

SCOMM

#46:21

PRELIMINARY SETTLEMENT AGREEMENT

The State of Alaska, Department of Natural Resources (DNR) and Chugach Electric Association, Inc. (Chugach) enter into the following conditional agreement concerning pending disputes and litigation concerning the valuation of the State's royalty share of gas:

(1) DNR and Chugach will vigorously support passage of the CS for SB 309 Resources (a copy of which is attached) (the Legislation), subject to mutually agreed-to amendments;

(2) DNR and Chugach agree to resolve the disputes at issue in ARCO Alaska, Inc. v. State of Alaska, Department of Natural Resources, and Chugach Electric Association, Inc., Case No. 3AN-85-6218 Civil, Chevron U.S.A. Inc. v. State of Alaska, Department of Natural Resources, and Chugach Electric Association, Inc., Case No. 3AN-85-7617 Civil, and Shell Western E&P, Inc. v. State of Alaska, Department of Natural Resources, Case No. 3AN-85-7633 Civil (collectively, the "Beluga River gas royalty litigation") concerning the royalty valuation of gas sold under Chugach's 1973 contracts with ARCO Alaska, Inc. (ARCO). Chevron U.S.A. Inc. (Chevron) and Shell Western E&P, Inc. (SWEPI) in accordance with the following terms:

(a) Supplemental gas for peak supply periods: the contract price, including all forms of consideration;

(b) Non-supplemental gas volumes for gas produced on or after April 15, 1985: 75 cents per mcf during 1985 and 1986, subject to ^{the contract} annual adjustment on the first day of each January in

proportion to the amount of increase or decrease in the United States of America GNP price deflator over the previous year. Payments for royalties from April 15, 1985 until the date of final settlement will be paid over three years plus interest subject to APUC approval;

(c) The dispute concerning royalty liability on tax reimbursement amounts on gas for the period prior to April 15, 1985: will be resolved in good faith negotiations between the DNR, Chugach and the Beluga River lessees (ARCO, Chevron and SWEPI);

(3) These agreements concerning settlement of the Beluga River gas royalty litigation are conditioned upon the following events:

- (a) Approval by the Chugach Board of Directors;
- (b) Passage of the Legislation;
- (c) Agreement with the Beluga River lessees (with regard to the post-April 15, 1985 royalty issues);
- (d) Court approval of the settlement; and

(4) Any remaining issues or disputes not specifically identified will be resolved by good faith negotiations.

CHUGACH ELECTRIC ASSOCIATION, INC.

Dated: _____

By: Joyce Murphy
President of the Board

ALASKA DEPARTMENT OF NATURAL RESOURCES

Dated: _____

By: Esther C. Wunnicke
Commissioner

STATE OF ALASKA
THE LEGISLATURE

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99811
907-465-3800

LEGISLATIVE AFFAIRS AGENCY

MEMORANDUM

February 25, 1986

SUBJECT: Sectional analyses of CSSB 309(Res), SB 309,
HB 403, SSHB 425 and HB 374

TO: Representative Marco Pignalberi

FROM: Theresa L. Bannister *TB*
Legislative Counsel

This memo contains the comparative sectional analysis that you requested for SB 309 and the statutes it amends, and the comparative sectional analyses that you requested for CSSB 309(Res), SB 309, HB 403, SSHB 425, and HB 374.

1. Comparative sectional analysis between SB 309 and the statutes it amends.

SB 309 adds a new section ((aa)) to the main oil and gas leasing section, AS 38.05.180, to deal with the valuation of natural gas taken in value by the state under an oil and gas lease issued under AS 38.05.180(f). There does not appear to be another section that deals with the criteria for such valuation. Section 2 of CSSB 309(Res) also adds a new section ((aa)) to the main oil and gas leasing section, AS 38.05.180, to allow the commissioner under specified conditions to amend existing an lease (at the request of a lessee) to value the state's in value royalty gas at the price paid for the gas by nonprofit electrical utilities to the lessee. Section 3 of CSSB 309(Res) allows the commissioner to sell in-kind royalty gas to a nonprofit electric utility at less than market value under certain conditions. AS 38.05.810(a) is the general provision for allowing sale of royalty resources under certain conditions at less than appraised value, and its valuation language is slightly different from that of CSSB 309(Res). Section 4 was added to CSSB 309(Res) to clarify that its language would govern state sales of royalty gas to nonprofit public electric utilities at less than market value.

2. Comparative sectional analyses of CSSB 309(Res), SB 309, HB 403, SSHB 425, and HB 374.

Section 1 of SB 309, HB 403, and SSHB 425 provide the legislative findings for the bills, are the same, and primarily state that the valuation of in value royalty gas must be based on the contract price of the gas rather than on the current market value of the gas. There are no findings in HB 374. The findings in CSSB 309(Res) deal primarily with the advisability of (1) allowing the commissioner to establish the value for in-value royalty gas sold to a nonprofit electric utility by using the contract price between the utility and the lessee, (2) giving the commissioner the authority to sell royalty gas to a nonprofit electric utility at less than market value, and (3) establishing a separate state policy for royalty gas being sold to nonprofit electric utilities for in-state generation of electricity.

Section 2 of SB 309, HB 403, and SSHB 425 are very similar, but do contain differences. Section 2 of SB 309 is not clear, but it appears to be attempting to state that royalty gas taken in value is to be valued by the state at the price of the lessee's long-term contract with a purchaser of the gas, unless clear and convincing evidence shows that the contract price was unreasonably low at the time the contract was entered into. Section 2 of HB 403 prohibits the commissioner from adjusting the valuation price for in-value royalty gas to the current market value if the royalty gas is measured by a long-term contract price and if the change would increase consumer prices, unless the commissioner determines in a writing supported by clear and convincing evidence that the long-term contract price is unreasonably low. Section 2 of SSHB 425 is not completely clear but appears to prohibit the state from valuing in-value royalty gas at a price greater than the price received for the gas under the long-term sales contract for the gas, unless clear and convincing evidence shows that the long-term contract price was unreasonably low at the time of contract. Section 2 of SB 309 and HB 403 apply to royalties from oil and gas leases entered into under (f) of AS 38.05.180; section 2 of HB 425 applies to royalties from oil and gas leases entered into under AS 38.05.180 generally. Section 2 of CSSB 309(Res) allows the commissioner, under certain conditions and upon the written request of an oil or gas lessee, to agree with the lessee to use the price contained in the lessee's sales contract to a nonprofit electrical utility as the valuation price for the royalty gas.

Representative Marco Pignalberi
Page 3
February 25, 1986

HB 374 is not comparable to section 2 of SB 309, HB 403, or SSHB 425, but is comparable to section 3 of CSSB 309(Res). HB 374 clarifies that a disposal of natural gas may be made to certain utilities for less than the appraised value determined under AS 38.05.810(a). Section 3 of CSSB 309(Res) allows the commissioner to sell in-kind royalty gas at less than the market value if the commissioner makes a written finding that the sale is in the best interest of the state. (See part 1 of this memo for the analysis of sec. 4 of CSSB 309(Res)).

Section 3 of SB 309 and HB 403 are identical applicability sections and apply the Act to leases issued before or after the effective date of the Act. Section 3 of SSHB 425 is nearly identical to SB 309 and HB 403, but makes the Act also apply to leases issued on the effective date of the Act. HB 374 has no provision comparable to sec. 3 of SB 309, HB 403, or SSHB 425. Sections 5 and 6 of are the applicability sections of CSSB 309; section 5 makes section 2 of the Act apply to royalty gas sales contracts by oil and gas lessees entered into on or after the effective date of the Act; section 6 makes the sales authority of the commissioner in section 4 apply to state contracts entered into on or after the effective date of the Act to sell new quantities of royalty gas to nonprofit electric utilities. CSSB 309(Res)

Section 4 of SB 309 gives the Act an immediate effective date. Section 4 of HB 403, section 4 of HB 425, and Section 7 of CSSB 309(Res) are the same. HB 374 has no effective date clause.

TLB:mkr
m3/077

Introduced: 5/4/85
Referred: Resources

1 IN THE SENATE

BY FAIKS, KELLY AND V. FISCHER

2

SENATE BILL NO. 309

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IN THE LEGISLATURE OF THE STATE OF ALASKA

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FOURTEENTH LEGISLATURE - FIRST SESSION

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A BILL

6 For an Act entitled: "An Act relating to the royalty value of a natural
7 gas lease on state land; and providing for an effective
8 date."

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. FINDING. The legislature finds that to provide for the
11 utilization, development and conservation of gas resources for the maximum
12 benefit of the people of the state, the value of production of gas for
13 purposes of computing the royalty reserved to the state must be based
14 primarily on the contract price of gas rather than the current market value
15 of the gas. This will encourage stable markets, promote investment, assure
16 reasonable energy prices and provide the maximum benefit to the people of
17 the state.

18 * Sec. 2. AS 38.05.180 is amended by adding a new subsection to read:

19 (aa) Notwithstanding other provisions of this section, if the
20 royalty share of natural gas reserved to the state under a lease
21 issued under (f) of this section is taken in value, the value of
22 production sold under a long-term sales contract may not be greater
23 than the price received for the production under the long-term sales
24 contract unless it is shown by clear and convincing evidence that the
25 long-term contract price was unreasonably low at the time of contract.

26 * Sec. 3. This Act applies to leases issued before or after the effective
27 date of this Act.

28 * Sec. 4. This Act takes effect immediately in accordance with AS 01.-
29 10.070(c).

Offered: 2/20/86
Referred: Rules

Original sponsors: Faiks, Kelly
and V.Fischer

1 IN THE SENATE

BY THE RESOURCES COMMITTEE

2

CS FOR SENATE BILL NO. 309 (Resources)

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IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FOURTEENTH LEGISLATURE - SECOND SESSION

5

A BILL

6

For an Act entitled: "An Act relating to royalty gas contracts; and pro-

7

viding for an effective date."

8

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9

* Section 1. FINDINGS. (a) The legislature finds that the best inter-

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est of the state will be served if the commissioner of natural resources is

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authorized to establish the value for royalty gas taken in value by the

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state and sold to a nonprofit electric utility by using the contract price

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between the lessee of the state and the nonprofit electric utility, whether

14

or not the royalty gas lease with the state establishes a different stan-

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dard for the valuation and if the lessee and the nonprofit electric utility

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are not related to each other. The legislature finds that this authoriza-

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tion should apply prospectively and does not intend the authorization to

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apply to the valuation of royalty gas that is sold by a lessee of the state

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under a contract entered into before the effective date of this Act with a

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nonprofit electric utility.

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(b) The legislature finds that it is also in the best interest of the

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state to give the commissioner explicit discretionary authority to sell

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royalty gas received in kind by the state to nonprofit electric utilities

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at a price that is below market value.

25

(c) The proper exercise of the discretion conferred by this Act on

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the commissioner would support and complement the other programs that

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assist the citizens of the state with their long-term electrical needs,

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including the power cost equalization program under AS 44.83.162 - 44.83.-

29

165 and hydroelectric and other programs for the generation of electricity.

1 (d) The state should adopt a policy for the sale of royalty gas to
2 nonprofit electric utilities for in-state generation of electricity that is
3 fundamentally different from the policies of the state for the sale of
4 royalty oil and for the sale of royalty gas for export from the state or
5 for uses other than in-state generation of electricity.

6 * Sec. 2. AS 38.05.180 is amended by adding a new subsection to read:

7 (aa) Within 90 days after the written request of a lessee of a
8 lease issued under this section, unless the commissioner makes a
9 written finding based on clear and convincing evidence that the con-
10 tract price is unreasonably low and that a prospective reduction in
11 royalty receipts would not be balanced by increased benefits to elec-
12 tric consumers, the commissioner shall enter into an agreement with
13 the lessee to use the price for the gas established in the contract
14 between the lessee and a nonprofit electric utility, if the lessee and
15 the utility are not related in management, ownership, or other aspect,
16 as the value of the state's royalty share of gas production sold by a
17 lessee of the state to a nonprofit electric utility. In this
18 subsection

19 (1) "nonprofit electric utility" includes an electric
20 cooperative organized under AS 10.25 and a municipal utility; and

21 (2) "price for the gas established in the contract" in-
22 cludes tax reimbursement amounts, deliverability and other charges,
23 and other forms of consideration paid by the nonprofit electric utili-
24 ty under the contract.

25 * Sec. 3. AS 38.05.183(h) is amended by adding a new subsection to
26 read:

27 (h) The commissioner may enter into a contract to sell royalty
28 gas taken in kind by the state to a nonprofit electric utility at less
29 than the market value of the royalty gas if the commissioner, after

1 considering the consumer benefits, other benefits, and detriments of
2 the sale, makes a written finding that the sale is in the best inter-
3 est of the state. In this subsection, "nonprofit electric utility"
4 includes an electric cooperative organized under AS 10.25 and a
5 municipal utility.

6 * Sec. 4. AS 38.05.810(a) is amended to read:

7 (a) Except as otherwise provided in AS 38.05.183(h), the [THE]
8 lease, sale, or other disposal of state land or resources may be made
9 to a state or federal agency or political subdivision, or the lease,
10 sale, or disposal of coal deposits suitable for mining may be made to
11 a utility owned and operated by a government agency or nonprofit
12 cooperative association organized to participate under the Federal
13 Rural Electrification Act for the purpose of generating electric power
14 and energy or the production of process steam, or both, for less than
15 the appraised value as determined by the director and approved by the
16 commissioner to be fair and proper and in the best interests of the
17 public, with due consideration given to the nature of the public
18 services or function rendered by the agency, subdivision, or utility
19 making application, and of the terms of the grant under which the land
20 was acquired by the state.

21 * Sec. 5. Section 2 of this Act applies to contracts entered into on or
22 after the effective date of this Act to sell to nonprofit electric
23 utilities gas produced under a lease issued under AS 38.05.180.

24 * Sec. 6. Section 3 of this Act applies to contracts entered into by
25 the state on or after the effective date of this Act to sell new quantities
26 of royalty gas to nonprofit electric utilities.

27 * Sec. 7. This Act takes effect immediately in accordance with AS 01.-
28 10.070(c).

Introduced: 4/26/85
Referred: House Special Committee
on Oil & Gas, Resources and Finance

1 IN THE HOUSE

BY PIGNALBERI

2

HOUSE BILL NO. 403

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

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FOURTEENTH LEGISLATURE - FIRST SESSION

5

A BILL

6 For an Act entitled: "An Act relating to the royalty value of a natural
7 gas lease on state land; and providing for an effective
8 date."

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. FINDING. The legislature finds that to provide for the
11 utilization, development and conservation of gas resources for the maximum
12 benefit of the people of the state, the value of production of gas for
13 purposes of computing the royalty reserved to the state must be based
14 primarily on the contract price of gas rather than the current market value
15 of the gas. This will encourage stable markets, promote investment, assure
16 reasonable energy prices and provide the maximum benefit to the people of
17 the state.

18 * Sec. 2. AS 38.05.180 is amended by adding a new subsection to read:

19 (aa) Notwithstanding other provisions of this section, if the
20 commissioner issues a gas lease under (f) of this section and the
21 royalty value of the production of gas removed or sold from the lease
22 is measured by a long-term contract price, the commissioner may not
23 adjust the long-term contract price to reflect the current market
24 value of gas if the commissioner determines the current market value
25 price adjustment would result in an increase in the consumer price of
26 the gas or unless the commissioner determines in a written finding
27 supported by clear and convincing evidence that the long term contract
28 price is unreasonably low.

29 * Sec. 3. This Act applies to leases issued before or after the

1 effective date of this Act.

2 * Sec. 4. This Act takes effect immediately in accordance with AS 01.-

3 10.070(c).

Introduced: 2/11/86
Referred: House Special Committee on
Oil & Gas, Resources and Finance

BY PEARCE, HANLEY, JENKINS
PIGNALBERI AND COLLINS

1 IN THE HOUSE

2 SPONSOR SUBSTITUTE FOR HOUSE BILL NO. 425

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FOURTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the royalty value of a natural
7 gas lease on state land; and providing for an effective date."
8

9 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. FINDING. The legislature finds that to provide for the
11 utilization, development and conservation of gas resources for the maximum
12 benefit of the people of the state, the value of production of gas for
13 purposes of computing the royalty reserved to the state must be based
14 primarily on the contract price of gas rather than the current market value
15 of the gas. This will encourage stable markets, promote investment, assure
16 reasonable energy prices and provide the maximum benefit to the people of
17 the state.

18 * Sec. 2. AS 38.05.180 is amended by adding a new subsection to read:

19 (aa) Notwithstanding other provisions of this section, if the
20 royalty share of natural gas reserved to the state under a lease
21 issued by the state under this section is taken in value, the value of
22 production sold under a long-term sales contract may not be greater
23 than the price received for the production under the long-term sales
24 contract unless it is shown by clear and convincing evidence that the
25 long-term contract price was unreasonably low at the time of contract.

26 * Sec. 3. This Act applies to leases issued before, on, or after the
27 effective date of this Act.

28 * Sec. 4. This Act takes effect immediately in accordance with AS 01.-
29 10.070(c).

Introduced: 4/12/85
Referred: House Special Committee on
Oil & Gas, Resources and Finance

1 IN THE HOUSE

BY COLLINS AND PIGNALBERI

2

HOUSE BILL NO. 374

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IN THE LEGISLATURE OF THE STATE OF ALASKA

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FOURTEENTH LEGISLATURE - FIRST SESSION

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A BILL

6 For an Act entitled: "An Act relating to the lease, sale, or disposal of
7 natural gas for a public use."

8 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9 * Section 1. AS 38.05.810(a) is amended to read:

10 (a) The lease, sale, or other disposal of state land or re-
11 sources may be made to a state or federal agency or political subdivi-
12 sion, or the lease, sale, or disposal of coal deposits suitable for
13 mining or of natural gas may be made to a utility owned and operated
14 by a government agency or nonprofit cooperative association organized
15 to participate under the Federal Rural Electrification Act for the
16 purpose of generating electric power and energy or the production of
17 process steam, or both, for less than the appraised value as deter-
18 mined by the director and approved by the commissioner to be fair and
19 proper and in the best interests of the public, with due consideration
20 given to the nature of the public services or function rendered by the
21 agency, subdivision, or utility making application, and of the terms
22 of the grant under which the land was acquired by the state.

STATE OF ALASKA
THE LEGISLATURE

LEGISLATIVE AFFAIRS AGENCY

POUCH Y - STATE CAPITOL

JUNEAU, ALASKA 99811

907-465-3800

MEMORANDUM

February 3, 1986

SUBJECT: Sectional analysis of HB 425
TO: Representative Drue Pearce
FROM: Theresa L. Bannister *tb*
Legislative Counsel

This memorandum contains the sectional analysis that you requested for HB 425.

Section 1 establishes the criteria for valuing the production of royalty natural gas taken in value and sold by the state under an oil or gas property lease.

Section 2 applies section 1 to oil or natural gas property leases issued by the state before the effective date of the act.

Section 3 gives the act an immediate effective date.

TLB:ml
M2/128

IMPACTS OF STATE ROYALTY GAS INCREASE ON RAILBELT CONSUMERS

Alaskans from Fairbanks to Homer face utility bill increases as a result of the Alaska Department of Natural Resources' decision to drastically raise the price of royalty gas in Cook Inlet. For Chugach Electric Association consumers in the Anchorage area, the impacts will be nearly \$3 million a year.

DNR's action was taken with virtually no advance notice to the parties involved, to the public or to the State Legislature. Litigation was initiated by the three producers against DNR on the revaluation in April 1985. Chugach is also involved in the litigation.

There are two major aspects of this issue: The additional costs to utility consumers of DNR's actions and, perhaps more important, the fundamental policy question of how royalty valuation is established.

On March 18, 1985, the Department of Natural Resources (DNR) issued a formal notice to the three Beluga River gas field producers -- ARCO, Shell and Chevron -- informing them that DNR would no longer accept royalty payments based on long-term contract price but would require payments based on the "prevailing market value."

This value was initially determined by DNR to be \$2.05 per thousand cubic feet (mcf), based on a Shell-ENSTAR (APL II) contract signed in December 1982. By contrast, Chugach currently pays \$.26/mcf for its Beluga gas, under long-term contracts on which the DNR had based its royalty price for the past 17 years.

Based on the \$2.05/mcf figure, the annual increase to Chugach retail and wholesale consumers would be approximately \$2.8 million -- the equivalent of a rate increase averaging about 3 percent. Even under a recent settlement offer by the state which would value the royalty gas at \$1.50/mcf, the impact would be approximately \$1.9 million annually -- an equivalent rate increase averaging about 2 percent.

Chugach negotiated its Beluga contracts in good faith and at arms length in 1965, and renegotiated with the producers in 1973. The contracts extend to 1998 or whenever 373 billion cubic feet (bcf) of gas is used, whichever comes first. That means the overall impact of the Beluga royalty revaluation alone could total more than \$30 million to consumers.

Additional financial impacts on Chugach consumers have resulted or could result from actions similar to or related to the Beluga royalty revaluation. Those actions are:

- a possible revaluation, identical to the state's, by the other Beluga royalty gas owners (the federal government and Cook Inlet Region, Inc.);

- the recent \$8.5 million settlement by ENSTAR relative to royalty gas from the Kenai field (raising ENSTAR's Kenai royalty price from \$.66 to \$1.95, and including retroactive payments);

- an increase in the cost of power purchased from Anchorage Municipal Light & Power, which was substantially impacted by the ENSTAR increase, and

- a possible increase in state gas severance taxes based on the Beluga royalty gas revaluation.

If all these actions occur, the impact on Chugach consumers would be approximately \$6 million annually -- the equivalent of about a 6 percent rate increase. Attachment A details the impacts.

Financial impacts also will be felt in the Fairbanks area, because Chugach has been selling wholesale power to Golden Valley Electric Association and Fairbanks Municipal Utility System over the Anchorage-Fairbanks intertie. ML&P also is selling power to Golden Valley. Golden Valley has estimated that its consumers will save more than \$600,000 this winter alone through purchases of power from Chugach and ML&P.

Copper Valley Electric Association also is concerned, because the Glenallen-based cooperative wants its consumers from Glenallen to Valdez to be intertied with the Railbelt utilities and reap the benefits of less expensive power.

Approximately three quarters of the state's estimated 560,000 residents live in the Railbelt between Fairbanks and Homer. Chugach serves nearly half the state's population through sales to its own retail consumers and those of Matanuska Electric Association, Homer Electric Association and the City of Seward. Thus, residents of the Matanuska and Susitna Valleys and on the Kenai Peninsula are directly affected.

In addition to the cost increases associated with the existing gas contracts, there is another major -- and perhaps even more important -- impact of DNR's royalty revaluation decision.

This is what could be called the uncertainty factor. If DNR is ultimately successful in setting royalty prices on what it determines to be the prevailing market value of a resource, utilities, producers and other purchasing parties will have no assurance of what future royalty gas components will be. This injects a real measure of insecurity into long-term gas contracts and, for Chugach at least, into power supply planning and ratemaking.

The uncertainty factor is an important public policy question for the state and is one that may well eclipse the cost-increase aspect of any given royalty lease revaluation. It could be argued that settling the price dispute over a specific revaluation without first resolving the underlying policy question is getting the horse before the cart.

It is important to note that although DNR's gas and oil lease form has given rise to dispute and litigation in many instances over the years, DNR has failed to propose regulations defining important lease terms. Proposed regulations would at least allow for a public discussion of the policy questions.

To resolve the problem raised by the state's royalty gas revaluation, Chugach is supporting passage of S.B. 309, or similar bills H.B. 403 and H.B. 425. Each of these bills would require DNR to tie royalty valuation to long-term contract price, thereby resolving the underlying policy question. A copy of each of the bills is attached.

Uncertainty in long-term price for royalty gas raises problems for Chugach and other utilities both in terms of long-term financing for generation projects and in efforts to ensure electric rate stability. Tying royalty price to long-term contract price allows DNR to continue to manage the state's resources for maximum value, while recognizing that these resources do not have a value independent of long-term contracts. DNR would still be permitted, on only six months' written notice, to take its royalty share in kind and sell it directly to a willing purchaser.

ATTACHMENT A

CHUGACH ELECTRIC ASSOCIATION, INC.
Rate Impacts Due to Market Valuation of Royalty Gas

January 10, 1986

| | <u>Retail:</u> <u>Dollars</u> | <u>Retail:</u> <u>Percent</u> | <u>Wholesale:</u> <u>Dollars</u> | <u>Wholesale:</u> <u>Percent</u> | <u>Total:</u> <u>Dollars</u> | <u>Total:</u> <u>Percent</u> |
|---|----------------------------------|----------------------------------|-------------------------------------|-------------------------------------|---------------------------------|---------------------------------|
| Current revenues | \$63,200,000 | | \$35,800,000 | | \$99,000,000 | |
| Impacts: | | | | | | |
| The state's Beluga royalty revaluation from \$.26/mcf to \$2.05/mcf | 1,501,164 | 2.38 | 1,278,769 | 3.57 | 2,779,933 | 2.81 |
| Possible federal/CIRI Beluga revaluation (based on state's \$2.05/mcf figure) | 1,000,776 | 1.58 | 852,513 | 2.38 | 1,853,289 | 1.87 |
| ENSTAR settlement | 420,853 | 0.67 | 358,505 | 1.00 | 779,358 | 0.79 |
| ML&P rate increase (resulting from ENSTAR settlement) | 337,500 | 0.53 | 287,500 | 0.80 | 625,000 | 0.63 |
| Possible state gas severance tax increase (based on state's Beluga royalty revaluation) | <u>87,100</u> | <u>0.14</u> | <u>74,196</u> | <u>0.21</u> | <u>161,296</u> | <u>0.16</u> |
| | \$3,347,393 | 5.30 | \$2,851,483 | 7.97 | \$6,198,876 | 6.26 |

STATE OF ALASKA 1986 LEGISLATIVE SESSION FISCAL NOTE

Revision Date : 2-11-86

REQUEST

Bill/Resolution No. : HB 425
 Title : ...Royalty Value of a
Natural Gas Lease
 Sponsor : Rep. Pearce
 Requestor : Oil & Gas Res Comm
 Date of Request : 02-11-85

FISCAL DETAIL

Agency Affected : Natural Resources
 BRU : Petroleum Management
 Components : _____

EXPENDITURES/REVENUES : (Thousands of Dollars)

| OPERATING | FY 86 | FY 87 | FY 88 | FY 89 | FY 90 | FY 91 |
|------------------------|---------|---------|---------|---------|---------|---------|
| PERSONAL SERVICES | | | | | | |
| TRAVEL | | | | | | |
| CONTRACTUAL | | | | | | |
| SUPPLIES | | | | | | |
| EQUIPMENT | | | | | | |
| LAND & STRUCTURES | | | | | | |
| GRANTS, CLAIMS | | | | | | |
| MISCELLANEOUS | | | | | | |
| TOTAL OPERATING | | | | | | |
| CAPITAL | | | | | | |
| REVENUE | (2,300) | (1,900) | (1,900) | (1,900) | (1,900) | (1,900) |

FUNDING : (Thousands of Dollars)

| | | | | | | |
|---------------|--|--|--|--|--|--|
| GENERAL FUND | | | | | | |
| FEDERAL FUNDS | | | | | | |
| OTHER | | | | | | |
| TOTAL | | | | | | |

POSITIONS :

| | | | | | | |
|-----------|--|--|--|--|--|--|
| FULL-TIME | | | | | | |
| PART-TIME | | | | | | |
| TEMPORARY | | | | | | |

ANALYSIS : Attach a separate page if necessary

FY 86 revenue losses include obligations incurred by producers since March 1985 royalty enforcement notice. See attached explanation.

Prepared by: Ned Farquhar *NF* Phone: 465-2400
 Division: Commissioner's Office *RMM* Date: 02-11-86

Approved by Commissioner: *Wm J. Arnold, Deputy* Date: 2/11/86
 Agency: Natural Resources

Distribution (by Agency preparing fiscal note):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

Fiscal Note Background
for HB 425

Passage of HB 425 would prevent enforcement of existing royalty collection provisions in Beluga Field oil and gas leases, and enforcement of royalty gas provisions in other fields. This fiscal note represents the impact of the legislation only on the Beluga Field royalty collections, although there are likely to be impacts in other fields.

The State issued an enforcement order for the Beluga Field in March, 1985, effective April 15, 1985. While the notice is contested by producers, there have been no payments made; if the notice were implemented as written, the State would currently receive \$2.8 million/year in increased royalty payments. Because the State has offered to settle the lawsuit at a lower value than embodied in the enforcement notice, however, the fiscal impact has been estimated at the proposed settlement value (\$1.50/mcf) that would be lost if SB 309 passes rather than at the value that would be recovered under the original notice.

Some of the revenue loss will be felt by the Alaska Permanent Fund, which receives 25% of the revenues from state oil and gas leasing. The remainder of the impact will be on the General Fund.

There will be other significant but currently incalculable fiscal impacts from passage of the bill. If the bill passes, the State will not collect full royalty value (as stipulated in existing oil and gas lease forms) prospectively on other state leases producing gas. Additionally, producers may seek retroactive compensation for what they may regard as past royalty overpayments, including several recent settlements on royalty gas pricing in Cook Inlet.

If the Legislature's action affects the State's position regarding valuation of other State royalty oil and gas (most notably North Slope oil) there could be revenue losses amounting to tens or hundreds of millions of dollars.

14-1936
Bannister
2/27/86

1 IN THE HOUSE

BY THE HOUSE SPECIAL
COMMITTEE ON OIL AND GAS

2 HOUSE BILL NO.

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FOURTEENTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to royalty gas contracts; and pro-
7 viding for an effective date."

8 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9 * Section 1. FINDINGS. (a) The legislature finds that the best inter-
10 est of the state will be served if the commissioner of natural resources is
11 authorized to establish the in-value royalty for gas sold to a gas or
12 electric utility by using the contract price between the lessee of the
13 state and the utility, whether or not the gas lease establishes a different
14 standard for the valuation and if the lessee and the utility are not re-
15 lated to each other. The legislature finds that this authorization should
16 apply prospectively and does not intend the authorization to apply to the
17 valuation for royalty purposes of gas sold by a lessee under a gas sales
18 contract entered into before the effective date of this Act.

19 (b) The legislature finds that it is also in the best interest of the
20 state to give the commissioner explicit discretionary authority to sell
21 royalty gas received in kind by the state to gas or electric utilities at a
22 price that is below market value.

23 (c) The legislature finds that the proper exercise of the discretion
24 conferred on the commissioner by this Act would support and complement the
25 other programs that assist the citizens of the state with their long-term
26 gas and electrical needs, including the power cost equalization program
27 under AS 44.83.162 - 44.83.165 and hydroelectric and other programs for the
28 generation of electricity.

29 (d) The legislature finds that the state should adopt a policy for

1 the sale of royalty gas to gas or electric utilities for in-state consumer
2 use and in-state generation of electricity that is fundamentally different
3 from the policies of the state for the sale of royalty oil and for the sale
4 of royalty gas for export from the state or for uses other than in-state
5 consumer use and in-state generation of electricity.

6 * Sec. 2. AS 38.05.180 is amended by adding a new subsection to read:

7 (aa) Within 90 days after the written request of a lessee of a
8 lease issued under this section, unless the commissioner makes a
9 written finding based on clear and convincing evidence that the con-
10 tract price is unreasonably low and that a prospective reduction in
11 royalty receipts would not be balanced by increased benefits to in-
12 state gas and electric consumers, the commissioner shall enter into an
13 agreement with the lessee to use the price for the gas established in
14 the contract between the lessee and a gas or electric utility, if the
15 lessee and the utility are not related in management, ownership, or
16 other aspect, as the value of the state's royalty share of gas produc-
17 tion sold by the lessee under the contract to the utility. In this
18 subsection

19 (1) "gas or electric utility" includes an electric coopera-
20 tive organized under AS 10.25, a municipal utility, and a gas or
21 electric utility regulated under AS 42.05; and

22 (2) "price for the gas established in the contract" in-
23 cludes tax reimbursement amounts, deliverability and other charges,
24 and other forms of consideration paid by the gas or electric utility
25 under the contract.

26 * Sec. 3. AS 38.05.183 is amended by adding a new subsection to read:

27 (h) The commissioner may enter into a contract to sell royalty
28 gas taken in kind by the state to a gas or electric utility at less
29 than the market value of the royalty gas if the commissioner, after

1 considering the residential consumer benefits, other benefits, and
2 detriments of the sale, makes a written finding that the sale is in
3 the best interest of the state. In this subsection, "gas or electric
4 utility" includes an electric cooperative organized under AS 10.25, a
5 municipal utility, and a gas or electric utility regulated under
6 AS 42.05.

7 * Sec. 4. AS 38.05.810(a) is amended to read:

8 (a) Except as otherwise provided in AS 38.05.183(h), the [THE]
9 lease, sale, or other disposal of state land or resources may be made
10 to a state or federal agency or political subdivision, or the lease,
11 sale, or disposal of coal deposits suitable for mining may be made to
12 a utility owned and operated by a government agency or nonprofit
13 cooperative association organized to participate under the Federal
14 Rural Electrification Act for the purpose of generating electric power
15 and energy or the production of process steam, or both, for less than
16 the appraised value as determined by the director and approved by the
17 commissioner to be fair and proper and in the best interests of the
18 public, with due consideration given to the nature of the public
19 services or function rendered by the agency, subdivision, or utility
20 making application, and of the terms of the grant under which the land
21 was acquired by the state.

22 * Sec. 5. Section 2 of this Act applies to agreements to establish for
23 a lease issued under AS 38.05.180 the in-value royalties on gas production
24 that is sold under a contract entered into on or after the effective date
25 of this Act between the state's lessee and a gas or electric utility.

26 * Sec. 6. This Act takes effect immediately in accordance with AS 01.-
27 10.070(c).
28
29

COOK INLET ROYALTY GAS VALUATION:
An Overview

A Presentation to the
Anchorage Caucus
by:

Esther C. Wunnicke, Commissioner
Alaska Department of Natural Resources

Kay Brown, Director
Division of Oil and Gas
Alaska Department of Natural Resources

Bill Van Dyke, Petroleum Manager
Division of Oil and Gas
Alaska Department of Natural Resources

February 6, 1986

2/5/86

COOK INLET GAS SUMMARY

Lease interpretation: Under the terms of its oil and gas lease contracts with the oil companies, the state is entitled to royalty payments determined by the higher of the price received by an oil company under its sales contract, or the value of the gas at the time of production. This means that the price received under a long-term gas sales contract does not control royalty valuation in those instances where inflation and market forces have caused the current value of the gas to be higher than the contract price.

DNR policy:

(1) As land manager for the citizens of the entire state, it is DNR's responsibility to obtain fair value for the state's oil and gas resources by collecting the full royalties to which the state is entitled under its oil and gas leases.

(2) DNR should not selectively abdicate its responsibility to enforce the royalty terms of the Cook Inlet gas leases just because utility companies have agreed as part of their gas purchase contracts to reimburse the oil companies for royalty collections made by the state. Any consumer subsidy should be the result of an affirmative, direct subsidy by the legislature as part of a comprehensive energy policy.

(3) DNR should not divert from uniform enforcement of the oil and gas leases, since such action could, in addition to directly reducing revenues from any leases from which royalties are not fully collected, also indirectly cause a much larger reduction in state revenues by impairing the state's ability to enforce the royalty provisions of the North Slope leases.

The potential consumer impact result from actions by Chugach, not the state. The risk that gas values might escalate to values in excess of the long-term gas sales price was a circumstance foreseen by the parties to those sales contracts. This is demonstrated by the fact that the contracts between the oil company lessees and Chugach Electric Association, Inc. (Chugach) specifically assign to Chugach the risk of any rise in royalty obligations. The state was not a party to those sales contracts. The contract price, the absence of an adequate price escalator or price reopener, and the assignment to Chugach of the risk of increased royalty obligations were all conditions established by contract between Chugach and the lessees without state participation.

Existing law provides an adequate mechanism for long-term royalty certainty: DNR is sympathetic to the desirability of long-term certainty in royalty matters. However, new statutory authorities are not necessary in order to provide such certainty. Royalty certainty can be attained by negotiation of long-term in kind gas sales contracts which parallel the contracts between the state's

lessees and their gas purchasers. This would allow an opportunity for DNR, the royalty board, and the legislature to evaluate the adequacy of the royalty over the life of the contract. This is preferable to being locked into a long-term royalty value set by prices established by lessees without any notice to or participation from the state.

Litigation: Last March DNR notified the Cook Inlet lessees of its determination to enforce the leases. The notices asserted that the most recent (December 1982) major contracts from the Kenai and Beluga River fields (the "APL II contracts") established the current value. These contracts had a base contract price of \$2.05 per mcf in 1985. The state subsequently indicated its readiness to accept a lower royalty value if presented with evidence that the current value of gas in Cook Inlet is less than the price established under the APL II contracts. Union, Marathon, ARCO, Chevron and Shell responded to the notices by suing the state.

Recent Cook Inlet Gas Sales Contracts:

| Date of Contract | Purchaser | Field | Starting Base Price |
|------------------|--------------|--|---------------------|
| 1982 | APL (Enstar) | Beluga | \$2.32 |
| 1982 | APL (Enstar) | Kenai, Beaver Creek or McArthur River | \$2.32 |
| 1983 | Chugach | Cannery Loop | \$1.80 |
| 1984 | APL (Enstar) | Lewis River | \$1.80 |
| 1985 | Tesoro | Kenai, Beaver Creek or McArthur River | \$2.01 |

Settlements achieved: In the last two months of 1985 DNR's royalty enforcement actions achieved significant success. Settlements relating to gas royalties due on production from the Kenai Field, and involving Marathon, Union, Alaska Pipeline Company (Enstar), CIRI, the U.S. Department of the Interior and the state, yielded the state about \$4 million in retroactive royalties, and will bring in excess of \$6.5 million per year more than the amounts which would have been paid under the lessees' prior reporting practices (including those increases attributable to the state's 90% interest in federal onshore royalties). Under the lessees' theory, the royalties would have been variously between \$0.21 and \$0.61 per mcf; under the settlement, the lessees will pay \$1.95 per mcf during 1986. The \$1.95 is squarely within the gas values established by recent Cook Inlet gas sales contracts, as well as the values established by Enstar's pending rates (\$2.1854 for Schedule C purchasers - "Large Commercial Service", and from \$1.6480 to \$2.0158 for sales to power plants). The settlements confirm the soundness of the royalty enforcement action taken last spring.

Remaining disputes: The major remaining dispute relates to the Beluga River field, the primary source of gas for Chugach.

Settlement negotiations during the last six months have failed to produce any resolution. Options explored have included underlifting the state's royalty share, thus delaying the royalty into the future; an in kind sale to Enstar or Chugach; and an in value settlement. The lessees (ARCO, Chevron and Shell) assert that they should not be required to contribute any monies to any settlement, since their sales contract with Chugach requires Chugach to reimburse the lessees for any additional royalty amount the state collects. Chugach, in turn, has been unwilling to agree to an acceptable value, and has indicated that it will seek legislative relief. Recently, the state made a formal offer to its lessees to settle the dispute for \$1.50 per mcf. This offer was rejected, but settlement efforts and discussions continue.

Consumer impact. Chugach estimates that a royalty rate of \$2.05 per mcf on state leases would increase retail consumer rates only about 2.32%, assuming the lessees were successful in asserting that their contracts with Chugach permitted them to pass the royalty burden on to Chugach, and further assuming that the APUC permitted Chugach to pass the burden on to its consumers. DNR estimates that a \$2.05 royalty would increase state revenues by about \$2.8 million per year. Under the \$1.50 per mcf settlement offer, the increased royalty income would fall to about \$2 million per year, and the magnitude of retail consumer impact would be correspondingly reduced to less than 2%. (A two per cent increase on a monthly bill of \$30 would be only \$0.60).

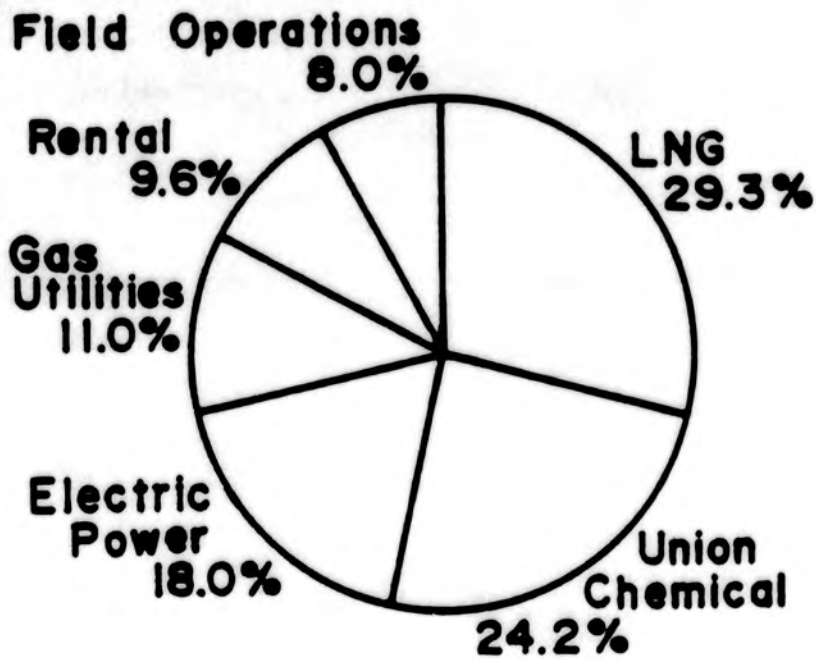
2/5/86

COOK INLET GAS ROYALTY SETTLEMENTS
(State leases and State share of federal royalties)

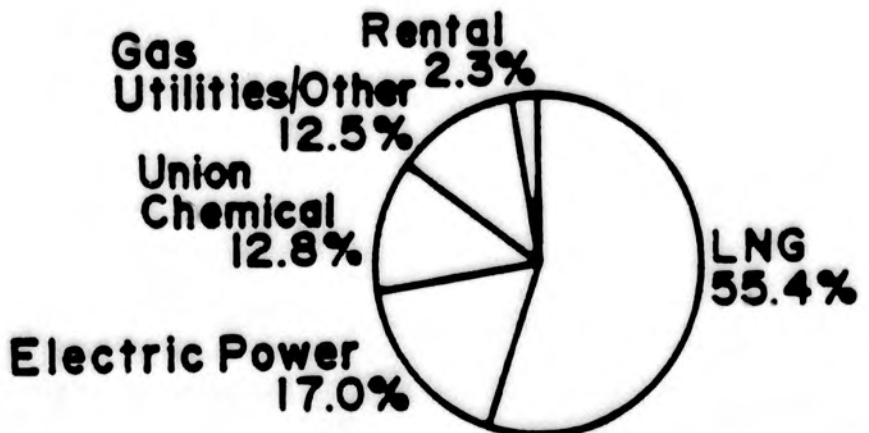
| Lessee | Scope of Settlement | Retro- active Payment (millions) | Current Monthly Value Under Settlement (per Mcf) | Estimated Additional Royalties per year (millions) |
|-----------------------|--|---|--|--|
| Phillips | North Cook Inlet Field gas sold as LNG in Japan | \$36.3 | \$2.32 | \$12.00 |
| Marathon | Kenai field gas sold as LNG in Japan | \$ 4.3 | \$2.32 | \$ 0.75 |
| Union and Marathon | All of Union's Kenai field gas disposition (including the following: urea/ammonia plant, rental gas, Enstar), plus Marathon's dispositions to Enstar under Enstar's 1975 contract | \$ 4.1 | \$1.95 | 6.90 |
| Total | | <u>\$44.7</u> | | <u>\$19.65</u> |

COOK INLET

Total Sales

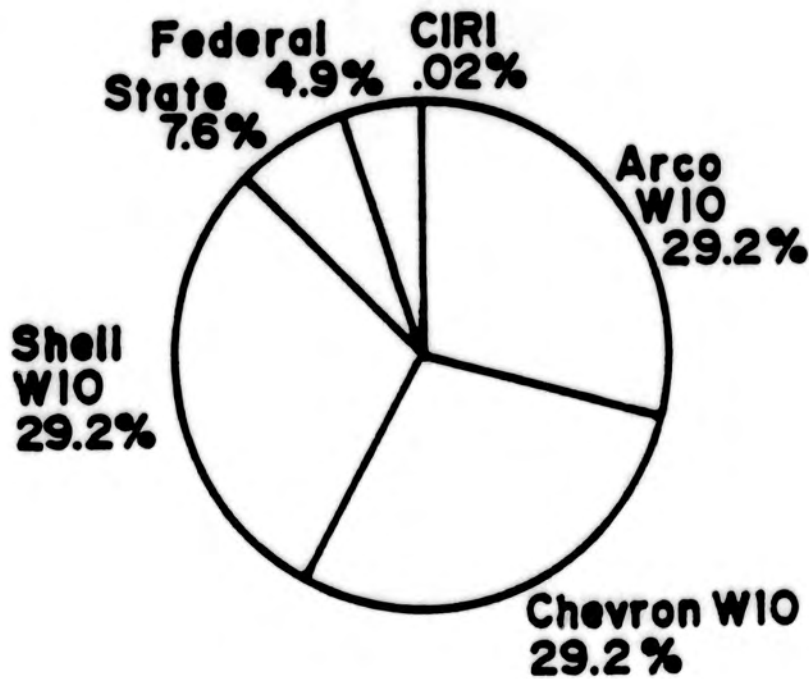


State Royalty Disposition

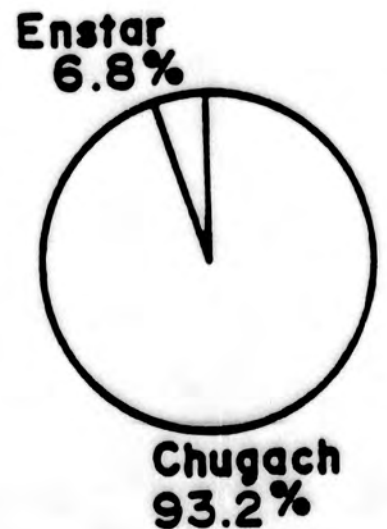


BELUGA FIELD

Royalty And Working Interest Ownership

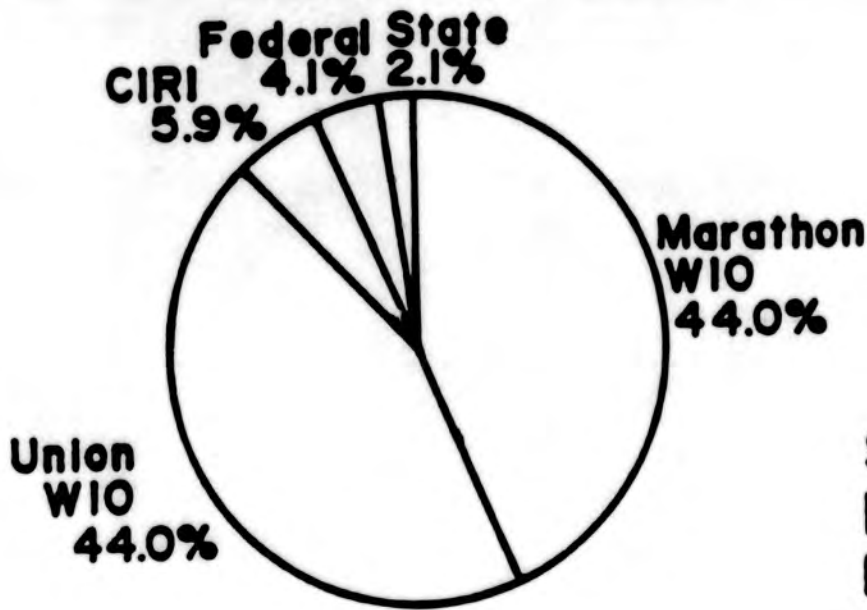


State Royalty Disposition

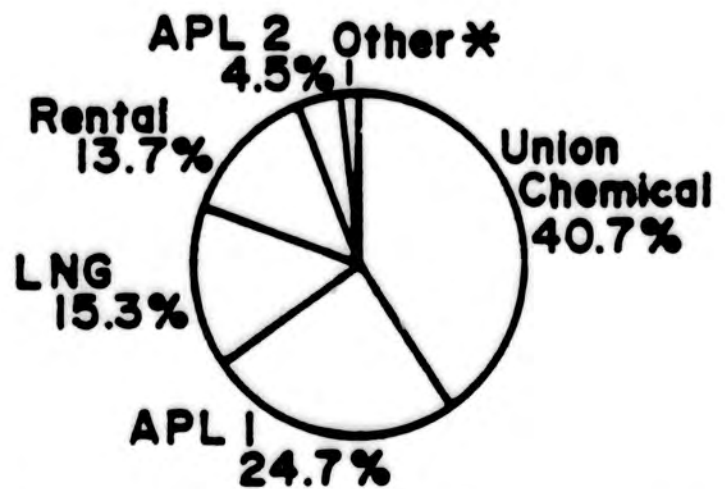


KENAI FIELD

Royalty And Working Interest Ownership



State Royalty Disposition



* APL-Nikiski 0.4%
 Union-Chevron Exchange 0.2%
 City Of Kenal 0.5%

COOK INLET GAS PRODUCTION
(For 1984)

| | Total MMCF/Month | State Royalty MMCF/Month |
|----------------------------------|---------------------|-----------------------------|
| Beluga River Field | | |
| For: Chugach | 1673 | 125 |
| Enstar | <u>121</u> | <u>9</u> |
| Total | 1794 | 134 |
| Kenai Field | | |
| For: APL 1 | 2029 | 42 |
| APL 2 | 369 | 8 |
| APL Nikiski | 31 | 1 |
| APL Kenai | 41 | 1 |
| Union Chevron Ex | 16 | 1 |
| Rental gas | 741 | 15 |
| Rental gas extra | 389 | 8 |
| Ammonia-Urea | 3352 | 67 |
| LNG | <u>1261</u> | <u>25</u> |
| Total | 8229 | 168 |
| McArthur River Field | | |
| For: Rental gas and ammonia-urea | 355 | 44 |
| Beaver Creek Field | | |
| For: APL 2 | 789 | 0 |
| Lewis River Field | | |
| For: APL 2 | 153 | 19 |
| North Cook Inlet Field | | |
| For: LNG | <u>3932</u> | <u>491</u> |
| GRAND TOTAL | 15,250 | 856 |

Excerpts from Lease Form DL-1
Pertaining to the Pricing of Royalty Products

11. ROYALTY ON PRODUCTION. Except for oil and gas used on said land for development and production or unavoidably lost, Lessee shall pay Lessor as royalty the following:

(a) On oil 12-1/2 percent in amount or value of the oil produced and saved and removed or sold from said land.

(b) On gas 12-1/2 percent in amount or value of the gas produced and saved and sold or used off said land or used for the extraction of natural gasoline or other products therefrom.

(c) On associated substances 12-1/2 percent in amount or value of such substances produced and saved and removed or sold from said lands.

15. ROYALTY IN VALUE. At the option of Lessor, which may be exercised from time to time upon not less than six months' notice to Lessee, and in lieu of royalty in kind, Lessee shall pay to Lessor the field market price or value at the well of all royalty oil and/or gas. All royalty that may become payable in money to Lessor shall be paid on or before the last day of the calendar month following the month in which the oil or gas is produced. The payments shall be accompanied by copies of run tickets or other satisfactory evidence of sales, shipments, and amounts or gross production.

16. PRICE. The field market price or value of royalty oil or gas shall not be less than the highest of: (1) The price actually paid or agreed to be paid to Lessee at the well by the purchaser thereof, if any; or (2) The posted price of Lessee in the field for such oil or gas at the well, if any; or, (3) The prevailing price received by other producers in the field at the well for oil of like grade and gravity or gas of like kind and quality at the time such oil or gas is removed from said land or run into storage, or such gas is delivered to an extraction plant.

RECENT CONTRACTS AND PURCHASE AGREEMENTS

| | <u>Purchaser</u> | <u>Field or Seller</u> | <u>Starting Base Price</u> |
|---------|------------------|------------------------|----------------------------|
| 1977 | Pac Alaska | Cook Inlet | \$1.46 per mcf |
| 1982 | Enstar | Beluga River | \$2.32 |
| 1982 | Enstar | Beaver Creek Field | \$2.32 |
| 1982-83 | Chugach | Beluga River | \$1.40-1.60 |
| | (Peaking Gas) | | |
| 1983 | Chugach | Cannery Loop | \$1.80 |
| 1984 | Enstar | Lewis River | \$1.80 |
| 1985 | Tesoro | Marathon | \$2.01 |
| 1985 | AEG&T | Enstar | \$2.04 |
| | (Homer Electric) | | |
| 1985 | ML&P | Enstar | \$1.60 |
| | (Anchorage) | | |

ALLOCATION OF GAS SOLD FOR CONSUMER USE
 (Assuming the State Prevails in the Pricing Dispute)

| | <u>TOTAL MMCF/MONTH</u> | <u>STATE ROYALTY SHARE MMCF/MONTH</u> |
|-------------------------------------|-----------------------------|---|
| Beluga River Field | | |
| Chugach - low priced | 1548 | 0 |
| - high priced | 125 | 125 |
| Enstar - high priced | 121 | 9 |
| Kenai Field | | |
| Enstar (APL 1) - low priced | 1776 | 0 |
| - high priced | 254 | 42 |
| Enstar (APL 2) - high priced | 368 | 8 |
| Enstar (Nikiski) - low priced | 32 | 1 |
| Enstar (City of Kenai) - low priced | 41 | 1 |
| Beaver Creek Field | | |
| Enstar - high priced | 789 | 0 |
| Lewis River Field | | |
| Enstar - high priced | 153 | 19 |
| Subtotal - low priced | 3397 | 2 |
| Subtotal - high priced | 1810 | 203 |
| GRAND TOTAL - all prices | 5207 | 205 |

2/5/86

COOK INLET GAS ROYALTY CHRONOLOGY

| <u>Month</u> | <u>Year</u> | <u>Description of Event</u> |
|--------------|-------------|--|
| March | 1964 | <u>Foster v. Atlantic Refining Company</u> , 329 F.2d 485 (5th Cir. 1964) holds that long-term contract price does not control royalty valuation when market value rises, even if this is burdensome on the lessee. |
| May | 1965 | Chugach Electric Association, Inc. enters into 20 year contracts with ARCO, Chevron and Shell for Beluga River gas, with an initial price of 15.2 cents per mcf, subject to a volume limit. |
| January | 1973 | Chugach renegotiates its 1965 contracts, extending the term to 1998 (unless the new, higher volume limit is reached earlier). The 1986 base price under those contracts is about 21 cents per mcf. |
| November | 1982 | Chugach obtains supplemental gas deliveries under the 1973 contract at a base price of \$1.48 per Mmbtu (approximately equivalent to \$1.48 per mcf). |
| December | 1982 | Alaska Pipeline Company (Enstar) signs contracts for gas deliveries from Beluga River (with Shell) and Kenai (with Marathon) at a price of \$2.32 per mcf, with annual adjustments based upon fuel price fluctuations (the "APL-II" contracts). This is the first totally new contract for Beluga River gas subsequent to the 1973 Chugach contract under which there were any deliveries. |
| March | 1984 | <u>Piney Woods County Life School v. Shell Oil Company</u> , 726 F.2d 225 (5th Cir. 1984), reh. den. 750 F.2d 69, cert. den. 105 S.Ct. 1868 (1985) reaffirms the soundness and continued validity of the rule in <u>Foster</u> , above. |
| May | 1984 | The state and Phillips settle their dispute concerning the valuation of Cook Inlet gas from state leases which is sold as LNG in Japan, using a formula which initially yields a royalty of \$2.40 per mcf. |
| May | 1984 | The federal government informs Union that virtually all gas royalties from the Kenai field, including gas sold under below-current-market, long-term contracts with Enstar, must be valued in accordance with the price under the APL-II contracts. |
| November | 1984 | DNR determines, in consultation with the Department of Law, to enforce the Cook Inlet lease terms requiring payment of gas royalty on the basis of current value. |

| | |
|---------------|--|
| February 1985 | U.S. District Judge Fitzgerald rules that Marathon must pay royalties on Kenai Field gas sold as LNG in Japan based upon the Japan sales price, less costs of transportation. Marathon calculates the netback value under the order to be about \$3.00 per mcf, while the federal government calculates the value to be about \$3.60 per mcf. The accounting remains in dispute in District Court, while the District Court's February 1985 decision is under appeal to the Ninth Circuit. |
| March 1985 | By written notice, DNR informs its Cook Inlet lessees of its determination to enforce the royalty requirements of the leases. |
| May/June 1985 | All Cook Inlet gas producers file separate lawsuits seeking judicial declaration of their royalty obligations under the leases. |
| July 1985 | The state and Marathon settle their dispute concerning the royalty value of Kenai Field gas sold as LNG in Japan in accordance with the terms of the May 1984 Phillips settlement. |
| November 1985 | The state, federal government and CIRI (all royalty owners in the Kenai field) settle most royalty issues for production from the Kenai field. Most significantly, royalty on gas used in Union's urea and ammonia plant and used to promote greater oil production from the Swanson River oil field, is set at \$1.85 per mcf for 1985 and \$1.95 per mcf for 1986, with annual adjustments thereafter based upon fluctuations in fuel oil prices. |
| November 1985 | The Secretary of the Interior issues a definitive order holding that Cook Inlet gas sold by Union and Marathon to Enstar must be valued for royalty purposes according to current market values. |
| December 1985 | The state, federal government and CIRI enter into a settlement agreement on the value of the royalty on Kenai gas sold to Enstar under long-term contracts. Under this settlement, the royalty owners receive \$1.85 per mcf for the part of 1985 at issue, and will receive \$1.95 per mcf for 1986 production, with annual adjustment thereafter based upon fluctuations in the oil prices. |
| January 1986 | The state offers to the producers to settle the dispute concerning the royalty value of gas sold to Chugach. This \$1.50 per mcf offer is rejected by the producers, but settlement discussions continue. |

