsidiary of TransCanada. Foothills owns the Canadian section of the Alaska Natural Gas Transportation System. TransCanada and Foothills own the Alaskan segment.

Tony joined Foothills Pipe Lines Ltd. in 1985 and worked in NOVA Gas International Ltd. from 1994 to 1998. Since then, Tony has held several senior positions in Business Development, Strategy and Transmission Planning at TransCanada. Tony has 24 years experience in the pipeline business.

Tony earned a Bachelor of Arts from Concordia University in Montreal in 1979 and is a graduate of the Executive Development program at the University of Calgary in 1988.

TransCanada is a leader in the responsible development and reliable operation of North American energy infrastructure. TransCanada's network of approximately 42,000 kilometres (26,000 miles) of pipeline transports the majority of Western Canada's natural gas production to key Canadian and U.S. markets. A growing independent power producer, TransCanada owns, or has interests in, approximately 7,700 megawatts of power generation in Canada and the United States. TransCanada's common shares trade on the Toronto and New York stock exchanges under the symbol TRP.

TransCanada (December 5, 2006)



ENBRIDGE

The background of the slide is a black and white photograph of a natural gas flare. A large, bright plume of white gas rises from the ground, creating a dramatic silhouette against a dark sky. The foreground shows a flat, open landscape.

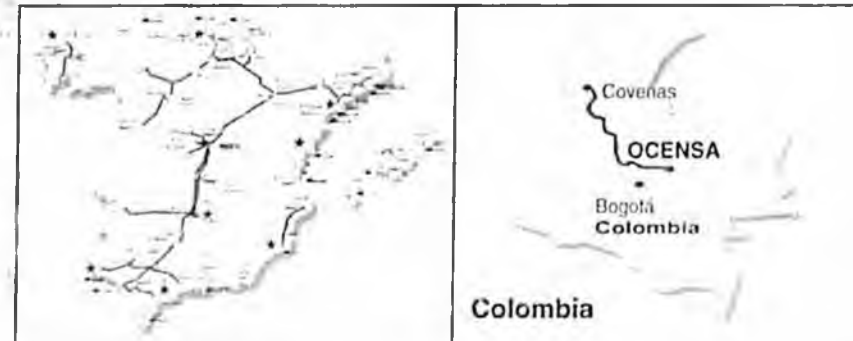
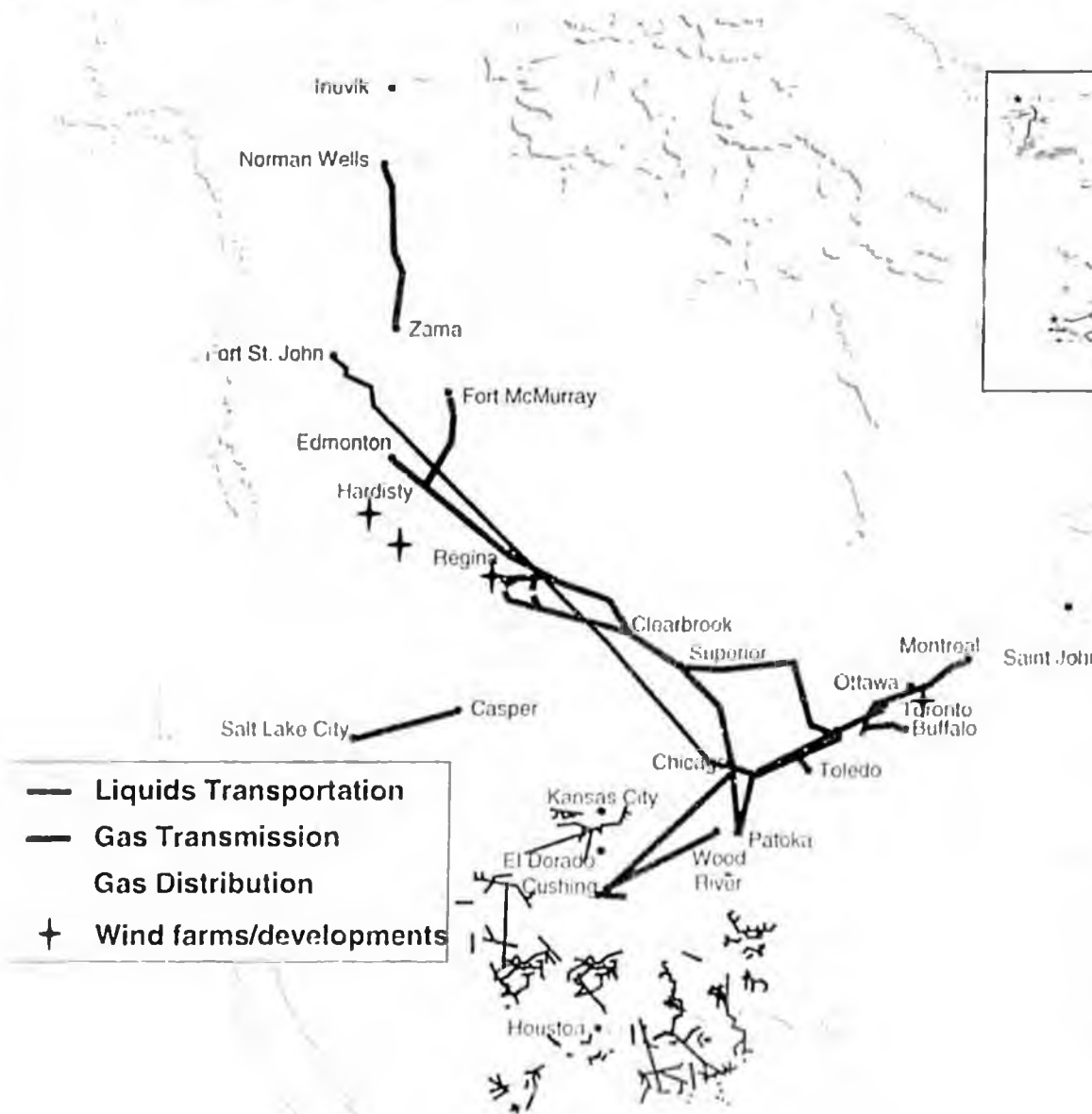
# Alaska Natural Gas Pipeline Senate Finance Committee

April 30, 2007

**Ron Brintnell**

**Director, Gas Development**

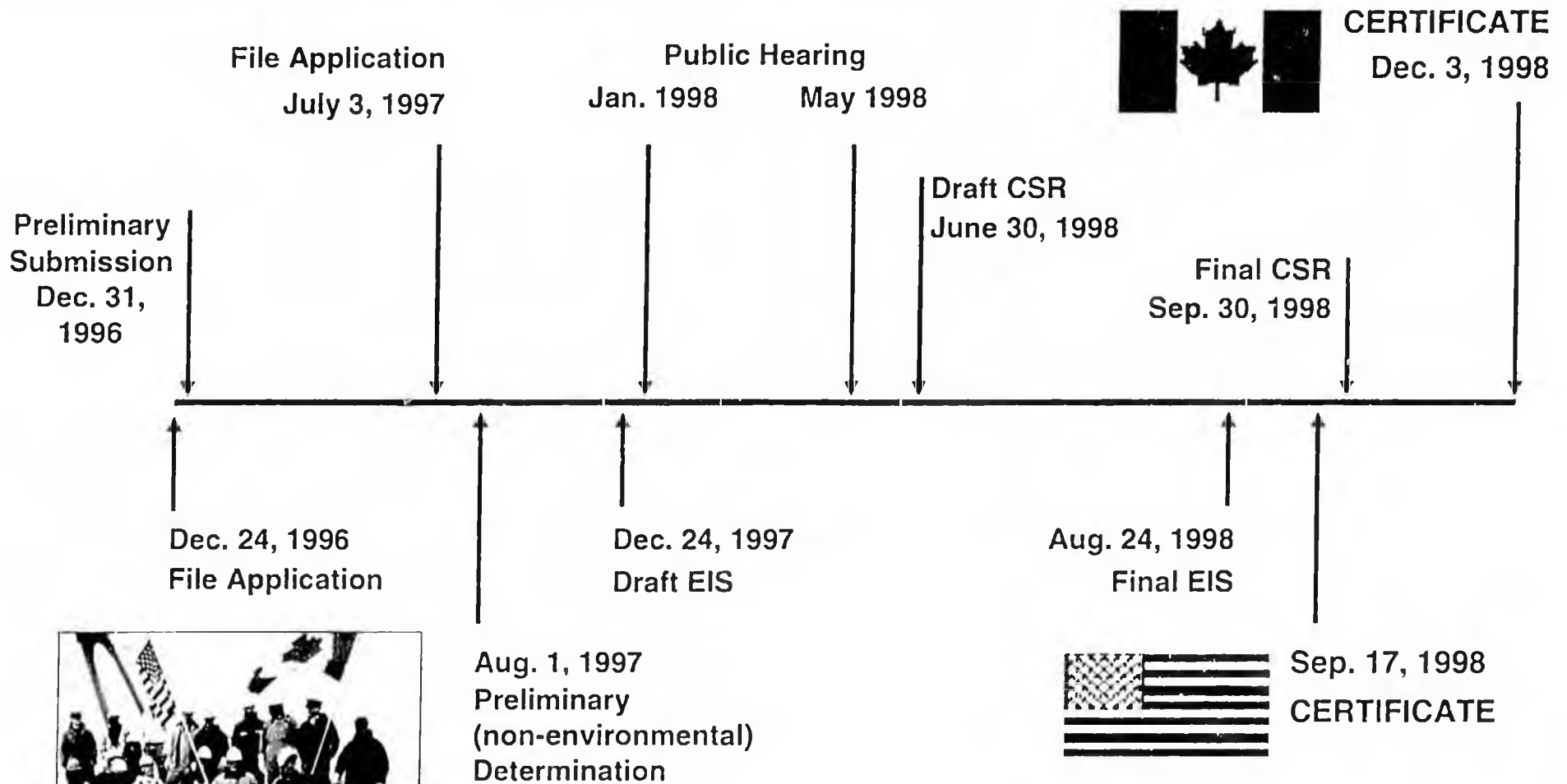
# Enbridge Overview



- Interest in 50,000 miles of pipelines
- Own and operate world's longest liquid petroleum pipeline
- Deliver 70% of WCSB crude oil production
- Deliver half of deep water Gulf of Mexico natural gas production
- Canada's largest natural gas local distribution company
- Employ 4,900 people
- One of the *Global 100 Most Sustainable Corporations in the World*



# Alliance Pipeline



# Moving the Project Forward Requires Producer Alignment



- **No producers No pipeline !**
- **Project is too risky - too big, too complex, too expensive - to move forward without producers**
- **Potential gas buyers see *no producers as no progress***
  - **Buyers' dilemma, switch to coal, go off-shore or wait for Alaska?**

# Moving the Project Forward Don't Just Focus On The Pipeline



- As drafted, AGIA is unlikely to produce significant commercial results.
- AGIA introduced as a catalyst to expedite the construction of a natural gas pipeline
- AGIA focus is on the pipeline and not entire project which requires Producer alignment
- AGIA adds unnecessary regulatory complexity
  - FERC process well defined and effective

# Moving the Project Forward Promote, Don't Stymie Innovation



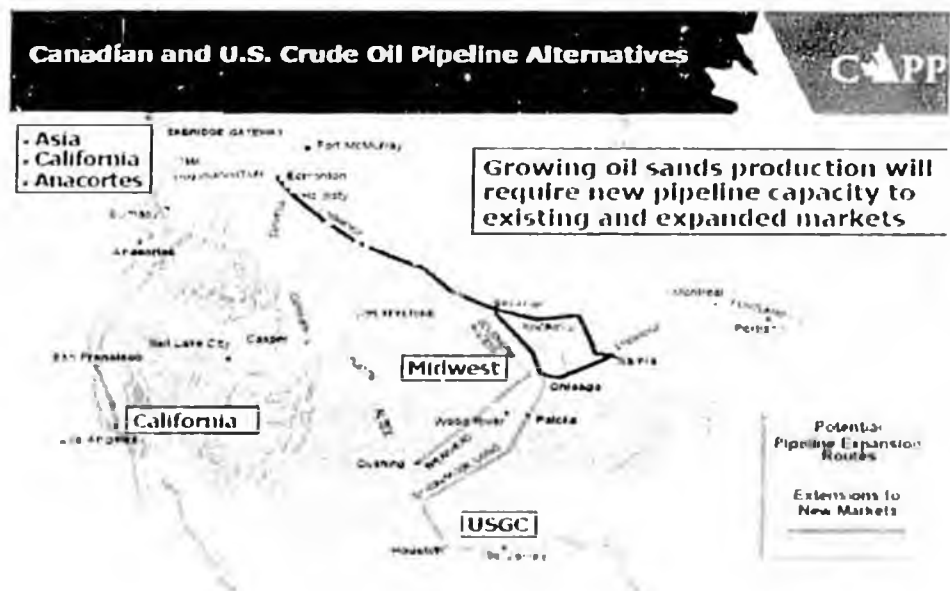
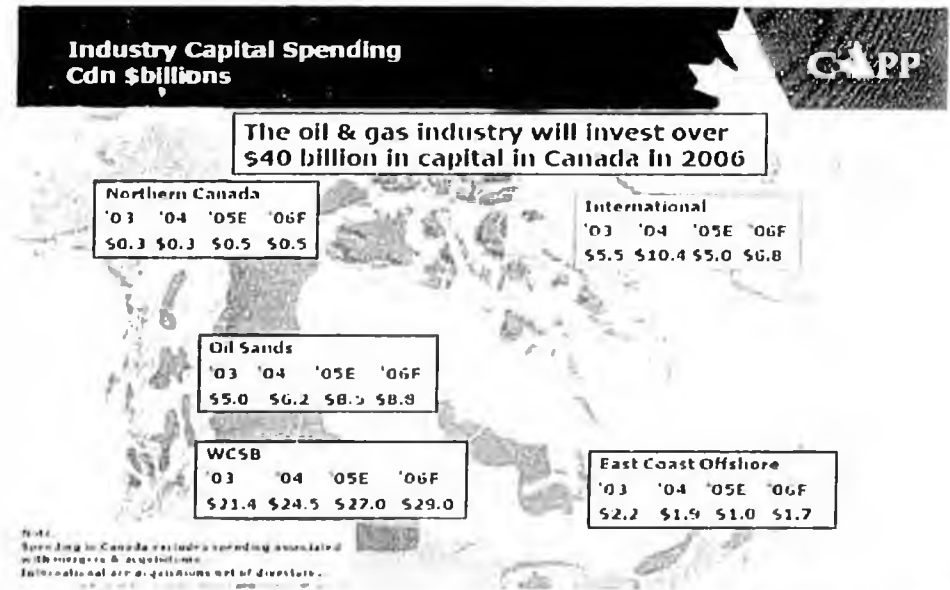
- Absolute requirements may result in not having the opportunity to evaluate creative solutions that add value in different ways
- This is not a standard RFP project



# Canadian Oil Sands Development Valuable Lessons



- Investment of \$125 billion
  - Significant new employment, tax revenue, long term growth
  - Extensive new pipeline development
  
- Resulted from proactive progressive political vision that facilitated development
  - Worked cooperatively with industry
  - Generating greater returns for all



# Moving the Project Forward Understand What Is Achievable



- Binding shipper commitment is required prior to spending significant \$'s on regulatory applications
  - Not commercially prudent to assume producers will show, or that gas can be “acquired”
  - Risk too high even with government cost sharing
- Even binding shipper/pipeline agreements will have conditions including:
  - An acceptable FERC Certificate
  - Acceptable Financing
  - Shipper resolution of Alaska state taxation issues
  - Defined project milestones / timing
- An unconditional commitment to proceed will not happen
  - Regulatory certificates may have conditions making project uneconomic
  - Events between application and certificate could make project uneconomic

# Moving the Project Forward Understand Canada



## No company has the exclusive right to build a pipeline to ship Alaskan gas in Canada

- 2 Options to Permit the Project Through Canada

### **NPA**

Northern Pipeline Act passed in 1977

Socio-economic baseline impact developed late 1970s

Certificates of Public Convenience and Necessity issued to Foothills Pipeline to build the Cdn portion of the Alaska Natural Gas Transportation System proposal.

Enshrines a 30-year old project never undertaken that has now significantly changed

### **NEB – CEAA**

Modern, efficient and transparent regulatory process

Dove-tails with FERC

Consistent with NAFTA

Contemporary, well understood processes:

First Nations participation

Environmental assessments and practices

Economic benefits through open competition

# Moving the Project Forward Understand Canada



“As we move forward, I am guided by **five principles** that I believe can be **applied to all pipeline decisions:**

- First, they **must not interfere with market forces.** We will **let the market decide.**
- Second, our decisions must be **supportive of a modern regulatory regime**
- Third there must be a **project management approach**
- Fourth, the **pipelines must support Aboriginal economic development**
- Finally, decisions **must ensure that Canadian benefits are realized**”

Honourable Jim Prentice

Minister of Indian Affairs and Northern Development

Presentation to Canadian Energy Pipeline Association Annual Dinner

May 2006

# Moving the Project Forward Final Thoughts



## Enbridge believes:

- Outstanding fiscal issues are the project's "elephant in the living room."
- An unconditional commitment to advance the project is not achievable
- AGIA will best serve Alaskans if it allows for the creativity and innovation that drives the market place.
- Government financial assistance is not essential
- Government can achieve key goals without adding to regulatory process
- Canada will be ready for this project, but claims of exclusivity will be denied
- Alaska should ensure that it does not create a process that is all about process