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Governor Bill Walker STATE OF ALASKA

June 15, 2015

The Honorable Kathy Giessel
Alaska State Senate
716 W. 4th Ave. Suite 511
Anchorage AK, 99501

The Honorable Benjamin Nageak
Alaska State House of Representatives
State Capitol Room 126
Juneau AK, 99801

The Honorable Dave Talerico
Alaska State House of Representatives
1292 Sadler Way Suite 328
Fairbanks AK, 99701

Dear Senate and House Resource Committee Chairs and Co-Chairs:

I want to inform you about the efforts of my administration to move the AK LNG project ahead. Attached is my letter dated June 8, 2015 to the heads of the producers' negotiating teams for the AK LNG project. We have identified a lack of urgency in the parties' resolution process. The methodology that the AK LNG team adopted for identifying problems and issues is excellent. However, there does not appear to be much process associated with resolving issues between the parties, and certainly not one with a sense of time urgency.

It is time to build this gas pipeline to Nikiski, and therefore the state needs to take the lead and proactively mediate and find resolutions within a time frame that will keep the project on schedule. The attached letter proposes a time frame and process for moving the issues to resolution.

To date, the producers have been working towards a 2nd quarter-2016 FEED decision. This meshes efficiently with a fall special session for legislative review of the proposed agreements. It also works well should voter consideration of a November 2016 constitutional amendment be required in addressing the fiscal certainty needs of the project. For these reasons, schedules should not be allowed to slide. Assuming that all the producers match the State's commitment to commercialize North Slope gas, we must push ourselves to close out these issues.

The attached letter identifies the key issues requiring resolution and the state's position on those issues. My hope is that with clarity of focus and attention, the producers and the state can stay the course on their intended timeline and give Alaskans a gas pipeline project from the North Slope to Nikiski that will provide the next generation the revenues they need to build a prosperous future.

Sincerely,



Bill Walker
Governor

cc: Janet Weiss
Dave VanTuyt
Joe Marushack
Pat Flood
Bill McMahon
Jim Flood

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Governor Bill Walker
STATE OF ALASKA

June 8, 2015

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Joe Marushack & Pat Flood
ConocoPhillips Alaska, Inc.
P.O. Box 100360
Anchorage, AK 99510-0360

Bill McMahon & Jim Flood
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22777 Springwoods Village Parkway
Spring, Texas 77389

Dear AK LNG Sponsors:

A few weeks ago, we jointly set a goal to finalize the term sheets for all major project enabling contracts by the middle of June. It is now June 8th. Despite the efforts of all parties, it is clear we are not on schedule to achieve this goal.

There are at least two major issues and at least three smaller major issues. I have summarized the State's listing of those issues along with my comments.

I am asking that this list be considered by the VAMOU on Tuesday to determine if consensus can be reached on the completeness of the list. The goal would be to gain agreement on a final list of major issues in order for our respective negotiating teams to share a common focus and issue prioritization. The resulting list would then be presented at the Sponsor Meeting on Wednesday with the Sponsor representatives tasked to resolve these major issues – especially the two large major issues. Resolution of these major sticking points will be a catalytic event enabling substantial progress on finalizing the terms of the project contracts.

To the extent there are issues remaining after the Sponsor Meeting where the parties are substantially apart, I would like the State to engage in a shuttle diplomatic effort with producers, with a goal of gaining issue closure or at least a clear understanding of the extent of remaining disagreement. Following the best efforts of our teams to reach closure on the major issues, I

would like to meet face to face during the week of June 15th with each Sponsor executive individually to attempt to resolve the remaining issues. I would like to resolve the major issues in these meetings so we can begin the process of drafting contracts

The AK LNG team will be briefing the Legislature on the 16th of June in Kenai, Alaska. After months of expectation, the people of Alaska and their elected representatives are anxious for concrete progress.

Large Major Issues

1. The largest issue is Joint Venture Marketing vs. Equity Marketing. The State believes it will be very difficult, if not impossible, for this project to proceed with the PBU and PTU fields with all the current participants outside a Joint Venture Marketing context.
2. Upstream issues – to the extent they are not resolved by Joint Venture Marketing. Most of the remaining upstream issues can be resolved through the use of separate Joint Ventures that would receive the gas from the PBU and PTU fields with support between the two Joint Ventures along the lines of the proposal attached as Appendix A.

Other Major Issues

3. Fiscal Stability: It will only deal with the gas dedicated to this Project from PBU and PTU. It will not include oil. The State is willing to consider a 25 year term in order to facilitate integrated project financing. The State believes a Constitutional Amendment will provide the certainty that all parties would like. Attached as Exhibit B is an example of what I envision the constitutional amendment might look like.
4. 48 inch line: Constructing a 48 inch line will alleviate the issues of open access and expansion. The Producers have stated they do not need or want a 48 inch line. The State is willing to pay for this expansion subject to legislative approval, but it would own all the benefits of the increased size. The State would also pay for installing the valves, pads etc. to accommodate four more compressor stations that will be added when demand exists from new developments or fields. The State intends to use this expansion capacity to encourage open access.
5. East vs. West Cook Inlet crossing: It is my understanding that the studies for the two routes are under way but that the tentative conclusion at this point in time is that the Western Route is the preferred alternative. The Matsu Valley constitutes the second largest population base in the State of Alaska and has some of the highest industrial potential in the State. Consequently, the State strongly prefers the Eastern Route since the studies to date do not indicate any insurmountable obstacles. Also, the Eastern Route will better enable this Project to better fulfill the statutory domestic gas mandate.

Sincerely,



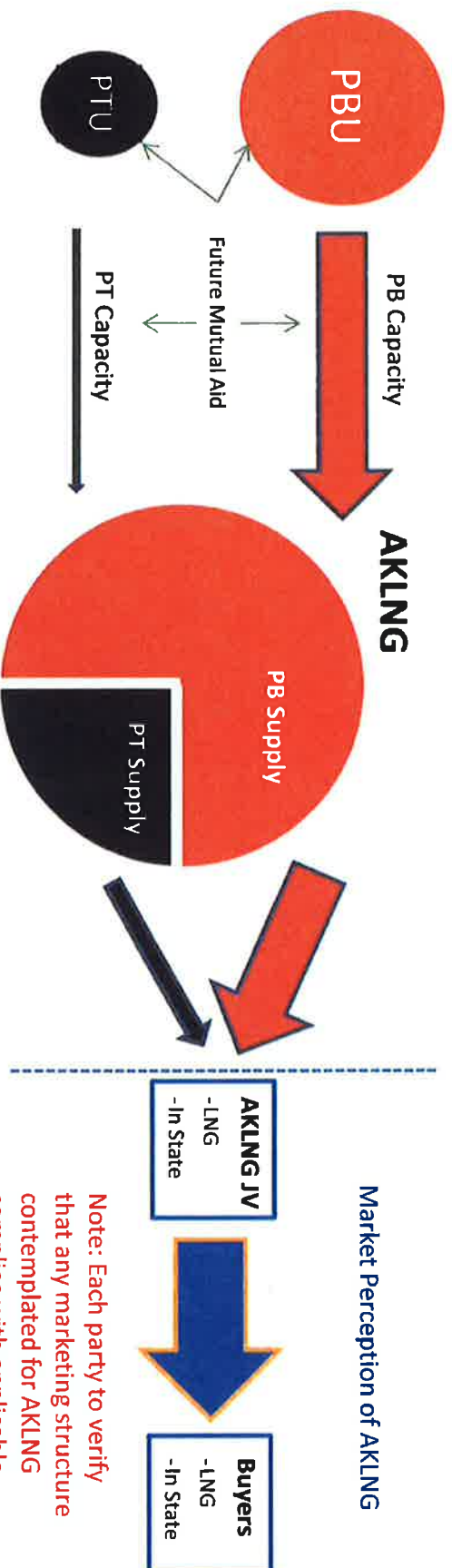
Bill Walker
Governor

Enclosure

Appendix A – Joint Venture Marketing Model

Appendix B – Sample Draft Constitutional Amendment

cc: Dona Keppers, SOA, Deputy Commissioner of Revenue
Dan Fauske, AGDC
Steve Wright, SOA, Department of Natural Resources
Audie P. Setters, SOA, Gas Team, General Manager



Note: Each party to verify that any marketing structure contemplated for AKLING complies with applicable anti-trust laws

Less complex than any acceptable FSA solution proposed to date

- Can explain to buyers, lenders and other State stakeholders
 - The JV revenue flows back to Titleholders in proportion to their respective participation
 - Any JV costs (including SPA penalties) flow back to Titleholders in proportion to their respective participation
 - The JV nominates supply from each Unit, and takes title at entry point to the relevant Transmission Line
- Gas Balancing and Mutual Aid:
- One month of borrow/loan gas each year for operational issues:
 - to be repaid in kind within one calendar year;
 - In place for 15 years after start-up
 - One time gas purchase option (approx. 2 months of PTU downtime):
 - 80 BCF (20 cargos) on an energy basis
 - Expires lesser of 5 years after triggered or year 15.
 - JVs can “bank” gas to ensure access to additional future gas;
 - Good faith mutual assist provision to ensure JVs avoid reputational damage to AKLING (dropped cargos)

APPENDIX B

Sample Draft Constitutional Amendment

* Section 1. Article IX, Constitution of the State of Alaska, is amended by adding a new section to read:

Section 18. Suspension of Taxation by Contract Authorized by Law. Contracts approved by a majority of the legislature and entered into by the executive branch by December 31, 2017 to provide fiscal terms for a liquefied natural gas project, including a gas treatment plant, gas pipelines, and a liquefied natural gas plant and related facilities, as provided by law are constitutional under this article. Such contracts as originally executed shall be binding upon future legislatures as to terms of gas taxation, but any amendments to such contracts executed between the parties shall not bind future legislatures as to any aspect of taxation.