



Interior Energy Project

Quarterly Report to the Alaska State Legislature Interior Energy Project

April 23, 2019



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LIST OF ATTACHMENTS

Attachment A: House Bill 105 Plan Memorandum

ACRONYMS LIST

DOT&PF	Alaska Department of Transportation & Public Facilities
AIDEA	Alaska Industrial Development and Export Authority
AS	Alaska Statute
FA	Financing Agreement
FEED	Front End Engineering and Design
FID	Final Investment Decision
FNG	Fairbanks Natural Gas
FNSB	Fairbanks North Star Borough
HB	House Bill
Hilcorp	Hilcorp Alaska, LLC
IEP	Interior Energy Project
IGU	Interior Gas Utility
LNG	Liquefied natural gas
Mcf	Thousand cubic feet
MOU	Memorandum of Understanding
PACE	Property Assessed Clean Energy
Pentex	Pentex Alaska Natural Gas Company, LLC
PSA	Purchase and Sale Agreement
RCA	Regulatory Commission of Alaska
RUS	Rural Utilities Service
SETS	Sustainable Energy Transmission and Supply Development Fund
SLA	Session Laws of Alaska
Titan	Titan Alaska LNG, LLC
USDA	United States Department of Agriculture

INTRODUCTION

House Bill (HB) 105 passed the 29th Alaska Legislature on April 27, 2015, and was signed into law on June 30, 2015. This legislation was enacted to renew and advance the Interior Energy Project (IEP), a project designed to bring low-cost energy to as many residents and businesses of Interior Alaska as possible, as quickly as possible. The financing package refreshed by this legislation provided the Alaska Industrial Development and Export Authority (AIDEA) the tools necessary to develop an integrated supply chain bringing lower-cost energy to residents and businesses through local utilities.

A critical component of the original financing for the IEP was the ability to provide financing for the project that would permit the development of a unified gas utility with competitive rates (Chapter 26, Session Laws of Alaska [SLA] 2013). The passage of initial legislation in 2013 provided AIDEA with several financial tools and a designated deposit of \$125 million into the Sustainable Energy Transmission and Supply Development Fund (SETS; Alaska Statute [AS] 44.88.660). The legislation included a limitation on interest charged for the project financing and an allowance for AIDEA to waive “any limitations or requirements of its regulation that are otherwise applicable to the Alaska Industrial Development and Export Authority sustainable energy transmission and supply development fund.” This language was retained in the IEP financing tools when HB 105 became law on June 30, 2015, expanding the possible sources of energy for the project.

HB 105 required AIDEA to provide written quarterly reports to the Alaska State Legislature on the status of the IEP. The specific bill language includes:

“The Alaska Industrial Development and Export Authority shall submit quarterly to the legislature a written report on the Interior Energy Project. The authority shall deliver the report to the senate secretary and the chief clerk of the House of Representatives and notify the legislature that the report is available. The report must include:

- (1) a description of project progress on all components;*
- (2) an update on the status of local distribution infrastructure buildout;*
- (3) to-date and anticipated conversions; and*
- (4) a financial accounting of funds expended and funds anticipated to be spent, including loans, grants, and bonds.”*

On September 21, 2017, the AIDEA Board considered and approved a development plan that met the requirements of HB 105 outlined above. Reaching this milestone provided the Authority access to the remaining IEP financial tools. AIDEA continued to advance IEP goals by pursuing consolidation of the existing natural gas utility infrastructure owned by AIDEA under Pentex Alaska Natural Gas Company, LLC (Pentex), with infrastructure owned by the Interior Gas Utility (IGU).

A copy of the HB 105 Plan Memorandum is included with this report as Attachment A. The projected cost of delivered natural gas to residential customers, from the HB 105 Plan Memorandum, is included as Table 1. Information contained in Table 1 is based on expectations of customer conversions reduced to 50 percent over an 8-year period due to a lower price of fuel oil.

Table 1: Summary Cost of Gas with Storage Tax Credit¹

Summary Cost of Gas - With Storage Tax Credit										
Anticipated Demand (Bcf)	0.75	0.75	1.19	1.83	2.55	3.25	3.90	4.41	4.75	4.95
Cost of Gas (\$/Mcf nominal)	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Natural Gas - Cook Inlet	\$7.72	\$7.72	\$7.72	\$7.72	\$7.87	\$8.03	\$8.19	\$8.36	\$8.52	\$8.69
Pipeline Trans. Cost to Pt. Mac. (3rd-party)	0.65	0.66	0.68	0.69	0.70	0.72	0.73	0.75	0.76	0.78
LNG Production - Titan Plant	4.28	4.34	3.22	2.53	2.19	2.02	1.92	1.88	1.87	1.89
Trucking - Pt. Mac. To Fairbanks	2.48	2.53	2.58	2.63	2.68	2.73	2.79	2.84	2.90	2.96
Subtotal - Cost to Utilities	\$ 15.12	\$ 15.25	\$ 14.19	\$ 13.57	\$ 13.45	\$ 13.50	\$ 13.64	\$ 13.83	\$ 14.06	\$ 14.32
Distribution, Storage, Vaporization	4.76	4.85	3.13	2.07	1.51	1.21	1.03	0.93	0.88	0.86
Total Cost of Gas before Financing	\$ 19.88	\$ 20.10	\$ 17.31	\$ 15.64	\$ 14.96	\$ 14.71	\$ 14.67	\$ 14.76	\$ 14.94	\$ 15.18
Debt	-	-	-	0.72	0.51	0.40	0.43	0.78	1.34	1.69
Total Cost of Gas (nominal)	\$ 19.88	\$ 20.10	\$ 17.31	\$ 16.35	\$ 15.48	\$ 15.11	\$ 15.10	\$ 15.54	\$ 16.28	\$ 16.87
Total Cost of Gas (real)	\$ 19.11	\$ 18.94	\$ 16.00	\$ 14.81	\$ 13.74	\$ 13.16	\$ 12.88	\$ 13.00	\$ 13.36	\$ 13.57
Equivalent Fuel Oil Price (nom. \$/gal)	\$ 2.74	\$ 2.77	\$ 2.39	\$ 2.26	\$ 2.13	\$ 2.08	\$ 2.08	\$ 2.14	\$ 2.25	\$ 2.33
Equivalent Fuel Oil Price (real \$/gal)	\$ 2.64	\$ 2.61	\$ 2.21	\$ 2.04	\$ 1.90	\$ 1.81	\$ 1.78	\$ 1.79	\$ 1.84	\$ 1.87
Planned Average Customer Rates*	\$20.20	\$20.20	\$17.31	\$16.35	\$15.48	\$15.11	\$15.10	\$15.54	\$16.28	\$16.87
Equivalent Fuel Oil Price (nom. \$/gal)	\$ 2.79	\$ 2.79	\$ 2.39	\$ 2.26	\$ 2.13	\$ 2.08	\$ 2.08	\$ 2.14	\$ 2.25	\$ 2.33
*Differs from Total Cost of Gas in 2018 and 2019 due to utility consolidation										

¹The projected cost of delivered natural gas to residential customers is based on 2015 analysis contained in the HB 105 Plan Memorandum.

The supporting documents for the HB 105 plan can be downloaded at www.interiorenergyproject.com/resourcesanddocuments.html.

This is the fifteenth quarterly report submitted under the requirements of HB 105. Each section of the report corresponds to one of the four items required by the legislation. This report augments information previously provided and covers the period from January 1, 2019, through March 31, 2019.

DESCRIPTION OF PROJECT PROGRESS ON ALL COMPONENTS

The IEP effort is structured on the following project components: Supply, Liquefaction, Transportation, Distribution (including Storage and Regasification), and Conversions.

Following negotiations in 2016, a non-binding Utility Integration Memorandum of Understanding (MOU) was approved by the IGU and AIDEA Boards in January 2017. The purpose of the MOU was to provide guidance and structure for a separate Financing Agreement (FA) and Purchase and Sale Agreement (PSA), designed to form a single, investment-grade natural gas sourcing and distribution utility within the Fairbanks North Star Borough (FNSB) through the sale of the AIDEA-owned Pentex Natural Gas System, commonly referred to as Fairbanks Natural Gas (FNG), to IGU.

Negotiations continued on the FA, PSA, and supporting documents through much of 2017. Work concluded in November 2017, leading to IGU Board approval of the FA and PSA on December 5, 2017, and AIDEA Board approval on December 7, 2017. The PSA and FA, as authorized, were signed on December 13, 2017. The signed PSA and FA can be found at www.interiorenergyproject.com.

Although the PSA and FA were signed in December, IGU approval was contingent on a final vote of the utility Board prior to the target closing date of May 31, 2018. Final closure of the utility consolidation was extended to June 14, 2018, by mutual consent of AIDEA and IGU, due to last-minute discussions. With these negotiations concluded, the IGU Board approved finalization of the consolidation deal on June 12, 2018, and the closing documents were signed on June 13, 2018. Under the terms of the PSA and FA, the IEP will now

progress utilization of the project financing authorized under Chapter 26, SLA2013, and capital funds appropriated in Sec. 11, Ch. 38, SLA2015, page 32, lines 17–25.

As required by HB 105, the status of Supply, Liquefaction, Transportation, Distribution (including Storage and Regasification), and Conversions is summarized below.

Supply

Titan Alaska LNG, LLC (Titan), a Pentex subsidiary, has a natural gas supply contract with Hilcorp Alaska, LLC (Hilcorp), to provide the current liquefaction facility with natural gas until March 31, 2021. This “All Requirements” Agreement provides Titan with enough capacity (5 million cubic feet/day) for its existing customers, and allows for the expansion of up to 15 million cubic feet/day upon 18 months’ advance notice to Hilcorp.

IGU has initiated discussions with potential natural gas producers for long-term supply to begin in spring 2021. IGU considered securing natural gas under terms of a possible liquefied natural gas (LNG) supply contract as described in the next section; however, IGU has terminated these discussions.

Liquefaction

Under the terms of the signed FA and PSA, steps are being taken to finalize the optimal design and commercial structure to increase the availability of LNG from the Titan plant through a Front End Engineering and Design (FEED) process. IGU contracted Braemar Technical Services to perform the FEED work. Braemar Technical Services began the work in late March 2019. At the completion of FEED, a determination will be made regarding whether to make a Final Investment Decision (FID). If the FID is approved, a commercial solicitation will be initiated to increase the capacity of LNG available for shipment to Interior Alaska. This agreed-upon plan and scope for expansion of LNG production capacity may be modified by mutual consent of IGU and AIDEA.

In addition to the Titan expansion evaluation, IGU engaged in discussions on an unsolicited proposal for LNG supply delivered to Fairbanks by Siemens Government Technologies, Inc. (Siemens) and the Knik Tribe. Siemens and IGU entered into an MOU to negotiate a long-term LNG supply agreement at a firm, fixed price. Unfortunately, after significant and good faith efforts to reach an agreement, Siemens and IGU were unable to come to terms for an LNG supply contract. Accordingly, IGU has determined that owning the liquefaction assets is in their best interests and, as a result, has ended their mutual efforts under the MOU.

LNG expansion under ownership and control of a consolidated natural gas utility structure will necessitate access to AIDEA project bonds that were pre-authorized with the passage of Chapter 26, SLA2013. HB 119, passed by the Alaska Legislature on May 12, 2018, extends access to the bonds for the purpose of project financing through June 30, 2023.

Transportation

Rail Option Update

IGU continues to explore the potential for shipments of LNG with the Alaska Railroad Corporation as part of the overall IEP effort. As work proceeds to increase LNG storage capacity in the FNSB, consideration will be given to facilitate delivery by rail in the future.

Trucking Update

The fleet has seen the addition of large-capacity Heil Trailers, which are also in service to transport LNG. These trailers are configured to facilitate the addition of a hitch at a later date, which will allow pulling an additional “pup” trailer if this proves to be feasible and is determined to be economically advantageous. Titan also utilizes two Kenworth T-800 trucks fueled by LNG as part of its fleet.

Distribution

Systems Expansion

No major changes have been made to the distribution system since the October 1, 2015, *IEP Quarterly Report*. Detailed maps of the build-out accomplished in 2015 are included in that report, available at www.interiorenergyproject.com.

IGU is continuing to work with the City of Fairbanks, FNSB, and Alaska Department of Transportation & Public Facilities (DOT&PF) during the road construction season to perform pipe installation in conjunction with road construction.

In December 2017, the AIDEA and IGU Boards agreed to initiate construction of a 5.25 million gallon LNG storage tank. Following a competitive Request for Proposals process, Preload Cryogenics was selected as the primary Engineering, Procurement, and Construction contractor for a facility with a double-walled, full-containment design.



Exterior view of the 5.25 million gallon LNG storage tank - Q1 2019

Work on the expanded LNG storage project continues on schedule. Construction on the project foundation began in January 2018 and progressed rapidly. As of April 1, 2019, the outer and inner tanks are substantially complete. Additionally, the final phase of the Balance of Plant work is underway, including final construction of pipe trench and installation of major components such as boil-off gas compressors, vaporizers, offload skid, electrical, and controls. The LNG storage project has a target completion date of fall 2019.

Design and engineering for an initial LNG receipt, storage, and regas facility located in North Pole are complete. IGU requested bids for the construction of the facility and is in the process of assessing these bids. The project is strategically located at this site in order to provide service using the distribution lines pre-installed in North Pole. The site can also facilitate service to the Golden Valley Electric Association generation plant in North Pole.

Systems Consolidation

A separate PSA and FA were signed on December 13, 2017, after having been negotiated over the course of the previous calendar year. These documents allow the consolidation of AIDEA-owned Pentex assets and IGU assets into a single, investment-grade, natural gas sourcing and distribution utility within the FNSB. Closure under these contractual agreements was anticipated to take place before May 31, 2018.

The deadline was extended, however, and closing documents were signed on June 13, 2018.

Legal representatives for AIDEA and IGU worked closely to compile the documents necessary to close the utility consolidation deal. The entities advocated for expedited consideration of Docket U-18-001 before the Regulatory Commission of Alaska (RCA) to allow the transfer of the FNG Certificate of Public Convenience and Necessity to IGU. The docket was approved by the RCA on April 30, 2018.

Conversion

Efforts to assist consumers with conversion to natural gas have centered primarily on access to favorable financing mechanisms and identification of possible low-cost loan funds. Work has also been done with



Interior tank suspended ceiling lowered into place – Q1 2019



Final inner tank row - Q1 2019

furnace and boiler manufacturers regarding new boiler components that may reduce the cost of individual customer conversion to natural gas.

Consumer Interest in Conversion Assistance

The Cardno Entrix *Interior Energy Project Natural Gas Conversion Analysis*, finalized in January 2014, identified a high level of interest in converting to natural gas as a lower cost, cleaner source fuel for space heat if the delivered price approached the target of \$15 per thousand cubic feet (Mcf). At the time the Cardno Entrix analysis was performed, many homeowners indicated a desire to forego financing conversion, and instead expressed a willingness to fund this action from personal savings due to the high cost of fuel oil. For individuals without personal funds for this purpose, the ability to finance all, or a portion, of the cost over an extended period scored high as a necessary tool to support their conversion to gas.

The ability to pass the obligation for repayment of conversion financing to a new owner, at the time of sale of a building, proved to be very attractive to residential owners. The ability to spread natural gas conversion costs over a 10- to 20-year period and the use of transferable financing are both attributes of two energy efficiency financing mechanisms described below that have achieved widespread use across the continental United States.

The current lower price of fuel oil increases the importance of conversion assistance that will incentivize property owners in the FNSB to switch to natural gas when it becomes available. With this in mind, the original Cardno Entrix estimates were recalculated to reflect more conservative rates of customer conversion based on lower fuel oil prices. However, just as the price of home heating oil declined unexpectedly, the future price is uncertain.

Property Assessed Clean Energy Financing

Property Assessed Clean Energy (PACE) is a means of financing improvements that increase the energy efficiency of commercial buildings. The improvements are financed with repayment accomplished through a voluntary assessment placed on the annual property tax bill. PACE financing is often structured to allow a longer payback period than is possible with conventional business loans. The strength of the PACE collection mechanism results in low-default/low-risk loans, which may justify a lower interest rate.

PACE legislation (HB 80) was passed by the 30th Alaska Legislature on April 17, 2017. HB 80 was signed into law on October 6, 2017. The Alaska Energy Authority is working with municipalities to determine how to best implement the law.

On-bill Financing

In order to remove ambiguity regarding the allowance of on-bill financing in Alaska, HB 374 was introduced on February 21, 2018. On-bill financing allows utility customers to borrow funds that are repaid via a voluntary line item added to their standard utility bill. This financing mechanism is often used by utilities to assist new customers in overcoming the initial cost of accessing a utility service.

Funds for on-bill financing may be provided by the utility itself or in conjunction with local, private sector financial institutions. Previous conversion surveys and focus group work performed as part of the IEP indicated that access to such a transferable financing mechanism would help incentivize

conversion to natural gas. Coupling this tool with low-cost loan funds will be helpful. HB 374 was approved by the Alaska Legislature on May 12, 2018.

Identified Funding Sources for Conversion Assistance

The Local Conversion Working Group has identified the following possible funding sources for conversion assistance:

- I. Commercial lenders
 - a. Commercial loans as part of a community-wide conversion program
- II. Local government
 - a. PACE-enabled conversion loans
 - b. Possible local government back-stop funding for PACE loans
- III. State sources
 - a. Air quality programs
 - b. Community Development Block Grants
- IV. Federal sources
 - a. United States Department of Agriculture (USDA) Rural Utilities Service (RUS) Energy Efficiency and Conservation Loan Program
 - b. USDA RUS Rural Energy Savings Program loans
 - c. Clean Water Fund
 - d. United States Environmental Protection Agency Targeted AirShed Grants
 1. Funding for the targeted airshed grants was increased to \$40,000,000 by federal budget action.

UPDATE ON THE STATUS OF LOCAL DISTRIBUTION INFRASTRUCTURE BUILD-OUT

No major changes were made to the distribution system in the last quarter other than work with the City of Fairbanks, FNSB, and DOT&PF to coordinate pipe installations that could be efficiently constructed in tandem with roadwork occurring in the FNSB. Detailed maps of the build-out accomplished in 2015 are included in the October 1, 2015, *IEP Quarterly Report*.

TO-DATE AND ANTICIPATED CONVERSIONS/CONNECTIONS

To-Date Conversions/Connections

Due to limited gas supply, no conversions are currently occurring. Until the supply is increased, there is not sufficient gas in winter to ensure uninterrupted service to additional customers. Expanded distribution lines installed previously have been pressurized and are available to supply gas to homes and businesses when additional natural gas is available.

Anticipated Conversions

The number of anticipated conversions provided in the October 1, 2015, *IEP Quarterly Report* was based on the analysis undertaken by Cardno Entrix. The report assessed “willingness to convert” based on a number of factors related to conversion costs, prior conversion history, survey data, and potential savings.

A copy of that report can be found

at interiorenergyproject.com/Resources%20and%20Documents/IEP_Conversion_Analysis_Final.pdf.

The significant change in the price of heating fuel required a fresh look at the “willingness to convert,” with specific attention paid to the closing of the cost gap between heating fuel and the IEP natural gas price targets. Cardno Entrix was engaged to update the analysis of “willingness to convert” based on a range of scenarios of lowered heating oil prices. In the most conservative scenario, expected conversions were projected to drop by approximately one-third from the original analysis.

The change in projected “willingness to convert,” combined with an extension of the time needed to reach conversions from six years to eight years, results in a revision to the number of anticipated conversions and the anticipated demand for the project. Table 2 depicts the anticipated number of conversions, by year, based on the revised Cardno Entrix analysis.

Table 2: Natural Gas Customer Projection¹

	2015	2016	2017	2018	2019	2020	2021	2022	2023
FNG	959	959	1,506	2,183	3,031	3,732	4,362	4,635	4,807
IGU	-	-	167	576	1,285	2,255	3,502	4,818	5,998

¹ Due to project delays, the first year in customer growth is not expected to occur until 2020.

Anticipated/Potential Connections

The anticipated mission expansions to the Department of Defense bases in the FNSB provide an opportunity to add significant natural gas demand for the consolidated utility system by installation of natural gas heating systems in the new housing units that will be required. The IEP team is working with the FNSB and the cities of Fairbanks and North Pole to explore mechanisms to ensure that those new housing units use natural gas space heating. Options to be considered include incentives (e.g., reduced cost connections) and potential building code or other mandates. The financial viability of the consolidated FNSB natural gas utility—and its ability to offer low rates attractive enough to drive conversion of existing residences—can be substantially enhanced by adding demand from the new housing units.

FINANCIAL ACCOUNTING OF FUNDS EXPENDED AND FUNDS ANTICIPATED TO BE SPENT, INCLUDING LOANS, GRANTS, AND BONDS

Table 3 outlines the IEP expenditures related to the \$57.5 million capital appropriation, the \$125 million of SETS fund capitalization, and the \$150 million of SETS bond authorization.

Table 3: Expenditures from and Remaining Funds of Legislative Appropriation & Authorization(s)

Expenditures* from and Remaining Funds of Legislative Appropriation & Authorization(s):				
	HCS CSSB 18 \$57.5 mill Cap Approp	SB 23 SLA 2013 \$125 mill SETS	SB 23 SLA 2013 \$150 mill Bonds	Total
Development Costs	IEP Phase 1 (Pre HB 105)			
	LNG Plant	7,585,150	-	7,585,150
	North Slope Pad	6,003,418	-	6,003,418
	Distribution	500,005	-	500,005
	Total	14,088,573	-	14,088,573
	IEP Phase 2 (Post HB 105)			
	Commodity	100,786	-	100,786
	LNG Plant	430,030	-	430,030
	Trucking	14,075	-	14,075
	Storage	1,517,594	-	1,517,594
	Distribution	26,000	-	26,000
	Project Management	528,916	-	528,916
	Due Dilligence & Deal Structuring	539,230	-	539,230
	Total	3,156,631	-	3,156,631
	Total	17,245,204	-	17,245,204
Loans & Investments	LNG Plant	-	-	-
	Trucking	-	-	-
	Storage	-	-	-
	Distribution	-	-	-
	FNG Loan**	-	60,500,000	60,500,000
	IGU Loan	-	43,366,087	43,366,087
	Sale of Pentex	40,254,796	21,133,913	61,388,709
	Total	40,254,796	125,000,000	165,254,796
Total	Total Expenditure	57,500,000	125,000,000	182,500,000
	Remaining Funds	-	150,000,000	150,000,000
Notes				
Financial data per unaudited accounting system records as of 04/04/2019.				
* Expenditures include Actuals, Encumbrances, and Commitments as of 04/04/2019.				
Legislative Appropriation & Authorization(s) only include those identified above and do not include AIDEA operating, Economic Development Fund, or other sources.				
** As directed by adoption of AIDEA Resolution G17-20 on 12/7/17, an additional \$45,500,000 of SETS financing has been authorized to Fairbanks Natural Gas to expand LNG storage in the FNSB.				

SUMMARY

The adoption of an HB 105 Plan by the AIDEA Board on September 21, 2017, provided access to IEP financing tools necessary to accomplish consolidation of the Pentex assets (FNG) with IGU under IGU's local control. Transfer of control of FNG to IGU was approved by the RCA on April 30, 2018. The IGU Board approved the close of the consolidation deal on June 12, 2018, and the final closing documents were signed on June 13, 2018.

As a result, work is underway to expand LNG storage capacity and to prepare to expand LNG production capacity. The IGU Board has approved the fiscal year 2019 operating and capital budgets for FNG.

The next quarterly report is due in July 2019.



Attachment A: House Bill 105 Plan Memorandum



MEMORANDUM

To: John Springsteen, Executive Director
Alaska Industrial Development and Export Authority

From: Gene Therriault, IEP Team Lead
Mark Gardiner, IEP Team Member
Dan Britton, CEO Pentex/Fairbanks Natural Gas

Date: September 20, 2017

Re: Interior Energy Project – HB105 Required Project Plan

This memorandum and accompanying attachments constitute an IEP project plan that complies with specific requirements of Chapter 39, SLA 2015 (HB105). In addition, the documents assess the impact of current low fuel oil prices on the IEP. Finally, this memorandum recommends the AIDEA Board approve this plan through consideration and adoption of Resolution No. G17-13.

The IEP Team recommends adoption of the HB105 compliant plan for development of the natural gas system in the Fairbanks North Star Borough (FNSB) based on incremental investment in system capital and continued low-cost utility operations. The AIDEA IEP HB105 Plan achieves the IEP objectives for significant customer rate reductions sufficient to support a critical mass of space heating fuel conversion to natural gas. The plan is based on proven municipal utility principles, establishing the foundation for integration of the existing Fairbanks Natural Gas (FNG) and Interior Gas Utility (IGU) natural gas distribution infrastructure in the FNSB into a single, consolidated utility. The Plan invests the appropriated capital funds, deploys designated funds from the Sustainable Energy Transmission and Supply (SETS) fund and makes prudent use of authorized bond financing in the early years – thereby matching the financial requirements for capital investment to the conservative estimated conversion and gas demand growth rates.

Background

In 2013, the Alaska Legislature, at the request of Governor Parnell and the Interior community, acted to authorize a financing package designed to bring North Slope gas to the Interior via trucked Liquefied Natural Gas (LNG). Financing for the project (the Interior Energy Project or “IEP”) included \$57.5 million of state appropriated funds and \$275 million of authorized project financing consisting of \$125 million appropriated to the SETS fund and an authorization of \$150 million in AIDEA bonds backed by a state “moral obligation” credit support. The financing portion of the project was contained in SB23 of the 2013 Legislative session.

In the remainder of 2013 and all of 2014, AIDEA proceeded to select a project partner and advance development of a LNG plant on the North Slope of Alaska. At the end of 2014, the project development Concession Agreement for the North Slope plant expired, leading to termination of the Concession Agreement in early 2015.

During the 2015 Legislative session, HB105 reauthorized the IEP financing with new language expanding alternatives (gas sourced from other than the North Slope, propane, or small diameter pipelines) for supplying energy to the Interior of Alaska. This legislation, introduced by Governor Walker and supported by the Interior community, passed both houses of the legislature unanimously and was signed into law June 30, 2015. One change in HB105 from the previous authorization was the addition of a requirement that the AIDEA Board approve, by resolution, a project plan for the Interior Energy Project. The specific language of that requirement states:

“(a) The Alaska Industrial Development and Export Authority, through the Alaska Industrial Development and Export Authority sustainable energy transmission and supply development fund (AS 44.88.660), may provide financing up to a principal amount of \$275,000,000 for the development, construction, and installation of, and the start-up costs of operation and maintenance for, a liquefied natural gas production plant and system and affiliated infrastructure in the state that will provide natural gas to Interior Alaska as a primary market and natural gas delivery and distribution systems and affiliated infrastructure that will provide natural gas to Interior Alaska, if the members of the Alaska Industrial Development and Export Authority approve by resolution a project plan. The project plan must

- 1. identify the source of the natural gas;*
- 2. include the estimated cost of the project;*
- 3. and include the estimated price of natural gas supplied to natural gas utilities in Interior Alaska before distribution to consumers. “*

This memorandum, and the associated attachments, provide the documentation for Board Resolution No. G17-13, RESOLUTION OF THE ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY APPROVING AN HB 105 COMPLIANT PROJECT PLAN FOR THE INTERIOR ENERGY PROJECT.

Project Plan

The project recommended by the IEP team to the AIDEA administration for action by the AIDEA Board is founded on a “Titan 2” LNG plant in the Cook Inlet area, co-located with the existing Titan LNG facility at Point MacKenzie presently serving Interior Alaska.

The proposed Titan 2 project will add approximately 100,000 gallons per day (3Bcf per year) of LNG capacity to the present output of the Titan facility. The existing Titan plant has a production capacity of 50,000 gallons per day. Estimated capital cost for the new plant capacity is \$46 million. That number will be refined and confirmed by early works Front End Engineering and Design (FEED) efforts prior to presenting a Final Investment Decision (FID) recommendation.

Additionally, FNG will construct a new 5.25 million gallon LNG storage facility in Fairbanks. The cost of this project component is estimated to be \$42 million and the storage facility is expected to qualify to receive a State of Alaska LNG storage payment of \$15 million under the provisions of AS 43.20.047. This storage project will meet the RCA’s requirement for five days of storage and provide an increased level of seasonal supply by storing LNG produced in the summer for use in the winter. Completion of this storage facility will allow the existing LNG tanks in South Fairbanks to be re-deployed to North Pole for initial supply to the existing IGU system.

The structure of the commercial and supply chain arrangements is as follows:

- I. The IGU or AIDEA SETS fund will acquire Pentex Alaska, LLC from the AIDEA Revolving Fund. Pentex is the parent company of Fairbanks Natural Gas, LLC, Arctic Energy Transport, LLC, and Titan Alaska LNG, LLC. Pentex and its subsidiaries constitute an operating natural gas enterprise currently providing natural gas utility service to 1,100 customers in Fairbanks.
- II. IGU and/or Pentex will continue to operate expanded liquefaction, transportation, storage, re-gasification, and distribution of the gas to existing and new customers in the FNG and IGU service areas.
- III. AIDEA will provide financing to IGU and/or Pentex consistent with HB105 authorizations and IEP goals, maintaining fiscal controls through loan terms and covenants.
- IV. IGU and/or Pentex will construct the Titan 2 addition integrated with the current Titan LNG plant. A copy of the Titan Expansion Development Plan is included as Attachment A.
- V. Titan will purchase feed gas for the expanded liquefaction plant. Gas will be provided into the plant via a gas sales agreement between Titan and Hilcorp Alaska. A copy of the gas sales agreement executed by the parties is included as Attachment B.
- VI. Titan will arrange for transport of the LNG to the Interior. Initially, this transport is expected to be accomplished via trucking in a manner similar to the present trucking arrangement. A summary of the large capacity trailer pilot project results and projected costs are included as Attachment C.
- VII. FNG will construct new LNG storage capacity sufficient to meet the RCA required 5-day minimum storage requirement as well as provide increased seasonal supply during peak winter months. A summary of the LNG storage expansion project is included as Attachment D.
- VIII. IGU and FNG will distribute natural gas from the LNG storage facilities to existing and new customers.

Specific HB 105 Required Components

(1) Source of Natural Gas

Titan recently executed a new gas supply contract with Hilcorp to provide Titan's current liquefaction facility with a term beginning April 01, 2018 and expiring March 31, 2021. The All Requirements Agreement provides Titan with enough capacity (5 MMCF/ Day) for its existing customers, and allows for the expansion of up to 15 MMCF/Day after Titan provides 18 months' notice to Hilcorp. This is enough capacity to allow for the expansion of the Titan facility as described in this memo.

(2) Estimated Cost of the Project

The estimated costs of the project, including future expansions of the combined distribution systems and LNG plant, are outlined in Table 1. The capital costs are split into three categories: Already Invested, Immediate, and Demand Dependent. The immediate capital costs will be incurred upon project sanction in order to meet the goals of the IEP. The immediate capital investment will allow for demand and corresponding revenue growth. Upon sufficient revenue

growth, IGU and/or Pentex will have the financial ability to incur revenue-backed debt to finance additional expansion of the LNG plant and combined distribution systems within the FNSB.

IEP Capital Program	Already Invested	Stage 1 & 2 - Consolidated Utility - Immediate	Stage 3 - Demand Dependent	Total
SOURCES OF FUNDS				
Capital Appropriation	\$ 15,060,000	\$ 42,440,000	\$ -	\$ 57,500,000
SETS Loans	42,400,000	82,600,000	-	125,000,000
Bond Financing - Capital	-	19,451,400	121,092,600	140,544,000
Storage Tax Credits	-	18,500,000	-	18,500,000
Commercial Financing	-	1,825,000	2,920,000	4,745,000
Utility Revenues	-	-	-	-
Total - Sources of Funds	\$ 57,460,000	\$ 164,816,400	\$ 124,012,600	\$ 346,289,000
USES OF FUNDS				
Pentex Acquisition	\$ -	\$ 59,575,000	\$ -	\$ 59,575,000
Liquefaction Development	-	46,200,000	25,000,000	71,200,000
Transportation	-	1,825,000	2,920,000	4,745,000
Storage & Regasification	-	52,000,000	-	52,000,000
Distribution	42,400,000	5,216,400	96,092,600	143,709,000
Other Project Costs (NS, etc.)	15,060,000	-	-	15,060,000
Total - Uses of Funds	\$ 57,460,000	\$ 164,816,400	\$ 124,012,600	\$ 346,289,000

Table 1

(3) Estimated Price of Natural Gas Supplied to Natural Gas Utilities Before Distribution to Consumers

The estimated price of natural gas supplied to Interior customers is outlined in Table 2. Under the project plan, the LNG plant is owned by IGU and/or Pentex and the capital costs are integrated into the entire utility, including the storage and distribution system. For purposes of HB105, the estimated price of natural gas (LNG) supplied to utilities is shown in the line labeled “Subtotal – Cost to Utilities”.

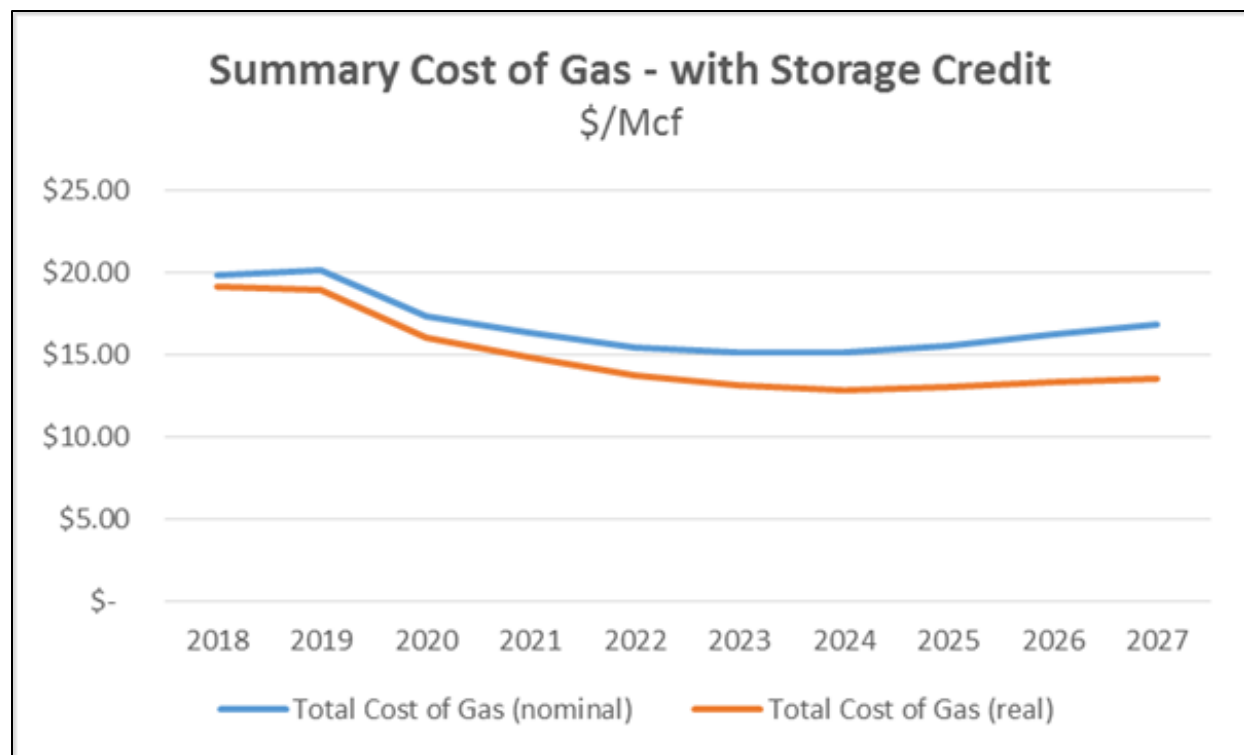
The cost of debt for the project recovers the pooled capital investment for all assets of the project identified in the category above. The total cost of gas is shown in nominal and inflation adjusted real dollars. The table below shows that after adjusting for inflation this project can meet the price goals of the IEP most years. It is anticipated that rates will be set slightly higher than costs in order to provide cash reserves and smooth out the impact to the end consumer of the year-to-year fluctuations in cost.

Summary Cost of Gas - With Storage Tax Credit										
Anticipated Demand (Bcf)	0.75	0.75	1.19	1.83	2.55	3.25	3.90	4.41	4.75	4.95
Cost of Gas (\$/Mcf nominal)	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Natural Gas - Cook Inlet	\$7.72	\$7.72	\$7.72	\$7.72	\$7.87	\$8.03	\$8.19	\$8.36	\$8.52	\$8.69
Pipeline Trans. Cost to Pt. Mac. (3rd-party)	0.65	0.66	0.68	0.69	0.70	0.72	0.73	0.75	0.76	0.78
LNG Production - Titan Plant	4.28	4.34	3.22	2.53	2.19	2.02	1.92	1.88	1.87	1.89
Trucking - Pt. Mac. To Fairbanks	2.48	2.53	2.58	2.63	2.68	2.73	2.79	2.84	2.90	2.96
Subtotal - Cost to Utilities	\$ 15.12	\$ 15.25	\$ 14.19	\$ 13.57	\$ 13.45	\$ 13.50	\$ 13.64	\$ 13.83	\$ 14.06	\$ 14.32
Distribution, Storage, Vaporization	4.76	4.85	3.13	2.07	1.51	1.21	1.03	0.93	0.88	0.86
Total Cost of Gas before Financing	\$ 19.88	\$ 20.10	\$ 17.31	\$ 15.64	\$ 14.96	\$ 14.71	\$ 14.67	\$ 14.76	\$ 14.94	\$ 15.18
Debt	-	-	-	0.72	0.51	0.40	0.43	0.78	1.34	1.69
Total Cost of Gas (nominal)	\$ 19.88	\$ 20.10	\$ 17.31	\$ 16.35	\$ 15.48	\$ 15.11	\$ 15.10	\$ 15.54	\$ 16.28	\$ 16.87
Total Cost of Gas (real)	\$ 19.11	\$ 18.94	\$ 16.00	\$ 14.81	\$ 13.74	\$ 13.16	\$ 12.88	\$ 13.00	\$ 13.36	\$ 13.57
Equivalent Fuel Oil Price (nom. \$/gal)	\$ 2.74	\$ 2.77	\$ 2.39	\$ 2.26	\$ 2.13	\$ 2.08	\$ 2.08	\$ 2.14	\$ 2.25	\$ 2.33
Equivalent Fuel Oil Price (real \$/gal)	\$ 2.64	\$ 2.61	\$ 2.21	\$ 2.04	\$ 1.90	\$ 1.81	\$ 1.78	\$ 1.79	\$ 1.84	\$ 1.87
Planned Average Customer Rates*	\$20.20	\$20.20	\$17.31	\$16.35	\$15.48	\$15.11	\$15.10	\$15.54	\$16.28	\$16.87
Equivalent Fuel Oil Price (nom. \$/gal)	\$ 2.79	\$ 2.79	\$ 2.39	\$ 2.26	\$ 2.13	\$ 2.08	\$ 2.08	\$ 2.14	\$ 2.25	\$ 2.33
*Differs from Total Cost of Gas in 2018 and 2019 due to utility consolidation										

Table 2

Visual Comparison of Total Cost of Gas to customers (nominal vs real)

Graph 1 utilized values from Table 2 to provide a visual comparison of the Total Cost of Gas (nominal) and the Total Cost of Gas (real) over time.



Graph 1

Comparison of AIDEA IEP Projected Gas Cost to Notional IEP Target Cost

Table 3 provides a comparison of the projected AIDEA IEP cost of gas versus the pre-IEP Pentex gas price and the notional IEP price target. In order to reflect an apples-to-apples comparison, all of the costs in this table reflect an assumed 2.00% rate of inflation.

Cost of Gas (with inflation)	2.00%									
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Pentex Rate (pre-IEP)	\$24.00	\$ 24.48	\$ 24.97	\$ 25.47	\$ 25.98	\$ 26.50	\$ 27.03	\$ 27.57	\$ 28.12	\$ 28.68
IEP Notional Target Rate	\$15.00	\$ 15.30	\$ 15.61	\$ 15.92	\$ 16.24	\$ 16.56	\$ 16.89	\$ 17.23	\$ 17.57	\$ 17.93
AIDEA IEP Rate - w/ Storage Credit	\$19.88	\$ 20.10	\$ 17.31	\$ 16.35	\$ 15.48	\$ 15.11	\$ 15.10	\$ 15.54	\$ 16.28	\$ 16.87
AIDEA IEP Rate - no Storage Credit	\$19.88	\$20.10	\$17.31	\$16.96	\$15.91	\$15.46	\$15.37	\$15.80	\$16.53	\$17.11
% of IEP Target Savings										
AIDEA IEP Rate - w/ Storage Credit	45.8%	47.7%	81.8%	95.4%	107.8%	114.6%	117.7%	116.4%	112.2%	109.8%
AIDEA IEP Rate - no Storage Credit	45.8%	47.7%	81.8%	89.1%	103.3%	111.1%	115.0%	113.8%	109.9%	107.6%

Table 3

As Table 3 shows, the LNG storage credit/payment enables the AIDEA IEP HB105 Plan to achieve the same level of savings as the IEP Notional Target rate by 2022.

Recommendations for AIDEA Board action

The IEP Team and the AIDEA administration recommend the AIDEA Board vote to pass Resolution No. G17-13 approving this HB105 compliant project plan.

AIDEA Board passage of Resolution No. G17-13 will accomplish the following actions:

- Approve an IEP Project Plan with components specified in HB105
- Authorize AIDEA access to full IEP funding to be deployed in pursuit of the project goals
- Authorize AIDEA to consider sale of Pentex Alaska, LLC to the IGU or the AIDEA SETS fund under separate action

This action provides the commercial structure and financing tools for IGU or Pentex to control the IEP project. This includes constructing the Titan 2 LNG plant, building additional LNG storage in Fairbanks, integrating the existing FNG and IGU distribution infrastructure and, as demand and revenue permit, future expansions of the infrastructure needed to increase the natural gas availability and utilization in Interior Alaska.

The IEP Team and the AIDEA administration have determined that this project plan provides a path to lower the cost of natural gas to Interior residents and businesses.

Attachments

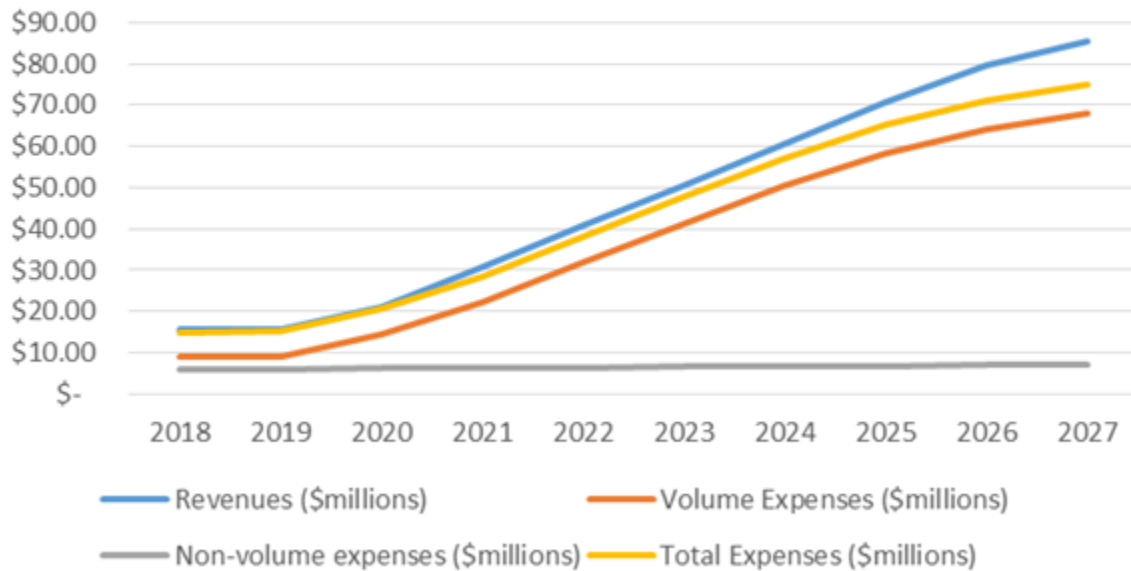
Attachment A: The development for the Titan 2 LNG plant expansion

Attachment B: Gas Sale Agreement between Titan Alaska LNG, LLC and Hilcorp Alaska

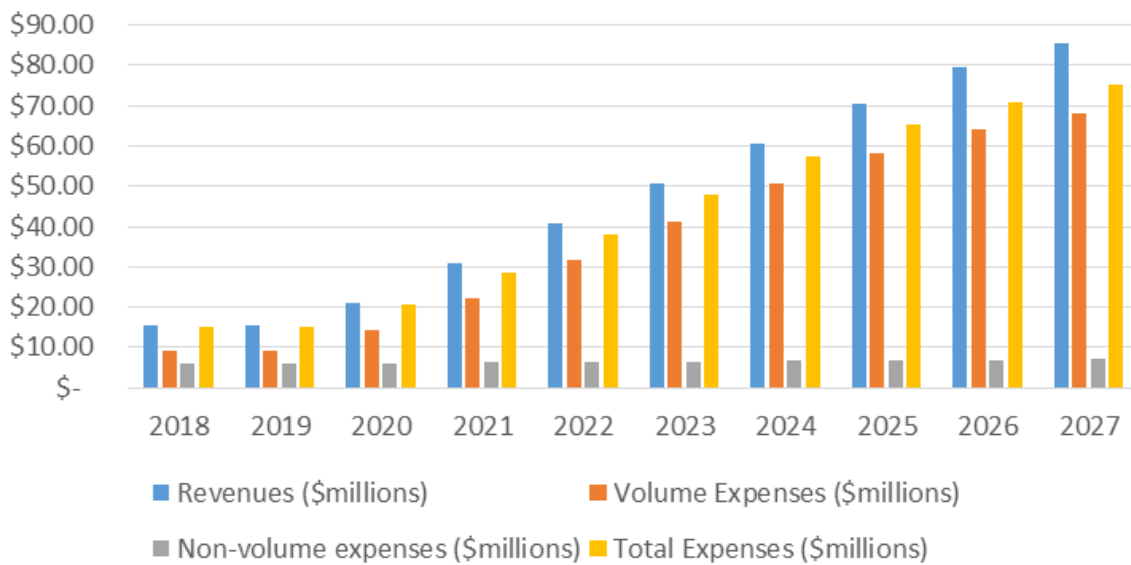
Attachment C: A summary of the large-capacity trailer pilot project results and projected costs

Attachment D: The development plan for expansion of LNG storage in Fairbanks

Projected
Revenues & Expenses (volume + non-volume)



Projected
Revenues & Expenses (volume + non-volume)



ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY

RESOLUTION NO. G17-13

**RESOLUTION OF THE ALASKA INDUSTRIAL
DEVELOPMENT AND EXPORT AUTHORITY APPROVING
AN HB 105-COMPLIANT PROJECT PLAN FOR THE
INTERIOR ENERGY PROJECT**

WHEREAS, the Alaska State Legislature authorized the Alaska Industrial Development and Export Authority (the “Authority”) to provide financing up to a principal amount of \$275,000,000 for the development, construction, and installation of, and the start-up costs of operation and maintenance for, a liquefied natural gas production plant and system and affiliated infrastructure and natural gas delivery and distribution systems that will provide natural gas to Interior Alaska as a primary market (the entire project is known as the “Interior Energy Project”);

WHEREAS, in 2015, the Alaska State Legislature passed chapter 39 of the 2015 Session Laws of Alaska (SCS CSHB 105(FIN) am S), hereafter referred to as “HB 105,” which concerned the Authority and the Interior Energy Project

WHEREAS, among other things required by HB 105, Section 9 of the law specified that in order for the Authority to deploy the financing approved for the Interior Energy Project the Authority had to approve by resolution a project plan;

WHEREAS, the staff of the Authority, working in conjunction with the Authority’s advisors, have developed a project plan for the Interior Energy Project, a complete copy of which with all attachments is appended to this Resolution;

WHEREAS, the proposed project plan for the Interior Energy Project meets all of the requirements of Section 9 of HB 105; and

WHEREAS, it is in the best interests of the Authority and in furtherance of the goals of the Interior Energy Project that the proposed project plan be approved.

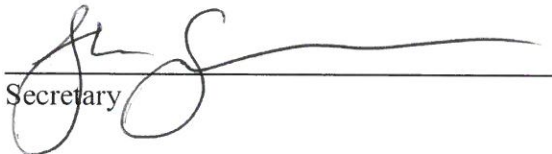
NOW, THEREFORE, BE IT RESOLVED BY THE ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY AS FOLLOWS:

The project plan for the Interior Energy Project that is appended to this Resolution is hereby approved.

Dated at Anchorage, Alaska, this 21st day of September 2017.




Chair


Secretary