

ALASKA LEGISLATURE COMMITTEE FILES - 2007-2008 - HRLS 12304

Disincentives for producers to build a gasline, so incentive to become an equity owner.

Galvin – ACES special session include DPR rather than accepting the tariff rate charge by shipper to look beyond that when no arms length involvement what was paid to establish fair market value. State courts and state agencies have established what they think is a fair rate and it is far less than the pipeline owner is charging.

Dickinson is saying the producers wouldn't participate because of the formula not using tariff rate for tax purposes. 43.55.150(a)

## Day 5 4<sup>th</sup> SPECIAL SESSION

Ramras 130 bcf a year consumption in Fairbanks. Ramras doesn't agree with Irwin's math of consumption of natural gas and is concerned about the issue before us right now. What is the smallest project we can do so we can move today?

Ramras does not hear a can do attitude about getting natural gas to Anchorage. Railbelt communities, Flint Hills, Agrium. Ramras hears natural gas to Alaskans after the Canadian line is built using \$500 million of our money.

per day .5 X 365 Irwin said they have the same math .5 bcf

Enstar met with Therriault the other day to talk about the bullet line and they said they need nothing from Alaska at this point. Would the state be willing to help pay down the debt on a bullet to keep the cost of natural gas affordable to Alaskans.

Galvin said yes it is something the state is considering but it needs to be based on facts and truths instead of unknowns and false assumptions. WE have a can do attitude and AGIA allows the discussion to occur and eliminates the bumper sticker solutions that have long term problems. Subsidies affect our taxes, oil revenues, and PFD's and we need to know which gives us the state as a whole the most.

The immediate to get gas to Alaskans has no conflict with AGIA. We can serve Alaskan market separately.

Spur lines off the main line are not in competition with the AGIA for a long term solution of Alaska's energy needs.

Galvin: Whether AGIA is going to preclude short term issues. Answer is no

Doogan: When does license end? When gasline is completed.

A year ago when legislature discussed AGIA Tony Palmer testified six times about where TransCanada would go after the open season that failed; he stated you could increase your contributions when going for a second open season to continue the course for certification. That didn't increase the limit it increased the contribution rate. Huggins said amendment was offered by the administration. Galvin said there was ample testimony about the concern to carry on after a failed open house. Galvin didn't check but thinks it could have been the administration's amendment in response from concerns voiced by TransCanada. He knows MidAmerica and Port Authority testified but don't recall if they testified about the contribution rate.

Transfer employees from their regular positions to a different location temporarily – second

Palmer said the reason they got a row through Yukon Territory twenty five years ago because the process and politics in Yukon was much more difficult and time consuming than Alberta and British Columbia so ROW in Yukon Territory was sought early.

Eight First Nations in Yukon; while we have the ROW, there are specific terms and conditions that lay out the benefits spelled out in a law passed 30 years ago. They will negotiate with individual First Nations groups. Dahlstrom if you are not able to negotiate with even one group would this allow them to sue over the gasline and put it to a stop.

Canadian section does not qualify for the rolled-in tolls up to 115%.

The MUST HAVE for two year open seasons was an easy on for TransCanada because it is good business practice. Other contracts don't have that requirement.

If you put a line in place and are successful you are looking future potential tcf's. Prudhoe estimates 24 tcf proven reserve; in Canada one line is being built with only 6 tcf proven basin.

Black Veatch analysis on potential expansion.

Wouldn't a user owned pipeline want to look for other gas shippers; not until you get to a 45% capacity level in the gasline. Do we want a pipeline that just encourages the big three to explore or one that solicit all explorers who want to move natural gas.

ANGSDA 2004 passed

Existing shippers cannot subsidize expanding shippers.

Carbon credits for lowering emissions.

Ramras – the notion that the states seed money is going to change the mind of gas producers to provide natural gas to this project is a “fool's errand”.

Galvin – producers have not expressed absolute rejection of providing natural gas. They have expressed desire to change fiscal certainty and some provisions of AGIA. It is a challenge to get the project gas but experts say there is a high likelihood the project will succeed.

Palmer said his company is not in the practice of spending \$100 million on a project knowing it is going to failed.

2:10 p.m. Fred Dyson – considers his colleague from Fairbanks' remarks out of line and a cheap shot. Has a letter from Exxon on his desk with interest in selling natural gas. Very few pipelines are built by producers in North America; most are built by an independent firm to transport gas for producers.

Doogan unique situation we are not divided in the house we are in. Not under rules normally under. Would like some instruction as to proportion of questioning and political posturing from the chair.

Huggin – everybody desires a chance to ask a question, give an answer and give an opinion.

Neuman- there is nothing to compare TransCanada's proposal to.

Gara – lower in not no tax for instate gas usage for a bullet line. Galvin - ACES legislation there was a global change to the taxing North Slope gas consumed in the state. The question of providing affordable gas to the state. If the state built the gasline we would be providing low cost transportation for the gas, but ultimately the gas price will be driven by the market.

Stedman – Palmer expressed \$100 million as comfort zone for expending for open season. Is there any connection between the 50/50 90/10 80/20 split and the probability success of the project. The incentive may have changed the probability of success of AGIA because there may have been no applications.

Gatto – knowing you're not a charity case; you must have done a lot of research before deciding to apply for AGIA. He is very hopeful TC has done their homework. He believes TC can do it and help Alaska pay their bills.

Samuels – need to continue to ratchet down on TC until they squeal then ratchet back one notch. Because we got one application we didn't get the competition we were promised. How are we going to get a better deal than what TC has offered being we didn't get the competition we thought we were going to get in AGIA.

Irwin - Fair, open predictive process. We could have asked for bidders and not get a fair best deal; We chose to very clearly define what we wanted and chose the best and final offer by date certain.

Got AGIA passed by legislature and then let the RFA reflecting what is in AGIA. I saw equity investment we might not have gotten in open bidding process.

Galvin – TransCanada didn't know who else was going to submit an AGIA application. They submitted the best offer they could come up with. We are here today with the best offer we got.

Kelly – how many real players did Palmer think was in the dog fight with AGIA.

Howliskowski and Ken Bird paper 2006

NPRA 2004 estimate oil numbers are on high side and gas numbers on the low side.

Alpine Play was Alpine field gas oil ratio 840

Arctic Alaska is grossly under explored:

>35 tcf proved reserves

119 tcf onshore & state waters

108 tcf federal offshore

Howliskowski said cost of production very close to those estimates of TransCanada.

Gt – what I see from Denali is a lot of wonderful ads.

Hawker – has heard Denali is a fraud a political ploy to delay to fool the public: Fackrell – not true 75 people in the field; spend \$40 million this year; 9 vice-presidents; in a few months will have up and running company. Major goal right now is to have a successful open season that will commence in 2010. They will have milestones that you can watch and determine if we are reaching them or not.

Stedman – if this was a sham what recourse would the parent companies have for misleading shareholders and public. What are federal repercussions if you are running a flim flam operation.

Fackrell - On July 22 will accompany FERC chairman to North Slope. Very common for producer to welcome government officials to visit North Slope operations to see what it is like and get a feel for it. The first segment of project is the largest gas treatment plant in the world. This plant will be larger than the 1977 and 1986 plants built on the North Slope combined.

Lynn - AGIA had some twenty must haves. Why didn't you apply under AGIA and which ones of the must haves were not acceptable to you. Ownership issue not pipeline issue. They told him under the terms of AGIA the project was not viable.

Wiel – the difference between Denali and AGIA is AGIA has penalties and consequences for not building a line with must haves.

Fackrell – we are spending \$600 million this year.

Joule – 30 years of a monopoly with producers. Open access

Fackrell “Our pipeline is an open access pipeline” reiterate “This is an open access pipeline.”

“All parties have a right to nominate gas for the gasline.” “Every two years Denali will solicit interest in expansion of the pipeline.”

Gara – FERC says we get rolling rates for voluntary expansion. For mandatory rates you can charge incremental rates. Will Denali commit to same schedule of voluntary expansion rolling rates for mandatory expansions.

Gara – can you guarantee AGIA terms for pipeline expansion

Fairclough – we're afraid of the lack of access to TAPS vs TransCanada's expansion from three customers to three hundred customers. Best of both worlds for many legislators is Denali and TransCanada. TransCanada said under AGIA they can't partner with Denali.

Fackrell – owners have said they are open to taking in partners for the gas pipeline.

Fairclough - What language in AGIA prevents a partnership?

Coghill – convinced of credibility of TransCanada to build a pipeline and the permits they hold on the Canadian side are very real. We are at the eve of voting on a license that could restrict a partnership. Have you had talks with TransCanada about partnership. Fackrell – you will have to ask the producers. Coghill – timing is an issue to know.

Coghill – Is it okay to assume there is 4 bcf available for a pipeline since you are working with is there a study underway that shows there is 4 bcf available to transport to market. Fackrell committed to have open season end of 2010.

Hoffman – construction plan. Have you come to any terms with the Canadian government to be sure the project you have planned will eventually be built. Is debt equity ratio favorable to Alaska? Fackrell – not committing to debt equity ratio in AGIA. Will negotiate with financial market. Does not have any agreements with Canada. Hoffman – have you had preliminary conversations with TransCanada about using permits in Canada? Fackrell has not had conversation with TC but producers may have.

Crawford – 1. Denali plans to solicit – why not Denali will solicit  
2. Read Denali intends to use 5 million tons of steel – TC is using 2.25 to 2.5 million tons of steel  
3. Under AGIA commitment to negotiate PLA.

Bundy – Will approval of TransCanada harm Denali? Fackrell – no matter what legislature decides Denali will still move forward. Do have a couple of concerns. 1. all for competition but the playing field needs to be level. Denali needs approval of permits in state. If Denali's permit process is slowed down not fair. 1. Fiscal certainty may be a problem with TC holding the license.

Seaton – estimate \$600 million to be spent for successful open season. How much spent in Canada? Don't know. How did we come up with this estimate? Have experience in field work in Alaska and experience in open seasons.

Seaton – unincorporated joint venture in Canada and corporate partnership in Alaska. Why difference? Fackrell – dealing with two countries with different laws. Canada has different process than U.S.

Seaton – is Denali going to commit that if there is nominated gas after two years and in reasonable increment Denali will commit to voluntary expansion instead of FERC mandatory process? Fackrell – out process today is to solicit and if demand is there expansion will happen. Is that a decision of the pipeline company or owners? Fackrell – in the end I have to make capital investment so I will have to evaluate it and take recommendation to owners.

Wiel – are you willing to commit to solicit open season within two years? Yes  
Are you willing to have time certain commitment for construction? Already have  
Are you willing to commit to cost overrun protection? Very committed to  
avoiding cost overruns.

Gatto – Denali had the choice to compete for the gold medal.

Protecting Alaska's interest:

Time certain open season

Date certain FERC application

Open season

Commitment to expansion

Fackrell – personally thinks if you vote for AGIA you are voting to keep producers out of the pipeline and are hurting the chances of the pipeline being constructed.

Roses said TC will spend \$84 million for open season and Denali \$600 million. Question not really answered.

Thomas – Fackrell role managing large, complex operations around the world. Off shore projects construction, pipelines.

Fackrell – looking at five take off points

Samuels – spent \$600 million in 36 months for open season

TC \$84 million to open season and \$611 million to FERC

How much will Denali spend to get to FERC? \$2 to \$3 billion to get to FERC license approval

French - if Fackrell tells us Denali will proceed even if license is issued to TC tells French Denali thinks State will pay treble damages.

Guttenberg – will Denali build gas facility in Prudhoe Bay? If open access starts downstream from the GTP there is a problem with open access? Fackrell says yes GTP will be built by Denali. Will have vp for pipeline from NS to Canada vp from Canada to Lower 48, vp for GTP

Guttenberg – intake outtake provisions – Fackrell we want customers and we want to fill the pipeline so open access.

Guttenberg – gas liquids interested in taking them off instate if economical. Are producers more interested in taking it to the end of the line. Fackrell 25 psi will not be stripping off hydrocarbon liquids at GTP. If you get to Yukon River could strip propane and reinject others in pipeline at any point along the line.

Hawker – 1<sup>st</sup> benchmark point – Palmer says they have exclusive rights of pipeline activity in Canada. Fackrell – Denali has subsidiary companies in Canada; do not believe BP and Conoco are shut off in Canada.

Hawker – do you anticipate working with TC or legal action to challenge TC's exclusive claims.

Fackrell – above ground Yukon River and seismic active locations.

Have 75 people in field this summer. Didn't want to lose summer.

Denali is up and running; regardless of decision here, Denali will move forward. Need to make customers aware of the cost. Don't want to be a bride waiting at the altar and nobody shows.

Doogan – how do you arrive at capacity of pipeline? Fackree – estimates of what is available in the state. Do you have to go to owners to get permission to expand. Solicit customers every two years, review the solicitations, and give recommendations to owners. Doogan said there has never been a voluntary expansion to a pipeline. Fackrell doesn't have information to answer that.

Stedman - State is going to be spending hundreds of millions of dollars for infrastructure improvements. Denali showed Haines port as an example. How does timeline work in so the state doesn't spend \$100 millions for infrastructure and have Denali or TC back out of construction of gasline.

Stedman – where is point of no return? Fackrell – after successful open season have confidence to get financing for construction.

Fackrell people ask can't you get it done sooner? Have to pre order steel; that won't happen until successful open season.

Gardner – would like a list of all elements of fiscal certainty.

Why we are here today

Negotiated stranded gas at \$3.50 high prices estimated 4 to 5 bucks

Economists of world usually 6 to 9 months behind.

Push pull going on during the lean years; the economics weren't there for producers to drill additional wells.

In the lower forty-eight a certified well is usually brought on line; in Alaska it could be six to eight years because as a practical matter if something is wrong with the well it takes another season to get to the well.

With everything single lease in default; there was an exception 7 certified wells that made it so the leases were not in default.

Gara – interested in the Supreme Court decision and what is recommendations of Porter? You don't mediate successfully unless both parties agree to it.

Therriault – state can't dictate what you do with lease; Porter – not so; if you reject a POD you have a right to make a proposal the producer follows.

Pt Thomson out of the equation and not available for first gas – 1 mcf a day

Goes from 4.5 to

4 mcf

3.5 mcf at the economic limit of moving forward

Not having Pt Thomson in the project the change is in economics and tariff from 50 cents to \$1 in tariffs.

Steve thinks DNR thought they couldn't talk to Exxon during this phase of the procedure. Thinks DNR and Exxon want to solve it. At this stage they should be able to sit down and talk about what the state wants.

Hopes DNR works with Exxon; he fears if we fight this battle DNR loses to Exxon because the State has not given Exxon a remedy.

Round table discussion

Continental Energy Systems Parent Enstar  
Harold Heinz  
Bill Walker  
Pat Galvin  
Radoslav Shipkoff

Galvin – ANGDA, Enstar, state working together to put together a structure to build a instate gasline

If gas is not discovered in Cook Inlet line will continue north to North Slope  
Eventually hook into main line for gas movement either direction

With announcement it is the beginning of the partnership; details need to be worked out and brought to public in the next few months;

Details of legislature January 2009

Price of gas has changed so dramatically that players are now interested

SCR 22 - Get Alaskan gas to Alaskans as soon as possible  
Timing right to get Cook Inlet exploration going again as soon as possible

460 mcf is what Enstar come up with as gasline moves south – Cook Inlet north may not be that amount.

Hawker-seems a deal was cut already and want to know how long state has been talking to Enstar and ANGDA.

Discussions have been going on quite awhile; discussions jointly just recently.  
Come to legislature with a clear role of the state and bind the state for that role  
Will come to legislature later to say what we want

It was a bit of a shotgun wedding; we were both drunk together a little bit last week.  
ANGDA comment

Heinz was contacted two Monday's ago; ANGDA and ENstar me the next Wednesday.

Dubay tried consistently to keep administration informed of ENSTAR project for quite a while and with the legislature

Huggins – two routs the Parks Hwy and Glenallen route. Dubay and ENSTAR has been working along Parks Highway route this summer.

Heinz wrote a two page letter to Enstar to see if there were ways to work together. A week ago starting talking about a business structure not just a project;

Heinz – governor has not asked either company to stop doing what they are doing. ANGDA doing wetlands assessment this summer.

Huggins – what impediments exist for Enstar to deliver gas to Alaskans. DUBay working on design from Foothills to Fairbanks.

Chenault – should be the happiest guy in this room – agrium plant employed 300 people through the years. Seems like we have a lot of natural gas we didn't know we had.

If the price of gas is too high and Agrium can't compete against the world market—catch 22 more talk needed;

Heinz – will cover ROW, permitting, designing, surveying (\$25 million) is a continuation of what ANGSDA is doing; they firmly received their route if is the best gasline route. Fairclough – triggering treble damages with 500 mcf limit for instate use.

Palmer has proposed offtakes, a line to Valdex, and cross Canada but never proposed an instatethem.

Fairclough – build a 28" line with 460 mcf a day but could be expanded to over 500 mcf. Palmer said as long as TransCanada line is not in operation it would not be a treble damage situation.

Porter – Fairbanks needs are 50 mcf; look fifteen twenty years down the road.

Palmer – you can't flag your molecules. If there is more than 500 mcf a day er

Galvin – 500 mcf per day from North Slope  
Cook Inlet Nenana Basin has no implications for treble damages because it is not coming from the North Slope.

Huggins – we put the treble damages in the law; we want instate gas consumption; we need to figure out how to do it without penalizing ourselves.

Salmon – open discussion of transporting fuel to river villages; possible with running gasline from Anchorage to Fairbanks.

Doogan – announcement of partnership yet to be formed, shipping gas yet to be found, in a direction we have yet determined;

Heinz – at least a third of Alaskans will not benefit from the instate line. Working with city of Tanana on how they would use propane in that community. Monday hired a propane coordinator to within one year on North Slope a commercial wholesale propane facility. Believe reasonably priced energy source.

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Salmon- oil and gas still dictating what the State should do; the legislature should be dictating what we want.

Ramras what a pleasure to be on same side as Galvin on this project; can I please have in writing a list of days and times of meetings with the producers and Enstar.

Wielow – add to list of those surprised about moving gas north. When legislature talked instate, administration was vehemently opposed saying big line was economy of scale and instate small line meant higher tariffs.

State's involvement of bullet line or spur line – Galvin

Talk about Cook Inlet running out of gas because know supplies are drying out; small discoveries on fringes but no big discoveries even though we have heard they are out there. Admin decided to combined two issues: encouraging exploration and providing short term solutions to energy needs.

Huggins – what was the timing problem of the resolution. Galvin can't remember.

Hawker asking DuBay – impediments to moving forward from corporate perspective to delivering gas to Alaskans. Mentioned RCA – give better understanding. Chugach Electric has filed as an intervenor who has counsel that has worked for the administration.

DuBay – RCA requirements are not impediments they are tasks  
Eisinger and Posey did represent state at one time

Heinz – oil and gas prices are significantly higher than just one year; there is extreme attraction to finding ways to increase production.

Cowdery – what would happen if the state incurred treble damages;

Pricing Cook Inlet North – and North to Cook Inlet

DuBay – no contracts beyond 2014 – new contracts not Henry Hub; hoping spur line will result in more production that demand which means a discount and better prices. North of \$300 for car rental for three days; reflection of more demand than rental cars than rental cars.

DuBay does not have taking over FNG in Fairbanks in their model

Last year and stronger last couple of months designing a line from Foothills to Cook Inlet; customers Fairbanks, Flinthills, Soldotna, Agrium; Nenana basin Doyon and Anadarko Foothills.

South to North and a lot o production potential found .north, would continue north

DuBay Conoca, Chevron, Marathon on a weekly basis

Heinz – do you drill wells before pipeline

Wyoming Natural Gas Authority stoc ' between pipeline firm and producers; State play a role in encouraging both to continue.

Porter – so long as treat all parties equally, there are no damages. If you extend an advantage to another company there is damage.

Skipkoff - Disagree with administration estimate of cost of plant because of assumption of location. Bechtel included consideration of low ambient temperature and high pressure pipeline to derive cost of construction of pipeline ; these considerations are unique to port authority project.

Seaton – what is Enstars commitment to servicing local communities with natural gas.

French – frustrated we have no cost for the project.

Reggie Joule – heard about using North Slope propane to supply communities up and down the Yukon River, but not Cook Inlet. Heinz - Cook Inlet Gas has no propane in it.

Green – thinking through what is being said whatever the state does to get into Enstar and ANGDA will slow it down.

Palmer certificate of public convenience and single window regulatory agency arrangement.

Proposal Phase: 100 – 150 people

Internal: 20 people  
Engineers  
environmental people  
People go through and implement open season

Contractual & sub-contracts to AK businesses

Definition Phase: 275 – 400 people

Internal team – 100 people retained by TC to move things along  
Would see that any openings are hired to Alaskans

Engineering any other contractual go to Alaskans

Execution and Construction Phase: 7,000 – 9,000 (does not include GTP)

Internal:

McGuire looking for more specifics– page 7 – what key internal roles:

Reciprocity for Canadian portion of projects

Fackrell said Rebuttal presumption of rolled in toll if there is mandatory expansion there is incremental rates.

If there is sufficient demand for an LNG plant in Valdez, TC will build the pipeline to Valdez.

Committed to going beyond a failed first open season

Reliable company to complete the project

Capital costs performance 42 to 48 inch line – internal work 1990 – 2003 costs 19% lower than competitors in Canada and 38% lower than competitors in U.S.

If you grant license it precludes a partnership- not true – have a provision in the application to allow this and precisely suggest it.

## Friday Roundtable Shippers

Huggins        4.5mcf daily volume  
                  Point Thomson  
                  Gas offtakes

Galvin – don't know what the potential offtake is will be combination of existing gas reserves being put into production and an estimate of what production will do in ten years. Offtake will be determined over time. Look at range of possibilities.

Porter – agree with commish the key is on open season what results are and Point Thomson. Cost to the state over ten year delay of Point Thomson at \$1 additional tariff.

Chevron – yet to find gas will not be an issue at open season however the ownership of Point Thomson must be resolved before open season.

Cathy Forester four pieces - Prudhoe Bay spent a year doing studies of what the oil losses would be with gas production scenario vs loss of gas; within reason Prudhoe will be able to supply a significant portion of the gas in the line as long as producers aggressively produce

Second – other oil fields out there besides Prudhoe Bay.

Third – undiscovered gas – there are huge numbers generated by USGS but until exploration occurs we won't know

- Fourth - Point Thomson
1. 2010 open season – Pt Thomson not there
  2. DNR and Exxon come to some terms and Exxon proceeds; AOOGC convinced PT Thomson should be developed as gas field
  3. DNR gives leases back to Exxon and Exxon puts it in production

Galvin - 1/3 to 40% of FT are proven reserves; significantly above with or without Pt Thomson

Fairclough what was original projection for oil production and length of extraction; Forester 9 billion barrels. Fairclough over time technology has allowed us to exceed that original estimate; technology will take us further than we anticipate on the natural gas.

Dave Van Tuyl BP Exploration - ACES structure provides disincentives to exploration on Prudhoe Bay.

Doogan – would you only commit to proven reserves in open season?

Palmer – most shippers do not have proven reserves for 25 years when they participate in open season

Dave Van – AGIA and TC structure prohibits opportunity for shippers and producers to negotiate rates. Concerned with difference between known and proven reserves.

Zager – Chevron – without PT Thomson \$125 billion loss in t

Wendy King – figure out what they think the field will produce; open season will be approached by each individual shipper separately to determine if they can take the risk of a twenty-five year commitment; each individual shipper will have to determine if they can take the risk of not being able to meet that commitment because if they don't make it they still are committed to paying the tariff.

Massey – Exxon doesn't know if Exxon could go forward in open season without knowing the fate of Pt Thomson.

Wendy King – a risky venture; companies will weigh all the economic criteria

What is the market price

What is the forecast profits

Deliverability

Known reserves

1. Pipeline is looking for fiscal stability
2. Shipper is looking at risk of being able to keep their commitment for providing volume agreed upon.

Dave Van Tuyl -

Key is what cost of project is

What terms pipeline company is going to offer during open season

What is cost of transportation of gas to shipper

Critical that cost to transport is as low as possible

Terms of tariff agreeable to shippers

Weil – without drilling wells at Pt Thomson how do you know what's there?

Marty – admit there is some uncertainty Yesterday awarded contract for ice road.

Palmer – tc put forward a provision that shares the risk with the shipper

75/25

70/30

60/40            ration expansion

**Paul Bloom – Goldman Sachs**

TransCanada will not indemnify anyone.

Massey – a low risk, but a risk that has to be dealt with before entering an agreement with TC. Termination risk  
Return on equity  
Cost of construction

Knee deep in money – DEPA said people will show up at open season- Massey said not true;

**Wendy King Conoco** - Item in AGIA not must have but statutorily required must accept FERC certificate regardless of the conditions and must sanction the project and move forward; TC has conditions that require more costs they must move forward; the project is driven by a schedule regardless of the effect of costs of the project;

600 million vs 84 million - deal with someone spending 1.5 to 2 % ultimate cost for getting to open season

Rollback discriminates against shippers 115% of original tariff and newer shippers 115% of a different rate

Fiscal package - 20 to 25 years fiscal stability from shippers; statutes can change but no fiscal stability for shippers to balance out flexibility in taxation

**John Zager** – look at quality of open season materials; must have confidence that the figures are realistic; price of gas cannot be controlled cost of steel can not be controlled; can't say whether

**Massey** - Denali nor Trans-Canada result in a commercially viable project; the two need to get together to become viable.

**Galvin** – Purpose of AGIA

Palmer – Kings comment of requirement to commit to date certain to receive FERC certificate doesn't exist; the date certain is to apply for a FERC certificate; applaud Massey on compromise observation; TC has put forward offers to compromise for many years now; can't do a comparison of Denali and TC because he hasn't seen Denali's commercial terms; TC has fifty years of experience in natural gas business in America; move 20% of North American gas everyday; have put forward open season proposals for years and will put forward with same standards as all others; hold assets in Canada that

no other party has; a number of uncontrollable costs exists in any project; TC has reasonable estimates of these uncontrollable costs;

Dickinson – one of must have commitment for date to apply FERC; December 2011 subject to issuance of license; slide 14 of presentation given to body seven times; October 2012; December 2011 was dependent on license by April of 2008; it is a sliding date dependent on issuance of license;

Crawford - waited since yesterday to ask question; waited eight years to see project start; main criteria to have lowest tariff possible; where does the lower tariff outweigh producer on line project; owner line could shift costs like TAPS;

Massey – producer owned pipeline can generate as low of a tariff as third party; tariff is driven by capital costs; financial strength can achieve lowest debt costs and go to market and pull in debt to 80% on the market; slight advantage to producer owned because of financial strength;

Zager – have not done analysis; weighing out things that are financial but not apple to apple comparison; premise that independent it has significant advantage – doesn't buy;

Wendy King – tariff conditions; strength of project sponsors; percentage of debt; when the project sponsor is strong no one is motivated to waste capital but on this project because the costs go back to the shippers the alignment encourages the producers to keep the costs down. Don't consider the history over the last four years a failure;

Dave Van Tuyl – financibility of this project is huge; FT commitments are substantial;

Fairclough, Commish Galvin – modification provisions can't diminish value of project to state and can't decrease success of project;

One item Palmer brought forward is 36,000 of natural gas pipeline transmission system impressive; highlight is started with 3 customers and now 300 customers; upstream competition is what Alaskans fear; realize TAPS lifeline for decades and much appreciated and hats off to team and people they employ but no the less when you say there is an open access in TAPS we only see the big three shipping in TAPS; tell me why Alaskans shouldn't feel threatened by the big three;

Wendy King – ability for explorer to use pipeline; if economically attractive the explorers can have space; Fairclough in reality heard from administration the tariff rates make it uneconomical to access the line; the admin has convinced her the tariffs are preventing explorers from using TAPS;

Porter – TAPS comes from historically issues; when oil sold for 14.84 it cost \$10 for production and \$5 tariff from TAPS loss is 16 cents a barrel; now oil is \$140 barrel now economic; Fairclough goes back to upstream competition which is 300 in Canada;

King – largest explorer; Conoco likes to get co-venture to share the risk; believe co-ventures will be able to get access to TAPS; believe ANCPA for expansion FERC can force mandatory expansion; should not ask initial shippers to take the risk for the cost of the project;

Dave – during open season anybody can get access to the gasline whether or not they have gas;

Massey – doesn't believe tariff is an issue with TAPS anymore; gasline will have significant incentive for expansion; starts at 4.5 bcf and can expand to 5.9 and to 6.5 without facing any hurdle; FERC protection for open access with ability to make expansion mandatory;

Zager – Chevron own 1% of TAPS; have foothills gas exploration and in event of find have no concerns about access;

Wendy King – have had success with Pioneer sharing with third party in last year;

Galvin – trust FERC for expansion but rolled in rates may not be approved by FERC; rebuttal presumption is not there with mandatory expansion; Fackrell was asked yesterday if every two years open season found successful open season would Denali commit now to expand; Fackrell said he would have to go back to owners for okay because expansion requires capital outlay.

King – if gas comes from federal lands, shippers could be paying more for transportation; want to be able to go to FERC;

Palmer – AGIA requires the company to voluntarily expand; initial shippers are always concerned with what will happen with tolls in the future. National Energy Board has had policy for more than 20 years for mandatory expansion and roll back provisions. Shippers are opposed but that is a policy call for the legislature;

Porter – when do you trust FERC and when don't you trust FERC; define subsidy – the initial shipping costs are not a subsidy; shipping from Chukchi is federal gas where you get no royalties and no taxes; 14% return and 965 points TC; FERC has approved 14% rates but have never approved a floating rate; Canada has approved a floating rate but 14% return would be high; return on equity won't get lower rate; cost of debt will lower tariff with stronger investors;

Palmer – Porter assumed that both parties would have the same capital costs; there is no external benchmark study; internal study from 1990 to 2003 TC 19% lower in Canada and 38% lower than any other company in US; have no data to compare Denali project because not aware of interstate or provincial project of parties in Denali; there are Rockies Express 55% equity times 13%; floating rate NEC 40% equity at 8.17% return;

Palmer to Fairclough there is no charge for a trade at the Alberta Hub and used NOVA transfers. If delivery is off the NOVA system there is a delivery charge;

Ramras - Tony Palmer – Who will be President of TC Alaska? Denali spending \$40 million this summer; Palmer is President and CEO of TC Alaska; spending 80 million in next 18 months; 3 direct reports engineering and consultings; not knowing whether we get a license we have not rented space; will you live here? Palmer has not made that decision; Palmer commitment to open season and to FERC filing; plan is in service by 2018;

Porter – timing for open season – usually a couple of summer field work; field work report attached to engineers report; can't understand why TC moved open season in July until Oct or November after review of two years of field reports; Palmer said they are doing field work this summer and next and conclusion of reports and review will be July 2010.

Galvin analysis of soonest gas delivery – license and timeline under TC and moving forward with FERC regardless of who gets FERC approval the moving forward of TC gets whoever transporting gas sooner;

Dave Van – not keen to have schedule drive project because that can result in train wrecks and massive cost overruns;

Jim Brown World wide gas marketing  
Mark Nelson commercial group working  
Norman Carter - financing  
Jim Morris - commercial attorney

Exxon is Alaska for over fifty years  
Largest leaseholder of discovered gas

Doubles Exxon's current U.S. gas production

Prior to 2000 \$3.00

FNG sale first sale of NS natural gas

Plan to pay plaintiffs on Exxon Valdez case.

Wile – plans to pay on Exxon lawsuit -

Marty Massey – deeply regret a tragedy; Exxon will abide by US Supreme Court decision.

Wile Brown Williams released report May 2008 that pipelines are getting built with thru put of 10 years. Massey said this project is too big to get financing for a ten year thru put.

Gara – mediation both parties have to want to do it

Massey – have not offered mediation but are fine with mediation if that is what the administration wants to do.

10,000 a day

One of third paths:

1. Expand
2. Oil recovery is not adequate go to gas production
3. Combination of oil and gas production

Massey thinks oil production first is the best route at Point Thomson.

Bundy –

1. Explain little more about cycling – is process that works around the world – 10,200 pounds of pressure; large distances between wells. Put two wells compression and gas put back into input well.
2. When will reserves be booked – is extremely important; there is a gate (do you have a commercially viable project?) next gate (is project sufficiently far along you know you are going to finish the project?) Somewher between sanction and project getting up.
3. If we were to approve AGIA would it harm the success of a pipeline? That's legislatures decision. Don't want to tell legislature what to do. The ? to ask does AGIA help align the parties to successfully allow the project to go forward.

Kerttula-

Hydro logics and cost analysis Black and Vetch came up with same thing Exxon came up with in 2001 at 45. bcf

Massey – Exxon doesn't have a hurdle rate-they look at the whole picture – does this project deliver the expectation.

Lynn-

Must haves

Gruenberg – South Florida Exxon delayed payment for years because the internal return rate was greater than the payoff. Massey said Exxon is not going to delay payment.

Therriault – some departments said Exxon said if we can't do this we will relinquish the leases.

Massey first time we have committed to bringing pt Thomson into production. Second hearing we committed to timeline and said if we didn't meet these commitments we

Therriault why would we accept a POD that would wipe out decisions retroactively to Mendke decisions.

Massey – guessed retroactivity is what state wanted.

Massey hard to predict what Exxon would do after open season to commit to one of two pipelines.

Huggins – Federal loan guarantees; Massey believes federal loan guarantees are extremely important to TC proposal being successful. If Exxon had access to them they would seriously consider it. It could be that a federally backed loan guarantee would be too expensive.

Wielokowski –

- Point 1: Get to book reserves once line up
- Point 2: Carry it as a footnote, not a debt.- current footnote 3 billion  
With Alaska production up to \$75 billion footnote

Pedro VanMears – it is not within scope of government anymore to

Massey – AGIA does not offer any financial predictability.

Massey – Exxon has to look at total deal tax rate, total revenue, can it be predicted over the term of the contract.

Massey – tariff predictability – what is pipeline capacity how much is available and what is tariff going to be.

Hoffman – is tax structure on the books acceptable? Massey – look more than tax structure.

Stedman – why should the state lock down oil taxes when the economics of oil and gas is not locked down. Massey the tax rate should be part of the totalitarian of a deal. The last deal made sense at that point in time but it doesn't have to apply to this deal.

Seaton – other 50% of gas not in Alaska do you own 50% of the pipeline the gas goes through? Massey the lower 48 sell at the wellhead so have very little to none of transportation costs.

**HB 3001**

**SB 3001**

**6/3-7/28/08**

**LIST OF**

**SPECIAL**

**SESSION**

**DOCUMENTS**

## Alaska State 25th Legislature Third and Fourth Special Session Documents

Third and Fourth Special Session Supporting Documents as presented on a daily basis.

If you have questions, please call the Legislative Information Office at 907-465-4648.

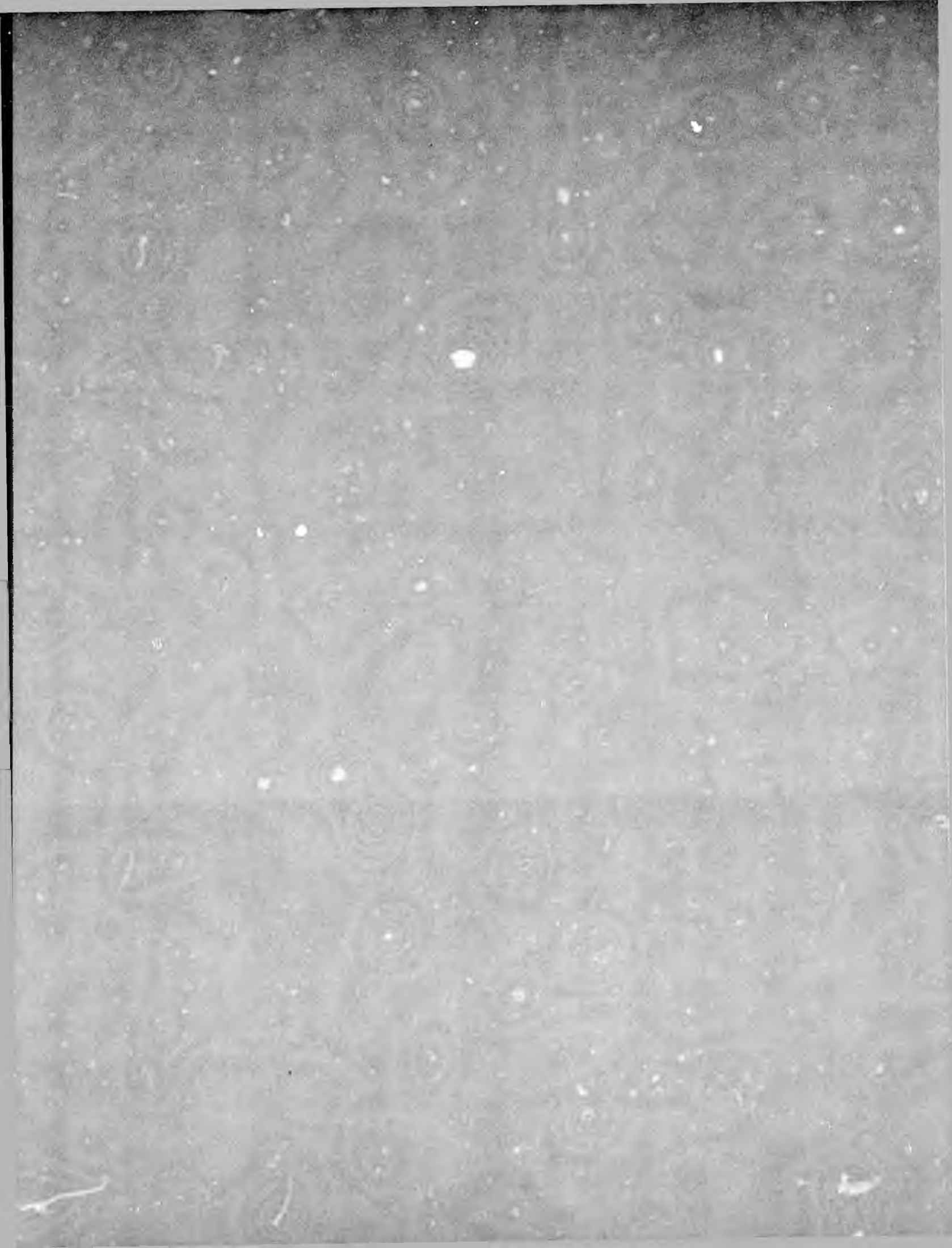
Date	Document
June 3rd, 2008	3rd Special Session Proclamation.pdf
June 4th, 2008	060408 LBA Econ One.pdf
June 4th, 2008	060408 LBA Muse Stancil - Impact Final Assessment.pdf
June 5th, 2008	060508 LBA Dickinson License Determination.pdf
June 6th, 2008	060608 AGIA Statute & RFA Refresher Special Session Joint Committee.pdf
June 6th, 2008	060608 TransCan AGIA Application Special Session Joint Committee.pdf
June 7th, 2008	060708 USGS (Long Version) Natural Gas Expl. Potential Special Session Joint Committee.pdf
June 7th, 2008	060708 USGS Natural Gas Expl. Potential Special Session Joint Committee.pdf
June 8th, 2008	060608 AGIA Training Strategic Plan Special Session Joint Committee.pdf
June 8th, 2008	060608 Short & Long Term Employment Special Session Joint Committee.pdf
June 8th, 2008	060808 Legal Issues Affecting Prod. Participa. Special Session Joint Committee.pdf
June 9th, 2008	060908 AGIA Incentives & Mandates Special Sessin Joint Committee.pdf
June 9th, 2008	060908 Challenges Alaskan LNG Special Session Joint Session.pdf
June 9th, 2008	060908 FERC Letter.pdf
June 9th, 2008	060908 LNG NPV Analysis Special Session Joint Committee.pdf
June 9th, 2008	060908 Prod. Incentives to Expand Special Session Joint Committee.pdf
June 10th, 2008	061008 Analysis of Project Costs Etc. Special Session Joint Committee.pdf
June 10th, 2008	061008 FERC Press Release.pdf
June 10th, 2008	061008 Financial Review of TC & Proposal Special Session Joint Committee.pdf
June 10th, 2008	061008 LNG NPV Analysis Special Session Joint Committee.pdf
June 10th, 2008	061008 LNG Project Costs & Schedule Special Session Joint Committee.pdf
June 10th, 2008	061008 Net Present Value Analysis Special Session Joint Committee.pdf
June 12th, 2008	061208 AGPA Fairbanks Special Session Joint Committee.pdf
June 12th, 2008	061208 AK Nat Gas Needs & Market 2008 Special Session Joint Session.pdf
June 12th, 2008	061208 ANGDA Fairbanks Special Session Joint Committee.pdf
June 12th, 2008	061208 Erstar Fairbanks Special Session Joint Committee.pdf
June 13th, 2008	061308 AGIA Training Strategic Plan Special Session Joint Committee.pdf
June 13th, 2008	061308 AGIA Written Findings & Summary May 2008 Special Session Joint Committee.pdf
June 13th, 2008	061308 DOT Infrastructure Improvements Needed Special Session Joint Committee.pdf
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June 14th, 2008	061408 AGIA Fairbanks Summary Special Sesssion Joint Committee.pdf
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June 17th, 2008	061708 AOGCC Cathy Foerster Testimony Special Session Joint Committee.pdf
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June 17th, 2008	061708 Chevron Pt. Thomson Special Session Joint Committee.pdf
	061708_AOGCC_Allowable_Gas_Offtake_Prudhoe_Bay_Special_Session_Joint_C

June 17th, 2008	ommittee.pdf
June 17th, 2008	061708 AOGCC North Slope Gas Sales Special Session Joint Committee.pdf
June 17th, 2008	061708 AOGCC Pool Rules for Pt. Thomson Field Special Session Joint Committee.pdf
June 17th, 2008	061708 Appendix to Pt. Thomson Res. Assess. DNR Special Session Joint Committee.pdf
June 17th, 2008	061708 DNR Glossary of Oil & Gas Terms Special Session Joint Committee.pdf
June 17th, 2008	061708 ExxonMobil Pt. Thomson Special Committee Joint Hearing.pdf
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June 18th, 2008	061808 DNR High Pressure Gas Reinjection Special Session Joint Committee.pdf
June 18th, 2008	061808 Gov Hickel Remarks Special Session Joint Committee.pdf
June 19th, 2008	061908 FERC Press Release on TAPS Tariff Special Session Joint Committee.pdf
June 19th, 2008	061908 Summary of Comm. Findings & Determin. Special Session Joint Committee.pdf
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June 20th, 2008	062008 EconOne Potential LNG Project Special Session Joint Committee.pdf
June 20th, 2008	062008 Enstar Special Session Joint Committee.pdf
June 20th, 2008	062008 SAIC AK Natural Gas Needs Special Session Joint Committee.pdf
June 20th, 2008	062008 SAIC AK Natural Gas Needs Updated Special Session Joint Committee.pdf
June 20th, 2008	062008 AK Gasline Port Authority Special Session Joint Committee.pdf
June 24th, 2008	062408 AGIA Summary, Findings & Determination Special Session Joint Committee.pdf
June 24th, 2008	062408 TransCan Statewide Hearing Presenta. for Special Session Joint Committee.pdf
June 26th, 2008	062608 AGIA Summary, Findings & Determination Special Session Joint Committee.pdf
June 26th, 2008	062608 TransCan Statewide Hearing Presenta. for Special Session Joint Committee.pdf
July 1st, 2008	070108 AGIA Summary, Findings & Determination Special Session Joint Committee.pdf
July 1st, 2008	070108 TransCan Statewide Hearing Presenta. for Special Session Joint Committee.pdf
July 8th, 2008	070808 AGIA Summary, Findings & Determination Special Session Joint Committee.pdf
July 8th, 2008	070808 TransCan Statewide Hearing Presenta. for Special Session Joint Committee.pdf

July 9th, 2008	070908 AK Gasline Port Authority Special Session Joint Committee.pdf
July 9th, 2008	070908 Point Thomson Unit Agreement Section 21 Special Session Joint Committee.pdf
July 9th, 2008	070908 Pt Thomson S. Porter LB&A Consultant Special Session Joint Committee.pdf
July 10th, 2008	071008 CBI Mediation Presenta. Special Session Joint Committee.pdf
July 10th, 2008	071008 Denali Project Special Session Joint Committee.pdf
July 10th, 2008	071008 Exxon Mobil Special Session Joint Committee.pdf
July 10th, 2008	071008 Exxon Mobil Written Testimony Special Session Joint Committee.pdf
July 10th, 2008	071008 Kalt Report provided by Exxon Mobil to Special Session Joint Committee.pdf
July 10th, 2008	071008 TransCan. Alaska Pipeline Workforce Plan Special Session Joint Committee.pdf
July 13th, 2008	071308 Bennett Jones Report Special Session Joint Committee.pdf
July 13th, 2008	071308 Keith Bergner Bio Special Session Joint Committee.pdf
July 13th, 2008	071308 Lawson Lundell The Crown's Duty to Consult & Accom. Special Session Joint Hearing.pdf
July 13th, 2008	071308 Lawson Lundell The Duty to Consult What Does it Mean to Project Special Session Joint Committee.pdf
July 14th, 2008	071408 APEGGA Letter to TransCan. Handout at Special Session Joint Committee.pdf
July 22nd, 2008	07222008 OHA Letter to Sen Green.pdf
July 22nd, 2008	07222008 SENR AGPA Presentation.pdf
July 28th, 2008	72808 HICKEL Testimony before SENR.pdf

For additional information, including correspondence with consultants, memos, and other work documents provided to the Legislature, go to Legislative Budget and Audit Committee, click on Gasline Proposals, then click on Gasline Document Logs.

Send questions and comments to Webmaster.



# STATE OF ALASKA



## *Executive Proclamation* by *Sarah Palin, Governor*

Under the authority of art. II, sec. 9, and art. III, sec. 17, of the Alaska Constitution, and in the public interest, I call the Twenty-Fifth Legislature of the State of Alaska into its third special session at Juneau, Alaska in the legislative chambers on June 3, 2008 at 5:00 p.m. to consider the following subject:

any action taken by the commissioner of natural resources and the commissioner of revenue under AS 43.90, the Alaska Gasline Inducement Act.

Dated at Juneau, Alaska this 27<sup>th</sup> day of March, 2008.

Done by



  
Sarah Palin, Governor

**HB 3001**

**SB 3001**

**6/4/08**

**SPECIAL**

**SESSION**

**DOCUMENTS**

# Comments to Legislature on TransCanada Proposal

June 4, 2008

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Senior Economist  
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## What Does TransCanada Propose to Do?

- **Construct and operate 1,700-mile, 48-inch pipeline from North Slope to Alberta, with initial capacity of 4.5 bcf/day, expandable to 5.9 bcf/day with addition of compression**
  - **Conditioned on receiving sufficient firm transportation commitments**
- **Pipeline would terminate at Boundary Lake on the British Columbia / Alberta border, where it would enter the “AECO Hub”**
  - **At AECO, shippers would arrange for extraction of valuable NGLs (either from third-parties or through construction of own facilities). “Residue” gas could be sold either in Canada or shipped to Lower-48.**
- **Construct and operate necessary Gas Treatment Plant (“GTP”), if not undertaken by another party**
- **Provide pipeline access for LNG facility if demand warrants**

# What Does TransCanada Propose to Do?

(cont'd)

## Offer tariffs reflecting:

- **20, 25 and 30 year firm transportation commitments**
- **Recourse and Negotiated Rates (Alaska); Negotiated Rates (Canada)**
- **Capital Structure of 70% debt / 30% equity (recourse), 75% debt / 25% equity (negotiated)**
- **Equity return floating at 965 basis points above 10-year T-bonds**
- **100% cost recovery (3.5MMBtu/day and above)**

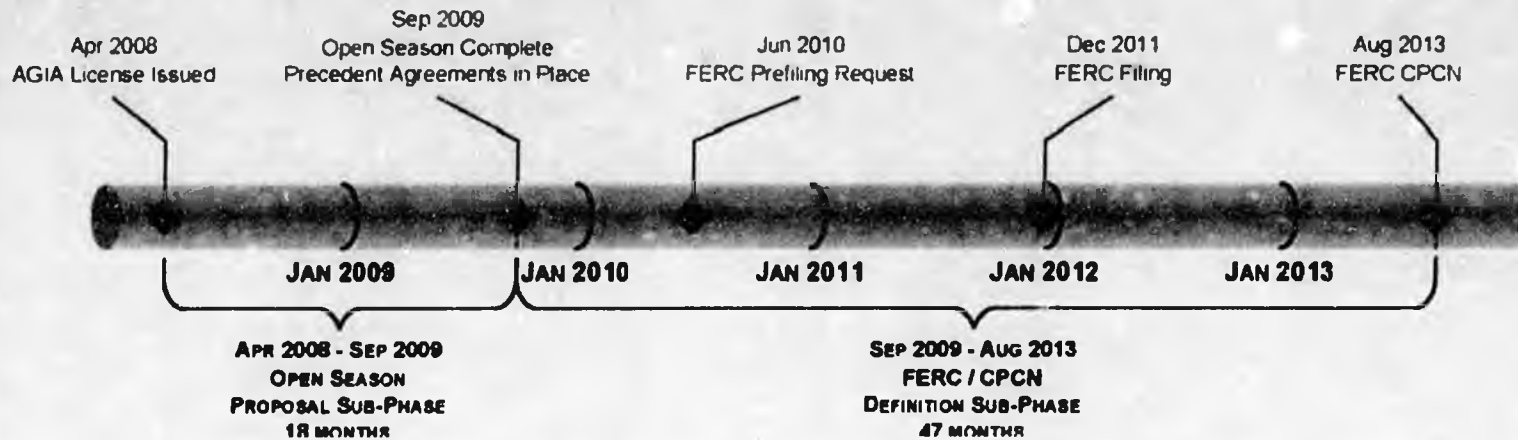
## What Does TransCanada Propose to Do?

(cont'd)

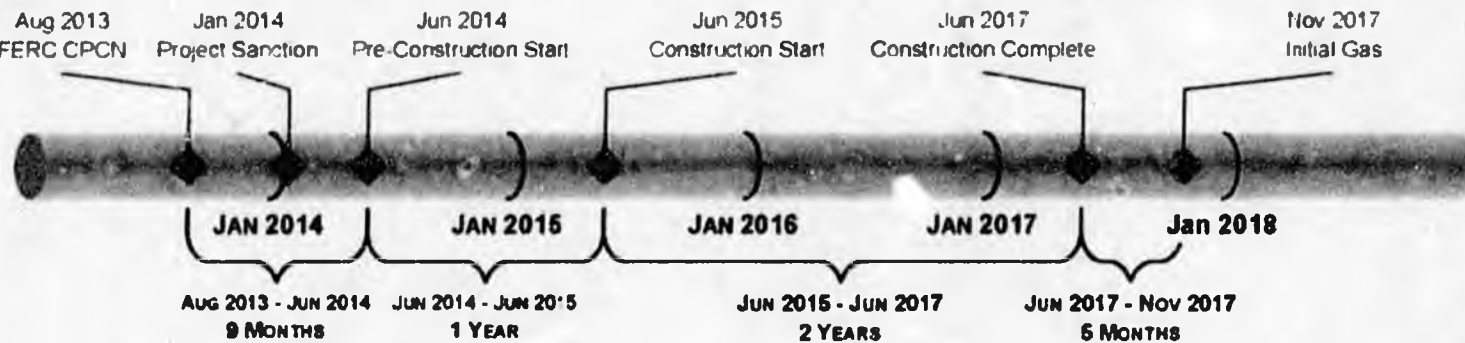
- **Assess market demand for expansion every two years through non-binding open seasons**
- **Offer rolled-in rates for expansions, subject to ceiling of 115% of initial tariff**
- **Provide minimum of 5 in-state delivery points, using distance-sensitive rates**

# Proposed Timeline (Assuming License Awarded April 2008)

## DEVELOPMENT PHASE



## EXECUTION PHASE



# What Does TransCanada Ask From the State?

- License
- Follow through on State commitments under AGIA
- State Contribution of \$500 million toward development cost of pipeline

	<u>Total Budgeted</u>	<u>State Reimbursement</u>	<u>Reimbursement Percentage</u>
	(Million Dollars)		(Percent)
	(1)	(2)	(3)
Open Season Period (Through Aug 2009)	\$82.3	\$41.2	50%
Certification Period (Sep 2009 - Aug 2013)	\$528.7	\$458.8	87%
<b>Total Pre-Construction</b>	<b>\$611.0</b>	<b>\$500.0</b>	<b>82%</b>
<b>Total After Construction</b>	<b>\$29,078.0</b>	<b>\$500.0</b>	<b>2%</b>

- Not to be included in tariff rate base



## What Does TransCanada Ask From the State?

(cont'd)

- **Engagement with ANS producers to reach agreement on fiscal terms**
- **Encouragement of robust exploration and development of North Slope gas resources**
- **Cooperation of State to reach out to stakeholders**
- **Cooperation of State in efforts with the Federal Government to obtain support for project**
- **Use of loan guarantees for cost overruns**
- **Exploration of alternative credit concepts, i.e., backstop Shipper contract**

## What Does TransCanada Ask From the State?

(cont'd)

- **In the event of an unsuccessful open season:**
  - **Expect State to use its position of sovereign government to encourage, induce and persuade ANS producers to commit gas**
  - **Expect State to thoroughly evaluate and seriously consider financial and commercial feasibility of dedicating significant State resources to underwriting an alternative financing mechanism for the project**

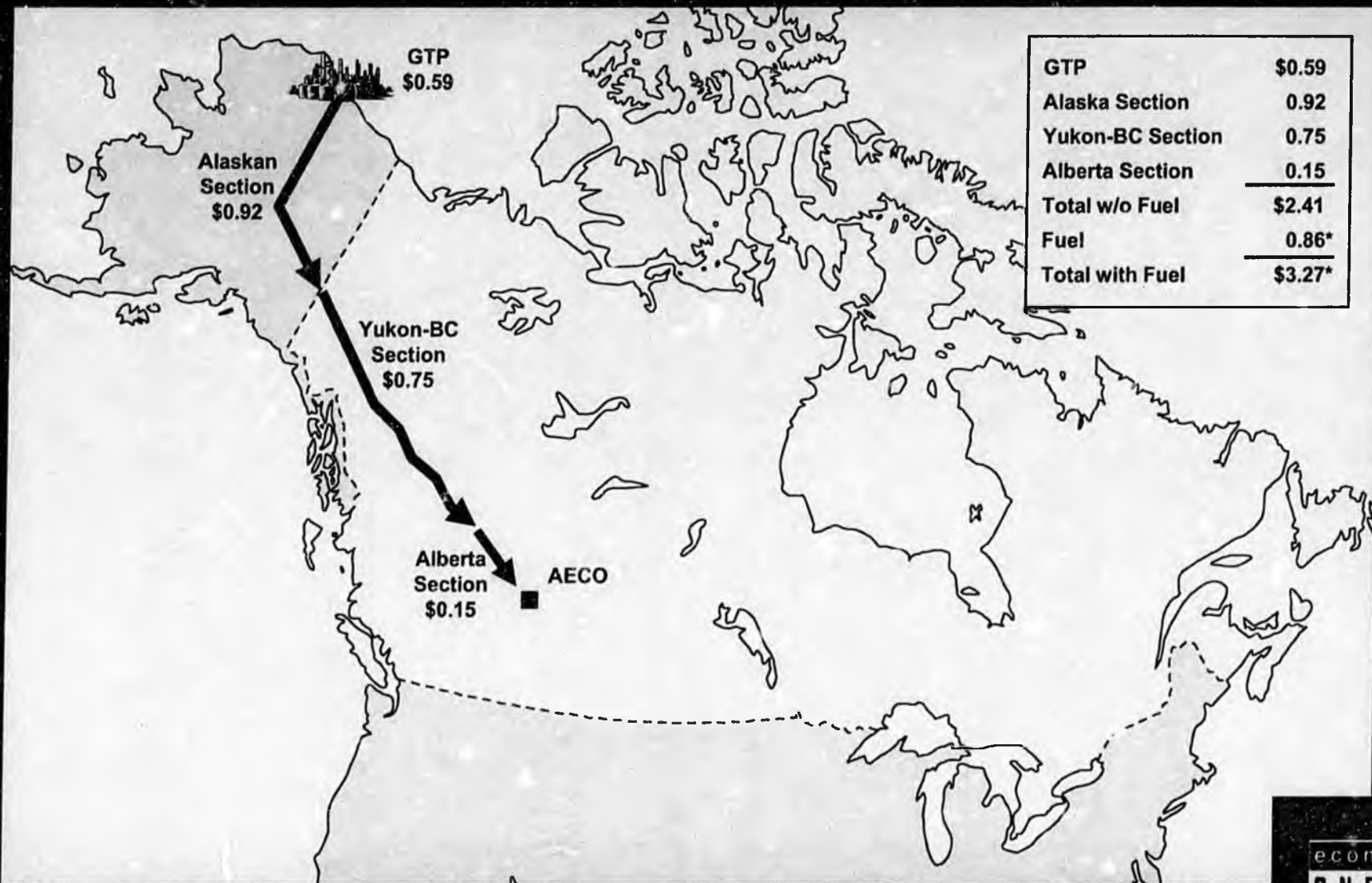
## How Does the State Subsidy Help?

- **Reduces risk to TransCanada**
  - **State shares in risk that project may not proceed to completion and is responsible for 82% (\$500 Million) of the targeted \$611 million in development costs**
- **Reduces tariff, which benefits resource owners: State and producers. Using TransCanada assumptions as to costs and tariffs, the \$500 million impacts the tariff as follows:**
  - **Estimated tariff to Alberta without subsidy is \$2.46/MMBtu**
  - **Estimated tariff to Alberta with subsidy is \$2.41/MMBtu**
  - **This is \$0.05/MMBtu**
  - **Over a 25-year period, this amounts to a reduction in tolls of \$2.2 billion. Approximately \$1.2 billion is expected to accrue to the State**

# Tariff Fundamentals

- **What is a tariff?**
  - **Document that sets forth rate and terms of service provided by a pipeline to shippers**
  - **The per-unit cost charged by a pipeline to ship gas from point of injection to point of extraction (Point A to Point B)**

# TransCanada's Tariff Estimates



\* 25-year average based on AEO2008 price profile at Henry Hub, with \$0.40/MMBtu differential to AECO.

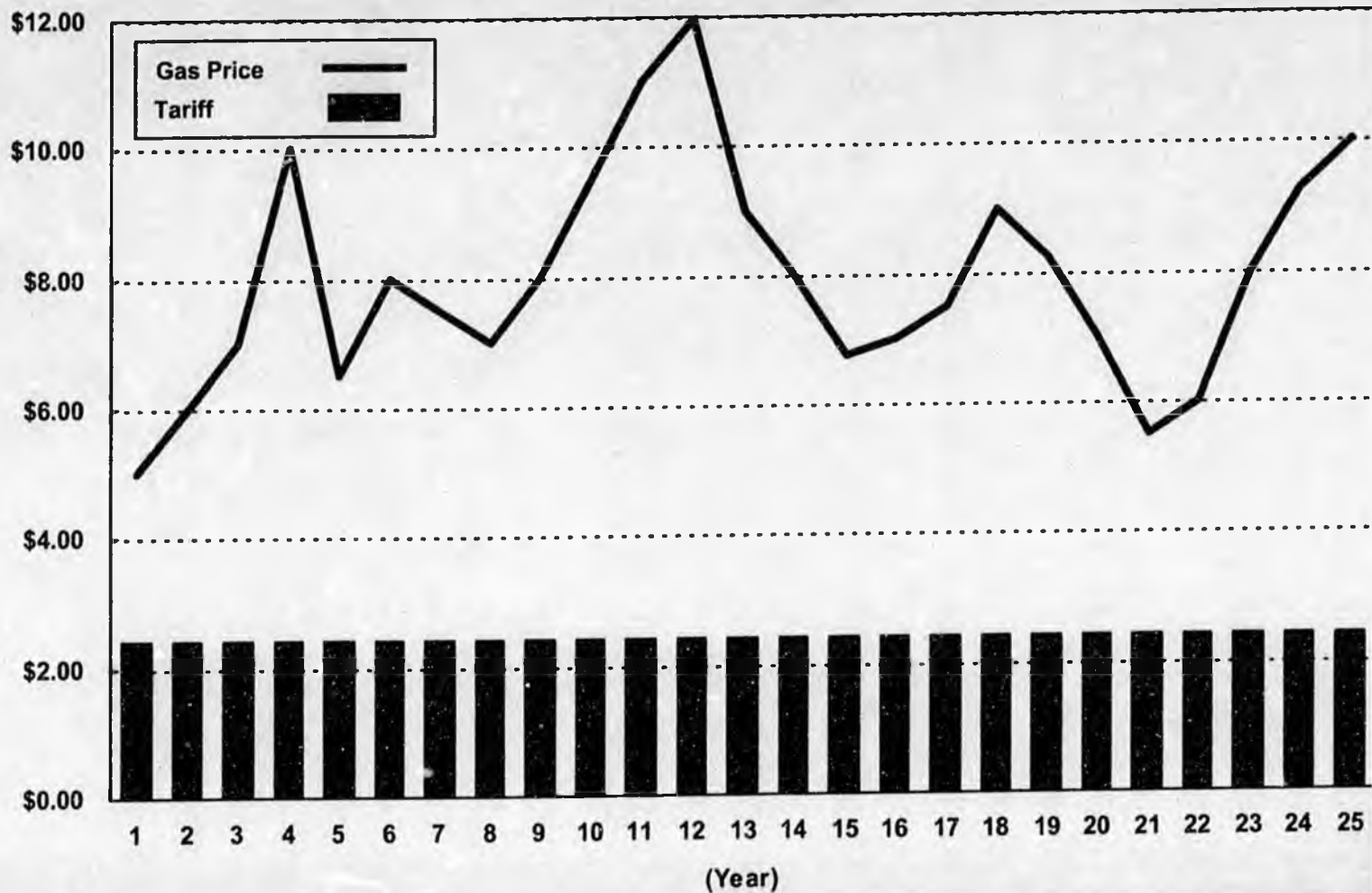


## Significance of the Tariff to Resource Owners

- All else equal, resource owners (State and producers) prefer lower tariffs; lower tariffs = higher netbacks
- In the case of gas, tariffs typically involve long-term “take or pay” commitments. Here we are talking about commitments likely ranging between 15 and 30 years
  - In this respect, gas pipeline tariffs are different than oil pipeline tariffs. With oil pipelines (such as TAPS), there is typically no take or pay aspect
  - Risk to shipper rises with length of commitment
  - Risk to shipper rises with level of tariff relative to the expected gas price
    - Tariff level is fixed while price of gas at market is unknown and variable

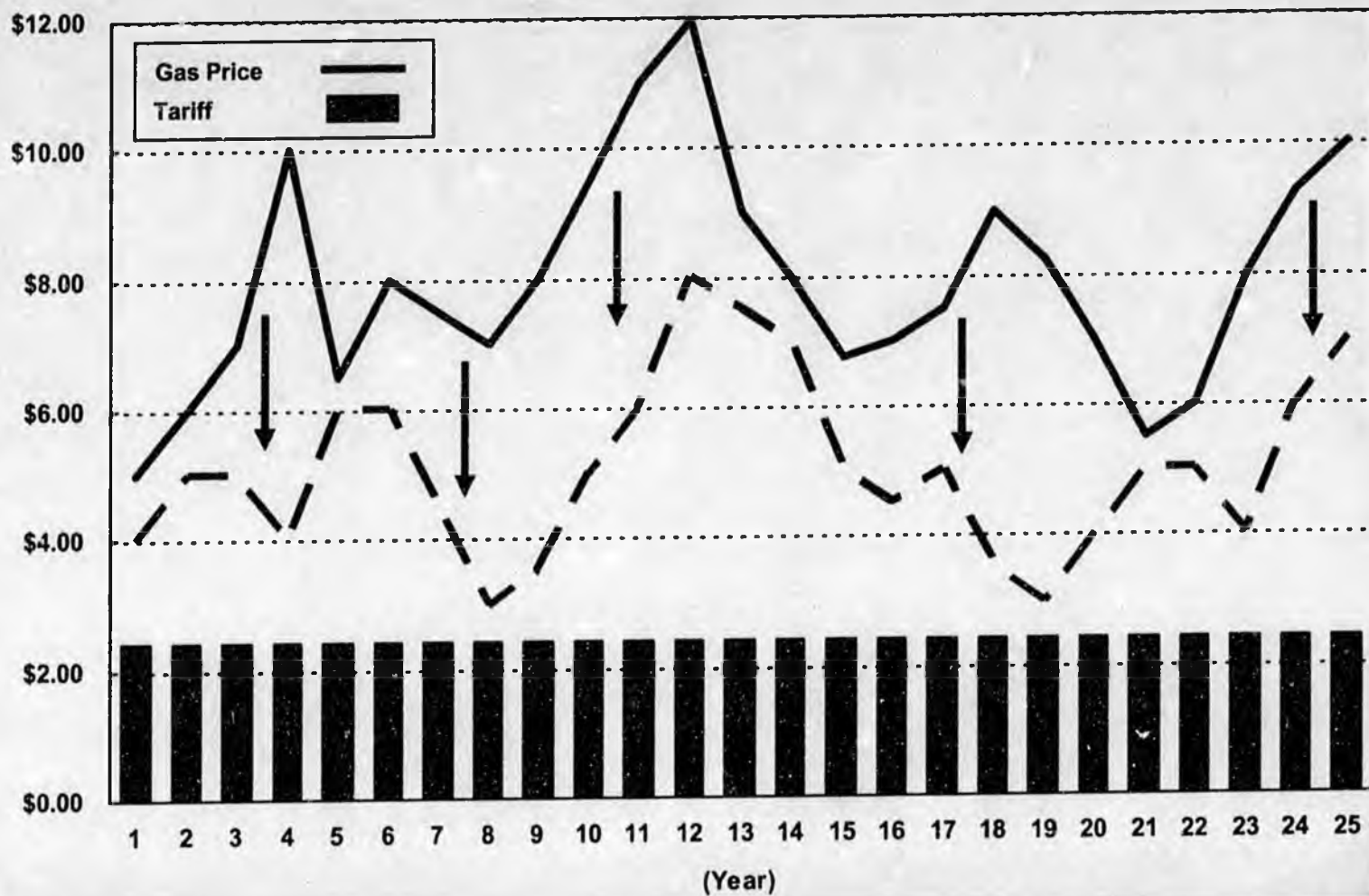
# Significance of the Tariff to Resource Owners

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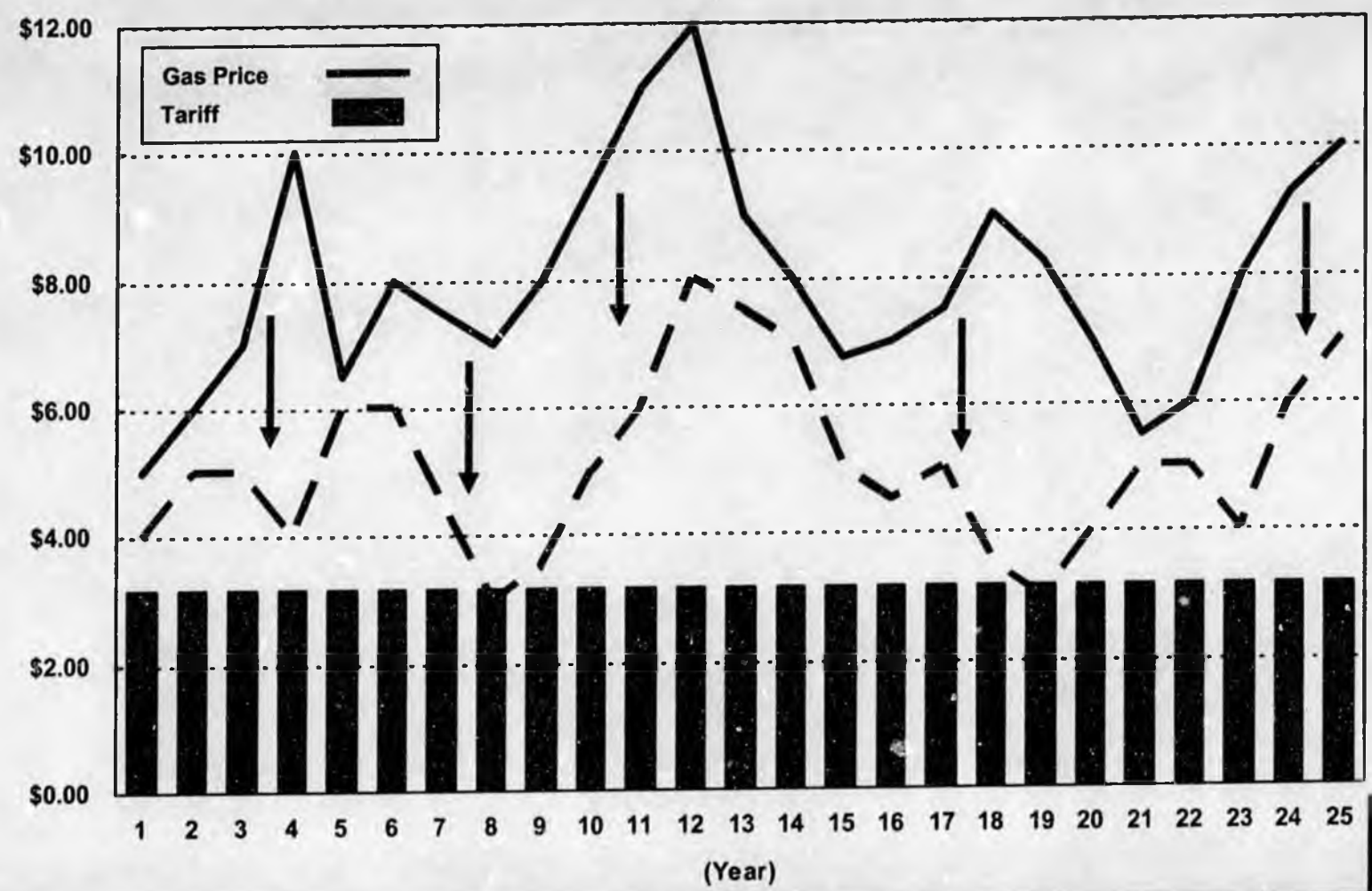
# Significance of the Tariff to Resource Owners

(cont'd)



# Significance of the Tariff to Resource Owners

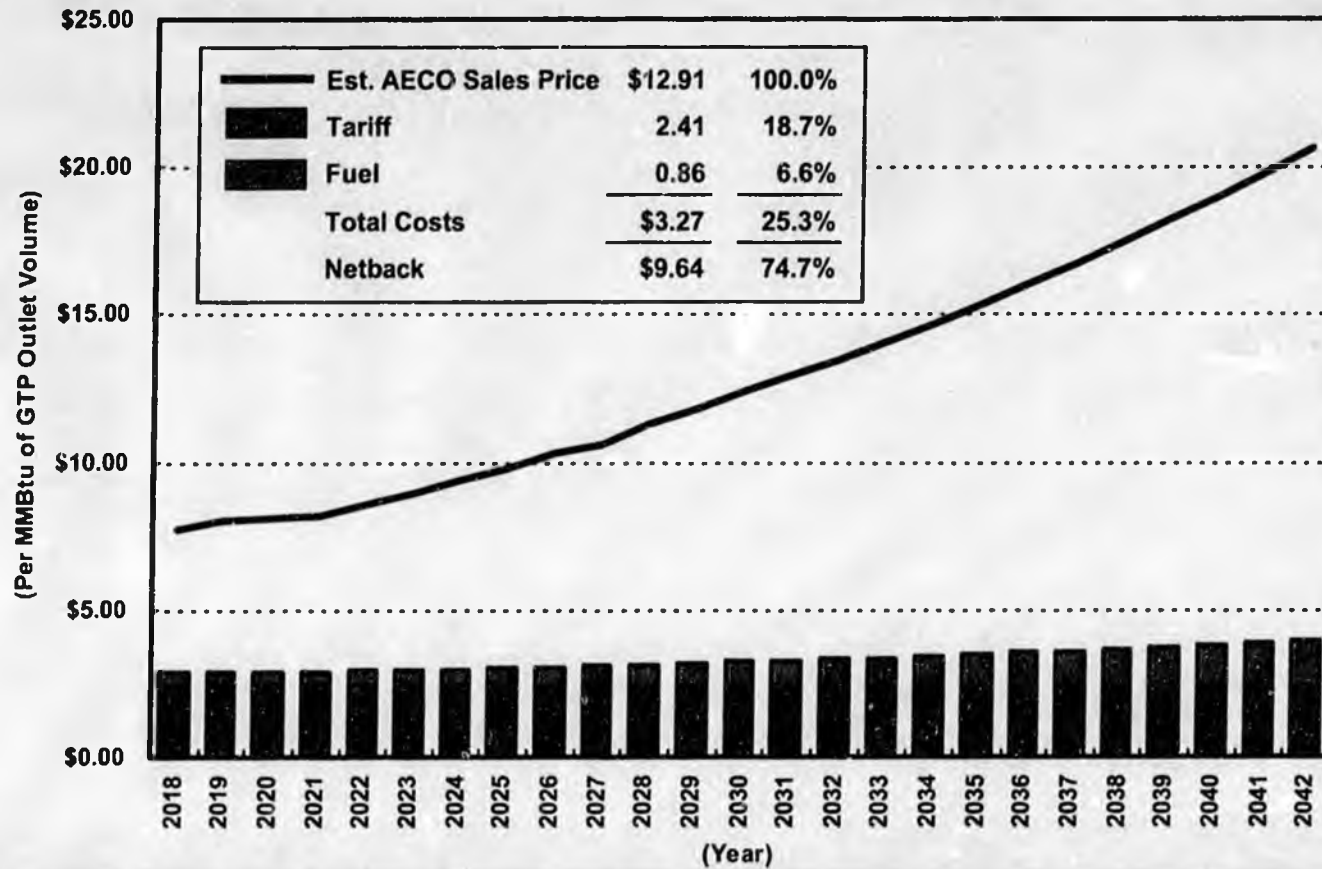
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# Significance of the Tariff to Resource Owners

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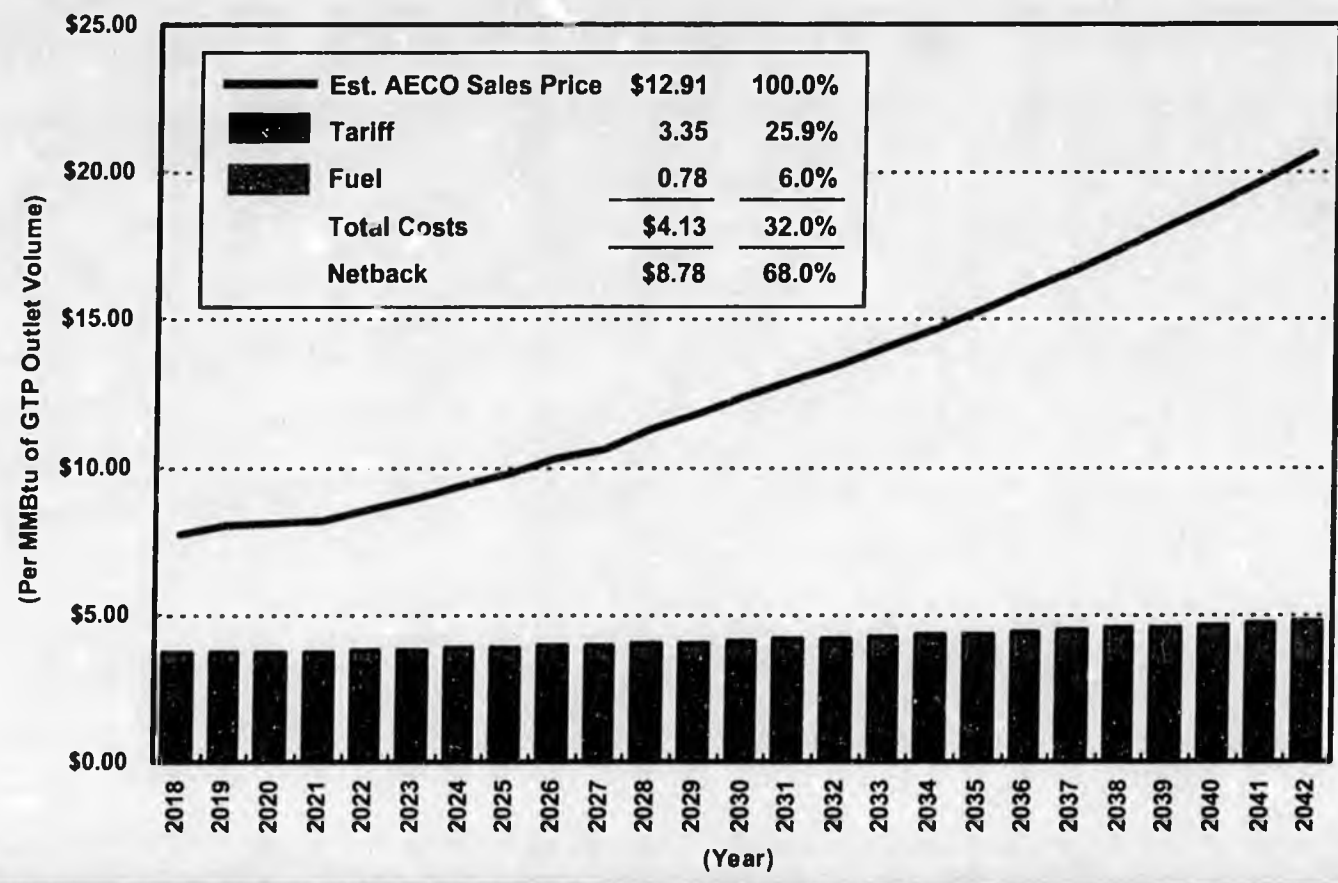
- Based on current projections by the EIA over 25 years beginning in 2018 and potential tariffs set out in the TransCanada application, the tariffs would be approximately 25% of the value of gas at AECO



# Significance of the Tariff to Resource Owners

(cont'd)

- Increasing capital costs by 50% would lead to tariffs being approximately 32% of the value of gas at AECO



# Significance of the Tariff to Resource Owners

(cont'd)

<u>25% Below EIA AEO 2008 Forecast</u>			<u>EIA AEO 2008 Forecast</u>			<u>25% Above EIA AEO 2008 Forecast</u>		
Est. AECO Price	\$9.56	100.0%	Est. AECO Price	\$12.91	100.0%	Est. AECO Price	\$16.26	100.0%
Tariff	2.41	25.2%	Tariff	2.41	18.7%	Tariff	2.41	14.8%
Fuel	0.58	6.1%	Fuel	0.86	6.6%	Fuel	1.13	6.9%
Total Costs	<u>\$2.99</u>	<u>31.3%</u>	Total Costs	<u>\$3.27</u>	<u>25.3%</u>	Total Costs	<u>\$3.54</u>	<u>21.8%</u>
Netback	\$6.57	66.7%	Netback	\$9.64	74.7%	Netback	\$12.72	78.2%

# Tariff Fundamentals

(cont'd)

- **Tariffs are regulated**
  - **U.S. is regulated by the Federal Energy Regulatory Commission (FERC)**
  - **Canada is regulated by the National Energy Board (NEB)**
  - **Charged with insuring that rates are “just and reasonable”**
  - **Opportunity for shippers to challenge tariffs through rate proceedings**

## Recourse Rates

- **Traditionally, tariffs have been based on “cost of service.” Tariff rates under a traditional cost-based approach are known as “Recourse” rates**
- **These tariffs provide for recovery of operating costs, capital costs and a “reasonable” return on invested capital**
- **Initial tariffs would be established by FERC in filings by the pipeline during certification. These rates could be challenged in FERC and/or NEB by shippers in rate proceedings**

## Recourse Rates and Cost of Service

- **Key elements of cost of service include:**
  - **Return on Investment**
  - **Return of Investment (Depreciation)**
  - **Operating Expenses**
  - **Non-Income Taxes (e.g., Property Taxes)**
  - **Income Taxes**

# Recourse Rates and Cost of Service

(cont'd)

➤ **Cost of service elements in TC estimates:**

	<u>Total</u> (Billion Dollars) (1)	<u>As Percent of Total</u> (Percent) (2)
<b>Return on Investment</b>	<b>\$33.2</b>	<b>32%</b>
<b>Return of Investment (Depreciation)</b>	<b>\$33.2</b>	<b>32%</b>
<b>Operating &amp; Maintenance</b>	<b>\$9.5</b>	<b>9%</b>
<b>Non-Income Taxes</b>	<b>\$15.8</b>	<b>15%</b>
<b>Income Taxes</b>	<b>\$12.3</b>	<b>12%</b>
<b>Total</b>	<b>\$104.0</b>	<b>100%</b>

## Cost of Service -- Return on Investment

- Return on Investment is calculated as:

$$\underline{\text{Rate Base}} \times \underline{\text{Rate of Return}}$$

- Rate Base is:

$$\underline{\text{Gross Plant (Initial Capital Investment + AFUDC)}}$$

$$- \underline{\text{Accumulated Depreciation}}$$

$$= \underline{\text{Net Plant}}$$

$$- \underline{\text{Accumulated Deferred Income Taxes}}$$

$$+ \underline{\text{Working Capital}}$$

$$= \underline{\text{Rate Base}}$$

## Cost of Service -- Rate of Return

- **Rate of Return is:**
  - **“Reasonable Return” on Investment (Rate Base)**
  - **Function of three components:**
    - **Capitalization Ratio (Debt, Equity)**
    - **Cost of Debt**
    - **Allowed Return on Equity**

# Cost of Service -- Rate of Return

(cont'd)

- **These elements are set by FERC to allow “Reasonable Return”**
- **Typically allow for passthrough of debt costs, plus**
- **Return on Equity consistent with business risk associated with the pipeline venture**
  - **FERC has approved Equity Returns in the range of 12-14%**
    - **Higher end of the range for “greenfield” projects**
    - **NEB returns have traditionally been lower**
- **Rate of return is one of the biggest issues for regulators**
- **Initial rates allowed by regulators can be revisited in an initial rate hearing 3-4 years after pipeline operation begin**
- **Initial return is likely to be reduced if business risk is judged to be lower**

# Negotiated Rates

- **Negotiated rates are also regulated by FERC**
- **However, as the name implies, these are rates that are “negotiated” between shipper and the pipeline company**
- **All elements are up for negotiation. This includes:**
  - **Rate of Return**
  - **Length of commitment**
  - **Flexibility**
  - **Treatment of cost overruns**
  - **Future expansion issues**
  - **Changes in operating costs**

# Negotiated Rates

(cont'd)

- **Negotiated rates can result in lower tariffs than recourse rates through the process of commercial negotiation**
- **Negotiation takes the place of regulation. However, as the negotiation takes place with the backdrop of regulatory oversight (and recourse rate option/backstop), the process can help reduce tariffs charged**
- **Typically involve long-term shipping commitments**
- **Negotiated rates must be approved by FERC and NEB**
- **Regulatory bodies have viewed negotiation process favorably and are reluctant to modify them after the fact**

# Negotiated Rates

(cont'd)

- **A point for the State to consider:**
  - **The negotiation process can provide favorable results for the State by helping to keep tariffs down**
  - **State likely would not have opportunity to challenge these rates after the fact. The opportunity to challenge would be in the certification process**
  - **State's interest should be protected. However, this is the time to apply scrutiny**

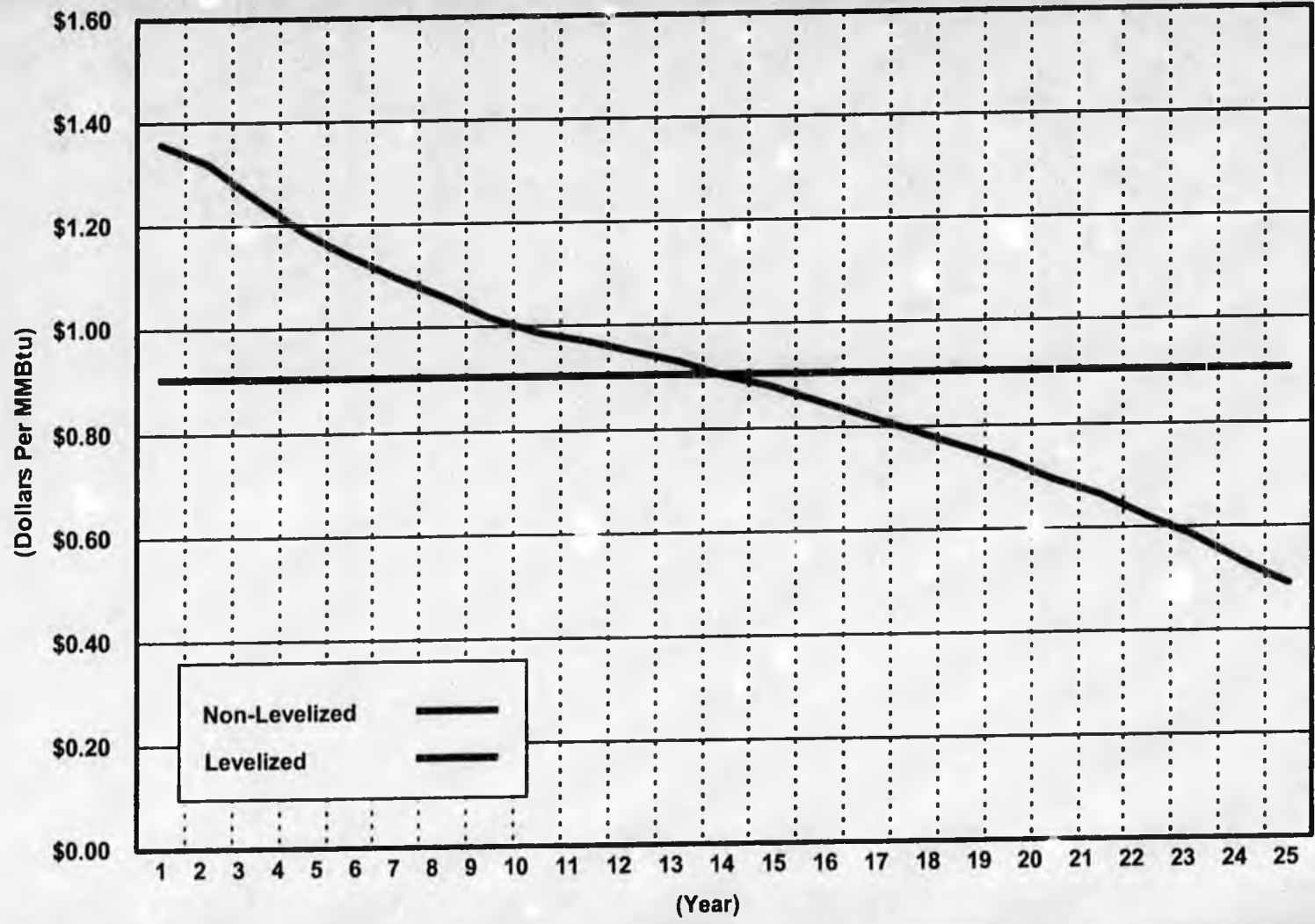
## Some Examples of Recourse and Negotiated Rates

	<u>Recourse</u>	<u>Negotiated</u>
Alliance Pipeline	\$0.53	\$0.54
Rex West	\$0.91	\$0.77 - \$0.79
Gulf Stream	\$0.66	\$0.57 - \$0.59
Maritimes & Northeast Phase IV	\$0.78	\$0.53

## The “Levelized” Tariff

- **A traditional cost-based tariff starts high and falls as a pipeline recoups its capital costs (i.e., return on investment and return of investment)**
- **This happens because the rate base falls over time as the pipeline is depreciated**
- **A levelized tariff is one in which the tariff is constant over time. The level of the tariff is set such that it results in the same Net Present Value (NPV) as the cost of service for the non-levelized tariff**

# Illustration of a Levelized Tariff



## Tariffs Proposed by TransCanada

- Offer 25, 30 and 35-year firm transportation services (FT)
- Offer Recourse Rate tariff for GTP and Alaska Pipeline Section; Negotiated Rate tariff for all sections
- No Recourse Rate offered for Canada, as this is not normal business practice in Canada (i.e., negotiated rates are the norm)

## Key Elements of Recourse Rate Tariff

- Provides for full recovery of capital costs on “straight line” basis over 25-year period, assuming initial transportation agreements are for this period
- 100% load factor rates for authorized overrun services
- Rate base will exclude Alaska portion of \$500 million State contribution
- Capitalization of 70% debt / 30% equity
- Expansions capitalized at 60% debt / 40% equity

# Debt Costs

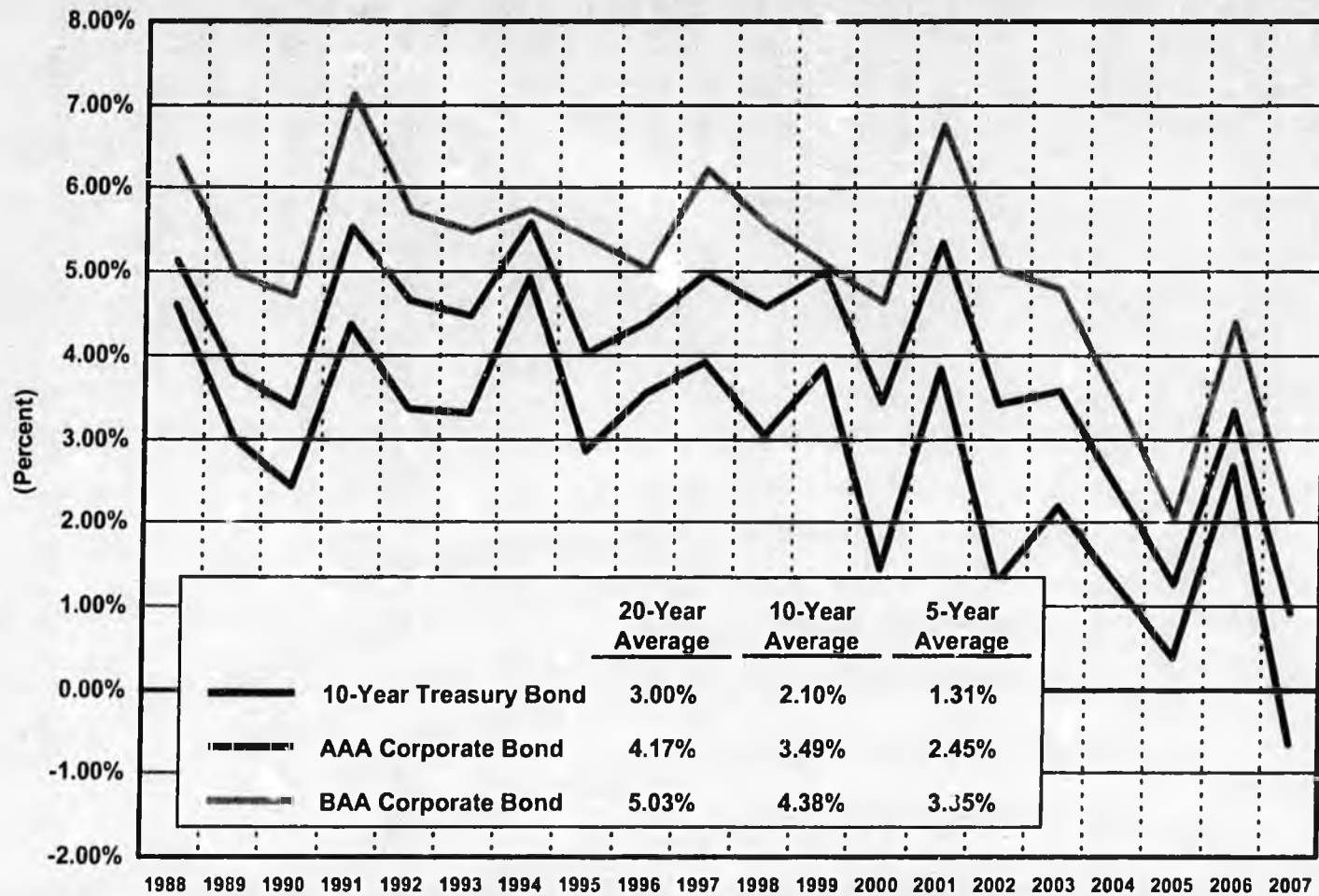
- **Debt costs will be weighted average cost incurred by pipeline**
  - **Contemplate U.S. loan guarantees**
  - **Loan guarantees were originally \$18 billion, up to 80% of project**
  - **They were indexed to inflation. In 2008 dollars, this is approximately \$20 billion**
  - **Assuming 75% debt, this would support project of \$26.8 billion in \$2008 if all the loan guarantee was used**
  - **TransCanada has assumed a number for loan guarantee debt of 4.7%. Based on expectations of inflation in the 2.5% range, this may be somewhat low**
  - **Borrowing without the U.S. loan guarantee is estimated at 150 basis points higher (i.e., 6.2%)**



# Debt Costs

(cont'd)

***Inflation Adjusted* Historical 10-Year T-Bond and Corporate Bond Rates**



Source: Federal Reserve Bank.



# Potential Borrowing Costs for Guaranteed Loan

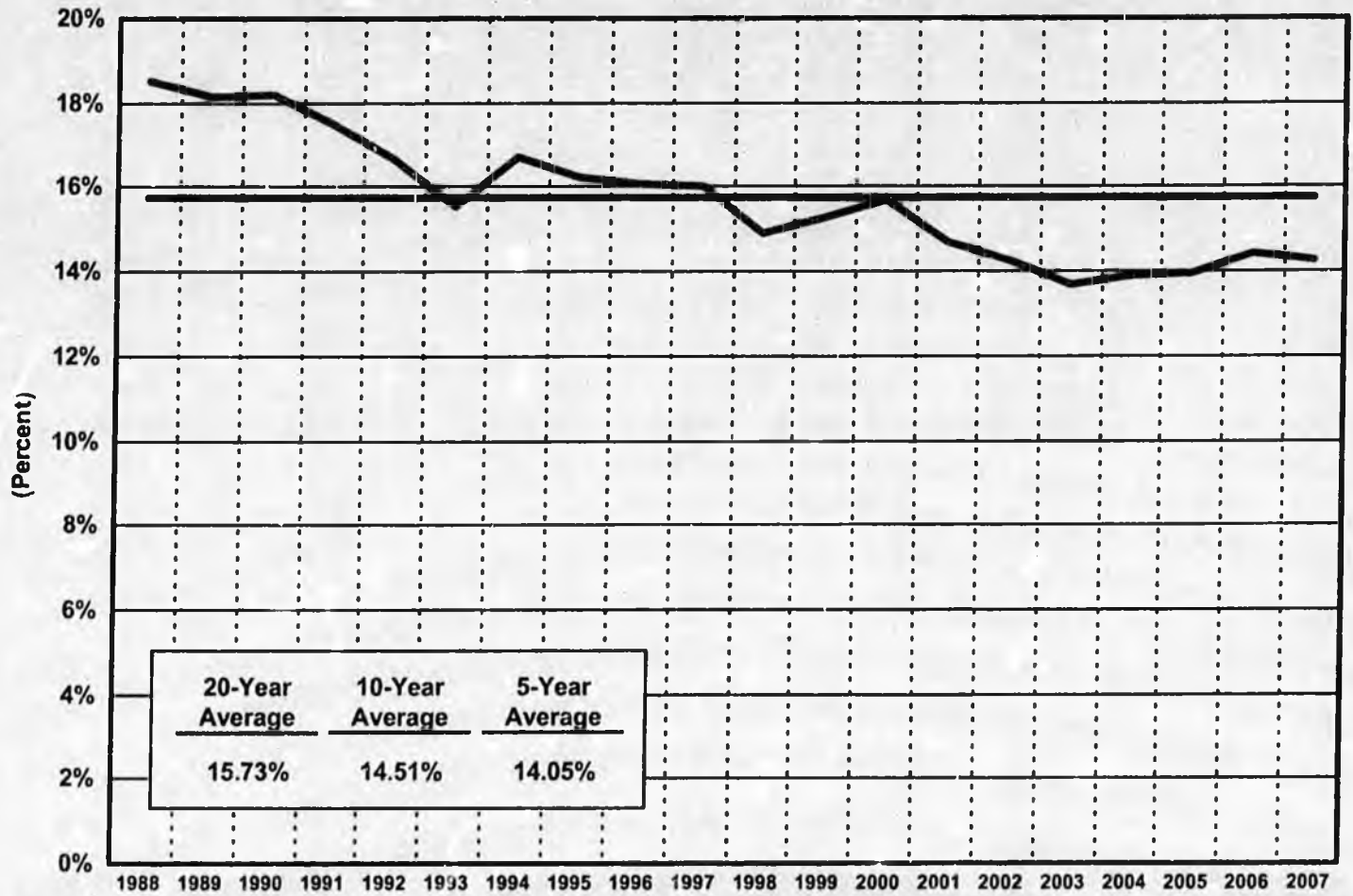
-- Rates Using Historical Premiums over Inflation --

	<u>20-Year Average</u>	<u>10-Year Average</u>	<u>5-Year Average</u>
	(1)	(2)	(3)
<b>Inflation Projection</b>	<b>2.50%</b>	<b>2.50%</b>	<b>2.50%</b>
<b>Risk-Free Premium</b>	<b>3.00%</b>	<b>2.10%</b>	<b>1.13%</b>
<b>Margin</b>	<b>0.50%</b>	<b>0.50%</b>	<b>0.50%</b>
<b>Total</b>	<b>6.00%</b>	<b>5.10%</b>	<b>4.13%</b>



# Equity Costs

## 965 Basis Points Above Historical 10-Year T-Bond Rates



Source: Federal Reserve Bank.



# Potential Equity Return Under Proposal

-- Rates Using Historical Premiums over Inflation --

	<u>20-Year Average</u>	<u>10-Year Average</u> (Percent)	<u>5-Year Average</u>
	(1)	(2)	(3)
<b>Inflation Projection</b>	<b>2.50%</b>	<b>2.50%</b>	<b>2.50%</b>
<b>Risk-Free Premium</b>	<b>3.00%</b>	<b>2.10%</b>	<b>1.13%</b>
<b>Equity Premium</b>	<b>9.65%</b>	<b>9.65%</b>	<b>9.65%</b>
<b>Total</b>	<b>15.15%</b>	<b>14.25%</b>	<b>13.28%</b>



# Key Elements of Recourse Rate Tariff

(cont'd)

- **Depreciation will be on straight-line basis over 25 years (i.e., 4% per year)**
- **Operating costs, income and other taxes are passed on to shippers**
- **Fuel gas will be recovered from shippers based on actual pipeline losses**
  - **4.40% GTP**
  - **2.15% Alaska & Yukon-BC Sections**
  - **0.90% Alberta Section**
- **Shippers retain title to natural gas liquids entrained in the gas and are free to dispose (i.e., sell or process them as they see fit)**

# Negotiated Rate Tariffs

- **Most new pipeline construction works off negotiated tariffs**
- **TransCanada proposes to offer 25, 30 and 35-year negotiated tariffs**
- **TransCanada proposes that its negotiated rates would incorporate:**
  - **Levelized tariff**
  - **70% debt / 30% equity capital structure through date of operation, falling to a 75% debt / 25% equity capitalization for period of operation**
  - **Expansions would be 60% debt / 40% equity structure**
  - **Equity and Debt rates proposed are the same as for recourse rates (i.e., 965 basis points over cost of 10-year T-Bond and actual debt costs)**
  - **Return on Equity reduction offered for negotiated rates**
- **In addition, TransCanada proposes to use U.S. loan guarantees to finance cost overruns if available**

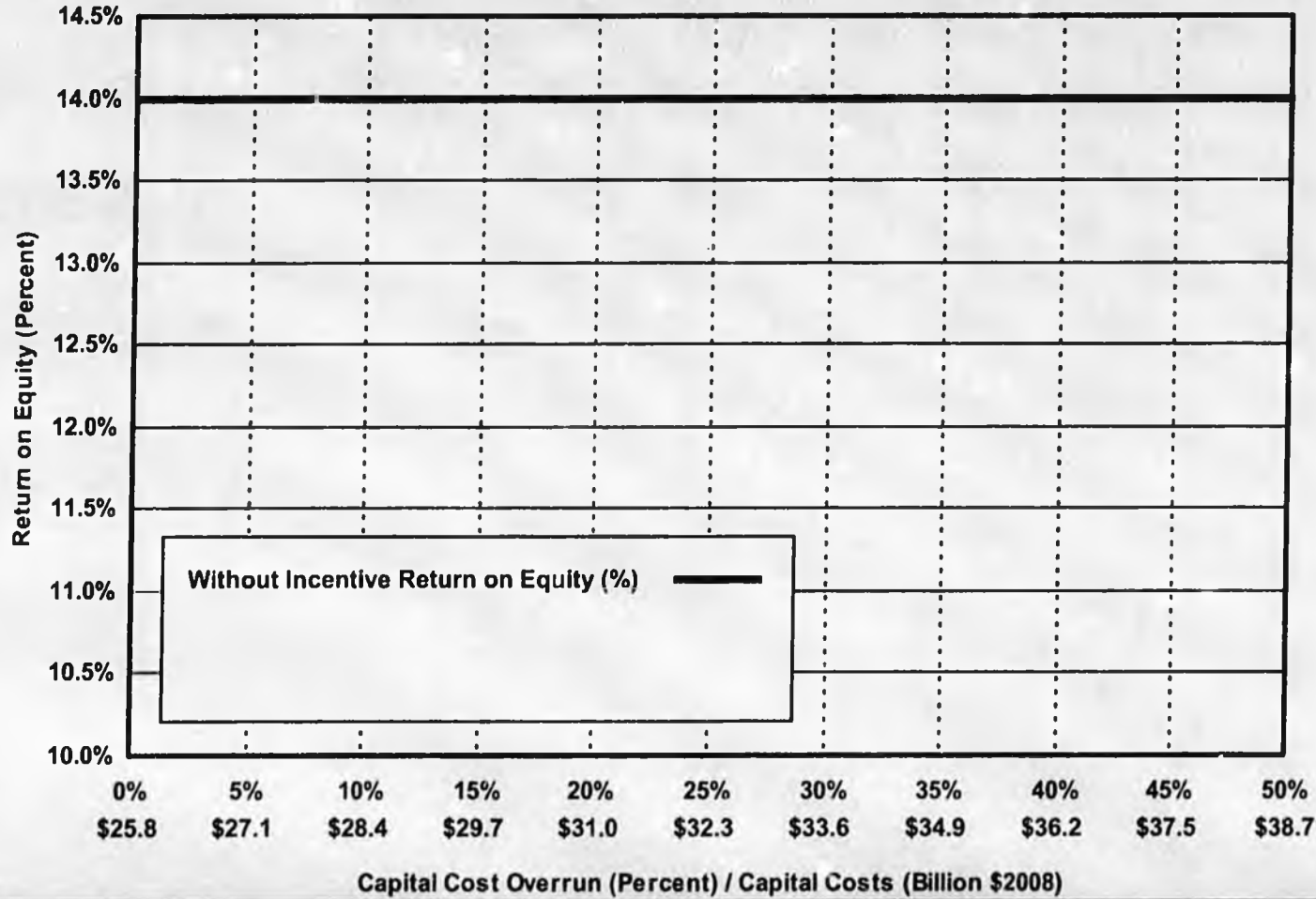
# Negotiated Rate Tariffs

(cont'd)

- Shipper must agree to accept treatment of rolled-in rates under AGIA
- Shipper must agree not to seek or support changes to the economic parameters that underpin the negotiated rate design at FERC and NEB
- Notwithstanding the terms offered by TransCanada, the actual terms to be negotiated between shippers and TransCanada, with the exception of those mandated under AGIA, such as treatment of rolled-in rates, are open for negotiation
- There is no requirement to accept the economic parameters proposed by TransCanada. Shipper can bargain for lower rates, increased flexibility, and alternative vehicles for protection against cost overruns than those offered
- See earlier differences in Recourse and Negotiated Rates
- TransCanada proposes to offer equity ownership in the pipeline "Anchor" shippers who subscribe in the initial Open Season

# Incentive Adjustments to Return on Equity

Assumes 75% debt / 25% equity



# Incentive Adjustments to Return on Equity

Assumes 75% debt / 25% equity

