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State publishes analysis of LNG export project fiscals

(Anchorage, AK)—The Alaska Department of Natural Resources today released an in-depth study of the commercial aspects of the Alaska LNG project that the three major North Slope oil producers and TransCanada Corp. are now pursuing.

The LNG project – one of the largest projects of its kind in the world – would pipe gas from the North Slope to a tidewater port in Southcentral Alaska. Gas would be available to Alaskans and also shipped to Pacific Rim markets. The 30-year project would provide cheaper in-state gas supplies, billions of dollars in annual state revenues and new economic opportunities for thousands of Alaskans.

"The goal of the study is to inform near-term decisions about the fiscal aspects of an LNG project in Alaska – big decisions that involve our royalties, taxes, or even a potential equity stake in the project. This information will help us deliver on our constitutional obligations to maximize the benefits of developing Alaska's North Slope natural gas resources," said Natural Resources Commissioner Joe Balash.

The 191-page Alaska North Slope Royalty Study, produced by Black & Veatch, analyzes key issues that state agencies and legislators will consider before setting fiscal terms for a gasline. The study examines LNG market conditions and the global supply chain, reviews fiscal terms that have been established for successful LNG export projects around the world, and looks at the commercial risks of various business structures for an Alaska project.

The study demonstrates that an LNG export project can compete for a place in the Asian LNG markets, but it will likely take changes to Alaska's fiscal terms to ensure a successful project. "We have some work to do, but the good news in this report is that we don't have to sacrifice our royalty revenue in the future to get a project going," Balash said.

The study also demonstrates that a misalignment of interests between the State and project sponsors could lead to diminished value for the State's royalty. North Slope lessees pay a minimum of 12.5 percent royalty on all hydrocarbons produced and sold. The value of that royalty is measured at the lease after transportation costs are deducted. Depending on the business and financing structure chosen by project sponsors, those transportation charges can be higher or lower—with the opposite impact on royalty values. “If we can find a way to better align our interests with the project sponsors, we can ensure Alaskans get the full value of their ownership of the resource,” Balash said.

The study looked closely at the state’s royalty rates and terms, which are managed by DNR. Royalties paid by the producers are the primary way the state benefits from its ownership of the North Slope’s hydrocarbon resources, and they are the foundation of revenue deposited to the Alaska Permanent Fund.

While in some parts of the world, governments have chosen to reduce or zero out their royalties to improve the economics of an LNG project, state officials are concerned that this option could undermine payments to the Permanent Fund and limit the amount of gas available to Alaskans. A 20 to 30 percent equity investment in the project can provide the same or better revenue than collecting taxes and royalty alone, according to the study.

“If we do it right, direct state participation in the project can allow the other project sponsors to structure their business and financing in whatever way benefits them. That would leave us free to structure our share of the business in whatever ways maximize the benefits to Alaskans,” Balash said.

The study also indicates that taking the state’s royalties for gas production “in value” may protect the state’s interests better than taking the royalties “in kind.” If the State were left to market LNG itself, it could end up receiving lower prices overseas for its share of the gas. The study details the pros and cons of either approach.

The Black & Veatch analysis focused on revenues, but Alaskans will benefit in multiple ways from a successful project. In the coming weeks, DNR will publish additional work regarding the value of in-state energy opportunities and expansions of the pipeline and/or the LNG plant.

To read the study, go to dnr.alaska.gov/commis/priorities/ak_lng.htm.

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