



MEMORANDUM

DATE: April 26, 2018

TO: Board Members
Alaska Industrial Development and Export Authority

FROM: John Springsteen
CEO / Executive Director

RE: North Slope Pad
Prudhoe Bay Chemical's Sublease

RECOMMENDATION

The following action is recommended relating to the North Slope Pad: We have concluded negotiations with Prudhoe Bay Chemical (PBC) to sublease approximately 1/3 of the North Slope Pad and the associated pipeline right-of-way for the installation and operation of a methanol production facility. Staff recommends approval of a sublease agreement, which will allow Prudhoe Bay Chemical (PBC) to construct and operate a methanol plant and gas pipeline on the AIDEA's North Slope Pad. The draft Ground Sublease is attached.

BACKGROUND

AIDEA holds a State of Alaska Department of Natural Resources (DNR) lease (ADL 419409) for the right-of-way for an operations pad and associated pipeline on the North Slope. A gravel pad and driveways were constructed on this lease to accommodate a Liquefied Natural Gas (LNG) facility to liquefy and ship natural gas to Fairbanks.

AIDEA is currently making annual payments to DNR of just under \$90,000 for the lease and administrative costs.

The existing lease is only viable if it is being used as a right-of-way lease for a gas tie-in, pipeline, and an LNG facility. If it is not used for this purpose, DNR must approve a change in use. The lease also requires that construction of the LNG facility commence within three years. This past summer AIDEA was able to extend the lease for one year by demonstrating that we were "working on construction" in negotiating a Use Agreement with Prudhoe Bay Chemical (PBC) for a methanol plant. In late 2017, the draft terms of a sublease were developed for the use of the pipeline right-of-way and one third of the pad for this facility.

In December 2017, AIDEA met with DNR to begin due diligence to amend our lease for the installation and operation of a methanol plant instead of an LNG plant, utilizing a gas pipeline. AIDEA and PBC coordinated with DNR to prepare a formal application, which was submitted

February 5, 2018. Approval is pending by the DNR State Pipeline Coordinator's Office. DNR indicated analysis/due diligence for this decision can take approximately 30 days, with an additional 30 days required for public comment. DNR has not yet published any notice soliciting public comment on the proposed change in use.

The Interior Gas Utility (IGU) requested this North Slope Pad be included in the AIDEA sale of Pentex Alaska Natural Gas Company, LLC. The transfer of the AIDEA rights to IGU is also under review by DNR; however, this is an independent request from the PBC sublease. Nevertheless, we have consulted with IGU about the PBC sublease, incorporated their suggested revisions into the lease, and they have concurred.

PBC SUBLEASE AGREEMENT

The terms of the Sublease have been agreed to by AIDEA and PBC, and reviewed by the IGU.

Key terms include:

- PBC will sublease 5.207 acres of the pad (1/3 pad) and 100% of the Right of Way (2.525 acres) as shown in Figure 1.
- The PBC sublease has a potential 30-year term with an initial term of 10 years with two additional 10-year extensions. This is consistent with the DNR term of 30 years.
- PBC has the option to renew the Sublease at the end of each 10-year term until the expiration of the DNR lease. If DNR allows an extension past 30 years, PBC has the right to a corresponding additional extension. Monthly rent adjusts at each renewal based on the consumer price index.
- Term begins 6 months after DNR approval or at start of construction.
- Cost to PBC for the Sublease is \$19,166/month based on a 30 year/8% amortization rate on \$6,533,293 of capitalized construction costs and 30% of the DNR rent and administrative cost of \$90,000/year. DNR periodically adjusts the cost of the lease based on appraisals and the amount of staff time to manage the lease on any given year
- A Security Deposit equal to 3-months' rent, or \$57,498, will be collected. This deposit is refundable at the end of the Initial 10-year Term.
- Temporary use of the remaining portion of the Pad for construction up to 18 months is allowed as long as there is no other user.
- PBC will be responsible for all pad maintenance and repair until such time as there is a second sublease.
- If additional DNR terms required as part of their due diligence are not agreeable to both parties, or if DNR approval is not obtained within 180 days, the Sublease will be null and void.
- PBC has the option of cancelling Sublease prior to the commencement of the Initial Term.

- The Sublease does not require a construction start date, except that PBC must commence construction within the time period DNR requires to keep the underlying DNR lease in effect.

DNR LEASE CONDITIONS

The existing lease is a non-exclusive lease. As such, DNR reserves the right to authorize other third-party activities on the leasehold if those activities do not unreasonably interfere with our rights under the lease. It is assumed that any third-party activity will have to share in costs. DNR has not indicated it is entertaining other third-party activities, but it is important to keep that possibility in mind – this lease is to generate and support activity on the North Slope and DNR will not allow it to be idle. They have the ability to terminate the lease if timely development is not pursued.

The existing lease is a single use, right-of-way lease to AIDEA. If another user is found for the remaining 2/3 of the pad not subleased to PBC, and if the new user qualifies for a right-of-way lease (meaning its use will involve pipeline activities), then a new sublease between AIDEA and the new user for that portion of the pad and right-of-way will be required. DNR approval of the new sublease will be needed but should be obtainable

However, if another user is found for the 2/3 of the pad not subject to the proposed PBC sublease, and if the new user is not eligible under the right-of-way lease statutes (i.e., the new use is not for a pipeline related activity), then a new Division of Mining Land and Water (DMLW) lease for the area the other user will utilize may have to be sought. There is no guarantee that DMLW would approve such a new non-pipeline lease, at least not without going through DNR's competitive bidding process.

AIDEA MISSION SUITABILITY

The PBC methanol project is consistent with AIDEA's mission and also is supportive of the State's interest in expanding energy production on the North Slope. Approximately 40 construction and 6 permanent operating jobs will be created. This plant will provide a commodity that is currently being imported from outside the state and driven 800 miles to the slope. This plant will be run by an Alaskan company, utilizing Alaskan employees to produce a product here that should lower the operating costs for the North Slope producers.

ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY

RESOLUTION NO. G18-03

**RESOLUTION OF THE ALASKA INDUSTRIAL DEVELOPMENT
AND EXPORT AUTHORITY APPROVING A SUBLEASE OF THE
NORTH SLOPE PAD WITH PRUDHOE BAY CHEMICAL, LLC**

WHEREAS, the Alaska Industrial Development and Export Authority (the “Authority”) acquired a leasehold interest in a tract of North Slope land owned by the State of Alaska as a part of the Interior Energy Project, which land is legally described as:

A designated portion of Section 3, Township 10 North, Range 14 East, Umiat Meridian, Barrow Recording District, Second Judicial District, State of Alaska;

WHEREAS, the Authority improved the land with the construction of a gravel pad on it (the “North Slope Pad”);

WHEREAS, the Authority originally planned to utilize the North Slope Pad as the site of a liquefied natural gas (LNG) production plant meant to supply Interior Alaska, but the plans for the construction of the LNG production plant on the site were later cancelled;

WHEREAS, the Authority has the opportunity to put the North Slope Pad to productive use by subleasing a portion of it to Prudhoe Bay Chemical, LLC, which intends to construct and operate a methanol production plant on the site;

WHEREAS, the staff of the Authority has negotiated a proposed sublease with Prudhoe Bay Chemical, LLC and the proposed sublease (the “Sublease”) has been provided to the Board;

WHEREAS, the Sublease is subject to certain conditions precedent, including the condition that the approval of the Alaska Department of Natural Resources must be obtained;

WHEREAS, the Authority intends to transfer the North Slope Pad to the Interior Gas Utility at the time of the closing on the Authority’s sale of Pentex Alaska Natural Gas Company, LLC to the Interior Gas Utility;

WHEREAS, the staff of the Authority has consulted with the Interior Gas Utility about the Sublease and the Interior Gas Utility has indicated the Sublease is acceptable to it; and

WHEREAS, whether or not the pending Pentex transaction with the Interior Gas Utility closes, proceeding with the Sublease is in the best interest of the Authority.

NOW, THEREFORE, BE IT RESOLVED BY THE ALASKA INDUSTRIAL DEVELOPMENT AND EXPORT AUTHORITY AS FOLLOWS:

Section 1. The Sublease with Prudhoe Bay Chemical, LLC is approved. On behalf of the Authority, the Executive Director is authorized to execute the Sublease in the same form presented to Board or with any non-material changes to the form of the Sublease that the Executive Director determines to be necessary and appropriate.

Section 2. Upon the satisfaction of the conditions precedent set out in the Sublease, the Executive Director is authorized to have the Authority perform all of its obligations under the Sublease.

Section 3. The Executive Director is authorized to take all other actions, necessary or expedient in fulfilling the purposes of this Resolution.

Dated at Anchorage, Alaska, this 26th day of April 2018.





Chair



Secretary