

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILES 8672

2491 SCOMM 107: HOUSE SPEC. COMM. ECONOMIC DEVELOPMENT, 1997-98

of each year, but in no event later than 60 days after such date, a report (the "Reserve Report") in form and substance satisfactory to the Majority Lenders, and in the case of the December 31 Reserve Report, prepared by the engineering staff of the Company and audited by Netherland, Sewell & Associates or other independent petroleum consultant(s) acceptable to the Majority Lenders (the previous acceptability of an independent petroleum consultant satisfactory to the Majority Lenders shall have no bearing on such consultant's present or future acceptability), which Reserve Report shall evaluate the Hydrocarbon reserves included in the Mortgaged Property as of each such date and which shall, together with any other information reasonably requested by any Lender, set forth the total Proved Hydrocarbon reserves by accepted and customary reserve category attributable to such Mortgaged Property, together with a projection of the rate of production and future net income with respect thereto as of each such date. The June 30 Reserve Report shall be an unaudited Reserve Report prepared by the engineering staff of the Company and shall update the most recent Reserve Report. Notwithstanding the foregoing, (i) if the Company or any of its Subsidiaries acquires additional Oil and Gas Properties that, in the determination of the Majority Lenders, materially affects

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the E&P Borrowing Base, then the Majority Lenders may require that an initial Reserve Report relating to such newly acquired Oil and Gas Properties be prepared by Netherland, Sewell & Associates or other independent petroleum consultants acceptable to the Majority Lenders, to be delivered to the Lenders concurrently with the next required Reserve Report and (ii) if there is a material adverse effect on Tesoro LP because of a change in the value of the Hydrocarbon reserves included in the determination of the E&P Borrowing Base (other than solely as the result of a change in the price of natural gas), then the Majority Lenders may require that a Reserve Report relating to all of the Oil and Gas Properties included in the determination of the E&P Borrowing Base be prepared by Netherland, Sewell & Associates or other independent petroleum consultants acceptable to the Majority Lenders, to be delivered within 60 days after the request therefor by the Administrative Agent on behalf of the Majority Lenders."

Section 2.03 Amendments to Article VI.

(a) Section 6.05(n) of the Credit Agreement is hereby amended in its entirety to read as follows:

"(n) Indebtedness, not to exceed \$18,000,000 in the aggregate, incurred by Tesoro Northshore or Tesoro Alaska, to be used for (i) the purchase (in fee or leasehold), construction, and/or upgrading of retail outlet stores or (ii) modifications to the hydrocracker located at the Kenai

Refinery, subject, however, to the execution of an intercreditor agreement satisfactory in form and substance to the Administrative Agent and Documentation Agent."

(b) Section 6.06(p) of the Credit Agreement is hereby amended in its entirety to read as follows:

"(p) Liens securing up to \$18,000,000 of Indebtedness permitted by Section 6.05(n);"

ARTICLE III. CONDITIONS

The enforceability of this Second Amendment against the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders is subject to the satisfaction of the following conditions precedent:

Section 3.01 Loan Documents. The Administrative Agent shall have received multiple original counterparts, as requested by the Administrative Agent, of this Second Amendment executed and delivered by a duly authorized officer of the Company, each of the Guarantors, the Administrative Agent, the Documentation Agent, each Issuing Bank and each Lender, as applicable;

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Section 3.02 Corporate Proceedings of Loan Parties. The Administrative Agent shall have received multiple copies, as requested by the Administrative Agent, of the resolutions, in form and substance reasonably satisfactory to the Administrative Agent, of the Boards of Directors of the Company and the Guarantors, authorizing the execution, delivery and performance of this Second Amendment, each such copy being attached to an original certificate of the Secretary or an Assistant Secretary of the Company or the Guarantors, as applicable, dated as of the Effective Date, certifying (i) that the resolutions attached thereto are true, correct and complete copies of resolutions duly adopted by written consents or at meetings of the Boards of Directors, (ii) that such resolutions constitute all resolutions adopted with respect to the transactions contemplated hereby, (iii) that such resolutions have not been amended, modified, revoked or rescinded as of the Effective Date, (iv) that the respective articles of incorporation and bylaws of the Company and the Guarantors have not been amended or otherwise modified since the effective date of the Credit Agreement, except pursuant to any amendments attached thereto, and (v) as to the incumbency and signature of the officers of the Company or the Guarantors, as applicable, executing this Second Amendment.

Section 3.03 Representations and Warranties. Except as affected by the transactions contemplated in the Credit Agreement and this Second Amendment, each of the representations and warranties made by the Company and the

Guarantors in or pursuant to the Financing Documents, including the Credit Agreement, shall be true and correct in all material respects as of the Effective Date, as if made on and as of such date.

Section 3.04 No Default. No Default or Event of Default shall have occurred and be continuing as of the Effective Date.

Section 3.05 Security Instruments. All of the Security Instruments (subject to any partial releases thereof) shall be in full force and effect and provide to the Administrative Agent the security intended thereby to secure the Indebtedness.

Section 3.06 Other Instruments or Documents. The Administrative Agent or any Lender or counsel to the Administrative Agent shall receive such other instruments or documents as they may reasonably request.

ARTICLE IV. MISCELLANEOUS

Section 4.01 Adoption, Ratification and Confirmation of Credit Agreement. Each of the Company, the Guarantors, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders does hereby adopt, ratify and confirm the Credit Agreement, as amended hereby, and acknowledges and agrees that the Credit Agreement, as amended hereby, is and remains in full force and effect.

Section 4.02 Ratification and Affirmation of Guaranty. Each of the Guarantors hereby expressly (i) acknowledges the terms of this Second Amendment, (ii) ratifies and affirms its obligations under the Second Amended and Restated Guaranty Agreement dated as of

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January 28, 1997, in favor of the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders, as amended, supplemented or otherwise modified ("Guaranty Agreement"), (iii) acknowledges, renews and extends its continued liability under the Guaranty Agreement and agrees that such Guaranty Agreement remains in full force and effect; and (iv) guarantees to the Administrative Agent, the Documentation Agent, each Issuing Bank and each Lender to promptly pay when due all amounts owing or to be owing by it under the Guaranty Agreement pursuant to the terms and conditions thereof.

Section 4.03 Successors and Assigns. This Second Amendment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns permitted pursuant to the Credit Agreement.

Section 4.04 Counterparts. This Second Amendment may be executed by one or more of the parties hereto in any number of separate counterparts, and all of such counterparts taken together shall be deemed to constitute one and the same

instrument and shall be enforceable as of the Effective Date upon the execution of one or more counterparts hereof by the Company, the Guarantors, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders. In this regard, each of the parties hereto acknowledges that a counterpart of this Second Amendment containing a set of counterpart execution pages reflecting the execution of each party hereto shall be sufficient to reflect the execution of this Second Amendment by each necessary party hereto and shall constitute one instrument.

Section 4.05 Number and Gender. Whenever the context requires, reference herein made to the single number shall be understood to include the plural; and likewise, the plural shall be understood to include the singular. Words denoting sex shall be construed to include the masculine, feminine and neuter, when such construction is appropriate; and specific enumeration shall not exclude the general but shall be construed as cumulative. Definitions of terms defined in the singular or plural shall be equally applicable to the plural or singular, as the case may be, unless otherwise indicated.

Section 4.06 Entire Agreement. This Second Amendment constitutes the entire agreement among the parties hereto with respect to the subject hereof. All prior understandings, statements and agreements, whether written or oral, relating to the subject hereof are superseded by this Second Amendment.

Section 4.07 Invalidity. In the event that any one or more of the provisions contained in this Second Amendment shall for any reason be held invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision of this Second Amendment.

Section 4.08 Titles of Articles, Sections and Subsections. All titles or headings to Articles, Sections, subsections or other divisions of this Second Amendment or the exhibits hereto, if any, are only for the convenience of the parties and shall not be construed to have any effect or meaning with

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respect to the other content of such Articles, Sections, subsections, other divisions or exhibits, such other content being controlling as the agreement among the parties hereto.

Section 4.09 Governing Law. This Second Amendment and the rights and obligations of the parties hereunder and under the Credit Agreement shall be governed by and construed in accordance with the laws of the State of Texas and the United States of America.

THIS SECOND AMENDMENT, THE CREDIT AGREEMENT, AS AMENDED AND SUPPLEMENTED HEREBY, THE NOTES, AND THE OTHER FINANCING DOCUMENTS CONSTITUTE A WRITTEN LOAN AGREEMENT AND REPRESENT THE FINAL

AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES.

THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES.

[SIGNATURES BEGIN NEXT PAGE]

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IN WITNESS WHEREOF, the parties hereto have caused this Second Amendment to be duly executed and delivered by their proper and duly authorized officers as of the Effective Date.

COMPANY:

TESORO PETROLEUM CORPORATION

By: /s/ G. A. Wright
Name: G. A. Wright
Title: Vice President and Treasurer

ADMINISTRATIVE AGENT,
ISSUING BANK AND LENDER:

BANQUE PARIBAS, individually, as an Issuing
Bank and as Administrative Agent

By: /s/ B. Malone
Name: Brian Malone
Title: Vice President

By: /s/ Larry Robinson
Name: Larry Robinson
Title: Vice President

DOCUMENTATION AGENT,
ISSUING BANK AND LENDER:

THE BANK OF NOVA SCOTIA

By: /s/ F.C.H. Ashby
Name: F.C.H. Ashby
Title: Senior Manager
Loan Operations

CORRECTION

**THE FOLLOWING DOCUMENT(S)
HAVE BEEN REFILMED TO
ASSURE LEGIBILITY OR PAGINATION**



Rev. 6/98

Central Microfilm Services
Department of Education
State of Alaska

AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES.

THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES.

[SIGNATURES BEGIN NEXT PAGE]

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IN WITNESS WHEREOF, the parties hereto have caused this Second Amendment to be duly executed and delivered by their proper and duly authorized officers as of the Effective Date.

COMPANY: TESORO PETROLEUM CORPORATION

By: /s/ G. A. Wright
Name: G. A. Wright
Title: Vice President and Treasurer

ADMINISTRATIVE AGENT,
ISSUING BANK AND LENDER: BANQUE PARIBAS, individually, as an Issuing Bank and as Administrative Agent

By: /s/ B. Malone
Name: Brian Malone
Title: Vice President

By: /s/ Larry Robinson
Name: Larry Robinson
Title: Vice President

DOCUMENTATION AGENT,
ISSUING BANK AND LENDER: THE BANK OF NOVA SCOTIA

By: /s/ F.C.H. Ashby
Name: F.C.H. Ashby
Title: Senior Manager
Loan Operations

LENDERS:

BANK OF SCOTLAND

By: /s/ Annie Chin Tat
Name: Annie Chin Tat
Title: Assistant Vice President

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CHRISTIANIA BANK OG KREDITKASSE

By: /s/ Williams S. Phillips
Name: Williams S. Phillips
Title: Vice President

By: /s/ Peter M. Dodge
Name: Peter M. Dodge
Title: First Vice President

THE FIRST NATIONAL BANK OF CHICAGO,
Individually and as an Issuing Bank

By: /s/ D. Andrew Bateman
Name: D. Andrew Bateman
Title: Authorized Agent

FIRST UNION NATIONAL BANK OF NORTH
CAROLINA

By: /s/ Michael J. Kolosowsky
Name: Michael J. Kolosowsky
Title: Vice President

NATIONAL BANK OF CANADA

By: /s/ John T. Dixon
Name: John T. Dixon
Title: Vice President

By: /s/ Doug G. Clark
Name: Doug G. Clark
Title: Vice President

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THE FROST NATIONAL BANK

By: /s/ Jim Crosby
Name: Jim Crosby
Title: SVP

DEN NORSKE BANK ASA

By: /s/ Byron L. Cooley
Name: Byron L. Cooley
Title: Senior Vice President

By: /s/ Morten Bjornsen
Name: Morten Bjornsen
Title: Senior Vice President

GUARANTORS:

TESORO ALASKA PETROLEUM COMPANY
TESORO EXPLORATION AND PRODUCTION
COMPANY
TESORO PETROLEUM COMPANIES, INC.
DIGICOMP, INC.
TESORO TECHNOLOGY PARTNERS COMPANY
INTERIOR FUELS COMPANY
TESORO ALASKA PIPELINE COMPANY
TESORO NORTHSTORE COMPANY
TESORO REFINING, MARKETING & SUPPLY
COMPANY
TESORO NATURAL GAS COMPANY
TESORO BOLIVIA PETROLEUM COMPANY
TESORO VOSTOK COMPANY
KENAI PIPE LINE COMPANY
TESORO MARINE SERVICES COMPANY
TESORO COASTWIDE SERVICES COMPANY
COASTWIDE MARINE SERVICES, INC.

By: /s/ G. A. Wright
Name: G. A. Wright
Title: Vice President and Treasurer

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TESORO GAS RESOURCES COMPANY, INC.
TESORO FINANCIAL SERVICES HOLDING COMPANY

By: /s/ J. B. Fabian
Name: Jeffrey B. Fabian
Title: President

VICTORY FINANCE COMPANY

By: /s/ David W. Dupert
Name: David W. Dupert
Title: President

TESORO E&P COMPANY, L.P.

By: TESORO EXPLORATION AND PRODUCTION
COMPANY, as its general partner

By: /s/ G. A. Wright
Name: G. A. Wright
Title: Vice President and Treasurer

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THIRD AMENDMENT TO
AMENDED AND RESTATED CREDIT AGREEMENT

Among

TESORO PETROLEUM CORPORATION
as the Company

and

BANQUE PARIBAS
Individually, as an Issuing Bank and as Administrative Agent,

THE BANK OF NOVA SCOTIA
Individually and as Documentation Agent

and

THE FINANCIAL INSTITUTIONS
NOW OR HEREAFTER PARTIES HERETO

Effective as of September 15, 1997

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THIRD AMENDMENT TO
AMENDED AND RESTATED CREDIT AGREEMENT

This THIRD AMENDMENT TO AMENDED AND RESTATED CREDIT AGREEMENT (this "Third Amendment") executed effective as of September 15, 1997 (the "Effective Date"), is by and among TESORO PETROLEUM CORPORATION, a Delaware corporation (the "Company"); BANQUE PARIBAS, individually, as an Issuing Bank and as Administrative Agent, THE BANK OF NOVA SCOTIA, individually and as Documentation Agent, and each of the lenders that is a signatory hereto or which becomes a party hereto as provided in Section 9.07 (individually, a "Lender" and, collectively, the "Lenders").

W I T N E S S E T H:

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WHEREAS, the Company, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders are parties to that certain Amended and Restated Credit Agreement dated as of June 7, 1996, as amended by First Amendment to Amended and Restated Credit Agreement dated as of March 21, 1997 and Second Amendment to Amended and Restated Credit Agreement dated as of March 31, 1997 (the "Credit Agreement"), pursuant to which the Lenders agreed to make loans and issue Letters of Credit to and for the account of the Company; and

WHEREAS, the Company, the Guarantors, the Administrative Agent, the Documentation Agent, and the Lenders desire to amend the Credit Agreement in the particulars hereinafter provided;

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, the parties hereto agree as follows:

ARTICLE I. DEFINITIONS

Section 1.01 Terms Defined Above. As used in this Third Amendment, each of the terms "Company", "Credit Agreement", "Effective Date", "Third Amendment", and "Lenders" shall have the meaning assigned to such term hereinabove.

Section 1.02 Terms Defined in Credit Agreement. Each term defined in the Credit Agreement and used herein without definition shall have the meaning assigned to such term in the Credit Agreement, unless expressly provided to the contrary.

Section 1.03 Other Definitional Provisions.

(a) The words "hereby", "herein", "hereinafter", "hereof", "hereto" and "hereunder" when used in this Third Amendment shall refer to this Third Amendment as a whole and not to any particular Article, Section, subsection or provision of this Third Amendment.

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(b) Section, subsection and Exhibit references herein are to such Sections, subsections and Exhibits to this Third Amendment unless otherwise specified.

ARTICLE II. AMENDMENTS TO CREDIT AGREEMENT

The Company, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders agree that the Credit Agreement is hereby amended, effective as of the Effective Date, in the following particulars.

Section 2.01 Amendments and Supplements to Definitions.

(a) The definition of "Agreement" in Section 1.01 of the Credit Agreement is hereby amended to mean the Credit Agreement, as amended by this Third Amendment and as the same may from time to time be further amended, supplemented or modified.

(b) The following terms, which are defined in Section 1.01 of the Credit Agreement, are hereby amended in their entirety to read as follows:

"Applicable Margin" shall mean (i) 0% per annum with respect to Base Rate Loans, and (ii) 1.0% per annum with respect to Eurodollar Loans; provided, however, that during any Deficiency Period, the "Applicable Margin" as would otherwise be in effect shall be increased by 2.0% per annum for both Base Rate Loans and Eurodollar Loans.

"Borrowing Base" shall mean at any time the amount equal to the sum of (i) eighty five percent (85%) of Eligible Accounts plus (ii) seventy percent (70%) of the Loan Value of Eligible Inventory; plus (iii) one hundred percent (100%) of the E&P Borrowing Base.

"Cash Flow" shall mean, as to any Person, the sum of the net income of such Person after taxes for any period plus, to the extent deducted from net income, all non-cash items, including, but not limited to, depreciation, depletion and impairment, amortization of leasehold and intangibles, deferred taxes and write-offs of exploration costs and producing lease abandonments plus, but without duplication, to the extent deducted from net income, cash not to exceed \$15,000,000, and all non-cash items related to that certain special incentive compensation award program which will be funded if the Company's stock price reaches an average price per share of \$20 or higher over 20 consecutive trading days after June 30, 1997, and before December 31, 1998; in each case for such period and determined as to such Person.

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"Consolidated Tangible Net Worth" shall mean, at any time and from time to time, the sum of preferred or common stock not subject to a mandatory redemption obligation (other than a mandatory redemption obligation that can be satisfied by the tendering of common stock of the Company) as of the date of determination, par value of common stock, additional paid-in capital of common stock and retained earnings, plus to the extent deducted from net income, cash not to exceed \$15,000,000 and all non-cash items related to that certain special incentive compensation award program which will be funded if the Company's stock price reaches an average price per share of \$20 or higher over 20 consecutive trading days after June 30, 1997, and before December 31, 1998, less treasury stock (if any), less goodwill, cost in excess of net assets acquired and all other assets as are properly classified as intangible assets, all as determined as to the Company and its Subsidiaries on a consolidated basis.

"EBITDA" shall mean, as to the Company and its Subsidiaries on a consolidated basis and, for each Rolling Period, the amount equal to net income of the Company and its Subsidiaries, less any non-cash income included in net income to the extent the applicable cash was not received at any time during such Rolling Period, plus, to the extent deducted from net income, interest expense, depreciation, depletion and

impairment, amortization of leasehold and intangible, other non-cash expenses (including, but not limited to taxes (excluding Bolivian taxes paid in kind), plus, but without duplication, to the extent deducted from net income, cash not to exceed \$15,000,000 and all non-cash items related to that certain special incentive compensation award program which will be funded if the Company's stock price reaches an average price per share of \$20 or higher over 20 consecutive trading days after June 30, 1997, and before December 31, 1998; provided, that, gains or losses on the disposition of assets shall not be included in EBITDA.

"Eligible Inventory" shall mean, at any time, all inventory (as such term is defined in Section 9-109(4) of the UCC) of the Inventory Borrowing Base Parties, including, without limitation, but without duplication, the In Transit Inventory, inventory in the Tesoro Terminals, inventory at the KPL Facility (as defined in clause (x) below), and Consigned Inventory for which each of the following statements is accurate and complete (and the Company by including such inventory in any computation of the Borrowing Base shall be deemed to represent and warrant to the Administrative Agent, each Issuing Bank and each Lender the accuracy and completeness of such statements):

(a) Said inventory is, and at all times will be, free and clear of all Liens (except for perfected Liens in favor of the Administrative Agent and, in the case of In Transit Inventory described in the definition of In Transit Inventory below, Liens securing the payment of tariffs owed by Tesoro Alaska to a common carrier

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transporting feedstocks or blendstocks through the Trans-Alaska Pipeline System or the KPL Facility, as defined below), and the Administrative Agent has a first priority, perfected security interest in such inventory;

(b) Said inventory does not include capitalized goods which are part of inventory of any Inventory Borrowing Base Party;

(c) Said inventory is located in the states of Alaska, California, Texas, Louisiana, Oregon or Washington, or the Yukon territory or British Columbia, Canada, or to the extent that it qualifies as In Transit Inventory, is located in the territorial waters of the states of Alaska, California, Oregon, Texas, Louisiana, Washington or the Yukon territory or British Columbia, Canada (and not in international waters); and

(d) Said inventory, excluding Consigned Inventory, is not stored at any terminal other than a Tesoro Terminal.

For purposes of this definition, "In Transit Inventory" shall mean, at any time, feedstocks, blendstocks or refined products, including asphalt, solely owned by an Inventory Borrowing Base Party that are in transit:

(x) to the Kenai Refinery (i) from Pump Station No. 1 on the Trans-Alaska Pipeline System, including feedstocks or blendstocks in storage at the Valdez Terminal in Valdez, Alaska, (ii) in a tanker or barge located within Alaska, California, Washington or the Yukon territory or British Columbia, Canada or their respective territorial waters (and not in international waters) that has been time chartered by any Inventory Borrowing Base Party, (iii) in or on any pipeline, terminal, dock or storage tank of the KPL in the area of Cook Inlet, Alaska (the "KPL Facility"), or (iv) in the Cook Inlet pipeline system in the area of Cook Inlet, Alaska, including feedstocks or blendstocks in storage at the Drift River Terminal in Drift River, Alaska;

(y) from the Kenai Refinery (i) in a tanker or barge located within Alaska, California, Oregon, Washington or the Yukon territory or British Columbia, Canada or their respective territorial waters (and not in international waters) that has been time chartered by any Inventory Borrowing Base Party, (ii) in the Anchorage Pipeline owned by Tesoro Alaska Pipeline Company (formerly known as the Nikiski Alaska Pipeline), or (iii) in the KPL Facility (as defined in Clause (x) above); or

(z) between Alaska, California, Washington, Texas, Louisiana Oregon or the Yukon territory or British Columbia, Canada and in their respective territorial waters (and not in international waters) and is inventory in which the Administrative Agent has been granted a first priority perfected Lien which is in effect at such time.

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(c) Sect . 1.01 of the Credit Agreement is hereby further amended and supplemented by adding the following new definitions where alphabetically appropriate, which reads in their entirety as follows:

"Consigned Inventory" shall mean inventory owned by an Inventory Borrowing Base Party being held in storage tanks of a third party pursuant to a consignment arrangement between such Inventory Borrowing Base Party and such third party, but not commingled with any other inventory or goods of such third party or other Persons, and for which such Inventory Borrowing Base Party has complied with the requirements of the Uniform Commercial Code, including Section 9.114 thereof, such that such Inventory Borrowing Base Party will have priority over a secured party who is or becomes a creditor of such third party.

"Third Amendment" shall mean that certain Third Amendment to Amended and Restated Credit Agreement dated as of September 15, 1997, by and among the Company, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders.

Section 2.02 Amendments to Article II. Section 2.20(a) of the Credit Agreement is hereby amended by replacing the last sentence thereof in its entirety with the following sentence:

"During the period from and after the effective date of the Third Amendment until the next Redetermination Date occurring after October, 1997, unless redetermined pursuant to any unscheduled redeterminations, the amount of the E&P Borrowing Base shall be \$56,000,000."

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Section 2.03 Amendments to Article V. Section 5.15(h) of the Credit Agreement is hereby amended in its entirety to read as follows:

"(h) Quarterly Borrowing Base Reports. As soon as available and in any event by the 105th day after the end of the fourth calendar quarter of each year and the 60th day after the end of each of the first three calendar quarters of each year of the Company, a quarterly Borrowing Base Report dated and reflecting amounts as of the last day of such calendar year or quarter, as the case may be, which have been reconciled to the financial statements delivered pursuant to Subsection 5.15(a) or (b), as the case may be, and in the case of the fourth calendar quarter, as soon as available and in any event by the 60th day after the end of the fourth calendar quarter of each year, a preliminary Borrowing Base Report for the prior four calendar quarters not reconciled to such financial statements, upon which the Borrowing Base will be determined for the interim period until receipt of the reconciled Borrowing Base Report for such period; provided, however, the Majority Lenders may, at any time, require up to four additional Borrowing Base Reports per calendar year and the Company may, at any time, submit up to four additional Borrowing Base Reports per calendar year, in addition to the four additional Borrowing Base Reports required by the Majority Lenders."

Section 2.04 Amendments to Article VI.

(a) Section 6.01 of the Credit Agreement is hereby amended in its entirety to read as follows:

"Section 6.01 Consolidated Tangible Net Worth. Permit Consolidated Tangible Net Worth as of the end of the calendar quarter to be less than \$189,950,000 plus 75% of the Company's consolidated net income aggregated for each of the calendar quarters from and after July 1, 1997 in which consolidated net income is positive; provided if at any time the Company

issues equity securities of any kind, such minimum amount of Consolidated Tangible Net Worth shall be permanently increased by an amount equal to 75% of the net cash proceeds from the issuance of such equity securities."

(b) Section 6.02 of the Credit Agreement is hereby amended in its entirety to read as follows:

"Section 6.02 Consolidated Current Ratio. Permit the ratio of (i) consolidated current assets to (ii) consolidated current liabilities (excluding current maturities of the Notes) to be less than 1.3 to 1.0 at any time. As used in this Section 6.02 "consolidated current assets" shall mean assets which would, in accordance with GAAP, be included as current assets on a consolidated balance sheet of the Company and its Subsidiaries and "consolidated current liabilities" shall mean liabilities which would, in accordance with GAAP, be included as current liabilities on a consolidated

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balance sheet of the Company and its Subsidiaries; provided, however, for the sole purpose of calculating such ratio, consolidated current liabilities shall not include accrued amounts related to that certain special incentive compensation award program which will be funded if the Company's stock price reaches an average price per share of \$20 or higher over 20 consecutive trading days after June 30, 1997, and before December 31, 1998, except to the extent that the cash component of such accrual exceeds \$15,000,000, such excess shall be included in consolidated current liabilities."

(c) Section 6.03 of the Credit Agreement is hereby amended by replacing the second sentence thereof in its entirety to read as follows:

"As used in this Section 6.03, "cash flow coverage ratio" shall mean, as to the Company, and for the Rolling Period ending on such Quarterly Date, the ratio of (i) the sum of (A) Cash Flow of the Company and its Subsidiaries on a consolidated basis, plus (B) the difference between (x) the lesser of the Aggregate Revolving Credit Commitments or the Borrowing Base on the last day of the applicable Rolling Period and (y) the outstanding principal amount of the Revolving Credit Loans on the first day of the last calendar quarter of such Rolling Period, plus (C) interest expense of the Company and its Subsidiaries on a consolidated basis to (ii) the sum of (A) regularly scheduled principal payments of Funded Indebtedness paid in cash, plus (B) cash interest expense of the Company and its Subsidiaries on a consolidated basis, plus (C) capital expenditures by the Company and its Subsidiaries on a consolidated basis, excluding capital expenditures made by way of (x) exchanges of equity and (y) loans provided by third parties to the extent not prohibited by Section 6.05, plus (D) cash dividends actually paid by the Company and its Subsidiaries on a consolidated basis."

(d) Section 6.05 of the Credit Agreement is hereby amended by adding thereto a new Subsection (o) as follows:

"(o) Unsecured letters of credit (other than Letters of Credit) not to exceed \$25,000,000 in the aggregate; provided, however, if an unsecured letter of credit is issued for the benefit of the State of Alaska, all unsecured letters of credit (other than Letters of Credit) shall not exceed \$40,000,000 in the aggregate."

(e) Clause (v) of Section 6.08 is hereby amended in its entirety to read as follows:

"(v) in an aggregate amount not to exceed \$10,000,000, repurchase the common stock issued by the Company from (A) shareholders owning 100 shares or less pursuant to an oddlot buy back program and (B) the open market or private sales for employee benefit or compensation plans, and"

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ARTICLE III. CONDITIONS

The enforceability of this Third Amendment against the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders is subject to the satisfaction of the following conditions precedent:

Section 3.01 Loan Documents. The Administrative Agent shall have received multiple original counterparts, as requested by the Administrative Agent, of this Third Amendment executed and delivered by a duly authorized officer of the Company, each of the Guarantors, the Administrative Agent, the Documentation Agent, each Issuing Bank and each Lender.

Section 3.02 Corporate Proceedings of Loan Parties. The Administrative Agent shall have received multiple copies, as requested by the Administrative Agent, of the resolutions, in form and substance reasonably satisfactory to the Administrative Agent, of the Boards of Directors of the Company and the Guarantors, authorizing the execution, delivery and performance of this Third Amendment, each such copy being attached to an original certificate of the Secretary or an Assistant Secretary of the Company or the Guarantors, as applicable, dated as of the Effective Date, certifying (i) that the resolutions attached thereto are true, correct and complete copies of resolutions duly adopted by written consents or at meetings of the Boards of Directors, (ii) that such resolutions constitute all resolutions adopted with respect to the transactions contemplated hereby, (iii) that such resolutions have not been amended, modified, revoked or rescinded as of the Effective Date, (iv) that the respective articles of incorporation and bylaws of the Company and the Guarantors have not been amended or otherwise modified since the effective date of the Credit Agreement, except pursuant to any amendments attached thereto, and

(v) as to the incumbency and signature of the officers of the Company or the Guarantors, as applicable, executing this Third Amendment.

Section 3.03 Representations and Warranties. Except as affected by the transactions contemplated in the Credit Agreement and this Third Amendment, each of the representations and warranties made by the Company and the Guarantors in or pursuant to the Financing Documents, including the Credit Agreement, shall be true and correct in all material respects as of the Effective Date, as if made on and as of such date.

Section 3.04 No Default. No Default or Event of Default shall have occurred and be continuing as of the Effective Date.

Section 3.05 Security Instruments. All of the Security Instruments (subject to any partial releases thereof) shall be in full force and effect and provide to the Administrative Agent the security intended thereby to secure the Indebtedness.

Section 3.06 Other Instruments or Documents. The Administrative Agent or any Lender or counsel to the Administrative Agent shall receive such other instruments or documents as they may reasonably request.

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ARTICLE IV. MISCELLANEOUS

Section 4.01 Adoption, Ratification and Confirmation of Credit Agreement. Each of the Company, the Guarantors, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders does hereby adopt, ratify and confirm the Credit Agreement, as amended hereby, and acknowledges and agrees that the Credit Agreement, as amended hereby, is and remains in full force and effect.

Section 4.02 Ratification and Affirmation of Guaranty. Each of the Guarantors hereby expressly (i) acknowledges the terms of this Third Amendment, (ii) ratifies and affirms its obligations under the Second Amended and Restated Guaranty Agreement dated as of January 28, 1997, in favor of the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders, as amended, supplemented or otherwise modified ("Guaranty Agreement"), (iii) acknowledges, renews and extends its continued liability under the Guaranty Agreement and agrees that such Guaranty Agreement remains in full force and effect; and (iv) guarantees to the Administrative Agent, the Documentation Agent, each Issuing Bank and each Lender to promptly pay when due all amounts owing or to be owing by it under the Guaranty Agreement pursuant to the terms and conditions thereof.

Section 4.03 Successors and Assigns. This Third Amendment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns permitted pursuant to the Credit Agreement.

Section 4.04 Counterparts. This Third Amendment may be executed by one or more of the parties hereto in any number of separate counterparts, and all of such counterparts taken together shall be deemed to constitute one and the same instrument and shall be enforceable as of the Effective Date upon the execution of one or more counterparts hereof by the Company, the Guarantors, the Administrative Agent, the Documentation Agent, the Issuing Bank and the Lenders. In this regard, each of the parties hereto acknowledges that a counterpart of this Third Amendment containing a set of counterpart execution pages reflecting the execution of each party hereto shall be sufficient to reflect the execution of this Third Amendment by each necessary party hereto and shall constitute one instrument.

Section 4.05 Number and Gender. Whenever the context requires, reference herein made to the single number shall be understood to include the plural; and likewise, the plural shall be understood to include the singular. Words denoting sex shall be construed to include the masculine, feminine and neuter, when such construction is appropriate; and specific enumeration shall not exclude the general but shall be construed as cumulative. Definitions of terms defined in the singular or plural shall be equally applicable to the plural or singular, as the case may be, unless otherwise indicated.

Section 4.06 Entire Agreement. This Third Amendment constitutes the entire agreement among the parties hereto with respect to the subject hereof. All prior understandings, statements and

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agreements, whether written or oral, relating to the subject hereof are superseded by this Third Amendment.

Section 4.07 Invalidity. In the event that any one or more of the provisions contained in this Third Amendment shall for any reason be held invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision of this Third Amendment.

Section 4.08 Titles of Articles, Sections and Subsections. All titles or headings to Articles, Sections, subsections or other divisions of this Third Amendment or the exhibits hereto, if any, are only for the convenience of the parties and shall not be construed to have any effect or meaning with respect to the other content of such Articles, Sections, subsections, other divisions or exhibits, such other content being controlling as the agreement among the parties hereto.

Section 4.09 Governing Law. This Third Amendment and the rights and obligations of the parties hereunder and under the Credit Agreement shall be governed by and construed in accordance with the laws of the State of Texas and the United States of America.

THIS THIRD AMENDMENT, THE CREDIT AGREEMENT, AS AMENDED AND SUPPLEMENTED HEREBY, THE NOTES, AND THE OTHER FINANCING DOCUMENTS CONSTITUTE A WRITTEN LOAN AGREEMENT AND REPRESENT THE FINAL AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES.

THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES.

[SIGNATURES BEGIN NEXT PAGE]

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IN WITNESS WHEREOF, the parties hereto have caused this Third Amendment to be duly executed and delivered by their proper and duly authorized officers as of the Effective Date.

COMPANY: TESORO PETROLEUM CORPORATION

By: /s/ G. A. Wright
Name: G.A. Wright
Title: Vice President and Treasurer

GUARANTORS: TESORO ALASKA PETROLEUM COMPANY
TESORO EXPLORATION AND PRODUCTION
COMPANY
TESORO PETROLEUM COMPANIES, INC.
DIGICOMP, INC.
TESORO TECHNOLOGY PARTNERS COMPANY
INTERIOR FUELS COMPANY
TESORO ALASKA PIPELINE COMPANY
TESORO NORTHSTORE COMPANY
TESORO REFINING, MARKETING & SUPPLY
COMPANY
TESORO NATURAL GAS COMPANY
TESORO BOLIVIA PETROLEUM COMPANY
TESORO VOSTOK COMPANY
KENAI PIPE LINE COMPANY
TESORO MARINE SERVICES COMPANY
TESORO COASTWIDE SERVICES COMPANY
COASTWIDE MARINE SERVICES, INC.

By: /s/ G. A. Wright

Name: G.A. Wright
Title: Vice President and Treasurer

TESORO GAS RESOURCES COMPANY, INC.
TESORO FINANCIAL SERVICES HOLDING
COMPANY

By: /s/ Jeffrey B. Fabian
Name: Jeffrey B. Fabian
Title: President

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<PAGE>

VICTORY FINANCE COMPANY

By: /s/ David W. Dupert
Name: David W. Dupert
Title: President

TESORO E&P COMPANY, L.P.

By: TESORO EXPLORATION AND
PRODUCTION COMPANY, as its general
partner

By: /s/ G.A. Wright
Name: G.A. Wright
Title: Vice President and Treasurer

ADMINISTRATIVE AGENT,
ISSUING BANK AND LENDER:

BANQUE PARIBAS, individually, as an Issuing
Bank and as Administrative Agent

By: /s/ Brian Malone
Name: Brian Malone
Title: Vice President

By: /s/ Barton D. Schouest
Name: Barton D. Schouest
Title: Managing Director

DOCUMENTATION AGENT,
ISSUING BANK AND LENDER:

THE BANK OF NOVA SCOTIA

By: /s/ F.C.H. Ashby
Name: F.C.H. Ashby
Title: Senior Manager
Loan Operations

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<PAGE>
LENDERS:

BANK OF SCOTLAND

By: /s/ Annie Chin Tat
Name: Annie Chin Tat
Title: Vice President

CHRISTIANIA BANK OG KREDITKASSE

By: /s/ William S. Phillips
Name: William S. Phillips
Title: Vice President

By: /s/ Peter M. Dodge
Name: Peter M. Dodge
Title: First Vice President

THE FIRST NATIONAL BANK OF CHICAGO,
Individually and as an Issuing Bank

By: /s/ Dixon P. Schultz
Name: Dixon P. Schultz
Title: Vice President

FIRST UNION NATIONAL BANK OF NORTH
CAROLINA

By: /s/ Michael J. Kolosowsky
Name: Michael J. Kolosowsky
Title: Vice President

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<PAGE>

NATIONAL BANK OF CANADA

By: /s/ William Handley
Name: William Handley
Title: Vice President

By: /s/ Doug Clark
Name: Doug Clark
Title: Vice President

THE FROST NATIONAL BANK

By: /s/ Jim Crosby
Name: Jim Crosby
Title: Senior Vice President

DEN NORSKE BANK ASA

By: /s/ Bryon L. Cooley
Name: Bryon L. Cooley
Title: Senior Vice President

By: /s/ William V. Moyer
Name: William V. Moyer
Title: First Vice President

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FILED AS OF DATE: 19971114

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FILER:

COMPANY DATA:

COMPANY CONFORMED NAME:

TESORO PETROLEUM CORP /NEW/

CENTRAL INDEX KEY:

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STANDARD INDUSTRIAL CLASSIFICATION:

PETROLEUM REFINING [2911]

IRS NUMBER:

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STATE OF INCORPORATION:

DE

FISCAL YEAR END:

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 1997

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER 1-3473

TESORO PETROLEUM CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

DELAWARE	95-0862768
(State or Other Jurisdiction of	(I.R.S. Employer
Incorporation or Organization)	Identification No.)

8700 TESORO DRIVE, SAN ANTONIO, TEXAS 78217-6218
(Address of Principal Executive Offices) (Zip Code)

210-828-8484
(Registrant's Telephone Number, Including Area Code)

=====

Indicate by check mark whether the Registrant (1) has filed all reports
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of
1934 during the preceding 12 months (or for such shorter period that the

Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

=====

There were 26,750,314 shares of the Registrant's Common Stock outstanding at October 31, 1997.

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TESORO PETROLEUM CORPORATION AND SUBSIDIARIES
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 1997
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PART I - FINANCIAL INFORMATION

ITEM 1.

FINANCIAL STATEMENTS

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TESORO PETROLEUM CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands except per share amounts)

	September 30, 1997 ----	December 31, 1996<FN1> ----
ASSETS		
<S>	<C>	<C>
CURRENT ASSETS		
Cash and cash equivalents	\$ 7,379	22,796
Receivables, less allowance for doubtful accounts of \$1,420 (\$1,515 at December 31, 1996).	83,899	128,013
Inventories:		
Crude oil and wholesale refined products, at LIFO.	55,431	55,858
Merchandise and other refined products	14,333	13,539
Materials and supplies	5,138	5,091
Prepayments and other	9,452	12,046
	-----	-----
Total Current Assets.	175,632	237,343
	-----	-----
PROPERTY, PLANT AND EQUIPMENT		
Refining and marketing.	358,792	328,522
Exploration and production (full-cost method of accounting) . .	257,003	198,480
Marine services	38,953	33,820
Corporate	13,170	12,531
	-----	-----
	667,918	573,353

Less accumulated depreciation, depletion and amortization. . .	291,113	256,842
Net Property, Plant and Equipment	376,805	316,511
OTHER ASSETS	35,377	28,733
TOTAL ASSETS	\$ 587,814	582,587
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES		
Accounts payable.	\$ 57,473	80,747
Accrued liabilities	30,567	33,256
Current income taxes payable.	1,951	13,822
Current maturities of long-term debt and other obligations. . .	9,778	10,043
Total Current Liabilities.	99,769	137,868
DEFERRED INCOME TAXES.	24,552	19,151
OTHER LIABILITIES.	45,786	42,243
LONG-TERM DEBT AND OTHER OBLIGATIONS, LESS		
CURRENT MATURITIES.	90,104	79,260
COMMITMENTS AND CONTINGENCIES (Note 4)		
STOCKHOLDERS' EQUITY		
Common Stock, par value \$.16-2/3; authorized 50,000,000 shares; 26,498,745 shares issued (26,414,134 in 1996).	4,416	4,402
Additional paid-in capital.	190,093	189,368
Retained earnings	134,043	110,295
Treasury stock, 66,998 shares at cost	(949)	-
Total Stockholders' Equity	327,603	304,065
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY.	\$ 587,814	582,587
	=====	=====

<FN>

The accompanying notes are an integral part of these condensed consolidated financial statements.
 <FN1> The balance sheet at December 31, 1996 has been taken from the audited consolidated financial statements at the condensed.

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TESORO PETROLEUM CORPORATION AND SUBSIDIARIES
 CONDENSED STATEMENTS OF CONSOLIDATED OPERATIONS
 (Unaudited)
 (In thousands except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1997	1996	1997	1996
	----	----	----	----
<S>	<C>	<C>	<C>	<C>
REVENUES				
Refining and marketing.	\$ 198,815	203,661	534,986	563,767
Exploration and production.	19,821	26,476	61,769	83,933
Marine services	32,433	32,660	98,266	87,467
Other income.	403	(725)	4,609	4,378
	-----	-----	-----	-----
Total Revenues	251,472	262,072	699,630	739,545
	-----	-----	-----	-----
OPERATING COSTS AND EXPENSES				
Refining and marketing.	188,014	194,156	508,926	545,303
Exploration and production.	3,054	2,416	8,836	8,767
Marine services	29,691	30,273	93,406	82,153
Depreciation, depletion and amortization.	11,357	10,026	34,183	29,797
	-----	-----	-----	-----
Total Operating Costs and Expenses	232,116	236,871	645,351	666,020
	-----	-----	-----	-----
OPERATING PROFIT	19,356	25,201	54,279	73,525
General and Administrative	(3,416)	(3,056)	(9,599)	(8,960)
Interest Expense, Net of Capitalized Interest in 1997	(1,481)	(4,142)	(4,634)	(12,142)
Interest Income.	135	7,100	1,459	7,681
Other Expense, Net	(1,233)	(1,254)	(3,465)	(8,802)
	-----	-----	-----	-----
EARNINGS BEFORE INCOME TAXES AND EXTRAORDINARY ITEM.	13,361	23,849	38,040	51,302

Income Tax Provision		5,382	7,686	14,292	17,159
		-----	-----	-----	-----
EARNINGS BEFORE EXTRAORDINARY ITEM		7,979	16,163	23,748	34,143
Extraordinary Loss on Extinguishment of Debt, Net of Income Tax Benefit of \$886 in 1996.		-	(2,290)	-	(2,290)
		-----	-----	-----	-----
NET EARNINGS	\$	7,979	13,873	23,748	31,853
		=====	=====	=====	=====
EARNINGS PER SHARE					
Earnings Before Extraordinary Item.	\$	.30	.61	.88	1.30
Extraordinary Loss, Net of Income Tax Benefit . . .		-	(.09)	-	(.09)
		-----	-----	-----	-----
Net Earnings.	\$	.30	.52	.88	1.21
		=====	=====	=====	=====
WEIGHTED AVERAGE COMMON AND COMMON EQUIVALENT SHARES					
		26,938	26,816	26,857	26,370
		=====	=====	=====	=====

<FN>

The accompanying notes are an integral part of these condensed consolidated financial statements.

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TESORO PETROLEUM CORPORATION AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS
(Unaudited)
(In thousands)

	Nine Months Ended September 30	
	1997	1996
	-----	-----
	<C>	<C>
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES		
Net earnings	\$ 23,748	31,853
Adjustments to reconcile net earnings to net cash from operating activities:		
Extraordinary loss on extinguishment of debt, net of income tax benefit . .	-	2,290
Depreciation, depletion and amortization.	34,643	30,386
Loss on sale of assets.	30	678
Amortization of deferred charges and other.	622	1,316
Changes in operating assets and liabilities:		
Receivable from Tennessee Gas Pipeline Company.	-	50,680

Receivables, other trade.	45,882	(6,228)
Inventories	358	16,901
Other assets.	(3,219)	793
Accounts payable and other current liabilities.	(38,557)	8,066
Obligation payments to State of Alaska.	(3,406)	(3,145)
Deferred income taxes	5,401	12,051
Other liabilities and obligations	5,569	2,760
	-----	-----
Net cash from operating activities	71,071	148,401
	-----	-----
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES		
Capital expenditures	(95,082)	(46,050)
Acquisition of Coastwide Energy Services, Inc.	-	(7,720)
Other.	(3,155)	(3,259)
	-----	-----
Net cash used in investing activities.	(98,237)	(57,029)
	-----	-----
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES		
Borrowings, net of repayments of \$28,500 in 1997 and \$112,000 in 1996, under revolving credit facilities.	15,828	-
Payments of long-term debt	(3,287)	(2,885)
Purchase of treasury stock	(1,098)	-
Other.	306	1,144
	-----	-----
Net cash from (used in) financing activities	11,749	(1,741)
	-----	-----
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(15,417)	89,631
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	22,796	13,941
	-----	-----
CASH AND CASH EQUIVALENTS, END OF PERIOD \$	7,379	103,572
	=====	=====
SUPPLEMENTAL CASH FLOW DISCLOSURES		
Interest paid, net of \$313 capitalized in 1997 \$	1,654	8,879
	=====	=====
Income taxes paid. \$	20,764	3,925
	=====	=====

<FN>

The accompanying notes are an integral part of these condensed consolidated financial statements.

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TESORO PETROLEUM CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1 - BASIS OF PRESENTATION

The interim condensed consolidated financial statements and notes thereto of Tesoro Petroleum Corporation and its subsidiaries (collectively, the "Company" or "Tesoro") have been prepared by management without audit pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Accordingly, the accompanying financial statements reflect all adjustments that, in the opinion of management, are necessary for a fair presentation of results for the periods presented. Such adjustments are of a normal recurring nature. Certain information and notes normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the SEC's rules and regulations. However, management believes that the disclosures presented herein are adequate to make the information not misleading. The accompanying condensed consolidated financial statements and notes should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 1996.

The preparation of these condensed consolidated financial statements required the use of management's best estimates and judgment that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of results for the full year.

Certain reclassifications have been made to amounts previously reported to conform to the current presentation of financial information.

NOTE 2 - ACQUISITION

In July 1997, the Company purchased the interests held by Zapata Exploration Company ("Zapata"), a wholly-owned subsidiary of Zapata Corporation, in two jointly held contract blocks (Block 18 and Block 20) in southern Bolivia. Zapata held a 25% interest in Block 18 and a 27.4% interest in Block 20. The purchase price was approximately \$20 million, which included working capital and assumption of certain liabilities. The assignment of interests has been approved by the Bolivian government. The Company's net proved Bolivian reserves, which were estimated to be 253 billion cubic feet equivalent at 1996 year-end, increased more than 30% as a result of the acquisition.

NOTE 3 - LONG-TERM DEBT

In September 1997, the Company negotiated an amendment to its \$150 million corporate revolving credit facility ("Credit Facility"). The amendment reduces the rate on cash borrowings under the Credit Facility to (i) the London Interbank Offered Rate ("LIBOR") plus 1.0% or (ii) the prime rate. Fees on outstanding letters of credit are reduced to 1.0%. The amendment also increases the Company's borrowing base and makes certain covenants in the Credit Facility less restrictive. Additionally, the Company is now permitted to utilize unsecured letters of credit outside of the Credit Facility up to \$40 million (none outstanding at September 30, 1997). Under the Credit Facility, the Company had letters of credit of \$33.9 million, primarily for royalty crude oil purchases from the State of Alaska, and cash borrowings of \$11.9 million outstanding at September 30, 1997.

In early October 1997, the Company completed an expansion of the hydrocracker unit at its Alaska refinery. The expansion, together with the addition of a new, high-yield jet fuel catalyst, has an estimated cost of approximately \$19 million and is expected to improve the Company's refinery feedstock and product slate beginning in the fourth quarter of 1997. In October 1997, the National Bank of Alaska ("NBA") and the Alaska Industrial Development and Export Authority ("AIDEA"), under a loan agreement ("Hydrocracker Loan") entered into between the Company and NBA, provided a \$16.2 million loan to the Company towards the cost of the hydrocracker expansion. One-half of the loan was funded by NBA and the other half was funded by AIDEA. The Hydrocracker Loan matures on or before April 1, 2005 and requires 28 equal quarterly principal payments beginning April 1998 together with interest at the unsecured 90-day commercial paper rate (5.55% at October 30, 1997) plus (i) 2.6% per annum on 50% of the amount borrowed and (ii) 2.35% per annum on the other 50% borrowed, each to be

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adjusted quarterly. The Hydrocracker Loan is secured by a second lien on the refinery. Under the terms of the Hydrocracker Loan, the Company is required to maintain specified levels of working capital and tangible net worth.

NOTE 4 - COMMITMENTS AND CONTINGENCIES

The Company is subject to extensive federal, state and local environmental laws and regulations. These laws, which change frequently, regulate the discharge of materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of petroleum or chemical substances at various sites or install additional controls or other modifications or changes in use for certain emission sources. The Company is currently involved with a waste disposal site near Abbeville, Louisiana, at which it has been named a potentially responsible party under the Federal Superfund law. Although this law might impose joint and several liability upon each party at the site, the extent of the Company's allocated financial contributions to the cleanup of the site is expected to be limited based upon

the number of companies, volumes of waste involved and an estimated total cost of approximately \$500,000 among all of the parties to close the site. The Company is currently involved in settlement discussions with the Environmental Protection Agency and other potentially responsible parties at the Abbeville, Louisiana site. The Company expects, based on these discussions, that its liability will not exceed \$25,000. The Company is also involved in remedial responses and has incurred cleanup expenditures associated with environmental matters at a number of sites, including certain of its own properties.

At September 30, 1997, the Company's accruals for environmental expenses amounted to \$8.7 million, which included a noncurrent liability of approximately \$3.1 million for remediation of Kenai Pipe Line Company's ("KPL") properties that has been funded by the former owners of KPL through a restricted escrow deposit. Based on currently available information, including the participation of other parties or former owners in remediation actions, the Company believes these accruals are adequate. In addition, to comply with environmental laws and regulations, the Company currently anticipates that it will make capital improvements of approximately \$3 million in 1997 and \$8 million in 1998. The Company also expects to spend approximately \$6 million by the year 2002 for secondary containment systems for existing storage tanks in Alaska.

Conditions that require additional expenditures may exist for various Company sites, including, but not limited to, the Company's refinery, retail gasoline outlets (current and closed locations) and petroleum product terminals, and for compliance with the Clean Air Act. The amount of such future expenditures cannot currently be determined by the Company.

NOTE 5 - STOCKHOLDERS' EQUITY

STOCK REPURCHASE PROGRAM

On May 7, 1997, the Company's Board of Directors authorized the repurchase of up to 3 million shares (approximately 11% of the current outstanding shares) of Tesoro Common Stock in a buyback program that will extend through the end of 1998. Under the program, subject to certain conditions, the Company may repurchase from time to time Tesoro Common Stock in the open market and through privately negotiated transactions. Purchases will depend on price, market conditions and other factors and will be made primarily from cash flows. The repurchased Common Stock is accounted for as treasury stock and may be used for employee benefit plan requirements and other corporate purposes. For further information on the repurchase program and related restrictions, see "Capital Resources and Liquidity" in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 2 herein.

INCENTIVE COMPENSATION STRATEGY

In June 1996, the Company's Board of Directors unanimously approved a special incentive compensation strategy in order to encourage a longer-term focus for

all employees to perform at an outstanding level. The strategy provides eligible employees with incentives to achieve a significant increase in the market price of the Company's Common Stock. Under the strategy, awards would be earned only if the market price of the Company's Common

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Stock reaches an average price per share of \$20 or higher over any 20 consecutive trading days after June 30, 1997 and before December 31, 1998 (the "Performance Target"). In connection with this strategy, non-executive employees will be able to earn cash bonuses equal to 25% of their individual payroll amounts for the previous twelve complete months and certain executives have been granted, from the Company's Amended and Restated Executive Long-Term Incentive Plan ("Plan"), a total of 340,000 stock options at an exercise price of \$11.375 per share, the fair market value (as defined in the Plan) of a share of the Company's Common Stock on the date of grant, and 350,000 shares of restricted Common Stock, all of which vest only upon achieving the Performance Target.

NOTE 6 - ACCOUNTING PRONOUNCEMENTS

In February 1997, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings Per Share." SFAS No. 128 becomes effective for the Company in the fourth quarter of 1997. At that time, the Company will be required to present "basic" and "diluted" earnings per share and to restate earnings per share data presented in prior periods. Early adoption is not permitted. The Company believes that the adoption of SFAS No. 128 will not materially impact its earnings per share disclosures.

In June 1997, the FASB issued SFAS No.130, "Reporting Comprehensive Income," and SFAS No.131, "Disclosures about Segments of an Enterprise and Related Information." Both Statements become effective for periods beginning after December 15, 1997 with early adoption permitted. The Company is evaluating the effects these Statements will have on its financial reporting and disclosures. The Statements will have no effect on the Company's results of operations, financial position, capital resources or liquidity.

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ITEM 2.

TESORO PETROLEUM CORPORATION AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS - THREE AND NINE MONTHS ENDED SEPTEMBER 30, 1997
COMPARED TO THREE AND NINE MONTHS ENDED SEPTEMBER 30, 1996

SUMMARY

Net earnings of \$8.0 million, or \$.30 per share, for the three months ended September 30, 1997 ("1997 Quarter") compare with net earnings of \$13.9 million, or \$.52 per share, for the three months ended September 30, 1996 ("1996 Quarter"). For the year-to-date period, net earnings of \$23.8 million, or \$.88 per share, for the nine months ended September 30, 1997 ("1997 Period") compare with net earnings of \$31.9 million, or \$1.21 per share, for the nine months ended September 30, 1996 ("1996 Period"). Results for the 1996 Quarter and Period included revenues from sales of natural gas at above-market prices under a contract with Tennessee Gas Pipeline Company ("Tennessee Gas") which was terminated effective October 1, 1996. Results of operations in 1997 and future years will no longer include above-market revenues from this contract. Significant items, including the impact of the Tennessee Gas contract, which affect the comparability between results for 1997 and 1996 are highlighted in the table below (in millions except per share amounts):

<TABLE>
<CAPTION>

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1997	1996	1997	1996
	----	----	----	----
<S>	<C>	<C>	<C>	<C>
Net Earnings As Reported	\$ 8.0	13.9	23.8	31.9
Extraordinary Loss on Debt Extinguishment, Net of Income Tax Benefit.	-	2.3	-	2.3
	-----	-----	-----	-----
Earnings Before Extraordinary Item	8.0	16.2	23.8	34.2
	-----	-----	-----	-----
Significant Items Affecting Comparability, Pretax:				
Operating profit from excess of Tennessee Gas contract prices over spot market prices	-	8.5	-	24.6
Interest and reimbursement of fees and costs from resolution of litigation.	-	7.9	-	7.9
Income from collection of Bolivian receivable.	-	-	2.2	-
Income from retroactive severance tax refunds.	-	-	1.8	5.0
Costs of shareholder consent solicitation resolved in April 1996	-	-	-	(2.3)
Employee terminations, restructuring costs and other	-	(.7)	-	(4.5)
	-----	-----	-----	-----
Total Significant Items, Pretax	-	15.7	4.0	30.7
Income Tax Effect	-	4.4	1.2	8.3
	-----	-----	-----	-----

Total Significant Items, Aftertax	-	11.3	2.8	22.4
	-----	-----	-----	-----
Net Earnings Excluding Significant Items and Extraordinary Loss	\$ 8.0	4.9	21.0	11.8
	=====	=====	=====	=====
Earnings Per Share:				
As Reported.	\$.30	.52	.88	1.21
Extraordinary Loss	-	(.09)	-	(.09)
Significant Items:				
Impact of Tennessee Gas contract prices over spot market prices	-	.23	-	.68
Other significant items.	-	.20	.10	.17
	-----	-----	-----	-----
Excluding Significant Items and Extraordinary Loss	\$.30	.18	.78	.45
	=====	=====	=====	=====

</TABLE>

As shown above, net earnings of \$8.0 million (\$.30 per share) in the 1997 Quarter would compare to \$4.9 million (\$.18 per share) when excluding the significant items in the 1996 Quarter. The resulting increase in net earnings in the 1997 Quarter was mainly attributable to improved profitability from each of the Company's business segments together with lower corporate interest expense. For the year-to-date periods, excluding significant items, net earnings would have been \$21.0 million (\$.78 per share) for the 1997 Period compared to \$11.8 million (\$.45 per share) for the 1996 Period. The increase in the 1997 Period was primarily due to higher spot market natural gas prices, better refined product margins and lower corporate interest expense. A discussion and analysis of the factors contributing to the Company's results of operations are presented below. The Company conducts its operations in the following business segments: Refining and Marketing, Exploration and Production, and Marine Services.

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<TABLE>

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REFINING AND MARKETING

(Dollars in millions except per unit amounts)

Three Months Ended September 30,		Nine Months Ended September 30,	
1997	1996	1997	1996
----	----	----	----

<S>	<C>	<C>	<C>	<C>
Gross Operating Revenues:				
Refined products.	\$ 177.5	169.9	486.9	465.7
Other, primarily crude oil resales and merchandise. . . .	21.3	33.8	48.1	98.1

Gross Operating Revenues	\$	198.8	203.7	535.0	563.8
		=====	=====	=====	=====
Total Operating Profit:					
Gross margin.	\$	34.2	31.7	94.8 <i>18%</i>	85.5 <i>15%</i>
Operating expenses.		23.3	22.3	68.7	67.1
Depreciation and amortization		3.4	3.0	9.7	9.0
Loss on sale of assets and other.		.1	.7	.1	.7
		-----	-----	-----	-----
Operating Profit	\$	7.4	5.7	16.3	8.7
		=====	=====	=====	=====
Capital Expenditures	\$	11.8	3.1	30.6	6.9
		=====	=====	=====	=====
Refinery Throughput:					
Barrels per day		43,192	41,165	48,225	45,760
% Alaska North Slope crude oil.		68%	69%	77%	71%
Refined Products Manufactured (average daily barrels)<FN1>:					
Gasoline		11,351	10,953	12,499	12,717
Middle distillates.		17,999	17,690	20,400	19,143
Heavy oils and residual product		12,587	11,638	14,140	12,829
Other		1,910	2,214	2,500	2,709
		-----	-----	-----	-----
Total Refined Products Manufactured.		43,847	42,495	49,539	47,398
		=====	=====	=====	=====
Refinery Operations - Product Spread (\$/barrel)<FN1>:					
Average yield value of products manufactured.	\$	23.81	25.07	23.83	23.87
Cost of raw materials		17.92	19.33	18.69	19.03
		-----	-----	-----	-----
Refinery Product Spread.	\$	5.89	5.74	5.14	4.84
		=====	=====	=====	=====
Non-Refinery Margin, included in operating profit above (\$ millions)<FN1><FN2>	\$	10.8	10.0	27.1	24.9
		=====	=====	=====	=====
Total Segment Product Sales (average daily barrels)<FN3>:					
Gasoline.		18,592	18,073	18,156	18,751
Middle distillates.		37,844	32,123	30,138	30,159
Heavy oils and residual product		13,748	16,489	17,700	14,594
		-----	-----	-----	-----
Total Product Sales.		70,184	66,685	65,994	63,504

	=====	=====	=====	=====
Total Segment Product Sales Prices (\$/barrel):				
Gasoline.	\$ 35.23	34.52	33.90	32.35
Middle distillates.	\$ 27.00	29.33	28.46	28.08
Heavy oils and residual product	\$ 18.40	17.03	17.53	16.86
Total Segment Gross Margins on Product				
Sales (\$/barrel)<FN4>:				
Average sales price	\$ 27.49	27.70	27.03	26.76
Average costs of sales.	22.80	23.16	22.52	22.43
	-----	-----	-----	-----
Gross Margin	\$ 4.69	4.54	4.51	4.33
	=====	=====	=====	=====

<FN>

<FN1> Amounts reported in prior periods have been reclassified to conform with current presentation.

<FN2> Non-refinery margin includes margins on products purchased and resold, margins on products sold in markets outside of Alaska, intrasegment pipeline revenues, retail margins, and adjustments due to selling a volume and mix of products that is different than actual volumes manufactured.

<FN3> Sources of total products sales include products manufactured at the refinery, products drawn from inventory balances and products purchased from third parties. The Company's purchases of refined products for resale averaged approximately 24,700 and 13,600 barrels per day for the three months ended September 30, 1997 and 1996, respectively, and approximately 15,500 and 12,100 barrels per day for the nine months ended September 30, 1997 and 1996, respectively.

<FN4> Gross margins on total product sales include margins on sales of purchased products, together with the effect of changes in inventories.

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REFINING AND MARKETING

THREE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH THREE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$7.4 million from the Company's Refining and Marketing segment during the 1997 Quarter represented a 30% improvement from the 1996 Quarter. The continued success of the Company's program to sell a larger portion of its refinery production within the core Alaska market, together with generally favorable industry conditions, contributed to this improvement. The Company's sales of gasoline and asphalt in Alaska increased in the 1997 Quarter as compared to the 1996 Quarter. Jet fuel sales also increased due to growing trans-Pacific air cargo traffic through the international airport in Anchorage.

The Company's refinery product spread averaged \$5.89 per barrel in the 1997 Quarter, a \$.15 per barrel improvement from the 1996 Quarter. The Company's refined product yield values decreased by 5% to \$23.81 per barrel in the 1997 Quarter from \$25.07 per barrel in the 1996 Quarter, while the Company's feedstock costs decreased by 7% to \$17.92 per barrel in the 1997 Quarter from

\$19.33 per barrel in the 1996 Quarter. The 1997 Quarter and 1996 Quarter both included scheduled turnarounds, during which the refinery was not fully operational. Margins from non-refinery activities increased to \$10.8 million during the 1997 Quarter from \$10.0 million in the 1996 Quarter due primarily to higher retail sales and improved margins on refined products sold outside Alaska.

The increase of \$7.6 million in revenues from refined products sales during the 1997 Quarter was primarily due to higher sales volumes, which rose 5% to 70,184 barrels per day in the 1997 Quarter from 66,685 barrels per day in the 1996 Quarter. Other revenues declined by \$12.5 million due primarily to lower sales volumes of previously purchased crude oil together with lower prices. During the 1997 Quarter, the Company had less crude oil available for resale as refinery throughput averaged 2,027 barrels per day more than in the 1996 Quarter. Costs of sales decreased in the 1997 Quarter due to lower prices for crude oil and refined products. The \$1.0 million increase in operating expenses included higher employee costs associated in part with expanded marketing efforts and higher professional fees. The 1996 Quarter included a \$.7 million write-down of a West Coast terminal that was subsequently sold.

NINE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH NINE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$16.3 million in the 1997 Period compares to operating profit of \$8.7 million in the 1996 Period. The Company's refinery spread of \$5.14 per barrel in the 1997 Period improved 6% from the prior year period. The Company's production of jet fuel, a product in short supply in Alaska, was higher in the 1997 Period principally due to the use of an improved catalyst in the hydrocracker unit, a change made during the refinery turnaround in the 1996 Period. Margins from non-refinery activities increased to \$27.1 million during the 1997 Period as compared to \$24.9 million in the 1996 Period due primarily to higher retail sales and improved margins on refined products sold outside of Alaska.

Revenues from sales of refined products in the Company's Refining and Marketing segment increased by 5% during the 1997 Period due to higher sales volumes and prices. Other revenues declined by \$50.0 million during the 1997 Period due primarily to lower sales volumes of crude oil together with lower prices. During the 1997 Period, the Company had less crude oil available for resale as refinery throughput averaged 2,465 barrels per day more than in the 1996 Period and fewer spot purchases of crude oil were made. Costs of sales decreased in the 1997 Period due to lower volumes of crude oil. The \$1.6 million increase in operating expenses included higher employee costs and professional fees.

FUTURE IMPACT. The improvement in Refining and Marketing results have been due in part to the Company's marketing program to sell a larger portion of its refinery production within the core Alaska market. In addition, favorable summer and fall weather conditions in Alaska increased the demand for the Company's in-state sales during the 1997 Period. In early October 1997, the Company completed an expansion of its refinery hydrocracker unit, which

increases the unit's capacity by approximately 25% to 12,500 barrels per day and enables the Company to produce more jet fuel. The expansion, together with the addition of a new, high-yield jet fuel catalyst, has an estimated cost of \$19 million with a projected payback period of two years and is expected to favorably impact this segment's results beginning in the fourth quarter of 1997. The Company is also expanding its Alaskan retail operations with the construction of new outlets and remodeling of existing outlets. With respect to crude oil supply, beginning in October 1997, a subsidiary of the Company has contracts to purchase all of the approximately 34,000 barrels per day of Cook Inlet production for various periods of more than one year. In the 1997 Period, the Company processed approximately 9,300 barrels per day of Cook Inlet crude, or 19% of the refinery's throughput. The increase in Cook Inlet crude oil as a refinery feedstock will enable the Company to

*Sells Crude to
Subsidiary
Trio to P.O.*

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produce higher-valued products. Although the aforementioned initiatives are expected to improve the fundamental earnings potential of this segment, future profitability of this segment will continue to be influenced by market conditions, particularly as these conditions influence costs of crude oil relative to prices received for sales of refined products, and other additional factors that are beyond the control of the Company.

<TABLE>

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EXPLORATION AND PRODUCTION

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1997	1996	1997	1996
(Dollars in millions except per unit amounts)				
<S>	<C>	<C>	<C>	<C>
U.S. <FN1> <FN2>:				
Gross Operating Revenues	\$ 15.9	23.0	53.3	73.4
Other Income (primarily retroactive severance tax refunds)	-	-	1.9	5.0
Production Costs	1.5	1.3	5.0	3.8
Administrative Support and Other Operating Expenses . . .	.6	.2	1.7	2.2
Depreciation, Depletion and Amortization	7.0	6.2	22.2	18.9
Operating Profit - U.S.	6.8	15.3	26.3	53.5
BOLIVIA:				
Gross Operating Revenues	3.8	3.4	8.4	10.5
Other Income (related to collection of a receivable) . . .	-	-	2.2	-
Production Costs	.3	.2	.7	.6
Administrative Support and Other Operating Expenses . . .	.5	.6	1.3	2.1

Depreciation, Depletion and Amortization.	.5	.4	1.0	1.0
	-----	-----	-----	-----
Operating Profit - Bolivia	2.5	2.2	7.6	6.8
	-----	-----	-----	-----
TOTAL OPERATING PROFIT - EXPLORATION AND PRODUCTION. . . . \$	9.3	17.5	33.9	60.3
	=====	=====	=====	=====

U.S.:

Average Daily Net Production:				
Natural gas (Mcf)	79,683	80,612	86,317	88,723
Oil (barrels)	93	39	119	15
Average Prices:				
Natural gas (\$/Mcf) -				
Spot market<FN3> \$	2.01	1.71	2.08	1.77
Average<FN2> \$	2.01	2.92	2.08	2.85
Oil (\$/barrel) \$	18.23	20.93	19.44	20.59
Average Operating Expenses (\$/Mcfe) -				
Lease operating expenses \$	.21	.14	.18	.12
Severance taxes.	-	.04	.03	.04
	-----	-----	-----	-----
Total Production Costs.	.21	.18	.21	.16
Administrative support	.09	.01	.07	.08
	-----	-----	-----	-----
Total Operating Expenses. \$	.30	.19	.28	.24
	=====	=====	=====	=====
Depletion (\$/Mcfe) \$	.93	.82	.92	.77
	=====	=====	=====	=====
Capital Expenditures. \$	16.3	11.7	32.5	27.1
	=====	=====	=====	=====

BOLIVIA:

Average Daily Net Production:				
Natural gas (Mcf)	26,856	20,945	18,452	21,355
Condensate (barrels)	760	605	529	611
Average Prices:				
Natural gas (\$/Mcf) \$				
	1.13	1.31	1.20	1.33
Condensate (\$/barrel) \$				
	15.00	16.92	16.23	16.50
Average Operating Expenses (\$/Mcfe) -				
Production costs \$	.10	.11	.11	.10
Value-added taxes.	-	.08	-	.07
Administrative support	.20	.24	.25	.24
	-----	-----	-----	-----
Total Operating Expenses. \$	.30	.43	.36	.41
	=====	=====	=====	=====
Depletion (\$/Mcfe) \$	.19	.17	.18	.15
	=====	=====	=====	=====
Capital Expenditures. \$	20.0	.8	26.0	5.7

=====

<FN>

<FN1> Represents the Company's U.S. oil and gas operations combined with gas transportation activities.

<FN2> Results for 1996 included revenues from above-market pricing provisions of a contract with Tennessee Gas which was terminated effective October 1, 1996. Operating profit for the three and nine months ended September 30, 1996 included \$8.5 million and \$24.6 million, respectively, for the excess of these contract prices over spot market prices. Net natural

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gas production sold under the contract averaged approximately 14 Mmcf per day for both the three months and nine months ended September 30, 1996.

<FN3> Includes effects of the Company's natural gas commodity price agreements which amounted to a loss of \$.19 per Mcf for the three months ended September 30, 1996, and losses of \$.06 per Mcf and \$.15 per Mcf for the nine months ended September 30, 1997 and 1996, respectively.

<FN4> Mcf is defined as one thousand cubic feet; Mcfe is defined as net equivalent one thousand cubic feet.

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EXPLORATION AND PRODUCTION - U. S.

THREE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH THREE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$6.8 million from the Company's U.S. operations in the 1997 Quarter compares to operating profit of \$15.3 million in the 1996 Quarter. The 1996 Quarter included revenues from the sale of natural gas at above-market prices under a contract with Tennessee Gas. The excess of these contract prices over spot market prices contributed approximately \$8.5 million to operating profit in the 1996 Quarter. When excluding the incremental value of the Tennessee Gas contract from the 1996 Quarter, operating profit from the Company's U.S. operations for the 1997 Quarter would be relatively unchanged as total production volumes remained flat during both quarters and increases in spot market natural gas prices were offset by increased depreciation and depletion and operating expenses.

Prices realized by the Company on spot market natural gas production increased to \$2.01 per Mcf in the 1997 Quarter from \$1.71 per Mcf in the 1996 Quarter. On a weighted-average basis, the Company's natural gas sales price was \$2.92 per Mcf in the 1996 Quarter due to sales under the Tennessee Gas contract. The Company's production averaged 80.2 million cubic feet equivalents ("Mmcfe") per day in the 1997 Quarter compared to 80.8 Mmcfe per day in the 1996 Quarter. This decrease in the Company's production consisted of a 14.0 million cubic feet ("Mmcf") per day decline from the Bob West Field partially offset by a 13.4 Mmcfe per day production increase from other U.S. fields. The Company's production outside of the Bob West Field rose to 23% of total production during the 1997 Quarter, as compared to 6% in the 1996 Quarter. In September 1997, production began from the Company's interest in the Vinegarone East Field in Val

Verde Basin of Southwest Texas at an initial flow rate of approximately 12 Mmcf per day gross (8.6 Mmcf per day net). Drilling is underway on two development wells in this field. In addition, the Cuellar 1 well, which was discovered during the 1997 Quarter in the Wilcox Trend of South Texas, began production in October 1997 at 8.0 Mmcf per day gross (6.0 Mmcf per day net). The Company's net U.S. production reached 90 Mmcf per day in late October 1997.

Gross operating revenues from the Company's U.S. operations, after excluding amounts related to Tennessee Gas, increased due to the higher spot market prices. Production costs increased by \$.2 million in the 1997 Quarter due primarily to higher per-unit lease operating expenses from the Company's newer fields. Depreciation and depletion increased by \$.8 million, or 13%, due to a higher depletion rate.

From time to time, the Company enters into commodity price agreements to reduce the risk caused by fluctuation in the prices of natural gas in the spot market. During the 1996 Quarter, the Company used such agreements to set the price of 38% of the natural gas production that it sold in the spot market and recognized a loss of \$1.2 million (\$.19 per Mcf) related to these price agreements. The Company did not have any such transactions during the 1997 Quarter.

NINE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH NINE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$26.3 million from the Company's U.S. operations in the 1997 Period compares to \$53.5 million in the 1996 Period. Comparability between these periods was impacted by certain significant items. The 1996 Period included operating profit of \$24.6 million from the excess of Tennessee Gas contract prices over spot market prices. Results of operations in 1997 and future years will no longer include above-market revenues from this contract which was terminated effective October 1, 1996. Operating profit also included retroactive severance tax refunds of \$1.8 million and \$5.0 million in the 1997 and 1996 Periods, respectively. Excluding the incremental value of the Tennessee Gas contract and retroactive severance tax refunds, operating profit from the Company's U.S. operations would have been \$24.5 million in the 1997 Period compared to \$23.9 million in the 1996 Period. The resulting increase of \$.6 million was primarily attributable to higher spot market prices for sales of natural gas partially offset by higher depreciation and depletion.

Prices realized by the Company on its spot natural gas production increased 18% to \$2.08 per Mcf in the 1997 Period from \$1.77 per Mcf in the 1996 Period. The increase in average spot market prices was attributable in part to unusually high prices received during January and February when there was unusually cold weather combined with below-normal natural gas storage levels. On a weighted-average basis, the Company's natural

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gas sales price was \$2.85 per Mcf in the 1996 Period due to sales under the

Tennessee Gas contract. The Company's production averaged 87.0 Mmcfe per day in the 1997 Period, a decrease of 1.8 Mmcfe per day from the 1996 Period. This decrease in the Company's production consisted of a 13.9 Mmcfe per day decline from the Bob West Field partially offset by a 12.1 Mmcfe per day increase from other U.S. fields. Production from the Bob West Field, which accounted for 95% of the Company's total U.S. production in the 1996 Period, was reduced to 81% in the 1997 Period.

Gross operating revenues from the Company's U.S. operations, after excluding amounts related to Tennessee Gas, increased due to the higher spot market prices. Production costs increased by \$1.2 million during the 1997 Period due to higher per-unit lease operating expenses from the Company's newer fields. Administrative support and other operating expenses decreased by \$.5 million. Depreciation and depletion increased by \$3.3 million, or 17%, due to a higher depletion rate.

From time to time, the Company enters into commodity price agreements to reduce the risk caused by fluctuations in the prices of natural gas in the spot market. In addition, from time to time the Company has entered into price agreements with collars, under which no payments will be made by either party unless the price falls below a designated floor price or above a designated ceiling price, at which time the Company receives or pays the difference, respectively. During the 1997 and 1996 Periods, the Company used such agreements to set the price of 11% and 37%, respectively, of the natural gas production that it sold in the spot market. During the 1997 and 1996 Periods, the Company realized losses of \$1.6 million (\$.06 per Mcf) and \$2.9 million (\$.15 per Mcf), respectively, from these price agreements. At September 30, 1997, the Company has no remaining price agreements outstanding for the year.

EXPLORATION AND PRODUCTION - BOLIVIA

HYDROCARBONS LAW. In 1996, a new Hydrocarbons Law was passed by the Bolivian government that significantly impacts the Company's operations in Bolivia. The new law, among other matters, granted the Company the option to convert its Contracts of Operation to new Shared Risk Contracts. On November 6, 1997, the Company completed the conversion of its Contracts of Operation for Block 18 and Block 20 into four Shared Risk Contracts. The new contracts have an effective date of July 29, 1996 and extend the Company's term of operation, provide more favorable acreage relinquishment terms and provide for a more favorable fiscal regime of royalties and taxes. The new contract for Block 18 is extended to the year 2017. The new contracts for Block 20 are extended to the year 2029 for Block 20-West and Block 20-East, which are in the exploration phase, and to the year 2018 for Block 20-Los Suris that is in the development phase.

FARMOUT. A farmout agreement executed June 19, 1997, between the Company and Total Exploration Production Bolivie, S.A. ("Total"), an affiliate of Total S.A., became effective on a portion of Block 20-West on November 6, 1997. Pursuant to the farmout agreement, Total established a financial guarantee to

the Bolivian government to guarantee the performance of exploration work on Block 20-West. Under the farmout agreement, Total has the right to drill, at its sole cost, two exploratory wells to earn a 75 percent interest in the farmout area which consists of 315,000 acres of Block 20-West. The assignment of interest by the Company to Total, which is subject to reversion if Total does not earn the interest, has been approved by the Bolivian government and is expected to become effective in the fourth quarter of 1997. It is anticipated that Total will spud the first well by mid-1998.

YPFB AND YPF CONTRACT. The Company's Bolivian natural gas production has been sold to Yacimientos Petroliferos Fiscales Bolivianos ("YPFB"), which in turn sells the natural gas to Yacimientos Petroliferos Fiscales, SA ("YPF"), a publicly-held company based in Argentina. Currently, the Company's sales of natural gas production is based on the volume and pricing terms in the contract between YPFB and YPF. The contract to sell gas to YPF expired March 31, 1997 and a contract extension was signed effective April 1, 1997 extending the contract term two years to March 31, 1999 with an option to extend the contract a maximum of one additional year if the pipeline being constructed from Bolivia to Brazil is not complete. In the contract extension, YPF negotiated an 11% reduction in the minimum contract volume it is required to import from Bolivia, which in turn resulted in a corresponding 11% reduction of Tesoro's minimum contract volume.

ACCESS TO NEW MARKETS. A lack of market access has constrained natural gas production in Bolivia. Preliminary work on a new 1,900-mile pipeline that will link Bolivia's gas reserves with markets in Brazil has begun and the pipeline is expected to be operational in early 1999.

THREE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH THREE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$2.5 million from the Company's Bolivian operations in the 1997 Quarter compares to

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operating profit of \$2.2 million in the 1996 Quarter. With the Company's purchase of Zapata's interests in Block 18 and Block 20 in July 1997, the Company now holds a 100% interest in both blocks, subject to the farmout agreement with Total (see Note 2 of Notes to Condensed Consolidated Financial Statements). Beginning in the 1997 Quarter, the Company's net share of production from Block 18 increased by approximately 33% as a result of this purchase. Block 20 is currently shut-in waiting on the construction of the pipeline to Brazil, which is expected to be operational in early 1999. Natural gas prices for Bolivian production fell to \$1.13 per Mcf in the 1997 Quarter, a 14% drop from the 1996 Quarter.

NINE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED WITH NINE MONTHS ENDED SEPTEMBER 30, 1996. Operating profit of \$7.6 million from the Company's Bolivian

operations in the 1997 Period compares to operating profit of \$6.8 million in the 1996 Period. The 1997 Period included income of \$2.2 million related to the collection of a receivable for prior years production. Excluding this income, operating profit would have decreased by \$1.4 million as production of natural gas and condensate fell by 14%. As discussed above, the Company's production rose during the 1997 Quarter due to the purchase of the Zapata interests in July 1997 which will also benefit future periods. However, earlier in the year, the Company's Bolivian natural gas production was lower due to a reduction in minimum takes under the new contract between YPFB and YPF and also due to constraints arising from repairs to a non-Company-owned pipeline that transports gas from Bolivia to Argentina. A replacement pipeline is now operational, which has restored full capacity. During the 1996 Period, production was higher due to requests from YPFB for additional production from the Company to meet export specifications. Natural gas prices declined to \$1.20 per Mcf in the 1997 Period compared to \$1.33 per Mcf in the 1996 Period. Administrative support and other operating expenses decreased by \$.8 million in the 1997 Period due primarily to the reduced production levels.

<TABLE>

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MARINE SERVICES

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in millions)	1997	1996	1997	1996
	----	----	----	----
<S>	<C>	<C>	<C>	<C>
Gross Operating Revenues:				
Fuels	\$ 25.2	26.0	77.6	70.4
Lubricants and other.	4.2	4.1	12.3	10.9
Services.	3.1	2.6	8.4	6.2
	----	----	----	----
Gross Operating Revenues	32.5	32.7	98.3	87.5
Costs of Sales	22.9	24.5	72.6	66.7
	----	----	----	----
Gross Profit	9.6	8.2	25.7	20.8
Operating Expenses and Other	6.5	5.8	20.4	15.4
Depreciation and Amortization.	.4	.4	1.2	.9
	----	----	----	----
Operating Profit	\$ 2.7	2.0	4.1	4.5
	=====	=====	=====	=====
Sales Volumes (millions of gallons):				
Fuels, primarily diesel	39.1	37.8	116.2	107.4
Lubricants.	.7	.7	2.0	1.9
Capital Expenditures	\$ 2.0	1.2	5.3	6.2

</TABLE>

For the 1997 Quarter, gross operating revenues declined by \$.2 million due primarily to lower fuel sales prices partly offset by increased fuel volumes. The \$1.6 million decrease in cost of sales correlates to these lower fuel market prices. The 19% increase in service revenues was associated with the increased rig activity in the Gulf of Mexico and the Company's focus to serve these customers. The improvement of \$1.4 million in gross profit was partly offset by higher operating expenses associated with the increased sales volumes and service revenues.

For the 1997 Period, gross operating revenues increased by \$10.8 million, with an 11% increase in fuels and lubricants revenues and a 35% increase in service revenues. These increases were mainly due to added locations and associated volumes stemming from an acquisition consummated in February 1996 together with internal growth initiatives. Costs of sales during the 1997 Period increased due to the higher volumes and also included a \$.7 million charge associated with inventory valuations as market prices declined from year-end levels. The improvement of \$4.9 million in gross profit during the 1997 Period was offset by higher operating and other expenses associated with the increased activity and upgrades to facilities and services.

The Marine Services segment's business is largely dependent upon the volume of oil and gas drilling, workover, construction and seismic activity in the Gulf of Mexico.

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GENERAL AND ADMINISTRATIVE

General and administrative expense increased by \$.3 million and \$.6 million during the 1997 Quarter and Period, respectively. These increases were primarily due to higher employee costs partially offset by reduced professional fees and insurance costs.

INTEREST EXPENSE AND INTEREST INCOME

Interest expense decreased by \$2.6 million and \$7.5 million during the 1997 Quarter and Period, respectively. These decreases were primarily due to the Company's redemption of \$74.1 million of public debt in November 1996 which has resulted in interest expense savings of approximately 60% in the 1997 Quarter and Period.

Interest income decreased by \$6.9 million and \$6.2 million during the 1997 Quarter and Period, respectively. The 1996 Quarter and Period included interest of approximately \$7 million received from Tennessee Gas in conjunction with the collection of a receivable which resulted from underpayment for natural gas sold

in prior periods. The 1997 Period included interest income of approximately \$.4 million related to the collection of a Bolivia receivable.

OTHER EXPENSE, NET

For the 1997 Period, other expense decreased by \$5.3 million primarily due to charges incurred in the prior year period for shareholder consent solicitation costs of \$2.3 million, which was resolved in April 1996, together with a write-off of deferred financing costs and employee termination costs with no material comparable costs recorded in the current period.

INCOME TAX PROVISION

Income taxes decreased by \$2.2 million and \$2.8 million during the 1997 Quarter and Period, respectively. These decreases were primarily due to lower earnings.

IMPACT OF CHANGING PRICES

The Company's operating results and cash flows are sensitive to the volatile changes in energy prices. Major shifts in the cost of crude oil used for refinery feedstocks and the price of refined products can result in a change in margin from the Refining and Marketing operations, as prices received for refined products may or may not keep pace with changes in crude oil costs. These energy prices, together with volume levels, also determine the carrying value of crude oil and refined product inventory. The Company uses the last-in, first-out ("LIFO") method of accounting for inventories of crude oil and U.S. wholesale refined products. This method results in inventory carrying amounts that are less likely to represent current values and in costs of sales which more closely represent current costs.

Likewise, changes in natural gas, condensate and oil prices impact revenues and the present value of estimated future net revenues and cash flows from the Company's Exploration and Production operations. The Company may increase or decrease its production in response to market conditions. The carrying value of oil and natural gas assets may be subject to noncash writedowns based on changes in natural gas prices and other determining factors.

Changes in natural gas prices also influence the level of drilling activity in the Gulf of Mexico. The Company's Marine Services operation, whose customers include offshore drilling contractors and related industries, could be impacted by significant fluctuations in natural gas prices. The Company's Marine Services segment uses the first-in, first-out ("FIFO") method of accounting for its inventories of fuel. Changes in fuel prices can significantly impact inventory valuations and costs of sales in this segment.

CAPITAL RESOURCES AND LIQUIDITY

OVERVIEW

The Company's primary sources of liquidity are its cash and cash equivalents, internal cash generation and external financing. During the first nine months of 1997, the Company made capital expenditures exceeding \$95 million, which were funded through a combination of cash flows from operations of \$71 million, external financing of \$16 million and available cash balances. Subsequently, in October 1997, the Company obtained a \$16.2 million term loan to finance the expansion of the refinery hydrocracker unit (see Note 3 of Notes to Condensed Consolidated Financial Statements). At September 30, 1997, the Company's debt-to-capitalization ratio was 22% which enhances the Company's ability to access capital markets.

The Company is focused on its strategic plans to make operational improvements and continues to assess its asset base in order to maximize returns and develop full value through strategic diversification and acquisitions in all of its operating segments. This ongoing assessment includes, in the Exploration and Production segment, evaluating ways in which the Company could diversify its oil and gas reserve base and offset the impact of declining production through domestic development, exploration and acquisition outside of the Bob West Field. In the Refining and Marketing segment, the Company has been engaged in studies to improve profitability and has also evaluated possible joint ventures, strategic alliances or business combinations; such evaluations have not resulted in any significant transaction but operating strategies have been implemented to optimize the product and feedstock slates, improve efficiencies and reliability, and expand marketing to increase placement of products in Alaska. In the Marine Services segment, the Company continues to pursue opportunities for expansion as well as optimizing existing operations.

The Company operates in an environment where its liquidity and capital resources are impacted by changes in the supply of and demand for crude oil, natural gas and refined petroleum products, market uncertainty and a variety of additional risks that are beyond the control of the Company. These risks include, among others, the level of consumer product demand, weather conditions, the proximity of the Company's natural gas reserves to pipelines, the capacities of such pipelines, fluctuations in seasonal demand, governmental regulations, the price and availability of alternative fuels and overall market and economic conditions. The Company's future capital expenditures as well as borrowings under its credit arrangements and other sources of capital will be affected by these conditions.

STOCK REPURCHASE PROGRAM

On May 7, 1997, the Company's Board of Directors authorized the repurchase of up to 3 million shares (approximately 11% of the current outstanding shares) of Tesoro Common Stock in a buyback program that will extend through the end of

1998. Under the program, subject to certain conditions, the Company may repurchase from time to time Tesoro Common Stock in the open market and through privately negotiated transactions. Purchases will depend on price, market conditions and other factors and will be made primarily from cash flows. The repurchased Common Stock is accounted for as treasury stock and may be used for employee benefit plan requirements and other corporate purposes. Repurchases of Common Stock are subject to the restricted payments provision of the Credit Facility as described below.

CREDIT ARRANGEMENTS

The Company has financing and credit arrangements with a consortium of nine banks under a corporate revolving credit agreement ("Credit Facility") which provides total commitments of \$150 million. The Credit Facility, which extends through April 2000, provides for cash borrowings up to \$100 million and issuance of letters of credit, subject to a borrowing base (which was approximately \$147 million at September 30, 1997). The Company, at its option, has currently activated total commitments of \$100 million. Outstanding obligations under the Credit Facility are secured by liens on substantially all of the Company's trade accounts receivable and product inventory and by mortgages on the Company's refinery and South Texas natural gas reserves. Under the terms of the Credit Facility, the Company is required to maintain specified levels of consolidated working capital, tangible net worth, cash flow and interest coverage. Among other matters, the Credit Facility contains covenants which limit the incurrence of additional indebtedness and restricted payments. An amendment to the Credit Facility, which was negotiated in September 1997, reduces interest rates and certain fees, increases the Company's borrowing base and makes certain covenants less restrictive. Additionally, the Company is now

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permitted to utilize unsecured letters of credit outside of the Credit Facility up to \$40 million (none outstanding at September 30, 1997). Under the Credit Facility, the Company had letters of credit of \$33.9 million, primarily for royalty crude oil purchases from the State of Alaska, and cash borrowings of \$11.9 million outstanding at September 30, 1997.

The terms of the Credit Facility allow for open market stock repurchases and the payment of cash dividends subject to a cumulative amount available for restricted payments (defined as the difference of (i) the sum since December 31, 1995, of (a) \$5 million and (b) 50% of consolidated net earnings of the Company in any calendar year and (ii) any restricted payments made since June 1996). At September 30, 1997, the cumulative amount available for restricted payments was approximately \$54 million. Annually, however, the aggregate of open market stock repurchases and cash dividends cannot exceed a maximum of \$5 million. In addition, the Credit Facility permits the Company to repurchase a limited amount of Common Stock up to \$10 million annually, specifically for oddlot buyback

programs and employee benefit or compensation plans. While the Board of Directors has no present plans to pay dividends, from time to time the Board of Directors reevaluates the feasibility of declaring future dividends.

In addition to the Credit Facility, a subsidiary of the Company has a three-year line of credit with a bank which provides up to \$10 million for the purchase of real estate and equipment for the Company's Marine Services segment at the bank's prime rate. The loan facility is not guaranteed by the Company and is secured only by such real estate and equipment that are financed. Beginning in March 1998, credit availability is reduced quarterly by 6.667%. At September 30, 1997, \$ 4.8 million was outstanding under the loan facility.

In early October 1997, the Company completed an expansion of the hydrocracker unit at its Alaska refinery. The expansion, together with the addition of a new, high-yield jet fuel catalyst, has an estimated cost of approximately \$19 million and is expected to improve the Company's refinery feedstock and product slate beginning in the fourth quarter of 1997. In October 1997, the National Bank of Alaska ("NBA") and the Alaska Industrial Development and Export Authority ("AIDEA"), under a loan agreement ("Hydrocracker Loan") entered into between the Company and NBA, provided a \$16.2 million loan to the Company towards the cost of the hydrocracker expansion. The Hydrocracker Loan matures on or before April 1, 2005 and is secured by a second lien on the refinery. Under the terms of the Hydrocracker Loan, the Company is required to maintain specified levels of working capital and tangible net worth. See Note 3 of Notes to Condensed Consolidated Financial Statements.

CAPITAL SPENDING

During the first nine months of 1997, the Company's capital expenditures totaled \$95 million which were financed with available cash reserves, internally-generated cash flows from operations and external financing. In addition, the Company has obtained outside financing, as discussed above, for expansion of the refinery hydrocracker unit. Although capital expenditures for the remainder of the year had been projected to reach \$65 million, actual capital spending will be less due to a number of factors, including the extent to which properties are acquired and the timing of capital projects. Capital expenditures for the remainder of the year are expected to be funded by cash flows from operations and external borrowings under the Company's credit arrangements.

The Exploration and Production segment accounts for \$101 million of the projected capital expenditures, with \$71 million planned for U.S. activities and \$30 million in Bolivia. Planned U.S. expenditures include \$22 million for property acquisitions; \$17 million for development drilling (participation in 16 wells), field facilities and workovers; \$13 million for leasehold, geological and geophysical; and \$19 million for exploratory drilling (participation in 14 wells). For the first nine months of 1997, actual U.S. expenditures were \$32 million, principally for participation in the drilling of five development wells

(all completed) and nine exploratory wells (seven completed). In Bolivia, projected capital expenditures of \$30 million for the year included an increase for the purchase of additional contract interests in July 1997 (see Note 2 of Notes to Condensed Consolidated Financial Statements). The projection in Bolivia includes \$3 million for one exploratory well and \$2 million for workovers and field facilities, with the remainder planned for three-dimensional seismic. Capital spending for the first nine months of 1997 totaled \$26 million in Bolivia, primarily for the purchase of additional contract interests, exploratory drilling, seismic activity and workovers. Although the Company continues to pursue exploratory, development and acquisition opportunities, as discussed above, actual capital expenditures for the remainder of the year may vary from projections.

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Capital spending for the Refining and Marketing segment is projected to be \$50 million for the year, including costs for the refinery hydrocracker expansion and a multi-year capital program to improve marketing operations. During the first nine months of 1997, the Refining and Marketing segment had spent approximately \$31 million towards capital projects.

In the Marine Services segment, capital spending for 1997 is currently projected at \$8 million, a \$21 million reduction from the original budget. This projection, of which \$5 million was spent during the first nine months of 1997, is now primarily directed towards expansion and improvement of operations along the Gulf of Mexico rather than acquisitions.

CASH FLOWS

Components of the Company's cash flows are set forth below (in millions):

<TABLE>

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Nine Months Ended
September 30,

1997 1996

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Cash Flows From (Used In):

Operating Activities	\$	71.1	148.4
Investing Activities		(98.2)	(57.0)
Financing Activities		11.7	(1.8)
		-----	-----
Increase (Decrease) in Cash and Cash Equivalents	\$	(15.4)	89.6
		=====	=====

</TABLE>

Operating cash flows of \$71 million during the 1997 Period included a \$46 million decrease in receivables due in part to collections related to high product and crude oil sales volumes at 1996 year-end and to a Bolivian receivable representing production sold in prior years, partially offset by income tax and other payments. The 1996 Period operating cash flows of \$148 million included a \$67.5 million receipt from Tennessee Gas and reduced working capital requirements. Net cash used in investing activities of \$98 million during the 1997 Period included capital expenditures of \$58 million for the Company's Exploration and Production activities, \$31 million for Refining and Marketing operations and \$5 million for Marine Services. Net cash from financing activities during the 1997 Period included borrowings of \$16 million under revolving credit facilities partially offset by payments of other long-term debt and purchases of treasury stock. At September 30, 1997, the Company's net working capital totaled \$76 million, which included cash and cash equivalents of \$7 million.

ENVIRONMENTAL

The Company is subject to extensive federal, state and local environmental laws and regulations. These laws, which change frequently, regulate the discharge of materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of petroleum or chemical substances at various sites or install additional controls or other modifications or changes in use for certain emission sources. The Company is currently involved in remedial responses and has incurred cleanup expenditures associated with environmental matters at a number of sites, including certain of its own properties. At September 30, 1997, the Company's accruals for environmental expenses amounted to \$8.7 million, which included a noncurrent liability of \$3.1 million for remediation of KPL's properties that has been funded by the former owners of KPL through a restricted escrow deposit. Based on currently available information, including the participation of other parties or former owners in remediation actions, the Company believes these accruals are adequate. In addition, to comply with environmental laws and regulations, the Company anticipates that it will make capital improvements of approximately \$3 million in 1997 and \$8 million in 1998. The Company also expects to spend approximately \$6 million by the year 2002 for secondary containment systems for existing storage tanks in Alaska.

Conditions that require additional expenditures may exist for various Company sites, including, but not limited to, the Company's refinery, retail gasoline outlets (current and closed locations) and petroleum product terminals, and for compliance with the Clean Air Act. The amount of such future expenditures cannot currently be determined by the Company. For further information on environmental contingencies, see Note 4 of Notes to Condensed Consolidated Financial Statements.

SCOMM

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MAPCO COMMENTS ON GASOLINE PRICES

April 8, 1998

There have been several articles recently in Alaska newspapers which expressed concerns about gasoline prices in Alaska. On behalf of MAPCO, I am pleased to respond to some of those concerns.

First, I need to note that crude oil is not the only component or cost involved with refining gasoline. Crude cost accounts for less than half of the retail price of gasoline. MAPCO and other Alaska refiners pay fair market value for the crude we purchase and we pay a pro-rated tariff to get it to our refinery. For one of our crude contracts with the State of Alaska, MAPCO pays a \$.15 per barrel premium for the crude oil.

The other costs of refining product in Alaska are all higher than at lower 48 refineries. Electricity is an ingredient of refining and we pay several million dollars per year to GVEA for electricity. We pay twice the cost for electricity here compared to our Memphis refinery. And electricity costs are two to three times higher here than for refineries in the Pacific Northwest. The chemicals, fuel, labor and transportation components of refining and distributing our refined product are all considerably higher here than in the lower 48 states. The average rate of pay at our North Pole Refinery is about \$10.00 per hour higher than for comparable positions at our Memphis refinery. This is a 50% higher cost for labor at our Alaska refinery. Alaska has some of the most stringent environmental standards that impact costs at the refining, wholesale and retail levels. In addition, MAPCO paid a \$30 million quality bank penalty in 1997 for the 600 million gallons of refined product sold, which equates to \$.05 per gallon. Or you can look at the quality bank penalty as adding \$2.10 to the cost of each barrel of crude we refine. The \$70 million jet fuel expansion we are currently doing at our refinery would cost in the \$45 to \$50 million range in Memphis. So it follows that refined product prices will also be higher in Alaska than elsewhere in the Country.

But the prices in Alaska are much lower than they would be without the presence of the Alaska refiners. When I left for college at the University of Oregon driving down the Alcan Highway with Jim Dodson in the fall of 1963, the price of gasoline in Fairbanks was around \$.55 per gallon. We arrived in Eugene, Oregon, and paid about \$.26 per gallon. It was after 1969 when Tesoro started refining in Alaska that prices dropped. In 1978 gasoline was \$.859 in Fairbanks and it was \$.609 in Eugene. The percentage price difference had dropped considerably by 1978. MAPCO started refining gasoline in 1985 and prices dropped again. Today the price of gasoline in Fairbanks is \$1.209 and in Eugene, Oregon it is \$1.109. The gap has narrowed considerably. I should note that today the price of the Fairbanks Daily News-Miner is \$.75 and the cost of the Eugene Register Guard is \$.50. The news paper here costs 50% more than in Eugene, while the gasoline is only 9% more in Fairbanks. I should comment that I think the price of the Fairbanks Daily News-Miner is a bargain and is very reasonable in view of the costs associated with publishing the news paper here in Fairbanks.

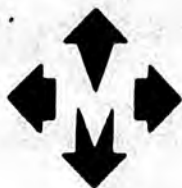
I also wanted to point out that some of the data used in analyzing gasoline prices was not correct as pertains to the Fairbanks and Anchorage markets. The data provided to Senator Frank Murkowski by AAA that was quoted in some news articles appeared to show a price of \$1.269 for Alaska. The Fairbanks price is \$1.209 and the Anchorage price is about \$1.159. So the after tax price of Alaska gasoline is in the \$.89 to \$.94 per gallon range as opposed to \$1.00 per gallon. The price of gasoline in the bush areas is really not relevant to the analysis in my opinion since they can only receive fuel once or twice a year in relatively small volumes.

MAPCO is proud of our refining activity and the positive influence we have had on fuel prices over the 20 years we have operated at our North Pole Refinery. We are proud that in 1998 we supported 688 Alaskan vendors with \$450 million in spending. We spent more with everyone of those vendors than we would have for comparable goods or services in the lower 48 States. But that is a fact of life in Alaska. Our presence here means that \$450 million multiplies around the Alaska economy a number of times and helps thousands of Alaskans directly or indirectly. As an example, we pay approximately \$1.8 million in property taxes that are shared between the Fairbanks North Star Borough and the City of North Pole. Our refining and retail operations employ about 500 Alaskans with a total for payroll and benefits of approximately \$20 million per year. This payroll amount is in addition to the total paid to vendors in 1997.

Attached are three graphs showing that our price of gasoline, jet fuel and diesel fuel have fallen as fast, and in some cases faster, than crude oil prices have fallen since a year ago. We feel we have been very fair and sensitive to the Alaskan consumer, and we pledge to maintain that sensitivity and fairness in the future.

For additional information contact:

Jeff Cook, Vice President External Affairs
MAPCO ALASKA PETROLEUM Inc.
(907) 488-5104



MAPCO ALASKA PETROLEUM INC.

APRIL 9, 1998

Jeffrey J. Cook

VICE PRESIDENT

EXTERNAL AFFAIRS & ADMINISTRATION

Gasoline Price Comparisons in Selected U S Cities

(Price per gallon of regular, unleaded motor gasoline at self-service pump)

ACCRA Cost of Living Index - Second Quarter 1997

SELECTED CITIES-Price w/tax

Anchorage, AK	\$1.32
Fairbanks, AK	\$1.42
Juneau, AK	\$1.44
Kodiak, AK	\$1.66
Bakersfield, CA	\$1.37
Los Angeles, CA	\$1.38
San Francisco, CA	\$1.53
Boise, ID	\$1.35
Billings, MT	\$1.40
Reno, NV	\$1.44

OIL PRICES

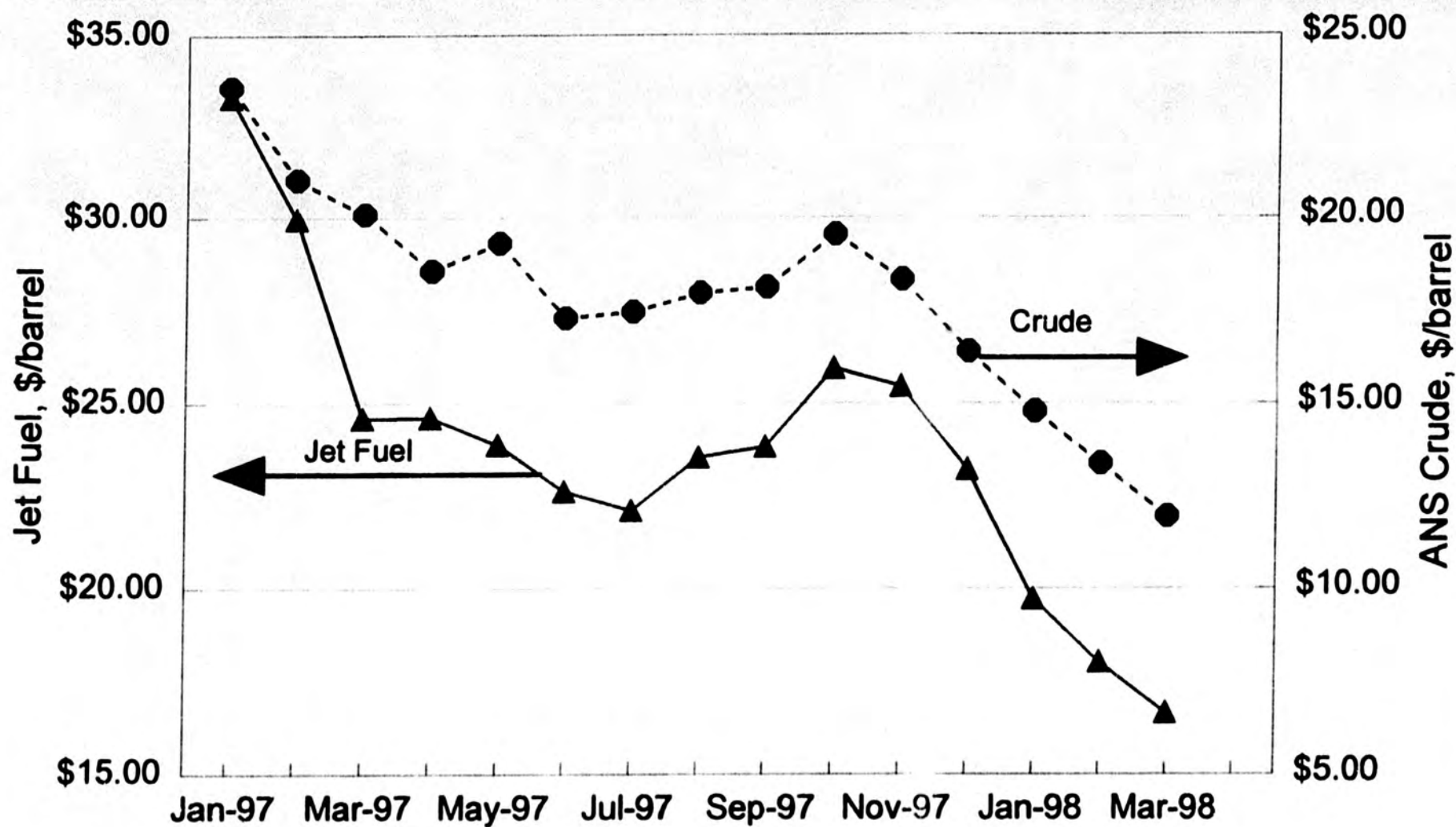
Wednesday, April 8, 1998			
CRUDE GRADES	Wed	Tue	Yr. Ago
OFFSHORE			
European "spot" or free market prices			
Arab 17	10.75	10.66	15.15
Arab 17V	8.75	8.66	12.10
Iran 17	11.33	11.39	15.85
Forties	12.05	12.98	17.45
Brent	12.80	12.71	17.40
Bonny 17	12.83	12.77	17.55
Urals-Vladik	11.90	11.73	16.15
DOMESTIC			
Spot market			
WTI	15.55	15.55	17.75
WTI Sour, Mid (1000-1225)	13.20	12.93	16.92
US SW 37.28 (1000-1494)	14.85	14.53	18.49
US SW 37.28 Pacific Del	12.72	12.62	13.25
Open market crude oil values in Northwest Europe around 17.50 GMT in dollars per barrel, for main loading ports in country of origin for prompt loading, except as indicated.			
REFINED PRODUCTS			
Fuel Oil, No. 2, 15.4 gal.	4283	4214	5044
Diesel Fuel, 15.4 gal.	4423	4359	5200
Gasoline, unleaded, premium	5027	4956	5245
Gasoline, unleaded, premium	5172	5095	5418
Gasoline, unleaded, reg.	4522	4450	5150
Gasoline, unleaded, reg.	4757	4683	5052
Propane, non-het. Mont Belvieu, Texas, 24.1	2828	2828	3481
Propane, wet-het. Mont Belvieu, Texas, 24.1	2813	2812	3472

PRICE OF GASOLINE IN FAIRBANKS ONE YEAR AGO PER AMERICAN CHAMBER OF COMMERCE RESEARCH ANALYSIS SURVEY WAS \$1.42 per gallon. PRICE TODAY IS \$1.21 per gallon. THAT IS A DROP OF \$.21 per gallon.

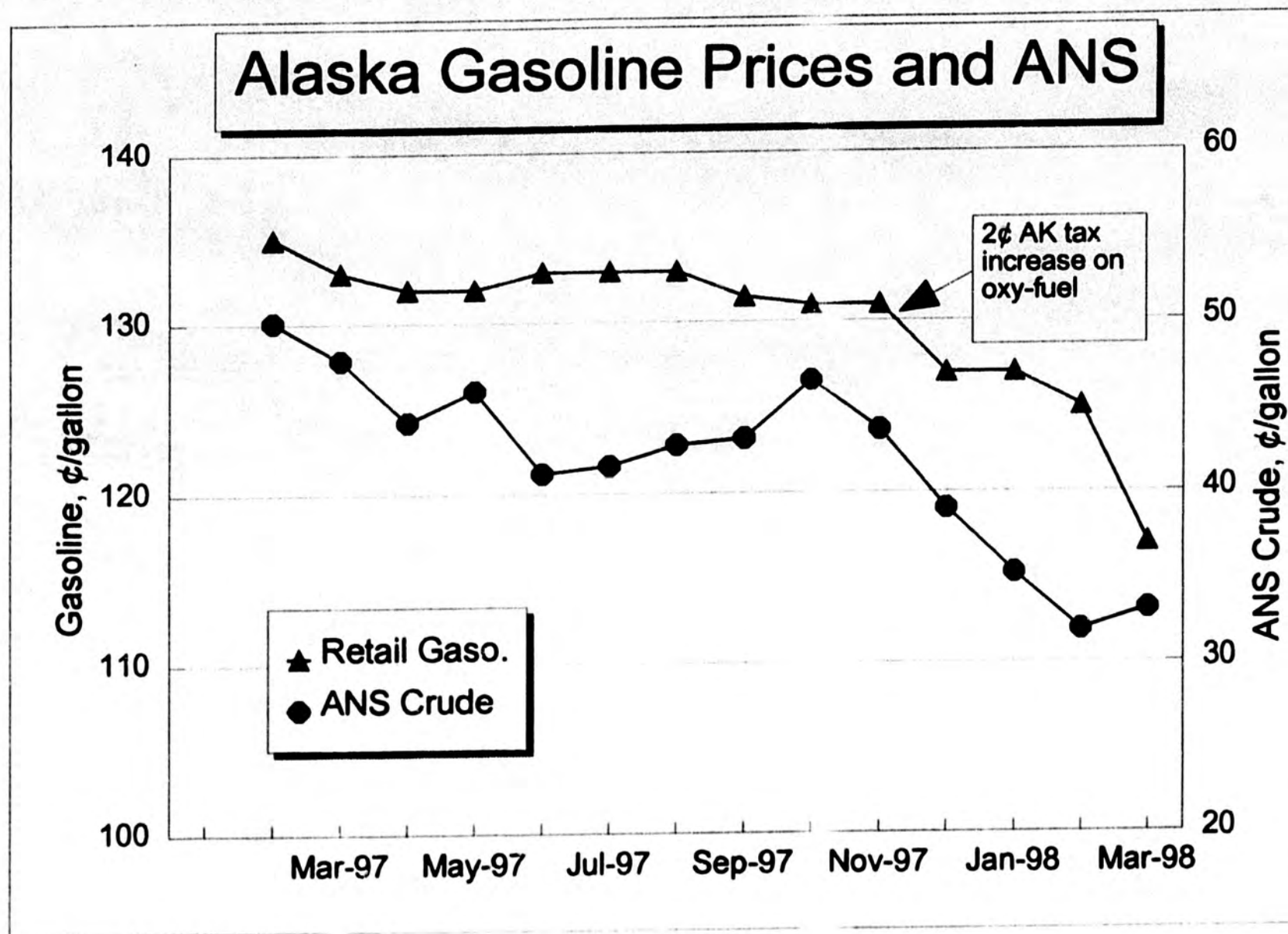
PER WALL STREET JOURNAL OIL PRICES, PRICE OF NORTH SLOPE CRUDE ONE YEAR AGO WAS \$18.20 per barrel. PRICE AT CLOSING 4-8-98 WAS \$12.72 per barrel. THAT IS A DROP OF \$5.48 PER BARREL IN ONE YEAR. IF ONE WERE TO ASSUME CRUDE OIL WAS THE ONLY COMPONENT OF GASOLINE AND THERE WAS A LINEAR DROP IN PRICE, GASOLINE SHOULD HAVE DROPPED BY \$.13 per gallon (\$5.48 per barrel drop divided by 42 gallons per barrel).

ACTUAL DROP IS \$.21 per gallon. PROJECTED DROP FROM CRUDE PRICE IS \$.13 per gallon. RETAIL PRICE HAD ACTUALLY DROPPED FASTER THAN THE CORRESPONDING DROP IN CRUDE PRICE.

Jet Fuel Price at Anchorage International Vs. ANS

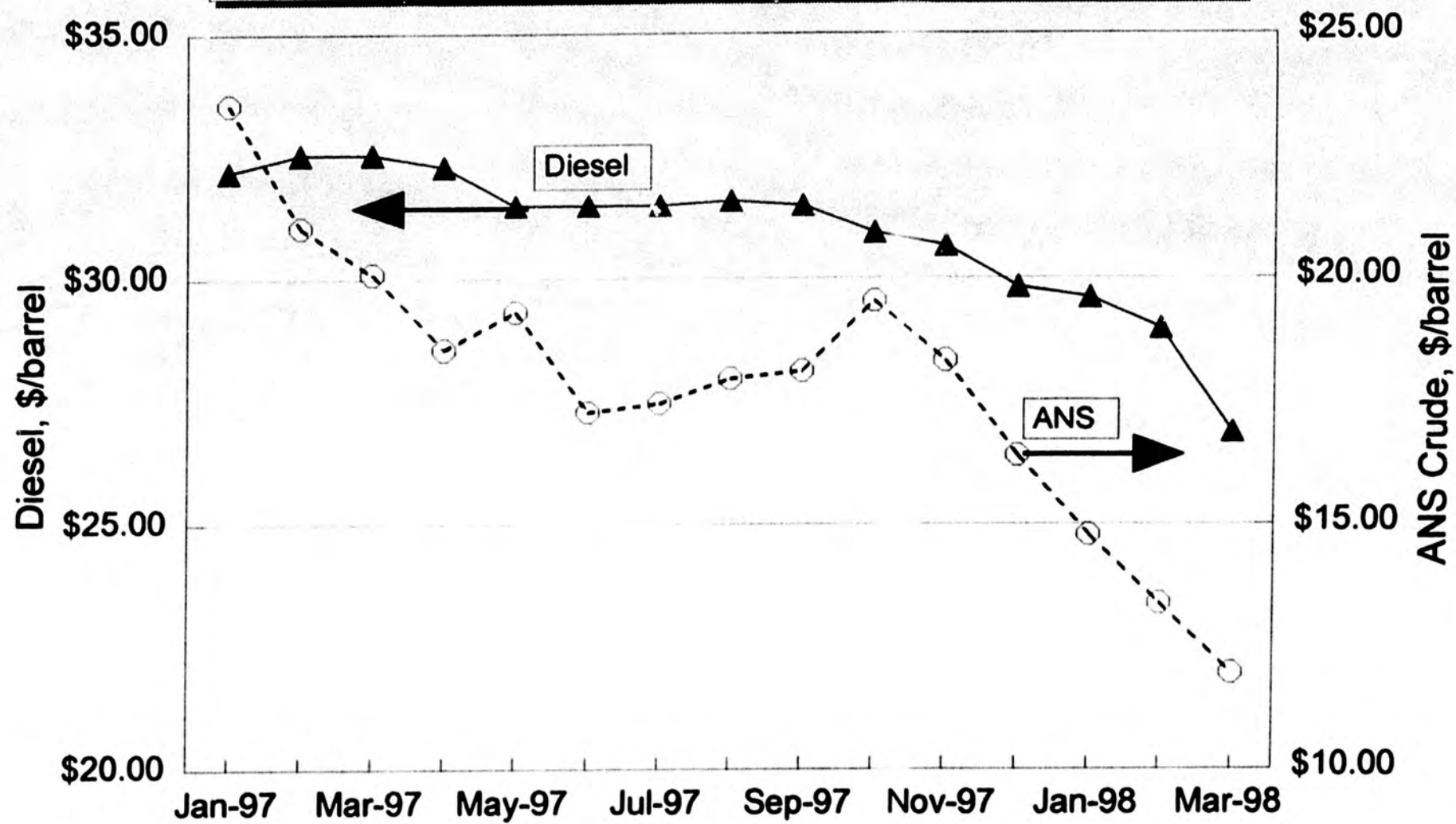


Alaska Gasoline Prices and ANS



03/27/98

Anchorage Rack Diesel Vs. ANS



MAPCO ALASKA PETROLEUM Inc. POSITION PAPER

FIVE YEAR ROYALTY OIL CONTRACT WITH STATE OF ALASKA

April 2, 1998

MAPCO ALASKA PETROLEUM Inc. (MAPI) is seeking ratification of a new five year royalty oil contract from the Alaska State legislature. The contract was unanimously recommended for legislative approval by the Alaska Royalty Oil and Gas Development Advisory Board at their February 17, 1998, meeting. Approval of the contract is now before the legislature in the form of SB 329 and HB 469. -

The contract has been signed by the Alaska Commissioner of Natural Resources and the President of MAPI. The contract calls for the sale of approximately 28,000 barrels per day (bpd) of North Slope royalty crude to MAPI. The contract will be effective December 1, 1998, and calls for MAPI to pay the State Royalty-in-Value price for the royalty oil plus a \$.15 per barrel premium. Over the five years of the contract, the State could receive an additional \$7.665 million in gross revenues over what they would receive from other Prudhoe Bay lessees for the royalty oil.

The effective date of December 1, 1998, coincides with the expiration of a current one year contract MAPI now has with the State for 13,000 bpd of royalty oil. The new contract will replace the volume in the one year contract and add the additional volume to provide feed-stock for the \$70 million refinery expansion currently underway at MAPI. The cornerstone of this expansion is the addition of a third crude unit to the refinery. The new crude unit will begin shipping the additional production approximately December 1, 1998.

The \$70 million expansion project currently has 50 Alaska workers on site. Construction employment will peak at about 375 workers this summer. Over 30 Alaskan vendors and contractors will be working on the refinery expansion. Once completed, the new crude unit will produce an additional 14,000 bpd of jet fuel for Alaska's growing air cargo and air passenger business. An additional 25 rail cars of jet fuel will be shipped daily on the Alaska Railroad from Fairbanks to Anchorage when the project is completed. Local property tax payments by MAPI will increase, revenues to GVEA and ARRC will increase, and vendors and contractors will benefit from both the construction and the ongoing operation of the third crude unit. Also, a total of 19 permanent new employees will be hired at the refinery and the Anchorage terminal to support the production expansion.

MAPCO has refining, marketing and retail activities throughout Alaska. MAPI employs 155 people in the refining and marketing business and about 350 workers at the 28 MAPCO Express retail stores in Alaska. MAPI spent approximately \$450 million with over 680 Alaskan vendors and contractors in 1997. In addition, MAPI provided approximately \$500,000 in funding to educational institutions, non profit organizations and for event sponsorships in 1997. MAPI has its refining headquarters at North Pole near Fairbanks and its marketing headquarters in Anchorage.

For more information contact Jeff Cook at (907) 488-5104