

ALASKA LEGISLATURE COMMITTEE FILES, 2003-2004 8672

10968 HOUSE RESOURCES

HB

246



FRANK H. MURKOWSKI
GOVERNOR
GOVERNOR@GOV.STATE.AK.US

HB 244
P.O. BOX 110001
JUNEAU, ALASKA 99811-0001
(907) 465-3500
FAX (907) 465-3532
WWW.GOV.STATE.AK.US

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

April 3, 2003

The Honorable Pete Kott
Speaker of the House
Alaska State Legislature
State Capitol, Room 208
Juneau, AK 99801-1182

Dear Speaker Kott:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill that would amend AS 38.05.140(c) to increase the upland acreage limit for oil and gas leases from 500,000 acres to 750,000 acres, except for land north of the Umiat Meridian baseline.

Currently, under AS 38.05.140(c) oil and gas lessees may hold not more than a total of 500,000 acres on tide and submerged land and no more than 500,000 acres on uplands. While oil and gas leases with certified wells and those included within units are excluded from these acreage limitations, many operating oil and gas companies are already either at the existing 500,000 acre limitation or close to it. The bulk of this acreage is located on the North Slope and Beaufort Sea.

In the past few years, the Department of Natural Resources has been encouraging exploration of frontier areas such as the North Slope foothills. The bill would increase the maximum upland acreage to 750,000, of which no more than 500,000 acres could be located north of the Umiat Meridian baseline. Thus, companies would be able to lease and explore acreage in Alaska's frontier basins while still maintaining their interests on the North Slope.

I urge your prompt and favorable action on this measure.

Sincerely,

Frank H. Murkowski
Governor

FISCAL NOTE

STATE OF ALASKA
2003 LEGISLATIVE SESSION

Fiscal Note Number: _____
 Bill Version: HB 246
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept: Affected: Natural Resources
 Title Limit on Oil & Gas Lease Acreage BRU Resource Development
 Component Oil and Gas Development
 Sponsor House Rules
 Requester House Oil and Gas Component No. 439

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES (1004)	**	**	**	**	**	**
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2003) cost: 0.0
 Mark this box (X) if funding for this bill is included in the Governor's FY 2004 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

By increasing the maximum onshore acreage to 750,000 but limiting the 250,000 acreage increase to south of the Umiat Meridian Baseline, companies would be able to lease and explore acreage in some of Alaska's frontier basins while still maintaining their interests on the North Slope.

** There will be positive revenue impact to the state from additional bonus bids, rentals, and eventually, production royalties. It is impossible to accurately predict at this time what this increase in revenues might be.

Prepared by: Mark D. Myers Phone 269-8800
 Division Oil and Gas Date/Time 4/22/2003
 Approved by: Tom Irwin, Commissioner Date 4/22/2003
 Agency Natural Resources

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

(907) 465-3867 or 465-2450
FAX (907) 465-2029
Mail Stop 3101

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

May 13, 2003

SUBJECT: Draft CSHB 246 () (Work Order No. 23-GH1135\D)

TO: Representative Hugh Fate

FROM: Jack Chenoweth
Assistant Revisor of Statutes

The draft enclosed with this memo fairly closely follows the text provided by the Department of Law. For reasons that go to avoiding judicial interpretation and conforming to terms regularly used in the criminal code, AS 11, I've substituted "knowingly violates" for "wilful violation" in AS 38.05.036(h) [page 3, at line 4], and tied the word "knowingly" to the definition spelled out in AS 11.

On page 1, at lines 9 and 10, I retained in this draft the words "oil and gas contracts, agreements, or leases under this chapter." The draft you provided had bracketed them for purposes of repeal. However, without the limiting language, since audits under "this chapter" (AS 38.05, the "Alaska Land Act") may also include audits on resources apart from oil and gas -- coal, minerals, etc. -- and since the appropriate single subject for this draft as set out in the title involves "oil and gas," to avoid a question about complying with the bill's one subject, I took the easy course and opted to maintain the limitation.

JBC:lmb
03-205.lmb

Enclosure

23-GH1135D
Chenoweth
5/13/03

CS FOR HOUSE BILL NO. 246()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

**Offered:
Referred:**

Sponsor(s): HOUSE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to oil and gas, to certain audits regarding oil and gas royalty and net**
2 **profits, to audits regarding costs relating to exploration incentive credits and oil and gas**
3 **exploration licenses, and to the limitation on upland acreage that a person may take or**
4 **hold under oil and gas leases; and providing for an effective date."**

5 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

6 *** Section 1.** AS 38.05.036(a) is amended to read:

7 (a) The department may conduct audits regarding [DEPARTMENT OF
8 REVENUE SHALL AUDIT REPORTS, PAYMENTS, AND PAYMENTS DUE
9 RELATING TO] royalty and net profits under oil and gas contracts, agreements, or
10 leases under this chapter and regarding costs related to oil and gas exploration
11 licenses and exploration incentive credits under this chapter or under AS 41.09.

12 For purposes of audit under this section,

13 (1) the department may examine the books, papers, records, or
14 memoranda of a person regarding matters related to the audit; and

1 **(2) the records and premises where a business is conducted shall**
2 **be open at all reasonable times for inspection by the department.**

3 * Sec. 2. AS 38.05.036(b) is amended to read:

4 (b) The Department of Revenue may **obtain from the department** [INSPECT
5 ALL REPORTS AND OTHER] information [FILED IN SUPPORT OF OR] relating
6 to royalty and net profits payments **and to exploration incentive credits under this**
7 **chapter or under AS 41.09**, whether or not that information is confidential. **The**
8 **Department of Revenue may use the information in carrying out its functions and**
9 **responsibilities under AS 43**, and shall hold that information confidential to the
10 extent required **by an agreement with the department or by AS 38.05.035(a)(9),**
11 **AS 41.09.010(d)**, [UNDER OIL AND GAS AGREEMENTS, CONTRACTS, OR
12 LEASES, OR BY THIS CHAPTER] or AS 43.05.230.

13 * Sec. 3. AS 38.05.036(c) is amended to read:

14 (c) **The department may obtain from the Department of Revenue all**
15 [ALL] information obtained **under AS 43** [BY THE DEPARTMENT OF REVENUE]
16 relating to royalty and net profits **and to exploration incentive credits.** **The**
17 **department may use the information for purposes of carrying out its**
18 **responsibilities and functions under this chapter and AS 41.09** [PAYMENTS,
19 INCLUDING INFORMATION OBTAINED UNDER AS 43, MAY BE MADE
20 AVAILABLE TO THE DEPARTMENT, IN THE FORM OF SUMMARIES AND,
21 WHEN IN FURTHERANCE OF THE DEPARTMENT'S ROYALTY AND NET
22 PROFITS FUNCTIONS, RELEVANT PORTIONS OF THE AUDITS]. Information
23 made available to the department that was obtained under AS 43 is confidential and
24 subject to the provisions of AS 43.05.230.

25 * Sec. 4. AS 38.05.036 is amended by adding new subsections to read:

26 (f) Except as otherwise provided in this section or in connection with official
27 investigations or proceedings of the department, it is unlawful for a current or former
28 officer, employee, or agent of the state to divulge information obtained by the
29 department as a result of an audit under this section that is required by an agreement
30 with the department or by AS 38.05.035(a)(9) or AS 41.09.010(d) to be kept
31 confidential.

1 (g) Nothing in this section prohibits the publication of statistics in a manner
2 that maintains the confidentiality of information to the extent required by an
3 agreement with the department or by AS 38.05.035(a)(9) or AS 41.09.010(d).

4 (h) A person who knowingly violates (f) of this section is punishable by a fine
5 of not more than \$5,000, by imprisonment for not more than two years, or by both. In
6 this subsection, "knowingly" has the meaning given in AS 11.81.900.

7 (i) In the course of carrying out its responsibilities under this section, the
8 department may subpoena any person to appear and produce books, records, papers, or
9 memoranda bearing upon matters relating to an audit under this section and to give
10 testimony or answer interrogatories under oath regarding those matters. The
11 department may administer oaths to persons who are so subpoenaed. A subpoena
12 issued under this section may compel attendance of a witness or production of a
13 document or thing, located inside or outside the state, to the maximum extent
14 permitted by law.

15 (j) A subpoena may be served by the commissioner of public safety or a peace
16 officer designated by the commissioner of public safety, by a person designated by the
17 department, or as otherwise provided by law. A subpoena may also be served by
18 registered or certified mail for delivery restricted only to the person subpoenaed. The
19 return delivery receipt must be addressed so that the receipt is returned to the
20 department.

21 (k) If a person who is subpoenaed neglects or refuses to obey the subpoena
22 issued as provided in this section, the department may report the fact to the superior
23 court or the appropriate court of another jurisdiction, and may seek an order from the
24 court compelling obedience to the subpoena. The court, to the maximum extent
25 permitted by law, may compel obedience to the subpoena to the same extent as
26 witnesses may be compelled to obey the subpoenas of the court.

27 (l) The department may conduct audits under this section concurrently with
28 Department of Revenue audits or investigations under AS 43.

29 * **Sec. 5.** AS 38.05.140(c) is amended to read:

30 (c) A person may not take or hold at one time phosphate leases on state land
31 exceeding in the aggregate 10,240 acres. A person may not take or hold sodium leases

1 or permits during the life of sodium leases on state land exceeding in the aggregate
2 acreage 5,120 acres, except that the commissioner may, where it is necessary in order
3 to secure the economic mining of sodium compounds, permit a person to take or hold
4 sodium leases or permits for up to 15,360 acres. A person may not take or hold at any
5 one time oil or gas leases exceeding in the aggregate 500,000 acres granted on tide and
6 submerged land, including leases held both as lessee and under option or
7 operating agreement from others. A person may not take or hold at any one time
8 oil or gas leases exceeding in the aggregate 750,000 [AND 500,000] acres on all
9 land other than tide and submerged land, of which not more than 500,000 acres may
10 be located north of the Umiat Meridian baseline, including leases held both as
11 lessee and under option or operating agreement from others. Where more than a
12 single person holds an interest in an oil or gas lease, each person shall be charged only
13 with that percentage of the total acreage that [WHICH] corresponds to its percentage
14 share of the total beneficial interest in the lease.

15 * Sec. 6. AS 43.05.040(a) is amended to read:

16 (a) The department may examine the books, papers, records, or memoranda of
17 any person to ascertain the correctness of a return filed or to determine whether a tax
18 [OR A PAYMENT FOR OIL OR GAS ROYALTY OR NET PROFITS SHARES
19 UNDER A CONTRACT, AGREEMENT, OR LEASE UNDER AS 38.05] is due, or
20 in an investigation or inspection in connection with tax matters [OR MATTERS
21 RELATING TO OIL AND GAS ROYALTY OR NET PROFITS UNDER
22 CONTRACTS, AGREEMENTS, OR LEASES UNDER AS 38.05]. The records and
23 the premises where a business is conducted shall be open at all reasonable times for
24 official inspection, and the department may subpoena any person to appear and
25 produce books, records, papers, or memoranda bearing upon tax matters [OR
26 MATTERS RELATING TO OIL AND GAS ROYALTY OR NET PROFITS
27 UNDER CONTRACTS, AGREEMENTS, OR LEASES UNDER AS 38.05], and to
28 give testimony or answer interrogatories under oath respecting tax matters [OR
29 MATTERS RELATED TO OIL AND GAS ROYALTY OR NET PROFITS UNDER
30 CONTRACTS, AGREEMENTS, OR LEASES UNDER AS 38.05], and the
31 department may administer oaths to persons who are so subpoenaed. A subpoena

1 issued under this section may compel attendance of a witness or production of a
2 document or thing, located either inside or outside the state, to the maximum extent
3 permitted by law.

4 * **Sec. 7.** AS 43.05.230(a) is amended to read:

5 (a) It is unlawful for a current or former officer, employee, or agent of the
6 state to divulge the amount of income or the particulars set out or disclosed in a report
7 or return made under this title, except

8 (1) in connection with official investigations or proceedings of the
9 department, whether judicial or administrative, involving taxes due under this title;

10 (2) in connection with official investigations or proceedings of the
11 child support enforcement agency, whether judicial or administrative, involving child
12 support obligations imposed or imposable under AS 25 or AS 47;

13 (3) as provided in AS 38.05.036 pertaining to audit functions of the
14 Department of Natural Resources;

15 (4) as provided in AS 43.05.400 - 43.05.499; and

16 (5) as otherwise provided in this section.

17 * **Sec. 8.** AS 38.05.036(d), 38.05.036(e), and AS 43.05.010(15) are repealed.

18 * **Sec. 9.** The uncodified law of the State of Alaska is amended by adding a new section to
19 read:

20 **TRANSITION.** (a) Litigation, hearings, investigations, and other proceedings
21 pending under a law amended or repealed by secs. 1 - 4 and 6 - 8 of this Act, or in connection
22 with functions transferred by secs. 1 - 4 and 6 - 8 of this Act, continue in effect and may be
23 continued and completed notwithstanding a transfer or amendment or repeal provided for in
24 secs. 1 - 4 and 6 - 8 of this Act.

25 (b) Contracts, rights, liabilities, and obligations created by or under a law amended or
26 repealed by secs. 1 - 4 and 6 - 8 of this Act and in effect on June 30, 2003, remain in effect
27 notwithstanding this Act's taking effect. Records and appropriations of agencies of the state
28 whose functions are transferred under secs. 1 - 4 and 6 - 8 of this Act shall be transferred to
29 implement those provisions of this Act.

30 * **Sec. 10.** Section 5 of this Act takes effect immediately under AS 01.10.070(c).

31 * **Sec. 11.** Except as provided in sec. 10 of this Act, this Act takes effect July 1, 2003.



Richard P. Mott
Vice President
Exploration & Land
P.O. Box 100360
Anchorage, AK 99510-0360
Phone 907.263.4556

April 9, 2003

Representative Vic Kohring, Chairman
House Special Committee on Oil and Gas
Legislature of the State of Alaska
Alaska State Capitol, Room 24
Juneau, Alaska 99801-1182

Senator Scott Ogan, Chairman
Resources Committee
Legislature of the State of Alaska
Alaska State Capitol, Room 103
Juneau, Alaska 99801-1182

Re: **House Bill No. 246**
Senate Bill No. 172

ConocoPhillips Alaska, Inc. supports House Bill No. 246, and Senate Bill No. 172 both of which provide for an increase in the limitation on acreage that a person may take or hold under oil and gas lease in the State of Alaska. An increase in the acreage limitation will encourage additional investment by the oil and gas industry in the exploration and development of Alaskan resources.

A handwritten signature in black ink that reads "Richard P. Mott". The signature is fluid and cursive, with a prominent flourish at the end.

Richard P. Mott
Vice President
Exploration & Land

Cc: Mike Tibbles
Legislative Liaison
Office of the Governor
P.O. Box 110001
Juneau, Alaska 99811-0001

Mark Myers, Director
State of Alaska
Department of Natural Resources
Division of Oil & Gas
550 West 7th Avenue, Suite 800
Anchorage, Alaska 99501-3510

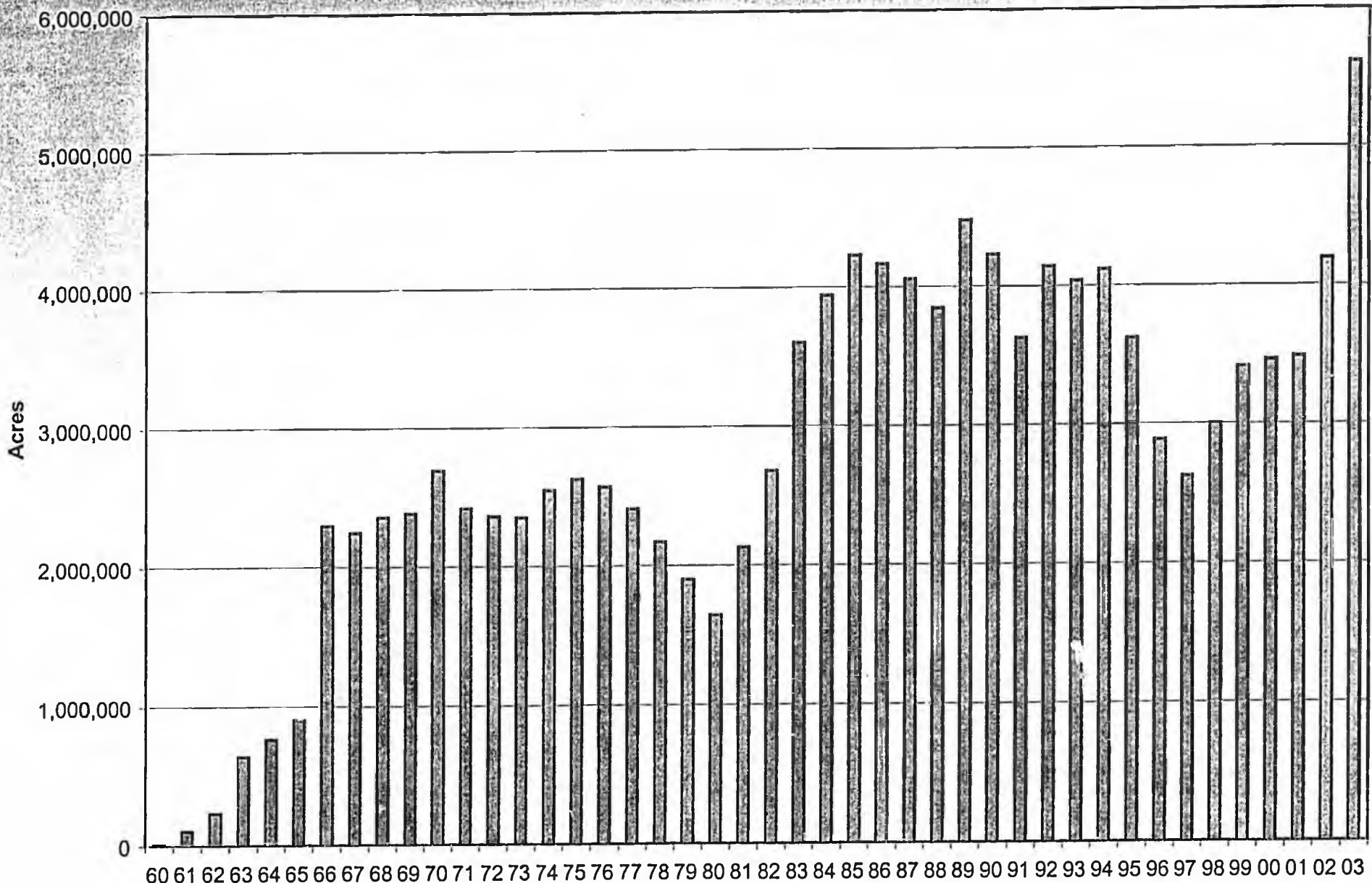
CONOCOPHILLIPS COMMENTS

THE
FOLLOWING
DOCUMENT(S)
ARE
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ORIGINAL
COPIES

Acreage under Oil & Gas Lease 1960 – 2003

(Does not include acreage under Exploration License)

GRAPH OF O&G ACERAGE



60 61 62 63 64 65 66 67 68 69 70 71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 00 01 02 03

Acreage figures for 2003 current to April 1.
Includes conventional, shallow natural gas, lease expirations and relinquishments.

HOUSE COMMITTEE REPORT

(7)

Date Referred to Committee: April 4, 2003

FURTHER REFERRALS: Resources

Date of Committee Action: 04/29/03

The HOUSE SPECIAL COMMITTEE ON OIL AND GAS Committee considered:

HB 246

HOUSE BILL NO. 246

LIMIT ON OIL & GAS LEASE ACREAGE

"An Act relating to the limitation on upland acreage that a person may take or hold under oil and gas leases; and providing for an effective date."

Recommends it be replaced with HCS or CS for _____ (_____)
 For Senate Bills with new title: Technical Title New Title: HCR _____ Same Title New Title

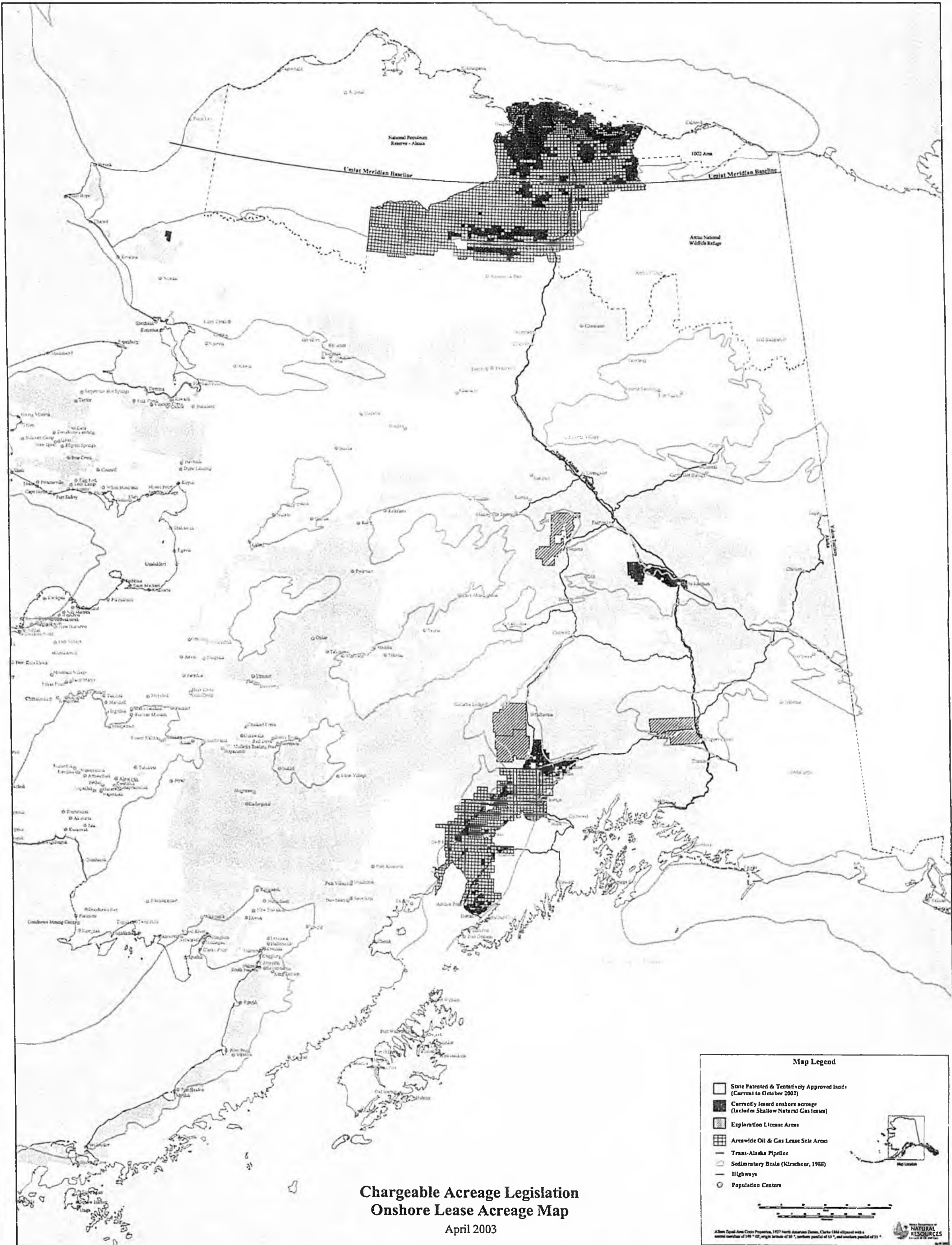
- attach amendments
- add new referral to _____ Committee
- Letter of Intent _____ Committee

List of Abbrev for Depts.:
 ADM
 CED
 COR
 CRT
 EED
 DEC
 DFG
 GOV
 HSS
 LEG
 LAW
 LWF
 MVA
 DNR
 DPS
 REV
 DOT
 UA

<u>NEW FISCAL NOTES</u>				
*Assigned by Chief Clerk's Office				
List by Dept(s):	*FN#	Fiscal	Indet.	Zero
DNR				✓

<u>PREVIOUS FISCAL NOTES</u>				
List by Dept(s):	FN#	Fiscal	Indet.	Zero

<u>Signing with recommendations</u>	Printed Last Name	DP	DNP	NR	AM
	Holm	✓			
	Kerattula	✓			
	CRAWFORD	✓			
	Fote	✓			
Chair:	Lohring	✓			
Chair:	Lohring	✓			



**Chargeable Acreage Legislation
Onshore Lease Acreage Map**
April 2003

Map Legend

- State Patented & Tentatively Approved lands (Current to October 2003)
- Currently leased onshore acreage (includes Shallow Natural Gas leases)
- Exploration License Areas
- Area-wide Oil & Gas Lease Sale Areas
- Trans-Alaska Pipeline
- Sedimentary Basins (Kirchoff, 1968)
- Highways
- Population Centers

Alaska Equal Area State Projections, 1977 North American Datum, Clarke 1866 ellipsoid with a spheroid flattening of 1/298.257, angle of strike of 90°, northern parallel of 63°, and southern parallel of 33°

NATURAL RESOURCES

HB

267

ALASKA STATE LEGISLATURE

Interim:
600 East Railroad Avenue
Wasilla, Alaska 99654
(907) 373-1842
Fax (907) 373-4729



Session:
State Capitol Building
Juneau, Alaska 99801-1182
(907) 465-2186
Fax (907) 465-3818

REPRESENTATIVE VIC KOHRING DISTRICT 14

SPONSOR STATEMENT

HB 267

RAILROAD BONDS FOR NATURAL GAS TRANSPORT

This legislation would be a significant step toward the construction of a natural gas pipeline to commercialize North Slope gas reserves.

HB 267 authorizes the Alaska Railroad Corporation to issue bonds for the pipeline project, leveraging the ability of the corporation to issue tax-exempt bonds for industrial development. This financing plan can push pipeline construction that much closer to reality, resulting in jobs for Alaskans and revenue to the state while delivering natural gas to a waiting public and market.

The Alaska Railroad's ability to issue tax-exempt bonds to finance industrial development was approved in 1983 by the U.S. Congress with the transfer of the Alaska Railroad from federal to state ownership. Congress reaffirmed Alaska Railroad's authority to issue tax-exempt bonds in the Tax Reform Act in 1986.

Estimates prepared by Goldman Sachs and the Department of Revenue suggest the financing plan presented in this bill will increase the economic viability of the natural gas line construction project by saving the facility owners more than \$1 billion over the life of the project.

The bill allows Alaska Railroad to provide financing for the acquisition, construction, improvement, maintenance, equipping and operation of facilities for the transportation of natural gas resources within and outside the state. It specifically authorizes Alaska Railroad to negotiate issue up to \$17 billion in bonds for construction of a natural gas pipeline.

While Alaska Railroad would issue the bonds, neither Alaska Railroad nor the State would own the gas line nor be liable for the debt. That responsibility would fall on the private companies that build, own, and operate the gas line. The bill requires that prior to issuing bonds, Alaska Railroad must determine that any contract or lease is sufficient to pay back the bonds as scheduled, maintain reserves for the payments, and pay all costs necessary to secure the bonds.

The railroad is a vital link in Alaska's economy. Many towns have sprouted up because of the role of Alaska Railroad, which supported construction of the Alaska Highway during World War II and the subsequent military buildup in our state. It also helped in building the Trans-Alaska Pipeline System; and along its more than 600 miles of track, it carries seven million tons of freight and a half-million passengers each year. Alaska Railroad also provides jobs for 700 Alaskans.

THE
FOLLOWING
DOCUMENT(S)
ARE
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Subject: LNG Meeting with Korea Gas Corp.

Date: Tue, 25 Feb 2003 18:37:09 -0900

From: Bill Noll <bill_noll@dced.state.ak.us>

To: Edgar Blatchford <edgar_blatchford@dced.state.ak.us>, Frank_Homan@gov.state.ak.us

Edgar and Frank:

Per Jim Clark's request I took part in the Feb. 21st natural gas discussions with Mr. Kim, Jong-Sool of Korea Gas Corporation.

As I reported telephonically on Feb. 22nd, the discussions went well. Following are some pertinent facts.

1. There were two meetings on Feb. 21st, one at 10:00 a.m. in the offices of Jeff Lowenfels and Wayne Lewis, and then at 6:30 p.m. for dinner at the Captain Cook Hotel.
2. Attending the 10:00 a.m. meeting: Noll, Kim, Rep. Fate, Rep. Harris, Rep. Whittaker, Paul Funs, Scott Heyworth, John Urbina (Baum & Co.), Geoff Urbina, John Bitney (Anch. rep for Baum), and Craig Richards (from Wohlforth's firm, on contract to Alaska Railroad for bonding matters).
3. Attending the 6:30 p.m. dinner: Noll, Kim, Rep. Whittaker, Funs, Heyworth, both Urbina's, Bitney, Brad Whitmore (Yukon Pacific), and Bill Walker. Dinner was hosted by the Urbina's (Baum & Co.).
4. Mr. Kim is Senior Executive Vice President and a Member of the Board of Korea Gas Corporation (Kogas). During the course of the meetings he said that he would be the point of contact for discussions about Alaska gas. All parties had a lively and positive exchange. Mr. Kim has a degree from the United States in electrical engineering, and he speaks English very well. He is 56 years of age.
5. Kogas now sources gas from Oman, Qatar, Indonesia, Malaysia and Brunei. Mr. Kim sees a need for an added 17mm tons of LNG in Korea in the 2010 - 2015 timeframe. Kogas is looking at possible sources to fill that need, including renewing existing contracts, new pipeline sources, and mid-contract adjustments. By the conclusion of the morning meeting Mr. Kim said he would now consider Alaska as a possible source for a portion of that need, citing the united presence of Alaska's Executive and Legislative Branches along with the private sector in pushing for the project.
6. I noted to Mr. Kim that our Governor has considerable international and energy experience and that he will no doubt make a visit to Korea with a strong delegation but not until after the end of the Legislative session. I told Mr. Kim that the Governor will soon appoint the members of an authority to work on the question of our gas. While I made no commitments on the outcome of the authority's work, I assured Mr. Kim that the commercialization of our gas is of high interest.
7. Funs and Urbina presented a very brief overview of the proposed LNG project, citing a price of \$3.50 per mmbtu delivered to Korea (CIF). Mr. Kim's comment: "Good price." Mr. Kim said that Kogas is now paying from \$4.00 to \$5.70 per mmbtu CIF.
8. Kogas LNG is currently delivered by a fleet of 17 tankers (price \$160 - \$175 million each), all built in one of three Korean yards and operated by four Korean shipping companies under long term contracts with Kogas. Yukon Pacific figures that their export project will need 12 tankers.

9. Mr. Kim stated in both meetings that Kogas would discuss a 5% - 10% equity interest in the Alaska project. I assume that this could be offered in the form of capital goods (such as the ships). Mr. Kim repeated to me that Kogas could discuss a long term commitment contract with Alaska, so long as the price point risk was equally shared by the State. No details, of course, but his point was repeated by him and by me to be sure of the words, and his meaning was clear. (FYI, the price point per mmbtu for international LNG is often pegged to a basket of crudes known as the Tokyo Crude Cocktail or TCC. The LNG price point fluctuates with the price of those crudes. Higher crude prices equate to lower risk for LNG sellers and higher prices for LNG consumers. Lower crude prices equate to the opposite, and herein is the need for risk analysis on the seller side -- such as Alaska.)

10. There were many other items discussed, the details of which could be summarized by the technical people at the meetings. I can report that the atmosphere was quite positive. The House members seemed very encouraged by the meeting.

11. Frankly, I was also pleasantly surprised by Mr. Kim's forthcoming nature and comments. There are many more things to be done, but this was an encouraging meeting with one of the major LNG end-users. Again, Mr. Kim asked that he be the point of contact at Kogas for future discussions. I departed the dinner along with Rep. Whittaker, telling Mr. Kim that I would see him in Seoul.

12. I spoke with Paul Fuhs today (Feb. 25th). He is now in Juneau. I asked him to look into inviting Tokyo Gas to Alaska for a similar meeting.

Best regards, Bill

FISCAL NOTE

STATE OF ALASKA
2003 LEGISLATIVE SESSION

Fiscal Note Number: _____
 Bill Version: HB 267
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: DCED
 Title Ak Railroad Bonds For Nat. Gas Transport BRU _____
 Component Alaska Railroad Corporation
 Sponsor Representative Kohring
 Requester House Oil & Gas Component No. _____

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Personal Services						
Travel						
Contractual			163,000.0			
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	163,000.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Bond Proceeds			163,000.0			
TOTAL	0.0	0.0	163,000.0	0.0	0.0	0.0

Estimate of any current year (FY2003) cost: 0.0
 Check this box (X) if funding for this bill is included in the Governor's FY 2004 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

Please see analysis continuation.

Prepared by: Wendy Lindskoog, Director of External Affairs Phone 265-2516
 Division Alaska Railroad Corporation Date/Time 4/23/03 2:51 PM
 Approved by: Edgar Blatchford, Commissioner Date 4/23/2003
 Agency Department of Community & Economic Development

FISCAL NOTE

**STATE OF ALASKA
2003 LEGISLATIVE SESSION**

BILL NO. HB 267

ANALYSIS CONTINUATION

The bill authorizes the issuance of up to \$17 billion in revenue bonds by the Alaska Railroad Corporation (ARRC) to pay for 70% of the construction of a natural gas pipeline. Based upon current estimates, ARRC could issue \$14,265,000,000 in bonds as early as state Fiscal Year 2006. ARRC will act as a conduit for the issuance of these bonds to allow the debt to be issued as tax exempt. Through modeling, the tax exemption has been shown to reduce the cost of financing the project by over one billion dollars. The Bonds would be solely secured by revenues generated by the pipeline. The Alaska Railroad will bear no liability and have no responsibility for repayment of the bonds.

The projected costs of issuing the bonds detailed here will be paid with bond proceeds at closing. Anticipated professional services include those related to financial advisors, attorney's fees (bond counsel, underwriter's counsel, tax counsel, negotiating with producers), rating agencies, underwriters, printing, travel, public notices, and the feasibility consultant. ARRC will front certain minor necessary reimbursable costs from corporation revenues.

For purposes of this fiscal note, it is assumed that bonds with a face value of \$14.265 billion will be issued in FY 2006. The bonds are expected to be issued with a 25 year term and for modeling purposes carry an interest rate of 6.5%. As the project will not generate revenue while under construction, the first two years of interest payments will be made with bond proceeds. Following construction, annual debt service will begin at approximately \$1.3 billion, growing to \$1.4 billion in year 6 and then gradually lowering to \$800 million in the final year. However, ultimately, issuance amounts, dates, term, interest rate, and other significant variables will be dependent upon the financing structure determined by market conditions at the time of sale of the bonds.

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

(907) 465-3867 or 465-2450
FAX (907) 465-2029
Mail Stop 3101

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

May 6, 2003

SUBJECT: Sectional summary - HB 267

TO: Representative Vic Kohring
Attn: Ben Grenn

FROM: Tamara Brandt Cook
Director *TBC*

Sec. 1. Findings, intent and purpose dealing with the power of the Alaska Railroad Corporation to provide financing for transportation for natural gas resources.

Sec. 2. Adds a power of the Alaska Railroad Corporation to provide financing for the acquisition, construction, improvement, maintenance, equipping, and operation of facilities for the transportation of natural gas without regard to whether the facilities are or will be owned by the corporation or located on land owned by the corporation.

Sec. 3. Requires the Alaska Railroad Corporation to enter into an agreement with certain terms to protect its bonds if the corporation issues bonds to provide financing for a facility to be owned in whole or part by an entity other than the corporation.

Sec. 4. States that bonds of the corporation issued to finance natural gas transportation facilities are issued by an instrumentality of the state for a public purpose.

Sec. 5. The legislature authorizes the corporation to issue bonds in an amount not to exceed \$17,000,000,000 to finance the construction of a natural gas pipeline and facilities for the transportation of natural gas recovered from the North Slope.

Sec. 6. Immediate effective date.

TBC:med
03-492.med

Alaska State Legislature
House Finance Committee

REPRESENTATIVE
BILL WILLIAMS

Co-Chair

(907) 465-3424

Fax: (907) 465-3793

INTERIM ADDRESS

50 Front Street, Suite 203

Ketchikan, Alaska 99901

(907) 247-4627

Fax: (907) 225-7157



State Capitol, Juneau, Alaska 99801-1182

REPRESENTATIVE
JOHN HARRIS

Co-Chair

(907) 465-4859

Fax: (907) 465-3799

INTERIM ADDRESS

State Capitol, Room 507

Juneau, AK 99801-1182

January 21, 2003

John Urbina, Executive Vice President & Manager
Alaska and Northwest Public Finance
George K. Baum & Company
731 N Street
Anchorage, Alaska 99501

Dear Mr. Urbina,

I am aware of your expertise based on your involvement with financing of various Valdez projects, including the Alyeska marine terminal for the Trans Alaska oil pipeline and the current proposal for the hospital. Based on your firm's experience in public financing in Alaska over the past twenty-eight years, I am writing to request your assistance in evaluating economic data concerning the proposed gas pipeline from Alaska's North Slope to Valdez.

As you know, Alaskan voters overwhelmingly created the Alaska Natural Gas Development Authority during the last general election. The approval of funding for the Authority must occur as part of the budget deliberations by the House Finance Committee. As Co-Chairman of the Committee, I anticipate there will be questions whether the project is sufficiently economic to warrant being pursued by the State of Alaska.

In responding to a request from me, Yukon Pacific Corporation has recently supplied the most current project description and economic data for a gasline to Valdez. I have enclosed this as an attachment to this letter.

I would appreciate it if you would analyze the financing and bonding implications of this data from both a private and public financing point of view. You may contact Yukon Pacific Corporation for any clarifications on their model if it is necessary.

It would be interesting to know your opinion on debt service coverage required to sell the bonds for this project, potential returns to the Authority and the State of Alaska from owning the project, rates of return on the pipeline, and whether or not you believe the bonds for this project could be sold if Yukon Pacific's project assumptions hold true.

Sincerely,

A handwritten signature in black ink, appearing to read "John Harris", written over a horizontal line.

Representative John Harris

CORRESPONDENCE
RE: AK/NW PUBLIC FINANCE

George K. Baum & Company
INVESTMENT BANKERS SINCE 1928

January 30, 2003

Representative John Harris
Co-Chair House Finance Committee
Alaska State Legislature
State Capitol
Juneau, AK 99801

Dear Representative Harris:

George K. Baum & Company is pleased to respond to your request to analyze economic data for a gasline to Valdez. In our analysis we have utilized information supplied to you by Yukon Pacific Corporation.

Yukon Pacific Corporation Information

Your office has furnished us with Yukon Pacific Corporation detail on projected revenue breakdown and expenditures including, capital outlays, expenses for gasline products, gas purchase expenses and other costs.

Yukon Pacific Corporation detail was supplied for two cases:

1) Base Case, which revenues include:

- LNG sold to North America & Asia
- LPG sold to Asia
- Ethane sold to Valdez
- Natural gas sold to TAPS
- Natural gas sold to Alaska residents
- Total Operating income over 39 years \$103.6 billion

2) Lean Case, which revenues include:

- LNG sold to North America & Asia
- LPG sold to Asia
- Natural Gas sold to Alaska Residents
- Total Operating income over 39 years \$103.8 billion

We make no statement as to the accuracy or validity of information supplied to us by your office or by the Yukon Pacific Corporation. Material supplied to us is attached as Exhibit A.

Analysis

Our analysis, in accordance with your request, entailed the examination of each Yukon Pacific Corporation scenario "base case" and "lean gas case" for three different financing options. The financing options analyzed were 70% tax-exempt debt and 30% equity; 70% taxable debt and 30% equity; and, 100% tax-exempt debt.

For each case we computed debt service coverage, potential revenues to the Authority and State of Alaska, and an internal rate of return for the gasline project where appropriate. Detail on our financial models is attached as Exhibit B.

Our results are summarized in the attached Chart A.

Viability of Project


The cornerstone of our analysis is the projected revenue derived from throughput "take-or-pay" and/or "ship-or-pay" contracts with end users. It is imperative that the contracts be in place for rating and bond marketing purposes. In addition, it is important to note, that our analysis assumes that tax-exempt debt for all or a portion of the gasline project can be issued through the Alaska Railroad Corporation (ARRC). Local bond counsel has opined favorably on the ARRC issue. If the ARRC option is not available only 25% to 30% of the project can be financed tax-exempt and a portion if not all of the tax-exempt debt would be subject to "private activity" bond cap allocation by the State Bond Committee. Furthermore, the tax-exempt portion of debt financed outside of the ARRC option would be limited to those purposes permitted by current tax law.

Based on the information and market assumptions supplied to us by Yukon Pacific Corporation for our analysis we believe the project can be financed in the bond market if the ARRC vehicle is available. We believe the best option would be to have some equity contribution from private sponsors. A State owned facility would entail some production and market risk the State of Alaska may not want to assume. Also, there are issues such as unrelated business income tax that the State may be subject to unless all revenues were utilized for public purposes.

According to projections provided by YPC and our analysis we are showing, depending on model assumptions, annual revenues to the State of between \$350 million to \$1.0 billion. This underscores the importance of this project to the State.

We hope this information is of interest and help to you. We are available for further consultation to you and your staff and assistance with any presentation before House Finance Committee meetings and/or hearings. Should you require any additional material or clarification on our analysis please let us know. Any questions regarding detail on "base case" or "lean gas case" assumptions should be directed to Yukon Pacific Corporation.

Sincerely,



John D. Urbina

Attachments

Chart A
Exhibit A
Exhibit B

Chart A

George K. Baum & Co. Summary of Corporate Finance & Public Finance Models						
	Corporate Finance Model				Public Finance Model	
	30% Equity / 70% Tax-Exempt		30% Equity / 70% Taxable		100% Tax-Exempt Debt	
	Base	Lean	Base	Lean	Base	Lean
Internal Rate of Return (ROB) ⁽¹⁾	13.11%	13.17%	11.64%	11.66%	N/A	N/A
Years Debt Amortized	17 years	17 years	24 years	24 years	39 years	39 years
Minimum DSCR	1.53x	1.53x	1.50x	1.50x	2.00x	2.00x
Average DSCR ⁽²⁾	2.15x	2.16x	2.47x	2.47x	2.52x	2.53x
Average Annual State Revenues in millions ⁽³⁾	350 - 400	350 - 400	350 - 400	350 - 400	500 - 1,000	500 - 1,000
Average Annual Local Municipality Revenues in millions ⁽⁴⁾	50 - 100	50 - 100	50 - 100	50 - 100	50 - 100	50 - 100

⁽¹⁾ Public Models: The IRR calculation does not apply to a project funded by 100% debt.

⁽²⁾ Corporate Models: The longer term amortization is due to the desire to have a minimum DSCR of 1.5x; hence, since the principal payment is lower for the 8% scenario versus the 5% scenario, the average DSCR for the 8% scenario is higher.

⁽³⁾ Corporate Models: Annual amounts are a function of royalty tax, severance tax and ELF levels.

⁽⁴⁾ Corporate Models: Annual amounts are a function of mill levy calculation on property or PILT.

1. 04

FAX NO. 206 388 0000

JAN-29-2003 WED 03:27 PM GKB



Alaska State Legislature

REPRESENTATIVE JOHN HARRIS

District 35 - Valdez, Cordova, Whittier, Clondike, Delta Junction, Tatitlek, Kory Lake, Paxson, Gakona, Chenega Bay

December 24, 2002

Ward Whitmore
Director of Project Development
Yukon Pacific Corporation
1400 West Benson, Suite 501
Anchorage, AK 99503

Dear Mr. Whitmore:

At the November election, the voters of Alaska overwhelmingly adopted Proposition 3, which establishes an Alaska Gasline Authority. As the incoming co-chairman of the House Finance Committee, I will be overseeing that committee's deliberations on a budget for the authority.

I would appreciate the opportunity to meet with you to receive any information you may be willing to share with legislators concerning potential project configurations, project economics, including construction costs, potential markets and revenues, and any other information you believe would help us in our deliberations.

I am also concerned about public statements made recently by others that infer that Yukon Pacific is expecting to be paid up front for your permits, even before we know whether the project will move forward. I would appreciate a letter from you explaining your outlook on negotiations concerning the use of your permits for this project.

As you know, this project is very important to my district, as well as the rest of the state, and I want to do all I can to give the issue fair consideration.

Sincerely yours,

A handwritten signature in dark ink, appearing to read "John Harris".

Representative John Harris

Cc: Governor Frank Murkowski

Co-Chair Community and Regional Affairs Committee, Member: Resources, Labor and Commerce, Oil and Gas, Fisheries and Regulation Review
Session: State Capitol, Juneau, Alaska 99801-1182 • Phone: (907) 465-4859 Fax: (907) 465-3799
Interim: P.O. Box 1245, Valdez, Alaska 99686 • Phone (907) 835-2836 Fax: (907) 835-3732

**CORRESPONDENCE
RE; YUKON PACIFIC CORP.**



**YUKON
PACIFIC
CORPORATION**
TRANS-ALASKA GAS SYSTEM

January 2, 2003

Representative John Harris
Alaska State Legislature
PO Box 1245
Valdez, Alaska 99686

Dear Representative Harris:

Thank you for your letter dated December 24, 2002. We obviously share your view regarding the importance of a LNG project to the state and to Valdez.

You expressed concern about public statements made by others than infer that Yukon Pacific Corporation (YPC) is expecting upfront payment for its permits. You also requested that we explain our outlook on negotiations concerning use of our permits.

YPC is a subsidiary of CSX Corporation. Neither YPC nor CSX has authorized any person(s) to speak on behalf of either corporation regarding YPC's permits or other aspects of the Trans-Alaska Gas System (TAGS). As your letter has just done, please contact us directly to determine our position on any matter.

The staff at YPC will be happy to meet with you to address questions and particulars regarding the content of YPC's permits and technical aspects of TAGS. CSX will conduct any negotiations regarding access to YPC's permits and other assets. I can, however, address CSX's general approach regarding negotiations for YPC's permits.

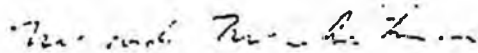
CSX is flexible regarding the terms used to value YPC's assets. CSX's general view is that the value of the permits is tied to the success of the project. CSX is not expecting an upfront buyout of YPC's permits

Representative John Harris
January 2, 2003

Page 2 of 2

YPC continues to work on the TAGS project and we are excited regarding the prospects for a LNG project to Valdez. There is an enormous amount of work ahead. YPC will work with any qualified sponsor wanting to advance a LNG project in a meaningful way, and will be responsive to requests from such a sponsor. We look forward to working with the State of Alaska regarding the project.

Regards,



Ward Whitmore
Director of Project Development

Cc: Andrew Fogarty (CSX)

Yukon Pacific Corporation

Trans-Alaska Gas System

Introduction

Yukon Pacific Corporation (YPC) is the sponsor of and holds major permits for the Trans-Alaska Gas System (TAGS). TAGS is a project that would transport Alaska's North Slope natural gas by pipeline to Valdez, Alaska, where the gas components would be separated into various products for sale to markets within Alaska, along the west coast of North America and in Asia.

TAGS was originally envisioned as a project to produce and sell LNG (liquefied natural gas) exclusively to Asian markets. A potentially large LNG market is developing along the west coast of North America. A recent publication of the American Gas Association identifies a LNG project from South Alaska as a principle option for moving North Alaska gas to markets in North America or North Asia.

A number of LNG receiving terminals are being proposed for the Baja Peninsula of Mexico and California to serve the natural gas and electrical power markets in the western United States. It is YPC's understanding that the LNG supply to these receiving terminals has not yet been secured. The opportunity exists for TAGS to be a major supplier of LNG to these facilities and/or other terminals located along the U.S. West Coast and possibly British Columbia.

Economies of scale required for the TAGS project may be achieved if TAGS can secure a significant portion of the LNG market along the west coast of North America. A TAGS project delivering natural gas to the lower-48 would benefit Alaska and the United States overall because this would reduce the dependency of the United States on foreign energy, any potential aid from state or U.S. federal governments would be applied to a project within the United States, and the United States would benefit economically from the construction and operation of a domestic project.

The Prudhoe Bay field is the largest reserve of natural gas on Alaska's North Slope. The Prudhoe Bay field will be over 30 years old by the start of TAGS. Hydrocarbons, specifically propane, currently used for enhanced oil recovery operations at Prudhoe Bay may be available for sale via TAGS as LPG (liquefied propane gas) to markets around the Pacific Rim. The sale of large quantities of propane via TAGS represents a potentially valuable market that could enhance the economic viability of TAGS.

YPC is investigating configurations of TAGS that accommodate both the emerging LNG market to the west coast of North America and the potential availability of large amounts of propane from Prudhoe Bay. YPC is considering two general configurations: one based upon various value added options such as supplying feedstock to an Alaskan petrochemical industry, and a second option based on LNG and LPG sales without value added options. Economic analyses show that this new configuration of TAGS may be economically viable with, or without the value added options.

YPC is presenting the results of our economic analyses with the goal of engaging other parties interested in commercializing natural gas from Alaska's North Slope.

In 1987, CSX Corporation acquired a direct majority interest in YPC and now holds approximately 88 percent of its shares. The remaining interest is held primarily by a charitable trust established by former Alaska Gov. Walter Hickel, one of the co-founders of YPC.

The project development activity at YPC includes field programs to gather data along the pipeline route from the North Slope of Alaska to Valdez. YPC continues to develop in-house analytical software for evaluation of pipeline designs and a geographical information system containing technical information for TAGS.

Project Economics

YPC is evaluating two stand-alone configurations of TAGS: a Base Case and a Lean Gas Case. In both cases, economic analyses have shown that the potential benefits are significant and warrant further consideration by entities interested in commercializing North Slope natural gas. Analyses show that the TAGS project economics are enhanced by, but not dependent upon the value added options available to the project.

Both the Base and the Lean Gas cases include the costs for a gas conditioning plant on the North Slope, a pipeline with compressor stations to deliver the gas to Valdez, a facility to separate the hydrocarbon components at Valdez, and a liquefaction plant with marine terminal at Valdez. The capital costs also include a fleet of LNG and LPG tankers, plus a LNG receiving facility on the west coast of North America.

In both cases, the average flow of natural gas entering the TAGS pipeline on the North Slope, including fuel, is estimated at 2.2 bscfd (billion standard cubic feet per day). YPC has selected a 36-inch diameter pipeline, with relatively small sized gas compressors located periodically along the route, to accommodate the 2.2 bscfd flow. The capacity of the 36-inch pipeline can be increased to 3 bscfd by the addition of gas compression.

YPC's economic model generates economic parameters from the perspective of the gas producers assuming that they own the project, and also from a prospective assuming that a group of investors would own the project and buy the gas from the gas producers. Both perspectives are based upon generation of after tax cash flows that are used to determine a rate of return on equity for the project. The model calculates a separate cash flow for the value of the gas purchased from the gas producers after consideration of royalty, severance taxes, state taxes and federal taxes. Economics for the overall project including gas purchase revenue are based upon the sum of the cash flows for the project and the gas purchase value.

YPC has completed economic analyses for the stand-alone projects according to a methodology used by the Alaska Legislature Joint Committee on Natural Gas Pipelines. This methodology employs adjustment of the gas purchase price until the return on equity for the downstream infrastructure equals 12 percent. Per this methodology, the 12 percent value reflects the value that would be allowed by the U.S. Federal Energy Regulatory Commission (FERC) for a typical pipeline project.

The project economics are calculated for two scenarios. The first scenario is based upon the assumption that the North Slope gas producers would own and operate the entire project. The economics for this scenario include the value of the natural gas on the North Slope. The second scenario is based upon the assumption that the North Slope gas producers would not participate in the project and that other investors would build the project and purchase the gas from the gas producers. This second scenario reflects the project for which the Joint Committee on Natural Gas Pipelines has assumed FERC would allow a 12 percent return on equity.

According to this methodology, the economics for the new stand-alone configurations of TAGS are:

	<u>Base</u>	<u>Lean Gas</u>
Economic summary		
Overall project including gas purchase revenue		
Return on equity (%)	17.5	16.6
Return on investment (%)	12.6	12.1
Gas purchase price		
Thermal basis – per million btu (\$/mmbtu)	0.94	0.84
Volume basis – per 1000 standard cubic feet (\$/mscf)	1.15	0.96
Percent of gross project revenues	32	28
Project excluding gas purchase revenue		
Return on equity (% , typical FERC)	12.0	12.0
Project volume		
LNG (MTA – million metric tons per annum)	12.5	13.5
Propane (1000 bpd - barrels per day)	100	76
Ethane to petrochemical feed (1000 bpd)	47	none
NGL blended into TAPS (1000 bpd)	17	none

Hydrocarbons are desired for their energy content and thus gas purchase and sale contracts are ultimately based on a thermal, or btu, basis. Recent discussions of Alaskan gas projects have referred to gas prices on a volumetric, or mscf, basis. The above table expresses gas purchase prices on both a thermal and volumetric basis determined according to the hydrocarbon content of the conditioned natural gas at the inlet of the pipeline.

The results of the economic models are, of course, dependent on the assumptions used for the various economic parameters and prices. YPC believes that its capital cost assumptions are generally conservative. YPC estimates the capital costs, expressed in year 2000 dollars, for the Base Case to be:

	\$ billion
Gas conditioning plant	2.1
Pipeline with compressor stations	4.0
LNG plant and marine terminal	3.9
12 LNG tankers	2.1
4 LPG tankers	0.5
1 bscfd LNG receiving terminal on the west coast of North America	0.4
TOTAL	13.0

The capital costs for the gas conditioning plant are based upon those published by the PBU for their proposed LNG project from South-central Alaska. The capital costs for the pipeline, compressor stations and liquefaction plant with marine terminal were prepared for YPC by Willbros Inc., Michael Baker, Jr. Inc., and Kellogg Brown & Root.

The following product prices, expressed in year 2002 dollars, were used in the economic analyses of the Base and Lean Gas cases:

	\$/mmbtu
Natural gas delivered within Alaska	2.50
LNG delivered to North America	3.25
LNG delivered to Asia	3.50
Propane delivered to Asia as LPG	4.38
Ethane to petrochemical feed	2.00
Natural gas liquids to TAPS	3.00*
* Equivalent to \$13.87/barrel	

The above prices are considered as representative of the various markets. The actual prices and market quantities required to support the project will be determined through negotiations among the various stakeholders in the project.

The price assumed for natural gas delivered within Alaska is at or below gas prices reported for recent gas contracts for in-state utility grade gas. The price for LNG to North America is within the range of price estimates offered by the Alaska Department of Revenue for LNG delivered to this market. LNG and LPG prices to Asia, and ethane delivered for petrochemical feedstock are based upon historical trends. The price of natural gas liquids to TAPS is an estimate reflecting the value after transport to Valdez, but prior to loading onto the oil tankers.

The project economics were based upon the following general economic assumptions:

Debt to equity ratio	70/30
Interest during construction and for debt financing	8 %
Debt service duration	15 years
Yearly inflation for nominal dollars	2.5 %

TAGS project size

Various projects have been proposed to commercialize North Slope natural gas by construction of large capacity pipelines from Alaska through Canada to the Lower-48. Some of these proposals include an option to install a secondary, or spur, pipeline to an LNG facility at tidewater in South-central Alaska. The TAGS project can be configured as a spur project from a Canadian pipeline and YPC does not dismiss this as a possibility. The configuration discussed in this document, however, consists of a stand-alone project that does not rely upon the installation of a pipeline through Canada.

PBU (Prudhoe Bay Unit) member companies recently presented information for a pipeline project through Canada to Chicago with an initial volume of 4.5 bscfd expandable to 5.6 bscfd. YPC offers no comment on this proposal other than to adopt it as the PBU gas pipeline project.

PBU member companies presented information to the Alaska Legislature in 2001 regarding a LNG project from tidewater in South-central Alaska to Asia. The PBU referred to this 7-8 MTA project as the "market entry project" and provided capital costs for this configuration. Again, YPC offers no comment on this proposal other than to adopt it as the PBU LNG project.

YPC's new configuration of TAGS is based upon a volume of 2.2 bscfd of conditioned gas entering the pipeline on the North Slope of Alaska. The preferred scenario, or Base Case, for TAGS is based upon delivery of 7.6 MTA of LNG (1 bscfd natural gas equivalent) to the west coast of North America and 5.0 MTA of LNG (0.66 bscfd) to Asia. The remainder of the pipeline gas consists of propane for ultimate sale as LPG, ethane for extraction and sale to a petrochemical plant, natural gas for sale within Alaska, natural gas liquids for extraction and sale to the Trans-Alaska Pipeline System, and project fuel.

TAGS is based upon delivery of approximately one fifth the amount of natural gas to the Lower-48 market proposed for the PBU gas pipeline project. The difference is that this smaller volume of gas is targeted to the U.S. west coast instead of the U.S. mid-west. Although small relative to the PBU gas pipeline project, delivery of 1 bscfd of natural gas (7.6 MTA of LNG) to the US west coast represents a large LNG project.

The TAGS Base Case is based upon delivery of approximately 60% of the volume of LNG specified by the PBU as the "market entry" project from Alaska to Asia.

The new configuration of TAGS targets market volumes to the Lower-48 and Asia that are less than those specified by the pipeline and LNG projects recently evaluated by the North Slope gas producers to serve these respective markets. The new configuration of TAGS differs from these projects in that both markets will be served simultaneously thereby providing a collective volume large enough to achieve the economies of scale necessary to support the overall project.

Propane sale via TAGS

The existing production facilities at Prudhoe Bay concentrate propane and other hydrocarbons from approximately 8.5 bscfd of natural gas produced from the field into a single stream of approximately 0.45 bscfd. This stream is reinjected back into the reservoir as part of the enhanced oil recovery (EOR) project at Prudhoe Bay. The new configurations of TAGS are based upon extraction of propane contained in this stream with subsequent sale of the propane as LPG to Asia.

The PBU has projected that the enhanced oil recovery project may be completed by around the year 2010 which is the earliest date now projected for the start-up of TAGS. YPC has assumed that the life of the enhanced oil project may extend past 2010 and has configured TAGS to mitigate the impact on the EOR project due to the removal of the propane.

Historically, LPG (propane) has commanded a higher price in Asia than LNG. The price differential has been increasing over the last ten years thus indicating a strengthening LPG market. Articles in trade journals (example: "Trade recovery pushes world LPG demand past 200 million tonnes", Oil & Gas Journal, June 24, 2002) also indicate a strengthening LPG market. Existing and recently announced LNG projects around the Pacific Rim include LPG sales to the Asian market.

The sale of LPG to Asia will add significant revenue to TAGS thereby supplementing LNG revenue and enhancing project economics. The propane will be extracted upstream of the liquefaction plant in Valdez thereby minimizing the size of the capital-intensive liquefaction facilities.

Value added options and Lean Gas Case

The option exists to extract ethane and/or butane along with the propane upstream of the liquefaction facilities in Valdez. The ethane and butane can be used as feedstock to a petrochemical industry at tidewater in South-central Alaska. A petrochemical industry would provide new employment and a tax base within Alaska and as such represents a true "value added" use of Alaska's natural resources. Similar

to propane, extraction and sale of ethane and/or butane adds value to TAGS by supplementing LNG revenues.

TAGS can accommodate either a raw gas from oil production facilities or a residue gas leaving the existing gas handling facilities at Prudhoe Bay. Use of a raw gas may provide for an increase in near term oil production by allowing oil wells that are currently shut-in to be put on-line. The gas from these wells would simply be sent to TAGS for subsequent disposition via the gas project. YPC has included no credit for this potential increase in oil production in the TAGS project economics.

A raw field gas contains hydrocarbon components that can be blended into the crude oil flowing through TAPS (the Trans-Alaska Pipeline System). Hydrocarbons extracted from natural gas and mixed into the TAPS oil pipeline are referred to as blendable natural gas liquids or generically as NGL. YPC has assumed that if a raw gas feed is used for TAGS the resulting NGL can be removed from the gas in Valdez and blended into TAPS immediately upstream of the Valdez Marine Terminal. As noted above, use of a raw gas will result in incremental crude oil production at Prudhoe Bay. The relative amounts of crude oil and NGL tendered to TAPS will be the same regardless of whether the NGL is blended into TAPS on the North Slope or blended in Valdez. YPC has included revenue from the sale of the NGL in the project economics since the investment for TAGS includes facilities to transport and separate the NGL for delivery to TAPS in Valdez.

The TAGS Base Case configuration is based upon successful implementation of all the value added options. YPC is also considering a fall back scenario based upon the assumption that for some reason a petrochemical industry is not viable in Alaska and a raw field gas cannot be used as feed to TAGS. The benefits of increased crude oil production and the associated NGL will not be achieved without use of a raw gas feed to TAGS. The fall back scenario is referred to as the Lean Gas Case since it is assumed that residue gas leaving the processing facilities at Prudhoe Bay will be used as feed to TAGS. Some of the ethane and propane, and most of the butane and NGL, are removed from the gas in the processing facilities thus the residue gas is "lean" with respect to the amount of these components remaining in the gas.

Impact on oil production

Oil loss attributed to a major gas sale appears to be tied to the amount of gas removed from the reservoir and the corresponding drop in reservoir pressure. One would expect relatively less adverse impact on oil with a gas sale of 2.2 bscfd to TAGS since this is the smallest of the Alaskan gas projects currently being proposed. The TAGS project would thus represent a gain in oil production compared to a reference case of the PBU pipeline project through Canada.

A finite volume of hydrocarbons must be reinjected to recover a prescribed amount of oil targeted by the Prudhoe Bay enhanced oil recovery project. A reduction in the volume of injectant would defer, not preclude, recovery of the oil target. A material balance around the conditioning plant proposed for TAGS shows that use of the CO₂ and butane byproducts can be used to keep the injectant volume approximately 60 percent whole on the rate. The adverse impact on the EOR project is expected to be negligible because this project will be near or at the end of its life by the time of TAGS start-up, and the byproducts from the gas conditioning plant can be used to mitigate the reduction of injectant volume.

Availability of energy for use within Alaska

Utility grade natural gas can be made available anywhere along the gas pipeline with the installation of minimal equipment. The gas flowing through the pipeline will be free of carbon dioxide and water

moisture. A utility grade natural gas can be obtained simply by dropping the pressure of the gas from pipeline conditions with the advantageous use of heat exchangers, valves, separators and pumps.

LNG and LPG will be temporarily stored in Valdez. The opportunity exists for transport of these products to tidewater communities throughout Alaska.

YPC is focusing its resources on development of the basic TAGS infrastructure since without this infrastructure derivative energy projects within Alaska cannot occur. YPC does not underestimate the potential complexities involved with serving the diverse energy needs within Alaska. The successful implementation of an Alaskan energy distribution system based on the TAGS project will likely depend more on transportation issues rather than the price of the commodity itself. YPC does not see its role as usurping the function of local energy utilities or the marine transportation industry within Alaska.

YPC fully expects that TAGS will allow various energy projects to occur within Alaska and remains willing to work with parties interested in developing these projects.

Summary

Through the configurations presented, Yukon Pacific Corporation has demonstrated that there are significant benefits to be realized by developing a pipeline that utilizes the large, undeveloped gas resource in Alaska's North Slope. Yukon Pacific Corporation is ready to work with all parties interested, and we welcome any constructive input or participation to advance the project.

Questions regarding this document should be sent to:

Ward Whitmore
Director of Project Development
Yukon Pacific Corporation
1400 West Benson Blvd., Suite 525
Anchorage, Alaska 99503
Phone: 907-265-3108
e-mail: wwhitmore@ypc.com

HOUSE COMMITTEE REPORT

(7)

Date Referred to Committee: April 15, 2003

FURTHER REFERRALS: Resources
Finance

Date of Committee Action: 4/24/03

The HOUSE SPECIAL COMMITTEE ON OIL AND GAS Committee considered: HB 267

HOUSE BILL NO. 267

AK RAILROAD BONDS FOR NAT.GAS TRANSPORT

"An Act relating to the Alaska Railroad; authorizing the Alaska Railroad Corporation to provide financing for the acquisition, construction, improvement, maintenance, equipping, or operation of facilities for the transportation of natural gas resources within and outside the state by others; authorizing the Alaska Railroad Corporation to issue bonds to finance those facilities; and providing for an effective date."

Recommends it be replaced with HCS or CS for _____ (_____)
 For Senate Bills with new title: Technical Title New Title: HCR _____ Same Title New Title

- attach amendments
- add new referral to _____ Committee
- Letter of Intent _____ Committee

List of Abbrev for Depts.:

- ADM
- CED
- COR
- CRT
- EED
- DEC
- DFG
- GOV
- ISS
- LEG
- LAW
- LWF
- MVA
- DNR
- DPS
- REV
- DOT
- UA

<u>NEW FISCAL NOTES</u>				
*Assigned by Chief Clerk's Office				
List by Dept(s):	*FN#	Fiscal	Indet.	Zero
CED		✓		

<u>PREVIOUS FISCAL NOTES</u>				
List by Dept(s):	FN#	Fiscal	Indet.	Zero

<u>Signing with recommendations</u>	Printed Last Name	DP	DNP	NR	AM
	Holum	✓			
	McQuire	✓			
	Fote	✓			
	Kerthila			✓	
	CRAWFORD	✓			
Chair:	Habring		X		
Chair:	Habring		X		

ConocoPhillips
Alaska, Inc.

Wendy D. King
Director, External Strategies

P.O. Box 100360 - Suite ATO 2038
Anchorage, Alaska 99510-0360
Phone (907) 265-6026
Fax (907) 265-6838

May 6, 2003

Rep. Vic Kohring
State Capitol
Juneau, Alaska 99801

Re: *ConocoPhillips Supports HB 267 (An Act authorizing the Alaska Railroad Corporation to provide financing for the transportation of natural gas resources.)*

Dear Representative Kohring,

ConocoPhillips supports passage of HB 267, which authorizes the Alaska Railroad Corporation to provide financing for a potential North Slope gas pipeline project. ConocoPhillips' three-pronged strategy to make a gas pipeline through Alaska and Canada a reality includes the following:

1. Federal legislation to streamline permitting;
2. Federal fiscal legislation—which provides insurance against the risk of extreme price volatility;
3. State fiscal certainty and clarity – which will be progressing with the recently passed HB 16, reauthorizing the Stranded Gas Development Act.

If ConocoPhillips is successful in securing these three items, we will continue to move forward on the project. Financing this potentially \$20 billion project will be a significant priority for any company that pursues the Alaska gas pipeline project, and we support the State providing as many tools as possible to choose from when the time comes. While it is too early to select specific financing vehicles, HB 267 will add a potentially valuable option.

Thank you for being supportive of efforts to commercialize Alaska North Slope Gas.

Regards,

Wendy D. King
Wendy King
Director, External Strategies
ANS Gas Development
ConocoPhillips Alaska



Alaska Gas Pipeline Financing Alternatives

Natural Gas Pipeline Policy Council



February 7, 2002

Table of Contents

TAB	
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Key Assumptions and Background	4
■ Rates on Debt	
■ Credit	
■ Size	
■ Discount rates	

Tab 1
***Tax-Exempt Approach
to Alaska Gas Pipeline
Financing***

Similar Alaska Development Projects Benefited From Tax-exempt Financing

- Valdez—Producers took advantage of tax exemption for “dock and wharf” related assets which support TAP oil exports. Bonds issued by City of Valdez. Proceeds loaned to producers.

- Fort Knox—AIDEA tax-exempt financed solid waste disposal facility at Fort Knox Gold Mine.

- Snettisham—Tax-exempt financing of Snettisham Dam by AIDEA, used by AEL&P.

Historical Tax-Exempt Precedent for TAPS

\$100,000 Exxon Valdez Terminal

OFFICIAL STATEMENT

\$250,000,000
City of Valdez, Alaska
5.50% Marine Terminal Revenue Bonds
(Exxon Pipeline Company Project)
Series A
due May 1, 2007

The Bonds will not constitute general obligations of the City or a charge against the general credit or taxing power of the City or the State of Alaska. The Bonds are payable from and secured by the revenues derived under a Sublease Agreement between the City and

EXXON PIPELINE COMPANY
Payment of the principal of, premium, if any, and interest on the Bonds is guaranteed by
EXXON CORPORATION

The Bonds are redeemable on or before 10 days' notice (a) at the discretion of Exxon Pipeline Company, as a whole or in part at any time, at 100% of the principal amount on and after May 1, 1993 to and including April 30, 1994 and at decreasing periods thereafter; (b) pursuant to mandatory redemption provisions on May 1, 1998 and on 5 May 1 thereafter to and including May 1, 2006 at 100% of the principal amount; and (c) in the event of certain of the above events, at a call at any time, at 100% of the principal amount, with accrued but unpaid interest, in each case together with accrued interest to the date of redemption.

Interest on the Bonds will be payable on November 1, 1997 and thereafter semi-annually on May 1 and November 1 of each year. Principal and interest are payable at the corporate trust office of The Bank of New York, the Trustee and Paying Agent, in New York, New York. The Bonds will be issued initially as coupon bonds, dated May 1, 1997, in the denomination of \$1,000, and may subsequently be registered as to principal only, or as both principal and interest in denominations of \$1,000 or any multiple thereof.

Successful bidders have agreed to purchase the Bonds at a price of 98 1/8%. Reference is made to "Description of the Bid Processors" and "Terms of the Bidding" herein. Certain of such bidders may register bonds on the over-the-counter market, in negotiated transactions or otherwise, at less than par value. There is an agreement between the City, Exxon Pipeline Company or Exxon Corporation and any such bidder as to the price at which any such resale of Bonds may be made and accordingly given to be paid by the bidder in those sales may vary between resulting bid price and change from time to time.

In the opinion of Messrs. Chapman and Cutler and Messrs. Wolford & PBN, Bond Counsel, interest on the Bonds is exempt from Federal income taxation to the extent, upon the conditions and subject to the restrictions stated in the "Tax Exemption" herein.

The Bonds are offered herein, as and if issued by the City, subject to the approval of legality by Bond Counsel, the approval of certain legal matters by Messrs. Deane Park & Woodward, which firm has been designated by Exxon Pipeline Company and Exxon Corporation as counsel for the Purchaser, and certain other conditions. It is expected that delivery of the Bonds will be made on or about May 12, 1997 at the office of Morgan Guaranty Trust Company of New York, 11 Broad Street, New York, N. Y., against payment therefor.

May 1, 1997

\$200,000 ARCO Valdez Terminal

NEW ISSUE

In the opinion of Bond Counsel, based upon existing statutes, regulations, court decisions and rulings, including a ruling from the Internal Revenue Service dated January 19, 1977, interest on the Series 1977 Bonds described herein is exempt from all present Federal income taxes except under certain conditions as explained under the caption "Tax Exemption" herein. Further, in the absence of bond counsel, under existing statutes, such interest is also exempt from all present Alaska taxes except for inheritance and estate taxes and taxes on transfers by or in contemplation of death.

OFFICIAL STATEMENT

\$265,000,000
CITY OF VALDEZ, ALASKA
5.90% MARINE TERMINAL REVENUE BONDS
(ARCO Pipe Line Company Project)
Series 1977

Dated: February 3, 1977 Due: February 1, 2017

Price: 99.5%
 (Plus accrued interest from February 3, 1977)

Payable, except to the extent payable from proceeds of the Series 1977 Bonds or from income from the temporary investment of such proceeds, solely from and secured solely by a pledge of payments derived from the revenues of the Project by the City to

ARCO PIPE LINE COMPANY

The Series 1977 Bonds will not constitute general obligations of the City or a charge against the general credit or the taxing power of the City or the State of Alaska. The Trustee will receive an unconditional guaranty of the payment of the principal of, premium, if any, and interest on the Series 1977 Bonds from

ATLANTIC RICHFIELD COMPANY

The Series 1977 Bonds will be issuable as coupon bonds in the denomination of \$1,000 each, registrable as to principal only, and as fully registered bonds without coupons in the denomination of \$5,000 and any integral multiple thereof. Coupon bonds and fully registered bonds will be interchangeable as explained under the caption "The Bonds" herein. Principal, premium, if any, and semi-annual interest (February 1 and August 1, commencing August 1, 1977) on the coupon bonds will be payable at the principal office of Seattle First National Bank, 1977 on the coupon bonds will be payable at the principal office of the holder at the principal office of the Trustee, Washington, as Trustee, or at the option of the holder at the principal office of Morgan Guaranty Trust Company of New York, in New York, New York, as Paying Agent. Principal and premium, if any, on fully registered bonds are payable at the principal office of the Trustee. Interest on fully registered Bonds will be paid by check or draft mailed by the Trustee.

The Series 1977 Bonds will be subject to redemption prior to maturity as described herein.

The Series 1977 Bonds are offered, subject to prior sale, when, so and if issued by the City of Valdez, Alaska and accepted by the Underwriters named below, subject to the approval of legality by Messrs. Chapman and Cutler and Messrs. Wolford & PBN, as bond counsel, and the approval of certain legal matters by Messrs. Hulse Rock Cohen Campbell Gortlieb & Woodward, as counsel for the Underwriters, and in certain other conditions. It is expected that delivery of the Series 1977 Bonds will be made on or about February 10, 1977, in New York, New York, against payment therefor.

BLYTH EASTMAN DILLON & CO.
 INCORPORATED
HACHE HALSEY STUART INC.
 INCORPORATED
MERRILL LYNCH, PIERCE, FENNER & SMITH
 INCORPORATED
DEAN WITTER & CO.
 INCORPORATED

Dated: February 8, 1977

Tax-exempt Financing for Alaska Gas Pipeline

- Alaska railroad statute permits tax-exempt bonds to be issued by the Railroad, and such bonds would not be “private activity bonds” requiring volume cap or being subject to AMT, despite the private use of the pipeline.

“Obligations issued by such entity shall be deemed to be obligations of the State...[means tax-exempt]...but not obligations within the meaning of section 103(b)(2) [means not private activity bonds]”

- The actual ownership of the assets may still be in the hands of private parties allowing them to use depreciation benefits.
- The credit would be “ship-or-pay” contracts, not the Railroad’s or the State’s general credit or assets.

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Tab 2
Pipeline Precedent

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Alliance Pipeline

CONFIDENTIAL



U.S. \$550,000,000
Alliance Pipeline L.P.
3.996% Senior Notes due 2019
7.877% Senior Notes due 2025

The \$550 million senior notes due 2019 (the "2019 Notes") and the \$200 million senior notes due 2025 (the "2025 Notes") (collectively, the "Notes") are being issued by Alliance Pipeline L.P. ("Alliance Pipeline" or the "Issuer"), a Delaware limited liability partnership, formed to develop, design, finance, construct, commission and operate the Alaska USA Pipeline, which is a portion of the Alaska Pipeline System. The Alaska Pipeline System is a natural gas pipeline system in Alaska, USA, which will consist of an approximately 1,825 mile single pipeline (the "Alaska Pipeline System") and a series of smaller pipelines located in Canada, and related infrastructure. The System has been designed to transport 1.25 billion cubic feet ("bcf") of natural gas per day ("d") ("NGL") to a firm transportation outlet in the northeastern United States and northwestern Canada. The Alaska Pipeline System is a firm transportation outlet in the northeastern United States and northwestern Canada. The Alaska Pipeline System is a firm transportation outlet in the northeastern United States and northwestern Canada. The Alaska Pipeline System is a firm transportation outlet in the northeastern United States and northwestern Canada.

Offering Prices
Senior Notes due 2019: 100%
Senior Notes due 2025: 100%

The offering prices set forth above do not include accrued interest, if any, which on the Notes will accrue from March 8, 2001, and will be paid by the purchaser if the Notes are delivered after March 8, 2001.

The Notes have not been registered under the Securities Act and are being offered and sold in the United States only by Goldman, Sachs & Co. ("Goldman, Sachs & Co.") as the sole U.S. dealer. The Notes are being offered and sold in the United States only by Goldman, Sachs & Co. as the sole U.S. dealer. The Notes are being offered and sold in the United States only by Goldman, Sachs & Co. as the sole U.S. dealer.

Joint Lead Managers and Joint Lead Bookrunner
Goldman, Sachs & Co.
ABN AMRO Incorporated
Banc of America Securities LLC
Scotia Capital (USA) Inc.
The Royal Bank of Scotland, Financial Markets
JPMorgan

Offering Circular dated March 1, 2001.

CONFIDENTIAL



U.S. \$300,000,000
Alliance Pipeline L.P.
7.77% Senior Notes due 2015

The 7.77% senior notes due 2015 (the "Notes") are being issued by Alliance Pipeline L.P. ("Alliance Pipeline" or the "Issuer"), a Delaware limited liability partnership, formed to develop, design, finance, construct, commission and operate the Alaska USA Pipeline, which is a portion of the Alaska Pipeline System. The Alaska Pipeline System is a natural gas pipeline system in Alaska, USA, which will consist of an approximately 1,825 mile single pipeline (the "Alaska Pipeline System") and a series of smaller pipelines located in Canada, and related infrastructure. The System has been designed to transport 1.25 billion cubic feet ("bcf") of natural gas per day ("d") ("NGL") to a firm transportation outlet in the northeastern United States and northwestern Canada. The Alaska Pipeline System is a firm transportation outlet in the northeastern United States and northwestern Canada. The Alaska Pipeline System is a firm transportation outlet in the northeastern United States and northwestern Canada.

Offering Price: 100%
Interest on the Notes will accrue from the date of issuance.

The Notes have not been registered under the Securities Act and are being offered and sold in the United States only by Goldman, Sachs & Co. ("Goldman, Sachs & Co.") as the sole U.S. dealer. The Notes are being offered and sold in the United States only by Goldman, Sachs & Co. as the sole U.S. dealer. The Notes are being offered and sold in the United States only by Goldman, Sachs & Co. as the sole U.S. dealer.

Goldman, Sachs & Co.
Scotia Capital Markets (USA) Inc.
Chase Securities Inc.
Nesbitt Burns Securities Inc.

Offering Circular dated June 18, 1998.

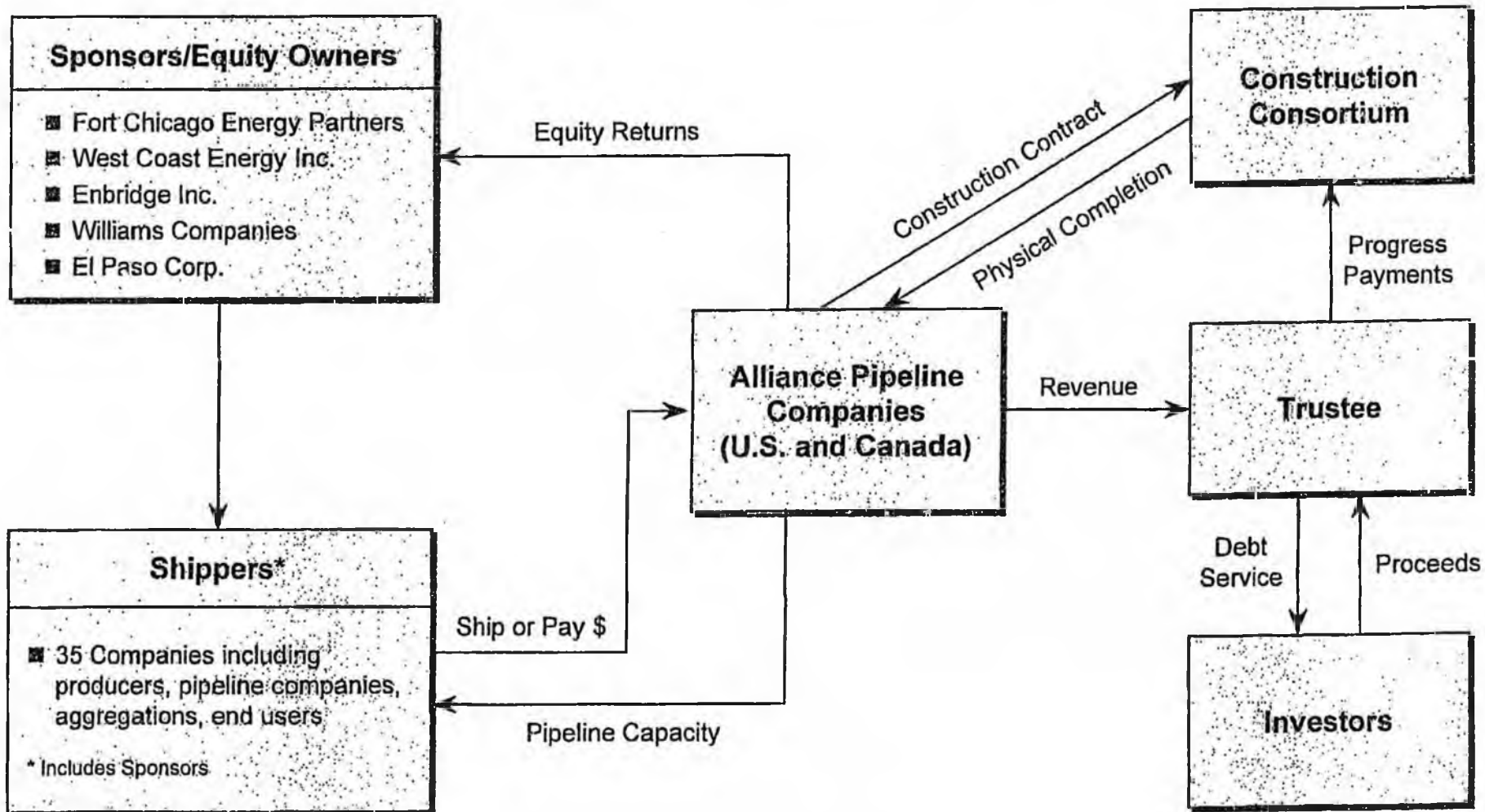
Ship-or-Pay contracts are the key credit item.

Example from Alliance Pipeline:

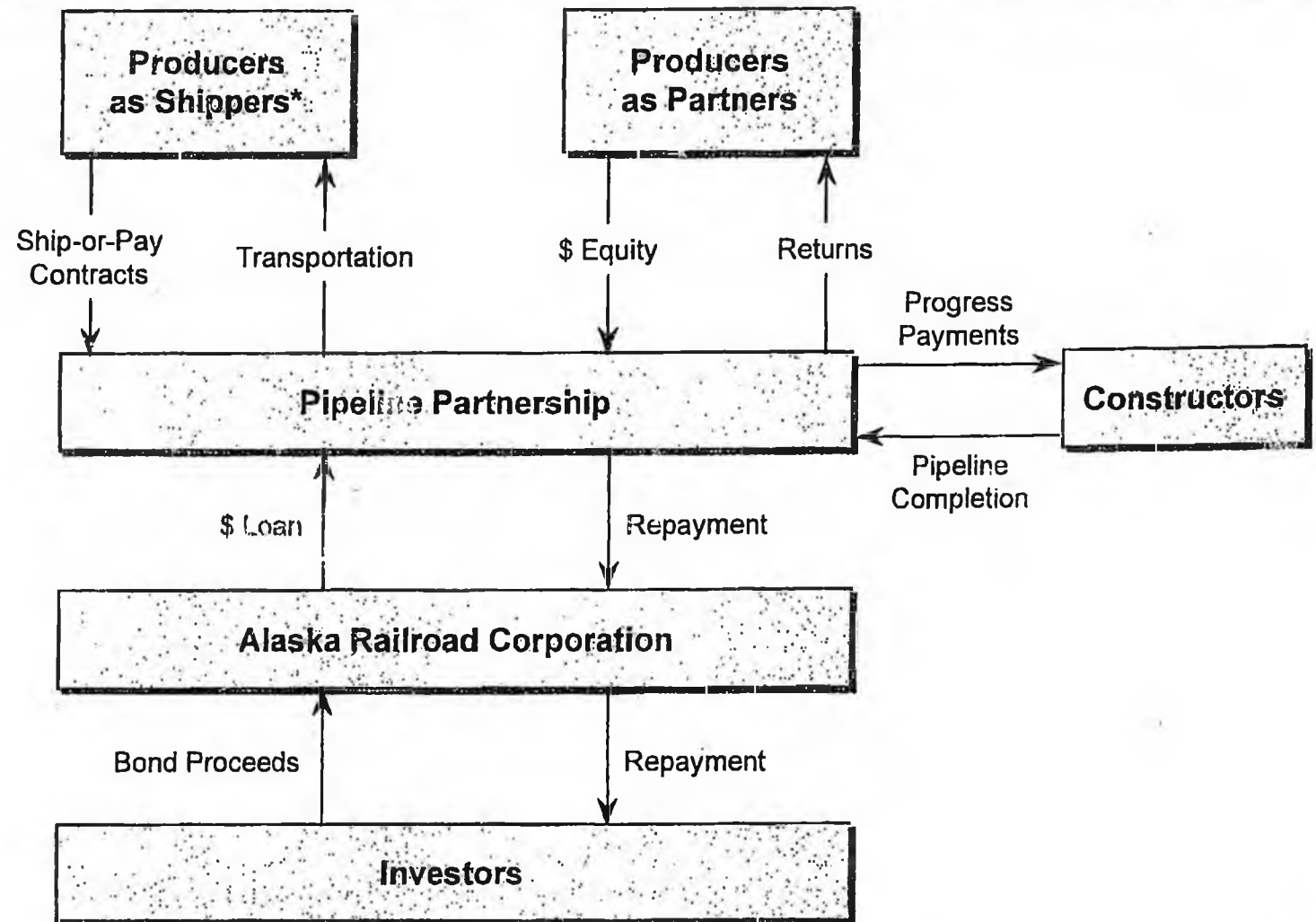
"All of the 1.325 b.c.f.d. of firm transportation capacity of the System has been contracted by the shippers. . ."

- Contracts require payment regardless of pipeline use
- 72.5% of shippers have investment grade rating
- 14.9% were not investment grade, but accepted by lenders
- 12.6% were required to post letters of credit
- Contracts were 15 years in length

Alliance Pipeline Structure



Schematic of Alaska Gas Pipeline Financing Arrangement



* Shippers would likely include users other than producers.

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Tab 3
Analysis of Tax-Exempt
Financing Benefits

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Present Value Analysis of Financing Alternatives—Taxable Debt

Taxable Analysis		Not Lease Payment		Depreciation		Loss Tax Shield		Net		M/A Altern Tax	
Prin/Int	Int	Cap/Cor	Cap/Earn	Dep	Proj Cost	Dep	Proj Cost	Proj Cost	Proj Cost	Proj Cost	Proj Cost
A	B	C	D	E	F	G	H	I	J	K	L
\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
1/1/02											
1/1/03	1,264,748,575	925,822,580	398,928,015								
1/1/04	1,264,748,575	1,008,189,744	258,558,831								
1/1/05	1,264,748,575	1,083,533,303	171,215,272								
1/1/06	1,264,748,575	1,108,458,828	76,289,747								
1/1/07	1,264,748,575			1,580,388,576	988,889,750	928,124,513	852,244,062			852,244,062	
1/1/08	800,485,000			1,858,416,675	1,808,042,526	1,285,744,094	572,070,881			572,070,881	
1/1/09	604,615,000			1,788,783,800	1,705,238,273	1,188,301,000	603,492,800			603,492,800	
1/1/10	583,025,000			1,728,811,525	1,538,413,415	1,095,801,875	831,208,550			831,208,550	
1/1/11	587,305,000			1,870,884,400	1,392,563,832	1,015,136,726	655,547,875			655,547,875	
1/1/12	578,630,000			1,813,088,475	1,244,716,309	934,051,681	878,030,814			878,030,814	
1/1/13	598,430,000			1,580,819,925	1,178,784,305	886,819,434	683,800,491			683,800,491	
1/1/14	634,835,000			1,568,128,376	1,178,784,305	866,033,849	702,094,528			702,094,528	
1/1/15	875,020,000			1,554,568,400	1,178,784,305	843,810,819	710,652,581			710,652,581	
1/1/16	717,890,000			1,538,892,700	1,178,784,305	820,392,372	719,470,320			719,470,320	
1/1/17	782,735,000			1,523,804,050	1,178,784,305	785,360,876	728,523,174			728,523,174	
1/1/18	810,260,000			1,508,588,575	1,178,784,305	768,799,561	737,787,014			737,787,014	
1/1/19	880,345,000			1,487,808,475	1,178,784,305	740,982,000	747,247,475			747,247,475	
1/1/20	813,090,000			1,445,307,500	1,178,784,305	710,578,877	758,848,173			758,848,173	
1/1/21	888,585,000			1,487,425,150	1,178,784,305	678,757,790	786,548,710			786,548,710	
1/1/22	838,625,000			1,234,017,775	589,382,153	403,351,820	830,655,855			830,655,855	
1/1/23	697,655,000			1,020,688,650		132,440,107	888,248,644			888,248,644	
1/1/24	728,715,000			892,438,125		108,128,481	884,311,844			884,311,844	
1/1/25	780,010,000			881,782,850		82,730,784	878,081,587			878,081,587	
1/1/26	791,360,000			828,541,500		56,244,416	872,387,085			872,387,085	
1/1/27	822,540,000			892,455,900		28,665,519	883,780,381			883,780,381	
	\$14,879,395,000	\$20,122,820,400	\$4,214,004,435	\$28,943,931,100	\$19,879,395,000	\$14,867,761,651	\$16,575,559,448			\$16,575,559,448	\$7,227,936,387

Present Value Analysis of Financing Alternatives—Tax-Exempt Debt

	Principal		Interest		CAPL Corpus		GAPI Earnings		Not Lease Payment		Depreciation		Lease Tax Shield		Increased After		Net After Tax Pmts		PV of Net After Tax Pmts	
	A	B	C	D	E	F	G	H	I	J	K	L	M	N	O	P	Q	R	S	T
1/1/02	\$																			
1/1/03		919,353,025	723,373,781	195,980,044																
1/1/04		919,353,025	771,157,140	148,198,885																
1/1/05		919,353,025	822,096,889	87,255,836																
1/1/06		919,353,025	876,401,527	42,852,298																
1/1/07	371,320,000	919,353,025			1,280,873,825															
1/1/08	674,480,000	895,218,025			1,569,878,025															
1/1/09	650,850,000	851,378,125			1,502,228,125															
1/1/10	631,590,000	809,072,875			1,440,662,875															
1/1/11	618,203,000	768,018,525			1,386,219,525															
1/1/12	602,780,000	727,838,525			1,330,618,525															
1/1/13	611,825,000	688,655,825			1,300,480,825															
1/1/14	641,820,000	648,887,200			1,290,707,200															
1/1/15	673,125,000	607,188,800			1,280,283,800															
1/1/16	705,790,000	563,415,775			1,268,205,775															
1/1/17	738,855,000	517,538,425			1,257,394,425															
1/1/18	775,385,000	469,448,850			1,244,813,850															
1/1/19	812,370,000	419,050,125			1,231,420,125															
1/1/20	850,985,000	366,246,075			1,217,151,075															
1/1/21	891,020,000	310,937,250			1,201,957,250															
1/1/22	745,455,000	253,020,850			988,475,850															
1/1/23	593,385,000	204,588,375			783,951,375															
1/1/24	602,345,000	186,258,350			775,601,350															
1/1/25	628,485,000	126,648,925			756,053,925															
1/1/26	648,485,000	85,737,500			735,232,600															
1/1/27	680,545,000	43,520,425			713,065,425															
	\$14,143,985,000	\$14,118,384,250	\$3,100,029,338	\$494,388,964	\$24,685,883,850	\$19,243,865,000	\$12,171,212,420	\$685,300,000	\$13,107,671,531	\$8,084,100,702	\$48,084,100,702									

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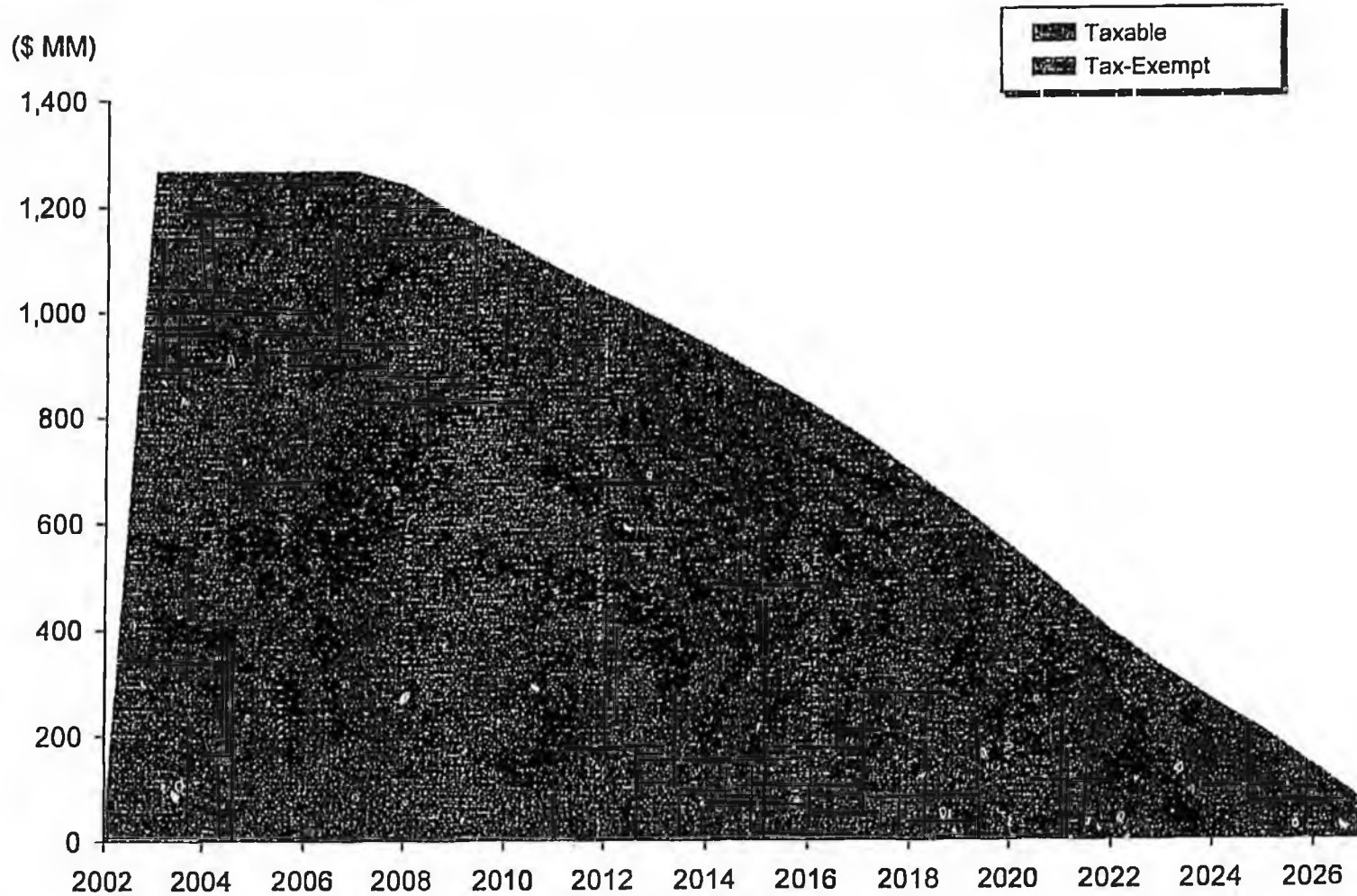
Present Value Analysis of Financing Alternatives Taxable vs. Tax-Exempt—Private Ownership

Assumptions	
Taxable Scenario	Tax-Exempt—Private Ownership Scenario
Par Face Amount	\$14,143,905,000
Rate	6.500%
Discount Rate	8.500%

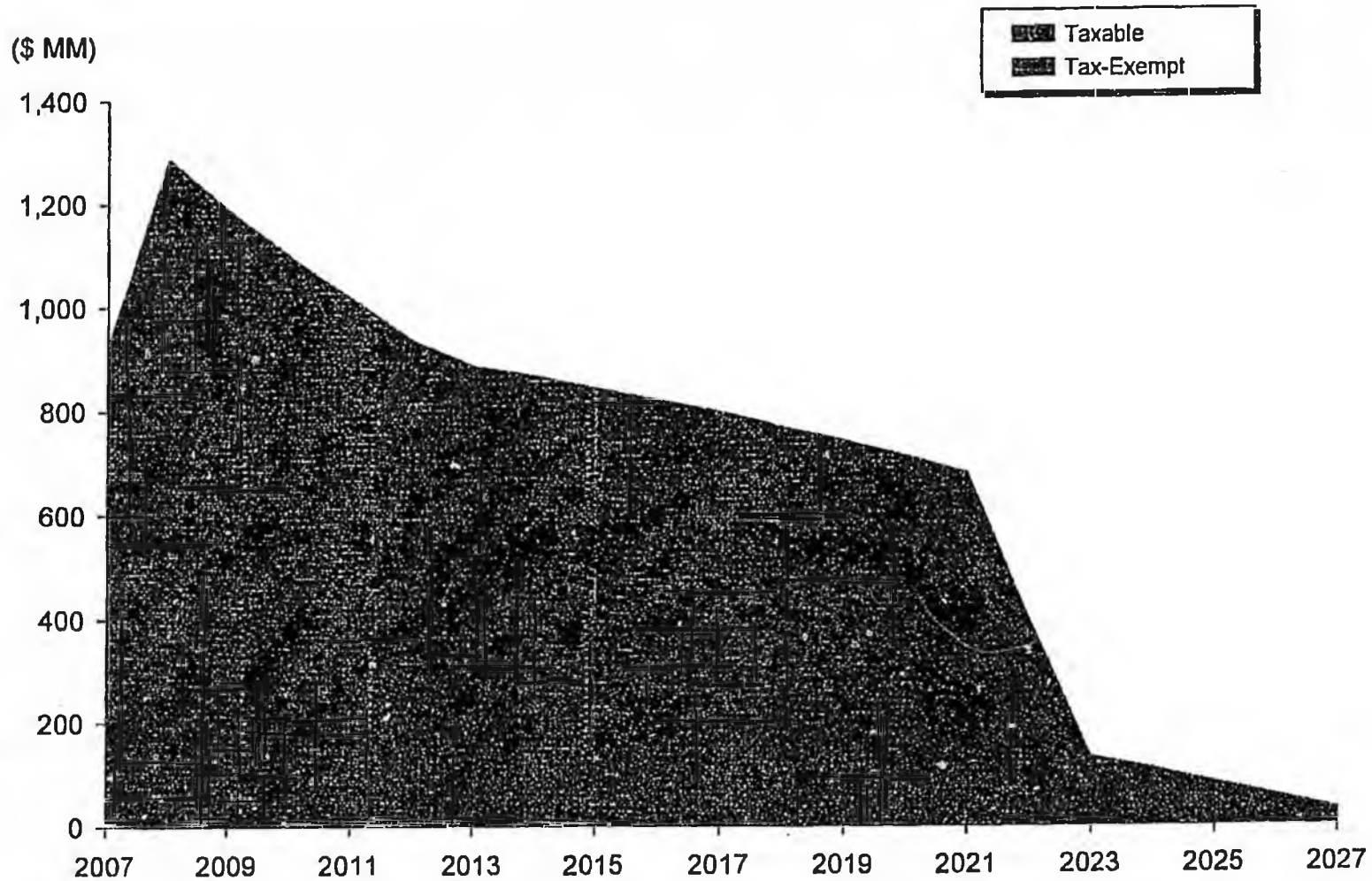
Date	Taxable Scenario		Tax-Exempt Projection Ownership Scenario		Comparisons	
	Net After-Tax Payments	PV of Net After-Tax Payments	Net After-Tax Payments	PV of Net After-Tax Payments	Difference in After-Tax Payments	Difference in PV
1/1/02	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
1/1/03	-	-	-	-	-	-
1/1/04	-	-	-	-	-	-
1/1/05	-	-	-	-	-	-
1/1/06	-	-	-	-	-	-
1/1/07	852,244,062	652,244,062	552,236,704	552,236,704	100,005,358	100,005,357.60
1/1/08	572,670,881	526,930,059	447,263,288	447,263,288	66,682,348	179,072,128.76
1/1/09	603,482,800	510,637,571	433,110,905	433,110,905	91,924,798	257,498,784.02
1/1/10	631,208,550	491,719,214	418,313,588	418,313,588	86,786,634	332,804,442.58
1/1/11	655,547,875	469,889,534	397,366,854	397,366,854	101,148,229	405,407,123.48
1/1/12	679,036,814	447,850,108	378,347,850	378,347,850	105,380,329	474,809,381.07
1/1/13	693,600,481	421,038,528	355,389,446	355,389,446	65,849,082	540,558,463.55
1/1/14	702,084,620	392,040,285	330,650,808	330,650,808	109,941,140	601,848,140.14
1/1/15	710,652,581	365,123,949	307,679,473	307,679,473	111,807,092	659,393,815.72
1/1/16	719,470,328	340,129,063	286,341,977	286,341,977	113,775,083	713,180,701.43
1/1/17	728,623,174	316,899,897	266,515,079	266,515,079	115,828,876	768,565,519.20
1/1/18	737,267,014	295,300,031	248,084,153	248,084,153	117,907,255	810,781,307.46
1/1/19	747,247,475	275,183,880	230,840,261	230,840,261	120,147,963	856,029,119.32
1/1/20	758,846,173	256,466,098	215,000,944	215,000,944	122,366,051	896,494,271.05
1/1/21	768,549,710	238,311,226	200,181,321	200,181,321	124,588,784	935,339,806.48
1/1/22	800,695,955	224,477,382	189,155,751	189,155,751	145,170,382	974,266,421.91
1/1/23	808,249,544	214,782,533	179,848,300	179,848,300	143,875,397	1,012,588,052.92
1/1/24	804,311,844	198,483,108	164,742,077	164,742,077	141,933,721	1,047,534,266.11
1/1/25	878,091,567	179,378,683	150,761,299	150,761,299	139,216,901	1,078,255,317.27
1/1/26	872,297,085	163,442,809	137,781,196	137,781,196	135,568,330	1,107,884,011.79
1/1/27	863,780,381	149,000,000	122,000,000	122,000,000	135,568,330	1,133,535,665.08
Total	\$15,676,559,440	\$7,227,836,387	\$6,084,100,702	\$6,084,100,702	\$2,487,887,919	\$1,133,535,665

* Debt service is net of the construction and CAPI funds' interest earnings.

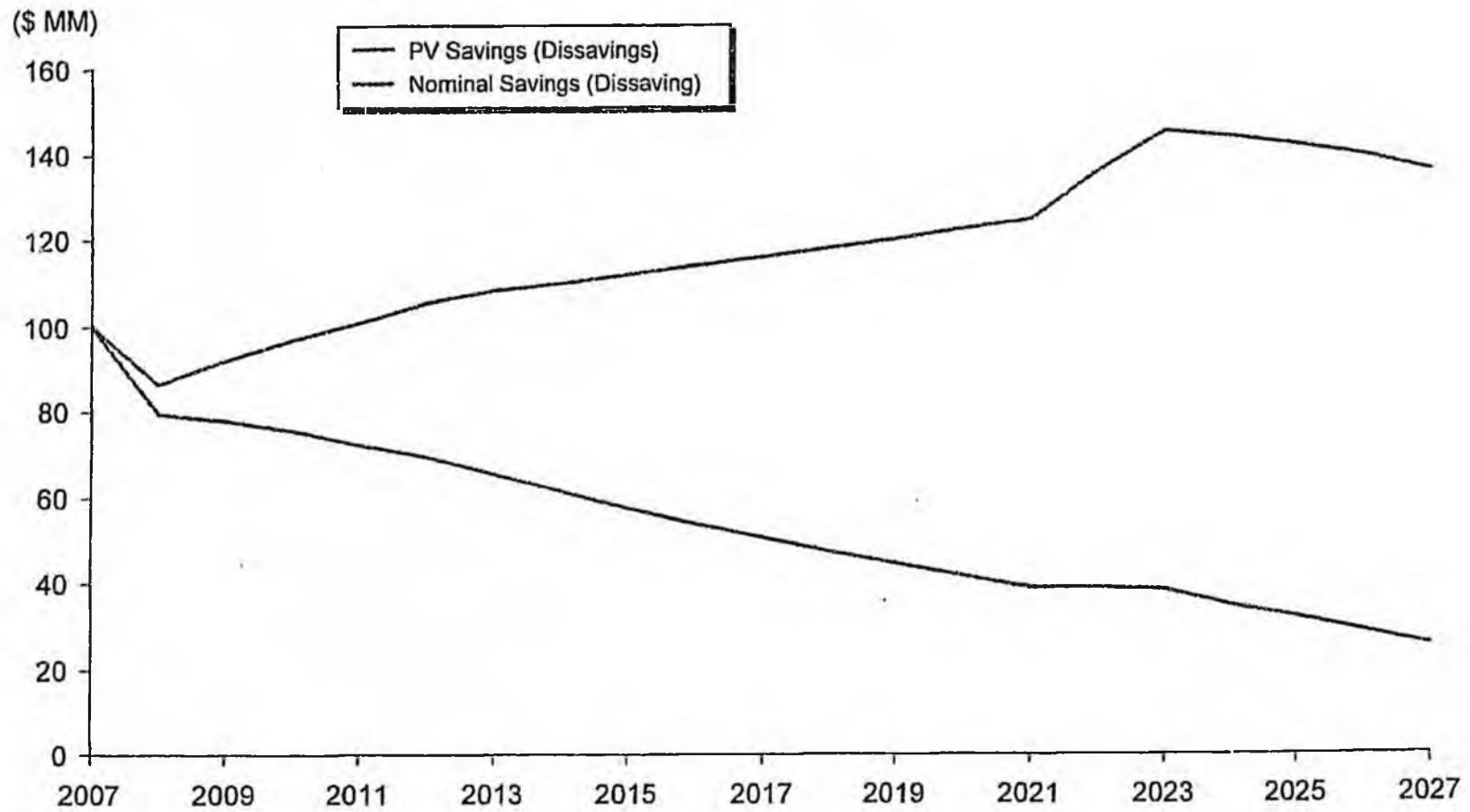
Taxable vs. Tax-Exempt—Private Ownership Gross Interest Cost



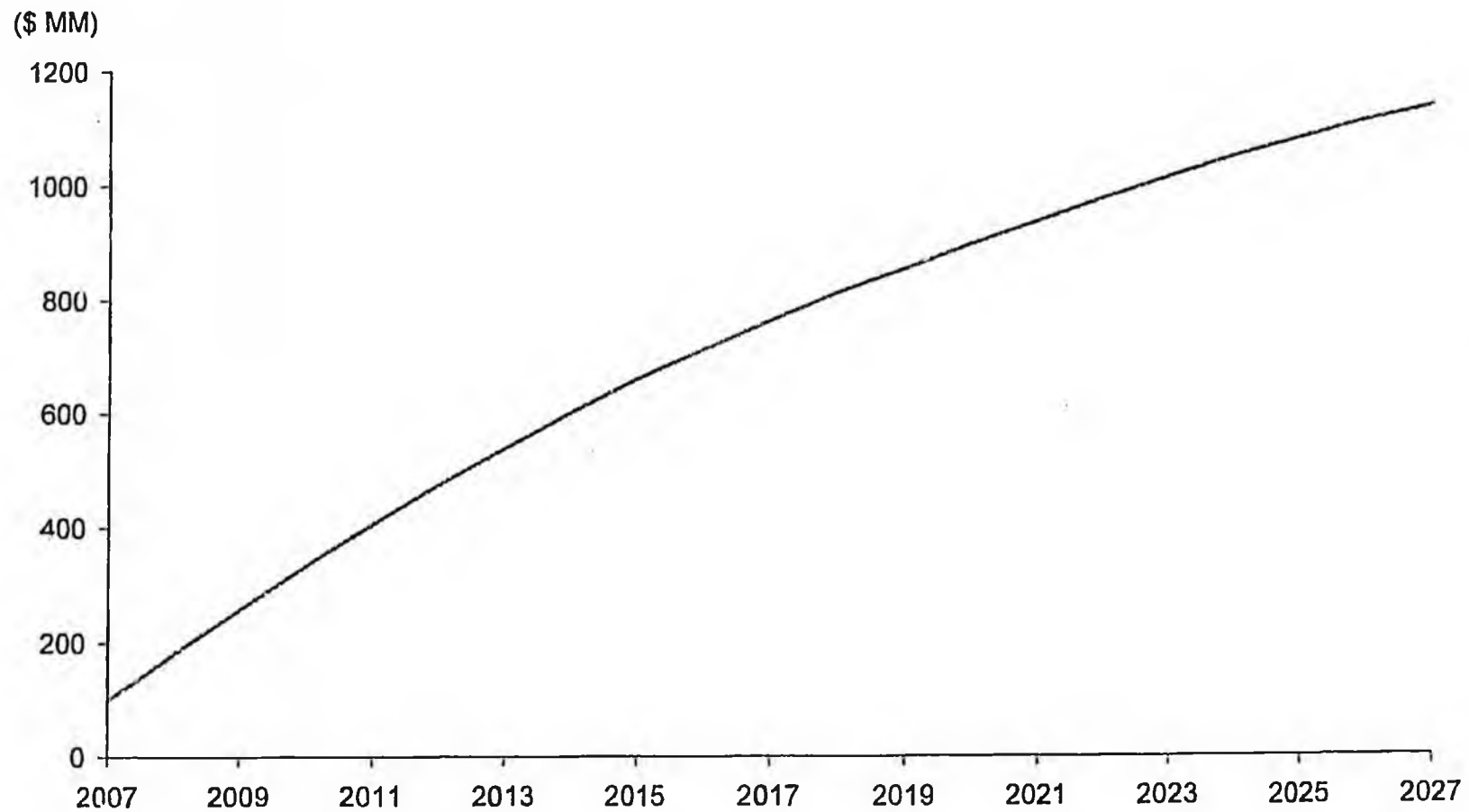
Taxable vs. Tax-Exempt—Private Ownership Tax Benefits to Producers or Pipeline Association with Lease Expense, Depreciation & Interest



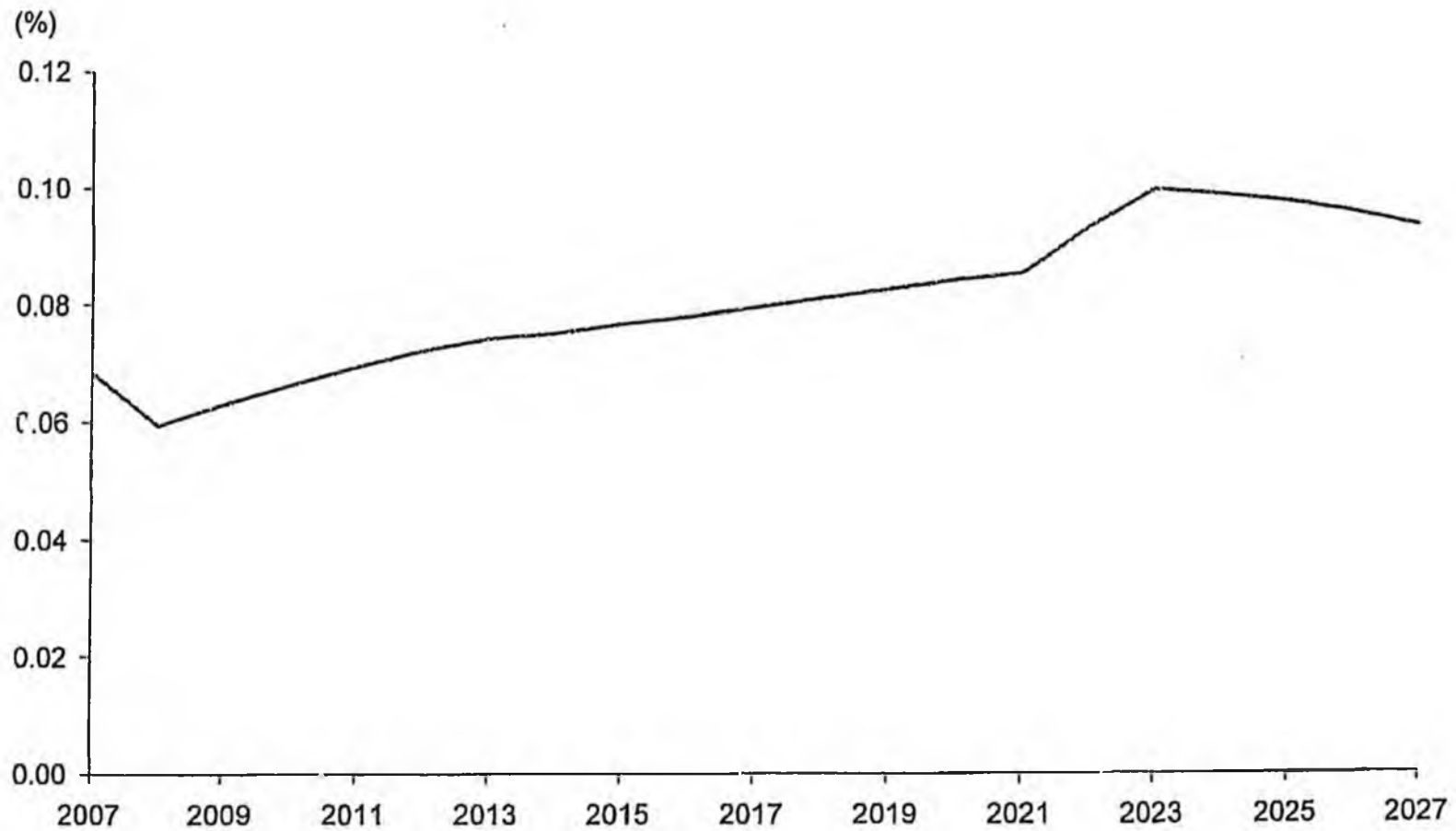
Taxable vs. Tax-Exempt Private Ownership Annual Present Value Savings From Using the Tax-Exempt Structure



Taxable vs. Tax-Exempt Private Ownership Cumulative Present Value Savings From Using the Tax-Exempt Structure



Taxable vs. Tax-Exempt—After-Tax Private Ownership Savings per MCF From Using the Tax-Exempt Structure



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2/6/2002 9:26

Tab 4
Assumptions

Assumptions

Financing Assumptions

- Dated/Delivered: 1/1/02
- Principal/Interest: January/July
- 30% Equity Contribution
- 41% Corporate Federal/State Tax Rate
- Multi Tranche Financing Over Construction
- 4-Year Level Construction Draw Schedule

Project Assumptions

- Total Project Cost: \$17 billion
- 4-Year Construction Schedule
- 1.46 Billion TCF/Yr (4 BCF/Day) into pipeline
- 10% line loss

Key Assumptions

Assumption	Rationale
6.5% tax-exempt cost of debt	100 bps above typical insured municipal revenue bonds today (allowing for size premium)
8.5% taxable cost of debt	Alliance Pipeline yielding 7.9% <ul style="list-style-type: none"> Alaska Pipeline bigger (+) Alaska Pipeline strong credits (-)
8.5% after tax WACC (weighted average cost of capital) for producers	External data <ul style="list-style-type: none"> Ibbotson Assoc. Large Petroleum Median WACC 8.78% Goldman Sachs research average WACC of BP/Exxon Mobil/Phillips 8.20%
Tax rate of 41%	Combined State/Federal marginal rate
Size of \$16 billion debt	Larger than, but comparable to <ul style="list-style-type: none"> MTA re-cap \$14.5 billion* LIPA municipalization \$9 billion Cal Power Bonds \$12-\$13 billion*

* Pending

HB

277

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**Testimony before the House Oil & Gas Committee
on H.B. 277**

**Richard A. Fineberg, P.O. Box 416, Ester, Alaska 99725
April 22, 2003**

Thank you for the opportunity to testify on H.B. 277. I believe this proposal to further emasculate the Regulatory Commission of Alaska (RCA) has enormous potential to do harm on two fronts. First, this bill strikes a sharp blow against the healthy competitive environment that is essential to continued oil development in this state by eviscerating the commission's authority to deal constructively with pipeline tariffs in a variety of significant ways. At the same time, this bill adversely affects the State Treasury by preventing the commission from promoting just and reasonable pipeline tariffs.

This is special interest legislation, pure and simple. The special interest is that of the three major owners of the Trans-Alaska Pipeline System (TAPS), who own more than 90 percent of TAPS and a similar percentage of the North Slope production that they ship through the pipeline they control. Over the last three decades I have observed the harmful economic and environmental effects of this unhealthy synergy from a variety of perspectives -- as a reporter during pipeline construction (1974-1978), as a senior advisor to the Governor on oil and gas policy (1987-1989) again as a reporter (1989-90) and as a consultant (1990 - present). Between June 2000 and May 2001, I served as the Staff Expert Witness for the Public Advocacy Section of the RCA in the first phase of its TAPS rate case, which I will discuss below. Based on this experience, I believe the RCA, its decision in the TAPS case and its continued efforts are the targets of the carefully aimed bullets fired by HB 277, to the detriment of the public interest.¹

Pipeline tariff issues require focused and careful analysis. That function is performed by the RCA under the Alaska Pipeline Act (AS 42.06). On November 27, 2002, the RCA issued a thorough and well-crafted order on Trans-Alaska Pipeline System (TAPS) tariffs.² That order authoritatively documents the enormous profitability

¹ My most recent assessment of the enormous profits the TAPS Owners realize from the tariffs filed under TSM -- along with a conservative reckoning of the separate benefits secured through the dismantling provision -- can be found in *The Emperor's New Horse: How Big Oil Gets Rich Gambling on Alaska's Environment* (Alaska Forum for Environmental Responsibility, June 2002), Chapter 5 (on line at www.alaskaforum.org).

² Regulatory Commission of Alaska, *Order Rejecting 1997, 1998, 1999 and 2000 Filled TAPS Rates; Setting Just and Reasonable Rates; Requiring Refunds and Billings; and Outlining Phase II Issues*, Docket P-97-4, Order #151 Nov. 27, 2002 (on-line at www.state.ak.us/rca). The order held that TAPS tariffs between 1997 and 2000 were 57% above the "just and reasonable" levels mandated by AS 42.06 and that between 1977 and 1996 the same tariff methodology, applied linowide, resulted in tariffs that exceeded just and reasonable levels by \$9.9 billion. Although the 1977-96 tariffs were not at issue in the RCA hearing, historical tariffs had to be calculated to determine the correct tariffs for the years at issue. These central conclusions have two significant effects:

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of TAPS under the 1985 TAPS Settlement Methodology (TSM). I think it is fair to characterize this order as historical in its significance. Three indications of this order's importance to the state are:

→ (1) The statement of the Department of Natural Resources Division of Oil and Gas that "[e]xcessive tariffs create barrier to entry for all oil and gas companies not owning an interest in TAPS;"³

→ (2) The listing of lower TAPS tariffs by 17 key industry participants and observers as the top priority for 2003 (with streamlined permitting) and "one of the most important incentives the state could offer;"⁴ and

→ (3) The Alaska Permanent Fund Board of Trustees decision to investigate "all maintenance and operational practices, including tariff and facility pricing," that could limit development of state oil leases.⁵ Each of these statements referenced RCA's November 27, 2002 order.

The Department of Natural Resources has estimated that reduced tariffs on TAPS – if applied line-wide – would increase state revenues by \$110 million per year. At present, the TAPS Owners are pocketing that excessive revenue.⁶ Although RCA tariffs govern only eight percent of oil shipped through TAPS (the portion going to in-state refineries), the RCA order indirectly calls into question the interstate tariffs governed by the Federal Energy Regulatory Commission (FERC) for two reasons: (1) FERC approved a virtually identical, ad hoc formula settlement in 1985; and (2) as the RCA put it, the commission order marks "the first time in more than 20 years of TAPS operations that a regulatory agency has reviewed TAPS rates for consistency with statutory standards."⁷ Clearly, the RCA decision – 168 pages in length, with approximately 300 pages of endnotes and worksheets – renders the 1985 settlement more vulnerable to challenge at FERC. Perhaps this is one reason the TAPS Owners have filed every

(1) Because transportation charges are subtracted from the market price to determine the basis for assessing royalty and severance taxes, the state loses approximately \$0.21 to \$0.23 for every dollar increase in the TAPS tariff (and vice-versa). By this reckoning, between 1977 and 1996 the overcharges allowed under the TAPS settlement methodology (TSM) cost the state \$2.1 to \$2.5 billion in revenue.

(2) Because an independent shipper pays TAPS tariffs out of pocket while a producer-shipper pays an affiliated company, excessive tariffs (plus the allowable profit on all charges) amount to a transfer payment rather than an out-of-pocket cost; benefits to TAPS owners are further compounded by tax treatment.

³ Alaska Division of Oil and Gas, "Gas Line: Examples of the Cost of 'Fiscal Certainty'," Dec. 9, 2002 (briefing slide).

⁴ "'Good news' wanted in 2003," *Petroleum News Alaska*, Jan. 19, 2003, p. 1.

⁵ Sean Cockerham, "Oil lease probe sought – Permanent Fund: Corporation worries smaller companies are shut out, state is being shortchanged," *Anchorage Daily News*, Feb. 20, 2003 (on-line).

⁶ Allen Baker, "State weighs pipeline fees – \$110 Million: If rates are cut, Alaskans, small producers benefit," *Anchorage Daily News*, Dec. 31, 2002, p. A-1.

⁷ Regulatory Commission of Alaska, "The Regulatory Commission of Alaska Rejects Rates for the 1997-2000 Intrastate Trans-Alaska Pipeline System, Sets Just and Reasonable Rates, and Requires Refunds and Filings by Carriers," Nov. 27, 2002 (press release; on-line).

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imaginable legal challenge to the initial decision – both at the RCA and in court – in an effort to preserve their ill-gotten gains. Not surprisingly, their lobbyists have now shown up on your doorstep.

By way of background, it should be noted that the TSM was negotiated between the state, represented by the Department of Law, and the TAPS Owners.⁸ In the years since the settlement, the Department of Law has steadfastly defended the settlement, relying on the agreement's "duty to defend" clause⁹ to argue on behalf of the gains to the TAPS Owners conferred by defects in the complicated methodology and post-settlement changes in conditions.

The direct benefits of identifying and reducing excessive TAPS tariffs are quantified and defended in the RCA decision. But that decision also deferred – and served notice that the commission intends to deal with – another matter of enormous public concern and special interest to the TAPS Owners: The tariff provisions governing TAPS dismantling, removal and restoration (DR&R) were reserved for a "Phase II" proceeding. Recently, the RCA determined that the commission had broad jurisdiction over DR&R under state law, and that it would continue the proceeding to hear that issue.¹⁰ The industry's accelerated or front-loaded collection and retention of approximately \$1.6 billion in funds for the future dismantling of the pipeline is an undeserved windfall to the TAPS Owners of enormous proportions. The 1985 settlement delivered this windfall to the TAPS Owners at shipper and public expense. The financial benefits to the TAPS Owners and the policy consequences for the state were first quantified in 1986 by the Staff Expert Witness for the Alaska Public Utilities Commission, predecessor to the RCA.¹¹ Since then, DR&R problems have come to public attention at least four times; in every instance, the state administration has failed to remedy the problem, thereby continuing to penalize the state treasury and place the environment at potential risk.¹²

While the DR&R provision has major implications for public policy, a relatively minor aspect of the TAPS DR&R terms may provide the best illustration of the complicated nature of pipeline tariff issues – and the potential for TAPS owners to profit from that complexity at state expense. TSM allows the TAPS owners to collect from

⁸ *Settlement Agreement between The State of Alaska and ARCO Pipe Line Co., BP Pipelines Inc., Exxon Pipeline Co., Mobil Alaska Pipeline Co., Union Alaska Pipeline Co. with Respect to the Trans Alaska Pipeline System*, June 28, 1985 (Federal Energy Regulatory Commission Docket OR 78-1), p. 1.

⁹ *Settlement*, Section I-3.

¹⁰ Regulatory Commission of Alaska, *Order Denying Indicated TAPS Carriers' Motion to Cancel Prehearing Conference and Ruling on DR&R Question*, Docket P-97-4, Order #157, March 6, 2003 (on-line at www.state.ak.us/rca).

¹¹ *Prefiled Testimony of Rudolph L. Bertsch* (Alaska Public Utilities Commission Docket No. P-86-2), December 17, 1986, pp. 63-70.

¹² For a summary of DR&R issues in the context of the TAPS tariff, see Richard A. Finberg, *The Emperor's New Hose: How Big Oil Gets Rich Gambling with Alaska's Environment* (Alaska Forum for Environmental Responsibility, June 2002, Chapter 5 (on-line at www.alaskaforum.org)).

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shippers an income tax surcharge on all DR&R payments as part of the tariff. But instead of actually making those payments to the Internal Revenue Service (IRS), it is a matter of public record that the pipeline owners obtained a special ruling allowing annual deductions on DR&R income -- long before that money is actually spent on dismantling. For the TAPS owner shipping its own oil, the unnecessary income tax collection is simply a transfer to from the company's production arm to its transportation subsidiary. But that phantom transportation cost penalizes non-owner shippers and reduces the production arm's royalty and severance tax basis, saving the company -- and costing the state -- an estimated \$0.21 to \$0.25 per dollar.¹³ Two final notes on this subject: (1) In 2000 your colleagues tried -- without success -- to find out how much the state has lost over the years as a result of this scam.¹⁴ (2) As mentioned above, this is only one of the several defects in the DR&R component of TSM -- and by no means the most important.

The immediate, short-term fiscal consequences of the TAPS DR&R loophole described in the preceding paragraph are small compared to the long-term policy implications. One of the most egregious parts of HB 277 is the proposed statutory requirement that RCA support of rate methodologies agreed to in settlement agreements with the State. Over the years, the RCA and its predecessors have supported the use of a standard utility rate-making methodology for pipelines to ensure just and reasonable tariffs that promote robust competition. In my estimation, it would be an act of short-sighted blindness to overturn this important precedent. Note in this regard that TSM which HB 277 seeks to defend, is a complicated, hybrid methodology. Although you can make a case for negotiating complicated departures from standard methodology, from a policy standpoint there is much to be said for the clarity of a straight-forward approach. The income tax example discussed in the preceding paragraph provides an illustration of why hybrid settlements are so difficult to apprehend and track; the RCA's order on TAPS demonstrates the enormous fiscal implications of this particular hybrid settlement concoction.

As mentioned above, I participated in the RCA hearing on TAPS on which the commission's November 2002 TAPS order was based. For five weeks, the commissioners, the attorneys for the shippers and the commission's Public Advocacy Section spent much of their time trying to penetrate the smoke screen erected by the industry, with the state's help, in defense of its hybrid methodology. Had the fiscal and public policy consequences not been so great, this magic lantern show would have been hilarious.

In conclusion I would note that Executive Order 111 has already begun to dilute commission authority by weakening the link between the public and the RCA. The executive order states that the purpose is to assure "efficient administration" by avoiding "possible duplication of effort or the taking of inconsistent positions by separate agencies

¹³ Richard A. Finberg. "New filings reveal oil pipeline owners' tax scam." *Anchorage Daily News*, Feb. 8, 2000, p. B-8.

¹⁴ See: Alaska State House Oil and Gas Committee hearing, April 13, 2001 and letter from Michael A. Barnhill, Assistant Attorney General, to Rep. Jim Whitaker, May 23, 2000.

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of state government."¹⁵ Our government depends on checks and balances; when did consistency with other state policies become the purposes of a quasi-judicial regulatory agency? I am also concerned that the transfer of the Public Advocacy Section to the Attorney General's Office further separates that unit from the public it was created to represent. The importance of public involvement in the regulatory process was brought home last month, when FERC finally issued its report on energy price gouging California – two years after the crisis, long after Enron's collapse and only after insistent prodding from Congress and the General Accounting Office.¹⁶

The fiscal and broader policy issues served by the RCA's efforts are summarized in the a January 3, 2003 *Anchorage Daily News* "compass" by Walter B. Parker, which I am submitting with this testimony. Historically, almost everybody who has looked seriously and independently at this complicated issue has concluded that the 1985 TAPS tariff settlement undermines competition by ratifying exorbitant tariffs that do not satisfy the statutory requirements of just and reasonable tariffs. I do not argue that the commission or its Public Advocacy Section are models of efficiency. That's not the point. In the case of pipeline tariffs, the RCA has done a masterful job of protecting the public interest in an area of great importance to Alaska's continued development. To the extent that the RCA's ability to function as an independent regulator is emasculated, the agency will not be able to implement that order or do justice to any tariff issue – including DR&R. For these reasons, I am particularly troubled by measures such as HB 277 that dilute the authority of the commission, whose links to the public it represents have already been weakened by Executive Order 111.

Thank you for your kind attention.

¹⁵ Executive Order No. 111, March 5, 2003.

¹⁶ See: Edward Iwata, "Panel: FERC dropped ball on Enron," *USA Today*, Nov. 11, 2002 (on-line) and Mark Sherman (Associated Press), "FERC Finds Widespread Power Manipulation in California," *Washington Post*, March 26, 2003 (on-line).

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Attachment 1.

Author's Sectional Analysis of H.B. 277 (23-LS0280AD):

Section 1 amends a key enabling section of the Alaska Pipeline Act, which enumerates the duties of the commission regarding pipelines, to curtail the authority of the state pipeline commission to regulate the abandonment of pipeline facilities. This section also removes from the commission the authority to investigate performance and compliance with lease terms (*AS 42.06.140(a)*).

Section 2 creates a new subsection that specifically denies the commission jurisdiction over dismantlement, removal and restoration of any part of a pipeline facility (*AS 42.06.250(c)*).

Section 3 further curtails the commission's authority in the complex arena where state and federal jurisdictions overlap. Where the framers of the Alaska Pipeline Act sought to ensure that the state commission would have broad powers to investigate pipeline tariff issues "except to the extent they are preempted by federal law," this legislation would deny the commission authority to "consider revenue collected on interstate transportation when evaluating intrastate rates or tariffs" (*AS 42.06.245*).

Section 4 further limits commission authority regarding abandonment by specifying that the required commission finding, prior to abandonment, that continued service is not required by public convenience and necessity applies only to service and not to "any portion of a pipeline" (*AS 42.06.290(a)*).

Section 5 establishes a new subsection saying that any pipeline settlement with the state is considered to be in the public interest and conclusively just, reasonable and nondiscriminatory and therefore beyond the purview of the commission unless the state brings a protest or petition that a particular rate does not conform to the settlement terms (*AS 42.06.370(d)*).

Section 6 changes the interest rates on refund payments so that the rates under AS 9.30.070(a) replace the rates under AS 45.45.010(a) (*AS 42.06.400(b)*).

Section 7 specifies that any commission orders regarding rates must be limited to future tariffs and may not be retroactive (*AS 42.0.410(a)*).

Sections 8 through 11 ensure that this act applies to any matters pending before the Regulatory Commission of Alaska on the effective date, that the refund provisions of Section 6 are retroactive to August 7, 1997 and that Section 5 is contingent on Executive Order 111 taking effect.

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Attachment 1.

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"Lower pipeline tariffs deserve look"**By Walter B. Parker****"Compass"*****Anchorage Daily News, January 3, p. B-4***

Alaskans pay a high price today for a bad deal the Alaska Department of Law struck with the owners of the Trans-Alaska Pipeline System (TAPS) in 1985. That is the clear and unmistakable message of the monumental order on TAPS tariffs issued by the Regulatory Commission of Alaska (RCA) Nov. 27.

According to that decision, in recent years the 1985 TAPS Settlement Agreement has resulted in average TAPS tariffs that were 57% too high. Perhaps even more significantly, the Commission calculated that the 1985 agreement enabled TAPS owners to charge \$9.9 billion over just and reasonable costs between 1977 and 1996.

As a general rule, lower TAPS tariffs mean higher state revenues. If the RCA tariffs governed, the state would have at least \$2.5 billion more for schools, roads and other public purposes.

Unfortunately, the RCA order sets TAPS tariffs only for in-state oil shipped between 1997 and 2000; earlier years were not on the table and Federal Energy Regulatory Commission (FERC) governs rates for more than 90% of TAPS oil.

Other factors complicate the situation. The 1985 settlement allows TAPS owners to offset reductions in intra-state tariffs by increasing inter-state rates. Moreover, separate contractual agreements and regulations use the inter-state rate to calculate royalty and severance on the intra-state oil shipments.

According to the RCA, these factors could result in short-term state revenue losses of less than \$10 million per year. But to take that revenue from the state, the TAPS owners would have to petition FERC to increase the same tariffs that RCA found unjust and unreasonable in a 486-page decision that RCA calls "the first time in more

*"Lower pipeline tariffs deserve look," Anchorage Daily News ("Compass")
January 3, 2003 (Page 2)*

than twenty years . . . that a regulatory agency has reviewed TAPS rates for consistency and statutory standards."

Uncertainty about small, short-term revenue effects should not obscure the following fundamental and long-term public policy truths:

- Lower pipeline tariffs encourage development by reducing total transportation costs;
- Lower pipeline tariffs increase state revenues because transportation costs are subtracted from the price of a barrel of oil before royalty and severance taxes are calculated.

In view of these important considerations, the context of the RCA case deserves further consideration. Historically, the commission and its predecessors favored the widely accepted depreciated operating cost methodology permitting pipeline operators to charge tariffs sufficient to cover repayment of investment, operating costs, taxes and a fair rate of return on investment. Instead of following this standard to determine TAPS tariffs, in 1985 state lawyers agreed to an unconventional TAPS methodology in an effort to end eight years of litigation. The RCA approved the settlement provisionally but left the door open for future protests.

In 1997 Tesoro, then refining oil shipped through TAPS, filed a tariff protest later joined by Williams Alaska, which operates the North Pole refinery, and the RCA Public Advocacy Section. All three parties argued that excessive TAPS tariffs violated the terms of the Alaska Pipeline Act, whose purpose is to insure access to common-carrier pipelines at just and reasonable rates

To deal with legal maneuvering and intense wrangling over document production covering a complicated history, the RCA issued more than 100 procedural orders, listened to five weeks of testimony, reviewed expert reports and sifted through the voluminous record before calculating appropriate tariffs.

The RCA was clearly unimpressed with the defense of the settlement rates presented by the TAPS owners and the state. Rejecting the case presented by the TAPS owners and the state, the commission ordered the TAPS owners to reduce in-state tariffs

*"Lower pipeline tariffs deserve look," Anchorage Daily News ("Compass")
January 3, 2003 (Page 3)*

for 1997-2000 by an average of approximately \$1.00 per barrel. Presumably, orders reducing 2001 and 2002 in-state TAPS rates will follow.

Don't expect the TAPS owners, who have spent nearly \$15 million on this case, to give up their ill-gotten gains without a fight; court appeals are likely.

Looking forward, just and reasonable TAPS tariffs will have a far more salutary effect on state revenue and future oil development than almost anything else the state might do. The RCA decision presents the state with a unique opportunity to correct its previous, misguided course.

Walter B. Parker of Anchorage has been active in state transportation and resource development issues for 56 years. He has served as Commissioner of Highways, Director of Technical Staff for the State Pipeline Coordinators Office and Chair of the Alaska Oil Spill Commission, among other things.