ALASKA NATURAL GAS
TRANSPORTATION PROJECTS
OFFICE OF THE FEDERAL COORDINATOR

Oct. 7, 2011

Senator Lesil McGuire
Alaska State Legislature
716 W. 4th Avenue, Suite 430
Anchorage, AK 99501-2133

Dear Senator McGuire:

As I read (and have re-read) your letter of August 9, I looked to the fact that a key element of the federal Alaska Natural Gas Pipeline Act of 2004 (which created this office) was a presumption "that a public need exists to construct and operate the proposed Alaska natural gas transportation project" to make North Slope gas available to markets in the Lower 48. But Congress also understood that Alaska consumers need access to North Slope gas as well. To that end, the act included language requiring that the project also address in-state needs. To help make the project feasible, the act authorizes generous federal financial assistance through a multibillion-dollar loan guarantee.

The Alaska Legislature's approval in 2007 of the Alaska Gasline Inducement Act was consistent with the objectives of the federal act, and signaled the state's willingness to materially assist in developing the project envisioned by Congress — and long envisioned by Alaskans.

When the Alaska Legislature sent HB 369 to the governor in April 2010, it marked a shift by the state to a more aggressive approach to securing in-state access to North Slope gas. You were a co-sponsor of that bill and, as you note in your letter — and as you have repeatedly pointed out in various legislative deliberations — nothing in that legislation directs a shift against the objectives established by Congress or the state's longstanding goal of a large-diameter gas line to serve out-of-state markets. To the contrary, HB 369 directs that the plan for development of an in-state natural gas pipeline be "compatible but not competitive" with the project envisioned by Congress to bring North Slope gas to the larger North American market.

As the Alaska Gasline Development Corp. July 1 report stated, the larger pipeline project envisioned by Congress would likely bring natural gas to Fairbanks and Anchorage at "significantly lower cost" than the far smaller in-state project analyzed by AGDC. And, as ADGC stated, its project was never intended to compete with a large-diameter pipeline. In accordance with the mandate of House Bill 369, the smaller in-state project analyzed by AGDC is being developed "as a fallback."[1]

[1] AGDC Report, p. 3-12.

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The report concludes that the in-state pipeline could conceivably be designed, financed and built by the private sector, but acknowledges that "in all probability [that] will not happen," at least not in the timeframe envisioned.

State involvement may be the answer, the report said. AGDC correctly notes that a larger state financial commitment to the project than the almost $400 million presumed in the report might be required to move the in-state gas line to actual construction. AGDC interviewed officials with 11 North American pipeline companies to get their opinions of the project. Without identifying who said what, AGDC reported the following comments:

- The state could demonstrate its faith in the project "by assuming some of the transportation commitment risk and backstop a shortfall in capacity if it exists after an open season." The report states that 20-year shipping commitments for 100 percent of the pipeline capacity will be needed to secure attractive financing.

- Acknowledging the risk that the actual pipeline costs could greatly exceed the planning estimates, the best way to mitigate the risk would be to develop a tariff structure that recovers all costs, including any overruns, from the pipeline users. Most of the pipeline companies said they would be reluctant to accept the risk of construction cost overruns, "and many expressed the opinion that the State of Alaska should participate through both a capital subsidy, if necessary, and through firm transportation bids of royalty gas to help guarantee capacity."

- "Most of the builder/owner/operators said that the State of Alaska needs to wholly subsidize the project development costs before a successful open season," the report said. (This is similar to the $500 million in cost reimbursement the state pledged to AGIA licensee TransCanada to help cover development costs of the larger pipeline.)

- The report also warns that more state financial involvement may be necessary: "It is important to note that preliminary feedback from potential builder/owner/operators indicates that their appetite for certain risks is very limited. If that feedback is confirmed through the process of selection and negotiation with a builder/owner/operator, then more state involvement will be necessary to complete the project."

The July AGDC report suggests that a backstop commitment by the state of up to $7.5 billion might necessary to move the in-state project forward.

You asked whether the Office of the Federal Coordinator had considered potential synergies between the TransCanada/ExxonMobil larger pipeline (AGIA) and the smaller in-state line (AGDC). More specifically, you asked if we could identify any financial means or other ways in which the state's efforts to meet the need for gas within Alaska could be combined with the state's concurrent efforts to promote a major pipeline into North American markets, thereby improving the odds of success for both.

The answer, hopefully, is yes. Alaska needs both projects, and both projects are linked by the same source of gas; the same daunting economic hurdles; and much of the same engineering, permitting, routing and timing issues. They are especially linked by the reality that each project makes the other one more economically and politically attractive to Alaska. The lowest-cost gas for Alaskans would come from tapping into the economies of scale of the larger pipeline. And the money to help pay for that in-state distribution system could come from the public revenues that would be earned from a large-volume pipeline taking Alaska gas to market.

The Federal Coordinator's office is sponsoring a public forum on the questions raised in your letter to help people look at the issue, consider the options and the benefits of state financial involvement in a gas line. The forum is scheduled for 5:30 to 7 p.m. Tuesday, Oct. 18, at the University of Alaska Anchorage Fine Arts Recital Hall. We have contracted with Gavel-to-Gavel for a live video stream on the web and later rebroadcast on statewide television.

We will have a report available at the forum, setting out the issues and presenting some options for Alaskans to consider.

I offer the services of our office to assist you and your colleagues and the governor as you work toward finding the best answer to Alaska's energy and fiscal future.

Sincerely,

Larry Persily
Federal Coordinator
Alaska Natural Gas Transportation Projects

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SENATOR LESIL MCGUIRE

August 9, 2011

Mr. Larry Persily
Office of the Federal Coordinator
Alaska Natural Gas Transportation Projects
1717 H Street NW, Suite 801
Washington, D.C. 20006

Dear ~~Mr.~~ Persily, Larry

Thank you for the work you have done to ensure federal cooperation and assistance for a large-diameter pipeline to move Alaska North Slope gas to Lower 48 markets. As you know, the Alaska Gasline Development Corporation (AGDC) recently released a plan for the Alaska Stand Alone Pipeline (ASAP) project which included preliminary cost estimates, financing alternatives and an assessment of environmental, market and technical issues for an in-state line. Over the next few months the Alaska State Legislature and the Governor will be reviewing this report and considering what, if any, actions need to be taken to further the project while, at the same time, working on the Alaska Pipeline Project (APP) licensed under the Alaska Gasline Inducement Act (AGIA).

As policymakers evaluate the ASAP report and continue to monitor progress on APP, there will be a tendency for some to continue to pitch one project against the other. Doing so ignores the cooperative operating environment in which both are currently being developed. I fear that if Alaskans characterize the projects as competing prospects we could miss opportunities to fully develop North Slope gas and thereby minimize the benefits of gas development to Alaskans and our nation.

As you are well aware, it was I who insisted on the inclusion of language that directed the AGDC to prepare a plan that was “compatible not competitive” with the AGIA project. I fought for this language because I felt that it was important to avoid costly litigation that could cause unnecessary delays for both projects and because I truly believe that the two efforts, if developed in concert, could complement each other and ensure gas deliveries to Alaskans and the Lower 48 states.

Has the Office of the Federal Coordinator (OFC) generally considered potential synergies between the APP and ASAP projects? More specifically, has your office identified or could you identify financial means or other ways in which the State of Alaska’s efforts to meet the need for gas within Alaska could

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be combined with the state's concurrent efforts to promote a major pipeline into North American markets, thereby improving the odds of success for both?

Again, the Office of the Federal Coordinator has been an invaluable resource for Alaskans and I have greatly appreciated the public forums and educational opportunities you have provided for the public. Any information you could provide that could help Alaskans evaluate these projects in a holistic context would be greatly appreciated.

Thank you for your continued service.

Sincerely,

Lesil

Alaska State Senator Lesil McGuire

Senator.Lesil.McGuire@legis.state.ak.us