

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 86/2

542 SCOM116: JOINT SPEC. COMM. ROYALTY OIL & GAS 1977-78

AGREEMENT FOR THE SALE OF NORTH COOK INLET ROYALTY GAS
FROM THE STATE OF ALASKA
TO ALASKA PIPELINE COMPANY

APR 12 1971

OIL & GAS BO

This memorandum ("Agreement") reflects the intent of the State of Alaska ("the State") and Alaska Pipeline Company ("APC") regarding APC's purchase of the State's 1/8th (one-eighth) royalty share of natural gas produced at the North Cook Inlet Gas Field, which is operated by Phillips Petroleum Company ("Phillips").

WHEREAS, Union Oil Company of California ("Union") as Operator of the Kenai Gas Field and the gas transmission line from the Kenai Gas Field to the North Kenai Road now supplies APC's total requirements for natural gas at the Kenai Gas Field and at three (3) pipeline taps on the North Kenai Road;

WHEREAS, APC has an early and urgent need to purchase additional natural gas for its customers in the vicinity of the North Kenai Road, and has applied to the State to acquire the State's 1/8th royalty share of gas produced by Phillips at the North Cook Inlet Gas Field to the extent any portion or all of such royalty gas may be available to APC without causing additional investment by Phillips, and

WHEREAS, the royalty gas and the Kenai Field Gas are sufficiently similar that exchange rather than literal transfer of the royalty gas may be of advantage to all parties concerned including APC's ultimate gas consumers and such exchange may be practical because of the Kenai Gas Field's interconnection with the North Cook Inlet Gas Field which has allowed exchanges to be made from time to time in the past, and

WHEREAS, APC considers that the merit of proceeding to purchase this royalty gas is sufficient to justify its installing the necessary pipeline, compressors, and connections to facilitate the literal transfer of this gas into APC's existing pipeline as an alternative to exchanging in the event such exchanging is found to be impractical either before or after the purchase has begun, and

WHEREAS, the proposed sale of the royalty gas is seen to be in the public interest of the citizens of Alaska and the gas consumers served by APC (as evidenced by various statements which are of public record),

NOW THEREFORE, the State and APC agree as follows:

1. The State agrees that it will give notice to Phillips that it elects to take its royalty gas in kind within one year of the date of such notice (but not sooner than six months following such notice except at the consent of Phillips), upon APC's completion of negotiations for exchanging or APC's completion of its pipeline connection in the alternative. Whether taken by exchanging or by literal transfer, APC will pay to the State, for remittance to Phillips, an amount calculated to cover Phillips' reasonable costs for dehydrating and transporting the gas from its offshore platform at the North Cook Inlet Gas Field to its liquefaction plant on the North Kenai Road near Kenai, Alaska. In addition, APC will pay to the State the wellhead price in effect as wellhead value for calculation of severance taxes payable by Phillips to the State from year to year, amended as of June 1 of each year to June 1, 1984, provided

however that such price as determined each June 1, to be effective on deliveries from June 1 through May 31 of the following year, shall not be less than the highest price paid for gas produced in the area designated as Exhibit A hereof during the twelve preceding months at wellhead for gas of comparable quality and at comparable terms and conditions of delivery.

Said payments shall be made on or before the 20th day of the month following the month in which the purchases occur.

2. The State and APC agree that the quantity and quality of gas purchased by APC hereunder shall be at the sole determination of Phillips, provided that APC shall be entitled to receive, at a mutually agreeable point of delivery at or near the Phillips liquefaction plant, gas of the quality and at the pressure existing in Phillips' pipeline, and in daily volume of one-eighth (1/8th) the total volume delivered by Phillips during the preceding day, except that by mutual agreement other delivery volumes may be in effect from time to time if necessary and desirable to suit the mutual interests of Phillips and APC.
3. This Agreement shall not serve to predispose APC's opportunity to develop an exchange agreement with Union, it being agreed that such an exchange agreement may be desirable and preferable to APC's installing of the pipeline and compressors which otherwise would be required.
4. This Agreement shall not be used to require Phillips to submit to any form of regulation by the Alaska Public Utilities Commission or by any other administrative or legislative body or agency, whether federal, or state, or other which would not be applicable if this Agreement did not exist. In the event of such regulation being asserted and implemented, then this Agreement shall terminate and become null and void.
5. This Agreement shall not be used to require Phillips to make additional investment except on terms to which Phillips and APC may agree, it being understood that in the event additional investment by Phillips should become necessary in order for Phillips to meet its contractual obligations as to production and transportation of gas from its North Cook Inlet Gas Field to its liquefaction plant and in the further event that APC is unwilling or unable to participate in or to reimburse Phillips as reasonably necessary for that investment, then this Agreement shall terminate and become null and void, or in the alternative at its option, APC shall agree to reduce deliveries hereunder as necessary to enable Phillips to meet its contractual obligations without making such additional investment.

15. It is doubtful that the State could transfer the existing transport situation with Phillips to another party without Phillips consent. The State lease provides that when the Lessor elects to take its royalty in-kind, the Lessee shall deliver it free of charge on said land or at such place as Lessor and Lessee mutually agree upon. Further, the transport charge itself may be open to negotiation between Phillips and Alaska Pipeline.

16. The Phillips-Marathon contract with Tokyo Gas and Tokyo Electric expires June 1, 1984, unless extended. The State of Alaska North Cook Inlet royalty gas availability is dependent upon continued production from Phillips platform. At present, production from the North Cook Inlet gas field is not certain beyond June 1, 1984.

CONCLUSIONS

The growth of population and increased commercial activity of the Anchorage area and its environs served by Alaska Pipeline and its distribution affiliate Alaska Gas and Service is consuming the gas reserves of that system at a rate greater than originally anticipated. A source of additional gas reserves to that system could be made available from the State's royalty gas share of the production from the North Cook Inlet Unit gas field which is now being liquefied by the Phillips-Marathon LNG and exported to Japan. Alaska Pipeline has offered to take this gas as it becomes available through production for the LNG plant and pay the State the same price that the State would otherwise receive from Phillips for that gas. The sale is necessarily dependent on reasonable exchange or transportation arrangements being consummated between Phillips and Alaska Pipeline.

Under these circumstances it is in the best interest of the State of Alaska to take the North Cook Inlet Unit royalty gas in kind and sell the gas to Alaska Pipeline for use in the Cook Inlet area served by that system.

DECISION

Pursuant to the authority vested in the Commissioner of the Department of Natural Resources, under AS 38.05.180-183 and AS 38.06.010-080, and under the Alaska Oil and Gas Leasing Regulations pursuant thereto, and with the concurrence of the Alaska Royalty Oil and Gas Development Advisory Board, I do hereby:

- (a) determine that it is in the public interest to take the State of Alaska royalty share of gas production from the North Cook Inlet Unit gas field in-kind;
- (b) determine that it is in the public interest to enter into a negotiated sale of the North Cook Inlet Unit gas field royalty gas to Alaska Pipeline.

Date:

Commissioner DNR

Approved:

Alaska Royalty Oil & Gas Development Advisory Board

Date:

6. APC shall install and operate, at its cost, all gas metering and compression equipment required hereunder, if any, on land provided by the State (or Phillips) without charge to APC. If such metering equipment is installed and operated by APC, it shall conform to recognized industry standards and shall be available for inspection and verification by the State (or Phillips) at all reasonable times. In the event APC develops an exchange agreement such that no metering equipment is required hereunder, then APC and the State agree to accept the metering performed by Phillips (and by Union or others), subject to APC's right of inspection and verification at all reasonable times.
7. The State shall not be deemed to be in control of gas taken by APC hereunder whether by exchange or otherwise, and APC shall not be deemed to be in control of gas it receives except from the downstream flange of its metering equipment, if any is installed.
8. It is the intent of this Agreement that APC shall receive all of the royalty gas produced by Phillips during the term hereof, each day of such production. Failure of APC to receive such gas each day, except with the consent of Phillips and the State or by force majeure, shall require APC to forfeit its right to subsequent receipt of that gas not taken. Recurring or continuing failure of APC to receive such gas, without such consent and not due to force majeure or other reasonable cause, or failure of APC to make timely payment therefor, may serve as the basis for termination of this Agreement by the State at its option.
9. This contract shall become binding on APC the day of its approval by the legislature and shall terminate on June 1, 1984 or earlier as provided herein, except that it may be extended indefinitely by mutual agreement. APC shall not be required to take delivery of gas hereunder prior to one year after the effective date hereof if an agreement is reached for exchange as contemplated in paragraphs (1) and (3) hereof, or 18 months from the effective date hereof if an exchange agreement is not obtained and it thus becomes necessary for APC to install a pipeline and compressors in order to receive gas hereunder.

This Agreement was executed on _____, 1976.

for the State of Alaska

for Alaska Pipeline Company

by _____

by _____

STATE
of ALASKA

MEMORANDUM

DEPARTMENT OF NATURAL RESOURCES
Division of Oil and Gas

RECEIVED
APR 14 1975

TO: Guy R. Martin
Commissioner

ALASKA ROYALTY
OIL & GAS BOARD

Attn: Bill Fackler
Deputy Commissioner

DATE : April 9, 1976

FROM: O. K. Gilbreth, Jr.
Director

SUBJECT: North Cook Inlet Royalty Gas
for 10 MMCF/D Take or Pay Contract
for Alaska Pipeline Company

To furnish the Alaska Pipeline Company 10 MMCF/D it will be necessary to commit by individual leases since the entire field is unitized.

The most recent sales data for North Cook Inlet state royalty gas has averaged 16.007 MMCF/D for the past year. The following tabulation shows how this average equates back (Col. 5) to each Tract (Col. 1) and Lease No. (Col. 2) based on acreage Participation (Col. 4).

Column No. (1)	(2)	(3)	(4)	(5)	(6)	(7)
				Royalty Gas - 12 month average - MMCF/D		
Tract No.	Lease No.	No. Acres	Percent Lse. Participation	Tracks All	Tracks 2,3,7	Tracks 2,3,7,8
2	ADL-17589	4375.5	44.7324	7.1603	7.1603	7.1603
3	ADL-17590	640.0	6.5430	1.0473	1.0473	1.0473
7	ADL-18740	800.0	8.1787	1.3092	1.3092	1.3092
8	ADL-18741	640.0	6.5430	1.0473	-	1.0473
11	ADL-37831	3326.0	34.0029	5.4428	-	-
	Totals	9781.5	100.0000	16.0069	9.5168	10.5641
Variations $\pm$ 10 MMCF/D					- .4832	+ .5641
Peak Month - MMCF/D				19.409	11.5390	12.8090
Variation $\pm$ 10 MMCF/D					+ 1.5390	+ 2.8090
Low Month - MMCF/D				9.954	5.9180	6.5690
Monthly variation $\pm$ 10 MMCF/D					- 4.0820	- 3.4310

Column 6 shows the summation of tracts 2,3 and 7 come the closest to a 10 MMCF/D total with 9.5168 MMCF/D for a variation difference of -483,200 CF/D. The summation of tracts 2,3,7 and 8 are also shown, but result in a slightly larger variation of +564,100 CF/D.

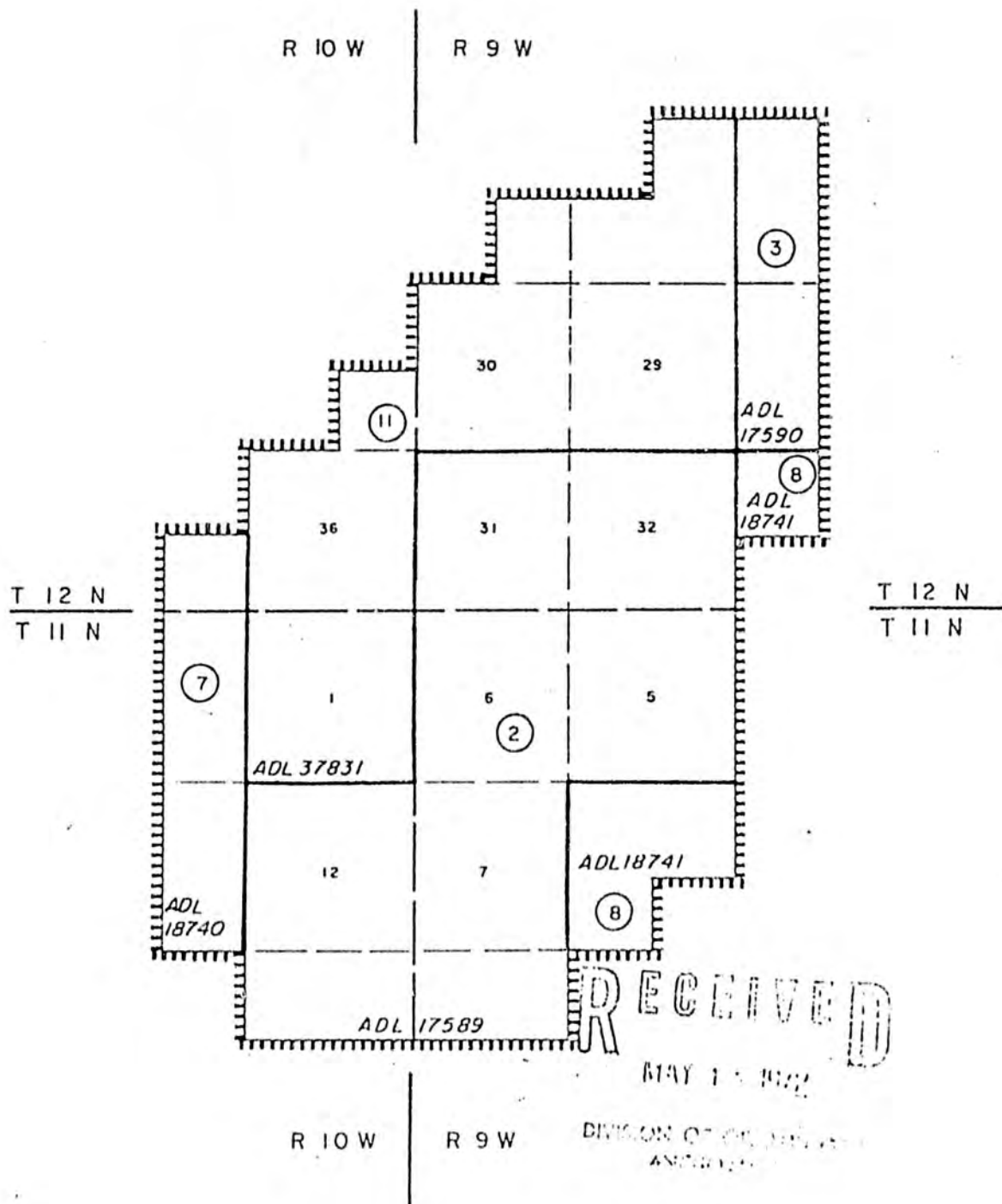
We have shown the maximum high and low variations which may be expected by inclusion of the Peak month and Low month data under Columns 5, 6 and 7. This shows that a monthly variation of from +1,539,000 CF/D to - 4,082,000 CF/D may result from tracts 2,3 and 7 (Col. 6).

A copy of Exhibit "A" from the unit agreement is attached for your convenience.

Attachment

AGO 801751

all members
4-14-76
AK



(Contracted 2-1-72)

ADL 17589
ADL 17590
ADL 18740
ADL 18741
ADL 37831

LEGEND

----- Unit Boundary
——— Tract Boundary
③ Tract Number

AGO 801752

EXHIBIT "A"
TO ACCOMPANY

CONTRACTED
NORTH COOK INLET
UNIT AGREEMENT
COOK INLET BASIN, ALASKA

Scale 1" = 1 mi

Feb. '72



ALASKA PIPELINE COMPANY

General Offices Located at 3000 Spenard Road
P.O. Box 6288 Anchorage, Alaska 99502 / Phone (907) 277-5551
Telex 25-187

April 2, 1976

Mr. Bill Fackler, Executive Director
State of Alaska Oil and Gas Royalty Board
Department of Natural Resources
Pouch M
Juneau, AK 99811

RECEIVED RECEIVED
APR 05 1975 APR - 5 1976

ALASKA ROYALTY
OIL & GAS BOARD

Department of
Natural Resources

Dear Bill:

This is written to furnish you with some background information relating to our past and present "flow through" situations and why we feel that the APUC actions have served to "inhibit" our search for new and probably higher priced non-royalty reserves.

Enclosure A contains our previous "flow through" provision while Enclosure B contains the one presently in effect.

A brief description of the sequence of events leading to the change is as follows:

December 15, 1974 - AGAS agreed to a gas price increase (19.5¢/MCF) to become effective July 1, 1975 in order to obtain gas in the quantities required by its customers. The APUC and major customers were notified in advance of completion of negotiations.

December 20, 1974 - The APUC ordered an investigation and public hearing on the tariff flow through provisions.

March 21, 1975 - AGAS filed new rates giving effect to the increased cost.

April 24, 1975 - The APUC rejected AGAS newly filed rates.

May 2, 1975 - AGAS notified suppliers to not proceed with any investment in workover and/or new wells required to meet its contractual commitments.

May 6, 1975 - The APUC ordered an investigation of the anticipatory breach of contract indicating that it might for good cause shown revoke AGAS certificate of public convenience and necessity.



ALASKA PIPELINE COMPANY

General Offices Located at 3000 Spenard Road
P.O. Box 6288 / Anchorage, Alaska 99502

Mr. Bill Fackler, Executive Director
April 2, 1976
Page Two

May 8, 1975 - AGAS agreed to withdraw its tariff flow through provisions.

May 12, 1975 - The APUC accepted AGAS tariff filing of March 21, 1975 as an interim request for rate relief and set hearing date of June 19, 1975.

July 1, 1975 - The APUC granted an increase of 12.78¢/MCF.

July 9, 1975 - AGAS requested reconsideration of the July 1, 1975 order.

July 31, 1975 - The APUC denied AGAS request of July 9, 1975.

July 31, 1975 - AGAS filed proposed new cost of gas flow through tariff provisions to replace those withdrawn May 12, 1975.

August 28, 1975 - The APUC suspended the filing of July 31, 1975 and set hearing date of October 30, 1975.

December 17, 1975 - The APUC issued its order modifying the flow through provisions filed July 31, 1975.

AGAS subsequently petitioned for reconsideration of the order of December 17, 1975 and the APUC denied the petition. In addition to the above mentioned actions there have been a series of requests, hearings, and orders relating to AGAS further attempts to recoup its increased costs.

In concept, the idea that a full rate hearing for each fuel cost change is an appropriate means of consumer protection, appears valid. Our actual experience with the process indicates it is not. The following experiences have led us to this conclusion:

- (1) Rate cases are expensive and time consuming processes. We have devoted an inappropriate amount of internal time and talent in our year long battle that began with the negotiated gas cost increase. We have spent approximately \$320,000 on attorneys and other specialists in regulatory matters in attempting to recover costs incurred by us in good faith for the benefit of our customers. The benefit of hindsight indicates we made a timely and appropriate



ALASKA PIPELINE COMPANY

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Mr. Bill Fackler, Executive Director

April 2, 1976

Page Three

business decision, yet one that has been costly to the owners of the Company. Common sense tells us that a similar occurrence in the future could result in a new management team.

- (2) The uncertain outcome of hearings before an appointed regulatory agency with a recent history of rapid change in composition and philosophy makes long term commitments an extremely risky course of action.

A fuel cost flow through provision which would not require the company to assume the burden of proof in a full rate hearing for each fuel cost change would reduce the business risk to an acceptable level. Such provision would not prevent the Commission from ordering rate decreases in instances where the use of the provisions would result in an excessive profit to the utility.

Bill, I hope that this helps to explain our situation and to give you some insight into the constraints under which we labor as we strive to acquire additional reserves.

Very truly yours,

Harold F. Schmidt
Senior Vice President

HFS:jdj

Enclosures

PURCHASED GAS COST ADJUSTMENT CLAUSE
WITHDRAWN MAY 12, 1975

708 Purchased Gas Cost Adjustment - Company's rates are based on the current wellhead cost of a firm supply of natural gas at the gas field. In the event this price is increased or decreased, or taxes on such gas are increased or decreased, above the amount(s) payable on April 15, 1972, then the Company may, after appropriate notice to the Alaska Public Utilities Commission as required by AS 42.05.411, place into effect a like increase or decrease in the rate theretofore in effect. Such adjustment shall begin with bills rendered during the month subsequent to the effective date of the increase or decrease at wellhead.

PURCHASED GAS COST ADJUSTMENT CLAUSE
CURRENTLY IN EFFECT

708 Purchased Gas Cost Adjustment - The gas supply contracts existing on December 1, 1975, contain escalation clauses which result in periodic increases or decreases in the cost of purchased gas. Any increase in the cost of purchased gas to the Company under the escalation clauses that the Company becomes responsible for after July 1, 1976, may be passed on to the customers of the Company. Such an increase may be reflected in the rates paid by the customers for gas used by the customer after the date the Company is responsible for paying the increase. The increase, however, may not be charged to the customers of the Company unless the Company meets the conditions specified in Order No. 3 in Docket U-75-68. The Company may not flow through to its customers any increases in the cost of gas resulting from alterations, changes, or amendments of any part of the escalation clauses existing on December 1, 1975. The Company also may not flow through to its customers any other increase in the cost of gas except as specified in this Section and the Royalty Gas Section of this tariff. The increases flowed through to the customers pursuant to this section may not exceed 5¢/MCF per calendar year.

In the event the price which the Company must pay to purchase gas to serve the Company's customers is decreased the Company shall decrease its rates to its customers to fully reflect the entire decrease in the purchased gas cost.

Royalty Gas - The cost of gas purchased from the State is greater than the cost of gas purchased from other suppliers. The gas purchased from the State must be taken by the Company as produced. The Company must therefore distribute this gas to its customers when taken and it must be sold at a higher rate than the gas it now purchases from other suppliers. In order to insure a proper price of gas as a result of the commingling of the higher priced State gas and the lower priced gas from other suppliers the Company shall, month to month, increase or decrease the bills of customers to reflect the average cost per MCF of gas on an MCF basis which shall be computed as the product of the volume of gas purchased from the State each month multiplied by the price of that gas, plus the product of the volume of gas purchased from other suppliers during the month multiplied by the cost of this gas, and the sum of the products thus computed divided by the total volume of gas purchased. The flow through increases or decreases pursuant to this section of the tariff are subject to the conditions set forth in Order No. 3 of Docket U-75-68.

PROPOSAL

Alaska Pipeline Company and its distribution affiliate Alaska Gas and Service, Division of Alaska Interstate Company have requested the right to purchase the State of Alaska's royalty share (1/8 or 12 1/2%) of the North Cook Inlet gas field operated by Phillips Petroleum Company.

Alaska Pipeline Company supports their request with the following reasons.

1. Without this gas, Alaska Pipeline Company may not be able to continue serving the Bernice Lake power plant of Chugach Electric Association, or, if an alternate source of gas is found, the cost to Alaska Pipeline's customers is likely to be substantially more than the purchase of State royalty gas. This purchase will be of material benefit to Alaska Pipeline's residential and commercial gas customers and of even greater benefit to Chugach Electric Association and all its customers from Homer to Talkeetna. More than 50 percent of Alaska's population would be affected either as gas consumers or as power customers.

2. Alaska Pipeline is prepared to accept delivery of this gas immediately, on an "if and as available" basis, and at the same price the State would receive for this gas which is being liquefied and shipped to Japan.

Assuming that delivery to Alaska Pipeline can be made by exchange or displacement, there would be no necessity for capital expenditure

for new pipelines or other facilities at present. If additional pipeline facilities or compression becomes necessary to maintain delivery, Alaska Pipeline would participate in such cost.

3. Alaska Pipeline recognizes that deliverability of North Cook Inlet royalty gas is dependent upon the Phillips Marathon LNG plant use. They have adequate deliverability under contract from the Kenai gas field so that deliverability from the North Cook Inlet gas field is not a problem and that differences in flow rate can be adjusted or compensated within their system.

Based on current production rates, Alaska Pipeline assumes that an average of 15,000 MCF per day of North Cook Inlet royalty gas would be available. This amounts to approximately 5.5 BCF per year or a total of 75 BCF over the 15 year period desired by Alaska Pipeline. 82.5

FINDINGS

1. Alaska Pipeline Company's Nikiski contract with Union-Marathon for 10 BCF expires May 1, 1977. This gas supply is used to service the North Kenai Road area including the Bernice Lake power plant owned by Chugach Electric Association which consumes approximately 90 percent of the total daily volume.

2. The increased load placed on the Bernice Lake generating facilities while waiting on repair of Chugach's submarine cable across Knik Arm and construction of an alternate land line to Wasilla greatly increased gas consumption which may result in

exhaustion of the Nikiski contract reserves in 1976 prior to the end of contract.

3. The need to replace the diminished gas reserves of the Nikiski contract and the desirability to augment the gas reserves of the Anchorage contract has led Alaska Pipeline to write Union, Marathon, Phillips and Shell seeking an additional 75 BCF of gas reserves over a 15 year period with no favorable results to date.

4. North Cook Inlet royalty gas is similar in composition and quality to Kenai field gas and therefore interchangeable with each other in any proposition. Gas from the two fields is blended as feedstock to the Phillips-Marathon LNG plant.

5. The necessary pipeline systems now exist to allow an exchange to be made so that Alaska Pipeline could receive the royalty gas equivalent at its Kenai gas field connection.

6. The deliverability of North Cook Inlet royalty gas is dependent on LNG plant use activity and therefore would not be a constant volume.

7. Alaska Pipeline's Anchorage contract provides sufficient deliverability and also is interruptible so that Alaska Pipeline has sufficient flexibility to receive North Cook Inlet royalty gas on an "if and as deliverable" basis.

8. Alaska Pipeline could construct a pipeline to deliver the royalty gas to its pipeline to Anchorage if the proposed gas exchange is not possible.

9. In the event that additional pipeline facilities or compression is necessary to maintain delivery of North Cook Inlet royalty gas, Alaska Pipeline would participate in such cost.

10. Alaska Pipeline proposes to pay to the State the same price which the State otherwise would have received from Phillips' for its use of North Cook Inlet royalty gas for the duration of the Phillips-Marathon LNG export to Japan and thereafter not less than

(1) the average price in effect during the last full year prior to termination of the export contract, and not less than

(2) the price in effect, from year to year, for gas purchased by Alaska Pipeline at the Kenai gas field (from Union-Marathon).

11. Alaska Pipeline proposes to purchase 1/8th of the production of the North Cook Inlet gas field, day by day and year by year. They understand that at current production rates, approximately 15,000 MCF/D, or 5.5 BCF/year, would be available. Alaska Pipeline would not require any particular amount by day, month, year, or in total; or could take a specified amount if the operators so desired.

12. Present production from the North Cook Inlet gas field is 44.2 BCF per year (1974). This gas is 70 percent of the feedstock for the Phillips-Marathon LNG plant which is contracted for export to Japan. To maintain the present contract requirements it will be necessary for Phillips to increase the gas production from the North Cook Inlet gas field by an amount equal to the present State royalty gas volume plus an amount to compensate for the additional royalty on the increased production. Thus the present annual production of 44.2 BCF would have to be increased to approximately 51 BCF per year to maintain contractual requirements plus the volume of royalty gas requested by Alaska Pipeline. The increased production would increase the State royalty volume to approximately 17,500 MCF per day.

Present information indicates the field reserves are adequate for the increased production but the field life will be shortened by the amount of the increased production of course.

13. The pipeline from the North Cook Inlet gas field platforms to the LNG plant is wholly owned by Phillips. The State of Alaska royalty value is received at the wellhead minus a transportation charge of 5.55 cents per MCF to the LNG plant. This point of taking means that the State receives royalty value on all gas used by Phillips for plant fuel, shrinkage, etc.

14. Transport of gas for Alaska Pipeline from the North Cook Inlet platform to shore might be construed as qualifying the pipeline for Alaska Public Utilities Commission jurisdiction. This situation would be objectionable to Phillips.

Suggested Royalty Gas Sale Contract Provisions

Price

Alaska Pipeline agrees to pay the State the same price which the State would have otherwise received from Phillips for export of the North Cook Inlet royalty gas to Japan for the duration of that export including any escalations in (±) price received by Phillips, and not less than the highest price paid in the area by any buyer to any seller of gas of similar quality.

Quantity & Deliverability

Alaska Pipeline recognizes that deliverability of North Cook Inlet gas field royalty gas is dependent upon Phillips-Marathon LNG plant consumption and that a uniform daily production cannot be specified by the State. Alaska Pipeline agrees to take or pay for a total volume of 50 BCF of natural gas on an if and as deliverable basis.

DRAFT

Phillips Petroleum Company opposes the request for the following reasons:

1. Phillips worked diligently to provide a market for North Cook Inlet gas. No markets for the gas were found in Alaska or on the West Coast of the United States. The only possible market was export of LNG to Japan.
2. Phillips developed the North Cook Inlet gas field at considerable risk and expense for wells, platform, pipelines, liquefaction plant and LNG tankers. All these facilities were designed to utilize all of the gas production from the field.
3. The increased gas production to supply this new market resulted in additional income to the State through royalty and taxes, also substantially increased the tax base and local tax income of the Kenai Borough and town of Kenai.
4. Phillips has negotiated several price increases with their customers resulting in a three fold increase from the original price. Each increase was shared with the State by an increase in the wellhead price used as the basis for royalty payments. While the delivered

price increased about three times the wellhead price increased approximately five times. It is the highest price received by the State for its royalty gas.

5. The taking of the North Cook Inlet royalty gas inkind and separately disposing of it to a third party will impose an economic hardship on Phillips. Such action will necessitate increased production to meet contract requirements and cause earlier abandonment of the platform, pipeline, liquefaction and transportation facilities due to early depletion of the gas reserves. Additional wells will probably be required to meet delivery requirements and compression equipment will be necessary at an earlier date resulting in added costs to Phillips with no increased benefits to Phillips or the State.



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

April 2, 1976

RECEIVED
APR -5 1976

Mr. Guy T. Martin
Commissioner of Natural Resources
11th Floor, State Office Building
Pouch M
Juneau, Alaska 99817

Department of
Natural Resources

Dear Commissioner Martin:

The purpose of this letter is to confirm our oral proposal made to the Alaska Royalty Oil and Gas Development Advisory Board during its March 30/31 meeting in Juneau.

The proposal can be outlined as follows:

1. The State take North Cook Inlet royalty gas in kind and sell such gas to AGAS.
2. AGAS will take delivery of the gas at the platform. This presumes that--
 - (a) an arrangement can be made whereby, for suitable compensation, Phillips will transport the gas via their existing system to a point adjacent to the LNG plant.
 - (b) the APUC waives jurisdiction over the Phillips facilities to the extent that they may otherwise come under regulation due to the transport of the "royalty" gas.
3. The price will be equal to the Phillips price for royalty gas exported to Japan or equal to the highest price paid in the Cook Inlet area for similar quality gas.
4. The proposal is to cover the "life of the contract" and will terminate on or about June 1, 1984.
5. AGAS will take or pay

This presumes that--

- (a) it may be agreed with the State that royalty will be taken in kind for resale to AGAS on a selective lease by lease basis so that the volume in question will approximate AGAS' North Road requirements or (see (b))

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ALASKA ROYALTY
OIL & GAS BOARD

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

Commissioner Guy T. Martin
Continuation Sheet #2
April 2, 1976

- (b) if suitable exchange arrangements can be made with others or if AGAS chooses to build the pipeline connection to its Anchorage line--it may be agreed with the State that all of the royalty be taken in kind for resale to AGAS.
 - (c) The notice date regarding the State taking royalty in kind be so arranged as to permit AGAS a reasonable length of time to make exchange arrangement with others or to build the required pipeline facilities on a reasoned schedule.
6. The volume of gas expected to be taken in kind for resale to AGAS over the life of the contract is approximately 40 BCF with the actual amount being dependent upon the date of commencement, the arrangement agreed to under #5 above and the actual rate at which the field is produced.
7. It is understood that a deliverability feature is not required in this agreement.

Very truly yours,


Harold F. Schmidt
Senior Vice President

dh



ALASKA PIPELINE COMPANY

General Offices Located at 3000 Spenard Road
P.O. Box 6288 Anchorage, Alaska 99502 / Phone (907) 277-5551
Telex 25-187

March 22, 1976

RECEIVED
MAY 10 1976
Department of
Natural Resources

Mr. Bill Fackler, Executive Director
State of Alaska Oil and Gas Royalty Board
Department of Natural Resources
Pouch M
Juneau, AK 99811

Dear Bill:

By using reserves out of the Anchorage contract rather than new reserves we have been able to contract for a one year only extension of service on the North Kenai Road. While we are still hoping to have the North Cook Inlet royalty committed to us during this legislative session we have relieved the supply situation temporarily. It should also be noted that Homer Electric Association now has an offer from Kenai Utility Service Corporation and should no longer present a problem with respect to the royalty gas. Copy is enclosed.

Whatever the outcome of our negotiations with Union and Marathon on exchanging versus pipelining, or for some additional gas for the North Kenai Road area, we need to and are prepared to contract for the royalty gas for the life of production. This gas would supplement our present supply for Anchorage which otherwise will soon become inadequate.

We hope the Royalty Board will take action at its next meeting. We expect to attend.

Very truly yours,

Harold F. Schmidt
Senior Vice President

RECEIVED
MAR 24 1975

HFS:jdh

Enclosure

ALASKA ROYALTY
OIL & GAS BOARD



ALASKA PIPELINE COMPANY

General Offices Located at 3000 Spenard Road
P.O. Box 6288 Anchorage, Alaska 99502 / Phone (907) 277-5551
Telex 25-187

March 22, 1976

Mr. Guy T. Martin
Commissioner of Natural Resources
11th Floor, State Office Building
Pouch M
Juneau, AK 99811

RECEIVED
MAR 26 1975

MAR 24 1976

Department of
ALASKA ROYALTY Natural Resources
OIL & GAS BOARD

Dear Commissioner Martin:

Thank you for your letter of March 17, 1976. We would greatly appreciate it if you could please send us at once copies of the requests for North Cook Inlet Royalty Gas which you have received from Homer Electric Association, Phillips Petroleum, and Pacific Alaska LNG, together with copies of the response(s) made by the State.

We do not propose to enter a "competitive bid", nor is it timely or proper to debate the relative merits of a pipeline compared to exchanging gas when the need is for an urgent decision on committing the gas to us during this session of the legislature. We have presented our case in full to the best of our information and ability, over a period of several months. We agreed to accept the State's request for a Cook Inlet area favored nations clause and we agreed to accept a take or pay provision, neither of which to us appeared to be necessary or appropriate in the circumstances.

We are distressed by your prediction that our offer to purchase this gas is not likely to be presented to this session of the legislature, and by your having indicated that each party must "present its complete case". We know that lower priced gas is available to Homer (but not to us) and that Homer cannot be considered a bona fide contender for this gas. Copy of a letter on this is enclosed. We know that Pacific Alaska LNG already has (indirectly) caused us to have to pay nearly 100% more for gas at the Kenai gas field, and that they too cannot be considered a bona fide contender at present for this gas. We are aware that Phillips would prefer to continue taking this gas for export to Japan, but they are prepared to cooperate to deliver it to us if the State will so decide.

We have now arranged that when our present supply of gas for the North Kenai Road is exhausted in the next month or so we will begin taking gas there which originally was intended for the Anchorage area. It is a stop-gap measure and cannot be considered to be anything but that. We must soon make a decision as to our public responsibility to continue or not to continue such operation.



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Mr. Guy T. Martin
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As you know, in 1972 we acquired acreage in the Susitna Valley in the hope of exploring for additional gas, and in 1974 we commenced a \$2.5 million exploratory well, together with an independent partner (Amarex, Inc.). We still hope to continue such exploration, but the State's actions have discouraged our partner from risking further investment in Alaska: legislation to tax reserves in place, criminal prosecution on allegations of ecological damage (which are groundless, to our knowledge and opinion) and the threat of confiscatory production taxes are a compelling disincentive to such further risks. We now have no alternative but to try to stretch our existing reserves as far as possible or to pay what the traffic will bear for additional reserves from existing gas sources. Unfortunately rate making decisions at the Alaska Public Utilities Commission have stalled the Municipality of Anchorage from assembling its waste heat recovery plant which would save 1/2 of the gas now being wasted. This matter has been appealed to the courts. The Commission has acted to inhibit us from purchasing any gas except State royalty gas by refusing to grant flow through tariffs to cover higher priced other new gas, and has refused to reconsider our protest of that decision.

About all we can do, other than pointing out the seriousness of our situation to you, is to consider enforcing conservation of our gas reserves by terminating our contract to serve the Chugach Bernice Lake power plant and to begin interrupting Chugach's other plants since Chugach has a generous reserve of gas at Beluga and can burn oil in Anchorage and at Bernice Lake.

We will attend the March 30 meeting of the Royalty Board, and we can only hope that on further review you will recognize that our proposal is the one and only bona fide offer and that it is clearly in the public interest that we be allowed to purchase the North Cook Inlet royalty gas at the earliest opportunity.

Very truly yours,

Dale Teel
President

DT:jdH

cc: Honorable Jay Hammond, Governor of Alaska, via Mr. Bill Gordon
Honorable George Sullivan, Mayor of Anchorage
Mr. L. J. Schultz, Manager of Chugach Electric Association
Mr. Bill Rhodes, Manager of Homer Electric Association
Mr. Oscar L. Thomas, Vice President of Kenai Utility Service
Alaska Public Utilities Commission
All Royalty Board Members

AGO 801770

Attachments: Commi()ner Martin's Letter of March 1,
Oscar Thomas' Letter of March 17, H. F. Schmidt's Letter to B. Fackler

March 17, 1976

RECEIVED
MAR 24 1975

Mr. Bill Rhodes, General Manager
Homer Electric Association, Inc.
P. O. Box 255
Homer, Alaska 99603

ALASKA ROYALTY
OIL & GAS BOARD

Dear Bill:

Reference is made to our recent conversation regarding a possible natural gas sales agreement between K.U.S.Co. and H.E.A. The purpose of the agreement would be to provide fuel for power generation at a site approximately 6.5 miles north of Wildwood access road on the Kenai Spur Road.

We are of the present opinion that the feasibility exists to provide fuel gas for your proposed generating facilities at a cost considerably below that of any alternate sources known to us. In general, we propose that such an undertaking could be accomplished as follows:

1. The sale would be made under the rates and conditions outlined in Schedule III of our published Tariff, a current copy of which is enclosed herewith. The volume of 4,000 MCF of gas per day mentioned in our discussion represents a total annual volume of 1,460,000 MCF. Computed on a monthly basis the daily sales volume would carry an annual cost of \$704,380.00, or an average weighted cost of 48.24¢/MCF. It is noteworthy that if the cost of royalty gas, which might be obtainable from the State of Alaska, was set at 56¢/MCF the differential would be 7.76¢/MCF, or approximately 16%. The annual cost differential would equal some \$113,150.00. Although our rates are subject to regulation by the Alaska Public Utilities Commission it is my personal belief that, all things being equal, the rates quoted herein could be sustained throughout the life of our existing gas supply contract which terminates in 1987.
2. Service to your facility would involve a requirement for capital expenditures estimated at \$475,000.00 to \$500,000.00 (at projected 1977 costs). We would require a non-interest bearing advance-on-construction in the total amount of the initial investment which would be subject to refund in its entirety. The refund would be made at the rate of 10% of the total revenues derived from your account in those calendar years when such revenues equalled or exceeded \$700,000.00. The refund provision would, of course, become inoperative

AGO 801771

Mr. Bill Rhodes, General Manager
March 17, 1976
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at such time as the initial advance had been returned. Referring back to our illustrated rates and the suggested cost of royalty gas, the annual savings of \$113,150.00 combined with a yearly \$70,000.00 refund on the construction advance relates to a 2.73 year pay-out, exclusive of the cost of money.

3. The service facilities installed would remain under our ownership with maintenance and operating costs to be born by us.

4. Resale of gas would be prohibited, as would the extraneous use of gas for purposes other than power generation.

5. Point of delivery would be at the downstream flange of a block valve located on the downstream side of a metering run located on your site. Delivery pressure would be 200 P.S.I.G.

6. You may recall our conversation with Mr. Dale Teel, President of Alaska Gas and Service Co. regarding a waiver which would allow us to serve you in his certificated area. He has since confirmed that he would support, before the A.P.U.C., an agreement reached between K.U.S.Co. and H.E.A. that would culminate in your withdrawal from competition for the Cook Inlet royalty gas. Such support would undoubtedly satisfy any objections the A.P.U.C. might put forth before granting us the necessary authorization to proceed.

Some of the provisions suggested herein are unique in our experience. Consequently, final commitment to this proposal, or any similar plan, would necessarily involve approval by our Board of Directors.

There are other alternatives which could be considered in connection with the utilization of our currently unused gas reserves. At your convenience we will be most happy to discuss these with you or to further explore the possibilities outlined herein.

Very truly yours,

KENAI UTILITY SERVICE CORPORATION

Oscar L. Thomas, Vice-President

OLT:jc

Enc.

cc: J. M. Covington
Dale Teel

AGO 801772

March 17, 1976

Mr. Dale Teel
Alaska Pipeline Company
P. O. Box 6288
Anchorage, Alaska 99502

Dear Mr. Teel:

I appreciate the letter confirming your statements at the February 23, Board meeting. While we share your desire to resolve this issue in a timely manner, a review of the situation indicates a number of items which must be settled first before the Board can proceed.

The Board now has four requests for the North Cook Inlet field royalty gas; Alaska Pipeline Company, Homer Electric Association, Phillips Petroleum and Pacific Alaska LNG. AS 38.05.183 requires the sale of royalty be made to the highest responsible bidder unless the Commissioner with written approval of the Board determines that the best interest of the State does not require it. In this event, the Commissioner must publish the specific findings and conclusions supporting that decision.

The Board must decide the answers to the following questions among others: what are the relative merits of a competitive bid sale compared to a negotiated sale? Which sale is in the best interest of the State? Is there another source of gas supply which could be used? What is the optimum volume of gas to be sold from the State's viewpoint? What are the relative merits of an additional 30 mile pipeline compared to an exchange of gas?

It is obviously essential that each interested party present its complete case to the Board so that the record will reflect all pertinent information. The Board's findings and conclusions will be made based on that record, and this process is unlikely to be carried on in the best public interest under severe time constraints.

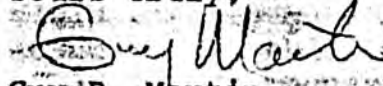
Mr. Dale Teel
March 17, 1976

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The Board must have sufficient time to consider all aspects of this sale in order to make the best decision possible given its assigned statutory priorities. A review of the problems that remain to be resolved indicate that it is unlikely that a sale can be accomplished in time to be presented to this session of the Legislature. We intend to keep working toward that goal, but believe that a good decision is more in the State's interest than a hurried decision.

I want to reiterate my direct assurances to you at the last Royalty Board meeting that an adequate gas supply for Anchorage and all Alaskan consumers is the highest present priority for this Administration. It will continue to be so as we develop this sale. Working not only in the context of royalty gas, but regarding other short-term supply possibilities, it is our intent to see that your supply difficulties are fully and successfully addressed. I look forward to working with you over the coming months on this matter.

Yours truly,



Guy R. Martin
Commissioner

GRM:dk



Alaska Gas and Service Company

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TELEX 25-187

March 20, 1976

Senator Mike Colletta
Alaska State Senate
Pouch V
Juneau, Alaska 99811

Dear Senator Colletta:

The amendment to exempt taxes on reserves dedicated to regulated public utilities is contained in SB 699, by the Rule Committee by request. Our attorney, Paul Robison, has prepared a legal memorandum on the propriety and necessity for making this exemption to the reserves tax and a copy of it is enclosed to you.

We hope passage of this bill can be given early consideration, and we will be available for further information if desired.

Very truly yours,

Dale Teel
President

dh

Enclosure

DIVISION OF ALASKA INTERSTATE COMPANY

AGO 801775

TO

JUSTIFYING THE EXEMPTION OF RESERVES OF REGULATED
UTILITIES FROM THE TAX ON OIL AND GAS RESERVES AND SHOW-
ING THAT SUCH EXEMPTION NOT ONLY MEETS THE TESTS OF
CONSTITUTIONALITY BUT IS CLEARLY IN THE PUBLIC INTEREST

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JUSTIFYING THE EXEMPTION OF RESERVES OF REGULATED UTILITIES FROM THE TAX ON OIL AND GAS RESERVES AND SHOWING THAT SUCH EXEMPTION NOT ONLY MEETS THE TESTS OF CONSTITUTIONALITY BUT IS CLEARLY IN THE PUBLIC INTEREST

The exemption of:

"any oil or gas reserves committed to or produced for use or resale by public utilities which are regulated by the Alaska Public Utilities Commission"

as a new sub-section (5) under AS 43.58.020, does not violate the United States Constitution or the Alaska Constitution and is consistent with the legislative policy contained in extant revenue and taxation laws pertaining to the oil and gas industry in Alaska.

An inquiry of constitutionality has arisen with regard to the above proposed exemption.

Our review of the questions leads us to conclude that there are no federal constitutional questions raised by such proposed legislative act, and the only question posed is whether or not such amendment would violate the Commerce Clause or Equal Protection clause, Article I, §8 of, and the Fourteenth Amendment to the Constitution of the United States, and Article I, §1 or Article IX, §4 of the Alaska Constitution.

Although the power of the State to act in this area free from federal restraint is discussed rather fully immediately hereafter, the second question concerning equal protection is of much greater interest and concern to the Legislature and is discussed commencing on page 4.

CONCERNING THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION

Clearly, there is no violation of the commerce clause, because as stated in Modern Constitutional Law, Antieau Volume II

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"States and their political subdivisions" realty located there, even though it is owned and used by a firm engaged therein solely in interstate commerce. Comparably, tangible personal property that has acquired a situs there can be taxed by such a state without violating the commerce clause.

In taxing the real and personal property situated and used within its borders, a State may employ any reasonable means of reaching its full or actual value as part of a going concern." (Citing Pullman Company vs. Richardson 261 U.S. 330, 67 L Ed 682, 43 S Ct. 366 (1923); Railway Express Agency, Inc. vs. Virginia 358 U.S. 434, 3L Ed 2d 450, 79 S Ct. 411, (1959) and Adams Express Company vs. Ohio State Auditor, 166 U.S. 185, 41 L Ed 965, 17 Sct. 604 (1897)).

At Section 10:54, p. 119 the treatise says:

"Again, in upholding a state tax upon the storage and withdrawal of gasoline which came into a state from interstate commerce and was shortly thereafter to be used to power interstate vehicles, the Supreme Court observed: 'Here the tax is imposed on the successive exercise of . . . the storage and withdrawal from storage of the gasoline. Both powers are completely exercised before use of the gasoline in interstate commerce begins.'" Nashville, C & St. L.R.Co. v. Wallace (1933) 288 US 249, 77 L Ed 730, 738, 53 S Ct. 345, 87 ALR 1191.

On another occasion, the Supreme Court ruled valid Wyoming's tax of 4 cents per gallon upon all gasoline used in the state, when applied to an airline that brought in the gasoline, kept it in tanks at an airfield, and withdrew it as needed for its planes. "A State," said the court, "may validly tax the 'use' to which gasoline is put in withdrawing it from storage within the State, and placing it in the tanks of the planes, notwithstanding that its ultimate function is to generate motive power for carrying on interstate commerce." Edelman v Boeing Air Transport (1933 289 US 249, 77 L Ed 1155, 1157, 53 S Ct. 591.

Although at this writing no state can tax the use of gasoline or oil as the power moving interstate commerce through the state, any state can tax gasoline or oil as property so long as it is part of the common mass of property within the state, and can by excise tax reach any handling or use of the gasoline or oil up to the moment it begins powering interstate commerce. (Emphasis added.)

In, Institute on Oil & Gas Law & Taxation, Seventh Annual Southwestern Legal Foundation, Matthew Bender & Co. 1956 in a treatise entitled "The Commerce Clause and the States' Power to Tax the Oil & Gas Industry" by Professor of Law Paul J. Hartman of Vanderbilt University, p. 387 at 449, it states:

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to tax any subject of taxation. Jurisdiction is an incident of sovereignty, and is one of the residuary powers possessed by each state as a consequence of the delegation by the people of certain enumerated powers to the Federal Government." Citing McCullach v. Maryland 4 Wheat 316 (U.S. 1819).

At pp. 395-396 it sets forth:

"1. Property Taxes on Oil and Gas Transported in Interstate Commerce

After oil and gas have been produced and are being marketed, they may encounter a property tax. The criterion used by the (U.S. Supreme) Court to determine the validity of property taxes on oil and gas transported across state lines has been made to depend to a very considerable extent on whether the tax was imposed before interstate movement had begun, or after it had ceased, or during certain interruptions of that movement. The tests of tax validity have, in most instances, been mechanical with but little consideration given to the economic consequences of the tax in question. It is believed that the cases we shall examine will support that proposition.

In the property tax case of Coe v. Errol, 116 U.S. 517 (1886), the Court combined in one sentence an expression of its desire for a dividing line between a taxable local activity and non-taxable interstate commerce, and a determination of where that line should be, when it said of the tax in question:

"There must be a point of time when they [taxed logs] cease to be governed exclusively by the domestic law and begin to be governed and protected by the national law of commercial regulation, and that moment seems to us to be a legitimate one for this purpose, in which they commence their final movement for transportation from the State of their origin to that of their destination."

"The principles expressed in Coe v. Errol have influenced judicial thinking in the field of state taxation virtually ever since. The doctrine of this case, of course, was coexistent with the idea that manufacture and production were not interstate commerce even though all the products were transported beyond the borders of the producing state and with no realistic separation between the production and the beginning of transportation." Hope Natural Gas Co. v. Hall, 274 U.S. 284 (1927) (production of gas); Utah Power & Light Co. v. Pfof, 286 U.S. 165 (1938); Oliver Mining Co. v. Lord, 282 U.S. 172 (1923); Heisler v. Thomas Colliery Co., 260 U.S. 245 (1922).

However, after the production process was completed and the commodities had started their interstate transportation, the Court has uniformly forbidden the states to impose a property tax on the commodities while in transit. Hughes Brothers Timber Co. v. Minnesota, 272 U.S. 69 (1926), Champlain Realty Co. v. Brattleboro, 260 U.S. 366 (1922); Western Oil Refining Co. v. Lipscomb, 244 U.S. 346 (1917).

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In 71 Am Jr. 2d. Sec. 426. p. 729-730 it states:

"With respect to state taxation of natural gas, or taxes based upon the production, transportation, or distribution thereof, a state may impose a tax upon the value at the wells of natural gas produced within its limits, although the gas is transported into other states for consumption."

Clearly, there is no federal constitutional question under the commerce clause, and as will be developed in what follows there is no impediment to the proposed amendment under:

EQUAL PROTECTION CLAUSES OF THE STATE OR FEDERAL CONSTITUTIONS

In 71 Am Jur 2d, Sec. 310, p. 624 it states:

"The power of the legislature to exempt from taxation, although of wide scope, is restricted by fundamental federal constitutional limitations. There is, however, nothing in the Federal Constitution to prevent a state from granting exemptions from taxation, so long as the grant does not violate fundamental rights secured by the Constitution. The power of a state to exempt from taxation is only precluded by the Fourteenth Amendment, where such power is arbitrarily exercised." (Emphasis added.)

The proposed amendment is not arbitrary, and is consistent with the principles governing the legislative prerogatives as will be seen by a consideration of the Alaska Constitution, the authorities in point, and the case law interpreting it.

In 84 C.J.S., Sec. 216, p. 414, it is said:

"Hence, where not prohibited or restricted in its exercise by constitutional provisions, the legislature of a state has full power to exempt any persons or corporations or classes of property from taxation, but only from taxes within its jurisdiction. The legislature has power to limit the exemption on any terms or conditions whatsoever, according to its views of public policy or expediency, subject only to the limitation that the exemption and the classification on which it is based shall be reasonable and not arbitrary."

Consistent with this stated authority, the Constitution of Alaska, Article IX, provides:

"Section 4. Exemptions. The real and personal property of the State or its political subdivision shall be exempt from taxation under conditions and exceptions which may be provided by law. All, or any portion of, property used exclusively for non-profit religious, charitable, cemetery, or educational purposes, as defined by law, shall be exempt from taxation. Other exemptions of like or different kind may be granted by general law. All valid existing exemptions shall be retained until otherwise provided by law."

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To the extent that equal protection or equality and uniformity may be impliedly contained in this constitutional grant of authority to the legislature, 84 C.J.S., Sec. 221, p. 427 states:

"Although exemptions of persons or property under some constitutional provisions relating to taxation and exemption have been held to violate constitutional provisions with respect to equality and uniformity, constitutional provisions with respect to equality and uniformity, although restricting and limiting the exercise of the power to exempt, do not prohibit the creation of reasonable exemptions, ..."

"However, the constitutional requirement is violated wherever particular persons or properties, selected arbitrarily from a class on which the burden of taxation is imposed, have been exempted therefrom,⁹⁷ and has been held violated if the exemption does not serve a public purpose.⁹⁸

AS TO SPECIFIC EXEMPTIONS OF PUBLIC UTILITIES

The basic observation of fact and law contained at p. 5 of *The Economics of Regulation*, Chas. F. Phillips, Jr., published by Richard D. Irwin, Inc. (1969) is important:

"The position of the regulated industries in the American economy is unique. In contrast to most other industrialized countries which have nationalized these industries, we have relied on private ownership, controlled by state and federal agencies, to provide services which are more or less essential to the economy and which are public in their nature." Argued Justice Harlan in *Smyth v. Ames*: "A railroad is a public highway, and none the less so because constructed and maintained through the agency of a corporation deriving its existence and powers from the State It performs a function of the State". And Justice Brandeis, in the *Southwestern Bell Telephone Co. v. Missouri Public Service Comm.* case, remarked that "the company is the substitute for the State in the performance of the public service, thus becoming a public servant."

The cases cited are the classic U.S. Supreme Court cases of *Smyth v. Ames*, 169 U.S. 466, 544 (1898) and *Missouri ex rel Southwestern Bell Telephone Co. v. Missouri Public Service Comm.* 262 U.S. 276, 291 (1923).

The same has been recognized of a natural gas company by the California Public Utilities Commission in *Re: Southern California Gas Co.* 35 PUR 3d 300 (1960) in which the headnote 7 states:

"A public utility is created for public purposes and performs a function of the state; it acquires the status of a quasi trustee, p. 309."

The public purpose or public use classification of public utilities has been carried through to the area of taxation. In *City of*

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the Court said at p. 663:

"That the use of essential public utility property in the operation of the utility is a public use cannot be gainsaid. . . . Public utilities are created to render service to the public and for the service a charge is made. Any incidental use allied to the main public purpose is likewise public use." (Emphasis added).

The headnote (5) at p. 657 concludes that:

"Use of essential public utility property in operation of a utility is a "public use" within statutory and constitutional provisions relating to exemption of property from taxation." (Emphasis added.)

In a case directly in point with the rationale of the proposed amendment, Utah Power & Light Co. v. Emmitt Pfoest, U.S. Supreme Court, 286 U.S. 165, 76 L. Ed. 1038, 52 S.Ct. 548 (1932) upheld an Idaho statute which levied a license tax on production of electricity, but which exempted energy used for pumping water for irrigation purposes on lands within the State. The Supreme Court said the exemption was "not precluded by the equal protection clause of the Fourteenth Amendment". (p. 186).

The appeal to the U.S. Supreme Court was from the District Court which upheld the reasonableness of the classification embodied in the exemption based on an earlier decision of the Idaho Supreme Court, Williams v. Baldridge, 48 Idaho 618, 284 Pac. 203 (1930). The Williams case involved a similar Idaho statute which granted to producers of electrical energy an exemption from the general property tax of property used in producing or transmitting power for pumping water for irrigation purposes. The Idaho court said: "The exemption is made to apply to the property of all power companies used in developing or transmitting electrical energy for pumping water for irrigation purposes with certain exceptions. . . . The pumping method is expensive. By minimizing such expense, land, otherwise unfit for cultivation, is made available for settlement. It is well recognized that where the plenary power of the Legislature to exempt from taxation has not been limited by a constitutional provision, it may exercise this power to encourage private initiative and thereby further the public welfare. A classification for

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purposes of exemption must not be arbitrary. In view of the climatic conditions in this State and the necessities of agriculture, we do not believe that a tax exemption statute designed to permit wider use of electrical energy for irrigation purposes raises a classification so arbitrary and discriminatory as to be merely capricious." (Emphasis added).

ALASKA COURT DECISIONS ARE CONSISTENT WITH THE ABOVE STATEMENTS OF AUTHORITY AND CASE LAW

In the case of In the Matter of Delinquent Tax Roll of The City of Anchorage, 1954, 16 Alaska Reports 286 (1956) the Federal District Court held:

"Classification of property under statute exempting from taxation public utility district and association operating utilities under an arrangement with the Rural Electrification Administration, is a reasonable classification." (headnote 4).

"Statute exempting from taxation public utility district and association operating utilities under arrangement with the Rural Electrification Administration was not in violation of territorial organic act which requires only that all taxes shall be uniform upon same class of subjects." (headnote 6).

This decision was reversed in City of Anchorage v. Chugach Electric Association, 17 Alaska Reports 481, 252 F. 2d 412 (1958), but not on the basis of the classification or tax exemption, but on the finding that the legislature had not carried the exemption over into a subsequent amendment of the tax statutes. (See page 494)

As to the question of public purpose, in the case of DeArmond v. Alaska State Development Corporation, 376 P 2d 717 (1962) the legislative act and the appropriation of funds for the development corporation were subject to the public purpose analysis.

The case headnotes state:

1. "The phrase "public purpose" within constitutional provision prohibiting the levy of a tax or appropriation of public money except for a public purpose represents a concept which is not capable of precise definition, and is a concept which will change as conditions create changing public needs, and whether a public purpose is being served must be decided as each case arises and in light of particular facts and circum-

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stances of each case. Const. Art. 9, §6."

2. "Where the legislature has found that a public purpose will be served by expenditure or transfer of public funds or use of public credit, the Supreme Court will not set aside finding of legislature unless it clearly appears that such finding is arbitrary and without any reasonable basis in fact. Const. Art 9, §6."

The Alaska Supreme Court reaffirmed these statements in the case of Walker vs. State Mortgage Association, 416 P 2d 245 (1966).

Again, in the case of Suber vs. Alaska State Bond Commission 414 P 2d 546 (1966), the Alaska Supreme Court ruled as to public purpose:

"Courts will not interfere with Legislature's exercise of discretion in choosing means to effect a public purpose unless it is clearly shown that legislative determination that a public purpose will be served by means chosen is arbitrary and without any reasonable basis in fact." (headnote 5)

And as to equal protection, the Court ruled:

"No denial of equal protection occurs in regard to legislative enactment if a rational basis for classification contained in the enactment may reasonably be conceived." (headnote 8).

"Demands of equal protection do not require that there be perfect equality and uniformity, or that the entire field of governmental action be covered by one legislative enactment." (headnote 9).

Equating the requirements of equal protection to the 14th Amendment, the Alaska Supreme Court in 12th Century Investment Company vs. City of Juneau, 359 P 2d 783 (1961) ruled:

"The equal protection clause of 14th Amendment does not prohibit inequality in taxation which is not shown to be result of intentional or systematic undervaluation of some but not all of taxed property in single class, USCA Const. Amend. 14" (headnote 3).

"Equal protection does not compel adoption of iron rule of equal taxation; it does not forbid differences in tax burdens founded upon substantive and reasonable differences between objects taxed. USCA Const. Amendment 14." (headnote 4.)

The Alaska Supreme Court reaffirmed these statements in the later case of Hoblitt vs. Greater Anchorage Area Borough, 473, P 2d 630 (1970) at Page 632.

PROPOSED AMENDMENT IS CONSISTENT WITH ALASKA LEGISLATIVE POLICY

Not only does the foregoing legal discussion clearly sustain the separate classification of public utilities as a result of their performance of a public purpose, it is a classification and distinction consistently accorded to public utilities by the Alaska Legislature in the entire scheme of taxation of the oil and gas industry.

Here follows a listing of the oil and gas taxes showing the consistent legislative policy in taxing public utility functions:

Kind of Tax	Description	Status of Public Utilities Regulations
Property Tax, Oil and gas, ad valorem (AS 43.56.010.210)	State Annual tax at 20 mils of value of property for exploring, producing oil or gas, transporting oil by pipeline:	Exempt: retail distribution of natural gas and pipeline systems operated as utility regulated by APUC are exempted by AS 43.56.210(6)
Property Tax ad valorem (AS 43.58.010-200)	State Annual Tax at 20 mils of value of levee on property having proven reserves of oil or gas	Exemption Proposed and justified herein
Motor Fuel Oil Tax (AS 43.40.010-100)	Tax per gallon of fuel sold, delivered or transferred.	Exempt- Fuel used in power plants of public utilities to generate electric energy for sale to general public exempted from tax by (AS 43.40.100)

It is not in the public interest to discourage the acquisition, development, and holding of natural gas reserves by public utilities by taxing such reserves. The public welfare will be served by inducements to public utility companies which are engaged in transmission and distribution of natural gas to the ultimate consumers and to the electric utilities to acquire and hold reserves. The following article from Alaska Construction and Oil is worthy:

"America's natural gas shortage is a dismal picture which is only beginning to be perceived in its true dimensions by the American public.

There are now in the United States approximately 40 million homes housing 135 million gas consumers who, for all practical purposes, are incapable of escaping from exclusive reliance upon natural gas.

Virtually 2/3 of our entire population live in homes fueled by natural gas, with no alternative except going without fuel.

To many people, reference to the energy shortage produces thoughts of oil." or coal (added by writer)

Whatever may be the historical explanation for this, the importance of natural gas in the energy picture of the United States cannot be overemphasized. It provides about one-third of all the energy consumed in the nation.

In this era of environmental consciousness, gas assumes even greater importance because it is the cleanest burning of all the fossil fuels.

It is in this total context of the importance of gas that alarm can properly be sounded because of the rapid deterioration of the country's gas supply. Statistics are available in abundant measure, but reference to our experience in 1973 dramatizes the need to develop additional supplies. Whereas the country consumed in that year 22 trillion cubic feet, new discoveries accounted for only 7 trillion cubic feet, one-third of what was consumed. If we continue at this pace, the nation will have no gas in the year 1990!

This stark fact accounts for the uniform cry of those engaged in the transportation and distribution of gas that the country expedite domestic exploration, coal gasification, and the importation of liquefied natural gas (LNG)." Alaska Construction and Oil, April 1975, page 32.

There can be no more legitimate public purpose than to encourage, by all means, including tax incentives, Alaska's natural gas industry, and particularly Alaska's public utilities utilizing gas to do everything in their power to acquire and hold as much natural gas in terms of supply and reserves as they reasonably can

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WILSON MCCASKEY
WILSON H. REYNOLDS
WILSON S. FRANKEL
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NORFOLK 279-7431

WIL A. BARRETT
WILSON BUILDING
303 77
NORFOLK, AK. 99101
NORFOLK 333-4859

to insure that this essential space heating resource and electric power generating resource will not be in short supply during the adverse winters experienced in Alaska, and at today's prices rather than at costs of several times today's prices a few years hence.

PRACTICAL NECESSITY FOR EXEMPTION OF PUBLIC UTILITIES FROM
THE TAX ON THEIR GAS RESERVES.

Although the reserves tax on regulated Public Utilities may produce only 1 to 2 million dollars per year in State Revenues, substantially all of this amount, when determined, will be passed on to the Utility Rate Payers unless the requested amendment is enacted. Considerable effort, some of which may be counter-productive, has already been expended by members of this Legislature to minimize public utility rates charged the consumer.

The Public Utility Commission has already granted Alaska Gas & Service Co. (ANGC) and Kenai Utility Service Corporation authority to pass this reserve tax to be paid by the utilities, on to the consumer. This will not only result in additional operating costs to these utilities (detailed computation and separate identification on customers' bills), but will result in circuitous, cumbersome, and costly re-computation and billing by the power companies (Municipality of Anchorage-ML&P, and Chugach Electric Association, Inc.) of the reserves tax collected from them by the gas utilities for gas purchased for electrical power generation. The electric utilities, through tax flow through provisions either existing or yet to be approved by the Alaska Public Utilities Commission, will have to perform detailed accounting computations and itemized billing to collect this portion of the reserves tax from their individual electric consumers.

We have not explored the extent of the adverse effect of the pass-on of this tax to the Kenai Native Association in their generation and supply of electricity to their Wildwood facilities with gas purchased from Kenai Utility Service Corporation on which they too would pay the reserves tax.

MR. F. ROBISON
MR. H. MCCASKEY
MR. H. REYNOLDS
MR. S. FRANKEL
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the impact on electric utilities and their rate payers, consider the fact that Chugach Electric Association which, if the exemption is not granted, will also have to pay and collect from its customers the taxes on its Beluga gas reserves which are also used in generating power for some or all of its customers in the Anchorage, Eagle River, Palmer, Wasilla, Talkeetna, Seward, Hope, Moose Pass, Sterling, Homer, Seldovia and Whittier areas.

It is worthy of note that should gas become available to serve Fairbanks, Kodiak or other areas while this tax is in effect, users there as well as their electric rate payers would be equally affected.

The writer is not familiar with the effect and impact of this tax on the community of Barrow and leaves it to their representatives to so determine. Hopefully, the legislators who have read this far will now consider the further and seemingly impossible dilemma facing the public utilities and the Alaska Public Utilities Commission if they are not given the exemption here sought.

The reserves tax first impacts the producer. Marathon-Union as to Alaska Gas & Service's and Kenai Utility Service Corporation's and Standard Oil of California as to Chugach Electric Association's reserves. In computing the tax they are given credit as to certain other taxes they have paid. AS 43.58.030, 43.58.180 and 43.55.018. These credits inure to the benefit of the utilities named herein and their rate payers to the extent such credits are available during the first two years the tax is collected. However, we have been advised by the Department of Revenue and the Oil and Gas Division of the Department of Natural Resources that these producers will continue to receive credits under 43.58.180 in future years until the full amount of the reserve tax has been offset. We have not been able to learn and understand how this will work and have absolutely no idea whether these future credits can and will be passed on to the public utilities in adjustments to cost of future gas purchases. If it does not occur it is unfair to all of the rate payers who will have paid the reserves tax the first

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two years.

But what if these utilities do receive future years credits over the life of the gas fields or until the full amount of the reserves tax has been offset? Can the utilities simply treat it as an overall reduction in operating expense (cost of gas)? If so, new customers who did not pay the tax during the first two years when it was collected from them will participate in the benefit of the passed through credits at the expense of the rate payers who actually paid it. If the Commission or a court in an action by a rate payer who paid the tax initially requires the utilities to keep records of the names and amounts of the first customers who paid the tax for the first two years and give credits or refunds to them the enormity of the exercise and its expense over a period of say 15 years would conceivably equal the amount of the credits or refunds and the cost of this service would then be borne by all new rate payers who would receive no benefit therefrom along with the old rate payers. This leaves, without discussion, the discouraging problem of dealing with credits or refunds accruing to the original tax paying rate payer who has discontinued service, moved, died, or if a business entity, ceased to exist.

Relief by the Legislature from this nightmare is earnestly solicited by enactment of the Amendment appearing at the beginning of this Memorandum.

ROBISON, McCASKEY, REYNOLDS & FRANKEL

By Paul F. Robison
Paul F. Robison

March 17, 1976.

PAUL F. ROBISON
KENNETH McCASKEY
ROBERT H. REYNOLDS
MARVIN S. FRANKEL
ENDALL E. FARLEIGH
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ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

March 9, 1976

Mr. Guy Martin
Commissioner of Natural Resources
State Office Building
Juneau, Alaska

Dear Commissioner Martin:

We wish to confirm to you that we have assented (at the Board's Meeting on February 23) to the "take or pay" requirement for purchase of royalty gas, on the condition that it would be available for the life of production rather than just to June of 1984. ✓

We are not able to confirm with Marathon that they have considered or will consider extending our contract by more than one year. We certainly will continue negotiating with them and hope that some way can be found to avoid an emergency in service to the Chugach Bernice Lake power plant. ✓

We have discussed Homer's interest in purchasing gas for a new power plant with Mr. Oscar Thomas, who is the Vice President and General Manager of Kenai Utility Service Corporation, and further confirmed the comments we made by letter of February 27. For the reasons given, we cannot believe Homer is a bona fide competitor for North Cook Inlet royalty gas and we cannot do more than to assure them that we would utilize this gas for service to Bernice Lake whether or not they purchase it from Chugach; and that if they build the new power plant in our service area, we would also utilize this gas to serve such a new plant. We cannot guarantee any particular price for the gas, however, because it is subject to the decision of the Alaska Public Utilities Commission.

We hope the Royalty Board will act soon to resolve this matter.

Very truly yours,

Dale Teel
President

dh

RECEIVED
MAR 11 1976

Department of
Natural Resources

RECEIVED
MAR 12 1976

ALASKA ROYALTY
OIL & GAS BOARD



ALASKA PIPELINE COMPANY

P. O. BOX 6288
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3000 SPENARD ROAD
PHONE (907) 277-5551

February 27, 1976

RECEIVED
MAR 2 1976
Department of
Natural Resources

Mr. Guy Martin
Commissioner of Natural Resources
State Office Building
Juneau, Alaska

Dear Commissioner Martin:

We were very surprised that Homer Electric Association appeared at the February 23 meeting of the Royalty Board and represented that they would be equally or more qualified to be the purchaser of North Cook Inlet royalty gas. We have written them to ask that they reconsider and withdraw from this matter and to reassure them that we would utilize the royalty gas to serve the Bernice Lake power plant whether or not Homer may be successful in purchasing it from Chugach Electric and/or to serve the additional unit if Homer is successful in obtaining funding for such a unit.

It has come to our attention that Homer could purchase gas from Kenai Utility Service Corporation (KUSCo) within the city limits of Kenai or on the premises of "Wildwood Station", which now belongs to the Kenai Native Association. KUSCo has adequate reserves and deliverability to provide this service and now has a filed tariff (SCHEDULE III - INTERRUPTIBLE POWER PLANT SERVICE) in effect which would provide Homer's requirements at less than 50¢ per MCF as compared to 60¢ or more for royalty gas from the North Cook Inlet gas field. In fact, KUSCo will forfeit these reserves back to the producers if no sale is effected.

It would appear that Homer's requirement for fuel for an additional generating unit would be met almost ideally by gas from KUSCo. A copy of KUSCo's Schedule III is enclosed as information.

We have attempted to purchase gas from KUSCo, but are not able to do so because their contract specifies that it is for use at Kenai (rather than resale at wholesale). We believe that the facts in this matter do not admit any bona fide "competitiveness" from Homer for State royalty gas, and that the public interest requires that we be given priority consideration. Homer cannot make use of any gas at present, nor in fact can it now commit to do so at some future date since such commitment would be contingent upon its purchase of the Bernice Lake power plant and/or its purchase of an additional generating unit. Homer has lower priced gas available from KUSCo. Homer has no experience in the handling of high pressure natural gas.

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

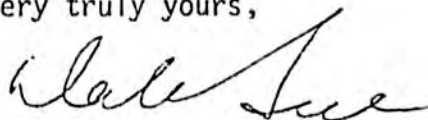
Mr. Guy Martin
February 27, 1976
Continuation Sheet #2

KUSCo's cost of gas is fixed by contract until 1986, at a very favorable price. With the known recent increases in price and demand for Alaskan natural gas and the increases which may reasonably be expected in the future, it appears to us that the customers of Homer are eminently better served by utilizing a source of gas that has a known cost for the next ten years. In our own situation, by averaging this relatively small amount of higher priced gas into the lower cost of our present supply, our customers will not be adversely affected by the higher priced royalty gas to the extent that customers of Homer would be.

We ask the Royalty Board not to allow Homer's last minute appearance to delay the negotiations of royalty gas to us, and that the sale be presented for approval by the legislature this session.

We will attend the March 2 meeting of the Royalty Board, to answer any further questions.

Very truly yours,



Dale Teel
President

dh

Enclosure

cc: Bill Rhodes

JUN 10 1975

KENAI UTILITY SERVICE CORPORATION

State of Alaska
Public Utilities Commission

KENAI UTILITY SERVICE CORPORATION

SCHEDULE III - INTERRUPTIBLE POWER PLANT SERVICE

(I)

AVAILABILITY: To natural gas service used for the generation of electricity or steam as central station service.

1. Once instituted, application of this schedule shall continue for not less than twelve (12) consecutive months.
2. Service under this schedule may be interrupted on not less than two (2) hours notice, and for not more than ten (10) days in any calendar month, during the period October through March.
3. While receiving service under this schedule, the customer shall maintain standby fuel and facilities, in the interest of public health and welfare, so that curtailment or interruption of service hereunder will be compatible with customer's power plant operation.

CHARACTER OF SERVICE: Natural gas having a heating value which is approximately 1,000 BTU per cubic foot.

MEASUREMENT: All deliveries shall be metered volumetrically and corrected to a base of 14.65 psia and 60° F. assuming absolute pressure of 14.7 psia.

MONTHLY RATE:

For the first	1,500 MCF or less per month	\$1,100.00
For the next	8,500 MCF per month	\$ 0.59/MCF
For the next	40,000 MCF per month	\$ 0.54/MCF
For the next	50,000 MCF per month	\$ 0.49/MCF
For the next	200,000 MCF per month	\$ 0.44/MCF
For all over	300,000 MCF per month	\$ 0.39/MCF

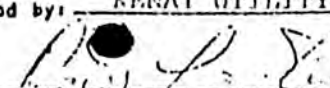
SUMMER SEASONAL DISCOUNT: During the months of April through September, a seasonal discount of \$0.05 per MCF will be allowed, provided however, that such discount shall apply only to the first 150,000 MCF per month, and provided further that the monthly minimum bill shall be not less than \$1,100.00

SERVICE REGULATIONS: Service supplied hereunder is subject to the orders of regulatory bodies having jurisdiction, and to the Company's Rules and Regulations currently on file.

Tariff Advice No. 6

Effective July 20, 1975

Issued by: KENAI UTILITY SERVICE CORPORATION AGO 801793

By:  Title: Vice-President



Alaska Gas and Service Company

GENERAL OFFICES LOCATED AT 3000 SPENARD ROAD
P. O. BOX 6288 ANCHORAGE, ALASKA 99502 / PHONE (907) 277-8551
TELEX 25-187

February 25, 1976

RECEIVED
MAR 1 1976

Mr. Bill Rhodes
Homer Electric Association, Inc.
P. O. Box 255
Homer, AK 99603

Department of
Natural Resources

Dear Bill:

I believe our mutual interests generally and, especially our mutual interest in the State royalty gas from the North Cook Inlet are thwarted by the appearance of our being in competition for this gas, as at the Royalty Board meeting of February 23. I also believe that if we could resolve this matter between ourselves, the Board was (and is) ready to approve the committing of this gas to us for the life of the field, and to so recommend for early approval in this session of the legislature. I fear that if we do not resolve the matter, then the Board (or the legislature) may not act in time for us to begin taking this gas prior to the termination of our present contract with Union-Marathon, and thus there would be a necessity to interrupt gas service to the Bernice Lake power plant. As you know, this plant burned oil for the first ten years and it is still equipped to burn oil upon such interruptions of gas. But the price of oil is now much greater than our price for gas, and the availability of oil may not be assured even at that price.

Service to this plant requires 50% to 100% of the royalty gas available on a daily basis, and we have from the outset been representing that we would utilize the royalty gas to maintain this service. Thus there is in fact no competition between us for the North Cook Inlet royalty gas except as to any "handling charge" we would require for making the sale. As you know, we now have "postage stamp" rates (uniform throughout our service area). All of our prior filed rates for power plants have been extinguished, and replaced by special contracts. The special contracts must be filed with the Alaska Public Utilities Commission, and thus our "handling charge" is subject to the approval of the Commission. We already have obtained approval from the Commission to commingle royalty gas with Kenai Field gas and to "flow through" the increased average cost of gas to our customers throughout our "postage stamp" distribution system. To the extent that you may take portions (or all) of the royalty gas from us, we should exclude its increased cost from the calculation of "flow through" to our other customers, in order not to compound any cost increases. This would require us to depart from the "postage stamp" rate design, as to our sale to you only.



Mr. Bill Rhodes
February 25, 1976
Page Two

We believe that the urgency and importance of our reaching early and appropriate agreement with the State are such that we should ask you to withdraw your request to purchase this royalty gas. To encourage you to do so, we would assure you that if you are successful in purchasing the existing Bernice Lake power plant from Chugach Electric Association and if you are further successful in obtaining funding to build additional generation facilities to serve Pacific Alaska LNG Company, we would commit to you the gas necessary for this generation out of the State royalty gas we are attempting to purchase. Thus you would be assured of reasonable pricing for fuel for these requirements. We are experienced in the handling, measurement, and pressure regulation of natural gas, and we believe our record of operating as well as our APUC Certificate of Public Convenience and Necessity fully qualify us to provide natural gas service to you.

We expect that because of our existing organization and expertise, your cost for fuel from us, including any "profit" to us, may be less than for your purchasing this gas directly and handling it. Your investment for pipelines and connections, odorization, measurement, and pressure and temperature regulation would be substantial. It would require compliance with the Pipeline Safety Act and perhaps a Certificate from the APUC. The safe handling of gas requires competent engineering and operations. We have this capability. Moreover, we are well suited to obtain gas for your requirements in excess of the availability (or the deliverability) of royalty gas, since we have a relatively large reserve at the Kenai gas field and we are continually negotiating for additional gas supplies.

I cannot over-emphasize the adverse effects of allowing the appearance of competition to preclude the earliest possible conclusion of negotiating the sale of the North Cook Inlet royalty gas to us. Personally, I would not expect early action by Chugach to sell the Bernice Lake plant to you. Several times in the past we have negotiated with Homer, even to the point of having a contract cleared with the respective attorneys, only to have REA threaten to withhold further financing if Homer were to begin generating its own power. Similarly, I would not expect that Pacific Alaska LNG Company can act early (by 1979) to utilize the royalty not taken at Bernice Lake. In contrast, we could begin taking most of the royalty gas almost immediately, and certainly we could take all of it upon completing a pipeline intertie in one year or less. If, because of the apparent competition, sale of this royalty gas were to be submitted to a bidding process, the result might be an even higher price than the present royalty payment and an ultimate sale to a third party (even Phillips) who would not be oriented to solving either our short term or long term needs, or Homer's.



Alaska Gas and Service Company

GENERAL OFFICES LOCATED AT 3000 SPENARD ROAD
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TELEX 25-187

Mr. Bill Rhodes
February 25, 1976
Page Three

I hope that we can reach agreement prior to the meeting of the Royalty Board next Wednesday, March 3. I believe that if you could withdraw from this matter by letter or by so indicating on a copy of this letter, we could expect to obtain this royalty gas at the earliest opportunity, which is in our mutual interest for both the short term and the long term.

Very truly yours,

Dale Teel
President

DT:jdh

bcc: Bill Fackler

AGO 801796



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

RECEIVED
FEB 09 1975

February 3, 1976

ALASKA ROYALTY OIL & GAS BOARD

Mr. Bill Fackler
Executive Director
State of Alaska Oil and
Gas Royalty Board
Department of Natural Resources
Juneau, Alaska

RECEIVED
FEB - 6 1976

Department of
Natural Resources

Dear Bill:

We are continuing our negotiations with the various producers for a supply of natural gas to serve our customers on the North Kenai Road. It now appears that we will be able to continue purchasing from Union-Marathon for the duration of the term of the contract, which is to May 1, 1977. After the remaining reserve quantity has been taken (within a few months from now), we would expect to be paying them the price we offered for state Royalty Gas -- 55.8¢ per MCF.

We have not resolved the longer future of a gas supply for the Kenai Road area, however, and we are continuing negotiations toward that objective.

✓
As to our purchasing Royalty Gas, we have concluded that we probably will have to build a pipeline to move this gas into our pipeline to Anchorage rather than to rely on the paper exchanges we had visualized earlier. This in turn leads us to require a longer term than was proposed by the Royalty Board at the December meeting, since it is impractical for us to try to amortize such a pipeline over the 7 years or less which would be available to June of 1984. For this reason, we ask that the Board should reconsider and allow our purchase of Royalty Gas to continue for the life of production from the North Cook Inlet Gas Field.
✓

We also can foresee the strong desirability or necessity of providing that if we are at times unable to take the full quantity of this Royalty Gas, no penalty should attach to such inability except that we would forfeit the right to receive any gas we were unable to take from day to day. We realize that the producer (Phillips) would have to assent to such a provision and we have not obtained such assent as yet. However, we hope that it can be obtained without undue difficulty.

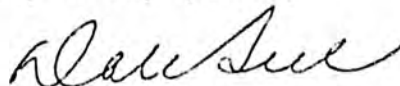
Mr. Bill Fackler
Page #2

While we are continuing our efforts to obtain more gas for the North Kenai Road area directly from the producers, and while we are optimistic about the prospect for success in these efforts, our need for obtaining the Royalty Gas is not diminished. Accordingly, we request that the changes we are proposing above be considered by the Royalty Board at its meeting on February 23.

We also would ask that you confirm the Royalty Board's support of our request to the Alaska Public Utilities Commission with respect to its jurisdiction over Phillips and Phillips' facilities, as Phillips has discussed in their letter of January 9, 1976 (copy enclosed). The need for such support was discussed at the Royalty Board's December meeting, and we would hope that you can so confirm to the Commission at the earliest opportunity. The sooner a waiver is received from the Commission the better will be our prospect of concluding the various negotiations and proceeding toward the necessary pipeline construction.

We will plan to attend the next meeting of the Royalty Board unless we are otherwise advised in the meantime.

Very truly yours,



Dale Teel
President

DT:dh

Enclosure

cc: Mr. John Horn, Phillips
Mr. Bart Emery, Marathon
Mr. Larry Bradford, Union
Mr. Roger Kemppe, City

RECEIVED
FEB 09 1975

ALASKA ROYALTY
OIL & GAS BOARD

→ Transcript of minutes, p 40 + 43, attached were provided by Jo Ann Leach 4/14/77 as satisfying the reference for Bd. support for a waiver from APUC for Phillips pipeline & fac.

AGO 801798



PHILLIPS PETROLEUM COMPANY

BARTLESVILLE, OKLAHOMA 74004

918 661-6600

NATURAL RESOURCES GROUP
Gas and Gas Liquids Division

January 9, 1976

North Cook Inlet Field
Royalty Gas

File: 1-Ho-20-76-G&GL

Mr. Dale Teel
Alaska Gas & Service Company
P. O. Box 6288
Anchorage, Alaska 99502

Dear Dale:

Relative to Alaska Pipe Line's efforts to acquire the State's royalty gas from the North Cook Inlet Field operated by Phillips for purposes of good order, we set forth below certain matters, the satisfactory resolution of which is a necessary prerequisite to any participation by Phillips.

- Where are the differences?*
1. The 5.55¢ per Mcf is not an appropriate place differential for the gas. This is a number that has been worked out and used as a deduction for computing wellhead value of the gas for purposes of paying royalty and taxes. It does not, however, represent what we believe the appropriate differential for the arrangement you contemplate. We are willing to enter into negotiations with you in an effort to arrive at a satisfactory number.
 2. Neither Phillips nor any of its facilities can be subjected to possibility of being classified as a public utility by the Alaska Public Utility Commission. The utility aspects of any exchange of gas involving North Cook Inlet gas or facilities must be resolved to the satisfaction of Phillips prior to Phillips entering any agreements.
 3. Since Marathon Oil Company would be involved in any exchange of North Cook Inlet Field gas, it would be APL's responsibility to work out these arrangements with Marathon.

The above doubtless will not be the only complicating matters to arise, however, we will work with you in an effort to mutually resolve additional problems as they develop.

Very truly yours, AGO 801799

John Horn
John Horn

JH:pla

1.1.1.1 D

Board Meeting Called to Order 10:10 a.m. Dec. 10, 1975,
Chairman Martin brought the board back into session.

Mr. Martin:

We are at the point on the agenda where we take up discussions and reports. Fred I wonder if, Fred Boness from the Attorney General's Office could just briefly outline the report that he filed on the A-G-Phillips situation regard to public utilities.

Fred Boness:

At the last royalty board meeting Phillips raised the possibility that a sale of, or the state taking its gas in-kind might have the effect of subjecting the Phillips pipeline to either FPC or APUC jurisdiction depending on where the gas was sold. Specifically APUC jurisdiction if it was sold to Anchorage Natural Gas Company. I reviewed that possibility and filed a memorandum with the commissioner which indicates that it was my conclusion that there was indeed a possibility that at least limited jurisdiction by the Public Utilities Commission and cited the situation which took place in the Marathon, the Union Marathon Pipeline which exists from the Kenai field to the LNG plant. It does have sales off that to the City of Kenai and Anchorage Natural Gas and there is limited jurisdiction exercised by the PUC in that pipeline. I believe the situation would likely be an analog to the Phillips Pipeline.

Mr. Martin:

Fred, is it your view that, if jurisdiction ^{distinct} applied, and you considered that a likelihood or at least the ~~distinct~~ possibility, could that jurisdiction be waived as a precedent.

Mr. Boness:

The Public Utility Commission does have the authority to grant exemptions under one of its provisions and that could be exercised. The exact, the exact determinance of whether it would be or not specified in the law and it would require a ruling by the APUC.

Mr. Martin:

Do you have any idea, or does anybody have any idea, what might be the time consideration on a waiver at that time?

Mr. Boness:

No, I'm afraid I don't. I haven't talked to the APUC. I would think it would be perhaps two, three-maybe not-I would not think more than six months. Certainly the APUC acts much faster and swifter than the FPC. I think we have that kind of comparison.

End discussion this topic.

guy Martin:

-43-

until all transportation or exchange arrangements have been completed to the satisfaction of the parties involved. Now detailing all aspects of that, I would like to point out some points. First: with regard to the termination date of the contract it is related to the termination of the Phillips contract and the possible implications of a failure Phillips to produce beyond that point. Second; the price is in fact, the highest price in the area and it is my feeling that this is an important aspect of the agreement for the reason that the board may very well, the board and the state may very well, wish from time to time to be in the position of doing something which is unpalatable, as it is in this case, to remove royalty gas from the user that has served an important public purpose in the state. But the board I think and the state will not want to be in position of attempting to set prices from time to time and place to place and to choose from among consumers in the state. The safest and most consistent standard therefore should be the highest price and we intend that this term will bear that out. We have also indicated that the point of delivery will be the wellhead, and, while we believe that will substantially alter the nature of the original offer made by Alaska Pipeline Company, we believe it is quite important that the state not be responsible for that transportation to shore. That is be a negotiated item between Phillips and the purchaser. The state I should say at that point, that after having made this decision, fully intends that the decision be carried out and we think it is in the best public policy that this be carried out. I am requesting now and I think we will be requesting later that some terms of agreement, some measure of agreement, some point of agreement be found between Phillips and A N G for the delivery of this gas. I think that terminates my discussion with the exception of one point and that is that the PUC problem has not been one that has escaped our attention. It's our belief that this is a separate function, not one that the board can control as was suggested in the A N G offer. It was suggested in the A N G offer that the state would be capable of somehow dictating the outcome of that regulatory procedure. This, of course, is not the case, we will not attempt to do so. Now, I will indicate that it will be my intention to communicate the sentiments I just communicated with regard to our desire for success of this sale to the PUC with the request that they formulate the necessary procedures to protect Phillips from regulation in order to make this sale successful. So let me terminate my remarks at this time and ask for the comments and response of the board.

John Horn:

Mr. Chairman, let me make one small comment, the expiration date of our contract with the Japanese is June 1, 1984 rather than May 1.

Mr. Martin:

Thank you, John, very much. I will amend that.

AGO 801801

STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

POUCH M - JUNEAU 99811

Alaska Royalty Oil & Gas Development Advisory Board

January 12, 1976

Mr. Dale Teel
Alaska Pipeline Company
P.O. Box 6288
Anchorage, Alaska 99502

RECEIVED
JAN 20 1976

Department of
Natural Resources

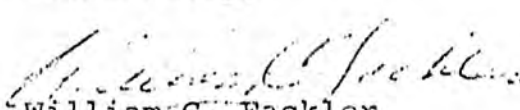
Dear Mr. Teel:

At the January 7, 1976 meeting of the Alaska Royalty Oil and Gas Development Advisory Board I was instructed to write you concerning evidence of your efforts to obtain a gas supply from the local gas producers to replace the "Nikiski" contract.

You will remember that this point was discussed by several members of the Board with you at the December meeting. The Board desires copies of your solicitations to the local producers and their replies to your requests.

I hope that this will not be a great inconvenience to you and that we may expect an early response.

Yours Truly,


William C. Fackler
Executive Director

cc: Board Members

RECEIVED
JAN 20 1976

ALASKA
OIL & GAS BOARD

See enclosures:

Alaska Pipeline Company to Union
Alaska Pipeline Company to Marathon
Letter from Marathon
Letter from Phillips

AGO 801802



PHILLIPS PETROLEUM COMPANY

BARTLESVILLE, OKLAHOMA 74004

918 661-6800

NATURAL RESOURCES GROUP
Gas and Gas Liquids Division

January 9, 1976

North Cook Inlet Field
Royalty Gas

File: 1-Ho-20-76-G&GL

Mr. Dale Teel
Alaska Gas & Service Company
P. O. Box 6288
Anchorage, Alaska 99502

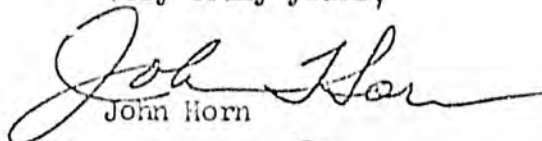
Dear Dale:

Relative to Alaska Pipe Line's efforts to acquire the State's royalty gas from the North Cook Inlet Field operated by Phillips for purposes of good order, we set forth below certain matters, the satisfactory resolution of which is a necessary prerequisite to any participation by Phillips.

1. The 5.55% per Mcf is not an appropriate place differential for the gas. This is a number that has been worked out and used as a deduction for computing wellhead value of the gas for purposes of paying royalty and taxes. It does not, however, represent what we believe the appropriate differential for the arrangement you contemplate. We are willing to enter into negotiations with you in an effort to arrive at a satisfactory number.
2. Neither Phillips nor any of its facilities can be subjected to possibility of being classified as a public utility by the Alaska Public Utility Commission. The utility aspects of any exchange of gas involving North Cook Inlet gas or facilities must be resolved to the satisfaction of Phillips prior to Phillips entering any agreements.
3. Since Marathon Oil Company would be involved in any exchange of North Cook Inlet Field gas, it would be APL's responsibility to work out these arrangements with Marathon.

The above doubtless will not be the only complicating matters to arise, however, we will work with you in an effort to mutually resolve additional problems as they develop.

Very truly yours,


John Horn

JH:bla

AGO 801803

Alaska Royalty Oil & Gas Development Advisory Board

January 2, 1976

Mr. Dale Teel
Alaska Pipeline Company
P.O. Box 6288
Anchorage, Alaska 99502

Dear Mr. Teel:

The Royalty Board has received your letter of December 12 with proposal revision of pages 3 & 4 of your "Draft for Discussion Purposes" dated December 7. The same letter suggested January 2 as a most probable date for your return from vacation.

W. C. Fackler
151-47
In the interest of continued progress in this matter, I am enclosing a copy of the Board provisions included in the Commissioner's proposal for the sale of North Cook Inlet field royalty gas.

Following your review, the Board would appreciate your comments on the provisions.

Yours Truly,



William C. Fackler
Executive Director

Enclosure

AGO 801804

"Commissioner's Proposal in concept" was approved by John Fackler of Royalty Board
has being the above mentioned "Board provisions included in the Commissioner's proposal for the sale of North Cook Inlet field royalty gas"

See also

April 26, 1976

North Cook Inlet Field Royalty Gas
Commissioner's Proposal in Concept

The Commissioner of Natural Resources has recognized that the increasing growth of the Cook Inlet area of Alaska with its resultant increase in the use of natural gas requires that additional natural gas reserves be allocated for that purpose from State of Alaska royalty gas. From the standpoint of size of uncommitted gas reserves, geographical location and possible pipeline access, the North Cook Inlet field royalty gas appears the best available supply at this time. Pursuant to AS 38.05.182 the Commissioner proposes that it is in the best interest of the State to take in kind the State's royalty share of the gas production from the North Cook Inlet gas field and requests the consent of the Alaska Royalty Oil and Gas Development Advisory Board for this change.

The Commissioner further proposes to dispose of the North Cook Inlet field royalty gas to Alaska Pipeline Company and its subsidiaries through a negotiated contract. The proposed contract will contain the following provisions:

1. Purchaser agrees to take 1/8 of daily production from the North Cook Inlet gas field on an if and as deliverable basis for the contract period. The State will report to the Purchaser each month the amount of royalty gas produced by Phillips during the prior months.

The approximate average daily royalty gas share of the production from Phillips' North Cook Inlet field platform is 17,000 MCF. Gas production from the platform varies as LNG plant needs dictate therefore no daily amount can be specified.

2. Point of delivery will be the wellhead.
3. Purchaser is responsible for measurement costs, and any compression or dehydration costs if or when necessary.
4. The contract expires on June 1, 1984, unless extended by mutual agreement for a period not to exceed one year.
5. The price of the gas will be equal to the price the State otherwise would have received from Phillips for its royalty gas for export as LNG to Japan; but not less than the highest price paid by any purchaser in the Cook Inlet area for a similar sale of gas of similar quality. The price will be adjusted yearly on the anniversary date of the contract.

6. The contract shall not be effective until

- all necessary permits and authorizations by governing bodies are obtained

- all transportation or exchange arrangements have been completed to the satisfaction of the parties involved.

- six month's notice required under lease

The Commissioner request approval of the above proposed conceptual plan by the Alaska Royalty Oil and Gas Development Advisory Board.

North Cook Inlet Field Royalty Gas
Commissioner's Proposal in Concept
Procedure

1. Commissioner determines that the best interests of the State are served by the taking in kind of the State's royalty gas share of the production of the North Cook Inlet gas field.

Requires consent of the board.

2. Commissioner determines that it would not be in the best interest of the State to sell the North Cook Inlet field royalty gas by competitive bid.

- a. Requires prior written approval by board.
- b. Requires Commissioner make public in writing the specific findings and conclusions upon which that determination is based.



**Marathon
Oil Company**

Findlay Ohio 45840
Telephone 419/422 2121

December 19, 1975

Mr. Dale Teel, President
Alaska Pipeline Company
P. O. Box 6288
Anchorage, Alaska 99502

Dear Dale:

RE: GAS SUPPLY FOR THE
NORTH KENAI ROAD AREA

This will acknowledge receipt of your letter dated December 12, 1975, and the attachments thereto, in connection with the above referenced subject.

Marathon is not presently in a position to discuss a long term commitment of up to 50 BCF of our Cook Inlet Area gas reserves.

We are fully aware of your supply situation on the North Kenai Road and we are willing to enter into a new short-term contract with you similar to our existing contract of May 1, 1967, with appropriate changes to fit current circumstances and subject to the following general quantity and price provisions: ✓

1. The contract expiration date would be May 1, 1978, or until the seller has delivered a total additional five (5) BCF of gas, whichever occurs first. If your company were to contract for one-half of this volume from some other company, this volume would be reduced by one-half or to 2-1/2 BCF. ✓
2. The price for the additional gas would be 55.8¢ per MCF in accordance with your offer. This price would become effective for gas taken after your present commitment of ten (10) BCF has been delivered. ✓

Alaska Pipeline Company
December 19, 1975
Page 2

We recognize that the foregoing proposal will not solve your long-term supply problem, but we feel it will provide you sufficient time to further consider your supply situation.

If the foregoing proposal is of interest to you, I would be glad to meet with you sometime during the week commencing January 12, 1976, to discuss this matter further. Please let me know as soon as possible if you desire such a meeting.

Yours very truly,

W. B. Emery II
W. B. Emery II

WBEKK:sm

AGO 801810



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

December 12, 1975

DUPLICATE
ORIGINAL

Mr. Bart Emery
Marathon Oil Company
539 South Main Street
Findlay, Ohio 45840

Dear Bart:

The State of Alaska Oil and Gas Royalty Board has voted to authorize the Commissioner of Natural Resources (Guy Martin) to negotiate the sale of North Cook Inlet Gas Field royalty gas to us, subject to final approval at the Board's January meeting and then approval of the legislature.

(Sawdusky)

I have sent Sam informally copies of all correspondence, etc. in this matter except the enclosed preliminary drafts of proposed memoranda of agreement (APC with Union as operator, and APC with State); letters of support by City and Chugach; and the material I obtained at the Board meeting of December 10.

Board member (Dr.) Arlon Tussing (University of Alaska Economist) questioned whether or not we had diligently tried to get gas from "others," and I expect he will inquire further on this point at the January meeting. The vote was unanimous, with that reservation. Accordingly, I am writing now to ask whether or not Marathon would be willing to offer us our requirements up to 50 BCF over a period prior to June 1, 1984. Deliverability would be up to 15 MMCFD; take or pay at 10 MMCFD; delivery at any combination of the Kenai master meter and the three existing taps on your Kenai to Nikiski pipeline; at the price of \$5.8¢ per MCF but not less than the highest price paid by any purchaser in the Cook Inlet area for a similar sale of gas of similar quality, adjusted yearly on the anniversary date of the contract, provided that we would have the option to terminate on one year's notice upon paying such higher price.

This same proposition was mentioned to John Horn of Phillips verbally, and his response was that since the royalty purchase (by others than us) would not be eliminated by such a decision, he would prefer to see us proceed to

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

Mr. Bart Emery
December 12, 1975
Page 2

take the royalty. If you, or Union, would prefer to sell to us at these terms, from either of you individually or as equal partners, rather than for us to take this 50 BCF of North Cook royalty, I would like to discuss it further with you at the earliest opportunity. If you are not interested in this proposition, I would like to have it of record in order to have an answer for Dr. Tussing. Also, we would have to work out a short term and long term solution to a gas supply for the North Kenai Road area: we expect to be out of the present 10 BCF in April 1976, but even without delay or opposition we may not be lined up for North Cook Inlet gas before that date or maybe even six months after that date. I would propose for your consideration that we should "borrow" gas from the "Anchorage" contract, on the basis that we would repay through exchange from royalty gas in the ratio of 2 to 1, or, if we do not get gas to exchange, we would need to have one year's extension of the Nikiski contract at the present price etc., but agree that all deliveries we take from you during that period would reduce the "Anchorage" reserve dedication by 200% of the amount of deliveries actually taken at the pipeline taps on the North Kenai Road. In this way we could live with our existing rate structure but would have compelling reason to resolve the supply situation as soon as possible.

I hope that we can get together with Sam and Al here to work out the "exchange" for royalty gas as an operating problem in the event that is the course to be taken. In the event of getting a supply from you instead of royalty gas, I would like to have a meeting with you at the earliest available date in order to be ready at the January meeting of the Royalty Board (or sooner).

Season's greetings to you - it seems December just isn't my month to relax these days, remembering last year and the prior contract anniversary dates.

Cordially,

Dale Teel
President

DT/j

cc: Sam Sandusky

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

Mr. Bart Emery
December 12, 1975
Page 3

Enclosures

- *Memorandum with Union as Operator (Draft Proposal)
- *Memorandum with State of Alaska (Draft Proposal)
- Letter of December 6 from Phillips Petroleum Company
- Commissioner's Presentation to Royalty Board, December 10

- *With transmittal letter dated December 7



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

December 12, 1975

DUPLICATE
ORIGINAL

Mr. Larry Bradford
Union Oil Company of California
P. O. Box 7600
Union Oil Center
Los Angeles, California 90017

Dear Larry:

✓ The State of Alaska Oil and Gas Royalty Board has voted to authorize the Commissioner of Natural Resources (Guy Martin) to negotiate the sale of North Cook Inlet Gas Field royalty gas to us, subject to final approval at the Board's January meeting and then approval of the legislature.

What?
I have sent Gene ^(Griffin - Union) informally copies of all correspondence, etc. in this matter except the enclosed preliminary drafts of proposed memoranda of agreement (APC with Union as operator, and APC with State); letters of support by City and Chugach; and the material I obtained at the Board meeting of December 10.

✓ Board member (Dr.) Arlon Tussing (University of Alaska Economist) questioned whether or not we had diligently tried to get gas from "others," and I expect he will inquire further on this point at the January meeting. The vote was unanimous, with that reservation. Accordingly, I am writing now to ask whether or not Union would be willing to offer us our requirements up to 50 BCF over a period prior to June 1, 1984. Deliverability would be up to 15 MMCFD; take or pay at 10 MMCFD; delivery at any combination of the Kenai master meter and the three existing taps on your Kenai to Nikiski pipeline; at the price of 55.8¢ per MCF but not less than the highest price paid by any purchaser in the Cook Inlet area for a similar sale of gas of similar quality, adjusted yearly on the anniversary date of the contract, provided that we would have the option to terminate on one year's notice upon paying such higher price.

This same proposition was mentioned to John Horn of Phillips verbally, and his response was that since the royalty purchase (by others than us) would not be eliminated by such a decision, he would prefer to see us proceed to

AGO 801814

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

Mr. Larry Bradford
December 12, 1975
Page 2

take the royalty. If you, or Marathon, would prefer to sell to us at these terms, from either of you individually or as equal partners, rather than for us to take this 50 BCF of North Cook royalty, I would like to discuss it further with you at the earliest opportunity. If you are not interested in this proposition, I would like to have it of record in order to have an answer for Dr. Tussing. Also, we would have to work out a short term and long term solution to a gas supply for the North Kenai Road area: we expect to be out of the present 10 BCF in April 1976, but even without delay or opposition we may not be lined up for North Cook Inlet gas before that date or maybe even six months after that date. I would propose for your consideration that we should "borrow" gas from the "Anchorage" contract, on the basis that we would repay through exchange from royalty gas in the ratio of 2 to 1, or, if we do not get gas to exchange, we would need to have one year's extension of the Nikiski contract at the present price etc., but agree that all deliveries we take from you during that period would reduce the "Anchorage" reserve dedication by 200% of the amount of deliveries actually taken at the pipeline taps on the North Kenai Road. In this way we could live with our existing rate structure but would have compelling reason to resolve the supply situation as soon as possible.

I hope that we can get together with Gene here to work out the "exchange" for royalty gas as an operating problem in the event that is the course to be taken. In the event of getting a supply from you instead of royalty gas, I would like to have a meeting with you at the earliest available date in order to be ready at the January meeting of the Royalty Board (or sooner).

Season's greetings to you - it seems December just isn't my month to relax these days, remembering last year and the prior contract anniversary dates.

Cordially,

Dale Teel
President

DT/j
cc; Gene Griffin

AGO 801815

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

Mr. Larry Bradford
December 12, 1975
Page 3

Enclosures

- *Memorandum with Union as Operator (Draft Proposal)
- *Memorandum with State of Alaska (Draft Proposal)
- Letter of December 6 from Phillips Petroleum Company
- Commissioner's Presentation to Royalty Board, December 10

- *With transmittal letter dated December 7



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

December 12, 1975

Mr. Guy Martin
Commissioner of Natural Resources
State of Alaska
Juneau, Alaska

Dear Commissioner Martin:

I have revised pages 3 and 4 of the "Draft for Discussion Purposes," dated December 7 to reflect my understanding of the resolution of the Royalty Board on December 10, and to update the pricing which was given to me that day by Mr. John Horn of Phillips.

I will be available here until December 18 and expect to be back about January 2 (maybe December 29) and hope we can make some further progress either by telephone, mail, or a further meeting.

As you will see, I have copied Union, Marathon and Phillips in order to keep them apprised of developments in this matter.

Very truly yours,

Dale Teel
President

DT/j

cc: Bradford, Griffin (Union)
Emery, Sandusky (Marathon)
Horn, Swetnam (Phillips)

RECEIVED
DEC 16 1975

ALASKA ROYALTY
OIL & GAS BOARD

RECEIVED
DEC 15 1975

Department of
Natural Resources

- 3 -

4. It is of the essence of this Agreement that no regulatory jurisdiction of the Alaska Public Utilities Commission or other regulatory authority shall attach to Phillips or to Union as a consequence of the sale of the State royalty gas to APC under this Agreement, it being clearly understood that the utilization of "exchange" rather than literal transfer of the State royalty gas is done at the request of and for the convenience of the State and APC and not at the request of or for the benefit of either Union or Phillips. It is further understood and agreed that in the event this agreement is ever interpreted or used by the Alaska Public Utilities Commission or any other administrative or legislative or judicial body or agency, whether federal, state, or other, to assert and implement such regulatory jurisdiction, then this agreement shall terminate and become null and void.
5. At the date of the Agreement, the following are in effect with respect to royalty gas:

Price at wellhead: 50.25¢ per MCF

Charge for delivery from
North Cook Inlet Gas Field
to Phillips LNG Plant on the
North Kenai Road

5.55¢

Note: these prices
are only estimates
- subject to
verification

Total 55.80¢ per MCF

In the event a higher wellhead price than stated above is paid in the Cook Inlet Area (as defined in APC's contract with Union as amended effective December 18, 1974), by any purchaser for a similar sale of gas of similar quality, APC shall have the option (a) to meet such higher wellhead price as of the anniversary date of deliveries under this contract, and continue purchasing the royalty gas, or (b) to give the State one year's notice of termination of this Agreement, it being understood that during said notice period APC shall nevertheless continue to purchase whatever amount of royalty gas may be available to APC as described herein, at the higher price.

6. The Agreement shall be binding upon its execution and the approval of the legislature of the State of Alaska, but deliveries hereunder shall not commence until the date (a), all the gas reserves available to APC from Union by the terms of APC's

- 4 -

contract with Union dated May 1, 1967 have been purchased by APC or (b), May 1, 1977, whichever shall occur first.

Unless terminated as provided herein, this Agreement shall continue in effect until June 1, 1984.

for Alaska Pipeline Company
Its _____

For the State of Alaska
Its _____



ALASKA PIPELINE COMPANY

P. O. BOX 6288
ANCHORAGE, ALASKA 99502

3000 SPENARD ROAD
PHONE (907) 277-5551

December 7, 1975

RECEIVED
DEC 8 1975

**ALASKA ROYALTY
OIL & GAS BOARD**

Mr. Guy Martin, Commissioner
Department of Natural Resources
State of Alaska
Juneau, AK 99801

Dear Commissioner Martin:

Enclosed are 10 copies of my drafts of the elements of proposed general provisions which could be embodied in contracts for our purchase of State royalty gas from the North Cook Inlet Gas Field. I do not want to represent that these drafts have had legal consideration, but only that they indicate my ideas of the intent of contracts which would have to be negotiated.

I believe that we should and can hope that Union and Phillips will agree that the transaction as described offers great benefit to the majority of Alaskans without unreasonable or unfair impact on them.

We must hope that the general context and intent of these drafts can be endorsed by the State so that we can obtain a final decision in time to assure uninterrupted service to our customers on the North Kenai Road.

I will be arriving in Juneau Monday night and be available for discussion of our position on Tuesday and Wednesday.

Very truly yours,

Dale Teel
President

DT:jdh

Enclosures

cc: Each member of the Royalty Board
Alaska Public Utilities Commission
Municipality of Anchorage
Chugach Electric Association, Inc.

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

NORTH COOK INLET STATE ROYALTY GAS
SALE TO ALASKA PIPELINE COMPANY
("Anchorage Natural Gas")

This memorandum ("Agreement") reflects the intent of the State of Alaska ("the State") and Alaska Pipeline Company ("APC") regarding APC's purchase of the State's 1/8th (one-eighth) royalty share of natural gas produced at the North Cook Inlet Gas Field, which is operated by Phillips Petroleum Company ("Phillips").

WHEREAS, APC has an early and urgent need to purchase additional natural gas for its customers in the vicinity of the North Kenai Road, and has applied to the State to acquire the State's 1/8th royalty share of gas produced by Phillips at the North Cook Inlet Gas Field to the extent any portion or all of such royalty gas may be available to APC without causing additional investment by Phillips or additional operating expense by Union Oil Company of California ("Union"), and

WHEREAS, Union as Operator of the Kenai Gas Field and the gas transmission line in the North Kenai Road now supplies APC's total requirements for natural gas at the Kenai Gas Field and at three (3) pipeline taps on the North Kenai Road and will continue to do so subject to terms and conditions of APC's various contracts and agreements with Union which contemplate or would allow APC's purchasing variable amounts of this royalty gas on an "if and as available" basis, and

WHEREAS, the royalty gas and the Kenai Field Gas are sufficiently similar that exchange rather than literal transfer of the royalty gas will be of advantage to all the parties concerned including APC's ultimate gas consumers and such exchange is entirely practical because of the Kenai Gas Field's inter connection with the North Cook Inlet Gas Field which has allowed exchanges to be made from time to time in the past, and

WHEREAS, the proposed sale of the royalty gas is seen to be in the public interest of the citizens of Alaska and the gas consumers served by APC (as evidenced by various statements which are of public record),

NOW THEREFORE, the State and APC agree as follows:

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

- 2 -

1. The State will report to APC each month the amount of royalty gas produced by Phillips during the prior month, together with a schedule showing the amount of such gas produced each day of the prior month.
2. Within one month following receipt of the data from the State (per paragraph (1) above), APC will obtain from Union an analysis of the amount of royalty gas which shall be deemed by all parties to have been sold to APC by the State, and APC shall pay therefor to the State within 30 days thereafter, at the price which otherwise would have been payable to the State by Phillips, and pay to Phillips the transportation charge thereon which otherwise would have been in effect received by Phillips for delivery of North Cook Inlet gas to the Phillips LNG plant on the North Kenai Road.
3. It is the intent of APC and the State that APC will pay the State for and will be deemed to have received from the State whatever quantity of gas (from 0% to 100% of the total quantity of royalty gas produced by Phillips) which Union shall determine to be appropriate in the circumstances and to be supportable by meter readings and calculations which Union and APC and the State will maintain on file, and available for release to any interested party on request. It is the further intent of the State and APC that the determination of how much of the State's total royalty share of natural gas produced from the North Cook Inlet Gas Field by Phillips can be deemed to have been sold to APC will be the responsibility of Union, as Operator of the Kenai Gas Field and the gas transmission line in the North Kenai Road.

In making said determination, Union shall use reasonable discretion and judgment in balancing and accounting for gas supplied to APC from the Kenai Gas Field and from the North Cook Inlet Gas Field. No other responsibility shall derive to Union as a result of this Agreement, nor shall this Agreement be used to impose any obligation on Union which would cause increased operating expense to Union or to impose any obligation on Phillips which would require Phillips to add investment for transmission (or compression) without compensation therefor which is reasonable and acceptable to Phillips. In the event such investment becomes necessary for Phillips, APC would have the option either (a) to participate equitably in that investment, or (b) to agree to compensate Phillips at an agreed price per MCF or per month, or (c) to terminate its taking of royalty gas within one year of the date when these options are presented to APC for decision.

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

- 3 -

4. It is of the essence of this Agreement that no regulatory jurisdiction of the Alaska Public Utilities Commission or other regulatory authority shall attach to Phillips or to Union as a consequence of the sale of the State royalty gas to APC under this Agreement, it being clearly understood that the utilization of "exchange" rather than literal transfer of the State royalty gas is done at the request of and for the convenience of the State and APC and not at the request of or for the benefit of either Union or Phillips. It is further understood and agreed that in the event this agreement is ever interpreted or used by the Alaska Public Utilities Commission or any other administrative or legislative or judicial body or agency, whether federal, state, or other, to assert and implement such regulatory jurisdiction, then this agreement shall terminate and become null and void.
5. At the date of the Agreement, the following are in effect with respect to royalty gas:

Price at wellhead:	45¢ per MCF	Note: these prices are only estimates-- subject to verification
Charge for delivery from North Cook Inlet Gas Field to Phillips LNG Plant on the North Kenai Road	<u>5.45¢</u>	
Total	50.45¢ per MCF	

In the event Phillips may offer the State a higher wellhead price than stated above, as a result of repricing of gas exported as liquid (LNG) to Japan, APC shall have the option (a) to meet such higher wellhead price and continue purchasing the royalty gas, or (b) to give the State one year's notice of termination of this Agreement, it being understood that during said notice period APC shall nevertheless continue to purchase whatever amount of royalty gas may be available to APC as described herein, at the higher price offered by Phillips.

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

- 4 -

In the event Phillips' export of North Cook Inlet gas as LNG to Japan is terminated and Phillips continues to produce gas at the North Kenai Gas Field for any other disposition, then the price of royalty gas sold to APC hereunder shall be not less than the average price during the year prior to the termination, nor less than the average price paid by APC for gas it purchased from others during the prior year (which after December 31, 1985 will be the "area price" as defined in APC's contract with Union as amended effective December 18, 1974).

6. The Agreement shall be binding upon its execution and the approval of the legislature of the State of Alaska, but deliveries hereunder shall not commence until the date (a), all the gas reserves available to APC from Union by the terms of APC's contract with Union dated May 1, 1967 have been purchased by APC or (b), May 1, 1977.

Unless terminated as provided herein, this Agreement shall continue in effect until the end of commercial production of natural gas from the North Cook Inlet Gas Field or the end of commercial production of natural gas from the Kenai Gas Field, whichever shall occur first.

For Alaska Pipeline Company
Its _____

For the State of Alaska
Its _____

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

MEMORANDUM OF UNDERSTANDING

This memorandum reflects the intent of Union Oil Company of California ("Union") as Operator of the Kenai Gas Field and a gas transmission line in the North Kenai Road for the interest of both Union and Marathon Oil Company ("Marathon") with respect to the natural gas requirements of Alaska Pipeline Company ("APC") at the Kenai Gas Field and from three (3) pipeline taps in the North Kenai Road. Union-Marathon have supplied this service under contracts as amended from time to time, since the first advent of natural gas service in Alaska in 1961. The parties recognize that APC has applied for and expects to purchase the State of Alaska's 1/8th (one-eighth) royalty share of gas produced at the North Cook Inlet Gas Field by Phillips Petroleum Company, which is brought to the North Kenai Road by Phillips' pipeline for liquefaction and export to Japan. Since Phillips' pipeline is interconnected with Union-Marathon's pipeline at or near the North Kenai Road, and since the composition of North Cook Inlet gas is virtually identical to Kenai field gas, the sale of this royalty gas can in effect be accomplished by "exchanges" such that literal delivery of this gas need not be made.

Existing meters can be utilized to account for the amount of North Cook Inlet gas field production and thus the amount of royalty gas; together with data from other meters, displacement or "exchanges" can be postulated by accounting rather than any additional metering or literal physical transfer of North Cook Inlet gas to APC.

Union as Operator is agreeable to providing an analysis of data furnished to Union by the State of Alaska (or Phillips) and by APC and from Union's various meters, and calculating the net result of the displacement or "exchanges" which APC's purchase of State royalty gas will entail.

Union will analyze the data furnished to them each month and advise the various parties (Marathon, Phillips, State of Alaska, U.S.G.S., and APC) of the amount of North Cook Inlet gas which is to be deemed by all parties to have been taken by APC from the State of Alaska for payment purposes. Union, as Operator of the Kenai gas field, will advise these parties and will calculate the net quantity of gas which is to be deemed to have been taken from the Kenai gas field.

ALASKA PIPELINE COMPANY

ANCHORAGE, ALASKA

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The parties understand and agree that neither this memorandum nor any other aspect of APC's purchasing State royalty gas shall incur for Union any responsibility whatsoever, other than the derivation and calculation of the amount of State royalty gas for which APC is to make payment to the State of Alaska.

As Operator of the Kenai Gas Field and the Kenai North Road gas transmission line, Union will continue delivering gas to APC at the Kenai gas field and at the three (3) pipeline taps now existing, and will rely on APC to cause the State of Alaska (Phillips) to operate as necessary so that no additional deliverability (demand) is imposed, above the contractual amount of 160,000 MCF per day plus the excess, if any, of State royalty gas above the amount of gas taken by APC at the three pipeline taps on the North Kenai Road. As Operator, Union would be free to work out whatever production scheduling it deems appropriate, directly with Phillips, so that no additional operating expense will accrue to Union; however, Union will not impose any unreasonable schedule on Phillips.

At such times as Phillips may be unable to meet the production scheduling desired by Union, then APC agrees to accept whatever production scheduling may be mutually satisfactory to Union and Phillips; and if no such production scheduling can be agreed upon or cannot be made by Phillips, then and to that extent neither Phillips nor Union shall become liable in consequence. It is the good faith of APC and Union that APC will receive the State royalty gas only to the extent it may be available without additional investment for transmission (or compression) by Phillips or Union, provided however, that in the event royalty gas available to APC is less than 10,000 MCF per day, then Union will provide the difference for a period of not less than one year. APC would expect to have the option, in the event investment is necessary for Phillips to continue delivering State royalty gas, to participate equitably in that investment, or to pay a mutually acceptable price per MCF or per month therefor, or to terminate its taking of the State royalty gas.

APC will pay to Union, for its services as Operator in this arrangement, the amount of 2 per MCF of State royalty gas purchased hereby, but not less than 2 per month, plus the price Union may elect to apply to any gas taken at the three pipeline taps and not returned by exchange within one year of such delivery.

DT/js

AGO 801826



Alaska Gas and Service RECEIVED

GENERAL OFFICES LOCATED AT 3000 SHERARD ROAD
P. O. BOX 6288 ANCHORAGE, ALASKA 99502 / PHONE (907) 277-5555
TELEX 25-187

Department of
Natural Resources

December 2, 1975

Alaska Public Utilities Commission
1100 MacKay Building
338 Denali Street
Anchorage, 99501

Gentlemen: Filing of Special Contract
with
Chugach Electric Association

Our filings for permanent and revised interim rates did not include Rate PI, which theretofore was in effect only for the Bernice Lake power plant of Chugach Electric Association. As contemplated in those filings, Rate PI has been extinguished. Service to this power plant is now made by a special contract which reflects the same price and general terms which are contained in the special contract for service to the municipality's power plants in Anchorage -- that contract having been approved by Order of the Commission on August 30, 1974 (Docket U-74-83). Copy of the special contract with Chugach is enclosed for the Commission's information and file, since by its terms it is subject to acceptance by the Commission.

Our stipulation with Alaska Legal Services and the Order of the Superior Court dated November 12, 1975 anticipated the extinguishment of Rate PI and the establishment of revised interim rates (special contract provisions) for service to power plants, and the special contract with Chugach is consistent with that stipulation and Order.

Our testimony to the Commission on October 30 and 31 in Docket U-75-68 (requesting reinstatement of our flow through provisions tariff Sections 708 and 709) also anticipated the extinguishment of Rate PI and the negotiation of this special contract for service to Chugach's Bernice Lake power plant.



Alaska Gas and Service Company

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TELEX 25-197

Alaska Public Utilities Commission
December 2, 1975
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This special contract is also consistent with and was anticipated in our informal discussions with various members of the Commission and its staff in connection with our proposed purchase of State royalty gas from the North Cook gas field. Our presentations to the State of Alaska Oil and Gas Royalty Board of October 10 and November 10 in support of this proposal also anticipated this special contract with Chugach and the extinguishment of Rate PI. We believe that our application to purchase this royalty gas may be considered or decided by the Royalty Board on December 10, as to policy rather than detailed or final action. This special contract and our tariff Section 708 are key elements for that transaction.

We believe that both the municipality and Chugach will affirmatively support our application for the royalty gas, and we would also hope that the Commission will do so also, prior to the December 10 meeting.

For all the reasons given, we request that the Commission should give emergency attention to and acceptance of the enclosed special contract with Chugach and to the reinstatement of Section 708 of our tariffs, so that our position to the Royalty Board will be clearly established prior to the meeting of December 10.

Very truly yours,

Dale Teel
President

DT/js

cc: Mr. L. J. Schultz, General Manager
Chugach Electric Association
Mr. Roger Kempel, Attorney
Municipality of Anchorage
Mr. Guy Martin ✓
Commissioner of Natural Resources

AGO 801828

TO:

Guy R. Martin
Commissioner

DATE : November 19, 1975

FROM:

William C. Fackler
Deputy Commissioner

SUBJECT:

Analysis of North Cook Inlet
Royalty Gas Proposal by
Alaska Natural Gas

Anchorage Natural Gas (ANG) proposes that State take North Cook Inlet Field gas royalty in-kind and sell to ANG at same rate as State now receives in royalty payments from Phillips.

Daily volume dependent on LNG plant use but ANG used average of 15 mmcf/d, total of 75 bcf for contract over 15 year period as basis for proposal.

Reference ANG brochure "Summary" page 1.

1. ANG will take delivery immediately on "if and as available" basis and pay price State now receives.

This statement is apparently based on assumption that ANG will simply replace State and receive gas at LNG plant gate with payment to State at present royalty rate of 50.45 cents per MCF at the plant gate. This price includes a 5.45¢ per MCF transport charge from platform to LNG plant.

There are two problem areas.

- a. Transport of ANG gas for resale from platform to shore might be construed as qualifying the pipeline for APUC jurisdiction. If so, PPCO would ^{probably} object. Also 5.45¢ per M transport charge