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TRANSCRIPT OF TESTIMONY OF

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March 18, 1978

BEFORE THE SPECIAL COMMITTEE ON ROYALTY OIL AND GAS

Committee:

Senators:

Representatives:
Chairman Bill Miles
Al Osterback
Chat Chatterton
Mike Miller

CHAIRMAN MILES:

Okay. We'll call this meeting of the House Special Royalty Oil and Gas meeting to order. I'd like to welcome the people here in Juneau.

At the Committee table we have Vice Chairman of the Committee, Representative Al Osterback, Representative Chat Chatterton, Representative Mike Miller, House Majority Leader, and myself, Bill Miles, Chairman of the Committee.

Very briefly, I'd like to explain to the people in Juneau that we are tele-conferencing this hearing. What that, in essence, does is make the comments from the witnesses and from the Committee members available live and direct to Anchorage, Fairbanks, and Nome. We have similar electronic networks set up to both listen and speak in those areas.

The procedure that will follow today in this tele-conferencing hearing is we will take testimony from the witnesses in Juneau... all the witnesses who desire to make a statement for the benefit of those in Anchorage, Fairbanks, and Nome. I doesn't look like we're going to have too many witnesses. Then we'll go on equal footing into Nome, Fairbanks, and Anchorage taking one witness from each area.

Perhaps, for the benefit of the people on the other end of these microphones, I'll give just a short recap of what the Committee's done this week. On Monday we held a joint hearing with the Senate Oil and Gas Committee, and the principal witnesses were the ladies and gentlemen representing ALPETCO, the firm with whom the state has a tentative commitment for the sale of royalty oil. On Tuesday we had Commissioner Robert LeResche, the Chief Negotiator for the state, outline his views of the historical aspects of the contract and answer a number of questions relating to certain aspects of the contract. On Wednesday a Legislative Consultant, Milton Lipton, who is Vice President of Walter Levy (indisc.) & Associates, spent the evening with us discussing various aspects of world, national, and state economy, if you like to call it that... and again answering questions about the specific contract and the concept of the proposed contract. Thursday evening we had a marathon session that lasted from seven until eleven in the evening with Legislative Consultants from Battelle Northwest who discussed the issue of the state taking its royalty oil in kind as opposed to the state taking its royalty oil in value. Following Mr. Swift and Mr. Clummett (indisc.) from Battelle, we had Dr. Arlon Tussing, of the University of Alaska, speak to a number of issues related to the sale of royalty oil.

That essentially brings us to today's hearing because, in our unusual wisdom, we decided to take St. Patrick's night off, and I'd like to clear with Anchorage and Fairbanks that I went to bed at eight o'clock. It was a very disappointing St. Patrick's night for me.

Subsequent to this hearing, we intend to go through the specific contractual provisions with the representatives from the Department of Natural Resources, the state's negotiator, as well as representatives from ALPETCO. We also have two outstanding studies that will, hopefully, be in the first part of April. We have (indisc.) specific questions relating to the contract to Battelle Northwest. Additionally, we have a net benefit study in progress by I.S.E.R. at the University of Alaska. Following this week of hearings, we are going to address specific questions, further specific questions, to the principals, both the Department of Natural Resources and the representatives from ALPETCO. Hopefully, we'll be able to get a response within seven to ten days and accumulate all the existing information plus the responses to these questions and the outstanding study and make a decision one way or another on the contract.

One final point before we turn the microphone over to our first witness in Juneau, is, for the record, Dr. Tussing requested that his statement before the Royalty Oil and Gas Advisory Board be included in the record that has been distributed to Committee members and is in the record. Additionally, statements from a Wilson A. Rice and Matthew Berman, Trustees of Alaska and Anchorage, will be included in the formal record of the hearing. With that in mind, we'll turn the microphone and the floor over to Mr. Honig, Chairman of ALPETCO. Mr. Honig.

MR. HONIG:

Thank you, Mr. Chairman.

Representatives Osterback, Chatterton, and Miller, we appreciate the opportunity of appearing before you again after you've conducted a long week of hearings on the Alaska Petrochemical Company project and its proposal to build a petrochemical facility in Alaska to process Alaska royalty oil.

Most of the testimony we've heard this week addressed the risks involved and the rewards for taking those risks and whether the ALPETCO proposal involves any state subsidy or not. I'd like to address these three subjects briefly in rebuttal, and these subjects are the risks, the rewards, and the subsidies.

First, let's look at the subsidies. One newspaper account said the contract includes provisions for both direct and indirect subsidies for the plant. It said that any direct subsidy in the form of a negotiated reduction in price of oil would have to be approved by the voters. But it said the contract also gives ALPETCO an option on seventy percent of any future royalty oil which might be sold cheaper than Prudhoe Bay oil. These are misleading statements in our opinion. ALPETCO's right to up to seventy percent of other royalty oil is neither a subsidy nor does it give ALPETCO a veto on future competition, as has also been said. This Section 2.3 of the contract merely prevents the state, in the future, from engaging in unfair competition. Once ALPETCO's plant is running, if the state should then decide to sell royalty crude oil to someone else at a lower price than we are bound to pay under the contract, then we have the right to that same lower price for that quantity being offered at a lower price than ours. This is only fair, and it's a customary provision in long-term supply contracts.

Regarding the other so-called direct subsidy, the contract makes it as hard as is possible for ALPETCO to ever reduce the price it will pay the state for the royalty crude. Any reduction of the price provision must be approved first by the Administration, second by the Legislature, and, finally, by a vote of all the voters. I fail to see how either of these provisions can be referred to as subsidies.

As Milton Lipton told you, nothing will fly without a firm quantity. The contract must assure availability, he said. Regarding the contract generally, Mr. Lipton also said it was "carefully drawn, imaginative, and favorable to the state." He told the Committee that it represents maximum effort on the part of ALPETCO and the state. ALPETCO is getting no bargain, he said.

Secondly, a lot has been said this week about risks to the state, and less has been said about the rewards to the state. Most things in life involve some risks, in the broader sense, and usually we face some trade-off between risk and reward. It would have been safer to have stayed home this morning, but we took the risk of leaving so we could be rewarded with each other's company.

Let's divide risks and rewards into near-term, say the next five years, and long-term, beyond five years. Near-term to risks have been discussed by your consultants. One felt that ALPETCO might flood the California market with crude oil, undercut prices for the oil, and thus lower the average value that Alaska would receive for its royalty oil and severance tax. This scenario, we feel, is extremely remote. ALPETCO cannot take any crude at all on an interim basis until it has long-term financing commitment for a least one-and-a-half billion dollars and it has at least seventy percent of the plant output under long-term contracts before we can take any crude on an interim basis.

Besides, ALPETCO cannot borrow money to finance interim crude purchases from our banks unless it is already under contract for sale and for sale at a profit. So, it's difficult to see how this is probable at all. The only other near-term risk I recall being mentioned is that ALPETCO might be unable to put the project together within the next eighteen months. This is certainly possible. We cannot guarantee the project will fly, but we're betting several years of effort and at least ten million dollars that it will fly in that eighteen-month period. Suppose it doesn't. On the down side, maybe two years have gone by and Alaska is still without a plant. There is no project, but the state still has its oil and it has spent no money. Where is the risk, then, except for ALPETCO's loss? Some of your consultants have said such a two-year delay might be a plus for the state. The markets may be better by then. So, there's no risk here for the State of Alaska.

On the other hand, what are the near-term rewards? There are two big ones. One is employment and the other is contracting work for Alaskans. During the five-year construction period it is estimated that the construction jobs in Alaska will approximate four thousand employees. The total construction man hours in Alaska is estimated by engineers by over thirty-four million man hours spent in Alaska. Additionally, ALPETCO will make the maximum use of local sub-contracting and local supply firms. Add to these the support jobs and the indirect services, and the near-term rewards are immense.

But the long-term risks and the long-term rewards are the most important. What are these? The worst long-term risk mentioned by your consultants is that the plant will be built and running, perhaps for several years, the one-and-a-half to two-and-a-half billion dollars will have been invested, and then the economy sours, or the petrochemical industry sags, or the big companies somehow squeeze

ALPETCO so that ALPETCO starts losing money and has to shut the plant down. This could happen. It's possible. It can happen no matter how big the company is that owns a petrochemical plant or any other kind of plant, for that matter. But this is not a function of the contract plans proposed. It is a fact of life; a risk we take in pursuit of greater rewards. It's not too probable in ALPETCO's case that that will happen, because for ALPETCO to get financing, it must prove to the lenders that this risk is minimal. But, suppose the completed petrochemical plant does fall on hard times. The State of Alaska takes back its crude oil, in that event. It does not have to give ALPETCO anything. It does not have to lower the price on the oil.... that's up to you. If bad times occur, then at that time, not now, you, the Legislature, the administrative part of the government, must make a decision. Do nothing, and get your oil back, or work with a new owner to operate the plant. But, if you want to lower the price; that is, pay for the crude, then the voters must also approve it after you have approved it. Whatever the risk is to ALPETCO, ALPETCO is willing to take it. We're not newcomers to Alaska. We've taken risks in Alaska before, because we believed in the future of the State.

In 1959 we took a risk in Alaska. We invested sixteen million dollars. It doesn't sound like much today, but it was an awful lot...amount of money then. We invested it in a natural gas pipeline distribution system for Anchorage. This was long before Prudhoe Bay, long before high fuel prices. That project...that investment was so risky that in order to borrow the money we had to get the oil companies who were willing to sell us the gas to co-sign our notes. We didn't have any customers at all to begin with. But, we had faith in the growth of Alaska. We had faith in that project. We took a risk, and we've enjoyed the reward... so have the people of Anchorage and so have the people of Alaska.

This contract is a good contract for Alaskans. It creates permanent jobs...almost three thousand permanent jobs. It creates a large, additional tax base; approximately forty-nine million a year in today's dollars. It creates an investment for almost thirty-five thousand Alaskans to participate in the affairs and the profits of the company. It also provides profits to be shared in an endowment trust for the benefit of Alaska. As Mr. Lipton said, if it comes to fruition, this project has many advantages to the State. Even Arnold Tussing said, it will benefit Alaska if ALPETCO can put it all together. What we ask of you is the opportunity to try. Thank you, Mr. Chairman.

CHAIRMAN MILES:

Thank you very much, Mr. Honig. Questions from the Committee?

I have a comment on the point about subsidy, and we seem to have

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gone 'round and 'round on this before. You stated that this is neither a subsidy nor a veto over future contracts, or words to that (indisc.). I still have a tendency to disagree with you on that. There are clauses in the contract which state that we have to build a (indisc.) tank. I think that one of your consultants priced that at roughly at nine million dollars, and it won't get paid for that until the termination of the contract twenty-seven years down the pike. To me that appears to be a subsidy.

Additionally, there is a specific clause in the contract, and I believe you referred to it, about the...if there is a price change, the Administration, the Legislators, and the voters have to ratify that. Well, the very existence of that clause indicates that in the future there may be a request for a less than in-value price change or reduction of price change. I think we've both discussed this. I'd just like to have those comments on the record, and you are certainly free to respond, Mr. Honig, but....

MR. HONIG:

I'd like to make a comment on each of them, if I may.

CHAIRMAN MILES:

Certainly, Sir.

MR. HONIG:

With respect to (indisc.), I suppose that could be viewed as a subsidy. Actually, the agreement provides that we will repay the State the value of that pack at the end of the contract and at end-of-contract values on crude. So, I really think it's more of an investment of nine million dollars, if you want to look at it that way, than it is anything else.

CHAIRMAN MILES:

Well, you could look at it that way or as a subsidy for twenty-seven years.

MR. HONIG:

Yes, I suppose you can look at it either way. It was considered I think by most as one of the nits in the many, many months of negotiation. It is a lot of money, but it is not a lot of money relative to the amounts we are talking about in the contract.

On the second point about the provision in the contract that any price change must also be...any lowering of price must be voted on by the voters, as you've been told, I believe, earlier this week this provision was insisted on by the Governor, and I think it is significant because, if there were no such provision at all

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in the contract, if the contract were silent on any provision of price, then, as we all know, ALPETCO and the Administration and the Legislature could agree on any term outside of the contract by mutual consent and could modify the contract by mutual consent without every going to the public for a vote. So, the fact that the clause is in there certainly doesn't weaken the contract. It simply says that ALPETCO and the Administration and the Legislature cannot get together and agree on a price reduction unless and until the people vote on it and also approve it. So, I think it's a strength and not a weakness because, as I said, absent that provision, it would be easier to modify the price downward.

CHAIRMAN MILES:

My point in raising the voter approval is not to say whether it's a good idea or a bad idea, it's just to make very clear that the parties to the negotiation, the Administration and ALPETCO, were cognizant to the fact that this request for price reduction is an important part of the contract and that they were very aware of it and that it's a very real possibility. That's the point that I would like to make.

Questions from the...Representative Chatterton.

MR. CHATTERTON:

Thank you, Mr. Chairman.

Mr. Honig, I have in front of me here what is numbered page five of the flash cards that you presented the middle of last week in your direct testimony in support of this deal. The title of it is No Risk to Alaska Performance Bench Marks. I have, since that time, gone through the contract sort of very rapidly, and I could not find there...and I wondered, with reference to that list, at what bench mark, in time, or performance, or commitment do you earn the right to take all or part of the state's royalty oil. When do you qualify to do that?

MR. HONIG:

We qualify to do that after we have obtained a permanent financing commitment for at least one-and-a-half billion dollars. And we cannot take any oil from the state until we have obtained that commitment, written commitment for financing, and have furnished the state with a copy of that commitment.

MR. PRATT:

Mr. Chatterton, specific reference is made to Article 10.2, subsection D...it's on page 32 of the contract.

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MR. CHATTERTON:

All right. As I have said, I have gone through this and I could not see in Article 10.2, subsection D, A, B. C, or on, up through H.

MR. PRATT:

All right. May I take you to page 6? Mr. Chairman, I'm Henry Pratt, for the record...also with ALPETCO. Article 2.2, Initiation of First Delivery, the first sentence says...After the date Buyer has obtained the financing commitment referred to in Article 10.2(3)(d)... So, if you go back to 10.2(3)(d), that's within the eighteen months after the effective date, and (d) is obtain or cause contractually bound third parties to obtain written commitments to lend or invest at least one-and-a-half billion dollars.

MR. CHATTERTON:

In other words, all you have... If I understand, then, all you have to have is a showing that you have people willing to loan you up to 1.5 billion dollars. Is that right?

MR. HONIG:

That is correct; plus the things that would be necessitated in order to get such a written commitment. No lender is going to give a written commitment to lend us or anyone else that much money or less than that much money unless he's sure that he can be repaid, and unless he's as sure as he can be that he will be paid the interest as well as be repaid the principal. So, as we...as our bankers and investment bankers testified earlier this week, they are willing to commit the financing on this project provided we have it put together. And put together means provided we have, in addition to the long-term contract with the state, ratified by the Legislature, we must have contracts to sell the products over a long period of time in order for the lenders to be as sure as they can be that they will be repaid. So, when you get the financing commitment, it says a lot of things, and it provides a lot of security I would think for the state, because the lenders are pretty hard-boiled about lending money.

MR. CHATTERTON:

Mr. Chairman, if I may continue.

Thank you for that. I understand what you say, but you are under the understanding and the state is under the understanding that once you have the showing, the finance ability, the borrowing ability of one-and-a-half billion dollars, why you then have... and under the terms of the contract...the right to take all or

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part of 150 million...150 thousand barrels a day of royalty oil. Is that correct?

MR. HONIG:

Not quite. I think that it's not only the borrowing capability but we must have a written commitment by lenders to lend us that money. Our capabilities could be one thing, but this requires a commitment that we could borrow the money for this project.

MR. CHATTERTON:

All right. You have here....let's go out here eighteen months into the future and you come to our Commissioner of Natural Resources, and there is the Melon or the Hunt Estate, or something like that, says yes; they are willing to proceed to loan you one-and-a-half billion dollars for the purpose of constructing a plant. Now you would say that the Commissioner would look at that and say, here is a bona fide offer to loan one-and-a-half billion dollars. Right?

MR. HONIG:

To build a plant...yes.

MR. CHATTERTON:

To build a plant.

MR. HONIG:

Right.

MR. CHATTERTON:

And, having made that choice with that instrument, you then would say the contract entitles you to start purchasing up to 150 thousand barrels a day of royalty oil. Right?

MR. HONIG:

Right.

MR. CHATTERTON:

Very good. Now, does that have any guarantee, that in itself, that you are ever going to build a plant?

MR. HONIG:

Yes, I think it does, because, like any contract, you can't read any one phrase out of context, and if we proceed with the bench marks, which you referred to, in the contract, and as outlined

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on page 5 of the presentation to the Committee, at that same time, which eighteen months after the contract has been ratified by the Legislature, we must within the eighteen months not only get the financing commitment referred to but we must also have committed to spend ten million dollars, we must have contracts to sell at least seventy percent of the output, we must have completed our environmental impact assessment, we must have filed for permits, and we must have finalized the plant design. Then, beyond the eighteen months, let's say we've done all those things, there's still no plant built, obviously, we have subsequent bench marks provided for in the contract which require us not only to report at intervals to the state on our progress but also to do certain...commit certain acts during the ensuing months. And the next bench mark is at the end of twenty-four months. And it says we must have committed at least one-hundred million dollars, and at thirty months we must have commenced construction. Now, if we fail to do that, then the state has the right to cancel our contract, to terminate our contract, and take the oil back if we've been taking any at all at that time. And the bench marks go on up to seventy-two months, at which time we must have committed at least one-and-a-half billion dollars.

MR. CHATTERTON:

Thank you. Mr. Chairman, if I may continue. Correct.

On page 33 of the contract...it's under 10.2(3)...I can't keep up with myself...but it says within thirty months you shall commence construction of the petrochemical facility.

MR. HONIG:

Yes.

MR. CHATTERTON:

And, I'm not quite sure what that facility is. I would have no question but what for you to continue and, under this contract, you would have had by that time to commence construction of the core refinery unit, which, basically, is to handle...gives you a product slate. There's no question about that. Beyond, other than that point, I see nothing other than the continual commitment of money to the project. Nothing about that it has to be constructed, or completed, or anything.

MR. HONIG:

Well, there is nothing in the contract that I recall that specifically sets forth the exact configuration of the plant. That was discussed; it was considered. It was agreed by all that would be probably unnecessarily restrictive and would not accomplish for the State of Alaska what it was interested in accomplishing.

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And that was to process the crude oil in-state and to add value in-state. And, so, to say exactly how many towers the plant would have or any other details of the configuration was deemed to be unnecessary. And, money talks and for us to invest at least one-and-a-half billion dollars in a plant, in a facility, means that we'd better be able to process something.

MR. CHATTERTON:

Thank you. Mr. Chairman, if I may continue.

I realize we are all honorable men, but I'm not sure that we will be here five years from now. And, I'll be quite frank with you, I'm paranoid...but they tell me that paranoia is the mother of discretion many times...and so we proceed. Now, in quick summary, in eighteen months you have to have a letter from...a letter unequivocably saying that there is a place that is proceeding, willing, at beck and call, to loan you up to 1.5 billion dollars. At the end of thirty months, why you have had to start construction on a core, at least started construction on something. And, as you pointed out, the contract does say that you will have to have about thirty thousand barrels a day ability for in-state sales, as I recall the contract through here. Now, having accomplished all these things up through this point, why you would be in conformance with the contract, you have no question about that.

MR. HONIG:

Right.

MR. CHATTERTON:

All right. Now, in the meantime, you could be taking 150 thousand barrels a day of crude oil.

MR. HONIG:

Once we have the financing commitment.

MR. CHATTERTON:

Once...yes...after the eighteen months period. You triggered that off. And you can be doing this, and you can be doing very well at this, I might add, financially you can be doing very well at this. And you can build a thirty thousand-barrel-a-day refinery, and you still are in compliance, I believe, with the contract. And you can still spend up to 1.5 billion dollars on that whole project. And you haven't gone beyond that. Now, aren't you in compliance with the contract?

MR. HONIG:

Haven't gone beyond what?

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MR. CHATTERTON:

The thirty thousand-barrel-a-day feedstock products refinery and taking 150 thousand barrels a day of oil.

MR. HONIG:

Well, Mr. Chatterton, you are more familiar with the oil business than I, I'm sure, and if we spend a billion and-a-half dollars and all we have is a refinery to process thirty thousand barrels of fuels a day, I think it will be owned by the bank long before we got that far. Now, as far as intentions are concerned, if I may I'd like to call your attention to...on page 14...to the paragraph 4.21 which says Construction Obligations. As I mentioned, we have to read...we can't take things out of context, and I know you didn't mean to. This says - In consideration of the obligations assumed by each party herein, Buyer will proceed with reasonable diligence to design, construct, start up and thereafter initiate operation of a petrochemical manufacturing facility with fuels refining capacity in the State of Alaska. Such facility shall include facilities for the manufacture of energy fuels, aromatics, olefins and, certainly if you manufacture either of those aromatics or olefins, then you are making petrochemicals, and petrochemical derivatives of such basic feedstocks, and will include "offsite" facilities such as power supply, water supply, port facilities and administration buildings. Final process configuration and production rates of the various products listed above will be determined by (i) marketing considerations based on sales contracts for the products and (ii) process optimization of the overall facility design to produce the desired products in the most effective manner. Variations in process optimization will occur throughout the anticipated life of the facility. Such facilities shall be hereinafter referred to as the "Petrochemical Facility."

MR. CHATTERTON:

Okay. Thank you very much, Sir. Thank you, Mr. Chairman.

CHAIRMAN MILES:

While we're on the cost of the facility, how much will the facility cost?

MR. HONIG:

The rough estimate we have, and it certainly should not be confused as a definitive estimate because, as you know, a definitive estimate cannot be obtained until all the products slate is set and we know exactly what will be made, but the rough estimate that we had made by Brown & (indisc.) is that it would cost approximately 2.5 billion dollars. That includes the offsite facilities

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such as the dock, the port facilities, as well as the utility facilities which would be...

CHAIRMAN MILES:

I think there was some confusion a couple of weeks ago about whether it was 2.5 or 1.5. I was confused on it, anyway. I don't know how that happened.

Why wouldn't, if it is 2.5, why wouldn't that expenditure be included in the contract. The contract only states 1.5. And, if we are using these time and expenditure bench marks, which have been very carefully set out in the contract, why wouldn't it go up to 2.5? The reason I ask is that all state revenue estimates that you've provided are based on a two-and-a-half-billion-dollar total project, and we are, by definition in the contract, including the total project costs back to January of '75. But, if the benefits that you cite to the state over the twenty-five or twenty-seven-year period of the contract total 1.3 billion dollars on a two-and-a-half-billion-dollar facility, if, in fact, we don't have a two-and-a-half billion-dollar facility, if we only have a one-and-a-half-billion-dollar facility, our benefits are going to be reduced substantially.

MR. HONIG:

Well, I don't know about the last part of that statement, Mr. Chairman, about the benefits being reduced substantially. There would be some fewer jobs, I suppose, and some smaller tax base, but I don't know whether it would be substantial. In answer to your primary question, there were basically two reasons for not going on and on and on up to the two-and-a-half billion or not making the two-and-half billion required in this time frame. One is that, as Mr. Moore has told the Committee, from Bonner & Moore, that a facility of this size must be phased in. It's impossible to either erect or to start up a refinery of this size and this scale all at once. So it must be done gradually, it must be done in phases. And, for instance, the first phase would be the core refinery which you referred to and, along with that, the required utilities for the larger complex and the port facilities. And the next phase might be an aromatics unit. The next phase might be an olefins unit; the next phase might be another olefins unit, depending upon the contracts for the sale of the product. But, it will have to be phased in, and that was one reason for these numbers.

The other reason for these bench marks being what they are is that in negotiating the contract terms Commissioner LeResche said more than once, do not make the bench marks too optimistic. Set the bench marks so that you, in your own feeling, feel they will be obtainable and that we don't have to go back to the Legislature to revise bench marks. So we hope, I think, to beat all of them

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if we can...to do better than what's set forth here. But that was the second reason for making it a billion-and-a-half instead of two-and-a-half. As a matter of fact, when it gets past the eighteen-month bench mark, if we succeed in...as we and the consultant refer to it...when we succeed in putting it all together, which means we have the sale of the products in long-term contracts. We'll have the design finished. We'll know what we are going to make more particularly. And we have the financing commitment. When all those things are done. From then on the likelihood of it not going forward is very remote because, as I mentioned earlier, the lenders, the life insurance companies who buy the long-term bonds and commit to buy the bonds, are going to be sure that we have the proper engineers, that we have the proper design, that we can sell the products, that we can make the products we're going to sell, and that we'll be able to repay the debt.

CHAIRMAN MILES:

I see. I think you can understand my concern about that, though, because it's a monumental economic decision we're being asked to make and a billion-and-a-half dollars does represent substantial... I think it's substantially less return to the state than two-and-a-half billion dollars. The tax base alone is a substantially smaller figure.

MR. HONIG:

Yes...I can understand that. I think, though, that sometimes all of us can get lost in looking at what's before us, so to speak. And I think we need to back off and realize that the main thing here from the standpoint of the State of Alaska is to add value to products in Alaska. That's the main thing. And when we get into such a detail as the bench marks, while we think they're good to have, they're not the main part of the project. They're just to help us all be sure it goes forward.

For instance, on the natural gas pipeline, I haven't heard any bench marks mentioned. Does it have to spend a certain amount by a certain time? I haven't heard of it if it does. So, I think this contract goes much further than any I've seen. I don't think the Alyeska Pipeline had any bench marks that had to be met by any particular time...any constraints placed on it by the state, that is. So I think...I'm not belittling the bench marks. I think they are excellent. But I think that to quibble about whether it should have been eighteen months, or twenty-four, or one, or one-and-a-half, or two we lose sight of what the main purpose is. And that is to build a petrochemical facility in Alaska to help Alaska.

CHAIRMAN MILES:

Yes. I wasn't quibbling over the six months, but I was quibbling over the thing in dollars, and I think I'm damn well justified in doing it.

MR. HONIG:

I didn't mean to infer you were. I think that from what we hear that to build a petrochemical facility, we'll spend far more probably than the two-and-a-half before it's over.

CHAIRMAN MILES:

Representative Chatterton.

MR. CHATTERTON:

Thank you, Mr. Chairman.

Mr. Honig, I didn't have a chance to thank you for reading that Article 4.2.1. It is certainly the intent, it is your intent, I know, there's no question. It's my intent; it's the intent of the State of Alaska. But, remember my paranoia. And we're down thirty-six months down the line now, after this contract has been signed, and you started construction on a core refinery which can handle thirty thousand barrels a day. At the end of eighteen months you already have in hand the letter that says you have bank (indisc.). You are available at the bank to the 1.5 billion dollars. And, so, here we are merrily going along. You're taking 150 thousand barrels each day of royalty oil.

MR. HONIG:

We may be.

MR. CHATTERTON:

You may be or any part of it. You are, or will shortly, be running thirty thousand barrels a day of it through your core refinery on it's completion and the balance, the remaining 120 thousand, or any portion of it, why...in Article 13 of the contract you can be trading or exchanging any place that you so wish. You're the broker for that. You have title to it, and you're the broker for anything over the thirty thousand barrels a day. That is Article 13 I assure you. It's on page 40 of the copy of the contract I have, which is basically a brokerage clause. If you agree.

MR. HONIG:

I'm sorry. What was the question?

MR. CHATTERTON:

It's page 40. Well, I was mentioning this is a brokerage clause;

It's in the contract. It permits you anything over and above the thirty thousand barrels a day that you're running through the inside-Alaskan refinery, you can dispose of it in any way you wish - sell it, trade it, exchange it. And you have a free hand, do you not?

MR. HONIG:

Not in the...to the extent that I think your question implies. Let's go back to what you termed, and what we termed, the core refinery. I think that we may not be communicating too well there, perhaps.

The core refinery referred to is not a thirty thousand barrels-a-day refinery. The thirty thousand barrels a day item is the minimum amount of fuels we agree, Arctic fuels for Alaska, we agreed we would have the facility capable of manufacturing. But the core refinery, if you have the presentation that you referred to earlier that we made to the Committee on Monday, if you'll look at page 21 of that presentation there is a schematic of the petrochemical facility. And you'll see there that it shows refinery, and it shows going into the refinery crude oil, and it shows coming out the things you mentioned - gasoline, diesel jet fuel, heating oil, and fuel oil. But also out of this refinery you will see that this refinery must also feed the aromatics plant, part of which goes to market and part which goes into the olefins plant, and it also must supply the feed separation plant which goes into the olefins plant.

My point being that, yes, we must have started construction of the refinery. But, once the refinery is built, it will have to serve more than just the thirty thousand barrels. It will have to serve the aromatics plant and the olefins plant. And for us to spend, or invest, a billion-and-a-half dollars in the plant... as I said earlier, you may rest assured that to do it and to live with our lenders...we'll have to build more than just a small refinery to make thirty thousand barrels of fuels.

MR. CHATTERTON:

Thank you. There's no question. I understand that you'll build this in modules and you'll build this refinery, and I'm sure you'll build it large enough to run 150 thousand barrels a day through it. And, until you have the satellite plants, the aromatics plant, and until you have the feedstock preparation plant for the olefins plant, why you're going to ship the bottoms out. They're going to go south someplace. It's obvious. And the products are only going to be used in Alaska to the extent the products can go south.

But, this is the point I'm really trying to get to that bothers me a little bit is...you are, at least at this point, and as I

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see this contract, we have a....and there is no economic incentive despite the border-plate language that our intent is to build. But, right now, there is no economic incentive for you to proceed with putting an olefins plant in or an aromatics plant. You are brokering the oil...

MR. HONIG:

I don't agree.

MR. CHATTERTON:

...you are making the products, and I come to the point that the breach of contract clause seems very weak. To me, I'm no attorney, but to me the state is not suffering any economic loss. I'm hard-pressed to see how the state could ever break this contract.

MR. HONIG:

Well, I think that the point I disagree with you on is the statement about economic requirements, or economic incentive I believe is the term you use. There is every economic incentive for us to build the olefins plant and to build the aromatics plant. You may recall from Chem System's presentation, one of their charts showed the projected rate of growth for basic petrochemicals as compared to petroleum products. And they show that the growth in petroleum products is going to be far, far less during the next ten, fifteen, twenty years than the growth and the need for petrochemicals.

The other thing that comes into play on economic incentive is the fact that less value is added by a fuels refinery, and we must add more value than that, in our opinion, in order to support this project in Alaska. We feel that to build a fuels refinery in Alaska would be marginal at best. And we would have no interest in doing so - to build a fuels refinery only. Because it's by adding the value that not only do we create more jobs and more tax base in Alaska, but we also create a more valuable product so that we are shipping out of Alaska not something that we've converted from $13.00 a barrel to $17.00 a barrel, or $15.00 a barrel. But we're shipping something out that now has a value of $30.00, $40.00, $50.00 a barrel in the form of petrochemical products. So, this is why our economic incentive parallels Alaska's desire.

MR. CHATTERTON:

Thank you very much, Sir. Thank you, Mr. Chairman.

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CHAIRMAN MILES:

On that point about the additional phasing in of various plants... I almost flunked chemistry in high school... The only reason my chemistry prof passed me was that I had to promise him not to take it in college. That's a true story. But are aromatics and olefins solely restricted to crude oil-based processing as a feedstock?

MR. HONIG:

Mr. Chairman, I'd like to preface any answer by almost the same preface you made. I don't think I flunked chemistry but certainly the last time I had it was in high school. I'm not a chemical engineer; I'm not a petrochemical executive. Maybe that's why I'm Chairman of the Board.

CHAIRMAN MILES:

They say that about Legislators.

MR. HONIG:

But, as you know, our Chief Executive Officer is Gordon Cain, who was here earlier this week along with our consultants in the form of Chem System, so I have to preface any answer to say that this will be the blind leading the blind, but I'll try to answer your question with that caveat.

Petrochemicals, I suppose, in the U. S. really got a big start on the Gulf Coast many years ago when natural gas was at give-away prices, and oil companies would build refineries to make gasoline, primarily, and oils that they were interested in. And, kind of a by-product was the gas, which often was flared for too long and is still being flared in parts of the world. And this cheap hydrocarbon, this cheap gas, which, you know, they might pay a nickel in NCF for it at that time, was found to be an excellent cheap feedstock to make ethylene. And so ethylene plants were built. And the ethane in natural gas is still a good feedstock to make ethylene. The only thing that's changed is is that it's no longer cheap and it's no longer plentiful, no longer in over-supply. It's still a good feedstock. However, as I believe Peter Spitz pointed out to the Committee earlier this week, there are petrochemical products which cannot be made from ethylene or from ethane. And to make the full spectrum of petro-chemical products, the feedstock must be oil. I think he also pointed out something that many people don't realize, and that is, I think he said that ninety percent of the petrochemical plants today are being fed by crude oil, not natural gas. But that doesn't mean that ethane is not good feedstock; it's an excellent feedstock for ethane, but it won't make all the spectrum of products that crude oil will make.

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CHAIRMAN MILES:

Well...okay. Let me try it again, because, if you answered my question, I didn't pick it up. The aromatics plant and the olefins plant, that's a vital part of your plant. Can they be provided feedstock by specifically...from, specifically, crude oil or also gas and, or, gas liquids?

MR. HONIG:

Well, I think that the aromatics can only be made from crude oil. Is that right, Mr. Chatterton? We're in your field more than mine now.

MR. CHATTERTON:

I didn't quite flunk chemistry, but I would say the aromatics' basic feedstock would have to be crude oil and not the gas oils - quote, unquote.

MR. HONIG:

And what about olefins?

MR. CHATTERTON:

Olefins, why that's an unsaturated paraffin which would normally be coming from your gas oils or your methanes, and methanes could be constructed from it. Right.

CHAIRMAN MILES:

Okay. The reason I asked the question is I brought it up once before and didn't feel that there was possibly the strongest language possible which requires the actual processing. And I just wanted to...the actual processing of oil in-state, and I just wanted to find out about that.

MR. HONIG:

Well, if you use the terms olefins or aromatics then you're generally considered to be into petrochemicals.

CHAIRMAN MILES:

Both gas-based and oil-based.

MR. HONIG:

Yes.

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CHAIRMAN MILES:

So, that's what you're envisioning then?

MR. HONIG:

Yes. Yes.

CHAIRMAN MILES:

So, that's what you're envisioning, then, is future gas-based petrochemicals and purchase of gas...

MR. HONIG:

No, not necessarily. This refinery is envisioning running on crude oil as a feedstock. And, as Mr. Spitz told the Committee earlier this week, I believe, it would be designed so that it could also use gas liquids if and when any were available also as a feedstock. But it's not...the project is not centered on the use of gas at all or dependent on the use of gas liquids.

CHAIRMAN MILES:

I see.

MR. HONIG:

When you say gas oils that's not the same thing as saying gas liquids.

CHAIRMAN MILES:

I understand that. But, if we can't make olefins with just crude oil, then there at some time has to be...we at least have to look at the purchase of gas and...

MR. HONIG:

No, you can make olefins with just crude oil. You can make olefins with just crude oil.

CHAIRMAN MILES:

Without any gas liquids?

MR. HONIG:

Oh, yes. You can make the whole spectrum of petrochemicals from crude oil. You cannot make the whole spectrum from gas, but you can from crude oil. Crude oil is the broader feedstock.

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CHAIRMAN MILES:

Which excludes...when you define crude oil, then you're excluding the methanes, ethanes, propanes, and butanes?

MR. HONIG:

Yes. Yes.

CHAIRMAN MILES:

Okay.

UNIDENTIFIED SPEAKER:

Mr. Chairman, just a very brief question. I realize that you want to get into the tele-conferencing, and people are standing by patiently. If I could, for just a moment, I would like to pursue Mr. Chatterton's paranoia. As the bumper sticker says, just because you're paranoid doesn't mean you're not edgy. But, I really, for a million-and-a-half bucks you're going to see not just a thirty thousand barrel capacity.

Say you were producing 125 thousand...processing 125 thousand barrels a day. For the entire length of this contract is there anything to keep you from brokering and selling just plain crude oil for twenty-five thousand...for time infinatum?

MR. HONIG:

No, there's not.

UNIDENTIFIED SPEAKER:

So, there's nothing in the contract that absolutely ties down that all the oil that would be sold to your company, even after given a certain amount of even start-up years, would be processed in Alaska. Is that correct?

MR. HONIG:

That is correct, except that, having invested in the facility, it would certainly behoove us to add as much value to as much product as we can in Alaska. And I can't imagine why we would want to broker when we have a facility to make petrochemicals unless petrochemicals, for some reason, fell on hard times. But normally that would also be reflected in the crude oil price. So, I think that it's not likely that we would be brokering crude oil, because we have to pay the state the full price for that, you know...the full price at the time. So there's no windfall here that would cause us to, or tempt us to, want to broker crude oil. As a matter of fact, the only reason that came up in the

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first place is that, as you know, one of our present owners is Alaska Consolidated Shipping, and that's the company that a majority of its stock is owned by six regional native corporations in Alaska. And they became interested when they formed the company almost two years ago, I guess. They were interested at that time in trying to buy the crude oil from the state so they could ship it. They were interested in the shipping, primarily. And the other stockholder in Alaska Consolidated Shipping being Sea Train Lines of New York. And so, they wanted to do the shipping and create jobs for the natives and create profits for the corporation, then, in turn, for the stockholders. And they are still interested in shipping now that they're a part of ALPETCO. And the only reason that we asked for interim crude at all was the thought that perhaps we would be able to maybe sell some to the Federal Government to put in the strategic petroleum reserves, or maybe...there are not many probable sales because of the glut on crude on the West Coast. But there might be some that we can't even think of now. And we would be able to, while we were building the refinery, be able to buy and ship, and sell, some of the crude. And that was the only reason for the provision.

UNIDENTIFIED SPEAKER:

One other final question in that direction. I'm not a member of this Committee, and I appreciate very much the courtesy of the Chairman allowing me to sit in today. And I'm...although I've looked over the contract cursorily, I'm not into it in all the detail that the members of the Committee are.

Is there any prohibition against you selling the crude, for instance, to the Orient? I know that the oil companies that are producing and members of the pipeline (indisc.) cannot, but I'm wondering...I don't know whether the state is similarly restricted or, in this case, the person that the state sells the crude to.

MR. HONIG:

My information is we could not.

UNIDENTIFIED SPEAKER:

You could not. Okay, that's what I was curious about.

MR. HONIG:

That is on the "no-no" list for export, I think...currently on the Federal level, and we could not.

UNIDENTIFIED SPEAKER:

I assumed that was the case, but, as I say,...

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MR. HONIG:

I think it goes beyond just crude oil. I think we could not sell naphtha; we could not export naphtha out of the U. S., even.

UNIDENTIFIED SPEAKER:

Then, one real...last, final question. Getting back to the point on (indisc. - cough) that you mentioned, which is certainly desirable if those are jobs filled by Alaskans...a little less desirable for jobs filled by Oklahomans...

(LAST PART OF TAPE INDISCERNIBLE - END OF TAPE)

(BEGINNING OF SECOND TAPE)

MR. HONIG:

(First part not recorded.) We started it before we were selected - a training program for both shipping and petroleum operations. And we made arrangements with the International Seafarers Training School at Piney Point, Maryland, to take two natives from Alaska as trainees under the sponsorship of our company. And they are rotated and, when they have finished their training, two more will take their place. We also started two natives training at a refinery in Texas, which is about a thirty-five thousand barrel-a-day refinery owned by Sea Train. And we have two natives training there and they, by the way, are getting very good marks. There are very good reports on them. They are interested, and they're applying themselves, and they're learning. And, while those are token amounts as far as people go, it's a beginning. And we, certainly...our intention is to have extensive training programs for Alaskans and to hire to the extent possible in Alaska.

I think we have another motivation perhaps the pipeline did not have, or any pipeline would not have. And that is that we are building a facility in one spot. It doesn't cover nine-hundred or eight-hundred lineal miles. It's all in one place. And, because of that, the history of these plants, as I think Mr. Norris of Brown & Root testified to the Committee this week, the history of this is that when you build a plant such as this a large percentage of the people who work on building it, various trades, end up continuing as permanent employees to work in the maintenance and the operation of the plant. Because they've helped put it together and they're familiar with it and, therefore, they can help maintain it or help operate it. And I think that I heard a statistic that seems to bear this out the other day, and that was that when Collier Chemical expanded its plant on the Kenai eighty-five percent, I was told, eighty-five percent of the additional employees required were Alaskans, which is certainly, I think, a good statistic.

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So we think that for all those reasons because of the native involvement in our company, because of what we want to do, and because of the nature of this animal - the construction being in one place - we think we will be able to realize maximum local hire and do a good job with the training.

UNIDENTIFIED SPEAKER:

Mr. Chairman, may I just offer one comment as an expansion on Mr. Honig's point. This project, we are told by our consultants, and certainly that seems to prove true, cannot afford a high turn-over in personnel. It has to have permanent personnel who are stable. And they've found all over the world that the only stable work force that you can have for a project like this is local people - people who live in the area or people who come from the area of the state that it happens to be in or the country, as the case may be. The transit person has no place in this type of an operation otherwise your operation costs and training just go sky-high.

CHAIRMAN MILES:

Yes, I was thinking primarily of the four thousand construction (indisc.)...

MR. HONIG:

I might mention, in addition to that, we worked very closely with the AFL CIO business agents on this (indisc.)
agents in their recent meeting here two weeks ago did endorse the project and the contract, and they (indisc.) to be satisfied with all the terms.

UNIDENTIFIED SPEAKER:

Thank you, Mr. Chairman. Thank you, Mr. Honig.

CHAIRMAN MILES:

Representative Osterback.

MR. OSTERBACK:

May I thank you, Mr. Chairman. Now, I would like either one of you gentlemen to answer a question. What will your products be - diesel fuel, jet fuel, or...?

UNIDENTIFIED SPEAKER:

Yes. For Alaska we would make Arctic diesel, we would make some gasoline, and fuels for use in the state. Outside of the

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fuels part, we would make the basic petrochemicals, the aromatics, and the basic olefins. And we would make ethylene, we would make propylene, and we would probably make ethylene glycol, we'd make styrene, and we'd make zylene, probably. And then these basic petrochemicals we would hope to be able to bring in plants in Alaska to take those derivative products and make them into a wider range of petrochemical products.

Where this chain stops, we can't know today. But, as you know, a large host of products are made from the basic petrochemicals.

MR. OSTERBACK:

On your fuel, your gasoline, diesel fuel, jet fuel, would you be distributing that in Alaska?

MR. HONIG:

We have said, in our initial application to the state, that we would not...it was not part of our plan to set up a distribution system in Alaska. We would prefer to make those fuels available to existing distribution systems in the state. So, we would make them and sell them to distributors, probably.

MR. OSTERBACK:

Well, the reason I brought this up... Like our airport in (indisc.) Bay when they were using a lot of fuel there - jet fuel- they would have Norwegian tankers and Dutch tankers come in. Are there some regulations between the different countries where they have to take so much fuel from the Norwegian or the Dutch tankers?

MR. HONIG:

Not to my knowledge.

MR. OSTERBACK:

I could never figure out why they'd come all the way over here, you know, to deliver fuel.

MR. HONIG:

That doesn't make any sense. I don't know of any such regulation. I see no reason why they could not use fuel made in Alaska.

MR. OSTERBACK:

Yes. It seems like it would make it cheaper. Maybe they're getting cheaper fuel from over there. I don't know.

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MR. HONIG:

That's a long haul from...

MR. OSTERBACK:

But, they've been coming in there a long time with big tankers. Sometimes we'd have a (indisc.) of tankers. Most of the time it was Norwegian and Dutch tankers.

MR. HONIG:

I see no reason why they couldn't use fuel made in Alaska.

MR. OSTERBACK:

I thank you, Mr. Chairman.

CHAIRMAN MILES:

Mr. Honig, the...I understand that the Department of Environmental Conservation believes an environmental impact statement may be necessary on the project. This is kind of a lengthy procedure; is that going to back you up at all if that requirement comes out?

MR. HONIG:

We hope not, and we will begin immediately on it once the contract is approved. We were hesitant, as were the other applicants, to spend large amounts of money on any phase of the forward movement of the project until the state had made a selection and decided what it was going to do.

CHAIRMAN MILES:

How long might it take in your estimation to (indisc.)?

MR. HONIG:

I think that it would probably take a good portion of the eighteen months that we have to prepare that...to do that. As you know, we have not finally decided on a site even at this point, so it would be impossible to begin that work unless we did it at a number of places until the site selection has been determined.

CHAIRMAN MILES:

Additional questions? Mr. Pratt.

MR. PRATT:

Mr. Chairman, if I just might, with one final remark, call to your

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attention the copy that I think we provided the Committee last Monday - Project Information Submitted to the Institute of Social and Economic Research - will perhaps provide Mr. Chatterton and yourself with better insight to the product mix that we anticipate at this particular point in time. The income statement shows the breakdowns of the olefins, the aromatics, and the fuels. And I think may very well provide you with some of the information you were curious about.

MR. CHATTERTON:

Mr. Chairman. Thank you, Mr. Pratt. I do recall the rather illuminous reports that you have filed along about, I think, October 15th or so, and if you haven't materially changed your product mix, why, I suspect I know a little about what it is. Thank you.

CHAIRMAN MILES:

Are there additional questions from Committee members? If not, it's the Chair's intention to call a five minute recess, and give Mr. Honig a chance to get a glass of water. And I suspect we may have some questions, Mr. Honig, from Anchorage, Fairbanks, and Nome if you could stay around to respond to any statements. It would be helpful.

MR. HONIG:

Be very glad to.

CHAIRMAN MILES:

Are there other witnesses in Juneau that would like to make a statement? Okay. As there are none, I would ask Carol, and April, and Myrtle in Anchorage, Fairbanks, and Nome to stand-by. We are going to take a very short break and will be back and will begin testimony in Fairbanks. We will go to Nome to see if Miss Johnson has any witnesses and then to Anchorage.

It's the intent to take one witness from each of the areas until all witnesses have been heard. So, again, we will start in Fairbanks, take one witness from Nome, and then one from Anchorage. And right now we will take a very short break.

(RETURN FROM BREAK)

CHAIRMAN MILES:

We will call this meeting of the House Royalty Oil and Gas Committee back to order. It's my understanding that there are two witnesses to testify in Fairbanks and one in Anchorage. It's also my understanding that the Fairbanks witnesses have delayed

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attending other meetings to present testimony to the Committee. If there is no objection from Anchorage, I would like to proceed with taking both the Fairbanks witnesses, contrary to what we said before, because they are in a hurry to get to other meetings. Is there any problem in Anchorage, Miss Dickinson (ph)?

MISS DICKINSON (ph):

There'll be no problem, Mr. Chairman. It'll be fine.

CHAIRMAN MILES:

Thank you very much. That being the case, we'll now go to April Moore in Fairbanks with her witnesses.

Miss Moore, if you could, could you give us a count from one to ten so we could adjust our volume here in Juneau?

MISS MOORE:

Mr. Chairman, one, two, three, four, five, six, seven, eight, nine, ten.

Our first witness will be Dr. William Wood, and I'm going to ask him to introduce himself to you at this time.

CHAIRMAN MILES:

Thank you very much. Dr. Wood.

DR. WOOD:

I've just been waiting here, but not patiently, for about an hour and three-quarters. This is a Saturday in Fairbanks with bright, blue skies, and full of sunshine, and the North American Sled Dog Championship, and the Winter Carnival, and I don't know what all else goes on.

CHAIRMAN MILES:

Be glad you have sunshine, Dr. Wood.

DR. WOOD:

(Indisc.), if that's what you were requesting. I am (indisc.) the President Emeritus, University of Alaska. I have read the preliminary ALPETCO proposal with the late John Barber, discussed the details with the Fairbanks Industrial Development Board last summer. I have read the revised and the standard proposal now up for final consideration by the State Legislature. I have examined in depth the rationale behind the ALPETCO proposal and applaud it. I have studied the outline of the contract negotiated

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by the State Royalty Oil and Gas Board. I have not had an opportunity to examine the final contract wording. It's up to the elected representatives of the people of Alaska to do just that.

State Government represents the residents of Alaska. Industry represents stockholder residents of Alaska and elsewhere. Both represent people. The ALPETCO proposal recognizes this fact by showing interest in and concern for people; in particular, the people who choose to reside in Alaska. It states, without fanfare, the advantages to Alaskans of making use of the human value-added concept. What's more (indisc.) in presenting the case where opportunities provided Alaskans by the petrochemical project is not just to earn a living but for the satisfaction of using one's enthusiasm, energy, skill, knowledge, and creatability to good purpose.

The proposed petrochemical project would create nearly three throusand very desirable jobs directly and about seven thousand to nine thousand as secondary and tertiary spin-off, or supporting, services jobs. These jobs are badly needed in Alaska if our present crop of high school and university students are going to have a fair chance to continue to live in this state. I'm particularly aware of this point as I've just spent the week on a project visiting each of the five high schools in this area to talk with juniors and seniors concerning their career plans. This is, part of a local Rotary Club project.

In addition to the jobs I have mentioned, there are also those unknown (indisc.) government jobs, both the necessary and the unnecessary, that will undoubtedly come about as a result of the project. The taxes, local and state, to be derived from the project would be substantial. It would make possible social, educational, and cultural improvements that likely could not be accomplished otherwise.

The day is past when Alaskans can rely upon the fond, but futile, hope that someone will come along to do something nice for us someday. ALPETCO shows concern for Alaskans by proposing to establish in Alaska endowment trust - a charitable trust fund to improve its social, educational, cultural, and environmental conditions in Alaska. This is a generous proposal, and most companies don't make this. You have to go and ask them for contributions to various items of this sort.

The risks to Alaska in processing natural resources in the state, when you gain the tremendous rewards for applying the valued added, are exceedingly minimal, in spite of all the consultants you have heard...exceedingly minimal under the contract that's proposed for approval now by the Legislature. Anyone can find fault with another's proposition. It requires no genius (indisc.), not even very much brain power, and practically no courage. Whether it's one person with an idea and determine to propel that idea into good use, it is easy to find a hundred to find fault with a proposal to say it won't work...and a thousand who would sit on their hands and do nothing. Doing nothing with natural and human resources is a way to remain in colonial status forever. The road to serfdom is paved with doing nothing.

I can be a very suspicious old man where big industry, or big government, or big social, do-good causes are involved. On the ALPETCO project I have no reservation of consequence. John Barber was completely convincing in presenting the initial proposal to us. The improved version, now for a decision, is an opportunity Alaskans cannot, in good conscience, afford to miss. The proposal merits the support of Alaska. Thank you very much.

CHAIRMAN MILES:

Thank you very much, Dr. Wood. Your message is certainly quite clear and convincing.

MR. HONIG:

Mr. Chairman, may I make a comment in response to Dr. Wood?

CHAIRMAN MILES:

Mr. Honig, you have the floor, Sir.

MR. HONIG:

Dr. Wood, you mentioned the late John Barber and I know you felt as we do that there was no one who was more dedicated, or determined, or energetic, or enthusiastic than he was about this project. And, you'll be interested to know and we so informed the Committee on Monday that it is our intention to name this refinery in memory of John Barber.

DR. WOOD:

I'm delighted to hear it. He was no one's fool. I don't think this was his idea originally, as he explained it. But, as he worked on it, the idea grew upon him. He saw its possibilities, and he dedicated himself to it. And I admire a man of that caliber.

MR. HONIG:

We all do.

CHAIRMAN MILES:

Dr. Wood, one final comment...Bill Miles speaking. I would like to make you and other Fairbanksans aware of the statement that Bonner & Moore, the consultants on this project, have made concerning

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the petrochemical refinery, and I'll quote directly from their report. This is a quote: "If the state were to award a royalty oil contract to a group proposing to build a fuels refinery, then royalty gas could be considered independently. If the state were to award a royalty oil contract proposing to build a petrochemical refinery, then it should be understood that natural gas liquid availability, at the right price, would likely require that the oil project be abandoned or converted to the use of natural gas liquid if that option were within the power of the state." End of quote.

I think that residents of Fairbanks, as actively in pursuit as they seem to be of various options concerning the development of the gas industry, should be aware of that finding by the consultants.

DR. WOOD:

We have a small refinery here at the North Pole; one which is taking care of local needs, and the products come from the refining of the crude, twenty-five to thirty thousand barrels a day, and that will go up, we think. And we're delighted with it, frankly, and we hope that it will continue to be the success it has every promise of being.

Now, we're deeply interested in the gas fuel of petrochemical development in Alaska, and we realize that this is complementary to the development of the petroleum fuel petrochemical plant that is under consideration now. And I don't see that there is any conflict that they'd have to work together. And I don't see where you would have to shut one down once the other one began. I've not found anyone that I've talked with in the petrochemical field that would say that this is so. I've talked with people from Dow and some of the other major petrochemical companies, and that isn't their opinion. I don't (indisc) Bonner & Moore make this statement; perhaps I don't quite understand all of the nuances of what they've written. I've read the statement.

CHAIRMAN MILES:

It's certainly not my intention to debate the issue with you or anyone else, but it is a statement by the consultants and we have a responsibility to take all information into consideration before making that decision. It's a statement which directly affects Fairbanks.

DR. WOOD:

Well, if the project is good for Alaska, it will be good for Fairbanks. I think we are determined to see that that's true.

CHAIRMAN MILES:

Thank you, Doctor. I think our Representative Chatterton would

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like to make a statement. Representative Chatterton.

MR. CHATTERTON:

Thank you, Mr. Chairman. Good day, Dr. Bill. How're you doing?

DR. WOOD:

Very fine, Chat...very good.

MR. CHATTERTON:

Dr. Bill, I am sorry that my hopefully searching and not nit-picking questions were causing you to wait impatiently, but let me ask you one question.

DR. WOOD:

(Indisc.) is equal, and we could read your discussion. I wasn't just spending a Saturday afternoon listening to the hearings, I wanted to have something to say in the hearings 'cause that's what I thought the exercise was all about. I must have misunderstood.

MR. CHATTERTON:

That sounds fine. No question in your mind, why, whatever we do down here you want to see it done in the best interest of the people, I guess, of Alaska. Right?

DR. WOOD:

(Indisc.), or we'd change voices.

MR. CHATTERTON:

Sounds great. Have a good day, Dr. Bill.

DR. WOOD:

The same to you, Sir.

CHAIRMAN MILES:

At this time, April, can you bring the second Fairbanks witness forward, please, and ask him or her to state their name for the record?

MISS MOORE:

Mr. Chairman, our next witness will be Mr. Terry Palczer.

MR. PALCZER:

Thank you, Mr. Chairman, and Committee members for the opportunity to testify, finally. I, too, have been waiting impatiently but enjoyed Mr. Chatterton's searching comments on the contract.

I will preface specific contract provisions with a few general comments.

CHAIRMAN MILES:

Can you state your name for the record, please, Sir?

MR. PALCZER:

It has taken considerable effort to produce these contracts, particularly the sales price...

CHAIRMAN MILES:

Excuse me. Can you please state your name for the record, please?

MR. PALCZER:

Terry Palczer, Fairbanks, Alaska.

I will preface specific contract provisions with a few general comments. It is (indisc.) the administration has undertaken considerable efforts to produce these contracts, particularly the sales price provision for Legislative consideration. And, for that, the Administration is commended. Public input would have been appreciated in the administration's negotiation stages. It is recognized that this Committee, the (indisc.) Committee, or the Legislature must either approve or disapprove the contract's (indisc.). It is also recognized that an expeditious recommendation by this Committee, (indisc.) Committee, and/or Legislature could be incorporated by the administration, the Royalty Oil & Gas Advisory Board, and ALPETCO with due consideration and speed. With a considerable amount of give and take, and through verbal negotiations, it is unconceivable that the working relationship that exists will expedite any proposed modifications to the contract.

The (indisc.) to specific provisions (indisc.), the following comments were presented. Article 2.2 Initiation of First Delivery recommends that deliveries start concurrently with the operation and production of the first phase of the petrochemical facility. Article 2.4 Buyer Option in the Event Certain Quantities Not Delivered. I question the obligation of future royalty oil by negotiated sales rather than through competitive processes. But also ask, if this provision is included in the ALPETCO contract, that the NPR (ph) contract, North Port Refining (ph) contract, is also strengthened with these guarantees.

Articles 4.2 and 4.3 - Construction Obligations and Production of Energy Fuels for Intrastate Use. I interpret this to mean that the minimum requirements are to provide facilities for a thirty thousand-barrels-per-day fuels refinery. I question whether this necessarily obligates ALPETCO into the long-term 1.5 billion-dollar investment.

Article 4.2.2 Siting of Petrochemical Facility recommends a change in the time limit for the Commissioner and ALPETCO to select site. It presently reads that in a succession of (indisc.) each selection has as much as a six months' delay. Specifically, the Commissioner must respond in ninety days on each specific site selection, and ALPETCO, in turn, has another ninety days to respond ad infinitum. There is no time limit in that respect.

Article 4.4 Establishment of a Charitable Foundation. I suggest that the contributions begin upon financing production instead of ten years after production starts. (Indisc.) in the future, potentially in the middle nineties.

Articles 5, 6, 7, 8, and 9. I think that the basic (indisc.) for having accounting procedures appear to be complete. As provided by Article 2.2 and Article 13, ALPETCO could potentially become an oil broker (indisc.) at the citizens of Alaska's expense.

Article 10.2 (10) suggests re-modification. There is too much latitude for delay, plus the opportunity to re-negotiate the terms of Article 10.10...excuse me...Article 10.2. Specifically, if you add up all the time frame that the Commissioner has for planning delays, there are fifty-two months of potential delay in the over-all project. What if the time required for delay potentially happened from (indisc.).

Article 10.3 Termination by Buyer suggests a change to a (indisc.) termination with only two sites selected...that's the present terms... with only two sites selected. This suggests a modification along with 4.2.2. of the considerations previously discussed. This one refers to ALPETCO has the option, terminate its agreement, along with other agreements, after two sites have been turned down by the Commissioner. There is no consideration by the buyer for premature, which I interpret as premature, termination.

Articles 11 through 24 (indisc.) comment except with Article 13 in regards to the offering of oil.

Article 25.2 Local Training suggests that a change be incorporated; that there should be a continual program of local training as job opportunities permit. The natural limitations do not adequately address this program. Potentially, ALPETCO would not have to expend any dollars if outside sources materialize in sufficient quantity.

Finally, I have just a few editorial comments. The contract (indisc.) described is offering no risks (quote-unquote) to the

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State of Alaska. I propose that a risk associated with the failure of the added value concept to create benefits to the people of Alaska is of concern. The strengths of the contract are in the oil pricing, billing, and accounting procedures rather than the insuring of no risk of jobs, benefits, etc.

Additional covenants, similar to Article 5.5 Covenant to Aid in Obtaining Governmental Permits to assist in the other (indisc.) of the project - for example, to assist in feasibility financing, to assist in locating a suitable site without trying to find out if there is a site that's (indisc.) a suitable site, to assist in minimizing the risks that do remain - the one of non-performance. I'm concerned that ALPETCO may opt out of the agreement. Essentially, (indisc.) these agreements are (indisc.) to purchase for a more profitable adventure such as petrochemicals and natural gas liquids feedstock. The (indisc.) being buying time by the administration in an election year promoting development and of ALPETCO having an edge in future ventures as described above. (Indisc.) constructive (indisc.), the intent being to strengthen the (indisc.) and ensuring in-state profits of the royalty oil.

Hopefully, the recommendations of this Committee will serve to not necessarily approve the contract, due to scare tactics of some that any modifications will kill the agreement, but to act in the full interests of the people of Alaska. Thank you very much.

CHAIRMAN MILES:

Thank you very much, Mr. Palczer. Are there comments or questions from the Committee?

Thank you very much, April. We certainly appreciate the comments from Fairbanks. As usual, they are to the point, direct, and most interesting and helpful to the Committee deliberation. If there are no further comments from Fairbanks, we will now switch to Carol Dickinson (ph) in Anchorage.

Carol, can you come in, please?

MISS DICKINSON (ph):

Yes, Mr. Chairman. We have just one person wishing to testify, Mr. Jerry McCutcheon.

CHAIRMAN MILES:

Thank you. Mr. McCutcheon, you may have the floor, Sir.

MR. MCCUTCHEON:

For the record, my name is Jerry McCutcheon.

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If this is a preliminary hearing to obtain data on the irregularities of the contract negotiations and send it back to the administration, this doesn't make sense. But if this is a hearing in which you are going to say you approve totally, then it's a little (indisc.) from the public to (indisc.).

If we have (indisc.) follow the pattern of another El Paso gas bill, and another Cooke Inlet land swap where the State of Alaska got bilked out of about five billion dollars of minerals. I fail to see why this contract is before the Legislature. I have it on reasonably good authority that the contract is still under negotiation as late as the early part of this week. (indisc.) the contract really doesn't belong (indisc.).

Next, the law says, not just one but many times, the Commissioner must have prior written permission for (indisc.) in the contract. And, if you are going to accept that, it seems to me we should (indisc.) a law, if we shouldn't sit there and say...well, the law doesn't really mean what it says, (indisc.), it means something else because there's a lot of things somewhere else that say something different. I think we should really get the clear intention (indisc. - cough) that read the law. Otherwise, we are going to render our laws and our contract negotiations meaningless, and anyone in the future who (indisc.) Alaska is going to realize that they are not going to be able to negotiate a law, or (indisc.) a transaction, because somebody has probably already gotten the inside track. And, if that happens to be them...it's great, but, if it's not them, why they're going to be out.

There are legal questions over prior written permission and then there's a legal question over the sale of oil from yet undiscovered oil reserves. I won't go into it too far, but you have a staff and I suggest you look at those. And, if you have doubts, then hire an independent expert, one who's really independent, and render an opinion. Not like I've seen some other people (indisc. - cough) on the El Paso contracts where the other consultants were hired to render opinions which were favorable rather than which were more factual and representative than a broad section of opinion might be had in the market place.

I can find no evidence that the Royalty Board addressed a number of various issues that it has supposed to have addressed before approving any contract. I think there's six, or seven, or eight various items that (indisc.). I can find it in none of (indisc.). I don't know whether it can be found in writing as to what determination has been made.

There is substantial evidence that the negotiations were other than an arm's length transaction. The obtaining of a (indisc.) public opinion poll that should publicly be receptive to less than a fair market price for a (indisc.) to promote a plant in Alaska. Then all the participants were told that only fair

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market price would be accepted. Well, then, there was one who was encouraged to submit on the basis of being able to go to the public and obtain a reduction. You can be sure they will go to the public. They'd be damned fools if they didn't. (Indisc.) it's a corporate interest once they have started to maximize their return and their yield and (indisc.). You have six regional corporations, I understand, and you have the (indisc.) at which the plant is located, then you have the region where the plant is located, all of which would be affected by the plant. And if a state-wide candidate were to have that many votes in his pocket, he would be unbeatable. But, it's worse than just that. There is no other candidate. It would be a one-man race with no opponent, and millions of dollars would be dumped into the election. And that combination should not be permitted to happen. If you're going to rubber-stamp this contract, at least change that section of the contract so that as much money must be spent in opposing any reduction as is spent for.

The (indisc.) that appears in the contract does not change (indisc.), serves notice (indisc.) the State serves notice, and there is no (indisc.) but it's going to take oil. And, after it serves the notice and the (indisc.) is now beginning to take it on, then a court suit is mounted, and ALPETCO is prevented from taking the oil, and the producers have made other arrangements, are we going to be in the same jackass position that we got into in Anchorage International Airport after the Hammond administration destroyed the prettiest stand of timber in Anchorage to build a runway which is scheduled to be abandoned in 1990? And now the State has brought the proceedings, and we'll probably lose Federal financing for the project.

I think the risk here to the State of Alaska is just far too great to bear. The contract should be returned and no negotiations re-opened. If ALPETCO has really made the best offer, and is sure of itself, it would surely again win the contract. They are not sure, and they know that attending the special (indisc.) at less than arm's length transactions would not...they would not be able to gain those advantages again. At this time, I think giving the same conditions which ALPETCO's got the contract under, I think we'd see far larger and more knowledgeable bidders enter the arena.

Again, I can't see the hurry on the...with this project or this contract. (Indisc.) here (indisc.), I guess we used to call it (indisc.) scouting services, a remark by Fish & Game. Fish & Game seeks to (indisc.) on the selection of a refinery site. The Commissioner of Fish & Game, Ronald (indisc.), has recommended that the State delay for two years the decision on a refinery site for processing Alaska's (indisc.)royalty share of Prudhoe Bay oil. He said the delay would allow the completion of the environmental studies to determine the effect of the refinery's

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discharges on the fish. (Indisc.) said he told Commissioner of Natural Resources, Herbert (indisc.), in a recent memorandum that the studies are needed to evaluate the potential effects of waste (indisc.) on fisheries and biological productivity of a potential site. The Commissioner of Environmental Conservation, Ernest (indisc.), noted his department would issue such permits for such studies, as (indisc.) opinion will be considered along with those of other agencies as well as the general public. He also said he believed the State selection will be made on criteria other than water (indisc.) if water (indisc.) the issue.

Well, if we're in good company (indisc.), I don't see why we can't take a couple of months off and do this thing right instead of all the (indisc. - cough).

With the letter of financial commitment, I thought of the very kind of letters that came...internal letters that came by the State and the City of Valdez when prospective bidders on land in Valdez... and they are totally meaningless. What they do is they go get a letter and then they go get another letter, which they don't make public, and it tells the bank that they're all sewed up. It's done all the time. And I think you're going to have to get that part of the contract very iron-clad and it's going to have to be under oath and the bank's assurance for committing. It's no trick at all to get those kind of letters of commitment.

Then there's the subject of...that was raised here about flooding (ph) California's oil. California is already flooded with sulfur (indisc.)...sulfur-content oil. And oil wells are already being shut-in.

There is a possibility that Alaska's products, or Alaskan production, may be curtailed (indisc.). The Carter Administration may be forced to relent and allow an oil trade to Japan or Canada. I think Mr. Chatterton probably apprised you more of the situation when the question was raised (indisc.) oil and gas (indisc.).

The trade question, I'm going to open a crack in the door now, raises the question what will happen if the trade is allowed to proceed. Would the so-called enormous profits then inure to ALPETCO, or would they inure to the State? Second, it is my guess that if the Legislature would go to the President and get a concession for the state's royalty oil, and (indisc.) the state's royalty oil, I'd think he'd more than welcome the chance to make the exchange. Or at least...it would help him escape from the situation that is now out on the West Coast or which could ameliorate the growing glut on the West Coast. I wouldn't go to a Congressional delegation. I'd get a consultant like (indisc.) Doscher (ph) who'll (indisc.) a compre-

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hensive docket (ph) and (indisc.) delegation from the Legislature to raise the questions of the draft and let them take along their expert.

I would also like to note at this time the Doscher and Dougherty Report which the Legislative Affairs (indisc.) distributing is not the final draft. And I didn't know that until yesterday. (Indisc.) parts of that report (indisc.) the draft (indisc. - fades).

Returning to the contract at hand, I find no indication that a plant with gas liquids was considered versus the plant based upon oil. And, if we're going to be again in the position of where we only have one plant, then shouldn't we take the best one we can and run with that? It is my understanding, and this I just heard again when Mr...Chairman Miles quoted from the Bonner & Moore Report, and that's not my source, that a plant based upon gas liquids would drive a petroleum-based petrochemical plant - if they were both located in Alaska - right to the wall. And, if this is true, and again (indisc.) that they are located in Fairbanks, are we Alaskans going to have to subsidize ALPETCO? Or will the State be willing to.....would the State be willing to subsidize ALPETCO, in this case? Or would ALPETCO, having been on the scene, being given the possibility of a State subsidy, preclude the possibility of a gas liquids plant? I think this becomes important, because we have, at this juncture, an outlet for our royalty oil. While we may not be getting very much for it, far less than was ever anticipated, that is the problem of the Administration and the Legislature. But it is probable. The question about the gas liquids.... We do not have an outlet for our gas liquids at this time. And at what the market might be, I think it's very important, and (indisc.) the Bonner & Moore stage and (indisc.) variety studies, it appears that the shipping of the gas liquids and their shipment to an area such as Fairbanks is still, at this juncture, an economic possibility... with or without a gas line, and I don't think that gas line is ever going to go.

I appreciate Mr. Chatterton's remarks the other day. (Indisc.). This question of having one competitor like ALPETCO and another competitor, say like a plant based on gas liquids, which is un-subsidized, raises the question - should the State of Alaska engage, or allow itself to be engaged in such a manner that it enters the private arena in private enterprise? It (indisc.) to subsidize one competitor against another competitor, of both in the same state? (Indisc.) of gas liquids, but apparently we have another one of the competitors which is interested in this project, and wasn't expected, is about to proceed purchasing oil from the North Slope producers and have built a plant in Valdez. But the State, in view of that, still belongs in the business with the possibility of allowing a subsidy at a later date.... and subsidizing one competitor against another.

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We have questionsnot only about possible dishonesty in the way the contract negotiations were handled, we have philantropical questions about possible subsidy and the role of the State as subsidies and I'd like to return now to the question of future reservoirs. It seems to me that it says here supply. Supply means that amount of oil or gas that is reasonably anticipated to be producible and deliverable from (indisc) known reservoirs when a specific time period approved by the board (indisc) this section. If you think and quickly run on your computer, you will find that 150,000 barrels a day for the life of this contract would run to 1.4 billion barrels of oil. Now the operators on Prudhoe Bay despite all their balleyhoo and State of Alaska's administration of Natural Resources balleyhoo, is only (indisc) to produce 6.5 to 7 billion barrels of oil. The royalty share of that is a little something less than 900,000,000 barrels. That means that this potential of another 600,000,000 barrels open here . I'd like to know where it's going to come from. Is it -- there's a total lack of appreciation of what the (indisc) reservoir really amounts to and just how large and big it is. That reservoir is the crown jewel of the western hemisphere is the biggest one we have ever found. There are oil fields that are larger in the western hemisphere than that, but the single reservoir of that kind of oil is not. The probability -- there is no probability that the State of Alaska has found another one on its land. It (indisc) less to do about it and there are other rumors that there might be one under the Arctic Wildlife Range, but that -- concocted by myself and Less Gregg (ph) in Don Young's office about 4 years ago. So I really don't think so. It's just (laughter) (indisc) certain issues. From 1970 to 1976, we only found 2 billion barrels of oil in the United States, that's all. So for the next 7 years we quote (indisc) rate, if all discoveries were to be found in Alaska, we could not reach the requirement for this bill, the one-eighth or 2 billion, Or 250 million barrels and you are still substantial (indisc)

It just doesn't seem to be very real. Even if you projected this on to the necessary amount of decades, that it would take, it literally is committing the State of Alaska to all the oil they get in the future. And I don't think that your -- the State of Alaska is ever going to find enough oil to actually satisfy all the requirements that this contract may imply and probably get -- and for the most probable implications which will occur from it because of the (indisc) go to get a reduced price in opening up the contract negotiations again.

I think I'd better quit at this juncture. Thank you very much.

MR. CHAIRMAN: Thank you very much Mr. McCutcheon. Are there other witnesses Miss Dickinson in Anchorage?

MISS DICKINSON:

No, Mr. Chairman. There are none.

AGO 559462

CHAIRMAN MILES:

Well, thank you very much Carol in Anchorage, and April in Fairbanks. We certainly appreciate the time that the witnesses put in the unexpected delay and certainly feel their testimony was valuable and with that we'll sign off on the teleconference portion of this hearing. Thank you again.

UNIDENTIFIED SPEAKER:

Bill, do you have a question for the (indisc) ?

UNIDENTIFIED SPEAKER

There is one question. Where'd she get the idea this contract is still under negotiation?

CHAIRMAN MILES:

Would you like to raise that?

UNIDENTIFIED SPEAKER:

Yeah, why don't you ask that.

CHAIRMAN MILES:

Carol, in Anchorage, are you still there?

MISS DICKINSON:

Yes.

CHAIRMAN MILES:

Yes, there's one question that Representative Chatterton would like to raise, with Mr. McCutcheon. Is he still there?

MISS DICKINSON:

Yes he is.

CHAIRMAN MILES:

Okay. Representative Chatteron.

MR. CHATTERON:

Thank you Mr. Chairman. Jerry, a quick question. You mentioned at the start of your testimony there something about the contract still being under negotiation. As far as I think any of us here understands, why that is negative. We've got a firm thing before us that we're reviewing. I hope there isn't anything

AGO 559463

f lowing. Could you sort of enlarge on that comment please?

MR. MCCUTCHEON:

Well, this is one of those things that I heard from a very reliable source the other day at the Royalty Oil and Gas Board Hearing and I'd rather not go beyond that. You can check it out for yourself. You'll know if all of a sudden you wind up with a slightly different contract in your hand or the best way I suppose is to call the administration before you and ask them. But I'd certainly -- I'm just passing a little heresay information and I'd rather not go beyond that.

MR. CHATTERTON:

Thank you Jerry, very much, I appreciate it.

MR. MCCUTCHEON:

You're welcome.

CHAIRMAN MILES:

Are there other questions for Mr. McCutcheon? Thank you again Mr. McCutcheon and Carol. We appreciate your time and to you also April and the witnesses in Fairbanks.

MISS DICKINSON:

Thank you Mr. Chairman.

CHAIRMAN MILES:

If there's nothing further then to come before this committee, we'll be placing an ajournment motion shortly. Do you have a final comment Mr. Honig.

MR. HONIG:

I think Mr. Pratt may have.

MR. PRATT:

Yes, I've turned this off. Mr. Chairman, if I might, just a very brief statement that I had not intended to give, but I think that it is appropriate. Should this be on or off? I think it's interesting to note that no one in our group and no one in the administration has used any scare tactics and I don't believe there's been any hurry before the legislature, at least not on our part. But I think it is significant to recount somewhat the history of a few items. And unlike the royalty gas contracts the entire process of sale leading to the resolution before you, has without question been the most thorough over an extended period of time of almost a year, with substantial public participation, administration participation, and legislative participation. The State Energy Policy Committee with you as Chairman, Mr. Miles, and five other members of the legislature began its participation in the royalty oil sale early last fall and continued until January of this year. On December 6 the Energy Policy Committee made 11 contractual recommendations to the Governor. The specific recommendations included 11 different clauses in the contract. In addition you made 6 policy recommendations. All of this input was not available to the negotiation of the gas contracts last year and in addition, the Energy Policy Committee, I believe, adequately kept the members of the Legislature informed on on-going negotiations of the various proposals including the various contract proposals. I personally feel the Legislature should be commended. It was the Legislature last year which directed the role the oil should be taken in kind and it was the Legislature which established the State Energy Policy Committee. For the first time Alaska has a framework for an energy policy plan and for the first time the Legislature has had considerable input into a royalty sale of natural resources.

The royalty oil contract before you between the State of Alaska and Alaska Petrochemical has great potential for the people of this state and the several thousand permanent new jobs and the millions of dollars of tax revenues, the endowment trust and in providing new industrial base of development for the state. All through what we in ALPETCO consider to be a non-subsidized, no risk contract. This Legislature has the unqualified opportunity to be the first in Alaska's history to lay claim to having established the first major industrial base for a stronger and more stable future. I think that with those remarks, I am not urging you into any action. I'm sure that you're going to take a great deal of further consideration. But I do want to remind the committee, and more particularly the public, that the Legislature has been working on this diligently for some time and I'm sure will continue to work on it for some time and I would not like the impression left that you did not know what was going on and nobody else knew what was going on throughout the last 12 months.

Thank you Mr. Chairman.

CHAIRMAN MILES:

Thank you Mr. Pratt. To your statement just a short response. The knowledge that we have with the exception of the formal letter was knowledge gained in hindsight only to the deliberations when Commissioner LeResche would bring myself or other members up to speed it -- insofar as the State Energy Policy Committee was concerned we did represent the 11 formal contractual recommendations to the Governor and Commissioner LeResche, but generally the knowledge we had was after-the-fact and sort of a reporting -- sort of a reporting sampling. I think that's a -- that is important that we record that -- have that response

AGO 559465

recorded.

Are there final comments from committee members? Representative Chatterton.

MR. CHATTERTON:

Thank you Mr. Chairman. I don't know -- trying -- rolling around in my mind protocol here so I think I will address this question to you Henry. Representatives of your clients met with the Governor in Anchorage yesterday. Did they?

MR. PRATT:

At a public meeting? Is that the one you are referring to?

MR. CHATTERTON:

I'm asking you if they met.

MR. PRATT:

Yes.

MR. CHATTERTON:

Was that a public meeting? You led me to a question now.

MR. PRATT:

Yeah, it -- my understanding of it is representatives of our company up here with the Governor yesterday at a pre-planned public meeting on the entire royalty oil contract.

MR. CHATTERTON:

Right.

MR. PRATT:

Fairbanks the day before.

MR. CHATTERTON:

To your knowledge during public or non-public, was there any discussion of modification of the contract that this committee has before it?

MR. PRATT:

I have no understanding or idea of what took place at either meeting other than there were some 60 to 70 people there and that there was a question and answer period.

AGO 559466

MR. CHATTERTON:

Would you be willing to find out for me by Monday whether there was any further discussion of any changes in the contract, please?

MR. PRATT:

I'd be very happy to to the extent that I can and perhaps maybe Connie Barlow can also inquire from the administration's point of view.

MR. CHATTERTON:

I'd appreciate it. Thank you. Thank you, Mr. Chairman.

MR. HONIG:

Mr. Chairman, if I were to make a response to that question which has been raised as Chairman of the Board of ALPETCO, I know of no discussions conducted by anyone in ALPETCO or with anyone in the administration with respect to consideration of any change of any sort in the ALPETCO contract, and I think if that had been discussed by ALPETCO respresentatives, I think I would have heard about it.

MR. PRATT:

Mr. Chairman, I'm sorry, I didn't even understand the thrust of Mr. Chatterton's question. I thought you meant that any members of the audience suggest changes to the contract such as Mr. Paulser (ph.) did.

(Simultaneous speech. Indisc.)

MR. PRATT:

I'm sorry, I did not understand your question. I also would like to make one other response and may it in a very serious vein. Mr. McCutcheon of Anchorage made a reference to questions regarding the dishonesty in the way the contract negotiations were handled. I not only resent that comment, but I know of nothing that could even resemble such conduct at any time during the negotiations. Mr. LeResche, in my opinion, and in the opinion, I think, of the other applicants, conducted all of the negotiations on a very high plane and in almost an aloof manner as far as any of the applicants are concerned, and certainly there was never any hint that any of us noticed at any quarter of any dishonesty whatsoever.

CHAIRMAN MILES:

Thank you very much. Any further comments? Then we'll stand adjourned.

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House
Special Committee on Royalty Oil and Gas

Public Rebuttal

Testimonies, hearing to Roy Board,
Berman
Bill Rice

ALPETCO - Charles Honig

Risks & rewards & subsidies

I Subsidies - Direct or Indirect subsidies

Direct - Lower price
ALPETCO - 23. not subsidy, not veto
Prevents state from unfair
competition.
Why should you get lower
price? Do you have a ~~b~~
surplus capacity?

AGO 559468

Customary in other contracts,
Lipton said: imaginative,

RISKS Near term:
) Flood W.C. with crude oil
Lower in-value
Can't borrow money from banks if we don't sell
oil at profit

What if not done by 18 mos?
No 6.9 deal, 2 years may be good for AK

BENEFITS Employment
34, mil man hours

Sub contracts

Long-term risks:
plant built & running, fails,
it could happen to anyone,
not a function of contract

AGO 559469

State doesn't have to do anything, that it doesn't want to.

ALPETCO used to risks.

Endowment trust

Questions:

Miles: Subsidies, $9 million for line & tank fill, AK not repaid until 27 years.

Voter referendum makes it clear that there may be a request for a price change.

Hon. q: Will repay state, value on crude, with interest, looked upon as an investment in $9 mil.

Miles: or subsidy for 27 years

Hon. q: Provision, if contract silent on lower price, ~~#~~ 3 parties could decide upon price rather than 4. Strengthens contract not weakens it.

AGO 559470

Miles: Request is clear, real possibility

Chat: Page 5, Slide presentation,

What benchmark can you take royalty oil,

Hong: After attaining financing ~~equipment~~ commitment for 1.5 bill. on

10.2. Se

Could 1.5 billion

Contract commits them to certain acts,

Chat: 30 mos, commence construction ~~by~~ of facility by, core refinery,
nothing else says plant must be constructed

Hong: No other commitments as to configuration in contract

Chatterton:

AGO 559471

Only required to an instate refinery for 30,000 b/d for in-state.

4.2 aromatics
olefins obviously petrochemicals

$2.5 billion
Miles: Why isn't + expenditure included in contract?
All figures based upon $2.5 billion,
benefits reduced.

Hon.g: ~~Small~~ Fewer jobs
Smaller tax base

Pessimistic bench-marks

Gas contract

Chatterton: p. 40 Article 13
Can sell anything in excess
of the domestic needs

Honig: 30,000 b/d is not core refinery —
large ~~more needed~~ complex needed to
Making fuel products, if State

AGO 559472