Appendix J

Assistant Attorney General's Letter and Counsel's Opinion on Anti-trust Issues

STATE OF ALASKA

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

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March 17, 2005

Senator Ben Stevens
State Capitol Room 111
Juneau, AK 99801-1182

Representative John Harris
State Capitol Room 208
Juneau, AK 99801-1182

Dear Senator Stevens and Representative Harris:

Recently there has been much public discussion of the antitrust consequences of a producer owned North Slope gas pipeline vis-à-vis an independently owned pipeline. We have requested that Morrison and Foerster, our pipeline counsel, and specifically their antitrust experts, examine these issues. I have attached an analysis prepared by them. Based on what we know today, they conclude that there is no reasonable likelihood that the FERC would deny certification of a producer owned pipeline on competition grounds and that the FERC has an ample set of remedies to deal with competition issues as they arise without resorting to a complete ban on producer ownership. We stand ready to answer questions about the analysis and to further assistance as you may request.

We note that antitrust issues have been raised in the context of TAPS also. The federal regulatory framework for gas and oil pipelines is considerably different and this affects an antitrust analysis. In addition, TAPS is an undivided joint interest pipeline, an ownership structure that necessarily raises antitrust issues. These issues may not present themselves in the context of a gas pipeline. Both the TAPS owners and independent parties have been quite willing to raise putative antitrust issues where it assists other objectives. Nonetheless, careful antitrust analysis on a clearly stated set of facts can provide relatively clear answers as I believe we have obtained here.

Sincerely,

SCOTT J. NORDSTRAND
ACTING ATTORNEY GENERAL

By: Wil L. Condon
Wilson L. Condon
Assistant Attorney General

WLC:cb
Attachment

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STATE OF ALASKA

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March 17, 2005

Senator Gene Therriault
State Capitol Room 119
Juneau, Alaska 99801-1182

Representative Ralph Samuels
State Capitol Room 126
Juneau, Alaska 99801-1182

Dear Senator Therriault and Representative Samuels:

Recently there has been much public discussion of the antitrust consequences of a producer owned North Slope gas pipeline vis-à-vis an independently owned pipeline. We have requested that Morrison and Foerster, our pipeline counsel, and specifically their antitrust experts, examine these issues. I have attached an analysis prepared by them. Based on what we know today, they conclude that there is no reasonable likelihood that the FERC would deny certification of a producer owned pipeline on competition grounds and that the FERC has an ample set of remedies to deal with competition issues as they arise without resorting to a complete ban on producer ownership. We stand ready to answer questions about the analysis and to further assistance as you may request.

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Sincerely,

SCOTT J. NORDSTRAND
ACTING ATTORNEY GENERAL

By: Wil L. Condon
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STATE OF ALASKA

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March 17, 2005

Representative Ethan Berkowitz
State Capitol Room 404
Juneau, AK 99801-1182

Dear Representative Berkowitz:

Recently there has been much public discussion of the antitrust consequences of a producer owned North Slope gas pipeline vis-à-vis an independently owned pipeline. We have requested that Morrison and Foerster, our pipeline counsel, and specifically their antitrust experts, examine these issues. I have attached an analysis prepared by them. Based on what we know today, they conclude that there is no reasonable likelihood that the FERC would deny certification of a producer owned pipeline on competition grounds and that the FERC has an ample set of remedies to deal with competition issues as they arise without resorting to a complete ban on producer ownership. We stand ready to answer questions about the analysis and to further assistance as you may request.

We note that antitrust issues have been raised in the context of TAPS also. The federal regulatory framework for gas and oil pipelines is considerably different and this affects an antitrust analysis. In addition, TAPS is an undivided joint interest pipeline, an ownership structure that necessarily raises antitrust issues. These issues may not present themselves in the context of a gas pipeline. Both the TAPS owners and independent parties have been quite willing to raise putative antitrust issues where it assists other objectives. Nonetheless, careful antitrust analysis on a clearly stated set of facts can provide relatively clear answers as I believe we have obtained here.

Sincerely,

SCOTT J. NORDSTRAND
ACTING ATTORNEY GENERAL

By: Wilson L. Condon
Wilson L. Condon
Assistant Attorney General

WLC:cb
Attachment

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MORRISON & FOERSTER LLP

MEMORANDUM

TO: Wil Condon
State of Alaska

FROM: Robert H. Loeffler

DATE: March 11, 2005 FILE: 08083/93

RE: Antitrust Questions

In an exchange of correspondence between Representative Ethan Berkowitz and the Chairman of the Federal Energy Regulatory Commission, a question has been raised "whether the ANS Producers, given the history of prohibiting producer ownership, would be precluded from owning an Alaska natural gas pipeline to bring Alaska gas to the lower 48 states." Berkowitz letter of January 4, 2005. You have asked us to analyze the potential competitive issues raised by the Berkowitz letter and answer specifically the issue of producer preclusion.[1] Our analysis of the competitive issues is contained in the attached memorandum from my partner Bradley Lui. Before joining Morrison and Foerster, Mr. Lui was a trial attorney with the Transportation Energy and Agriculture Section of the Antitrust Division of the Department of Justice. His section was responsible for the Division's antitrust enforcement program with respect to transportation matters, including pipeline issues. In developing our views, we have also consulted with Dr. Frederick Warren-Boulton, a leading antitrust economist, who was Deputy Assistant Attorney General and Chief Economist of the Antitrust Division of the Department of Justice in the early 1980s.

Our memorandum describes the standard competitive analysis that would be conducted on the facts as we know them today. Based on the facts that we know today, we see no reasonable likelihood that the Commission would deny certification of a producer owned pipeline based on the identified competitive issues and that the remedies available to the Commission, exclusive of denial of certification, are sufficient to address any competitive issues that may arise.

Please let us know if you have any questions.

[1] We note that the Chairman Wood's response of January 28, 2005, did not answer specifically the question posed by Representative Berkowitz but noted the Commission's responsibility to promote competition in the development of the North Slope resources, the relevance of the competitive issues to the ongoing open season rulemaking, and the fact that no application had been presented to the Commission. The January 28 letter stressed that the Commission would do everything it can to "preclude antitrust abuses and promote competition in the authorization, construction, and operation of a future Alaska natural gas pipeline" and that the "antitrust issues … are still valid and will be addressed by the Commission."

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MEMORANDUM

TO:	State of Alaska	COPIES:	Robert H. Loeffler
FROM:	Bradley S. Lui		
DATE:	March 11, 2005	FILE:	08083/93
RE:	Alaska Natural Gas Pipeline - Producer Owned Pipeline Project		

This memo addresses potential competitive issues that might arise if the three largest owners of the proven natural gas reserves on the North Slope, *i.e.* BP, ConocoPhillips, and ExxonMobil (individually, a "Producer" and collectively, the "Producers") were to build, own and operate a pipeline to transport natural gas from the North Slope to Canada and ultimately to the lower 48 states (the "Gas Pipeline").

As will be discussed below, Producer ownership of the Gas Pipeline does not raise any significant competitive concerns. The requirements of the Alaska Natural Gas Pipeline Act as well as the recently issued FERC regulations implementing that Act provide sufficient safeguards to prevent the Producers from operating the pipeline in an anticompetitive manner. In addition, the Producers are likely to have an incentive to encourage non-affiliated shippers to ship their gas on the Gas Pipeline, as it would allow them to spread the fixed costs of the pipeline across greater volumes and would also potentially allow them to recover a portion of their return on investment from those shippers.

I. Factual and Regulatory Background

A. Factual Background

For more than 30 years, various entities have proposed building a pipeline to carry natural gas from the North Slope to Canada and the lower 48 states. In 1976, there were great hopes that a Gas Pipeline would be built when the Alaska Natural Gas Transportation Act was enacted. Unfortunately, those hopes were not rewarded in the ensuing thirty years. More recently, the State has witnessed a revival of interest in the Gas Pipeline with a number of consortia vying for the right to build the Gas Pipeline. Included among those competing groups, is a group composed of the Producers. Other groups seeking to build the Gas Pipeline include MidAmerican, TransCanada, and certain other third party investor groups.

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B. Regulatory Background

In order to facilitate the construction of the Gas Pipeline as well as to promote development of North Slope gas resources, the Congress enacted the Alaska Natural Gas Pipeline Act in 2004 (the "Gas Pipeline Act"). The Act authorizes the FERC to review and act upon applications for the "issuance of a certificate of public convenience and necessity authorizing the construction and operation of" a Gas Pipeline. *See* Gas Pipeline Act § 103. The Gas Pipeline Act specifically directs the FERC to develop and issue regulations governing the conduct of open seasons for the Gas Pipeline and that such regulations shall "promote competition in the exploration, development, and production of Alaska natural gas." Gas Pipeline Act §103(e)(2)(B). Moreover, the Gas Pipeline Act requires that "for any open season for capacity exceeding the initial capacity, [the regulations shall] provide the opportunity for transportation of natural gas from other than from the Prudhoe Bay and Point Thomson units." Gas Pipeline Act § 103(e)(2)(C). In addition, the Act provides that the FERC may order the expansion of the Gas Pipeline "if the Commission determines that such expansion is required by the present and future public convenience and necessity." Gas Pipeline Act Sec. 105.

On February 9, 2005, the FERC issued regulations governing open seasons on the Gas Pipeline as directed by the Gas Pipeline Act. Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects, 70 Fed. Reg. 8269 (Feb. 18, 2005), Order No. 2005, Docket No. RM05-1-000, (to be codified at 18 C.F.R. pt. 157)(the "Open Season Regulations"). Those regulations provide that "the Commission will consider the extent to which a proposed project has been designed to accommodate the needs of shippers who have made conforming bids during the open season, as well as the extent to which the project can accommodate low-cost expansion, and may require changes in project design necessity [sic] to promote competition and offer a reasonable opportunity for access to the project." 18 C.F.R. § 157.37 In addition, in considering any capacity expansion proposal, "the Commission will consider the extent to which the expansion will be utilized by shippers other than those who are initial shippers on the project and, in order to promote competition and open access to the project, may require design changes to ensure [access]." 18 C.F.R. § 157.36.

In addition, the operations of the Gas Pipeline will be governed by existing legal requirements contained in the Natural Gas Act, including its anti-discrimination provisions, 15 U.S.C. § 717c(b), and the FERC's detailed Standards of Conduct regulations, 18 C.F.R. Part 358. 15 U.S.C. § 717c(b) would prohibit the Producer owners of the Gas Pipeline from giving preferential treatment to its production affiliates. Similarly, 18 C.F.R. § 385.5 would require the Producer owners of the Gas Pipeline to enforce the Gas Pipeline's tariffs in a non-discriminatory manner and would prohibit the Producers' Gas Pipeline affiliate(s) from sharing information gained from pipeline customers, including non-affiliated shippers, with the Producers' production affiliates. The Standards of Conduct also will require that the Producers operate their Gas Pipeline affiliate independently of their marketing/production affiliates.

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II. Discussion

A. Legal Framework

Under the current Producers' proposal for the Gas Pipeline, the Producers and the State would jointly own and operate the Gas Pipeline. As a joint collaboration amongst several entities, the Producer Gas Pipeline would be analyzed for antitrust purposes as a joint venture.

Under the U.S. antitrust laws, the formation of a joint venture is unlawful only if the effect of the transaction is to lessen competition substantially in one or more relevant markets. This analysis is performed under either Section 7 of the Clayton Act, 15 U.S.C. § 18 or Section 1 of the Sherman Act, 15 U.S.C. § 1. Generally, the analysis of whether the proposed transaction would violate either Section 1 or Section 7 has three steps:

First, is the basic purpose of the joint venture lawful? Specifically, is the purpose of the collaboration to enhance competition, or is it simply a pretext for an anticompetitive agreement to fix prices, divide markets or reduce output? If it is a pretext, it is *per se* unlawful under Section 1 of the Sherman Act. *See, e.g., Timken Roller Bearing Co. v. United States*, 341 U.S. 593 (1951); *United States v. National Lead Co.*, 332 U.S. 319 (1947).

If the purpose of the joint venture is to create a new product, or achieve some efficiency in the development, manufacturing, marketing or distribution of existing products, however, it will be held unlawful only if the anticompetitive effects of the joint venture outweigh its procompetitive effects under a rule of reason analysis. *Copperweld Corp. v. Independent Tube Corp.*, 467 U.S. 752, 768 (1984). Procompetitive effects would include enabling the parties to research and develop new products, enabling them to distribute existing products in a more efficient manner, and providing them with access to markets or channels of distribution that they otherwise would lack. As a general matter, the greater the degree of economic integration between the parties, the more likely the purpose of the collaboration will be viewed as procompetitive. *See, e.g., Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 214 (D.C. Cir. 1986)("*Rothery*").

Second, is the collaboration likely to lessen competition substantially? Assuming that the purpose of the collaboration is legitimate, the second step is to analyze whether the collaboration will lessen competition substantially in any relevant market. This step requires an analysis of the markets in which the parties compete, their market shares, and the likelihood that the collaboration between them would diminish competition in those markets. *NCAA v. Board of Regents*, 468 U.S. 85, 105-12 (1984). If the collaboration lessens competition, an antitrust agency or court will then analyze whether the resulting loss of competition is likely to be outweighed by the procompetitive efficiencies that result from the venture. *Id.*

Third, does the collaboration contain any unlawful "ancillary" restraints? The final step of the analysis is to determine whether the collaboration contains any ancillary restraints on

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competition that are broader than necessary to achieve the legitimate purpose of the transaction. *Rothery*, 792 F.2d at 224. U.S. antitrust law recognizes that parties to collaborative agreements often must agree on competitive matters such as product prices, output and marketing plans in order for the collaboration to operate successfully. If the parties attempt to extend such agreements beyond the legitimate scope of the collaboration, however, those collateral agreements may be held unlawful. *Id.* In other words, it is important the parties do not agree to any restrictions on their competitive activity beyond those necessary to accomplish the procompetitive objectives of the joint venture. So, for example, if the Producers, as part of the joint venture agreement, were to agree on the prices they would charge for gas in the downstream market, they would be agreeing to an ancillary restraint that was broader than necessary to achieve the purpose of the joint venture. The prices to be charged in the downstream market have no legitimate connection to the lawful purpose of the joint venture (the transportation of gas) and thus an agreement on such prices would be an ancillary restraint. Moreover, because it would be a naked price fixing agreement, it would be an unlawful ancillary restraint.

B. Producer Ownership of the Gas Pipeline Would Not Violate The Antitrust Laws

When the analytical framework used to analyze joint ventures under the antitrust laws is applied to the proposed Producer Gas Pipeline, it is clear that Producer ownership of the Gas Pipeline likely would not violate the antitrust laws.[1]

The basic purpose of the Producer Gas Pipeline is to carry North Slope natural gas to Canada and ultimately the lower 48 states. North Slope natural gas has been stranded for over thirty years because there has been no practical means to transport the gas to the lower 48 states. With the Gas Pipeline, the owners of North Slope gas reserves (including the State as royalty owner) finally will be able to bring their gas to market. This will increase the supply of natural gas available to consumers in the lower 48 states and will thereby increase competition in the sale of gas in the lower 48 states.[2] Unquestionably, the purpose of the project is procompetitive and lawful.

Moreover, it does not appear that a Producer Gas Pipeline is likely to lessen competition substantially in any relevant market. None of the North Slope gas reserves are currently being marketed to consumers. Thus, the pipeline's transportation of the gas to market can only increase competition in the sale of gas. Moreover, it is extremely unlikely that each of

[1] The analysis of any ancillary restraints in the Producers' Gas Pipeline proposal is outside of the scope of this memorandum. The Producers' Gas Pipeline proposal is not complete and it would be premature and highly speculative to undertake an ancillary restraints analysis at this time. For the purposes of this discussion, this memo will assume that the Producers' proposal does not contain any ancillary restraints on competition that are broader than necessary to achieve the purpose of the joint venture.

[2] We would note that even if sales of North Slope natural gas were to increase the share of gas sales that each of the producers has in the lower 48 states, this would not imply a reduction in competition. The point is that the overall supply of gas has increased in the lower 48 states resulting in an increase in competition above what existed *ex ante*. It cannot be the case that increasing the supply of natural gas into the market *reduces* competition.

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the individual Producers or the State would ever be in a position to build a separate pipeline in competition with the proposed Gas Pipeline. Thus, the fact that the Producers and the State are collaborating in building the pipeline would not reduce competition in the transportation of gas from the North Slope. And, with respect to competition in the exploration for and production of North Slope gas, it does not seem likely that the collaboration between the parties to build the Gas Pipeline would reduce competition in that sector. Indeed, the Gas Pipeline should have the opposite effect. It would likely increase competition in that sector because the Gas Pipeline would make it possible for the Producers and the State as well as others to bring the gas to market, rewarding exploration and production efforts.

C. It Does Not Appear That Producer Ownership of the Gas Pipeline Would Lead to Significantly Less Competition In The Transportation of North Slope Natural Gas Than An Independent Pipeline

While Producer ownership of the Gas Pipeline would be lawful under the antitrust laws, the next question that needs to be addressed is whether Producer ownership of the Gas Pipeline is likely to lead to substantially less competition in the transportation of gas from the North Slope than if the Gas Pipeline was owned by a company that (1) was not affiliated with any North Slope Gas Producer and (2) has no downstream natural gas sales (an "Independent Owner"). In other words, would there be differences in incentives between the Producers and an Independent Owner that would lead the Producers to operate the Gas Pipeline in a manner that would lead to less competition in any relevant market than if an Independent Owner operated the Gas Pipeline? And, if there is such a difference in incentives, would the Producer owners of the Gas Pipeline be in a position to use the Gas Pipeline to their anticompetitive advantage?

The obvious difference between Producer ownership of the Gas Pipeline and Independent ownership of the Gas Pipeline is the fact that the Producer Owner competes downstream in the sale of natural gas while an Independent Owner has no presence in the downstream markets. In the past, the U.S. Department of Justice and others expressed concern that Producer Owners might have the incentive to deny shipping capacity to North Slope gas producers not affiliated with the Producer Owners. *See, e.g.,* Report of the Attorney General - Alaska Natural Gas Transportation Act of 1976. The ostensible theory was that the Producers would deny access to the Gas Pipeline to non-affiliated shippers in order to eliminate competition in the downstream sale of natural gas. Consequently, the Department argued that the Gas Pipeline should not be owned by any company affiliated with a Producer.[3]

[3] Much has changed since the Attorney General issued his report in 1976. It is worth noting, for example, that the ban on Producer ownership of equity in the 1977 Presidential Decision, based upon the views of the Attorney General in 1976, was abandoned when President Reagan signed into law the "waivers of law." one of which permitted a degree of equity ownership by the Producers. Companies are now required to separate their production and transportation functions, 18 C.F.R. § 358.4, the wellhead price of natural gas is no longer regulated, and all interstate gas pipelines must hold open seasons so that all shippers have an equal opportunity to bid for pipeline capacity.

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In order for there to be a competitive difference resulting from the fact that Producer Owners sell gas in the downstream market while an Independent Owner would not, two conditions must exist: (1) the Producer must have the ability to deny access to the Gas Pipeline to non-affiliated shippers in order to reduce competition in the sale of gas in a relevant market; and (2) the Producer's position in the downstream business of selling gas must give it an incentive to block access to the Gas Pipeline to non-affiliated shippers in order to reduce competition in the downstream sale of gas. The memorandum will first address the issue of whether the Producers could deny access to the Gas Pipeline to a non-affiliated shipper. For if a Producer, for anticompetitive reasons, could not deny access to the Gas Pipeline, then there would not be any competitive issue arising from Producer ownership of the Gas Pipeline. We will then turn to the issue of whether the Producers have the incentive to act anticompetitively vis-à-vis a non-affiliated shipper.

1. The Gas Pipeline Act and the Open Season Regulations Ensure That The Needs of Third Party Shippers Will Be Accommodated

While the Department of Justice's concerns about Producer ownership of the Gas Pipeline might have been applicable to the situation that existed almost thirty years ago, those concerns are not relevant to the situation today. Beginning in the 1980's, the FERC restructured the natural gas industry by requiring operational separation of pipeline transportation functions and marketing functions and open access for all customers. In the case of the Gas Pipeline, the requirements are even more specific. The Gas Pipeline Act, the Open Season Regulations, and the FERC's Standards of Conduct regulations have provisions designed to prevent the owners of the Gas Pipeline from using the Gas Pipeline for anticompetitive purposes. Indeed, the Gas Pipeline Act specifically directs the FERC to develop regulations for Open Seasons for the Gas Pipeline that "promote competition in the exploration, development, and production of Alaska natural gas." Gas Pipeline Act § 103(e)(2)(B). The FERC has just completed drafting those regulations which include detailed regulations concerning access to capacity in the Gas Pipeline's open seasons. The regulations are already in effect and provide strong open access protections for shippers and strengthen the affiliate independence requirements that would apply to the Gas Pipeline, including a Producer Gas Pipeline.

In order to build the Gas Pipeline, the Producers will need to apply for and obtain a certificate of public convenience and necessity from the Commission. In reviewing any application for a certificate of public convenience and necessity to build and operate the Gas Pipeline, the Commission "will consider the extent to which a proposed project has been designed to accommodate the needs of shippers who have made conforming bids during the open season, as well as the extent to which the project can accommodate low-cost expansion, and may require changes in project design necessity [sic] to promote competition and offer a reasonable opportunity for access to the project." Open Season Regulations § 157.37, 70 Fed. Reg. at 8282. Thus, the owners of the Gas Pipeline will have to make an affirmative case that the Gas Pipeline will have sufficient capacity to meet the needs of shippers.

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This process should ameliorate any concerns that the Producers would build an "undersized" Gas Pipeline to prevent non-affiliated North Slope natural gas shippers from competing with them in the downstream sale of gas. As the Commission explained in Order 2005:

> to further meet the concerns expressed by parties who are worried about obtaining access to an Alaska pipeline, we have added new sections 157.36 and 157.37, which make clear that the Commission will examine proposed pipeline designs, as well as expansion proposals to ensure that *all interested shippers* are given a fair opportunity to obtain capacity both on an initial project and on any voluntary expansion. As stated elsewhere in this order, we believe it in both the sponsor's and shippers' best interests to build a pipeline to accommodate all qualified shippers who are ready to sign firm agreements. We will carefully review project design and the documentation relating to the allocation of capacity, with the goal of promoting our open access and pro-competition policies.

70 Fed. Reg. at 8282, Order 2005, Slip Op. at 36. The regulations and Order 2005 make it clear that the Gas Pipeline should be designed so that it will accommodate all shippers making genuine bids for capacity and the Commission will take appropriate action to ensure that this is the case. Moreover, if a non-affiliated shipper or other interested party feels that the Producers are proposing to build a Gas Pipeline that has insufficient capacity, it can object to the Producer proposal at the Commission and seek Commission action to remove the concern.

Even after the Gas Pipeline is built, there should not be any substantial concern that Producer Owners of the Gas Pipeline could refuse to expand the capacity of the Gas Pipeline to accommodate the needs of a non-affiliated shipper for anti-competitive reasons. Section 105(a) of the Gas Pipeline Act, gives the Commission the authority to "order the expansion of the Alaska natural gas project if the Commission determines that such expansion is required by the present and future public convenience and necessity."[4] Thus, if a non-affiliated shipper believes that the Gas Pipeline has refused to increase its capacity for impermissible reasons, it can seek relief from the Commission.[5]

Moreover, with respect to ongoing operations of the Gas Pipeline, the Natural Gas Act antidiscrimination provisions, as well as the FERC's detailed Standards of Conduct

[4] With respect to voluntary expansions of the pipeline, the Open Season Regulations require that "any open season for capacity exceeding the initial capacity of an Alaska natural gas transportation project must provide the opportunity for the transportation of gas other than Prudhoe Bay or Point Thomson production." Open Season Regulations § 157.36. 70 Fed. Reg. at 8288. Moreover, "in order to promote competition and open access to the project, [the Commission] may require design changes to ensure that all who are willing to sign long-term firm transportation contracts that some portion of the expansion capacity be allocated to new shippers or shippers seeking to transport natural gas from areas other than Prudhoe Bay and Point Thomson." *Id.*

[5] For the Canadian portion of the Gas Pipeline, Osler, Hoskin & Harcourt has informed us that the Canadian National Energy Board has similar powers to require the expansion of the Gas Pipeline to accommodate third party shippers under subsections 71(2) and (3) of the National Energy Board Act.

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regulations, should preclude any effort by the Producers to favor their shipping affiliates to the detriment of non-affiliated shippers. Under 15 U.S.C. § 717c(b), the Gas Pipeline cannot grant any "undue preference or advantage" to any shipper, subject any shipper to "undue prejudice or disadvantage" or "maintain any unreasonable differences in rates, charges, service, facilities or in any other respect." Similarly, under the FERC's Standards of Conduct, a gas pipeline "must treat all transmission customers, affiliated and non-affiliated, on a nondiscriminatory basis, and must not operate its transmission system to preferentially benefit an Energy Affiliate." 18 C.F.R. § 358.2(b). Consequently, the Producers could not discriminate in favor of their own affiliates in order to give their shipping affiliates a competitive advantage vis-à-vis a non-affiliated shipper or to place non-affiliated shippers at a competitive disadvantage to the affiliated shippers.

2. The Producers Would Have The Same Incentive To Allow Third Party Shippers To Ship on the Gas Pipeline As An Independent Owner

As owners of the Gas Pipeline, the Producers will have an incentive to encourage rather than discourage third party shipments on the Gas Pipeline. Increasing the volumes of gas shipped on the line will allow the fixed costs of the pipeline to be spread over a greater number of units of gas and thus lower the shipping costs of the Producers' production affiliates. In addition, the Producers will, of course, earn a return on the third party shipments. So long as the third party shipments will provide positive returns to the Gas Pipeline, the Producers will have the incentive to carry the shipments, just as an Independent Owner would.

The question that then must be addressed is whether this incentive would be overcome by some other incentive unique to the Producers. In the past, some have argued that the Producers would have the incentive to prevent third party shipments in order to eliminate competition in the downstream sale of gas. But for this to make sense, one or more of the Producers would have to possess market power in some relevant downstream gas market.[6] This is because unless they have market power in the downstream gas market and are able to charge higher than competitive prices, the incremental third party sales of gas will not have any effect on the prices that they charge. The Producer would be a price taker and unable to influence prices. And, if there is no ability of any of the producers to affect prices, then none of the Producers would have a reason to attempt to block the third party sales.

Based upon information supplied by the Lukens Energy Group, none of the Producers has market power in the downstream sale of gas. According to estimates complied by Lukens Energy Group, in 2015 the Producers respective shares of equity gas production in Canada and the U.S. (*i.e.*, excluding the marketing of third party gas) will be: BP - 7.3%, ConocoPhillips - 5.8%, and ExxonMobil - 7.9%. These market shares are far below the level necessary for any one of those companies to be able to exercise market power. Thus, the

[6] It should be noted that the analysis of whether the Producers are likely to exercise market power should be based upon the sales and market position of each of the Producers on an individual basis. Each of these companies is a competitor in the downstream sale of gas. Therefore, it would not be appropriate to aggregate their sales to analyze whether it is likely that they have collective market power. (This assumes, of course, that the companies will comply with the law and not engage in collusive behavior in violation of Section 1 of the Sherman Act.)

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Producers would not have an incentive to block third party shipments of gas on the Gas Pipeline in an effort to maintain prices above a competitive level.

Alternatively, if the cost of producing third party gas is lower than the cost of producing the Producers' gas, one might argue that the Producers could try to block third party Alaskan gas shipments in order to prevent them from undercutting the prices of the more expensive Producer gas. However, given that the Producers will be obtaining their gas from existing wells and will be able to utilize existing infrastructure to produce their gas, it seems implausible to believe that the Producers' cost of production for Prudhoe Bay and Point Thomson will be higher than the production costs of third party producers. Consequently, it is unlikely that the Producers would attempt to block third party gas shipments to prevent cheaper gas from being brought to market.

Based upon the facts stated above, the Producers would not appear to have any incentive to withhold capacity from a third party shipper for anticompetitive purposes. Rather, they would have the contrary incentive - to encourage third party shipments so as to earn income from those shipments and reduce their own shipping costs. Thus, Producer ownership of the Gas Pipeline does not appear to present any significant competitive problems.

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