Stranded Gas Hearings

(0409011330 Minutes)

The Lower 48 Market for Alaska Natural Gas
John Carruthers, VP Upstream Development

JOHN CARRUTHERS, Vice President, Upstream Development, Enbridge Pipelines, Inc. ("Enbridge"), echoed earlier comments stating that the Lower 48 market is large and growing. He said that Enbridge recognizes the importance of Alaskan gas to those in Alaska based on the attendance of these meetings. However, it's more important for the Lower 48 consumers, who need to play a role. Although there needs to be greater recognition of that role, there are significant hurdles to achieve it. In fact, Enbridge would be one of the players. In order to place Enbridge's position in context, Enbridge participated as an owner in the Alliance Pipeline System that moves liquid rich gas from the western Canadian sedimentary basin to Chicago. The aforementioned gas has characteristics similar to those one would see in Alaska gas. Furthermore, Enbridge brings market perspective to the table in that Enbridge is the owner of Canada's largest LDC. In that vein, Mr. Carruthers turned to the earlier concern regarding the viability of the indices. He pointed out that Enbridge participates in those indices as a buyer, and characterized the indices as generally a very sufficient and sophisticated tool, though there has been some improvement with regard to [the transparency of the indices]. As long as the [indices] are liquid enough, which can be the case for Alberta and Chicago, it should be sufficient for [Alaska].

MR. CARRUTHERS noted the following potential end-use shippers: LDCs, power generators, marketers, large industrial users, and government as a commercial entity. He then focused on LDCs since they will be the key [end-use shipper]; as stated in a Purvin & Gertz study: "LDCs are one of the few market participants with the creditworthiness, client base, and commercial interest to encourage investments with long-term contractual support and/or equity participation. Their support is required to ensure adequate gas supply in a timely fashion." Mr. Carruthers opined that the aforementioned summarizes the issue from a Lower 48 market perspective. He said that there isn't much argument with regard to the need for gas in North America. In fact, most studies would say that over the next 10 years, approximately 15 bcf a day of new supply is needed, which would include Alaska's supply. What's important to note is that Alaska gas can economically access a lot of the market, the Midwest and Northeast in particular.

MR. CARRUTHERS turned to who could and who is going to take the risk on a pipeline. If one thinks of the benefits to consumers of an Alaska gas project with costs approaching $20 billion, the benefits to consumers are far more [than the cost]. The NPC study specified that consumers would see a price reduction of $.60-$.80 for three to four years after the arrival of Alaska gas to the market. Therefore, Alaska gas would be positive for consumers in the amount of approximately $50 billion. He noted that further studies have supported the aforementioned analysis. Although Alaska gas would be approximately 5 percent of the total supply, it impacts all gas. Mr. Carruthers specified that some consideration should be given with regard to the volume and the price that can be committed, as well as to contract length, delivery points, and regulatory acceptance of long-term capacity commitments. He noted that during the era when there was more supply than demand, contract lengths were shortened and some utilities were penalized for having long-term contracts.

MR. CARRUTHERS addressed market participation in supporting and taking on some of the risk in Alaska gas. Marketers have played a diminished role and they are unwilling to commit to long-term contracts. Therefore, sellers would probably hesitate to sell to marketers on a long-term basis unless they met some credit hurdles. The LDCs would like to commit to long-term contracts, but are restricted from doing so by public utility commissions. In order to commit to a long-term contract, there must be assurances that those contracts would be supported in future rate cases. However, there have been cases in which there weren't assurances and, as a result, there was an economic impact. Based on today's market, there has been little willingness to commit to fixed-price commodity contracts. It's easier to have floating price contracts with the liquid hubs. The aforementioned is exacerbated by the fact that Alaska gas remains in the future. "So, you've got the added complexity ... [of] going into a long-term contract but the first day of that isn't for a few years, so that does make it even more difficult," he opined.

Even with the FERC's attempts to streamline, there has been an increase in legal challenges resulting in delay. However, the energy bill, should it pass, addresses a number of those issues.

MR. CARRUTHERS relayed that Enbridge does see a need for long-term contracts. Although historically the producers have been the one to take the position on the pipe, he opined that in this case there is the potential, because of the significant benefits to consumers and lack of known long-term resources, for the consuming end to take a position on the pipeline. The aforementioned would require a shift in policy. The NPC study emphasized the aforementioned in the following quote:

> New pipeline and storage infrastructure are generally financially supported by long-term contracts for a period of ten to twenty years. Companies are less willing to invest dollars in needed infrastructure if contract durations for existing or new pipeline/storage capacity are shortened by the impact of regulatory policies.

MR. CARRUTHERS said, therefore, that [Enbridge] has been focusing on whether the regulatory policies can be changed such that people could take a position. Because Alaska's resource is large and well known, there isn't the risk that occurs in some basins in which the gas still has to be found. He further explained that in Alaska's case, the cost of the pipeline is the market risk.

MR. CARRUTHERS moved on to in-state market participation, and informed the committee that currently, Enbridge is actively reviewing a spur line to Anchorage/Kenai. The spur line depends upon the quality of gas on the market side, the projected growth rate, and the existing infrastructure in terms of distribution. If the aforementioned is considered during the initial development of a gas pipeline, it could be more economic than if it is simply an add on. Mr. Carruthers noted that Enbridge will continue to also look at the Lower 48 market. He expressed the need to reaffirm that Enbridge believes there is potential for the market to share a risk in the Alaska gas pipeline by taking a shipping commitment. Although it makes sense conceptually, there are many regulatory hurdles that would be fairly time consuming. "But we do think that does align Alaska and the producers interests in the pipeline, and we could share risk more broadly," he said. He noted that Enbridge is reviewing that very notion to determine the amount of risk it might take and under what conditions.

SENATOR SEEKINS turned attention to the Enbridge slide entitled, "Alaska Gas is Good for Lower 48 Market". He said he understood Mr. Carruthers to say that delay in this construction project raises prices for the consumer in the short-term. Would that be the case in the long-term, if this project came on-line in two years, he asked. If so, would it be in the best interest of an owner of a large supply of natural gas to delay construction of the project.

MR. CARRUTHERS replied no, adding that one would have to have an expectation that prices will increase at an even more significant rate. Mr. Carruthers said that he didn't expect people to delay [construction]. Furthermore, if prices increase too highly, demand will go offshore, from which it takes some time to recover. High prices could also result in fuel substitution or other "infrastructure builds." Therefore, if people don't foresee Alaska gas on the horizon, more LNG, coal, or nuclear may be developed. Mr. Carruthers opined that there is some risk of waiting too long.

SENATOR THERRIAULT asked if there is anything that the state controls in its regulatory scheme that could be problematic.

MR. CARRUTHERS reiterated that long-term commitments on gas have been discouraged. In this era, he said, he believes the utility commissions need to review things that support new sources of gas.

SENATOR THERRIAULT posed a situation in which there is more of a push for new power generation to use natural gas. However, natural gas isn't tied into long-term contracts, and this results in price fluctuations. The American consumer is accustomed to, and expects, a very level price per kilowatt from the producers. He asked if that dynamic will have to change as more generation moves over to natural gas, and therefore moves to more long-term contracts in order to ensure stability.

MR. CARRUTHERS opined that consumers would become more and more frustrated with the high prices and the volatility, both of which are [reduced] by long-term secure sources of gas, adding that Alaska provides the aforementioned.