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STATE OF ALASKA

THE REGULATORY COMMISSION OF ALASKA

Before Commissioners:

Kate Giard, Chairman
Dave Harbour
Mark K. Johnson
Anthony A. Price
Janis W. Wilson

In the Matter of the Gas Sales Agreement)
Between ENSTAR NATURAL GAS COMPANY,)
A DIVISION OF SEMCO ENERGY, INC. and)
MARATHON OIL COMPANY Filed as TA139-4)

U-06-2
ORDER NO. 15

DISSENTING STATEMENT OF
COMMISSIONER DAVE HARBOUR

BY THE COMMISSION:

Summary

Respectfully, the majority should have approved Tariff Advice 139-4, the gas sales agreement between ENSTAR¹ and Marathon² designated as APL-5, subject to reasonable conditions. The majority's decision,³ a novel, quasi-rejection of TA 139-4,

¹ENSTAR Natural Gas Company (ENSTAR) is a division of SEMCO Energy, Inc. (SEMCO). Alaska Pipeline Company (APLC) is a wholly-owned subsidiary of SEMCO. APLC, not ENSTAR, is the actual party to APL-5. The commission has historically regulated APLC and ENSTAR as a single entity. The use of the name ENSTAR in this proceeding includes both APLC and ENSTAR.

²Marathon Oil Company (Marathon).

³Order U-06-2(15), *Order Rejecting TA139-4 as a Base Supply Contract Having the Effect of Increasing the Current Average Cost of System Gas Supply but Allowing TA139-4 to Take Effect Immediately as a Base Supply Contract Having the Effect of Decreasing the Current Average Cost of System Gas Supply and Requiring Filings*, dated September 28, 2006.

1 is based on errors in form, judgment, and substance; it results in a decision that fails to
2 follow commission precedent and is unsupported by the evidence in the record.

3 Discussion

4 As required by our statutes⁴ and regulations,⁵ ENSTAR filed Tariff Advice
5 Letter 139-4 (TA139-4), asking us to approve APL-5, a new gas sales agreement (GSA)
6 it had negotiated with Marathon. When adjudicating a GSA filed as a tariff, the
7 commission typically (a) approves the GSA, (b) rejects the GSA, or (c) approves the
8 GSA subject to certain conditions. If the parties do not agree to implement any
9 commission-imposed conditions, the GSA cannot be activated. If the parties accept
10 commission-imposed conditions, they are required to file an amended GSA that
11 includes those conditions for final commission approval. In the present docket, the
12 majority took none of the above-referenced actions. Rather, through Order U-06-2(15),
13 the majority simultaneously rejected and allowed the contract, provided that gas
14 purchased under the GSA decreases "...the current average cost of system gas
15 supply."⁶ This circuitous process gives ENSTAR redundant rights it already enjoys
16 under its current tariff.⁷

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18 ⁴AS 42.05.361(a).

19 ⁵3 AAC 390(a).

20 ⁶Order U-06-2(15) at 1.

21 ⁷Had the majority *simply rejected* TA139-4 without condition or waiver the *status*
22 *quo* result would have been materially the same as the "reject-allow" decision in that,
23 ENSTAR's (existing) tariff requires we approve any gas sales agreements that increase
24 ENSTAR's current average cost of gas.

25 Tariff Sheet 90, Section 708(f), provides:

26 [A]dditional contracts or revisions of base supply contracts having the effect
of decreasing the current average cost of system gas supply become
effective immediately without notification.

1 Even if the majority's result were correct — which I dispute — its
2 “yin-yang, yin-yang” decision that “rejects-allows” the contract, “without approval,” “to
3 the extent” prices are lower, is poor form and fails to give the parties and subsequent
4 commissions guidance for dealing with similar situations in the future. Commissions
5 must strive to logically and clearly adjudicate proceedings where the record is
6 assembled at great cost, in good faith and under the assumption that a clear and
7 reasonable decision will result therefrom. That is not what happened here.

8 The Majority's Decision Fails to Properly Consider the Evidence in the Record.

9 The two key issues upon which the majority decision is based, and with
10 which I disagree, are contained in the majority's statement that “ENSTAR did not meet
11 its burden of demonstrating that gas supplies...are reliable and that the price is
12 reasonable.”⁸ For the reasons discussed herein, I believe that the majority's decision
13 lacks substance and fails to consider the evidence in the record.

14 *The majority's statement that, “ENSTAR did not meet its burden to demonstrate
15 that gas supplies...are reliable”*

16 The majority acknowledges the extreme shortages ENSTAR's customers
17 face⁹ and illustrates the impressive array of efforts ENSTAR has and is undertaking to
18 meet those shortages, citing several gas supply contracts with varying terms and
19 conditions.¹⁰ Order U-06-2(15) accepts that ENSTAR responsibly “notified other Cook
20 Inlet producers of its need for new gas supplies.” It acknowledges that Marathon was
21 the “only producer that offered to meet ENSTAR's unmet requirements.”¹¹ When

22 ⁸Order U-06-2(15) at 37, stating “...we conclude that ENSTAR has failed to meet
23 its burden of proof that APL-5 achieves a reliable gas supply at a reasonable price.”

24 ⁹*Id.* at 5 (Ex. A).

25 ¹⁰*Id.* at 5, l.16.

26 ¹¹*Id.* at 3.

1 questioned as to whether the only entity capable of meeting its needs had it “over a
2 barrel,” ENSTAR provided convincing responses¹² supporting a rational conclusion that
3 while supply was the essential priority, price was carefully considered and negotiated.¹³

4 Having clearly and responsibly demonstrated the shortage challenge and
5 the actions it took to meet that challenge, ENSTAR next properly approached the issue
6 of reliability of the gas supply offered by Marathon.

7 First, ENSTAR established that it has developed a responsible mix of
8 supply that will allow it to keep its demand commitments through 2016.¹⁴

9 Second, ENSTAR responsibly negotiated a contract, the term of which
10 could coincide (i.e., in the year 2016 range) with the construction of a North Slope gas
11 pipeline and accompanying spur line to Southcentral Alaska.¹⁵ The contract allows
12 Marathon to supply additional gas should ENSTAR need more but does not require
13 ENSTAR to take more.¹⁶ I commend the parties for creating a way to accommodate the
14 possible arrival of North Slope gas while also having a back up plan.

15 Third, Marathon has the ability to acquire gas for resale to ENSTAR, as
16 the majority properly noted.¹⁷

17 Fourth, Marathon has committed proven reserves to this contract.¹⁸

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19 ¹²Tr. 1046, l. 22 and Tr. 285, l. 20.

20 ¹³Tr. 285.

21 ¹⁴H-1 at 3, “ENSTAR Gas Supply Nov. 2005” chart, reflecting supply
22 contributions from Beluga, Moquawkie, Unocal and Marathon, including the APL-5
increment filling a growing supply gap projected from 2009 to 2016 and beyond.

23 ¹⁵Tr. 1050, l. 5.

24 ¹⁶H-1 at 4, “Term”.

25 ¹⁷Order U-06-2(15) at 15.

26 ¹⁸H-1 at 5, “Proven Reserves”.

1 Fifth, ENSTAR responsibly recognized earlier concerns about gas supply
2 contracts and negotiated improvements in APL-5 designed to meet those commission
3 concerns.¹⁹

4 Finally, the majority challenged the importance of APL-5 as a reliable
5 GSA. It listed a number of ideas²⁰ leading readers to conclude that Marathon might not
6 be able to supply all the gas ENSTAR expects, as illustrated by its gas supply chart.²¹
7 This reasoning is inappropriate for too many reasons to list here. Suffice that the
8 majority should be delighted and not critical if Marathon's assumed supply deficiencies
9 are accurate, for since the majority believes the contract price is too high, it must also
10 be pleased that less gas will be sold for that price.

11 ENSTAR clearly met its burden to establish that APL-5 presents a
12 reasonable gas supply solution for ENSTAR's customers.²²

13 The majority's statement that, "ENSTAR did not meet its burden to demonstrate
14 that ...the price is reasonable."

15 The majority carefully organized the price arguments in Order U-06-2(15)
16 but then viewed them through the lens of "the glass is half empty."²³ The majority
17 begins by turning the tanker of precedent toward a new and unknown azimuth when it
18 cavalierly dismisses the commission's earlier efforts to carefully deal with Southcentral

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20 ¹⁹Tr. 1049.

21 ²⁰Order U-06-2(15) at 30.

22 ²¹H-1 at 3.

23 ²²I have chosen not to address at length the majority's apparent theory [Order
24 U-06-2(15) at 27] that the ERA's reauthorization of the LNG export license could
25 produce *more* reserves in the Inlet: such conjecture is pure speculation and requires an
26 assumption that an LNG sale would provide more incentive for discovery of new
reserves than a local buyer willing to pay a higher price.

²³Order U-06-2(15) at 31-36.

1 Alaska's natural gas shortage.²⁴ In a prior, relevant docket, the commission was dead
2 serious about the natural gas shortage²⁵ and its response to that shortage.²⁶ Time has
3 exacerbated the exigency, not abated it.²⁷ The standard of review and precedent
4 established by that docket is not neutralized by any significant, distinguishing factor in
5 this docket. Earlier commissions, acting in similar circumstances, appropriately were
6 guided by the public interest.²⁸ Without citing any convincing, distinguishing factor, the
7 majority challenges almost every nook and cranny of APL-5 while our precedent clearly
8 provides that the commission "[w]ould not speculate whether a better agreement could
9 have been obtained."²⁹ One notes that this majority not only speculated; it acted on its
10 own speculation that a lower price should be demanded.

11 In 2001, when faced with essentially the same evidence and argument in
12 another docket, the commission concluded "[t]he evidence persuades us that ENSTAR
13 must pay a competitive price to attract necessary capital and encourage exploration....
14 The HHF price is necessary...."³⁰ The 2006 majority veers its decision away from the

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16 ²⁴Order U-06-2(15) at 31.

17 ²⁵Order U-01-7(8), *Order Conditionally Approving TA117-4 (Gas Sales*
18 *Agreement) and Requiring Filing*, dated October 25, 2001, at 5, "Natural gas reserves,
19 while plentiful in the past, are declining." Docket U-01-7, *In the Matter of the Gas Sales*
20 *Agreement Between ALASKA PIPELINE COMPANY, a Wholly-owned Subsidiary of*
21 *SEMCO ENERGY, INC., of Which the ENSTAR NATURAL GAS COMPANY is a*
22 *Division, and the UNION OIL COMPANY OF CALIFORNIA, Filed as TA117-4.*

23 ²⁶Order U-01-7(8) at 4, noting "we are guided by our obligation to act in the public
24 interest. The GSA is a commercially negotiated agreement. We will not speculate
25 whether a better agreement could have been obtained by ENSTAR, with Unocal or with
26 another potential supplier."

²⁷Tr. 1697.

²⁸*Id.*

²⁹*Id.*

³⁰Order U-01-7(8) at 9.

1 stable course of precedent, beckoned by a new siren call: “[s]peculation that the use of
2 Henry Hub by one utility provides sufficient incentive to result in Cook Inlet reserves
3 growth.”³¹ The majority failed to follow precedent charted by our able predecessors
4 without offering sufficient reason for changing course; furthermore, sound judgment in
5 our current circumstances urges that it would be wiser—indeed, essential—to err on the
6 side of secure supply.

7 The majority argues, rightly I believe, that

8 [p]ricing terms are negotiated as a whole, that each element is adjusted and
9 fine-tuned to counterbalance each other element of the contract to arrive at
10 terms the contracting parties can embrace. If we were to assess individual
11 items with the intent of conditioning our approval on a change in one or more
12 individual elements, we would be disturbing that balance.³²

13 Similarly, our predecessor commission stated in another docket that,
14 “While Marathon and the PAS advocate disapproval of the entire GSA, we do not find
15 cause for such action. No party convincingly demonstrated a fatal flaw in any GSA
16 condition. We are satisfied that the negotiations were at arms-length, and that the GSA
17 ... is in the public interest.”³³ Our predecessor commission then went on to do in 2001
18 what I urge we do here — approve the contract with reasonable modifications.
19 However, the majority ignored our precedent and contradicted its own intent by
20 critiquing most of the individual major features of the GSA before finally concluding it
21 should be disapproved.

22 The majority erroneously and without proof proclaims that “ENSTAR has
23 not sufficiently justified that radical departure in this record”³⁴ referring to its use of

24 ³¹Order U-06-2(15) at 28.

25 ³²*Id.* at 33.

26 ³³Order U-01-7(8) at 6.

³⁴Order U-06-2(15) at 33.

1 Henry Hub with APL-5 pricing and terms. APL-5's features are supported by precedent
2 and are not radical; and our record clearly defeats the majority's conclusion.³⁵
3 Unfortunately, the majority is so sure of its own judgment that it ventures off to
4 uncharted areas, creating and raising its own proxy index from the ashes of our record
5 without evidentiary support. Thus is born the majority's "ENSTAR WACOG"³⁶ Index.
6 Advocates of this new index state that by its very nature it,

7 [r]epresents a diverse base of suppliers, both willing and able to meet
8 ENSTAR's deliverability and swing....blend of legacy pricing based on
9 proven reserves combined with the exploration-driven Henry Hub.³⁷

9 The majority cites no support legitimating these claims and, in fact,
10 ignores the lengthy record in this docket regarding the time-honored, market-respected
11 value of various legitimate proxy indices — values such as transparency, volume,
12 liquidity — which the ENSTAR WACOG Index" is not proven to have. Requiring
13 ENSTAR to find gas that lowers its average cost of existing gas contradicts the logic
14 and evidence that new gas will be more expensive than older reserves³⁸ and, therefore,
15 command a higher price.³⁹ Also, APL-5 contains benefits to consumers that may not be
16 reflected in gas that is forced into the market via the majority's "lower priced" concept
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22 ³⁵Tr. 669.

23 ³⁶Weighted average cost of gas (WACOG).

24 ³⁷*Id.*

25 ³⁸Tr. 661.

26 ³⁹Tr. 658.