ALASKA SENATE LEGISLATURE

Senate Resources Committee

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Presentation by

John Ellwood
Vice President, Engineering & Operations

Foothills Pipe Lines Ltd.

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Foothills Pipe Lines Ltd. / Alaska Highway Gas Pipeline Project

My name is John Ellwood. I am Vice President, Engineering and Operations at Foothills Pipe Lines Ltd. ("Foothills"). We appreciate your invitation to discuss the transportation of Alaska North Slope natural gas to markets in the lower-48 states through the Alaska Natural Gas Transportation System ("Alaska Highway Project"). I understand that your committee wishes to explore with us the current status of our pipeline project with a particular focus on our permits.

Let me begin by telling you about Foothills. Our company is jointly owned by Westcoast Energy Ltd. ("Westcoast") and TransCanada PipeLines Limited. ("TransCanada"), the two major players in the Canadian gas pipeline business. Our corporate mission is very specific: to build and operate the Alaska Highway Pipeline Project. We were leaders in the project that was conceived twenty-five years ago, and we are just as committed today.

Between Westcoast and TransCanada, we have nearly 100 years of experience in developing, building and operating gas pipeline projects. We have been involved with every major Canadian gas pipeline project built in the last fifteen years.

Our existing pipeline systems provide access to five of North America’s largest natural gas markets. Together, these systems have the capability to move fifteen billion cubic feet per day of gas from Western Canada to the consuming markets. Canadian gas accounts for almost 20% of all gas consumed in the United States and all of that gas currently moves through pipelines owned in whole or in part by TransCanada and Westcoast.

This map shows the existing and planned pipeline network of Westcoast and TransCanada.

TransCanada, Westcoast and Foothills have developed leading edge gas pipeline design, construction and operating technology, including expertise in dense phase designs. We are also well known for our development of environmentally sound design, construction and operation practices. We believe that our expertise in northern, remote and difficult terrain gas pipeline construction and operations is second to none.
Building and operating pipelines is our core business.

The Alaska Highway Project is the Alaskan gas pipeline project approved in accordance with the Alaska Natural Gas Transportation Act of 1976 ("ANGTA") in the U.S., the 1978 Northern Pipeline Act in Canada, and the 1977 Agreement Applicable to a Northern Natural Gas Pipeline between the two countries ("U.S./Canada Agreement"). The project is shown in black and green on this map. As approved, the Alaska Highway Project is a 4,800-mile international pipeline project commencing at Prudhoe Bay and terminating in the Midwest and California market areas. It is important to note that the southern part of this pipeline has been constructed and is in full operation. The route for this system parallels the Trans Alaska Pipeline System ("TAPS") to Fairbanks, where it angles southeast, following the Alcan Highway to the Alaska-Yukon border with Canada, down through the Yukon Territory and northern British Columbia, and into Alberta. In Alberta, the pipeline splits into two legs. The Eastern Leg proceeds southwest, crossing the U.S.-Canada border at Monchy, Saskatchewan and terminating near Chicago. The Western Leg proceeds southwest, crossing the U.S.-Canada border near Kingsgate, British Columbia and terminating at a point near San Francisco, California.

Foothills and TransCanada are the two remaining partners of the Alaska Northwest Natural Gas Transportation Company (Alaska Northwest), a partnership formed to construct and operate the Alaska portion of the Alaska Highway Project. In addition, Foothills is the Canadian sponsor of the Alaska Highway Project, and the majority owner and operator of the Canadian portions of the Eastern and Western Legs of the Alaska Highway Project.

Foothills has continuously championed the Alaska Highway Pipeline Project from the very beginning.

The Project is back "on the list" of possible solutions to the current North American concerns about high energy prices and the adequacy of natural gas supplies.
At the outset, there are some basic points that we should delineate:

- It is important to remember that this pipeline crosses the territory of two countries with different regulatory and political regimes.

- The Project has a long history, which adds unique attributes. The permits which have been issued are a product of this history and to understand the former requires an appreciation of the latter. Significantly, ANGTA in the U.S. and the Northern Pipeline Act in Canada create expedited procedures for completing the chosen system, the Alaska Highway Project.

- The pipeline permitting process can be very time consuming. In addition to the substantial work already completed on both the Alaskan and Canadian portions of the Alaska Highway Project, the special legislative and regulatory procedures in place in the U.S. and Canada will assist in expediting the construction and initial operation of the Project and keeping unnecessary delays to a minimum.

**Historical Background**

As I indicated, there are important historical dimensions associated with this project. We might focus on the time frame 1976-1982. Originally there were three competing Alaskan natural gas pipelines proposed. As shown on this map two of the projects were overland pipelines through Alaska and Canada. The third project would have transported gas by pipeline to tidewater, following the route of the “TAPS” pipeline, where the gas would be liquefied and transported to California by liquefied natural gas (“LNG”) tankers.

The U.S. Congress enacted the Alaska Natural Gas Transportation Act of 1976 with a purpose to provide an expedited process with respect to the selection of a single transportation system for the delivery of Alaska natural gas to the lower forty-eight states and to expedite construction and initial operation of the chosen transportation system.

With respect to the transportation of Alaska North Slope gas to markets in the lower 48 states, ANGTA superseded the usual Natural Gas Act (“NGA”)
process for granting Federal regulatory authorization to construct and operate a pipeline. ANGTA assigned the responsibility for the overall Alaska pipeline agenda to the President and Congress. Much the same approach was followed in Canada, where the Government took an active role in the decision regarding the Alaska natural gas pipeline. The reason for the creation of this extraordinary authority was that the governments wanted to expedite a cumbersome regulatory approval process in order to move more quickly to a solution.

Prior to 1978, a Canadian Board of Inquiry (The Berger Inquiry) examined a proposal to move Alaska gas across the North Slope and along the Mackenzie Valley. At the same time the National Energy Board ("NEB") held a hearing to determine which of the two overland pipeline routes was acceptable to Canada. Both processes rejected the North Slope route (primarily for environmental reasons) and the NEB recommended the Alaska Highway (Alaska Highway Project) option, being promoted by Foothills. The Berger Inquiry recommended that no pipeline should be built along the Mackenzie Valley for at least a decade and that a pipeline across the northern Yukon should never be built.

During this same period of time the Federal Power Commission (later to become the Federal Energy Regulatory Commission ("FERC") came to a split decision on the question of which route should be selected.

Following the enactment of the ANGTA, the President selected the Alaska Highway route and the Alaska Highway Project with his Decision and Report to Congress on the Alaska Natural Gas Transportation System ("President's Decision" or "Decision").

In 1977 just prior to the President issuing his Decision, the U.S. and Canada signed the U.S./Canada Agreement. This agreement or treaty, established the route, chose the companies who would build and operate the system, established tolling principles, and set the terms and principles to be followed in facilitating the construction and operation of the Alaska Highway Project pipeline. The President's Decision reflected the U.S./Canada Agreement. The Decision and the Agreement were subsequently approved by the U.S. Congress.
In 1978 Canadian Parliament enacted the Northern Pipeline Act. The Act:

1) incorporated all of the terms of the U.S./Canada Agreement

2) issued statutory certificates of public convenience and necessity to the respective subsidiaries of Foothills Pipe Lines Ltd.,

3) created the Northern Pipeline Agency to "facilitate the efficient and expeditious planning and construction of the pipeline"

4) established the methodology and rules for setting the Canadian tolls and tariffs for the pipeline

5) selected the route for the pipeline across Canada and

6) established Terms and Conditions respecting the socio-economic, environmental, construction and operations matters.

The complete Alaska Highway Project is shown on the attached map.

The President’s Decision designated Alcan Pipeline, a subsidiary of Northwest Pipeline Company (Northwest), as the party who would construct and operate the Alaska pipeline segment of the Alaska Highway Project. This authority was later assigned to Alaska Northwest, a partnership assembled by Northwest. At one time Alaska Northwest consisted of eleven (11) partners, all subsidiaries of U.S. or Canadian pipeline companies.

Given the magnitude of the pipeline undertaking Alaska Northwest sought to recruit the North Slope Producers to join the project and assist the financing of the pipeline. The Producers expressed a willingness to join but were restricted by the President’s Decision that disallowed the producers taking an equity position in the pipeline. In 1981, President Reagan submitted and Congress approved a Waiver of Law package allowing producer participation and including in the project, the North Slope gas conditioning facility.

In 1980, before the Waiver of Law was passed, Alaska Northwest and the Alaska Producers entered into a Cooperation Agreement providing for joint funding of the design and engineering of the Alaska Highway pipeline and the gas conditioning facility. Following the approval of the Waiver of Law,

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the scope of the Cooperation Agreement was expanded to encompass efforts to achieve the remaining regulatory approvals and to jointly pursue financing arrangements. The two sides anticipated that affiliates of the Producers would join the Alaska Northwest Partnership.

Design, engineering, environmental, financing and regulatory work proceeded along parallel tracks in Alaska and in Canada during this period of time.

As world wide energy supply and demand came back into balance and the "energy crisis" eased, the focus of the pipeline shifted to the pre-building of the southern portions of the Alaska Highway Project. There was a disagreement between Canada and the United States over this issue, primarily as it related to the export of Canadian natural gas to the U.S. market.

The Canadian Government was unwilling to authorize the Pre-build or the gas exports without further assurance from the United States that the entire Alaska Highway Project, including the Alaska segment, would eventually be completed. This assurance was forthcoming in a letter from President Carter to Prime Minister Trudeau, along with a Congressional resolution. As a result the southern Pre-build pipeline section was completed by 1982. This involved constructing 650 miles of 36 and 42 inch pipeline from Caroline, Alberta to Monchy and Kingsgate on the US border. The Pre-build and subsequent expansions were constructed pursuant to the Northern Pipeline Act and its regulatory regime managed by the Northern Pipeline Agency.

When the Pre-build construction began it was widely anticipated that North American natural gas demand would quickly resume its upward trend. However the market did not recover as anticipated and demobilization of the Alaska Highway Project soon began.

In order to remobilize, we will be required to make modifications and enhancements to various elements of the Alaska Highway Project regime. Pipeline designs will have to be modified so that the Project can respond to capacity and gas quality requirements of the shippers. We will have to incorporate the latest technology and techniques necessary to ensure that the maximum environmental protection measures are in place. We do not expect any difficulty in introducing these revisions which are so obviously of benefit to all parties.
Recently other parties have raised issues related to payments that might be due to withdrawn partners pursuant to the Alaska Northwest Partnership Agreement. We are confident that if any return of the withdrawn partners’ original investment is required it can be resolved within the context of an economically viable project.

Clearly there is a lot of work still to be done. It is very important to understand is that the advantages that come with the unique ANGTA and NPA regulatory regimes far outweigh the alternative of starting from scratch. Using the existing statutes and treaty we can assist in having Alaska natural gas into the U.S. market sooner, with competitive transportation costs and at the same time reducing project risks for all stakeholders.

In our capacity as the managing partner of Alaska Northwest we have maintained the Alaska Highway Project in good standing. We have kept the project alive to ensure that the advantages and benefits of the Project could be used in remobilization plans to expedite construction of the pipeline. We particularly wished to preserve what we see as the “special and unique fast track” regulatory regime.

Foothills and its shareholders have expended time and effort to keep the permits current and to optimize the project design. We do not intend to quit the field now that success is within sight.

The Alaska Permits – Federal

A substantial amount of work has been completed by the Alaska Highway Project sponsors to date. Before discussing the specific permits held by Alaska Northwest it is important to better understand the unique regulatory and legislative framework under which these permits were issued, namely ANGTA.

ANGTA and the President’s Decision remain in effect and can be terminated only by another act of Congress. ANGTA does not create a perpetual priority for the Alaska Highway Project. Rather, it establishes a priority designed to ensure that the Alaska Highway Project will be completed and begin initial operation in accordance with the decision of the President and
Congress. Once the Alaska Highway Project is in operation additional projects may be considered under the Natural Gas Act.

In implementing this priority, ANGTA requires that Federal agencies and officers expedite and issue “at the earliest practicable date” all permits and authorizations required by the Alaska Highway Project. In addition, ANGTA provides that applications and requests with respect to permits and authorizations required by the approved system “shall take precedence” over any similar applications and requests. Furthermore, ANGTA limits the discretion of Federal agencies and officers to include in certificates and permits for the Alaska Highway Project any conditions that would obstruct the system’s expeditious construction and initial operation.

As required by ANGTA, the FERC in 1977 expeditiously issued a conditional certificate of public convenience and necessity for the Alaska Highway Project. That certificate contains no expiration date and is still in effect today.

In addition, Alaska Northwest holds a federal right-of-way grant issued in 1980 by the Department of Interior’s Bureau of Land Management. That grant does not expire until December 2010, and may be renewed at the request of Alaska Northwest.

Furthermore, Alaska Northwest holds two recently extended Clean Water Act wetlands permits issued by the Army Corps of Engineers in coordination with many other agencies. Those permits were extended through September of 2007.

While these various federal permits were issued some time ago, they all are valid today. Indeed, nothing in ANGTA or in the certificates and authorizations issued for the Alaska Highway Project thereunder provides for the expiration of the chosen system’s priority because completion of the Alaska segment was postponed until the U.S. domestic market could support it. Rather, the Alaska portion of the Alaska Highway Project has been held in reserve until the need for additional natural gas arises in the Lower 48 states is such that this section can be completed. As sponsors we have actively protected the preserved Alaska segment by maintaining all necessary certificates and permits and actively overseeing the rights-of-way.
We recognize that these certificates and permits need to be "updated" to capture changes in technology, markets and environmental requirements. We will do such updating, and it can be done within the ANGTA framework. To that end, a couple of additional points need to be emphasized before I move on to the State permits.

- First, ANGTA clearly envisions and provides for the ability to condition and to amend these permits. These powers are subject only to the limitation prohibiting changes in the "basic nature and general route" and actions that will "otherwise" prevent or impair in any significant respect the expeditious construction and initial operation of the Alaska Highway Project.

- Second, the Alaska Highway Project sponsors' requests for both new permits and amendments to existing permits must be given priority under ANGTA. This priority translates into a timing advantage for the Alaska Highway Project.

- Third, the authority of the Office of Federal Inspector, as transferred to the Secretary of Energy, also continues in effect today to expedite and coordinate federal permitting, enforcement of permit conditions, and facilitation and oversight of the construction and initial operation of the U.S. portion of the Alaska Highway Project.

- Fourth, ANGTA also provides for expedited and limited judicial review of actions taken by Federal agencies and officers.

- Finally, the Alaska Northwest Partnership is well along in permitting the Alaska Highway Project.

The Alaska Permits – State of Alaska

On the state side, Alaska Northwest has a pending State of Alaska right-of-way lease application. Recently, we have initiated discussions with the State officials regarding perfecting and processing the pending application. Also at the state level, Alaska Northwest holds certificates of reasonable assurances issued pursuant to Section 401 of the Clean Water Act and a determination of consistency with the Coastal Zone Management Act.
Additional Alaska Permits

While Foothills already holds the major permits necessary to construct the remainder of the Alaska Highway Project, there are additional permits and authorizations that will need to be obtained. For example, the Alaska Highway Project sponsors will need to acquire a permit under the Clean Air Act. However, these additional permits will be procured as the Project proceeds, and such procurement will not cause a delay in the expeditious construction of the Alaska Highway Project.

The Canadian Permits

On the Canadian side, Foothills holds two unique certificates or permits:

- Certificate of public convenience and necessity.
- Yukon right-of-way.

Certificate of Public Convenience and Necessity

The certificate of public convenience and necessity ("certificate") is the Order issued following a successful hearing before the National Energy Board (NEB) of a pipeline application. The information that is required to be filed for hearing purposes is delineated in regulation and includes details about supply and markets, environmental impact assessment, engineering, construction and operations plans and details about connecting pipeline facilities.

The preparation of the required hearing information generally takes one to two years to complete and the length of the hearing will be proportional to the level of controversy surrounding the issues.

Foothills has completed this phase of the process. We have the "certificates" that entitle us to build a pipeline, subject only to terms and conditions set out in the Alaska Highway Project regime.
The "certificates" are statutory. They were issued by the Parliament of Canada when it enacted the Northern Pipeline Act and are in keeping with the principles and intent of the U.S./Canada Agreement.

We acknowledge that the "certificates" were legislated 20 years ago and that some have raised questions about their scope and validity. Others suggest that the certificates are dated and accordingly must be reissued. The "certificates" are valid. We are on solid legal ground in this regard.

Changes to the pipeline design to accommodate new technical issues and improvements have previously been granted by the Northern Pipeline Agency both at the time of the construction of the original Pre-build facilities and later during the facility expansion.

However, fundamental changes to the Canadian "certificates" would require changes to both the legislation and the treaty. For example another project could not be approved under the Alaska Highway Project regime. Further the Northern Pipeline Act (incorporating the U.S./Canada Agreement) provides that the route for Alaska natural gas will be along the route set forth in Annex 1 to the U.S./Canada Agreement i.e. the Alaska Highway route. In the face of the provision of the Northern Pipeline Act and the U.S./Canada Agreement, a treaty with the force of law, it is difficult to see how the National Energy Board could entertain applications either for alternative pipeline routes for delivery of Alaska gas through Canada or applications by companies other than Foothills following the Foothills highway route for delivery of Alaska gas through Canada.

Given the above we may well ask what remains to be done before the project can proceed?

First of all, we do not have a commercial arrangement negotiated with the Alaska North Slope producers or other shippers. Achieving this commercial arrangement is our number one priority. We are confident that the mutual interests of all sides will ultimately lead to satisfactory arrangements.

Following the successful completion of such a commercial agreement, there are a number of terms and conditions that must be satisfied. These are set out in the Northern Pipeline Socio-economic and Environmental Terms and Conditions. It is our view that the terms and conditions are broad enough to accommodate modern environmental, engineering and construction...
practices. In fact, we addressed this issue when we pre-built the southern portion of the Alaska Highway Project pipeline.

Detailed design and engineering work also must be completed and approvals must be obtained from the Northern Pipeline Agency. It is this mechanism that I referred to when I indicated that we had a "fast track" regulatory process.

The Yukon Right-of-Way

I will take a few minutes to describe the status of our right-of-way through the Yukon. Foothills has been granted an easement in the Yukon. The current term of the easement is September 2012 and provisions are in place to renew the easement for a further term of 24 years. It is important to note that the easement is protected under the Encumbering Rights provisions of the Umbrella Final agreement which has been signed by the Government of Canada, the Government of the Yukon and the Yukon First Nations. The Final Settlement Agreements that have been negotiated with the Yukon First Nations contain specific provisions relating to the easement. In addition, the compressor stations locations and permanent access to the proposed stations are protected.

What does this mean? From our perspective this translates into certainty of land tenure and a significant timing advantage. Foothills has developed an excellent working relationship with the Yukon First Nations over the years and we are building on that relationship. Like the Canadian "certificates" the easements also constitutes an important asset. An asset not easily replicated.

Conclusion

Let me summarize and focus on some of the key points.

Foothills is a company with real pipelines and real customers.

When combined with our shareholders TransCanada and Westcoast, we transport 20% of all the natural gas consumed in the United States. And we have the know-how and the where-with-all to build the Alaska Highway Pipeline.

We have been involved in this project for 25 years.
We and our former partners have invested heavily to achieve the permits, certificates, rights-of-way and much of the engineering on the Alaska Highway pipeline.

A basic message that I want to leave with you is this, we have a...very unique and solid regulatory framework, it is a very valuable framework in terms of saving money and avoiding costly delays when building a pipeline. It is more than a collection of permits. It is a package, designed specifically to expedite building the Alaska Highway pipeline.

This framework can neither be duplicated nor terminated easily. It is a one-of-a-kind regime. I urge all Alaskans to take full advantage of it.

Finally let me raise one other issue and that is the matter of the pipeline route decision. Before we can move from discussion to action this must be resolved. Anything this committee can do to bring clarity to the routing debate will be a positive development.

Ultimately all stakeholders must find some common ground and go forward.

So where do we go from here?

A commercial agreement between pipelines and producers is the next major mile post for the Project.

Once a satisfactory commercial arrangement is achieved ... the flag drops; from that point on we believe that our regulatory framework will allow “shovels to be in the ground” within 24 months.

This is a very large project. It will involve many companies. It will cost a lot of money and there will be lots of issues to address and benefits to share.

Foothills and its shareholders intend to be major players in the development and operation of this important pipeline and we believe that we bring value to the Project and value to Alaska.

Thank you, and I am now prepared for questions.
Joe, here's what I've got on your question yesterday asking how many additional megawatts would be subject to the waste-to-energy tax credit in the year 2011.

As you know, we estimate that the tax credit would stimulate 200 megawatts of additional electricity. However, we estimate that it would be five years before any of this electricity is available. Furthermore, the full 200 megawatts would not be available immediately in the fifth year; additional production would grow to 200 megawatts over a period of time.

For purposes of a rough calculation, we assume that the credit becomes effective in FY 2002 and that no electricity eligible for the credit is generated for 5 years, i.e., until FY 2006. We further assume that for the next 4 years, from FY 2007-2010, the amount of electricity eligible for the credit increases incrementally, by 50 megawatts per year. As a result, the full 200 megawatts of electricity is being produced in FY 2010 through 2012.

If you accept our estimate that the cost of the credit is $27 million per year (assuming 200 megawatts/yr), then the cumulative cost of the credit through the year FY 2012 is something around $121.5 million (which is the sum of $6.75m + $13.5m + $20.25m + $27m + $27m +$27m). Of course, this number will vary if assumptions are different concerning how quickly the tax credit stimulates new production.

On the question of equivalent barrels of oil, Katie advises that IWSA has done an estimate showing that 200 megawatts of electricity displaces, on a Btu basis, 2.8 million barrels of oil per year. She says she's got the mathematical proofs if you want 'em!

I think I mentioned to you in an earlier phone message that Mike Pate from my office took IWSA in to visit with Treasury Department folks yesterday afternoon. Katie was in that meeting if you have questions. Hope this is helpful.
Joe,

I'm glad to hear that. Please remind me--did I send you the full set of policy recommendations (about 12) that we put together, or just a few selected ones? If only a few, I will send you the complete set. Also, did I send you our new report on "Using Targeted Energy Efficiency Programs to Reduce Peak Electrical Demand" by Nadel et al?

Please let me if you would like to meet to go over any of this, and last but not least (as I mentioned over the phone), I really hope the Administration does not proceed in proposing a major cut in energy efficiency and renewable energy R&D and deployment programs for FY02. This is not only a bad idea, but it would be severely criticized by folks like us and I believe it would tarnish the overall effort to advance a broad, balanced set of energy policy initiatives.

Howard

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Reply Separator

Subject: national energy policy
Author: "Kelliher Joseph" <Joseph.Kelliher@hq.doe.gov> at internet-mail
Date: 02/27/2001 1:39 PM

Howard, thanks for the information you sent me. I just wanted to restate our interest in your specific recommendations on energy efficiency elements for incorporation in the Administration's national energy policy.
Joe Kelliher: Attached is a short document which includes NPRA's current thinking as to what changes in national energy policy are needed to help the refining sector.

I would like specifically to highlight three:

One. We believe that the Administration is missing an important opportunity to improve energy policy by not addressing the onroad diesel sulfur rule. This rule will have a greater adverse supply impact than any other in the next five years and should be reviewed. Instead of requiring essentially 100% of onroad diesel output to be reduced from 500 ppm to 15 ppm sulfur by mid-2006, at a cost of $8 billion, the Administration could move the required supply date back to 2008-9 and provide a reduction in the excise tax for 15ppm sulfur diesel sold in advance of the 2008 date. This could provide all the necessary supply for new trucks which need the diesel in 2006-7 (probably only 5% of demand). There are no environmental benefits from using the new diesel in old truck engines, so the program in its current form constitutes massive waste, since those trucks aren't a sufficient force in the market until 2008 at the earliest. This change will help prevent loss of diesel supply and refinery closures which will take place under the rule in its current form. The overall benefits of the program are not reduced. We would like to talk with you more on this.

Two. The EPA's enforcement campaign against U.S. refineries should be halted and reexamined. As you know, it is impossible to build new refineries, so the industry has had to add capacity at existing sites in an attempt to maintain an adequate supply of products for consumers in the past twenty years. Even at that, the industry has been able to keep U.S. capacity only flat over the past decade, so new demand has been met by increased imports of refined products. The Browner EPA launched an extensive and coordinated campaign against the industry, alleging that capacity additions during the past twenty years were not appropriately permitted. This despite the fact that refinery improvements were made with the knowledge of both state and federal environmental agencies and in keeping with permitting requirements as they were understood at that time. The EPA
n section 114 requests, in effect blanket subpoenas, to most refiners, and many are now facing notices of violation and legal action. A few have settled because they believe that it is easier to pay a fine, sign a consent decree and move forward than resist. All this comes at a time when federal and state authorities have urged the industry to continue its herculean efforts to produce product all-out to avoid shortages. EPA's actions are really nothing more than an attempt to discredit the industry and collect tribute in the form of fines in order to allow refiners to get on with their business. We believe that everyone in the industry should obey the law, and we believe that they do, often under difficult circumstances. But this activity goes far beyond the pale of reasonable enforcement activity and should cease.

Three. The Unocal patents, recently upheld by a federal court of appeals in a decision that the Supreme Court let stand, provide no real benefit to the industry or consumers. The huge royalties granted by a California District Court--5.3/4 cents/gallon--are far in excess of the cost of even the reformulated gasoline program and may well cost consumers over $200 million per year when implemented. The existence of the patents will increase the cost of gasoline, reduce supply, and eliminate all of the incentive for overcompliance with environmental regulations. The patent will also make it even harder to use ethanol in gasoline where ozone problems exist during the summer months (e.g. Chicago and Milwaukee). The Administration should study this issue and take steps to put any royalty collections on hold. Otherwise, this situation will affect Midwestern and East Coast gasoline supplies adversely this summer, as it did last year.

The rest of our thinking is attached. Thank you for your call yesterday. I'm available to discuss these matters with you at any time.

Bob Slaughter
NPRA 202.457.0480 x 152; home

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<<natenergyp012.doc>>
**National Energy Policy: Themes**

- Stable, reliable and affordable supplies of energy and more efficient energy use are essential to maintaining living standards and supporting economic growth.

- Greater emphasis should be placed on diversifying the sources of US energy supplies. Domestic supplies can be enhanced through incentives for improved recovery from existing fields and through improved access to promising acreage.

- Energy policy cannot just focus on the "upstream" sector, i.e. exploration and production. There needs to be a clear understanding that local/regional bottlenecks can occur in producing and distributing feedstocks and products. Further, refineries have been operating near maximum capacity and it has been almost twenty years since a new refinery has been built.

- Petroleum product pipelines are increasingly challenged by the proliferation of "boutique" (area-specific fuels) due to limits on their ability to handle segregated shipments and availability of adequate storage tank capacity. And, additional constraints may arise from the need to gain regulatory approvals for new facilities or pipelines, e.g., the Longhorn pipeline recently agreed not to carry MTBE products in order to gain approval.

- Siting and permitting challenges can seriously delay needed modifications/expansions of existing manufacturing (refining and petrochemical) capacity and constrain additions to downstream infrastructure (e.g. pipelines).

- No single action or single fuel can resolve all energy concerns. The nation needs a balanced mix of policies – which fosters a mix of fuels and balances environmental goals and energy supply concerns.

- A balanced approach to energy policy should examine both demand and supply. Incentives for greater energy efficiency (e.g. through the use of lighter weight materials in vehicles) can play an important role.

- Regulatory programs that distort markets can divert energy supplies from essential (i.e., where there are limited, if any, substitutes) and/or highest valued markets. For example, environmental programs are increasingly drawing natural gas to use in electric generation, thus depriving petrochemical manufacturers of feedstocks or making them so costly that the US petrochemical industry is placed at a competitive disadvantage in global markets.

- Both energy and environmental policy should be based on sound science and the best and most current data available. Cost-benefit analyses and reasonable risk assessment are key tools for choosing the most effective policies to achieve national goals. Regulations should:
  - take into account the cumulative effect of regulations in that sector;
  - set performance goals and avoid mandating specific technologies or setting product specifications;
  - provide adequate leadtime and avoid overlapping requirements wherever possible;
  - provide flexibility through the use of market-based incentives; explicitly evaluate their impact on energy supplies; and
be fairly and consistently enforced, without retroactive reinterpretation of regulations through enforcement programs.

Potential Energy Policy Improvements

Process

- Require annual study by Secretary of Energy of refining and product distribution infrastructure including assessment of cumulative impact of regulations and specific recommendations for improvements.

- Periodic OMB-led review of supply impact of environmental regulations. Could be included as part of National Energy Policy Plan.

- Require Energy Impact Analysis for new regulations.

- Enhance regulatory certainty, e.g., avoid retroactive reinterpretation of regulations such as in recent EPA NSR enforcement actions.

Incentives

- Accelerated depreciation for clean fuels upgrades.

- Accelerated depreciation for pollution control equipment on stationary sources.

- Tax credits for energy efficiency improvements.

- Investment tax credit for clean fuel capital investments.

- Relief from Alternative Minimum Tax to ensure any incentives offered are not automatically recaptured.

- Excise tax incentives for early introduction of clean fuels, e.g. for low sulfur gasoline and diesel.

Streamlining/Flexibility

- Reasonable guidance on BACT and LAER for Tier 2 gasoline and diesel sulfur programs. Guidance on the emissions level and cost used to determine BACT/LAER requirements. [NOTE: Current draft guidance is not reasonable on this point].

- Allow for trading of credits from mobile source emission reductions with stationary sources.

- Expedited permitting review. Provision of greater certainty that once permits are approved, they will not have to be reopened/renegotiated due to third party intervention.
- Linkage between regulatory implementation deadlines and permitting process, e.g., if delay in permitting despite good-faith efforts to comply, the regulatory deadline is adjusted.

**Fuels**

- Reassess the sequencing of major fuel regulatory programs. Eliminate the overlap in timing between the gasoline sulfur and diesel sulfur requirements.

- Eliminate 1.5% minimum oxygen requirement for RFG.

- No additional product specifications (such as aromatics caps) that will further constrict gasoline supplies. Focus on performance goals not product specs.

- Reassess mobile source air toxics program to allow greater flexibility through trading among refineries. Reevaluate baseline calculation to remove penalty on refiners who are cleaner than average. Reevaluate standard in light of state programs that limit MTBE use (e.g., Connecticut, New York) which could make regulatory requirement unattainable or very expensive.

- National Academy of Sciences study of MTBE to provide a science-based assessment of impact on groundwater and effectiveness of remediation technologies and including assessment of role of MTBE in meeting gasoline demand.

- Determine appropriate sequencing for any future off-road diesel requirements. Avoid overlap with other regulations, set a reasonable standard for sulfur content.
50% more energy efficient homes!

Pulte Homes southwest division has utilized technical assistance from DOE's Building America program to create what one residential expert calls "the best production house in the world," which won the 2001 National Association of Home Builders Energy Value Award. In Tucson, Phoenix and Las Vegas, Pulte Homes has worked with DOE to redesign the energy features of its basic models. Using advanced insulation techniques, highly efficient equipment and windows, and right-sized heating and cooling systems, the homes look the same but perform so well they use half the energy for heating and cooling at virtually no increase in construction costs. The whole building, systems engineering approach used in Building America allows the builder to add more insulation and more efficient windows while reducing the size of the heating and cooling equipment. The trade-off means no added cost to the builder, better value for the buyer, reduced electric load for the utility, and improved affordability.

For more information, you may contact Randy Foltz or Dave Beck at Pulte Homes (702 256-7900).
Helpful to use redline method if you can!
CORE PRINCIPLES FOR RELIABILITY LEGISLATION

Accreditation of a single North American SRRO
- FERC to approve a single SRRO.
- Procedures for an applicant to apply for SRRO status, and the procedures and requirements for FERC to approve such an application.
- Requires that all system operators be members of the SRRO.
- Provides procedures for the SRRO to modify its procedural, governance and funding rules.

Authority for that SRRO to set and enforce standards
- Specifies the procedures for the SRRO to file with FERC for approval of reliability standards.
- Provides that such proposed standards are to be approved unless FERC finds that they are unjust, unreasonable, unduly discriminatory or preferential, or otherwise not in the public interest.
- Provides that FERC is to give due weight to the technical expertise of the SRRO.
- Gives the SRRO the authority to enforce its standards, subject to FERC review.

Allowance for the SRRO to delegate authority for implementation of standards and enforcement of compliance to regional organizations
- Permits the SRRO to delegate certain authority to regional entities by agreement.
- Such agreements would be filed with FERC for approval.

Funding authority
- Provides for the assessment and allocation of SRRO and regional entity costs to system operators, to be recovered from system users, through a non-bypassable charge.

International arrangements
- Governs international agreements and recognition of the SRRO.

Anti-trust protections
- Provides for a rebuttable presumption that activities undertaken under the Act are in compliance with the antitrust laws.

Transition mechanism
- Provides for the optional filing with FERC of existing standards by NERC and regional councils prior to approval of an SRRO, which FERC could approve and enforce.

March 1, 2001