

AK LEGISLATURE SPECIAL COMMITTEE FILES SCOMM 155 3323

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Topic: Imposition of Requirements on the State of Alaska

Issues: TransCanada relies on numerous and significant State activities in its AGIA application. TransCanada expects or has asked the State:

- to "negotiate upstream fiscal terms with producers"
- to "thoroughly evaluate and significantly consider dedication of significant State resources to underwrite project financing"
- to work with TransCanada "to seek authorization to use federal loan guarantees to fund cost overruns"
- to work with TransCanada to establish a "bridge shipper" mechanism funded by the federal government

Facts:

- Section 1.14 (Rejection of Applications) of the AGIA RFA provides: "An Application shall be rejected if it requires additional actions by the legislature or by the Commissioners beyond those actions identified by AGIA."
- Among others, TransCanada has included the following State actions in its Application:
 - "TransCanada will work with the State to jointly seek authorization to use the **Federal loan guarantee** available for the APP to fund any cost overruns" (Executive Summary, page 16);
 - "TransCanada, in partnership with the State, would seek to establish a mechanism through which the U.S. Government would assume some or all of the initial risk of the Project by acting as a **bridge shipper**" (Executive Summary, page 16).
 - "TransCanada will rely on the State to take all feasible actions exclusively within its authority as a sovereign power to ensure a favorable economic environment for potential Shippers, including a) **engaging with the ANS producers to reach agreement on a commercially reasonable and predictable upstream fiscal regime**, (Page 2.2-52).
 - "TransCanada expects the State to fully utilize all of the authorities at its disposal as a sovereign government, taxing authority, natural resource lessor and royalty owner to encourage, **induce and persuade the ANS Producers** and explorers for new gas to commit gas reserves to the Project" (Page 2.2-57);
 - "TransCanada expects the State to thoroughly evaluate and seriously consider the financial and commercial feasibility of **dedicating significant State resources** to underwriting an alternative financing mechanism for the Project" (Pages 2.2-57 to 2.2-58);

Observations and Implications:

- While some may represent these as mere suggestions and creative thinking, it appears TransCanada could be "relying" on the State to take certain actions, and thus may not feel obligated or compelled to fulfill its commitments if the State does not deliver.
- Under the terms of the AGIA RFA, TransCanada's application should have been rejected, if it requires additional actions by the State beyond those included in AGIA.
- Many of the numerous proposals, reliances, and expectations that TransCanada identifies for the State would require significant State funds and policy choices not included under AGIA.
- If the State is willing to undertake these new requirements, other potential applicants should be given equal opportunity to propose a project under this broadened interpretation of AGIA.
- TransCanada's requirements suggest that they are unwilling or unable to advance the project without substantial participation of the State or Federal government beyond what is described in AGIA.

Topic: Amendments and Modifications to Project Plan

Issue: TransCanada's application envisions making changes to their proposed project plan in a manner not allowed under AGIA.

Facts:

1. AGIA (AS 43.90.210) allows a licensee to amend or modify its project plan (i.e. scope and schedule) only if the amendments or modifications are:
 - a) regulatory mandates,
 - b) needed to improve the NPV of project to the State, or
 - c) necessary because of unforeseen circumstances that were outside the licensee's control before license was issued.
2. During the Development Phase, a detailed Scope Management Plan will be developed by TransCanada for the project's Execution Phase. This plan will be based upon TransCanada's FMO Scope Management Guide (page 2.3-11).
3. During the Development Phase, a detailed Schedule Management Plan will also be developed by TransCanada for the Execution Phase. The Schedule Management Plan would contain processes, standards and requirements for updating schedules and reporting variances from the baseline schedule (page 2.3-11).
4. The Project Key Risk Assessment and Mitigation chart included in the TransCanada application (pages 2.7-5 to 2.7-8) describes certain risks and impacts to the project that will affect schedule, cost and the design basis. These items are unrelated to regulatory mandates or State NPV improvements, and since TransCanada describes them, they are by definition foreseeable. For example, the following items in the chart described as risks and impacts to the project could be quantified or addressed in advance by TransCanada with detailed contingency plans:
 - 2.3 – complexity of environmental issues
 - 3.1 – "heated market" for construction labor and equipment
 - 4.1 – First Nations issues regarding consultation in Canada
 - 5.1 – permafrost issues, slope stability, trenching
 - 5.2 – pipe and material availability
 - 5.3 – river crossing challenges
 - 5.4 – tight labor market

Observations and Implications:

- **There is no specific reference or other recognition in the TransCanada application to the prohibition on amendments or modifications to the project plan** (including scope and schedule) in AGIA (AS 43.90.210) unless such amendments or modifications are directly related to the three specific occurrences referenced in Fact #1.

- The TransCanada Scope Management Plan and Schedule Management Plan appear to **allow for amendments or modifications to the TransCanada project plan** that are related to activities or influences outside the three specific circumstances referenced in AS 43.90.210, and are not subject to the State's approval (Page 2.3-11 and Appendix B2, PMO Scope Management Guide).
- **The TransCanada application does not adhere to the requirements of AS 43.90.210** as it includes provisions for changing the project plan (scope and schedule) due to circumstances not referenced in the law, and not subject to the State's approval.
- It is not possible to know what amendments or modifications will be allowed because **the Administration has not made its contract (the "license") with TransCanada available to the public or the legislature.**
- If the Administration was to allow any modifications or amendments not permitted by AGIA, **potential bidders who did not bid because of AGIA's constraints could sue.**

Topic: TransCanada's Cost Estimate Quality at Open Season

Issue: TransCanada will have at best a "Class 4" estimate available at Open Season. This is a relatively low quality cost estimate with significant uncertainty, meaning that shippers will be asked to make binding commitments to a service with an ill-defined cost. This creates three potentially costly outcomes for shippers and the State:

1. Shippers (including the State) commit in the open season based on a Class 4 estimate, but final costs come in substantially higher, reducing the netback.
2. Shippers do not participate in the binding open season, recognizing the high risk associated with the low quality cost estimate.
3. The State funds 90% of the cost for TransCanada to improve its estimate beyond Class 4.

Facts:

- TransCanada estimates its proposed project to cost \$26.5 billion in 2007\$'s, \$0.6bn of which will be spent in the "Development Phase" and \$25.9bn of which will be spent in the "Execution Phase" (Tables 2.5.1 and 2.5.2).
- These estimates are of "Class 5" quality, as defined by the American Association of Cost Engineers (Section 2.5, paragraph 1).
- AACE defines cost estimates in terms of expected accuracy as follows:

Class	AACE Title	Upside	Downside	Project Definition Complete
1	"Bid/Tender"	+ 3 to 15%	- 3 to 10%	50-100%
2	"Bid/Tender"	+5 to 20%	- 5 to 15%	30-70%
3	"Budget Authorization"	+10 to 30%	-10 to 20%	10-40%
4	"Feasibility"	+20 to 50%	-15 to 30%	1-15%
5	"Concept Screening"	+30 to 100%	-20 to 50%	0-2%

- TransCanada intends to upgrade their estimate to "Class 4" during the "Proposal Sub-Phase" of the Development Phase (Section 2.5, paragraph 8).
- The "Proposal Sub-Phase" extends from receipt of license through completion of a binding open season (Attachment 2.6-2).
- The time period for updating this estimate to Class 4 is shown in Attachment 2.6-2 by the bar labeled "Pre-FEED" (Front-End Engineering Design).
- This Pre-FEED bar extends through open season, shown on the same Attachment.
- TransCanada spends 50% of Open Season Period costs (\$41.5 million), and 10% of the Certification Period costs (\$83.1 million), with the State required to pay the remaining \$500 million [Section 2.11(1)(a) and (b)].

- TransCanada does not use the cost estimate available at the time of open season to define the cost overrun liability for shippers. Instead, it establishes this baseline with the "Base Capital Cost" estimate that will only be available at the time of FERC certification (Certificate of public convenience and necessity or "CPCN"), four years after the open season [Section 2.2.3.6(1), Attachment 2.6-2].
- If the project proceeds to completion, TransCanada may include its just and reasonable costs in the tariff which shippers pay, meaning TransCanada bears no risk.

Observations and Implications:

- The best quality estimate that would be available for an open season is of Class 4 quality (+20 to 50% / -15 to 30%), although even that may not be available
 - since the pre-FEED bar on Attachment 2.6-2 coincides with the open season, it is not clear that a Class 4 estimate will actually be available for the open season, or if the open season will be based on the current Class 5 estimate.
- A "rush to open season" increases the probability of a failure due to the poor project definition, low quality cost estimate and resulting high risk placed on potential customers. It also results in the State funding 90% of the cost to upgrade the estimate.
- If the open season fails (an insufficient number of precedent agreements are signed), TransCanada bears the risk of \$124.6 million, the State risks \$500 million, and no pipeline results.
- TransCanada's proposal is a savvy way for them to transfer risk to the State and Shippers.

Topic: Commitment to Build

Issue: TransCanada has not committed to build a pipeline, contrary to the Administration's own assertions that AGIA will deliver a pipeline. Specifically, TransCanada has reserved the right not to proceed with construction if:

- it does not find the terms of debt financing acceptable;
- it does not find the terms of a FERC certificate acceptable;
- it believes that the aggregate volume of shipping commitments is insufficient;
or
- its Board chooses not to proceed with construction.

Facts:

- In Governor Palin's January 9th letter to ConocoPhillips CEO James Mulva, the Governor states "*...the alternative ConocoPhillips has proposed...does not meet the terms the Legislature established in AGIA to ensure that an open access gas pipeline is built...*" and critiques ConocoPhillips for "*an unenforceable promise that the producers might build a pipeline.*" (emphasis in original)
- AGIA requires the licensee to :
 - accept a certificate if offered by FERC [AS 43.90.200(a)]
 - sanction the project after obtaining the certificate [AS 43.90.200(b) and (c)] or abandon the project, transfer the certificate, data, etc to the State
- AGIA does not describe any permissible conditions precedent for either obligation.
- As TransCanada stated in its AGIA application:

"Commencement of construction by TransCanada would be subject to the following conditions precedent, which may be waived by TransCanada:

- *receipt of final authorizations from the appropriate regulatory authorities (FERC in Alaska and Northern Pipeline Agency in Canada) to proceed with construction, and transportation terms and conditions in such authorizations that are acceptable to TransCanada;*
- *securing of all rights-of-way, easements, accesses and major permits that are in form and substance acceptable to TransCanada;*
- *receipt of financial commitments from financial institutions on terms that are acceptable to TransCanada for funding the debt requirement of the Project;*
- *confirmation, to the satisfaction of TransCanada, that all Shippers which have executed PAs with TransCanada and other interconnected pipelines and facilities are not in default of those PAs and have either satisfied or have waived the conditions precedent;*
- *all Shippers have obtained certificates, permits, orders, licenses and authorizations from regulators or other governmental agencies in the United*

States and Canada as are necessary to enable Shipper, or others designated by Shipper, to export from the United States and import into Canada, and be delivered to the ultimate destination of Shipper's gas;

- *confirmation that Shippers which have executed a PA with TransCanada have executed the TSA, and in the opinion of TransCanada that the aggregate shipping commitments under all these executed TSAs are sufficient to meet the minimum volume requirement for the Project; and*
- *receipt of approval from TransCanada Corporation's, TC Alaska LLC's and Foothills' respective Board of Directors to proceed with construction."*

[Section 2.2.3.3 of Application, "Conditions Precedent to Proceed to Construction", page 2.2-60 (emphasis added)]

Observations and Implications:

TransCanada's conditions ensure that they control their company's risk exposure. However, TransCanada, not the State, controls whether the conditions in TransCanada's AGIA application are met and, therefore, whether a pipeline ever gets built under AGIA.

Topic: ANNGTC Withdrawn Partner Liability

Issue: Although TransCanada did not disclose this fact in its AGIA application, TransCanada potentially faces a multi-billion dollar liability associated with an earlier attempt to advance an Alaska gas pipeline project. This liability represents a real risk to potential TransCanada partners and the State, and if realized, could prevent a TransCanada project from advancing.

- TransCanada failed to disclose the risk of potential withdrawn partner liability in its AGIA application.
- TransCanada has not shown that the risk of potential withdrawn partner liability will be avoided through its proposed corporate structuring and the use of affiliates and subsidiaries.
- TransCanada has not proffered any waivers from withdrawn partners relieving TransCanada of any potential liability.
- TransCanada has not addressed the fact that even if it were to obtain a parent guarantee, the market capitalization supporting the guarantee is approximately half of the potential liability at project sanction (\$20 billion v. \$37 billion) and thus insufficient to backstop the risk to TransCanada and any partners.
- TransCanada has not addressed the fact that if the potential withdrawn partner liability was passed on to shippers through the tariff it would significantly reduce the netback to the State.
- TransCanada has not addressed the fact that the potential withdrawn partner liability could encumber not only TransCanada but any partner to the Alaska gas pipeline project, including the State.

Facts:

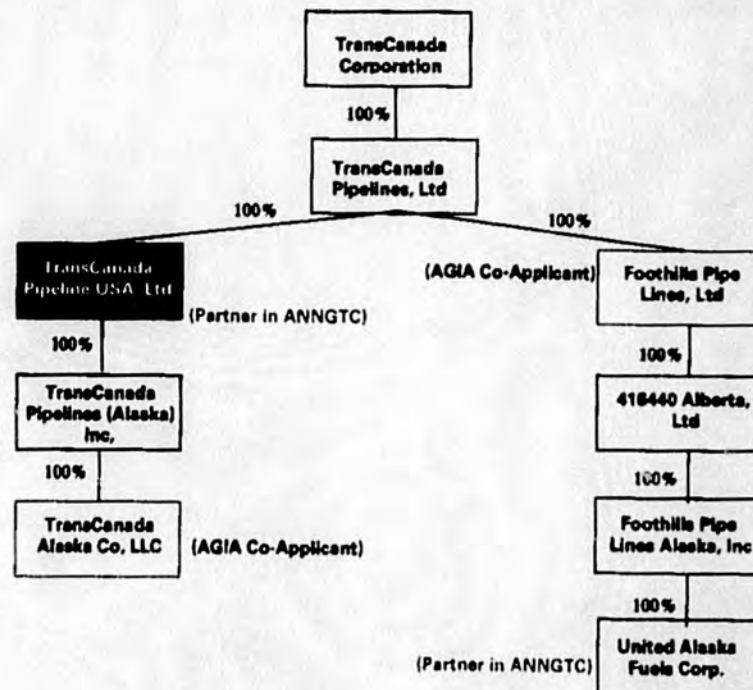
- AGIA requires an applicant to provide "information relevant to the commissioners' evaluation of the readiness and ability of the applicant to complete the project" [AS 43.90.130(19)].
- ANNGTC was formed in the 1970's in an attempt to build an Alaska natural gas pipeline project and spent several hundred million dollars to obtain a conditional FERC certificate in Alaska. (April 12, 2007 Alaska Northwest Natural Gas Transportation Company (ANNGTC) submission to FERC, page 1) ("Submission").
- Many partners have since withdrawn from ANNGTC. As these partners withdrew, they retained rights of repayment, except in the case of "undue hardship," from the partnership upon project startup. At the end of 2006, the liability reported by ANNGTC to FERC for these withdrawn partners was \$8.9 billion (Submission pages 2 and 11).
- The withdrawn partner liability will continue to increase at 14% per year (Submission page 9), and is expected to reach \$37bn by TransCanada's assumed project startup date of 2017.
- The withdrawn partners include entities owned by Sempra Energy, NiSource, Williams, MidAmerican, Loews, and PG&E. According to TransCanada, one partner

has transferred its rights to a trust for the benefit of the California Public Utilities Commission.

- TransCanada's market capitalization is approximately \$20bn as of January 23, 2008 (source: Yahoo finance), which is just over half the potential liability at startup.

Observations and Implications:

- TransCanada claims that payment of the withdrawn partner liability would cause undue hardship on the pipeline company and would therefore not be payable under the partnership agreement. Given the projections of potential project revenues that TransCanada provided in its application, however, it is not clear that the hardship clause would apply.
- ANNGTC's acknowledgement, cited in TransCanada's January 24, 2008 letter to the State, of the "uncertainties" created by its "contingent liabilities" conflicts with TransCanada's denial of any risk associated with the withdrawn partner liability. ●
- TransCanada identifies its AGIA applicant, TransCanada Alaska Co, LLC, as a subsidiary of TransCanada Pipeline USA, which is an ANNGTC partner (see diagram below, replicated from TransCanada's January 24, 2008 letter to the State). This corporate structure demonstrates the relationship between ANNGTC and the AGIA co-applicant, confirming the relevance of this withdrawn partner liability.
- Even a small uncertainty attached to such a large potential liability creates a very significant and potentially insurmountable concern to potential partners, shippers and the State.



Topic: Foothills Rights Under the NPA

Issue: Foothills rights under the Northern Pipeline Act (NPA) were established in 1977. Foothills would have to expend significant work to bring their certificates current as environmental laws have evolved, aboriginal rights have been established, and physical development along their certificated route has occurred. These developments suggest that Foothills rights under the NPA are of little or no value to the project, and in fact may result in additional cost and delay.

Facts:

- Certain Foothills subsidiaries are named as the project sponsors under the NPA, and have the rights and responsibilities as defined in that Act (NPA Schedule II).
- These subsidiaries hold conditional certificates of public convenience and necessity for portions of a pipeline route through Canada [NPA 21.(1)-(3)].
- Conditions on these certificates include, but are not limited to (NPA Schedule III):
 - Design, manufacture, location, etc must be consistent with drawing and specifications provided in applications submitted in the 1970's
 - The final design must still be approved by the Canadian government
 - Before approval, provide further studies related to socio-economics, environment, fisheries and agricultural concerns
 - Canadian labor and procurement plan, etc.
- The NPA requires that Alaska shippers pay not less than two-thirds of the cost of service for a pipeline in Canada from Dawson to Whitehorse, if built, for the benefit of Mackenzie Delta gas (NPA Schedule 1 paragraph 6). The State will be responsible for paying its proportionate share of this additional cost.
 - When the NPA was enacted, a moratorium on development in the Mackenzie River valley existed ("the Berger Moratorium"). Therefore, the NPA envisions the potential for a "Dempster Lateral" along a separate route, the assist in the development of Canadian Mackenzie Delta gas. Furthermore, the NPA requires Alaska shippers to pay a significant portion of the cost of this line (estimated at \$549 - \$705 million in 1985 \$'s, per NPA Annex III, or approximately \$1.1bn - \$1.4bn in 2007 \$'s adjusting for inflation per the US Bureau of Labor Statistics).
- Environmental law in Canada has evolved from the 1970's to today (CEAA enacted in 1995 and YESAA enacted in 2003). TransCanada acknowledges that "New and additional information will be required to meet mandatory conditions and prepare required plans and programs." [Application Section 2.2.13(4)].
- Development has occurred along the route originally specified in the Foothills conditional certificate, especially in and around Whitehorse, YT.

- Aboriginal rights have been defined and precedent established since the 1970's. TransCanada acknowledges the need for further consultation with, and accommodation of, First Nation interests [Application Section 2.2.13(5)].

Observations and Implications:

- Pipeline and compression technology have evolved significantly from the 1970's to today. The NPA authorizes the construction of a very specific system which cannot be constructed today, as the technology of the day has surpassed the specifications of the Act. An amendment to the NPA would be required to allow a modern gas pipeline to be constructed along the certificated route.
- The required "new and additional" environmental information will require an Environmental Assessment (Canadian equivalent of an EIS), putting Foothills in essentially the same position as any other applicant under the traditional Canadian National Energy Board process.
- The possible imposition of additional cost associated with the Dempster Lateral on Alaska shippers (including the State) would reduce the netback realized for every cubic foot of Alaskan gas produced.
- TCPL's use of historic NPA authorizations in Canada will:
 - Not expedite the project
 - Not reduce the project cost
 - Not help resolve aboriginal rights.

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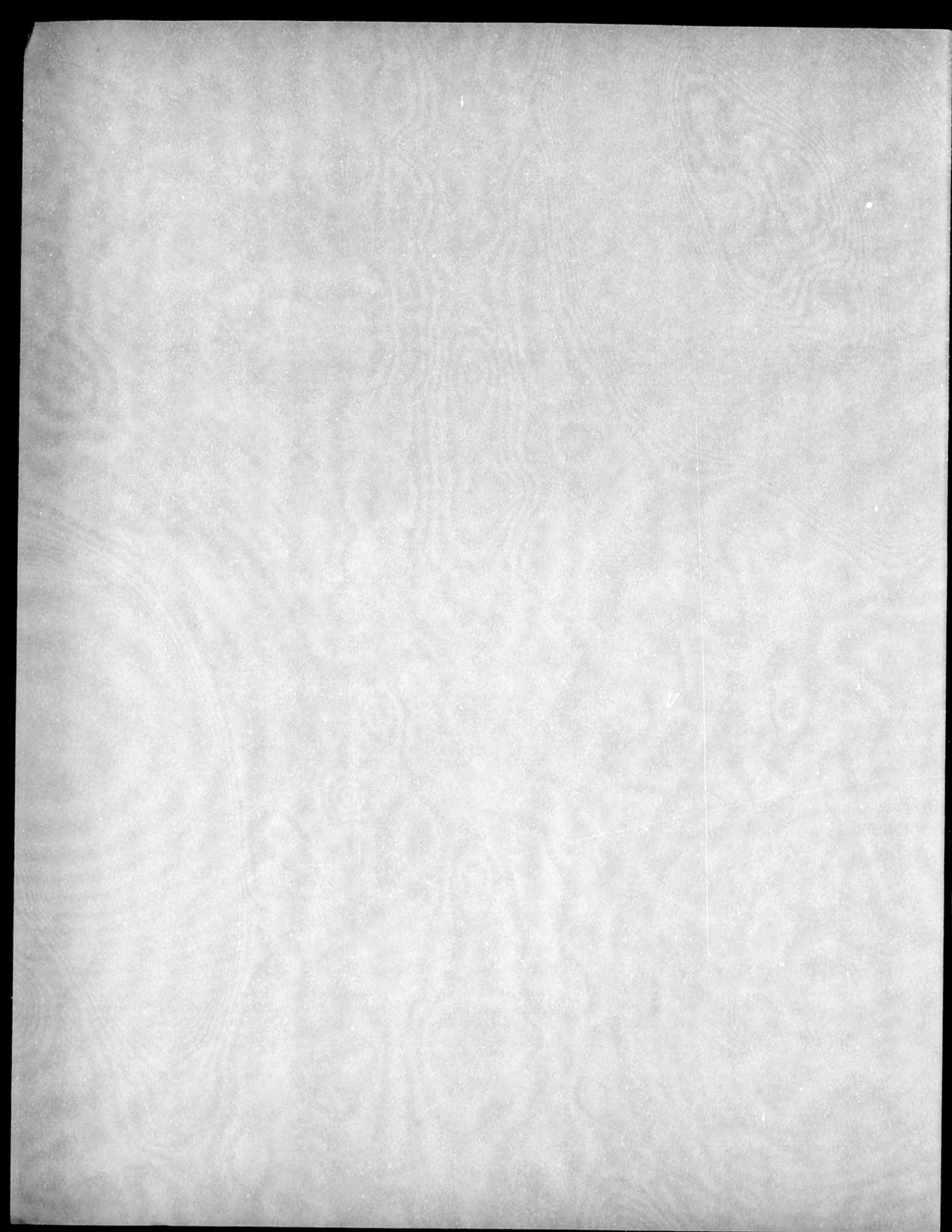
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ALASKA SPECIAL SESSION REPORT

June 10, 2008

OVERVIEW

Tour D'Alaska

Today is the final day of meetings in Juneau, and legislators aren't expected to return to the capital city until after July 8. Why the month off in the middle of a special session? According to Senate President Lyda Green, the "road show" is an important opportunity to hear from Alaskans.

Others call it a stall tactic. "I think it's pretty disingenuous," said Rep. Scott Kawasaki. "I don't think we need the entire Legislature to go to Barrow. That's not really the way we should be spending the public's money."

Rep. Ralph Samuels, the lone legislator to have cast a vote against Gov. Sarah Palin's Alaska Gasline Inducement Act, defended the Tour D'Alaska to a reporter: "If we don't reach out to the public, you're going to criticize us for that. You're damned if you do and damned if you don't."

The first stop is Fairbanks' Carlson Center where three days of hearings kick off on Thursday. Local leaders are advertising a rally Thursday evening to tell legislators, "We need energy now!"

"The energy situation is desperate. We can't wait until 2020," proclaims a print advertisement featuring Fairbanks North Star Borough Mayor Jim Whitaker along with the mayors of North Pole and the City of Fairbanks. The borough is a participant in the Alaska Gasline Port Authority, whose pipeline application under AGIA was deemed incomplete.

From Fairbanks, the show moves to the downtown Howard Johnson's in Anchorage next week. A full schedule including updated times and locations is available on BASIS.

In-state gas issues will clearly occupy a big chunk of the public's attention. But as Revenue Commissioner Pat Galvin told legislators, there is a balancing that needs to take place. Rep. Mike Chenault, whose district includes the Agrium fertilizer plant currently shuttered for lack of feedstock, offered an example of the trade-offs legislators face:

"If you bring gas in cheap enough that it opens up Agrium to go back in operation—350 good-paying jobs, 100 contractors—it's great for the community. But if it's too cheap, the exploration companies that are exploring for gas currently and providing gas in the Cook Inlet can't make money; they pull up stakes and go home. There's 500 jobs there that are good-paying jobs. So it's a balancing act."

Legislators also have to contend with the state's constitutional requirement to obtain the maximum value for its resources. And legislators outside the Railbelt have observed that it's unfair for the state to subsidize cheap gas to one part of the state at the expense of the state treasury.

Meantime, legislators seem to be gaining comfort with the idea of granting TransCanada a license. Samuels, an open skeptic of the Palin administration's strategy, acknowledged that it might work. "For years people have been trying to get the producers and TransCanada to make a deal, and if this deal would facilitate that, then even I would consider it a success."

For the record, Samuels still says it'll be hard to convince him to vote for the license.

All administration documents pertaining to AGIA, including consultants' studies, presenters' handouts and TransCanada's application, can be found at <http://www.gov.state.ak.us/agia/>. The Legislature's documents can be accessed via the Legislature's home page or at <http://www.legis.state.ak.us/specdocs.asp>

ADMINISTRATION PRESENTATIONS

Commissioners findings: "no" means they own us

In their June 8 overview of the commissioners' findings, Natural Resources Commissioner Tom Irwin and Revenue Commissioner Pat Galvin explained and defended their findings that TransCanada Alaska's natural gas pipeline plan is "likely to succeed," and is better for the state than a producer-owned pipeline or a smaller liquid natural gas pipeline.

"The reward is so huge; to me the risk is so small," Irwin said.

Irwin began by reviewing the Stranded Gas Development Act process, which culminated in 2006 when the Legislature declined to act on a tentative contract former Gov. Frank Murkowski negotiated with the three major North Slope producers. Irwin said the state made numerous concessions: "More than \$10 billion in future royalty revenues from the state to the producers, unquantifiable losses of production taxes, conceding sovereignty of the state in judicial, legislative and administrative issues. And nothing in this contract ensured development."

During 2006, he noted, natural gas prices rose to \$6/MMBtu. "We were in this odd stalemate, and it seems incredible that we have gas at this price, we have huge volumes of it, we have a market that's hungry for clean energy, and nothing was moving forward."

Irwin was Murkowski's commissioner of natural resources until the fall of 2005, when he and six others in his department resigned in protest of what they viewed as excessive and illegal concessions by Murkowski's gas team.

He said the Alaska Gasline Inducement Act (AGIA), proposed by Gov. Sarah Palin's team in 2006, was intended to encourage expedited construction of a gas pipeline through an open and transparent process that encouraged competition. Of the five applicants for a state "license," only one application—TransCanada's—was deemed complete.

In order to make a fair evaluation of the project's likelihood of success, Irwin said, the commissioners formed legal, commercial, financial and hydrocarbon reserves teams to evaluate the proposal and compare it to LNG and producer-owned options.

Irwin said the commissioners had experts evaluate various risks:

- Even without Pt. Thomson's estimated 9 trillion cubic feet of disputed gas, Alaska has enough natural gas resources to fill the pipeline for decades beyond the 25-year threshold. "The risk that there will be insufficient resources to fill the pipeline is low."

- The producers' concern that TransCanada may owe up to \$10 billion in liability to former partners of a defunct consortium that once sought to build an Alaska pipeline is not a significant threat. Irwin said the law firm of Greenberg Traurig and financial consultant Goldman Sachs opined that "the potential claims against TC Alaska and its affiliates are extremely weak ... and the risk of litigation over this issue does not present a significant barrier to the TC Alaska project's likelihood of success."

- TransCanada's proposed commercial terms are reasonable. The producers can construct and own a gas treatment plant on the North Slope and can purchase an equity share in the pipeline.

- Natural gas prices are not likely to decline enough to make the project uneconomic.

In comparison, Irwin said, a pipeline from the North Slope to an LNG plant in Valdez results in less value to the state and the major North Slope producers. Costs are significantly higher. The chance of success is lower, Irwin said, because of the need to negotiate multiple and concurrent agreements, and because there's no guarantee the project would get a license to export the gas to Asian markets. "That's a clear and evident risk—getting that export license, particularly if we don't have energy going to the United States first."

A so-called bullet line through Alaska terminating at a liquid natural gas (LNG) facility in Southcentral—a popular option with many in the state—also faces "significant risk" of not receiving an export license, Irwin said. But he assured lawmakers that the TransCanada proposal would not preclude liquefaction. "The door is wide open to someone who wants to come in and do an LNG project."

Irwin contended that an independently owned pipeline is more aligned with the state's interest than a producer-owned pipeline.

"Such an entity [producer-owned] is not driven to keep costs low," Irwin warned. "We've learned that the hard way. We've learned that all the way to the Supreme Court." The state has been in protracted litigation over the tariff on the producer-owned TAPS line.

High tariffs act to discourage new entrants, Irwin said, and the key for adding long-term jobs for Alaskans is a pipeline that encourages exploration and development.

Irwin concluded with a harsh assessment of what would happen if legislators vote down the AGIA license:

"We will wait and hope they do something but understand, they're not here because they love Alaska, they're here to make money, and they will look worldwide at their decisions. It's okay to stand up for what's right for Alaska. But 'no' means we're subservient to them; they own us."

Rep. Anna Fairclough opened questioning by suggesting the commissioners used inconsistent inflation assumptions in their evaluations by using 1 percent themselves and asking their consultants to use a 4 percent inflation factor.

Galvin said they wanted to test sensitivities by doing the analysis across a wide range of variables. "Trust but verify," said Irwin.

"I understand the sensitivities and issues because I sat through the 40 hours of presentations," Fairclough retorted. "But the people at home just get a sound bite from the media."

She asked whether there is an answer to the question of where the additional 2.5 Bcf/day would come from to fill TransCanada's 4.5 Bcf/day line, assuming Prudhoe Bay cannot produce the entire amount.

Irwin reassured her Alaska has the necessary gas resources.

"When did you ask [the Alaska Oil and Gas Conservation Commission] for that analysis?" Fairclough pressed.

Galvin said he did not have that information.

"What I don't want to hear is spin telling me where product is available," Fairclough said. She requested presenters give facts instead of "throwing darts at a project that's not before us," implying a producer-owned line.

Sen. Charlie Huggins told the commissioners it would be more helpful if they would share both pros and cons of TransCanada's project. "If there are downsides I think it's important that you share those and not let us discover them."

Irwin said he would do that.

Sen. Bert Stedman asked about the difference in regulation of a common carrier—such as an oil pipeline—and a contract carrier such as a gas pipeline.

In an oil line, said Irwin, if the line is full space can be made on a proportional basis for newcomers wanting to ship gas. In a gas line, where shipping commitments are made on a long-term contract basis, that's not the case. Irwin reiterated that a producer-owned gas line also wouldn't have an incentive to keep costs down because they pay the tariff to themselves.

"Why doesn't Exxon own all the pipelines in the world if it's such a sweet deal?" asked a skeptical Stedman.

Irwin said they have a high investment hurdle rate, and suggested it would be a good question to ask Exxon.

Rep. Bob Roses asked Irwin what Alaska loses or recoups if the state awards TransCanada a license under AGIA and TransCanada is unable to get shipping commitments and backs out. "TransCanada also gets a chance to say 'yes' or 'no,'" Roses said.

That's why AGIA mandates going beyond an initial open season, Irwin said. "If we stopped at open season we felt it would be a clear invitation to the producers, 'Don't put your gas in, and the TransCanada project is done.'"

But Irwin acknowledged the risk: "Will we get the gas? Tough issue."

Irwin expressed confidence that ultimately, rational companies acting on behalf of their shareholders would participate in a well-designed gas line project. If the producers continue to pursue their own pipeline, all the better, he added. "If we have two competing lines at that point, super."

Roses asked about financing under a scenario where TransCanada's proposed pipeline gets lower firm transportation commitments than expected.

Galvin said the administration asked its consultant to model a scenario where no additional gas is found and there is unused capacity as Prudhoe Bay declines. The shippers would still make sufficient returns, Galvin said. "That was actually a very significant finding for us."

Galvin confirmed Roses' understanding that if TransCanada backs out because the company thinks the project is uneconomic, and the state disagrees, the dispute would go to an arbitrator and the state would get its money back if the arbitrator deems the project economic.

"I'm ready to vote on this now," said Rep. Les Gara. Delay loses a field season and sets the process back, he warned.

Senate President Lyda Green defended the schedule she and House leadership set. "I don't want anyone to think we're delaying," she said, arguing that public participation and thorough vetting are needed for a decision of this magnitude. "If we want to blame someone, we can blame the process," she said, noting that the Palin administration had postponed several key dates.

Galvin: State bound only by AGIA

On June 6 Revenue Commissioner Pat Galvin reviewed the Alaska Gasline Inducement Act (AGIA) and the administration's request for applications (RFA).

The AGIA statute has three primary parts, Galvin said: the license application requirements and process; the terms of the AGIA license; and the upstream inducements. AGIA requires the state to provide a matching contribution of up to \$500 million to a licensed project and an AGIA project coordinator. The state is not required and has no legal obligation, once a license is issued, to support and defend the licensee's application before regulatory bodies, such as the Federal Energy Regulatory Commission (FERC), he said. "The administration's expectation is that the state would act as a good partner and would recognize the value our partner is seeking to acquire in this process, and we would not undertake means to undermine that expectation."

Rep. Anna Fairclough asked Tony Palmer, TransCanada's vice president for Alaska business development, to comment on the state's option not to defend the licensee's application before the FERC.

"We clearly would hope the state will be with us but it is not a legal requirement," Palmer said.

AGIA provides a mechanism should the state want to get out of the license and back a different project, but it will cost the state three times the licensee's expenditures to do that, Galvin said, noting the triple damages are limited to the licensee's expenditures and do not include state matching funds.

The state should do all it can to help advance every project, commented Rep. Mark Neuman.

"We will do everything we can ... to grant permits and authorizations to allow every project to move forward," Galvin said. But the state must not undermine TransCanada's project by providing financial assistance to a competing project: "We see value in the TC Alaska project so we are going to hold firm and move forward. If a competing project wants to move forward we will not stand in the way."

If the AGIA licensee wants out, the state is entitled to recoup all its matching funds with interest, along with the licensee's work product and other remedies provided by law, explained Galvin. If the Alaska subsidiary of TransCanada is purchased in the future, the new owner would be subject to these requirements as would all equity partners, he said.

Fairclough asked if the state can access TransCanada's work product if there is no contract breach.

Galvin said there are multiple situations where the state could acquire that information. The state could purchase the data at the licensee's net cost if the project is abandoned or not sanctioned within the required timeframes after FERC certification.

When the state helps pay the upfront costs it should get some of that information to put in its bank, Fairclough said. "I would like to know if we are acquiring some information for that \$500 million investment."

The state will have access to the data, Galvin explained, but whether it is public is subject to other provisions of law intended to protect the licensee's proprietary interests.

House Majority Leader Ralph Samuels asked a hypothetical question about the value of the work product should TransCanada opt to get out of the license and join with the producers on a project after spending \$100 million dollars of its money and \$500 million of state funds.

TransCanada's Palmer called this a moot question. TransCanada believes if granted the license it has lost the freedom to act in such a manner, he said. "TransCanada will have obligations to the state as our partner to pursue the project through AGIA." He said the company could not negotiate outside of AGIA without the state's permission.

If you found the project uneconomic would you still need the state's consent to get out of the contract? Samuels asked.

Yes, Palmer said.

Galvin said the request for applications (RFA) further defined the statute and the relationship among the parties. The RFA provided the assumptions for applicants to use in their cost and tariff estimates. It also expanded the definition of the project, allowing expansions to be financed with less than the 70 percent debt AGIA requires for the initial mainline project. Galvin said the RFA established what project plan changes will require commissioner approval and included general contractual terms such as methods for dealing with conflicts between the licensee and the state.

From a legal perspective the license is a contract, Galvin said. "The license constitutes the final contractual agreement between the state and the licensee." The RFA explicitly states that the license consists of the AGIA statute, the RFA and TransCanada's application, including all responses to additional information. "All obligations are spelled out between the state and licensee."

Neuman pointed to Barry Pulliam's June 5 presentation outlining TransCanada's requests of the state. Pulliam is with Econ One, one of the consultants retained by the Legislative Budget & Audit Committee (LB&A). The company's requests, he pointed out, include state engagement with the North Slope producers to reach agreement on fiscal terms and state cooperation in seeking federal government approval for use of loan guarantees for cost overruns. Neuman suggested it might be necessary for the state to enter into a contract with TransCanada to set sideboards on those requests. Could they be an off-ramp for TransCanada if the state does not act on those requests?

TransCanada is saying it hopes and expects that the state, as a good partner, will seriously consider these requests, but they are not conditions on the license or state obligations, Galvin said.

Palmer concurred. "I hope you are with me on these but they are not requirements."

Pressed by Sen. Kim Elton, Palmer said he agrees that issuance of the AGIA license does not obligate the state to more than the requirements in AGIA.

Rep. Mike Hawker called TransCanada's expectations "pretty profound," and questioned whether it is the state's intent to pursue them as "a good partner."

The state has an obligation to its partner to look at them in good faith and evaluate whether it wants to pursue them, said Galvin, noting that several would require legislative approval.

Rep. Les Gara said he suspects the North Slope producers would ask for tax breaks before committing gas to this project and TransCanada might become convinced that state should do that. If TransCanada doesn't agree with the state's decision on a tax rate will it see that as a state breach of the AGIA license? he asked Palmer.

"The level of fiscal take that the state will require of the producers is your business and theirs, not TransCanada's. We won't be involved," Palmer said, noting that if the state reaches an agreement on fiscal terms that allows the project to proceed he would be very pleased. "But that is your prerogative as a sovereign."

Sen. Bill Wielechowski expressed concern that TransCanada might be willing to give up control of this project by granting more than 50 percent ownership to equity partners.

Palmer said his company has not determined the exact terms and structure it will offer for equity partnerships but pledged to take this concern into consideration when making those decisions.

Galvin assured legislators that the license would transfer to the new owner along with its obligations and, should the license be breached, liability. "Whoever acquires the license also assumes this liability."

TransCanada: Pipelines are our business

Tony Palmer, TransCanada's vice president for Alaska business development, described the company's 50-year history in the pipeline business, its rationale for submitting an AGIA application and the project's benefits. Palmer, who has worked in pipeline development for the past 23 years, said TransCanada owns 36,500 miles of pipelines, including 12,000 miles of natural gas pipelines in the United States. "If we construct this pipeline for you it will increment our U.S. pipelines by 6 percent in terms of mileage."

The Alaska project is a very large investment opportunity for TransCanada in its core competency, the gas-pipeline business, Palmer said. "It is within our geographic footprint, it has synergies with our existing business, we have no conflicts with this business and certainly no conflicts with owning the pipe, operating the pipe nor expanding the pipe."

TransCanada sees the Alaska gas pipeline as a commercially viable project with strong economics. The company examined the supply-demand fundamentals for the project and commodity price expectations in preparing its AGIA application. "We are a conservative company and we would not give imprudent estimates," Palmer said: "We are not in the business of proposing to you that we will spend \$611 million, \$500 million of yours and \$111 million of ours, and then saying 'let's stop.' If we are successful in getting the customers and in moving this project with a certificate, it's our business to complete the pipeline and to successfully operate it over the next 30 or 50 or 100 years."

Palmer said TransCanada has done a great deal of thinking about how to move this project forward and how to align itself with the stakeholders required to make this project a success. He explained the company's history with the Alaska pipeline project, noting the Canadian government granted the company the rights to build the Canadian portion of the pipeline 30 years ago, and it began work on the Canadian prebuild seven years later. TransCanada still holds those rights, he said. This is a massive project in terms of capital costs but in terms of miles of pipe it is a manageable project for TransCanada. The company is currently constructing the Keystone oil pipeline, which is longer than the Alaska project and will have capital costs of \$13 billion to \$15 billion, about half the cost of the Alaska project.

AGIA does not require construction of a pipeline nor would any party guarantee a pipeline, whether the state offers them the rights under AGIA or not, Palmer said. No single party owns the rights to the 1,715 miles of land from the Prudhoe Bay to Alberta. Cooperation, collaboration and compromise are required to move this project forward, he said, pointing out TransCanada compromised in its AGIA application. "We think that if all stakeholders, the state of Alaska, the governments of the United States and Canada, TransCanada and the parties that hold the leases either today or in the future are prepared to compromise and collaborate this project can be a success and can be a success soon."

Palmer said development of Western Canada's gas resources has a striking parallel to Alaska. Western Canada initially had a small local market that has grown significantly. Western Canadian gas was the farthest gas from major markets and remains so. TransCanada started its pipeline system in Western Canada 50 years ago with three initial customers. Today it has 300 customers. "We also had a high potential basin. We think you have the same."

TransCanada is inherently aligned with the state's objectives for North Slope basin development, Palmer said. Fostering competition in the upstream end of the pipe is critical to achieving Alaska's basin development in the short term and long term, he said. Two years before TransCanada's project was completed in 1958, there were 180 natural gas wells completed in Western Canada. Over the last five years there have been between 13,000 and 16,000 natural gas wells completed each year. That's where the employment comes from, Palmer said. It's that drilling and servicing that will drive Alaska's economy, not the 50 to 75 jobs that will come from running this pipeline on an ongoing basis.

Palmer said TransCanada has a massive U.S. business that is integrated across North America: "We move 20 percent of North American gas. ... We move two-thirds of Western Canadian gas each and every day in our 36,000 miles of pipe. No other party has that record."

External parties analyzed the company's operating costs and found them 25 to 35 percent lower than its competitors, Palmer said. "TransCanada has not built its business by overcharging its customers."

In last 15 months, TransCanada has developed billions of dollars of pipelines and power projects, according to Palmer. The company has raised \$3 billion of equity in the financial markets in a very difficult time and \$2 billion in debt in last 15 months. "I would suggest to you that we have done so because we have a successful track record, we have financial capacity and we have good projects."

TransCanada's objectives for the Alaska project are early in-service, encouraging long-run basin development and providing equitable treatment for all customers. Spare capacity on TransCanada's existing North American pipelines will grow over the next decade, providing sufficient capacity for Alaska's entire gas supply. Palmer assured lawmakers that TransCanada will move Alaska gas where its customers want it moved, not solely to the Alberta market as some have suggested. He pointed out that TransCanada constructed 7,000 miles of pipeline in the 1990s and did so on schedule and within 0.6 percent of budget.

TransCanada agreed to all the "must-haves" required by AGIA, Palmer said, showing a listing of how the company met each requirement.

Sen. Bill Wielechowski asked if TransCanada would consider a 70-30 debt-to-equity ratio for pipeline expansions. The company has proposed 60-40 for expansions.

Palmer said the initial project has access to an \$18 billion federal loan guarantee, making the 70-30 ratio feasible. He noted it is not available for expansions so TransCanada believes expansions should be funded on a more traditional pipeline basis. "Our proposed 75-25 [for operations] for a project of this scale and this risk from a pipeliner's standpoint, is a very skinny pipeline equity ratio," he said. "It's not fair and we do not believe it is equitable to be funding future expansions without a loan guarantee on a basis that is not a fair balancing of risk and reward."

Sen. Charlie Huggins asked why the Canadian government is not offering a similar guarantee for this project. Is it unreasonable to ask for that?

"I do not believe ... Canadian government officials believe that they need to provide an incentive for you to move U.S. gas through Canada on the way to the lower 48," Palmer pointed out that the government agreed in a treaty with the United States 30 years ago to grant Alaska's gas the same tax treatment as Canadian gas. "That's what Canada believes it has done to advance the project."

How much money does Canada expect to gain from all sources if this is a successful project? Huggins asked.

In undiscounted dollars the Canadian federal government and the Yukon and British Columbia governments will receive total direct taxes of \$8 billion U.S. over 25-year life of pipeline, Palmer said, assuming no expansions.

Palmer listed the competitive enhancements TransCanada included in its AGIA application: inexpensive expandability of the pipeline, ownership of the gas treatment plant if no third party is willing to build it, equity opportunities for shippers committing gas in the initial open season and 75 percent debt as opposed to the 70 percent minimum in AGIA, which Palmer says will reduce tolls by nine cents per MMBtu or \$150 million per year if the project is shipping 4.5 Bcf/day of gas.

TransCanada has also offered to reduce its return in the event there is a 40 percent capital cost overrun and the federal loan guarantee does not cover cost overruns, and has offered a liquid natural gas (LNG) alternative if insufficient gas is committed through Canada, Palmer said: "We have done so to compete. That's not our preferred project [or] the project we think is the best for Alaskans nor the best for TransCanada."

Palmer said Western Canadian producers would benefit some \$10 billion from the addition of Alaska gas into TransCanada's pipeline system at Fort Nelson during the first 15 years. TransCanada will propose to Canadian regulators a toll reduction on its system of 13 to 18 cents per MMBtu, shifting approximately \$3 billion of that value to the Alaska project.

TransCanada's 15,000-mile pipeline system is the Alberta or AECO hub, Palmer explained. The Alberta hub is the most liquid market in North America, he said, and gas must enter TransCanada's system to trade at the hub. The hub would provide shippers the ability to move Alaska gas to markets across the United States. Palmer said there would be a 30- to 40-cent higher netback for Alaska gas—"more money in your pocket"—by entering this system because it uses existing pipelines from Alberta.

Rep. Craig Johnson asked if North Slope producers would have access to the AECO hub if they build an Alaska gas pipeline.

"If they do not interconnect with TransCanada's Alberta system they would have no access to the Alberta hub," Palmer said TransCanada believes it has the right to build the Canadian portion of the Alaska pipeline project. "If they got past that issue they would have to physically connect to have access to the hub."

Huggins asked when TransCanada estimates gas would be available through this pipeline for in-state use.

Palmer said 2018.

If the state participates in construction of a 1.5 Bcf/d bullet line project to ship gas as far as Homer does that violate the terms of AGIA? Huggins asked.

State participation in a project in excess of 500 MMcf/d would violate AGIA, Palmer responded. He said volumes above that threshold would take gas away from the larger pipeline project, jeopardizing its viability.

Revenue Commissioner Pat Galvin said the Palin administration is committed to getting gas to Alaskans as quickly as possible. But a small-capacity export project could eliminate the prospects for a major pipeline project. "A smaller-capacity line is a short-term potential fix to the local energy issue but could cost the state tremendously in the long term."

A smaller gas project can move forward, he added, if it is economic on its own, not requiring a state contribution.

Huggins said his constituents are concerned that issuance of the AGIA license might preclude making gas available to Alaskans. "We want to make sure we don't ... reduce our flexibility."

Rep. Mark Neuman said Alaska residents want access to low-cost energy as soon as they can get it. "Alaskans want access to our gas resources before 2018."

The administration has learned a lot about natural gas pipelines during the AGIA process, Galvin said, noting studies show the timeline for an LNG project is nearly identical to an overland route. "I caution you not to set up in your own mind or constituents' minds ... a choice between those projects now." Decisions to get gas to Alaskans must be based on actual facts and studies.

Natural Resources Commissioner Tom Irwin said as the pipeline project moves forward it will stimulate gas exploration in the state. "A lot of exploration will happen between now and [2020] that makes other gas available."

Huggins expressed concern that the shortage of gas supplies in Cook Inlet will limit development. "People are not willing to bet on the exploration for the delivery of gas."

Palmer said he understands how difficult the in-state gas issue is for Alaskans and the Legislature, and TransCanada hopes to serve that market. It will be 2018, however, before it can do so. "I suspect this body is going to weigh the value of early delivery of in-state gas relative to the employment and benefits of larger project."

TransCanada has committed to rolled-in tolls for the Alaska portion of the project up to 115 percent of initial tariffs, Palmer said, noting that rolled-in tolls are the norm in Canada. The levelized negotiated toll for a 4.5 Bcf/d project in nominal dollars, including fuel, would be \$2.76 MMBtu in 2018 to the Alberta hub. The company has estimated capital costs at \$27 billion [2007 U.S. dollars excluding an allowance for costs used during construction].

Palmer said TransCanada's project schedule was originally based on license issuance on April 1, 2008. Issuance of the license in August results in a 10-month net delay in the schedule, due to the loss of four summer months this year, he said. Under the revised schedule the open season would be complete in July 2010 and first gas would be shipped in September 2018. Palmer said TransCanada is committed to abide by its updated schedule if it receives the license in August. He later said that

should the Legislature approve the license in early July, and he knows that in advance, the schedule could be moved up by more than one month.

TransCanada's application provides the opportunity for parties that commit gas in an initial open season to become equity partners in the project. This will attract customers, Palmer said, improving the likelihood of project success.

Palmer said TransCanada's AGIA obligations are not conditional on a review of Alaska's upstream fiscal terms, but the company requests the state review those terms before the initial open season.

TransCanada can accommodate the extraction of natural gas liquids either in Alaska or downstream, Palmer explained. Shippers of gas will decide where to remove them, he said, pointing out that less gas moving down the pipe will result higher tolls. Palmer noted that TransCanada's system in Alberta is straddled by very large natural gas liquids extraction facilities. "I suspect they will vigorously compete for that business."

TransCanada Alaska Company, LLC will build the Alaska section of the project under the regulatory guidelines in the Alaska Natural Gas Pipeline Act of 2004, Palmer said; in Canada, Foothills Pipeline Ltd. will build under the Northern Pipeline Act.

TransCanada Alaska Company, LLC was never a partner in the original Alaska Northwest Natural Gas Transportation Company (ANNGTC) partnership and owes no obligation to that partnership or the withdrawn partners, Palmer said. ANNGTC was formed 30 years ago to construct the Alaskans section of a North Slope pipeline project. The partnership holds some assets, engineering and geotechnical work and regulatory approvals, but concluded it could not make a viable proposal to build the project and played no role in TransCanada's AGIA application.

Palmer noted that the partnership agreement does not contain a non-compete clause. The statement by some parties that there is a \$10 billion liability to that partnership today is simply not correct, Palmer said, noting there is only a contingent liability if ANNGTC builds project, puts it into service, and payment of the liability would not pose undue hardship on ANNGTC. The remaining two partners intend to formally dissolve partnership, he said. "We have started to have discussions with federal authorities about turning back some of the assets, specifically a right-of-way and original certificate issued by FERC."

Rep. Les Gara asked if the state studied this issue and is satisfied it is not a liability.

Galvin said the state took the North Slope producers' concerns seriously and had legal counsel discuss the producers' analysis with them. The state looked at how this liability could affect shippers should it be included in the rate base and if it was a potential barrier to their participation in the project. "The advice back to us is that it should not be a barrier for participation in this project or result in a hindrance to financing the project."

Gara asked if any of the withdrawn partners expressed an interest in bidding with TransCanada on the AGIA license.

Palmer said TransCanada was not approached by any of the withdrawn partners to join in its AGIA application.

Neuman, in comparing the TransCanada and "Denali" projects, asked why TransCanada is proposing to spend \$80 million to develop a Class IV engineering report before the open season, while the Denali sponsors are spending upwards of \$600 million to develop a Class I or II engineering report, which he described as a more detailed report.

Palmer said he would not speak to other parties' estimates to get to open season or FERC certificate. Based on its 50 years of experience and the information it has available today, TransCanada believes with \$84 million it can come up with a very credible capital cost estimate to hold an open season, Palmer said.

In its economic analysis the state evaluated the risk if TransCanada's cost estimate was off at the open season in terms of the impact on the tariff and ultimately the impact on the profitability to the producers and that risk is relatively small, Galvin said. "From an industry perspective the norm is to go to the level where TransCanada is proposing because the additional clarity of having the engineering get down to a granule level doesn't increase your confidence greatly."

Rep. Ralph Samuels suggested the state negotiate with TransCanada to see if it can get a better deal than what the company offered in its AGIA application.

Irwin said the administration made a conscious decision to have a fair, open and competitive process. It asked AGIA bidders for their best and final offer by a date certain and a high-quality company honored the state's rules. "We gave a promise," he said. "At this point to go back and say we want more. ... We would not be honoring our word to them."

Galvin pointed out that TransCanada did not know who would apply under AGIA and so put forth the best offer it could make. "AGIA created competition in eyes of applicants ... and we got the best offer available."

Rep. Mike Kelly asked Palmer how many companies TransCanada thought would submit AGIA applications.

Palmer said TransCanada had market intelligence that certain parties it had thought would apply would not, but it expected one major competitor would make a strong bid to compete with his company. "I pushed the board to get to this level."

Attorney says producers can't warehouse gas

With his trademark impassioned rhetoric and forceful confidence, a longtime state contract attorney Spencer Hosie impressed upon legislators the producers' duty to produce their natural gas holdings if conditions are economic.

"Do they have the veto power over a third-party pipeline to tender the gas?" Hosie asked. "No."

Three times the San Francisco oil and gas attorney with the firm Hosie McArthur LLP called Gov. Sarah Palin's Alaska Gasline Inducement Act a "game-changer." He addressed legislators by telephone on June 8 and 9.

Hosie reviewed what he calls the producers' duty to develop and market Alaska's natural gas. Under long-term leases signed decades ago the producers agreed to use their expertise and money to develop Alaska's North Slope gas. In exchange, they would get 87.5 percent of the value of that gas. The remaining 12.5 percent is the state's royalty share.

Calling it a relationship of mutual benefit, Hosie emphasized that under the agreement the oil companies give up the right to make decisions based solely on their own self-interest.

While the state's and producers' economic interests are aligned in some ways, Hosie says in one way they diverge: it is in the interest of the state as landowner to develop the resource right away. At times the oil companies don't want to do that—if they have an opportunity to earn more for their investment dollars elsewhere, that's a rational choice.

But it's not a choice they're free to make, according to Hosie. Under the lease, if the project is economic on its own merits they have an obligation to develop it. "That's the deal they made when they got the lease." Alaska's gas doesn't have to be the *most* profitable opportunity, it just has to be profitable under reasonable commercial terms.

Advancing an argument against tax concessions the producers have said they need, Hosie said under the lease, the companies agreed to take a risk. "The notion that they're entitled to a reduced risk is contrary to the deal they made."

Sen. Tom Wagoner asked if royalty rates have changed since the state negotiated its 12.5 percent share. Hosie said averages under newer leases are in the 24-25 percent range.

"If we get into negotiations [with the leaseholders] as to additional gives from the state, we should keep that in mind," Wagoner said.

"The state has honored that deal by living with the 12.5 percent," Hosie added.

Reviewing history, Hosie noted the oil industry has said they don't believe the pipeline project is economic. That led to the state's Stranded Gas Development Act and a failed tentative contract with the producers negotiated by former Gov. Frank Murkowski.

At that point, Hosie said, the state was left with three options, none of them good: concede to the producers' demands; wait for the producers to deem the project economic; or sue the producers to compel development. The legal avenue was probably the least attractive, he said: "It would be right out of Dickens' *Bleak House*—it would take a decade or more and it would be a black hole in terms of money and time."

The Palin administration, Hosie said, found a fourth way: AGIA sidesteps the issue of whether you can compel the producers to build a line by finding a third-party to build it.

Rep. Anna Fairclough questioned the accuracy of a claim Hosie made that Alaska could take its royalty gas and sell it at below-market prices for in-state use, including for the Agrium fertilizer plant on the Kenai Peninsula. When Hosie addressed legislators on his second day, he acknowledged that he had erred.

"I was wrong," the attorney said, citing a 1979 case in which Judge Allen Compton said it's unconstitutional for Alaska to sell its royalty-in-kind below market value.

"I want Alaskans to know this legislature has to work within the parameters of laws," said Fairclough.

Fairclough asked Hosie who determines when "reasonable commercial terms" exist—the Federal Energy Regulatory Commission (FERC) or the court system—noting that Hosie said litigation isn't in the state's interest.

Hosie said if negotiations fail, he assumes it would go to the court system. He reiterated that the state doesn't have to prove the gas pipeline would generate the high investment returns the producers normally seek, only that shipping the gas is economic. If the line is in progress and the producers refuse to ship their gas, Hosie said litigation would be much simpler than litigation attempting to force someone to build a line.

"The only question would be are the terms under which they could tender [the gas] such that production of the gas would be economic. That's fairly straightforward ... especially when contrasted to, 'Is it economic to build this \$30-billion pipeline?'" The latter question, he said, would involve more complex arguments such as the cost of building the line and prices at future dates.

Rep. Les Gara asked whether the producers' public pronouncements that they are planning a pipeline project might undercut their arguing in the future that a project is not economic.

"Absolutely," said Hosie.

Rep. Ralph Samuels contended that the TransCanada proposal does not offer strong protections against cost overruns. "The reality is the more it costs, the more they make," because an independent pipeline company makes its money by charging tariffs based on costs. Samuels said he can't see how cost questions could be avoided in litigation over whether it's economic for the producers to ship their gas.

Hosie responded that if TransCanada is moving forward with a project the question would be, given what the project costs, is it economic to ship gas? That's a very different question, he said, from fighting about whether it would be profitable to build a pipeline.

Observing that the state pays Hosie "\$500 or \$600" an hour, Samuels asked Hosie if he'd be willing to "put some skin in the game" if he's so confident. Would he be willing, for example, to take the litigation and do any work for free beyond three years?

Hosie said the true test of whether a lawyer believes in the integrity of a case is whether the attorney will take it on contingency. "And I would absolutely love that opportunity." He added that he charges Alaska \$309 hourly, a rate he said is sharply discounted from his corporate clients.

Rep. Jay Ramras expressed concern about the impacts of declining reservoir pressure on Prudhoe Bay if too much gas is removed, a concern the producers have expressed.

"If reservoir pressure is an issue, why then do you have 'Denali'?" responded Hosie, citing the name ConocoPhillips and BP have given their proposed pipeline project. "You shouldn't have to guess," he added. Echoing Revenue Commissioner Tom Irwin, he said, "Trust but verify."

Geologists offer rosy picture of gas reserves potential

"Alaska is an under-explored frontier gas province," geologist Dave Houseknecht told Alaska legislators in a June 7 presentation.

Houseknecht, of the U.S. Geological Survey, said his agency estimates total undiscovered gas in arctic Alaska is likely 227 trillion cubic feet (Tcf), based on probabilistic modeling, including 108 Tcf of gas in the Outer Continental Shelf (OCS), federal offshore waters. In addition, there is an estimated 35 Tcf of known natural gas reserves on the North Slope.

"What we've discovered is that our oil numbers are probably a bit on the high side and our gas numbers are probably a little bit conservative," Houseknecht said.

The geologist stressed how little Alaska's gas has been explored compared to lower 48 reserves. On the North Slope, for example, there have been three wells drilled for every 1000 square miles, compared to 250 wells per 1000 square miles in Wyoming.

"If this gas were in the lower 48 it would have been thoroughly explored and would have been producing gas for decades," he said of Alaska's gas. He noted that older estimates pegged Alaska's gas reserves at 90 Tcf, but technological advances in the 1990s have allowed for the addition of unconventional resources to the resource base—namely gas hydrates, overpressured basin-centered gas and coalbed gas.

In response to a question from Rep. Ralph Samuels on the status of gas hydrate research, Houseknecht said his agency is participating in a collaborative research effort and expects to release

its first estimate of technically recoverable reserves within three months. In a few years the agency expects to release an estimate of the quantity that is both technically and economically recoverable.

Sen. Fred Dyson asked about recoverable natural gas reserves in the Cook Inlet basin.

Houseknecht cited a "badly out of date" 1995 estimate of 2 Tcf, and said that number is expected to go up significantly. Bob Swenson, Alaska's Oil and Gas Division director, said the state has a more recent estimate of 17 Tcf.

Sen. Bill Wielechowski expressed concern that gas from the Outer Continental Shelf (OCS), which is federally owned and generates no royalty to the state, might be put through the pipeline. He asked at what point that gas might be developed and ready to go into an Alaska pipeline.

Houseknecht said he expects more offshore development now that the Chukchi lease brought in so much money, but does not know if bidders are looking for liquids or gases. OCS development will likely come later: "We believe OCS gas is farther on the horizon than onshore and state gas."

Swenson agreed, explaining that economics generally favor development of reserves closer to infrastructure first, even if those reserves are smaller.

Rep. Mike Kelly asked about Alaska's total liquids reserves.

Total liquids—crude oil and natural gas liquids—are estimated at 27 billion barrels (bbls) on Alaska's North Slope (including the National Petroleum Reserve-Alaska and the Arctic National Wildlife Refuge), Houseknecht said. Offshore there is likely an additional 15 bbls in the Chukchi Sea and 8 bbls in the Beaufort Sea, for a total of 50-plus billion barrels, according to the geologist.

As an aside, Houseknecht told his Alaska audience, "You'll be interested to know, in my 16 years in Washington I've taken the worst beatings of my life over the ANWR issue."

Rep. Mike Chenault said he's more interested in hearing from the Alaska Oil and Gas Conservation Commission (AOGCC) about gas offtake in Prudhoe Bay. Chenault said in a follow-up interview that he is skeptical that there is sufficient supply without Pt. Thomson gas to fill TransCanada's proposed 4.5 Tcf/day pipeline. The estimated 9 Tcf of gas at Pt. Thomson is currently tied up in litigation between the state and primary leaseholder ExxonMobil, which says the gas is uneconomic to produce.

The North Slope can provide 2.7 Tcf/day, which is reduced to 2.1 Tcf/day when carbon dioxide is removed, Chenault said. "So if the administration and TransCanada are saying they can build it without Pt. Thomson, then where's the other gas coming from? Maybe there's an explanation there, but I haven't heard that explanation yet."

When Rep. Anna Fairclough asked Natural Resources Commissioner Tom Irwin the following day where the missing gas would come from, he said the question is out there, but assured her, "We have the gas resources to make this project happen."

The AOGCC is scheduled to address legislators and the public in Anchorage on June 17. The commission is an independent quasi-judicial agency of the state charged with overseeing oil and gas development and ensuring maximum recovery of the resource.

Pro-jobs message draws legislative approval

Wearing his signature plaid work shirt, Alaska's Labor Commissioner Click Bishop garnered applause when he expressed his commitment to turning the gas pipeline into job opportunities for Alaskans.

Bishop said his plan could do for the Alaskan workforce what the Marshall Plan did for U.S. foreign policy: "This can be our legacy. With your help, my help, my staff's help, we're going to put Alaska back on that map."

Bishop and his staff outlined their plan to ensure that Alaskans are trained and ready for a gas pipeline and other resource development jobs, and for ensuring that those jobs are available to Alaskans. The plan is to identify skills gaps and then minimize those gaps through career awareness, effective labor exchange, job center networks and accessible training services.

The challenges to meeting the goals include economic cycles, a constant ebb and flow of workers, lack of awareness of high-paying blue-collar and professional jobs, the cost and accessibility of training, and job barriers such as driver's licenses and drug-free policies.

When Sen. Gary Stevens asked Bishop how he plans to help Alaskans access training opportunities, Bishop's candor drew laughter: "I'm going to come to the legislature and ask for your help—financially."

Stevens expressed support for improved training opportunities. "The present system does not work."

Brynn Keith, an analyst with the Alaska Department of Labor and Workforce Development, told legislators the department worked with industry partners to identify 113 AGIA-related occupations and used existing occupations supply and demand data to identify potential gaps. In 2006, she said, nonresidents accounted for more than 16 percent of workers in AGIA-related occupations. "That represents a significant opportunity for Alaskans."

Keith shared specific data for seven occupation groups. In 2006 the job class with the highest proportion of nonresidents—34.8 percent—was welders, cutters, solderers and brazers, with an average hourly wage of \$25.05. At 12.4 percent, civil engineers had the lowest proportion of nonresidents, and made an average of \$36.64 hourly.

Thirty-seven percent of workers in AGIA occupations were 45 years old or older in 2006, according to Keith. The "oldest" category of workers was operating engineers and other construction equipment operators, with 50 percent age 45 or older. On the other end, only 34.6 percent of carpenters were age 45 and older. Keith said the aging workforce is not an Alaska-specific situation.

Conrad Mulligan of the engineering consulting firm Arcadis presented modeling of short- and long-term employment generated by an Alaska gas pipeline. Mulligan broke down the project into a construction phase, operation phase and exploration and development phase, with separate assumptions for each, and used data from TransCanada's AGIA application, the Division of Oil and Gas and the state's consultants.

In the first phase—construction—for the first three to four years, Mulligan said an overland pipeline would create jobs numbering in the hundreds. Jobs would then spike for about two years, peaking at 15,000, and would drop off quickly thereafter. For a liquid natural gas (LNG) project, Mulligan said the peak would last longer and top out at about 16,000 jobs. The projections assume a gas treatment plant and LNG facility would be fabricated outside Alaska, major equipment and materials would be purchased outside, and the labor force would be constrained by size of the camp in Valdez.

In the operations phase, a TransCanada or producer-owned overland pipeline would generate about 200 operations jobs, Mulligan projects. An LNG project would generate about 600 operations jobs, including 400 jobs at an LNG plant in Price William Sound.

In the exploration and development phase, Mulligan assumes a producer-owned pipeline (which he referred to as "non-open access") would have no capacity expansion beyond 4.5 Bcf/day. Hence there would be no exploration and development work until current fields decline below a certain threshold. There would be approximately 47,000 exploration and development jobs between 2015 and 2045, but job creation could be delayed as late as 2026, according to Mulligan.

A TransCanada pipeline, in contrast, would have capacity expansions up to 5.9 Bcf/day and reasonable tariffs, Mulligan assumed. Consequently there would be favorable explorer economics and an exploration and development "rush." Mulligan projects 72,000 such jobs between 2015 and 2045, with jobs created as early as 2015.

Mulligan contended that an independently owned pipeline would create new natural gas jobs sooner. That's important for offsetting job losses as existing oil fields decline, and to maintain the existing skill sets and talent pool in the state, he said.

Rep. Anna Fairclough noted that the Trans-Alaska Pipeline System construction boom led to a spike in crime, and said she hopes the state looks at its law enforcement capacity.

Bishop said law enforcement is one of the categories included in the 113 AGIA-related job classes the department has identified.

Fairclough asked how the state would handle the big rise in unemployment following construction.

Some of the jobs are transferable to the exploration phase, Bishop said, adding that the state's plan includes future training of incumbent workers.

Sen. Fred Dyson raised concern that Alaska not grant Canadian workers labor rights without ensuring reciprocal privileges. Sen. Charlie Huggins asked Bishop to provide information on cross-border labor status so Alaskans can have that information up front.

Bishop said he has reached out to the Yukon Territory premier to discuss reciprocity so Alaskans could work on the 360 miles of line going through the Yukon, where he said there is a very small labor pool with a population of just 30,000.

The commissioner's jobs-for-Alaskans message resonated with legislators, who rewarded him with several bursts of applause.

CONSULTANTS

An army of advisors

The following tables list the small army of attorneys, economists and other consultants advising the administration of Gov. Sarah Palin, and the separate cadre advising legislators under the aegis of Legislative Budget & Audit Chair Rep. Ralph Samuels. While some of the names are familiar, those who advised on a gas pipeline contract negotiated by Palin's predecessor, Gov. Frank Murkowski, migrated to LB&A. Conversely, several who worked for LB&A under former chair Sen. Gene Therriault were scooped up by the Palin administration.

Palin's AGIA Contractors

Contractor	Scope of Work	Dates	total contract (thousands)
Dept. of Natural Resources			
Westney Consulting Group, Inc.	Assist gas line team/review & analyze application	6/07-6/08	\$3,940
Black & Veatch, Corp.	Assist gas line team/review & analyze application	9/07-6/08	\$2,525
Goldman Sachs	Assist gas line team/review & analyze application	2/08-6/08	\$2,500
Arcadis	Assist gas line team/analyze documentation & findings	10/07-6/08	\$750
PetroTel, Inc.	Assist gas line team/modeling	10/07-12/08	\$700
Energy Project Consultants, Inc.	Assist gas line team/review & analyze application	9/07-6/08	\$625
Energy Capital Advisors, LLC	Assist gas line team/review & analyze application	6/07-6/08	\$375
Gas Strategies	Assist gas line team/review & analyze application	2/08-6/08	\$350
W.R. Harper, Jr.	Assist gas line team/review & analyze application	6/07-6/08	\$140
Brown, Williams, Moorhead & Qu	Assist gas line team/review & analyze application	11/07-6/08	\$100
Wood Mackenzie	Research: North American gas service/global LNG/macro oils	11/07-10/08	\$96
Leverent Consulting	Assist gas line team/managing documents	10/07-6/08	\$60
MCB Communications	Gas line communications services	4/08-8/08	\$45
Northwest Development Co.	Peer review of request for applications	6/07-6/07	\$5
Dept. of Revenue			
Gaffney, Cline & Associates	Gas line fiscal and tax analysis	2/08-9/08	\$300
Dept. of Law			
Greenberg Traurig	Legal work	n/a-1/09	\$5,425
Bennett Jones	Legal work	n/a-12/08	\$900
Heenan Blaikie	Legal work	n/a	\$200
Total			\$19,036

Note that the Department of Law has other AGIA advisors—such as Spencer Hosie of the law firm Hosie McArthur LLC—who are not included on this list because they have long-term contracts to advise the state on an ongoing basis.

Legislative Budget & Audit Committee AGIA Contractors

Contractor	Scope of Work	Dates	Hourly rate	Amount* (thousands)
Econ One (Barry Pulliam, lead)	Analysis/advice on natural gas pipelines	1/08-12/08	\$350/hr. (Pulliam), others from \$225/hr. to \$575/hr.	\$300
Saul Ewing LLC (Bill Mogel, principal atty.)	Analysis/advice on AGIA applications	4/07-12/08	\$400/hr. (Mogel)	\$250
Steve Porter	Analysis/advice on natural gas pipelines	12/07-12/08	\$250/hr.	\$200
Dan Dickinson	Analysis/advice on natural gas pipelines	12/07-12/08	\$180/hr.	\$200
Benjamin Schlesinger and Associates, Inc. (Dr. John Neri, project director)	Analysis/advice on AGIA proposals and other gas line proposals submitted to state	2/08-12/08	\$240/hr. (Neri), others from \$45/hr. to \$400/hr.	\$100
Muse, Stancil & Co. (Lesa Adair, director)	Financial evaluation: natural gas pipeline development in Alaska	4/08-6/08	\$350/hr. (Adair), others from \$295/hr. to \$360/hr.	\$100
David Wood & Associates	Identify appropriate fiscal designs for development of Alaska natural gas	4/08-12/08	\$250/hr.	\$75
Alaska Natural Resources to Liquids	Provide overview of North Slope gas-to-liquids option	4/08-6/08	n/a	\$35
			Total	\$1,260

*Includes reimbursement of expenses.

ALASKA SPECIAL SESSION REPORT™

June 7, 2008

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ALASKA SPECIAL SESSION REPORT

June 7, 2008

OVERVIEW

The slog begins

Interviews with a cross section of legislators from around the state—and from varying political affiliations—suggest lawmakers are likely to approve an administration-backed license that would grant exclusive rights to a Canadian team seeking to build a pipeline to transport Alaska's North Slope natural gas reserves to Outside markets.

"They're not in the political business, they're in the business business," said House Speaker John Harris of TransCanada, speaking at a June 3 press conference. Harris did not indicate how he would vote, but he said the license will come to a floor vote. "I would venture to say the House will act within 45 days."

Lawmakers must first endure the remainder of seven days of marathon hearings that started Wednesday in Juneau, and a traveling air-and-road show to six Alaska communities. The final vote on Gov. Sarah Palin's proposal is not expected before the Fourth of July holiday. Legislators must act by August 1, 60 days after she officially forwarded her proposal to award the license to TransCanada Alaska Company, LLC and Foothills Pipe Lines Ltd., affiliates of Calgary-based TransCanada Corporation.

Whichever way legislators are leaning, they emphasize the imperative to diligently examine the proposal from all angles before promising incentives that include \$500 million in state money.

So far there is only one item on the agenda of the special session, the one-page SB 3001 and companion HB 3001. Introduced June 3 at Palin's request, the bill would enact the following language:

APPROVAL OF ISSUANCE OF LICENSE UNDER THE ALASKA GASLINE INDUCEMENT ACT. The commissioner of revenue and the commissioner of natural resources are authorized to issue a license under AS 43.90.010 – 43.90.990 to TransCanada Alaska Company, LLC and Foothills Pipe Lines Ltd., jointly as licensee.

This is not the first time legislators have summered in Juneau to ponder a plan to jump-start a gas pipeline. In 2006 Gov. Frank Murkowski called lawmakers into a June special session to consider his scheme for building a producer-owned pipeline under the state's Stranded Gas Development Act. Unmoved by ten days of browbeating by Murkowski and his surrogates in Centennial Hall, most legislators concluded that Murkowski's proposed concessions to the producers were untenable, and declined to bring the plan—which remained incomplete—to the floor. Two months later Palin defeated Murkowski in the August primary.

This time, legislators are controlling the venue and the agenda. Seated at folding tables in the Legislative Affairs Agency building's gymnasium atop a temporary rubberized floor covering (protecting the handiwork of former House Speaker Pete Kott a.k.a. Pete's Hardwood Flooring), legislators wave their arms to draw the attention of a microphone-toting page, who proffers the mike like a talk-show host. And a talk show it is, albeit a wonky one featuring number-laden PowerPoint presentations of up to 90 slides.

Despite the current positive outlook for Palin's AGIA license proposal, there seems to have been no diminution in personal acrimony between the governor and legislative leaders, particularly Senate President Lyda Green, who abruptly called a Senate floor session at 10:15 a.m. Friday, 15 minutes after the administration and TransCanada were set to begin their official pitch to lawmakers.

Apparently no one notified Palin, and at 10:05 when she arrived to observe the proceedings only a few legislators were present, including most of the Republican Senate minority.

"In all my years, I've never seen it so petty," said minority member Sen. Con Bunde.

The ill-timed Senate floor session featured the secretary reporting on bills the governor had signed.

The governor returned when the meeting convened an hour later and sat on the sidelines with legislative staff reading e-mails on her two Blackberries, as her commissioner of revenue began the state's presentation.

As always when a legislature meets, other agendas occasionally intrude. Today marks the deadline for legislators to override the governor's line-item vetoes in the capital budget. There is no joint session scheduled, and legislative leaders have said they don't believe they have the three-quarters supermajorities needed to override appropriations vetoes. Nine members are excused this weekend and it is unlikely that Sen. John Cowdery, who is recovering from surgery and has not attended any gas line sessions, will attend.

Palin is expected to introduce a bill later this month with her proposal to provide \$1.2 million in subsidy payments to help offset high energy costs. At Tuesday's House floor session several legislators rose to describe the woes their constituents face from rising energy costs.

Rep. Mary Nelson, a Bethel Democrat, said diesel fuel is now \$6 a gallon in Bethel, and higher in surrounding villages: "The implications of the [energy] crisis in our rural villages is huge. ... We don't need to prove there is a problem. There is a problem, clear and simple." Table banging signaled many legislators' agreement.

Rep. Harry Crawford also received table-pounding approbation when he rose to say legislators must think long-term. "The eye on the prize is making a long-term difference in the lives of Alaskans," said the Anchorage Democrat. "We have money today to make a long-term difference."

Haines Republican and commercial fisherman Rep. Bill Thomas described the pitiful fishing season thus far, and said he didn't even cover the cost of fuel on his first fishing trip. "Energy costs are getting us all."

But others bristle at the notion of establishing what they see as another handout. "This may well be the single worst public policy proposal I've seen in 30 years of watching state government," wrote Rep. Mike Doogan in his e-mail newsletter.

Special session schedule

According to the latest information from House Speaker John Harris' office, the schedule for the special session is as follows:

- June 3: *Juneau*: convene; bills introduced
- June 4-5: *Juneau*: presentations by legislative consultants
- June 6-10: *Juneau*: presentations by TransCanada and Palin administration (roundtable including Legislative Budget & Audit consultants on final day)
- June 12, 10-5: *Fairbanks (Carlson Center)*: in-state gas issues
- June 13, 9-5: *Fairbanks*: TransCanada/Palin administration/LB&A consultants
- June 14, 9-5: *Fairbanks*: TransCanada/Palin administration/public testimony
- June 16, 9-5: *Anchorage (location TBA)*: regulatory agencies
- June 17, 9-5: *Anchorage*: Pt. Thomson issues
- June 18-19, 9-5: *Anchorage*: TransCanada/Palin administration
- June 18-19, 6-8p: *Anchorage*: public testimony
- June 20: *Anchorage*: in-state gas issues
- June 24, 1-5p: *Mat-Su (Palmer Train Depot)*: TransCanada/Palin administration/LB&A consultants
- June 24, 6-8p: *Mat-Su*: public testimony
- June 26, 1-5p: *Kenai (Soldotna Sports Center)*: TransCanada/Palin administration/LB&A consultants
- June 26, 6-8p: *Kenai*: public testimony
- June 30: *Barrow*: community celebration day
- July 1: *Barrow (location TBA)*: agenda and time to be announced
- July 8: *Ketchikan (location TBA)*: TransCanada/Palin administration/LB&A consultants

Special sessions, including the current conclave, are limited to 30 days. Gov. Sarah Palin is expected to call a second special session to immediately follow the first. Under AGIA, the Legislature is not permitted to amend the license. Legislative leaders say they expect to return to Juneau in July for an up-or-down vote on the AGIA license.

LEGISLATIVE CONSULTANTS

Four consultants hired by Legislative Budget and Audit Committee chair Rep. Ralph Samuels addressed legislators on June 4 and 5; three gave presentations and one, John Neri, made informal comments and answered questions. Following are stories based on their presentations and lawmakers' questions and comments. The prodigious PowerPoint presentations and other documents are available on the committee website: <http://lba.legis.state.ak.us/>. Click "Gasline Proposals." When that displays click "Gasline Proposals Document Log." After the log appears, scroll down to presentations dated "6/4/08" and later.

Opening presentation: questions and comments

Economist Barry Pulliam of the California-based EconOne consulting firm opened the hearings with a review of what TransCanada proposes to do:

Build a pipeline:

- construct and operate a 1700-mile, 48-inch pipeline (initial capacity: 4.5 billion cubic feet per day, expandable to 5.9 bcf/day) from Alaska's North Slope to the Alberta-British Columbia Border, where Alaska's gas will join an existing network of pipes known as the AECO Hub;
- construct and operate a gas treatment plant on the North Slope—necessary for shipping gas—if no other entity does so;
- provide pipeline access for shipments to a liquid natural gas (LNG) plant if demand warrants.

Offer tariffs reflecting:

- 20-year, 25-year and 30-year firm transportation (FT) commitments with negotiated and recourse (cost-based) rates in Alaska and negotiated rates in Canada;
- a 70 percent-30 percent debt-to-equity ratio for recourse rates; 75:25 ratio for negotiated rates; expansions to be capitalized at a 60:40 ratio (a higher debt percentage means a lower tariff);
- a floating rate of return 9.65 percent higher than the 10-year U.S. treasury bond rate—this corresponds to about 14 to 16 percent based on historical T-bond rates;
- 100 percent cost recovery at 3.5 MMBtu/day.

Offer in-state use and expansion provisions:

- assess market demand by holding a non-binding open season every two years;
- offer rolled-in rates for expansions until tariffs reach 115 percent of their initial level (rolled-in rates spread the cost of expansion over all shippers; under incremental rates, the new shipper bears the full cost of expansion);
- provide a minimum of five in-state gas delivery points using distance-sensitive rates (i.e., shippers pay a reduced tariff for gas that travels a shorter distance) —there would be one rate for all of Alaska based on a weighted average of in-state deliveries.

TransCanada's proposed timeline calls for an initial open season in fall of 2009; in an open season shippers make long-term firm transportation (FT) commitments to ship their gas through the line or pay for the capacity if they do not—hence “ship-or-pay” commitments. As several legislators observed, that timeframe has already slipped.

TransCanada's timeline—based on April 2008 approval—proposes to reach certification from the Federal Energy Regulatory Commission (FERC) by 2013, when the company would begin construction, with first gas flowing in November 2017.

[On Friday, June 6 TransCanada presented an amended timeline projecting conclusion of the initial open season in July 2010, FERC certification by October 2012, and first gas by September 2018. Tony Palmer, TransCanada's vice president for Alaska business development, told lawmakers the new timeline is based on AGIA license issuance in August 2008. That four-month delay has rolled back the project timeline by 10 months, Palmer said, because the company will have to postpone until next spring field work originally planned for this summer. He assured lawmakers that if the license is granted on August 1, the company will commit to the dates in its revised schedule.]

In exchange for TransCanada's commitments, the state would provide \$500 million in the development phase—subject to a 50 percent match from TransCanada through the initial open season and a 10 percent company match from the open season through FERC certification; according to Pulliam the state's share would amount to 82 percent of TransCanada's \$611 million in expected outlays in the development stage, and 2 percent of the \$29 billion in total construction costs.

TransCanada may not include the state's \$500 million contribution in its cost base for the tariffs. That cost reduction translates to a 5-cent per million British thermal units (MMBtu) reduction in the tariff, according to the state, or \$2.2 billion to shippers over 25 years, of which \$1.2 billion accrues to the state. With the subsidy, TransCanada expects the tariff to Alberta to be \$2.41/MMBtu.

The state would also be bound to provide the other incentives promised in the Alaska Gasline Inducement Act (AGIA), such as a streamlined state regulatory process.

TransCanada also asks for the state's help in encouraging the producers to commit their gas to the line, and in convincing federal agencies to support TransCanada's requests, such as using federal loan guarantees to cover cost overruns.

Pulliam reviewed tariffs, noting a few key concepts: the tariff is fixed, while gas prices fluctuate; shippers, including the state, generally prefer a lower tariff, while pipeline owners make more money with a higher tariff; longer-term shipping commitments confer higher risk for shippers (hence they may be discounted). Based on current price projections, TransCanada's proposed tariff amounts to 25 percent of the net value of the gas at AECO over 25 years. Pulliam gave an extensive explanation of how recourse (cost-based) and negotiated tariffs are calculated.

Legislators didn't hold their questions or comments, and by the time Pulliam got past the first of his 60 slides it was nearly an hour into his presentation. As promised, Rep. Ralph Samuels, who presided over the first two days of proceedings, put no limits on legislators' questions.

Rep. David Guttenberg asked who has the rights to extract high-value natural gas liquids (NGLs) such as ethane, propane and butane from the gas stream. Without directly answering the question, Pulliam said if the gas liquids are removed in Alaska, the quantity would exceed the state's demand and the state would have to arrange to export them. The combination of pipe and marine infrastructure needed is not likely to be economically viable.

Lesa Adair, a consultant with Muse, Stancil & Co., agreed. "It's really more efficient to move everything on that one system than to build multiple systems to transport the products."

Sen. Charlie Huggins, who chairs the Senate's Special Committee on Energy, said employment is important to Alaskans. "I think it's important for us to look at that from top to bottom ... so that Alaskans have jobs out of this rather than us, once again, just exporting our raw resource."

Rep. Berta Gardner seized on a reference Pulliam made to owners of the gas, asking him, "Can you be specific as to who in your opinion owns the gas?"

"That really is a legal question," Pulliam deflected, but he added, "In my lay understanding the ownership lies with the producers."

Rep. Reggie Joule raised another issue: "One of the things that we hear over and over is that the country is hungry for gas. If some of this gas is going to be used in the tar sands, if some of our gas is going to be used in Canadian markets, how much of our gas is really going to get used in the lower 48?"

Joule continued: "Part of the argument against an all-Alaska gas line to get [gas] to the Asian market—is, we're really going to tick off the United States. It seems to me that if we're not getting the gas to U.S. market it kind of flies in the face of the argument."

Pulliam said there is a distinction between the physical and economic fate of Alaska's gas. Physically, the gas is commingled with other gas when it reaches the Alberta hub. So while the actual molecules from Alaska may be removed in Alberta, the overall supply increase effectively pushes gas into the lower 48. "It is effectively moving gas into the United States."

Samuels added, "Economically, for the state of Alaska—set aside the political concerns with the loan guarantees—if we sold our gas at the tar sands and we got the best price at the tar sands because we didn't have to pay the tariff to Chicago. ... Pure economics, we'd make the most market at the best market with the [lowest] tariff we can get."

Pulliam concurred, reiterating that if Alaska's gas is removed in Canada, it still increases the supply to U.S. markets.

The shorter the distance, the higher the return to the state, added Therriault.

Referencing the proposed timelines, Rep. Harry Crawford, a steelworker by trade, expressed frustration that it takes four years to receive a FERC certificate and only two years to build: "I can't tell you how much that irritates me. America needs our gas and there's no sense in holding it up this way."

Consultant John Neri, a regulatory expert, said it typically takes 24 months for FERC to opine on pipeline issue. "I'm not sure why it's four years" in TransCanada's proposal, he said.

Rep. Sharon Cissna asked how TransCanada proposes to minimize negative impacts of the pipeline.

Pulliam said he couldn't recall anything in TransCanada's proposal on that issue.

Dan Dickinson, a consultant to former Gov. Frank Murkowski on Murkowski's gas pipeline proposal, suggested the state could consider establishing a mechanism like the municipal advisory group Murkowski's team—which included Dickinson—had proposed. "That work already started and may be a good place to pick up."

Rep. Mike Doogan noted that TransCanada would like the state to negotiate fiscal terms with the producers to encourage them to ship their gas through the line. If legislators approve the license, he asked, is the state obligated to reach fiscal terms?

Pulliam said he believed it was just one of the things TransCanada would like the state to do, but was not a legal requirement.

[On Friday, June 6, Revenue Commissioner Pat Galvin and TransCanada's Tony Palmer separately confirmed that granting the license would not obligate the state to anything beyond what's offered in AGIA.

Galvin said the state encouraged AGIA applicants to propose ideas beyond the AGIA requirements that could add value to their projects. TransCanada's proposals have potential value, he said, and if the Legislature awards the license the administration will evaluate each one to determine if they are appropriate and will help make the project successful. TransCanada hopes the state will consider these proposals, Galvin said, but they are not conditions on the license or requirements of the state.

TransCanada expects the state will act as a good partner, Palmer said, and be as committed to this project as his company. These proposals are initiatives TransCanada is proposing to advance the pipeline project, he said, but they are not legal requirements. "Would I hope that you are with me on those things? Absolutely I would hope so."]

Huggins said he would like to see the AGIA license terms written into a contract. "It clears up the ambiguity of what one party thinks, one wishes, and brings it all together ... so that later on down the line it's not, 'Remember when you were briefed on the fourth of June in the gym, we answered it.'"

Rep. Mike Hawker pointed out, and Pulliam concurred, that the \$1.2 billion expected to accrue to the state as a result of the state's \$500 million contribution to the project isn't a one-to-one comparison, because the \$1.2 billion is spread over 25 years.

Rep. Gabrielle LeDoux asked about TransCanada's proposal to use the \$20 million in federal loan guarantees to back cost overruns as a hedge against that risk. Pulliam said it's unclear to him whether or not the company plans to reserve the federal loan guarantee for cost overruns.

Hawker opined that it's a lengthy and uncertain process to obtain the loan guarantee.

Financial assessment: "It's just really big"

Lesa Adair, vice president of the Texas-based consulting firm Muse Stancil & Co., told legislators the \$26 billion pipeline project (or \$29 billion, depending on assumptions) TransCanada proposes would be a financial and management stretch for the company—and for anyone—but that the company likely can handle it.

"They do have the core competencies to manage a project like this—it's just really big," she told legislators on June 5. Adair presented a financial assessment of the Alaska pipeline project's impact on TransCanada, and a comparable assessment for BP and ConocoPhillips.

TransCanada is a Canadian energy company that wholly owns six pipeline systems and is affiliated with six others in North America. With current market capitalization of \$23 billion, \$13 billion in long-term debt and 2007 net income of \$1.2 billion, the company's vision is to become the leading energy infrastructure company in the continent, Adair said.

With current market capitalization of \$144 billion and \$228 billion respectively, ConocoPhillips and BP dwarf TransCanada, Adair noted. ConocoPhillips has \$20 billion in long-term debt and 2007 net income of \$12 billion; BP has \$21 billion in debt and 2007 net income of \$29 billion.

Both ConocoPhillips and BP are buying back stock, Adair said. "That's a sign they have lots of cash but not as many good projects as they'd like."

TransCanada's small size relative to the producers means the Alaska project is very significant for the company, she said. TransCanada projects its net income would jump from \$1.6 billion in 2017 to \$2.4 billion in 2018 as a result of the pipeline going into service.

In the last five years, TransCanada has doubled its net income and has nearly doubled its long-term debt, Adair said. The "midstream" energy services sector TransCanada occupies has been in favor with investors. "At today's market capitalization, taking on this project will be highly leveraging to TransCanada, both positive and negative," she said. It would likely require raising additional equity, but if successful would significantly strengthen the company.

Assuming those who hold rights to the gas—the three major North Slope producers—commit to shipping their gas through the line, the project developer would still face significant risks, Adair said:

- Construction risk (weather delays, design delays, construction quality issues, etc.)
- Capital cost risk (inflation in cost of labor, materials; interest rate risk)
- Operating cost risk (depending on how shipping commitments are structured)
- Credit risk (creditworthiness of companies backing the shipping commitments)
- Regulatory risk (permitting problems)

If all of the firm transportation (FT) capacity is sold before construction, revenue risk is mitigated, she said. If some but not all of the capacity is sold, revenue risk is reduced but not eliminated. Adair said the other scenario she was asked to evaluate—the case where no one commits to shipping gas through the line until two years of operation—likely won't come to pass. "Everyone I talked to said, 'We don't believe that's a valid reference case.'"

That's because the way a pipeline owner recoups construction costs is by charging shippers a regulated fee—a tariff—to ship the gas. Shippers make long-term "firm transportation" (FT) commitments to ship their gas through the line or pay for the capacity if they don't use it. Without that revenue stream, potential financiers won't finance the line.

Asked how legislators should weigh the risk of cost overruns, Adair said: "I think it's something the market's going to have to grapple with, and something you are going to have to grapple with. The management of that construction risk is going to be key to getting a project financed."

The company can pass some, but not all, of the risk on other entities such as construction contractors, she said. Cost overruns due to regulatory delays, for example, can't be laid off on contractors. "There are certain inherent risks to a project that lie with the owners of the project."

The cost of the Alaska project far exceeds TransCanada's cumulative capital spending in the last five years, Adair said.

In contrast, the capital required is in line with ConocoPhillips' and BP's budgets, according to Adair. Those companies are used to taking on big financial risks and investors expect them to do so.

Adair explained that the pipeline's relatively low but guaranteed rate of return fits with TransCanada's investment philosophy, but provides lower returns than BP and ConocoPhillips typically earn.

Why, then, asked Sen. Bill Wielechowski, would the producers want to own the line?

"Because it's not about the pipeline to them," Adair said. "The reserve value will always outweigh the value of the pipeline to them." Owning the line gives the producers intangible benefits that come with control over such things as maintenance and costs, she said.

Rep. Mark Neuman expressed concern that given rising energy prices and development of alternative energy sources, demand for natural gas might fall.

Adair dismissed the notion, saying demand is currently met with imports and every forecast she's seen shows growth in demand. "The question today is what is that source to meet that demand, Alaska gas or LNG?"

Rep. Mike Hawker expressed concern that the public might come away with an overly optimistic impression of the project. "I'm very concerned about this false precision that gets built into these projections," he said of TransCanada's income projections. He noted that Adair isn't privy to the assumptions and numbers behind the projections.

Hawker also disputed TransCanada's claim that the company has no potential liability stemming from an earlier abandoned effort to build an Alaska pipeline [see **TransCanada and contingent liabilities**, *ALASKA OIL AND GAS LEGISLATIVE REPORT*, March 3, 2008]. Some have raised concern that the former partners in that venture can claim some of the profits from the line if TransCanada successfully builds it. "It seems to me we're headed for a cataclysmic legal battle," Hawker said.

"Is TransCanada capable of pulling this off?" asked Rep. David Cuttenberg.

They'll need help, but they have the competence, Adair said: "Whatever team manages development of the project is going to have to go out and pull together human capital." With prices up, there are lots of projects. "People—just people—are hard to come by."

The key, she said, is how the company negotiates its contracts. "They certainly have the core competencies given everything they operate and their experience in cold climates."

Dickinson: first, do no harm

Dan Dickinson said he was hired to point out "things to look for," and questions to ask. A former state tax division director turned consultant, Dickinson helped craft and later championed Gov. Frank Murkowski's petroleum production tax and natural gas pipeline proposal.

Dickinson seemed to suggest the 20 "must-haves" in AGIA—the demands the state makes in exchange for the "inducements" the state provides—are of less value than they might appear.

He broke down the must-haves into categories, designating seven of them as procedural issues related to obtaining the AGIA license. He pointed out that there is no enforceable commitment to sanction or build a pipeline. He also pointed out inconsistencies and ambiguities in TransCanada's application, noting that it assumes legislators will grant an AGIA license in April 2008.

Dickinson also portrayed the deal as better for TransCanada—and worse for the producers—than the company and the Palin administration suggest. He said that consistent treatment of costs yields TransCanada undiscounted cash flow contribution (money, in lay terms) over 25 years of \$109 billion, not \$16 million as suggested by administration consultants. Likewise, the producers make only \$74 billion according to his formulation, not \$183 billion.

And he pointed to seemingly illogical conclusions to cast doubt on some of the models used. He showed an analysis by administration consultants Black & Veatch that suggests a one-year delay in the project increases Alaska's total take from \$64 billion to \$66 billion. The increased revenue comes in the production tax as a result of progressivity.

When Rep. Les Gara expressed confusion about what Dickinson was getting at, Dickinson said, "It's precisely the frustration you're feeling that should make you ask questions about this model."

The consultant suggested legislators should not necessarily assume that current high gas prices would continue. "Bubbles burst, what goes up must come down," Dickinson said. He displayed a chart of inflation-adjusted energy prices over time showing what he called dramatically rising prices since 2000. "There's no particular reason to think this rise will continue until 2020," he said. "I think there will be a correction."

Dickinson also suggested that instead of looking at how much money the producers make under TransCanada's proposals, legislators should ask if the producers would make *more* money if they owned the line. In a simplistic sense, he said, if the producers owned it, they would get the money TransCanada expects to get from its ownership--\$74 billion or \$154 billion, depending on the analysis.

Dickinson suggested the state would need to make additional concessions—i.e., tax stability—to get the producers to ship their gas through the line.

Sen. Hollis French commented, “I bridle a little when I hear suggestions that we need to offer fiscal certainty.” He noted that AGIA promises ten years without changing the tax structure. “Before we do more I would like to see FT commitments.”

Dickinson suggested that the AGIA provisions intended to guarantee an open access line may be unnecessary because FERC has jurisdiction over rates and access issues. “Does TransCanada’s commitment really make a difference?” he asked. And although no one suggested otherwise, he asked “Are rolled-in rates money out of TransCanada’s pocket or just rearranging dollars between shippers?”

Dickinson encouraged legislators not to view awarding a license as the end of the competition and “the crowning of a winner,” because favorable treatment of one project would discourage competition.

“Maybe I’m missing the point here, but to me the competition happened,” commented Rep. Beth Kerttula. The issue now hinges on availability of gas to ship through the line, she said.

Dickinson described a scenario under which the state grants TransCanada a license but ultimately backs a producer-owned line. “If all the work that occurred to get through to a [FERC] certificate occurred, and then at that point the state changed horses, we would be responsible for three times the liability of the unreimbursed amount, which is about \$111 million, and you multiply that three times.”

The comment raised Gara’s hackles. “Are you suggesting at all that we consider granting a contract to someone and then breaching it?” Gara asked. “What does that do to our reputation if we grant a license and then pull it in favor of somebody else?”

Dickinson said that wasn’t his intent, that he was suggesting there might be a three-way negotiation between the producers, TransCanada and the state, that resulted in TransCanada agreeing not to claim triple damages.

Dickinson said TransCanada’s champions invoke five major reasons for supporting it, including enforceable commitments and a “dazzling” amount of profit for all involved. He then questioned each claim. But he perhaps inadvertently encouraged legislators to approve the deal by suggesting they instead consider an alternative justification for approving the license: it “probably won’t harm the prospects for a line and may strengthen them.”

Using a football analogy, Dickinson said legislators shouldn’t ask if awarding the license will be the touchdown play, but will it move the ball forward. “Are you better off having run that play or not?”

That inspired Sen. Con Bunde to poll the consultants on whether approving the license would harm the prospects for a pipeline.

Dickinson said he doesn’t believe it would, though he said there are conditions under which the state will owe TransCanada money.

Barry Pulliam ventured, “I don’t personally see harm.”

Lesa Adair said she agreed with Pulliam, and noted there are many more steps before there will be a pipeline.

“I see no harm,” said John Neri.

Bunde thanked the consultants and said, "Rep. Samuels, if we were on the floor I'd call the question."

INTERVIEWS

On June 5, 6, and 7 ALASKA SPECIAL SESSION REPORT's Rebecca Braun asked several legislators for their prognostications on the coming debate, and how they expect to vote. Following are their edited and condensed responses. The six unedited transcripts are available to subscriber-clients on request. E-mail rbraun@alaska.com.

A seventh legislator declined to be interviewed. Rep. Kevin Meyer, an Anchorage Republican and House Finance Co-chair who works as a procurement specialist for ConocoPhillips, said because of his employment he will not publicly discuss oil and gas issues. But he will cast a vote on the AGIA license, he said, because his constituents expect and want him to do so.

Harry Crawford: Keep the heat on the producers

Rep. Harry Crawford, a Democrat, has represented East Anchorage's District 21 since 2001. An ironworker by trade, he was a key supporter of an unsuccessful 2006 initiative to impose a tax on undeveloped gas reserves held in large North Slope fields.

Do you think the bill granting the license to TransCanada will pass?

I believe that it will pass in the House. I won't predict what will happen in the Senate.

What do you think your vote will be?

I expect that I'll be voting for the license—not because I like the proposal so much, but it's a way to keep the process moving and keep the heat on the producers. At some point, if the heat stays on the producers, they're going to come to the table and work out some sort of compromise.

If you could go back and change AGIA [the Alaska Gasline Inducement Act] knowing what you now know, is there anything you'd change?

There are some real interesting things they've come out with this morning, questions that haven't quite been answered. [It] probably should have [had] some more detail spelled out in it.

What do you see as the biggest risk to the state if you grant the license?

My one real worry is that at some point the producers come in and negotiate another deal. I don't want them to take control of this process, take control of the TransCanada [project], and continue to delay that way. I want some leverage that forces the producers, so they're not in control.

Let's say five years from now there's been a failed open season and things are looking bad and you're sitting at the Finance Committee table looking at a \$200 million appropriation to TransCanada for reimbursement under this license. What do you do?

At the point of that failed open season, that's where I go into second gear. That's when the reserves tax comes screaming back and it's going to be a lot tougher this time than it was last time.

Do you see the recently announced Conoco-BP gas pipeline proposal ("Denali") as genuine progress or more of the same?

AGIA induced the producers into coming up with a proposal of their own. If AGIA wasn't there I don't think "Denali" would be there.

It was said last week in the hearings in Anchorage that getting Alaska gas to the marketplace in the lower 48 lowers the cost to American consumers by about \$200 million over the life of the project. That in itself is a lot of reason for the producers not to want to get Alaska gas to the marketplace—because that comes out of their pocket.

Do you have any particular concerns with TransCanada's proposal?

[Rep.] Les Gara brought up one point that I don't think was thought through [when we approved AGIA]. The state has to help defend [TransCanada's] guaranteed rate of return in front of the FERC. I don't think that should be a requirement. That was in the TAPS proposal, that we had to defend Alyeska's rate of return. And that bit us.

... The whole structure of having an independent pipeline works better.

When do you predict the session will end?

I think that we're going to take every bit of the time that we have available to us.

Bob Roses: Leaning more towards approval

A freshman Republican representative, the former high school math teacher won the right to represent his a northeast Anchorage neighborhood in the 2006 general election, gaining 55 percent of the votes in House district 19.

Do you the AGIA license will pass?

I think it probably will. We're hearing that it doesn't hurt to giving them the license and it could help. Today we heard there could be some potential difficulty in a producer-owned pipe getting access to the Alberta hub. There would have to be considerable negotiations and possible legal action, which would tie up the process several years waiting for a permit decision.

Where do you lean on your vote?

I'm probably leaning more towards approval at this point. It's a bit of a change [from a few days ago].

If you could go back and revisit AGIA, would you make any changes?

Absolutely. When we had the bill in the Resources Committee, I offered a number of amendments that I thought would have made the process more fluid and would have improved the chances that the producers as well as other pipeline companies would bid on it. Three or four of the 20 "must-haves" I felt were obstacles to anybody with good business practices. I also offered an amendment that would have reduced the treble damages, a big issue that everybody keeps bringing up. None of those passed.

What do you see as the biggest risk to the state if we approve the license?

The biggest risk to us if we approve this license I think has to do with the treble damages and the \$500 million. And continued delay if they claim it's not economic.

Is there anything in TransCanada's proposal or about the company that gives you pause?

The company itself I think is a phenomenal company. I think that on a level playing field they probably are a phenomenal choice, but not being able to access the information for a producer pipe, there's nothing to compare it to. Based on what I hear they have the knowledge, the experience and the infrastructure to be able to pull the project off.

How do you view the ConocoPhillips-BP proposal—as a serious project or more of same?

I view it as a serious proposal.

Do you think we're better off with a producer- or independent-owned line?

I don't know. Quite honestly I think we're better off if the state owned the line. Then we can control all the parameters. The only thing we're doing then is getting people to monetize the gas. We'd make the money off the transportation, we'd make the money off of the taxes, we'd make the money off the transportation costs—it's a triple win.

Where does LNG fit in with that scheme?

I don't think the economics of the LNG line prove out. I see that as a project that comes in after we reach capacity in the line. As these new explorations come up, we extend the pipe, and that takes care of the first expansion.

When do you think the session will end?

60 days. A significant percentage of the membership wants to make sure we've looked at everything under a fine microscope and checked and double-checked before we sign on the dotted line, and in some ways I don't disagree—as much as I would like to have a summer. But that's what I agreed to do when I took this job. And legislators' questions provide information for the administration and TransCanada, so when they do the negotiations they are aware of our concerns.

Hollis French: Puts the ball back in the producers' court

A former North Slope oil field worker, French is an attorney who has represented Anchorage's Spenard area in the state Senate since 2003. French currently chairs the Senate Judiciary Committee and is a prominent Democratic member of the Senate's ruling bi-partisan majority.

Do you think the bill granting the AGIA license to TransCanada will pass?

Yes.

Do you think you will vote for it?

I haven't made up my mind. I lean in favor of an independent pipeline builder and TransCanada looks like the one with the greatest chance to go, so I start off favorably disposed.

If you could go back now and revisit the AGIA process, is there anything you'd change in the bill?

There were some interesting questions today about treble damages. [Legislative consultant] Dan Dickinson said there are ambiguities in that statute. I haven't had a chance to go back and revisit it but that's something we focused on in Senate Judiciary so if there are ambiguities there I feel a little bit responsible. So I want to go back now and see. That's the example that comes to mind most rapidly.

What do you think is the biggest risk to state if you grant the license?

The gas supply. The whole thing hinges on the gas supply. Theoretically there's no risk at all if you give it to Conoco and BP because they have the gas supply, but you could say they won't nominate it until they have tax terms, so that's the same problem you have with TransCanada.

If you give a license to TransCanada and nothing happens you're also out \$500 million.

Yes, you only get back the \$500 million if you have a pipeline, through a reduced tariff.

But everything indicates that it's an economic project; the ball is almost back in BP and Conoco's court. When Goldman Sachs says this pencils out, when Black & Veatch says this pencils out and EconOne says this pencils out, when TransCanada says this pencils out, at some point the earth sort of shifts. Can BP and Conoco now say it's not economic?

If it's so economic, why do you need to give a \$500 million incentive?

That's a great question, except that we get it back. It lowers that tariff so it's an economic stimulus that pays itself back.

Alaskans have had some recent experience with "independent outside experts"—Pedro van Meurs comes to mind—not always giving the public their real opinion. Do you have any reservations about the fact that these consultants are paid by the administration?

Some. Where you get your money from definitely lends a certain bias to your perspective. On the other hand, Goldman Sachs has to go back into the world and do business and if they say this is an economic project when the reality suggests that it's clearly not, they damage their own business prospects, much the same way that TransCanada could not continue to build pipelines if it had cost overruns on every one of its projects.

You're conspicuously absent from the special energy committee where the bill was sent. What do you make of that?

Given the format of the proceedings I guess I don't feel any disrespect. Everybody's free to ask questions. It isn't as if we have to wait until the committee members have asked their questions before someone else gets to go.

Is there any significance to being on the committee?

At some point I assume there'll be a committee vote on moving the license to the floor. That's sort of a ministerial task. This is such a big topic I don't see any likelihood of it dying [in committee]. It's got to come to the floor.

What's your biggest concern about the TransCanada proposal?

At least two people have come to me independently in the last week and said, "You gotta worry about First Nations—there are First Nations in western Canada and no one's talking about it." The administration's findings skipped over that in like two sentences. So I'm contemplating a Judiciary hearing on that topic three weeks from now, when the road show is between Mat-Su and the Kenai.

When you predict the Legislature will finish?

Sometime in July, after the fourth.

Gene Therriault: *Why would anyone vote no?*

Therriault has represented the Fairbanks suburb of North Pole in the Legislature since 1993, serving first in the House, and, since 2001, in the Senate. He served as Senate President in 2003 and 2004 before losing out to Ben Stevens in what led to an acrimonious rift within the Senate Republican caucus. As leader of the Senate's five-member Republican minority, he has often supported legislative initiatives pushed by Gov. Sarah Palin.

Do you think the license will pass?

If the vote were to happen today I think it would pass, overwhelmingly, because those people who I suspect are in the "no" column have not come up with a reason to justify their position, from my perspective, and even the consultants that we heard today when pressed a little bit said, "We don't think it hurts, it might in fact help." So why would you vote no?

And your vote?

If I were to vote today, it would be yes.

If you were to go back and redo AGIA, is there anything you would change?

I don't think so. If there was something in AGIA that they just couldn't incorporate, I think we would have heard about it from TransCanada. Or we would be hearing more from the producers if one of the must-haves were just a killer for them.

What do you see as the biggest risk to state in granting the license to TransCanada?

I haven't sensed anything that is a tremendous risk. The \$500 million—there's no risk there to me, especially when we've seen the numbers there. We get a return, and we get all those other things.

What if we spend the \$500 million and no FT commitments are made?

The players are all on the court. I believe a pipeline will be built and I believe it will include TransCanada. Even if what we get for the \$500 million is better information, as we get closer to the point where I believe the companies will ask the state for an economic give, we will be in a better position to evaluate whether it's legitimate, or whether it's too much, and what our counter-offer should be. And it will be billions of dollars.

Do you think the ConocoPhillips-BP proposal is a legitimate proposal or more of the same?

I can't tell. But when they put "Denali" on the table and they came around individually for meetings in offices, I just wanted to verify, so I said, "So Conoco, you're removing your proposal [submitted in November]?" They said, "Yeah, it's like it never existed." And I said, "So, when will we get information on your new proposal?" And they said, "Well, it's not a proposal, it's a project." And I said, "So therefore I will have less information on it than I will on the Conoco [proposal]?" And they said, "That's right."

So there's even less for me to look at as far as whether it's real or not than there was with the Conoco proposal.

Do you agree with Dan Dickinson that some AGIA provisions are redundant or unnecessary because of federal regulations?

Shame on us if we rely on a federal agency, [one] that we have no control over, for all of our protection. I think that's a bad move as sovereign.

Plus, the FERC regulatory package doesn't necessarily apply across the board.

When do you think the session will end?

Middle of July. July 14.

Wes Keller: "I'm really excited about it."

A former legislative aide to Sen. Fred Dyson, Keller was appointed by Gov. Sarah Palin to his Wasilla House seat in 2007, replacing the resigned (and since convicted) Vic Kohring. A

Republican, Keller has taken a much different approach to oil and gas issues than his pro-petroleum predecessor.

Do you think the AGIA license will pass?

Yes.

Do you think you'll vote for it?

Yes.

You weren't a legislator when AGIA passed. From your perspective now, are there things you wish your colleagues had done differently?

Nothing right off the top of my head.

What do you see as the biggest risk to the state in granting the license?

If TransCanada does not get awarded the license now, I think it's just kind of like kicking your chair back and walking away from negotiations, because we'd only have one option—we'd have to wait and see what the producers decide to do. They have said what they are going to do, and I hope they follow through, but it's nice to feel like at least we have enough of a place at the table to keep track of what's going on.

Do you think the ConocoPhillips-BP proposal is real or more of the same?

I think it's more of same [delay tactic], if you presume that oil prices are going to be high, which I tend to. There was a couple really telling things [said] in Anchorage. One of them was the number the savings would be to North America if the pipeline gets built. That savings come from somewhere and it comes from the shareholders of the producers. So the point is that delay, if the prices are high, works to their shareholders' benefit. They're not doing anything wrong, but if they're out to maximize the benefit of the leases they have, the slower it goes the better.

Do you see anything in TransCanada's proposal that gives you pause?

No. In fact, I'm really excited about it. I'd much rather have someone doing it that has half their skin in the game than somebody that just maybe has a fingernail tied in. That's the difference in the size of the company. TransCanada has a lot to lose if they fail so I think TransCanada's going to be a lot more motivated to get the job done.

And it provides a significant consistent cash flow for TransCanada. I used to be a custom home builder, so I worked feast-and-famine. That really limits what you can have on line as far as quality personnel and that kind of stuff. Even though it's just going through their bank account, the cash flow is really important for them to maintain as a bigger company.

When do you think the session might end?

That's a question that I hadn't even thought—being the new kid I'm just trying to get through [laughing]. Campaigning is pretty much eaten up, so is vacation.

Bert Stedman: A set-up for a failed open season

Republican Stedman co-chairs the Senate Finance Committee. He has represented Sitka and surrounding areas of Southeast Alaska in the state Senate since 2005.

Do you think the bill will pass?

I don't know. Hopefully the other legislators are not locked into their positions yet, and will let this process unfold and look at the information.

Which way do you lean on approving the license?

I think the markets are going to give us a gas line. The oil basin in Prudhoe Bay is now 30 years old or so. The adage of "30 years waiting for a gas line" isn't quite accurate because you can't take the gas before the oil or you end up losing value. And with the price of gas being \$9, \$10, \$12 and the price of oil—

Are you saying we're going to get a pipeline regardless, so perhaps that argues against giving this license and benefits to induce it?

I think with those issues along with the market demand we'll see construction of a gas line. How we, the state, decide to craft it, if we're going to try to do some engineering through the AGIA process or we're going to let the market evolve and then deal with our gas tax structure in the time frame.

Are you saying, we don't need to give this license because all these outside factors will get us a pipeline anyway?

Oh, I think we'll get a pipeline—the markets are going to push a pipeline forward. ... The pieces are in line to move forward with construction of a gas line. During the time frame of the [past] 30 years there was virtually a nonstop momentum.

You voted for AGIA. Is there anything you'd change now with a little bit of hindsight?

There's no doubt there's things in that bill that I'm uncomfortable with. I don't like the \$500 million. I think it's way too high. I don't like the 90-10 split, I think that is extremely out of line. After a 50-50 split to an open season, the state reimburses 90 percent [of the applicant's costs] to FERC certificate. That is too aggressive of a position, especially with the natural evolution of the marketplace pushing a gas line forward.

The question is do we need to spend \$500 million to push this forward, and do we want to use the \$500 million and the state's position to put TransCanada in a better position to negotiate with the producers.

Do you regret your vote on AGIA?

Oh, I don't know. I think AGIA would have passed anyway.

Clearly there were some things in AGIA—in the initial bill there was 80 percent reimbursement and at the end we went up to 90 [percent], which to me was really bizarre, and the triple damages is another issue. I think you can accomplish the same incentives with substantially less exposure to the state.

Sen. Huggins' suggestion, to do a contract to clean some of this stuff up if we go forward, is something that we need to consider. We should be looking at minimizing and controlling our risk. I argued that through the AGIA process. I wasn't very successful.

What would be the advantages of writing a contract between the state and TransCanada?

Cleaning up the understanding of the duties of the state and TransCanada.

But at the end of the day if there's two projects going forward, and one project is with folks that had gas and one without, and the group that has the gas and wants to do a project and commit their gas—with virtually the same timeframe— why would you do the other project?

Do you see the Conoco-BP proposal as a genuine proposal or more of the same?

It's definitely not more of the same. I think that's a political sound bite thrown out to the public. This is the first time in the history that I'm aware of that those companies—and you might as well include Exxon in the group—have ever talked about going to a pre-application process to FERC.

What do you see as the biggest risk to the state if we grant the license?

The producers going forward to FERC and committing their own gas to their own project, while the state has a contractual obligation to TransCanada and the financial exposure of \$500-plus million.

FERC has never, as far as I know, issued a certificate without any firm transportation shipping commitments. And from my meetings with FERC, [I believe] they would prefer to have one applicant versus two competing applicants because of the sheer magnitude of the workload to go through the certificate process.

What do you see as the biggest flaw in the TransCanada proposal?

Exposure to the state: \$500 million and 90 percent. As I recall, the last group [i.e., the previous legislature] walked away from 50 percent and \$50 million exposure [under Gov. Murkowski's proposal]. I think we could have gotten TransCanada or some other entity at the table for a lot less.

And triple damages.

We should be clear that AGIA is set up for a failed open season and for that applicant to ask for FERC certificate without firm transportation commitments.

What's your prediction on when the session ends?

The end of 60 days.