From the desk of ***Richard A. Fineberg***
P.O. Box 416, Ester, Alaska 99725
Phone / Fax (907) 479-7778 ◦ E-mail: fineberg@alaska.net

July 29, 2008
(Rev.)

Senator Fred Dyson
Senate Special Committee on Energy
Juneau, Alaska 99811

Re: Additional Questions About Confidentiality and Gas Pipeline Tariffs

Dear Senator Dyson:

Thank you for taking the time yesterday afternoon to follow up on my testimony last Friday and allowing me about my concerns about confidentiality and natural gas pipeline tariff data. As I have testified, I am sensitized to this issue by my experiences on TAPS. I recognize that the natural gas regulation regime is different; my intent is to share, as fully as possible in the limited time available to us, the importance of understanding how these nuts and bolts issues may affect policy deliberations. TAPS history aside, this letter focuses primarily on current AGIA-related issues. Based on the feedback during my testimony and our conversation yesterday, I remain in disagreement with the assumption that we can proceed safely now and fix these problems somewhere down the road.

You mentioned during our discussion yesterday that the AGIA statute provisions should resolve my concerns about confidentiality. On further review of the statute, I believe my concerns stand. I will deal with the specifics of the AGIA statute below. But first I must ask a critical question that, as far as I can tell, does not appear addressed by this statute:

Do confidentiality grants by other state statutes and agencies and federal statutes and agencies reduce the effectiveness of this statute in making data available?

Based on work in TAPS – and, over the years, in various other venues[1] – I have seen this problem occur a number of times. When this problem occurs, busy state analysts simply may not have the time to obtain the information that would be required to get to the questions of concern and the critical information does not make it into the policy record. And because confidentiality has narrowed the world of players in this arcane game, those who might have critical facts or might

[1] It should be noted that through the years I have also had occasion to work intensively with state and federal agencies – sometimes for extended periods and, occasionally, in the private sector – on a variety of other Alaska, national and transnational petroleum revenue and development issues.

understand the implications of the missing information are excluded and are unable to give policy makers the assistance they need.

The AGIA Statute:

Now, to the provisions of the AGIA statute itself:

AS 43.90.150 *(Proprietary information and trade secrets: Applicant requesting confidentiality must demonstrate information is proprietary and confidential. (b) Commissioners (jointly) make the determination)*
– HB0177F, p. 11

- *Since one commissioner alone cannot determine that that the applicant has failed to demonstrate the information is proprietary, rejection of a asserted confidentiality requires individual determinations by personnel from both departments. But joint departmental proceedings are administratively complicated and require individuals from two departments to divert from their statutory assignments. These considerations raise two questions:*
  - *If applicant raises a confidentiality exclusion, will the over-worked personnel in two agencies both be able to (1) recognize the potential significance of the withheld data and (b) delve into the detail necessary to determine the necessity to defeat that barrier?*
  - *Does the confidentiality assertion reduce the number of persons who have sufficient background to recognize that a potential problem may exist, thereby making it unduly difficult for the state to raise the question?*

AS 43.90.220 *(Records, reports, conditions, and audit requirements.)*
– HB0177F, p. 16

220 (c) . . . *enables commissioners to conduct hearings and investigative inquiries, compel attendance and production of documents regarding "information relating to the project."*

In view of Commissioner Galvin's acknowledgment that he would think carefully the interests of the partners before challenging at FERC, in the search for information necessary to support that challenge:

- *Does this provision enable the commissioners to obtain information about other financial arrangements between shippers and the pipeline companies (for example, loan guarantees and repayment terms, etc.) that might be tied to pipeline-related arrangements?*
- *How does this language guarantee timely production of the required information. Does the general desire to complete the project as soon as possible tilt the playing field against challenges that might slow the project down?*

220(d): . . . between license and commencement of commercial operations, state shall have seat at the table, receive all relevant notices, enjoy same access as equity owners, receive reports or information "the commissioners reasonably request."

– HB0177F, p. 16

- *Why doe the state's seat at the table end with "commencement of commercial operations"?*
- *Can the state effectively monitor operating agreements, including tariffs, (say) ten years from now?*

220(e) *. . . all proprietary, privileged and trade secrets information "received . . . by the commissioners" are not subject to public disclosure.)*

– HB0177F, p. 17

- *Does this clause undercut Sec. 150 by broadly applying the exception to AS 40.25 to "all" documents rather than limiting withholding from the public disclosure to the documents determined by the commissioners to have demonstrated that the information in question is proprietary, privileged or a trade secret to meet the definition, as spelled out in Sec. 150(b)?*

- *Should there be a clause that requires aggregated, summary data on pipeline operations relevant to tariffs to be prepared for public disclosure?*

AS 43.90.900 (Definitions)

(6) *"commissioners" means DOR and DNR, "acting jointly."*

– HB0177F, p. 29

- *It is truly wonderful to see the agencies working together under the Palin Administration. But this question remains: In view of the constraints that necessarily exist, does the necessity for commissioners to act jointly reduce the possibility of gathering the information necessary to protect state interests in a timely manner?*

(20) *"proprietary" information means "treated by an applicant as confidential" and "public disclosure . . . would adversely affect the competitive position of the applicant or materially diminish the commercial value of the information to the applicant."*

– HB0177F, p. 30

- *By this definition, an illegitimate deal benefiting the applicant could be deemed proprietary. Here's a hypothetical example of a transaction whose disclosure arguably "would adversely affect the competitive position of the applicant or materially diminish the commercial value of the information to the applicant:" An over-reported contractor cost*

could increase the contractor's payment (through its profit element on a fixed rate of return contract), constituting a legal kick-back that could artificially inflate pipeline costs, to the benefit of the pipeline company and, consequently, its financiers, while reducing reported project NPV and, in train, state royalty and production tax payments.

- *Given the questions about field costs that necessitated correction of the PPT bill in the ACES special session last fall, it is difficult to believe that the state is suddenly able to combat such machinations on a project of this financial magnitude and geographic scope.*

The Alliance Example

In consideration of the Alliance Pipeline, I believe we may have stumbled upon precisely the kind of problem that received insufficient attention, despite the impressive teamwork and effort that the administration has poured into the AGIA process. When I asked about the Alliance case, a knowledgeable administration analyst responded dismissively that Alliance tariffs went up because of cost overruns. Wait a second: Are we suddenly not worried about cost overrun effects on pipeline tariffs?

When I pushed this question further, the administration representative countered that even a producer-owner would have no incentive to increase costs on a pipeline because the pipeline rate of return is regulated and therefore significantly lower than the internal rate of return that a producer seeks. This is an impressive assumption that requires accepting a host of other implicit assumptions to reject two other reasonable hypotheses:

(1) the possibility that a producer might view the pipeline guaranteed rate of return as a portfolio hedge or cash-flow insurance policy during periods when natural gas prices – which are notoriously volatile – crater; and

(2) producers may be motivated – at least in part and perhaps to a significant degree – by the drive for basin control.

I would very much like to believe that the AGIA team did work through these issues carefully and accord them the weight they deserve. But I see no sign of this in the AGIA presentations. And it is difficult for me to accept this proposition when the question Senator Wielechowski asked me in the hearing Friday about independent v. producer-owned pipelines led to two pieces of apparently conflicting summary data that: (1) did not identify Alliance's unusual position in the pipeline world and its significance in to our deliberations; (2) did not identify for the consideration of policy makers the importance of cost overruns on Alliance, or their apparent tariff effects.

Please do not misunderstand: I am not tendering my limited research on the Alliance issue as the reason for my concerns. Rather, I revisit Alliance issues

because they illustrate the kind of issue whose significance may be overlooked when confidentiality and complexity combine to overload state policy makers, their staffs and their consultants.

In any event, I hope these questions will be of use to you in your deliberations today.

Sincerely,

Richard A. Fineberg

Cc: Senator Charlie Huggins, Chair
Senate Special Energy Committee