

SB 4418

SENATE FINANCE COMMITTEE REPORT

DATE: 3/27/92

FURTHER:

DATE TURNED INTO OFFICE: 4-16-92

The Finance Committee considered SENATE BILL NO. 448

"An Act approving the sale of Kuparuk River Unit royalty oil by the State of Alaska to Petro Star Valdez Refinery Joint Venture; and providing for an effective date."

and recommends:

- replace with _____ CS _____ (FINANCE)
- or adopt previous _____ CS _____
- attaches amendment(s)

- same title
- new title
- technical title change (HB only)

adopts _____ Letter of Intent

further referral to the _____

do pass

do not pass

no recommendation

individual recommendations

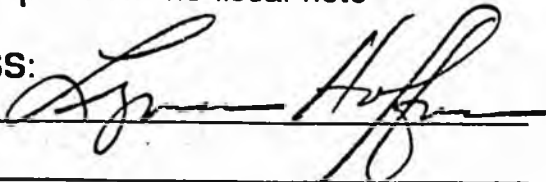
NEW FISCAL NOTES: Dept/Date

zero fiscal notes _____

fiscal notes _____

appropriation--no fiscal note

DO PASS:



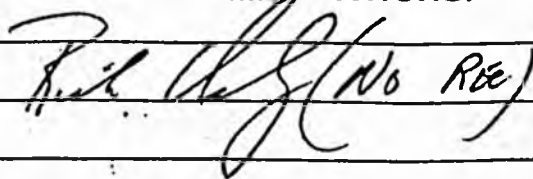
PREVIOUS FISCAL NOTES: Dept/Date

zero fiscal notes DNR 2-27-92

DNR 2-27-92

fiscal notes _____

OTHER RECOMMENDATIONS:

 (No Rec)

1. 

Co-Chair: Signature/Recommendation

2.  Do pass

Co-Chair: Signature/Recommendation

FISCAL NOTE

No. 1

Bill Version: SR 448

(S) Publish Date: 3-11-92

STATE OF ALASKA
1992 LEGISLATIVE SESSION

Revision Date: _____ Department Affected: Natural Resources

Title: Petro Star Royalty Oil Contract BRU: Petroleum Management

Component: Petroleum Management

Sponsor: Rules Committee for Governor

Requestor: _____ COMPONENT SERIAL NO.

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EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	-0-	-0-	-0-	-0-	-0-	-0-
TRAVEL	-0-	-0-	0	0	0	-0-
CONTRACTUAL	-0-	-0-	-0-	-0-	-0-	-0-
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	0

CAPITAL						
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REVENUE						
FUND SOURCE:						

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
FUND SOURCE:						
TOTAL	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

Division of Oil and Gas staff handles a number of royalty-in-kind contracts. Existing staff will handle the proposed contract with Petro Star Valdez Refinery Joint Venture.

Prepared By: Bob Loeffler Phone: 762-2578

Division: Oil and Gas Date: 2-27-92

Approved by Commissioner: Harold C. Heinze

Agency: Natural Resources Date: 2-27-92

FISCAL NOTE

No. 2

Bill Version: SB 448

(S) Publish Date: 3-11-92

STATE OF ALASKA
1992 LEGISLATIVE SESSION

Revision Date: _____
Title: Approving the Sale of Kuparuk River Unit Royalty
Oil by the State of Alaska to Petro Star Valdez Refinery

Department Affected: Revenue
BRU: Revenue Operations
Component: Oil & Gas Audit

Sponsor: _____
Requestor: _____

Component Serial No.

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Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL						
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REVENUE FUND SOURCE						
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FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER FUND SOURCE						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS:

Prepared by: Robert L. Doss, Director

Phone: 276-1363 ext. 225

Division: Oil & Gas Audit Division

Date: Feb. 27, 1992

Approved by Commissioner: *David Axelrod*

Agency: Revenue

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

SENATE BILL NO. 448

IN THE LEGISLATURE OF THE STATE OF ALASKA

SEVENTEENTH LEGISLATURE - SECOND SESSION

BY THE SENATE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

Introduced: 3/11/92
Referred: O&G, RES, FIN

A BILL

FOR AN ACT ENTITLED

1 "An Act approving the sale of Kuparuk River Unit royalty oil by the State of Alaska
2 to Petro Star Valdez Refinery Joint Venture; and providing for an effective date."

3 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

4 * Section 1. The March 4, 1992 "Agreement for the Sale and Purchase of State Royalty Oil" between
5 the State of Alaska and Petro Star Valdez Refinery Joint Venture, for the sale of Kuparuk River Unit
6 royalty oil, is approved and ratified.

7 * Sec. 2. This Act takes effect immediately under AS 01.10.070(c).

WALTER J. HICKEL
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

March 11, 1992

The Honorable Richard I. Eliason
President of the Senate
Alaska State Legislature
State Capitol
Juneau, AK 99801-1182

Dear President Eliason:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill that provides for legislative approval of a royalty oil contract between the state and Petro Star Valdez Refinery Joint Venture for the sale of Kuparuk River Unit royalty oil. Also transmitted with this bill is a copy of the resolution of the Alaska Royalty Oil and Gas Development Advisory Board recommending approval of that contract in accordance with AS 38.06.040(a)(3) and 38.06.050(a), and providing the report required by AS 38.06.070(c).

The contract is also described in the finding issued by the Commissioner of Department of Natural Resources on March 4, 1992. Copies of the Commissioner's preliminary finding and the draft contract have been sent to the Legislature and made available to the public for review. The Commissioner's final finding and the signed contract are attached.

A bill approving the contract is being introduced for legislative approval for two reasons. First, as a matter of comity, I respect the Legislature's desire to have a direct voice in major disposals of royalty oil. Therefore, although this and previous Administrations have consistently taken the position that the statutory requirement of legislative approval of royalty oil contracts (AS 38.06.055) is unconstitutional, the contract itself contains provisions requiring approval by the Legislature before it takes effect.

Second, this legislation would ratify the royalty oil contract. This ratification would cure any procedural defect that might have occurred in the process of entering into this contract.

I urge your prompt consideration and passage of this bill.

Sincerely,

A handwritten signature in cursive script that reads "Walter J. Hickel".

Walter J. Hickel
Governor

The Alaska Royalty Oil and Gas Development Advisory Board

Resolution 92-1

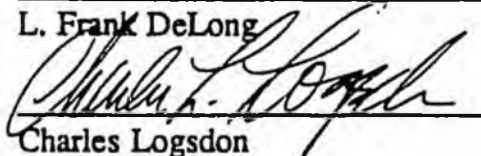
On January 23, 1992, the director of the division of oil and gas ("director") provided the Alaska Royalty Oil and Gas Development Advisory Board ("board") with preliminary findings and proposed contract for a long-term sale of up to about 30,000 barrels per day of Kuparuk River Unit royalty oil to Petro Star Valdez Refinery Joint Venture, a joint venture comprised of Petro Star Valdez, Inc., (a subsidiary of Arctic Slope Regional Corporation), Harbor Enterprises, Inc., and Alaska Refining, Inc. (collectively "joint venture"). The joint venture will process the oil in a refinery proposed for Valdez.

The proposed contract was discussed between representatives of the division of oil and gas (DOG) and the joint venture over the past year culminating in a draft contract. On January 23, 1992, the director made public the proposed contract and the Preliminary Finding and determination of the Commissioner of the Department of Natural Resources. The director notified the public that the proposed sale would be discussed at the board's meeting on February 6, 1992 and invited them to attend.

On February 6, 1992, the board met to discuss the sale and to take public comment on it. The meeting was attended by representatives of the DOG, representatives of the joint venture, and members of the public. The board received a presentation from the DOG staff regarding the proposed sale and contract, questioned the staff about them, and made several suggestions. The staff will implement those suggestions. At the conclusion of the discussion, the voting members of the board, who attended the meeting, unanimously approved the proposed sale and recommended that the proposed contract be approved by the legislature.

Based on the board's review of the contract for the sale and purchase of royalty oil between the State of Alaska and the joint venture, the Commissioner's findings and determinations regarding the proposed sale, and the information presented at public meeting of the board, the board is of the opinion that the proposed disposition of Kuparuk River Unit royalty oil to the joint venture meets the requirements of AS 38.06 and 11 AAC 26. The board adopts the Commissioner's finding and determinations, and recommends that the Seventeenth Alaska Legislature approve the agreement for the sale and purchase of royalty oil from the Kuparuk River Unit to Petro Star Valdez Refinery Joint Venture.

L. Frank DeLong



Charles Logsdon

Glenn A. Olds

The Alaska Royalty Oil and Gas Development Advisory Board

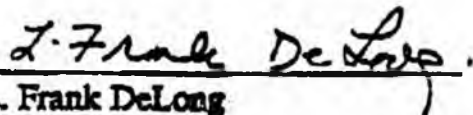
Resolution 92-1

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L. Frank DeLong

Charles Logsdon

Glenn A. Olds

SUMMARY OF PROPOSED PETRO STAR CONTRACT

THE REFINERY

- 30,000 barrel per day refinery to be built on private land in Valdez.
- Expected products, approximately 110 million gallons per year (¼ of the purchased oil volume):
 - at least 20 million gallons per year of jet fuel for Mark Air;
 - approximately 10 million gallons per year heating fuel and marine diesel, available in Valdez for Prince William Sound consumers; and
 - the balance will be marine diesel sold to Petro Marine Services, a marine fuel distributor servicing south central Alaska. Most of this fuel will be sold in Seward, Kodiak, and Dutch Harbor.
- \$30 million capital investment; \$25 million of which will be in Alaska. 16-20 permanent jobs with an annual payroll of approximately \$1.7 million. Approximately \$400,000 per year in property taxes.
- Construction could start as early as this spring; operation, as early as next winter.

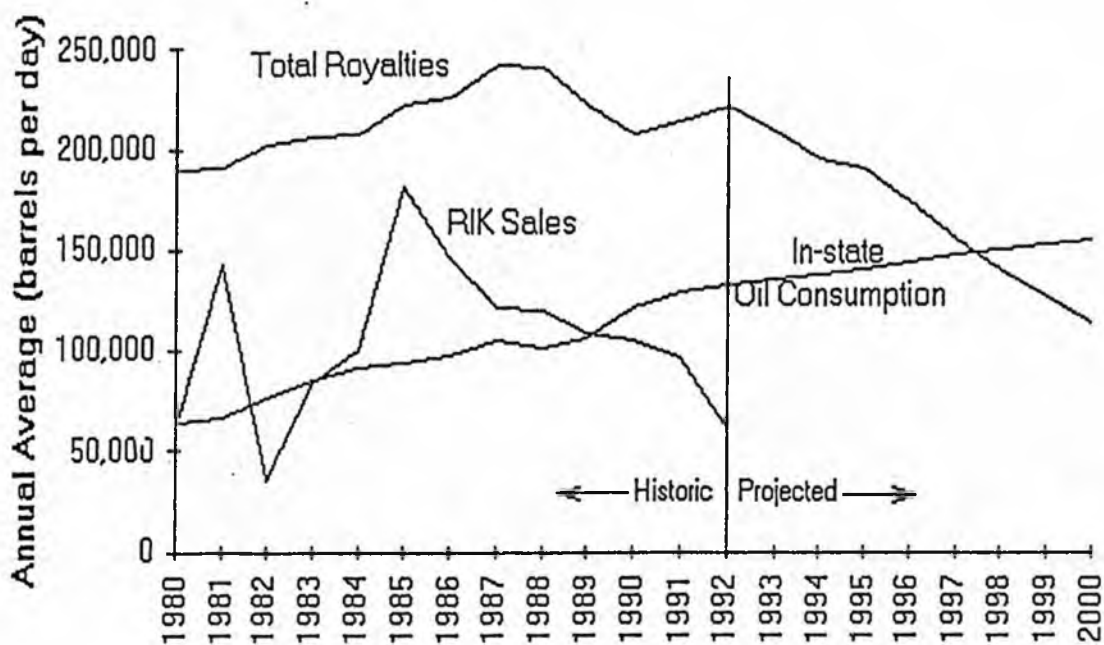
SALE OF IN-KIND ROYALTY OIL

- 30,000 barrels per day from the Kuparuk River Unit (approximately 80% of Kuparuk's Royalty Oil); amount is expressed as a percentage of production, and will decline as Kuparuk production declines.
- 10-year contract beginning seven months after the legislature approves the sale, or when the refinery is ready to process the oil (whichever is later).
- Price would be the weighted-average per-barrel value paid to the state by ARCO and BP. These two companies own approximately 95% of production from the Kuparuk field.

WHO IS PETRO STAR VALDEZ REFINERY JOINT VENTURE? A joint venture of three Alaskan Companies:

- Petro Star Valdez Inc, a subsidiary of the Arctic Slope Regional Corporation;
- Alaska Refinery Inc, a wholly owned subsidiary of Neil Bergt Trust; and
- Harbor Enterprises which operates Petro Star Marine Services.

Consumption, Royalties, and Sales



Recent Developments: Cancelled Contracts

Comparison of recent with last summer's deliveries
(Figures in barrels/day)

	Jul-91	Feb-92	Date of Last Delivery
GVEA	4,610	0	Jan. 31, 1992
Chevron	21,145	0	Larger contract: August 31, 1991; Chevron-Petro Star contract: December 31, 1992
Petro-Star	2,864	0	December 31, 1991
Mapco	29,082	19,459	Continuing (Contract expires 2004)
Tesoro	50,817	41,184	Continuing (Contract expires 1995)
Total	108,517	60,642	
Avail Royalties:	210,990	204,404	

SUMMARY OF DIFFERENCES
Between
PROPOSED AND TYPICAL PREVIOUS CONTRACTS

PRICE TERM, *Previous Contracts.* Price = (RIV weighted-average netback value) + (Field Cost). Interim price is the producer-reported price with provision for retroactive revision based on the outcome of ANS Royalty Litigation. (The 1985 Petro Star-Chevron contract also required an escrow).

Proposed Contract. Same price except that the netback value is not all Kuparuk producers; it is the volume-weighted average of ARCO's and BP's Kuparuk netback. BP and ARCO are the only Kuparuk lessees to have settled their ANS Royalty Litigation obligations. Together they own 94.5% of Kuparuk production. As there is an agreed-to methodology for valuing the netback of these two companies, there is no need for an escrow, and no need for retroactive ANS Royalty Litigation adjustments. The value of the 94.5% should be an adequate proxy for the remaining 5.5%.

PRICE PREMIUM, *Previous Contracts.* Negotiated contracts executed after December 1984 have included a price premium above the average netback value. The premium was primarily intended to compensate the state for selling "west-coast oil" at an average of the west-coast and gulf netbacks.

Proposed Contract. The small and decreasing proportion of gulf sales, and the small volume proposed to be sold to Petro Star JV mean that the proposed contract will not noticeably displace the lessees' west-coast sales. For these reasons, and to encourage the jobs, income, tax, and consumption benefits from in-state refining, the proposed contract does not include a premium.

SECURITY, *Previous Contracts:* Letter of credit worth 90-days of oil (and the value of the RIK company). ***Proposed Contract:*** Letter of credit worth 90-days of oil (and the value of the RIK company). However, for the first time we have required a parent company to be a signatory: ASRC.

NGL FIELD COST, *Previous Contracts.* Not specified in previous contracts. The state is currently in dispute with some north slope lessees (including ARCO and BP) concerning the field cost for NGLs. If a field cost for NGLs is established that is different from field costs for oil, the RIK purchasers receive a retroactive adjustment to previous bills.

Proposed Contract. NGLs are not currently exported from Kuparuk; thus, there is no current problem for NGL field costs at Kuparuk. If NGLs are exported, the contract specifies that Petro Star will pay its share of the producer-reported field costs and will receive a credit if a separate NGL field cost (or any field cost different from the current) is established.

LATE PAYMENT PENALTY. Previous contracts have required 1% late payment penalty after one business day. The proposed contract requires 5% after 10 business days. The new term is more in line with current commercial business practices.

INTEREST. The previous Petro Star contract specified an annual interest rate of prime rate plus 1.25%. The proposed contract specifies the statutory rate required by Cha 23 SLA 91. If Petro Star JV overpays, the state will have to credit back the amount of the overpayment plus interest to Petro Star JV, just as Petro Star JV will have to pay the amount of any underpayment plus interest to the state.

BEST EFFORTS. Previous contracts required best efforts to market product in Alaska (equal to at least 23% of amount processed). This has been omitted from the proposed contract. It is virtually impossible to enforce, and it is unneeded given the requirement to process 80% of purchased oil in refinery, and given the contractual arrangements of joint venture to sell in-state.

SUMMARY OF PUBLIC PROCESS

PRELIMINARY FINDING & DRAFT CONTRACT. Notice of the preliminary finding and draft contract was mailed to the division's 450-person mailing list. (Approximately 100 individuals and agencies received copies). Notice and Royalty Board meeting was the subject of a display advertisement in the two Anchorage Papers, and papers in Fairbanks, Juneau, and Valdez.

FEBRUARY 6, 1992: MEETING OF THE ALASKA ROYALTY OIL AND GAS DEVELOPMENT ADVISORY BOARD. Board met in part to consider proposed royalty sale. Approximately 50 people attended the meeting. When Commissioner Heinze called for public testimony, no one asked to testify. The board adopted the department's finding, and recommended the legislature take appropriate action to effectuate the sale.

PUBLIC COMMENT RECEIVED. In response to the mailing and advertisements, the department received four letters commenting on the proposed sale. Two letters were received from one respondent (Prince William Sound Conservation Alliance). The letters and the department's response are contained in Appendix B of the Final Finding.

FINAL FINDING & CONTRACT. Mailed to same list as preliminary finding.

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

WALTER J. HICKEL, GOVERNOR

400 WILLOUGHBY AVENUE
JUNEAU, ALASKA 99801-1796
PHONE: (907) 465-2400
FACSIMILE: (907) 586-2754

March 11, 1992

The Honorable Sam Cotten, Chair
Senate Special Committee for Oil and Gas
State Capitol
Juneau, AK 99811-1182

Dear Senator Cotten:

Subject: SB 448, which provides for legislative approval of a contract between the state and Petro Star Valdez Refinery Joint Venture for the sale of Kuparuk River Unit royalty oil.

Position: The Department of Natural Resources supports this bill.

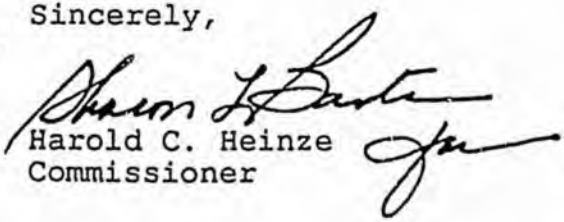
Background: Petro Star Valdez Refinery Joint Venture (Petro Star JV) wants to build and operate a refinery in Valdez. Petro Star JV has asked to purchase 30,000 barrels per day of the state's north slope royalty oil to refine into jet fuel, marine diesel, and heating fuel. The refinery will be located on private land, adjacent to Dayville Road east of the Trans Alaska Pipeline terminal. Petro Star JV will sell approximately 20-40 million gallons per year of jet fuel to MarkAir Inc., and approximately 10 million gallons per year of heating and marine diesel fuels to local communities.

The contract contains a local hire clause which states in part that Petro Star JV "agrees to employ Alaska residents and Alaska companies to the extent they are available, willing and qualified for all work performed in Alaska in connection with the Agreement."

On March 4, 1992, the Department of Natural Resources made a written finding that this disposal of state royalty oil is in the best interest of the state and maximizes the benefits to Alaska citizens. The Alaska Royalty Oil and Gas Development Advisory Board unanimously approved this royalty oil sale and recommended the Petro Star JV contract be approved by the Legislature.

Please let me or Oil and Gas Director James Eason know if you have questions about the Petro Star JV contract.

Sincerely,


Harold C. Heinze
Commissioner

cc: Committee Members
Paul Fuhs, Legislative Liaison, Office of the Governor
James Eason, Director, Division of Oil and Gas