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**Alaska North Slope LNG Project
Testimony for the House Special Committee on Oil and Gas
(January 13, 2000)**

Mr. Chairman, for the record, my name is Steve Alleman. My current assignment is as the Commercial Manager for the Alaska North Slope LNG Project, I reside in Anchorage, and I am employed by Phillips Petroleum Company. Thank you for the opportunity to testify today on behalf of the Sponsor Group.

Today, I will provide an overview of the status of the project and then will be happy to address questions. The Sponsors presented testimony to this committee on two occasions last year, and to avoid repetition, I will use those statements as foundation and discuss new developments, activities and plans since we last visited with the committee.

I am very pleased to be here today to say that the Alaska North Slope LNG Project has made considerable progress this year. As you will hear, we have a solid forward plan for commercializing North Slope gas via LNG and to our knowledge, no one is applying more resources and money than us to do so.

Most recently, the membership in our group has changed. BP is now a 12 percent member. This is a very welcome addition, considering BP's extensive North Slope lease position and operations, its world wide project experience, and its interest in pursuing all options to commercialize Alaska gas. In addition to BP, the other members, of course, are ARCO Alaska, Foothills Pipe Lines, Marubeni Corporation and Phillips Petroleum. As we have often stated, and it is even more true today, this is a very experienced and strong group that we believe provides the best chance for commercialization of North Slope gas via the LNG option.

The object of this group is the same as when we formed in 1998: to develop a competitive LNG export project at the earliest possible time as market conditions warrant. To be competitive, we need to exploit our advantages and overcome our challenges. An Alaska project has several positives including a developed resource, proximity to the market, and political stability. But it has two significant challenges:

the cost of an 800-mile pipeline and the fact that the project needs to be appropriately sized to afford it the best chance to enter the market.

Previous State studies and our own internal studies point to a potential answer to the cost issue. To be competitive, an Alaskan LNG project needs cost reductions unique to Alaska, it needs federal and state fiscal modifications and certainty. Our studies suggest that the combined level of federal and state fiscal relief that is needed may be politically feasible. This is because relief that occurs early in the project can help improve the project economics while still providing federal and state revenues later in the project.

The issue of project size requires creative thinking and effort. We believe that the marketability and timing of an LNG project improve if it is smaller. History shows that the successful mega-LNG projects serving East Asia started with a small size then built up in steps. Our analysis convinced us that previously studied projects of 14-15 million tons per year were just too large to be competitive with other market entry projects.

Accordingly, over the past year, we have worked to improve our chances with the marketplace by reducing the size of our project while at the same time evaluating our opportunities for further cost reductions. We completed an updated and detailed assessment of market conditions. This helped us determine the largest volume project that could enter the market in a reasonable timeframe. We are also systematically engineering the project to ensure that the optimum size can be achieved. We are now optimizing our Market Viable Project, or as we call it, our MVP.

This past fall, we announced this MVP as a 7-million ton per year LNG export project, which has been established, as our working basis for further refinement and optimization. This is about half of the project size that has been assumed for over a decade. Again, our motivation is to develop a project that is appropriately sized to gain a toehold in the market while at the same time having the ability to expand that project as market conditions warrant. Thus, with a projected pre-shipping cost of \$5-6 billion, we have significantly reduced our project risk in the areas of market, capital cost, and financing.

As for the market and what it is telling us about timing and the overall prospects for an Alaska project, there are encouraging signs. While the economic turmoil of the past few years in our target Asian markets has negatively impacted near term demand for LNG, there seems to be good prospects for substantial, sustained growth in the long term. However, we must face the reality that the competition for market share will be fierce. While the LNG marketplace will favorably view the positive aspects of an Alaskan project that I mentioned earlier, these savvy buyers will ultimately commit to an Alaskan project only when it becomes economically competitive with their best alternatives.

Therefore, we think it is important to clarify our thinking on two points. As a result of our in depth analysis and LNG market experience, the Sponsor Group does not subscribe to the idea of a "market window" for an Alaskan project. We do believe, however that once an Alaskan project is economically competitive, then it can legitimately vie for a share of what we project to be a long term, more sustained demand growth. Second, we recognize that the affirmative decision that will cause an Alaskan project to happen will come from the market, not from the investors or from government. LNG projects are not like oil development; you can not afford to "build it and they will come". The market will drive this project and the LNG buyers will need to be enticed to an Alaskan project by making it economically competitive.

To maintain a continuous market presence; to be available to respond to market questions; as well as to provide information on our project to these LNG markets, the Alaska North Slope LNG Project announced in September of 1999, its opening of a market liaison office in Tokyo, Japan. This office is located in Marubeni's Tokyo complex and is maintained by Marubeni personnel. As a Sponsor group member, Marubeni provides its own project and market expertise complimented by the experience and expertise of the other sponsors including that of Phillips Petroleum Company who, as you know, has been marketing LNG to Japan from Alaska for over 30 years.

Often we get the question: "What is the schedule for starting up the project?" In light of my earlier statement, the more relevant question

is: "What are the activities and schedule for making the project economically competitive and enticing to the LNG buyers"? In just a moment, I will address that question. But first, I want to discuss the matter of pipeline route and LNG plant site that is sometimes associated with the question of project timing.

As we announced this past fall, the project sponsors have narrowed the route and site to two alternatives: first to Anderson Bay in Prince William Sound and second to Nikiski in Cook Inlet.

When we narrowed our site selections to two alternatives, we found that neither was clearly better than the other. The Cook Inlet route may offer some cost advantages and more naturally fits with Cook Inlet's role as the center for gas usage in Alaska. While the Prince William Sound route has some existing permitting, which may give it a nominal time advantage.

But the real question is not where does permitting stand today, but what is required to fully permit either alternative to the point where construction of a project can occur. Based upon our sponsors' expertise of actually permitting and then building multi-billion dollar projects as well as from the benefit of external analysis, we determined that both locations require substantial additional permitting and refinement before a project is ready to fund. Therefore, this perceived time advantage could be mitigated with cooperation from the federal and state government.

Further, we found that permitting for either alternative was not the pacing item for a market driven startup. We believe that it is better to identify an economically competitive project first, and then optimize the project for location. Neither site works if the overall project isn't doable.

And now, let me answer the question I posed earlier about our ongoing activities to make the project competitive. As I do so, please keep in mind my earlier comments that an Alaskan project needs cost reductions and fiscal modifications before it can be competitive.

The sponsor agreement calls for the completion of the first stage of the Alaska North Slope LNG Project work about mid-year. At that time, we will have completed the pre-conceptual engineering, the various optimization studies and the revised cost estimate for the MVP. At that time, we will have a revised understanding of the economics of the project and the information necessary to begin discussions with the LNG markets.

We are planning for success. We are developing our specific Stage 2 plan for key work products necessary to move this project beyond Stage 1. We will spend the balance of Stage 1 refining our economics, optimizing our systems and pipeline designs and preparing to move into Stage 2, if the Sponsors so decide. One major factor in this decision is whether the Stage 1 findings in June sufficiently suggest that we have the potential for an economically viable project. Another major factor in the decision will be the level of federal and state government support expected as the project proceeds. On this point, I would quickly point to what an important, positive signal the 1998 Stranded Gas Development Act, HB-393 gave to the sponsor group, when it was organizing for Stage 1.

By this summer, we will also have completed a variety of commercial initiatives necessary to advance the project. Federal fiscal modifications will be leveraging to the economic viability of the project. The completion of key elements of our first stage of work allows us to provide better definition of the MVP for discussions in Washington. In the near future, we will finalize an internal draft of a "white paper" on federal issues which will layout various ways forward and which will serve as the initial foundation for federal discussions in the coming months.

Also, before the end of Stage 1, we plan to submit an application for state fiscal relief under the Stranded Gas Development Act (HB 393). This will begin what we expect will be a multi-year process of negotiating and developing a proposed state fiscal contract. We would not expect that proposed contract to be submitted to the legislature earlier than the 2002 session.

I would like to use my last topic as the springboard for Sponsor Group's legislative interests in 2000. For this session, we hope that

the Alaska Legislature will favorably consider legislation in the area of commercial regulation of instate gas. We have developed a legislative concept that will provide that the instate gas volumes be regulated on a non-discriminatory basis that does not jeopardize the security of long term, contracted export volumes. The intent of this concept is first, to be applicable to all stranded gas pipelines; second, to be complementary to a non-discriminatory federal process; third to clarify state and federal jurisdictions; fourth to provide the rules for instate gas transportation and sales; and finally, to provide needed exemption from public utility designation. This concept would need amendments to the Pipeline Act, Public Utilities Act and Right-of-Way Leasing Act. Legislation in this area would resolve a key uncertainty in the area of commercial regulation and we respectfully recommend it to the Legislature.

In summary, Mr. Chairman, I would like to quickly highlight some, but not all, of the key activities that have been keeping us busy since we last met, those include:

- Development and refinement of an economic model specific to this project
- Description and definition of our 7 MTA, projected pre-shipping \$5-6 billion - Market Viable Project
- LNG Plant site selection analysis and reduction to two preferred locations
- Pipeline route analysis and reduction to two preferred alternatives
- Cooling medium analysis and selection for the LNG Plant
- Development of key cost estimating assumptions
- Development of a contract and technology selection strategy
- Numerous internal and external pipeline, plants and system design evaluations and optimizations
- Opening of our market liaison office in Tokyo
- Development and drafting of needed pipeline regulatory legislation
- HB393 application development for filing this spring
- Initial discussions and project updates to the Alaska delegation, DOE, and DOC in Washington, DC.
- Numerous contacts, meetings and project updates to the administration and legislators
- Project updates to the Port Authority Mayors as well as to the Anchorage, Kenai and the Matanuska-Susitna boroughs

... as well as many other previous and ongoing activities.

I hope that this brief overview of our plans and basic thinking will show the committee that the sponsors are actively trying to commercialize Alaska North Slope gas. At this point, I would like to thank the Chairman for the opportunity to testify and would be happy to address the committee's questions.