AGIA
Legislative Special Session

Incentives and Mandates for Pipeline Expansions

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AGIA "Must Haves" Regarding Expansion

- Bi-annual Open Season Offerings
  - Allows shippers to plan, reduces risk premiums
- Capital Structure Certainty
  - Helps to lower rates for shippers
- Rolled-in Rates
  - Shares the benefits of scale economies, level playing field

Producer incentives for pipeline development investments are different than for expansion

Development

- Cost control
- Operating control
- Capacity certainty
- Expansion timing
- Strategic

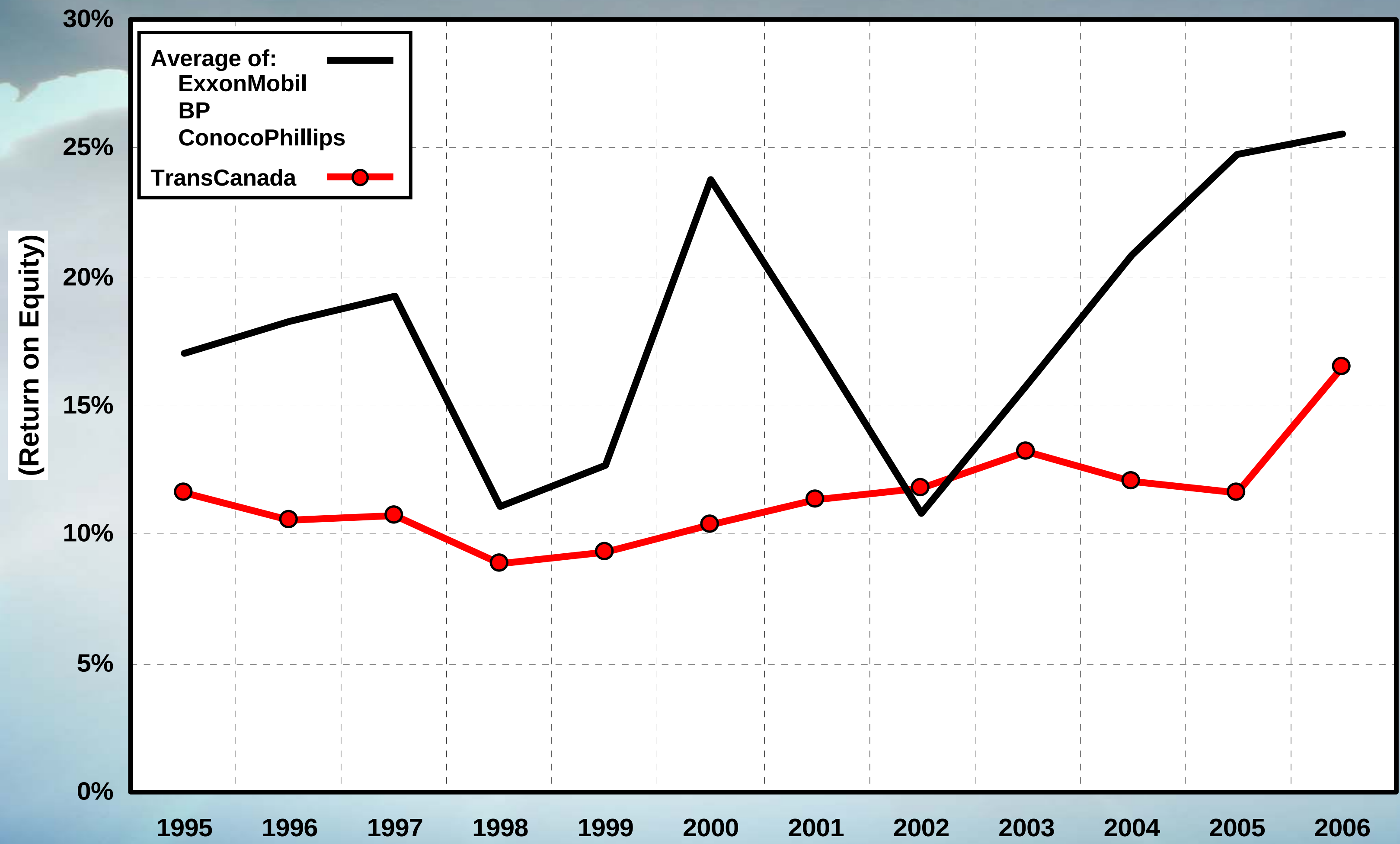
Expansion

- Outlet for increased equity production
- ?

Pipeline v. Producer Returns on Equity

- Gas pipeline regulated rates of return on equity (ROE) generally recognize lower levels of operating risks than other industries
  - FERC ROEs of 14% or less are common
  - ROEs granted to pipelines prior to in-service are often reduced in subsequent rate cases
- Exploration and Production company shareholders require relatively higher (15% – 20%+) ROEs to compensate for higher perceived risks

Producers Shareholders Expect Higher ROEs than do Pipeline Companies



Source: Value Line (March 16, 2007).

What is a producer pipeline's incentive to expand pipeline capacity for non-owners?

- ROEs typically will not meet a producer's required rates of return on capital
- Potential for increased competition in lease acquisition and reserves development
- Call on capital that is needed for other purposes
- It is not what they want to do (core competence)
- Regulatory complications