

**ALASKA STATE LEGISLATURE
HOUSE JUDICIARY STANDING COMMITTEE**

Anchorage, Alaska
November 21, 2008
9:19 a.m.

MEMBERS PRESENT

Representative Jay Ramras, Chair
Representative Nancy Dahlstrom, Vice Chair (via teleconference)
Representative Bob Lynn
Representative Ralph Samuels

MEMBERS ABSENT

Representative John Coghill
Representative Max Gruenberg
Representative Lindsey Holmes

OTHER LEGISLATORS PRESENT

Representative Scott Kawasaki (via teleconference)

COMMITTEE CALENDAR

OVERVIEW(S): MATTERS PERTAINING TO HIGH GAS PRICES IN ALASKA
AND WHY GAS PRICES HAVE NOT FALLEN AT THE SAME RATE AS IN THE
LOWER 48

- HEARD

PREVIOUS COMMITTEE ACTION

No previous action to record

WITNESS REGISTER

REPRESENTATIVE MIKE HAWKER
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided comments and asked questions during
the presentation on matters pertaining to high gasoline prices
in Alaska.

SENATOR DONALD OLSON
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

REPRESENTATIVE MIKE KELLY
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

KIP KNUDSON, Manager
External Affairs
Tesoro Alaska Company
Anchorage, Alaska

POSITION STATEMENT: Provided comments and responded to questions during the presentation on matters pertaining to high gasoline prices in Alaska.

JEFF COOK, Director
External Affairs
Flint Hills Resources
North Pole, Alaska

POSITION STATEMENT: Provided comments and responded to questions during the presentation on matters pertaining to high gasoline prices in Alaska.

CLYDE (ED) SNIFFEN, JR., Senior Assistant Attorney General
Commercial/Fair Business Section
Civil Division (Anchorage)
Department of Law (DOL)
Anchorage, Alaska

POSITION STATEMENT: Provided comments and responded to questions during the presentation on matters pertaining to high gasoline prices in Alaska.

BARRY PULLIAM, Senior Economist
Econ One Research, Inc.
El Segundo, California

POSITION STATEMENT: Provided comments and responded to questions during the presentation on matters pertaining to high gasoline prices in Alaska.

JERRY McCUTCHEON
Anchorage, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

DONALD WESTLUND

Ketchikan, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

DOLORES "DORRIE" FARRELL

Sitka, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

TIM LUTHER

Kodiak, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

DICK COOSE

Ketchikan, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

MICHAEL E. McCARTHY

Homer, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

JAVEN OSE

Anchorage, Alaska

POSITION STATEMENT: Provided comments during the presentation on matters pertaining to high gasoline prices in Alaska.

ACTION NARRATIVE

CHAIR JAY RAMRAS called the House Judiciary Standing Committee meeting to order at [9:19:47 AM](#). Representatives Dahlstrom (via teleconference) and Ramras were present at the call to order. Representatives Lynn and Samuels arrived as the meeting was in progress. Representative Kawasaki (via teleconference) was also in attendance.

Overview(s): Matters pertaining to high gas prices in Alaska

[9:20:05 AM](#)

CHAIR RAMRAS [announced that the only order of business would be consideration of matters pertaining to high gas prices in Alaska and why gas prices have not fallen at the same rate as in the Lower 48].

CHAIR RAMRAS remarked that although the general perception in Alaska might be that there is only the one commodity of crude oil and that the price of it sets the price of retail gasoline, there are actually two separate commodities, that of crude oil, and that of refined gasoline. In the Lower 48, there are very large, complex refineries with the capability of selling gasoline to a much larger market than Alaska's market; in contrast, Alaska's market for gasoline products is small and static. He surmised that if a producer of crude oil is also a refiner of other petroleum products, then the price of crude oil can become another variable in gasoline pricing decisions, as are the level of competition and the level of demand. In Alaska, however, there isn't much competition and the level of demand stays fairly constant.

CHAIR RAMRAS said he is questioning whether retail gasoline prices in the Lower 48 have been artificially reduced by the decrease in demand due to conservation efforts. He used an example involving rental car rates in the Lower 48 to illustrate how an increase in supply coupled with a decrease in demand encourages competition and thus a lowering of prices. Chair Ramras then noted that Representative Joule has mentioned to him that in Kotzebue, gasoline is delivered only once a year and so the price is still what it was set at when the town's current supply was delivered - that being about \$7.85/gallon.

[9:30:26 AM](#)

REPRESENTATIVE MIKE HAWKER, Alaska State Legislature, opined that in Alaska, the retail price of gasoline is driven by two factors: the cost to produce the product, and the level of competition. Alaska is very limited with regard to the number of refineries that manufacture gasoline. He offered his understanding that to date there has been no evidence of illegal activity on the part of gasoline retailers. He surmised that the question becomes what effect Alaska's lack of competition with regard to gasoline manufactures has had on the retail price of gasoline. He offered his understanding that government regulation can also have an impact on the level of competition present in any given market. This raises the question of to what degree should Alaska regulate [the sale of gasoline].

CHAIR RAMRAS spoke of Tesoro Corporation's falling stock price and the effect competition is having on its refineries outside of Alaska, and used an example involving Alaska Airlines to illustrate what effect competition or a lack thereof can have on pricing. He then noted that the refineries in Alaska are very

small and that the volume of gasoline they produce is also very small compared to refineries in the Lower 48, and that this, too, could account for Alaska's higher retail gasoline prices.

REPRESENTATIVE LYNN characterized what he pays at the gas pump as being too much.

[9:36:05 AM](#)

SENATOR DONALD OLSON, Alaska State Legislature, noted that in his district, towns have been hit hard by the high price of petroleum products, particularly the schools, because, as in Kotzebue, the towns' bulk fuel tanks were filled when prices were extremely high. Such high prices could have the effect of encouraging people in rural areas to move to urban centers. He warned that if the industry won't regulate itself, the legislature will have to do it.

CHAIR RAMRAS explained that the committee has been looking specifically at the pricing of gasoline in the Railbelt and Southeast Alaska. He noted that Wrangell, which just got a new supply of gasoline from Seattle and therefore should have the cheapest retail gasoline prices in the state, doesn't; this is evidence that the market is not working as it should, and perhaps actually constitutes an instance of price gouging. He again spoke about Tesoro Corporation's stock prices, and opined that refiners in the Lower 48 aren't making much of a profit because they have an excess of supply. He mentioned that a lobbyist he's spoken with has asked whether the committee would also be investigating barge companies and distributors.

CHAIR RAMRAS then read bullet point number 3 of a Department of Law (DOL) press release dated 11/20/08 [original punctuation provided]:

Alaska does not have a price gouging law. Sellers of all goods and services (including gasoline) are not required to sell products on a "cost plus" basis. Thus, it does not matter what it costs the seller to acquire the goods or provide a service. Sellers can sell their products for whatever the market will bear. There is no "cap" on the amount of profit any business can make.

CHAIR RAMRAS opined that the governor should speak with refiners and ask them for relief from their high gasoline prices.

[9:43:56 AM](#)

REPRESENTATIVE MIKE KELLY, Alaska State Legislature, raised the issue of people possibly banding together and instituting a cooperative model as a way of dealing with high gasoline prices, but noted that such a model does carry the risk of, in the future, not being able to take advantage of competitive pricing. He cautioned against government regulation of Alaska's refining industry.

CHAIR RAMRAS relayed that the committee would be considering price gouging legislation, and will be providing information about model legislation in a forthcoming committee report. He mentioned that the committee would hold another meeting on the issue of high gasoline prices in January, before the start of the next session, and spoke briefly regarding how that meeting might be proceeding and who might be testifying. He surmised that any lowering of gasoline prices that occurs over the next few months will be the result of market changes rather than the result of anything specific that the legislature or the administration might be doing.

[9:50:34 AM](#)

KIP KNUDSON, Manager, External Affairs, Tesoro Alaska Company, turned the committee's attention to page 1 of his PowerPoint presentation, and relayed that Tesoro Alaska Company has been adding value to Alaska's economy for close to 40 years, and is ingrained in the Kenai Peninsula community. Turning attention to page 2 of his PowerPoint presentation, he explained that gasoline is a commodity in both Alaska and the Lower 48, and that Wikipedia defines "commodity" in part as:

... anything for which there is demand, but which is supplied without qualitative differentiation across a market. In other words, copper is copper. Rice is rice. ... One of the characteristics of a commodity good is that its price is determined as a function of its market as a whole.

MR. KNUDSON surmised that this is basically saying that supply and demand - not manufacturers - determines commodity prices. Gasoline is a fungible product in that there is no qualitative difference between one refiner's gasoline and another's. He noted, however, that this is not as true so much anymore because certain states and regions in the Lower 48 are now requiring refiners to make what he called "boutique fuels" - specifically

gasoline - and these are not fungible; this has created what he called "fuel islands" in the Lower 48. For example, states in the Northwest have just started to migrate over to a new gasoline formula because they are now mandating the introduction of ethanol [into the fuel]; this means that anyone in Alaska who wanted to go down south and buy "Neat (ph) 87 octane fuel" would have some difficulty even finding it because most refiners are now making a product to which ethanol can be added. Nonetheless, all refiners are still making essentially the same kind of product - a fungible product.

[9:55:41 AM](#)

MR. KNUDSON explained that if a commodity market experiences an oversupply, prices fall, and if demand for a commodity cannot be met, prices increase. In the short term, commodity markets are completely uncaring about what it costs to manufacture the commodity; again, it is supply and demand which determines market prices. In the long run, however, if the price of a commodity falls below what it costs to produce the commodity, eventually a producer/manufacturer will go out of business; supply will then tighten, and prices will rise again. In response to comments, he opined that the gasoline commodity market in Alaska is functioning normally, notwithstanding challenges, adding that his company has provided the DOL with a lot of confidential information confirming that point.

MR. KNUDSON, turning attention to page 3 of his PowerPoint presentation, explained that over the past couple of decades, gasoline refining/marketing has become very complicated, particularly as a result of government interaction. For example, there are new rules and regulations that the industry has had to come into compliance with and make capital investments in, in order to stay in business. And soon the U.S. Environmental Protection Agency (EPA) will be requiring industry to remove benzene from gasoline, and will be instituting significant regulation of greenhouse gases. Furthermore, Tesoro Alaska Company, because its refinery is located "on tidewater in the Cook Inlet," will have deal with regulations designed to protect beluga whales.

MR. KNUDSON turned attention to page 4 of his PowerPoint presentation, and explained that it illustrates the amount of investment that the refining industry has had to make in order to stay in business under environmental regulatory requirements. Notwithstanding this investment, the price of gasoline, as illustrated on Page 5 of his PowerPoint presentation, has

historically remained relatively constant when adjusted for inflation. In response to a question, he explained that his company's refinery in Kenai has a "nameplate" capacity of 72,000 barrels. In response to other questions, he acknowledged that when a small refinery makes a "regulatory investment," there are fewer barrels across which to spread that cost, and then spoke briefly about Tesoro Corporation's other refineries, adding that the refinery in Alaska doesn't have an extensive conversion capability.

[10:06:58 AM](#)

MR. KNUDSON, turning attention to page 6 of his PowerPoint presentation, noted that Tesoro Alaska Company is an independent refiner, as are all of Alaska's refineries, and thus has to buy its oil on the open market. As an independent refiner, the company's economic model is based on being more efficient and providing a competitive alternative to an integrated major [producer]. An independent refiner doesn't profit from high [retail] prices but instead makes a profit or suffers a loss based on the difference between the market cost of crude oil and the market price of the refined products, and so the goal of an independent refiner is to make a profit, both when retail prices are high and when they are low.

MR. KNUDSON turned attention to page 7 of his PowerPoint presentation, and explained that although there are only two manufacturers of gasoline in Alaska, there are a lot of "marketers". Refiners make a variety of products but have very little ability to differ the amounts of the products they make, and all refiners have "minimum run rates" and all strive, at all costs, to avoid having to turn off their refineries. Refiners, like all manufactures, follow best practices that encourage "just-in-time inventories," because otherwise they will be punished financially if they have either too much crude oil or too much refined product in their tanks at any given time. Refiners also build storage and distribution networks to satisfy customer needs without engaging in long-term storage of either raw crude oil or refined product.

MR. KNUDSON indicated that refiners are faced with the dilemma of selling all the products they produce daily, and Tesoro Alaska Company sells its 50,000 barrels of daily product through a multitude of channels, such as those listed on pages 8 and 9 of his PowerPoint presentation: retail sales at Tesoro stations; wholesale branded rack sales, both through distributors and through dealers; wholesale unbranded rack

sales, both on contract and via open rack; and bulk sales. He noted that Tesoro Alaska Company also exchanges gasoline - as a fungible commodity product - with other refineries, and that this is a standard operating practice throughout the world.

10:14:07 AM

MR. KNUDSON, turning attention to page 10 of his PowerPoint presentation, said it illustrates that Alaska's gasoline demand is very small compared with all other Petroleum Administration for Defense District (PADD) V states. Referring to page 11 of his PowerPoint presentation, which illustrates refinery locations in the U.S., he explained that two of the refineries on the North Slope are just topping plants operated by the producers, who generally just use what they produce at those plants to further their own oil production efforts as opposed to selling it on the commercial market. Alaska, essentially, then, just has [three] refineries, and the reason that the state has so many - given its size - is because of the demand for jet fuel, also known as distillates; Alaska's demand for jet fuel is more than three times its demand for gasoline, as illustrated via page 12 of the PowerPoint presentation, and Alaska's refineries are primarily designed to produce jet fuel.

MR. KNUDSON, referring to page 13 of his PowerPoint presentation, mentioned that approximately one-third of what his company's Kenai refinery produces is considered "the bottoms," for which there is no market in Alaska and which usually sell at a loss. Page 14 of the PowerPoint presentation illustrates that Alaska's gasoline demand is subject to seasonal swings - demand is greater in the summer months and less in the winter months - and this causes difficulties for refiners as they attempt to adhere to their run rates. Page 15 of the PowerPoint presentation states that seasonal swings can hurt a business's return on investment regardless of what kind of business it is.

MR. KNUDSON indicated that page 16 of his PowerPoint presentation illustrates that on a monthly average, Alaska's retail sites only sell a bit more than half the gasoline that Washington's retail sites sell and only about one-third of the gasoline California's retail sites sell. Page 17 of the PowerPoint presentation illustrates that Tesoro's branded outlets constitute only about 15 percent of Alaska's total retail outlets; he added that Tesoro also supplies only about 15 percent of Alaska's total retail market. [Page 18 of the PowerPoint presentation is a duplicate of page 10.] Page 19 of the PowerPoint presentation shows an overhead view of Tesoro

Alaska Company's Anchorage tank farm. Turning attention to page 20 of his PowerPoint presentation, he explained that maintaining maximum throughput is essential for a successful fuel terminal, and that in order to maximize its throughput at the Port of Anchorage, Tesoro leases storage to its competitors.

[10:21:45 AM](#)

MR. KNUDSON referred to page 21 of his PowerPoint presentation, and explained that the commodity price for fuel is determined by [the price of] the last barrel going into a particular market to satisfy the demand in that market. He mentioned that this is where the concepts of import parity and export parity come into play, and that all producers play a critical role. Referring to page 22 of his PowerPoint presentation, he said it illustrates recent volatility in the Pacific Northwest spot market, adding that the recent daily price swings are unprecedented. Risk constitutes a cost, and a company must protect itself against risk in order to stay in business.

MR. KNUDSON turned attention to pages 23 and 24 of his PowerPoint presentation, which illustrate some retail gasoline prices in Anchorage and Juneau on 11/21/08. The lowest retail price listed for Anchorage is \$2.76/gallon, and the lowest retail price listed for Juneau \$3.22/gallon, which includes a 5 percent sales tax. Juneau has no refineries, and is a pure import market, though it is 1,000 miles closer to the Pacific Northwest spot market than Anchorage is. Turning attention to page 25 of his PowerPoint presentation, he said it compares [both before-tax retail gasoline prices and rack rates] in Anchorage with those of Seattle. With the exception of the steep rise and the steep fall in the price of Alaska North Slope (ANS) crude oil, he remarked, the "pricing curves" are on par with historical trends. In other words, it appears that Alaska's commodity market is working roughly just as it always has. Since an independent refiner makes money based on the difference between the market cost of crude oil and the market price of the refined products, it can be troublesome when the price of crude oil and the Pacific Northwest spot market price, for example, get close, just as they are now. If this persists, it could result in a refinery going out of business, and supply will subsequently decrease.

MR. KNUDSON, referring to page 26 of his PowerPoint presentation, said it illustrates the spread - as a percentage - between the price of ANS crude oil and [the before-tax retail gasoline price] in Anchorage. From December 2007 through

October 2008, the percentage was exceptionally low, but is now moving back to "normal" levels. He again pointed out that a refiner has to be able to make a profit in both a high-price environment and a low-price environment. Referring to page 27 of his PowerPoint presentation, he said that the refining industry is one of the few successful value-added industries in Alaska. Tesoro Alaska Company has been adding value to Alaska's oil for 39 years and has employed Alaskans to make products that Alaskans buy. Economists in the Lower 48 have determined that the [job multiplier] for a refinery is nine, much higher than for other industries, and this means that in Kenai, Tesoro accounts for approximately 1,800 jobs - 200 jobs in the refinery itself, and each of those jobs multiplied by nine. In-state refineries, by supplying jet fuel, have helped underpin the growth of the international air cargo industry in both Anchorage and Fairbanks, and this demand for jet fuel has in turn helped underpin the ability of in-state refineries to make more gasoline and diesel. For example, even though Alaska is geographically distant from large fuel markets, the reliability of its refineries' gasoline supply is excellent.

MR. KNUDSON, turning attention to page 28 of his PowerPoint presentation, said that Tesoro is continuing to provide proprietary data to the DOL, and that Tesoro maintains the belief that the DOL's confidential forum is the correct process through which to investigate gasoline prices. In conclusion, he urged the legislature to wait for the DOL's report before getting too far ahead with any legislative proposals, surmising that that report could assist the legislature in its deliberations. In response to a question, he offered his understanding that the DOL intends to conclude its investigation before the end of the year.

REPRESENTATIVE HAWKER noted that the DOL is investigating whether the high retail gasoline prices in Alaska are the result of any criminal activity, but that the legislature, via these meetings, is instead considering policy issues related to those high prices. Referring to page 25 of Mr. Knudson's PowerPoint presentation, he asked why retail gasoline prices in Anchorage began to diverge dramatically from Seattle's retail gasoline prices in April 2008, and why Alaska's prices didn't decrease when Seattle's retail gasoline prices and the price of ANS crude oil decreased.

[10:39:59 AM](#)

MR. KNUDSON said he could not point to a reason why, and reminded members that the Pacific Northwest commodity market is geographically distinct from Alaska's commodity market. Furthermore, demand in the West Coast's gasoline markets has dropped significantly, thus immediately altering the supply:demand relationship in those markets; in Alaska, in contrast, the supply:demand relationship did not change as fast or at all, and this might account for the aforementioned divergence. However, historically, similar divergences occur roughly every September, and some of that has to do with how, in the summertime, the gasoline supply on the West Coast must be altered in order to comply with [more stringent environmental] regulations, but need not be altered in the wintertime, thus essentially increasing the supply and resulting in a decrease in price.

MR. KNUDSON, in response to comments, opined that because the Pacific Northwest spot price has been at or below the ANS crude price this fall - as illustrated via page 25 of his PowerPoint presentation - this indicates that the Pacific Northwest market is out of balance. Perhaps Alaska's commodity market is, in fact, in balance. In response to a question, he said he doesn't know how many days Tesoro Alaska Company could store an excess supply of gasoline before finding itself in trouble, but reiterated that his company simply cannot allow such a thing to happen.

CHAIR RAMRAS questioned whether a boycott on gasoline stations would bring retail prices back down in the near term.

MR. KNUDSON acknowledged that lowering consumer demand would definitely have an impact on Alaska's supply:demand relationship. In response to questions, he concurred that the gasoline manufacturing capacity of refineries in Alaska, especially during winter months, exceeds demand; in other words, because of the demand for jet fuel, Alaska's refineries could find that they are making too much gasoline to properly account for seasonal swings in demand. In response to comments, he explained that all refiners in Alaska have to calculate how much gasoline they can produce without having to export it at a loss.

REPRESENTATIVE HAWKER suggested that the high in-state prices Alaska's refiners are setting are subsidizing any losses that might result from exporting excess supply to the Lower 48.

[10:48:54 AM](#)

CHAIR RAMRAS asked what the rack rate is at [Tesoro's Kenai refinery].

MR. KNUDSON said he hasn't been provided with that information.

CHAIR RAMRAS asked Mr. Knudson to provide the committee with the current rack rates at all of Tesoro Corporation's refineries.

MR. KNUDSON said he would, but warned that that information would not reflect Alaska's market and that the fuel at the company's other refineries could not be transported to Alaska.

CHAIR RAMRAS predicted that the DOL's investigation will conclude that Alaska's high retail gasoline prices are not the result of illegal activity, and again opined that the governor herself should be speaking to Alaska's refiners about those high prices because no one has been able to explain, to his or his constituents' satisfaction, the disparity between Alaska's retail gasoline prices and retail gasoline prices in the Lower 48. He then expressed disfavor with the DOL's statement in its press release that the administration can do nothing to lower Alaska's retail gasoline prices.

REPRESENTATIVE LYNN surmised that the governor is not unaware of the problem, and expressed satisfaction with the steps being taken thus far.

REPRESENTATIVE KELLY offered his belief that the high price of gasoline at the refinery level is caused by too much government regulation, and cautioned against rushing to add another layer of government regulation in an attempt to address the issue. It may instead be more appropriate to simply continue having the refiners justify to the legislature why Alaska's gasoline prices are so high.

[10:58:49 AM](#)

JEFF COOK, Director, External Affairs, Flint Hills Resources, said he did not have any new information to add to that which he provided at the previous two meetings on this topic. He relayed that Flint Hills Resources is continuing to provide the DOL with requested information, and is working on a presentation for the committee's next meeting on the topic of high gasoline prices in Alaska. He noted that he, too, is precluded by law from disclosing information about his company's pricing strategies, and relayed the names of individuals from his company who might be speaking at the next meeting.

11:02:38 AM

CLYDE (ED) SNIFFEN, JR., Senior Assistant Attorney General, Commercial/Fair Business Section, Civil Division (Anchorage), Department of Law (DOL), relayed that the DOL will be meeting with Delta Western, Inc.; Holiday Stationstores, Inc.; and Costco Wholesale Corporation. Delta Western, Inc., he explained is one of Southeast Alaska's primary fuel suppliers, and operates a barge transportation company. Obtaining data from such a company could provide the DOL with a better picture of why Southeast Alaska's pricing structure is as it is. As a barge operator, Delta Western, Inc., is largely responsible for setting the wholesale price of fuel in Juneau and other Southeast Alaska communities; retailers then use that price as a benchmark when setting their retail prices.

MR. SNIFFEN said that although Delta Western, Inc., is not the only wholesale provider of fuel in Southeast Alaska, it is a significant player, purchasing fuel in the Pacific Northwest and having "terminaling" capacity of between 10 million and 15 million gallons in Juneau. When Delta Western, Inc., fills those tanks, it might take Juneau consumers several months to use up that supply, throughout paying the price set when the tanks were filled up. The dynamics of fuel pricing in an import market such as Juneau's, therefore, are a lot different than in the Railbelt, where refineries are located. In response to a question, he surmised that he would be able to get data from Delta Western, Inc., and other companies regarding how fast Juneau consumers go through Juneau's fuel supply, adding that that information would be included in the DOL's final report.

MR. SNIFFEN explained that the DOL has been working with Barry Pulliam from Econ One Research, Inc., to try to make sense of all the data the DOL has been gathering throughout its current investigation into why retail gasoline prices in Alaska haven't fallen at same rate as retail gasoline prices in the Lower 48. He indicated that having a better understanding of all the market factors responsible for gasoline pricing being what it is will enable the DOL to better determine whether Alaska's high retail gasoline prices are indeed the result of illegal activity. He said he anticipates that the DOL's investigation should be concluded by the start of the next legislative session.

MR. SNIFFEN explained that his office was recently asked by the attorney general to provide the public with an update on its

investigation, and did so in the form of the aforementioned press release; however, providing factually accurate information without divulging confidential information was difficult to do.

CHAIR RAMRAS noted that Petro Star, Inc. (PSI), has provided the committee with written testimony.

[11:12:09 AM](#)

BARRY PULLIAM, Senior Economist, Econ One Research, Inc., in response to a question, concurred that on the issue of gasoline pricing, there are complexities in the market place to be considered; for example, one must recognize that the retail price of gasoline is dependent upon both the market price of crude oil as well as other factors such as the cost to manufacture gasoline and the cost of distributing it, with the latter actually constituting another market. So although Alaska and the rest of the country, particularly West Coast states, have to reckon with the market price of crude oil and share similar types of distribution systems, the composition of the "downstream" markets is very different in the rest of the country than it is in Alaska.

MR. PULLIAM also acknowledged that perhaps folks in the Lower 48 are benefiting from more competition, since anytime a market has more competitors, the quicker pricing will respond to changes in raw material costs. Mr. Pulliam then referred to page 25 of Mr. Knudson's PowerPoint presentation, and noted that the price of ANS crude oil appears to have peaked in July 2008, and that over the course of the next four and a half months the price dropped by about \$100 a barrel. This was an unprecedented drop, and must be taken into account when considering the issue of retail gasoline pricing. All other parts of the country except Alaska and Hawaii responded fairly quickly to the change in crude oil prices, with only a small lag in the lowering of retail gasoline prices; this is the result of competition. In Alaska, market forces are actually working, though in a delayed manner, to bring retail gasoline prices down, he opined. Mr. Pulliam concurred with the data on page 25 of Mr. Knudson's PowerPoint presentation indicating that [Pacific Northwest spot market] prices for gasoline in the Lower 48 have fallen below ANS crude oil prices, which, he relayed, he hopes don't fall any lower than they are now.

MR. PULLIAM, in response to a comment, predicted that unless the price of crude oil falls below where it is now, gasoline prices in the lower 48, at least at the wholesale level, "have probably

made their run," and opined that having those prices remain below the cost of crude oil is not sustainable. There has been some "fattening" in the margin between rack rates and retail prices, and that's getting worked off; in the last week or so, for the first time this fall, there has actually been a bit of an acceleration in the speed with which Alaska's prices dropped compared to how much prices in the Lower 48 have dropped. He predicted that retail gasoline prices in Anchorage are going to continue to fall, and so again urged the legislature to keep in mind the unprecedented drop in crude oil prices - an anomaly in and of itself.

CHAIR RAMRAS asked Mr. Pulliam what the legislature could do now to bring immediate relief to constituents with regard to retail gasoline prices.

[11:24:44 AM](#)

MR. PULLIAM surmised that nothing can be done within the next month or so to lower Alaska's retail gasoline prices at the same rate as retail gasoline prices are lowering in the rest of the country; nothing, that is, short of imposing some sort of regulation to that effect. He mentioned that when regulatory solutions were attempted elsewhere, they failed.

CHAIR RAMRAS said his constituents want something done now and won't be satisfied with the answer that nothing can be done.

MR. PULLIAM clarified that he did not mean to say that prices in Alaska won't continue to move towards parity with prices in the Lower 48 between now and [the end of the year]; rather, prices in Alaska will continue to decline, and the gap in pricing levels will continue to narrow.

MR. PULLIAM, on the issue of the possible unintended consequences of attempting to regulate pricing, suggested that such regulation could limit participation in Alaska's gasoline industry; could reduce competition; could limit profit opportunities; could result in underinvestment in the industry; could result in product [both gasoline and jet fuel] shortages; and could result in a decline in the quality and/or choice of products. Furthermore, there is also the possibility that such regulation could result in even higher retail prices, as occurred in Hawaii when that state chose to regulate gasoline pricing; once a price cap is set, people tend to price their product at that level, thus eliminating the potential for competition [to keep prices low]. Another point to consider is

that regulating the price of petroleum products will require extra personnel to monitor prices, and so the question will then become at what level is that done and at which locations.

MR. PULLIAM, in response to comments and a question, acknowledged that the market in Southeast Alaska doesn't respond in the same way that the market in Western Alaska does, regardless that they are both import markets, because of differences in scale. Therefore, when considering the concept of regulation as the means of reducing prices, the legislature must also keep in mind that the situation is different in the Railbelt, for example, than it is in other locations around the state; in other words, regulation that works in Anchorage may not work elsewhere in the state.

REPRESENTATIVE HAWKER asked whether the lag in pricing parity could be the result of a difference in the supply/procurement process in the various Alaska markets.

MR. SNIFFEN said he is not sure but would be seeking more information on that point. He too remarked on the recent narrowing of the gap in pricing parity, and also offered his belief that that gap will continue to narrow, and mentioned some retail prices he's seen recently. On the issue of what can be done now, he said that the DOL is currently very limited in what it can do legally to stop someone who might be charging high prices absent any actual criminal activity. Furthermore, it could very well be that Alaska's high gasoline prices are simply the result of unconscionable pricing practices, and although existing statutes would allow the DOL to put a stop to such practices, [it could be difficult to prove that they are actually occurring].

CHAIR RAMRAS, after making comments and in response to a question, acknowledged that he has not yet asked the governor to meet with Alaska's refiners regarding their pricing practices.

[11:45:49 AM](#)

MR. SNIFFEN ventured that it might be easier to find evidence of collusion than evidence of unconscionable pricing practices. And even if any such evidence is found, it might still not result in a lowering of prices. In conclusion, he suggested that absent any criminal activity, [consumers] must just let the market work itself out.

CHAIR RAMRAS asked whether the recent repeal of the State's motor fuel tax of \$.08 has really been passed on as a savings to the consumer.

MR. PULLIAM said the data indicates that retail prices did drop by that amount once the repeal took effect, but acknowledged that he is unable to say whether rack rates would have come down anyway even if the tax had not been repealed. He pointed out, however, that in the short term, gasoline taxes don't affect a market's supply:demand relationship. In response to another question, he explained that retailers still aren't charging consumers that \$.08 tax, but added that he can't say whether wholesale prices are higher now than they otherwise would be had the tax not been repealed.

REPRESENTATIVE HAWKER, again referring to page 25 of Mr. Knudson's PowerPoint presentation, opined that Alaska retailers have simply raised their prices by \$.08.

CHAIR RAMRAS agreed, and characterized the retail gasoline prices that Alaskans are paying as unconscionable compared to what consumers are paying in the Lower 48. He then listed some of the information that might be included in the aforementioned forthcoming committee report, and spoke of how the committee might be proceeding after the lunch break.

The committee took a recess from 11:54 a.m. to 1:27 p.m.

CHAIR RAMRAS, on the issue of possible future legislation, indicated that one piece of legislation might pertain to increasing the state's anti-trust penalties, and another might address instances of price gouging.

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MR. PULLIAM, in response to a request, offered his understanding that the price-gouging statutes in other states are all triggered by the declaration of a state of emergency - such as would result from a hurricane - and are intended to prevent retailers from taking undue advantage of consumers during such times. One challenge with that type of legislation, however, is in defining exactly what constitutes price gouging, because in order for any such legislation to be meaningful in Alaska, the behavior of price gouging would have to be quantifiable.

CHAIR RAMRAS noted that another piece of possible future legislation might authorize State regulation of the industry,

and might take into account market differences in Alaska's various regions.

MR. PULLIAM said that in going that route, one would have to consider several things, one being at what level should regulatory oversight be imposed; for example, there is the refinery level, the "rack level," and the retail level, and each level has different challenges to contend with. Furthermore, particularly in Alaska, geographic factors would also have to be considered. This was an issue when Hawaii chose to regulate, because the outlying islands had to barge gasoline into smaller terminals with different distribution systems, and so a different factor had to be calculated depending upon the destination of the gasoline. Alaska's situation would be even more complicated because there is no central point through which the product would first flow.

MR. PULLIAM explained that any type of regulatory measure would have to give market participants the incentive to provide petroleum products reliably in all locations, so as not to run the risk of having a shortage. Another challenge is that in trying to find the correct level of regulatory oversight, one runs the risk of setting the price either too low or too high. The balance is delicate, he opined, and surmised that the State - presumably via the Regulatory Commission of Alaska (RCA) - would spend a lot of time and energy trying to design and monitor the details of such regulatory oversight. In response to a question, he suggested that the State should consider whether there is any artificial barrier to competition, such as overregulation or a lack of infrastructure. Consider, for example, that the more terminaling capacity there is in the state, the better, because it opens up the possibility of bringing product in from elsewhere, and that threat of competition could act as a disciplinary tool for the market.

CHAIR RAMRAS noted that the jet fuel producers in Alaska have been very responsive to the market.

MR. PULLIAM pointed out, though, that buyers of jet fuel can form consortiums and pool their buying power, which is not something typically seen with regard to gasoline, perhaps because doing so would raise antitrust issues.

REPRESENTATIVE HAWKER asked what the State could do to encourage competition.

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CHAIR RAMRAS mentioned that the written testimony from PSI touches upon that topic. He then remarked on the hazard of having an excess supply on the market, as has occurred in the Lower 48 when existing refineries have expanded.

MR. PULLIAM characterized refining as a cyclical business - in that both capacity and demand can fluctuate quickly - one requiring large investment as well as being risky.

CHAIR RAMRAS observed that if an entrepreneur were to bring gasoline up to Alaska, he/she would run risk of not being able to sell that gasoline at a price sufficient to cover costs, particularly given that Alaska's refineries already manufacture enough gasoline to satisfy the needs of the state.

MR. PULLIAM, in response to a comment, explained that although the historical pattern is for Alaska's gasoline prices to lower at a slower rate than gasoline prices in the Lower 48, they do still continue to lower; therefore, if this historical pattern maintains itself, Alaska's gasoline prices will lower further than they are now. He noted that rack rates in the Pacific Northwest have dropped below the price of crude oil, and opined that rack rates cannot stay below crude oil prices for prolonged periods of time. In response to a question, he also opined that even if demand does not increase, rack rates down south will have to increase above the price of crude oil in the long term, and that they most certainly will if demand increases.

MR. PULLIAM, in response to another question, offered his belief that Alaska's retail gasoline prices will fall because of competition in the market over the available margins between the cost of crude oil and the price of gasoline; those margins are high in Alaska. Retail prices are also likely to continue decreasing over the coming months since the demand [for gasoline] is lower in the wintertime. If prices don't continue to lower, he warned, then that would be cause for concern.

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MR. PULLIAM, in conclusion, cautioned the legislature against taking action now - particularly with regard to instituting regulatory oversight - based just on how the market has been behaving over the last few months; the legislature should instead gather more data [while] seeing whether the market corrects itself.

REPRESENTATIVE LYNN asked whether there is any correlation between the recent national and international financial crises and the high price of gasoline in Alaska.

MR. PULLIAM said that in general, the financial crises and deteriorating economy are having an impact nationwide, though probably a more immediate impact elsewhere than in Alaska. He predicted that if the economy stays weak, it could [reduce] Alaska's historical summer increase in demand, and this will in turn impact fuel prices.

CHAIR RAMRAS expressed a reluctance to interfere with the market via potential statutory or regulatory changes.

REPRESENTATIVE LYNN relayed that he has concerns as well because of the potential negative impact on the free market.

REPRESENTATIVE DAHLSTROM concurred.

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JERRY McCUTCHEON suggested that the State either hire an antitrust expert to investigate the gasoline pricing situation in Alaska, or ask the U.S. Office of the Attorney General to conduct an investigation into the matter. He opined that the level of gasoline pricing in Cook Inlet is inappropriate and would fall apart under truly close scrutiny. In response to a question, he offered his belief that antitrust behavior is taking place at the refinery level, and that the refiners are acting together to keep prices high.

CHAIR RAMRAS offered his understanding that only Legislative Council or the Legislative Budget and Audit Committee have the authority to hire legal counsel to pursue antitrust violations.

MR. McCUTCHEON opined that because there is so much money at stake, the legislature has a duty to get the best investigator it can even if it means that another committee at some other point in time authorizes it. In response to comments, he also opined that the committee's continuing on as it has been on this issue, without the benefit of professional investigatory expertise, is futile.

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DONALD WESTLUND said that considering how low retail gasoline prices currently are in the Lower 48, it seems that retail

gasoline prices in Alaska don't seem to decrease very fast, though they are quick to increase. In response to a question, he offered his understanding that currently the retail price of gasoline in Ketchikan is \$3.75/gallon or higher.

CHAIR RAMRAS read bullet point number 7 of the aforementioned DOL press release [original punctuation provided]:

Gasoline sold in Southeast Alaska is barged up from the Pacific Northwest and from Cook Inlet. Because fuel is only barged in once a month or every few months, it takes longer for prices to reflect current market conditions. It may take two or three months to exhaust current supply before less (or more) expensive gasoline is available and sold to retailers.

CHAIR RAMRAS recalled that previous testimony has indicated that in Juneau, it can take several months to exhaust the fuel inventory in order to make room for a new gasoline shipment, and that in places like Kotzebue, which is currently subjected to a retail gasoline price of about [\$7.85/gallon], bulk fuel supplies come in only once a year. He surmised that the DOL's final report will take up this issue in greater detail.

MR. WESTLUND noted that although barge transportation is touted as the cheapest form of transportation, [retail gasoline] prices aren't consistent in Southeast Alaska. For example, because Ketchikan is the first stop for barge shipments, one would assume that the price of gasoline in Ketchikan would be the cheapest, but it is not. He said this is really discouraging, particularly given that for his guided sport [fishing] business, he burns approximately 100-120 gallons of fuel every day, so when the price of fuel goes up, it takes more customers to pay for the fuel. When there are only three or four customers per day, that does not leave much margin for profit considering all the other costs that must also be met. In response to a comment, he relayed that he did not go commercial shrimping this year because of the cost of fuel.

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DOLORES "DORRIE" FARRELL said she echoes the concerns expressed by the two prior testifiers, though noted that the price of gasoline is not such an issue for her personally because there are so few roads in Sitka. She shared her belief that the [pricing] situation [in Sitka] began deteriorating about four or five years ago, when "Texaco was bought out by" Petro Marine

Services, adding that although she wrote letters of complaint to Representative Peggy Wilson and the attorney general's office, no action was taken. She said she disagrees with statements advocating that the free market be allowed to function as is, surmising that the nation's current fiscal situation is due to the federal government taking just that route. It's unconscionable, she opined, that in places where there is no competition, such as in [many communities in Southeast], a retail gasoline company can charge whatever it pleases; retail gasoline prices are quick to go up when the price of crude oil goes up, but it's months before consumers see any corresponding drop in retail gasoline prices when the price of crude oil decreases.

MS. FARRELL opined that there is a lot of injustice occurring, and that consumer affairs are a legitimate concern of both federal and state governments, which shouldn't simply stand back and allow the free market to find its own balance, particularly given that when there is no competition, prices get to remain extremely high. She questioned what effect the antitrust legislation of the early 1900s has been having. With regard to the [aforementioned DOL] press release, she said, "I just have a lot of issues with this," and recommended that a comparison study [of retail gasoline prices] in Sitka, Petersburg, and Juneau be made, since Sitka and Petersburg have "no real competition" but Juneau does. In response to a question, she mentioned that a [new] company in Sitka was recently charging \$3.65/gallon, and that Petro Marine Services recently dropped its price to \$3.61/gallon but not long ago was charging close to \$5.00/gallon. This lowering of retail prices by Petro Marine Services is the result of competition, she opined, and offered her understanding that there are plans for another company to start selling marine fuel in Sitka, but those plans are being fought with vigor by Petro Marine Services.

MS. FARRELL said that this is not right, and opined that it is the function of the legislature to address such situations as well as to consider how competition influences the price of gasoline in places like Juneau, for example. She then relayed that when she filled up her home heating oil tank a week ago, the price was \$3.974/gallon. This cannot go on, she opined, and questioned where people are going to turn to for help if the government won't do anything it. She relayed that the local utility has said that if people continue to convert to electric [heat], there will be blackouts.

CHAIR RAMRAS noted that the price of [number 1 heating oil] in Fairbanks is now approximately \$2.45/gallon, and that the price of home heating oil is a big concern in his community. He too remarked on the fact that retail gasoline prices in Wrangell should be some of the lowest in the state given that those tanks were just filled up with lower-cost gasoline from Seattle, but are instead still some of the highest prices, and surmised that the DOL will be investigating that situation as well.

MS. FARRELL pointed out that although the news on the radio periodically announced that Hawaii had the highest price of gasoline, the price quoted was always \$.90 to \$1.00 lower than the price of gasoline in Alaska, even though Hawaii is further from the mainland than Sitka. She opined that consumer affairs must be an active, basic, functioning part of government, and remarked, "If government doesn't protect its citizens, what is its purpose?"

REPRESENTATIVE DAHLSTROM relayed that gasoline is \$2.74/gallon in Eagle River - the lowest it's been in a long time.

CHAIR RAMRAS, in response to a question, confirmed that the committee has not yet heard from the RCA.

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TIM LUTHER - regarding the statement in the DOL's press release that a community's retail gasoline prices won't go down until the community has exhausted its existing, more-expensive fuel inventory - pointed out that that's not what occurs when the cost of the new inventory exceeds the cost of the old inventory: prices rise immediately even when there is still [lower-priced] fuel in inventory. He opined that the DOL's argument should apply in both situations.

CHAIR RAMRAS said in Barrow the price of gasoline is much lower than in Kotzebue, because Barrow got its supply when the [rack rate] was lower. Wrangell, on the other hand, just had its fuel supply topped off at what should have been a rack rate of about \$2.00 or less, but still has a retail price of \$4.76/gallon.

MR. LUTHER recollected that gasoline in Kodiak, which has two suppliers of gasoline, was consistently at about \$4.64/gallon for about a year and then increased to a bit over \$5.00/gallon when the price of crude oil spiked. He questioned whether maintaining a certain price simply because there's no competition could be considered price gouging, and why retail

prices in Alaska are taking so long to decrease given that retail prices in the Lower 48 are declining rapidly. He also noted that although there is a decline in gasoline usage during the winter months, there is an increase in heating oil usage during those months; currently, the price of home heating oil in Kodiak is \$3.61/gallon, and some residents can go through about 100 gallons in about a week and a half.

CHAIR RAMRAS again offered his understanding that the DOL will be asking questions of those companies that obtain their gasoline supply via barge.

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DICK COOSE opined that the DOL's press release doesn't contain much in the way of new information, but does contain some serious errors. For example, although bullet point number 7 says that fuel is only barged to Southeast Alaska once a month or every few months, in the summer, gasoline is barged to Ketchikan every two weeks or more often depending on the demand. About a month ago, the City of Ketchikan got a fuel delivery for its diesel generators, with a transportation cost of only \$.22/gallon; meanwhile, retail gasoline prices in Ketchikan are now about \$1.70/gallon more than prices in the Lower 48. He characterized this discrepancy as outrageous.

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MICHAEL E. McCARTHY provided the committee with the diesel fuel prices he'd paid in Alaska and in various other locations while on a trip down south, including the dates he purchased his fuel, and offered his belief that those prices have had an impact on tourism. And as of yesterday, he noted, the price of gasoline in Homer was \$3.34/gallon, whereas the national average price was down to \$2.02/gallon. He questioned why the recent unprecedented reduction in the price of crude oil has not been reflected at the pumps [in Homer]. Historically, gasoline was always less expensive than diesel, but now it is not, and he said he found that to also be true in Denmark, Norway, and Sweden when he was there a few months ago. He then listed some prices to illustrate his point.

MR. McCARTHY said he has since compared diesel and gasoline prices between Wyoming and Alaska - since those two states are similar in population, distribution [networks], and oil and gasoline production - and found that the prices for both diesel and gasoline are higher in Alaska than in Wyoming. After

listing some of those prices, he questioned why Alaska's prices were so high. He suggested to the committee that they consider instituting a prohibition against usury-like gasoline pricing in Alaska, and opined that there is no reason why the record profits recently enjoyed by the major oil producers should result in a burden being placed upon the citizens of Alaska and the rest of the country.

CHAIR RAMRAS noted that "we" have enforced new, low-sulfur requirements for diesel fuel which may have impacted the price of diesel in Alaska, and surmised that that regulatory cost is being passed on to the consumer. The legislature, therefore, must be careful not to put further pressure on the consumer through statutory or regulatory changes that have unintended consequences.

MR. MCCARTHY offered his understanding, though, that Scandinavian countries have the same low-sulfur requirements - and, therefore, the same production costs - and yet diesel costs less than regular gasoline in those countries.

The committee took an at-ease from 2:47 p.m. to 3:01 p.m.

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JAVEN OSE questioned whether it is really in the best interest of Alaska's citizens to have to pay \$1.50 more [for fuel] than people pay in the Lower 48, particularly given that Alaska's citizens own the state's resources, including oil. He then asked whether members were familiar with the contract between Flint Hills Resources and the State of Alaska.

CHAIR RAMRAS indicated that members were not.

MR. OSE opined that members should become familiar with that contract. He then offered his understanding that during the "energy crisis," the State of Alaska did not increase "the amount of refined fuel," adding, "When you want the price to come down, you flood the market." He continued:

The amount of barrels per day allowed at the Flint Hills refinery is 22,000 at the bottom and 77,000 at the top, and for five years, we've been pumping [40,000 - 45,000 barrels] and taking the rest in money and shoving it in the legislature or shoving it in the permanent fund.

MR. OSE opined that the state of Alaska is in the oil business, that the people are getting gouged, and that it's up to the legislature to do something about that. One way to address the problem is for the State to take part in the oil business; regardless that the State has failed in its involvement with other public sector industries, no one is losing money in the oil business today. He recommended that the legislature or the administration put out either a general order or an executive order requiring that [gasoline] prices in Alaska be fixed. He named Iraq, Iran, Saudi Arabia, and Venezuela as countries which sell their gas at world market prices and provide gas to their citizens at very low prices. He questioned why the legislature doesn't simply order Flint Hills Resources to produce the maximum amount allowed. The opportunity is there to give the people of Alaska \$1/gallon gasoline, but is instead taking care of its resource in "a very poor fashion," he opined, particularly given that gasoline prices in some areas of the Lower 48 have dropped down to \$1.65/gallon. That's outrageous, he remarked.

MR. OSE asked how much it costs for the Flint Hills Resources refinery to producing a gallon of gasoline.

CHAIR RAMRAS explained that that is considered to be confidential information.

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MR. OSE opined, then, that the solution is for the State of Alaska to have its own refinery, and characterized the refiners currently operating in Alaska as price gougers. On the issue of gasoline prices in Alaska increasing one day after a new [higher-cost] shipment arrives but taking months to drop after a lower-cost shipment arrives, Mr. Ose characterized that as crazy, adding "We own it, let's act like we own it." In response to comments, he opined that the refineries are where the problem is, and that they are contractually required to accommodate the State in its requests that the refineries refurbish, rebuild, or update their facilities, or increase the amount of refined product they produce.

MR. OSE, in conclusion, urged the legislature to step up to the plate and do something about the situation; for example if the State were to start producing jet fuel, Anchorage could once again become "the air crossroads of the world." In response to comments, he said, "It falls, not in the governor's lap, it falls in the legislature's lap - let's get some cheap gas here

until that stuff runs out" - and surmised that even if the governor were to issue an executive order to put a price freeze on gasoline of \$1.00/gallon, "we'll argue it for the next 10 years in court, but we'll get 10 years' worth of \$1/gallon gasoline."

ADJOURNMENT

There being no further business before the committee, the House Judiciary Standing Committee meeting was adjourned at 3:15 p.m.