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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
    - o 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 if 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:

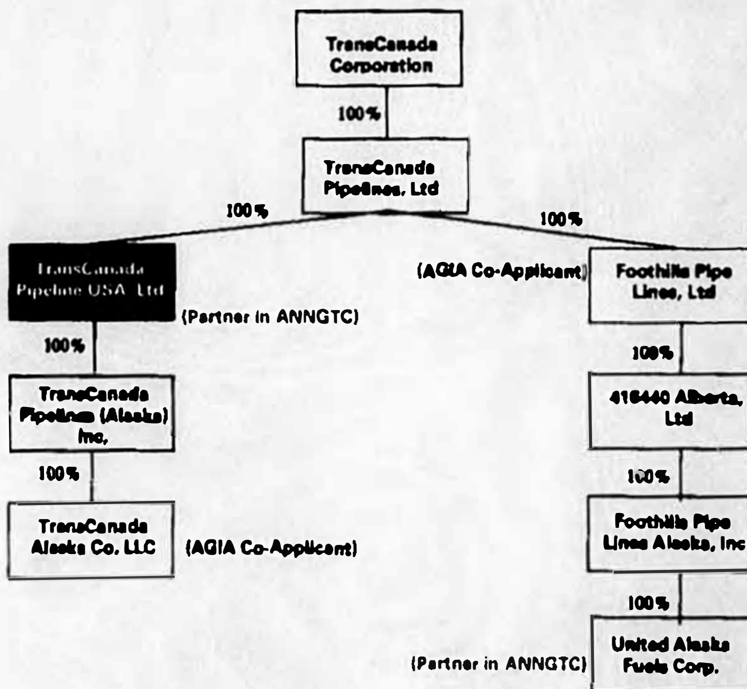
- AGIA requires an applicant to provide "information relevant to the commissioners' evaluation of the readiness and ability of the applicant to complete the project" [AS 43.90.130(19)].
- ANNGTC was formed in the 1970's in an attempt to build an Alaska natural gas pipeline project and spent several hundred 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.