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

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

BY THE COMMISSION:

Summary

We reject Tariff Advice Letter 139-4 (TA139-4) which includes the gas supply contract, APL-5, because ENSTAR[1] did not meet its burden of demonstrating that gas supplies pledged under the contract are reliable and that the price is reasonable. We allow APL-5 to go into effect without our approval to the extent that APL-5 has the effect of decreasing the current average cost of system gas supply in any

[1]ENSTAR Natural Gas Company is a division of SEMCO Energy, Inc. (SEMCO). Alaska Pipeline Company (APLC) is a wholly-owned subsidiary of SEMCO. APLC, not ENSTAR Natural Gas Company, 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.

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year of its implementation subject to ENSTAR making supplemental filings addressing Section 2.7.4 of APL-5.

Background

At issue in this proceeding is TA139-4 filed November 14, 2005, in which ENSTAR requested our approval of a new gas supply contract, APL-5, with Marathon Oil Company (Marathon) providing for deliveries beginning in 2009.[2] ENSTAR operates under Certificate of Public Convenience and Necessity Nos. 4 and 141 as a natural gas transmission and distribution utility in Southcentral Alaska. Marathon is a current ENSTAR supplier under a Gas Purchase Agreement dated May 1, 1988.[3]

ENSTAR requested that the commission approve the addition of APL-5 as a base supply contract to its tariff[4] and also requested inclusion of all costs related to the contract in the calculation of ENSTAR's Gas Cost Adjustment.[5]

ENSTAR's tariff requires we approve any gas sales agreements that increase ENSTAR's current average cost of gas. Tariff Sheet 90, Section 708f, provides:

> Base Supply Contracts.
>
> The base supply contracts are those contracts in effect on September 1, 1987. Additional contracts or revisions of base supply contracts having the effect of increasing the current average cost of system gas supply will be made, subject to Commission approval, by filing with the Commission, 45 days prior to the proposed effective date of such addition or revision, a copy of such addition or revision. Additional 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.

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[2]H-1 at 1.

[3]T-9 at 5.

[4]H1-C (Tariff Sheet Nos. 89 and 221).

[5]*Id.*

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ENSTAR believes that a secure supply of gas that is reliably available when its customers most need it is the utility's absolute top priority.[6] ENSTAR's gas supply contracts require ENSTAR to provide an annual forecast of its needs and supplies for the next ten years each October[7] in its "Buyer's Annual Forecast."[8] ENSTAR calculates its annual gas requirements based on existing supplier commitments and identifies any year in which there may be a supply shortfall ("Buyers Unmet Requirements").[9] Under ENSTAR's contact with Unocal,[10] Unocal has the right to supply any projected shortfall for five years into the future, beginning October 10, 2004. ENSTAR may not take gas from any third party so long as Unocal's total commitment of gas brings ENSTAR's unmet requirements to zero.[11]

In October 2004, ENSTAR projected unmet requirements beginning in 2008 and 2009.[12] Unocal was unable to commit to provide all of the additional gas needed for 2009.[13] ENSTAR notified other Cook Inlet producers of its need for new gas supplies. Marathon was the only gas producer that offered to meet ENSTAR's unmet requirements, including its full swing requirements, beginning in 2009 and continuing for a reasonable period.[14]

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[6] T-1 (Izzo) at 3.

[7] T-7 (Dieckgraeff) at 19.

[8] H-1B at 3.

[9] H-1B at 4.

[10] H-26 at 11.

[11] *Id.*

[12] T-7 (Dieckgraeff) at 6.

[13] *Id.*

[14] T-7 (Dieckgraeff) at 10.

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ENSTAR's swing ratio is approximately 3.0, meaning its forecasted peak winter demand can be three times greater than its average daily demand. Chugach[15] and ML&P[16] have swing ratios ranging from 1.4 to 1.6 because electricity usage does not fluctuate as dramatically from season to season as does the demand for gas for space heating purposes. The industrial plants operating on the Cook Inlet - Agrium, the LNG[17] plant, and the Tesoro Refinery - have virtually no swing. They consume a more or less steady volume year-round.[18]

ENSTAR has elected not to develop storage to meet its deliverability requirements. Rather, ENSTAR "subcontracts" this important service to its suppliers.[19] Many gas distribution utilities in the Lower 48 use gas storage facilities to meet deliverability. SEMCO, in Michigan, uses a combination of leased and company-owned storage totaling 15.1 Bcf[20] to provide approximately 40 percent of its winter supply requirements and 25 percent of its peak-day requirements.

ENSTAR has contractual commitments from a 1988 contract with Marathon (APL-4), a 1982 contract with the Beluga producers (Chevron, ConocoPhillips, and ML&P), a 2000 contract with Aurora (also called the Moquawkie Contract), and a 2000 contract with Unocal.[21]

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[15]Chugach Electric Association, Inc. (Chugach).

[16]Municipality of Anchorage d/b/a Municipal Light & Power (ML&P).

[17]Liquefied natural gas (LNG).

[18]T-1 (Izzo) at 13.

[19]*Id.*

[20]One billion standard cubic feet (Bcf).

[21]T-7 (Dieckgraeff) at 6.

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The committed volumes supplied by the Beluga, Moquawkie, and APL-4 contracts are declining as illustrated by ENSTAR's 2005 Buyers Annual Forecast as follows:[22]

EXHIBIT A

TO THE OCTOBER 14, 2005 GAS SALES AGREEMENT BETWEEN MARATHON OIL COMPANY AND ALASKA PIPELINE COMPANY

ARTICLE XIVBUYER'S ANNUAL FORECAST

Buyer's Annual Gas Requirements (Bcf)	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Total Annual Requirements	26.70	27.50	28.30	29.0	29.7	30.30	31.00	31.60	32.20	32.70
Existing Commitments:										
Beluga	1.10	0.80	0.70	0.60	0.00	0.00	0.00	0.00	0.00	0.00
Marathon APL4	13.00	11.00	9.00	7.00	5.00	5.00	5.00	5.00	5.00	5.00
Moquawkie	1.80	1.50	1.10	0.80	0.60	0.50	0.30	0.30	0.20	0.00
Unocal Commitments	10.80	14.20	17.50	19.00	16.00	13.00	10.00	7.00	4.00	1.00
Total Existing Commit.	26.70	27.50	28.30	27.40	21.60	18.50	15.30	12.30	9.20	6.00
Unocal Conditional Option	0.00	0.00	0.00	0.00	3.00	6.00	9.00	12.00	15.00	18.00
Marathon APL5 Initial Annual Commitment	0.00	0.00	0.00	1.60	5.10	5.80	6.70	7.30	8.00	8.70
Marathon APL5 Additional Commitment	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total Marathon Commit.	0.00	0.00	0.00	1.60	5.10	5.80	6.70	7.30	8.00	8.70
Additional Third-Party Commitments	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Unmet Requirements*	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Starting in the mid-1970s, ENSTAR's first gas supply contract (APL-I) had a portion of its price indexed on a component of the producer price index. The price adjustment term for the Marathon APL-4 contract and Beluga Contract is based on the NYMEX[23] oil futures. The price adjustment term for the Moquawkie contract is based on the Gross Domestic Product Implicit Price Deflator (GDPIPD), a national measure of inflation. In the Unocal and NorthStar[24] contracts, the price itself is based on a

[22]H-1A, Ex. A at 44-46.

[23]New York Mercantile Exchange (NYMEX).

[24]As of the hearing date, there were no volumes committed from the NorthStar contract.

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36-month daily average Henry Hub natural gas futures.[25] We have attached an appendix which illustrates the differing prices of ENSTAR's gas supply contracts.

ENSTAR presents its new supply contract with Marathon which "should insure that ENSTAR has sufficient gas to meet all of its customers' requirements through at least 2016."[26] Marathon provides all the gas needed by ENSTAR above that which comes from fixed volume contracts. APL-5 is effective October 14, 2005, with the full requirements provisions effective for Contract Years 2009 through 2016.[27] Marathon makes available 62.8 BCF of Proven Reserves to meet its Initial Annual Commitment.[28] There are limits on Marathon's rights to sell gas produced from its Proven Reserves if it can not meet its obligations under APL-5.[29] ENSTAR will have a priority on Marathon's gas delivered into the Cook Inlet area, except for Marathon's existing commitments;[30] and any subsequent contract entered into or any existing contract modified by Marathon must recognize this priority.[31]

The contract price (Index Price) of gas under APL-5 is set annually in October for the next year beginning January 1.[32] The Index Price is calculated using the simple daily average price of the NYMEX Henry Hub natural gas futures market during the preceding twelve months ending September 30.[33]

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[25]T-7 (Dieckgraeff) at 16.

[26]H-1 at 2.

[27]H-1A at 1.

[28]*Id.*

[29]*Id.* at 2.

[30]H-1A, Ex. E.

[31]T-7 (Dieckgraeff) at 15.

[32]H-1A at 2.

[33]*Id.* at 3.

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The Index Price is discounted as follows to determine the Contract Price (defined in Section 3.1, p. 22 of APL-5) which is subject to a Floor and a Ceiling:

i. If the Index Price is $6.00 per Mcf[34] or less, the Contract Price equals the Index Price;

ii. If the Index Price is greater than $6.00 per Mcf and equal to or less than $8.00 per Mcf, the Contract Price equals $6.00 plus 80 percent of the difference between the Index Price and $6.00;

iii. If the Index Price is greater than $8.00 per Mcf and less than or equal to $10.00 per Mcf, the Contract Price is $7.60 plus 95 percent of the difference between the Index Price and $8.00;[35]

iv. If the Index Price is greater than $10.00 per Mcf, the Contract Price is $9.50 plus 85 percent of the difference between the Index Price and $10.00,[36]

APL-5 has a floor price, the minimum price Marathon will receive from ENSTAR, which is set at $4.25 adjusted annually by one-half the annual rate of inflation based on the GDPIPD.[37]

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[34]One thousand standard cubic feet (Mcf)

[35]H-1B, Section 3.1(iii) at 23.

[36]H-1A at 3.

[37]H-1B, Section 3.3 at 23-24 - The Floor Price is equal to the initial price of $4.25 times one plus the floor price adjuster divided by 2. The floor price adjuster is the GDPIPD for the quarter ended June 30 of the year before the price is calculated, divided by GDPIPD for the quarter ended June 30, 2006.

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APL-5 also has a ceiling price of $15.00 that is adjusted annually by one-half the annual rate of inflation based on the GDPIPD; however, the cap cannot change by more than 1.5 percent per year.[38]

APL-5 requires ENSTAR to pay Marathon $0.25 per Mcf as a gas transportation fee to ship the gas to ENSTAR's pipelines. There is also an Excess Peaking gas fee of $2.50 per Mcf for gas that Marathon provides in excess of its pro rata share of ENSTAR's peak day gas requirements. Additionally, APL-5 requires ENSTAR to reimburse Marathon for all production taxes on gas purchased by ENSTAR.[39]

We have previously decided the ENSTAR-Unocal Gas Sales Agreement (Unocal GSA)[40] and the ENSTAR-NorthStar Gas Sales Agreement (NorthStar GSA).[41]

Unocal Gas Sales Agreement

On October 25, 2001, we issued Order U-01-7(8) conditionally approving a Unocal GSA between ENSTAR and Unocal. Unocal and ENSTAR characterized the Unocal GSA as an exploration contract because the focus of the contract was

[38]H-1B, Section 3.4 - The Ceiling Price is equal $15.00 times one plus the ceiling price adjuster divided by 2. The ceiling price adjuster is the GDPIPD for the quarter ended June 30 of the Year before the Year for which the Price is calculated, divided by GDPIPD for the quarter ended June 30 of the Year two years before the year the Contract Price is calculated. However, the calculation of the ceiling price in any contract year, the ceiling price adjuster used in such calculation will not be more than 1.0300.

[39]H-1B, Article V.

[40]Docket U-01-7, *In the Matter of the Gas Sales Agreement Between ALASKA PIPELINE COMPANY, a Wholly-owned Subsidiary of SEMCO ENERGY, INC., of Which the ENSTAR NATURAL GAS COMPANY is a Division, and the UNION OIL COMPANY OF CALIFORNIA, Filed as TA117-4.* TA117-4 was filed December 12, 2000.

[41]Docket U-03-84, *In the Matter of the Gas Sales Agreement between ENSTAR Natural Gas Company, a division of SEMCO ENERGY INC. and NORTHSTAR ENERGY GROUP, INC. filed as TA125-4.* TA125-4 was filed August 8, 2003.

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exploration for new gas sources.[42] Under the contract Unocal committed to spend in excess of $10 million over two years looking for new gas fields.

The Unocal GSA was the first time we allowed a gas supply contract to be priced to a market index, Henry Hub natural gas futures. We found that ENSTAR needed to pay a competitive price to attract exploration capital and that a price tied to Henry Hub with a floor of $2.75 was a reasonable balance of the risks associated with gas exploration and the need to assure an adequate supply of gas to ENSTAR.[43]

Northstar Gas Sales Agreement

On March 23, 2004, we issued Order U-03-84(7), conditionally approving a full requirements gas sales agreement between ENSTAR and Northstar to serve Homer for twenty years beginning at the first delivery under the contract.[44]

NorthStar stated it would spend between $8 and $12 million for expenses associated with drilling, completing, and testing wells that target new gas reserves and constructing a pipeline.[45] We found that the investment required of NorthStar prior to the opportunity to sell gas, the requirement to prove additional reserves, and the requirement to drill a second 'commercial quality gas field' well as justifications for Henry Hub pricing.[46]

Hearing Proceeding

We convened a hearing on APL-5. It began on July 6, 2006, and continued through July 13, 2006, when it was recessed because Marathon refused to

[42]Order U-01-7(8) at 8.

[43]*Id.* at 9.

[44]Order U-03-84(7) at 4

[45]*Id.* at 5.

[46]*Id.* at 10.

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provide discovery we ordered. ENSTAR presented the testimony of Paul R. Carpenter (Carpenter); Anthony M. Izzo (Izzo); Oliver Scott Goldsmith (Goldsmith), and Daniel M. Dieckgraeff (Dieckgraeff).[47]

The hearing resumed on August 22, 2006. Intervenor James L. Walker (Walker) presented testimony and was cross-examined[48]. Marathon presented the testimony of Bruce B. Henning (Henning) and Catherine M. Elder (Elder).[49] The Attorney General (AG) presented its witness Arlon R. Tussing (Tussing).[50] Tesoro presented Benjamin Schlesinger (Schlesinger).[51] The final witness was C. Les Webber (Webber), sponsored by Marathon, who had previously been unavailable due to scheduling conflicts.[52] On Sunday, August 27, 2006, we heard closing argument by the parties.[53] The positions of the parties are summarized below.

Positions of the Parties

ENSTAR

ENSTAR requests Commission approval for the addition of APL-5 to Section 708 of ENSTAR's tariff as a base supply contract and for inclusion of all costs related to the contract in the calculation of ENSTAR's Gas Cost Adjustment, including Henry Hub pricing.

ENSTAR stated that it supports using a 12-month trailing average of the Henry Hub Index (Trailing HHI) because it provides 240 data points of actual

[47]Tr. at 118-1261.

[48]Tr. at 1298-1399.

[49]Tr. at 1399-1656.

[50]Tr. at 1687-2050.

[51]Tr. at 2052-2308.

[52]Tr. at 2318-2478.

[53]Tr. at 2054-2619.

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transactions in a highly liquid, transparent, and competitive natural gas market. ENSTAR added that the Trailing HHI reflects price changes more quickly than the 36-month trailing average HHI used in Unocal GSA and NorthStar GSA. ENSTAR stated that a 12-month trailing average in APL-5 buffers the Unocal GSA by reflecting falling prices. An additional advantage of the Trailing HHI price is that it is market-responsive, thereby mitigating the risk that, over the term of the contract, the price will be higher than the HHI price.[54]

ENSTAR asserted that the Henry Hub is a dominant market reference and the commission twice sent signals to the market indicating that contracts with trailing averages of Henry Hub represent a fair price. ENSTAR absolutely believes APL-5 is a fair market price, and that ENSTAR got this gas for less than straight Henry Hub price even with a ceiling. ENSTAR asserted that Cook Inlet gas is in scare supply and that APL-5 diversifies ENSTAR's supply portfolio.

ENSTAR maintained that the purpose of the Henry Hub price was to stimulate additional exploration and development of reserves in Cook Inlet. ENSTAR added that the price needs to be high enough to attract investment capital to this market compared to other markets. ENSTAR stated that the Henry Hub is what the Department of Energy (DOE) uses as a comparative reference. ENSTAR stated that two alternatives have been proposed, one on the West Coast and one in Alberta, but points out that both those markets have a lot of supply. ENSTAR added that the supply and demand balance in those markets is not the same as it is in the Cook Inlet market. ENSTAR hoped that, over the long haul, the Cook Inlet market would come into some sort of a balance.[55]

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[54]TA139-4 at 5.

[55]Tr. at 671-578.

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ENSTAR proposed the $4.25/Mcf price floor and the ceiling being capped at $15.00/Mcf, noting that the floor and cap are adjusted annually by one-half of inflation, but the cap cannot change by more than 1.5 percent from year-to-year. The purpose of the cap and floor is to force the price to fall within a relatively narrow range and to avoid extreme swings in price.[56]

ENSTAR explained that the floor and the ceiling were agreed to by the parties as a mutual allocation of risk.[57] ENSTAR explained that the floor and ceiling price were negotiated terms, and in its opinion, not arbitrary.[58]

APL-5 requires ENSTAR to pay a transportation fee of $0.25/Mcf to Marathon for transportation of all gas provided to ENSTAR. The transportation fee is intended to cover the construction, installation, and operation of Marathon's production, gathering, treating, and processing facilities; and all pipelines necessary to deliver gas to ENSTAR. The alternative, according to ENSTAR, would be to pay the actual tariff for each pipeline, which creates risks that arise from the new regulation of most Cook Inlet gas pipelines. ENSTAR added that the use of actual tariffs is also unworkable because Marathon will have two contracts with ENSTAR; and gas will be delivered simultaneously under both contracts starting in 2009, so there is no way to determine which gas molecules are from APL-4 or APL-5. ENSTAR does not think it wise to expose its customers to these risks and proposes a fixed rate as best for its ratepayers.[59]

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[56]TA139-4 at 5, Tr. 453.

[57]Tr. at 229.

[58]Tr. at 139.

[59]TA139-4 at 6.

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ENSTAR asserted that there is no limitation to the transportation fee, whether a pipeline is preexisting or constructed later.[60] ENSTAR added that Marathon has not indicated from where it plans to ship the gas. ENSTAR further added that it is conceivable that Marathon will be shipping gas through preexisting pipelines, newly-constructed pipelines, and newly-regulated pipelines.[61] ENSTAR stated that Marathon indicated it may ship gas over the Kenai-Nikiski Pipe Line, Cook Inlet Gas Gathering System, and Beluga, which are now regulated pipelines.[62]

APL-5 requires ENSTAR to pay a peaking gas fee of $2.50/Mcf, in addition to the price of the gas for all gas delivered in excess of Marathon's pro rata share of ENSTAR's peak day gas requirements. According to ENSTAR, the additional charge of $2.50/Mcf (in addition to the HHI price) was necessary, if ENSTAR requests and Marathon provides gas (1) in excess of Marathon's pro-rata share of what it would provide on the peak day or (2) in excess of the flow rate that if sustained for 24-hours would cause Marathon to supply more than its pro-rata share of the peak day requirement. However, if the reason for the request for excess gas is due to an inaccurate forecast by ENSTAR of its estimated peak day requirement, the incremental charge of $2.50/Mcf is not applied and the price payable is the HHI price.[63]

ENSTAR stated that the peaking fee contract provision supports the notion that a full requirements contract with swing has a great deal of value. ENSTAR continued that providing for swing is also costly for a producer not in a position to be

[60]Tr. at 851.

[61]Tr. at 852.

[62]Tr. at 853-854.

[63]TA139-4 at 6.

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able to itself go to the spot market and pick up emergency supplies to backfill a contract. ENSTAR stated that swing has value to a buyer and costs to a seller.[64]

ENSTAR also reported awareness that Marathon provided peaking gas to a third party at basically the same price as the peaking price under the Unocal contract. ENSTAR stated that the price for the peaking gas in the Unocal contract price is base price plus $1.00 per Mcf. ENSTAR stated that the reason Marathon received the $2.50/Mcf peaking fee was that it was part of the overall contract negotiations.[65]

APL-5 provides that ENSTAR will reimburse Marathon for all production taxes. ENSTAR asserted that the price includes all royalties. ENSTAR added that these provisions are essentially identical to the Unocal and NorthStar contracts.[66] ENSTAR added that the producers have insisted upon provisions for tax reimbursement in all of ENSTAR's gas supply arrangements since the mid-1970s. ENSTAR stated that no one needs to look further than the flurry of activity around production taxes in the recent legislative session to understand why. ENSTAR added that under the current statutory scheme, the provisions for oil production taxes also apply to gas production taxes.[67]

Marathon will be ENSTAR's full requirements supplier beginning in contract year 2009 and ending in contract year 2016; however, Marathon may provide gas into the future beyond 2018. ENSTAR added that APL-5 is a relatively short-term contract compared to ENSTAR's other gas supply contracts. Further, Marathon has committed to supply ENSTAR's unmet requirements through 2016 and Marathon has

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[64]Tr. at 283-286.

[65]Tr. 1179-1180.

[66]TA139-4 at 7.

[67]T-7 at 19.

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no right to "put" additional gas to ENSTAR unless shortfalls occur for specified reasons during those years. ENSTAR added that Marathon has an option to offer additional gas to ENSTAR under various circumstances; however, ENSTAR has the option to take or not take the optional gas. ENSTAR asserted the contract's term balances the need for an assured gas supply against the possibility that less expensive or alternative gas supplies might become available from the North Slope or new Cook Inlet discoveries or developments.[68]

ENSTAR offered three reasons why APL-5 does not have a limitation on the amount of gas that Marathon can purchase each year and resell. First, when gas is scarce it is not desirable to make it more difficult to discover, produce, deliver, or to otherwise limit the seller's alternatives to procure gas to meet ENSTAR's requirements. Second, Marathon is not obligated to but may wish, in the future, to develop storage facilities for meeting some of its commitments to ENSTAR. ENSTAR stated that purchasing gas when it is available (typically during the summer) and putting it into storage for the winter is very desirable because that maximizes the gas available for ENSTAR. Third, the proposed APL-5 is relatively short-term and it would be beneficial if Marathon can offer additional gas as a result of purchases. ENSTAR does not expect that Marathon will purchase significant quantities of gas to meet its obligations, but believes it unwise to constrain that option during the term of APL-5.[69]

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[68]TA139-4 at 4.

[69]TA139-4 at 5.

Marathon

Marathon supports APL-5 and offers its opinion that the agreement satisfied the "public interest" standard adopted by the commission.[70] Marathon stated that it invested significant amounts of capital to prove up and develop its gas reserves so it can fully serve ENSTAR. As a result of its investment Marathon can now provide a long term secure supply to ENSTAR and its customers.[71] Marathon added that in the contract negotiations it made significant concessions to benefit ENSTAR's customers regarding the pricing of the gas and other key terms.[72] Marathon stated that APL-5 was carefully structured to satisfy the commission's public interest standard, as well as to balance the needs of each of the parties and that in its opinion the public benefits from approval of APL-5.[73] Marathon was the only gas producer that offered to meet specific load-following needs of the ENSTAR customer base and is willing to also meet ENSTAR's unmet requirements beginning in 2009 and for a reasonable period thereafter.[74] In its role as an ENSTAR gas supplier meeting ENSTAR's considerable swing and peak requirements, Marathon suggests that it will incur significantly more cost than the cost of meeting the load of a customer who takes a relatively constant daily volume of gas over an extended period.[75] Marathon witness Henning[76] stated this contract has a very high likelihood of reducing ENSTAR's WACOG (weighted average

[70] *Comments of Marathon Oil Company* filed December 22, 2005 in TA139-4, at 1.

[71] *Id.* at 2.

[72] *Id.* at 3.

[73] *Id.* at 4.

[74] *Id.* at 2.

[75] *Id* .at 4

[76] T-14 (Henning) at 24.

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cost of gas). Marathon also stated in closing argument there was an extraordinary likelihood in this record that the result of APL-5 will be a decrease to ENSTAR's WACOG.[77]

Attorney General

The AG noted seventeen specific concerns with APL-5 and set them out in his statement of issues and early filed comments.[78] The AG's principal concern is whether the price of gas under APL-5 is unjust and unreasonable such that the pricing provision of APL-5 should be rejected in its entirety.[79] The AG identified three subcomponents of the price inquiry including:

(a) Whether it is appropriate to use the Henry Hub index (HHI) as a pricing proxy under the facts presented in APL-5;

(b) Whether APL-5's use of a twelve-month HH average would be prudent given HH market volatility and the resulting potential for consumer rate shock;

(c) Whether the price floor ($4.25/Mcf) and price cap ($15.00/Mcf) in APL-5 are reasonable.

The AG identified other concerns including such matters as the opportunity for arbitrage, peaking fees, transportation fees, and production taxes. The AG asked whether storage might render suspect Marathon's claim of high cost to meet deliverability and suggested that approval of one or all of the pricing provisions will require a determination of whether the inclusion of such term in APL-5 meets the

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[77]Tr. at 2529.

[78]*Attorney General's Statement of Issues,* filed June 28, 2006, and *Comments of the Attorney General* filed in TA139-4 on December 22, 2005.

[79]*Comments of the Attorney General*, filed December 22, 2005, in TA139-4, at 2.

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standard of fair, just, and reasonable.[80] The AG suggested that the APL-5 raises significant public policy issues and would, if adopted, impact all of ENSTAR's captive ratepayers.[81]

Intervenor Walker

Walker is a residential ratepayer who opposes APL-5.[82] Walker asked that the contract be rejected as the price terms are neither just nor reasonable.[83] Walker stated that the ENSTAR gas cost adjustment mechanism means ENSTAR's captive ratepayers will bear all of the economic and supply risk under APL-5. ENSTAR will bear no economic risk or supply risk at all if APL-5 is approved by the commission.[84] Walker added that public policy should encourage construction of gas storage facilities to ensure the long-term provision of utility services necessary for the public convenience and necessity.[85] Walker stated that the lack of gas production capability in Cook Inlet is not solved by this contract.[86] Walker objected to allowing companies the opportunity to take profits from Cook Inlet without requiring them to reinvest in Cook Inlet, thereby ensuring a long term gas supply for Alaska consumers.[87]

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[80] *Id.* at 2.

[81] *Id.* at 3.

[82] *Comments of James L. Walker*, filed December 19, 2005, in TA139-4, at 1.

[83] *Id.* at 1.

[84] *Id.* at 1.

[85] Tr. 1384-1385 and *Comments of James L. Walker,* filed December 19, 2005, in TA139-4 at 3.

[86] *Comments of James L. Walker,* filed December 19, 2005 at 1.

[87] *Id.* at 4

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