Introduction to Heads of Agreement (HOA) and the Memorandum of Understanding (MOU)

The Alaska LNG ("AKLNG") project will be world-scale and will supply domestic natural gas to Alaskans, create jobs for Alaskans, and open up Alaska natural gas for export to Asian-Pacific markets such as Japan, Korea, China and India.

But an LNG project on this scale is significantly more complex, commercially and technically, than the natural gas pipeline projects that the State has previously considered. The AKLNG project will require construction of one of the world's largest gas treatment plants on the North Slope, installation of a large-diameter, 800-mile gas pipeline running from the North Slope to Nikiski, five or more in-state offtake points, construction of a world-class liquefaction plant that can process up to 18 million tons of LNG per year, LNG storage tanks, and a marine terminal. The AKLNG project is estimated to cost between $45 and $65 billion dollars.

Successful LNG projects require the participants to negotiate and sign numerous complex commercial contracts covering areas as diverse as Pre-Front End Engineering and Design ("Pre-Feed"), Front End Engineering and Design ("FEED"), Engineering Procurement and Construction ("EPC"), project ownership and finance, gas balancing, gas processing, pipeline transportation, liquefaction, marine transportation, and LNG sales and purchase, to name just a few.

In order to advance a project of this size and complexity, and to lay the ground work for all the final contracts, all necessary parties must first have aligned interests. They must have general agreement on essential terms and agreement on the road map going forward. An agreement is the critical first step.

With the AKLNG project, this first step has been realized in the Heads of Agreement and Memorandum of Understanding.

Heads of Agreement

A "Heads of Agreement" is an understanding traditionally used among major natural gas project parties to outline the guiding principles and main issues necessary to advance a major natural gas project. It represents an important step on the path to legally binding project contracts and sets out the roles and responsibilities of the parties. It is not designed to cover all topics in detail, but is detailed enough to demonstrate to the parties that they have agreement on the essential project development principles and the road map going forward.

The State administration, AGDC, TransCanada, ExxonMobil, ConocoPhillips Alaska and BP Exploration Alaska have negotiated and signed such a Heads of Agreement for the AKLNG project. This Heads of Agreement was made public in advance of the opening of the Legislature so that the citizens of Alaska and the Alaska Legislature can understand the terms under which the AKLNG project is proposed to move forward before the Alaska Legislature is asked to deliberate and vote on enabling legislation that would authorize the State to proceed.

The Heads of Agreement has 10 main articles in addition to the definitions in Article 1. Below is a brief description of the subject matter of these articles.

Article 2 describes the set of guiding principles for the AKLNG project.

Article 3 identifies the benefits to all the parties if the project succeeds.

Article 4 describes the road map going forward. It sets out the details of the phased approach to project development, sets out the intention of the parties to complete the approximately $500 million dollar necessary Pre-FEED stage within 24 months, and recognizes the necessity of negotiating the detailed commercial contracts and of obtaining enabling legislation necessary to proceed to the critical FEED stage of the project.

Article 4 also recognizes that the parties will need to reassess the project information gathered during Pre-FEED before making a commitment in excess of a billion dollars to full-scale FEED.

Article 5 describes State participation in the project. In general terms, the State will participate in the AKLNG project consistent with the State Gas Share (which is the sum of the State's share of royalty-in-kind and "Tax as Gas").

Article 5 also describes that the State intends to enter into project implementation agreements with TransCanada, and an AGDC subsidiary to be created to hold and manage the State's ownership and participating interest in the project. It also provides for transparency through information flow to the State of Alaska, subject to confidentiality protections.

Article 6 describes the anticipated regulatory framework of the project. Article 6 sets out the project access and pro-expansion principles that all the parties have agreed to, as well as the process to obtain FERC confirmation of these principles.

Article 7 describes the necessity for the State, through Enabling Legislation, to establish and authorize its terms of participation in the project and acceptance of the State Gas Share.

Article 8 describes modifications to the State's royalty and gas production tax regime that all parties to the Heads of Agreement believe is necessary for Alaska natural gas to compete in world markets and for the project to be a success.

Article 9 discusses Producer payments in lieu of property taxes and project impact payments to offset increased services and other costs.

Article 10 acknowledges the necessity of State support in numerous areas, including permitting, infrastructure, and support for an export license.

Article 11 contains robust commitments to Alaska hire and content, and the parties' commitment to negotiate in good faith project labor agreements.

Memorandum of Understanding

In contrast to a Heads of Agreement, the Memorandum of Understanding ("MOU") is a bi-lateral understanding, which outlines more specifically the terms and details of an agreement between two parties in anticipation of the parties entering into binding contracts within the scope of the larger project.

TransCanada has significant experience with respect to understanding the commercialization of Alaskan natural gas. It is the pre-eminent builder and owner of major pipelines in North America. The State and TransCanada both believe that TransCanada's participation in the AKLNG project on behalf of the State, but in a more traditional commercial agreement than it previously had with the State under the AGIA project, will provide substantial benefits to both parties.

Exhibit C of the MOU between the State and TransCanada describes in some detail the commercial terms under which TransCanada will participate in the AKLNG project and provide midstream services (Gas Treatment Plant and pipeline transportation) to the State for its State Gas Share.

Exhibit B of the MOU also describes the State's option to obtain up to 40% ownership participation in TransCanada's midstream project ownership entity.

While more detailed commercial contracts for ownership, financing, transportation and project services must be negotiated as the project advances, the MOU, and particularly its Exhibits, set out the essential terms of the midstream services TransCanada will provide, including key processing and transportation commercial terms, pipeline and Gas Treatment Plant expansion terms, as well as the State's option to obtain up to 40% ownership participation in TransCanada's midstream project ownership entity.

Once enabling legislation is approved, the parties can take the next critical step in development to refine the costs, technical engineering, regulatory and fiscal challenges the project faces – challenges that must be addressed before the parties commit the billions of dollars necessary to complete the project.