

## Gas pricing point linked to Outside

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Like everyone else, I got a jolt when I opened my Enstar Natural Gas Co. bill this month. I knew about Enstar's 22 percent rate increase but reality doesn't sink in until it's there in black and white.

Things should get better, though. Enstar's cost of buying gas from Cook Inlet producers, which is what is driving up my bill, will moderate next year, because Enstar's cost is based on an average of past crude oil and Lower 48 gas prices.

Those were very high -- thus the delayed spike in Enstar's gas cost -- but they are now much lower. Because of the lag, the utility's cost for buying gas will be lower next year, and likewise, hopefully, my gas bill.

Most people are surprised to learn that the price of natural gas for Enstar (as well as Chugach Electric Association, which generates 90 percent of its electricity with gas) is based on a mix of world oil prices and, for 60 percent of Enstar's supply, natural gas prices in the Lower 48.

It's a reasonable question. The gas is produced here in Southcentral Alaska, after all. Shouldn't the local producing costs, with a reasonable profit, determine the price instead of the price at the Lower 48's Henry Hub gas-trading center, the price reference for part of Enstar's supply? Or world oil prices?

This very problem is vexing the Regulatory Commission of Alaska, which regulates consumer gas and electricity prices.

In 2001 the RCA commissioners approved one Enstar contract with prices linked to the Henry Hub index in Louisiana. But since they have balked at approving new contracts for Enstar similarly linked to Lower 48 prices. In its most recent ruling the commission accepted the principle of a Lower 48 link but suggested using a mix of prices in gas-producing regions rather than trading hubs, a proposal the producing companies rejected.

That put Enstar in a fix because as late as November the utility didn't have enough gas under contracts approved by the RCA to meet all of its needs for 2009. That's sobering, given our recent cold snap. A last-minute compromise resulted in a one-year bandage for the utility, where the producers agreed to sell gas to Enstar at prices slightly under the utility's current average cost. The RCA accepted this.

However, the utility expects even greater demand for gas in 2010 and even bigger supply needs in 2011 and 2012. The utility is going out soon to solicit new supply contracts to fill those gaps, but how the gas is priced remains the central, unresolved issue.

The problem is that any market transaction needs a price. Getting a market price is simpler in the Lower 48, because there is a grid of pipelines, and buyers and sellers can shift gas from one place to another. Trading points like Henry Hub have thousands of daily transactions. Prices are published, the information is accessible and the system is highly transparent.

Southcentral Alaska, in contrast, is a small, regional natural gas market not physically connected to the Lower 48. The only sales of gas are the producers' sales to the utilities, the sale of gas to the Nikiski liquefied natural gas plant for export to Japan and, until recently, to Agrium Corp. for its now-idled Nikiski fertilizer plant. Given such few transactions, some external price reference is needed.

For many years crude oil was the reference point because both oil and gas involve energy units being sold. In 2001 the RCA approved use of the Henry Hub gas index for some of Enstar's supply.

Should the sales price of gas, as LNG, in Japan be used? It could, but this isn't perfect because the volume of gas exported as LNG is fixed under long-term contracts, and the plant does not buy from other producers. The LNG plant's future is also uncertain given the dwindling production from Southcentral gas fields.

The argument for a Lower 48 price point is that even if there isn't much competition in the Cook Inlet gas market, there is certainly competition for the investment funds needed to explore for and find more gas. If we want more gas exploration, and geologists say there is probably more to be found, we have to have a price that lets the companies get the funds needed to drill new wells.

Since our regional gas industry competes for funds in the Lower 48, shouldn't we want projects here to be as financially attractive as projects Louisiana or Texas, to get capital for our Alaska projects? If we want that -- and at this point remember our recent cold snap -- the price here has to be at least equal, or even rise a little higher given drilling costs here, than in Louisiana and Texas. If prices are lower, yet our costs are higher, there's little wonder why there's little drilling and we're running low in gas supply.

North Slope gas could meet our supply needs, but it won't be cheap. We have other options. We could free up gas supply by making more electricity with hydro and wind, and even generate power or make a usable substitute for gas from our ample coal supplies.

These are complex issues, but we must face them. If we dither, our only other option is to import gas, as liquefied natural gas, most likely from Asia. For a resource-rich state like Alaska, that would be an irony.

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