

**Resource Development Council – Alaska Support Industry Alliance
May 11, 2010 – Anchorage, Alaska**

**Larry Persily, Federal Coordinator
Alaska Natural Gas Transportation Projects**

Thank you for that welcome. I wish I had something equally enthusiastic to offer in return.

I look out and see 200 of you who paid \$35 or \$40 each to hear my opinions. I've got to tell you, no one has ever paid that much to hear me before. I gave away my opinions for free in newspapers, on radio and TV and at luncheons for years. If I had known you were this loose with your money, I would have started charging long ago.

I wonder — could I get a show on Fox?

Let's talk about the gas line.

I'm not here to tell you it will be built this decade. But I assure you it is not dead; shale gas has not driven a silver stake through the Alaska pipeline; the market has not forgotten us. It may not be paying as much attention as we would like, but that could change.

Patience.

A national commitment to using more natural gas to keep the lights on, computers running and air conditioners cooling could help the outlook for the Alaska pipeline.

The natural gas share of U.S. electrical generation doubled between 1990 and 2009, climbing from 12 percent to 23 percent. Power generators were the only gas customers to increase their use during that period — industrial demand has been dropping for the past 15 years. Commercial and residential demand has been essentially flat, and most analysts expect those trends to continue.

It's that trend in power generation that gives us hope. Cambridge Energy Research Associates forecasts another doubling in gas demand from electrical utilities by 2030.

Anyone who has ever tracked the accuracy of the state's oil price forecasts — especially the ones I worked on — knows the further out they go, they less accurate they are. But Alaska really needs those strong electrical demand forecasts to come true.

Natural gas is cleaner burning than all other hydrocarbon fuels for electricity, except the state-owned Healy coal plant — which isn't emitting any pollution.

A new, combined-cycle natural gas-fired power plant emits one-third as much carbon dioxide as the average U.S. coal-fired plant. And no soot or mercury.

So why haven't all of the nation's electrical utilities abandoned coal and switched to natural gas?

Coal is cheap, abundant, domestic. Its price has been much more stable over the years than gas. It employs an awful lot of workers in a lot of states, plus it has the backing of the railroads that haul all that coal.

You haven't seen an effective lobbying campaign until you have stood in front of a fully loaded coal train pulling out of Wyoming or West Virginia, heading for Congress.

And, yes, the coal industry is working to clean up its emissions. It will continue as a key source of power generation for decades.

Maybe the best political hope for the natural gas industry — the best hope for the Alaska pipeline — is for gas to capture future growth in generating capacity and the conversion of older coal-fired plants ready for retirement.

That is happening. Calpine, which recently purchased several generating plants from Mid-Atlantic power company Pepco, announced it will convert two coal-fired stations to gas. Canada's Atco Power said it would convert its coal plants in Alberta if it can get long-term price stability on gas supply contracts.

The Canadian government is considering making gas-fired power plants the national standard. Canada's environment minister met last month with the owners of 51 coal-fired power plants to talk about converting older units to gas.

The biggest boost to gas demand for power plants could come from the president's energy policy that is built in great part on cleaner-burning natural gas — and domestic sources for that gas.

I have met with the president's top energy advisor and senior White House staff, and I can tell you the president supports the Alaska pipeline and wants his staff to look for ways the federal government can help bring all the players together for success.

I didn't move to Washington for the farm-raised salmon served in East Coast restaurants. I moved there to push the limits of my authority toward helping the project.

Among the pieces that have to fall into place is price stability. As Atco's chairman said, it makes no sense to build a 1,000-megawatt, gas-fired power plant if you don't know what your fuel costs will be.

Utilities like stability; their customers like stability; but the gas market has been anything but stable in the past decade.

Shale gas is changing that. It's making gas buyers feel more comfortable that all that new supply will put an end to price volatility. Alaska gas may be able to come along for the ride. We can grab a piece of the market so long as our gas can be delivered for the market price — nothing more.

North Slope producers, pipeline owners and the state may have to accept less profit from the gas than they would like. If shale is going to hold down prices in North America long term, and if Alaska is to get a pipeline, everyone involved in the project will have to accept the prospect of tighter profit margins. Everyone one at the table will have to acknowledge the risks and share in them.

Looking at the potential pipeline tariffs presented by the two project proponents, it could cost \$4 to \$4.50 per thousand cubic feet to clean and transport North Slope gas all the way to Lower 48 markets. That doesn't leave much, even if gas recovers to a long-term range of \$6 or \$7, as many expect.

Construction cost overruns could destroy the margin.

Gas prices below projections could ruin the project's economics.

The pipeline cannot afford any more risk than it already has.

This year's two open seasons to solicit shipper interest in the line will tell us how the market views the project.

One open season closes the end of July; the other is expected to close in early October. Unlike oil and gas lease sale bids, the envelopes will not be opened to the public the minute after bidding closes.

The pipeline developer and potential shippers will enter closed-door commercial negotiations. Those could last several months, without a word publicly of what's going on.

Maybe we'll know something early next year; maybe not.

Alaskans need to understand silence does not mean failure; it just means there isn't any immediate good news.

If shippers and a pipeline developer can reach a tentative, conditioned deal, it would be filed with the Federal Energy Regulatory Commission and subject to public disclosure.

The process is similar to an earnest money deal on a house — you negotiate a price with the seller, conditioned on the appraisal, the engineer’s inspection, getting a loan, a move-in date, and whatever else you want to put in the offer.

The open season is just a step.

A couple of points about shale gas before I move on.

Yes, it will be a dominant force in meeting U.S. energy needs for decades to come. The “shale gale,” as it is called, is producing close to 15 percent of domestic gas flow.

But shale gas is not perfect.

The U.S. House Energy and Commerce Committee and the Environmental Protection Agency are reviewing the practice of hydraulic fracturing — when drillers inject millions of gallons of water and a blend of chemicals deep underground to fracture the shale so that the gas can escape.

A lot of residents living near shale gas plays are worried about water quality. Nowhere is drilling more controversial than in New York and Pennsylvania, which sit atop the massive Marcellus Shale. The Pennsylvania House voted last week 157-33 to stop any further leasing of state forest lands for gas exploration.

New York State has closed two watersheds to drilling.

Even in Texas, some residents above the Barnett Shale are questioning the wisdom of putting gas wells in residential areas amid worries of air and water quality.

And although shale gas is much closer to market than Alaska, its production costs are much higher.

Dealing with all that water is costly, especially handling produced water from the well. Whether treating it or storing it deep underground — either way it’s expensive.

A typical deep shale gas well needs 5 million gallons of water for drilling and fracking — that’s as much as an average golf course uses in a month.

Some would say that means golf courses use too much water, but in deference to my golfing friends I’ll move on.

Meanwhile, Alaska is not the only player that needs new pipe. Ours may be the longest, and certainly the most expensive, but all that shale gas needs a way to market, too.

Shale gas needs investment dollars. The nation's pipeline companies added \$27 billion in new pipe nationwide the past three years, with \$6 billion more expected this year.

Those new pipes will move Rockies gas to California and as far east as Ohio, while taking shale gas from Louisiana and Arkansas to market, and moving Marcellus gas to East Coast buyers.

And there is the issue of the Gulf of Mexico oil spill. Some are saying public reaction to offshore drilling will drive public support toward an onshore gas pipeline.

Maybe, maybe not. But so what?

Public opinion will not decide the future of the Alaska pipeline; the market will decide whether it gets built.

A chorus of cheers for onshore gas and a chorus of boos for offshore oil are not going to change the economics of the project.

I'd suggest people stop speculating about how the gulf spill might or might not affect the gas line and return to reality: The project is huge, the risks are massive, and the line needs more than someone else's misfortune to succeed.

The Senate Energy Committee last week recommitted its support for boosting the project's federal loan guarantee to \$30 billion, from the old cap of \$18 billion. Now we just need to wait for Congress to pass the energy bill — no easy feat, I'll admit.

Meanwhile, officials in Washington and Ottawa are working on the project, making plans for the permit applications they hope will be filed, getting together to identify problems and starting to solve them now, not later.

The Office of Federal Coordinator is ready, too.

In addition to bringing together agencies to ensure that permit applications proceed smoothly, we're working up a prototype of something called GIS mapping. We've taken a 20-mile-long section in the Atigun Pass and built up an incredible amount of data sets, layering them on top of each other to show terrain, geology, cultural sites, ground cover, water, slopes and more. The prototype will soon be available online for everyone to see.

My hope is to push for funding to provide such detailed mapping for the entire pipeline route in Alaska.

That would be a route into Canada and points south. The law that established the Office of Federal Coordinator is clear: The office is to assist in a pipeline that brings North Slope gas to the Lower 48.

An exclusively export project is not entitled to the loan guarantee or permitting assistance of the Alaska Natural Gas Pipeline Act of 2004.

I know, however, that many Alaskans are as enthusiastic over shipping Alaska LNG to Asia Pacific markets as they are pessimistic of a pipeline to the Lower 48.

Let me share some facts with you about an exclusively export market for Alaska gas.

North America consumes three times as much natural gas in an average day as Japan, Taiwan, China, South Korea and India combined. That's not denying that the Asia Pacific market is growing faster than the North America market — it is.

But an Alaska LNG project would have to grab a much bigger share of that growth to be viable than taking a small slice of the much larger U.S. market.

More than 90 percent of the world's gas was delivered by pipeline in 2007; just 8 percent by LNG tanker.

Alaska gas has a lot of low-cost competition in the Asia Pacific LNG market — Australia, Papua New Guinea, Indonesia, Malaysia, Russia and Qatar — none of which need an 800-mile pipeline through the Arctic to get their gas to a liquefaction plant at tidewater.

The Asia Pacific market is in the middle of an LNG supply boom, with new projects totaling 16 billion cubic feet per day coming online between last year and 2015.

Not to mention that China and India are trying to develop their own domestic production, and each has pipeline options to LNG.

And for those who look at past long-term contracts, where gas prices have been linked to oil, generating huge margins for LNG, look again. Spot market and short-term sales contracts now comprise almost 20 percent of the Asia Pacific LNG trade — and growing.

Projections of eternal profits from LNG linked to high oil prices could be wrong.

Remember predictions just a few years ago of a foreign LNG wave hitting the U.S., filling in for declining North American production? Promoters tried selling LNG receiving terminals up and down the West and East Coasts.

They were wrong.

One of the losers was a company that spent six years pushing an LNG receiving terminal near the mouth of the Columbia River; it filed for bankruptcy last week, with \$130 million in debts. It had a FERC license, but no gas supply, no gas buyers, no financing.

I can't leave without commenting on the push to build a smaller pipeline to serve Alaskans. While I understand the frustration that has led to the proposal, I caution Alaskans to be careful.

The pipeline right of way from the North Slope is only so wide; there are only so many good spots for construction camps, gravel pits and a gas treatment plant. There also are concerns about a safe separation from the oil pipeline, blast radius, and other issues.

Be careful to make sure one dream doesn't get in the way of another dream.

A large pipeline moving gas out of state is Alaska's best bet for tens of billions of dollars in tax and royalty revenues, the availability of gas for in-state use and the lowest tariffs for in-state deliveries. Anything else comes up short in one of those categories.

For those who have written off the chances of a large steel pipe moving Alaska gas to the Lower 48: What if you're wrong?

ExxonMobil, BP, ConocoPhillips and TransCanada have spent in the neighborhood of \$400 million total since 2000 to look at the viability of the project. They're still looking, still spending.

Wait for the open seasons to close, wait for the commercial negotiations that will follow. Wait to see what the producers ask of the state. Wait to see what the White House can do to help.

And wait to see what the nation does about reducing carbon dioxide emissions and turning to natural gas.

If it doesn't work, I'll be the first to admit it. But it's worth waiting just a little bit more.