

HB

454

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

March 18, 1994

The Honorable Robin Taylor
Chair, Senate Judiciary
Room 30
State Capitol
Juneau, AK 99801-1182

Re: FY 94 Oil and Gas
litigation supplemental
HB 454

Dear Senator Taylor:

The Department of Law urgently requests Judiciary Committee approval of a supplemental appropriation for oil and gas litigation in FY 94 in the amount of \$18,450,000. The appropriation is contained in HB 454 now pending in your committee.

The department is now in the trial preparation stage for four major cases. Two of these cases involve royalty matters set for trial in the spring of 1995. The remaining cases are tax matters set for formal administrative proceedings. All of these cases are complex, involving substantial amounts of time and expense to prepare. The legislature partially funded the FY 1994 oil and gas special litigation budget request unit by appropriating \$10.358 million (l. 11-12, sec. 25, ch. 65, SLA 1993) of the estimated \$25 million needed to finance a full year of litigation activities. Because of the expense of document collection, production and organization, the need to take numerous depositions, and the employment and preparation of experts for all of these cases, the original appropriation has been fully expended.

Consequently, it is imperative that a special supplemental appropriation bill be introduced for consideration by the legislature at the earliest possible time. There is precedent for expedited consideration of an oil and gas litigation-related supplemental appropriation (see, e.g., ch. 2, SLA 1983; ch. 1, SLA 1981). Without early enactment of a supplemental appropriation, we will be forced to shut down our litigation effort at the most crucial pretrial period. Our efforts in the royalty cases are being driven by scheduling orders imposed by the Superior Court. Our efforts in the tax cases are being driven by the policy of the administration to resolve long standing tax disputes that may add significantly to state revenues.

WALTER J. HICKEL, GOVERNOR

PLEASE REPLY TO:

- 1031 WEST 4TH AVENUE, SUITE 200
ANCHORAGE, ALASKA 99501-1994
PHONE (907) 269-5100
FAX: (907) 276-3697
- KEY BANK BUILDING
100 CUSHMAN ST., SUITE 400
FAIRBANKS, ALASKA 99701-4679
PHONE (907) 451-2511
FAX: (907) 451-2546
- P.O. BOX 110300-DIAMOND COURT HOUSE
JUNEAU, ALASKA 99911-0300
PHONE (907) 465-3600
FAX: (907) 465-6735

The supplemental will complete funding in FY 94 for the following major activities:

1. Royalty Cases.

In re ANS Royalty litigation (formerly known as State v. Amerada Hess). This case is scheduled for trial beginning in Spring 1995. The case involves the validity and method of calculation of charges assessed by North Slope producers for the state's royalty oil produced in the form of natural gas liquids. We are incurring significant expense to process over 2,500,000 documents produced by our opponents during discovery. We are also conducting oral depositions of persons who may provide relevant evidence concerning the state or the producer's case. Experts were hired to prepare reports to support the cases of the respective parties. These reports were exchanged with our opponents and we must now depose these experts. In order to be ready for trial, it is crucial to continue funding these activities.

MAPCO. The department is also deeply committed to prosecuting the state's claims against MAPCO for a retroactive price adjustment under certain royalty oil contracts. This case is also scheduled for a Spring 1995 trial. The recovery of over \$100 million is at stake in this case. All other royalty oil purchasers have either admitted liability or settled for substantially all of the state's claims. MAPCO is alone in its denial of liability and is defending this case in a manner which appears to be calculated to cost the state the maximum amount to obtain a judgment. Again, the continuation of funding is crucial to keep up the pace set by MAPCO and the Superior Court.

2. Oil and gas tax cases.

Tax proceedings conducted before the Department of Revenue are confidential. Accordingly, the department is unable to disclose the specific taxpayers, issues, or amounts at issue. It is expected that the cases currently being developed will require the processing of millions of documents and the employment of several experts. Development of these cases is contingent upon additional funding since existing appropriations are fully committed.

3. TAPS cases.

TAPS Corrosion Case. The TAPS corrosion case between the state and the TAPS owners is stayed to permit the parties to undertake a cooperative corrosion control program. The parties hope that the program will provide a basis for settlement of the dispute. The department is expending substantial amounts through

The Honorable Robin Taylor
Chair, Senate Judiciary

March 18, 1994
Page 3

outside counsel to support the cooperative program. It is possible that the program will either continue and the case will settle, or the parties may abandon the cooperative program and return to litigation. If the program continues, the state will incur substantial sums to provide expert support for the program. If the case returns to litigation, the costs of preparing for hearing before the Federal Energy Regulatory Commission could be substantial. Presently, we expect that the cooperative program will be extended by FERC. However, we must be prepared for the other eventuality.

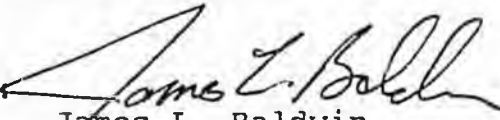
TAPS audit. The department gave the TAPS owners notice of the state's right to audit for tariff review purposes. An audit was last done through 1986. The audit may provide a basis for questioning substantial expenses recovered by the owners through the TAPS tariff. It is expected that the legislature and public will be critical of the time lag since the last audit. It is imperative that the administration anticipate this criticism by moving forward now with the audit. The shortfall in available appropriations will delay the audit. The main audit firm has expressed a reluctance to begin in earnest without assurance of funding. Additionally, Alyeska appears prepared to litigate our right of access to their documents. The litigation will add an unanticipated expense to our audit effort.

In closing, please let me stress the importance of enacting an early supplemental. A temporary cessation of trial preparation would be required in the absence of an early supplemental. This will have a devastating effect on the state's oil and gas litigation. Our trial teams would, for the most part, be disbanded. Reconstruction of the teams later would be difficult and, in the long term, more expensive for the state than continuing our current level of activity. The emergency measures described here would send a signal of weakness to the producers. A shutdown now would make it far more difficult (if not impossible) to arrive at settlements that are acceptable to the state.

Sincerely,

BRUCE M. BOTELHO
ATTORNEY GENERAL

By



James L. Baldwin
Assistant Attorney General

JLB:tg

The Honorable Robin Taylor
Chair, Senate Judiciary

March 18, 1994
Page 4

cc: The Honorable Steve Frank
Co-Chair Senate Finance

Bruce M. Botelho
Attorney General

Dick Pegues, Director
Administrative Services Division