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BP EXPLORATION

ARCO Alaska, Inc.



April 1, 1999

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The Honorable Ramona Barnes
State Capitol, Room 403
Juneau, AK 99801-1182

Dear Representative Barnes:

A new era in the Alaskan oil industry is about to begin. With the announcement today that BP Amoco will purchase ARCO, we are taking the first step in the process of combining two companies with long and successful histories in Alaska into a single new enterprise with the experience, expertise and financial resources to ensure a long and successful future in Alaska.

We know that this announcement comes as a surprise, and it creates uncertainty and concern because of the important role our companies have played in Alaska for the past several decades. We want to assure you that BP Amoco's acquisition of ARCO is crucial to ensuring the long-term health of the Alaskan oil industry -- the industry that has been the foundation of Alaska's economy for a quarter of a century. It comes as a result of ARCO approaching BP Amoco with a proposal that BP Amoco purchase ARCO to create a new enterprise. We are taking our destinies in our own hands in order to survive and thrive through extremely difficult business conditions.

Combining our companies will be good for Alaska. The short-term pain of job losses as we eliminate overlap in our activities, primarily in our Anchorage headquarters functions, will be more than offset by long-term stability and growth potential. Efficiencies gained by combining our strengths will enhance our ability to attract investments to our Alaskan projects and position Alaska to continue to play a pivotal role as a U.S. energy provider for decades to come.

Alaska will continue to be a cornerstone of our global activities, and our new combined organization will maintain the same high environmental, safety and social standards that BP Amoco and ARCO have always maintained separately.

- BP Amoco will invest \$5 billion in North Slope development over the next five years or so, which exceeds projected 1999 capital spending by ARCO and BP Amoco combined, as well as ARCO's and BP's combined capital spending during the past five years;
- BP Amoco will increase its financial support of community organizations by 50% from the current combined ARCO-BP Amoco level;
- BP Amoco will make Alaska the centerpiece of its global gas activities in its efforts to commercialize North Slope gas. The company will continue the ARCO-led gas sponsor group, relocate our gas technology center to Alaska, and build a gas-to-liquids pilot plant on the North Slope;
- BP Amoco will honor all current agreements with ARCO's contractors and suppliers, and will continue to treat all business partners fairly and equitably, with dignity and respect;

The Honorable Ramona Barnes

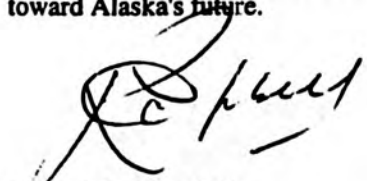
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April 1, 1999

- Organized labor will continue to play an important role in BP Amoco's North Slope construction activities;
- BP Amoco will continue to work cooperatively and collaboratively with all levels of government;
- BP Amoco will continue its efforts to provide job and business opportunities for Alaskans whenever possible;
- BP Amoco will honor ARCO's commitments to build new "Millennium Class" double-hull tankers and is fully committed to a tanker renewal program that complies with the Oil Pollution Act of 1990;
- BP Amoco will continue to be actively involved in state and federal lease sales and continue to pursue exploration and development opportunities in Alaska;
- BP Amoco will treat all employees with respect and dignity. The new organization will be designed to minimize disruptions and will be composed of about equal numbers of BP Amoco and ARCO personnel. Those who lose their jobs will receive generous severance packages. *Int'l*

Until government approval is secured, BP Amoco and ARCO will continue to operate as separate and independent companies. Safety and environmental performance will remain the #1 priority for BP Amoco and ARCO throughout the governmental approval process, and we will allow nothing to distract us from this commitment.

Working together, Alaskans and our two companies have overcome many common challenges and seized many mutual opportunities in the past. We ask for your continuing support as we move toward combining BP Amoco and ARCO into a single company with the same commitment to work with you toward Alaska's future.


Richard C. Campbell
President
BP Exploration (Alaska) Inc.


Kevin O. Meyers
President
ARCO Alaska, Inc.

Legislators finance team for BP study

By ROBERT KOWALSKI ^{ADN}
Daily News Juneau Bureau 4-9-99

JUNEAU — State lawmakers Thursday agreed to hire legal experts to conduct a study for the Legislature of the BP Amoco purchase of Atlantic Richfield Co.

The Legislative Council authorized leaders of the House and Senate to spend up to \$50,000 to hire lawyers to review the \$25.6 billion acquisition, which would join Alaska's two largest oil producing companies.

The review will cover state and federal law and other issues related to the deal, such as Alaska's oil industry taxation, said Sen. Mike Miller, a North Pole Republican and chairman of the Legislative Council.

"We really don't know what it means to Alaska," Miller said Thursday.

Miller said the Republican majority in the Legislature has chosen two of its lawmakers, Sen. Rick Halford of Chugiak and House Speaker Brian Porter of Anchorage, to oversee the review of the BP-Arco deal.

Miller said he expects legislative leaders to choose legal counsel to conduct the study within two weeks.

"This is a time-sensitive issue," he said. BP and Arco announced the purchase last week. The Legislature is scheduled to complete its session next month.

Gov. Tony Knowles last week directed four of his top officials to study the acquisition.

Attorney General Bruce Botelho, Revenue Commissioner Wilson Condon, Natural Resources Commissioner John Shively and John Katz, the head of Knowles' Washington, D.C., office are reviewing the BP-Arco purchase for the administration.

The Legislative Council is a panel of lawmakers that acts on behalf of the full Legislature when it's not in session.

□ Reporter Robert Kowalski can be reached at rkowalski@adn.com.

Arco execs would receive cash, stock in merger deal

Kenet 4-8-99

ANCHORAGE (AP). — Some Arco executives are in line for big severance payments if shareholders approve BP Amoco's takeover.

Arco chairman and chief executive Mike Bowlin will get \$11.6 million in pay and stock, according to the company proxy statement. Bowlin will also get a retirement of \$900,000 per year for the rest of his life.

Other senior executives will get smaller golden parachutes of three years' salary, two years of bonus pay and stock.

Ken Thompson, former Arco Alaska Inc. president and a current executive vice president in Los Angeles, will get about \$3 million in stock and \$1.6 million in pay. Other Arco employees will get smaller severance deals if BP terminates them.

BP Amoco's \$25.6 billion deal to buy Arco is expected to close by the end of the year.

BP thinks the deal will save the company \$1 billion a year, much of it in Alaska, where BP and Arco

have twin staffs, different buildings and dual operations in the Prudhoe Bay field.

BP predicts 2,000 Arco layoffs worldwide if the deal is approved, 400 of them in Alaska. While the fate of other top executives is undecided, Bowlin said he will leave the new company.

Bowlin's severance, and the pay for other Arco employees, is guaranteed by something called "a change of control arrangement" that Arco management put into effect in 1997.

Bowlin said last week that the agreement helped expedite the BP deal by taking the problem of employee pay off the table.

The change-of-control agreements are a relatively new development for corporate America, adopted as waves of mergers swept industry in the past 10 years. The goal is to give executives income security so they can pursue any options—including ones that eliminate their jobs—to help shareholders.

ADN 4-10-99

BP wrong buyer for Arco

I am a lifelong Alaska resident and am writing to express my opposition to the sale of Arco Alaska Inc. to BP Amoco.

I feel it would create an anti-competitive environment that would damage the Alaska oil industry and is against the best interests of Alaska and the United States. I feel it would have a negative effect on future lease sales and oil development.

If this sale goes through, we will have a situation in which any dollar spent by BP Amoco in Alaska would first have to compete with BP's projects around the world, including in Third World countries where development costs are lower because of lax environmental, safety and health regulations. This would have a terrible effect on our industry in Alaska, which directly translates into jobs and state revenue.

This would be the exact opposite of the situation we now have, in which Arco's primary interests are and always have been in Alaska. Don't forget that all major oil fields on the North Slope were discovered by Arco, including Prudhoe Bay, Kuparuk, Lisburne, Alpine, Tarn and Tabasco.

Please take a careful look at this proposed deal and let your representatives in Juneau and Washington know how you feel. I suggest that there is one solution that might satisfy both Alaskans and BP shareholders. If the sale of Atlantic Richfield Co. is approved, the Federal Trade Commission should require BP Amoco to divest itself of all properties now operated by Arco Alaska Inc. These properties should be sold to an independent company to preserve the competitive, innovative, healthy oil industry of Alaska. If you value your Permanent Fund check, get busy and write some letters.

— Greg Sarber
Anchorage

'Partner' was just a line

Well, shucks! Now I understand the real meaning of that Arco video tune: "We can make it happen, yeah!" They surely did a number on us. After all, a partner would consult with his partner beforehand, wouldn't he? Oh, yeah, you gotta hand it to them, though. It takes a special talent to give new meaning to the concept of "partner."

And with BP, which has flown its banner on an equal level with our state and national flags for years, I guess we can now expect to see it flying above those other two. Well, hey! Bigger and bigger is better and better, right?

As for our governor, he did issue that invitation, didn't he? We've surely been opened for the business.

— Charles Konigsberg
Anchorage

Merger study ^{ADN 4-12-99} Legislature has little time to act

State lawmakers were stunned by the announcement of the BP-Arco merger. Now they are coming to their senses.

Thursday, legislators approved \$50,000 to hire lawyers to review the agreement that will transform Alaska's two largest oil-producing companies into one. That was a good move, though \$50,000 may not be enough to do the job. Good advice is expensive, and the Legislature needs the best available.

The merger will leave one company with 75 percent of Prudhoe Bay oil and 75 percent of the trans-Alaska oil pipeline. The Legislature needs to know all it can about the facts of this power concentration and the potential economic, financial and social results.

But before lawmakers can get answers, they need to know what kind of questions to ask. Informed questioning inevitably will require the help of experts familiar with merger issues, the oil industry and the economics of Alaska oil.

House Speaker Brian Porter and Sen. Rick Halford have been asked to lead the Arco-BP review. The choice is a good one. Speaker Porter has the right temperament and Sen. Halford has the experience to pursue Alaska's interests in the merger.

They do not, however, have much time, as Sen. Halford freely acknowledges. The merger process probably will be over by the end of the year. Lawmakers must work quickly to become informed, to make recommendations and work with the Knowles administration, which is addressing the merger on its own track.

The BP-Arco merger is the biggest oil issue to come before the Legislature since the mid-1970s, when Alaska's oil tax policy for the pipeline was written. Speaker Porter and Sen. Halford have a monster responsibility, but so do their colleagues on both sides of the isle.

Allow me to share with you my thoughts on the BPA ARCO merger.

What's good for Alaska

1. The elimination of redundant (and non-value adding) activities throughout BPA ARCO should lead to a lower cost structure.

Specifically, ARCO services a corporate headquarters in LA, and a research center and international headquarters in Plano,

Texas -- the elimination of these offices results in significant cost savings.

2. Lower lease operating costs here in Alaska (due to cost savings) would improve the economics of Alaskan projects relative to the BPA worldwide portfolio.

3. Elimination of senior ARCO management is a plus given their horrendous track record of costly decisions (e.g., Anaconda, Henderson Clay, Union Texas Petroleum, etc.). A recent oil journal referred to these decisions as the largest systematic destruction of wealth in the history of corporate America. On the flip side, John Browne's business performance is quite impressive.

4. The Alaskan oil field jobs that remain should be more stable.

What's not so good for Alaska

1. The lack of competitors in lease sales.

2. The lack of corporate and cultural diversity. Diversity leads to new ideas and risk taking; essential ingredients in the oil and gas business.

3. Multiple and strong competitors often evaluate "what's best for Alaska" during heated debates and discussions. The thinly veiled threat is that one competitor will provide information to the state which shows that the other competitor's position isn't in Alaska's best interests. With less competition the state will be almost solely responsible for understanding and articulating its own position -- a job it can scarcely do now given its staffing levels. AOGCC & DNR petroleum professionals do a yeoman's job, but it's simply not going to be enough in the future.

4. The immediate job losses will not only be the 400 positions announced, but also the ripple effect in the oil field contractor community and the economy in general. Also, BPA announced 6,000 lost jobs at the outset of the Amoco merger; now that number is in excess of 10,000. What assurances do you have that BPA won't up the job cuts at a later date?

What's uncertain for Alaska

1. Alaska will compete for funding on a global basis. It's too complex to predict if this will benefit or hurt Alaskan oil and gas projects because it involves the economics (subject to unpredictable oil price fluctuations) and changing politics throughout the world.

2. Whether the political alignments BPA will try and formulate (e.g., native corporations, oil and gas service providers, etc.) in order to get consensus for this merger, will create win-win or win-lose situations in the eyes of Alaskans and their legislators.

What's Alaska to do?

Move rapidly to beef up the AOGCC with a number of Alaskan oil and gas professionals with the skills more akin to those found on the Texas Railroad Commission. You'll need people the caliber of Pat MaGuire (Best Reservoir Engineer in Alaska) and Harold Heinze (former ARCO Alaska President) in this watchdog organization to effectively protect the state's interests. You want more scientists and accountants in this organization, not politicians (unless they have a technical background).

Alaska is fortunate to have petroleum experience in the political realm with Joe Green, John Shively and Wilson Conden, but politics are transitory and you cannot expect this kind of understanding to be around forever. Alaska's legacy must be an institution which transcends politics. If the AOGCC is not appropriately strengthened, then Alaska is flying blind. If Alaska strengthens its AOGCC as I've outlined, then I would very much support the BPA ARCO merger

Personally and professionally, the BPA ARCO merger is positive for me. My petroleum background, workstyle and performance rankings should fit nicely with the new BPA Alaska organization. I'll have access to technical experts and resources throughout the world whereas now with ARCO I'm quite limited. I'm accepting the risk of losing my job, in exchange for a more business-like and accountable organization. On balance I support this merger from a personal viewpoint.

Thanks for listening,

Jerry Foster
2540 Brandy Cir.
Anch, AK 99516

Short Bio

Born in Fairbanks (wife born in Juneau, kids born in Anchorage)
'82 Honors Graduate UAF Petroleum & Geological Engineering
Outstanding Petroleum Engineering Alumni UAF
Licensed Professional Engineer State of Alaska in Petroleum Engineering
Former Board of Directors Society of Petroleum Engineers Alaska Section
+17 years ARCO employee

COMMENTS ON THE BP/ARCO MERGER RELATIVE TO AOGCC OPERATIONS

During a recent teleconference with Senators Wilken, Green and Elton, we were asked to comment on the impact of the BP/ARCO buyout on the Commission's ability to comply with its statutory obligations to provide oversight to the people of Alaska.

For a long time the Commission has not had the resources to fully analyze and evaluate the industries proposals and representations. However the Commission has benefited indirectly from the fact that the two major operators spend a significant amount of effort in ensuring their individual interests are protected. As a result of this effort many issues are brought to light, in a timely manner, that might not otherwise have surfaced under the new condition. The Commission is generally shown the composite results of many technical meetings that were held between the major companies. While this is expedient, it does not expose the alternatives and the reasons for the final choices. Our decisions are by necessity, based on the composite information rather than independent evaluation.

If we look at the scenario of one major operator, it is clear that the iterative process will not be present as before. It is therefore incumbent on the state to pursue their oversight role much more vigorously to insure that the iteration on decisions is robust and that the states' best interests are considered. Another important factor involved with the combination of workforces, is that significant layoffs and cost reductions will ensue. This situation will impact the experience levels of personnel, training and both routine and long term maintenance activities.

In order to mitigate the potential lack of proper oversight, the commission should move forward in several areas.

- Increase the number of petroleum inspectors from four to seven. This will allow two full time inspectors on the slope with 24 hour, seven days week coverage and one inspector in the Cook Inlet. The inspection program will then be able to witness a much larger percentage of equipment and operations.
- Increase the number of professional staff by three. These would be comprised of a senior petroleum engineer, a senior petroleum reservoir engineer and a senior petroleum geologist. The addition of these specialists would give us the ability to better analyze the operators' proposals on new projects and perform needed analysis on existing reservoir performance.
- Continue to move forward on our initiative to handle data electronically both in storage and retrieval. By leveraging up on the work already completed by the state ITG on DMV and others, we can rapidly and cost

effectively move from an all paper system to an electronic one. This will allow greater interface capability with the operators for processing data for evaluation as well as regulatory filing.

- **Intensify our efforts and program to optimize the use of our reservoir modeling software. Our program, while it is "state of the art" is not capable of the sophisticated analysis the operators programs are. It is however, robust enough to check overall results and pose questions on various aspects of evaluation and decision. We may also require additional modules for our existing software.**
- **Provide funding to hire consultants on specialized needs basis. This would allow regular work to continue and to utilize the consultant for focused projects avoiding the need for additional hiring of regular employees.**

There also exists a current matter of dire urgency at the Commission. We have a \$160,000 shortfall for the 1999 fiscal year. This will require that the Commission shutdown for the month of June. All new drilling activity will cease.

A related issue that has been unsettled for more than three years is the poor repair that the Commission building is in. Either the building should be fixed or the Commission should be moved.

QUESTIONS re: BP Amoco Buyout of ARCO

- How unusual is the single operator concept for a field as large as Prudhoe Bay?

- Should the state now begin encouraging other, large oil companies (such as the French companies Total or Elf) to come into Alaska perhaps vying with BP/Exxon for oil leases?

- Is it likely the pending power that BP will wield in the Alaska oil patch will frighten off any potential participation by other large, international oil companies?

- Perhaps Alaska simply needs to offer additional encouragement for new investors (from the oil industry) to come to Alaska? If so, in what form should the encouragement take?

- If the state began encouraging other, large oil companies to enter the Alaska oil patch would it require any significant regulatory changes in existing law, taxes, etc dealing with oil/gas recovery, etc?

- Regulations likely would hurt the smaller operators more than BP ...are there suggestions for regulation or even taxation changes?

- Pertaining to the transportation of oil, while the oil pipeline is regulated and the operators cannot charge beyond a reasonable amount and must carry oil for non-owner companies, the use of oil tankers is NOT regulated.

- should there be a kind of guarantee that BP and Exxon provide at least some tanker capacity for other Alaska operators?
- will the existing (& planned) fleet of tankers - including the new double hull ARCO contracted tankers under construction - provide ample capacity for future needs? In other words, if operators other than Exxon and BP wish to ship oil will Exxon and BP be capable of providing space aboard their tankers?
- Is BP planning to build additional tankers (beyond that for which ARCO has contracted) or will it modify existing tankers to fit the double hull requirement?

- While pipeline use would likely be no problem for future non-BP/Exxon usage such is likely not the same for other Prudhoe Bay facilities. Would it be reasonable to suggest to BP that at least some of the North Slope/Prudhoe Bay facilities be made available (obviously not for free) to new companies that may begin projects there.

- Is it likely that enforcing the acreage lease cap of 500,000 acres ...(perhaps encouraging BP to give up some of its less desirable tracts) ... might actually encourage exploration efforts by moderate-sized oil companies, such as Anadarko and others?

- How can the state encourage the construction of peripheral pipelines ... to bringing oil or gas from small fields ...to the North Slope facilities? Would it be reasonable to extract a concession from BP which tends to encourage construction of small field, peripheral pipelines? Would encouragement for construction of peripheral pipelines ultimately encourage so-called wildcat exploration efforts by smaller companies, thereby - hopefully - locating additional oil finds?

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Knowles team studies merger

By ROBERT KOWALSKI
Daily News Bureau
JUNE 4 - 2:49

JUNE 4 — Gov. Tony Knowles on Thursday directed a team of his top legal, financial and resource officials to review BP Amoco's \$25.6 billion purchase of Atlantic Richfield Co. and its impacts on the state jobs, competition and revenues.

One of the officials, Attorney General Bruce Botelho, termed the buyout "the major single change in the oil industry" since construction of the trans-Alaska oil pipeline concluded in 1977. "It is a dramatic event. ... It raises significant concerns. It also raises potential opportunities."

As the administration was gearing up to respond to the oil deal, the Legislature was formulating plans. The Republican leadership plans to hire outside counsel with expertise in state and federal anti-trust law as early as next week, said Sen. Rick Halford, R-Chugiak.

Lawmakers continued to express varying degrees of shock at the announcement of the

Please see Back Page, KNOWLES

KNOWLES: State team to weigh effects of merger

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BP-Arco deal Thursday, four days after word first began to leak out.

"All we're doing now is having an emotional reaction," said Rep. Joe Green, an Anchorage Republican and the House majority leader. "There are a lot of people in the state ... who are dismayed."

The administration group will study whether the deal complies with state and federal anti-trust law, Botelho said.

It also will consider implications of the BP acquisition of Arco on issues like jobs, the environment, transportation of oil, and revenues the state collects from the oil industry.

Together, BP and Arco control 75 percent of Alaska oil production and in recent years have provided about three-fourths of the state's general fund budget.

Along with Botelho, the administration team includes Natural Resources Commissioner John Shively, Revenue Commissioner Wilson Condon and the head of Knowles' Washington, D.C., office, John Katz.

Knowles was vacationing Thursday and didn't comment in person on the BP acquisition.

"The state of Alaska has enjoyed a strong, mutually productive partnership with BP and Arco, and I would expect that to continue," he said in a statement.

Although BP on Thursday said it has been in acquisition discussions with Arco since January, Knowles first heard about the deal Sunday evening, spokesman Bob King said.

Botelho said the state's review will be thorough and could take weeks to complete. "We will be examining only what is in the best interest of the state of Alaska," he said.

When asked whether the state could block the BP acquisition on antitrust grounds, Botelho said: "I think that's an issue of some debate."

Botelho said state law authorizes Alaska to seek to stop a corporate merger under some circumstances, based on concerns about the effects on competition.

"At this point, my view is that power does exist theoretically to block the merger," he said.

Botelho said the state also can make its case before the Federal Trade Commission, which must approve the BP-Arco deal. He said the FTC's review of the deal could take the remainder of the year to

complete.

But Halford said making an antitrust argument will be complicated by the fact that Alaska benefits from competition between companies in oil exploration and development and also by efficiencies the firms might gain by combining operations.

"The state has some inherent difficulties in the sense that we're on both sides of the equation," said Halford, the chairman of the Senate Resources Committee.

Halford also said it may realistically be too late for Alaska to block the deal.

"It's not necessarily a genie that can be put back in the bottle, even if you wanted to," he said. "We may already be fully committed."

Botelho said the state also will have standing to review the acquisition before the Federal Energy Regulatory Commission, which regulates the trans-Alaska oil pipeline.

BP and Arco, which combined would become the world's second largest oil company, own 72 percent of the pipeline.

Botelho said he and the other members of Knowles' team expect to produce a list of issues about the acquisition as early as next week.

"I think we're doing what it is that the people of Alaska

would expect us to do," Botelho said. "That is, fairly examine it and keep as our one focus what is in the best interest of the state of Alaska. That doesn't preclude an outcome which would say this merger should not go forward."

Condon said one issue the state may address is the different oil value arrangements it has with BP and Arco, which affect the amount of money they pay the state. "This merger does give us the opportunity to look at those arrangements and seek to modify them if it makes sense to do so," he said.

Earlier this year, BP Amoco's chief executive officer, Sir John Browne, suggested Alaska consider revising its oil taxation structure.

"I hope he's changed his mind," Condon said Thursday.

One issue the combined companies will have to address is a state law that lets one entity own no more than 500,000 acres of onshore leases that are not in production.

Together, BP and Arco hold leases on 870,000 such acres.

"That is clearly (an issue) that is on the table," Botelho said.

□ Reporter Robert Kowalski can be reached at rkowalski@adn.com.

BP plan to cost 400 jobs

By BEN SPIESS
Daily News reporter

ADN
4-2-99

BP Amoco and Arco announced Thursday that the proposed \$25.6 billion merger between the two oil giants will lead to about 400 layoffs in Alaska.

All current Arco Alaska Inc. projects in Alaska will continue unaffected by the merger, said Dick Olver, head of exploration and production for BP. Olver also announced capital spending plans of \$5 billion over the next five years in Alaska, slightly ahead of spending in the past five years.

BP will also relinquish control of about 360,000 acres under lease for oil and gas development to meet the terms of an Alaska law that limits the acreage one company can hold. To meet the terms of federal shipping law, BP Amoco will turn the Arco tanker fleet over to Alaska Transportation Co. The ships will comply with laws that prohibit a foreign company owning ships that move between domestic ports.

Most of the layoffs will be in BP and Arco's Anchorage offices, Olver said. After absorbing and consolidating Arco's holdings worldwide, BP expects to save up to \$1 billion a year, the company said. About \$200 million in savings will come from streamlining the two companies' operations in Alaska, where they are the state's top two oil producers.

No layoffs or other proposed changes will take effect until the takeover is finalized.

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INSIDE



BP's John Browne

■ THE DEAL: Worried about Arco's ability to compete, chairman Mike Bowlin last year began mulling mergers. C-1

■ NEW CRUDE: BP Amoco announces plans to build a \$70 million plant to convert natural gas into liquid. C-1

■ ARCO'S LEGACY: The company that is now Atlantic Richfield leaves a long and rich legacy in Alaska. C-1

BP-ARCO: 400 lay-

Continued from Page A-1

which Oliver said is six to nine months away.

Much remains to be sorted out about the future of Alaska's oil monolith. Whether the companies will combine in one Anchorage office building is undecided. How the Prudhoe Bay field will be handled is unknown. Each company operates half of Prudhoe, the nation's largest oil field, and they have duplicate living and operating facilities. Even the name of the new Alaska company is undecided, except that it will not include "Arco."

Oliver said that BP intends to raise charitable giving from the combined company statewide by 50 percent.

In Juneau, initial shock at the merger news has given way to serious concern.

In recent years, 75 percent of Alaska's general fund budget came from North Slope oil. Now 74 percent of Alaska's oil reserves could be in the hands of one company.

Arco chairman and chief executive Mike Bowlin approached BP in January about selling Arco. Oliver said that for BP, Arco has three central selling points.

First, by unifying Alaska operations, BP estimates it can cut North Slope production costs by 80 cents a barrel. The savings could boost profitability as production off the giant Prudhoe Bay field begins to wane and smaller fields scramble for development dollars.

Second, Arco has large gas reserves in Indonesia and off China. Asia is an area where BP Amoco is weak and market growth promises to be strong. The purchase moves BP Amoco from being the ninth-largest gas player in the region to the No. 3 player beyond Royal Dutch, Shell and Exxon.

Third, Arco is the largest gas retailer in California, Washington, Oregon and other West Coast states. As in Asia, Arco is strong where BP, which has concentrated retail efforts in the Midwest and East, is weak. The West is another booming market.

Arco could have remained independent, said Arco Alaska spokesman Ronnie Chappell. The decision to go to BP Amoco was not one of sur-

vival but of profitability.

"When prices get as low as \$10 a barrel, a company like ours has serious cash-flow problems," Chappell said.

Arco's Alaska operations are among the company's most efficient. But citing Arco holdings in places like China, Algeria, Ecuador or Venezuela, Chappell said that "we have opportunities that we cannot capitalize on soon enough for the people who are investing with us."

Indeed, when oil prices fell in the past 15 months, Arco's stock prices fell farther and harder than those of its large competitors like Exxon, BP or Royal Dutch Shell.

"Long term and short term, this is good for shareholders," Chappell said.

Arco stock rose sharply to meet the 20 percent stock premium that BP proposes to pay on acquiring the company. Thursday, Arco stock fell 69 cents to \$72.44. BP Amoco shares rose on news of the takeover bid early this week but lost much of the gain Thursday, sliding \$5.12 to \$95.81.

Whether wedding almost all of Alaska's oil resources to a single company is good is less clear. A Legislature that rarely finds anything to agree on has found a common cause of concern — the vulnerability of state finances to a single company. Gov. Tony Knowles, who found out about the deal Sunday afternoon, has formed a team of cabinet members to address the questions raised by the merger.

"From taxation to regulation to the bully pulpit, we've got to hope we'll be successful," said Wilson Condon, commissioner of the Department of Revenue.

BP and Arco officials in Alaska say that they will bid for leases in the National Petroleum Reserve lease sale in May as if the two companies were separate.

"We will act as if we were competitors until the deal closes," Oliver said. "Do you think the FTC may be worried about competition issues? Do you think in that environment we would not spend as if the companies were separate?"

Reporter Ben Spies can be reached at bspies@edn.com.

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**The Proposed Merger
Between BP and ARCO:
Issues for the State**



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Introduction

- The recent announcement that BP and ARCO intend to merge has caused the State to reexamine--or, at least, to begin the process of reexamining--the principles underlying the way oil and gas on the North Slope is leased, produced, transported, and marketed.

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- The proposed merger has in some minds pitted the paradigms of diversity and competition against claims of economic benefits attributable to greater efficiency.
- In the end, it is up to the State to pursue the path that will best satisfy the Alaska Constitution's mandate:
 - that the State's resources be used, developed and conserved in a manner that maximizes the benefits of those resources for Alaskans.

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• Topics of Discussion

- I thought it would be helpful, first, to describe the principal aspects of the State's current fiscal regime.
- An understanding of the fiscal regime is, of course, an important prerequisite for evaluating the economic effects of the proposed merger upon the State.

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- Second, I'll describe various aspects of North Slope oil and gas leasing, production, transportation, and marketing, particularly as they may relate to BP and ARCO, and I'll describe some of the effects of the proposed merger on these various aspects of North Slope oil and gas development.
- Finally, I'll talk about some of the issues the proposed merger raises for the State, and some of the questions the State will have to answer before it can know whether the terms of the proposed merger are in the State's best interests.

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The Fiscal Regime Applicable to North Slope Oil and Gas Development

- The State fiscal regime that applies to North Slope oil and gas development has four principal parts:
 - the severance tax,
 - the property tax,
 - the oil and gas corporate income tax, and
 - the royalty obligation.

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PROPERTY TAX

- The State imposes an annual tax of 20 mils on oil and gas exploration, production, and pipeline transportation property. AS 43.56. Municipalities may also impose taxes on this property, and they generally do.
- The municipal tax is a credit against the State property tax, so as a general proposition most of the property tax obligation faced by the North Slope producers and their affiliates flows directly to the municipalities with oil and gas property within their boundaries.

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CORPORATE INCOME TAX

- Alaska imposes a corporate income tax of 9.4 percent on income earned from business activity that is taxable in the State.
- For an oil and gas corporation, the DOR first ascertains the worldwide income of the corporation and its affiliates.

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CORPORATE INCOME TAX

- The portion of that worldwide income that is subject to state tax is determined by using apportionment factors.
- Those factors compare the corporation's sales, property, and barrels produced in the State with its sales, property, and barrels produced everywhere.

SEVERANCE TAXES AND ROYALTIES

- Severance taxes and royalties differ in some significant particulars.
- They are administered, of course, by different agencies, but, more importantly, the producers' royalty obligations are contractual--which is to say that they are defined first by the terms of the leases (and, ultimately, unit agreements) that the producers sign with the State.

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SEVERANCE TAXES AND ROYALTIES

- The severance tax, on the other hand, is an exercise of sovereign power.
- Despite these differences, severance taxes and royalties share important similarities.

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SEVERANCE TAXES AND ROYALTIES

- The taxable value, and the value for royalty purposes, of ANS is determined upon what is referred to as a “netback” basis.
- This means that the State starts by looking at the value of the crude at the point at which it reaches its destination market, for example, the United States West Coast.
- On the West Coast, the principal measure of the value of ANS-- both for royalty and tax purposes--is the publicly reported ANS spot price.

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SEVERANCE TAXES AND ROYALTIES

- From the destination value, the State subtracts the costs of transporting the oil from the North Slope.
- These transportation costs generally have two principal components:
 - TAPS
 - Marine Transportation

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SEVERANCE TAXES AND ROYALTIES

- There are other deductions as well
 - There is, for example, an allowance for the costs of converting gas to NGLs at Prudhoe Bay
 - And a field cost allowance (i.e., a deduction for some of the costs associated with removing gas and water from oil) at Prudhoe Bay for royalty purposes

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NORTH SLOPE OIL AND GAS LEASING, PRODUCTION, TRANSPORTATION, AND MARKETING

- LEASING

- OUTSIDE UNITS

- AS 38.05.140(c) provides that, outside of existing units, a person may not hold more than 500,000 acres in onshore State oil and gas leases.
 - The same 500,000 acre limitation applies to offshore oil and gas leases.

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LEASING

- LEASING OUTSIDE UNITS

- The combined company would have 870,349 acres in onshore oil and gas leases, or 370, 349 more acres than permitted by law.
 - Offshore, the combined company would have 351,120 acres of oil and gas leases that are not within units.
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LEASING

- LEASING WITHIN UNITS

– See Charts

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PRODUCTION

- According to DNR's figures in its Historical and Projected Oil and Gas Consumption
 - BP ships approximately 40% (including NGLs and RIV) of the barrels that move down TAPS
 - ARCO ships 28%

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PRODUCTION

- TAPS throughput today is approximately 1.16 million barrels per day.
 - That translates into approximately 470,000 bbd for BP
 - And 323,000 bbd for ARCO

323,000
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TRANSPORTATION-TAPS

- TAPS OWNERSHIP PERCENTAGES--1985
 - BP -- 34%
 - ARCO -- 21%
 - Exxon -- 20%
 - Other -- 25%
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TRANSPORTATION-TAPS

- TAPS OWNERSHIP PERCENTAGES--TODAY
 - BP -- 50%
 - ARCO -- 22%
 - EXXON -- 20%
 - Other -- 8%

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TRANSPORTATION-TAPS

- TAPS OWNERSHIP PERCENTAGES--
TOMORROW?

- BP -- 72%

- EXXON -- 20%

- Other -- 8%

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TRANSPORTATION-TAPS FEEDER PIPELINES

- TAPS FEEDER PIPELINE OWNERSHIP PERCENTAGES

- ENDICOTT

- BP -- 57%
 - EXXON -- 21%
 - Other -- 22%

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TRANSPORTATION-TAPS FEEDER PIPELINES

- TAPS FEEDER PIPELINE OWNERSHIP PERCENTAGES

- Milne Point

- BP -- 91%

- Oxy -- 9%

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TRANSPORTATION-TAPS FEEDER PIPELINES

- Kuparuk
 - BP -- 38%
 - ARCO -- 57%
 - Unocal -- 5%
- Kuparuk Pipeline Tomorrow?
 - BP -- 95%

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TRANSPORTATION-TAPS FEEDER PIPELINES

- Oliktuk (a pipeline bringing NGLs from Prudhoe to Kuparuk for EOR)
 - Today -- ARCO -- 100%
 - Tomorrow? BP -- 100%

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TRANSPORTATION-TAPS FEEDER PIPELINES

- ALPINE
 - Today -- ARCO -- 100%
 - Tomorrow? BP -- 100%



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TRANSPORTATION-TAPS FEEDER PIPELINES

- BADAMI
 - BP -- 100%



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TRANSPORTATION-TANKERS

- TANKER OWNERSHIP PERCENTAGES (by tonnage)--
TODAY
 - BP -- 41%
 - ARCO -- 32%
 - EXXON -- 21%
 - Other (Tesoro, Chevron) -- 6%

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TRANSPORTATION-TANKERS

- TANKER OWNERSHIP PERCENTAGES (by tonnage)--
TOMORROW?
 - BP -- 73%
 - EXXON -- 21%
 - Other (Tesoro, Chevron) -- 6%

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MARKETING

- Today, 100% of BP's ANS production is sold to third parties, either for cash or for an exchange of other crude.
- None of it is internally refined.

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MARKETING

- Most--the vast majority-- goes to the US West Coast.
- Some is sold here, some is shipped to Hawaii, and some is shipped to Asia.

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MARKETING

- ARCO has two refineries on the West Coast (one near Los Angeles and the Cherry Point refinery in Washington)
- The combined capacity of these refineries is estimated to be 457,000 bbd, or 140,000 bbd more than ARCO's current estimated production

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MARKETING

- Of BP's estimated combined (post merger) production of 790,000 bbd, approximately 460,000 could be refined internally
 - Instead of selling 470,000 bbd to third parties as it does today, BP might have only 330,000 bbd or so available to sell
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What This Means

- This merger, assuming it goes through, is likely to have significant effects on the way Alaskan oil and gas resources are leased, produced, transported and marketed.
- If nothing else, it will place BP in a position of dominance over all aspects of ANS development.

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Next Steps

- The Administration has identified six areas of serious concern where the state will be examining the proposed merger. They are:
 - The value of North Slope crude oil,
 - Marine transportation,
 - Operation of the Trans-Alaska oil pipeline,
 - The development of other North Slope facilities and fields,
 - Natural gas development,
 - Leasing of acreage for oil and gas development, currently held and future sales.

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Next Steps

- First, the value of North Slope oil. BP currently has had an incentive to keep the ANS spot price as high as possible.
- One result of this merger may be a reversal in that role. Because BP-Amoco will now find itself refining its own crude in its own West Coast refineries, the incentive to keep ANS spot prices high may disappear. We want to closely examine what effect this may have on Alaska taxes, royalties and revenues.

Next Steps

- Second, marine transportation. As a post-merger producer of more than 70 percent of oil produced from the North Slope, the new BP-Amoco will also control more than 70 percent of the available Jones Act tanker capacity for transporting Alaskan oil to West Coast markets.

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Next Steps

- We're pleased BP already has indicated plans to proceed with ARCO's construction of three new millennium-class tankers for the Alaska market.
- However, this level of control raises potential concerns about the availability and cost of marine transportation for companies other than BP-Amoco and Exxon. We want to examine the implications of essentially only two companies involved in the transportation of Alaska oil.

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Next Steps

- Third, operation of the Trans-Alaska oil pipeline. Right now, there is the potential for competition among the pipeline affiliates of the North Slope producer.
- But after the merger, BP will control more than 70 percent of the pipeline and this will remove much of this potential for competition. We need to closely examine the impacts of reduced competition and the possible effects on the tariffs charged for shipping oil down the pipeline.

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Next Steps

- Fourth, is development of other North Slope facilities and fields. This administration, working with the Legislature, has provided incentives for the development of new North Slope fields, especially around Prudhoe Bay and Kuparuk.
- We want to make sure the newly merged company continues its interest in developing these satellites, which provide jobs for Alaskans and work for Alaska businesses.

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Next Steps

- In addition, with BP owning 70 percent or more of the development infrastructure on the North Slope, we also must address the question of when and under what terms others can use this infrastructure, because
 - we want to ensure the greatest possible competition for future lease sales and development on the North Slope, and
 - we want to avoid the economically wasteful and environmentally unsound practice of building duplicative facilities.

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Next Steps

- Fifth, is the development of North Slope natural gas.
As you know, this development has been a top priority of the administration and it has worked with the Legislature to encourage its development.
- To its credit, ARCO has taken the lead in natural gas development, forming a consortium to determine the economics of gas commercialization.

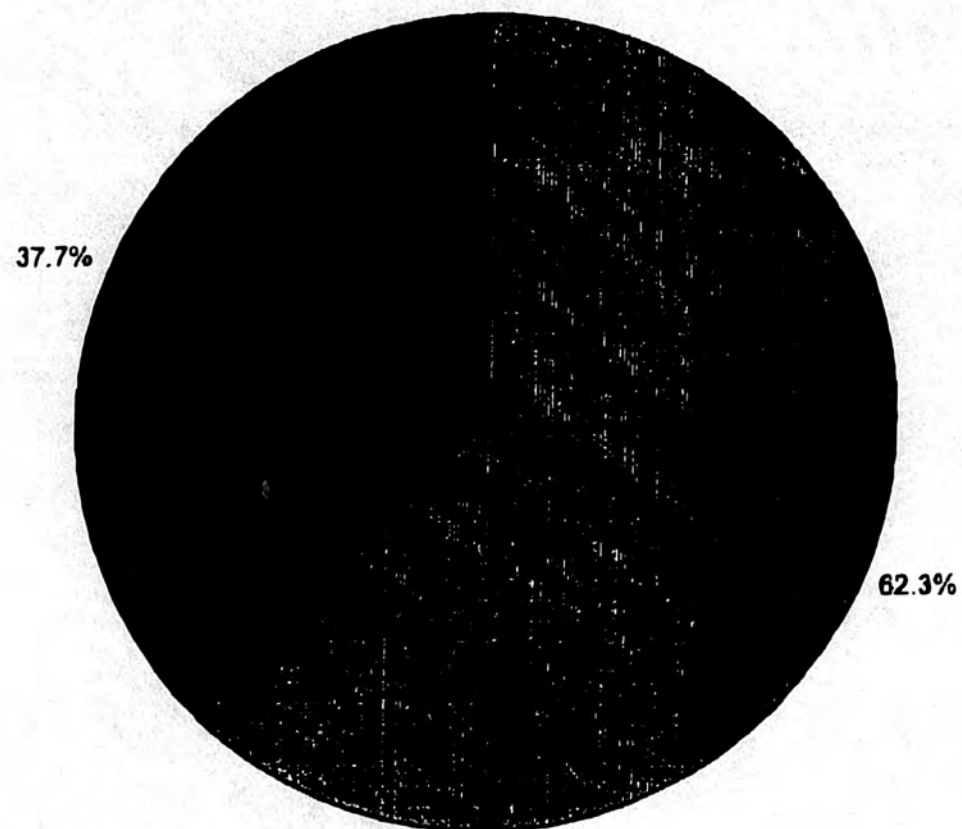
Next Steps

- Our review will include an examination of ways to encourage the production of North Slope gas and we will review BP-Amoco's approach to the new gas to liquids technology which they've discussed with a new pilot project on the North Slope.
- We want to make sure the merger creates no obstacles to natural gas development and the construction of a gas pipeline.

Next Steps

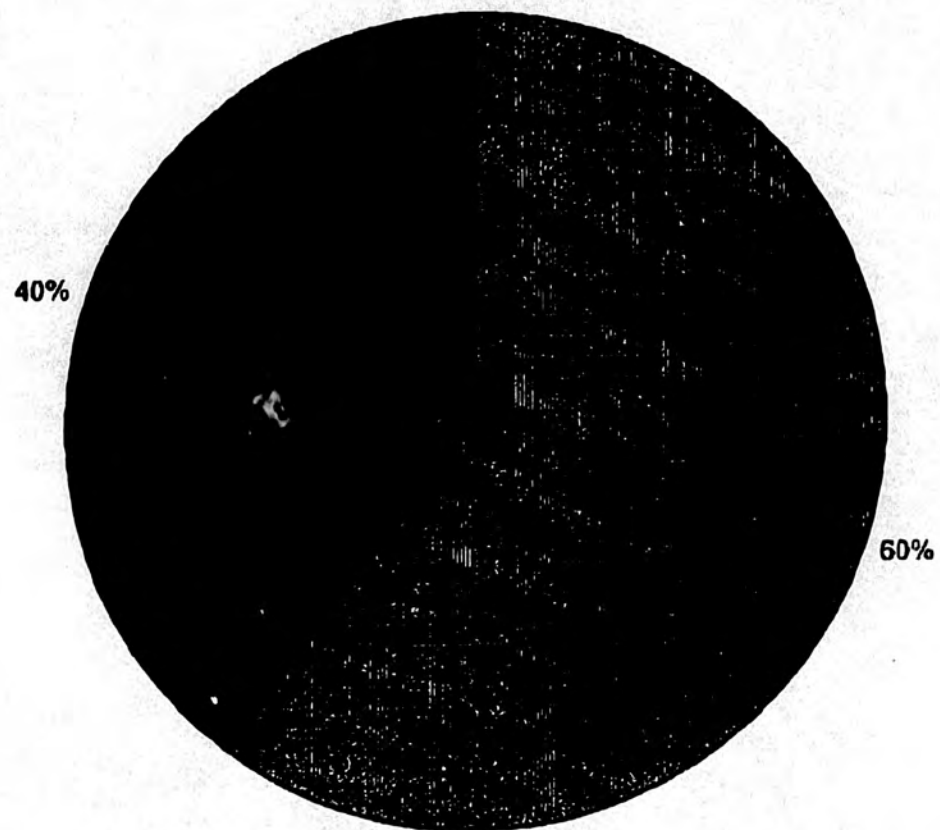
- Sixth, is the issue of leasing land for oil and gas development. There has been competition among the companies developing North Slope oil. And we've worked to encourage even more leasing, with area-wide leasing.
- With the proposed merger, we want to make sure this heightened interest continues as the state and federal government make available lands for oil and gas leasing.

PT. MCINTYRE - POST MERGER



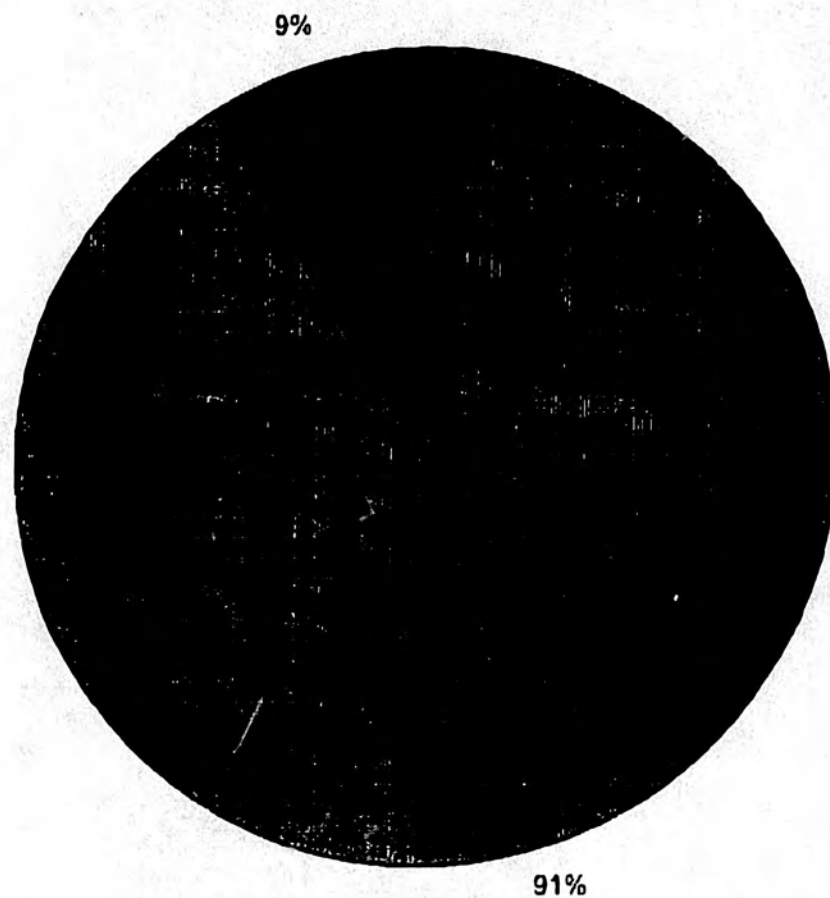
BP
EXXON

LISBURNE - POST MERGER

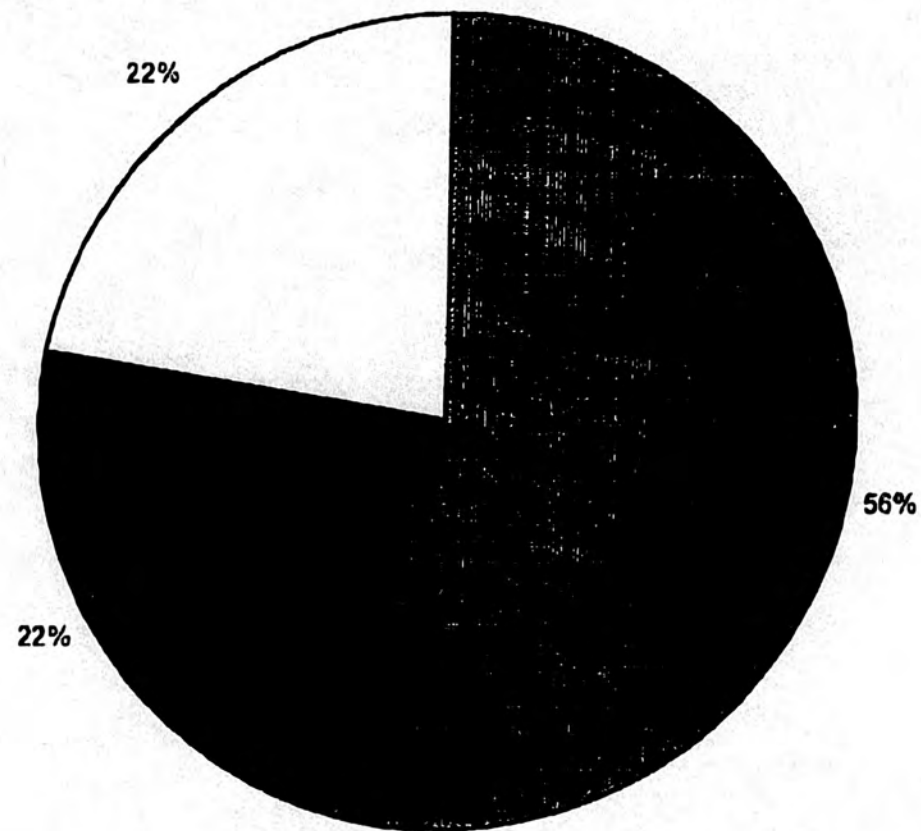


■ BP EXPLORATION
■ EXXON

MILNE POINT - POST MERGER

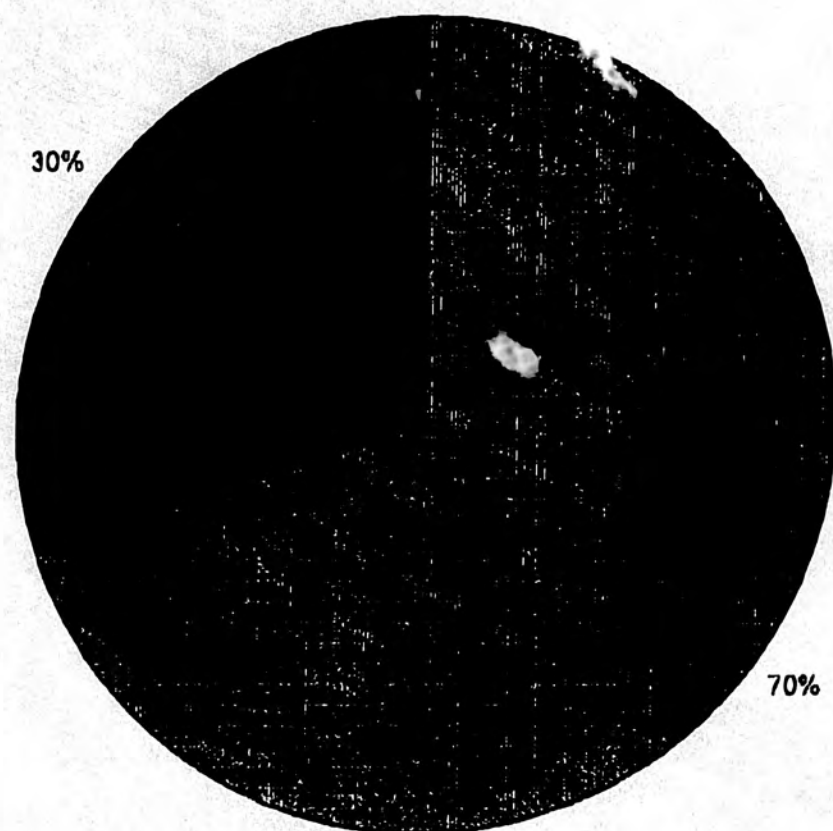


ALPINE - POST MERGER



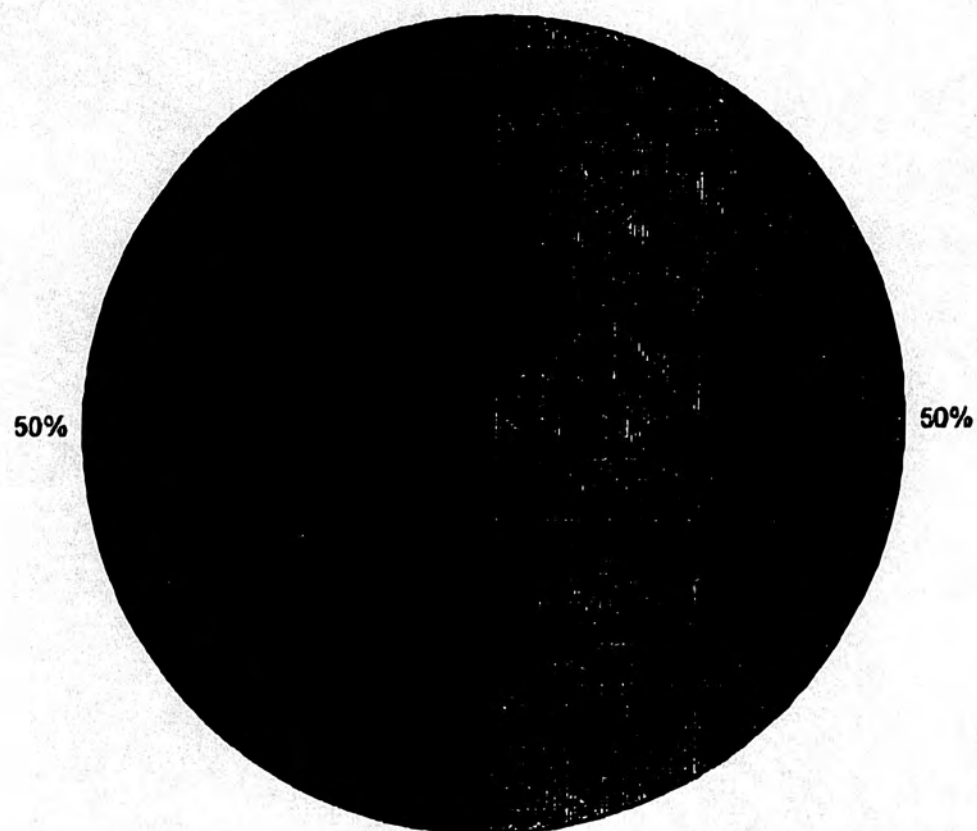
■ BP
■ ANADARKO
□ UNION TEXAS

BADAMI - POST MERGER



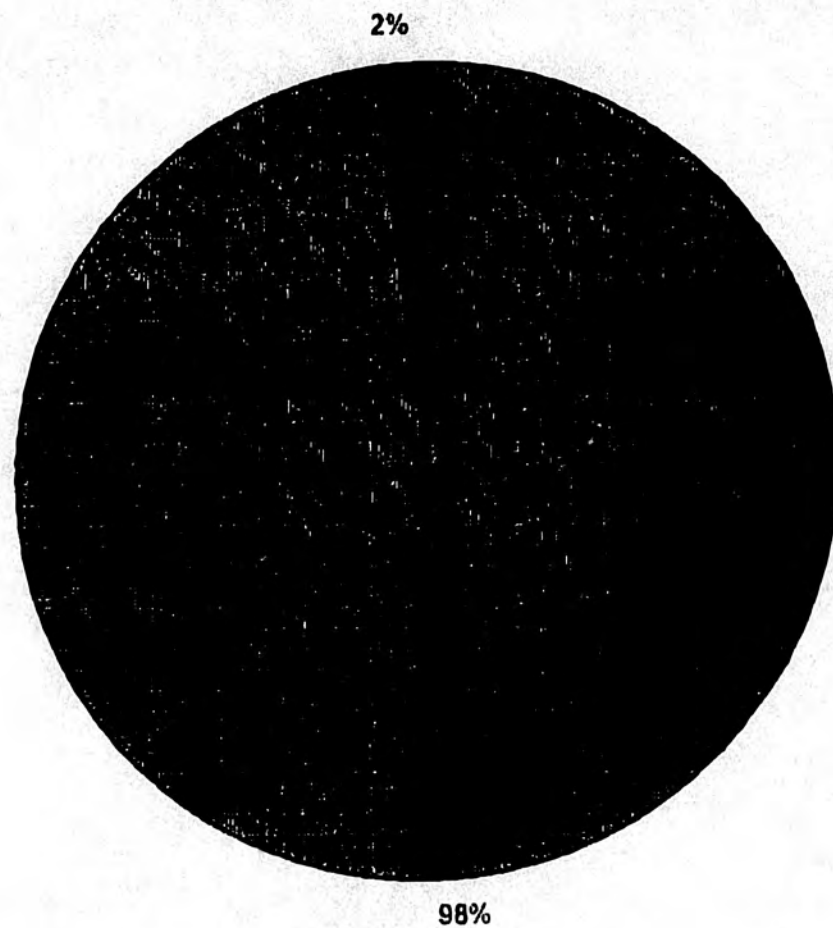
■ BPX
■ PETROFINA

NORTH PRUDHOE - POST MERGER



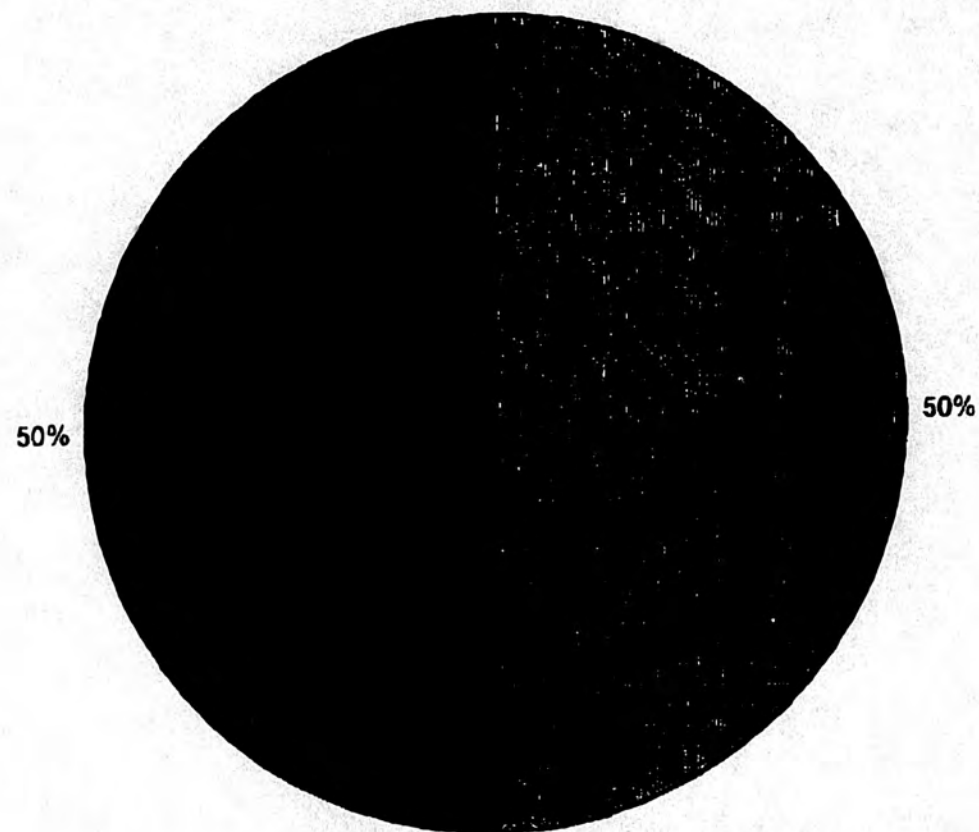
■ BP
■ EXXON

NORTHSTAR - POST MERGER

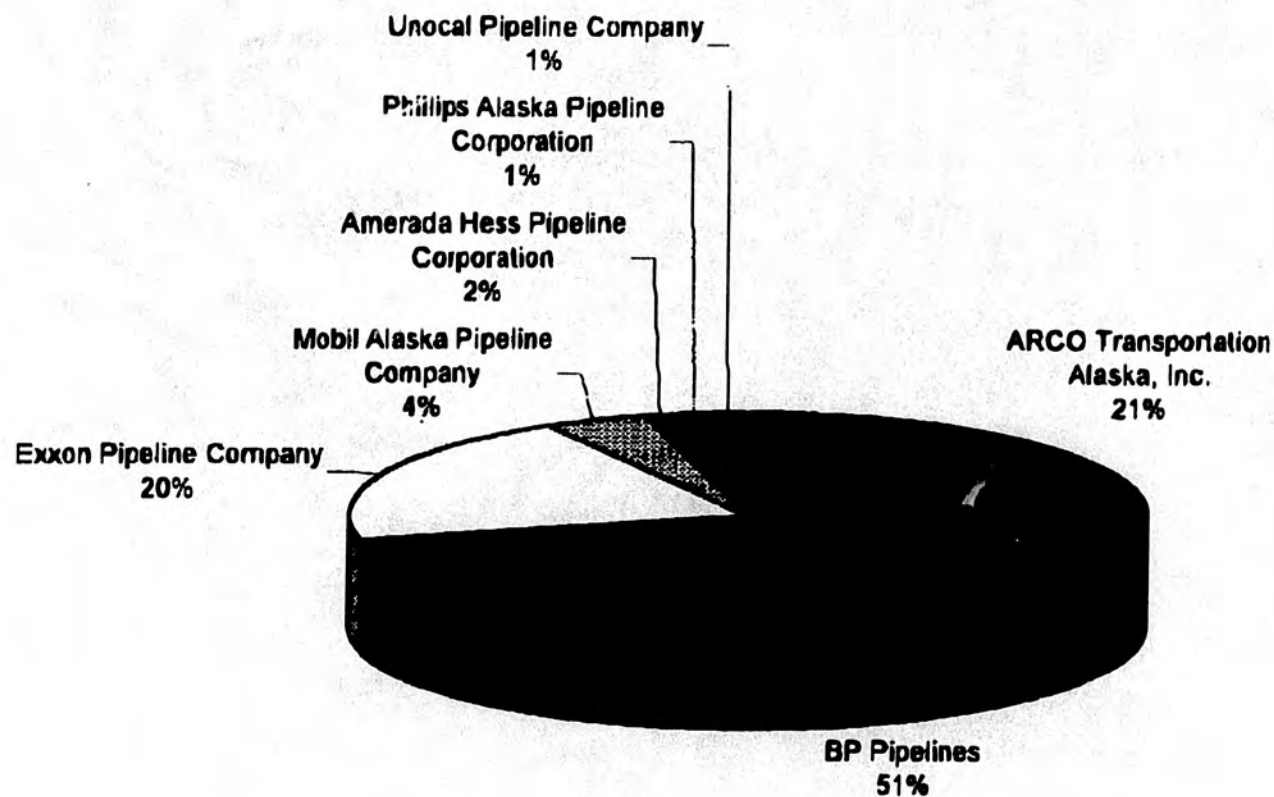


■ BP EXPLORATION
■ MURPHY E & P

WEST BEACH - POST MERGER

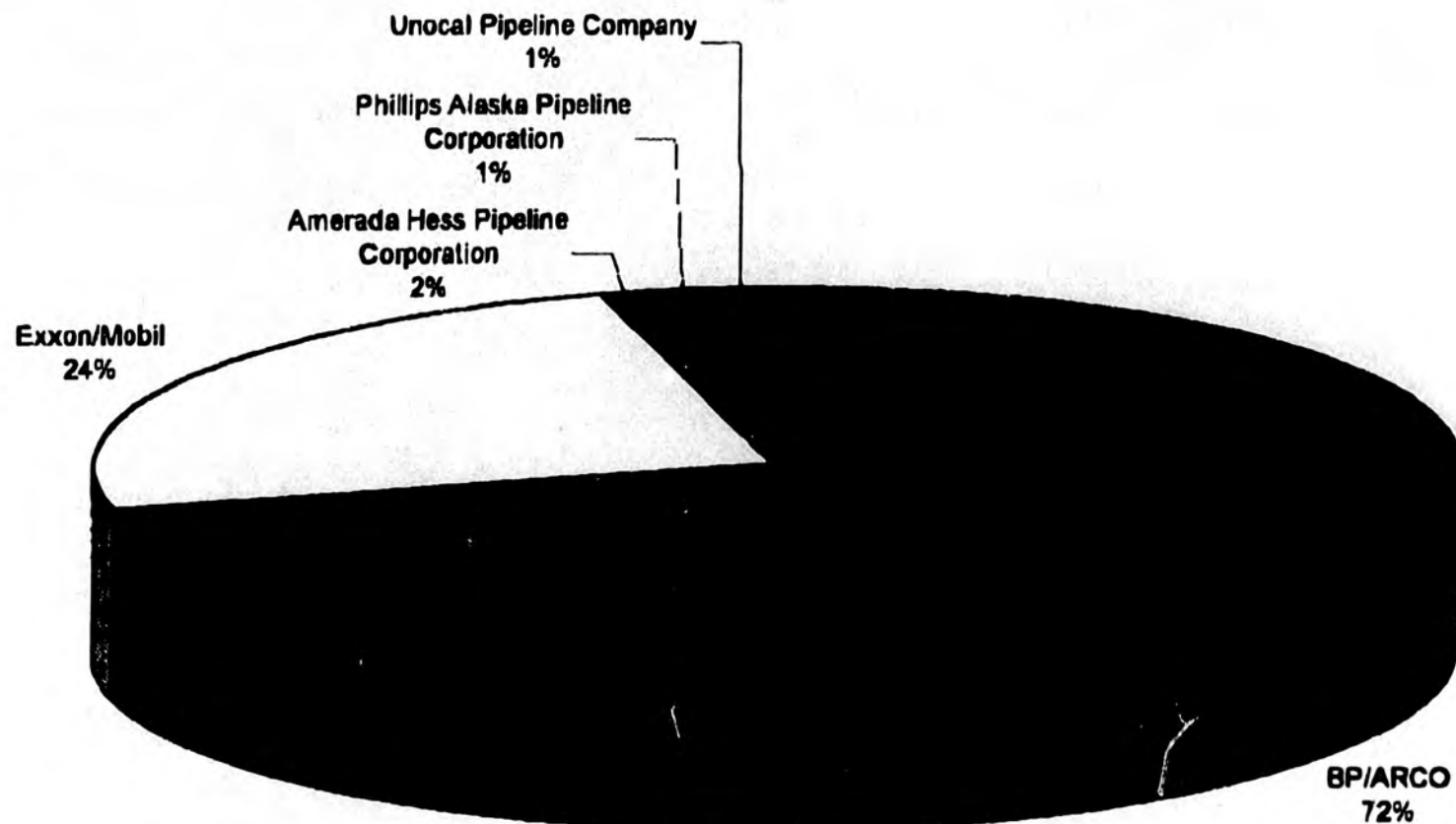


■ BP
■ EXXON



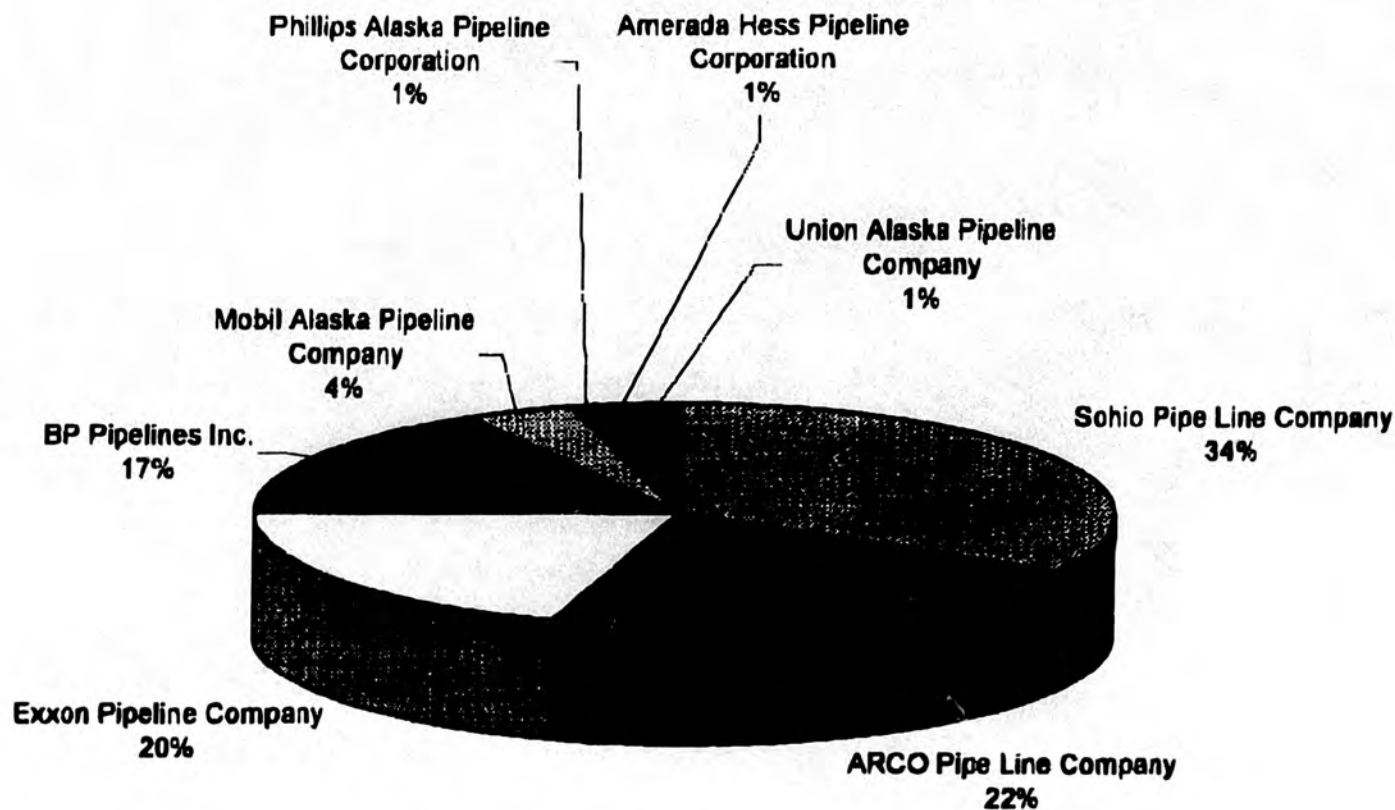
**Trans Alaska Pipeline System
Current Ownership Shares**

■ ARCO Transportation Alaska, Inc.	■ BP Pipelines	□ Exxon Pipeline Company
▨ Mobil Alaska Pipeline Company	■ Amerada Hess Pipeline Corporation	▨ Phillips Alaska Pipeline Corporation
■ Unocal Pipeline Company		



**Trans Alaska Pipeline System
Post Merger Shares**

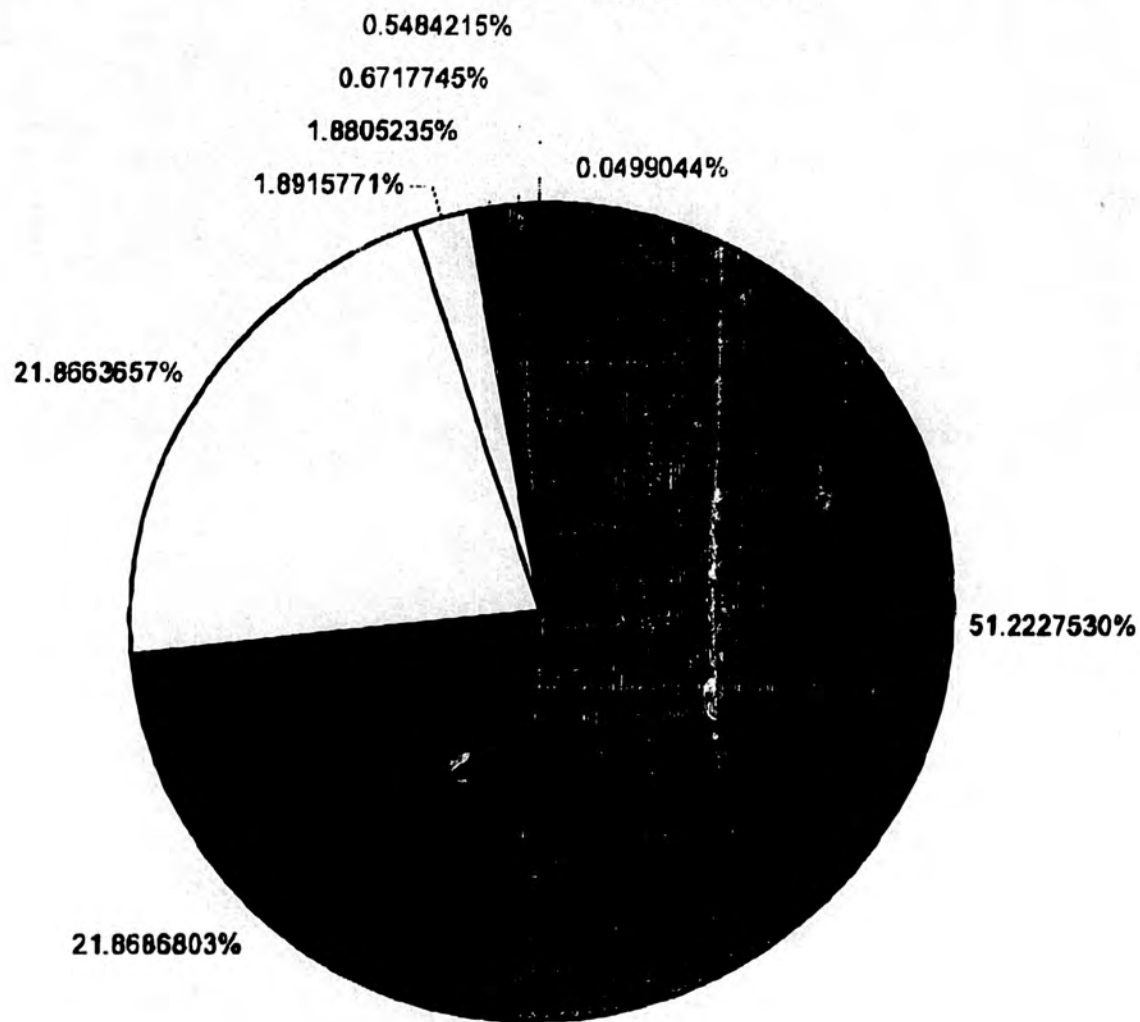
■ BP/ARCO □ Exxon/Mobil ■ Amerada Hess Pipeline Corporation ■ Phillips Alaska Pipeline Corporation ■ Unocal Pipeline Company



**Trans Alaska Pipeline System
1985 Settlement Percentage Ownership Shares**

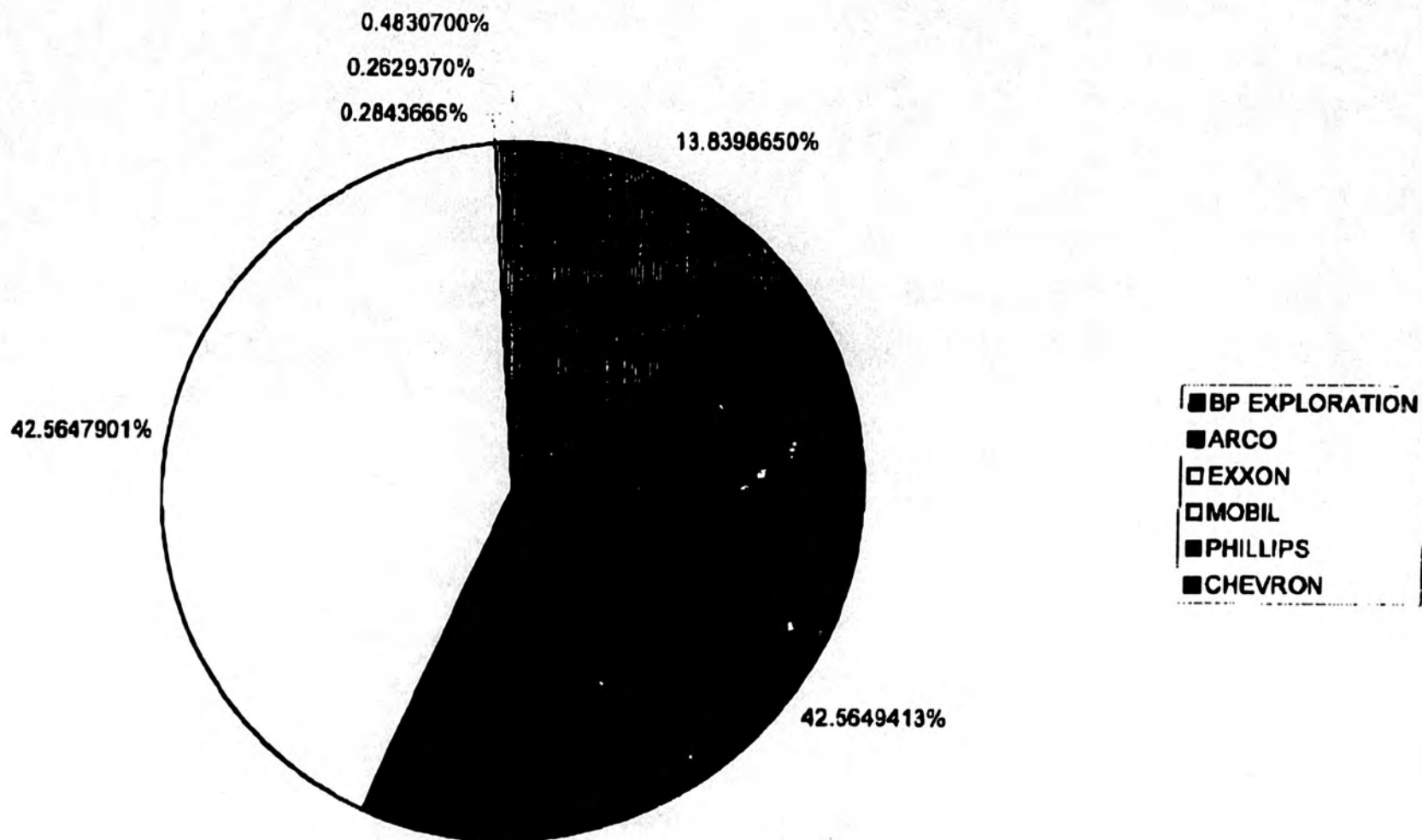
■ Sohio Pipe Line Company	■ ARCO Pipe Line Company	□ Exxon Pipeline Company
■ BP Pipelines Inc.	■ Mobil Alaska Pipeline Company	■ Phillips Alaska Pipeline Corporation
■ Amerada Hess Pipeline Corporation	■ Union Alaska Pipeline Company	

PBU OIL RIM

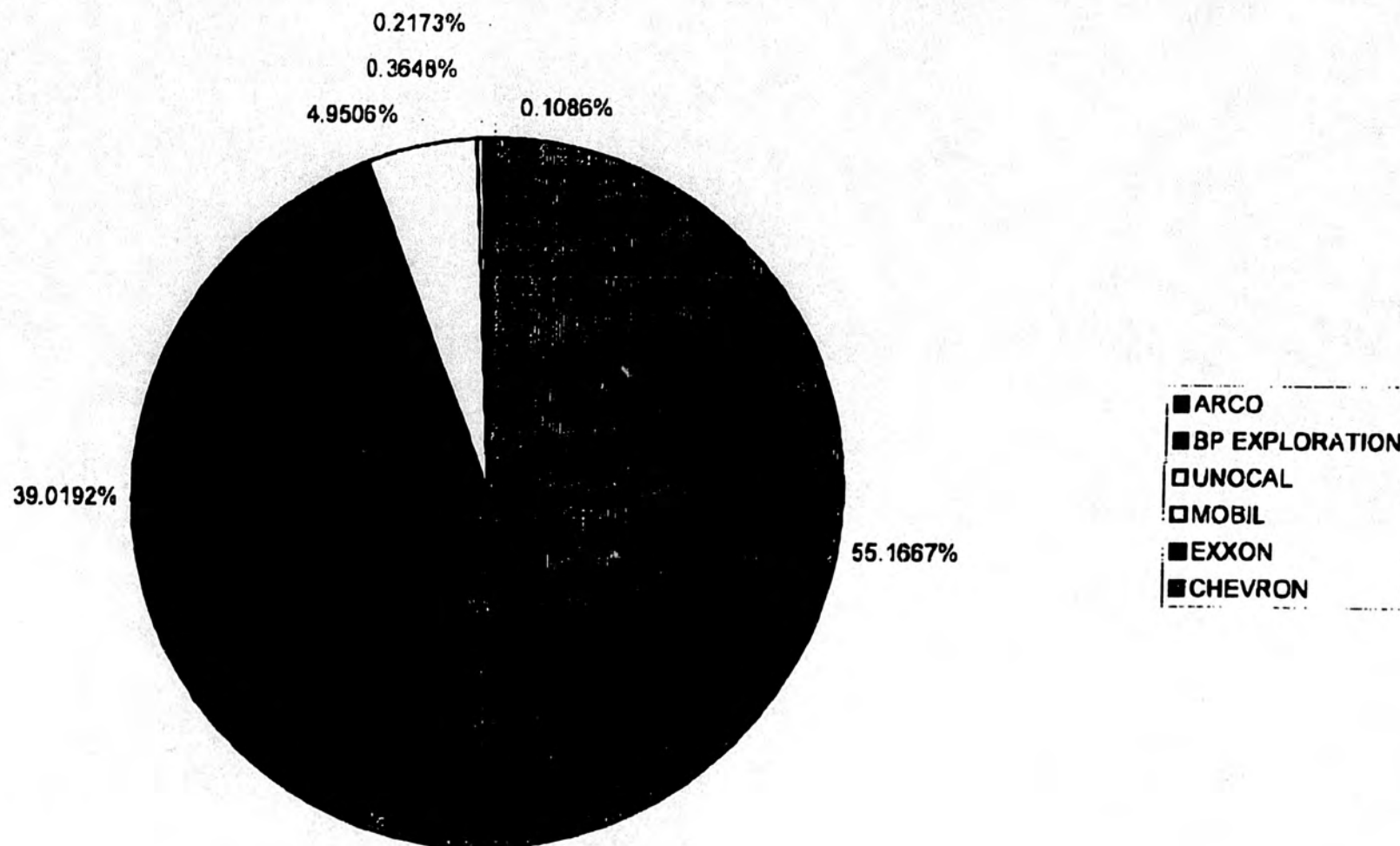


- BP EXPLORATION
- ARCO
- EXXON
- MOBIL
- PHILLIPS
- CHEVRON
- TEXACO
- FORCENERGY

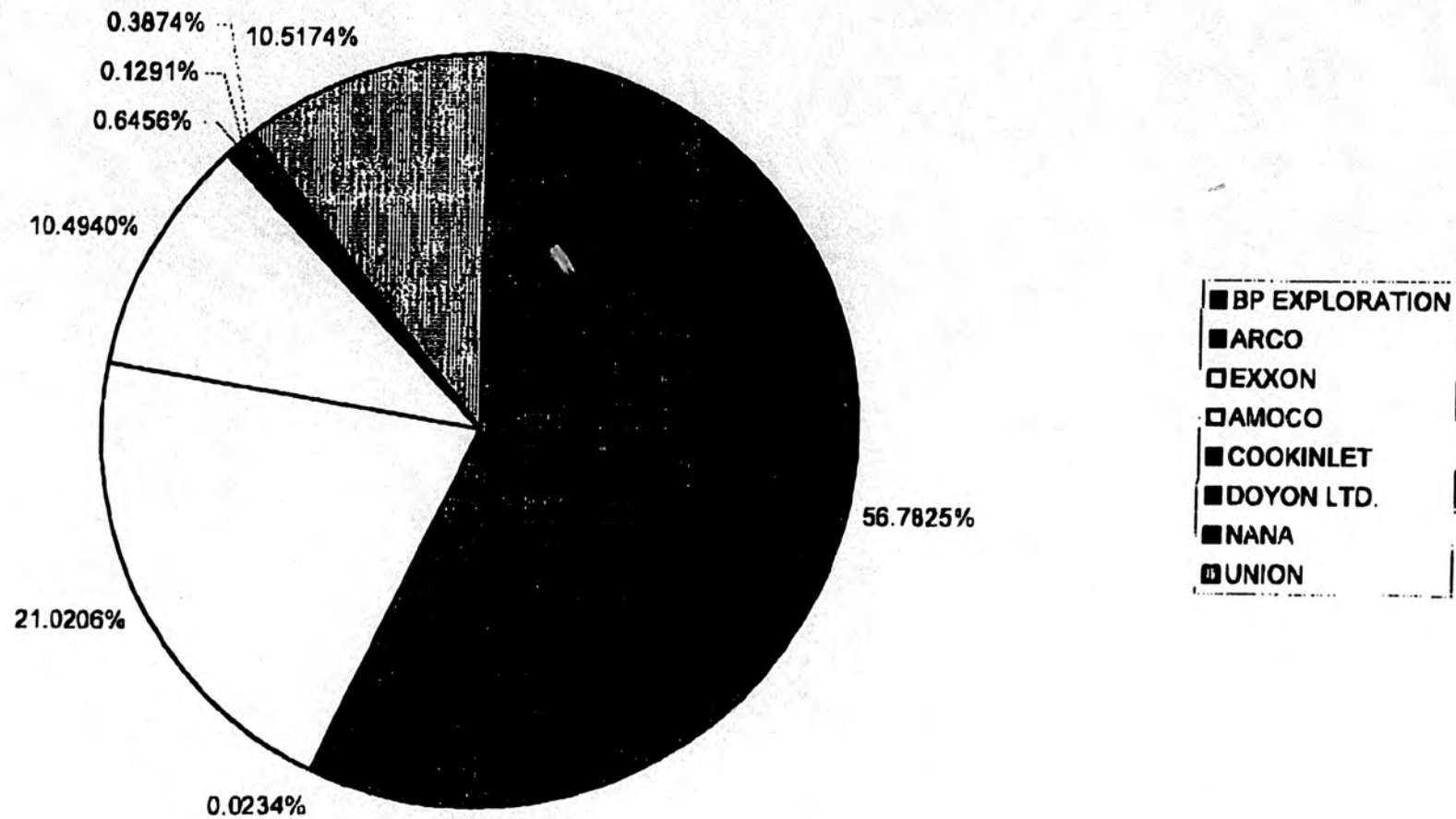
PBU GAS CAP



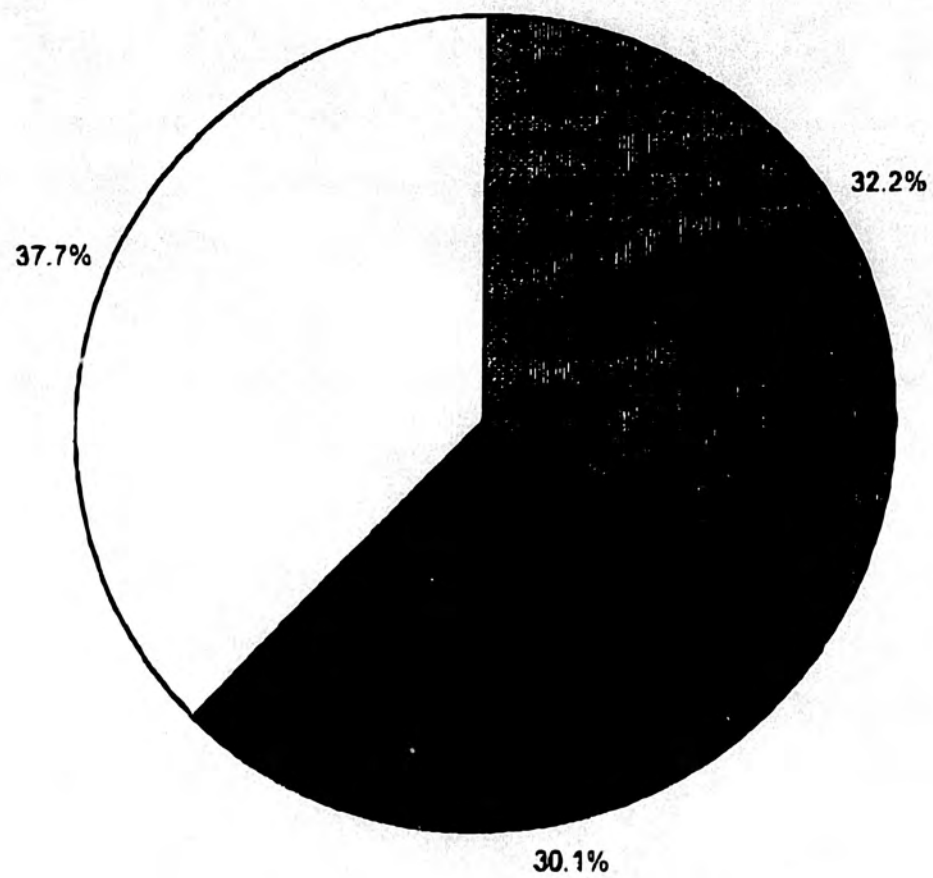
KUPARUK RIVER UNIT



DUCK ISLAND UNIT ENDICOTT P.A.

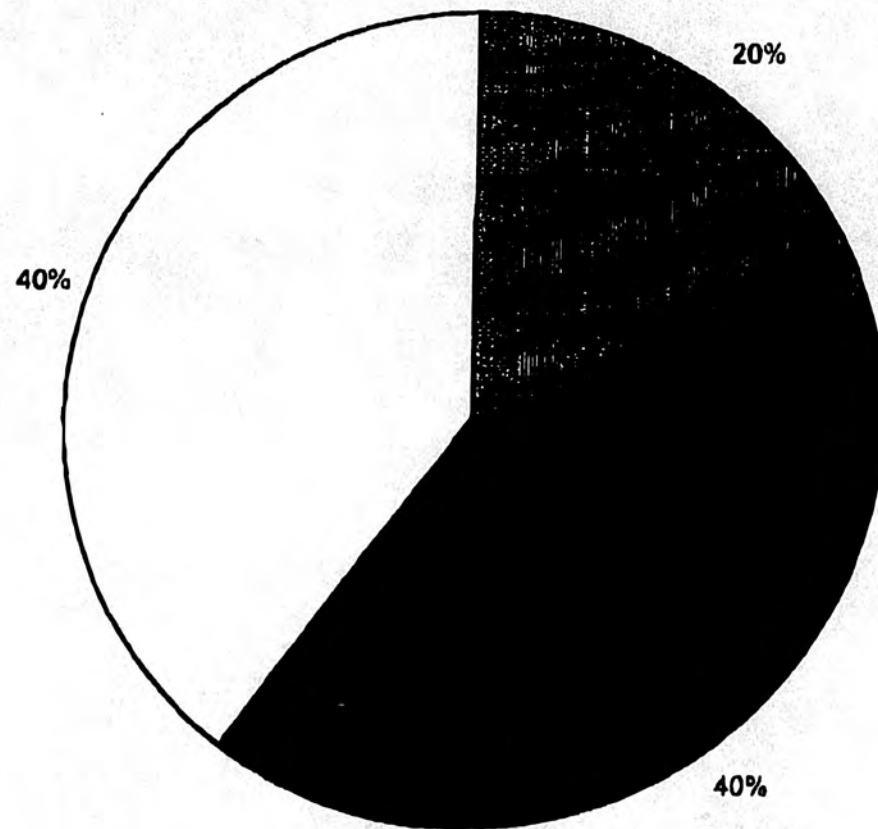


PT. MCINTYRE P.A.



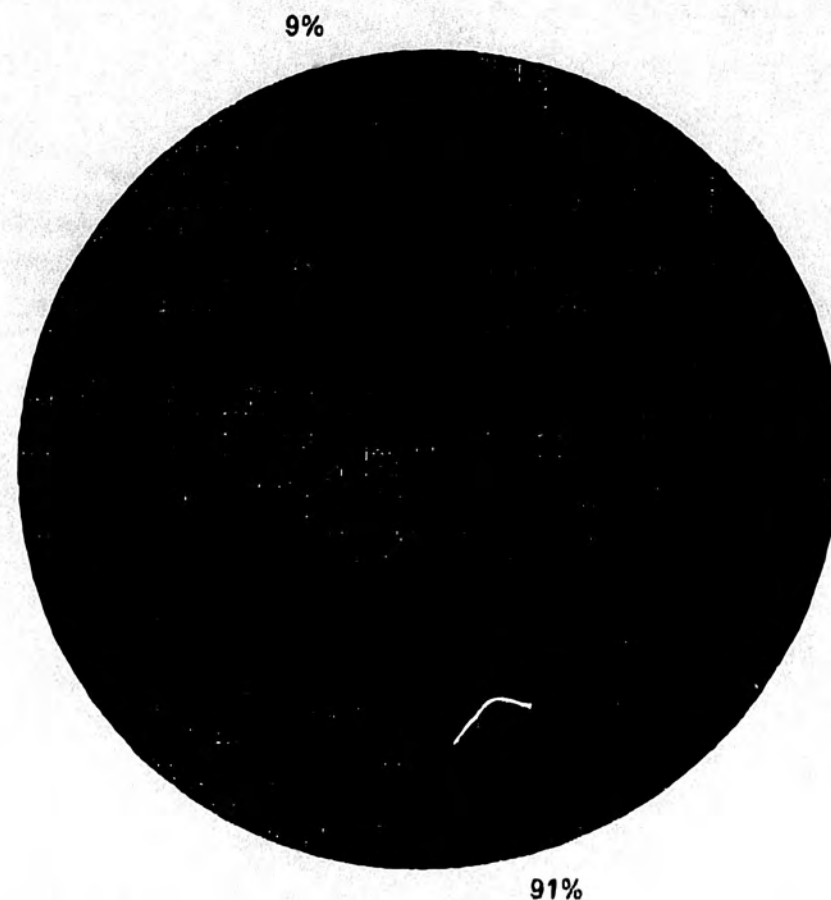
■ BP EXPLORATION
■ ARCO
□ EXXON

LISBURNE P.A.



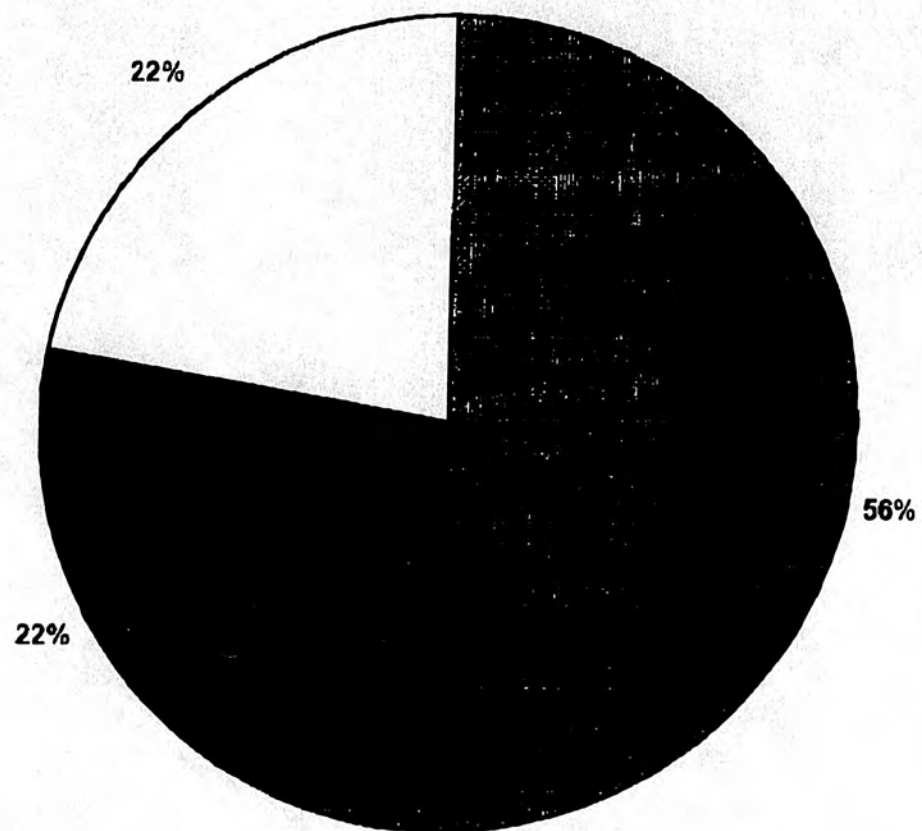
■ BP EXPLORATION
■ ARCO
□ EXXON

MILNE POINT UNIT



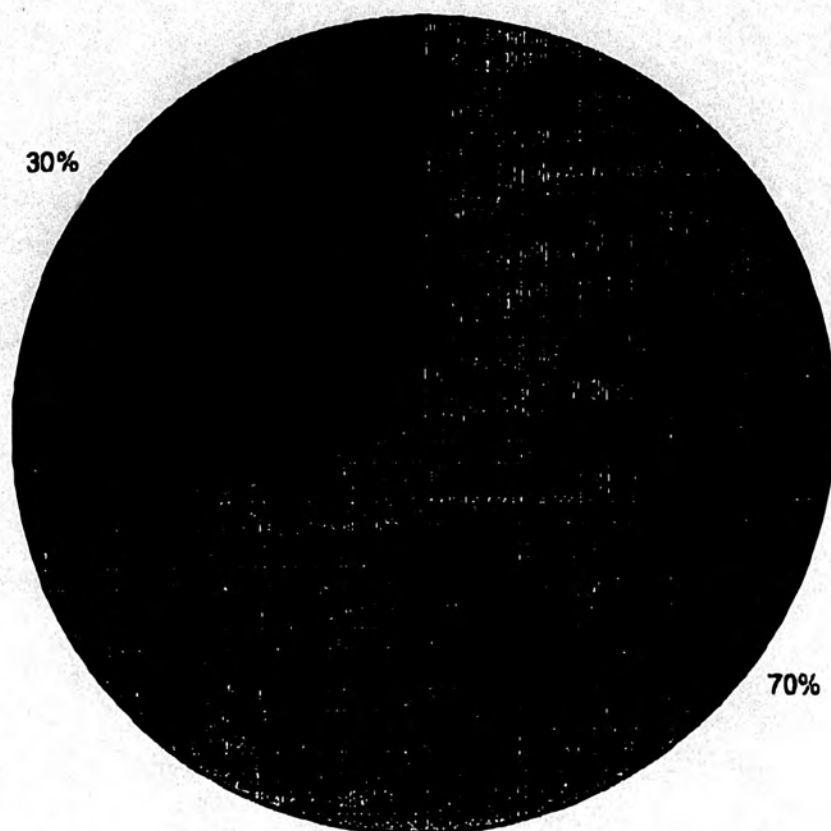
■ BP EXPLORATION
■ OXY

ALPINE



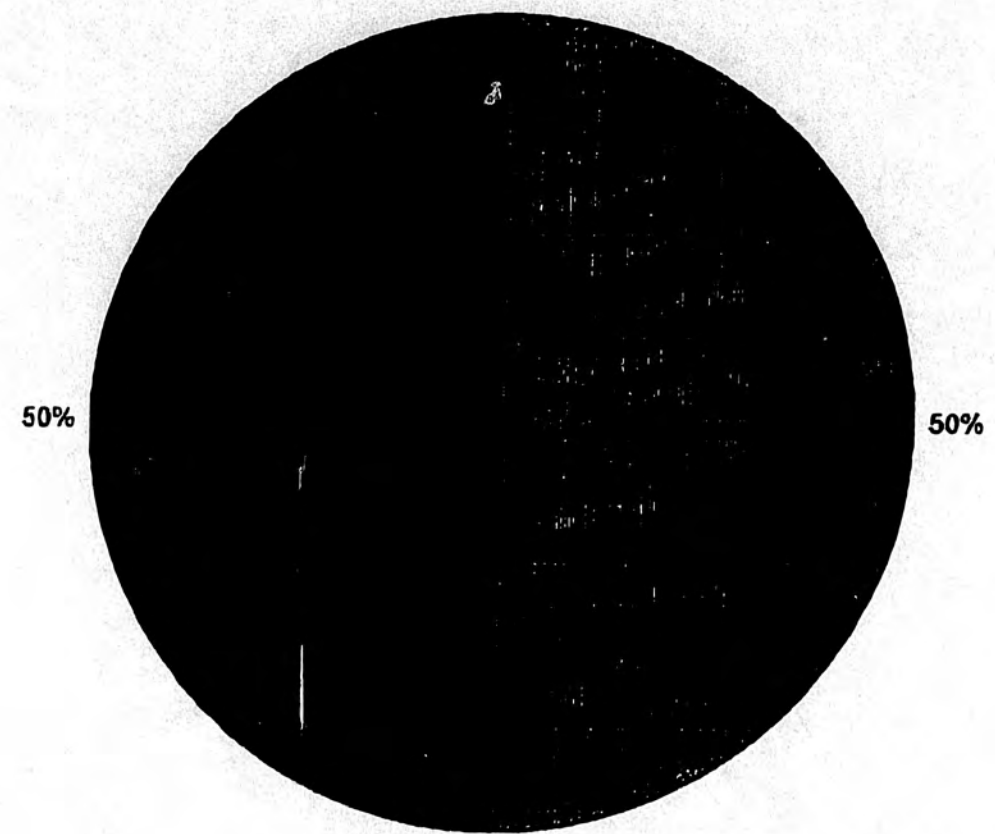
■ ARCO
■ ANADARKO
□ UNION TEXAS

BADAMI UNIT



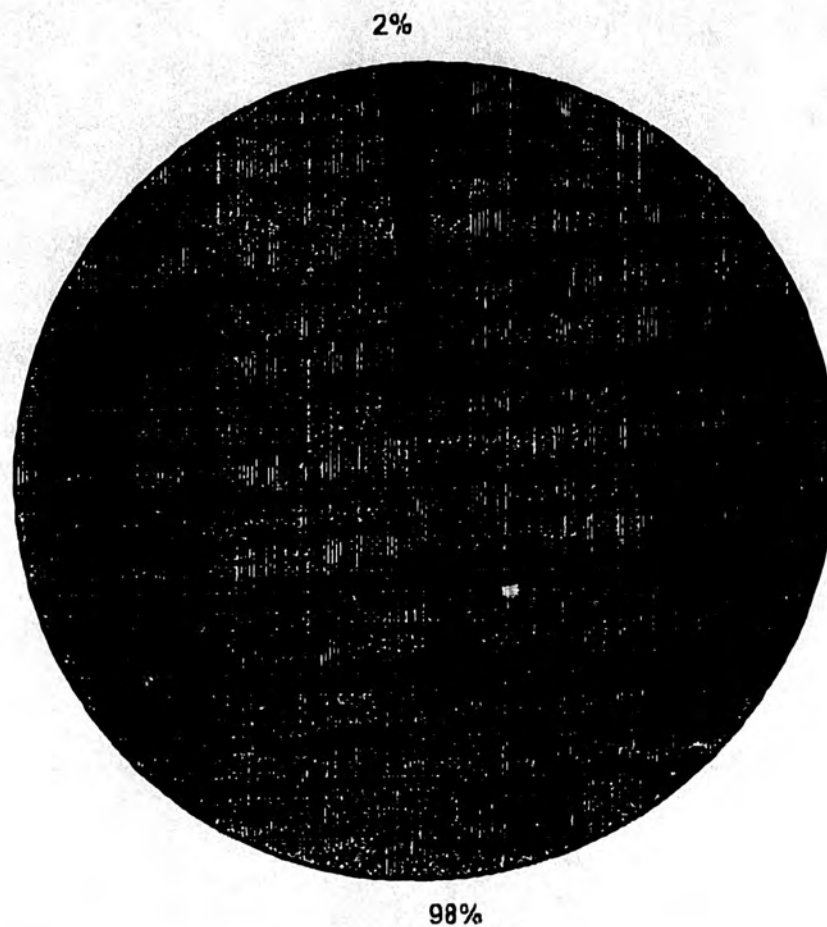
■ BPX
■ PETROFINA

NORTH PRUDHOE P.A.



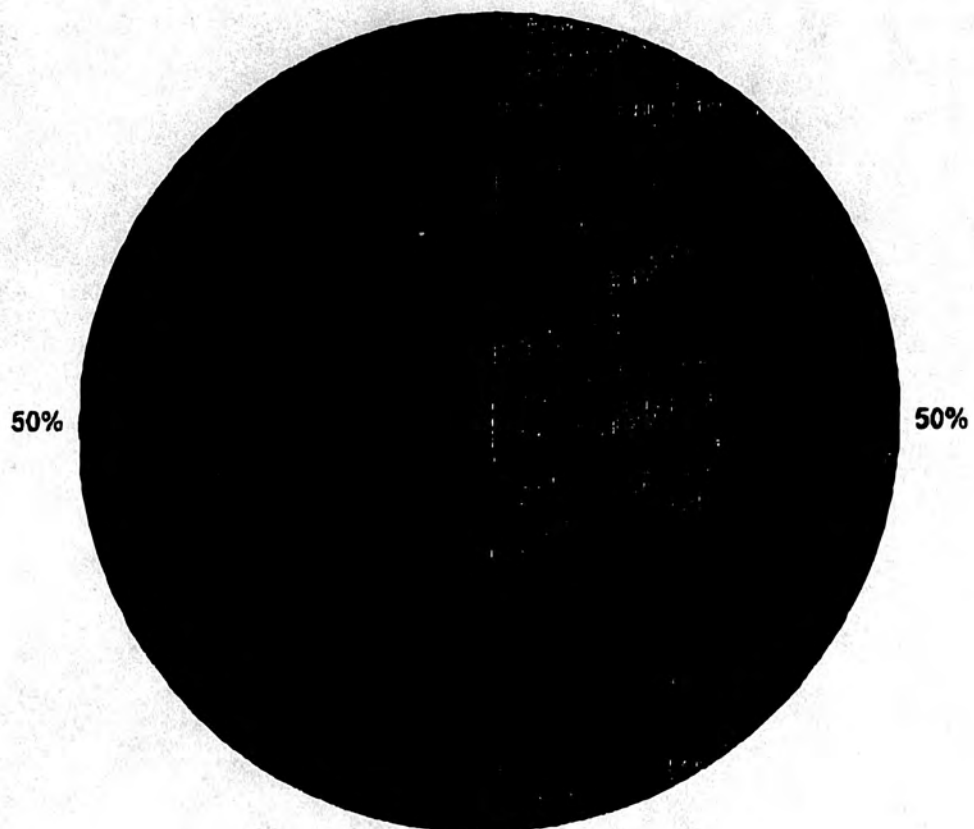
■ ARCO
■ EXXON

NORTHSTAR UNIT

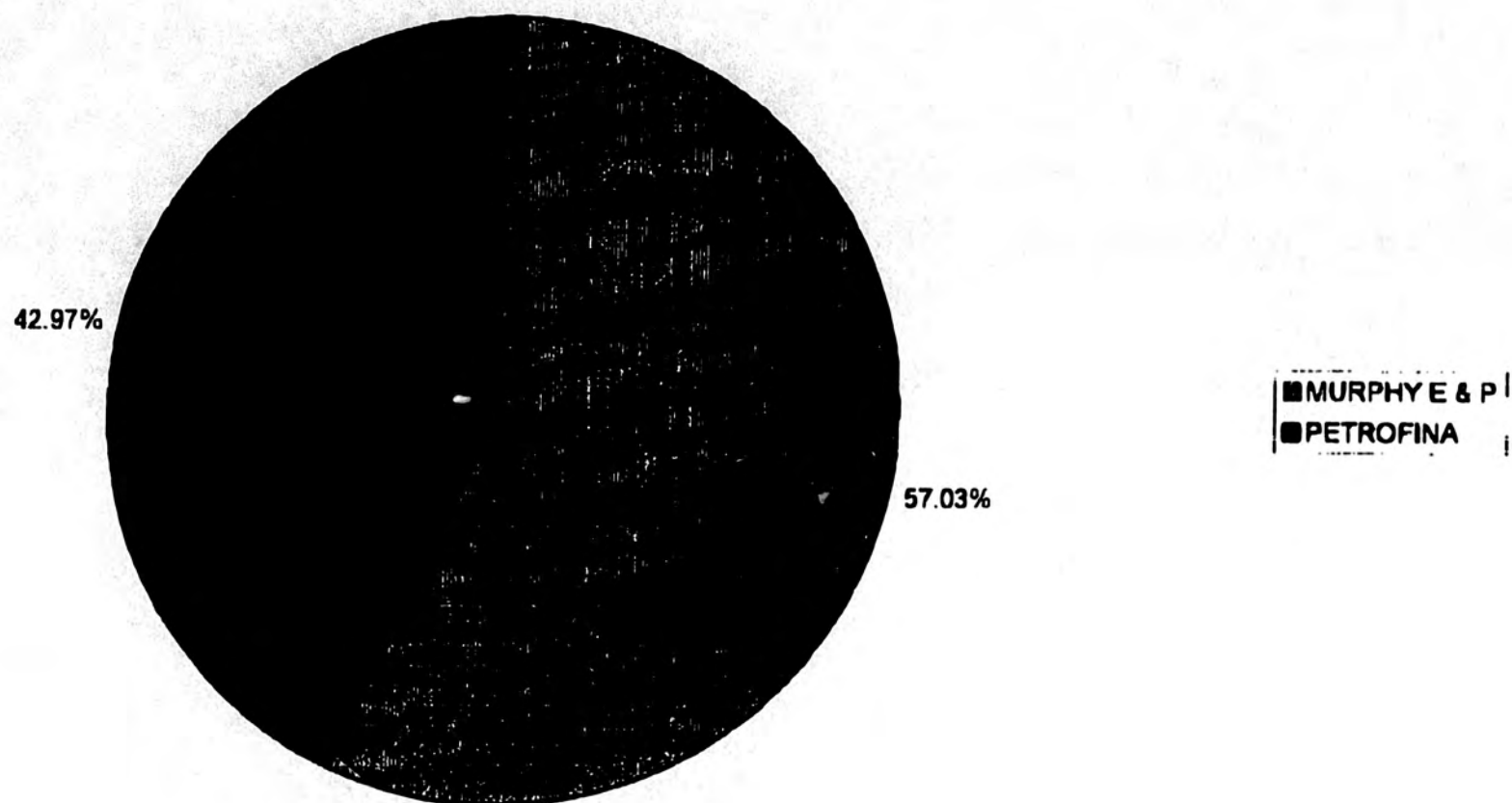


■ BP EXPLORATION
■ MURPHY E & P

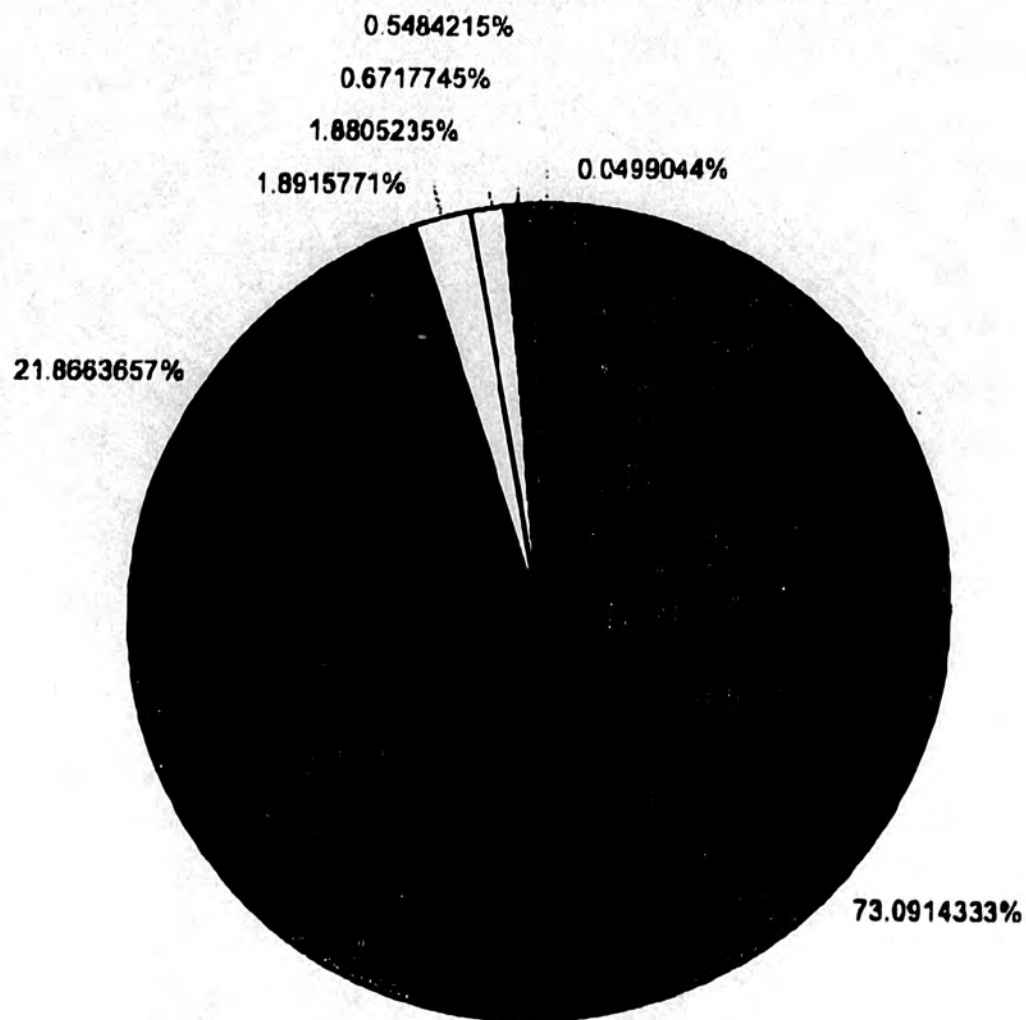
WEST BEACH P.A.



SANDPIPER UNIT

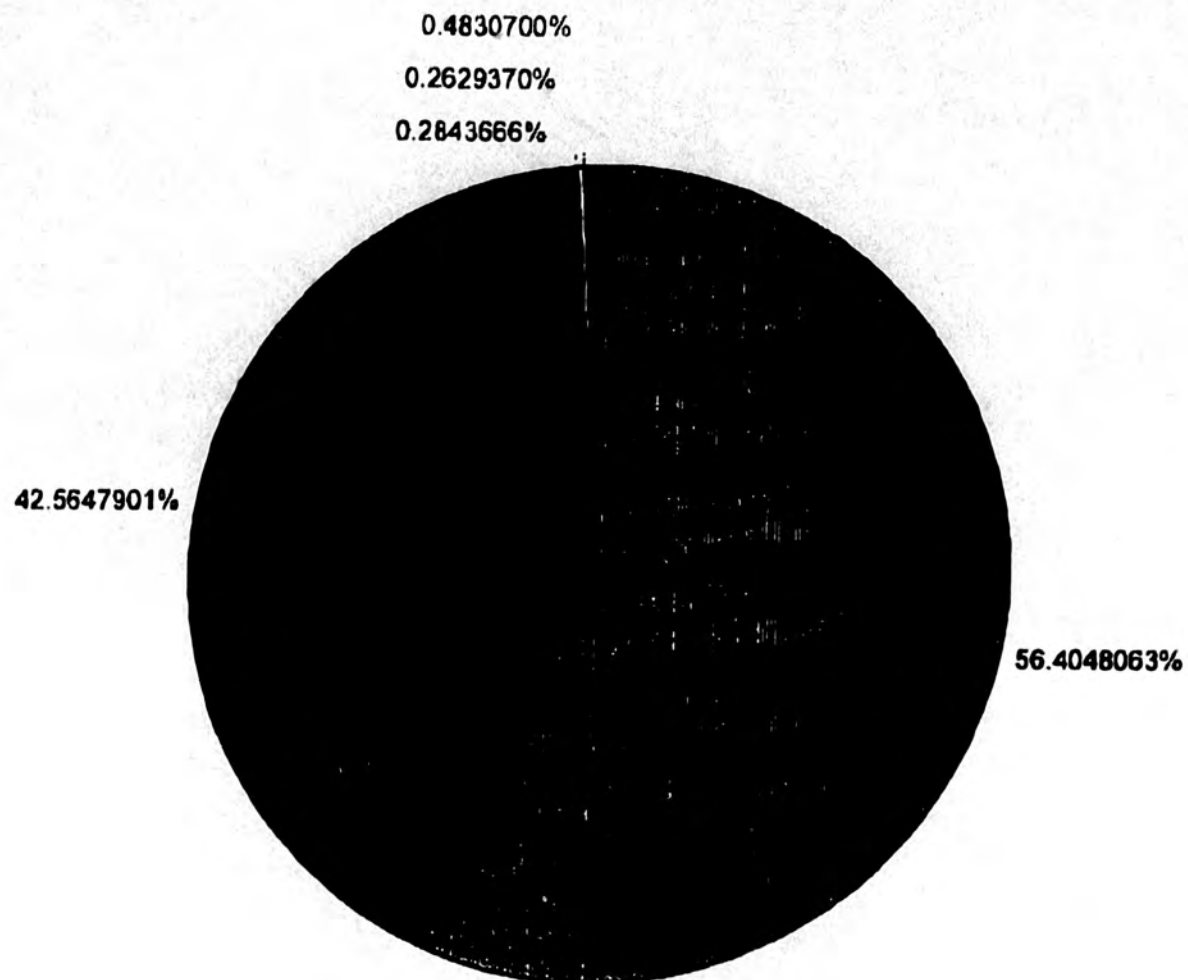


PBU OIL - POST MERGER

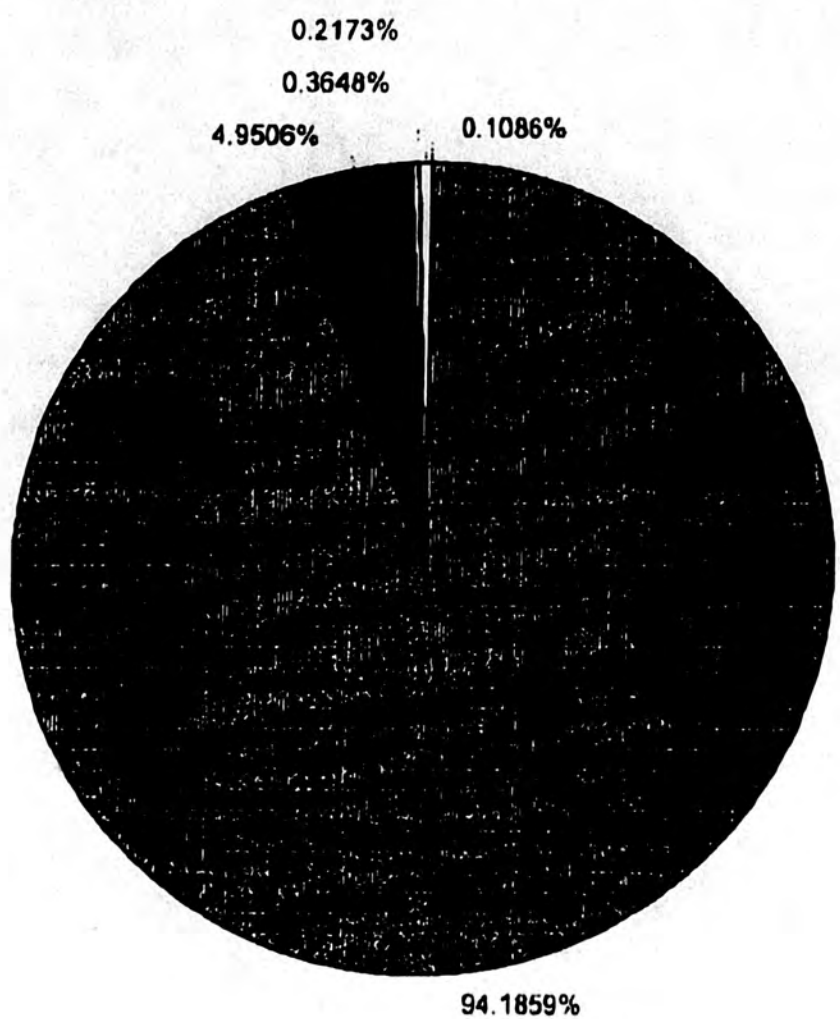


- BP
- EXXON
- MOBIL
- PHILLIPS
- CHEVRON
- TEXACO
- FORCENERGY

PBU GAS - POST MERGER



KUPARUK - POST MERGER



- BP
- UNOCAL
- MOBIL
- EXXON
- CHEVRON

DUCK/ENDICOTT - POST MERGER

