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Alaska State Legislature

SENATE Resources Committee

POUCH V
STATE CAPITOL
JUNEAU, ALASKA 99811
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Official Business

BETTYE FAHRENKAMP, Chairman
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DICK ELIASON
DON GILMAN
BOB MULCAHY
ARLISS STURGULEWSKI

March 25, 1982
5:00 p.m.

House Finance Committee Room
Room 519 - Capitol Building

Meeting with House Joint Committee on Oil and Gas

MEMBERS PRESENT

Senator Fahrenkamp
Senator Gilman
Senator Fischer
Senator Mulcahy
Senator Sturgulewski

Representative Halford
Representative Cotten
Representative Randolph
Representative Rogers
Representative Fanning

Hearing: Presentation by the Department of Natural Resources, the Alaska Royalty Oil and Gas Development Advisory Board, Doyon, Ltd., and Tesoro Alaska Petroleum Co., on the proposed Alaska royalty oil contracts.

The meeting was called to order by Rep. Halford, Chairman.

Dick Lyon, Chairman, Alaska Royalty Oil and Gas Development Advisory Board, presented two resolutions passed by the Board, recommending that the Legislature approve the Tesoro contract, and disapprove the Doyon contract. Mr. Lyon stated that the function of the Board was to make the extensive contract negotiations as public as possible while still holding private negotiations. The conclusions of both resolutions were read into the record.

John Katz, Commissioner, Department of Natural Resources, presented the Tesoro contract for approval, with the full support of the administration. The Commissioner stated that the Department agrees with Board's recommendation on the Doyon contract, while disagreeing with one of their premises for the recommendation.

Mr. Katz outlined the procedural criteria used by the Department in its contract negotiations: that the decisions must be fair and be perceived to be fair by all participants and the public; that there should be an effort to institutionalize the royalty oil and gas decision-making process; that there should be a clear paper trail documenting the decision-making process; that the process should

increase the knowledge of state royalty oil and gas decision makers; that the standard form for royalty oil and gas contracts should be improved; that the Department should improve its working relationship with the Board.

The culmination of the effort was a very tough, workable contract form and the findings document.

Commissioner Katz testified that when he came on-board, the Department revised the pending solicitation to reflect the in-state preference in the statutes. They received 29 responses. In a winnowing process, they met with all respondents who wanted to, made a series of findings, and allowed rejected respondents a chance to refute the Department's conclusions. They continued negotiations with 8 or 9 serious proposals.

Mr. Katz reviewed the policies applied in the negotiations:

- 1) a clear--but not absolute--preference for in-state taking of royalty oil and gas;
- 2) parity between all parties in terms of major contract conditions;
- 3) adopting a weighted average field pricing system for the North Slope, with contractual adjustments pending the result of the Amerada Hess litigation, with 3% above the higher of the state treasury rate or the prime rate to be paid;
- 4) a twelve year term;
- 5) retain a significant uncommitted volume for future options;
- 6) establish an option fee to be paid on contractually committed oil not taken by the processor;
- 7) no interim taking--no state oil to finance a project that wouldn't be otherwise financable;
- 8) the state is willing to be the 100% supplier of royalty oil to in-state processors, to provide a secure base for operations and future expansion;
- 9) return oil--oil that is left at the end of the refining process--requires the payment of a quality penalty if put back in the trans Alaska pipeline for downstream use;
- 10) attempted to gain concessions for rural Alaska;
- 11) attempt to use royalty oil to complement coal development through the development of petrocake.
- 12) there is a definite negative impact on in-value price and severance taxes from Alaskan oil due to displacement of west coast oil, that could amount to \$10 million per year, as a rough estimate, but that this possible loss to the state is outweighed by other benefits;
- 13) royalty oil should not be used as leverage to enter into other than the petroleum market;
- 14) all contracts should have adequate security.

Commissioner Katz made the following observations:

- 1) that the Department was negotiating the contracts at a time when their leverage for negotiation couldn't have been worse; there is an oversupply of oil, and potential purchasers have alternative sources of supply; however, the state had a satisfactory alternative in that the state could let the producers take the oil in-value and sell it for the state; the producers are the best long-term marketers of Alaskan crude oil;
- 2) in some situations it would be to the state's advantage to offer royalty oil for purchase by competitive auction, but two factors work against it; first, auctioned oil would displace west coast oil, with a negative effect on in-value and well-head price; second, while the state did well in some competitive solicitations last summer, oil producers are still the best long-term marketers of oil.

Commissioner Katz summarized the current status of the contract negotiations. There are five contracts still pending. The Tesoro contract is recommended for approval. The Doyon contract will be recommended for approval if they can have the financing in place in a few weeks. There are three other good possibilities being negotiated, with Chevron, Provident Oil, and Suneel. There are a number of questions to be answered on the Provident and Suneel contract proposals. The state intends to commit itself to a written process to address these questions, preparatory to further contractual negotiations.

Bob Maynard, Assistant Alaska Attorney General, addressed the issue of pricing systems. The "exhibit B" purchasing system attached to the Alpetco contract presents a regrettable position with respect to the Amerada Hess litigation, requiring the purchaser to pay the higher of either the price reported to the state by the producer, or the average of all other producer prices, resulting in a term higher than the weighted average price but lower than the highest price.

The basic difference between the exhibit B pricing and the system used in the proposed Tesoro contract is that by the exhibit B system, Alpetco paid the state as if the state had won the lawsuit, and Alaska will have to pay them back if the case is lost; Tesoro will pay the state as if the state had lost the lawsuit, and pay the state the difference should the state win.

Commissioner Katz, in response to a question from Senator Fischer, addressed the issue of alternative pricing systems. There are negative impacts on state revenues by using the weighted average field price, but the contractual adjustments pending resolution of the Amerada Hess litigation, with the 3% above prime aspect will recapture the difference.

All pricing system alternatives were examined, and exhibit B pricing was rejected for two basic reasons: first, the recapture mechanism currently being used is good; second, exhibit B pricing impairs in-state oil utilization because of the uncertainty regarding the price

for long periods after the actual transaction. To serve in-kind taking, the Department felt the state should deviate from exhibit B pricing, recognizing that there will be adjustments in the aftermath of the Amerada Hess litigation.

Jeff Haynes, Deputy Commissioner of Natural Resources, stated that the market situation has changed considerably in the last twelve years, and would change considerably in the next twelve. The basic decision regarding the pricing was to tie it to the price that seven-eighth's of North Slope crude was sold for. The two-tier pricing system is in place for specific and economically justifiable reasons. It is possible that exhibit B pricing without the Amerada Hess adjustment could be a premium price in twelve years; the situation could change; it is hard to predict. Given the market influences, however, it is more likely to be less. The Department believes that its estimates are as accurate as possible.

Commissioner Katz, in response to a question from Senator Fahrenkamp, stated that there is no direct assurance that the lower price to processors will be reflected in consumer costs. That sort of guarantee would be difficult to negotiate. That is why the Department continues to negotiate with Doyon--it is good for the state to promote competition, to increase benefits to consumers.

In response to comments from Rep. Halford, Commissioner Katz pointed out that there is an inherent statutory conflict between maximum revenues for the state and the preference for in-state use. In the case of the Doyon contract, there is no question that another refinery would lead to significant price competition in the greater railbelt area. The trade-offs are difficult to quantify, but the Department will provide the legislature with such figures for cost-benefit analysis as are available.

In response to questions from Rep. Rogers, Commissioner Katz stated the legislature should enact a statute to approve the contracts. If Doyon can get financing satisfactorily in place in the next few weeks, the Department would recommend legislative approval. If, however, the legislature enacted legislation approving the Doyon contract without adequate financing in place, the Department would recommend that the Governor veto the bill.

In response to further questioning, Mr. Katz stated that if the Doyon contract is not approved this session, the Department would continue to pursue it over the interim. The Attorney General's office advises the Department that this solicitation can continue until terminated at the Commissioner's discretion. Commissioner Katz would like to bring this solicitation to a conclusion in the next few months, with an outside limit at the end of Governor Hammond's current term. After that conditions will change, and warrant a new solicitation.

The Department has been advised that Tesoro would have to enter a new solicitation for additional oil for expanded facilities, such as a hydrocoker. This is also relevant in the light of the policy only to provide royalty oil for "imminent" projects; which is another reason the Department wants to terminate this solicitation in a timely manner. It was with this situation in mind that the Department retained a quantity of oil for future options.

Deputy Commissioner Haynes pointed out that paragraph 2.13 of the Tesoro contract contains a provision recognizing the statutory preference for in-state use of royalty oil and the manufacture of petroleum products; which means that Tesoro would automatically be involved in future solicitations.

Commissioner Katz stated that the current solicitation could be amended simply, to allow continued negotiations with Tesoro, and that the statutes, while favoring mass solicitations, do allow for individual negotiations, which could be used to allow for supply for further Tesoro expansion.

Bob Maynard pointed out that it is a problem of wording; Tesoro's expansion can't come under the current solicitation, but the solicitation can be amended to allow for it.

Commissioner Katz, in response to question from Rep. Rogers, pointed out that if the state wanted to renegotiate the contract with Doyon, they could go about it two ways: (1) withdraw the contract, make the desired changes, and send it back through the Board process; or (2) the Legislature could waive that procedure in the enacting legislation for the renegotiated contract.

Mr. Katz stated that the return oil situation was not as serious a problem for processors on the trans-Alaska pipeline, who can put residual oil back into the line. The state has a good policy of selling all title to royalty oil at Pump Station #1. The Department looked at cooperative agreements for Doyon to sell the return oil to a downstream processor, but the arrangements did not work out. Chevron dropping out of the negotiations had a material effect on the Doyon contract.

Mapco's return oil under existing contract is owned and sold by them. Depending on market conditions, this can either be a benefit or a drag to the processor.

Deputy Commissioner Haynes stated that it depended on the market; in the case of the Fairbanks refinery, they can dump residual oil back into the pipeline, and pay a quality penalty, but then sell it as Alaska North Slope (ANS) crude at Valdez, in competition with the producers. It has been both a good and bad deal for them in past years. With the failure of the Chevron to buy the return oil, Doyon will have to sell ANS crude.

John Katz, in response to a question from Rep. Cotten, pointed out that although he did not agree that it is constitutionally required, the Governor has set a clear policy that he wants a legislative decision for

the approval or disapproval of royalty oil contracts.

Bob Maynard pointed out an additional advantage to statutory approval, that in doing so, the Legislature would be "ratifying" the contracts, curing any procedural faults that may have occurred up to that point.

John Katz stated that the state is selling at the weighted average of what all North Slope producers charge. Sohio made an offer to buy most of the royalty oil at a greater than weighted average price for resale to in-state processors, but policy dictated that the state couldn't allow a private concern to make what should properly be public decisions regarding state royalty oil.

In response to a question from Senator Fahrenkamp, the Commissioner stated that the Suneel proposal is still active, but not the highest priority. The unanswered questions on this project will not be resolved in time for consideration by this Legislature. If the questions could be resolved in time, the Legislature would have the option of allowing the contract to go through the usual royalty oil procedure, or waiving the process in enacting legislation this session.

Senator Halford noted that the Department recommends that the Legislature approve the Tesoro contract, and approve the Doyon contract, with a four-year moratorium on option fees, if a financing package goes through. Two separate pieces of enacting legislation should be introduced.

Jeff Haynes presented a summary of highlights of both contracts:

The Tesoro contract calls for the purchase of 46,000 barrels per day, which is about the maximum the Tesoro refinery can handle. Tesoro also currently contracts for about 8,500 barrels per day of royalty oil from the Cook Inlet. These reserves are declining. Tesoro can vary the amount to be taken, up to 46,000 barrels per day, on six month's notice. The state can impose a permanent top-limit equal to the greatest amount taken in the first five years of the contract. Tesoro can permanently terminate the contract on nine months notice. The price is the producer's weighted average field price, subject to adjustment as a result of the Amerada Hess litigation. Any money owed the state would be paid at the higher of the state treasury rate or the prime rate plus three percent. The contract term is twelve years, and the oil is to be processed in-state, with an equal-value exchange provision. The oil will have to be processed at the Nikiski refinery, and there are standards for how much of certain products they shall produce. Tesoro is committed to completion of feasibility studies for expansion, to include a petroleum coker. The state retains an option on the residual oil and petrocoker, and can assign its use. The performance and guarantee reservation structure is a fee paid to the state on contractually committed oil, if not actually taken--about fifteen cents per barrel per day. The security terms require a letter of credit worth two month's supply of oil. The Attorney General's Office thinks that the local hire provision in the contract goes as far as the state is constitutionally allowed.

Doyon had two contracts in the course of negotiations: one to purchase the Mapco refinery; one to build a new refinery. The contract to take over the Mapco refinery was withdrawn.

The volume of the Doyon contract is 50,000 barrels per day; the price and term are the same. The in-state processing provision is similar, except that it includes a definition of a required schedule; they are required to build, open and operate a new refinery by December 1, 1983, or the contract will terminate. The contract contains a provision for a future new refinery or new royalty oil contracts, and contingencies to cover the state's interests should Doyon acquire the Mapco refinery.

In response to Senator Sturgulewski, Mr. Haynes stated that unlike the Charter Oil contract, which had many complexities and procedures for legislative review of the fulfilment of the conditions of the contract, the Doyon proposal was not for a world-class facility, and was simpler to track.

Bob Maynard pointed out that the contracts have a conflict clause, similar to the procedure for administrative review of regulations, whereby contract disputes or ambiguities regarding a term of the contract shall be determined by the Commissioner first, and that the buyer must adhere to the Commissioner's decision, unless there is a preponderance of evidence to the contrary.

The Committee adjourned at 7:00 p.m.



Alaska State Legislature

SENATE

Resources Committee

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March 26, 1982
8:15 a.m.

House Finance Committee Room
Room 519 - Capitol Building

Meeting with House Joint Committee on Oil and Gas

Members Present

Senator Fahrenkamp
Senator Gilman
Senator Sturgulewski

Representative Halford
Representative Cotten
Representative Randolph
Representative Rogers

Hearing: Presentation by the Department of Natural Resources, the Alaska Royalty Oil and Gas Development Advisory Board, Doyon, Ltd., and Tesoro Alaska Petroleum Co., on the proposed Alaska royalty oil contracts (continuation from March 25, 1982).

The meeting was called to order by Rep. Halford, Chairman.

Avrum Gross, General Counsel for Doyon, Ltd., stated that the contract had been negotiated by Dick Edwards and Marco Pignalberi. Doyon has worked since its inception to put together a competing refinery in Fairbanks. They have acquired the equipment and completed the engineering and land-acquisition work, simultaneously negotiating with the state for the last five or six months.

Mr. Gross became involved in early January. At that point, Doyon had the opportunity to negotiate to purchase the North Pole refinery, and switched over to negotiating both contracts with the state. Negotiations for purchase collapsed after about six weeks. By this time, the status of the refinery construction financing had changed. The financiers had pushed Doyon to pick-up the refinery. The return oil was the main problem in negotiations; for every 30,000 barrels to pass through the refinery, 20,000 barrels are returned to the pipeline, and would have to be sold by Doyon. Marketing that amount of oil without a substantial loss is difficult. They were originally intending to dispose of return oil to Chevron under contract, but that contract fell through. This has been the major snag in obtaining financing; Doyon will have

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a much better idea of their ability to dispose of return oil in two to three weeks.

Mr. Gross noted that this is not a contract like the Alpetco contract, where Doyon could market oil as it sees fit. The contract requires Doyon to build a refinery and get it on line by December 1, 1983. As a new project, it is difficult, amounting to a \$100 million investment in a world oil situation not conducive to major investment.

Mr. Gross suggested that the Legislature put the Doyon contract on hold for two or three weeks, and Doyon will make another presentation to the Legislature at that time.

In response to a question from Rep. Halford, Mr. Gross stated that he was surprised at the Advisory Board's reaction to the four-year waiver on option fees. Mr. Tim Wallace, President of Doyon, testified before the Board in Fairbanks, and was asked no question regarding the waiver. The negotiations for the contract took 5 months, and Doyon made trade-offs to gain this concession. The only way to determine if the clause is indeed anti-competitive would be to do an analysis of Mapco's situation. To come "out of the blue" and pick on one term without considering the other factors and the conditions of the Mapco contract is not a correct procedure.

In response to Senator Fahrenkamp, Mr. Gross recommended that the Legislature put the contract into legislation, and hold in committee, awaiting financing. At some point, the Legislature will have to make a judgement on the good-faith and viability of the Doyon proposal. In the interim until the refinery is completed, the royalty oil would be marketed by the producers, at no loss to the state.

In response to Rep. Randolph, Mr. Gross stated that the financing for refinery construction had been in place with the Continental Bank in Chicago. As the emphasis shifted to negotiating for the Mapco refinery, the bank made a financial commitment to the purchase, and withdrew its commitment to construction. When it became clear that the purchase might not go through, the situation for construction had changed. Continental wanted to change the terms and seek involvement by others in the financing, primarily because of the risk involved with the return oil. Return oil has been the major drain on the North Pole refinery profits. When Mr. Gross last spoke to Continental, they were willing to finance a major portion of the project, insisting on the financial involvement of others. If Doyon can find a way to dispose of the return oil, he sees no problem in putting together a financing package.

In response to Rep. Rogers, Mr. Gross stated that provision had been made to store the purchased equipment until financing was available, and that on-site work had been shut down for the time being. If Doyon is able to continue work in this construction season, they could have the refinery in place before the December 1983 deadline.

In response to Rep. Cotten, Mr. Gross stated that not having the contract approved until the next legislative session would create a problem, in that the contract is an integral part of the financing package. However, the Doyon proposal is not a speculative proposition; they are committed to follow through on the project.

Mr. Gross stated that Tim Wallace was negotiating with several oil companies for a contract for the return oil. There is the problem caused by the current oil glut. Doyon is not concerned with making a profit on the return oil, but with avoiding a loss. The North Pole refinery has had enormous losses in the past, but has recently made arrangements to avoid more serious losses.

Jeff Haynes stated that the Department made the four-year option waiver concession to Doyon as a new entrant. The most difficult philosophical question in the negotiations was reconciling being totally market neutral and yet encouraging competition. The bottom line for the Doyon contract is the Mapco contract. Doyon would prefer to have the Mapco contract for competitive reasons, but the Mapco contract has provisions that are not recognized as being in the best interest of the state at this time. The Department was under intense pressure from Doyon throughout the negotiations to make concessions; but the only significant concession was the waiver on reservation fees.

Mr. Haynes stated that there was an advantage to a refinery on the transAlaska pipeline, in terms of return oil. They have to sell Alaska North Slope crude oil with a quality penalty, rather than residual oil, which is a bigger problem. The Department tried to work out a deal with Chevron to use the residual oil from the Mapco refinery, which would have been to Doyon's advantage on some occasions, but Mapco didn't want to give up their absolute rights to the return oil, so the contract fell through.

Deputy Commissioner Haynes stated that in terms of Doyon's financing, the Department was applying the criteria that they would contract for royalty oil only for projects that were operating now or were imminent. The Department concurs with the Advisory Board's recommendation to postpone the Doyon contract if financing is not in place in short order, but disagrees with the Board's stand on the reservation fee issue.

In response to Senator Fischer, Mr. Haynes stated that it might not be appropriate for the Legislature to pass an approval bill for the Doyon contract, conditioned on a finding by the Commissioner or Governor that financing was in place, because the Department does not want to see a group with a supply contract but no deal put together, using the contract as leverage for financing. They prefer to have the issue settled in the course of the Legislature.

Avrum Gross pointed out that the contract has a built-in time limit. With the construction season in Fairbanks being what it is, if Doyon

cannot begin construction next year, the new refinery might not happen. If the Legislature were to approve the contract, the time limit for completion is built-in.

Jeff Haynes, in response to questions, stated that there could be problems with conditional legislative approval of the contract. At some point after this session, stretching the solicitation procedure out would be unfair to other parties to the negotiations. The Department has used the standard that processing facilities must either be operating or imminent. A supply contract will not make a project viable if it were not viable otherwise. In terms of conditional approval, the state has to look at the other proposals. Others wanted more barrels for expansion, which could yield more competition. The total amount requested added up to more than the state has available; the state rejected their proposals. It would be unfair to them to extend the time for Doyon too long.

Dick Lyons, Chairman, Alaska Royalty Oil and Gas Development Board, stated that in the Board's perspective, the imminency of a project was a concern. They did not want to commit state crude to any project which wasn't going forward. There was the issue of competition. Both proposed contracts--Tesoro and Doyon--involve about \$1 million per day in royalty oil. The crude would be sold for dissimilar prices under similar conditions and terms. If it were a private supplier, and not the state, federal law would prohibit it.

In response to Rep. Halford, Mr. Lyons stated that if the Legislature were to introduce bills for both contracts, the Board could meet in short order to consider a financing package for the Doyon project, if one were to come forward.

Rep. Halford stated that the Legislature should move forward with both proposals this session, and hear from the Department of Natural Resources and the Advisory Board on the financing package for Doyon, if one is forthcoming.

Mr. Gross stated that the Legislature is probably just as qualified to judge on the merits of a financing package as the Board, and could speed the decision process by waiving Board review.

Dennis Jurin, President, Tesoro Alaska Petroleum Company, testified that Tesoro has the capacity to supply over 100 percent of the gasoline required in the state at present. The company started in 1969 with an 18,000 barrel per day capacity refinery in Kenai, and has expanded it to almost 50,000 barrels per day. They did it on the basis of a relatively small Cook Inlet royalty oil contract, and each expansion after inception had no other subsidy than an opportunity to buy royalty oil on a competitive basis.

Mr. Jurin stated that Tesoro was a respondent in the 1977, when the North Pole refinery requested a contract. The Tesoro proposal was not approved, and Tesoro did not push the issue, which, in hind-sight, the company should have. Due to rapid growth through aggressive marketing, Tesoro has placed itself in a vulnerable position, with most of their

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supply of crude coming from foreign sources and spot market purchases. The Cook Inlet supply is dropping at a rate of about one percent per month. The majority of the supply is either foreign or domestic short-term contracts, subject to interruption. Tesoro wants a relatively secure long-term supply contract not subject to rapid changes.

Mr. Jurin stated that Tesoro is considering expansion of their facilities. They began research in November, 1981 on market growth in Alaska, the probable product-mix and preliminary engineering. It is possible that as much as 70,000 barrels per day could not be fully utilized until 1995, and Tesoro might settle on about 55,000 to 60,000 barrels per day. One primary consideration in their planning is what happens to the Advisory Board recommendations here. A gasoline producing refinery in Fairbanks would effectively close that market to Tesoro in the Interior, as is the diesel and turbine fuel market already, due to production by the North Pole refinery. It costs Tesoro eight to nine cents per barrel to transport gasoline to the Interior, and an on-site refinery there would have an unbeatable competitive edge. Therefore the decisions here have a lot to do with what Tesoro builds in the Kenai.

Mr. Jurin discussed the return oil situation. The west coast utilities are the largest users of residual oil; they will have abundant supplies from other sources. Tesoro intends to convert the residual oil to petcoke or use a hydrogenation process to convert it to turbine or diesel fuel. They are currently running a pilot plant project on their feedstocks to test the processes. Union Oil Research is the licensor of Tesoro's first hydrocracker in Kenai; they are negotiating with them for a possible second facility, and have engaged engineers for design investigation.

Mr. Jurin stated that Tesoro's corporate finance group is meeting with financial institutions to determine the best way to finance the expansion. All the decisions will probably be made this year. The proposed contract requires Tesoro to periodically report to the Commissioner on the progress of evaluation, planning and development of the project. The contract would remove a degree of vulnerability in supply, and help maintain Tesoro as a formidable competitor in Alaska. The difference between the Tesoro proposal and others is that Tesoro is not planning to go ahead in the future, but are proceeding with the project on its own merits at this time, not because of the benefit of some sort of subsidy. Tesoro has an unblemished record in dealing with the state on its existing contract.

Senator Fahrenkamp stated that estimates of the price break for a processor buying royalty oil from the state run from one to three dollars per barrel, and asked if a long-term contract would result in cost reductions passed on to consumers.

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Mr. Jurin replied that he didn't know what the future price situation would be; the cost of raw materials is not the only factor. A long-term contract would mitigate abrupt shortages in supply which have been brought on in the past by economic supply shortages, requiring that Tesoro reduce production runs. Tesoro will do whatever possible to maintain the competitive or below market pricing.

In response to Rep. Halford, Mr. Jurin stated that Tesoro currently supplies 27 to 28 percent of the market directly, with the remainder being supplied by Chevron, Union, Texaco and independent operators. Tesoro will probably never supply the whole state, due to competitive differentials in transportation costs. Tesoro serves mainly the lower railbelt and Kenai area. They provide 78 percent of the turbine fuel to the Anchorage International Airport, and will probably supply more with an arrangement for another hydrocracker plant. The potential loss to the state by the west coast offset may change; the gulf coast prices have been traditionally higher than the west coast. Tesoro would not be looking for a long-term contract if they thought that there would be an ample future supply of oil. Projections predict that there will be more shortages than surpluses over the long run.

In response to Rep. Cotten, Mr. Jurin stated that Tesoro has a contract with San Deigo Gas and Electric to purchase the return oil. The contract began in 1972, and has been renewed through 1984. Tesoro intends to expand their facilities to process the return oil. They don't have a guaranteed market in the pipeline.

Jim Smith, President, Tesoro Alaka Crude Oil Company, in response to Rep. Cotten, stated that whether the price Tesoro would pay for oil would be greater than the average weighted price, if they purchased it from a producer other than the state depends upon variable market conditions. Tesoro is currently buying ANS crude from Sohio on the spot market, probably paying more than they would pay other producers, but the other producers are not willing to sell.

The Committee was adjourned at 9:50 a.m.



Alaska State Legislature

SENATE Resources Committee

Official Business

BETTYE FAHRENKAMP, Chairman
VIC FISCHER, Vice-Chairman
BRAD BRADLEY
DICK ELIASON
DON GILMAN
BOB MULCAHY
ARLISS STURGULEWSKI

MEMBERS PRESENT

Senator Fahrenkamp
Senator Eliason
Senator Gilman
Senator Mulcahy
Senator Sturgulewski

POUCH V
STATE CAPITOL
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April 7, 1982
3:10 p.m.

Beltz Room
Room 211 - Capitol

Hearing:

SB 880 Sale of royalty oil by the State of Alaska to Doyon, Ltd.
SB 881 Sale of royalty oil by the State of Alaska to Tesoro Alaska
Petroleum.

Senator Fahrenkamp explained that the Committee was to either accept or reject the contracts, but could not amend them.

SB 881

Dennis Jurin, President, Tesoro Alaska Petroleum Company, spoke in support of SB 881, stressing that projections predict that over the long run there will be more shortages of oil than surpluses. Although crude oil prices are very difficult to predict even for the short term, Jurin was confident that the selling of oil in kind would not result in depreciation of the State's revenue. He reviewed his company's "good track record" and the direct positive economic impact they continue to have on the state. He concluded by stating his company's need for a long-term, stable supply of crude oil to continue refinery operations.

Senator Mulcahy moved SB 881 and asked unanimous consent.

SB 880

John Katz, Commissioner, Department of Natural Resources, described two items of concern in the Doyon contract. One is the four year waiver on option fees, which is an incentive to new entry but may be anti-competitive. The other is Doyon's lack of financing. Katz suggested that the Committee has three options: to approve the contract, disapprove the contract, or approve the contract contingent on a finding by the Commissioner of the Department of Natural Resources that, by a date certain, financing is firm and adequate, and that all other essential aspects of the program have been maintained.

Senate Resources Committee

April 7, 1982

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Tim Wallis, President, Doyon, explained that their financing is contingent on getting rid of the return oil. A contract to this effect needs to be negotiated, and a search for an equity partner completed. He stated that a 6-month period would be "comfortable" for meeting these goals.

Senator Mulcahy moved that Doyon be given until September 1, 1982 to obtain financing, while maintaining all other essential elements.

Senator Mulcahy moved CSSB 880 with individual recommendations.

The meeting was adjourned at 4:00 p.m.

STATE OF ALASKA

**DEPARTMENT OF COMMERCE &
ECONOMIC DEVELOPMENT**
ROYALTY OIL AND GAS ADVISORY BOARD

JAY S. HAMMOND, GOVERNOR

4/6/82

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April 2, 1982

Senator Jalmar M. Kerttula
President of the Senate
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

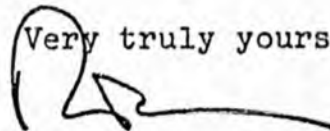
Dear Mr. President:

In accordance with AS 38.06, the Alaska Royalty Oil and Gas Development Advisory Board is required to examine proposed sales of royalty oil or gas and prepare a written recommendation to the Legislature that it approve or disapprove a proposed sale.

Forwarded herewith is the Board Resolution 82-1 relating to the "Agreement for the Sale and Purchase of Royalty Oil" between the State of Alaska and Tesoro Alaska Petroleum Company dated February 26, 1982. The Board has recommended that this sale be approved by the Alaska State Legislature.

Also forwarded herewith is the Board Resolution 82-2 relating to the "Agreement for the Sale and Purchase of Royalty Oil" between the State of Alaska and Doyon, Ltd., dated February 26, 1982. The Board has recommended that this sale be disapproved by the Alaska State Legislature.

Very truly yours,



Richard A. Lyon
Chairman

cc: Senator Bettye M. Fahrenkamp

Enclosures

ALASKA ROYALTY OIL AND GAS DEVELOPMENT ADVISORY BOARD

Resolution 62-1

WHEREAS, the State of Alaska, through the Commissioner of the Alaska Department of Natural Resources, and the Tesoro Alaska Petroleum Company have entered into an "Agreement for the Sale and Purchase of Royalty Oil" dated the 26th day of February 1982; and

WHEREAS, in accordance with AS 38.06.055(a) ". . . the Commissioner of Natural Resources may not enter into a sale, exchange, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas under AS 38.05.183 without the prior approval of the Legislature. . ."; and

WHEREAS, according to AS 38.06.055(a), ". . . a sale, exchange encumbrance, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas may not be made by the commissioner of natural resources under AS 38.05.183 without prior review of the proposed sale, exchange, encumbrance or other disposition by the board. A written recommendation of the board on the proposed sale, exchange, encumbrance or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas shall be submitted to the legislature at the time a resolution approving the proposed sale, exchange, encumbrance or other disposition is introduced in the legislature"; and

WHEREAS, in accordance with AS 38.06.040(a), the board shall

- (2) "hold public hearings on proposed sales, exchanges, or other disposals of royalty oil or gas to determine whether the proposals comply with AS 38.06.070;
- (3) examine proposed sales, exchanges or other disposal of, and

recommend to the legislature that it approve or disapprove a proposed sale, exchange or other disposal of

(A) the oil or gas that is obtained by the state as royalty under AS 38.05.182; or

(B) the rights to receive future oil or gas production under state leases"; and

WHEREAS, the board did, on February 26, 1982, meet and receive from the commissioner of natural resources the above mentioned agreement with Tesoro as well as a document entitled "Review of Alaska Royalty Oil Policy and Findings on Proposed Disposal of State Royalty Oil" dated February 26, 1982 and the board did act and call public hearings, in accordance with the regulations outlined 3 AAC 56, in Anchorage on March 15, 1982 and Fairbanks on March 16, 1982 and received no public comment pertinent to this agreement; and

WHEREAS, in accordance with AS 38.06 and AS 38.05, the commissioner of natural resources is required to submit to the board, in writing, certain Findings or Determinations relating to the disposal of oil and gas royalty interests and the board has received the required Findings and Determinations; and

WHEREAS, the board members had the opportunity to review the agreement, related Findings and Determinations and Public Testimony during the period February 26, 1982 until March 25, 1982; and

WHEREAS, the board did, on March 25, 1982, meet to discuss the agreement, related Findings and Determination, and Public Testimony to insure that this disposal is in accordance with the statutory purpose and criteria set forth in AS 38.06 as well as

the board's "Basic Principles and Policies" as outlined in the board's development plan, and

THEREFORE, the board finds as follows:

1. that the commissioner of natural resources has followed the board policies and applicable statutes and regulations relating to the disposal of oil and gas royalty interests.
2. that the board agrees that the sale of the royalty oil interests to Tesoro-Alaska Petroleum Company as per the agreement is in the best interest of the state because
 - (a) the oil is to be refined or processed or traded for other oil to be processed in the existing Tesoro refinery near Kenai, Alaska.
 - (b) Tesoro-Alaska is an in-state refiner who supplies products to the Alaska market with price or supply benefits to state citizens.
 - (c) the price the state will receive for this royalty interest appears to be substantially equivalent to or greater than the price the state would receive by taking this royalty in-value.
 - (d) that Tesoro-Alaska is a highly qualified company who has been operating its refinery to produce products for the Alaska market for over 12 years.
 - (e) that adequate security provisions have been included in the agreement.
 - (f) that this agreement is consistent with the criteria outlined in AS 38.06.070.

AND THEREFORE BE IT RESOLVED THAT the Alaska Royalty Oil and Gas Development Advisory Board recommends to the Twelfth Alaska

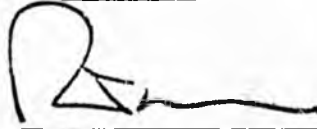
Legislature that the "Agreement for the Sale and Purchase of Royalty Oil" between the State of Alaska and Tesoro Alaska Petroleum Company, dated February 26, 1982 be APPROVED.

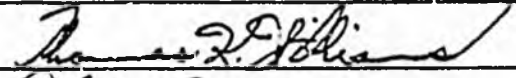
Board Member Charles P. WEBBER moved the adoption of the Resolution. Board Member Don TEPPER seconded.

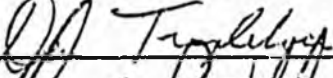
The vote was as follows:

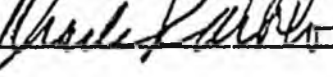
APPROVE


DISAPPROVE



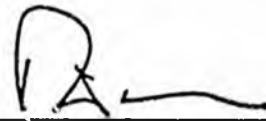








Adopted this 25th day of March 1982.



R.A. Lyon

Chairman

LEGISLATION SUMMARY

SB 881: "An Act relating to the sale of royalty oil by the State of Alaska to the Tesoro Alaska Petroleum Company; and providing for an effective date."

Sec. 1: Approves and ratifies the Tesoro Alaska Petroleum Company Alaska royalty oil contract.

Sec. 2: Immediate effective date.

PRIME SPONSOR: Rules (Governor's request)

4/7
53881

AGREEMENT FOR THE SALE AND
PURCHASE OF ROYALTY OIL

THIS AGREEMENT entered into as of the 26 day of February, 1982, by and between the STATE OF ALASKA ("Seller") and TESORO ALASKA PETROLEUM COMPANY, an Alaskan corporation ("Purchaser"),

ARTICLE I
DEFINITIONS

As used in this Agreement, the following terms shall have the following meanings:

1.1 "Commissioner" means the Commissioner of the Alaska Department of Natural Resources.

1.2 "Day" means a period of twenty-four (24) consecutive hours beginning at 12:01 a.m., Alaska Standard Time.

1.3 "Leases" means the oil and gas leases which are subject to the terms of the Unit Agreement.

1.4 "Lessee" means any person owning a working interest in any of the Leases.

1.5 "Month" means the period beginning at 12:01 a.m., Alaska Standard Time, on the first day of the calendar month and ending at the same time on the first day of the next succeeding calendar month.

1.6 "Oil" or "crude oil" shall have the same meaning as the word "oil" under the Unit Agreement.

1.7 "Point of Delivery" shall have the meaning set out in Article 2.4.

1.8 "Royalty Oil" means the oil which the Seller may take in-kind (amount) as its royalty under the Leases whether or not Seller has elected to take or is taking that royalty in in-kind.

1.9 "Daily Royalty Oil" means the quantity of Royalty Oil produced by the Lessees each day.

1.10 "Unit Agreement" means the Prudhoe Bay Unit Agreement effective April 1, 1977, by and between Seller and the Lessees, as it may be amended from time to time.

ARTICLE II

SALE OF ROYALTY OIL

2.1 Quantity. Seller agrees to sell to Purchaser and Purchaser agrees to buy from Seller up to that quantity of oil equal to 24.533% of the Daily Royalty Oil less Cook Inlet Royalty ("Maximum Quantity"). "Cook Inlet Royalty" means that daily volume of oil expected to be sold to Purchaser by Seller during the month of July in each calendar year under the agreement entitled "Agreement for the Sale and Purchase of State of Alaska Royalty Oil" entered into on January 31, 1969 and extended on March 8, 1977 and again February 24, 1978 and any renewals or extensions thereof or any new contract between Seller and Purchaser for the purchase and sale of crude oil produced from the Cook Inlet of Alaska. The determination of Cook Inlet Royalty shall be made no later than thirty (30) days

prior to the beginning of each calendar year. Upon at least nine (9) months written notice to Seller, Purchaser may increase or decrease the amount of oil to be tendered by Seller at the Point of Delivery, but the amount tendered by Seller under this Agreement shall not exceed the Maximum Quantity. It is understood and agreed that the volume of Daily Royalty Oil available to Seller will vary and may be interrupted from time-to-time, and depends upon a variety of factors, including the rate of production from the Leases. Seller disclaims and Purchaser waives any representation, covenant or warranty, express or implied, as to the specific quantity or the total or daily, monthly, average, or aggregate volume of Royalty Oil to be sold or tendered under this Agreement. Seller warrants that it has good title to the oil tendered under this Agreement. Seller shall hold the Purchaser harmless from all liens, encumbrances and valid adverse claims that may affect the Royalty Oil at the time the Royalty Oil is tendered to the Purchaser.

If Purchaser has not taken the Maximum Quantity of oil within five (5) years after the effective date of this Agreement, Seller, at its option, may permanently decrease the Maximum Quantity to the lesser of: (1) the greatest percentage of Daily Royalty Oil tendered by Seller within that five-year period, or (2) the maximum amount of oil that can be processed at Purchaser's refinery located at Kenai, Alaska. Purchaser may permanently decrease the Maximum

Quantity or terminate this Agreement upon nine (9) months written notice to Seller.

If Seller underlifts or stores Royalty Oil at Prudhoe Bay, or if Seller recovers underlifted or stored Royalty Oil, the quantity of Royalty Oil tendered under this Agreement shall be calculated as if no Royalty Oil was underlifted or stored or recovered.

2.2 Quality. The Royalty Oil sold shall be the same quality as the oil delivered by the Lessees to the Seller at the Point of Delivery. It is understood and agreed that the quality of the Royalty Oil sold may vary from time to time. Seller disclaims, and Purchaser waives, any guarantee, representation, or warranty, either expressed or implied, of the merchantability, fitness for use, or suitability for any particular use or purpose, or otherwise, of any of the oil delivered under this Agreement or as to any specific, average or overall quality or characteristic of Royalty Oil to be sold or tendered under this Agreement.

2.3 Price of the Royalty Oil. The price for the oil tendered under this Agreement shall be equal to the amount that Seller would have received from its Lessees for the Royalty Oil tendered if that royalty had been payable in money (taken in value) rather than taken in kind, plus the Field Cost Allowance incurred by that oil as determined under the Prudhoe Bay Royalty Settlement Agreement (dated April 1, 1980 for reference purposes only), which was entered as part of a final judgment dated August 13, 1980 in

State of Alaska, et al. v. Amerada Hess Corp., et al.,
(Superior Court for the State of Alaska, First Judicial
District at Juneau)("Amerada Hess")("Settlement Agree-
ment")("Purchase Price"). The Purchase Price shall be
determined by Seller based upon the reports submitted by the
Lessees for royalty purposes or, when those reports are
unavailable, incomplete, or inaccurate, upon information
submitted by the Lessees for production tax or other tax
purposes, as may be adjusted from time to time as provided
in this Agreement. Buyer will only be entitled to review or
request material or information which is not confidential
under state law or regulation.

The method, basis and amount of royalty due Seller
when it takes its royalty in value from the Leases is
presently the subject of litigation in Amerada Hess. One of
the issues involved is the proper method to be used by the
Lessees in calculating the state's royalty when that royalty
is payable in money (in value). Until there is a resolution
of that dispute through judicial resolution or settlement,
the Purchase Price will be based upon the calculation of an
amount per barrel equal to the per barrel volume weighted
average of the in-value prices reported by the Lessees to
Seller for royalty purposes or, when the royalty reports are
unavailable, incomplete, or inaccurate, upon information
submitted by the Lessees for production tax or other tax
purposes, plus the Field Cost Allowance as determined under
the Settlement Agreement. Upon resolution of each of the

various issues that are or will be involved in Amerada Hess, adjustments will be made to previous payments in accordance with each resolution. If additional amounts are owed by Purchaser to Seller, interest on those amounts will be paid at a variable interest rate which is the higher of: (1) the prime rate as may be announced from time to time by The Bank of America, San Francisco, California plus three per cent (3%); or (2) the rate of return as is realized from time to time in the investment of the State of Alaska's general fund. Amounts owed from Seller to Purchaser shall be repaid at the rate set out in Article 5.6. Buyer will not voluntarily intervene or otherwise participate in Amerada Hess unless Seller expressly consents to that participation in writing. A settlement of Amerada Hess will be binding upon Buyer whether or not Buyer agrees with or consents to the terms of that settlement.

If any applicable law of the United States of America or any rule or regulation promulgated by a federal agency will, in the judgment of Seller, operate to prohibit or prevent Seller from receiving the full amount due under the above provisions, Buyer's obligation to pay the amount of the Purchase Price in excess of the amount permitted will be suspended or adjusted to the minimum extent required for Seller to comply with that law, rule or regulation.

2.4 Point and Time of Delivery. Simultaneous with receipt of its Royalty Oil from its Lessees, Seller shall tender the oil to Purchaser at the point at which Seller

receives the Royalty Oil from its Lessees. That point as presently agreed to by Seller and its Lessees in Article 2.3 of the Settlement Agreement is the custody transfer meters into the Trans Alaska Pipeline System at Prudhoe Bay.

2.5 Passage of Title and Risk of Loss. Title and risk of loss to the Royalty Oil sold under this Agreement shall pass from Seller to Purchaser for all purposes when Seller tenders the oil at the Point of Delivery.

2.6 Purchaser's Responsibility. Purchaser shall be responsible for the oil after passage of title. Purchaser will indemnify and hold Seller harmless from and against any and all claims, costs, damages (including reasonably foreseeable consequential damages), expenses or causes of action as a result of any loss, injury, or damage incurred by any party as a result of any transaction or event which relates to the crude oil after title has passed to Purchaser.

2.7 Transportation Arrangements. Purchaser shall make all necessary arrangements for transporting the oil sold under this Agreement from Point of Delivery, including satisfaction of line obligations and storage tank bottom requirements of the Trans Alaska Pipeline System, if any. If and as requested by the Seller, and at the time or times requested by Seller, Purchaser shall submit specific information concerning the arrangement it has made for transportation of the Royalty Oil sold under this Agreement through and away from the Trans Alaska

Pipeline System and for the resale or other disposal of the Royalty Oil. Such information may include the specific tenders of oil made to the Trans Alaska Pipeline System and identification of tankers which will transport the Royalty Oil. In addition, Purchaser will provide Seller, if and as requested by Seller, with satisfactory evidence or reasonable assurance of the existence and continuing validity of adequate arrangements for the transportation or disposal of the Royalty Oil subject to this Agreement. Failure to provide information, evidence or assurances requested will, at Seller's election by notice to Purchaser, be a material default under this Agreement.

2.8 Absolute Obligations. The obligations of Purchaser to accept, pay for, and arrange for the transportation of the Royalty Oil tendered or sold under this Agreement are absolute and will not be excused or discharged by the operation of any disability of Purchaser, event of force majeure, impracticability of performance, change in conditions, or any other reason or cause.

2.9 Date of First Delivery. On January 1, 1983, or seven months after statutory approval as set forth in Article VI, whichever is later, Seller will tender to Purchaser at the Point of Delivery the Maximum Quantity unless Purchaser, under the provisions of Article 2.1, decrease the amount of Royalty Oil to be tendered.

2.10 Performance Guaranty and Reservation Fee. If Purchaser does not take the Maximum Quantity on the Date of

First Delivery, Purchaser shall pay to Seller, in addition to the Purchase Price, an amount equal to 1.25% of the Purchase Price per barrel per day on the difference between the Maximum Quantity and the actual quantity tendered to and accepted by Purchaser ("Actual Quantity") for each day Purchaser does not take the Maximum Quantity on and after the Date of First Delivery. The payment of this fee shall end on the day that Purchaser accepts delivery of the Maximum Quantity. When Purchaser accepts the Maximum Quantity, all of the amounts paid under this Article 2.10 will be allowed to be credited against future payments for oil tendered under this Agreement except for an amount to be retained by Seller equal to .75% of the Purchase Price per barrel per day on the difference between the Maximum Quantity and the Actual Quantity for each day Purchaser did not take the Maximum Quantity on and after the Date of First Delivery. If Purchaser should hereafter decrease the amount of Royalty Oil to be tendered under this Agreement, Purchaser shall pay to Seller, in addition to the Purchase Price, an amount equal to .75% of the Purchase Price per barrel per day after the date that the decrease in the amount of Royalty Oil to be tendered by Seller takes effect on the difference between the Maximum Quantity and the Actual Quantity.

2.11 In-state Processing. Purchaser agrees that any and all of the Royalty Oil tendered under this Agreement shall be processed through Purchaser's refinery near Kenai,

Alaska, or shall be exchanged for other crude oil which shall be processed at that refinery. "Process" means producing oil products in significant quantities, but which quantities may be less than 32% of the volume of Royalty Oil tendered under this Agreement. "Exchange" means: (1) direct trades of equal volumes of crude oil; (2) trades of crude oil involving either cash or volume adjustments, or both, provided that those adjustments relate solely to quality or location differences; (3) sequential transactions in which Purchaser receives back crude oil from a party other than the party which receives the Royalty Oil in a trade from Purchaser; or (4) matching purchases and sales of crude oil. The terms under which Purchaser receives crude oil in any exchange shall not differ in any significant term from the terms under which Purchaser delivered Royalty Oil except for terms which adjust for differences in quality and location. Purchaser agrees that any trade or exchange shall not reduce the price to be paid to Seller and that trades or exchanges shall be at no cost or expense to Seller.

Purchaser's obligation to process Royalty Oil or exchanged oil in-state may only be suspended or excused under the provisions of Articles VIII and XI.

Seller may, at its option, waive the in-state processing requirement in whole or in part, if Seller is satisfied that Purchaser is using its best efforts to process the Royalty Oil tendered or the oil exchanged for Royalty Oil tendered under this Agreement at Purchaser's

refinery and that the waiver would not be contrary to the underlying intent of the other provisions of this Agreement.

2.12 Best Efforts. Purchaser agrees to use its best efforts to produce and market in Alaska an amount of crude oil products not less in volume than 32 percent of the Royalty Oil tendered under this Agreement. "Crude oil products" does not include residual fuel oil exported from Alaska unless the Commissioner, in his sole discretion, otherwise agrees, but does include bunker fuel loaded in Alaska. Purchaser also agrees to use its best efforts to nominate no more than that amount of Royalty Oil that will be necessary to produce and market crude oil products not less in volume than 32 percent of the Royalty Oil that will be tendered under this Agreement. On or before the 20th day after the end of each month of the term of this Agreement, the Purchaser shall provide to the Seller an affidavit certified by the Purchaser stating the quantity of crude oil products produced and marketed in the State of Alaska from in-state processing of the Daily Royalty Oil tendered under this Agreement.

A determination of "best efforts" under this Article shall include consideration of Purchaser's capabilities and the surrounding business circumstances. Purchaser's obligation to use its best efforts include reasonable, diligent, and good faith efforts, but shall not require Purchaser to produce and market crude oil products in Alaska at a loss. "Best efforts" would, however, require

Purchaser to produce and market products in Alaska even though Purchaser could make a greater profit by another disposition of the Royalty Oil or the products refined from that oil.

2.13 Future Dispositions of Royalty Oil. Seller recognizes that AS 38.05.183, which governs disposition of Royalty Oil by the State of Alaska, establishes a statutory preference for dispositions proposing (1) in-state processing of Royalty Oil and (2) in-state supply of products generated from processing of Royalty Oil, in that order. Seller represents that, in conjunction with future dispositions of Royalty Oil, Purchaser will be afforded the consideration contemplated by AS 38.05.183.

ARTICLE III

REPRESENTATION AND OBLIGATIONS OF PURCHASER

Purchaser warrants, represents, and agrees:

3.1 Good Standing and Due Authorization. Purchaser is, and at all times during the operation of this Agreement shall remain, a corporation qualified to do business in, and in good standing with, the State of Alaska. Purchaser has all necessary corporate power to enter into this Agreement and to perform its covenants and obligations under this Agreement. All necessary corporate action has been taken to authorize Purchaser's entering into this Agreement and performing its covenants and obligations under this Agreement.

3.2 Financial Condition. The financial information submitted to Seller is complete and correct and fairly presents Purchaser's financial condition at the time the information was submitted to Seller. The financial information was prepared in accordance with generally accepted accounting principles consistently applied. Since the date the information was submitted, the condition, business and properties of Purchaser have not been materially adversely affected in any way. Purchaser agrees to inform Seller immediately if during the term of this Agreement there is any material adverse change in the condition, business, or properties of Purchaser which would have an appreciable adverse effect on Purchaser's performance under this Agreement. Purchaser, in addition, will immediately inform Seller of any significant change in ownership of either the Purchaser or any of its affiliates or parent company, and of any change in Purchaser's operations or agreements which would appreciably affect Purchaser's performance under this Agreement.

3.3 Financial Statements. As soon as possible after the end of each fiscal year of Purchaser, and in any event within 120 days thereafter, Purchaser will furnish to Seller, at Purchaser's sole cost and expense, complete financial statements in the form filed with the Securities and Exchange Commission.

3.4 Expansion/Modification. Purchaser agrees, for so long as Purchaser, in its sole judgement, determines that

an expansion or modification of its in-state refining capacity is potentially viable for Purchaser, to conduct feasibility studies concerning the expansion or modification of its in-state refining capacity, including analysis of the various options for producing refined products and by-products, including petroleum coke. Purchaser shall report to Seller annually on the status of such studies.

3.5 Option to Purchase Resid. Subject to Purchaser's existing contracts, Purchaser grants to Seller an option to purchase all, or any quantity, of the residual oil ("resid") produced or refined from the Royalty Oil sold hereunder or the oil exchanged for the Royalty Oil. Seller shall exercise this option by giving Purchaser written notice nine (9) months in advance of purchase by Seller. The notice shall specify the quantity Seller will purchase. Thereafter Seller may increase, decrease, or terminate the quantity of resid by giving written notice nine (9) months in advance, and Seller may again, subject to Purchaser's existing contracts, commence purchases after having terminated such purchase by giving written notice nine (9) months in advance of Seller's purchase. Seller shall take the resid for a period of at least nine (9) months unless the Royalty Oil is run in Purchaser's refinery for a period of less than nine (9) months. In that case, Seller shall be obligated to purchase resid only for that shorter period of time.

This option shall remain in effect for the term of this Agreement. Failure to exercise this option for any period of time shall not affect Seller's right to exercise the option at a later time. This option, in whole or in part and for any term, shall be freely assignable by Seller and such assignment shall release Seller from all obligations to receive or pay for the resid sold under this option; provided, however, that Purchaser shall have the right to demand of an assignee of Seller reasonable security for the resid sold to that assignee. If authorized in an assignment by Seller, an assignee shall have the further right freely to assign that option, however, that assignment shall not release that assignee (or any subsequent assignee) of any responsibilities or liabilities to Purchaser unless agreed to by Purchaser in writing.

Seller shall pay the same price for resid as the highest price the Purchaser is offered for the same product from any other bona fide buyer of the resid. In the event Purchaser has no similar offer to buy from a bona fide buyer, the price shall be Purchaser's posted price for a like grade of resid in effect on date of loading at its Kenai, Alaska, refinery, provided, however, that at no time shall the price be more than the cost of the Royalty Oil purchased hereunder plus actual transportation cost to Kenai, Alaska. Purchaser shall have the right to supply a comparable or better quality of resid from any source, domestic or foreign, so long as the laid-in cost of the

resid at Seller's intended destination does not exceed the laid-in cost based upon Seller purchasing the resid at Kenai, Alaska.

3.6 Petroleum Coke. Purchaser agrees that if it modifies or expands its refinery at Kenai, Alaska so that the refinery is able to produce and handle petroleum coke, Purchaser will at that time enter into good faith negotiations with Seller for an option to purchase that petroleum coke.

ARTICLE IV

MEASUREMENTS AND TESTS

4.1 Measurement Standards and Procedures. The quantity and quality of the crude oil sold under this Agreement shall be determined at the Point of Delivery. Procedures and methods for measuring and metering the oil sold under this Agreement shall be in accordance with the practices then in effect at Prudhoe Bay, Alaska.

ARTICLE V

PAYMENTS AND ACCOUNTING

5.1 Billing. Seller will send to Purchaser, on or before the tenth (10th) business day of each month after delivery of Royalty Oil, an invoice statement of account of all Royalty Oil estimated to have been measured at the custody transfer meter into the Trans Alaska Pipeline System and tendered to Purchaser under this Agreement during the immediately preceding month according to the best information available to Seller, the estimated price or prices

applicable to those deliveries, and the total amount due ["initial billing"]. The estimates will be made by Seller according to the best information reasonably available to Seller. Seller may render its initial billing to Purchaser based in part upon information reported by the Lessees to Seller and information published by the U.S. government. Seller shall thereafter adjust its initial billing under this Article as soon as more accurate information concerning the quantity and price or prices of Royalty Oil delivered each month is available. Seller, however, shall not be required to adjust the initial billing prior to the sending of the next month's invoice statement of account.

5.2 Initial Adjustment. After the monthly invoice under Article 5.1, the subsequent monthly invoice will also state Seller's initial adjustments to be made, if any, to the invoice rendered in the immediately preceding calendar month, in accordance with any additional or more accurate information which may have become available to Seller. Whether or not initial adjustments are made, however, subsequent adjustments may be made under Article 5.5.

5.3 Payment. Purchaser will make payment of that amount billed under this Article within ten (10) days after receipt of the invoice statement of account. Payment shall be made without any deduction, set off, or withholding in immediately available funds to Seller at the following address:

Bank of America, NT & SA
San Francisco, California
Securities Department 3255
Credit to:

State of Alaska Investment Account

Payment may be made in such other manner or to such other address as Seller may specify in the invoice statement of account or by other written notice. All other payments to be made under this Agreement shall be paid in the same manner. If payment is due on a Saturday, Sunday, or legal holiday of the place where payment is to be received, payment shall be made on the next following business day. It is recognized that Seller may bill, and that Purchaser will pay, amounts that are based upon confidential information held or received by Seller. If confidential information is used as the basis for a billing, then upon request Seller will furnish Purchaser with the certified statement of the Commissioner that the amounts billed are correct based upon the best information available to Seller. Except for obvious clerical mistakes, if a dispute concerning a bill arises, it is agreed that Purchaser will pay the full amount billed by Seller pending final resolution of the dispute. Upon final resolution, the amount paid will be refunded to the Purchaser with interest, if such a refund is appropriate.

5.4 Payment to Lessee. Purchaser, at the request of Seller in the invoice statement of account or otherwise in writing, shall pay all or any portion designated by Seller of that payment required to be made to one or more of

the Lessees at an address or addresses and in the manner designated by Seller. The payment will be made within the time limit specified in Article 5.3. Seller may authorize and designate a third party to make the request and designate the amount, manner and place of payment under this provision. Unless otherwise specified, the balance of the payment due, if any, and payment for subsequent months, shall be made in accordance with Article 5.3.

5.5 Subsequent Adjustments. Purchaser acknowledges that more accurate information concerning the quantity of or Purchase Price for Royalty Oil tendered may subsequently become available to Seller. In the event that any such information should subsequently become available to Seller, Seller shall promptly furnish a corrected invoice statement of account to Purchaser and the parties will adjust the amount billed and pay or refund the amount of those adjustments.

In the event that Seller should render a corrected invoice to Purchaser, the parties will adjust the amount previously billed accordingly. Any amount to be refunded from Seller to Purchaser or paid from Purchaser to Seller will be paid within fifteen (15) days after the date of the corrected invoice. The time for paying an adjustment will be different, however, when the adjustment concerns an amount last invoiced more than sixty (60) days before the corrected invoice, in which case the amount will be paid by Purchaser or refunded by Seller, as the case may be, in

equal monthly installments over the same period of time as that over which the adjustment accrued or six (6) months, whichever is the shorter period. No adjustment will be made more than twelve (12) months after the date of the last original invoice to which the adjustment relates, except for adjustments resulting from (i) regulatory or court proceedings (including appeals) commenced or pending during that twelve (12) month period, whether or not Seller or Purchaser is a party to the proceeding, or (ii) bona fide audits by Seller of any Lessee(s) commencing at any time during the period six (6) years after the date of the last invoice to which such adjustment relates, or any resolution of disputes arising out of those audits. Adjustments due to audits or regulatory proceedings or court proceedings may be made at any time. The provisions of this Article 5.5 will survive any termination of this Agreement.

5.6 Interest. Except for adjustments made upon resolution of Amerada Hess under Article 2.3, the amount of all sums which are not paid when due under this Agreement or which are subsequently determined to be due under an adjustment under Article 5.5, or refunds, shall bear interest from the date accrued until paid in full at a variable rate per annum equal to the prime rate as announced from time to time by the Bank of America, San Francisco, California, plus one and one-quarter percent (1.25%) per annum.

5.7 Late Payment Penalty. Except for unintentional failures to pay, including clerical mistakes or

occurrences not within the reasonable control of Purchaser, or insignificant underpayments, if Purchaser fails to make payment within one day of the date that payment is due, then in addition to the amount due plus interest from the date that payment was due until the date of payment, Purchaser will pay an amount equal to one percent (1%) of the amount owed.

5.8 Payment to Third Parties. Seller may direct that Purchaser pay any amount due or which may become due directly to a third party in the manner and time as may be directed by Seller in written notice to the Purchaser if, in the Seller's sole discretion, the payment to the third party will assist Seller in monitoring or enforcing this Agreement.

ARTICLE VI

TERM

6.1 Term. This Agreement shall become effective upon execution by the parties and after enactment of legislation by the State of Alaska (including approval by the Governor) approving this Agreement. This Agreement shall be null and void if it is not so approved by September 1, 1982. Subject to the other provisions contained in this Agreement, Seller's obligation to sell and Purchaser's obligation to buy Royalty Oil shall begin seven (7) months after the above approval or January 1, 1983, whichever is later, and end January 1, 1995.

ARTICLE VII

DEFAULT OR TERMINATION

7.1 Default. If any one or more of the following events ("Events of Default") occur, then at Seller's option, Seller may terminate or suspend its obligation to tender and sell Royalty Oil and proceed to exercise any one or more of the rights and remedies provided in this Agreement:

(i) Except for obvious clerical errors, Purchaser does not pay in full any sum owed under this Agreement at the time when payment is due; or

(ii) Purchaser fails to observe or perform any of its other covenants and obligations under Article II; or

(iii) Purchaser does not perform any act required or contemplated under this Agreement and either: (a) the nonperformance continues for more than thirty (30) days after Seller has notified the Purchaser of Purchaser's nonperformance; or (b) Purchaser had failed to perform the same or any other act required or contemplated under this Agreement during the immediately preceding 12 month period; or

(iv) There is a material adverse change in Purchaser's condition, business or property which appreciably affects the ability of the Purchaser to perform any of its obligations under this Agreement, and Purchaser is unable to give Seller adequate assurance of continued performance either within fourteen (14) days of a request for such an assurance or within such other shorter time

period as Seller may reasonably request under the circumstances; or

(v) Any representation or warranty made by Purchaser in this Agreement proves to have been false or incorrect in any material respect at the time that the representation or warranty was made.

7.2 Failure to Pay Debts. If at any time Purchaser becomes unable to pay any of its debts when those debts are due, or should otherwise become insolvent (without regard to how that insolvency may be evidenced), Purchaser will immediately give notice of that fact to Seller. Whether or not that notice is given, if Purchaser becomes unable to pay any of its debts when those debts are due or should otherwise become insolvent, Seller's obligation to tender and sell Royalty Oil under this Agreement will automatically and immediately terminate without any requirement of notice or other action by Seller; however, Purchaser will nevertheless be and remain liable for payment and performance of all of its obligations and covenants under this Agreement with respect to Royalty Oil actually tendered by Seller to and after any such termination. Within thirty (30) days after receipt of Purchaser's notice or, if no notice is given, after Seller otherwise becomes aware (as determined in Seller's sole discretion) of Purchaser's insolvency, Seller will have the right, upon written notice to Purchaser, to reinstate all of Seller's and Buyer's

obligations under this Agreement retroactively to the date of termination.

7.3 Seller's Remedies. Upon the occurrence of any Event of Default or if Seller's obligation to tender and sell Royalty Oil under this Agreement is terminated or suspended under Article 7.1 and 7.2, all obligations of Purchaser accrued but not otherwise due and payable under this Agreement will immediately be due and payable in full. In addition, Purchaser will indemnify and hold Seller harmless from and against all other liability, damages (including reasonably foreseeable consequential damages), costs, losses and expenses (including reasonable attorneys' fees and disbursements) incurred by Seller and arising out of the Event of Default, termination, or suspension. Seller shall have the right cumulatively to exercise any and all other rights and remedies and to obtain all other relief available under applicable law or at equity, including mandatory injunction and specific performance. The Seller, upon occurrence of any Event of Default, in its sole discretion, may arrange for any disposition to third parties of Royalty Oil to be tendered and sold under this Agreement. Upon the occurrence of any Event of Default, the Purchaser is released from the obligations set forth in Articles 2.11 (In-State Processing) and 2.12 (Best Efforts) until the Event of Default no longer exists or the obligation of the Purchaser to take Royalty Oil under this Agreement expires. If upon occurrence of any Event of Default the Seller makes

arrangement for disposition to third parties of Royalty Oil or if the Purchaser is released from Articles 2.11 and 2.12, whether or not this Agreement is terminated, Purchaser will nevertheless be and remain liable to Seller for the full amount of the Purchase Price for that Royalty Oil in excess of the Purchase Price over any amount or amounts received by Seller on account of that disposition, net of the expenses of that disposition and for all other costs, expenses (including reasonable attorneys' fees and disbursements), damages (including reasonably foreseeable consequential damages) and losses incurred by Seller and arising out of the Event of Default or disposition.

7.4 Purchaser's Exclusive Remedies. Upon any breach of, or default in, the due and timely observance or performance of any of Seller's covenants or obligations under this Agreement, Purchaser acknowledges and agrees that Purchaser's remedies will not include a temporary restraining order or preliminary injunction preventing Seller from taking any action with regard to the Royalty Oil sold under the Agreement.

ARTICLE VIII

DISPOSITION OF OIL

8.1 Disposition of Oil Upon Default or Termination. Purchaser acknowledges and agrees that under the Unit Agreement and Leases Seller's election to take Royalty Oil in-kind can be revoked or reversed only upon the satisfaction of various conditions, including the giving of six (6)

months notice to return all or more than ten percent (10%) of Seller's then current nominations. Purchaser acknowledges and agrees that Seller's election to invoke its rights to return to taking its Royalty Oil in value on less than six (6) months notice, or to attempt to secure a waiver of any condition or requirement, is at Seller's sole and complete discretion. Notwithstanding termination of this Agreement for default or for any other reason, including expiration or termination under any provision contained in this Agreement, Purchaser shall continue to take and purchase Seller's Royalty Oil in the amount and for the price set forth in this Agreement for up to seven (7) months following termination of this Agreement if Seller, in its discretion, so requires.

8.2 Inability to Receive Oil. If for any reason Purchaser is unable or refuses to accept or receive any Royalty Oil tendered under this Agreement, Purchaser shall nevertheless be and remain responsible for the disposal of that Royalty Oil and for paying the Seller for the oil as though it had been received and accepted by Purchaser unless Seller, in its sole discretion, elects to waive this requirement.

8.3 No Right to Storage or Underlift. Purchaser waives and disclaims any interest or right that it may assert to storage of Royalty Oil, including by underlift or other means, to which Seller is or may come to be entitled under the Leases or any other agreement.

ARTICLE IX

WAIVER

9.1 Waiver. The failure of either party to insist upon strict performance of any provision of this Agreement shall not constitute a waiver of, or estoppel against, asserting the right to require that performance in the future. A waiver or estoppel in any one instance shall not constitute a waiver or estoppel with respect to a later breach of a similar nature or otherwise. A course of performance established by a party shall also not estop the other party from complaining of a later breach similar in nature.

ARTICLE X

VALIDITY

10.1 Validity. If any provision or clause of this Agreement or application of this Agreement to any person or circumstance is held invalid, that invalidity shall not affect other provisions or applications of this Agreement which can be given effect without the invalid provision or application. If, however, an invalidity should operate to impair any material right or remedy of a party to this Agreement, that party may terminate this Agreement by notice to the other.

ARTICLE XI

FORCE MAJEURE AND CHANGE IN CONDITION

11.1 Effect of Force Majeure. Except for

Purchaser's obligations to make payment of money for Royalty Oil tendered under this Agreement and except for Purchaser's obligations to accept and dispose of Royalty Oil, neither party shall be liable for any failure to perform the terms of this Agreement when the failure is due in whole or in substantial part to force majeure. The term "force majeure" as applied to this Agreement shall mean acts of God, strikes, lockouts and industrial disputes or disturbances, civil disturbances, arrests and restraints from rulers or people, interruptions by government or court orders or by present or future orders of any regulatory body having or asserting jurisdiction, acts of the public enemy, wars, riots, blockades, insurrections, inability to secure materials by reasons of allocations promulgated by authorized governmental agencies, epidemics, landslides, lightning, earthquakes, fires, storms, floods, washouts, explosions, breakage or accident to machinery or lines of pipe, freezing of wells or pipelines, or any other event or condition, whether of the kind herein enumerated or otherwise, not within the reasonable control of the party claiming the benefit of this excuse. If, however, any material obligation of Purchaser is excused or suspended because of a claim of force majeure for a period of 365 successive days or more, Seller will have the right to terminate this Agreement. Prior to the Seller exercising its right to terminate this Agreement the Seller and Purchaser shall enter into good faith negotiations to restore, to the

fullest extent possible, the Seller and Purchaser to the benefits and obligations that existed under this Agreement before the occurrence of the force majeure condition.

11.2 Responsibility. Upon the occurrence and discovery of an event providing the basis for a claim of force majeure, the party making a claim shall notify the other party to this Agreement of its claim of force majeure. Upon the occurrence of an event constituting force majeure that event shall, so far as possible, be remedied with all reasonable diligence and dispatch. Except for Purchaser's obligations to make payment of money for Royalty Oil tendered under this Agreement and except for Purchaser's obligation to dispose of Royalty Oil, the obligations of the disabled party to perform under this Agreement, insofar as they are affected by that force majeure, shall be suspended from the time that force majeure occurs and for so long as the disability caused should have continued had the party claiming the existence of the force majeure had remedied the event providing the basis of the claim of force majeure with reasonable diligence and dispatch, and for no longer. The settlement of strikes or lockouts or industrial disputes or disturbances will be entirely within the discretion of the party having the difficulty, and the above requirement that any force majeure shall be remedied with diligence and dispatch shall not require the settlement of strikes, lockouts, or industrial disturbances by acceding to the

demands of any opposing party therein when such course is inadvisable in the sole discretion of the disabled party.

ARTICLE XII

NOTICES

12.1 Method. All notices, requests, demands or statements shall be in writing, and may be delivered personally to the party to be notified or may be sent by registered or certified United States mail, postage prepaid, with a return receipt requested to such party. Notice deposited in the mail in this manner shall be effective upon the expiration of seven (7) days after it is so deposited. Notice given in any other manner shall be effective only if and when received by the addressee. For the purposes of notice the addresses of the parties to this Agreement shall be as follows:

If to Seller: State of Alaska
 Commissioner of Natural Resources
 Pouch "M"
 Juneau, Alaska 99811

and

 Commissioner of Revenue
 Pouch "S"
 Juneau, Alaska 99811

and

 Director, Division of Minerals
 and Energy Management
 555 Cordova Street
 Anchorage, Alaska 99501

If to Purchaser:

Tesoro Alaska Petroleum Company
8700 Tesoro Drive
P.O. Box 17536
San Antonio, Texas 78286

12.2 Change of Address. Each party may change its address for notice by giving notice of the change.

ARTICLE XII

RULES AND REGULATIONS

13.1 Rules and Regulations. This Agreement is subject to all present and future valid laws, orders, rules and regulations of the United States, the State of Alaska, and any duly constituted agency thereof.

ARTICLE XIV

SOVEREIGN POWER OF THE STATE

14.1 Sovereign Power of the State. This Agreement and its covenants shall not be interpreted as a limit on the exercise by the State of Alaska of any of its sovereign or regulatory powers, whether conferred on the State by constitution, statute or regulation, including but not limited to, its regulatory power over the Leases. The exercise by the State of Alaska of any sovereign or regulatory power will not operate or be deemed to enlarge any rights of Purchaser or to limit or impair any obligations or liability of Purchaser under this Agreement except for state statutes enacted after the effective date of this Agreement which have a direct and significant adverse affect on the ability of Purchaser to perform an obligation under this Agreement

other than the obligations to accept, dispose, and pay for Royalty Oil tendered under this Agreement.

ARTICLE XV

SECURITY

15.1 Letter of Credit. At least ninety (90) days before the Date of First Delivery, unless waived by Seller, Purchaser shall cause to be furnished to Seller an irrevocable stand-by letter of credit for the benefit of Seller, issued by a state or national banking institution of the United State which is a member of the Federal Deposit Insurance Corporation and has an aggregate capital and surplus of not less than \$100,000,000, or other banking institution acceptable to Seller in its sole discretion. The principle face amount of the letter of credit shall initially be \$48,000,000. The letter of credit shall be substantially in a form satisfactory to the Commissioner, but in any event shall not require any documents to be submitted in support of drafts drawn against this letter of credit other than the certified statement of the Commissioner or his designee and the Attorney General of the State of Alaska or his designee that Purchaser is liable to Seller for a sum equal to the amount of such draft, and that that sum is due and payable in full and has not been timely paid. In the event that Seller should have reasonable grounds for asserting any claims against Puchaser under this Agreement and does assert those claims in an aggregate amount in excess of the aggregate principal face amount of the letter

of credit then in effect, Purchaser shall upon Seller's request (whether or not Purchaser may deny, reject or otherwise resist such claims) cause the principal face amount of the letter of credit to be increased by an amount equal to the excess. The principal face amount of the letter of credit shall also be automatically increased by Purchaser without request from Seller whenever the face amount is less than the expected Purchase Price of sixty (60) days of Royalty Oil tenders under this Agreement, to an amount equal to the expected Purchase Price of sixty (60) days of Royalty Oil tenders. The principal face amount of the letter of credit may be decreased by Purchaser upon approval of Seller if the face amount is less than the expected Purchase Price of sixty (60) days of Royalty Oil tenders under this Agreement, to an amount equal to the expected Purchase Price of sixty (60) days of Royalty Oil tenders. The Commissioner may accept such other or additional security as he, in his sole discretion, considers adequate to protect Seller.

ARTICLE XVI

PREFERENTIAL HIRING AND NON-DISCRIMINATION

16.1 Compliance with Alaska Law. Purchaser will comply with all applicable Alaska statutes and regulations in effect at the time this Agreement becomes effective, as well as all amendments to them and subsequent enactments, providing for preferential hiring of Alaska residents and non-discrimination against them.

16.2 Preference to Qualified Alaska Residents. To the extent not superceded by or inconsistent with subsequently enacted legislation or regulations, Purchaser will use its best efforts to assure that work done by or for it within the State of Alaska in connection with this Agreement shall, to the extent they are available, willing and qualified, be performed by Alaska residents who, at the time of their initial employment by Purchaser, its contractors or subcontractors, fall within one or more of the following employment target groups, as determined by the State or an agency or agencies designated by the State:

(1) "chronically unemployed resident," defined as either:

(A) a resident who has been unemployed for a minimum of eight (8) months, cumulatively, of the twelve (12) months immediately preceding the time of application for determination of status, so long as the individual's income for the 12-month period does not exceed \$25,000; or

(B) a resident who has exhausted benefits available under the Alaska Employment Security Act, AS 23.20, within the (twelve) 12 months immediately preceding the time at which he makes the application for certification and is currently not eligible for unemployment benefits;

(2) "economically disadvantaged resident," defined as a resident whose total household income for the twelve (12) months immediately preceding the time of application for determination of status falls below seventy percent

(70%) of the minimums set by the U.S. Bureau of Labor Statistics "lower living standard income level" as adjusted for Alaska; and

(3) "training-qualified resident," defined as a resident who, within the twelve (12) months immediately preceding the time of application for determination of status, has successfully completed a program of job training designed to qualify the resident for employment on projects carried out in connection with this agreement.

16.3 Assurance of Compliance. Purchaser shall use its best efforts to assure that neither it, nor its contractors and subcontractors, hire nonresidents when residents falling within one or more of the employment target groups set out in Article 16.2 are known to be available, willing and qualified for employment for work performed in connection with this Agreement within the State of Alaska.

16.4 Exceptions. The requirements of this Article do not apply to bona fide administrative, executive or professional employees of the Purchaser or its contractors or subcontractors, as those terms are defined in 8 AAC 15.910.

16.5 Collective Bargaining Agreements. In implementing the requirements of this Article, Purchaser shall assure that it and its contractors and subcontractors use their best efforts to include in all collective bargaining agreements with labor unions covering work to be performed in connection with this Agreement provisions that will

assure employment preference to Alaska residents falling within the target groups set out in Article 16.2 in accordance with the requirements of this Article.

16.6 Non-discrimination. Purchaser shall assure that neither it nor its contractors or subcontractors engage in discriminatory practices against Alaska residents falling within the employment target groups set out in Article 16.2 who are employed or seeking employment by Purchaser or its contractors or subcontractors. Prohibited discriminatory practices include, but are not necessarily limited to:

(1) rejection of a resident referred to an employer by a collective bargaining agent in favor of a nonresident of similar qualifications in employment covered by a collective bargaining agreement;

(2) rejection of a resident in favor of a nonresident of similar qualifications in employment not covered by a collective bargaining agreement;

(3) termination of a resident in favor of a nonresident of similar qualifications; and

(4) differentiation in payment of wages, salaries, fringe benefits, and working conditions between a resident and nonresident.

16.7 Definitions. In this Article,

(1) "qualified" means able, by education, training and experience or combinations of them, to perform the duties and satisfy the terms and conditions which are usual in the offered employment, provided that the duties, terms

and conditions meet the reasonable standards of the industry as required of other employees performing the same type of work in the industry; and

(2) "resident" means a person who

(A) except for brief intervals, military service, attendance at an educational or training institution, or for absences for good cause, is physically present in the state for a period of at least 30 days immediately before the time that person's status is determined;

(B) maintains a place of residence in the state;

(C) has established residency for voting purposes in the state;

(D) has not, within the period of required residency, claimed residency in another state; and

(E) shows by all attending circumstances that that person's intent is to make Alaska his or her permanent residence.

ARTICLE XVII

APPLICABLE LAW

17.1 Alaska Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Alaska, excluding any conflict-of-law rule or principle which might refer such construction to the laws of another state or country.

17.2 Submission to Jurisdiction. Any legal action or proceeding arising out of or relating to this Agreement or for the enforcement of the covenants or obligation of either party must be instituted in a State court of general jurisdiction sitting in the State of Alaska, and Purchaser hereby irrevocably submits to the jurisdiction of that court in any such action or proceeding.

ARTICLE XIII

WARRANTIES

18.1 No Warranties. The purchase and sale of Royalty Oil under this Agreement is subject only to the warranties of Seller expressly set forth in this Agreement and Seller disclaims and Purchaser waives all other warranties, express or implied in law, whatsoever.

ARTICLE XIX

AMENDMENT

19.1 Amendment. This Agreement may be supplemented, amended or modified at any time, but only by written instrument duly executed by the parties to this Agreement. In addition, material amendments to this Agreement which appreciably reduce the consideration to Seller must be approved by the Legislature of the State of Alaska.

ARTICLE XX

SUCCESSORS AND ASSIGNS

20.1 General Prohibition. No assignment, pledge or encumbrance of this Agreement shall be made by either party without first obtaining the written consent of the

other party. The Commissioner may grant such consent on behalf of the Seller. The Commissioner shall have sole and complete discretion in granting or denying a proposed assignment, pledge or encumbrance. Subject to the above requirements in this Article, this Agreement will be binding upon and inure to the benefit of each of the parties and its successors and permitted assigns. In addition, if Purchaser gains or acquires a controlling interest in an entity which has an agreement with Seller for the sale of Royalty Oil ("Other Agreement"), then upon at least one year's notice Seller, at its option may require Purchaser to terminate either this Agreement or the Other Agreement. The choice of which Agreement to terminate will be Purchaser's. Purchaser may request that Seller waive this option in advance of Purchaser gaining a controlling interest in an entity which has an agreement with Seller for the sale of Royalty Oil. The Commissioner has sole and complete discretion in granting or denying the requested waiver.

ARTICLE XXI

HEADINGS

21.1 Headings. Headings used in this Agreement are for convenience only and shall not affect the construction of this Agreement.

ARTICLE XXII

RECORDS

22.1 Preservation of Records. Purchaser will

preserve and maintain all books, accounts, and records relating to or arising out of the performance of this Agreement, including but not limited to the purchase or sale of Royalty Oil and its refined products, for a period of six (6) years. Purchaser will also maintain and preserve all similar books, accounts, and records of which it has possession belonging to those third parties with whom it contracts for the performance of various parts of this Agreement. Neither Purchaser nor Seller shall be required to retain any records for more than six (6) years unless retention of such records is specifically required by applicable law or regulation. Purchaser shall either maintain its records within the State of Alaska or make such records available to Seller at Purchaser's principal office in the State of Alaska within thirty (30) days after written request by Seller.

22.2 Inspection of Records of Parties. Purchaser and Seller will accord to each other and to their authorized agents, attorneys, and auditors during reasonable business hours access to any and all property, records, books, documents, and indexes directly relating to the Purchaser's or Seller's performance of this Agreement and which are under the control of the party from which access is desired so that the other party may inspect, photograph and make copies of that property, records, books, documents and indexes. In no event, however, shall Seller be required to disclose any information, data, or records which are

required to be held confidential by state law or regulation. If the information obtained by Seller may be held confidential under state or federal law or regulation, Purchaser may request that that information be held confidential by Seller.

ARTICLE XXIII


INTERPRETATION OF TERMS AND CONDITIONS

23.1 Commissioner finding and review. In the event that there is a disagreement about the meaning or application of a word, term, or condition in this Agreement, Purchaser will present the arguments supporting its view in writing to the Commissioner for his consideration. The Commissioner will subsequently, within a reasonable time, issue a finding on the meaning or application of the disputed word, term, or condition, and setting forth the basis for his conclusions. Purchaser agrees to accept findings by the Commissioner under this Article as long as there is substantial evidence supporting the Commissioner's findings.

DATED this 26 day of February, 1982.

SELLER:

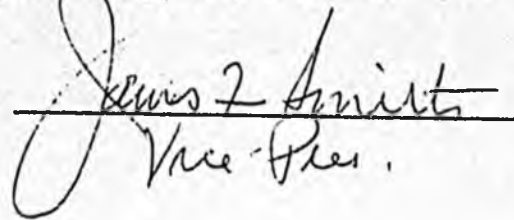
THE STATE OF ALASKA

 _____
Department of Natural Resources

PURCHASER:

Esso-Alaska Petroleum Company

By:


Vice Pres.



ALASKA OIL & GAS BOARD

SENATE RESOURCES COMMITTEE
LEGISLATION CHECKLIST

SB 881

BILL NUMBER _____

IDENTIFICATION:

BILL NAME: "An Act relating to the sale of royalty oil by the State of Alaska to the Tesoro Alaska Petroleum Company; and providing for an effective date."

SPONSOR(S): Rules (Governor's request)

RELATED BILLS PENDING:

DATE INTRODUCED: 3/29/82

REFERRALS

Resources
Finance

INITIAL RESEARCH:

INITIAL BILL SUMMARY COMPLETED

SUMMARY BY LEGAL DIVISION:
DEPT. OF LAW SUMMARY:

SPONSOR CONTACTED FOR BACKUP
MATERIALS:

FISCAL NOTE:

AGENCY RESPONSE:

OTHER INTERESTED SENATORS OR
REPS. NOTIFIED:

BACKGROUND RESEARCH:

SIMILAR BILLS INTRODUCED IN PREVIOUS LEGISLATURES:

RESPONSES FROM INTERESTED PERSONS AND/OR GROUPS:

OTHER STATE OR FEDERAL PRECEDENTS, REGULATIONS, LAWS:

HEARING PREPARATION:

CHAIRMAN BRIEFED:

DATE AND PLACE SET:

STAFF MEMO TO COMMITTEE:

TELECONFERENCE

BACKGROUND MATERIAL DISTRIBUTED

PSA/PRESS RELEASE

LIST OF WITNESSES:

SUGGESTED AMENDMENTS/CS DRAFTED:

Cliff Groh - Attorney for Tesoro - Notified



Alaska State Legislature

SENATE Resources Committee

Official Business

BETTYE FAHRENKAMP, Chairman
VIC FISCHER, Vice-Chairman
BRAD BRADLEY
DICK ELIASON
DON GILMAN
BOB MULCAHY
ARLISS STURGULEWSKI

POUCH V
STATE CAPITOL
JUNEAU, ALASKA 99811
(907) 465-3834
(907) 465-3835

TO: Senate Resources Committee
FROM: Senate Resources Committee Staff
RE: Committee Meeting, 4/7/82
DATE: April 5, 1982

Please find attached background information for
Wednesday's hearing on the following bills:

SSSB 796 TELECONFERENCE 1:30 -3:00 p.m.
Providing for the management of state owned
land in the Haines area, establishing the
Alaska Chilkat Bald Eagle Preserve and the
Haines State Forest Resource Management Area.

3:00 - 4:00 p.m.
SB 880 Sale of royalty oil by the State of Alaska
to Doyon, Ltd.

SB 881 Sale of royalty oil by the State of Alaska
to Tesoro Alaska Petroleum.

The meeting will be held in the Beltz Room.

TESORO ALASKA PETROLEUM COMPANY

- 2.1 QUANTITY: 24.533% of the daily royalty oil less Cook Inlet oil. 46,000 B/D deducted from this amount is an amount of Cook Inlet royalty Tesoro receives from its existing contract with the State.
- 2.3 PRICE OF OIL: In-value price.
- 2.4 POINT OF DELIVERY: Pump Station #1
- 2.5 PASSAGE OF TITLE: Title passes at point of delivery.
- 2.6 PURCHASERS RESPONSIBILITY: Purchaser responsible after passage of title.
- 2.7 TRANSPORTATION: Sole responsibility of purchaser.
- 2.9 DATE OF FIRST DELIVERY: January 1, 1983
- 2.10 RESERVATION FEE: Tesoro may vary the volume taken up to the maximum, but must pay fee on portion unused.
- 2.11 IN-STATE PROCESSING: Purchaser agrees all royalty oil processed through refinery near Kenai or exchanged for other crude which shall be processed through refinery at Kenai.
- 2.12 BEST EFFORTS: Purchaser agrees to produce and market in Alaska an amount of product not less than 32% of royalty oil tendered.
- 2.13 FUTURE DISPOSITION OF OIL: AS 38.05.183 will govern.
- 3.1 GOOD STANDING: Purchaser agrees to remain qualified to do business in the state of Alaska.
- 3.2-3.4 FINANCIAL CONDITION, FINANCIAL STATEMENTS, AND EXPANSION CLAUSES: Standard boiler type.
- 3.5 OPTION TO PURCHASE RESIDUAL: Purchaser grants to seller an option to purchase all or any quantity of residual oil produced or refined from the royalty oil.
- 3.6 PETROLEUM COKE: Purchaser agrees that if it modifies or expands its Kenai refinery to produce petroleum coke, State has option to buy.

ARTICLE V BILLING, ADJUSTMENT, PAYMENT: Standard clauses.

5.6 INTEREST: Adjustments due or owing upon resolution of
Amerada Hess shall bear interest equal to prime rate
(Bank of America) plus 1.25%.

6.1 TERM: 12 years, expire January 1, 1995

ARTICLE VII DEFAULT, FAILURE TO PAY DEBTS: Standard contract clauses.

15.1 LETTER OF CREDIT: Irrevocable stand by letter of credit.
Principle face amount \$48,000,000 (60 days of royalty
oil). Face amount may be adjusted.

ARTICLE XVI PREFERENTIAL HIRING AND NONDISCRIMINATION: Standard
clauses.