

ALASKA LEGISLATURE

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HOUSE and SENATE FINANCE COMMITTEE FILES, 1995-1996

discusses "production removed or sold from the lease" and the "share of the net profit derived from the lease" when describing the NP&L bidding method. (Emphasis added.) A plain reading of this language indicates that calculations are based on the money expended upon and earned from the lease. The statute does not suggest an intent to link these accounts to a particular lessee.

BP's analysis of the legislative history, the analogous federal statute, and other regulations support this reading, which is also apparent from the statute's face. For example, BP points to various reports contemplated by the Legislature when discussing the Alaska Land Act's 1978 amendments. Of particular interest is a 1977 report by Mason Gaffney, "Oil & Gas Leasing Policy: Alternatives for Alaska in 1977 (A Report to the State of Alaska, Jay S. Hammond, Governor, Department of Natural Resources, Guy Martin, Commissioner, and to the Alaska State Legislature, Interim Committee on Oil and Gas Taxation and Leasing Policy, Chancy Croft, Chairman)" (Feb. 1, 1977) (Microfiche No. 511-517, Anchorage Law Library). In this report, Gaffney discusses the net profit share in terms of a "net proceeds tax", and notes that this tax "is in rem: it is levied on the income and expenses attributable to a particular 'thing', in this case the leasehold". Id. at 52-53. He clearly distinguishes it from the example of an income tax, which is levied "in personam". Id.

The analogous federal statute and regulations, found in 43 U.S.C. § 1337(a)(1)(D), (E), (F) (West 1986) and 30 C.F.R. 220, also aid interpretation. In answer to a question about the assignability of the development account (called a "capital recovery account", in the federal scheme), the federal Minerals Management Service stated:

Because the NPSSL capital account is maintained by lease and includes all costs incurred during the term of the NPSSL, any costs incurred by the lessee would be carried forward to the assignee in the case of a farmout. That is, the assignee would begin NPSSL operation with the same balance in the NPSSL capital account as that remaining at the time of the farmout. December 3, 1985 letter from William S. Goldmiller, Chief, Royalty Valuation & Standards Division, United States Department of the Interior, Minerals Management Service, to Daniel Mills, Landman, Texaco U.S.A. (Doc. Supp. at 93.)

The federal statute, like the state statute, has language describing the NPSSL system in terms of profits derived "from the lease". Thus, the federal government's interpretation of the NPSSL as lease-specific, provides support for reading Alaska's NPSSL system in the same manner.

The three-fold purpose of AS 38.05.180 has been discussed in Kelly v. Zamarelio, 486 P.2d 906 (Alaska 1971), and includes an intent "to insure that leases on valuable oil and gas producing state lands will be made available to the public on a fair and equitable basis, that the state will be adequately compensated for its natural resources, and that the state's resources are developed in an orderly fashion".

Id. at 912. The purposes of the NPBL system specifically include avoiding premature lease abandonment, allowing less well financed operators to compete, and enabling payments to correspond with benefits. University of California, Walter J. Mead, Professor of Economics, "Comments From an Economic Perspective on House Bill No. 854 in the Legislature in the State of Alaska, Tenth Legislature -- Second Session", May 15, 1978. (Doc. Supp. at 415-416.)

11 AAC 83.219, as interpreted by DNR, furthers none of these aims and specifically detracts from some. For example, the fact that some of Marathon's expenses would be lost runs counter to the general purpose of fair and equitable availability of leases. Also, although the statute intends to insure adequate compensation of the state, DNR's interpretation would give the state, in this instance, more compensation than it would have had if Marathon had not transferred its interest. Thus, the regulation is not reasonably necessary to further the statute's purpose.

The correct interpretation of 11 AAC 83.219(b)(7) is that it pertains only to partial assignments of leasehold interests and would not apply to the complete assignment contemplated by BP and Marathon. This interpretation is consistent with the statute and furthers the statutory purposes by preventing double deductions of development costs.

Specifically, it prevents a development cost that is included in the assignor's development account from also being included in the assignee's development account. This interpretation gives effect to the regulation's requirement that "the lessee transferring the production interest must credit his development account for a like amount". 11 AAC 83.219(b)(7). This sentence would have no meaning under DNR's interpretation that the regulation applies to total assignments, as the assignor would have no development account to credit.

The effect of applying this regulation to a partial assignment is that there is no net change in the total amount of development costs that will be used to calculate net profits from the lease. It merely results in a reallocation of the total development costs.

The state alternatively argues that BP and Marathon are effectuating a partial assignment, because Marathon plans to retain an overriding royalty interest. The court finds that the agreement assigns all of Marathon's interests as lessee to BP, particularly given the fact that the regulation defines a lessee as someone who holds a "working interest" which, by definition, differs from a "royalty interest". See 11 AAC 83.295(27) and 11 AAC 83.295(30). Consequently, because this is a total assignment and the regulation, properly interpreted, applies to partial assignments, DNR's decision must be REVERSED.

DATED at Anchorage, Alaska this 25 day of July,

1991.

Dana Fabe
DANA FABE
SUPERIOR COURT JUDGE

I certify that on 7/25/91,
a copy of the above was mailed to each
of the following at their address of
record:

Mason / Maasera / Johnson
J. Jensen
Secretary / Deputy Clerk



Alaska State Legislature

Official Business

SENATE RESOURCES COMMITTEE

State Capitol
Juneau AK 99801

FAX MEMO

TO: ~~Mr. John Morgan/BP Exploration~~ (564-5514)
~~Commissioner John Shively, DNR~~ (269-8918)
~~Attorney General Bruce Botelho~~ (465-2075)

5900

FROM: Annette Kreitzer, Aide to
Senate Resources Committee 

DATE: April 1, 1996

RE: Requests for information from March 29 Resources meeting

Attached is the list of requests for information from the March 29 meeting of the Senate Resources Committee. Please provide the information to me as soon as possible. Information regarded by the state as confidential should be gathered to be disseminated during a confidential session of the committee. Please advise me, though, when the information is ready for the committee, so that the chairman can schedule a confidential session.

Thank you for your assistance.



Alaska State Legislature

Senate Resources Committee
Information Requests from Committee Members
re: SB 318: Northstar Lease Agreement
March 29, 1996 Hearing

State Capitol
Juneau AK 99801

Official Business

FIRST REQUEST:

- Halford: How much did BP pay Amerada Hess for the leases? (Available to Legislature under confidentiality measure).

SECOND REQUEST:

In response to question from Senator Pearce, Senator Leman requested BP provide details on what BP agreed to in BP's successful January bid on leases in Venezuela that are similar or the same as net profit share leases.

THIRD REQUEST:

Halford:

Want an analysis from Law re: conclusion as to whether development fund carries forward.

- ✓ Want list of other bidders on these parcels/leases in the sale (where BP acquired Amerada Hess leases).

If there is a lawsuit that stops development because of a change in the bid variable, what happens to the economic benefits (in the BP agreement)?

Want economic module to be run on 135 million barrels and on double that.

- ✓ Want to know what the projected severance tax rates will be.

FOURTH REQUEST:

- ✓ Pearce: Federal definition of net profit share. (Patrick Coughlin verbalized at 3/30/96 hearing, but this was not passed out to members for context of where the definition appears. Mr. Coughlin needs to provide the definition and its context to the committee.)

FIFTH REQUEST:

Leman: Wants list of how many and locations of employees from BP, CIRI, VECO and Arctic Slope and their subsidiaries. (after testimony from these companies regarding local hire)

SIXTH REQUEST:

- ✓ Leman: Wants BP to provide the committee comparable numbers for BP's decisions to proceed with other North Slope developments. Estimated per barrel development costs which BP management considered before committing to develop: 1) Kuparuk, 2) shallow oil deposits at Milne Point (Schrader Bluff), 3) Niakuk, 4) Pt. McIntyre and any other North Slope fields BP has developed.



BP EXPLORATION

Alaska Exploration & Developments

BP Exploration (Alaska) Inc.
700 East Benson Boulevard
P.O. Box 196612
Anchorage, Alaska 99519-6612
(907) 561-5111

April 2, 1996

Hon. Loren Leman
Chairman, Senate Resources Committee
Alaska State Legislature
State Capitol
Juneau, AK 99801

Dear Senator Leman:

Per the request by Annette Kreitzer of your staff on April 1, I have enclosed responses to your six requests regarding SB 318 on the Northstar Lease Agreement. If you require additional information, please do not hesitate to call me (907-564-4892) or Daryl Kleppin (907-564-5418) on my staff.

Very truly yours,

A handwritten signature in black ink, appearing to read "E. M. Luttrell", written over a horizontal line.

E. M. Luttrell
Vice President
BP Exploration, Alaska Inc.

BP Exploration, Alaska (Inc.)
Response to Requests by Senate Resources Committee
SB 318 - Northstar Lease Agreement

- 1.) How much did BP pay Amerada Hess for the leases?

The terms of the purchase agreement between Amerada Hess and BP for the Northstar leases are confidential. BP did not secure permission from Amerada to release that information under confidentiality agreements to specific staff within the Department of Natural Resources. We have requested permission from Amerada to provide that information to the Alaska Legislature under a similar confidentiality agreement.

- 2.) Please provide details on what BP agreed to in BP's successful bid on leases in Venezuela that are similar or the same as net profit share leases.

Both Alaska and Venezuela derive their oil income from a combination of taxes and royalties. In addition, Venezuelan law allows the State Oil Company (PDVSA) to participate in the new E&P ventures up to 35% by paying full proportionate costs including any historical costs which are inflated at the prime interest rate. Reporting in the recent press assumes that PDVSA will do so.

Assuming that PDVSA takes its 35% share, the total government take in Venezuela (taxes, royalty, PDVSA) equals about 92% of profits. A comparable value for Northstar in Alaska is about 62% (State royalty, severance, and income tax; Federal royalty and income tax).

Venezuela can take a higher proportion of the benefits since the costs of developing, operating and transportation are substantially lower. In Venezuela, BP's cost per barrel (F&D, lifting, transportation) is about \$2.00 per barrel. Comparable costs in Alaska are about \$7.00 per barrel. In Venezuela, BP looks to make a profit of about \$1.20 per barrel from a capital investment (F&D) of about \$1.00 per barrel (a 1.2 ratio). In Alaska, we look to make about \$3.25 per barrel on a capital investment of about \$3.50 per barrel (a .94 ratio).

Economically (and from a view of simple capital efficiency), both of these ventures look attractive to BP, although BP's profit per barrel in Alaska is higher than in Venezuela. We also expect a much greater reserve potential in Venezuela (up to possibly 1 billion barrels).

- 3.) a) Please provide analysis from Law re: conclusion as to whether development fund carries forward.

To be provided by Alaska Department of Law

- b) Please provide a list of other bidders on these parcels/leases in the sale (where BP acquired Amerada leases).

See attachment #1.

c) If there is a law suit that stops development because of a change in the bid variable, what happens to the economic benefits (in the BP agreement)?

To be provided by DNR staff.

d) Please provide economic model runs on 135 million barrels and on double that.

The DNR will provide for an upside development case with reserves of 160 million barrels.

e) What is the projected severance tax rates?

The ELF at field startup (1999) is .7 and goes to .03 in 2005 and zero there after. Therefore, the severance rate varies from 8.7% in 1999 to zero in 2006.

4.) Please provide Federal definition of net profit share.

DNR and Department of Law to provide.

5.) Please provide list of how many and location of employees from BP, CIRI, Veco, and Arctic Slope and their subsidiaries.

At year end 1995, BP employed 1,077 in Alaska of which 917 or 85.1% were Alaska residents. BPX would encourage it's Northstar Alliance contractors to provide similar data to the committee.

6.) Please provide to the committee a comparable number for BP's decisions to proceed with other North Slope developments. Estimate per barrel development costs which BP management considered before committing to develop: 1) Kuparuk; 2) shallow oil deposits at Milne Point (Schrader Bluff); 3) Niakuk; 4) Pt. McIntyre and other North fields BP has developed.

Field	Sanction Year	Development Cost (\$/bbl)	ANS WC (\$/bbl) (MOD)	ANS WC (1996\$) (real)
Kuparuk	1982	6.65	30	40
Endicott	1985	5.40	25	33
PBU: GHX-2	1992	4.45	18	19
Pt McIntyre	1992	2.30	18	19
Niakuk	1993	2.50	16	17
Not sanctioned				
MPU-Schrader Bluff	1996-97??	1.80	17	17
Northstar	1996-97??	2.90	17	17

Attachment #1

Sale 30 (12/79) Northstar Bidding

The following table outlines the sale 30 results (NPSL) showing the successful bidder and parties that bid unsuccessfully.

ADL 312798		
Bid Group/Co.	Co. Interest	NPS Bid
Amerada Hess	100%	93.20000%
Texas Eastern	50%	80.58789%
Texaco	50%	
Amoco	100%	71.12509%
Texas Gulf	10%	61.87000%
Conoco	48%	
Placid	22%	
Cities Service	20%	
Murphy	10%	40.79133%
Shell	90%	
Phillips	50%	34.48464%
Chevron	50%	

ADL 312808		
Bid Group/Co.	Co. Interest	NPS Bid
Texas Eastern	100%	85.25978%
Texas Gulf	6%	38.12530%
Gulf Oil	25%	
Conoco	25%	
Placid	16%	
Rowan	3%	
Cities Service	25%	
Unocal	100%	25.50000%
Phillips	50%	10.14550%
Chevron	50%	
Atlantic Richfield	40%	2.11111%
Murphy	10%	
Shell	50%	

ADL 312799		
Bid Group/Co.	Co. Interest	NPS Bid
Amerada Hess	100%	91.20000%
Amoco	100%	82.59999%
Texas Eastern	50%	80.56789%
Texaco	50%	
Rowan	2%	71.62539%
Conoco	20%	
Texas Gulf	5%	
Getty	0.2	
Placid	13%	
Gulf	20%	
Cities Service	20%	
Murphy	10%	56.77133%
Shell	90%	
Phillips	33%	43.26273%
Mobil	33%	
Chevron	34%	
Unocal	100%	32.00000%

ADL 312809		
Bid Group/Co.	Co. Interest	NPS Bid
Texas Eastern	100%	35.25978%
Amoco	100%	71.25009%
Marathon	50%	53.83000%
Amerada	50%	
Gulf	25%	46.37549%
Placid	16%	
Getty	25%	
Texas Gulf	6%	
Rowan	3%	
Cities Service	25%	
Unocal	100%	38.00000%
Mobil	34%	34.23333%
Phillips	33%	
Chevron	33%	
Atlantic Richfield	45%	31.89117%
Shell	55%	

State of Alaska
Department of Natural Resources
Division of Oil and Gas
3601 C Street, Suite 1380, Anchorage, Alaska 99503

Fax Confirmation Phone (907)465-2400 Fax (907)465-3886

FACSIMILE TRANSMITTAL

DATE & TIME: April 3, 1996 2:35 PM

PLEASE DELIVER TO: Annette Kreitzer
Alaska Senate Resources Committee

FAX NUMBER: 465-3810

NUMBER OF PAGES (including cover): 9

FROM: Ken Boyd

COMMENTS:

Attached is Kevin Banks' analysis of 1) the effect of a delay on the Northstar development and 2) an increase in the reserve estimates. Please call if you have any questions.

Attachment

MEMORANDUM
DEPARTMENT OF NATURAL RESOURCES

State of Alaska
DIVISION OF OIL AND GAS

TO: Ken Boyd
Director

DATE: April 3, 1996

FILE NO:

THRU:

TELEPHONE: 269-8799

FROM: Kevin Banks *KB*
Petroleum Economist

SUBJECT: Northstar Unit - Senate
Resource Committee
Requests

In response to Senator Halford's request about the effect on the economic benefits if a lawsuit delays development of the Northstar Unit, I analyzed the effect on economic benefits caused by a delay for any reason. In short, any delay increases the economic benefits to the state while decreasing the economic benefits to BPXA. The attached graph and table illustrate this point.

The graph shows that, as full production start-up is delayed beyond 1999, the net profit share falls and the supplemental royalty rises. The net profit share declines because the development account accrues interest at the prime rate. The supplemental royalty increases as the start-up date is delayed because of the effect of inflation, i.e., the supplemental royalty is triggered by a price that rises at just one-half the rate of inflation.

The first table shows in greater detail the effects of delaying full production start-up until 2002. This table is similar to one that was supplied in the DNR Northstar Briefing Paper, but includes a column to show the revenues from the supplemental royalty if the project is delayed.

I also considered Senator Halford's request to run the model at double BPXA's "most likely" reserve estimate of 130 million barrels. Following the hearing, I spoke to Senator Halford and he said I should be "realistic." Based on conversations with BPXA and DNR's resource evaluation staff, I do not believe that recovery of double the 130 million barrel estimate is realistic. Instead, I have run the model based on an assumption of 180 million barrels, which is the highest number put forward by either BPXA or DNR staff.

The four tables labeled "Reserves of 180+ Million Barrels" and "Reserves of 105+ Million Barrels" illustrate what happens to revenues if the reserves are much higher (though not doubled as Senator Halford suggested) and much lower than BPXA's "most likely" case. In the first two tables, I assume that reserves are 180 million barrels. This reserve estimate represents a 70 percent recovery rate—an unusually high number.¹ I also assumed that this recovery estimate is

¹Doubling the reserves as requested by Senator Halford would require a 100 percent recovery of BPXA's most likely original-oil-in-place estimate. The initial recovery rate for the Prudhoe Bay field was estimated at 40 percent. After substantial investment, the current recovery estimate has changed to 55 percent. A 70 percent recovery might be possible but only after extraordinary expense. Furthermore, the field would have to produce for many years before attaining this level.

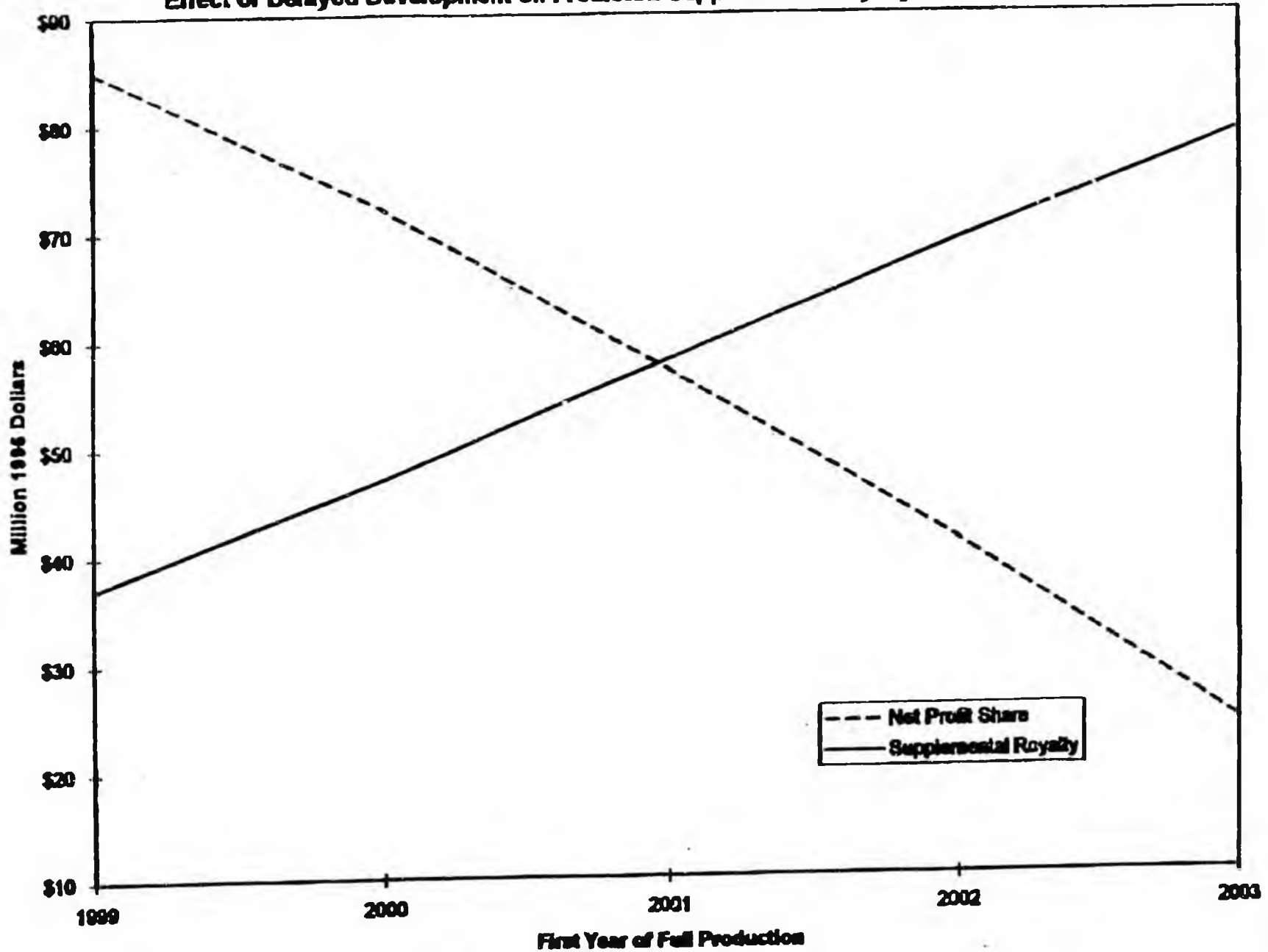
achieved by adding capital expenditures of only \$28 million to the most likely case for more drilling. BPXA's "upside" case envisions an additional \$91 million in capital expenditures to achieve reserves estimated at 160 million barrels. Other assumptions are held constant.

The second two tables show the downside, i.e., if reserves are only 105 million. In this case, I assume that the capital expenditures estimated for the most likely case are spent and the field never attains the most likely case production rates. Other assumptions are held constant.

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Northstar Proposal

Effect of Delayed Development on Predicted Supplemental Royalty and Net Profit Share



(This chart is based on BPXA's most likely estimate of reserves, capital and operating costs, and DOR's Fall '95 Base Price Forecast.)

Northstar Economic Evaluation



Estimated Total Revenues

Effect of Delay

Supplemental
Royalty and
1999 Development

Net Profit Share
and
1999 Development

Supplemental
Royalty and
2002 Development

Net Profit Share
and
2002 Development

(Real 1998 Dollars)

State Revenues

State Royalty	258	258	257	257
State Supplemental Royalty		0		0
MPSL	0		0	
State Share of Federal Royalty	16	16	16	16
Severance Tax	58	58	56	59
Spill & Conserv. Tax	3	3	3	3
Ad Valorem Tax	42	42	46	46
Income Tax	24	22	22	23
Total	485	481	469	444

Federal Revenues

Royalty (Net of State Share)	44	44	44	44
Income Tax	215	198	205	213
Total	259	243	249	258

BPXA Cash Flow

After Tax Funds Flow	349	318	331	348
Real Rate of Return	20.0%	19.9%	19.2%	20.4%

Totals may not add due to rounding.

(This table is based on BPXA's most likely estimate of reserves, original and operating costs, and DGR's Full 700 Base Price Payment.)

4/20/00, 1:01 PM

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Northstar Economic Evaluation

Estimated Total Revenues

At Reserves of
 180+ Million Barrels.*

With Supplemental
 Royalty

With Net Profit Share

(Real 1996 Dollars**)

State Revenues

State Royalty	363	363
State Supplemental Royalty	██████████	0
NP&L	0	██████████
State Share of Federal Royalty	23	23
Severance Tax	89	91
Spill & Conserv. Tax	4	4
Ad Valorem Tax	52	52
Income Tax	37	26
Total	639	934

Federal Revenues

Royalty (Net of State Share)	63	63
Income Tax	341	237
Total	404	300

BPXA Cash Flow

After Tax Funds Flow	581	389
Real Rate of Return	23.9%	21.7%

*2001 assumes 180 MMBO total reserves; additional 8 production wells; a two year increase in field life, and an additional \$20 million in capital costs over BPXA's most likely case.

**Totals may not add due to rounding.

Northstar Economic Evaluation

Estimated Total Revenues

At Reserves of 180+ Million Barrels.*	With Supplemental Royalty	With Net Profit Share
(Discounted Net Present Value**)		
State Revenues		
State Royalty	223	223
State Supplemental Royalty	[REDACTED]	0
NPSL	0	[REDACTED]
State Share of Federal Royalty	-14	14
Severance Tax	61	63
Spill & Conserv. Tax	2	3
Ad Valorem Tax	32	32
Income Tax	21	16
Total	389	524
Federal Revenues		
Royalty (Net of State Share)	39	39
Income Tax	195	149
Total	234	188
BPXA Cash Flow		
After Tax Funds Flow	281	194
Real Rate of Return	23.9%	21.7%

*DNR assumes 185 MMBO total reserves, additional \$ production wells, a two year increase in field life, and an additional \$26 million in capital costs over BPXA's most likely case.

**Assuming 10 percent nominal discount rate. Totals may not add due to rounding.

04-03-1998 15:08 907 465 3886 DNR OFFICE OF THE COMMISSIONER P.61

Northstar Economic Evaluation



Estimated Total Revenues

At Reserves of 105 Million Dollars* With Supplemental Royalty With Net Profit Share

(Real 1996 Dollars**)

State Revenues

State Royalty	206	206
State Supplemental Royalty	0	0
NPSL	0	0
State Share of Federal Royalty	13	13
Severance Tax	30	30
Spill & Conserv. Tax	2	2
Ad Valorem Tax	42	42
Income Tax	17	18
Total	340	312

Federal Revenues

Royalty (Net of State Share)	36	36
Income Tax	153	163
Total	189	199

BPXA Cash Flow

After Tax Funds Flow	234	256
Real Rate of Return	14.5%	15.1%

*DNR assumes 105 MMBO total reserves, the minimum production indicated by BPXA in its "Proposal for Modified Lease Terms"

**Assuming 3.2 percent inflation rate from DOR Fall 1996 Base Price Forecast. Totals may not add due to rounding.

Northstar Economic Evaluation



Estimated Total Revenues

At Reserves of 105 Million Dollars*

With Supplemental
Royalty

With Net Profit
Share

(Discounted Net Present Value**)

State Revenues

State Royalty	-136	136
State Supplemental Royalty	[REDACTED]	0
NPSL	0	[REDACTED]
State Share of Federal Royalty	-9	-9
Severance Tax	23	23
Spill & Conserv. Tax	1	1
Ad Valorem Tax	27	27
Income Tax	10	11
Total	-223	-207

Federal Revenues

Royalty (Net of State Share)	24	24
Income Tax	92	98
Total	116	121

BPXA Cash Flow

After Tax Funds Flow	92	102
Real Rate of Return	14.5%	15.1%

*DNR assumes 105 NBEDO total reserves, the minimum production indicated by BPXA in its "Proposal for Modified Lease Terms"

**Assuming 10 percent discount rate. Totals may not add due to rounding.

(This table is based on BPXA's most likely estimate of reserves, capital and operating costs, and DNR's Full Well Share Price Payment.)

04-03-1988 15:11 907 465 3886 DNR OFFICE OF THE COMMISSIONER

Postnet Fax Note Date 4/25/96

To: <i>Caroline Weitzler</i>	From: <i>Patricia J. K...</i>
Co Dept: <i>Greater Leasing</i>	Co: <i>INTL</i>
Phone #: <i>405-2095</i>	Phone #: <i>209-5900</i>
Fax #: <i>465-3810</i>	Fax #:

Net Profit Share Lease Ownership

01-Apr-96

LEASE NUMBER	NAME	WORKING INTEREST %
ADL 312798	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 312799	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 312808	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 312809	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 312827	BP EXPLORATION (ALASKA) INC	50
	AMEXADA HESS CORPORATION	50
	Total for Segment	1
ADL 312828	DOYON LIMITED	0.8
	NANA REGIONAL CORPORATION	1.5
	COOK INLET REGION INC	2.5
	BP EXPLORATION (ALASKA) INC	95.5
	Total for Segment	1
ADL 312834	ARCO ALASKA, INC	33.33333
	UNION OIL COMPANY OF CALIFORNIA	33.33333
	EXXON CORPORATION	33.33334
	Total for Segment	1
ADL 312866	EXXON CORPORATION	100
	Total for Segment	1
ADL 343108	EXXON CORPORATION	50
	BP EXPLORATION (ALASKA) INC	50
	Total for Segment	1
ADL 343110	PHILLIPS PETROLEUM COMPANY	50
	MOBIL OIL CORPORATION	50
	Total for Segment	1

LEASE NUMBER	NAME	WORKING INTEREST %
ADL 343111	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 343112	CHEVRON U.S.A. INC	33.33
	BP EXPLORATION (ALASKA) INC	66.67
	Total for Segment	1
	CHEVRON U.S.A. INC	100
	Total for Segment	A
	CHEVRON U.S.A. INC	33.33
	BP EXPLORATION (ALASKA) INC	66.67
	Total for Segment	B
ADL 355001	BP EXPLORATION (ALASKA) INC	100
	Total for Segment	1
ADL 355016	OXY USA INC	8.81
	BP EXPLORATION (ALASKA) INC	26.81
	BP EXPLORATION AND OIL COMPANY	64.38
	Total for Segment	1
	AMERADA HESS CORPORATION	50
	MIDGARD ENERGY COMPANY	50
	Total for Segment	A
ADL 355017	OXY USA INC	8.81
	BP EXPLORATION (ALASKA) INC	26.81
	BP EXPLORATION AND OIL COMPANY	64.38
	Total for Segment	1
ADL 355018	OXY USA INC	8.81
	BP EXPLORATION (ALASKA) INC	26.81
	BP EXPLORATION AND OIL COMPANY	64.38
	Total for Segment	1
ADL 355021	OXY USA INC	8.81
	BP EXPLORATION (ALASKA) INC	26.81
	BP EXPLORATION AND OIL COMPANY	64.38
	Total for Segment	1
	MIDGARD ENERGY COMPANY	50
	AMERADA HESS CORPORATION	50
	Total for Segment	A
ADL 355023	ARCO ALASKA, INC	100

LEASE NUMBER	NAME		WORKING INTEREST %
		Total for Segment	100
ADL 355024	ARCO ALASKA, INC		100
		Total for Segment	100
ADL 355029	EXXON CORPORATION		20
	ARCO ALASKA, INC		80
		Total for Segment	100
	AMERADA HESS CORPORATION		50
	EXXON CORPORATION		50
		Total for Segment	100
ADL 355030	ARCO ALASKA, INC		100
		Total for Segment	100
ADL 355031	ARCO ALASKA, INC		100
		Total for Segment	100
	HUNT PETROLEUM CORPORATION		18.80672
	ROSEWOOD RESOURCES INC		18.90756
	PLACID OIL COMPANY		64.28572
		Total for Segment	100
ADL 355032	ARCO ALASKA, INC		100
		Total for Segment	100
ADL 355034	ARCO ALASKA, INC		100
		Total for Segment	100
	HUNT PETROLEUM CORPORATION		18.80672
	ROSEWOOD RESOURCES INC		18.90756
	PLACID OIL COMPANY		64.28572
		Total for Segment	100
ADL 355035	ARCO ALASKA, INC		100
		Total for Segment	100
	ARCO ALASKA, INC		50
	TEXACO EXPLORATION & PRODUCTION		50
		Total for Segment	100
ADL 355036	UNION TEXAS PETROLEUM CORPORATION		12.5
	ARCO ALASKA, INC		87.5
		Total for Segment	100
	HUNT PETROLEUM CORPORATION		4.20168

LEASE NUMBER	NAME		WORKING INTEREST %
	ROSEWOOD RESOURCES INC		4.72880
	UNION TEXAS PETROLEUM CORPORATION		12.5
	PLACID OIL COMPANY		28.57143
	AMERADA HESS CORPORATION		50
	Total for Segment	A	100
ADL 255037			
	UNION TEXAS PETROLEUM CORPORATION		6.25
	ARCO ALASKA, INC		93.75
	Total for Segment	1	100
	HUNT PETROLEUM CORPORATION		2.10084
	ROSEWOOD RESOURCES INC		2.363445
	UNION TEXAS PETROLEUM CORPORATION		6.25
	PLACID OIL COMPANY		14.285715
	AMERADA HESS CORPORATION		25
	MIDGARD ENERGY COMPANY		25
	TEXACO INC		25
	Total for Segment	A	100
ADL 355038			
	UNION TEXAS PETROLEUM CORPORATION		6.25
	ARCO ALASKA, INC		93.75
	Total for Segment	1	100
	HUNT PETROLEUM CORPORATION		2.10084
	ROSEWOOD RESOURCES INC		2.363445
	UNION TEXAS PETROLEUM CORPORATION		6.25
	PLACID OIL COMPANY		14.285715
	MIDGARD ENERGY COMPANY		25
	TEXACO INC		25
	AMERADA HESS CORPORATION		25
	Total for Segment	A	100
ADL 355039			
	UNION TEXAS PETROLEUM CORPORATION		6.25
	ARCO ALASKA, INC		93.75
	Total for Segment	1	100
	HUNT PETROLEUM CORPORATION		2.10084
	ROSEWOOD RESOURCES INC		2.363445
	UNION TEXAS PETROLEUM CORPORATION		6.25
	PLACID OIL COMPANY		14.285715
	MIDGARD ENERGY COMPANY		25
	AMERADA HESS CORPORATION		25
	TEXACO INC		25
	Total for Segment	A	100
ADL 355040			
	ARCO ALASKA, INC		100
	Total for Segment	1	100
	TEXACO EXPLORATION & PRODUCTION		20
	ARCO ALASKA, INC		80
	Total for Segment	A	100

LEASE NUMBER	NAME	WORKING INTEREST %
ADL 364470		
	AMERADA HESS CORPORATION	11.35
	UNION TEXAS PETROLEUM CORPORATION	22
	ANADARKO PETROLEUM COMPANY	22
	ARCO ALASKA, INC	44.85
	Total for Segment	100
ADL 364471		
	AMERADA HESS CORPORATION	11.35
	ANADARKO PETROLEUM COMPANY	22
	UNION TEXAS PETROLEUM CORPORATION	22
	ARCO ALASKA, INC	44.85
	Total for Segment	100
ADL 364472		
	UNION TEXAS PETROLEUM CORPORATION	22
	ANADARKO PETROLEUM COMPANY	22
	ARCO ALASKA, INC	56
	Total for Segment	100
	ANADARKO PETROLEUM COMPANY	6.16
	ARCO ALASKA, INC	21.84
	UNION TEXAS PETROLEUM CORPORATION	22
	AMERADA HESS CORPORATION	50
	Total for Segment	100
ADL 364473		
	ANADARKO PETROLEUM COMPANY	22
	UNION TEXAS PETROLEUM CORPORATION	22
	ARCO ALASKA, INC	56
	Total for Segment	100
	ANADARKO PETROLEUM COMPANY	6.16
	ARCO ALASKA, INC	21.84
	UNION TEXAS PETROLEUM CORPORATION	22
	AMERADA HESS CORPORATION	50
	Total for Segment	100
ADL 364474		
	UNION TEXAS PETROLEUM CORPORATION	28
	ARCO ALASKA, INC	74
	Total for Segment	100
	ARCO ALASKA, INC	24
	UNION TEXAS PETROLEUM CORPORATION	26
	AMERADA HESS CORPORATION	50
	Total for Segment	100
ADL 364475		
	UNION TEXAS PETROLEUM CORPORATION	28
	ARCO ALASKA, INC	74
	Total for Segment	100
	ARCO ALASKA, INC	24
	UNION TEXAS PETROLEUM CORPORATION	26

LEASE NUMBER	NAME		WORKING INTEREST %
	AMERADA HESS CORPORATION		50
	Total for Segment	A	100
AD ¹ 354476	UNION TEXAS PETROLEUM CORPORATION		28
	ARCO ALASKA, INC		74
	Total for Segment	1	100
	ARCO ALASKA, INC		24
	UNION TEXAS PETROLEUM CORPORATION		28
	AMERADA HESS CORPORATION		50
	Total for Segment	A	100
AD ^L 364477	UNION TEXAS PETROLEUM CORPORATION		16.989
	ARCO ALASKA, INC		83.001
	Total for Segment	1	100
	ARCO ALASKA, INC		16.331
	UNION TEXAS PETROLEUM CORPORATION		16.989
	AMERADA HESS CORPORATION		66.67
	Total for Segment	A	100
AD ^L 354478	UNION TEXAS PETROLEUM CORPORATION		32
	ARCO ALASKA, INC		68
	Total for Segment	1	100
	ARCO ALASKA, INC		18
	UNION TEXAS PETROLEUM CORPORATION		32
	AMERADA HESS CORPORATION		50
	Total for Segment	A	100

Net Profit Share Leases - Ownership Within Units

01-Apr-96

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
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DUCK ISLAND

ADL	312838	BP EXPLORATION (ALASKA) INC	95.5
		COOK INLET REGION INC	2.5
		DOYON LIMITED	0.5
		NANA REGIONAL CORPORATION	1.5
Total for Segment			100

ADL	312834	ARCO ALASKA, INC	33.3333
		EXXON CORPORATION	33.3333
		UNION OIL COMPANY OF CALIFORNIA	33.3333
Total for Segment			100

KUPARUK RIVER

ADL	318923	ARCO ALASKA, INC	100
Total for Segment			100

ADL	318924	ARCO ALASKA, INC	100
Total for Segment			100

ADL	318938	ARCO ALASKA, INC	100
Total for Segment			100

ADL	318932	ARCO ALASKA, INC	100
Total for Segment			100

KUUKPIK

ADL	318928	ARCO ALASKA, INC	80
		EXXON CORPORATION	20
Total for Segment			100

		AMBRADA HESS CORPORATION	50
		EXXON CORPORATION	50
Total for Segment			100

ADL	318931	ARCO ALASKA, INC	100
Total for Segment			100

		HUNT PETROLEUM CORPORATION	16.80673
		PLACID OIL COMPANY	64.28572
		ROSEWOOD RESOURCES INC	18.90756
Total for Segment			100

ADL	318934	ARCO ALASKA, INC	100
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Post-41 brand tax transmitted memo 7671 # of pages 6

Annelle Kuntiger
 Director Leases
 Dept 465-2095
 Fax 465-3810

Patrick Conaghan
 on DNR
 Phone 269-8000
 Fax

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
		Total for Segment	1 100
		HUNT PETROLEUM CORPORATION	16.80673
		FLACID OIL COMPANY	64.28373
		ROSEWOOD RESOURCES INC	18.90756
		Total for Segment	A 100
ADL	14833	ARCO ALASKA, INC	100
		Total for Segment	1 100
		ARCO ALASKA, INC	90
		TEXACO EXPLORATION & PRODUCTION	90
		Total for Segment	A 100
ADL	14836	ARCO ALASKA, INC	87.3
		UNION TEXAS PETROLEUM CORPORATION	12.5
		Total for Segment	1 100
		AMERADA HESS CORPORATION	90
		HUNT PETROLEUM CORPORATION	4.30168
		FLACID OIL COMPANY	28.37149
		ROSEWOOD RESOURCES INC	4.72680
		UNION TEXAS PETROLEUM CORPORATION	12.5
		Total for Segment	A 100
ADL	14837	ARCO ALASKA, INC	93.75
		UNION TEXAS PETROLEUM CORPORATION	6.25
		Total for Segment	1 100
		AMERADA HESS CORPORATION	25
		HUNT PETROLEUM CORPORATION	2.10084
		MIDGARD ENERGY COMPANY	25
		FLACID OIL COMPANY	14.283713
		ROSEWOOD RESOURCES INC	2.363448
		TEXACO INC	25
		UNION TEXAS PETROLEUM CORPORATION	6.25
		Total for Segment	A 100
ADL	14838	ARCO ALASKA, INC	93.75
		UNION TEXAS PETROLEUM CORPORATION	6.25
		Total for Segment	1 100
		AMERADA HESS CORPORATION	25
		HUNT PETROLEUM CORPORATION	2.10084
		MIDGARD ENERGY COMPANY	25
		FLACID OIL COMPANY	14.283713
		ROSEWOOD RESOURCES INC	2.363448
		TEXACO INC	25
		UNION TEXAS PETROLEUM CORPORATION	6.25
		Total for Segment	A 100
ADL	14839	ARCO ALASKA, INC	93.75
		UNION TEXAS PETROLEUM CORPORATION	6.25

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
		Total for Segment	1 100
		AMERADA HESS CORPORATION	25
		HUNT PETROLEUM CORPORATION	21.0084
		MEDGARD ENERGY COMPANY	25
		PLACID OIL COMPANY	14.28715
		ROSEWOOD RESOURCES INC	1.363448
		TEKACO INC	25
		UNION TEXAS PETROLEUM CORPORATION	6.25
		Total for Segment	A 100
ADL	36446	ARCO ALASKA, INC	100
		Total for Segment	1 100
		ARCO ALASKA, INC	80
		TEKACO EXPLORATION & PRODUCTION	20
		Total for Segment	A 100
ADL	36447	AMERADA HESS CORPORATION	11.33
		ANADARKO PETROLEUM COMPANY	22
		ARCO ALASKA, INC	44.65
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	1 100
ADL	36447	AMERADA HESS CORPORATION	11.33
		ANADARKO PETROLEUM COMPANY	22
		ARCO ALASKA, INC	44.65
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	1 100
ADL	36447	ANADARKO PETROLEUM COMPANY	22
		ARCO ALASKA, INC	56
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	1 100
		AMERADA HESS CORPORATION	30
		ANADARKO PETROLEUM COMPANY	6.16
		ARCO ALASKA, INC	21.84
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	A 100
ADL	36447	ANADARKO PETROLEUM COMPANY	22
		ARCO ALASKA, INC	56
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	1 100
		AMERADA HESS CORPORATION	30
		ANADARKO PETROLEUM COMPANY	6.16
		ARCO ALASKA, INC	21.84
		UNION TEXAS PETROLEUM CORPORATION	22
		Total for Segment	A 100
ADL	36447	ANADARKO PETROLEUM COMPANY	22
		ARCO ALASKA, INC	56
		UNION TEXAS PETROLEUM CORPORATION	22

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
		ARCO ALASKA, INC	74
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
		AMERADA HESS CORPORATION	30
		ARCO ALASKA, INC	24
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
ADL	34475	ARCO ALASKA, INC	74
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
		AMERADA HESS CORPORATION	30
		ARCO ALASKA, INC	24
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
ADL	34476	ARCO ALASKA, INC	74
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
		AMERADA HESS CORPORATION	30
		ARCO ALASKA, INC	24
		UNION TEXAS PETROLEUM CORPORATION	26
		Total for Segment	100
ADL	34477	ARCO ALASKA, INC	13.801
		UNION TEXAS PETROLEUM CORPORATION	16.999
		Total for Segment	100
		AMERADA HESS CORPORATION	66.67
		ARCO ALASKA, INC	16.331
		UNION TEXAS PETROLEUM CORPORATION	16.999
		Total for Segment	100
ADL	34478	ARCO ALASKA, INC	68
		UNION TEXAS PETROLEUM CORPORATION	32
		Total for Segment	100
		AMERADA HESS CORPORATION	30
		ARCO ALASKA, INC	18
		UNION TEXAS PETROLEUM CORPORATION	32
		Total for Segment	100
MILNE POINT			
ADL	34501	BP EXPLORATION (ALASKA) INC	26.81
		BP EXPLORATION AND OIL COMPANY	64.36
		OXY USA INC	8.81
		Total for Segment	100
		AMERADA HESS CORPORATION	50

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
		MEDGARD ENERGY COMPANY	30
		Total for Segment A	100
ADL	148017	BP EXPLORATION (ALASKA) INC	26.81
		BP EXPLORATION AND OIL COMPANY	64.38
		OXY USA INC	8.81
		Total for Segment 1	100
ADL	148018	BP EXPLORATION (ALASKA) INC	26.81
		BP EXPLORATION AND OIL COMPANY	64.38
		OXY USA INC	8.81
		Total for Segment 1	100
ADL	148021	BP EXPLORATION (ALASKA) INC	26.81
		BP EXPLORATION AND OIL COMPANY	64.38
		OXY USA INC	8.81
		Total for Segment 1	100
		AMERADA HESS CORPORATION	30
		MEDGARD ENERGY COMPANY	30
		Total for Segment A	100
NON-UNIT PRODUCTION			
ADL	312827	AMERADA HESS CORPORATION	30
		BP EXPLORATION (ALASKA) INC	30
		Total for Segment 1	100
NORTHSTAR			
ADL	312798	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
ADL	312799	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
ADL	312830	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
ADL	312840	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
ADL	312841	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
POINT THOMSON			
ADL	312844	MOCON CORPORATION	100
		Total for Segment 1	100

UNIT	LEASE NUMBER	NAME	WORKING INTEREST %
ADL	343109	BP EXPLORATION (ALASKA) INC ECONOM CORPORATION	50 50
		Total for Segment 1	100
ADL	343110	MOORE OIL CORPORATION PHILLIPS PETROLEUM COMPANY	50 50
		Total for Segment 1	100
ADL	343111	BP EXPLORATION (ALASKA) INC	100
		Total for Segment 1	100
ADL	343112	BP EXPLORATION (ALASKA) INC CHEVRON U.S.A. INC	66.67 33.33
		Total for Segment 1	100
		CHEVRON U.S.A. INC	100
		Total for Segment A	100
		BP EXPLORATION (ALASKA) INC CHEVRON U.S.A. INC	66.67 33.33
		Total for Segment B	100

CAMBRIDGE ENERGY RESEARCH ASSOCIATES

FAX MESSAGE

**TO : ALASKA STATE LEGISLATURE
ATTN: SEN. DRUE PEARCE
FAX : 0019074653872**

Cambridge Energy Research Associates

C E R A



LATIN AMERICA ENERGY



WORLD OIL

INSIDE

Benefits to the Economy

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CERA ALERT

FEBRUARY 1, 1996

VENEZUELA LEAPS FORWARD: THE SECOND COMING OF OIL?

January 22, 1996 marked the day that Venezuela re-opened the door to direct private investment in its oil and natural gas sectors.* Sixty of the seventy-five companies that pre-qualified for the bidding round participated in the process that ended last week. Winners were chosen twice a day for the ten blocks containing an estimated 7 billion barrels of oil. An issue for many of the private investors was the amount of the take—the government participation in royalties and taxes—but the issue was not enough to derail investor interest.

Assuming that the PDVSA affiliate takes the maximum 35 percent share of the joint venture, the final division of profits in the profit sharing agreements will be between 88 and 92 percent for the government/PDVSA, leaving only 8 to 12 percent for the private investor consortium (see Figure 1, Venezuela: Bidding Round Results). This high level of take guarantees the government will receive large oil revenues in addition to what it already receives from PDVSA (between \$5 and \$6 billion per year).

More importantly, the low percentage of profits for the private investors may be an indication of a change in the emphasis of investor strategy—from the overall return on investment to securing long-term crude supplies. One reason this change is occurring for the Venezuelan bidding round is the sheer size of their natural resource base and the expectations of large prospects. Higher risk areas in Latin America are unlikely to be able to adopt similarly difficult terms, as seen in the lack of bids for the higher risk Catatumbo and El Sombrero blocks.

Benefits to the Economy

The success of the bidding rounds will provide a much needed boost to Venezuela's economy over the long term through the expected capital investments by the private companies. More importantly, the high rate of government participation and cash bonuses pledged provides a tremendous boost to the country's confidence.

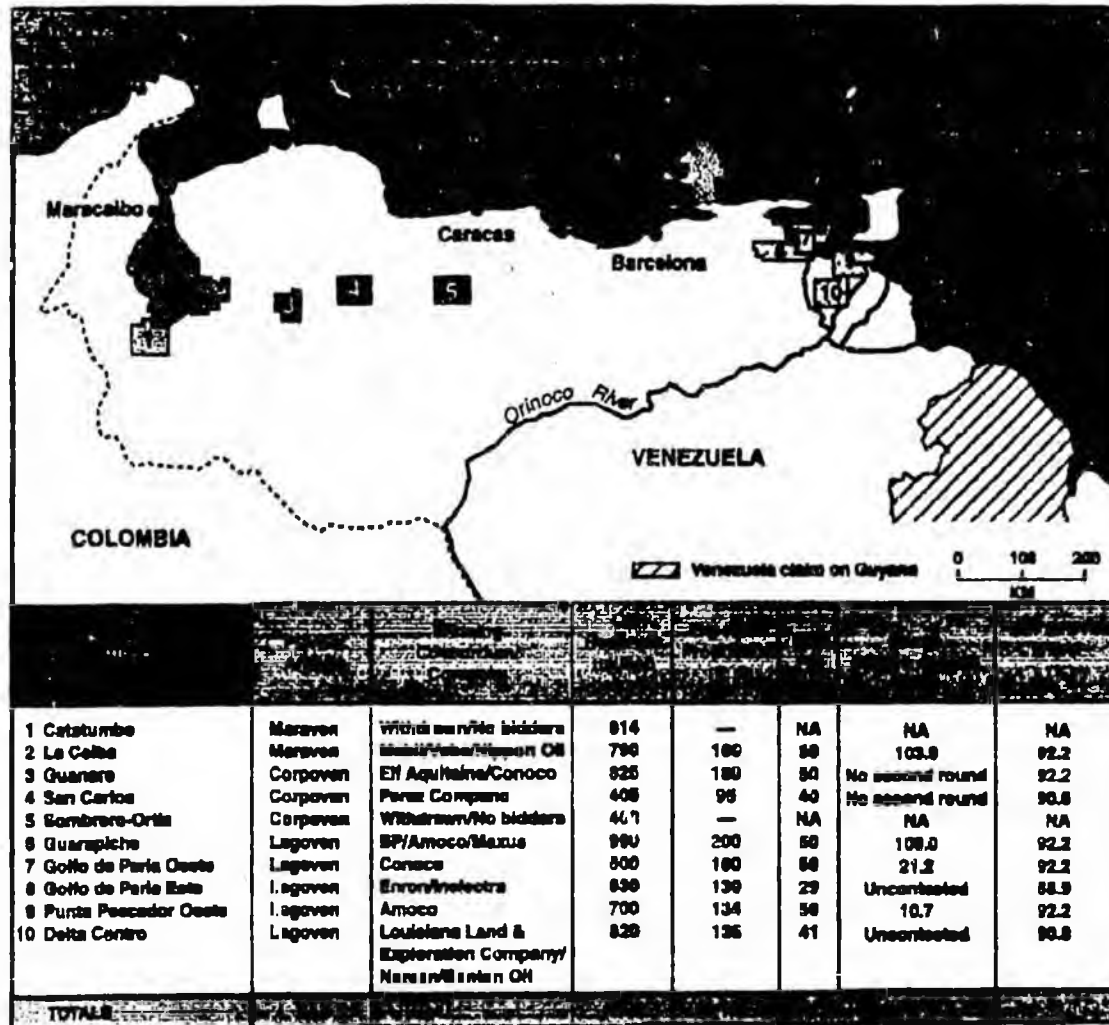
*See the upcoming CERA Private Report, *Venezuela Opens the Upstream: The Impact on Exports*, February 1996.

Cambridge Energy Research Associates

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The CERA Alert is part of CERA's Latin American Energy Retainer Advisory Service.
For more information, please contact Brian Ward at (617) 487-8446.

Figure 1
Venezuela: Bidding Round Results



Source: Cambridge Energy Research Associates, PDVSA

* C/L/M = Condensate/Light/Medium
** Includes royalty, income tax, and PEG.

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After enduring a multi-year recession, a rapidly devaluing currency, weak foreign investment, and a near-collapse of its banking industry, Venezuela needed some good news. And now it is in a position to lock up a long-term tax revenue stream if estimated production levels are realized.

In addition to the state, PDVSA is also reaping a very large benefit, for it now has secured the investment capital needed to expand liquid productive capacity over the next ten years. If the ambitious estimates are realized, these private companies will help increase capacity from today's level of

approximately 3.2 million barrels per day (mbd) to over 6.07 mbd by 2003. In terms of impact on the world oil market, PDVSA's export capacity would increase from nearly 2.0 mbd to over 4.7 mbd.

The Bottom Line

Surprisingly, five bids in the first round—which determined the state's share of profits—were for an additional royalty of 50 percent (allowable bids were between 0 and 50 percent). Four of the five bids resulted in a tie among the bidders, requiring that the cash bonus envelope be opened in order to break the tie. These bonuses ranged from \$10 million to \$109 million per block, or \$244.8 million in total. Eight of the 10 blocks were successfully auctioned off, with two blocks—Catatumbo and El Sombrero—being pulled from the process due to a lack of bidders. Importantly, the winning bids for five of the blocks included the maximum level of discretionary royalty to the government (50 percent).

Initial exploratory drilling could begin as soon as late 1996 if everything goes according to plan, but production is not expected for several more years. The government hopes this program will attract over \$500 million in investments over the first two years and reach an aggregate \$11 billion in new investments over the life of the 20-year program.

The Fiscal Terms: A Review

PDVSA's Role

If a block is found to be commercially viable, the developing consortium is required to enter into a joint venture profit-sharing agreement with a PDVSA subsidiary. The subsidiary has the right to take up to a 35 percent position in the joint venture—a value of which will be determined by taking a pro-rata percentage of the exploration costs. For example, if the exploration cost were \$1 billion and the subsidiary opted for a 35 percent share, then they would be required to pay the consortium \$350 million. However,

this amount is to be paid from the profits of the joint venture. In effect, the consortium will be lending the subsidiary the capital until a profit stream is realized but will be allowed to charge a market-based interest rate for the "loan." Once the consortium has been paid back, the joint venture will split the profits according to their respective share. If the block is not commercially viable, the consortium bears the entire financial risk.

The Government's Role

There are two components to the government's fiscal take in the profit sharing agreements—*income taxes and royalties*. The combined take for the government under the current structure is considered high in both absolute terms and also relative to other South American oil and gas investment opportunities.

- **Income taxes.** Income taxes are established by law, and changes would require Congressional approval. Currently, income taxes are set at 67.7 percent with a potential investment credit reduction of 2 percent.
- **Royalties.** The royalty component can be modified without a legislative change. In the case of the proposed profit sharing agreements, the royalty payment could be in two parts. The first part is established for the industry and is generally calculated at one sixth of the market value of the hydrocarbon produced. The government has the option to take all or part of the payment in kind.
- **The "PEG."** An additional royalty was invoked in the profit sharing agreements and was by design the determining factor in the winning bids. Called the Participacion del Estado en las Ganancias (PEG), it is an additional percentage of pre-tax profit offered by the private company or consortium during the bidding round. This percentage was bid up significantly in the most sought after fields, and determined which company was chosen. ■

Please mark your calendar for CERA's 15th Annual Executive Conference in Houston on February 13 and 14, 1998. For more information, call Brian Ward at (817) 441-2647.

CERA's new multiscenario study, *Latin America Energy: Scenarios to 2010*, will be available soon. For more information please contact Brian Ward at (817) 441-2647.

TONY KNOWLES, GOVERNOR

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

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February 22, 1996

The Honorable Drue Pearce
Capitol Building
Juneau, Alaska 99801-1182

Dear Senator Pearce,

Following our conversation yesterday, we have located a couple of articles reporting the Venezuela state petroleum company's (Pdvsa) recent signing of exploration and production profit sharing contracts. As noted in the January 15, 1996 Oil and Gas Journal article (page 24), this effort represented the first offering of exploration acreage in Venezuela since 1958, and encompasses a profit sharing plan designed to boost productive capacity by pursuing solo projects, joint ventures, and private oil company ventures in marginal field reactivation, exploration and production profit sharing deals, heavy oil projects and other ventures.

In the February 12, 1996 Oil and Gas Journal article (pages 31-34), details of the bidding are reported. Briefly, the contract/licenses garnered outlays of millions of dollars on each block, high profit sharing bonuses in the 40% to 50% range, high "tiebreaker" bonus bids in the millions of dollars, and provisions to purchase a working interest by paying a pro rata share of costs in the event of a commercial discovery.

Legal concerns apparently were raised by many oil companies regarding the structure of the tender offer and aspects of the proposed joint venture tax issues (OGJ, Feb. 12, 1996, pg. 34). Also, according to the January 29, 1996 Petroleum Intelligence Weekly (PIW), the major companies complained over the fiscal terms of the tender. Neither the tax issues nor the complaints over the fiscal terms appeared to dampen the impressive bidding.

I hope this information helps. Feel free to contact me if you have further questions.

Sincerely,


Kenneth A. Boyd
Director

Oil, gas potential seen on 10 Venezuelan blocks

Gregory D. Croft Karl W. Stauffer *Panera Petroleum Inc. San Leandro, Calif.*

Venezuela's congress approved on July 4, 1995, the offering of 10 exploration blocks after several months of discussions. This is the first new offering of exploration acreage in Venezuela since 1958 (OGJ, July 24, p. 21).

Terms for the offering include a sliding-scale royalty, various taxes, a fixed work commitment, and a government participation share. This last parameter is offered by the bidder, with the largest participation share being the winning bid.

The blocks are located in different parts of the country, but all 10 are located in basins that are prolific oil and gas producers. The following is a brief summary of the petroleum geology of each block.

Block 1, Catatumbo

Located on the southwestern shore of Lake Maracaibo, this area is essentially unexplored but lies between the major Lake Maracaibo oil production and the oil producing areas along both sides of the border with Colombia.

It is certain that almost all of the oil produced from the Venezuela-Colombia border area was sourced by the prolific Cretaceous La Luna formation in the Maracaibo basin and migrated to the southwest, in part through this block. A second, lesser source rock is the shale and coal of the Paleocene Orucue formation, but that unit tends to be gas prone.

Reservoirs in this block would mostly be Tertiary sandstones, especially those of the Mirador and Carbon-



era formations. Cretaceous carbonates with sand interbeds are also likely reservoir rocks. Possible traps include stratigraphic wedges as well as anticlines related to the thrust faults formed during the Miocene to recent uplift of the Merida Andes.

Block 2, La Celia

This block is east of the southern part of Lake Maracaibo and immediately south of prolific Motatan field, which produces from Eocene Misoa sandstones. Well productivities from the Eocene sandstones at Motatan are quite variable but can exceed 5,000 b/d.

Oil seeps along the

foothills of the Merida Andes just south of this block indicate that oil migrated through the block from north to south. The source of the oil is the La Luna formation.

The most likely reservoir rocks are the Misoa formation and other Tertiary sandstones, as well as fractured carbonates and sands of the Cretaceous Cogollo group. Traps are likely to be structures associated with the Andean uplift or with earlier, left lateral strike slip faulting.

Block 3, Guarema

The block is located in the northeastern part of the Barinas basin, which is the northern extension of Colombia's prolific Llanos basin. Sedi-

ments in this block reach thicknesses of about 15,000 ft. The source of the hydrocarbons on this block is again the La Luna equivalent, principally the Cretaceous Escudalosa formation.

The most likely reservoirs are sandstones of Tertiary age, particularly the Eocene Gobernador formation that produces in the older fields to the southwest. Other possible reservoirs are the sands and limestones of the Upper Cretaceous.

This relatively unexplored block (only one well has been drilled in the area) has the glamor of traps associated with large horizontal thrusts. In the foothills along this same mountain front are the

giant fields of the Furrial trend in eastern Venezuela and the Cusiana trend in the Llanos basin of Colombia.

Block 4, San Carlos

This block is located along the southern margin of the Merida Andes near the El Baul arch, which separates the Eastern Venezuela basin from the Barinas basin.

This is a relatively unexplored block that has interesting potential. Source rock is not considered a problem as the Escandalosa formation is either on the block or nearby.

Structurally this block is very complicated: it is at the intersection of two structural trends, has sedimentary section that wedges out against the El Baul arch, and has south verging thrust faults.

Likely reservoirs in this block are the sandstones of the Tertiary, particularly the Eocene, and possibly sandstones and carbonates of the Cretaceous. Likely traps are anticlines associated with thrust faults, possibly older Tertiary fault blocks, and updip pinchouts. Late structural movement associated with the Merida Andes may have destroyed earlier traps.

Block 5, El Sombrero

El Sombrero is located about 50 miles south of Caracas. The major natural gas accumulation at Yucal-Placer is located immediately east of and on trend with this block. To the southeast is the Las Mercedes area, which has produced about 200 million bbl of oil from sands that range in age from Miocene to Cretaceous.

Sediments in this block are up to 10,000 ft thick and hydrocarbons may be either oil or gas. The bounding thrust fault of the Coastal Range is close to the northern boundary of the block.

Possible traps in this block include anticlines and thrust structures related to the uplift of the Coastal Range and sand pinchouts to the south in younger units. The major source rocks here are probably the shales of the La

THE AUTHORS



Craft

Gregory D. Craft worked 11 years for Chevron Overseas Petroleum on 2D and 3D seismic interpretation projects in West Africa and Ecuador, and also in business planning. He left Chevron in 1994 to join Dr. Stauffer in founding Pantera Petroleum, a San Leandro, Calif., consulting firm specializing in Venezuela. He has an M.S. in geophysics from Stanford University.



Stauffer

Karl W. Stauffer's early employment was with Royal Dutch/Shell and later Chevron. He was loaned from Chevron to Petrolera de Venezuela from 1977 through 1979, during which time he prepared a series of studies including a regional evaluation of the petroleum potential of the Maracaibo basin. He left Chevron in 1984 to form Pantera Petroleum. He received a PhD in geology from Stanford University.

Luna equivalent formations, although some sourcing from Tertiary shales, especially of gas, may have occurred.

Block 6, Carapiche

This area is east of the city of Maturin along the famous Furrial trend, where many giant oil and gas fields have been discovered in the last 10 years. The recent discoveries have all been to the west of this block, but the geologic structure in the area trends east-west and continues through the block.

Source rock is not a concern in this area given the prolific nearby discoveries. The major source is again the La Luna equivalent, here called Querecual and San Antonio, although there is probably a secondary contribution from the Miocene Carapita formation.

Potential reservoirs include Miocene, Oligocene, and Cretaceous sandstones, as in the Furrial trend, as well as Plio-Pleistocene sands such as produce in Quiriquire and Pedernales fields. Traps are probably related to thrust-faulted structures, although there may be stratigraphic traps in

the younger Tertiary and flank traps against shale diapirs.

Reservoir quality and continuity are the principal risks associated with this block.

Blocks 7-9, Gulf of Paria

These blocks cover the southern part of the Gulf of Paria from the Venezuelan coast to the marine boundary with Trinidad. These are the only wholly offshore blocks. The blocks are located near the axis of the gravity low that marks the center of Tertiary sediment accumulation in the Eastern Venezuela basin.

Sediments here may be more than 30,000 ft thick. That there are hydrocarbons in the area is clear; Pedernales field is just onshore to the south, the Furrial trend is to the west, and the oil fields of southern Trinidad are on trend to the east.

Geological and structural trends do appear to continue all the way from the Furrial area into Trinidad, although facies changes of individual units also occur. Source rocks are largely the Querecual of Upper Cretaceous age, called the La Luna further west and

the Naparaima Hill in Trinidad.

The most likely reservoirs are Neogene sands and perhaps Paleogene and Cretaceous sands. Traps in these blocks may include thrust related structures as well as unconformities, stratigraphic traps, and traps against the flanks of shale diapirs.

Reservoir continuity may be a problem in these blocks.

Block 9, Punta Pescador

This block is located onshore and offshore the northernmost Amacuro delta. It is bounded to the north by the marine boundary with Trinidad and to the south shares in part a common border with Block 10.

Pedernales field to the west produces oil from stacked Pliocene and Miocene sandstone reservoirs on the flank of a shale diapir. The sedimentary section in this block is very thick, probably about 30,000 ft. The source rocks here are the Upper Cretaceous Querecual, called Naparaima Hill in Trinidad. Potential reservoirs include Neogene and perhaps Paleogene sands.

In addition to having deltaic-type structures that could serve as traps, this block may have structures related to earlier compression. Neogene submarine fan deposits could contain stratigraphic traps, and shale diapirism is also a likely trapping mechanism. A potential problem in this block is reservoir quality both due to the original facies and to compaction effects.

Block 10, Delta Centro

As its name suggests, this block is located in the middle of the Amacuro delta. In this block the sediment thickness is greater than in the productive Temblador-Tucupita trend to the southwest but less than in Block 9 to the north.

The source rock for the block would be the stratigraphic equivalent of the La Luna formation, either within the block or just beyond it. Possible reservoirs include

sandstones ranging in age from Pliocene to Cretaceous. Traps may include deltaic-type extensional structures, pre-deltaic compressional structures and stratigraphic wedges combined with faults.

This block has fewer data than any of the other blocks; no wells have been drilled within the block, and little seismic has been acquired. The unknown quality and continuity of sandstone reservoirs may be the greatest risk in this block.

A recent oil discovery at Las Piedras, just west of the block, flowed 2,700 b/d.

CONCLUSIONS

The blocks to be offered in Venezuela's upcoming exploration round include some very exciting exploration potential.

The blocks are located mostly in the deeper parts of Venezuela's two most important oil producing basins, and several of them are in structurally complex areas.

Many of the blocks are highly prospective for natural gas as well as oil, but operators will face a challenge marketing large quantities of gas in Venezuela's well-supplied gas market.

The offering also represents a watershed in Venezuelan politics in that foreign companies have not been able to obtain exploration acreage in Venezuela for many years.

NEVADA

Tide Petroleum of Nevada, Reno, staked the state's first wildcat to subthrust Palcozoics.

Permitted to 10,000 ft, it is the 2 Baseline Canyon Unit-Federal, in 21-1n-59c, Lincoln County. The spot is in Coal valley 25 miles south of Grant Canyon oil field.

N. DAKOTA

Armstrong Operating Inc., Dickinson, completed a Mississippian Lodgepole

discovery in Stark County.

The 29-1 Haller, in 29-139n-96w, 3 miles southwest of Dickinson, flowed 157 b/d of oil, 78 Mcfd of gas, and 35 b/d of water from 9,622-34 ft.

The discovery opens Ver-sippi field.

Baker Hughes Inc. reported 20 rotary rigs making hole in North Dakota in the week ended Sept. 1, compared with five in the same week in 1994.

OKLAHOMA

OXY USA Inc. staked an Ardmore basin wildcat in Johnston County.

The 1A Airport, in 21-4s-6e, 2 miles south of Tishomingo, is projected to 9,500 ft. The spot is 5 miles northeast of an abandoned one well oil field, PI reported.

PetroCorp Inc., Houston, is connecting two gas wells in the Misener Trend of Alfalfa County.

PetroCorp expects sales to start this month at 1.5 MMcfd of gas from the 19C-4 Janet. Sales started Aug. 25 from the 10C-1 Sherri, averaging 200 Mcfd.

TEXAS

South

Tesoro Petroleum Corp., San Antonio, might shoot a 3D seismic survey next year over a potentially significant discovery in Webb County.

The 1 Longoria, 40 miles east of Laredo on Tesoro's 2,200 acre South Guerra prospect, flowed 3.5 MMcfd of gas through a 3/4 in. choke with 4,090 psi wellhead pressure. The well encountered

80 ft of gross pay sand in the rested interval and three other pay sands untested behind pipe.

The discovery well is 4 miles southwest of and analogous to Guerra field, which has produced 125 bcf of gas.

Tests of the 1 Longoria continued to determine permeability and the need to fracture the pay sands. The company hopes to complete a directional delineation well by yearend to optimize contact with at least four identified prospective pay sands.

Mustang Oil & Gas Corp., a unit of Gulf Resources Corp., San Antonio, and Tesoro Petroleum Corp. opened new pays in Lopeno field in Zapata County.

The 1 Palmyra, enhanced by 3D seismic data, flowed as much as 10.7 MMcfd of gas on a 3/4 in. choke with 5,443 psig wellhead pressure from multiple zones in Eocene Upper Wilcox at about 11,000 ft. CAOF is 48,849 MMcfd.

The well cut 86 ft of gross pay sand in four producing intervals within the L-13, L-18, L-21, and L-22 sands.

Lopeno field, discovered in 1952, has produced about 120 bcf from L-5 through L-27 sands. Mustang used deviated drilling technology and multiple zone completion techniques that proved successful at Bob West gas field 6 miles southeast.

Gulf Coast

Nurvu Energy Co. completed a Brookeland field well that is the third well on its 58,000 acre joint venture with Texaco Exploration and Production Inc.

The 1H Springer, in Jasper

County, flowed 15.4 MMcfd of gas with 2,880 b/d of condensate through a 3/4 in. choke with 3,375 psi FTP.

The Cretaceous Austin chalk well produces through dual laterals a combined 9,082 ft long. True vertical depth is 11,830 ft.

Patterson Energy Inc., Snyder, Tex., has boosted its holdings in the Iola area of the Cretaceous Austin chalk trend in Grimes County to 3,700 acres.

The new holdings are near Patterson's Norwood and Davis wells, which were dual lateral completions.

UTAH

Amerac Energy Corp., Houston, formerly Wolverine Exploration Co., staked a wildcat in Summit County between Pineview and Bridger Lake fields.

Projected TD is 17,000 ft at the 1 Table Top Unit, in 16-1n-10e, 18 miles east of Pineview oil field.

Barrett Resources Corp., Denver, is preparing to complete its 3 Cave Gulch well that has established the deepest production in Cave Gulch Unit in the Wind River basin.

The well was hooked to sales in mid-August at 5 MMcfd of gas and 40 b/d of oil from perforations at 8,537-8,830 ft in a previously untested section of the Upper Cretaceous Lower Lance. TD is 9,050 ft.

Barrett plans to perforate additional zones in Lance.

The company recently staked the 10 Cave Gulch Unit, in 32-37n-86w, Natrona County, as a 9,200 ft Lance test in Waltman field.

API MONTHLY U.S. WELL COMPLETIONS*

	Oil wells	Footage	Gas wells	Footage	Dry holes	Footage	Total wells†	Footage
June 1995	529	2,917,495	771	5,088,457	381	2,254,434	1,681	10,258,386
May 1995	606	2,919,998	771	4,814,814	383	2,074,481	1,758	9,809,290
June 1994	518	2,813,313	747	4,590,358	517	2,064,888	1,802	10,368,784

*Total wells reported to API during June 1995 and stratigraphic and core tests. †Includes oil, gas, and dry holes plus service wells.

Pdvsa poised to sign first E&P profit sharing

Venezuela's state petroleum company Petroleos de Venezuela SA (Pdvsa) this month will sign its first exploration and production profit sharing contracts.

The effort represents Venezuela's most extensive offering of this type for private investment since nationalization 70 years ago. It also is the first offering of exploration acreage in Venezuela since 1958.

The program is expected to generate as much as \$12 billion in added investment in Venezuela's upstream sector the next 10-15 years.

Pdvsa goals

The E&P profit sharing program falls in line with Pdvsa's goal of boosting oil productive capacity to more than 5 million b/d by 2005 from the current level of slightly more than 3 million b/d, in expectation of growing world oil demand.

Pdvsa's 10 year business plan calls for total outlay of \$60 billion to hike productive capacity to 5.691 million b/d. That breaks out as \$33 billion for Pdvsa solo projects, another \$11 billion for joint ventures, and \$16 billion from private oil companies for marginal fields reactivation projects, E&P profit sharing deals, Orinoco heavy oil projects, and other oil and gas ventures.

Meantime, Pdvsa has earmarked about \$6 billion in capital spending this year, with most of the focus on E&P to underpin production and reserves growth.

The company also is moving to consolidate its growing global role as a refiner and marketer of heavy crudes and related products.

E&P program

The long awaited E&P profit sharing program is a departure from Venezuela's other recent efforts to attract private—especially foreign—investment to its upstream sector.

Pdvsa has signed some major "strategic alliance" agreements involving major oil companies for participation in heavy oil development/upgrading ventures (see table, OGJ, Aug. 14, 1995, p. 37).

In addition, Pdvsa is making progress in a 3 year old program targeting private investment to reactivate marginal oil fields in Venezuela (OGJ, June 12, 1995, p. 38).

Further, Pdvsa has all the elements in place except for a market for its liquefied natural gas export scheme, which includes offshore natural gas field development, in cooperation with foreign oil companies (OGJ, Sept. 4, 1995, Newsletter).

VENEZUELAN E&P PROFIT SHARING BIDDERS

Agip	Lazmo
Amoco	Maersk
Ampco	Marathon
Aradano	Marubeni
AARCO	Mazda
Asra Caspi	McQuarrie
Bentley Oil & Gas	Mitsui & Co.
BHP	Mitsui Oil
Box Energy	MOBIL
British Petroleum	Morgan Bros.
British Gas	Murphy Oil
Brown & Root	Nippon Oil
Canadian	Norbeco
Occidental	Norcan
Cia. Gen. de Combustibles	Norsk Hydro
Chevron	Numac
Clydesdale	OPIC
Coastal Corp	Oceana
Conoco	Petro
El Aguadone	Pennzoil
ENAP	Perez Companc
Enron	Petrobras
Enso	Petrolina
Enterprise plc	Petroplus
Esso	Pharmatrol
Fluor	Ranger
Gulf Canada	Repsol
Hess Oil	Royal Dutch
Husky	Shell
Hyundai	Seagull
Idemitsu	Stabil
Inepra	Talman
Japex	Tecpetrol
JNOC	Tekoku
Louisiana Land & Exploration	Texaco
	Total

The profit sharing scheme under Pdvsa's "apertura" (opening) oil program is the first time since nationalization in 1976 that private companies will be allowed to conduct E&P programs in Venezuela as equity owners.

The profit sharing deals call for exploration of 10 undeveloped blocks earmarked for joint ventures financed totally by private companies. Minimum investment is expected to be \$40-60 million/block.

The 10 blocks are spread over an area estimated at 4.5 million acres (see map, OGJ, Sept. 18, 1995, p. 85). Potential reserves are estimated at 7 billion bbl of high quality medium and light gravity crudes.

If commercial volumes of oil and/or gas are discovered, the private companies will form joint ventures with one of Pdvsa's subsidiaries, sharing the venture's profits and being reimbursed for exploration costs.

Companies, timetable

More than 200 companies have expressed an interest in the E&P profit sharing program, and about 70 have qualified to bid (see table).

Here is the schedule for opening sealed bids under the profit sharing program:

- Jan. 22, Catarumbu Block A, Zulia

and Merida states; La Ceiba Block B, Trujillo, Menda, and Zulia states.

- Jan. 23, Guanare Block C, Portuguesa state; San Carlos Block D, Cojedes and Portuguesa states.

- Jan. 24, El Sombrero Block E, Guarico state; Guarapiche Block F, Monagas and Sucre states.

- Jan. 25, West Gulf of Paria Block C and East Gulf of Paria Block H, both Sucre state.

- Jan. 26, Punta Pescador Block I and Delta Centro Block J, both Delta Amacuro state.

Pdvsa 1996 spending

Pdvsa's 1996 budget focuses heavily on its efforts to boost Venezuela's crude oil reserves to about 66 billion bbl, which it reckons would be an increase of about 1.6 billion bbl.

Oil & Gas Journal estimated Venezuela's proved crude reserves as of Jan. 1, 1996, at 64.5 billion bbl (OGJ, Dec. 25, 1995, p. 44).

Pdvsa said its 1996 E&P program includes more funds for exploratory drilling in new areas such as the South Andean flank and North and Central Monagas state.

Increased spending also will go for development and appraisal drilling, secondary recovery, and steam injection projects.

In addition, Pdvsa expects to increase Venezuela's gas reserves by about 585 million bbl of oil equivalent (BOE) to about 25 billion BOE.

Pdvsa reported production of Orimulsion, its boiler fuel that is an emulsion of extra heavy crude, water, and a surfactant, will total about 4.8 million metric tons in 1996, up 104,000 tons from 1995. It also reported production and marketing of coal from its Carbones del Guasare joint venture will be about flat in 1996 with 1995's level of 4.3 million tons.

Downstream plans

Pdvsa is pressing a program of upgrading and modernizing its refineries while eyeing possible further investments in refining abroad. All told, the goal is to add 600,000 b/d to worldwide refining capacity.

Plans call for increasing refining capacity in Venezuela by about 200,000 b/d by 2000 at a cost of about \$5.2 billion.

Current refining capacity in Venezuela is about 1.167 million b/d. Crude throughput is pegged at 983,000 b/d for 1996.

Much of the refining investment emphasis is on processing larger vol-

lines of heavy and extra heavy crudes.

Plans call for Pdvsa subsidiary Maraven SA to complete a \$2 billion upgrade of its 286,000 b/d Cardon refinery this year.

Pdvsa also plans to expand the 195,000 b/d Puerto La Cruz and 115,000 b/d El Palito refineries operated by its Corpoven SA unit.

Amuay project

In addition, Pdvsa subsidiary Lagoven SA will increase capacity of the hydrodesulfurization unit at its 571,000 b/d Amuay refinery. Plans call for expanding unit capacity to 250,000 b/d of high sulfur, heavy crudes from 190,000 b/d.

The project will allow the refinery to process feedstock from other refineries, distillates and gas oils, said Lagoven Refining Manager Heraldo Sifontes.

"That gas oil will be supplied to other refineries in the Pdvsa circuit to be used at catalytic cracking units for the production of gasoline," Sifontes said.

Amuay's expanded deep conversion capacity of 98,000 b/d breaks out as 64,000 b/d of flexicoking and 34,000 b/d of delayed coking.

During first half 1995, Amuay processed about 102,000 b/d of heavy crudes, the highest in 45 years of operation. That volume of throughput is expected to rise to about 170,000 b/d as expansion work progresses, Sifontes said.

"Refining hard to market heavy

crudes means greater operational and commercial flexibility for Lagoven," Sifontes said.

Pdvsa estimates about 73% of Venezuela's oil reserves are heavy and extra heavy crudes and 27% medium and light crudes and condensate.

Foreign refining

Pdvsa currently is negotiating the purchase of several refineries in the U.S. and possibly building another in Brazil, said Ronald Pantin, the company's strategic planning coordinator.

He did not disclose which plants are under consideration for purchase but said negotiations are based on an "association scheme" aimed at boosting Pdvsa's refining capacity by 100,000 b/d in the U.S., plus an additional 100,000 b/d of refining capacity in wholly or partly owned refineries at Lake Charles, La., Corpus Christi, Tex., Paulsboro, N.J., Savannah, Ga., Lemont, Ill., and Houston.

In addition, Pdvsa has 310,000 b/d of refining capacity at the Isla refinery in Curacao and a combined 260,000 b/d of capacity at refineries in Germany, Sweden, Belgium, and the U.K.

Heavy oil upgrading

As an adjunct to the refining expansion, Pdvsa continues to press projects with ARCO, Conoco, Mobil, and Total intended to produce a combined total of about 500,000 b/d of extra heavy crude and convert it into a more marketable synthetic crude.

Following an agreement last month setting up a \$2 billion heavy oil joint development/marketing venture be-

tween Chevron Corp. and Pdvsa unit Maraven SA (OGJ, Dec. 25 1995, p. 29), Mobil is expected to complete negotiations on a similar project involving Orinoco extra heavy crudes with Lagoven.

"The prospects for that project look very positive," said Lagoven Pres. Julius Frinkunas.

He noted the prefeasibility study for the project is complete, and the contract should get a final green light for signing in the first quarter.

Under their strategic association, Mobil and Lagoven would set up a joint venture to produce about 100,000 b/d of extra heavy crude from the Orinoco belt's Cerro Negro region. The Cerro Negro crude will be upgraded at Kening's syn-crude.

The deal is expected not only to open markets to Lagoven in the U.S. but also lead to other joint ventures involving the two companies in the U.S.

Last November, Maraven signed a 35 year, \$1.5 billion strategic association contract with Conoco Inc. to produce, transport, and upgrade 120,000 b/d of Orinoco extra heavy crude (OGJ, Nov. 13, 1995, Newsletter).

Earlier, Maraven signed a contract with Total covering a \$2.85 billion project to produce and upgrade 180,000 b/d of Orinoco crude.

A \$3.5 billion strategic association between Corpoven and ARCO to produce 165,000 b/d of Orinoco crude, upgrade that to 210,000 b/d of syn-crude, and export the syn-crude still is pending approval (OGJ, Oct. 3, 1994, Newsletter).

Protests linger over Shell Nigerian connection

Royal Dutch/Shell has come under more fire for its role in Nigerian operations.

In the latest development, London's Shell Centre buildings, U.K. headquarters for many of the company's international operations, was the starting point for a Jan. 4 protest against the company and Nigeria's military regime.

The Ogoni Community Association organized a march from Shell Centre to the Nigerian High Commission and on to St. James's Church, Piccadilly, for a memorial service for Ken Saro-Wiwa and eight other activists executed by the Nigerian government late last year (OGJ, Nov. 20, 1995, p. 37).

Also in London, members of Britain's Royal Geographical Society voted to expell Shell as one of their sponsors because of its Nigerian oper-

ations.

Meantime, Nigerian Minister of State for Petroleum Resources Kabir Chafe said threats by Britain and the U.S. to boycott Nigeria's oil won't harm his country's economy if they develop.

Chafe told Kaduna newsmen Nigeria would simply turn to other companies waiting to do business with his country if the U.K. and U.S. make good their threats.

Target Shell

Although Shell was once again the target of protests because of its supposed close links with government to facilitate its oil operations in Nigeria, the anti-Shell feeling was more muted than in recent months.

A Shell International spokesman said only about 30 protesters gathered outside Shell Centre, and there did not appear to be any reference to Shell in posters and banners they displayed.

The official said Shell had been asked to protest to Nigeria's government over 19 more Ogoni tribe protesters, currently held on the same charges, murder, as Saro-Wiwa and colleagues and due for trial at an undisclosed date.

In Kaduna, Chafe pointed out that Iran and Libya are under U.S. oil embargos but are still exporting their oil to other buyers.

He said Nigeria is bolstering its economic relations with China, Russia, and eastern European countries to forestall any embarrassment sanctions from the West might cause.

Pdvsa and lands biggest Asian supply contract for Orimulsion

Venezuela's Bitumenes Orinoco (Bitor) soon will sign a deal to sell 3.4 million tons/year of Orimulsion to Taiwan, matching its biggest sale to date.

Orimulsion is an emulsion of extra heavy crude oil, water, and a surfactant that is designed to back out coal as a low cost, environmentally preferred boiler fuel.

Bitor is a subsidiary of state owned Petroleos de Venezuela SA (Pdvsas).

Far East market push

Bitor Pres. Jorge Zemella said his company received "with great satisfaction" a report from Taiwan on the outcome of a tender by Taiwan's state owned power company to select new projects assigned to independent power producers (IPPs).

Zemella said Bitor affiliate MC Bitor Ltd. will "significantly penetrate" the Asian market with the Orimulsion sale to Taiwan.

Orimulsion will be the sole fuel of a power plant to be built by a group led by Intergerm at Lizhe in the Suao region on Taiwan's east

coast. Sales will begin in 2000.

The project is one of many proposed under a Taiwanese government initiative to solicit IPPs from the private sector to build power plants to meet Taiwan's soaring electric power demand.

Taiwan's Ministry of Economic Affairs recently chose from the first round of proposals seven groups to build a total of 7.11 million kw. Combined power capacity of 23 projects proposed under the first round totaled 30.3 million kw.

Oil products and natural gas will feed some of the other winning projects.

Lizhe project

Among the companies selected in the first round is a combine led by International Generating Co. (Intergerm), a joint venture of Bechtel Group and Pacific Gas & Electric affiliates. Other members of the group are Taiwan Synthene Rubber Corp., APED, and China Steel.

The combine's Lizhe plant will have an installed generating capacity of 1.5 million kw involving two units of 750,000 kw each.

One of the units will begin operations about mid-2000 and the second by the end of that year.

MC Bitor and Mitsubishi Corp. will supply those units about 3.4 million tons/year of Orimulsion for 25 years exported from the Jose terminal in Anzoategui state, eastern Venezuela.

It will be the largest supply contract of Orimulsion in the Asia-Pacific region. MC Bitor and Intergerm are reported to sign the agreement soon.

Zemella said, "The approval constitutes the most significant step forward in the Asia-Pacific region by Bitumenes Orinoco, through MC Bitor, in penetrating the electricity segment of the energy market in the Far East."

The market has been dominated by energy sources such as gas, coal, and conventional liquid hydrocarbon fuels.

The next step in marketing Orimulsion in the region is to prepare an environmental impact study to obtain permits from Taiwanese local and regional authorities.

Venezuela's E&D round mostly successful

Venezuela's first profit sharing exploration and development licensing round has yielded generally positive results.

Although two of the 10 blocks up for bid received no bids, some of the remaining blocks received hefty ones. State owned Petroleos de Venezuela (Pdvsas) netted about \$215 million in tiebreaker bonuses in the round, in addition to about \$15 million from the sale of data packages to prospective bidders.

The 10 blocks, covering 4.5 million acres, are believed to contain potential oil reserves of at least 7 billion bbl of medium and light grade crude in addition to substantial potential volumes of natural gas (see map, OGI, Sept. 18, 1995, p. 85). Preliminary estimates of potential oil reserves for the combined blocks ran as high as 23 billion bbl of light and medium gravity crude.

The tender marks the return of foreign companies to full equity participation in oil and gas E&D, a sector that Venezuela nationalized 20 years ago. It is expected to generate as much as \$12 billion in added investment in

Venezuela's upstream sector the next 10-15 years (OGI, Jan. 15, p. 24).

The tender was marred by litigation stemming from concerns over clauses in proposed profit sharing contracts.

The push to expand foreign investment in Venezuela's upstream oil sector underlies the government's goal of doubling oil revenues in 7 years from the current \$6 billion/year.

To meet that goal, Caracas is counting on investment by Pdvsas and private companies, especially foreign firms, to help jump productive capacity to 5.7 million b/d from today's 3.15 million b/d.

Venezuela currently claims to produce about 2.4 million b/d, close to its Organization of Petroleum Exporting Countries' quota of 2.359 million b/d. However, other sources have placed Venezuela's output considerably higher than that, exceeding quota by more than 300,000 b/d.

How the bidding went

Pdvsas voiced satisfaction with results of the E&D profit sharing license round. More than 75 companies pre-

qualified for the bidding.

"We are very pleased with the results," said Pdvsas Pres. Luis Giusti. "The most important thing is that the massive attendance of large, medium, and small companies has ratified investor confidence in the country's petroleum industry."

Beyond concerns over tax and currency issues, international oil and gas executives praised Pdvsas for a smoothly run tender.

"In some cases, we declined to submit bids simply because the risks in those areas were far too high or because we just did not have sufficient geological data to make a final decision," said one executive whose company failed to obtain a contract. "This by no means points to a lack of interest in Venezuela, which remains an attractive oil country."

Pdvsas estimates \$1 billion will be spent in the first 3 year exploration period for the profit sharing blocks and another \$10 billion the following 7 years. The contracts call for outlays of

at least \$40-60 million/block.

In the event of a commercial discovery, license terms call for a Pdvsa affiliate to have an option to purchase a working interest by paying a pro rata share of costs incurred to date.

Pdvsa is expected to hand over the signed contracts early this month to the Energy & Mines Ministry, which in turn will send the documents to the cabinet of ministers, then to

Ronald Pantin, Pdvsa strategic planning coordinator, expressed surprise that Amoco and the Total/Statoil combine each offered a 50% PEG. He noted industry sees only one major oil play in the area but added that a major natural gas strike is highly prospective there.

In addition, the swampy region poses logistical challenges.

Oil Co./Lismo plc, Petrobras Brasil-eim SA/Benton Overseas Petroleum & Investment Co., Unocal Corp./Japan Petroleum Exploration Co. Ltd., and Repsol SA/Enterprise plc.

Work commitment for the La Ceiba block in the first 5 year phase of exploration is about \$50 million. The minimum work commitment calls for drilling of three wildcats. Plans call for seismic surveys to get under way this year.

Ronald Wilson, president of Mobil Latin America business development ventures, noting Mobil is familiar with the La Ceiba area, said, "We expect to find large accumulations."

Mobil first operated in Venezuela in 1934 and, with the country's new efforts to attract foreign investment, seeks to expand its presence.

Mobil is currently negotiating a \$1.8 billion strategic association with Pdvsa subsidiary Lagoven SA to produce and upgrade 100,000 b/d of extra heavy crude from the Orinoco oil belt. In addition, Mobil recently returned to lubricant manufacturing and marketing in Venezuela last year, when it purchased 50% of local company CA Nacional de Gases & Lubricantes, the country's biggest lube plant.

Veba also has a long association with Pdvsa, dating to 1978 when it entered into a government backed accord between Germany and Venezuela for technical cooperation in the energy sector. In 1983, Veba and Pdvsa formed a joint venture, Ruhr Oel, to operate Germany's biggest refining system with throughput capacity of 440,000 b/d.

Conoco blocks

Conoco bid alone in winning the West Gulf of Paria block in shallow water off Venezuela's northeastern coast in the Caribbean Sea.

Competing against Conoco were the Canadian-South Korean group of Canadian Occidental Petroleum Ltd., Numac Energy Inc., Yukong Ltd., and Korea Petroleum Development Corp.; Agip/Norsk Hydro; and the Canadian-Argentine combine Talisman Energy Inc./Astra Capsa.

Conoco offered a 50% PEG plus a tiebreaker bonus of \$21.2 million compared with the runnerup Canadian-South Korean group's bid of \$20.2 million.

Terms call for a 4 year, \$30 million commitment to drill two wells and acquire seismic data in the western

RESULTS OF VENEZUELA'S LAZAR PROTE SHARING ROUND

Block	Area (sq km)	Estimated potential oil reserves (million bbl)	Estimated potential production (1,000 bpd)	Winning bidder(s) (%)	Profit sharing bonus (%)	Tiebreaker bid (million \$)	First year projected exploration investment (million \$)	Five year projected investment (million \$)
Guarema	1,688	825	180	Elf 50, Conoco 50	50	—	55	541
San Carlos	1,171	405	95	Compagnie BP 37.5, Amoco 37.5, Maxam 25	40	—	28	698
Guarapiche	1,900	990	200	Conoco 100	50	109	162	1,583
West Gulf of Paria	1,134	600	135	Envan 90, Ineletra 10	50	21.2	144	1,146
East Gulf of Paria	1,080	630	130	LL & E 37.5, Norcen 37.5, Benton 25	29	—	121	1,201
Delta Centre	2,138	820	180	Amoco 100	41	—	107	1,393
Punta Pescador	8,046	700	134	Mobil 37.5, Veba 37.5, Nippon 25	50	10.7	98	688
La Ceiba	1,742	791	180		50	104	120	1,482

*Catatumbo and El Sombrero blocks did not receive bids.

Venezuela's congress for final approval.

Exploration generally is expected to get under way in first quarter 1997.

Amoco blocks

Attracting the most interest in the bidding was the Guarapiche block in eastern Venezuela, which is believed to hold as much as 1 billion bbl of medium and light gravity crude.

A combine of Amoco Corp., British Petroleum Co. plc, and YPF SA unit Mayra Energia Corp. won the block based on a 50% pretax profit sharing bonus (PEG) plus a tiebreaker bonus of almost \$109 million.

Amoco bid solo to win the Punta Pescador block in eastern Venezuela, just east of the Guarapiche block in which the company is a partner. Amoco offered a 50% PEG and a tiebreaker bonus of \$10.7 million.

That topped a bid of 50% PEG and tiebreaker bonus of \$5.6 million by a combine of France's Total and Norway's Den norske stats oljeselskap AS.

Amoco plans to spend at least \$40 million to explore its Punta Pescador block. The block lies just south of gas fields Amoco is developing off Trinidad.

La Ceiba block

A close second to the Guarapiche bid was the winning offer for the La Ceiba block along the southeast edge of Lake Maracaibo, thought to hold 790 million bbl of oil reserves.

Here, a Mobil Corp. led group that includes Germany's Veba Oil AG and Japan's Nippon Oil Exploration U.S.A. Ltd. made a winning bid of 50% PEG and tiebreaker bonus of almost \$104 million.

Mobil and partners shared the 1,793 sq km La Ceiba block on the western shore of Lake Maracaibo on the first day of bidding, Jan. 22 (OGJ, Jan. 29, Newsletter). Interests in the block are Mobil 50%, Veba 30%, and Nippon 20%. Their winning tiebreaker bonus bid topped bids by nine other groups that matched the 50% PEG bonus.

Closest to the winning bid was Exxon/Shell, which offered a 50% PEG bonus plus a \$57.5 million tiebreaker bonus. Other bidding for La Ceiba were Amoco, Texaco Inc./Mitsubishi Corp./Maxus, Elf Aquitaine/Conoco Inc., Agip SpA/Norsk Hydro, Total/Statoil/Petronas Carigali, Marathon

Gulf of Paria between Venezuela and Trinidad. Exploration is to get under way right after the contract is signed.

Conoco combined with Elf Aquitaine 50-50 to take the Guanare block in Portuguesa state in western Venezuela. The block is in the foothills of the Menda Andes.

The work commitment calls for a 5 year, \$30 million outlay to drill four wells and acquire seismic data. Work is to get under way immediately after the contract is signed.

Conoco also has a strong presence in Venezuela.

It formed a joint venture, Petrozuata, with Pdvs's unit Maraven SA to produce 1.5 billion bbl of Orinoco extra heavy crude and convert it to synthetic crude, most of which will be processed in Conoco's U.S. refineries. Construction on the \$1.4 billion project is to get under way early in 1997.

Conoco also is a partner with Bitumenes Orinoco SA to convert Orinoco bitumen to Orimulsion. Pdvs's proprietary heavy oil/water/surfactant emulsion is used as a boiler fuel.

LL&E group block

A group made up of Louisiana Land & Exploration Co. (LL&E), New Orleans, Norcen Energy Resources Ltd., Calgary, and Benton Oil & Gas Co., Carpinteria, Calif., won the Delta Centro block in eastern Venezuela.

Operator LL&E will hold a 35% interest in the block. Norcen will take 35% and Benton 30%.

The Delta Centro block lies in a mostly marshy region of the Orinoco River delta in Northeast Venezuela's Delta Amacuro state.

The group's work commitment calls for acquiring and processing 1,300 line km of seismic data and drilling three wells in 5 years with an option to extend the exploration period 4 years.

Work is to get under way after the contract with Pdvs is signed.

LL&E Chairman M. Leighton Savage and noted the Delta Centro block's marshy terrain is similar to marshlands in Louisiana where LL&E has long operated.

Other bidding

Perez Compana SA took the San Carlos block in Cojedes and Portuguesa states of Southwest Venezuela.

The Argentina company topped a bid by Elf by offering a 40% PEG. Perez Compana currently is involved in reviving oil production in Venezuela under the country's marginal fields participation program.

A combine of Enron Corp. and

WATCHING THE WORLD



With David Knott from London

The unequal split of British Gas

Facing competition in U.K. gas markets, restrictions by government regulations, and massive gas contract debts, British Gas plc will split into two companies.

The former U.K. gas supply monopoly, privatized in stages beginning in 1986, will split into a large company, to be known as Transco International plc, and a smaller unit, British Gas Energy plc.

Chairman Richard Giordano said, "This demerger is about the creation of two separate companies that will manage our business more effectively to the advantage of our customers, shareholders, and employees."

But some pundits say the move is designed to protect the company's profitable businesses from losses in long term take or pay gas purchase contracts.

Ahead of gas market deregulation, U.K. operators developed gas fields to support their plans to supply gas directly to end users. Trading in gas began among companies. And with the glut of new gas the spot price fell.

Assets shored up

Because of the low spot price, British Gas is said to face losses of £1.5 billion (\$2.25 billion) on long standing contracts worth a combined £40 billion (\$60 billion).

The new Transco unit will get the biggest asset, British Gas' transportation and storage business, along with most of the exploration and production assets and the potentially lucrative power generation business and international operations.

British Gas Energy will be a comparative runt, given only the parent's supply and trading business. This is where it faces intense competition from new suppliers and big losses on

gas purchase contracts.

British Gas Energy also will get U.K. Morecambe Bay producing gas fields, which a spokesman said would allow it to compete with independents in liberalized markets.

Two fields with original reserves amounting to 6.6 tcf of gas, one of which has been on stream since 1985 and one since 1994, does not seem a great deal with which to take on fierce competition—particularly when British Gas estimated its reserves in 1994 at almost 2 billion bbl of oil equivalent.

Public outcry

British Gas said the smaller company will receive no exploration assets or expertise in the transfer. So it will face an immediate problem in replacing reserves to remain competitive.

Transco is to be like a utility with steady returns, while British Gas Energy will be more like a consumer company with ups and downs in income. And everybody knows how much a consumer business can die.

The outcry has been evidenced in the British press by the news that Cedric Brown, British Gas chief executive, is to retire Apr. 30.

Following a turn over Brown's 75% pay hike in December 1994, Britons are now incensed by reports that he will get a £4 million (\$6 million) retirement package and will be retained as a consultant for the demerger.

Government's original idea in privatizing British Gas was supposed to be to make a cumbersome giant efficient and profitable. This latest move is a warning against following political dogma to the detriment of practical considerations of gas supply.

Inectra won the East Gulf of Paria block.

Catatumbo block, southwest of Lake Maracaibo, and El Sombrero block, in Central Venezuela, failed to attract bids.

Noteworthy for their absence from the list of winning bidders was a combine of Exxon Corp. and Royal Dutch/Shell Group that was expected to dominate bidding. However, the combine bid conservatively for the La Ceiba and Punta Pescador blocks and came away empty handed.

Some prospective bidders were daunted by the stiff terms Venezuela

imposed on the profit sharing deals. They call for income taxes totaling 67.7% and royalties of 16.7% in addition to the PEG and tiebreaking bonuses.

A second try

Pdvsa on Jan. 29 tried again and failed to attract bidders for the Catatumbo and El Sombrero blocks.

Representatives from several private companies said high risks, low prospects for crude oil discoveries, and lack of geological data discouraged interest in those areas.

Juan Szabo, president of Venezuelan

Petroleum Corp. (CVP), said, "The lack of interest in some areas is relatively normal because each company chooses those blocks that fit their figures and their particular strategies."

CVP, a once defunct Pdvsa subsidiary, was revived specifically for the bidding process and given the portfolio of blocks to be tendered.

Winning bidders will sign the profit sharing contracts and set up joint ventures (JVs) with CVP. The Pdvsa unit will own as much as 35% of the JV stock, with the remainder held by foreign partners.

Pdvsa is considering putting together another tender for new blocks as part of its apertura, or "oil opening" policy, which includes profit sharing contracts, operating agreements, strategic associations, and alliances. A new round of bidding could occur as early as the end of this year or early next year.

Legal concerns

The tender was held against a backdrop of optimism in government and oil industry circles and concern among many oil executives regarding aspects of the proposed joint venture tax issues and Venezuela's onerous currency control regulations.

Venezuela currently is negotiating an economic restructuring accord with the International Monetary Fund, under which it had agreed to lift currency exchange controls in first quarter 1996.

In addition, a group of intellectuals including Central University of Venezuela Rector Simon Munoz and chamber of deputies (lower house) energy and mines committee Chairman Ali Rodriguez filed two lawsuits in Venezuela's supreme court over the proposed profit sharing contracts. They claimed the proposed clauses allowing international litigation to settle differences and barring municipal authorities from exercising autonomy on tax matters violate the constitution.

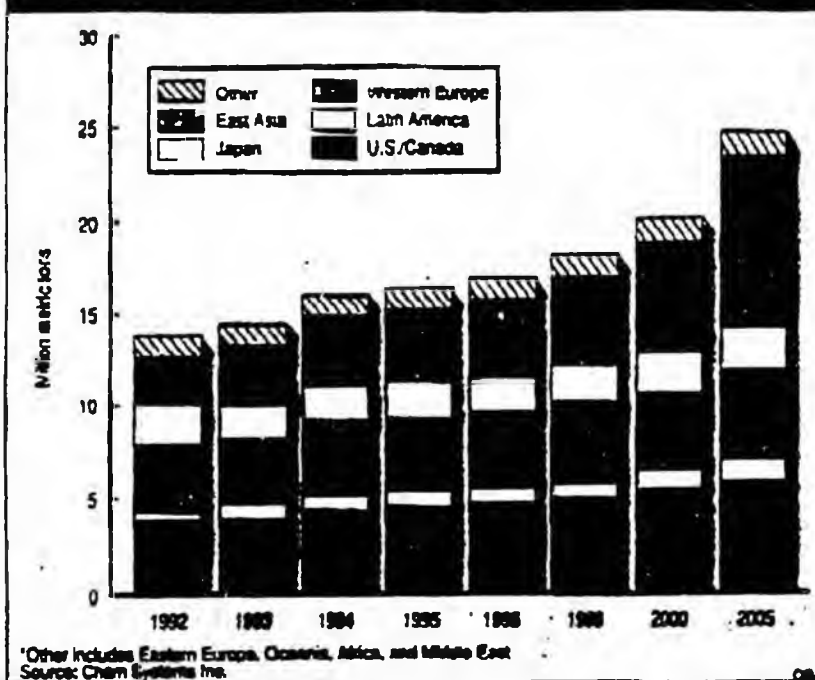
Giusti said there are no legal grounds for the lawsuits because under the constitution, municipal authorities have no autonomy to set taxes for the oil industry.

Regarding currency controls, Giusti said regulations currently allow companies to hold offshore dollar accounts and make profit remittances in foreign currency.

However, private oil companies contend issues such as municipal and other taxes and currency controls should be clarified in the contracts.

Government sources said a decree is being written to allow foreign companies operating in Venezuela to choose dollar accounting as the nation's stiff currency control system is put aside.

HOW WORLD STYRENE DEMAND WILL RISE



Strong styrene growth foreseen

Eastern Asia will lead hefty growth in world styrene demand through 2005.

Driving the region's 9.3%/year increase in styrene consumption are economic growth, improved standards of living, and increasing exports of finished products.

Those are the findings of a study by Chem Systems Inc., Tarrytown, N.Y.

The firm predicts world styrene consumption will increase at an average 4.1%/year through 2005, fueled by increased demand for polystyrene and acrylonitrile butadiene styrene (ABS).

Most styrene capacity expansion will take place in eastern Asia. Chem Systems expects additions in that region to total 2.5 million metric tons/year by 1998. This massive

capacity increase will reduce world operating rates, shift trade patterns, and squeeze profits in traditional exporting countries.

World styrene consumption increased 9.6% during 1994, making styrene one of the leaders in commodity petrochemicals' recent recovery.

Devalued growth was strong for all styrene derivatives, especially polystyrene and ABS, which combined account for 75% of world styrene consumption.

In 1995, says Chem Systems, growth in styrene demand was less than anticipated because of inventory adjustments and an unexpected slide in shipments to China after the country closed its southern border.

European gasoline prices. Furthermore, if the WTO orders Washington to relax restrictions on gasoline from foreign plants, imports from Brazil could soar to 30,000 b/d, as in 1993, instead of the meager 12,000 b/d of components state Petrobras has been selling to the US of late (p8). The loss of 110,000 b/d of gasoline supply in the East Coast — enough to cover more than 3.5% of local demand — could add 1¢ a gallon to prices, according to Houston-based Stone Bond.

An expected drop in the availability of spot barrels — as Tosco diverts gasoline from its nearby Bayway refinery into its filling stations to replace the lost barrels from Marcus Hook — could also prove a stimulant to New York Harbor prices, by weakening the heavy-selling firm's bearish influence over that market. Recent changes to the New York gasoline futures contract should further boost liquidity and price transparency.

Successful Tender Sets Stage For Next Act In Venezuela

Any remaining skepticism about the level of international company interest in Opec-member Venezuela's oil patch disappeared last week. At a licensing round for 10 exploration blocks, large foreign oil companies — led by British Petroleum, Conoco, and Mobil — bid aggressively in terms of both bonuses and proffered government take for the most prospective acreage, pushing the hemisphere's heavyweight closer to its goal of lifting burgeoning capacity from 3.1-million barrels a day to 5.5-million b/d in 2005. State Petroleos de Venezuela is now mulling over the next stage in the country's reopening, including the possibility of direct negotiations to reactivate smaller fields ahead of another competitive tender. Firms have conducted geological studies on some of Venezuela's oldest fields in PDV subsidiary Maraven's domain around Lake Maracaibo, with hopes of clinching direct service deals like the one Chevron signed for the Boscan field last month (PIW Dec.11.p8). Pennzoil has its eye on Mene Grande, and Canadian Occidental is targeting Cabimas, both of which now pump only a few thousand barrels a day. But political pressure still favors competitive bidding for most acreage awards, and PDV is already pondering which areas to offer in a third marginal-fields round at year's end.

Underscoring the majors' enthusiasm, despite complaints over fiscal terms and lingering uncertainties in the profit-sharing contract, the bidding opened with an impressive nine-way tie out of 11 participants for the prized La Ceiba block east of Lake Maracaibo. It was finally awarded to Mobil and partners Germany's Veba and Japan's Nippon Oil in a high-stakes runoff in which they posted a hefty \$104-million cash bonus. The runners-up were Exxon with Royal Dutch/Shell and Texaco with Mitsubishi and Argentine YPF. BP, Amoco, and YPF paid a \$109-million bonus in order to break a four-way tie for the coveted Guarapiche block in the swampy Delta region. Other blocks named fewer heads, and the gas-prone El Sombrero generated no bids at all. El Sombrero, which lies southwest of Caracas, is to be re-offered this week. As at La Ceiba, which holds an estimated 800-million barrels or more of reserves, the companies offered the government the maximum 50% share in pre-tax profits at offshore Gulf of Paria West and at onshore Guanara, Guarapiche, and Punta Pescador. Conoco won the first after posting a \$21.2-million bonus, and then teamed up with Elf Aquitaine as operator to win Guanara. Amoco got Punta Pescador with a \$10.6-million cash bonus. Enron with local consulting giant Inelectra was sole bidder for offshore Gulf of Paria East, offering Caracas a 29% profit share, while Argentine Perez Companc outbid Elf for the San Carlos tract in the central region, offering the state 40% of profits (PIW Jan.15.p8).

Impending changes in PDV's upper ranks, possibly even appointing savvy President Luis Giusti, probably won't shift the country's basic reopening campaign or its recession-driven grab for market share, given the gravity of the Caldera administration's domestic economic woes. Indeed, word that Giusti could take over the Finance Ministry raises the prospect of a further loosening in economic controls, a possibility that would spark even more interest in oil and gas projects. Talks with the Internacional Monetary Fund, however, seem to be faltering, as President Rafael Caldera continues to resist another hike in subsidized domestic gasoline prices. The high level of bonuses obtained in the bid round may feed opposition to an IMF deal. A PDV insider would likely replace Giusti.

LEGAL SERVICES

**DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA**

MAR 25 1996

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130 Seward Street, Suite 409
Juneau, Alaska 99801-2105

MEMORANDUM

March 25, 1996

SUBJECT: Renegotiation of State Oil and Gas Lease

TO: Senator Drue Fearce
President of the Senate

FROM: Jack Chenoweth
Legislative Counsel

I am responding to three questions set out in your March 22 memo.

1. I have not found explicit statutory or regulatory authority to renegotiate an oil and gas lease as seems to be contemplated in the North Star field lease. See by way of specific example, 11 AAC 71.205 authorizing amendment of timber and materials contracts except that the amendment "may not materially affect or change the meaning or intent of the contract," 11 AAC 71.205(b). The lease documents applicable to the North Star field lease may authorize or provide for renegotiation under specific circumstances, but I don't know this.

Even absent an explicit statute or regulation or provision in the lease, as a matter of general law, negotiations may be initiated to amend a competitively bid public contract. 72 C.J.S. Supp., "Public Contracts," sec. 24. However, amendments to competitively bid contracts are prohibited if the amendments proposed are "material," that is to say, competitively bid contracts may not be materially amended. McKinnon v. Alaska, 633 P.2d 281, 287 (Alaska 1981), Kenai Lumber Company v. LeRonde, 646 P.2d 215, 221 (Alaska 1982). Amendments to a contract are "material" if they involve the alteration of factors that influence the judgment or decision on the award of the contract. Brown v. Ward, 593 P.2d 247, 250 (Alaska 1979), Cousineau v. Walker, 613 P.2d 608, 613 (Alaska 1980). Based on the pre-lease analysis, the state's choice of leasing method—including the decision to take net profit share using the amount reserved as the bid variable (which I think is what is at work in the award of the original North Star field lease)—seems to be "material" by any measure.

2. Without having a notion of what the administration may choose to offer, still, I think the administration will, in one way or another, ask the legislature to ratify or validate modifications proposed to the North Star lease.

Senator Drue Pearce
March 25, 1996
Page 2

An Act or public enactment to validate the modification of a public contract is a form of curative legislation. Yelton v. Plantz, 89 N.E.2d 540 (Indiana 1950); C. Sands, Sutherland Statutory Construction, sec. 71.07. As a general rule, curative legislation is valid (1) when the legislature originally had power to authorize the acts that were done and (2) the curative legislation does not impair a vested right in violation of constitutional provisions prohibiting impairment of contract. Fairbanks North Star Borough v. State, 753 P.2d 1158, 1160 (Alaska 1988). The legislature might have authorized renegotiation of public contracts, and, depending on what is submitted, it is more probable than not that the proposed legislation would not impair a vested right (assuming that the state administration is prepared to waive the right to receive revenue under the original lease by shifting from one choice of leasing method to another).

A validating or curative act is usually subject to the "local or special" act limitations of a state constitution. C. Sands, Sutherland Statutory Construction, secs. 41.11 - 41.13. Even if it was a consideration in this instance, there is, it seems to me, good chance that the court would find the test of Abrams v. State, 534 P.2d 91 (Alaska 1975) to control and determine that the modification of an oil and gas lease with significant potential revenue-producing capacity is a matter of common interest to the whole state, having, through the contributions to the state treasury, probable statewide interest and impact, and therefore not subject to the local and special legislation prohibition provision.

It is also possible, of course, that the legislation sponsored by the administration will be general, in that it will authorize renegotiations of all or some types of oil and gas leases. That type of legislation, potentially applying to other leases as well as the North Star lease, would avoid the "local or special act" question altogether.

3. Your memo describes legislation that addresses the possibility that the state may receive less revenue than originally anticipated. It does not propose to withdraw money from the state treasury, therefore an act addressing renegotiation of the lease is not to be regarded as an appropriation.

JBC:glc
96-177.glc

LEGAL SERVICES

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MEMORANDUM

March 11, 1996

SUBJECT: Administration revocation or amendment of "net profit" oil and gas lease without legislative approval (Work Order No. 9-LS1783\A)

TO: Senator Drue Pearce
President of the Senate
ATTN: Stephanie Szymanski

FROM: Jack Chenoweth
Legislative Counsel

You have asked whether, under AS 38.05.180(p) or 38.05.180(s), the administration may revoke or amend a "net profit" oil and gas lease without prior legislative approval.

The answer must be yes. Neither AS 38.05.180(p), relating to leases made subject to a unitization agreement, nor AS 38.05.180(s), relating to leases subject to a communitization or similar drilling arrangement, imposes a limitation on the administration's right to reform or revoke an oil and gas lease that subjects the reformation or revocation to prior legislative approval.

The legislature's involvement in oil and gas leasing is rather limited. Under AS 38.05.180(h), the legislature is entitled to receive and review the five-year oil and gas leasing program proposed by the administration. Legislative approval of anything involving oil and gas leasing appears to be limited to disagreement with a decision by the administration to take state royalty oil or gas in cash rather than in kind. See AS 38.05.182(b). The legislature may also approve the sale of royalty oil that has been taken in kind. See AS 38.05.183. Apart from those, the legislature has not asserted authority to approve a proposed oil or gas lease and, consequently, cannot assert that the administration may not reform or revoke an oil and gas lease without legislative consent.

JBC:klb
96-179.klb

April 23, 1996

APR 23 1996

Gov. Tony Knowles
Rep. Joe Green
Rep. Sean Parnell
Rep. Con Bunde
Sen. Judy Salo
Sen. Loren Leeman

Re: BP lease negotiations at Northstar

Dear Governor, Senators, and Representatives;

I would like to express my strong opposition to the recent negotiations with BP concerning renegotiation of the net profits and royalty terms of the Northstar oil field. I believe renegotiating the terms for this field is a bad deal for the Alaskan resource owner and is unfair to the larger oil industry. I work as a petroleum geologist in Alaska and my objections to the Northstar deal are these two:

1. Probable reserve growth at Northstar

The proposed terms reported in the press show Alaska losing much income from Northstar if eventual reserves are much larger than estimated and receiving more income if the field is smaller than expected. However, a typical oil field increases reserves between 2 and 3 times from the time of first discovery to last eventual production. This reserve growth occurs because of initial conservative estimates mandated by the SEC, by conservative estimates by the company itself, by application of unexpected, new technology to existing fields, and sometimes by unexplained superior performance of the reservoir. Many companies count on reserve growth and work it into their future expectation and upside, even though these are not officially booked reserves. Reserve growth of 2 to 3 times the original estimate is typical for the worldwide industry and not unusual. On the North Slope of Alaska, every field of which I am aware has experienced dramatic reserve growth, with the possible exception of the Lisburne Field, discussed below.

Oil recovery from Prudhoe Bay, Kuparuk, and Endicott Fields are now far in excess of original expected recovery. Kuparuk is an example of a field that has nearly doubled the expected producible reserves and

yields more oil than reservoir parameters would predict. A "fudge factor" is used to increase expected output from wells because experience has shown that the reserves are systematically underestimated, even with very good reservoir data. These fields that perform so well are clastic (sandstone) reservoirs and Northstar is of this type. It is a reasonable, based on past experience, for the Northstar reserves to increase over its life and this increase will likely be in the range of 2 to 3 times today's estimate. This would be the expected case. It is exactly in this scenario that the State of Alaska is giving up the most value in the current renegotiation and I fear Alaska will lose much income in the long run.

The only exception to reserve growth for North Slope fields that I know of is the Lisburne field, which is a carbonate (limestone) reservoir, which is significantly different from the clastic reservoirs. So far the Lisburne Field has been a disappointment and limestone horizons have under performed. However, lower dolomite zones in the Lisburne were drilled in 1994 and the first well in these lower zones has produced far more oil from dolomites than previous wells in the limestone. This well (NK-26) has produced 1.2 million barrels of oil in about 2 years and more wells are planned for this interval. It remains to be seen if the Lisburne Field in the end will remain a disappointment.

2. Level Playing Field

Exploration in Alaska is based on all companies having an equal opportunity to bid and participate in the process. I find the process of renegotiating freely bid lease terms offensive to fair play and I fear it will in the long run tend to undermine the leasing process. Amerada and BP were both well aware of the implications of the lease terms at Northstar and willingly agreed to the lease stipulations. If these companies made a poor business decision, Alaska has no obligation to be a safety net for them.

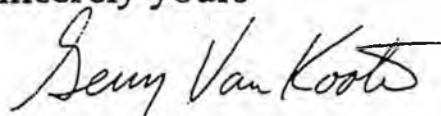
I find it particularly offensive that BP is using a political process to circumvent agreed lease terms. This approach rewards companies that can muster the most political pressure and has the sharpest negotiators. It also opens the political process to immense pressure from the oil industry. If BP is successful, I would expect every other company to come with requests for relief and the State will be hard pressed to deny these requests. We have already seen Unocal at the

table with relief requests for Cook Inlet fields. The renegotiation with BP feels like special treatment and a cozy relationship.

I feel if BP cannot develop Northstar under the very onerous lease terms, the lease should return to the State and be reoffered under new terms to all parties, including BP. This insures that everyone has equal opportunity to participate and bid the value they feel is appropriate. This system of leasing at both State and Federal levels has historically been highly successful in generating high value for lease tracts.

I appreciate the opportunity to express my views and thank you for your consideration.

Sincerely yours

A handwritten signature in cursive script that reads "Gerry Van Kooten". The signature is written in dark ink and is positioned below the typed name.

Gerry Van Kooten
4551 East 135th Ave.
Anchorage, Ak 99516
907-345-7900

April 24, 1996

An Open Letter to Mr. John C. Morgan, President BP Exploration (Alaska) Inc.

Thank you for sending me letters and brochures about BP's Northstar development. I agree with you Alaska is in a new era of oil development. This new era is causing the industry, the state and others to re-examine the business of oil development in Alaska's unique conditions. As one of the brochures points out Alaska is 39% of BP's world oil production. I believe BP is approximately 40% of Alaska's oil production. It is obvious we need each other.

I, like you, am glad the period of acrimonious attitudes between the state and the oil industry is becoming a thing of the past. As you know attitudes can shift every two or four years with elections. I have also come to notice attitudes shift with changes in the leaders of companies.

As part of the North Slope Alliancing programs and BP's efforts "to maintain an open dialogue with Alaskans" it would be good if all parties could get beyond the short term desire (like lowering the royalties on a specific oil field) and focus more on the long-term vision of our relationship. Like any relationship we each carry some history with us, or to use an American slang, we have to live with each others baggage, as well as our own.

The Dutch are using covenants between industry and government to create innovative partnerships. These agreements are being touted in some disciplines as a way to improve relationships and reduce costs. As part of our new era would the industry be willing to enter into a covenant with the people of Alaska for the development of the state's resources? These covenants could be put to a vote of the people to approve our long term relationship.

These covenants could include the new international standards on environmental management, ISO 14000. These standards are similar to the British Standard 7750 which I am sure BP staff are familiar with. The ISO 14000 standards are rapidly becoming the benchmark for leading corporate environmental programs.

In these days of partnering many streamlining steps are developed by employees. One approach used by a growing number of businesses is Open-Book Management. Open-book management is a way of running a company that gets everyone focused on helping the business make money. Simply put, employees who understand how the company makes money and how they contribute to the bottom line can then act to do so. I suggest you read the book *Open-Book Management: The Coming Business Revolution* by John Case. BP might explore using this approach to bring Alaskans and your company together so we both benefit from development of smaller fields.

One idea is to use one of the newly developing fields, such as Northstar, as a test case of open book management. As part of the "Alaska Energy Infobank" set up a Web page so all Alaskans, all the owners of the oil, can work with BP. Ideally, if BP makes money on Alaskan oil, so too will Alaskans make money on it being developed.

I know these ideas sound far fetched. As one of the brochures points out, "BP is going where no one has gone before." For BP's continued success in Alaska all of us need to go where no one has gone before. One of the ways to improve our dialogue is to get together and talk without a specific agenda, like lowering royalty shares. John Case's book provides several examples of how open-book management improves companies profit margin. This idea might help BP get the 2% more profit to make Alaska production as profitable as other parts of the world.

I agree with you that Alaskans need to get our fiscal house in order and close the "fiscal gap." Historically Alaskans have shown some financial wisdom, the Permanent Fund — our Prudhoe Bay — is one of the best run pools of wealth in the world. Though we can not rest on our laurels. This where I do not understand the wisdom of reducing Alaska's royalty shares so we decrease the money flowing into the treasury. Can't we work together so both your profit stays in the 40% range and Alaska stills receives revenue?

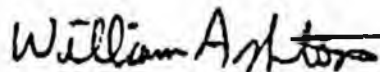
I suggest we work together though means other than advertising and direct mail to improve the relationship between the oil industry and the people of Alaska. In summary lets

1. Develop a vision for oil development in Alaska,
2. Use innovative ideas such as covenants, ISO 14000, and open-book management, and
3. Work together to go where no oil producing province has gone before.

BP has shown time and time again it meets the challenges of oil development in Alaska. I also believe Alaskans continue to meet the challenges of oil development. This is another opportunity.

I appreciate receiving your letters and information from time to time. If you have any questions please give me a call at 345-6600.

Sincerely,



William Ashton
200 W 34th Ave., #1120
Anchorage, AK 99503

Senator Loran Leman
Juneau, Alaska
FAX # 465-3810

Several years ago in an irreverent play called "Sister Mary Agnes Answers All Your Questions" a young man asks an elderly nun if God answers all prayers. Her answer is, "Yes, but sometimes the answer is no." Governor Knowles must not have seen the play, because his answer to BP's prayer is the wrong one.

Many people are watching your struggle to do the right thing in the face of heavy opposition. All we can ask is that you do your best to protect the interests and future of the State of Alaska. The stakes are high and the deck may be stacked. But you already know that.



Sheila M. Turner

Donald. W. Ince
3121 Capstan Dr.
Anchorage, AK 99516

April 22, 1996

Senator Loren Leman
State Capitol, Room 113
Juneau, AK 99801-1182

RE: Northstar Lease Terms

Dear Honorable Loren Leman,

I am writing this letter to voice my opposition to changing the Northstar lease terms as proposed by British Petroleum and Governor Tony Knowles. I have been following closely the developments regarding the Knowles-BP deal and I am convinced this is a terrible deal for Alaskans. I read in complete disbelief the manner in which Commissioner of Natural Resources John Shively has analyzed this deal. He essentially says we should trust his analysis that this is a good deal for Alaska. Unfortunately, examination of this deal simply does not support his statement.

There are basically three scenarios put forth for analysis as summarized in the chart below.

Northstar Oil Production	State Earnings		BP Pays Alaska (\$/barrel)	
	w/net profit	w/o net profit	w/net profit	w/o net profit
Case 1=130 million	\$444 MM	\$435 MM	\$3.42	\$3.35
Case 2=105 million	\$312 MM	\$340 MM	\$2.97	\$3.24
Case 3=180 million	\$934 MM	\$639 MM	\$5.19	\$3.55

In Case 1, if BP believes Northstar will produce 130 million barrels it is not clear why they would lobby so vigorously to change the lease terms. The difference they must pay to Alaska is only \$9 million or 7¢/barrel. In case 2, where Northstar produces only 105 million barrels, BP should negotiate to keep the net profit sharing provision. They would actually pay \$28 million less (27¢/barrel less) than if net profits were removed. BP obviously does not believe Northstar will produce only 105 million barrels. So, Alaskans must ask why BP is

spending so much time, money and effort to change these lease terms? The answer is clear when Case 3 is examined. They believe Northstar will produce significantly more oil than 130 million barrels. It is not difficult to understand why BP believes Northstar will become an over-achiever considering the past forecasts for other Alaska oil fields. Prudhoe Bay reserves have increased 35% from 9.6 billion to 13 billion barrels, BP's Niakuk field has increased 85% from 54 million to 100 million barrels since production began. BP's Endicott field has increased 200% from 300 million barrels in 1987 to 600 million barrels today.

BP is fighting hard to negotiate this upside potential away from Alaskans. If they succeed, BP will earn a \$295 million profit as shown in Case 3. If their negotiations fail to remove the net profit sharing provision, they will pay \$1.64/barrel more revenues to Alaska. BP has even resorted to intimidating Alaskans by threatening not to develop Northstar unless we give up our net profit share. When our Senate Resource Committee tried to modify the agreement BP's vice-president Eric Luttrell said, "BP will not reopen the negotiations and cannot agree to the changes." I would respectfully suggest that Alaskans tell Mr. Luttrell and BP that, "Alaskans cannot agree to changing the Northstar lease terms because we believe a deal is a deal and Northstar lease terms will not be reopened for negotiations."

Some legislators and other officials may believe this upside potential at Northstar is speculative and has no value. Obviously, BP believes exactly the opposite. They are hopeful Alaska will change the lease terms in return for something like a few jobs. But look carefully at the proposal. BP makes no binding agreement to construct modules in Alaska or hire Alaskans. The fifty permanent jobs BP estimates will be created by Northstar development will be needed regardless of what the lease terms are or who develops the field. So, it is very difficult for me to understand exactly what BP is offering Alaska residents that is tangible in return for us giving away our net profit share of Northstar.

I urge you to do the right thing and vote against changing Northstar lease terms.

Very truly yours,

Donald W. Ince
via fax



APR 22 1996

21 April 1996

The Honorable Loren Leman
Alaska State Legislature
State Capitol (MS 3100)
Juneau, Alaska 99801-1182

Dear Senator Leman:

I sincerely appreciated the opportunity to discuss with you last Friday, your concerns with the Northstar project. Your desire to insure that Alaska residents will benefit from the project and long-term opportunities for Alaskan contractors will be realized is commendable, and a desire I share as well.

I am writing this letter to further clarify VECO'S position regarding the Northstar project. We see this project as a real advancement for Alaskan contractors and Alaskan workers within the oil industry. On past projects, fifty percent (50%) of the craft labor has been performed in the lower 48 on all of the oil field facility projects. On GHX2 alone, this amounted to over three million man hours. On the Northstar project it is possible that one hundred percent (100%) of the craft labor will be performed in Alaska by Alaskan contractors employing available and capable Alaskans.

For years we have had to convince the oil companies that sea lift modules could be built competitively within the State of Alaska. With your support, the Northstar project will give us the opportunity to prove our position.

I am confident that the oil companies are able to make some of these marginal projects feasible by innovative approaches to the drilling, design, construction and operating philosophy of these developments.

It is important that legislation does not unduly inhibit that freedom



The Honorable Loren Leman
Page 2
21 April 1996

and flexibility. With the Northstar project, BP Exploration has committed to making this new opportunity a reality.

I have had a long relationship with BP and have always found them to be a trustworthy client. When they give their word, a contract is not needed! BP is a major player in the oil business throughout the world, and they have significant opportunities for investment in very attractive projects. Alaska is lucky to have such a partner to be in business with, and to help us realize our Alaskan potential for building our own infrastructure for modules utilizing our skilled labor, which will be advantageous in world market competition.

Your full support of this negotiated agreement will help to make this happen.

Sincerely,

A handwritten signature in cursive script that reads "Bill J. Allen".

Bill J. Allen
Chairman & CEO

COOK INLET REGION, INC.

April 22, 1996

VIA FAX: (907) 465-3810

Honorable Loren Leman
Chairman
Senate Resources Committee
State Capitol
Juneau, Alaska 99801-3810

Dear Senator Leman:

I am writing to you today as a follow up to my earlier testimony to the Committee and my conversations with you about Senate Bill 318. As you are aware, CIRI is heavily involved in the oil industry in Alaska through our own developments on the Kenai, as a working interest owner in Endicott, and through our three subsidiary companies, PEAK Oilfield Services, Construction Machinery, Inc. and Alaska Interstate Construction. So we benefit from more than our alliances and partnerships as a contractor on Alaska's North Slope.

It is our belief that SB 318, which would allow the development of Northstar, is a most vital piece of legislation. It will do more than just put hundreds of Alaskans to work and inject millions of private sector dollars into our economy. It will maintain flow in the Trans Alaska Pipeline. Clearly, the State must continue to support these smaller field developments or we will reach a point where it is uneconomic to transport oil through the pipeline. If the pipeline shuts down we can forget any future developments such as ANWR.

We believe the Executive Branch is properly empowered under the Constitution to negotiate deals within a general statutory framework established by the Legislature. And while the Legislative Branch may read into the record what it believes should be or should have been included in a contract, it is bad constitutional precedent and poor practical policy for the Legislature to get into the business of rewriting or re-negotiating contracts carefully negotiated by the Executive Branch.

I fully understand the role of the Legislature in our system of checks and balances and your duty to review what the Administration is proposing in terms of lease amendments. You have made it clear that -- had you negotiated the deal -- it would have been somewhat different. But this is the agreement that was hammered out between the State of Alaska and BP Exploration and should be the only agreement on the table.

Senator Leman
April 22, 1996
Page 2

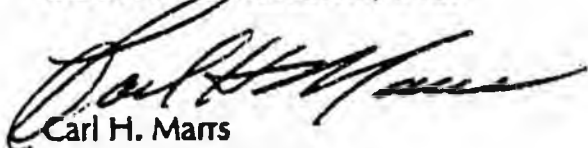
Cook Inlet Region, Inc. fully supports this negotiated agreement. For our part, we are satisfied that BP will do everything in its power to fulfill its commitments on local hire and local business participation in Northstar's development. We do not base this belief on misguided optimism, but on cold political reality. If, for any reason, BP does not live up to its commitments, they will find scarce support among Alaska businesses and public officials for any future development opportunities. Moreover, I am advised that there is a real danger, from a legal perspective, that this well-intentioned attempt to put more "teeth" into the Alaska hire and contracting provisions could amount to "throwing out the baby with the bath water." It also may substantially increase the chance that this entire piece of legislation will be ruled illegal or unconstitutional under state and federal law.

In summary, we believe BP means what they say and that the Northstar project is our best opportunity to forge a new standard for Alaskan's participation in oil development. It also sends the right message to other companies thinking about investing in Alaska. The legislature worked hard to pass HB 207 last year to send the message that Alaskans are willing to work with the industry on issues critical to the future development of Alaska's resources. This is one of those issues so let's — as Alaskans live up to the intent of HB 207 and pass SB 318 as recieved from the Administration.

Accordingly, on behalf of Cook Inlet Region, Inc., I strongly urge you to support SB 318 as it was introduced and keep this vital legislation moving forward. Thank you.

Sincerely,

COOK INLET REGION, INC.



Carl H. Marrs
President & CEO

CHM/dm
0028



Fax Transmittal Cover Page

Date: April 22, 1996

To: Honorable Loren Leman

Firm: Chairman, Senate Resources Committee

Fax Number: (907) 465-3810

City & State: Juneau, Alaska

From: **Brenda I. ta-Lee, Vice President, Human Resources**

ASRC Human Resources Department Fax Number: **(907) 852-9470**

Total number of pages, including cover page: 03 (Three)

If you do not receive all the pages, please call: **(907) 852-8633**

Fax Operator/Contact Person: **Julia Kaleak**

Original: Will Will Not **Be Mailed**

Comments: _____

URGENT - S.B.318

WE ARE TRANSMITTING FROM A MURATA F-75



April 22, 1996

Honorable Loren Leman
Chairman,
Senate Resources Committee
State Capital
Juneau, Alaska 99801-1182

VIA Fax: 907-465-3810

Dear Senator Leman:

Arctic Slope Regional Corporation (ASRC) owns several subsidiaries directly involved in the development of Alaska's oil resources. ASRC subsidiaries now rank as some of the largest multi-disciplined construction companies on the West Coast. They serve a diverse array of clients, including the oil and gas industry, government, mining, petroleum refineries and other private industries.

The economic health of Alaska's oil industry is very important to ASRC's overall well-being. That's why I'm writing you today about SB 318 - and to encourage you to give it speedy approval.

The agreement negotiated between the state and BP Exploration is a good deal for the state. One that maximizes the state's return, nurtures an exciting new business in Alaska and comes as close as the courts will allow to guarantee new jobs for Alaskans. It is also an agreement that requires all of us - BP, the state, and contractors - to partner together for the mutual benefit of all.

BP is willing to pay a multi-million-dollar premium to help us develop the expertise and infrastructure we need to build the much larger production modules Northstar will require. But the window of opportunity to develop the capabilities we need to build these large production modules is limited. Either we move now, or a non-Alaskan company will likely take over the market. Our subsidiary, Alaska Petroleum Contractors, has already made the large capital investment we need to turn a part-time fabrication business into full-time jobs for Alaskans. And we have a commitment from BP on Northstar that goes far beyond what any other oil company has offered to date.

We are, therefore, fully committed to Northstar's development and we believe BP is equally committed to honoring the terms of the agreement negotiated with the state. On behalf of Arctic Slope Regional Corporation, I strongly urge you to support SB 318 as it was introduced and to pass it from your committee.

Thank you.

Sincerely,

ARCTIC SLOPE REGIONAL CORPORATION

Jacob Adams
Jacob Adams, President





BP EXPLORATION

E. M. Luttrell
Vice President
Exploration, Alaska

BP Exploration (Alaska) Inc.
900 East Benson Boulevard
P.O. Box 196612
Anchorage, Alaska 99519-6612
(907) 564-4892

April 20, 1996

The Honorable Loren Leman, Chair
Senate Resources Committee
Alaska State Legislature
State Capitol
Juneau, AK 99801

Dear Senator Leman:

I appreciate the opportunity to comment further on the Senate Resources Committee Substitute for Senate Bill 318. For the reasons explained in my letter and testimony of April 18, 1996, BP will not reopen the negotiations of the agreement and cannot agree to the changes.

With respect to the 21-page findings of fact, BP believes the inclusion of such findings in the act itself is unprecedented. Although many portions of the findings are apparently quotations from testimony and evidence before the committee, we do not believe the findings are a complete or balanced reflection of this testimony and evidence. In addition, the findings describing the history of the leases and unitization are incomplete and seem largely irrelevant to the committee's decision. If the committee desires to make findings of fact such as those in CS 318, it seems more appropriate to include them in the committee record or in a separate committee report rather than in the act itself.

BP also requests that the effective date of the act not be delayed. There has been public testimony from at least one witness regarding a possible legal challenge to the legislation, and we would not want a challenge to be delayed due to a delayed effective date of the act.

Very truly yours,

A handwritten signature in black ink, appearing to be "E. M. Luttrell".

E. M. Luttrell
Vice President, Exploration and Development
BP Exploration (Alaska), Inc.

PETRO MARINE SERVICES

Petroleum Marketing to the Marine Industry

SB318

APR 17 1996

April 15, 1996

Senator Loren Leman
Room 113
State Capitol
Juneau, Alaska 99801-1182

Dear Senator Leman,

The Alaska Legislature is currently in the process of making a decision on the Northstar offshore oil field, located six miles north of Prudhoe Bay. According to BP Exploration (Alaska) Inc. officials, Northstar will yield about \$500 million in new government revenues and another \$500 million in direct spending in Alaska over the life of the project.

As a lifelong Alaskan and businessman, I can clearly see the benefits of this project. I consistently embrace and support projects that offer the opportunity to be a "win" for all parties. Northstar represents a creative -- and mutually beneficial -- approach to developing a field with marginal economics because of the 89-percent net profits requirements.

On the other hand, I recognize that in your position as a legislator, this may be a challenging decision. Northstar will break new ground for our traditional oil and gas policies. In any event, as I understand it, we are exchanging long-term risk for the short-term certainty of a 20-percent base royalty and the potential of another 7.5-percent supplemental royalty. While some will view this strategy as a "trade-off," from my perspective it is a symbol of a true partnering relationship between industry and the state.



P.O. Box 389 • Seward, Alaska 99664

Phone (907) 224-3190 • Fax (907) 224-3937

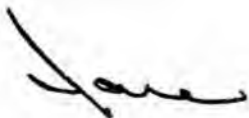
A HARBOR ENTERPRISES COMPANY

In addition, BP says that Northstar will directly create 500 construction jobs and 50 permanent jobs, as well as generate hundreds of indirect jobs. In my opinion, this is a substantial and significant step forward in positioning Alaska as an attractive state in which to conduct business.

At the present, I view the Alaska economy as being reasonably stable. While we are not experiencing dynamic growth, I have no overriding anxieties that we are facing a down cycle. If we are to maintain economic stability, I encourage the Legislature to continue to support the private sector in Alaska, which ultimately benefits all Alaskans. Accordingly, this letter is to respectfully request your support of the Northstar agreement as negotiated between BP and the Alaska Department of Natural Resources. Again, and for the record, I am squarely behind Northstar!

I appreciate your taking the time to consider my views.

Sincerely,



Dale R. Lindsey
President/Chief Executive Officer

PETRO MARINE SERVICES

Petroleum Marketing to the Marine Industry

STATE OF ALASKA

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

APR 22 1996

April 22, 1996

Honorable Loren Leman
Senator
Alaska State Legislature
Room 115 State Capitol
Juneau, Alaska 99801

Re: SB318 (Northstar Unit net profit
share reduction)

Dear Senator Leman:

You have requested our comments on the draft committee substitute to Senate Bill No. 318.

We recommend that the material set out beginning at page 1, line 5 through page 20, line 8 be deleted from the bill and placed in a separate committee report. The record speaks for itself, there is no need to select and insert excerpts of the record in the bill. It is sufficient that the committee investigate the facts and circumstances of the lease amendments and have a reasonable basis for the action it proposes. The technique of selecting excerpts from the record may be used by opponents of the transaction to argue that the committee placed too much, or not enough reliance on certain facts, when this was not the case. The committee will no doubt rely on the entire record in recommending a bill for passage by the Senate.

We believe that the insertion of an amended lease amendment in statute raises serious questions whether, in enacting this bill, the legislature would be violating the separation of powers doctrine implicit in the Alaska Constitution. The governor proposed a bill that would give the Department of Natural Resources the power to reduce a net profit share lease. The governor's version would also have the legislature ratify the amendments negotiated for the Northstar Unit. The draft committee substitute would enact a counteroffer to the leaseholder which differs from the agreement between the department and British Petroleum. The negotiation of lease agreements is an executive function, not a lawmaking function. Clearly the legislature may delineate the power that the department has when it acts in these matters. It is when the legislature attempts to negotiate on behalf of the state that the separation of powers doctrine has been violated.

TONY KNOWLES, 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) 451-2811
FAX: (907) 451-2846

P.O. BOX 110300-DIMOND COURT HOUSE
JUNEAU, ALASKA 99811-0300
PHONE: (907) 465-3600
FAX: (907) 465-6735

Hon. Loren Leman

April 22, 1996

Page 2

If the committee is determined to effect changes in the present lease amendment, it should consider redrafting the bill to set out limits on the power to reduce or change the net profits aspects of the North Star leases. If the legislature defines the power in a way that is inconsistent with the lease amendments presented, the parties must return to negotiations.

The lease provisions added in the committee substitute relating to local hire may present a legal defect that will lead to litigation. Protracted litigation may frustrate the purpose of the lease amendments. On page 28 lines 10 - 29, the provision appears to mandate resident hire on module fabrication projects. The provision also requires the lessee to ensure that all subcontractors practice local hire. These requirements appear to be similar to the local hire requirements that were struck down in Robison v. Francis, 713 P.2d 259 (Alaska 1986). For this reason, the committee is urged to recede from this proposed change to the lease agreement. It probably does not violate the United States or Alaska Constitutions to require a leaseholder to fabricate modules in Alaska.

Thank-you for the opportunity to comment on the draft committee substitute.

Very truly yours,

BRUCE M. BOTELHO
ATTORNEY GENERAL

By: 

James L. Baldwin
Assistant Attorney General

JLB:clh



BP EXPLORATION

E. M. Luttrell
Vice President
Exploration, Alaska

P.2/2

BP Exploration (Alaska) Inc.
900 East Benson Boulevard
P.O. Box 190612
Anchorage, Alaska 99519-0612
(907) 564-4892

April 18, 1996

Senator Loren Leman
Alaska State Legislature
State Capitol (MS 3100)
Juneau, Alaska 99801-1182

Subject: BP position on the CS for Senate Bill 318

Dear Senator Leman:

BP has reached a negotiated agreement with the State of Alaska to amend the Northstar unit leases. The Legislature has been asked to consider and ratify that agreement. Ratification will lead to the early development of Northstar to the mutual benefit of both Alaska and BP.

The CS (Committee Substitute) has altered the agreement, attempting to reopen the negotiation. All of the areas of the original agreement which have been amended in the CS version are areas which were carefully discussed and negotiated to arrive at a balanced agreement. Both we and the DNR have sought to explain to your committee the reason for these conclusions. BP will not reopen the negotiations and can not agree to the changes.

To be clear, BP and its contractors have heard the concern of the Legislature over local hire and we reaffirm our public commitment to maximize the job opportunities for Alaskans and Alaskan contractors represented by Northstar development.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric M. Luttrell', is written over a large, stylized scribble.

Eric M. Luttrell

EML/dd

cc: President Drue Pearce
Speaker Gail Phillips
Commissioner John Shively

April 15, 1996

To: Senator Loren Leman, Chair, Senate Resources Committee
From: Thomas Cook, 1848 Kalgin Street, Anchorage, Alaska 99504
(phone (907)333-1419; fax (907)338-9792)
Subject: SB318--Northstar Beaufort Sea Net Profit Share Leases

I respectfully offer the following comments to you and your committee in support of SB 318 that would amend the terms of certain leases overlying BP's Northstar Prospect by deleting the provisions for net profit shares to the state.

Let me begin by acknowledging that, as an oil and gas industry consultant, I sometimes work for various companies in the oil industry including BP Exploration. However, I assure you and your committee that my comments are those of a concerned citizen and are offered to you at my own initiative.

From June 1, 1978 until May 31, 1980, I served as Director of the Division of Minerals and Energy Management, Department of Natural Resources. It was during my period as Director that the State prepared for and conducted the 1979 Joint State/Federal Beaufort Sea Oil and Gas Lease Sale which resulted in the net profit share leases which are now at issue.

I became Director at the same time as the State's new oil and gas leasing statute took effect. With the passage of this new law, the Division faced a major task of developing regulations to implement the law and the various new bidding provisions provided for in the revised leasing statute. The Division also faced a major task implementing a leasing program under the new law. With these responsibilities before me, I realized that I should review the legislative history of the new leasing law. More importantly, I wanted to review the studies and analytical work that I assumed had been done by the Department of Natural Resources in support of the newly enacted law. When I requested copies of these studies which I presumed had been undertaken, I learned that none had been done, or at least none had been documented.

The only study I could lay my hands on was a consultant's report prepared for the Department by Mr. Mason Gaffney. The report recommended a variety of unorthodox bidding methods and leasing strategies without much analytical support and no citations as to where these policies had been used and with what

results. Based on my past experience and knowledge, I was very skeptical about the application of contingency bidding methods, "checker-board" leasing, and "two-stage" leasing and other unproven leasing techniques which Mr. Gaffney was recommending to the Department.

As Director, I was strongly opposed to contingency bidding and net profit share bidding in particular, for the following reasons:

1. Contingency bidding methods and net profit share bidding, as a type of contingency bidding, have the effect of shifting risk from the private sector to the public sector. Under contingency bidding and net profits bidding, the State accepts a promise (higher royalty, share of profits, or a work commitment) in lieu of cash up front (bonus bid) as a criterion for awarding a lease. Reward to the State then becomes largely a function of geologic risk (is oil present or not), and business risk (will future oil prices justify and support development). Industry is in a much better position to deal with these risks. It does so through joint bidding with partners, conducting exploration and development in many areas of the world, and counting on enough successful ventures to pay for the more numerous unsuccessful ventures. The State has no significant means of spreading or lessening risk other than to accept the highest competitive cash bid as a criterion for a lease award.

2. Net profit share bidding (and some other forms of contingency bidding) can lead to unrealistic or irresponsibly high bids. There are really no factors which practically constrain a contingency bid which is a promise costing nothing and bearing little in the way of obligations. Cash bonus bidding by its nature requires that a bidder carefully evaluate its bid in terms of available cash and its desire to aggressively proceed with exploration and development. History shows that tracts receiving high bonus bids receive timely exploration and expeditious development if exploration results in a commercial discovery.

3. Net profit share leases are likely to involve excessive administrative costs and disputes as to how the net profit due the State is to be calculated. Regardless of how tightly accounting and regulatory definitions are drawn, there will still be differences of opinion as to the allocation of costs and revenues, the treatment of depreciation, and questions of fair return on investment. It is quite possible or even likely that administrative costs and disputes leading to litigation would negate the worth of a net profit share to the State.

4. Net profit share leases necessarily cause the State to be involved in business and technical decisions which are best left the responsibility of the lessee. For example, if the State became concerned that the costs of development, however necessary and prudent for a safe operation, were too high, it might pressure the lessee to cut corners and undertake less than prudent development to cut costs and thus increase profits.

These were my primary concerns in opposing the use of net profit share leasing in the 1979 Beaufort Sea Lease Sale. With this background in mind, I urge the Legislature to delete the net profit share provisions from the Northstar leases.

In choosing net profit share as the bid variable in 1979, the State chose to forgo hundreds of millions of dollars in lease bonuses which would have been forthcoming under the proven system of cash bonus bidding. The opportunity for large cash bonuses has been lost because times have changed. The late 1970's were times of extremely high oil prices. State and industry experts alike shared a general view that oil prices would remain high and many believed oil prices would increase in the future. The outlook now is considerably more sober. The state cannot recapture the opportunity it lost in 1979 by canceling and offering the leases at another sale.

The best course of action for the State is to delete the net profit share provisions and allow BP Exploration to proceed with development. This will lead to real benefits in terms of royalty payments and taxes to the State, jobs and economic opportunities for contractors and businesses across the state.

The simple fact that the Northstar leases have remained undeveloped by the original lessees for over fifteen years --in spite of promising discoveries--is ample proof that the original lessees found development to be uneconomic under net profit share obligations averaging 90 percent.

The Northstar leases are now owned by BP Exploration, a company with a demonstrated commitment to responsible and diligent development of Alaska's oil and gas resources. The State Legislature now has the opportunity to undo a past mistake in choosing net profit share lease terms by deleting the onerous and uneconomic net profit requirements. To do otherwise would be a ratification of a costly mistake and another decision to forgo the development of Northstar with its many benefits to the State and its citizens.

Thank you for the opportunity to comment on this important legislation.

Sen. Loren Leman,

4-20-96

First of all I want to compliment you on your handling of the Northstar issue.

I also want to pass on a couple thoughts/ideas to you.

In this deal with BP can we establish a review board that looks at this every year to see if both parties are living up to their end of the deal?

And on this review board could we have a couple BP north slope employees on it.

Also give this review board the power to cancel the agreement or at least halt it until agreements are met.

Keep up the good work

Mark A. Niew

p.s. We had a rally in front of the BP building on the 17th, news came out but didn't give us any air time. But we had a lot of support from cars driving by, honking their horns and giving the "thumbs up" sign!

APR 19 1996

April 16, 1996

Dear Senator Leman:

I'm very disappointed not to have heard from you regarding my concerns about BP's request for royalty and tax relief on their proposed Northstar development. I must remind you that the oil BP is proposing to develop belongs to the CITIZENS of the State of Alaska. Any deals or concessions must be for the long-term benefit of our State.

To show you where BP is putting some of its money, please read the enclosed news release. There is a service available through BP that provides current events affecting the oil production, chemical, and refining industries. As you can see, BP's CEOs both present and past, are receiving very handsome bonuses. The attached article is receiving wide circulation on the Slope at present.

We along with the present contract employees, are very concerned about BP's current and proposed job cuts in its Prudhoe Bay unit. These cuts will more than offset any gains by BP's proposed added jobs at Northstar. Their press release and other public statements contains too many "weasel clauses".

They haven't shown to my satisfaction their commitment to build, hire, or buy Alaskan goods and services. Fairmont has, since my last letter to you, even transferred their buyers to Utah. It's obvious to me, and should be to you, that you don't move your buyers to Utah if you intend to buy Alaskan good.

Again, I wish BP success, but Alaska still provides almost half their world oil production, and I see no need to "GIVE AWAY THE FARM."

BP has figuratively "spit" on OUR written contract, so I'm very apprehensive about any "gentlemen's agreements" between Alaska and BP.

I've been told by a few of your colleagues that the State has no business telling BP how to manage its affairs. However, they are the ones approaching US, wanting to re negotiate something they previously agreed to.

Also, they provide us with "Gap Rap" information regarding the State budget, and the need to cut it.

Please "jawbone" BP into dealing openly and honestly with its employees and partners, the State of Alaska, and its citizens.

Sincerely,

William F. Bocast

William F. Bocast

P.O. Box 520626

Big Lake, AK 99652

FROM: Daily Mirror 03/19

BP bosses strike gold

The top brass at oil giant BP have struck black gold.

The company yesterday revealed 109 senior managers will be given more than six million shares.

The hand-out - worth nearly £34 million last night - is for helping profits gush in over the past five years.

But they could be worth even more by the time they get them in five years.

Shares allocated to seven directors under the scheme were worth £8.5 million last night.

New chief executive John Browne is the biggest winner with a £1.75 million windfall. *£2,800,000*

FROM: Financial Times 03/19

Former Chairman Gains from BP's £10.5m. Shares Pay-Out

Nine present and former directors of British Petroleum are to share in an award of £10.5m of shares under the company's long-term performance plan.

They include Mr. Robert Horton, the former chairman ousted in a boardroom coup in 1992, a year after the plan was initiated. Mr. Horton, now chairman of Railtrack, will get shares worth £227,00 at yesterday's price. *£363,200*

According to the company's annual report released yesterday, Mr. Horton "was able to initiate certain changes ... which have benefited the performance of the company." BP said these changes included reorganisation of the company's headquarters in 1990 which had boosted efficiency.

Other former executives who qualified for the award were Mr. Norton, managing director until last year, who gets *Hugh* £1.78m, and Sir David Simon, now chairman, who received £880,00 worth of shares. The largest recipients among current directors are Mr. John Browne, chief executive, who gets shares worth £1.73m, Mr. Steve Ahearn, finance director (£1.66m), Mr. Bryan Sanderson, head of chemicals (£1.65m) and Mr. Russel Seal, head of human resources (£1.17m).

Other former executives who qualified were Mr. Hugh Norton, managing director until last year, who gets £1.75m, and Sir David Simon, now chairman, who receives shares worth £860,000.

The largest recipients among current directors are Mr. John Browne, chief executive, who gets shares worth £1.7m, Mr. Steve Aheame, the finance director (£1.6m), Mr. Bryan Sanderson, head of chemicals (£1.6m) and Mr. Russell Seal, head of human resources (£1.1m).

The long term performance plan was introduced in 1991 to replace share options.

Share are awarded after five years based on BP's returns compared with other leading oil groups. Mr. Peter Sutherland, chairman of the remuneration committee, said BP had outperformed the stock market over the period, producing a return of 15 per cent a year. Earnings had increased by 37 per cent, and return on capital went up from 9 to 14 per cent. The awards were based on a 60 per cent achievement of the targets laid down in 1991.

Newsweek

February 26, 1996 \$2.95

CORPORATE



Robert B. Palmer, Digital
Cut 20,000 jobs



Albert J. Dunlap, Scott
Cut 11,000 jobs



Robert E. Allen, AT&T
Cut 10,000 jobs



Louis V. Gerstner Jr., IBM
Cut 60,000 jobs

KILLERS

Wall Street Loves Layoffs.
But the Public Is Scared
as Hell. Is There a Better
Way? BY ALAN SLOAN

STANDARD DIME GREENS TO DS OFORMA
RENGTH AFTER

can no longer count on staying with the likes of IBM forever. But nothing has taken the place of the benevolent Big Daddy employer, and that scares the pants off us. You can practically smell the fear and anger in white-collar America, because no one in CEO-land seems to care. Where will I find another job if I get downsized? Stop whining, unemployment statistics have barely budged despite huge white-collar firings. Will my boss ruin my life to make another cent of profit on her stock options? Cheer up, you're serving the greater good by being blown away by what economist Joseph Schumpeter christened "the gale of creative destruction." Except for oddballs like the chief economist at Morgan Stanley (who has warned for years that there would be a backlash) and the president of United Technologies (who recently unveiled a nifty program to help UT workers re-educate themselves for their next jobs), Wall Street and Big Business have been in perfect harmony about how in-your-face capitalism is making America great.

Wits at AT&T Corp. quip that chairman Robert Allen will soon fire everyone but himself, and AT&T will stand for Allen & Two Temps

are debatable, though Dunlap doesn't agree. Nor is it easy to get a handle on how many firings there actually are. Layoff numbers from the Chicago outplacement firm of Challenger, Gray & Christmas, an oft-cited source, are full of holes, as the firm readily admits. They include only publicly announced cuts. I'm not sure what federal job-cut numbers actually measure, and you can argue endlessly about how to interpret figures about workers' salaries and output. What really matters is that although unemployment is relatively low and the economy is still cranking out new jobs, millions of Americans believe they're being screwed by corporate America and Wall Street.

It's unfair to blame every job cut in America on Big Business and Wall Street. The world is changing, and no matter how big and rich a company is, it has to adapt or die. (Even NEWSWEEK hasn't been immune to job-cutting.) But Wall Street and Big Business have made a bad problem worse by being greedheads. Instead of keeping payrolls lean and helping employees to prepare for their next careers, lots of CEOs have messed up big time. They let their payrolls get bloated. Then to recoup, they offer up employees as human sacrifices to Mammon, god of Wall Street, hoping to get their stock price up. When the price rises, it's like Wall Street spitting on the victims' bodies. And the CEO gets a raise. How many CEOs of big, downsizing companies sacrificed some of their pay and perks to encourage a sense of community? Did they apologize publicly to the people they fired? Did they take any personal responsibility for mistakes that helped cause the problems they're solving with layoffs? No way, that's not macho.

WELL, NOW IT MAY BE BACKLASH TIME. SUDDENLY, white-collar woes are a hot issue in the 1996 presidential campaign. Al Dunlap of Scott Paper, the loudest spokesman for corporate hardball (page 48), duked it out with Labor Secretary Robert Reich on "Nightline." Bob Dole is making antibusiness noises. And Big Media from The New York Times to The Wall Street Journal attribute Pat Buchanan's strong showing in the Iowa caucuses to his attacks on business.

We're not going to argue about whether today's mass firings make economic sense. Companies like IBM and Sears and GM had to downsize or die. Other cuts—like some of those at Scott Paper—

Of course, no matter how sensitive or smart a CEO may be, there are tides that you just can't swim against. Take banking. Thanks to money-market mutual funds, national banking, teller machines and spiffy computers, many banks, bank branches and thousands of

Louis Gerstner
CEO

IBM

Salary: \$2,625,000

July 1993

60,000 layoffs



John McDonnell
Chairman, Former CEO

McDonnell Douglas

Salary: \$775,000

July 1990

17,000 layoffs



Ronald Allen
CEO

Delta Air Lines

Salary: \$175,000

April 1991

15,000 layoffs



Robert Stempel
Former CEO
General Motors
Salary: \$1,000,000
December 1991:
74,000 layoffs

Edward Brennan
Former CEO
Sears, Roebuck & Co.
Salary: \$1,075,000
January 1993:
50,000 layoffs



Robert Palmer
CEO
Digital Equipment
Salary: \$900,016
May 1991:
20,000 layoffs



bank jobs will vanish in the next few years. Electric utilities used to be great lifetime employers, too. They were regulated monopolies allowed to pass costs on to their customers. But regulators have started to let companies invade each other's turf. The result: utilities have started to combine, and will soon be zapping workers to get costs down. Ditto for local phone companies, thanks to the recent Telecommunications Act.

LOOK, YOU CAN'T STOP ADVANCES IN COMPUTERS AND communications and transportation. They're making national markets into global markets. Foreign companies whose names you can't even pronounce can take away your customers and kill you. Mistakes show up quickly. Product cycles are shorter than ever. Look at how IBM and Digital Equipment, once the world's two biggest computer makers, seemed to add the word troubled to their names almost overnight. (They both seem to be recovering.) A marvelous company like Motorola can have its stock smashed to smithereens, if its profits come in a hair or two below expectations. Indeed, one reason that chief executives are meaner and greedier than they used to be is the 1980s: no company was safe from raiders if its stock price was depressed. If you didn't unload your losers and fire "surplus" workers, a takeover troll would buy your company and fire everybody.

Yet while layoffs have traditionally been part of blue-collar life, the '90s is the first time white-collar workers have been slaughtered en masse. That helps account for the uproar. After all, agenda setters like politicians and we media-elite types live in a white-collar universe. Anyway, you could see why GM was firing 74,000 workers in 1991 or Sears was firing 50,000 two years later. Both companies were in desperate trouble, and

their survival was at stake. And the chairmen of GM and Sears were forced to walk the plank.

Today's layoffs are different. The symbol: AT&T. When AT&T, formerly the kindly Ma Bell, announced in January that it would fire 40,000 people as part of its breakup into three companies, the stock market went nuts. AT&T shares roared upward. Bob Allen, who I think wants to do the right thing, symbolized the clueless CEO when he talked to NEWSWEEK last month. He said he felt bad about firing people but saw no point in giving up some of his pay or perks as a shared sacrifice with the workers. And, he said, he saw no reason to apologize: "I wouldn't see any value of going on TV and crying." Allen, who had been ridiculed on Wall Street for AT&T's disastrous \$7.5 billion hostile takeover of computer maker NCR in 1991, made more than \$5 million when the value of his stock and options soared after the layoffs were announced. (He declined to talk last week.)

For another classic example of how CEOs seem to have forgotten how to deal with people, consider the recent combination of two giant New York City banks, Chase Manhattan and Chemical. Chase was pressured by Michael Price of the Mutual Series funds (whose stockholders include me) to get its stock price up and sold out to Chemical. The attraction to Chemical: the Chase name, which it's keeping, and its ability to cut 12,000 jobs from the combined banks. Those jobs would have probably vanished even without a takeover, but in a slower, more controlled way. Thousands of little people were fired to save money, while the new Chase kept all 36 outside directors, who get fat fees and dandy retirement packages.

And here's another company with no clue as to how things look to the outside world: troubled Apple Computer. Apple recently installed Gil-

The world is changing, and no matter how rich a company is, it has to adapt or die. But Wall St. and Big Business have made it worse by being greedheads.



Michael Miles
Former CEO
Philip Morris
Salary: \$1,000,000
November 1993:
14,000 layoffs



Frank Stroncz
CEO
Boeing
Salary: \$1,200,000
February 1993:
28,000 layoffs



William Johnson
Former CEO
Xerox
Salary: \$800,000
January 1993:
33,800 layoffs

bert Amelio as CEO. A company firing workers and eliminating its dividend to conserve cash is paying Amelio \$2.5 million a year of salary and bonus. At a minimum. Hello? For heaven's sake, Amelio was already on Apple's board; that makes him at least partly responsible for Apple's problems. How can you lay megabucks on him while paring workers to conserve cash? Only if you don't care about what anybody thinks. Consider Amelio's answer last week when NEWSWEEK asked him to justify his pay package: "It's a market-determined figure." Contrast that to Lee Iacocca's taking the helm of Chrysler for a dollar a year in 1978. Iacocca, who got fat stock options in addition to his dollar, has been no prize in recent years, as greed and ego overwhelmed his good sense. But he was an inspiration when Chrysler was croaking, and it really mattered.

Rather than fire workers to save a few bucks, Scherer Brothers Lumber stopped buying sports tickets and fresh flowers for receptionists' desks.

conglomerate that has cut 23,000 jobs since 1990. Last December, UT unveiled a new, expensive plan to help workers get re-educated. President George David says the United States can't stop production jobs from migrating overseas, so companies should help people upgrade their education before it's too late. "We load education into our first 21 years of life, and then think that we can leave the classroom essentially forever," he said. UT now gives employees time off to attend classes, pays for tuition and books, and will give employees who complete their studies 50 shares of UT stock, currently worth about \$5,200. You can go to nursing school or get a degree in creative writing, none of which has anything to do with UT's businesses. David hopes that 20 percent of his employees will use the plan. That would gradually increase the company's outlay to about \$50 million a year from the current \$11 million. "We're not softhearted," said David, whose face turned red when I suggested he sympathized with downsized workers. "It's in our interest to have an educated work force."

IACOCCA'S GREAT GESTURE WAS LONG AGO AND FAR AWAY. Now let's look at the behavior that convinced Stephan Roach, the chief economist at Morgan Stanley, that business is carving itself a disproportionate piece of a pie that's supposed to be shared with workers. Roach is hardly anti-business—he loved downsizing in the early 1990s. Yet a few years ago he realized something was wrong: workers' output was rising, but their incomes weren't keeping pace. "This isn't the way economics is supposed to work," he says. "It contradicted everything I was taught to believe." When he warned companies to do something before a political backlash struck, they giggled on Wall Street. I don't think they're giggling now.

There are no surefire solutions to these problems. But some companies are enlightened enough to know that helping their workers also helps them. Take United Technologies, a hard-boiled

Then there is John Grundhofer, chairman of First Bank System of Minneapolis, which recently collected a \$200 million fee for abandoning its proposed takeover of First Interstate Bank. With no fanfare, Grundhofer—who fired 2,000 employees when he joined the bank six years ago—recently gave each employee a \$750 bonus, about \$11 million in all. He wanted to show his appreciation to employees for having created a bank strong enough to bid for a company bigger than itself.

For decency, it's hard to top Malden Mills, which became famous last year when it kept 1,400 workers on the payroll after its plant in Lawrence, Mass., burned down. "What right do I have to destroy a major city just to get a few more dollars in the bank that I won't spend before I die?" said mill owner Aaron Feuerstein.

"The money would only go to my children and spoil them." Or take a company almost no one's ever heard of: Scherer Brothers Lumber Co., a building-supply company in suburban Minneapolis. President Mike Scherer said that officers don't draw bonuses until the company has given a 15 percent profit-sharing contribution to every eligible employee. And rather than firing workers to save a few bucks, the company eliminated fresh flowers for receptionists' desks, cut the top officers' pay temporarily by 25 percent and stopped buying professional sports tickets. "When you buy professional tickets, you're subsidizing people making tons more than I am, and they're still not happy," he says. "I'm not going to lay off our employees to subsidize them."

There is no magic bullet that will make the problem go away. Even eliminating short-term thinking isn't the answer. Proof: German and Japanese companies specialize in long-term thinking, and

they're more messed up than we are. The federal government can't save us. Can you see the Feds drawing up rules to define a good-jobs company in order to give it tax breaks? And we can't go back to the days of the 1950s and '60s, when big companies offered lifetime employment. Any company that tries that these days will be like an elephant in a piranha pond.

You solve this problem one company at a time, with innovative programs like United Technologies', decent behavior like Feuerstein's and Scherer's, intelligent and relatively cheap gestures like Grundhofer's. Let business act as if it cares about employees. Who knows? Business may even rediscover what many executives once knew but seem to have forgotten: that doing the right thing for your people is often the best thing you can do for your business.

With ANNE UNDERWOOD in New York, JOHN MCCORMICK in Chicago and DEBORAH BRANSCOMBE in Emeryville, Calif.

Villains? Heck No. We're Like Doctors.

Job cuts hurt, says Al Dunlap, but it keeps firms alive

ALBERT DUNLAP HAS BECOME the poster boy for the folks who say that CEOs have gone too far. The 58-year-old former CEO of Scott Paper, known to detractors as "Chain Saw Al," cut 11,000 jobs in 1994. After merging the company with Kimberly-Clark, he walked away with about \$100 million in salary, stock profits and other perks. Dunlap previously downsized seven other companies, including Diamond International and Lily-Tulip. When *NEWSWEEK* asked more than 50 CEOs of large American companies to discuss corporate restructuring, only Dunlap was willing to talk. Here's what he had to say:

When journalists and politicians spout off about corporate downsizing, it's the Al Dunlaps of the world who tend to get the blame. We're painted as villains; but we're not. We're more like doctors. We know it's painful to operate, but it's the only way to keep the patient from dying. Take the restructuring at Scott. We had to fire 35 percent of the work force. It was a difficult task. Coming from a working-class family (my father was a union steward), I know what

it's like when someone in the family loses a job. But while we had to cut some jobs, we were able to give 65 percent of the work force a more secure future than they might have otherwise had. And Scott's stockholders came out \$6.5 billion to the better.

So why are shareholders so important to workers? By doing a good job for them, we're encouraging them to invest, to build new plants and create new products. At the end of the day, that will mean more and better jobs down the road. And that's the point people need to remember: the only way corporate America is going to do right by its workers is to compete. And in order to compete, companies need to become efficient. That means if you have workers for whom you don't have a real job, you can't keep them on the payroll.

Let me put this in some historical perspective. In the '70s America lost its position as a leader in global business. Look at the industries we once had



that barely exist: shoes, machine tools and consumer electronics. Don't blame today's executives who are having to face up to the tough decisions—blame the executives who created bloated corporations that are noncompetitive. People are always criticizing companies that bring in record profits and then announce layoffs. What they don't realize is that if an organization doesn't make record profits, it doesn't have the money to invest in new plants and new technologies.

That's not to say that I don't

believe in CEOs' being accountable to their workers. I think a CEO has an obligation to communicate with workers and prepare them for the inevitable. Before the restructuring at Scott, I personally went around the world and talked to people on the shop floors. One of the things we told them was that we weren't keeping the

elitist tools of corporate America at the expense of workers. Our biggest cutback was to sell the 750,000-square-foot corporate headquarters and downsize 71 percent of the corporate staff. At one plant, the workers actually applauded me. People are pretty intelligent if you tell them what's going on and explain why you're doing what you're doing.

On the other hand, the politicians don't seem to be getting the message. They pander

to the public and polarize people. And they try to tell American industry how to conduct its business. The job of industry is to become competitive—not to be a social experiment. God help us if we pass legislation to make American companies less productive and compromise our global competitiveness. Then it won't be a case of a relatively small number of people losing their jobs. It will be huge numbers losing their jobs—and the death of the American free-enterprise system as we know it.

FACSIMILE COVER PAGE

To: Sen Loren Leman
From: Brad Humelsine
Pages (including cover): 1

Time: 09:55:42
Date: 04/19/96

Please find the following letter to BP. It was written in response to the direct mailing they made regarding Northstar.

This is the kind of sweet deal Alaska can do without.

Thank you,

Brad

James B. Humelsine
2553 LaHonda Drive
Anchorage, Alaska 99517
Phone (907) 276-7826

April 19, 1996

John C. Morgan President, Alaska
BP Exploration (Alaska) Inc.
900 East Benson Blvd.
P.O. Box 196612
Anchorage, Alaska 99519

Dear Mr. Morgan:

I am responding to the direct mailing you sent me regarding the Northstar oil field.

As a strong supporter of the oil industry in Alaska, but I am very disappointed in BP and its' handling of the Northstar affair. Your company purchased the field knowing full well, what the former owner had bid on the tracts. You also knew as the new owner would be bound by the same agreement. Since this tract was awarded by the competitive bid process, It should only be changed through the same bid process.

BP must feel they much to gain from this purchase and subsequent renegotiation, because in my 17 years in Alaska I have never seen such a concerted effort from an oil company to reopen a contract. In your letter you call this field "relatively small", however your PR effort is relatively large. You have spent a significant amount of money on advertising and other public relations efforts relating only to this field. Historically the themes of your advertising and PR campaigns have been the "good neighbor" or "look at we do for you Mr/ Mrs Alaskan", recently you have used increasingly more hard line themes such as "We are Alaska's biggest tax payer". But never before this have you said call you legislator and tell them "don't tinker with this deal we negotiated with the Governor". I closely follow the Ad campaigns of yours and other companies, I have witnessed your increasingly aggressive themes, and I do not approve of them, period. This another example of the bully attitude your company is pushing.

Sorry, Mr Morgan I am too smart to fall for such a ploy.

If this contract were to be successfully renegotiated, it would set a precedent that I am sure you would be happy to use many times in the future. I think this is wrong for Alaska, and should be stopped now.

Thank you for taking the time to read my response.

Respectfully,

Brad Humelsine

CC:

Rep. Cynthia Toohey

Sen Loren Leman

Gov. Tony Knowles



Executive Office
Mikera Center
Washington, PA 15301
412-223-2300

D. M. CHURCH
Director
Purchasing and Materials Management

April 10, 1996

Dear Supplier,

Effective May 1, 1996, Fairmont Supply Company will relocate and centralize its Price, Utah Western Purchasing functions into our Corporate Purchasing and Materials Management Department out of Washington, Pennsylvania.

All future correspondence should be forwarded to the following address:

Fairmont Supply Company
P. O. Box 501
Washington, PA 15301
Attn: Purchasing and Materials Management

Phone No.: 412-223-2200
Hours: 8:00 a.m. - 5:00 p.m. E.S.T.
Monday - Friday

Invoicing will remain as before.

Please update your files accordingly and notify the appropriate personnel of these changes at your company. If you have any questions or have any concerns, please contact Mr. Carl Grebner, Manager - Commodity Purchases.

Thank you,

D. M. Church
Director
Purchasing and Materials Management

Question to Alaskan Legislators
Is this where you intended for BP
Exploration to do their business?
Do we now go to Pennsylvania
to sell to the north slope oilfields?