

**ALASKA STATE LEGISLATURE  
HOUSE RESOURCES STANDING COMMITTEE**

April 6, 2022

1:05 p.m.

**MEMBERS PRESENT**

Representative Josiah Patkotak, Chair  
Representative Grier Hopkins, Vice Chair  
Representative Zack Fields  
Representative Calvin Schrage  
Representative Sara Hannan  
Representative George Rauscher  
Representative Mike Cronk  
Representative Ronald Gillham  
Representative Tom McKay

**MEMBERS ABSENT**

All members present

**COMMITTEE CALENDAR**

HOUSE BILL NO. 409

"An Act approving and ratifying the sale of royalty oil by the State of Alaska to Petro Star Inc.; and providing for an effective date."

- MOVED HB 409 OUT OF COMMITTEE

HOUSE BILL NO. 410

"An Act approving and ratifying the sale of royalty oil by the State of Alaska to Marathon Petroleum Supply and Trading Company LLC; and providing for an effective date."

- MOVED HB 410 OUT OF COMMITTEE

PRESENTATION(S): AKLNG UPDATE BY ALASKA GASLINE DEVELOPMENT CORPORATION

- REMOVED FROM AGENDA

**PREVIOUS COMMITTEE ACTION**

BILL: HB 409

SHORT TITLE: APPROVE PETRO STAR INC. ROYALTY OIL SALE

SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

04/04/22 (H) READ THE FIRST TIME - REFERRALS  
04/04/22 (H) RES, FIN  
04/04/22 (H) DNR, O&G BEST INTEREST FINDING AND  
DETERMINATION REPORT  
04/04/22 (H) RES AT 1:00 PM BARNES 124  
04/04/22 (H) -- MEETING CANCELED --  
04/06/22 (H) RES AT 1:00 PM BARNES 124

BILL: HB 410

SHORT TITLE: APPROVE MARATHON PETRO ROYALTY OIL SALE  
SPONSOR(S): RULES BY REQUEST OF THE GOVERNOR

04/04/22 (H) READ THE FIRST TIME - REFERRALS  
04/04/22 (H) RES, FIN  
04/04/22 (H) DNR, O&G BEST INTEREST FINDING AND  
DETERMINATION REPORT  
04/04/22 (H) RES AT 1:00 PM BARNES 124  
04/04/22 (H) -- MEETING CANCELED --  
04/06/22 (H) RES AT 1:00 PM BARNES 124

**WITNESS REGISTER**

JHONNY MEZA, Commercial Manager  
Division of Oil and Gas  
Department of Natural Resources  
Anchorage, Alaska

**POSITION STATEMENT:** During the hearing on HB 409 and HB 410, provided a PowerPoint presentation, "The Process for the Sale of ANS Royalty Oil In-Kind and the Proposed Contracts with Marathon and Petro Star," dated 3/25/22.

JOHN CROWTHER, Deputy Commissioner  
Office of the Commissioner  
Department of Natural Resources  
Anchorage, Alaska

**POSITION STATEMENT:** During the hearing on HB 409 and HB 410, answered questions.

DOUG CHAPADOS, President, CEO  
Petro Star Inc.  
Arctic Slope Regional Corporation  
Anchorage, Alaska

**POSITION STATEMENT:** Testified in support of HB 409.

CASEY SULLIVAN, Government and Public Affairs Manager  
Marathon Petroleum Corporation

Anchorage, Alaska

**POSITION STATEMENT:** Testified in support of HB 410.

**ACTION NARRATIVE**

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**CHAIR JOSIAH PATKOTAK** called the House Resources Standing Committee meeting to order at 1:05 p.m. Representatives Hopkins, Hannan, Rauscher, Cronk, Gillham, McKay, and Patkotak were present at the call to order. Representatives Schrage and Fields arrived as the meeting was in progress.

**HB 409-APPROVE PETRO STAR INC. ROYALTY OIL SALE**  
**HB 410-APPROVE MARATHON PETRO ROYALTY OIL SALE**

[1:05:29 PM](#)

CHAIR PATKOTAK announced that the first order of business would be HOUSE BILL NO. 409, "An Act approving and ratifying the sale of royalty oil by the State of Alaska to Petro Star Inc.; and providing for an effective date." and HOUSE BILL NO. 410, "An Act approving and ratifying the sale of royalty oil by the State of Alaska to Marathon Petroleum Supply and Trading Company LLC; and providing for an effective date."

CHAIR PATKOTAK explained that HB 409 and HB 410 relate to approving the sale of royalty in-kind oil to Petro Star Inc. and Marathon Petroleum Corporation, respectively. He noted that both bills do the same thing with two different companies and that the bills provide approval of the contracts for the sale of Alaska's royalty oil. He pointed out that the bills cannot be amended because they are negotiated, and the bills are subject to the approval or denial of the legislature. He stated that renewal of the contract must happen by April 21, [2022], or the contract will not be renewed. He disclosed that he and his family are shareholders of Arctic Slope Regional Corporation (ASRC) which owns Petro Star Inc.

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JHONNY MEZA, Commercial Manager, Division of Oil and Gas, Department of Natural Resources (DNR), provided a PowerPoint presentation, "The Process for the Sale of ANS Royalty Oil In-Kind and the Proposed Contracts with Marathon and Petro Star," dated 3/25/22 [hard copy included in the committee packet]. He displayed slide 2, "AGENDA," and said he would be reviewing what

royalty in-kind is, the history of royalty in-kind sales, the statutory and regulatory mandate for royalty in-kind, the process that DNR has followed for this sale of royalty in-kind oil, and the contract terms for Marathon and Petro Star.

MR. MEZA turned to slide 4, "1. WHAT IS ROYALTY IN-KIND? STATUTORY REFERENCE." He explained that the DNR commissioner can elect to take the state's royalty oil and gas in-value (RIV) or in-kind (RIK). When selecting the royalty in-value, he said, the department receives a share of the proceeds from the sale of oil or gas by the producers, determined by the royalty rate. When the department selects its royalty in-kind, he advised, the department is in charge of marketing that royalty oil [or gas]. He drew attention to the [3/23/22] letter from DNR depicted on the slide that informs the Senate president and the House speaker that the state is electing to take its oil and gas royalty in-value.

MR. MEZA moved to slide 5, "1. WHAT IS ROYALTY IN-KIND? CONTRACTUAL REFERENCE." He said this is where the department and the producers agree on the royalty share on the production. He noted that the example on the left side depicts a contract for an oil and gas lease and the example on the right side depicts a contract for a unit agreement.

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REPRESENTATIVE RAUSCHER drew attention to the statute depicted on slide 4, Sec. 38.05.182, which states that the royalty "may be taken in-kind rather than in money if the commissioner determines that the taking in-kind would be in the best interest of the state." He asked whether it must also be in the best interest of [the operator with which the commissioner is making the agreement].

MR. MEZA replied that in this determination for RIK it must be based on the best interest of the State of Alaska, including the citizens of the state of Alaska.

REPRESENTATIVE RAUSCHER asked whether both sides must agree on the agreement.

[1:11:33 PM](#)

JOHN CROWTHER, Deputy Commissioner, Office of the Commissioner, Department of Natural Resources (DNR), responded that DNR leaves it to the counterparty, the private company to enter this

negotiation and to conclude it, to determine if it's appropriate for their economic interest. The private company can choose not to receive RIK oil from the state if it determines that that's in its economic interest.

[1:12:16 PM](#)

MR. MEZA resumed his presentation. He displayed slide 6, "1. WHAT IS ROYALTY IN-KIND? STATE OWNERSHIP IN THE NORTH SLOPE (AS OF JANUARY 2022)." He said the map highlights the fields from which the state has ownership as the royalty owner, such as the Kuparuk River Unit and Prudhoe Bay units. He noted that the Bear Tooth and Greater Moose's Tooth units are federal land. He explained that royalty oil in-kind in the context of the proposed contracts before the committee, refers to the fields where the state has ownership.

MR. MEZA proceeded to page 8, "2. HISTORY OF ROYALTY IN-KIND ALASKA NORTH SLOPE OIL." He said the graph shows the total royalty from the North Slope that the state has received from November 1979 [to July 2021], with the grey line depicting the portion that has been selected by the DNR commissioner throughout this period to be taken in-kind. He related that the state has historically selected royalty oil both in-kind and in-value and that about 97 percent of royalty oil in-kind has been from the North Slope. He explained that the amount of RIK oil that the state can select depends on the level of production, the royalty rates the state has on its leases, and the demand from refineries.

MR. MEZA reviewed slide 9, "2. HISTORY OF ROYALTY IN-KIND TYPES OF CONTRACTS AND BUYERS." He noted there are both competitive and non-competitive, negotiated, sales. He said that 5 percent, 46 million barrels, is the royalty oil in-kind that the state has sold via competitive sales. Most of the oil that has been sold via this royalty in-kind program has been dedicated to in-state buyers.

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MR. MEZA next discussed slide 11, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND LEGISLATIVE APPROVAL." He drew attention to the statutory language depicted for Sec. 38.06.055, which requires the DNR commissioner to get legislative approval before executing the RIK contracts. He noted that per statute the sale of royalty by the DNR commissioner requires the [written] recommendation of the Alaska Royalty Oil and Gas

Development and Advisory Board. However, he continued, an exception to this requirement is if the sale of royalty is to relieve storage or market conditions, which can only be used for up to one year.

CHAIR PATKOTAK asked whether the legislature has ever denied a royalty in-kind negotiated contract that the administration has put forward.

MR. MEZA answered that he does not know of any denials by the legislature.

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MR. MEZA resumed his presentation. He displayed slide 12, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND RECENT HISTORY OF APPROVAL." He explained that the table lists the recent RIK oil contracts, beginning with Tesoro in 2016 [for five years] and Petro Star in 2016 [for one year and for four years]; with Marathon and Petro Star in 2021 [for one year], and the currently proposed contracts with Marathon and Petro Star in 2022 for three years and five years, respectively. He noted that for multi-year contracts the department has obtained the support and recommendation of the Royalty Board as well as the approval by the legislature. He further noted that in the cases where the contracts were for one year, these contracts were entered to relieve market conditions, so the department didn't need the review of the Royalty Board nor the approval of the legislature.

[1:19:00 PM](#)

REPRESENTATIVE HANNAN requested further detail on the one-year contracts, which appear to have similar conditions to what the legislature is currently being asked to approve for multiple years.

MR. MEZA responded that the statute includes an exception to the requirement for review by the Royalty Board or approval by the legislature when DNR enters a contract to relieve storage or market conditions. He said DNR entered these one-year contracts to relieve storage or market conditions because at that time the Royalty Board wasn't fully staffed and continuing the supply of royalty oil to the in-state refineries was needed to meet the demand by the citizens of the state.

REPRESENTATIVE HANNAN drew attention to the Marathon contract in 2021 which was 10,000-15,000 barrels per day. She noted that that is the same size as the contract the legislature is being asked to approve, but now it is over a period of three years rather than one year.

MR. MEZA confirmed that is correct.

MR. CROWTHER noted that that is a daily volume, so it occurs throughout the term, not over the full three-year term.

REPRESENTATIVE FIELDS asked whether the state gets a better deal for multi-year contracts or for the shorter-term contracts.

MR. MEZA answered that the additional value that the state obtains varies regardless of whether it is one year or multi-year. He said that overall, on average, the state obtains incremental revenue and besides the additional revenue which is a benefit to the state there is the benefit of supplying crude oil to in-state refineries and how that translates into refined products for the citizens of Alaska.

[1:22:31 PM](#)

MR. MEZA resumed his presentation. He discussed slides 13 and 14, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND ROYALTY BOARD REVIEW." On slide 13, he drew attention to the criteria the Royalty Board must consider under the statutory language of Sec. 38.06.070. On slide 14, he drew attention to the board review and recommendation required under the statutory language of Sec. 38.06.050. He noted that the right side of the slide depicts the documents that the Royalty Board has provided to the legislature effectuating the board's recommendation of the proposed contracts currently before the committee for Marathon and Petro Star. Through the review process, he continued, DNR must obtain unanimous vote for recommendation from the Royalty Board for each of these two contracts.

MR. MEZA moved to slide 15, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND COMPETITIVE VS. NON-COMPETITIVE SALE." He brought attention to the statute, Sec. 38.05.183, for the sale of royalty. He said the statute requires the sale be by competitive bid except when the DNR commissioner determines that conducting a non-competitive sale is in the best interest of the state. For that purpose, he explained, DNR issues a solicitation of interest gauging the responses from the market participants, and in the case of proposed contracts that are

non-competitive, this decision is in the best interest of the state. He noted that about 95 percent of the department's sales have been made in a non-competitive basis.

MR. MEZA reviewed slide 16, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND SALE WITHIN THE STATE OR FOR EXPORT?" He stated that the map depicts where the refineries are located within Alaska, and the map is intended to reflect that most of the sales of royalty oil in-kind have been dedicated for in-state refineries. He drew attention to the regulatory language under AS 38.05.183(d), which states: "Oil or gas taken in kind by the state as its royalty share or gas delivered to the state under AS 43.55.014(b) may not be sold or otherwise disposed of for export from the state until the commissioner determines that the oil or gas is surplus to the present and projected intrastate domestic and industrial needs."

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MR. MEZA proceeded to slide 17, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND INFORMATION ON IN-STATE REFINERIES." He related that in the proposed contracts DNR has asked for and received information from Marathon, which operates the Nikiski refinery, and Petro Star, which operates the North Pole and Valdez refineries. He reported that the production for the Nikiski refinery is around 55,000 barrels per day of refined product, which includes [30 percent jet fuel to Anchorage, 27 percent gasoline, and 43 percent a mix of liquid petroleum gas, distillate, vacuum gas oil, fuel oil, and seasonal asphalt.] He further reported that the North Pole and Valdez refineries have maximum capacities of 22,000 and 60,000 barrels per day, respectively, and the mix is [65 percent] jet fuel and [35 percent] ultra-low sulfur diesel, asphalt, and heating oil, with no gasoline produced by these two refineries. For all three refineries, he related, the majority of refined product is dedicated for consumption within Alaska, only a minor component is dedicated to outside of Alaska. Regarding where the refiners obtain their crude oil, he said the Nikiski refinery obtains about [60 percent] from the North Slope, [20 percent] from Cook Inlet, and [20] percent from other sources in the U.S. or foreign sources. For the two Petro Star refineries, he conveyed that 100 percent comes from the North Slope. He drew attention to the bottom of the table depicting the numbers of employees.

REPRESENTATIVE FIELDS asked where the 20 percent of non-Alaska crude oil comes from that is obtained by the Nikiski refinery.

MR. MEZA replied that DNR doesn't know that information. He suggested obtaining it directly from the company.

MR. CROWTHER related that Marathon has said in other legislative testimony that in recent years it has been closer to 90 percent within-Alaska sources. He offered his understanding that the majority has been from other U.S. sources, but that the company certainly also has international sources. He said the company keeps that information proprietary for commercial reasons.

[1:28:06 PM](#)

MR. MEZA resumed his presentation. He continued to slide 18, "3. STATUTORY AND REGULATORY MANDATE FOR ROYALTY IN-KIND PRICING REQUIREMENT FOR RIK." He said the graph depicts a critical piece of information for these contracts. He explained that the zero line on the graph represents the point at which the price of royalty oil in-kind equals the price of royalty oil in-value. He said the blue circles represent that the price the department received by selling royalty oil in-kind was greater than the proceeds that DNR received from the producers when choosing this royalty in-value. The red squares, he continued, show the few instances where the department obtained a lower price for its royalty oil in-kind than the royalty in-value. He pointed out that overall, on average, from January 2008 to December 2021, the state obtained 93 cents for each barrel of royalty oil in-kind in addition to what it would have received had the state elected all its royalty in-value. In other words, Mr. Meza advised, the state generated an additional \$137 million in revenue by entering these royalty oil in-kind contracts, and total proceeds from these RIK sales amount to almost \$11 billion. He stated that this complies with the regulatory language of 11 AAC 03.026(b) which requires that the price of royalty oil in-kind should be at least equal to the price of royalty oil in-value.

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MR. MEZA moved to the fourth section of his presentation. He drew attention to slides 20 and 21, "4. THE PROCESS THAT DNR FOLLOWED FOR THIS SALE OF RIK OIL." He displayed slide 20 and stated that for the Marathon and Petro Star contracts, DNR has followed the language from the statutes and regulations that determine how the process for the sale of royalty oil in-kind should be conducted. In this process, he said, DNR involved the Royalty Board in the decisions making the determinations by the commissioner required by the statute, but also the review by the

Royalty Board and the ability for the department to provide comments. He related that slide 21 shows that DNR evaluated the expiration date of these RIK processes and considered whether the sale of RIK should be done on a competitive or noncompetitive basis, and for sale within the state or for export, and whether it should be long-term or short-term contracts. He said the department published a Solicitation of Interest gauging the information from the market and evaluated those responses and decided to conduct a noncompetitive sale. The department informed the Royalty Board of this position, he continued, and conducted negotiations with the parties that show interest, which were Marathon and Petro Star. He said the department published a preliminary best interest finding showing why these proposed contracts are in the best interest of the state and DNR provided a 30-day public comment period. He advised that DNR received no comments from the public but there was an extensive review by the Royalty Board on these proposed contracts and DNR obtained unanimous approval. After that, he said, the department published a final best interest finding which was provided to the legislature, which is where the process currently is.

[1:32:08 PM](#)

REPRESENTATIVE FIELDS asked whether it is accurate to assume that if DNR was doing a competitive sale, realistically the only competing entities would be in-state refineries and not out of state refineries.

MR. MEZA replied that in the publication of this solicitation of interest, DNR obtained three responses from entities. Out of those three responses, he continued, only two showed interest in buying royalty oil in-kind. He said DNR therefore evaluated how much benefit the department would obtain by doing an auction with only two participants versus negotiating separately with each one.

REPRESENTATIVE FIELDS observed from the history of the program that the department has more frequently concluded that the noncompetitive route gets a better deal for the state. He asked whether that is primarily a result of the small number of bidders, so a competitive environment really isn't that competitive or whether other there are other factors that make the noncompetitive sale approach more beneficial for the state.

MR. MEZA responded that besides the number of responses it is also because of the requirement in regulations and statute that

the department make a written finding that in-state demand is met and before there can be royalty oil for export, the department needs to secure a price that is at least as much as royalty in-value.

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The committee took a brief at-ease.

[1:34:41 PM](#)

MR. MEZA resumed his presentation and reviewed the fifth section of his presentation provided on slides 22-28. He displayed slide 23, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR OVERVIEW OF RECENT AND PROPOSED RIK CONTRACT TERMS." He drew attention to the column labeled "Netback pricing" and stated that these contracts have the same valuation methodology, so there was no change with respect to the current proposed contract versus the ones that were entered about six years ago. He explained that a netback methodology is followed which uses the pricing of U.S. royalty oil in the U.S. West Coast and considers all the components that are necessary to determine the price of royalty oil at the field because that is the point where DNR, the state, transferred title of its royalty oil to the buyer. He advised that the state is not in charge of transporting or taking any risk when transferring that royalty oil. He said the column, "RIK differential," shows a key negotiating term of these contracts, which is the dollar deduction that determines the value of royalty oil. He noted that the value has increased from \$1.95 per barrel to \$2.25 per barrel for Petro Star and \$2.23 per barrel for Marathon.

CHAIR PATKOTAK asked whether the refined product from the oil that was taken in-kind is wholly used in the in-state market for sale or used by any state agencies.

MR. MEZA answered that the department provides royalty oil to the buyer, the refiner, and the refiner is the one extracting refined product from that crude oil, [the state] does not enter the market of refined products.

[1:37:25 PM](#)

REPRESENTATIVE RAUSCHER inquired whether there is a time specific date.

MR. MEZA returned to slide 21 and pointed out that the 1-year RIK contract with Marathon ends on 7/31/22. He said a provision with which DNR must comply is to provide three-month notice to the North Slope producers before electing this royalty oil in-kind. This three-month notice, he explained, means DNR must have the following contract with Marathon executed by 4/22/22. Should DNR take one week or one month longer than that, he continued, then it means the refinery will have one week or one month to be done with the royalty oil. While the refiner still has provisions from North Slope producers, he added, the royalty oil is also important.

REPRESENTATIVE RAUSCHER inquired whether the market volatility of the last month has given DNR pause on this or whether DNR remains comfortable.

MR. MEZA replied that DNR believes these contracts have been structured to account for that volatility, which has also occurred in the past. He related that there was substantial volatility during the 14-year period in which the state obtained a premium of \$0.93 per barrel, and so DNR is not that concerned about volatility.

[1:39:48 PM](#)

REPRESENTATIVE HANNAN requested elaboration on Chair Patkotak's opening reference to the date of 4/21/22.

CHAIR PATKOTAK offered his original understanding that it was 4/20/22.

REPRESENTATIVE HANNAN asked whether that is for a floor vote.

CHAIR PATKOTAK explained that both bills are moving through both bodies. He deferred to Mr. Crowther to provide further detail.

MR. CROWTHER answered that DNR must execute the contract by 4/22/22, and to execute the contract DNR must have an enacting bill from the legislature prior to that date. So, he stated, if both bodies of the legislature pass the bills and the governor signs the bills by 4/22/22, DNR can keep the contract and have an uninterrupted supply.

CHAIR PATKOTAK noted that consideration must be given to the time it takes for transmittal to occur after a vote.

MR. CROWTHER confirmed that is correct.

1:40:57 PM

REPRESENTATIVE HANNAN, regarding if that didn't happen, asked whether there would be an interruption in the contract or whether the bill would expire if not completed by 4/22/22.

COMMISSIONER CROWTHER responded that the bill does not expire on that date, there would just be an interruption in the contract and supply, and it would be up to the refinery, in this case Marathon, to either limit runs or to seek an alternative source of supply subject to that uncertainty.

REPRESENTATIVE HANNAN noted that she wanted it on the record as to whether it would be a delay rather than a disappearance.

1:42:09 PM

REPRESENTATIVE MCKAY observed on slide 21 that the contracts with Marathon and Petro Star go until 7/31/22 and 12/31/22, respectively. He offered his understanding that if [the bill was not signed by the governor by 4/22/22], then it would go back to the previous contract.

MR. CROWTHER answered that the shortfall or interruption would not occur in April; it would potentially occur at the end of that contract because DNR must do the 90-day notification. So, he continued, DNR would technically be tardy in not nominating those barrels to receive them with the upstream producers, and so in theory DNR wouldn't be eligible to receive them until "that Q3 2022 period, later in that period."

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REPRESENTATIVE RAUSCHER thanked Representative Hannan for her clarification because he was looking for the legislature's timetable, not the department's.

CHAIR PATKOTAK asked whether the panel had further questions.

1:43:55 PM

MR. MEZA resumed his presentation. He displayed slide 24, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR RIK DIFFERENTIAL IS THE SOURCE OF THE PREMIUM OF RIK OVER RIV." He explained that this slide provides a comparison of how the value of royalty oil is determined when the state selects its royalty in-value versus

royalty in-kind. He drew attention to the chart on the left depicting what happens when the state selects its royalty in-value. For this, he said, DNR allows some deductions related to the transportation of oil to the U.S. West Coast. He then drew attention to the chart on the right depicting royalty in-kind, which is not physically transported to the U.S. West Coast, but rather sold to an in-state refinery in Alaska. He brought attention to Step 2 highlighted in yellow on both charts for the oil in-value marine transportation allowance and the oil in-kind differential and noted that that comparison is what generates the premium to which he referred earlier.

MR. MEZA proceeded to slide 25, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR RIK DIFFERENTIAL IS THE SOURCE OF THE PREMIUM OF RIK OVER RIV." He said the blue line at the top of the graph represents the marine transportation allowance and the grey line represents the RIK differential. The vertical distance between those two lines, he continued, indicates the source of the incremental revenue that the state obtains by selling its royalty oil in-kind.

[1:45:22 PM](#)

MR. MEZA turned to slide 26, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR FLEXIBILITY FOR BUYER AND SELLER." He explained that there is some flexibility or benefits given to the royalty in-kind buyers, the refinery, as well as benefits and flexibility for the state. He advised that the buyer has the flexibility of nominating zero barrels or reducing their nominations subject to the approval of the commissioner. As the seller, he further advised, DNR has the flexibility of not guaranteeing any quantity, quality, or source of royalty oil because DNR is not a North Slope producer, it is a royalty owner and therefore protected from that type of risk. If the state were to have excess royalty to dispose of and the buyers were to have more demand for that, the contract would allow for additional sales of that royalty oil.

MR. MEZA moved to slide 27, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR OTHER PROVISIONS." He said DNR, or the state, being a seller and the refiners being a buyer could involve a risk of nonperformance or default of payment. To cover that risk, he explained, the department and buyers have agreed that the guarantor of these buyers, or refiners, provide either a letter of credit, surety bond, or opinion letter to DNR to protect from that default risk. The value of that financial assurance varies by refinery; it could be equal to 90 days' worth of royalty oil

for Marathon or 50 days' worth of royalty oil for Petro Star. There is a retroactivity clause in the contract in case there are revisions in the future after an invoice is paid by the buyer, allowing the buyer or the state to reflect more accurate information in that calculation. Last, there are two provisions that encourage the buyer, or refinery, to process the royalty oil within the state as refined products for the benefit of the citizens of Alaska and it encourages the buyer to employ Alaska residents to the extent that they are available, willing, and at least as qualified as other candidates.

MR. MEZA concluded his presentation with slide 28, "5. CONTRACT TERMS FOR MARATHON AND PETRO STAR CONTRACTS ARE IN THE BEST INTEREST OF THE STATE." He related that the additional revenue, which DNR is required to earn for each of these contracts, was \$31 million and \$23 million for the 2016 contracts. He said the estimated additional revenue for the proposed contracts is \$3-\$14 million for Marathon and \$17-\$19 million for Petro Star.

[1:48:12 PM](#)

CHAIR PATKOTAK explained he would now take public testimony on each of the bills individually.

[1:48:24 PM](#)

CHAIR PATKOTAK opened public testimony on HB 409.

[1:48:58 PM](#)

DOUG CHAPADOS, President, CEO, Petro Star Inc., Arctic Slope Regional Corporation (ASRC), testified in support of HB 409, Petro Star's proposed five-year royalty oil contract. He noted that Petro Star is a wholly owned subsidiary of Arctic Slope Regional Corporation (ASRC) and the state's only Alaskan owned refiner. He said Petro Star has fuel distribution terminals located in Anchorage, Valdez, Kodiak, Dutch Harbor, and Interior Alaska. He related that Petro Star also operates two of the state's three commercial refineries, one in North Pole and the other in Valdez, most of which draw crude oil directly from the Trans Alaska Pipeline System (TAPS). He pointed out that TAPS is the only source of crude oil supply to Petro Star, which means contracts such as the one currently before the committee are essential to Petro Star's continued operation. From this crude oil, he continued, Petro Star produces a variety of products, including jet fuel for commercial airlines, over 90 percent of the jet fuel consumed at Department of Defense and

U.S. Coast Guard installations located across the state, heating oil for residential and commercial customers, ultra-low sulfur diesel fuels for on- and off-road uses, marine diesel fuels, asphalt oil for road paving projects, and specialty low-sulfur turbine fuel for the exclusive use of Golden Valley and Copper Valley electric associations. Mr. Chapados said that as testified to by DNR staff and explained in the Best Interest Finding (BIF), this contract is good for the state in terms of maximizing the revenues generated from Alaska's royalty oil share. It also benefits Alaskans, he added, by helping to maintain the instate petroleum refining industry and preserving competition within the state's fuels markets. He urged the committee to approve the bill.

[1:51:30 PM](#)

CHAIR PATKOTAK closed public testimony on HB 409 after ascertaining that no one else wished to testify.

[1:51:42 PM](#)

REPRESENTATIVE HOPKINS moved to report HB 409 out of committee with individual recommendations and the accompanying fiscal note. There being no objection, HB 409 was moved out of the House Resources Standing Committee.

[1:52:08 PM](#)

CHAIR PATKOTAK opened public testimony on HB 410.

[1:52:28 PM](#)

CASEY SULLIVAN, Government and Public Affairs Manager, Marathon Petroleum Corporation, testified in support of HB 410. He stated that the availability, the flexibility, and the stability that this contract offers will have a positive impact on Marathon's ability to optimize its ongoing operation at its Kenai refinery. He said the Kenai refinery has been one of Alaska's longest in-state manufacturers producing quality transportation fuels that have moved Alaskans since 1969. He underscored that the legislation before the committee is the result of constructive dialogue and productive negotiations between the Division of Oil and Gas and Marathon, and the contract provides a positive shared value to all Alaskans. He pointed out that the division's best interest finding found that the state will continue to receive a price for its royalty in-kind oil that is in keeping with oil in-value. For Marathon, he

continued, the contract provides a stable supply of Alaska North Slope crude while also giving Marathon the flexibility to accommodate seasonal fluctuations in demand for refined product. He said Marathon is committed to its longstanding legacy of safely and reliably producing quality fuel. He urged the passage of HB 410.

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CHAIR PATKOTAK closed public testimony on HB 410 after ascertaining that no one else wished to testify.

[1:55:02 PM](#)

REPRESENTATIVE HOPKINS moved to report HB 410 out of committee with individual recommendations and the accompanying fiscal notes. There being no objection HB 410 was moved out of the House Resources Standing Committee.

[1:55:23 PM](#)

The committee took a brief at-ease.

[1:55:31 PM](#)

#### **ADJOURNMENT**

[There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 1:55 p.m.]