

HOUSE FINANCE COMMITTEE
April 11, 2014
6:36 p.m.

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CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 6:36 p.m.

MEMBERS PRESENT

Representative Alan Austerman, Co-Chair
Representative Bill Stoltze, Co-Chair
Representative Mark Neuman, Vice-Chair
Representative Mia Costello
Representative Bryce Edgmon
Representative Les Gara
Representative David Guttenberg
Representative Lindsey Holmes
Representative Cathy Munoz
Representative Steve Thompson
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Joe Balash, Commissioner Designee, Department of Natural Resources

SUMMARY

HB 287 APPROVE TESORO ROYALTY OIL SALE

HB 287 was HEARD and HELD in committee for further consideration.

#hb287

HOUSE BILL NO. 287

"An Act approving and ratifying the sale of royalty oil by the State of Alaska to Tesoro Corporation and

Tesoro Refining and Marketing Company LLC; and providing for an effective date."

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Co-Chair Stoltze discussed the meeting agenda.

Representative Wilson WITHDREW Amendment 1 (28-GH2862\A.3, Nauman, 4/9/14) that had been moved in a prior meeting [4/9/14 6:06 pm](copy on file).

Representative Wilson MOVED to ADOPT replacement Amendment 1, 28-GH2862\A.5, Nauman, 4/11/14 (copy on file).

Co-Chair Stoltze OBJECTED for discussion.

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Representative Thompson discussed that the replacement amendment made three changes. He pointed to page 3, line 7 of the amendment that changed the allowable credit from \$15 million to \$10 million per refinery. Second, the credit for investment would be changed from 10 percent to 40 percent with a maximum of \$10 million (page 4). The amendment maintained the \$20 million maximum for the two credits combined. Third, the amendment would expand the qualified infrastructure credit per refinery to include the transport of refined petroleum products or petroleum-based feed stock. The third change had been included to address getting piping to two of the refineries, which could also be used as part of the refineries' infrastructure.

Representative Gara asked for the location of the third change.

Representative Thompson replied that the third change appeared on page 5, lines 20 and 21.

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Co-Chair Stoltze asked the Department of Natural Resources (DNR) to comment on the amendment.

JOE BALASH, COMMISSIONER DESIGNEE, DEPARTMENT OF NATURAL RESOURCES, discussed that the amendment was supported by the administration. The underlying issue pertained to the unhealthy condition of Alaska's instate refineries. He

relayed that with the upcoming closure of the Flint Hills Refinery certain costs would increase for the Petro Star facility in North Pole. The department was greatly concerned about the potential consequences the state would face if it were to lose Petro Star's North Pole and Valdez Refineries. He addressed benefits provided by the instate refineries. He detailed that the Quality Bank fees paid by refineries were reflected back in increased revenue for the state; the fees included an increase in the state's royalty and a tax benefit. Estimates on royalty revenue were more precise given the information reported in royalty values; taxes were harder to assess due to the way the system was structured. He communicated that the royalty value on the Quality Bank payments was approximately \$20 million in 2013; the tax impact approached an additional \$30 million. Additionally, when the state sold its royalty in-kind (RIK) it typically sold it to instate refineries. In the past three years the state had achieved a higher value by selling in-kind than it would have received if the oil had been left in-value with the producers. The total difference for 2011 through 2013 exceeded \$136 million. He stressed that the figures represented real benefits to the state's treasury. He did not know exactly what the numbers would look like if the refineries shut down. He shared that the state would continue to look for opportunities to sell its royalty for some marginal premium; it was difficult to know whether it would be achievable. He theorized that if FERC got the Quality Bank formula exactly right, in theory the Quality Bank adjustment would no longer be necessary because oil coming out at the southern end of the Trans-Alaska Pipeline System (TAPS) would be more valuable. He did not subscribe to the theory.

Commissioner Balash elaborated that the issue was currently being contested with the Federal Energy Regulatory Commission (FERC); exactly what it would look like in the end was not known. However, it was currently known that the positive treasury impacts from the state's refineries exceeded the sticker price on the amendment. He believed the amendment was warranted and that the economic consequences of the refinery closures would be quite negative for Alaska in the long-term (particularly if there was a normalized ANS Crude price). He communicated that the department had considered multiple ways to address the challenge including selling the state's royalty at a discounted price. Additionally, the department had considered Quality Bank tax credits; however, each of the

options had created their own problems including an unlevelled playing field for certain refineries that were not connected with TAPS. He believed the amendment represented a solution with the right combination of items.

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Commissioner Balash continued to discuss support for the amendment. He detailed that the package provided an incentive to producers to choose to sell their oil to instate refineries. Second, the 40 percent capital investment credit was provided. Investments could be made in the facilities to increase efficiency and profitability in order for the refineries to compete more effectively for fuel products needed for military and commercial aviation and for home heating, diesel, and gasline. He shared that the refinery credit was modeled in part on the small producer credit associated with the oil and gas production tax. The figure was a fixed amount; a refinery would qualify if it refined an average of more than 17,500 barrels per day (over the course of a year). He furthered that the credit should keep a couple of North Slope operations from qualifying. The target was facilities that produced the products relied on by communities.

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Co-Chair Stoltze noted that the legislature was faced with many requests for money. He referred a \$20 million request from the Alaska Railroad Corporation for the current year and millions more in the coming years. He made additional remarks about the railroad. He spoke to the benefits the railroad provided to the tourism industry. He believed the cost under replacement Amendment 1 seemed modest comparatively. He discussed that the costs would buttress opportunities for the military. He acknowledged that the amendment represented an economic assist for businesses that were healthy in many aspects of their broader portfolio. He asked DNR to address how businesses behave and some of the underpinnings of the economy. He remarked that no business would request \$80 million in order to earn \$2 million in a year. He continued that it was not a business decision that would be made absent overall concern for all of the other economic activity.

Commissioner Balash communicated that DNR had historically gone through a fairly extensive best interest finding

process to support the sales. In the examination of economic benefits to communities (particularly in the Interior) the department was able to identify contributions that the refineries made. He elaborated that the refineries supported dozens to hundreds of high paying jobs to families that participated in the state's communities. The department had considered the potential effect of a Petro Star closure and had examined what the facilities produced and who the products were sold to. He detailed that Petro Star was the provider of jet fuel for the state's air force bases and to the Kodiak coast guard station; the product was manufactured in Alaska and was distributed via truck, barge, and rail. He addressed potential consequences of a Petro Star facility closure. A closure would result in increased cost pressure for the military and a knock-on effect for the continued operation of facilities in the Interior and Southcentral. He believed the closure would eliminate the state's chances to base the F-35. The department believed the opportunity to base the military plane in Alaska was important to the state and nation. He spoke to the upside down pricing position of ANS Crude versus West Texas International (WTI); currently the jet fuel coming in through the Port of Anchorage from external refineries was competing against Alaska produced jet fuel rather effectively; external sources were getting an increasingly larger share of the jet fuel market at the Ted Stevens International Airport in Anchorage.

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Commissioner Balash relayed that imported fuel would become the "price maker" if the state did not act and the refineries shut down due to the cost of crude oil. He surmised that the shift would likely cause the cost of jet fuel to increase.

Co-Chair Stoltze discussed a similar situation caused by the closure of the Agrium closure. He relayed fertilizer had increased from \$200 per ton to \$1,200 per ton.

Commissioner Balash shared that the international jet traffic in Anchorage drove a significant amount of economic activity, which benefitted Alaska statewide. He discussed that the air cargo fleet was generally made up of former passenger planes. Over time, larger and more fuel efficient planes would enter the cargo fleet. The department feared that incremental costs added to the jet fuel price in

Anchorage would make the state more challenged from a competitive standpoint. He detailed that some signs had already occurred related to the state's standing compared to other international air cargo hubs. He believed the state would need to keep a close eye on the issue and to ensure that it drove as much competition to the jet fuel as possible to keep prices at a reasonable level; the goal was to prevent companies such as FedEx and UPS from relocating. Ultimately the economic consequences would impact Alaskan residents. He discussed that the refining industry received significant blame and anger directed its way for the high cost of gasoline and home heating fuel; however, the cost was the price realized in the market for fuel that was produced locally. The concern related to refinery closure was that all of the fuel products used in-state would be priced on imported products. He surmised that potentially the Tesoro refinery at Nikiski could be maintained, but it would put the state at one refinery instead of three. Additionally, competition would be reduced. He believed that prices would increase for gasoline, diesel, home heating fuel, and marine diesel.

Co-Chair Stoltze remarked that asphalt was also included. He asked Commissioner Balash to discuss where the product was produced.

Commissioner Balash replied that Flint Hills had been the state's largest asphalt producer. He believed Tesoro would be able to help, but there would be an impact. The department was concerned about the economic consequences and the reduction in the overall quality of life in rural areas including North Pole, Valdez, and Nikiski, should the refineries close. He detailed that the closures would put pressure on local budgets and social service agencies. He added that stress in the home led to domestic violence and substance abuse. He remarked that well-paying jobs worked to remedy the problems. He pointed to the sticker-shock of the amendment, but the department believed something had to be done or the state would suffer real consequences. He surmised that Petro Star wanted to remain in business, but the company was owned by parent company Arctic Slope Regional Corporation (ASRC) that was not in the business of charity.

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Commissioner Balash discussed that ASRC had a responsibility to earn a return for its shareholders. He believed if Petro Star closed its refineries the situation would be similar to that of Flint Hills. He elaborated that Flint Hills was happy to sell its North Pole facility and infrastructure, but he was not aware of any credible buyers. He stated that the underlying business was challenged; the cost of crude was a real problem at present. Economic theory suggested that the problem was an anomaly that would normalize; WTI and ANS would converge back to historic norms. He stated that the problem had persisted for the past three years. He remarked that the first casualty had occurred and the goal was to prevent two more from occurring.

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Co-Chair Stoltze noted that the amendment was sponsored by the administration but was carried by members of the Interior delegation on the committee.

Representative Wilson addressed whether Alaska wanted instate refineries. She remarked that if the answer was no the state would be dependent on price. She did not believe it was the answer. She provided an example about competition between large and small stores; small stores closed because they did not have the ability to compete on the same level. She provided the capital-move as an example; it would devastate the Juneau economy. She compared the issue to the loss of Flint Hills for Fairbanks and the North Pole. She stressed that the state royalty oil contract was \$2.15 over the North Slope price. She detailed that the state had done very well buying oil from Flint Hills. She believed Tesoro provided a backup as it received oil from other places at a more affordable price. She discussed that currently the state refineries provided fuel to Eielson Air Force Base, Fort Wainwright, and Joint Base Elmendorf-Richardson (JBER). She discussed that heating oil had been affordable in the past; she could not imagine how much the cost would increase if oil had to be trucked to Fairbanks.

Representative Wilson continued to discuss the amendment. She spoke to the \$50 million investment requirement to receive a second \$10 million. She believed it would take efficiencies for the refineries to be competitive. She opined that Petro Star would have to do upgrades in order

to produce some of the product that Flint Hills had produced. She had not heard of anyone considering the purchase of the Flint Hills Refinery. She had asked Flint Hills whether the amendment would incentivize it to reopen the refinery; the answer had been no. She pointed to credits provided to tourism, fish, and the film industry. She emphasized that the state would be uneconomical in many areas until energy issues were solved for the Interior and rural Alaska. She asked whether five years made a difference. She pointed to a difference of \$6 between Lower 48 cost and North Slope costs. She referred to the Quality Bank and noted that 50 percent of federal taxes came back to the state. She acknowledged that the amendment would give significant money, but the industries were putting money in. She understood the amendment was a big ask.

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Representative Wilson stressed that losing the industry would have a significant impact. She believed that a loss of refineries meant that additional funds to the railroad would only act as a band aid. She stated that the future impact of refinery closures on the railroad was not yet known. She stressed that the refineries touched many industries. She thanked the committee for its consideration.

Representative Guttenberg asked about the nature of the state's refineries. He referred to the Quality Bank calculation and wondered if the state was getting the value out of the royalties or ANS; if not, he wondered if the administration had considered participating in action in front of FERC. He wondered about a lack of efficiency of scale. He opined that in some scenarios it would be part of the norm to keep refining in the state. He pointed to large refineries out of state that had cheaper product. He wondered whether the instate refineries were too small to do the job the state needed.

Commissioner Balash replied that the state had intervened in the Quality Bank dispute at FERC. The state's overarching goal and position in the proceedings was to ensure a fair system. The state had a financial interest in the royalty produced that was of higher quality (Alpine was the best quality crude produced on the North Slope); therefore, the state did not want to take a side in the proceeding that would harm the state's other interests. He

relayed that refineries operating on the TAPS corridor were not the most sophisticated refineries in existence; some refineries in the Lower 48 were able to recover products and value from an entire barrel of crude. One of the beauties of TAPS and the Quality Bank was that it did allow the refineries along the pipeline to take crude off, recover high-end product, and put the remainder back in TAPS. He was uncertain that a tremendous difference in the refinery operation would occur if they moved to a full barrel cracking system. He opined that it could be difficult. He believed Tesoro did a much more complete job of recovering the full barrel at its Nikiski Refinery; however, he did not know if the entire barrel was recovered. The administration was hoping the investment incentive would increase opportunities to improve the plants for more complete barrel recovery. He communicated that a \$50 million investment would require a company to make the \$50 million back in order to recover costs. He stated that at best Petro Star was breaking even, but could be in the red. He wondered how the company was going to recover its capital under current circumstances. The company would have to consider whether the investment improved its profitability enough to make it worthwhile.

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Commissioner Balash continued that the 40 percent investment incentive reduced the cost of making the investment.

Representative Guttenberg wondered how the return on investment was measured. He asked if success was based on the refineries remaining open. Commissioner Balash answered in the affirmative related to the short-term. He elaborated that in the long-term the state would like to see the locally produced jet fuel to earn back more of the product market share.

Representative Thompson thanked the commissioner for his presentation. He noted that the impact of losing a refinery would be felt statewide. He stated that the possibility of losing Eielson Air Force Base and jet fuel produced for JBER were huge for the state. He informed the committee that Petro Star also provided heating oil to Kodiak and propane to Valdez and Kodiak. The fishing fleet depended on local refineries for supply. He communicated that the Kodiak coast guard base was supplied from Petro Star Valdez

for diesel and aviation fuel. He underscored that the issue was not limited to the Interior; it impacted the entire state. He stressed that the cost to the state in increased prices and lost business could not be estimated. He emphasized the importance of the issue. He believed the credits would allow the refineries to streamline their businesses. He noted that Petro Star was currently in negotiations with the railroad to determine what it could do to access rail. He surmised that the amendment could potentially help the railroad as well. He conceded that it was a large chunk of money upfront. He referred to Commissioner Balash's testimony that the state would make extra money from the instate sale of royalty oil compared to shipping it out; figures included a minimum of \$20 million from the Quality Bank and approximately \$160 million in three years. He reiterated his support for the amendment.

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Representative Gara testified against the amendment. He agreed that the state needed to do what it could to keep the Petro Star refineries open. He stated that the company had not disclosed its losses from the current year. He remarked that Petro Star had been profitable the prior two years and before. He stated that the amendment would give the company \$10 million per year for five years whether or not it made a profit or paid taxes. He continued that the company would receive an additional \$10 million if it invested \$25 million in the purchase of transportation or manufacturing equipment. He detailed that Petro Star would receive \$200 million from the state in five years (half of the money for certain and the other half as long as it made \$25 million of investments). He believed it was a significant amount of money to give a company without asking the company what it needed and without knowing what the company's financial situation was. He opined that there had to be a better way for the state to help the business. He asserted that the amendment's worst problem was that Tesoro did not want the \$100 million it would receive in the five years. He noted that the company had testified previously that all it wanted was the renewal of its RIK contract. He noted that the state had been struggling with money. He wondered why giving the money away was a responsible decision.

Commissioner Balash replied that the opportunity to provide an incentive for instate refining was something the state needed to weigh carefully; it wanted to ensure that it did not pick winners and losers. He detailed that because the state had so few refineries operating, it presented a challenge. The administration had considered a Quality Bank credit. He relayed that the credit would have helped Flint Hills and Petro Star, but it would not help Tesoro in any way. He took exception to the characterization that the state did not ask Petro Star about its need; the administration had looked at the company's need. He was not going to share the company's tax information in public. Petro Star had asked for a volume of oil at a price discounted to royalty in-value; the company was prepared to take the lower cost for the state's crude.

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Commissioner Balash communicated that it could have been feasible if the state was confident it could limit the discount to the Petro Star contract only; however, because of the likely constitutional problem the solution would have presented from an interstate commerce and equal protection perspective, the state was concerned the discount would have extended to all 80,000-plus barrels of the state's royalty production. He stressed that a \$5 difference on all of the state's royalty production would cost far more than costs presented in the amendment. He returned to the question of picking winners and losers, which the state would do if it selectively sold its oil to one company at a discounted price. The administration was happy to consider alternatives, but it felt action was necessary due to potential long-term repercussions.

Representative Gara discussed that the bill represented a \$300 million cost to the state over the upcoming five years. He stated that \$100 million of the total would go to a company that had not asked for the money. He surmised that there had to be a better way to approach the issue. He could live with a low-interest loan or a loan that provided Petro Star with a five-year grace period on paying the state back. He noted that the state would need the money more in five years' time than it did at present. He requested that the administration present a more fiscally responsible solution. He had never heard of legislation that would give \$20 million per year to a company that did not need the funds. He expressed ire at the proposed

solution. He agreed that the state should take some action to help Petro Star in its first year of loss. He stated that if the company's first year of loss was \$5 million and the bill provided \$20 million the company could give the money to its shareholders or to ASRC. He stated that the bill guaranteed the company \$15 million in profits per year for the next five years if it had an annual loss of \$5 million. He believed the amendment represented a sloppy response to an important problem. He asked the administration to consider a low-interest loan. He equated the amendment to a \$220 Base Student Allocation increase that had been denied to schools.

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Co-Chair Austerman spoke against the amendment. He was upset by the lateness of the amendment that he felt was hijacking Tesoro's royalty. He agreed with Representative Gara that there was a better way to deal with the problem. He stated that the administration had spent significant time on items such as the shipyard in Ketchikan; through the Alaska Industrial Development and Export Authority (AIDEA) the shipyard had survived and had become a viable business. He continued that the state was investing money through AIDEA to expand the shipyard. He stressed that the funds were not just a giveaway. He knew for at least the past three years the administration had been working to help the refineries. He stressed that it was wrong for the administration to attach the amendment to a bill at the last minute. He opined that the strategy should have been introduced at the beginning of session or in the prior year. He underscored that the administration should have developed a business plan for the refineries to work with AIDEA on their long-term viability. He felt that it was unfair to put the issue before the legislature at the end of session. He would gladly work on a bill with AIDEA to help the refinery. He stated that ASRC had made an investment, but he had not heard them agree to put any money forward. He was uncomfortable being put in the position. He knew that Petro Star was a great company and that ASRC was a great corporation. He did not believe the administration's request was responsible.

Co-Chair Austerman referred to the seafood industry that had plummeted in 2001 when Chilean and farmed fish had driven the pink salmon price down to under \$0.05 per pound in some locations. Federal dollars had bailed the industry

out; it had made a big difference, but the funds had been matching grant programs. The \$50 million provided had not been a giveaway. He noted that some fishermen in affected areas did receive some money in the form of a grant. He did not believe the state could just give the money away to refineries without something. He reiterated his opposition to the amendment. He hoped the committee would not hold Tesoro's royalty hostage because of the issue. He would be happy to look at a bill if the administration proposed one that included a loan program through AIDEA that would help refineries become solvent in the long-term.

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Representative Munoz referred to the commissioner's testimony that one of the reasons instate refineries were struggling was because the price of ANS crude had not normalized. She asked for further detail.

Commissioner Balash answered that the department had a graph showing the difference between ANS West Coast and WTI on a cost per barrel basis. He detailed that in 2004 through 2007, ANS had been \$2 less than WTI. The prices had converged and had been nearly identical from 2007 to 2009. A price divergence began in 2010 and in 2011 ANS priced out at \$15 more per barrel than WTI. He detailed that conversations about the cost of refining began with the cost of the raw crude barrel of oil. The gap had narrowed and was closer to a \$10 difference at present. The department expected that in time the price would converge closer to historic trends; up until 2007, ANS had priced less than WTI. He did not want to make a prediction on whether it would occur again. He concluded that because oil was a fungible product traded globally it was expected that the differential would close at some point.

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Representative Munoz referred to prior industry testimony that Quality Bank payments had a profound effect on the business in a negative sense. She asked how much of the funds went to the state and how the payment had changed over the past several years.

Commissioner Balash answered that numbers from 2013 provided a good baseline for the prior couple of years. He detailed that in 2013 payments into the Quality Bank from

TAPS refineries were approximately \$112 million. Approximately \$20 million of the total had been returned to the state through increased royalty value. He noted that it was also necessary to look at the production tax equation. The state was not able to go through tax payer by taxpayer to determine the total impact, but because the production tax system was profits-based (it taxed on the margin at 35 percent) it could be determined that after taking the royalty aspect away, the amount was close to \$30 million. Combining the two figures totaled approximately \$50 million returned to the treasury from refineries.

Representative Munoz wondered how the funds were used by the state. Commissioner Balash replied that the payments into the Quality Bank were repairing or "making whole" other parties. He discussed that there were many varieties of crude produced on the North Slope; each oil field had its own API [American Petroleum Institute] gravity and quality (not all barrels were the same). Originally the Quality Bank had been a way to equalize the parties; each barrel put into TAPS may be different at the start, but once in the pipeline they were one blend of crude. He explained that the parties providing higher quality crude had contributed value to other parties with lower quality crude. There were facilities in North Pole and in Valdez that took crude off of TAPS and took the high quality oil for jet fuel, diesel, and gasoline and returned the remainder to the TAPS stream; therefore, the refineries made a payment to the other oil producers to keep the entities whole.

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Representative Wilson understood the concept of not wanting to pick winners and losers, but she did not understand it under the given context. She clarified that by instate refineries she had been referring to refineries in the middle of the state (i.e. North Pole). She explained that there were circumstances occurring in the North Pole refineries that were not happening in the other areas. She stated that Petro Star was under different stresses due to costs it had shared with Flint Hills. She detailed that the pipe running between the rail yard and Flint Hills represented \$3 million to \$4 million in additional cost for Petro Star. She emphasized that the system was not equal. She discussed a storage tax credit bill that had passed a

few years earlier; Anchorage had built a large storage tank with the credits.

Co-Chair Stoltze noted that the storage tank had been built south of Anchorage.

Representative Wilson agreed with the correction. She furthered that the storage tank allowed importing of cheaper fuels. She wondered why the Quality Bank could not be used for the refinery that needed it. She wondered if the reason was legal or moral. She wanted to help Petro Star for the next several years to allow time for the company to upgrade items that resulted from the loss of its partner or to allow time for another party to purchase the Flint Hills Refinery.

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Commissioner Balash answered that the hydrocarbon business, specifically the gasoline, diesel, and jet fuel markets were unregulated markets; the markets were trusted to produce a price that allowed a product to be continually supplied. Therefore, the administration had been careful to not upset the market balance or to provide a clear benefit to one party, which was the reason the administration had not focused solely on the Quality Bank. He did not characterize the issue as a question of mortality.

Representative Wilson pointed to the tax credit that had been provided to the storage facility south of Anchorage. She stressed that the state had already "unbalanced" the system by providing a credit to the facility. She surmised that the imbalance had caused part of the problem.

Commissioner Balash replied that the storage facility was for natural gas. He detailed that the gas was primarily utilized by public utilities, but there was an associated benefit that accrued to Tesoro because it relied on natural gas to operate its facility. He supposed there could be an argument that some of the other credits provided to support natural gas deliverability and long-term supply had been a benefit realized only by Tesoro.

Representative Wilson spoke to the legality of the issue. She stated that it had been established that life was not fair; Anchorage had natural gas, Juneau had the capital, and Fairbanks wanted its refinery. She wondered if there

was any legal reason why there could not be a credit for the Quality Bank. Commissioner Balash was not aware of a constitutional challenge that the item would present; however, he had not spoken with legal counsel.

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Representative Wilson communicated that she did not have plans to hold Tesoro's bill hostage. She was looking for a solution and wanted to address the issue further with the commissioner. She stated that it was not possible to keep everything equal. She did not believe her solution would disadvantage other refineries. Additionally, she did not believe there was any indirect competition. The refinery was using diesel; affordable gas may also make it more economical. She did think there were some legal reasons to help the refinery under the given circumstances. She spoke to avoiding spreading the benefit unequally to parties that may not need the help.

Representative Costello asked about the timing aspect. She wondered how long the administration had been considering the three options it had identified (two of which had been rejected).

Commissioner Balash replied that normally when the administration pursued legislation or made proposals to the legislature the process began in August. He detailed that the department advised the governor's office about certain topics it would like to see addressed by the legislature. He elaborated that a round of internal and external vetting occurred in the process. Under the current circumstance, the department had not had a specific proposal in mind in August; it had not believed there was a dire situation that warranted action. He relayed that there had been conversations about Quality Bank matters; the administration had been watching the spread between WTI and ANS and had believed it could wait the situation out. The department had believed the Quality Bank issue could have been resolved or settled at FERC. However, on February 4, 2014 when the news about Flint Hills had broken it had taken him by surprise. As the administration considered all of the components following the Flint Hills announcement he had thought about the revenue requirement for the lines running between TAPS and the North Pole Refinery facilities. He relayed that the revenue requirement for the lines was \$4.5 million in 2013. He stated that the revenue

requirement had been met by both refineries on an 85 percent to 15 percent ratio, the latter portion paid by Petro Star. He detailed that as a result Petro Star's payment would increase from less than \$1 million to \$4.5 million per year. He understood that 2012 was a thin margin for Petro Star and that 2013 would be a breakeven year at best. He stated that a Petro Star representative had confirmed his understanding of the cost consequences. Subsequently, he had asked Petro Star if it planned to close its refinery too. He relayed that the company could not answer in February. The company renewed its crude contracts in March; the severity of the situation prevented the company from knowing whether it would renew its contract for the following year.

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Commissioner Balash continued to answer the question. He discussed that Petro Star had asked what the state may be able to do in response to the situation. Ultimately the administration had asked Petro Star what it would take to keep the company in operation. The company had suggested that the state could sell it crude at a discounted price. He noted that the cost of crude and the Quality Bank were the two issues that were "killing" the company. He informed the committee that there was not much the administration could do about the Quality Bank; it could try to work out a settlement between parties, but if parties did not agree to a settlement, the issue would be left in the hands of FERC. He did not know how long the agreement would take. The administration had considered selling its royalty at a discount to Petro Star, but due to risks to the remainder of its royalty production from a royalty in-value perspective, the idea had been dismissed. The administration had begun looking at tax credits in the middle of March. Ultimately, the process had been compressed into approximately three weeks. He believed the legislature could improve the option presented to the committee.

Representative Edgmon understood that there were statewide impacts related to the refineries. He pushed for taking some action to address the problem. He observed that sometimes it took more than one try to get things right.

Co-Chair Stoltze had hoped to adopt the amendment during the meeting as a starting point. He remarked that it was

hard to edit a blank page. He had hoped to begin with a plan even if it was viewed to be flawed. He believed there were universal levels of discomfort even from the sponsors. He viewed the amendment like a committee substitute and reiterated that it was hard to work off of a blank page.

Representative Edgmon replied that the response did not answer his question. He stated that a plan b was needed, but he did not see it at the table. He strongly supported taking action that worked.

8:01:29 PM

Representative Gara stated that Petro Star had noted its profits had not been good in the past few years. He pointed to the high cost of ANS compared to WTI as one of the problems. He referred to the extra cost to Petro Star of approximately \$4 million due to the Flint Hills Refinery closure. He referred to the hope that crude oil prices would normalize. He hoped the administration could consider some type of financing provision for distressed companies. He noted that the amendment included language requiring the commissioner to make a best interest finding. He believed language could be devised requiring the commissioner to make a finding to justify the low interest loan for companies in need. He referred to prior testimony that Petro Star needed a few years to find ways to increase efficiency in its operations. He asked the administration to consider a loan for companies that met a certain standard. He did not object to the idea of a repayment holiday to allow the company time to get a financial breather.

Representative Holmes pointed to the sticker shock of the amendment. She referred to multiple conversations she had had about the amendment. She associated herself with comments made by Representative Edgmon. She did believe something needed to be done, but she was not comfortable with the amendment.

8:05:14 PM

Co-Chair Austerman believed that AIDEA was the appropriate way address the problem. He stated that the agency had the ability through simple legislation to bond and take care of industries. He did not believe it would take long to sit

down with the agency to develop a plan; it had been done before.

Co-Chair Stoltze remarked that the suggestion was good.

Commissioner Balash was happy to discuss the issue with AIDEA. The administration had discussed with AIDEA the possibility of refinancing the pipelines between TAPS and the North Pole refineries, but it had found that financing anything without some surety that the business was solvent had raised red flags.

8:07:06 PM

Representative Wilson WITHDREW replacement Amendment 1. There being NO OBJECTION, it was so ordered.

Co-Chair Stoltze noted that the issue would be discussed the following day.

Commissioner Balash appreciated the latitude given on the issue. He was confident that the approval of the royalty contract was not controversial. He did not want to hurt the bill for Tesoro.

Representative Gara remarked that there was no reason to address Amendment 2. He looked forward to a continued discussion on the issue.

Co-Chair Stoltze assumed that Amendment 2 presupposed the adoption of replacement Amendment 1.

Representative Gara replied that he had presupposed Amendment 2 would have been given more sideboards.

Co-Chair Stoltze thanked the committee for its honest dialogue. He discussed schedule for the following day.

Representative Gara clarified that he personally should have provided more sideboards for Amendment 2.

HB 287 was HEARD and HELD in committee for further consideration.

ADJOURNMENT

8:11:20 PM

The meeting was adjourned at 8:11 p.m.