

ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILE 8672

1216 SCOMM 46: HOUSE SPEC. COMMITTEE ON OIL AND GAS 1985-86

benefits and obligations that existed under this Agreement before the occurrence of the force majeure condition.

11.2 Responsibility. Upon the occurrence and discovery of an event providing the basis for a claim of force majeure, the party making a claim shall notify the other party to this Agreement of its claim of force majeure. Upon the occurrence of an event constituting force majeure, that event shall, so far as possible, be remedied with all reasonable diligence and dispatch. Except for Purchaser's obligations to make payment of money for Oil tendered under this Agreement and except for Purchaser's obligation to dispose of Oil, the obligations of the disabled party to perform under this Agreement, insofar as they are affected by that force majeure, shall be suspended from the time that force majeure occurs and for so long as the disability caused should have continued had the party claiming the existence of the force majeure remedied the event providing the basis of the claim of force majeure with reasonable diligence and dispatch, and for no longer. The settlement of strikes or lockouts or industrial disputes or disturbances will be entirely within the discretion of the party having the difficulty, and the above requirement that any force majeure shall be remedied with diligence and dispatch shall not require the settlement of strikes, lockouts, or industrial disturbances by acceding to the demands of any opposing party therein when such course is inadvisable in the sole discretion of the disabled party.

ARTICLE XII

NOTICES

12.1 Method. All notices, requests, demands or statements shall be in writing, and may be delivered personally to the party to be notified or may be sent by registered or certified United States mail, postage prepaid, with a return receipt requested to such party. Notice deposited in the mail in this manner shall be effective upon the expiration of seven (7) days after it is so deposited. Notice given in any other manner shall be effective only if and when received by the addressee. For the purposes of notice, the addresses of the parties to this Agreement shall be as follows:

If to Seller: State of Alaska
Commissioner of Natural Resources
Pouch "M"
Juneau, Alaska 99811

and

Commissioner of Revenue
Pouch "S"
Juneau, Alaska 99811

and

Director, Division of Oil and Gas
Pouch 7-034
Anchorage, Alaska 99510

If to Purchaser:

GOLDEN VALLEY ELECTRIC ASSOCIATION, INC.
P.O. Box 1249
Fairbanks, Alaska 99707

and (as long as the right to Oil is assigned thereto)

Vice President-Supply
MAPCO PETROLEUM Inc.
P.O. Box 645
Tulsa, Oklahoma 74101-0645

12.2 Change of Address. Each party may change its address for notice by giving notice of the change.

ARTICLE XIII
RULES AND REGULATIONS

This Agreement is subject to all present and future valid laws, orders, rules and regulations of the United States, the State of Alaska, and any duly constituted agency thereof.

ARTICLE XIV
SOVEREIGN POWER OF THE STATE

This Agreement and its covenants shall not be interpreted as a limit on the exercise by the State of Alaska of any of its sovereign or regulatory powers, whether conferred on the State by constitution, statute or regulation, including but not limited to, its regulatory power over the Leases. The exercise by the State of Alaska of any sovereign or regulatory power will not operate or be deemed to enlarge any rights of Purchaser or to limit or impair any obligations or liability of Purchaser under this Agreement, except for state statutes enacted after the effective date of this Agreement which have a direct and significant adverse effect on the ability of Purchaser to perform an obligation under this Agreement other than the obligations to accept, dispose, and pay for Royalty Oil tendered under this Agreement.

ARTICLE XV
SECURITY

Thirty (30) days prior to the Date of First Delivery, Purchaser shall cause to be furnished to Seller evidence that an irrevocable stand-by letter of credit for the benefit of Seller effective by Date of Delivery, will be issued by a state or national banking institution of the United States which is a member of the Federal Deposit Insurance Corporation and has an aggregate capital and surplus of not less than One Hundred Million Dollars (\$100,000,000), or other banking institution acceptable to Seller in its sole discretion. The principal face amount of the letter of credit shall initially be Five Million, Three Hundred Sixteen Thousand Dollars (\$5,316,000). The letter of credit shall be substantially in a form satisfactory to the Commissioner, but in any event shall not require any documents to be submitted in support of drafts drawn against this letter of credit other than the certified statement of the Commissioner or her designee and the Attorney General of the State of Alaska or his designee that Purchaser is liable to Seller for a sum equal to the amount of such draft, and that that sum is due and payable in full and has not been timely paid. In the event that Seller should have reasonable grounds for asserting any claims against Purchaser

under this Agreement and does assert those claims in an aggregate amount in excess of the aggregate principal face amount of the letter of credit then in effect, Purchaser shall upon Seller's request (whether or not Purchaser may deny, reject or otherwise resist such claims) cause the principal face amount of the letter of credit to be increased by an amount equal to the excess. The principal face amount of the letter of credit shall also be automatically increased by Purchaser without request from Seller whenever the face amount is less than the expected Purchase Price of sixty (60) days of Oil tendered under this Agreement, to an amount equal to the expected Purchase Price of sixty (60) days of Oil tendered. The principal face amount of the letter of credit may be decreased by Purchaser upon approval of Seller (which approval will not be unreasonably withheld) if the face amount is more than the expected Purchase Price of sixty (60) days of Royalty Oil tendered under this Agreement, to an amount equal to the expected Purchase Price of sixty (60) days of Royalty Oil tendered. The Commissioner may accept such other or additional security as she, in her sole discretion, considers adequate to protect Seller.

ARTICLE XVI

PREFERENTIAL HIRING AND NON-DISCRIMINATION

Purchaser agrees to hire and employ Alaska residents and Alaska companies to the extent they are available, willing and qualified for all work performed in Alaska that is performed under or in connection with this agreement. As used in this agreement "Alaska resident" means an individual who has resided in the State for one year at the time of hiring or employment and "Alaska companies" means those companies who are incorporated in the State of Alaska or whose principal place of business is in Alaska.

If this provision is determined to be unconstitutional by a court of competent jurisdiction, then Purchaser agrees to hire and employ Alaska residents and Alaska companies to the extent such preferential hiring is determined to be constitutional.

ARTICLE XVII
APPLICABLE LAW

17.1 Alaska Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Alaska, excluding any conflict-of-law rule or principle which might refer such construction to the laws of another state or country.

17.2 Submission to Jurisdiction. Any legal action or proceeding arising out of or relating to this Agreement or for the enforcement of the covenants or obligation of either party must be instituted in a State court of general jurisdiction sitting in the State of Alaska, and Purchaser hereby irrevocably submits to the jurisdiction of that court in any such action or proceeding.

ARTICLE XVIII
WARRANTIES

The purchase and sale of Royalty Oil under this Agreement is subject only to the warranties of Seller expressly set forth in this Agreement and Seller disclaims and Purchaser waives all other warranties, expressed or implied in law, whatsoever.

ARTICLE XIX
AMENDMENT

This Agreement may be supplemented, amended or modified at any time, but only by written instrument duly executed by the parties to this Agreement. Any material amendment to the contract which appreciably reduces the consideration received by the State requires prior approval of the Legislature of the State of Alaska.

ARTICLE XX
SUCCESSORS AND ASSIGNS

No assignment, pledge or encumbrance of this Agreement shall be made by either party without first obtaining the written consent of the other party. The Commissioner may grant such consent on behalf of the Seller. The Commissioner shall have sole and complete discretion in granting or denying a proposed assignment, pledge or encumbrance. Subject to the above requirements in this Article, this Agreement will be binding upon and inure to the benefit of each of the parties and its successors and permitted assignees. In addition, if Purchaser gains or acquires a controlling interest in an entity which has an agreement with Seller for the sale of Royalty Oil ("Other Agreement"), then Seller, at its option and on one year's notice, may require Purchaser to terminate either this Agreement or the Other Agreement. The choice of which Agreement to terminate will be Purchaser's. Purchaser may request that Seller waive this option in advance of Purchaser gaining a controlling interest in an entity which has an agreement with Seller for the sale of Royalty Oil. The Commissioner has sole and complete discretion in granting or denying the requested waiver.

ARTICLE XXI
HEADINGS

Headings used in this Agreement are for convenience only and shall not affect the construction of this Agreement.

ARTICLE XXII
RECORDS

22.1 Preservation of Records. Purchaser will preserve and maintain all books, accounts, and records relating to or arising out of the performance of this Agreement, including but not limited to the purchase or sale of Royalty Oil and its refined products, for a period of six (6) years. Purchaser will also maintain and preserve all similar books, accounts, and records of which

it has possession belonging to those third parties with whom it contracts for the performance of various parts of this Agreement. Neither Purchaser nor Seller shall be required to retain any records for more than six (6) years unless retention of such records is specifically required by applicable law or regulation. Purchaser shall either maintain its records within the State of Alaska or make such records available to Seller at Purchaser's principal office in the State of Alaska within thirty (30) days after written request by Seller.

22.2 Inspection of Records of Parties. Purchaser and Seller will accord to each other and to their authorized agents, attorneys, and auditors during reasonable business hours access to any and all property, records, books, documents, and indexes directly relating to Purchaser's or Seller's performance of this Agreement and which are under the control of the party from which access is desired so that the other party may inspect, photograph and make copies of that property, records, books, documents and indexes. In no event, however, shall Seller be required to disclose any information, data, or records which are required to be held confidential by state law or regulation. If the information obtained by Seller may be held confidential under state or federal law or regulation, Purchaser may request that that information be held confidential by Seller.

ARTICLE XXIII

INTERPRETATION OF TERMS AND CONDITIONS

In the event that there is a disagreement about the meaning or application of a word, term, or condition in this Agreement, Purchaser will present the arguments supporting its view in writing to the Commissioner for her consideration. The Commissioner will subsequently, within a reasonable time, issue a finding on the meaning or application of the disputed word, term, or condition, setting forth the basis for her conclusions. Purchaser agrees to accept findings by the Commissioner under this Article as long as there is substantial evidence supporting the Commissioner's findings. None of the above shall empower the Commissioner to set the price of the Oil should such price become subject to renegotiation pursuant to Section 2.3.

DATED this 8th day of February 1985.

SELLER: THE STATE OF ALASKA

Commissioner,
Department of Natural Resources

PURCHASER: GOLDEN VALLEY ELECTRIC ASSOCIATION, INC.

By _____
Michael P. Kelly
General Manager

STATE OF ALABAMA
OIL IN-KIND ROYALTY OIL CONTRACTS
(in barrels per day)

NOMINATION PERCENTAGES EFFECTIVE APRIL 1, 1985

PRUDHOE BAY UNIT

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	TERM	PRICE	
MAPCO	0.106667	35,000.06	11/26/79 - 12/31/2003	EXHIBIT B	1/
TESORO	0.213260	39,906.25	01/01/83 - 01/01/95	IN-VALUE	2/
CHEVRON	0.096000	10,000.00	05/30/84 - 01/01/95	IN-VALUE + \$.30	3/
GVEA 4/	0.026667	5,000.06	07/01/84 - 06/30/84	IN-VALUE + \$.30	3/
CHEVRON (COMP SALE)	0.026667	5,000.00	04/01/85 - 09/30/85	18.95	6/
CHEVRON (COMP SALE)	0.000000	15,000.00	04/01/85 - 03/31/86	18.95	6/
TEXACO (COMP SALE)	0.000000	15,000.00	04/01/85 - 09/30/85	18.96	6/
TEXACO (COMP SALE)	0.133333	25,000.00	04/01/85 - 03/31/86	18.96	6/
SOHIO (COMP SALE)	0.026667	5,000.00	04/01/85 - 09/30/85	18.43	6/
U.S. OIL (COMP SALE)	0.053333	10,000.00	04/01/85 - 03/31/86	18.96	6/
TOTAL RIK	0.922594	172,906.38			
TOTAL RIV	0.077406	14,513.62		IN-VALUE	2/
TOTAL RIK & RIV	1.000000	187,500.00			

NOMINATION PERCENTAGES EFFECTIVE OCTOBER 1, 1985

PRUDHOE BAY UNIT

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	TERM	PRICE	
MAPCO	0.106667	35,000.06	11/26/79 - 12/31/2003	EXHIBIT B	1/
TESORO PB 01	0.245330	45,999.30	01/01/83 - 01/01/95	IN-VALUE	2/
TESORO PB 02	0.130670	25,000.63	10/01/85 - 01/01/95	IN-VALUE + \$.35	5/
CHEVRON	0.096000	10,000.00	05/30/84 - 01/01/95	IN-VALUE + \$.30	3/
CHEVRON (COMP SALE)	0.000000	15,000.00	04/01/85 - 03/31/86	18.95	6/
TEXACO (COMP SALE)	0.133333	25,000.00	04/01/85 - 03/31/86	18.96	6/
U.S. OIL (COMP SALE)	0.053333	10,000.00	04/01/85 - 03/31/86	18.96	6/
TOTAL RIK	0.933334	175,000.06			
TOTAL RIV	0.066666	12,499.94		IN-VALUE	2/
TOTAL RIK & RIV	1.000000	187,500.00			

- 1/ Current EXHIBIT B price as of Oct 84 production month is \$18.28773.
- 2/ In-value price (10/84) = Weighted average price less field cost of \$.69 per barrel. Current in-value price as of Oct 84 is \$17.3365.
- 3/ In-value price (10/84) + \$.30 premium + \$.69 field cost.
- 4/ This contract will terminate 06/30/85. A long-term contract to GVEA for 5,000 bpd will be submitted to the Legislature this Session and commence four months after approval by the Governor and the Legislature.
- 5/ In-value price (10/84) + \$.35 premium + \$.69 field cost.
- 6/ This price will fluctuate monthly based on posted prices of West Texas Sour crude.

STATE OF ALASKA
 ANS IN-KIND ROYALTY OIL CONTRACTS
 (in barrels per day)

NOMINATION PERCENTAGES EFFECTIVE APRIL 1, 1985

KUPARUK RIVER UNIT

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	TERM	PRICE	
CHEVRON (COMP SALE)	0.222222	5,000.00	04/01/85 - 09/30/85	17.09	1/
CHEVRON (COMP SALE)	0.222222	5,000.00	04/01/85 - 09/30/85	17.09	1/
UNION (COMP SALE)	0.222222	5,000.00	04/01/85 - 09/30/85	17.45	1/
TOTAL RIK	0.666667	15,000.00			
TOTAL RIV	0.333333	7,500.00		IN-VALUE	2/
TOTAL RIK & RIV	1.000000	22,500.00			

NOMINATION PERCENTAGES EFFECTIVE OCTOBER 1, 1985

KUPARUK RIVER UNIT

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	PRICE	
CHEVRON (COMP SALE)	0.000000	0.00		
CHEVRON (COMP SALE)	0.000000	0.00		
UNION (COMP SALE)	0.000000	0.00		
TOTAL RIK	0.000000	0.00		
TOTAL RIV	1.000000	22,500.00	IN-VALUE	2/
TOTAL RIK & RIV	1.000000	22,500.00		

1/ This price will fluctuate monthly based on posted prices of West Texas Sour crude.

2/ In-value price (10/84) = weighted average price less field cost.
 of \$.40 per barrel. Current in-value price as of Oct 84 is \$16.4587,

STATE OF ALASKA
COOK INLET IN-KIND ROYALTY OIL CONTRACTS
(in barrels per day)

NOMINATION PERCENTAGES EFFECTIVE APRIL 1, 1985

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	TERM	PRICE	
TESORO	100.000000	6,718.75	01/01/84 - 09/30/85	IN-VALUE	1/
TOTAL RIK	100.000000	6,718.75			
TOTAL RIV	0.000000	0.00			
TOTAL RIK & RIV	100.000000	6,718.75			

NOMINATION PERCENTAGES EFFECTIVE OCTOBER 1, 1985

COMPANY	% OF DAILY ROYALTY OIL	QUANTITY	PRICE	
TESORO	0.000000	0.00		
TOTAL RIK	0.000000	0.00		
TOTAL RIV	100.000000	6,718.75	IN-VALUE	1/
TOTAL RIK & RIV	100.000000	6,718.75		

1/ In-value price (10/84) = weighted average price less transportation cost. Current in-value price as of Oct 84 is \$24.854.

STATE OF ALASKA
COMPETITIVE ROYALTY OIL SALE

PAGE 1

DEC. 11, 1984

PURCHASER	LOT #	ESTIMATED BARRELS PER DAY	CONTRACT LENGTH (IN DAYS)	TOTAL EST. BARRELS PER CONTRACT	BASE PRICE	PREMIUM	TOTAL REALIZED (1)	DIFFERENCE REALIZED (1) (2)
CATEGORY A: KUPARUK								
CHEVRON	* 1	5,000	182.5	912,500	916.92	98.82	916,187,750.00	9884,177.13
UNION	* 2	5,000	182.5	912,500	916.92	98.53	915,923,125.00	9539,552.13
CHEVRON	* 3	5,000	182.5	912,500	916.92	98.17	915,594,625.00	9211,052.13
SUBTOTAL		15,000		2,737,500			947,705,500.00	91,554,781.38
HIGHEST PREMIUM BID:			98.82	AVERAGE PREMIUM BID:		98.51		
CATEGORY B: PRUDHOE								
U.S. OIL	1	5,000	365	1,825,000	917.92	91.84	934,682,000.00	91,783,635.75
U.S. OIL	2	5,000	365	1,825,000	917.92	91.84	934,682,000.00	91,783,635.75
CHEVRON	* 3	5,000	365	1,825,000	917.92	91.83	934,583,750.00	91,685,485.75
CHEVRON	* 4	5,000	365	1,825,000	917.92	91.83	934,583,750.00	91,685,485.75
CHEVRON	* 5	5,000	365	1,825,000	917.92	91.83	934,583,750.00	91,685,485.75
TEXACO	* 6	5,000	365	1,825,000	917.92	98.64	933,872,000.00	9973,635.75
TEXACO	* 7	5,000	365	1,825,000	917.92	98.64	933,872,000.00	9973,635.75
TEXACO	* 8	5,000	365	1,825,000	917.92	98.64	933,872,000.00	9973,635.75
TEXACO	* 9	5,000	365	1,825,000	917.92	98.64	933,872,000.00	9973,635.75
TEXACO	* 10	5,000	365	1,825,000	917.92	98.64	933,872,000.00	9973,635.75
SUBTOTAL		50,000		18,250,000			9342,315,250.00	913,331,887.50
HIGHEST PREMIUM BID:			91.84	AVERAGE PREMIUM BID:		98.84		
CATEGORY C: PRUDHOE								
CHEVRON	* 1	5,000	182.5	912,500	917.92	91.83	917,291,875.00	9842,782.88
TEXACO	* 2	5,000	182.5	912,500	917.92	98.64	916,936,000.00	9486,827.88
TEXACO	* 3	5,000	182.5	912,500	917.92	98.64	916,936,000.00	9486,827.88
TEXACO	* 4	5,000	182.5	912,500	917.92	98.64	916,936,000.00	9486,827.88
SONIO	5	5,000	182.5	912,500	917.92	98.51	916,817,375.00	9368,282.88
SUBTOTAL		25,000		4,562,500			984,917,250.00	92,671,389.38
HIGHEST PREMIUM BID:			91.83	AVERAGE PREMIUM BID:		98.69		
TOTALS FOR ALL LOTS:		18	90,000	25,550,000			9474,938,000.00	917,557,978.25

(1) THESE PROJECTIONS ASSUME THAT CURRENT MARKET CONDITIONS AND PRICES CONTINUE.

(2) THIS AMOUNT IS THE DIFFERENCE BETWEEN THE ESTIMATED ROYALTY-IN-VALUE RECEIPTS BASED ON THE VOLUME WEIGHTED AVERAGE OF PRODUCERS' REPORTED NETBACK PRICES (OCTOBER) AND THE ESTIMATED RECEIPTS OF THE COMPETITIVE SALE BASED ON THE BID PREMIUM PLUS THE BASE PRICE.

(*) PRIORITY BIDDERS

STATE OF ALABAMA
COMPETITIVE ROYALTY OIL SALE

DEC. 11, 1984

NUMBER OF BIDS SUBMITTED:	49
NUMBER OF BIDDERS PARTICIPATING:	8
HIGHEST PREMIUM BID:	1.04
SUBMITTED BY: U.S. OIL	
ESTIMATED TOTAL REVENUES FROM SALE:	\$474,938,000
COMPANY WITH MOST WINNING BIDS:	TEXACO WITH 8 LOTS
NUMBER OF LOTS WON BY PRIORITY BIDDERS:	15
NUMBER OF LOTS WON BY NON-PRIORITY BIDDERS:	3

STATE OF ALABAMA
DEPARTMENT OF REVENUE
DIVISION OF TAX AND FOS

ESTIMATED PRODUCTION FOR PHASE I, II, AND SUPPLEMENTAL RIVER UNITS

(c) TENDON'S CURRENT CONTRACT CALLS FOR A MOLINUM QUANTITY OF 24,535 BBL OF DAILY PRODUCE. MOLINUM OIL, LESS COOK INLET MOLINUM PRODUCTION, THE QUANTITY IS 21,685 BBL IN 1964, AND WILL BE 21,363.535 BBL JAN. 1, 1965. THIS CONTRACT WILL BE INCREASED TO ITS MOLINUM QUANTITY ON OCTOBER 1, 1965 DUE TO OVERPRODUCTION OF THE COOK INLET CONTRACT ON THAT DATE. THE CONTRACT EXPIRES JANUARY 1965.

- (3) MOST OF THIS VOLUME (ABOUT 25,000 BPO), WHICH IS CURRENTLY BEING TRADED "IN WALE," WAS SOLD COMPETITIVELY FOR DELIVERY APRIL 1, 1965 THRU SEPT. 30, 1965. ON OCTOBER 1, 1965 IT IS ANTICIPATED THAT TROING WILL COMEORE DELIVERIES UNDER ITS 1279/63 PALADOC CONTRACT, WHICH HAS A MINIMUM QUANTITY OF 13,865 OF DAILY PALADOC ROYALTY OIL AND EXPIRES JAN. 1, 1965.
- (4) OCEANOGRAPH CONTRACT CALLS FOR A MINIMUM QUANTITY OF 5.66 OF DAILY PALADOC ROYALTY OIL. THE CONTRACT EXPIRES JANUARY 1, 1965.
- (5) DELIVERIES WILL COMEORE APRIL 1, 1965 FOR 25,000 BPO OF PALADOC NET UNIT ROYALTY OIL AND 15,000 BPO OF RUBBER RIVER UNIT ROYALTY OIL, AND WILL CONTINUE FOR ONE-YEAR, AND SIX-MONTH PERIODS, RESPECTIVELY, AS A RESULT OF THE DEC. 11, 1964 COMPETITIVE SALE. PRIOR TO THAT TIME THIS OIL BEARING "IN WALE."

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

BILL SHEFFIELD, GOVERNOR

POUCH 7-034
ANCHORAGE, ALASKA 99510

STATE OF ALASKA Alaska Royalty Oil & Gas Development Advisory Board Notice of Public Hearing

The Alaska Royalty Oil and Gas Development Advisory Board will hold a public hearing on a proposed sale of State royalty oil from the Prudhoe Bay Unit. The hearing will be held by teleconference on Wednesday, February 20, 1985, at 10:30 a.m. The teleconference system will be available at that time in Anchorage, Fairbanks, and Juneau. The public may appear at the following locations to present testimony:

Legislative Information Office
1024 West 6th
Anchorage, Alaska
278-9624

Legislative Information Office
315 Barnett Street, Suite 101
Fairbanks, Alaska
452-4448

State Office Building
10th Floor Conference Room
Juneau, Alaska
465-3836

The Department of Natural Resources has proposed a long-term, noncompetitive sale of State royalty oil from the Prudhoe Bay Unit to Golden Valley Electric Association (GVEA).

The proposed GVEA agreement is for the sale of 2.667% of the daily royalty oil available from the Prudhoe Bay Unit (approximately 5,000 bpd). The contract would commence four months after approval by the Governor and the Legislature, and would terminate June 30, 1995. The proposed contract includes a provision allowing either party to reopen price negotiations during the month of July, 1987 and every two years thereafter.

The Alaska Royalty Oil and Gas Development Advisory Board, under AS 38.06.040 (a)(2), is required to "hold public hearings on proposed sales, exchanges, or other disposals of royalty oil or gas to determine whether the proposals comply with AS 38.06.070."

AS 38.06.070 states the "criteria" the Board must consider in the exercise of its powers. These are:

- (1) the revenue needs and projected fiscal condition of the state;
- (2) the existence and extent of present and projected local and regional needs for oil and gas products and by-products, the effect of state and federal commodity allocation requirements which might be applicable to those products and by-products, and the priorities among competing needs;

- (3) the desirability of localized capital investment, increased payroll, secondary development and other possible effects of the sale, exchange or other disposition of oil and gas or both;
- (4) the projected social impacts of the transaction;
- (5) the projected additional costs and responsibilities which could be imposed upon the state and affected political subdivisions by development related to the transaction;
- (6) the existence of specific local or regional labor or consumption markets or both which should be met by the transaction;
- (7) the projected positive and negative environmental effects related to the transaction; and
- (8) the projected effects of the proposed transaction upon existing private commercial enterprise and patterns of investments.

The evaluation of proposed sales in accordance with the criteria and the public hearing process is to enable the Board to more effectively carry out its purpose to "facilitate the wise development of Alaska's oil and gas royalty interests by providing means and procedures for sales, exchanges or other disposition of those interests in ways calculated to promote private economic growth consistent with applicable environmental standards and public fiscal stability...." AS 38.06.010. The Board is required to recommend to the State Legislature whether the proposed sale to GVEA should be approved or rejected. AS 38.06.050

The Board solicits comments from the public concerning this proposed sale. You are invited to present a statement, oral or written, at the hearing or send it directly to the Chairman, Alaska Royalty Oil and Gas Development Advisory Board, c/o Kay Brown, Director, Division of Oil and Gas, Department of Natural Resources, Pouch 7-034, Anchorage, Alaska 99510.

Copies of the proposed meeting agenda, applicable Alaska statutes, regulations, and other information relating to the proposed sale may be obtained by contacting Sandra Schwartzbauer at 265-4274.

James B. Gottstein
Chairman

Pub: January 17, 1985

Proposed Agenda

**ALASKA ROYALTY OIL & GAS DEVELOPMENT ADVISORY BOARD
PUBLIC HEARING**

February 20, 1985

10:30 a.m. - 4:30 p.m.

(Teleconference with Anchorage, Juneau and Fairbanks)

**Legislative Information Office
1024 West 6th
Anchorage, Alaska**

**Legislative Information Office
315 Barnett Street, Suite 101
Fairbanks, Alaska**

**State Office Building
10th Floor Conference Room
Juneau, Alaska**

- (1) Opening remarks, roll call, approval of minutes of the previous Royalty Board meeting, adoption of agenda.
- (2) Overview of proposed non-competitive sale of royalty oil to Golden Valley Electric Association.
- (3) Public testimony on GVEA contract.
- (4) Royalty Board vote on GVEA contract for recommendation to Legislature, which must approve the contract (AS 38.06.050-055).
- (5) Report from Director, Division of Oil and Gas, on:
 - . Results of 2nd competitive Royalty Oil Sale;
 - . Proposed statute change; and
 - . Possible royalty oil solicitation.
- (6) Report from Jim Gottstein on underlift proposal.
- (7) Presentations by companies seeking to purchase royalty oil. *
- (8) Other business or announcements from board members.
- (9) Adjournment.

* Companies that wish to make a brief presentation to the board should call Roberta Staats at 265-4257 to schedule time on the agenda.



RECORDS CERTIFICATION



I, the undersigned, an employee of the State of Alaska, do hereby certify that the microfilm images on this microform are accurate reproductions of the original records of the State of Alaska as accumulated during the regular course of business, and that it is the established policy and practice of this State to microfilm its records and to dispose of the original records after microfilm reproductions have been made.


Signature of Camera Operator


Date

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STATE OF ALASKA



POUCH V
JUNEAU, ALASKA 99811
(907) 485-4941

HOUSE SPECIAL COMMITTEE ON OIL AND GAS

MEMORANDUM

To: All Interested Persons
From: Rep. Mike Davis, Chairman
House Special Committee on Oil and Gas
Date: March 20, 1986
Re: Valdez Oil Terminal Facility Oversight Hearing

The House Special Committee on Oil and Gas will conduct an oversight hearing regarding operations at Alyeska's Valdez Oil Terminal Facility at 4:00 p.m. on Thursday, April 3. The meeting will be held in Room 519 of the Capitol Building, and will be teleconferenced to the legislative information offices in Anchorage, Fairbanks and Valdez. Persons in other communities wishing to participate in the hearing may request, through my office, that additional teleconference connections be made for them.

Representatives from Alyeska, the Environmental Protection Agency, and the Alaska departments of Environmental Conservation, Labor and Law have been asked to participate in the hearing. Businessman Charles Hamel is also expected to participate by teleconference.

The main purpose of the hearing is to provide members of the House Special Committee on Oil and Gas with information regarding past and present problems associated with the water treatment plant at Alyeska's Valdez oil terminal, the status of state and federal investigations into operations at the facility, a description of state and federal compliance orders that have been issued to Alyeska, and the degree and timeliness with which the requirements of the compliance orders are being met.

Valdez Oil Terminal Facility Oversight Hearing - April 3

The purpose of the hearing is to provide members of the legislature with the following information regarding the oil terminal:

1. What operational problems have been associated with the terminal's water treatment plant since this facility came on-line in 1977?
2. To what extent have operational problems at the terminal's water treatment plant led to the uncontrolled release of toxic pollutants into Prince William Sound?
3. To what extent has the facility been operated in violation of its water-discharge permit?
4. Alyeska's oil spill contingency plan expired on Jan. 3. What is the current status of Alyeska's new oil contingency plan? What is Alyeska's degree of preparedness regarding the containment and cleanup of a major oil spill?
5. What hazardous chemicals have workers at the plant been exposed to, and what has been done to abate this threat to their health?
6. What is the present status of federal investigations into operations at the water treatment facility, including investigations by the Environmental Protection Agency, National Institute of Occupational Safety and Health, and the General Accounting Office? What actions are being taken by these agencies?
7. To what extent are investigations being directed toward Alyeska's alleged falsification of pollution tests, and toward the company having allegedly ignored internal documents that suggested correcting major operational deficiencies at the facility?
8. What is the present status of state investigations into operations at the water treatment facility? What actions are being taken by the Alaska Department of Environmental Conservation? What, if any, criminal charges are under consideration by the Department of Law?

J

TESTIMONY OF IVAN L. HENMAN

ALYESKA PIPELINE SERVICE COMPANY

House Special Committee on Oil and Gas
April 3, 1986

Good afternoon. My name is Ivan Henman, and I am in charge of the Ballast Water Treatment Facility Task Force established by Alyeska Pipeline Service Company to address the concerns raised about that facility--which I shall refer to as the BWT facility. Prior to this assignment, I was head of the Engineering Department at Alyeska. Also, I was Pipeline Superintendent for Alyeska from 1982 to 1985 and Terminal Superintendent at our Marine Terminal in Valdez from 1980 to 1982.

I would also like to introduce Bob McCollom and Dr. Richard Wade. Bob McCollom is the Vice President and Manager of Woodward-Clyde's Alaska operation. Bob has been in charge of the testing and studies which have been undertaken in response to the EPA Compliance Order.

Woodward-Clyde Consultants is a national consulting firm with extensive expertise in wastewater management. Their professional support staff includes Ph.D. level engineers and scientists in wastewater management and water quality.

Doctor Richard Wade is Director of Risk Management Services for International Technology Corporation from San Francisco, California. Dr. Wade has been retained by Alyeska to evaluate our industrial hygiene program and to be sure that we remain in compliance with regulations.

We are here in response to your request for information about the Valdez BWT facility including the status of our response to various action items included in the Compliance Order and Amended Compliance Order issued by the Environmental Protection Agency.

The jurisdiction of EPA and Alaska Department of Environmental Conservation is based upon the legal requirement for a permit before treated ballast water can be discharged from the BWT facility. It is called a National Pollutant Discharge Elimination System Permit, or for short, an NPDES Permit. NPDES Permits set limits on the level of pollutants which may be discharged with treated water and require compliance with the state water quality criteria.

In view of the various allegations about our Terminal, the EPA and ADEC last November requested a number of studies of the BWT facility's operation. Alyeska and its consultants embarked upon these studies, including an analysis of every process of the facility to determine if we are discharging sludge into the bay. We have literally looked at the plant inside and out and have even employed under-water cameras inside the tanks.

Most of these studies have been completed; all of them soon will be. All requirements of the Compliance Order have been submitted on or before the dates they were due. Both EPA and ADEC have met with Alyeska at least monthly and they have been kept completely informed of all our efforts. Their advice, recommendations, and suggestions as to the contents of the studies has been very welcome and helpful.

All of these extensive studies demonstrate that there is no sludge being discharged into Port Valdez, that there is no detectable damage to the environment of Port Valdez and Prince William Sound resulting from the operation of the BWT facility, and that the facility has been operated in compliance with applicable health and safety standards.

A brief history of the BWT plant may help to put the various allegations and the results of our studies into their proper context. The BWT facility treats the oily seawater, called ballast, which is carried in tankers arriving at the Marine Terminal to load crude oil. The seawater is pumped into the vessels when they leave ports elsewhere to begin their journeys to Valdez; this is done to provide stability when the

tankers are sailing without cargoes of oil. This ballast water is carried in the vessel's oil cargo compartments when they are empty of oil. This water becomes mixed with small amounts of oil remaining in the tanks. When the tankers arrive at the Marine Terminal, the ballast water must be pumped out of the oil cargo tanks so that the vessels may be loaded with crude oil. It is pumped directly to the BWT facility which separates the oil from the ballast. It does this mainly through gravitation in three large settling tanks.

To more easily understand the BWT facility, it may be helpful to think in terms of a three-stage treatment plant:

- ° First, gravity separation of the oil, water, and a small amount of solids. This occurs in the gravity settling tanks.
- ° Second, a chemical and air injection system to further reduce the amount of oil in the water. This secondary treatment takes place in the dissolved air flotation or DAF chambers.
- ° Third, retention in large impound basins for final separation before the treated ballast water is discharged into the waters of Port Valdez.

Gravity separation means that at each of the three treatment stages, oil--being lighter--rises to the top, and water settles out at the bottom. There will also be an emulsion layer between the oil and water, and this layer is composed of oil, water, and some solids. In addition, during the separation process, heavier solids, such as sand, will settle to the bottoms of the tanks, and they may carry some of the oil with them. Our recent studies have confirmed that this accumulation is substantially less than one inch per year in each of the tanks. This slow buildup of solids in the tanks means the tanks need only be cleaned when they are entered for periodic maintenance--normally every four to five years. That, in a nutshell, is how our system operates.

We believe Alyeska has compiled a good record in operating its BWT facility under the NPDES Permit. Despite its good record, Alyeska has been accused of producing large quantities of sludge at the BWT facility and dumping it into Port Valdez. This simply is not true.

I think if you look closely at these allegations regarding sludge, you will find many of them are based on references to the oil-water emulsion in the settling tanks. However, this emulsion is pumped to the crude system and ultimately loaded in tankers. It is not discharged with the treated effluent.

There is another area of possible confusion. The seawater taken in by the tankers as ballast just naturally contains suspended particles of silt. Most of these particles remain suspended in the ballast water throughout the treatment process, just as they were suspended when picked up by the tankers. This naturally occurring material is called TSS for total suspended solids. There is nothing unusual about the presence of this TSS in the discharge effluent from the BWT plant. By way of comparison, the TSS in our treated effluent is 50 times less than the TSS in water flowing into Port Valdez naturally from the Lowe River during the summer time.

The fact remains, the only thing discharged from our BWT facility is the treated ballast water. The recovered crude oil and the oil-water emulsion are pumped to our crude oil system.

The Compliance Order and Amended Compliance Order issued by EPA found that Alyeska had violated its NPDES Permit because sludge that had been separated or removed from one unit of the system had been reintroduced into another unit. Alyeska disagreed with those findings and with EPA's right to issue the order. Nonetheless, Alyeska agreed to cooperate to the best of its ability to comply with the studies required by the Compliance Order. We have done that.

The studies have confirmed that there has been no significant accumulation of sludge in the ballast water treatment process units. Measurements have generally been in the range of one to two inches in the tank bottoms and DAF chambers. The studies also confirm that there is no discharge of sludge to Port Valdez. We have also conducted extensive testing of the sludge that has been removed from the system. These tests show conclusively that this material is not a hazardous waste as defined by government regulations. The agencies have been advised of our findings, and they have not disagreed.

I said Alyeska's record of BWT operation is good. As with any plant, however, there are times when operations are less than 100 percent perfect. For the months October, 1985 through February, 1986, the monthly average of lab test results for aromatic hydrocarbons (BTX) in our effluent has averaged about 6.5 parts per million--slightly higher than the six parts per million authorized by the permit. Both EPA and ADEC have been kept fully informed of these results. These results followed a change in Alyeska's procedures for preserving effluent samples. This change was made because of a recommendation which arose out of an internal audit. It was not a requirement imposed by the Compliance Order. Nevertheless, we will be working with the EPA and ADEC to resolve the issue.

Perhaps the most important fact to recognize is that the available scientific evidence, including preliminary data taken by the University of Alaska last fall, indicates that there has been no detectable damage to the environment of Port Valdez and Prince William Sound as a result of Alyeska's operation of the ballast water system.

As to the alleged health hazards associated with the operation of the facility and the handling of sludge, we have found that company policies and procedures provide for a safe work environment. We have conducted our own industrial hygiene inspections of the facility and also retained industrial hygiene consultants to inspect our facilities in 1981 and again in 1984. And there have been other inspections.

In 1985, the Alaska Department of Occupational Safety and Health conducted an inspection of the Terminal. DOSH found no violations of health and safety standards. Also, in 1985, another industrial hygiene inspection was conducted at the Terminal by our consultant, IT Corporation. Again, the Terminal was found to be operating in accordance with applicable health and safety standards.

And, in 1986 the National Institute of Occupational Safety and Health (NIOSH) visited the Terminal to investigate alleged health hazards. We have cooperated fully with the investigation. The NIOSH report has just been received by Alyeska. NIOSH concluded there were no chronic health effects from chemical exposures at the BWT and informed the Alaska Department of Labor that they contemplate no further medical studies.

We feel that we have an outstanding record in the safety and health protection of our employees. Nonetheless, we are increasing our monitoring efforts to assure that our existing industrial health procedures and policies are followed by all employees and contractor personnel.

We have responded to any and all concerns about occupational safety and health at the Terminal. And we continue to respond to suggestions for improvement in our operating procedures and to initiate such improvements ourselves to assure the safety and health of the persons employed there.

In conclusion, I think the facility at Valdez has been one of the most analyzed of its kind in the world. We have made the operation and all of our records available for inspection by the appropriate government agencies. We have consistently operated the BWT system in a good faith effort to achieve its maximum effectiveness in accordance with its design. We have been cooperating with the agencies and meeting the requirements of the Compliance Order. We believe we have operated the facility in a manner to protect our employees, contractors, and the marine environment of Port Valdez and Prince William Sound. Thank you.



DEPARTMENT OF HEALTH & HUMAN SERVICES

Public Health Service

RECEIVED

APR 1 1986

OFFICE OF THE COMMISSIONER

Centers for Disease Control
National Institute for
Occupational Safety & Health
Robert A. Taft Laboratories
4676 Columbia Parkway
Cincinnati OH 45226-1998

March 26, 1986
HETA 86-132

Annette S. Thorn, M.D., M.P.H.
Medical Director of Occupational Health
Alaska Department of Labor
P.O. Box 1149
Juneau, Alaska 99802

Comm.	
Deputy	
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Info. Off.	
Adm. Asst.	
Int. Aud.	
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To: <i>File</i>	
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Dear Dr. Thorn:

I would like to report the findings of my investigations among workers at the Ballast Water Treatment Facility (BWT) at Alyeska Pipeline Service Company's marine terminal in Valdez, Alaska. You had requested a NIOSH investigation because of reports of health problems among contract laborers who performed such jobs as cleaning tanks, dissolved air flotation (DAF) cells, basins, and ponds, and because of workers' concerns about potential health effects resulting from exposure to organic vapors and sludge during this work.

According to the business manager for the Construction and General Laborers Union -- Local 341, about 75 union members have worked at the BWT. An estimated 40 have had more than minimal contact with sludge, and an estimated 15-20 of these had heavy exposure or health complaints. I interviewed a sample of 10 of these workers, 7 in Anchorage and 3 in Valdez..

During our walk-through inspection of the BWT, I interviewed 13 employees. These included eight maintenance employees and five others (operators and oil spill and marine technicians). I also interviewed by telephone one maintenance worker from a different shift who, I had been told, had health complaints.

Five of the eight maintenance workers at the plant (and the one interviewed by phone) reported headache, dizziness, or nausea sometimes when working around the DAF cells without a respirator. These symptoms typically resolved within two hours, sometimes within minutes, after leaving the area or putting on a respirator. One worker reported symptoms lasting 1-1/2 days after performing work (not his usual job) in the DAF area. Another worker reported a rash after contact with oil in the past, but had no current problem.

There was agreement among Alyeska employees that protective clothing and respirators were readily available, whether or not specifically required for a particular job. There was also general agreement that work involving the most

contact with sludge was done by contractors. Some Alyeska employees observed contract laborers using the same protective gear as Alyeska employees, but others said that this was not always the case.

The contract laborers reported acute irritative, respiratory, and other symptoms. They also reported a variety of chronic respiratory, dermatologic, neurologic, and other problems. Many reported that protective equipment was not readily available, that it was not in good condition, or that it was provided without adequate instruction in its use.

In summary, Alyeska maintenance workers reported self-limited symptoms associated with work in the DAF area without a respirator. Such symptoms are consistent with exposures to volatile organic compounds known to be present in the area. Although measured exposures have been within current Alaska Department of Labor standards, at levels that would not be expected to produce acute symptoms, exposure concentrations averaged over the duration of the job (rather than over the full shift) have not been determined for specific maintenance jobs. Furthermore, symptoms can occur even when air concentrations of individual substances are below their OSHA permissible exposure limits, especially when there is exposure to a combination of substances.

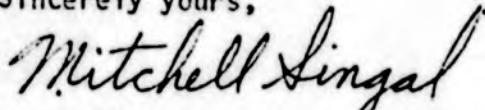
Except for their severity, the acute symptoms reported by contract laborers were comparable to those reported by Alyeska employees and were consistent with unprotected exposure to substances present in the BWT. We could not answer the question of whether unprotected or inadequately protected exposure was as common in the past as claimed by the laborers. Even if there were heavy exposures in the past, however, the reported chronic health problems, in my opinion, were sufficiently varied that they did not suggest a pattern of association with exposures at the BWT. (This does not rule out the possibility that there may be individual cases of health problems related to past exposures at the BWT, but evaluation of such cases on an individual basis is beyond the scope of a NIOSH investigation.) Given the lack of an identified chronic health effect characteristic of potential chemical exposures at the BWT, the relatively small group of workers with substantial exposure to sludge or other substances, the sporadic occurrence of such exposures, and potential exposures from other jobs over the years, I do not think that further epidemiologic investigation of past workers for chronic health effects attributable to exposures at the BWT would be productive.

On the basis of symptoms reported by Alyeska workers, *some maintenance tasks in the DAF area appear to warrant routine use of respirators.* Exposures associated with the various tasks should be monitored. Respirator usage can then be based on the exposure data.

Page 3 - Annette S. Thorn, M.D., M.P.H

Although no further medical or epidemiologic evaluation is contemplated, NIOSH plans to evaluate employee exposures during a tank cleaning operation, currently scheduled for April 1986.

Sincerely yours,



Mitchell Singal, M.D., M.P.H.
Assistant Chief
Medical Section
Hazard Evaluations and Technical
Assistance Branch
Division of Surveillance, Hazard
Evaluations, and Field Studies

cc:

Gary P. Bader
Mano Frey
Richard L. Wade
Donald Whorton, M.D., M.P.H.
Daniel Lawn
John P. Middaugh, M.D.
Don Praast
Charles Hamel
Allen Stayman

EPA STATUS REPORT ON
ALYESKA PIPELINE SERVICE CO.
VALDEZ, ALASKA
BALLAST WATER TREATMENT PLANT

This ballast water treatment plant is located at the southern end of the Trans-Alaska Pipeline and is one of the world's largest such facilities. Oily wastewater from tanker ballasting is treated prior to discharge into Port of Valdez, a subarctic fjord. This facility has been under an EPA National Pollutant Discharge Elimination System (NPDES) permit since start-up in 1977.

During a routine annual compliance inspection in 1984, several questions were raised by EPA concerning the operation of the facility. A Clean Water Act, Section 308 "Request for Information" was issued in January 1985. A joint EPA/Alaska Department of Environmental Conservation (ADEC) follow-up compliance inspection was done in April, 1985.

Based upon the response to the Section 308 "Request for Information" and the April inspection, a Clean Water Act, Section 309 Order was issued on July 12, 1985, which required the company to stop reintroducing sludges into the ballast water treatment plant and to submit a plan describing the procedures that would be followed in removing and disposing of all sludges. Specifically, EPA found that "on numerous occasions agents and employees of the respondent removed sludges from one part of the BWT (i.e. retention ponds) and reintroduced those sludges into the wastewater (i.e. 90 tanks) being treated within the BWT, in violation of Part II.A.6. of the NPDES permit.

The major pollutants of concern to EPA in ballast water coming into the plant and their ranges are as follows:

<u>Pollutant</u>	<u>Typical Ballast Water Ranges</u>
Oil & Grease	10-40 mg/l
Total Suspended solids	20-150 mg/l
pH	6-9
Aromatic Hydrocarbons	1-10 mg/l

"BWT" refers to the ballast water treatment facility. The treatment process consists of gravity settling in one of three "90 tanks", followed by dissolved air floatation (DAF), transfer to a retention or impound basin, and discharge to Port Valdez. The "80 tanks" are a part of the oil recovery system. Oil skimmed from these tanks is transferred with crude oil from the Trans-Alaskan Pipeline onto tanker ships.

As a result of implementing a laboratory quality assurance program required by the Compliance Order, the Company has modified its laboratory procedures for testing for BTX. Prior to October 1985, BTX samples were not acidified at the time of collection to preserve the sample. Since October monthly average BTX values in the plant effluent have been in violation of the permit limits.

Receiving water monitoring and computer modeling of the effluent plume in Port Valdez appear to show that violations of State water quality standards have occurred at the boundary of the mixing zone. Further study is underway to confirm this.

Further EPA/ADEC sampling inspections were conducted in July and August 1985. Based upon these visits and the Agency determination that the Company's response to the original order provided essentially a continuation of existing practices, an amended Order was issued on November 6, 1985. This amendment set out 13 specific actions required of the company with related time schedules for progress toward compliance with the 309 Order schedule for each action. A joint EPA/ADEC/Alyeska work group has been established to monitor progress toward compliance with the 309 Order.

EPA is developing a new discharge permit for the facility. At this time we anticipate soliciting public comment on the draft permit in June 1986. This schedule is subject to review. After addressing comments received on the draft permit and the Alaska Department of Environmental Conservation's certification under Section 401, EPA will finalize and issue the permit.

EPA is committed to completing the evaluations required for reissuance of the permit in as timely a manner as possible. While a number of aspects of the permit development process can proceed independently from the enforcement investigation, EPA feels that certain aspects of the permit must be closely coordinated with the enforcement investigation. In the interim, the existing NPDES permit has been continued under the Administrative Procedures Act, and as such remains fully effective and enforceable.

Attachments to this summary include:

1. Table 1, Enforcement Actions taken by EPA
2. Table 2, Status of Actions Required of Alyeska Under Section 309 Compliance Order
3. July 12, 1985 Section 309 Compliance Order
4. November 6, 1985 Amendment to Section 309 Compliance Order

TABLE 1. ENFORCEMENT ACTIONS TAKEN BY EPA

Jan. 28, 1985	Issuance Date of a Section 308 Formal Request For Information No. 11084-12-04-308
April 5, 1985	Letter From Robert S. Burd To Alyeska Requiring Retention of All Records Presently in Possession or Control of the Company
July 12, 1985	Issuance Date of Section 309 Compliance Order No. 1085-07-35-309A
Nov. 6, 1985	Issuance Date of Amendment to Section 309 Compliance Order No. 1085-07-35-309A

TABLE 2. STATUS OF ACTIONS REQUIRED OF ALYESKA
UNDER SECTION 309 COMPLIANCE ORDERS

March 20, 1986

Paragraph	Task	Due Date	Status
<u>309 ORDER NO. 0185-07-35-309A (7/12/85)</u>			
1	Cease reintroduction of sludge to treatment system.	Immediately.	See below.
2	Submit sludge handling plan.	9/15/85	Plan submitted on time. EPA's evaluation resulted in issuance of amended order.
<u>AMENDED 309 ORDER NO. 1085-07-35-309A (11/6/86)</u>			
	Consistent with the timeframes below, cease and desist reintroduction, resuspension, or re-entrainment of sludges into treatment plant.	See below.	See below.
10	Submit plan for transfer of wastewater from crude oil storage tanks to 90 tanks. Implement upon approval.	11/20/85	Plan submitted on time & implemented by Alyeska. Approved March 19, 1986.
11	Order equipment for continuous flow-weighted effluent sampling.	11/20/85	Completed on time.
5	Submit study of DAF flow velocity and plan for correcting any operational problems. Implement plan upon approval.	1/6/86	Plan submitted on time. Company notified that submittal was inadequate.
7	Submit study for treatment and disposal of DAF and impound basin "float". Implement upon approval.	1/6/86	Plan submitted on time. Under EPA/ADEC review.
6	Reinstall and operate originally designed equipment in DAF.	3/6/86	
OR			
	Submit plan for equivalent or better removal of sludges. Implement upon approval.	1/6/86	Plan submitted on time. Company notified that submittal was inadequate.

- | | | | |
|----|--|--------|--|
| 13 | Submit analytical quality assurance plan. Implement upon approval. | 1/6/86 | Plan submitted on time. Approved by EPA 2/21/86. |
| 12 | Submit evaluation of placement and design of effluent sampling system and plan to install most effective system for collecting a representative sample. Implement upon approval. | 2/6/86 | Plan submitted and implemented by Alyeska. |
| 11 | Install composite effluent sampler and commence operation. | 2/6/86 | Installed 11/27/85. In operation 2/1/86. |
| 8 | Submit operating plan for transferring only clarified wastewater from 80 to 90 tanks. Implement upon approval. | 3/6/86 | Plan submitted on time. Under EPA/ADEC review. |
| 2 | Submit study of settling characteristics of 90 tanks; determine settling time required for wastewater separation. | 3/6/86 | Plan submitted on time. Under EPA/ADEC review. |
| 3 | Submit plan to ensure only clarified wastewater is moved from 90 tanks to DAF unit. Implement upon approval. | 3/6/86 | Plan submitted on time. Under EPA/ADEC review. |
| 4 | Submit plan for routine removal of sludge from bottoms of 90 and 80 tanks. Implement upon approval. | 5/6/86 | |
| 9 | Submit plan for treatment and/or disposal of system-generated sludge. Implement upon approval. | 5/6/86 | |

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
Region 10
1200 Sixth Avenue
Seattle, Washington 98101

IN THE MATTER OF:

Alyeska Pipeline Service Company
1935 South Bragaw Street
Anchorage, Alaska 99512

NPDES Permit No. AK-002324-8

No. 1085-07-35-309A

COMPLIANCE ORDER

Pursuant to Section 309 of the Clean Water Act, 33 USC §1319, and the authority vested in the Administrator of the U.S. Environmental Protection Agency (EPA) which has been delegated to the EPA Regional Administrator, Region 10, the following FINDINGS OF FACT are made and COMPLIANCE ORDER issued.

FINDINGS OF FACT

1. Alyeska Pipeline Service Company (respondent) operates a ballast water treatment facility located near Valdez, Alaska. That facility discharges treated ballast water to Port Valdez.

1 2. Port Valdez is navigable waters of the United States as defined by
2 Section 502(7) of the Act, 33 USC §1362(7), and 40 CFR §122.2.

3 3. Respondent was issued a National Pollutant Discharge Elimination
4 System (NPDES) permit (the permit) with an effective date of September 10,
5 1980, and an expiration date of June 1, 1983, authorizing the discharge of
6 identified pollutants. Respondent submitted an application for reissuance of
7 its permit on August 20, 1982. Hence, the provisions of the permit remain in
8 effect under 40 CFR §122.6.

9 4. Part II.A.6. of the permit provides that "solids, sludges, filter
10 backwash, or other pollutants removed from or resulting from treatment or
11 control of wastewaters shall be disposed of in a manner to prevent any
12 pollutant from such materials from entering navigable waters, except as
13 limited in Part I.A."

14 5. Part II.A.6. of the permit means that once a pollutant (i.e., sludge,
15 solids, etc.) has been removed from the influent to, or wastewater within, the
16 Ballast Water Treatment Facility (BWT), that removed substance shall not be
17 reintroduced, reinjected, or returned in any way to the influent or wastewater
18 being treated by the BWT.

19 6. For the purposes of this ORDER and the permit, sludge is defined as
20 everything, regardless of its viscosity or solids content, that is above and
21 below the water phase except recoverable crude oil.

22 7. During the spring of 1983, approximately 500 gallons of sewage
23 treatment sludges were pumped into the oily water recovery system of
24 respondent's ballast water treatment plant, which is in violation of Part
25 II.A.6. of the permit.

1 8. On numerous occasions agents and employees of respondent removed
2 sludges from one part of the BWT (i.e. retention ponds) and reintroduced those
3 sludges into the wastewater (i.e. 90 tanks) being treated within the BWT, in
4 violation of Part II.A.6. of the permit.
5

6 ORDER
7

8 Based on the foregoing Findings of Fact, and pursuant to Section 309 of
9 the Clean Water Act, 33 USC 1319, it is hereby ORDERED as follows:

10 1. Immediately upon receipt of this ORDER, respondent shall cease and
11 desist the reintroduction of sludges back into the BWT. Recoverable crude oil
12 shall not be reintroduced into the BWT.

13 2. Within twenty (20) days after receipt of this ORDER, respondent shall
14 submit in writing, a plan describing the procedures that will be followed in
15 the removal and disposal of all sludges.

16 3. Submittals required by this ORDER shall be made to:

17
18 U.S. Environmental Protection Agency

19 1200 Sixth Avenue

20 Seattle, Washington 98101

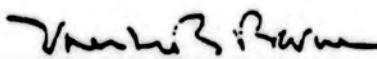
21 Attn: Mr. Don Dossett, M/S 513
22
23
24
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27

SANCTIONS

Notice is hereby given that violation of, or failure to comply with, any of the provisions of the foregoing ORDER shall subject respondent to civil penalties pursuant to Section 309(d) of the Act, 33 USC §1319(d).

Nothing in this ORDER shall be construed to relieve respondent of any obligations under any applicable federal, state, or local law.

Dated this 12th day of July, 1985.



Ernesta B. Barnes
Regional Administrator

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
Region 10
1200 Sixth Avenue
Seattle, Washington 98101

IN THE MATTER OF:

Alyeska Pipeline Service Company
1835 South Bragaw Street
Anchorage, Alaska 99512

NPDES Permit No. AK-002324-8

Amendment to Compliance Order

No. 1085-07-35-309A

Pursuant to Section 309 of the Clean Water Act (the Act), 33 USC §1319, and the authority thereunder of the Administrator of the U.S. Environmental Protection Agency (EPA), which authority has been duly delegated to the EPA Regional Administrator, Region 10, the following FINDINGS OF FACT are made and Amendment to above ORDER issued.

FINDINGS OF FACT

1. Pursuant to the Findings of Fact set out in ORDER No. 1085-07-35-309A issued to Alyeska Pipeline Service Company (respondent) this Amendment hereby supplements the provisions of said ORDER as follows:

ORDER

Based on the foregoing Findings of Fact (those more specifically set out in Order No. 1085-07-35-309A), and pursuant to Section 309 of the Clean Water Act, 33 USC §1319, it is hereby ORDERED as follows:

1. Consistent with the timeframes specified in provisions 2 through 10 of this amended ORDER (the ORDER), respondent shall cease and desist the reintroduction, resuspension, or re-entrainment of sludges into the ballast water treatment facility (BWT) or any part, stream, or segment thereof, or any stream flowing therefrom.

2. Within four (4) months of the date of the ORDER, respondent shall submit the results of a study which determines with reasonable accuracy the settling time required for effective separation of floating oil and suspended solids from wastewater in the 90 tanks. This study shall, at a minimum, include settling tests and chemical analyses of the effluent from the 90 tanks, and effectively profile the contents of the 90 tanks during typical settling periods. In addition, settling tests and chemical analyses shall be conducted on representative samples of the influent to the 90's tank.

3. Within four (4) months of the date of the ORDER, respondent shall submit an appropriate and comprehensive plan to ensure that only clarified wastewater is moved from the 90 tanks to the Dissolved Air Flotation (DAF) unit of the BWT. Upon approval by EPA, respondent shall immediately implement this plan.

4. Within six (6) months of the date of the ORDER, respondent shall submit an appropriate and comprehensive plan and schedule, based on the rate of sludge production, for regular and routine removal of sludge from the bottoms of the 90 tanks and the 80 tanks. Upon approval by EPA, respondent shall immediately commence sludge removal in accordance with the approved plan and schedule. Paragraphs 2, 3, and 4 can be addressed together in a single report.

1. 5. Within two (2) months of the date of the ORDER, respondent shall
2 submit the results of a study which effectively evaluates the flow velocity
3 configuration in the DAF cells and compares that flow velocity configuration
4 with design criteria for such cells. Where short circuiting or other
5 factors which may contribute to the inefficient operation of the cells are
6 identified, respondent shall submit with the study results, a plan for
7 correcting such operational problems. Upon approval by EPA, the corrective
8 action plan shall be implemented immediately.

9 6. Within four (4) months of the date of the ORDER, respondent shall
10 reinstall and operate the surface and bottom scrapers of the DAF unit as
11 originally designed. As an alternative, Alyeska may, within two (2) months,
12 submit a plan for the design, installation, and operation of an alternative
13 system which provides equivalent or better removal efficiencies of surface
14 and bottom sludges than the originally designed DAF system. Whichever
15 system is chosen shall effectively remove sludge from the DAF system. Upon
16 approval by EPA, the alternative corrective action plan shall be implemented
17 immediately.

18 7. Within two (2) months of the date of the ORDER, respondent shall
19 submit an appropriate and comprehensive plan for treatment and disposal of
20 the DAF and impound basin "float". Upon approval by EPA, respondent shall
21 immediately implement such plan. This plan may include a technical
22 evaluation of the feasibility of breaking the emulsion by introducing the
23 DAF and impound basin "float" into the oil layer of the 80 tanks.

24 8. Within four (4) months of the date of the ORDER, respondent shall
25 submit an operating procedure that ensures the transfer of only clarified
26 wastewater from the 80 tanks to the 90 tanks. Upon approval by EPA,
27 respondent shall immediately implement the procedure.

28 Amendment to Compliance ORDER - Page 3 Of 6

1 9. Within six (6) months of the date of the ORDER, respondent shall
2 submit the results of an engineering study which analyzes and selects an
3 appropriate and comprehensive plan for treatment and/or disposal of
4 system-generated sludge. Upon approval by EPA, respondent shall immediately
5 implement the plan.

6 10. Within two (2) weeks of the date of the ORDER, respondent shall
7 submit a plan describing all procedures to be followed to ensure that only
8 separated water and not sludge or oil/water emulsions are transferred to the
9 90 tanks from any of the crude oil storage tanks. Upon approval by EPA,
10 respondent shall immediately implement the plan.

11 11. Within the shortest reasonable time, such time not to exceed three
12 (3) months of the date of the ORDER, respondent shall install and operate a
13 continuous flow-weighted effluent sampler for collection and analysis of
14 composite samples for Total Suspended Solids (TSS) and Total Organic Carbon
15 (TOC). The equipment necessary to comply with this provision shall be
16 ordered within two (2) weeks of the date of the ORDER. The 24 hour
17 composite samples shall be analyzed daily. Results of these analyses shall
18 hereafter be submitted with the monthly discharge monitoring reports.

19 12. Within the shortest reasonable period of time, such time not to
20 exceed three (3) months of the date of the ORDER, respondent shall submit an
21 appropriate and comprehensive evaluation of the placement and design of the
22 present effluent sampling system, an evaluation of alternative methods of
23 collecting a representative effluent sample, identification of the most
24 effective effluent sampling system, the basis of that choice, and a plan for
25 installing such system. Upon approval by EPA, respondent shall immediately
26 implement the plan to install and continuously operate the alternative
27 effluent sampling system.
28

1 13. Within two (2) months of the date of the ORDER, respondent shall
2 submit a final quality assurance plan for all analytical methods to be
3 employed by respondent or its agents or employees in sampling and analyzing
4 waste streams or effluent from the BWT or any part thereof. Upon approval
5 by EPA, respondent shall immediately implement the plan.

6 14. Copies of all study plans to collect information pursuant to this
7 ORDER shall be submitted to EPA and ADEC as developed.

8 15. Should the various plans required in paragraphs 2 through 14 above
9 not meet with the approval of EPA, the ORDER may be further amended to
10 direct respondent to conduct specific actions by specific dates.

11 16. For the purposes of this document, the term "90 tank(s)" means
12 tanks 92, 93, and 94. The term "80 tank(s)" means tanks 80 and 81. The
13 term "float" means sludge that has separated from the waste stream by rising
14 to the surface layers of the DAF unit or impound basins. The term "plan"
15 includes, but is not limited to, design plans, modifications, proposed
16 construction schedules, construction, and operation of new or existing
17 equipment. The term "sludge" is defined in the original ORDER.

18 17. All of the requirements set out above that result in changes to the
19 current BWT shall be continuously operated and maintained until the issuance
20 of a new NPDES permit for the facility.

21 18. Submittals required by this Order shall be sent to:

22
23 U.S. Environmental Protection Agency
24 1200 Sixth Avenue
25 Seattle, Washington 98101
26 Attn: Water Compliance Section, M/S 513

27 and

28 Alaska Department of Environmental Conservation
437 E Street
Anchorage, Alaska 99501
Attn: Bob Martin

1 Nothing in this Order shall relieve respondent from fully complying with
2 all other requirements of NPDES permit No. AK-002324-8 and any applicable
3 federal, state, or local law.
4

5 SANCTIONS

6 Notice is hereby given that violation of, or failure to comply with, any
7 of the provisions of the foregoing ORDER may subject respondent to civil
8 penalties pursuant to Section 309(d) of the Act, 33 USC §1319(d).
9

10 DATED this 6th day of NOVEMBER, 1985.
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14 Ernesta B. Barnes
15 ERNESTA B. BARNES
16 Regional Administrator
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Alyeska's oil spill controls in question

Agency reviews response plan

By PATTI EPLER

Daily News business reporter

The company that runs the busy oil shipping terminal in Valdez may lack adequate equipment and trained personnel to contain anything effectively except the smallest oil spill, according to some state environmental officials and people who have worked for the company.

The state Department of Environmental Conservation is reviewing an oil spill contingency plan filed by Alyeska Pipeline Service Co., which operates the terminal and trans-Alaska pipeline for the eight oil companies that own the facilities. The plan expired Jan. 3 and must be re-certified by the state.

DEC is to meet with Alyeska this week to go over problems. Alyeska has told the state that some problems recently have been rectified, according to two DEC officials.

Concerns expressed by DEC field officers and others familiar with the company's clean-up plan include:

- Equipment is outdated, ill-suited for Prince William Sound and faulty because it has been allowed to deteriorate over the last several years.

- A lack of trained workers to run clean-up equipment. The company once had crews assigned solely to oil spill clean-up and equipment maintenance, but the crews were eliminated when Alyeska cutback on staff. Clean-up duties have been spread among other employees who have little training and other jobs to do.

- Inadequate inspection of oil tankers by state officials due to lack of money and manpower in the DEC Valdez office. By 1984, DEC's presence at Alyeska had dwindled to the point that one field officer was prompted to write in a memo to his supervisors in Anchorage, "We can no longer ignore the routine monitoring of Alyeska unless we do not care if a major catastrophic event occurs."

- A greater risk of oil spills because of an increased iceberg flow from the Columbia Glacier. More tankers also must anchor outside the terminal and wait for a spot at a berth to take on oil cargo, delaying response time if a spill occurs.

The Alyeska oil terminal is the largest facility of its kind in the nation and one of the largest in the world.

Each day the terminal loads aboard tankers about 1.7 million barrels of crude oil — nearly one-fifth of the nation's production.

Since the terminal started operations in 1977, there have been anywhere from a dozen to several dozen oil spills, depending on which agency is counting. All of the



Two tow floating booms through an oil slick in waters outside Alaska. So far, there have been no major spills at the Port of Valdez.

“We can no longer ignore the routine monitoring of Alyeska unless we do not care if a major catastrophic event occurs.”

— DEC field report

spills have been considered small.

But a few near disasters in the last eight years have sharpened the state's interest in ensuring that every possible oil spill can be handled.

DEC has been meeting with Alyeska to discuss problems that have become apparent to the state during mock spill drills, visits to the terminal and information supplied by employees. Alyeska also has raised issues of its own, said Paul O'Brien, DEC's oil spill program manager.

The two main concerns center on equipment and personnel — what type of equipment does Alyeska have, does it work, is it accessible and can people operate it, he said.

“Can the plan be executed in the field? That's really the bottom line for all contingency plans, whether it be Alyeska's or an exploratory

rig in the Beaufort Sea,” O'Brien said. “You can have a great document sitting on the shelf, but can it be executed?”

Alyeska believes it can. “We consider that Alyeska's oil spill response plan is one of the best and most comprehensive of its kind, and, based on the record of successful responses under the plan, we feel its effectiveness has been demonstrated,” said John Ratterman, a spokesman for the pipeline company.

He said Alyeska trains people for oil spill response, and drills are held periodically to test and enhance the equipment and skills of workers.

Ratterman declined to be more specific about the number of people now assigned to oil spill response compared with the past, or about what type of training is given and how often. He also

declined to address specific concerns about equipment.

He said Alyeska will meet with DEC again this week to answer some of its questions. “We do not feel it is appropriate to comment in any greater detail about our oil spill capability or about the meetings with the state while the state's review of the plan is continuing,” he said.

The Coast Guard also thinks Alyeska has done a good job responding to spills at the terminal and in the port, said Coast Guard Lt. Cmdr. Robert Diaz of the marine safety office in Valdez.

He noted that the spills have been minor to date, and he said the company has the equipment and staff to respond at least initially to a larger spill. “It's hard to gauge without a large spill actually occurring,” Diaz said.

“Alyeska is not just thrown to the wolves” in the event of a large spill, he said. Other clean-up groups and equipment from Alaska and the Lower 48 would be called in to help, he said.

But Alyeska is expected to handle the smaller spills and provide a first response to larger spills, said DEC's O'Brien.

O'Brien said he's sure Alyeska can get to a spill with the equipment it has.

But the state wants assurance the equipment will work and the people will know how to use it in light of concerns raised by DEC's own staff and problems evident during mock drills, he said.

The most recent drill monitored by the state was in September. Theresa Svancara, of DEC's Valdez office, reported that some workers were unfamiliar with equipment and didn't know how to do their assigned tasks. A list of people to be called in case more help was needed was outdated and useless, she said.

Some equipment did not work properly and Alyeska

was unwilling to test some procedures fully, Svancara wrote in a report of the drill. For example, she said, a hose to pump some of the “spilled oil” was not deployed fully because an Alyeska supervisor “said it would be too much work to roll it up again.”

“This type of attitude is not conducive to testing equipment to learn if it will work in various spill situations,” Svancara said.

“This spill drill, along with the one attempted (in 1984), pointed out the inadequacies in Alyeska's equipment and response capability.”

See Page J-2, ALYESKA



An Alyeska crew maneuvers a containment boom into position during a training session near the terminal.

Alyeska meets with DEC this week on oil spill response plan

Continued from Page J-1

ties," she said.

Dan Lawn, DEC's supervisor in Valdez, added this comment to Svancara's report: "The performance by Alyeska during this spill was similar to other drills the department has observed in the past. Again, there appears to be little or no improvement."

A report of the 1984 drill, written by a federal Environmental Protection Agency official, said the drill showed that the type of equipment used by Alyeska may not be suitable for conditions in Port Valdez.

An oil containment "boom" — an inflatable barrier used to corral oil and keep it from spreading — sank because of a faulty design that allows strong currents to push it over, the EPA report said.

The EPA report also questioned the adequacy of training and said "it appears that Alyeska did not treat this exercise as a realistic spill event."

About 55 tankers call at Port Valdez each month, leaving with hundreds of millions of gallons of crude oil bound for refineries in the Lower 48.

The Coast Guard recently told Alaska Sen. Frank Murkowski's office that since 1977 there have been 19 spills totaling about 8,400 gallons of oil.

Alyeska said there have been 12 spills of oily ballast water or crude oil since 1980 that have been more than 40 gallons in size. The largest tanker incident was the ARCO Alaska in 1984 and amounted to about 2,230 gallons, Ratterman said.

DEC's Bayliss testified at the Washington hearing that from 1977-79 there were at least 47 spills, and one alone was 1,300 gallons. Bayliss noted that most of the tanker spills before 1980 were just a few gallons each.

But the threat of a major spill is real. Last month, a tanker loaded with Alaska crude oil on its way from Valdez to an Outside refinery apparently ran aground in Port Angeles, Wash. Nearly 200,000 gallons of oil spilled from a rupture in the vessel's tanks, killing nearly a thousand waterfowl and shorebirds and threatening sensi-

tive marine habitats. A slick of the thick oil stretched for miles and fouled beaches. Clean-up costs have been estimated at \$3 million.

DEC's O'Brien said there have been a couple of close calls in Prince William Sound.

In 1980, a tanker laden with 35 million gallons of crude oil lost all power as it was outbound from Valdez, according to testimony in 1981 by then-DEC field officer Randy Bayliss. He was testifying before a Washington state council reviewing a plan for marine terminal operations in Port Angeles.

The fully loaded tanker was adrift and out of control for 17 hours. When the tanker finally regained power, it had drifted 26 miles and was less than 30 minutes from breakup on a rocky shoal at the northern end of Prince William Sound, Bayliss said.

Tugs surrounded the tanker but could not get a line on it because of high waves and lack of equipment on the tanker, Bayliss testified.

That near-mishap resulted in a change in Alyeska's oil spill contingency plan, O'Brien said. When the plan was retested in 1983, it required tankers to have a "quick-connect" towing system so tugs can hook up to the giant vessels if propulsion systems fail, he said.

More recently, DEC staff members have become increasingly concerned that staff cutbacks and an apparent cost-cutting campaign by Alyeska could lead to serious problems in the company's ability to handle oil spills.

In May 1984, Lawn wrote a four-page memo to his supervisors in Anchorage detailing the situation.

"Over the past several months, there has taken place a general discombobulating of the Alyeska Valdez Marine Terminal operational plan," the memo said. "Not only have there been severe personnel cuts, but operational plans and routine maintenance have been reduced drastically."

Lawn pointed out that DEC has not been able to inspect the facility adequately because of lack of money and staff. "Unfortunately, this has been a signal to Alyeska that the state is no longer interested" in the pipeline

project, he said.

Specifically, Lawn reported that many newer tankers had entered the Valdez trade and had never been inspected. The number of tankers calling at Port Valdez also had increased, he said.

But with the increase in shipping came a decrease in the number of persons assigned to marine operations, he said. At one time, there was a minimum of 14 people per shift, with two assigned to each loading tanker. By 1984, the number had dropped to an average of 11 people per shift with one person per tanker, Lawn said.

Lawn also criticized the cutback in workers on oil spill clean-up crews. He said the crews used to number four people per shift and were assigned only to oil spill clean-up.

In 1984, the number of people trained in oil spill response had been cut to two or three per shift and they were assigned other duties besides clean-up, he said.

Lawn warned that equipment was becoming outdated and training programs reduced. "The reliability of certain equipment is questioned, especially in a major spill situation," he said.

Lawn also said chances for oil spills were increasing because of an increased iceberg flow from the Columbia Glacier. An industry study in 1983 said there was no way to predict when ice from Columbia Bay, near the entrance to Valdez Arm, would move into shipping lanes, and vessels have refused to move through the area when it's dark, he said.

Tankers waiting for berth space have been forced to anchor several miles from the terminal and wait up to 100 hours before being able to take on oil, he said, adding that crews would not be able to respond to a spill as quickly.

Dave Decker, a Laborers Local 341 member who headed an oil spill crew for several years, echoed Lawn's concerns. Several other former and current Alyeska workers agreed with Lawn and Decker's assessment of the situation at the terminal.

The former workers, who requested anonymity, all had been laid off or fired. The current employees did not want their names used for fear of losing their jobs.

Decker worked at the terminal from 1979 until September 1984. He said he worked first for the contractor that provided oil spill clean-up crews, then in 1982 he stayed on as a union laborer when Alyeska eliminated the designated clean-up crews. Union laborers continued to respond to oil spills while performing routine maintenance throughout the terminal, he said.

Decker said while his crews were at the terminal, they tried to keep oil spill equipment in good shape. "But Alyeska never kept up with the technology of equipment," he said. "They depleted rather than upgraded it."

James Woodie, former marine superintendent and port captain for Alyeska, also expressed concern over cutbacks that seemed to result in an inability to handle a sizeable oil spill. Woodie was a 25-year veteran of the Coast Guard when he went to work for Alyeska in 1983, and had been commanding officer of the Coast Guard's Valdez office where he was responsible for oil spill clean-up operations from the regulatory side.

He was fired from the pipeline company in 1984 for insubordination. He declined to talk about his experience there because he has filed a lawsuit against Alyeska over his termination.

But a letter Woodie wrote to Alyeska soon after his departure outlines his concerns over several aspects of terminal operations, including oil spill response capabilities.

"Due to reduction in manning, age of equipment, limited training opportunities and lack of experienced coordination personnel, serious doubt exists that Alyeska would be able to contain and clean up effectively a medium or large oil spill," Woodie wrote.

He said proposed training was approved in theory but personnel never were sent to training programs. Cost-cutting measures limited purchase of new equipment, he said.

Alaska Pipeline Firm Is Accused of Polluting Sea Water Since 1977

Alyeska Documents Support Claims of Lax Procedures At Water-Treating Plant

Company Insists It Complies

By ANDY PASZTOR and ROBERT E. TAYLOR
Staff Reporters of THE WALL STREET JOURNAL

First, federal inspector Dianne Soderlund noticed a layer of brownish scum on water ready to be discharged into Valdez harbor from the trans-Alaska oil pipeline's water-treatment plant. Later, when she spotted an oil slick at the same location, suspicion turned to alarm.

"It appears," she concluded, "there are significant operational problems at the facility." The plant is supposed to screen out oil and toxic pollutants from huge quantities of ballast water poured into the harbor by tankers as they queue up at the pipeline terminal to load crude oil at the feet of majestic, snow-shrouded peaks.

But evidence is piling up that the plant hasn't been doing its job effectively and that sludge containing toxic pollutants isn't properly removed from water that the plant discharges back into the harbor.

Larger Questions

The preliminary warning from Ms. Soderlund to the Environmental Protection Agency came 17 months ago. Since then, a flurry of federal and state investigations has shaken public confidence in the pipeline's management and forced it to make costly improvements. The revelations also raise larger questions: Can state and federal officials adequately monitor pollution from such large, complex facilities? And why did it take them so long to act in this case?

Investigators have uncovered a history of questionable plant actions since the 1977 opening of the pipeline's huge southern terminal in Valdez, Alaska, which currently supplies roughly 15% of total U.S. oil needs. And the scrutiny is far from over. Still under investigation are the reasons why some pollution-control devices designed for the plant were never installed and others were disconnected or modified without notification to the EPA.

State probers are looking into further allegations of such criminal violations as submission of fraudulent environmental test results and false testimony to government regulators about potential hazards. Internal company documents show that some pipeline officials years ago suspected that the plant posed potential environmental hazards, but federal and state regulators contend that management failed to take steps to resolve the deficiencies until it was ordered to do so in the past few months.

Improprieties Denied

Alyeska Pipeline Service Co., which operates the pipeline for eight major oil companies, says that it has complied with all anti-pollution laws and that all allegations of record-tampering, improper discharges and other improprieties are unfounded. It calls the pipeline terminal's ballast-water treatment plant "probably the best and most modern" facility of its kind in the industry, arguing that the criticism is fanned by misunderstanding of plant operations.

The focus of all this attention is a sprawling complex of giant tanks and miles of piping designed to remove and dispose of harmful pollutants contained in the roughly 13 million gallons of ballast water discharged by tankers daily. Empty tankers take on ballast water for added stability on the voyage to Valdez, then pump it out to take on crude oil destined for the lower 48 states.

An EPA administrative order issued last summer accuses Alyeska of violating the treatment plant's water-discharge permit by systematically recirculating potentially harmful sludge. A second compliance order was issued in conjunction with Alaska's Department of Environmental Conservation. Government officials contend that transfers of oily water and sludge from tank to tank within the plant allowed high levels of potentially harmful pollutants to build up in the system over the years and flow unnoticed to the bay.

'Serious Threat'

Ihor Lysyj, the main consultant hired by the EPA, recently reported to the agency that the plant's deficiencies allow "uncontrolled quantities" of toxic pollutants to enter the harbor. He also informally told the agency that such pollution presents an "imminent and serious threat to the environment."

Mr. Lysyj, one of the country's leading experts on ballast-water treatment, estimates that the plant currently spews 1,600 pounds of pollution into the harbor every day, including "extremely toxic and hazardous substances." Assuming that that rate has remained steady since the pipeline began operations more than eight years ago, he calculates, the plant may have released enough potentially hazardous sludge to cover completely about four football fields three feet deep.

The EPA's consultant compares Alyeska's sludge-handling procedures to "vacuuming your house, dumping all the collected dust back on the carpet and then starting the whole process over again." Federal and state regulators are conducting tests to determine how much of the sludge ends up in the rich fishing grounds of Prince William Sound and whether there has been any damage to marine life.

Although pipeline executives deny vio-

Please Turn to Page 13, Column 1

Unsafe Harbor: Pollution of Ocean By Alaska Pipeline Firm Is Charged

Continued From First Page

lating any laws, they clearly are on the defensive. Under pressure from state and EPA officials, Alyeska appears to be spending millions of dollars to revise operating procedures, install new pollution controls and upgrade laboratory equipment at the treatment plant. The company also has promised to take additional steps that may be necessary to comply with what are likely to be more-stringent requirements for a new federal permit for continued operations at Valdez.

But local fishermen and some environmental groups complain that the state and EPA officials still haven't gone far enough. "The regulators did a very poor job over the years by failing to devote the necessary attention and expertise to supervise plant operations," contends Robert Blake, the president of the Cordova District Fishermen United and one of Alyeska's sharpest critics.

Budget Pressures

Some state and federal enforcement officials concede that budget pressures, staff shortages and the press of other business contributed to the problem. Harold Geren, the regional chief of the EPA's water-pollution-control programs, recalls hearing concerns from his staff about the adequacy of the treatment plant as far back as 1981. But work on permits for pulp mills, offshore oil rigs and other facilities, Mr. Geren says, diverted attention from Alyeska. "We've been hard-pressed keeping permits issued promptly," he says.

The original design called for the plant to remove sludge from the system and burn it in a large incinerator. But Alyeska never constructed the incinerator and says it wasn't legally required to do so. A spokesman says the company decided it was unnecessary because the amount of sludge produced in the beginning was less than anticipated. Alyeska has said it segregated and stored only 450 cubic yards of the stuff since operations began in 1977. Also, under standard procedure, some is channeled into outgoing crude oil.

State and federal officials argue that much more sludge than that should have been removed. They say its recovery was impaired by operating and equipment changes, many of which Alyeska made without the notification that EPA officials say is required. For instance, the company substituted small, paddlewheel skimmers for the large, sweeping arms designed to skim oily scum off the surface of one set of tanks; and it stopped using equipment designed to scrape sludge off the bottom of the same tanks and to heat water to separate it from oil.

Effectiveness Unimpaired?

Alyeska has told federal investigators that such changes didn't reduce the plant's effectiveness. But pipeline officials refuse to answer questions from The Wall Street Journal or discuss specifics until their discussions with the EPA are completed. Company officials previously said many of

the changes were intended to reduce costly maintenance problems. The company says it has fully complied with its water permit by generally curbing the plant's releases of oil, grease and three other oil-related pollutants specifically limited by the permit.

Investigators counter that the plant must be operated as efficiently as possible to remove all pollutants—regardless of whether they are explicitly mentioned in the permit. "There isn't any question that the practices we found are unacceptable, and they are violations of federal permit requirements," asserts Jamie Sikorski, former head of the EPA's clean-water compliance office for the region.

William Lamoreaux, a state environmental official who helped draft the plant's original operating permit, agrees. He says that a sludge pit, originally intended for temporary storage of wastes awaiting incineration, had been converted so that waste material was routinely pumped directly back into the ballast-water treatment tanks. Such recirculation of sludges was "never approved or contemplated by anyone involved at the beginning," Mr. Lamoreaux asserts.

For its part, Alyeska told the EPA in 1982 that toxic pollutants not specifically limited by the permit were found "in concentrations so low as to pose no possibility of significant or deleterious effects" on the port.

Earlier Documents

Nevertheless, company concerns about the amount of sludge generated by the plant—and what to do with it—have surfaced in internal Alyeska documents written at least as far back as 1978. In that year, the terminal's then superintendent, F.C. Jones, wrote a letter to engineers at Exxon Corp., one of the eight owners of the pipeline, complaining that the treatment plant "does not provide any facility to remove solids" and asking for their help in solving the problem. The letter went on to say that while some of the materials "exit in the water effluent," the plant's "high recirculation rate of solids is currently interfering in" the system's overall operation.

State and federal investigators are examining the letter, which was obtained separately by The Wall Street Journal along with other Alyeska documents on the plant. Exxon officials say they don't know what their company did in response to the letter. Alyeska documents say that an Exxon official studied the plant, found that the sludge disposal would cost at least \$1.5 million annually and urged instead that more oily waste be diverted into crude oil destined for outgoing tankers.

In December 1978, an internal memo from plant operators estimated that "solids have accumulated at a rate of 1 to 2 tons per day (dry basis)," which, if accurate, would be far more than Alyeska has claimed to have separated and stored. State and federal regulators say that the company appears to be leaning toward building an incinerator at the treatment

plant to dispose of stored sludge.

State officials also are investigating the adequacy of the pipeline's contingency plans for an oil spill. The EPA and congressional investigators are looking into allegations that Alyeska improperly used the treatment plant to dispose of some chemical wastes that didn't come from ballast water. And the state's attorney general has collected documents relating to Alyeska's earlier statements about sludge-handling and to the question of whether some plant workers may have been improperly exposed to harmful chemicals over the years.

Broker's Role

Some of the documents that investigators are using were obtained by Charles Hamel, an independent oil-transportation broker from Alexandria, Va. He has spearheaded criticism of Alyeska's management after contending that he suffered losses on some oil shipped through the pipeline that allegedly contained excess water. His allegations indirectly led to questions about the pollution-control practices at the plant, alerted Alaskan newspapers about the plant's apparent problems and prompted the EPA and the state to step up their investigations.

Investigators also have testimony from several former Alyeska employees claiming that their bosses encouraged or told them to tamper with pollution tests, report incorrect data and engage in other improper activities at the plant.

In sworn testimony to the Alaska Public Utilities Commission, Erlene J. Blake, a former plant laboratory technician, last year alleged it was "standard operating procedure at times" to "alter" such records. She told utility regulators that she was instructed to provide false reports to the EPA when the volume of treated water flowing into the bay exceeded maximum federal limits.

James Woodle, a former marine superintendent at the terminal, told the utility commission that "problem areas were masked and records modified" to suggest normal conditions at the treatment plant. Mr. Woodle also testified that plant operators were under instruction to disregard required safeguards if necessary in order to deal with unusually heavy incoming ballast flows. The operating principle, he said, was, "Just empty the tanks and make room."

Mr. Woodle is suing Alyeska, alleging that he was unfairly forced to leave the company before the investigations started. The company won't comment on the pending litigation.

Bill Ross, Alaska's top environmental official, several months ago confirmed that state officials, "working in concert with" the EPA, are conducting interviews and combing through Alyeska files to determine "whether any criminal violations may have occurred."

Many questions about the "sludge problem" at Valdez remain unanswered. But even the preliminary conclusions reached so far worry many scientists. David Shaw, a professor at the University of Alaska's Institute of Marine Sciences, who has studied Valdez harbor for Alyeska since the late 1970s, says of the increasing pollution on the sea bottom there: "I'm concerned it could be the tip of a serious problem."

Alyeska files show sludge problem

By PATTI EPLER

Daily News business reporter

Alyeska Pipeline Service Co.'s wastewater treatment plant in Valdez was producing so much toxic sludge two years after it started up that plant operators asked for Outside help to deal with the problem, according to documents from Alyeska's files.

The documents appear to directly contradict more recent statements by

the company that the plant has generated little sludge in more than eight years of operation.

The documents also indicate that at least two of the oil companies that own Alyeska advised it years ago that the plant wasn't working as well as

anticipated and suggested ways to improve it. British Petroleum said in 1979 it was unlikely the plant could comply with new environmental permits.

But Alyeska apparently rejected those opinions and listened instead to experts who told them the plant was operating well, the documents indicate. The experts included a chemist with The Standard Oil Co. — the

largest owner of the Alyeska facilities — and an environmental engineer for Alyeska.

The documents include reviews of the plant by oil company accountants, letters to and from Alyeska officials, minutes of high-level meetings and internal company memos. They tell a much different story — at least about

See Back Page, ALYESKA

ALYESKA: Files show sludge problem

Continued from Page A-1

the plant's first few years of operation — than Alyeska officials have told the public and government agencies for the past year.

Most of the documents were obtained by Charles Hamel, a former Virginia oil shipper who has waged a private war against Alyeska for the past five years. Hamel blames the pipeline company and its owners for the loss of his lucrative oil shipping business. He recently gave numerous documents to the government agencies investigating Alyeska and to the news media.

Alyeska officials are unwilling to answer questions about the documents, explain apparent discrepancies in recent public comments, or discuss operation of the plant.

"We continue to maintain that it would be inappropriate for us to pre-empt the investigations of the Environmental Protection Agency and the Alaska Department of Environmental Conservation by responding to inquiries from the news media," said John Ratterman, spokesman for Alyeska. He said the company has responded fully to questions from the agencies.

Frank Turpin, who was president of Alyeska from 1978 until last year when he became head of the state-owned Alaska Railroad, could not be reached for comment on Friday. Most of the documents pertain to the years in which Turpin headed Alyeska.

Alyeska operates the Valdez terminal and trans-Alaska pipeline for the eight oil companies that own the facilities. The owners are Standard Oil, British Petroleum, Atlantic Richfield, Exxon, Mobil, Union, Phillips and Amerasia Hess.

The environmental agencies are investigating allegations that Alyeska has discharged large amounts of toxic waste — called sludge — into Port Valdez. The sludge contains concentrated poisons such as hydrocarbons that in sufficiently large quantities could damage the marine environment. For that reason, the amount of sludge produced by Alyeska — and its disposal — is a crucial question for the agencies.

The EPA and DEC have said they are convinced that the plant has produced much more sludge than Alyeska acknowledges. They are awaiting the results of tests to help them determine whether excessive, and illegal, amounts of sludge have been discharged into the bay.

Alyeska contracted to have the University of Alaska Fairbanks conduct those tests.

Last July, EPA concluded that the way Alyeska ran the plant violated some conditions of its environmental permits. In November, it ordered Alyeska to make improvements in the treatment system that are likely to cost millions of dollars.

The primary purpose of the treatment plant is to clean the oil from about 13 million gallons of water brought to Valdez each day as ballast on oil tankers. The water stabilizes the ships on voyages from the Lower 48. Residual oil in the

tankers mixes with the ballast water and must be removed before the water can be pumped back into the sea.

Sludge is a byproduct of treating ballast water. The treatment separates the oily water into three basic elements: crude oil, clarified water and sludge or waste.

Last year, Hamel, the former oil shipper, publicly accused Alyeska of piping sludge into the waters of Prince William Sound. In denying the allegation, Alyeska said that in eight years the plant had produced only 600 cubic yards, roughly 344 tons, of sludge. Almost all the sludge has been stored at the plant while Alyeska figures out how to dispose of it, company officials said.

"They acknowledged that original plans for the plant called for construction of a huge incinerator to burn sludge, but it was never built," they said, because the plant never produced as much sludge as the engineers had predicted.

But a 1979 report by Exxon Research and Engineering Co., a separate review of the plant by British Petroleum and internal Alyeska memos say the plant was producing sludge and solid wastes in large enough quantities to hinder the treatment of ballast water.

In its first years of operation, the treatment process used a substance called alum to capture oily particles and separate them from the ballast water. The company soon realized that the powdery alum contributed to the large volume of solids. It switched to a liquid chemical that served the same purpose. But specialists from Exxon and British Petroleum believed the plant was continuing to produce large amounts of sludge.

On Sept. 20, 1978, F.C. Jones, at the time Alyeska's terminal superintendent, wrote to Exxon Research asking for help with the sludge problem.

"The present ballast water treatment plant design does not provide any facility to remove solids," Jones wrote. He said "a high recirculation rate of solids is currently interfering" with the water treatment and oil recovery processes.

A memo from Jones three months later said the solids appeared to accumulate at the rate of a ton or two a day.

In February 1979, G.W. Grove of Exxon Research wrote Alyeska with the results of his review of plant operations. He offered several suggestions for getting rid of the sludge, including incineration.

Grove calculated that the plant would generate at least 450 barrels of sludge, about 70 tons, each day "whether alum is used or not." Grove's estimate of sludge production is 500 times greater than Alyeska says was actually the case.

The cost of disposing of the sludge in 1979 was at least \$2 million a year, Grove wrote. Incineration in Valdez could cost more than \$5 million a year, perhaps less if water were removed before the sludge was burned, he said.

Ratterman, the Alyeska spokesman, refuses to discuss the incinerator or why it

wasn't built. But minutes from a September 1978 Alyeska meeting show that the company was concerned about the costs of sludge disposal.

Grove suggested that the best sludge disposal method might be to inject it into the recovered crude oil bound for Outside refineries. He also examined the idea of barging sludge to the Lower 48.

In December 1979, British Petroleum engineers wrote another report on the treatment plant for Alyeska, and suggested a study of solids and sludge "problems" with a goal of eliminating "the recent build-up of solids."

Moreover, BP was critical of the fact that Alyeska didn't let incoming ballast water sit long enough to allow crude oil to float to the top and sludge to sink to the bottom of its holding tanks.

At the time, BP was operating a similar facility in Scotland.

T. Pryor, a BP scientist, wrote that "it is thought unlikely that the existing effluent treatment facilities will be able to produce results compatible with the proposed new effluent limit..." The effluent limit was a condition of a new permit Alyeska was about to receive from the EPA in 1980. Pryor recommended that Alyeska look for better treatment methods.

Alyeska officials won't say why the BP and Exxon recommendations weren't followed.

In fact, in January 1980, about a month after BP submitted its review, an Alyeska official dismissed most of BP's concerns.

In 1980, Dick Mikkelsen, now Alyeska's chief environmental specialist, said he had been told by other Alyeska officials that the problem with sludge build-up had stabilized since use of alum had stopped.

"Before Alyeska commits to an expensive solids handling or (sic) removal system, I would suggest that we carefully study the extent of the problem," Mikkelsen wrote in a memo to one of his superiors.

BP's belief that the treatment plant would not be able to meet new federal permit requirements was unfounded, Mikkelsen said. He cited test results he said showed that the effluent was well within limits set out in the permit.

Still, two months later Mikkelsen was looking for ways to dispose of a lot of watery sludge.

A March 1980 memo from Mikkelsen recounts his conversations with a Kamai Peninsula company about disposing of 20,000 to 25,000 barrels, about 6,500 tons, of "sludge and oil/water emulsion" that had settled to the bottom of the tanks holding recovered crude oil. That's about 10 times more sludge — after 2½ years of operation — than Alyeska says has been generated since 1977.

In the summer of 1980, Alyeska again had the treatment plant evaluated, this time by The Standard Oil Co. The study found that the plant was complying with its permit "99.9 percent" of the time.

The report does not address the question of sludge accumulation or disposal.

Anchorage Daily News

Sunday, March 9, 1986

a-12

Pipeline owners quiet

By PATTI EPLER

Daily News business reporter

As much as possible, the eight oil companies that own Alyeska Pipeline Service Co. and its facilities have tried to keep Alyeska and its problems at a distance.

Officials with the owner companies — usually helpful and willing to talk about other issues like taxes and local hire — are steadfastly closed-mouthed about their Valdez oil shipping terminal and allegations that it is polluting Valdez bay.

Alyeska officials are the only people who can talk about Alyeska operations, said Perry Smith, a spokesman for Exxon Pipeline Co. "That's what Alyeska is for."

Exxon Pipeline Co. owns 20.3 percent of Alyeska.

"Our position remains that Alyeska is the operator for the plant," said Al Greenstein, an Atlantic Richfield

Co. spokesman in Los Angeles.

An Arco official — Hi Bond — chairs the "owners' committee" that closely oversees Alyeska. Arco Pipeline Co. owns 21.25 percent.

Greenstein reiterated Alyeska's position that it won't comment on the treatment plant while government agencies are investigating.

"We have full confidence in Alyeska," Greenstein said.

Chuck Webster, a spokesman for The Standard Oil Co. in Cleveland, also declined to discuss Alyeska. Standard Oil owns the single largest share of Alyeska, with 33.34 percent.

BP Pipelines Inc. owns 16.26 percent of Alyeska. British Petroleum also owns 55 percent of Standard Oil, but BP officials say that doesn't mean BP has any more control over Alyeska.

Officials at the company's

New York headquarters also refused to talk about Alyeska.

Ed Hoffman, a Mobil Oil Corp. official and member of the Alyeska owners' committee, also declined to elaborate on the committee's feelings about the allegations of pollution. He said the committee meets periodically and occasionally inspects the facility in Valdez.

"We have a lot of faith in Alyeska," Hoffman said.

He said Mobil is a minor owner of the pipeline company and doesn't have the involvement the larger owners do. Mobil Alaska Pipeline Co. owns 4.17 percent of Alyeska.

"I can tell you this," he said. "I'm not aware of any sludge problem."

Other owners include Union Alaska Pipeline Co., 1.34 percent; Phillips Alaska Pipeline Corp., 1.39 percent; and Amerasia Hess Pipeline Corp., 1.5 percent.

Journal article relates Alyeska's pollution ills

Pollution problems at Alyeska Pipeline Service Company's Valdez tanker terminal made national news today in a lengthy front-page article in the Wall Street Journal.

The article, headlined "Unsafe Harbor—Alaska Pipeline Firm Is Accused of Polluting Sea Water since 1977," contains relatively little that is new to Alaska readers. Instead, it summarizes the lengthy list of charges, countercharges, investigations, findings and denials that has been growing since Alaska newspapers began reporting on the situation at Valdez a year ago.

Problems at Valdez were brought to the attention of the Environmental Protection Agency 17 months ago, the Journal reported, after federal inspector Dianne Soderlund noticed a layer of brownish scum on water about to be pumped into the ocean from Alyeska's ballast water treatment system. Later, she noticed an oil slick at the same location.

The ballast water treatment system is intended to clean oily wastes out of the seawater that tankers carry to stabilize themselves as they head north to pick up crude oil at the Valdez terminal.

There is evidence that the treatment system isn't working right and that toxic sludge isn't properly removed from the water the plant sends into Valdez harbor, according to the Journal.

Alyeska did not respond to the News-Miner's request this morning for a comment on the article, but the article says Alyeska has denied any wrongdoing or improper discharges at the plant.

Ihor Lysyj, a ballast water expert hired as a consultant by the EPA, estimated the plant spews 1,600 pounds of pollution into the water every day, enough sludge to cover four football fields to a depth of three feet if the rate has been constant since operations began in 1977. Tests are under way to determine how much of the sludge has ended up in the rich fisheries of Prince William Sound and whether it has damaged marine life there.

Among the other revelations by the Wall Street Journal:

- Under investigation are the reasons why some pollution-control devices for the plant were never installed and why others were disconnected or modified without notice to the EPA;

- State officials are examining charges that fraudulent environmental test results were submitted and false testimony was given to government regulators about potential hazards;

- Internal Alyeska documents show that pipeline officials suspected years ago the plant might pose environmental hazards, but state and federal officials contend the company did nothing about it until it was ordered to do so a few months ago;

- Federal officials are studying whether Alyeska improperly used treatment system to dispose of chemical wastes that didn't come from ballast water;

- Alaska's attorney general is collecting documents about whether plant workers may have been exposed to harmful chemicals.

Anchorage Daily News



RECORDS CERTIFICATION



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Signature of Camera Operator


Date

SCOMM

#46:12

IN THE HOUSE -- Offered: 1/13/86
Referred: House Special Committee
on Oil and Gas and
Resources

IN THE SENATE - Offered: 1/13/86
Referred: Resources

EXECUTIVE ORDER NO. 61

Under the authority of art. III, sec. 23, of the Alaska Constitution,
and in accordance with AS 24.08.210, I order the following:

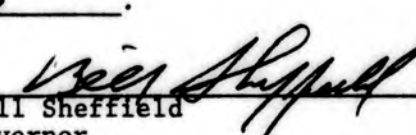
* Section 1. FINDINGS. As governor, I find that it would be in the
best interests of efficient administration to transfer the Alaska Royalty
Oil and Gas Development Advisory Board from the Department of Commerce and
Economic Development to the Department of Natural Resources.

* Sec. 2. AS 38.06.020 is amended to read:

Sec. 38.06.020. ESTABLISHMENT. There is established in the
Department of Natural Resources [COMMERCE AND ECONOMIC DEVELOPMENT]
the Alaska Royalty Oil and Gas Development Advisory Board.

* Sec. 3. This Order takes effect March 15, 1986.

DATED: Jan 10, 1986


Bill Sheffield
Governor

BILL SHEFFIELD
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

January 13, 1986

The Honorable Ben Grussendorf
Speaker of the House
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Dear Representative Grussendorf:

Under the authority of art. III, sec. 23, of the Alaska Constitution, and in accordance with AS 24.08.210, I am transmitting an executive order relating to the Alaska Royalty Oil and Gas Development Advisory Board. This order transfers the board from the Department of Commerce and Economic Development to the Department of Natural Resources.

In 1974, in response to the concern that the sale of royalty oil and gas should be made with substantial public involvement, the board was established within the Department of Natural Resources as the mechanism for providing that public review. At that time, the board was given significant controls over the discretion of the commissioner of natural resources to dispose of the state's royalty oil and gas, including the power to veto proposed contracts.

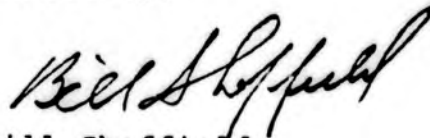
In 1980, the royalty statutes were amended. Partly because of friction between the board and the commissioner of natural resources, the board was transferred to the Department of Commerce and Economic Development, and its powers were substantially reduced. Its primary role since the 1980 amendments has been to hold public hearings on, evaluate, and advise the commissioner of natural resources and the legislature regarding proposed dispositions of the state's royalty.

In 1984, in response to the need for fiscal belt tightening, funding for the board was eliminated from the FY 85 budget of the Department of Commerce and Economic Development.

Without funding, the board could no longer retain its full-time staff -- an executive director and secretary. In their absence, the Department of Natural Resources has provided the necessary money and staff support to enable the board to fulfill its statutory review functions. Because of this close working relationship between the board and the Department of Natural Resources, and because the board's primary responsibilities are most closely related to the functions of that department in disposing of the state's royalty, I am convinced that it would be in the best interests of efficient administration to transfer the board back to the Department of Natural Resources.

The transfer has the support of the commissioners of natural resources and commerce and economic development, and the royalty board's other members. In addition, transfer of the board from the Department of Commerce and Economic Development to the Department of Natural Resources was included in HB 366, introduced in the 1985 session by the House Special Committee on Oil and Gas.

Sincerely,

A handwritten signature in cursive script, reading "Bill Sheffield".

Bill Sheffield
Governor

Sec. 24.08.110. Bills carry over. A bill introduced but not receiving final action in the first regular session of a legislature carries over in the same reading or status into the second regular session of the same legislature. (§ 40 ch 157 SLA 1959)

Revisor's notes. — Formerly AS
24.30.120. Renumbered in 1985.

Article 2. Constitutional Amendments and Executive Orders.

Section

200. Constitutional amendments
210. Executive orders

Sec. 24.08.200. Constitutional amendments. The legislature may propose amendments to the state constitution through the adoption of a joint resolution by an affirmative vote of two-thirds of the membership of each house. Resolutions proposing constitutional amendments shall be treated as bills. (§ 41 ch 157 SLA 1959)

Revisor's notes. — Formerly AS
24.30.130(a). Renumbered in 1985.

Sec. 24.08.210. Executive orders. An executive order proposing a change in the executive branch and requiring the force of law under art. III, sec. 23, Constitution of the State of Alaska shall be submitted to the presiding officer of each house on the day the house organizes. The legislature has 60 days of a regular session, or a full session if of shorter duration to disapprove the order. Unless disapproved by a special concurrent resolution introduced in either house, concurred in by a majority of the members in joint session, the order becomes effective at a date thereafter to be designated by the governor. An order submitted to but not disapproved by the legislature shall be published in the bound session laws and any codification of state law. (§ 12 ch 47 SLA 1961)

Revisor's notes. — Formerly AS
24.30.130(b). Renumbered in 1985.

Article 3. Filing, Printing and Distribution of Laws.

Section

300. Delivery by governor
310. Filing and effect

Collateral references. — 73 Am. Jur.
2d, Statutes, §§ 84-86.
82 C.J.S., Statutes, §§ 60-63.

Sec. 24.08.300. Delivery by governor. The governor shall sign and deliver to the presiding officer of each house a bill or resolution passed by both houses, and when the governor's office is to deliver the original enrolled copies of a resolution to the executive director of the Department of Administration. The director shall sign for each bill or resolution and the bill or resolution shall be photographed for duplication in the office of the governor. (§ 7 ch 157 SLA 1973)

Revisor's notes. — Formerly AS
24.35.010(a). Renumbered in 1985.

Sec. 24.08.310. Filing and effect. The original enrolled copies of executive orders having the effect of laws shall be filed with the governor to the legislature and the documents shall be kept on file for reference. Executive orders having the force of laws shall be printed and distributed as a part of the Alaska Statutes. (§ 32 SLA 1971)

Revisor's notes. — Formerly AS
24.35.010(b). Renumbered in 1985.

Sec. 24.08.320. Session laws. The governor is responsible for arranging for the printing and distribution of the laws of each session. The governor shall have the slip law copies of the enrolled bills and resolutions printed in quantity for one complete set to be distributed to the publisher of the publication of supplements to the Alaska Statutes. The publisher of education is to receive such copies for official state distribution and the cost of distribution on the basis of product. (§ 157 SLA 1959; am § 7 ch 47 SLA 1973)

STATE OF ALASKA 1986 LEGISLATIVE SESSION

FISCAL NOTE

EO 61 #1

Revision Date : _____

REQUEST 377-016-8

FISCAL DETAIL

Bill/Resolution No. : Executive Order
 Title : Transfer Royalty Oil Board from
Dept. of Commerce to Dept. of
Natural Resources
 Sponsor : Governor
 Requestor : Governor
 Date of Request : 12-31-85

Agency Affected : Natural Resources
 BRU : Oil and Gas

Components : Petroleum Management

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	-0-	-0-	-0-	-0-	-0-	-0-

CAPITAL						
---------	--	--	--	--	--	--

REVENUE						
---------	--	--	--	--	--	--

FUNDING : (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS :

FULL-TIME	-0-					
PART-TIME	-0-					
TEMPORARY	-0-					

ANALYSIS : Attach a separate page if necessary

Minimal additional administrative expense will be absorbed in Department's FY 87 Operating Budget.

Prepared by : Rod Mourant
 Division : Management

Phone : 465-2424

Date : 12-31-85

Approved by Commissioner : *Shawn F. Lister*
 Agency : Natural Resources

Date : 12-31-85

Distribution (by Agency preparing fiscal note) :

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

STATE OF ALASKA 1986 LEGISLATIVE SESSION FISCAL NOTE

REQUEST EO 61 #2
 Bill/Resolution No.: 377-016-84
 Title: Transfer of oil and gas royalty board.
 Sponsor: _____
 Requestor: _____
 Date of Request: _____

Revision Date: _____

FISCAL DETAIL
 Agency Affected: Dept. Comm. & Econ. Devel.
 BRU: _____
 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	-0-	-0-	-0-	-0-	-0-	-0-
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING : (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS : None

FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS : Attach a separate page if necessary

Prepared by: Joan Brown
 Division: Administrative Services

Phone: 465-2503
 Date: 12/31/85

Approved by Commissioner: [Signature]
 Agency: Dept. of Commerce & Economic Development

Date: _____

Distribution (by Agency preparing fiscal note):

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



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Date

21:07:15 #

SCOM

BILL SHEFFIELD
GOVERNOR



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

January 23, 1985

The Honorable Ben Grussendorf
Speaker of the House
Alaska State Legislature
Pouch V
Juneau, AK 99811

Dear Representative Grussendorf:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill relating to allowable depreciation methods for oil and gas producers and pipelines.

Section 1 of the bill repeals a statutory provision that requires corporations engaged in oil or gas production or pipeline transportation to use a depreciation method allowed under sec. 167 of the Internal Revenue Code, as that section read on June 30, 1981. (26 U.S.C. sec. 167.) Repeal of this provision will allow these corporations to use the ACRS (accelerated cost recovery system) method of depreciation, which is the method now permitted by federal law and used by most taxpayers for federal purposes.

The current provision creates problems both for taxpayers and the Department of Revenue. Strict compliance by the oil and gas companies is virtually impossible, because the law requires separate accounting for a corporation's worldwide assets. Likewise, the law is difficult for the department to administer. First, the department does not now have resources or personnel available to audit a major petroleum company's worldwide depreciation expense. Secondly, because the state depreciation deduction does not conform to federal depreciation, the department is unable to rely on sources such as the Internal Revenue Service and independent accountants to verify accuracy of deductions reported.

While repeal will benefit both the department and the companies, revenues will not be affected. The existing law renders no additional revenues to the state, other than revenues indirectly generated as a result of the accelerated collection of revenues. Under the current law, there is no difference in the total depreciation expense ultimately taken, although there may be a difference in the period of

time over which an asset is depreciated. While this timing difference may result in increased revenues in earlier years, the acceleration is offset by a corresponding decrease in revenues in subsequent years.

Section 2 of the bill makes the change in current law applicable to tax years beginning after December 31, 1984.

Sincerely,

A handwritten signature in cursive script, reading "Bill Sheffield".

Bill Sheffield
Governor

STATE OF ALASKA 1985 LEGISLATIVE SESSION
FISCAL NOTE

Page 1 of 2

Revision Date 10/19/84

REQUEST

Bill/Resolution No: HB 101
Title: Allowable depreciation methods
for oil & gas producers and pipelines
Sponsor: Governor
Requestor: _____
Date of Request: _____

FISCAL DETAIL

Agency Affected: Department of Revenue
Program Category Affected: Collection and
Management
BRU, Program of Subprogram(s) Affected: _____

Audit Division

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 85	FY 86	FY 87	FY 88	FY 89	FY 90
OPERATING						
100 PERSONAL SERVICES	-	-0-	-0-	-0-	-0-	-0-
200 TRAVEL	-	-0-	-0-	-0-	-0-	-0-
300 CONTRACTUAL	-	-0-	-0-	-0-	-0-	-0-
400 SUPPLIES	-	-0-	-0-	-0-	-0-	-0-
500 EQUIPMENT	-	-0-	-0-	-0-	-0-	-0-
600 LANDS & STRUCTURES	-	-0-	-0-	-0-	-0-	-0-
700 GRANTS, CLAIMS	-	-0-	-0-	-0-	-0-	-0-
800 MISCELLANEOUS	-	-0-	-0-	-0-	-0-	-0-
TOTAL OPERATING	-	-0-	-0-	-0-	-0-	-0-
CAPITAL	-	-0-	-0-	-0-	-0-	-0-
REVENUE	-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND	-	-0-	-0-	-0-	-0-	-0-
FEDERAL FUNDS	-	-	-	-	-	-
OTHER	-	-	-	-	-	-
TOTAL	-	-0-	-0-	-0-	-0-	-0-

POSITIONS:

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

ANALYSIS: Attach a separate page for analysis.

Prepared By: Maureen O'Brien *Maureen O'Brien*
Division: Audit Division

Phone: 465-2320
Date: 10/19/84

Approved by Commissioner: _____
Agency: _____

Date: _____

Distribution (by Agency preparing fiscal note):

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

"Page 2 of 2

An Act relating to allowable depreciation methods for oil and gas producers and pipelines --

Analysis:

Currently corporations engaged in oil or gas production or pipeline transportation in Alaska are required to use a different depreciation method for Alaska income tax purposes than the method used for Federal income tax purposes. The effect of the current depreciation provision is to create a difference in the time the depreciation expense is taken on the federal return and the time the depreciation expense is taken on the Alaska return. There should be no difference in the total depreciation expense ultimately taken. For Alaska, this law is most advantageous when the timing difference results in a smaller depreciation deduction for Alaska purposes in the earlier years of an asset's useful life as the state's revenues are then accelerated. This acceleration, however, will be offset by a corresponding decrease in revenues in later years. In summary, the existing law renders no additional revenues to the state other than those indirectly generated as a result of the accelerated collection of revenues.

The proposed amendment to AS 43.20.072 would return corporations engaged in oil or gas production or pipeline transportation in Alaska to a federal basis for depreciation. It is impossible to determine the exact impact on the state's revenues as a result of this amendment. There may be a short-term decrease in revenues, however, over the long-term there should be no impact on the state's revenues.

SUMMARY/EXPLANATION OF INTENT

The essential effect of the current depreciation provision in the law is to create a difference between the time when the depreciation expense is taken on the federal return and the time depreciation expense is taken on the Alaska return. There is no difference in the total depreciation expense ultimately taken although there may be a difference in the period of time over which an asset is depreciated. For Alaska, this law is most advantageous when the timing difference results in a smaller depreciation deduction for Alaska purposes in the earlier years of an asset's useful life, as the state's revenues are then accelerated. This acceleration, however, will be offset by a corresponding decrease in revenues in later years. Among the returns filed for 1982, the first year the law was in effect, there were some cases where the depreciation deduction for Alaska purposes was greater than that taken for federal purposes, resulting in a deferral of revenues. After netting this adjustment for all the oil and gas companies in 1982, this law resulted in approximately \$5 million in accelerated revenues.

From the taxpayer's viewpoint, the benefits the state derives from this acceleration of revenues are not commensurate with the burdens of efforts and costs required of the taxpayers to comply specifically with the unique demands of Alaska's law. A special computer program and separate accounting for a corporation's worldwide assets would be necessary to meet the law's exact requirements. None of the oil and gas companies audited to date have fulfilled the letter of the law; instead all have substituted calculations prepared for other purposes that approximated the Alaska requirement. It has been necessary for the department to deal with the variations by regulation.

From the Audit Division's standpoint, practically speaking, the law is exceedingly difficult, if not impossible, to administer effectively and efficiently because of the difficulty in auditing the taxpayers' compliance with it. An audit of a major petroleum company's worldwide depreciation expense is far beyond the scope of the Division's audits. By divorcing Alaska's depreciation deduction from the federal depreciation, the law deprives the state of its ability to rely on third parties such as the IRS and independent CPA's to insure the accuracy of the depreciation deduction. This reliance on third party policing is especially desirable in the instance of depreciation since the Division itself does not comprehensively audit the deduction.

Further complicating the situation as it stands, is the fact that, absent some very involved and detailed recordkeeping by the taxpayers, for certain other items of income and expense affected by depreciation expense, such as the computation of gain or loss upon the disposition of an asset and the relevant Section 1245 and 1250 recapture, the amounts reported will not properly reflect the federal/state differences. It is highly unlikely that taxpayers will prepare the requisite records; hence, more erroneous reporting will result.

In summary, the existing law renders no additional revenues to the state other than those indirectly generated as a result of the accelerated collection of revenues. Furthermore, the existing law is not being faithfully complied with by the taxpayers and cannot satisfactorily be audited by the Audit Division. The effect of the amendment to the law would be to return taxpayers to a federal basis for depreciation. This change would promote conformity with the law and enhances its effective administration.

An Act relating to allowable depreciation methods for oil and gas producers and pipelines --

Analysis:

Currently corporations engaged in oil or gas production or pipeline transportation in Alaska are required to use a different depreciation method for Alaska income tax purposes than the method used for Federal income tax purposes. The effect of the current depreciation provision is to create a difference in the time the depreciation expense is taken on the federal return and the time the depreciation expense is taken on the Alaska return. There should be no difference in the total depreciation expense ultimately taken. For Alaska, this law is most advantageous when the timing difference results in a smaller depreciation deduction for Alaska purposes in the earlier years of an asset's useful life as the state's revenues are then accelerated. This acceleration, however, will be offset by a corresponding decrease in revenues in later years. In summary, the existing law renders no additional revenues to the state other than those indirectly generated as a result of the accelerated collection of revenues.

The proposed amendment to AS 43.20.072 would return corporations engaged in oil or gas production or pipeline transportation in Alaska to a federal basis for depreciation. ~~It is impossible to determine the exact impact on the state's revenues as a result of this amendment. There may be a short-term decrease in revenues, however, over the long-term there should be no impact on the state's revenues.~~

SUMMARY/EXPLANATION OF INTENT

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From the taxpayer's viewpoint, the benefits the state derives from this acceleration of revenues are not commensurate with the burdens of efforts and costs required of the taxpayers to comply specifically with the unique demands of Alaska's law. A special computer program and separate accounting for a corporation's worldwide assets would be necessary to meet the law's exact requirements. None of the oil and gas companies audited to date have fulfilled the letter of the law; instead all have substituted calculations prepared for other purposes that approximated the Alaska requirement. It has been necessary for the department to deal with the variations by regulation.

From the Audit Division's standpoint, practically speaking, the law is exceedingly difficult, if not impossible, to administer effectively and efficiently because of the difficulty in auditing the taxpayers' compliance with it. An audit of a major petroleum company's worldwide depreciation expense is far beyond the scope of the Division's audits. By divorcing Alaska's depreciation deduction from the federal depreciation, the law deprives the state of its ability to rely on third parties such as the IRS and independent CPA's to insure the accuracy of the depreciation deduction. This reliance on third party policing is especially desirable in the instance of depreciation since the Division itself does not comprehensively audit the deduction.

§ 167. Depreciation

(a) General rule.—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

- (1) of property used in the trade or business, or
- (2) of property held for the production of income.

(b) Use of certain methods and rates.—For taxable years ending after December 31, 1953, the term "reasonable allowance" as used in subsection (a) shall include (but shall not be limited to) an allowance computed in accordance with regulations prescribed by the Secretary, under any of the following methods:

- (1) the straight line method,
- (2) the declining balance method, using a rate not exceeding twice the rate which would have been used had the annual allowance been computed under the method described in paragraph (1),
- (3) the sum of the years-digits method, and

(4) any other consistent method productive of an annual allowance which, when added to all allowances for the period commencing with the taxpayer's use of the property and including the taxable year, does not, during the first two-thirds of the useful life of the property, exceed the total of such allowances which would have been used had such allowances been computed under the method described in paragraph (2).

Nothing in this subsection shall be construed to limit or reduce an allowance otherwise allowable under subsection (a).

(c) Limitations on use of certain methods and rates.—Paragraphs (2), (3) and (4) of subsection (b) shall apply only in the case of property (other than intangible property) described in subsection (a) with a useful life of 3 years or more—

- (1) the construction, reconstruction, or erection of which is completed after December 31, 1953, and then only to that portion of the basis which is properly attributable to such construction, reconstruction, or erection after December 31, 1953, or
- (2) acquired after December 31, 1953, if the original use of such property commences with the taxpayer and commences after such date.

(d) Agreement as to useful life on which depreciation rate is based.—Where, under regulations prescribed by the Secretary, the taxpayer and the Secretary have, after August 16, 1954, entered into an agreement in writing specifically dealing with the useful life and rate of depreciation of any property, the rate so agreed upon shall be binding on both the taxpayer and the Secretary in the absence of

facts or circumstances not taken into consideration in the adoption of such agreement. The responsibility of establishing the existence of such facts and circumstances shall rest with the party initiating the modification. Any change in the agreed rate and useful life specified in the agreement shall not be effective for taxable years before the taxable year in which notice in writing by certified mail or registered mail is served by the party to the agreement initiating such change.

(e) Change in method.—

(1) Change from declining balance method.—In the absence of an agreement under subsection (d) containing a provision to the contrary, a taxpayer may at any time elect in accordance with regulations prescribed by the Secretary to change from the method of depreciation described in subsection (b)(2) to the method described in subsection (b)(1).

(2) Change with respect to section 1245 property.—A taxpayer may, on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year beginning after December 31, 1962, and in such manner as the Secretary shall by regulations prescribe, elect to change his method of depreciation in respect of section 1245 property (as defined in section 1245(a)(3)) from any declining balance or sum of the years-digits method to the straight line method. An election may be made under this paragraph notwithstanding any provision to the contrary in an agreement under subsection (d).

(3) Change with respect to section 1250 property.—A taxpayer may, on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year beginning after December 31, 1975, and in such manner as the Secretary shall by regulation prescribe, elect to change his method of depreciation in respect of section 1250 property (as defined in section 1250(c)) from any declining balance or sum of the years-digits method to the straight line method. An election may be made under this paragraph notwithstanding any provision to the contrary in an agreement under subsection (d).

(f) Salvage value.—

(1) General rule.—Under regulations prescribed by the Secretary, a taxpayer may, for purposes of computing the allowance under subsection (a) with respect to personal property, reduce the amount taken into account as salvage value by an amount which does not exceed 10 percent of the basis of such property (as determined under subsection (g) as of the time as of which such salvage value is required to be determined).

(2) Personal property defined.—For purposes of this subsection, the term "personal property" means depreciable personal

property (other than livestock) more acquired after October 16,

(g) Basis for depreciation.—The basis for depreciation of property and tear, and obsolescence are to be determined. The adjusted basis of the property shall be the adjusted basis provided for the purpose of determining the gain on the sale of the property.

(h) Life tenants and beneficiaries.—In the case of property held by one person or other person, the deduction shall be determined as if the person were the absolute owner of the property. In the case of property held by a life tenant, the deduction shall be apportioned between the life tenant and the trustee in accordance with the instrument creating the trust, or, in the absence of such instrument, on the basis of the trust income allocable to the life tenant. If the rate, the allowable deduction shall be determined as if the estate allocable to each.

(i) Limitation in case of property held by a partnership.—The suspension period.—

(1) In general.—Under regulations prescribed by the Secretary, paragraphs (2), (3), and (4) shall apply in the case of real property (as defined in section 48(c)) which is placed in service during the suspension period, or reconstruction, or erection of a building during the suspension period, or placed during such period, in accordance with the regulations prescribed by the Secretary. Paragraphs (3), (4), and (5) shall be applied for purposes of this subsection. In applying this paragraph, the amount taken into account only the amount properly attributable to construction placed in service before May 24, 1967.

(2) Exception.—Paragraph (1) shall not apply to real property selected by the taxpayer for depreciation (when added to the cost of the property) selected by the taxpayer under section 179. Under regulations prescribed by the Secretary, similar to the rules provided by paragraph (1), shall be applied for purposes of this subsection.

(3) Suspension period.—For purposes of this subsection, the term "suspension period" means the period beginning on March 10, 1966, and ending on March 10, 1967.

property (other than livestock) with a useful life of 3 years or more acquired after October 16, 1962.

(g) **Basis for depreciation.**—The basis on which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 1011 for the purpose of determining the gain on the sale or other disposition of such property.

(h) **Life tenants and beneficiaries of trusts and estates.**—In the case of property held by one person for life with remainder to another person, the deduction shall be computed as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant. In the case of property held in trust, the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each. In the case of an estate, the allowable deduction shall be apportioned between the estate and the heirs, legatees, and devisees on the basis of the income of the estate allocable to each.

(i) **Limitation in case of property constructed or acquired during the suspension period.**—

(1) **In general.**—Under regulations prescribed by the Secretary, paragraphs (2), (3), and (4) of subsection (b) shall not apply in the case of real property which is not section 38 property (as defined in section 48(a)) if the physical construction, reconstruction, or erection of such property by any person begins during the suspension period, or begins, pursuant to an order placed during such period, before May 24, 1967. Under regulations prescribed by the Secretary, rules similar to the rules provided by paragraphs (3), (4), (7), (8), (9), and (10) of section 48(h) shall be applied for purposes of the preceding sentence. In applying this paragraph to any property, there shall be taken into account only that portion of the basis which is properly attributable to construction, reconstruction, or erection before May 24, 1967.

(2) **Exception.**—Paragraph (1) shall not apply to any item of real property selected by the taxpayer if the cost of such property (when added to the cost of all other items of real property selected by the taxpayer under this paragraph) does not exceed \$50,000. Under regulations prescribed by the Secretary, rules similar to the rules provided by paragraph (2) of section 48(c) shall be applied for purposes of this paragraph.

(3) **Suspension period.**—For purposes of this subsection, the term "suspension period" means the period beginning on October 10, 1966, and ending on March 9, 1967.

(j) Special rules for section 1250 property.—

(1) **General rule.**—Except as provided in paragraphs (2) and (3), in the case of section 1250 property, subsection (b) shall not apply and the term "reasonable allowance" as used in subsection (a) shall include an allowance computed in accordance with regulations prescribed by the Secretary, under any of the following methods:

(A) the straight line method,

(B) the declining balance method, using a rate not exceeding 150 percent of the rate which would have been used had the annual allowance been computed under the method described in subparagraph (A), or

(C) any other consistent method productive of an annual allowance which, when added to all allowances for the period commencing with the taxpayer's use of the property and including the taxable year, does not, during the first two-thirds of the useful life of the property, exceed the total of such allowances which would have been used had such allowances been computed under the method described in subparagraph (B).

Nothing in this paragraph shall be construed to limit or reduce an allowance otherwise allowable under subsection (a) except where allowable solely by reason of paragraph (2), (3), or (4) of subsection (b).

(2) Residential rental property.—

(A) **In general.**—Paragraph (1) of this subsection shall not apply, and subsection (b) shall apply in any taxable year, to a building or structure—

(i) which is residential rental property located within the United States or any of its possessions, or located within a foreign country if a method of depreciation for such property comparable to the method provided in subsection (b)(2) or (3) is provided by the laws of such country, and

(ii) the original use of which commences with the taxpayer.

In the case of residential rental property located within a foreign country, the original use of which commences with the taxpayer, if the allowance for depreciation provided under the laws of such country for such property is greater than that provided under paragraph (1) of this subsection, but less than that provided under subsection (b), the allowance for depreciation under subsection (b) shall be limited to the amount provided under the laws of such country.

(B) **Definition.**—For building or structure rental property for any more of the gross rental income from such building or structure for such year (within the meaning of the preceding sentence) shall be the rental income from such building or structure for such year less the rental value of the

(C) **Change in method.**—In the computation of the taxable year, permitting a change in a method of

(3) **Property constructed after 1960.**—Paragraph (1) of this subsection shall apply, in the case of

(A) the construction of which was begun before

(B) for which a written contract, entered into after July 25, 1969, with respect to reconstruction, or erection thereof, was on July 25, 1969, binding on the taxpayer

(4) **Used section 1250 property.**—Paragraph (5), in the case of July 24, 1969, the original use of the taxpayer, the allowance shall be limited to an amount

(A) the straight line

(B) any other method which results in a reasonable allowance including—

(i) any declining

(ii) the sum of

(iii) any other method of application

(1)(C) of this subsection

(5) **Used residential rental property.**—In the case of section 1250 property which is residential rental property in paragraph (2)(B)) and the useful life of 20 years or more shall not commence with the tax-

(B) **Definition.**—For purposes of subparagraph (A), a building or structure shall be considered to be residential rental property for any taxable year only if 80 percent or more of the gross rental income from such building or structure for such year is rental income from dwelling units (within the meaning of subsection (k)(3)(C)). For purposes of the preceding sentence, if any portion of such building or structure is occupied by the taxpayer, the gross rental income from such building or structure shall include the rental value of the portion so occupied.

(C) **Change in method of depreciation.**—Any change in the computation of the allowance for depreciation for any taxable year, permitted or required by reason of the application of subparagraph (A), shall not be considered a change in a method of accounting.

(4) **Property constructed, etc., before July 25, 1969.**—Paragraph (4) of this subsection shall not apply, and subsection (b) shall apply, in the case of property—

(A) the construction, reconstruction, or erection of which was begun before July 25, 1969, or

(B) for which a written contract entered into before July 25, 1969, with respect to any part of the construction, reconstruction, or erection or for the permanent financing thereof, was on July 25, 1969, and at all times thereafter, binding on the taxpayer.

(4) **Used section 1250 property.**—Except as provided in paragraph (5), in the case of section 1250 property acquired after July 24, 1969, the original use of which does not commence with the taxpayer, the allowance for depreciation under this section shall be limited to an amount computed under—

(A) the straight line method, or

(B) any other method determined by the Secretary to result in a reasonable allowance under subsection (a), not including—

(i) any declining balance method,

(ii) the sum of the years-digits method, or

(iii) any other method allowable solely by reason of the application of subsection (b)(4) or paragraph (1)(C) of this subsection.

(5) **Used residential rental property.**—In the case of section 1250 property which is residential rental property (as defined in paragraph (2)(B)) acquired after July 24, 1969, having a useful life of 20 years or more, the original use of which does not commence with the taxpayer, the allowance for depreciation

under this section shall be limited to an amount computed under—

(A) the straight line method,

(B) the declining balance method, using a rate not exceeding 125 percent of the rate which would have been used had the annual allowance been computed under the method described in subparagraph (A), or

(C) any other method determined by the Secretary to result in a reasonable allowance under subsection (a), not including—

(i) the sum of the years-digits method,

(ii) any declining balance method using a rate in excess of the rate permitted under subparagraph (B), or

(iii) any other method allowable solely by reason of the application of subsection (b)(4) or paragraph (1)(C) of this subsection.

(6) Special rules.—

(A) Under regulations prescribed by the Secretary, rules similar to the rules provided in paragraphs (5), (9), (10), and (13) of section 48(h) shall be applied for purposes of paragraphs (3), (4), and (5) of this subsection.

(B) For purposes of paragraphs (2), (4), and (5), if section 1250 property which is not property described in subsection (a) when its original use commences, becomes property described in subsection (a) after July 24, 1969, such property shall not be treated as property the original use of which commences with the taxpayer.

(C) Paragraphs (4) and (5) shall not apply in the case of section 1250 property acquired after July 24, 1969, pursuant to a written contract for the acquisition of such property or for the permanent financing thereof, which was, on July 24, 1969, and at all times thereafter, binding on the taxpayer.

(k) Depreciation of expenditures to rehabilitate low-income rental housing.—

(1) **60-month rule.**—The taxpayer may elect, in accordance with regulations prescribed by the Secretary, to compute the depreciation deduction provided by subsection (a) attributable to rehabilitation expenditures incurred with respect to low-income rental housing after July 24, 1969, and before January 1, 1979, under the straight line method using a useful life of 60 months and no salvage value. Such method shall be in lieu of any other method of computing the depreciation deduction under subsection (a), and in lieu of any deduction for amortization, for such expenditures.

(2) Limitations.—

(A) The aggregate amount paid or incurred by the taxpayer in any low-income rental unit in any low-income rental account under paragraph (1) for consecutive years, including the amount of such expenditures, shall not exceed \$20,000.

(B) Rehabilitation expenditures incurred by the taxpayer in any taxable year in any low-income rental unit in any low-income rental account under paragraph (1) for consecutive years, including the amount of such expenditures, shall not exceed \$20,000.

(3) Definitions.—For purposes of this subsection:

(A) **Rehabilitation expenditures** means any amount paid or incurred for improvements to property (or related to the property) for a term of 5 years or more, in connection with the rehabilitation of an existing building for such term does not include the cost of a new building or any interest therein.

(B) **Low-income rental housing** means any building or part thereof which are held for occupancy by low-income individuals or families as determined by the Secretary in a manner consistent with the Housing Program under the Housing Act of 1937 pursuant to this subsection.

(C) **Dwelling unit.**—The house or an apartment used for residential purposes in a building or structure in a hotel, motel, inn, or other establishment in which one-half of the units in which are used for residential purposes.

(D) **Rehabilitation expenditures** means any amount paid or incurred for expenditures incurred with respect to the rehabilitation of low-income rental housing after July 24, 1969, and before January 1, 1979, shall be deemed to be incurred.

(l) Reasonable allowance in case of:

(1) Pre-1970 public utility property.

(A) **In general.**—In the case of public utility property, the term "reasonable allowance" means an allowance determined by the Secretary under subsection (a) means an allowance determined by the Secretary.

(i) a subsection (l) n

(2) Limitations.—

(A) The aggregate amount of rehabilitation expenditures paid or incurred by the taxpayer with respect to any dwelling unit in any low-income rental housing which may be taken into account under paragraph (1) shall not exceed \$20,000.

(B) Rehabilitation expenditures paid or incurred by the taxpayer in any taxable year with respect to any dwelling unit in any low-income rental housing shall be taken into account under paragraph (1) only if over a period of two consecutive years, including the taxable year, the aggregate amount of such expenditures exceeds \$3,000.

(3) Definitions.—For purposes of this subsection—

(A) **Rehabilitation expenditures.**—The term “rehabilitation expenditures” means amounts chargeable to capital account and incurred for property or additions or improvements to property (or related facilities) with a useful life of 5 years or more, in connection with the rehabilitation of an existing building for low-income rental housing; but such term does not include the cost of acquisition of such building or any interest therein.

(B) **Low-income rental housing.**—The term “low-income rental housing” means any building the dwelling units in which are held for occupancy on a rental basis by families and individuals of low or moderate income, as determined by the Secretary in a manner consistent with the Leased Housing Program under section 8 of the United States Housing Act of 1937 pursuant to regulations prescribed under this subsection.

(C) **Dwelling unit.**—The term “dwelling unit” means a house or an apartment used to provide living accommodations in a building or structure, but does not include a unit in a hotel, motel, inn, or other establishment more than one-half of the units in which are used on a transient basis.

(D) **Rehabilitation expenditures incurred.**—Rehabilitation expenditures incurred pursuant to a binding contract entered into before January 1, 1979, and rehabilitation expenditures incurred with respect to low-income rental housing the rehabilitation of which has begun before January 1, 1979, shall be deemed incurred before January 1, 1979.

(4) Reasonable allowance in case of property of certain utilities.—

(1) Pre-1970 public utility property.—

(A) **In general.**—In the case of any pre-1970 public utility property, the term “reasonable allowance” as used in subsection (a) means an allowance computed under—

(i) a subsection (l) method, or

(ii) the applicable 1968 method for such property. Except as provided in subparagraph (B), clause (ii) shall apply only if the taxpayer uses a normalization method of accounting.

(B) Flow-through method of accounting in certain cases.—In the case of any pre-1970 public utility property, the taxpayer may use the applicable 1968 method for such property if—

(i) the taxpayer used a flow-through method of accounting for such property for its July 1969 accounting period, or

(ii) the first accounting period with respect to such property is after the July 1969 accounting period, and the taxpayer used a flow-through method of accounting for its July 1969 accounting period for the property on the basis of which the applicable 1968 method for the property in question is established.

(2) Post-1969 public utility property.—In the case of any post-1969 public utility property, the term "reasonable allowance" as used in subsection (a) means an allowance computed under—

(A) a subsection (1) method,

(B) a method otherwise allowable under this section if the taxpayer uses a normalization method of accounting, or

(C) the applicable 1968 method, if, with respect to its pre-1970 public utility property of the same (or similar) kind most recently placed in service, the taxpayer used a flow-through method of accounting for its July 1969 accounting period.

(3) Definitions.—For purposes of this subsection—

(A) Public utility property.—The term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of—

(i) electrical energy, water, or sewage disposal services,

(ii) gas or steam through a local distribution system,

(iii) telephone services, or other communication services if furnished or sold by the Communications Satellite Corporation for purposes authorized by the Communications Satellite Act of 1962 (47 U.S.C. 701), or

(iv) transportation of gas or steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political

subdivision thereof, by any agency of the United States, or by a public commission or other similar body or subdivision thereof.

(B) Pre-1970 public utility property.—The term "pre-1970 public utility property" means public utility property in the hands of the taxpayer at any time before January 1, 1970.

(C) Post-1969 public utility property.—The term "post-1969 public utility property" means public utility property which is not pre-1970 public utility property.

(D) Applicable 1968 method.—The term "applicable 1968 method" means, with respect to property—

(i) the method of depreciation applicable with respect to such property for the first accounting period for which a return was filed before January 1, 1970,

(ii) if clause (i) does not apply, the method used by the taxpayer on a return for the first accounting period for which a return was filed before January 1, 1970, with respect to its public utility property of the most similar kind (or if there is no property of the most similar kind) in the hands of the taxpayer, or

(iii) if neither clause (i) nor clause (ii) applies, the subsection (1) method.

In the case of any section 1250 property, if the subsection (j) applies, the term "applicable 1968 method" means the method permitted under such section, or if the method is not nearly comparable to the applicable 1968 method, the method determined under the preceding sentence.

(E) Applicable 1968 method if taxpayer evidenced the intent to use a method other than its applicable 1968 method.—If the taxpayer (other than its applicable 1968 method) with respect to any property placed in service before August 1, 1969, or in the hands of the taxpayer for purposes of reflecting regulated books of account for the first accounting period, such other method shall be the applicable 1968 method with respect to such property of the same (or similar) kind placed in service.

(F) Subsection (1) method.—The term "subsection (1) method" means any method determined under this section which results in a reasonable allowance

division thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

(B) **Pre-1970 public utility property.**—The term “pre-1970 public utility property” means property which was public utility property in the hands of any person at any time before January 1, 1970.

(C) **Post-1969 public utility property.**—The term “post-1969 public utility property” means any public utility property which is not pre-1970 public utility property.

(D) **Applicable 1968 method.**—The term “applicable 1968 method” means, with respect to any public utility property—

(i) the method of depreciation used on a return with respect to such property for the latest taxable year for which a return was filed before August 1, 1969,

(ii) if clause (i) does not apply, the method used by the taxpayer on a return for the latest taxable year for which a return was filed before August 1, 1969, with respect to its public utility property of the same kind (or if there is no property of the same kind, property of the most similar kind) most recently placed in service, or

(iii) if neither clause (i) nor (ii) applies, a subsection (l) method.

In the case of any section 1250 property to which subsection (j) applies, the term “applicable 1968 method” means the method permitted under subsection (j) which is most nearly comparable to the applicable 1968 method determined under the preceding sentence.

(E) **Applicable 1968 method in certain cases.**—If the taxpayer evidenced the intent to use a method of depreciation (other than its applicable 1968 method or a subsection (l) method) with respect to any public utility property in a timely application for change of accounting method filed before August 1, 1969, or in the computation of its tax expense for purposes of reflecting operating results in its regulated books of account for its July 1969 accounting period, such other method shall be deemed to be its applicable 1968 method with respect to such property and public utility property of the same (or similar) kind subsequently placed in service.

(F) **Subsection (l) method.**—The term “subsection (l) method” means any method determined by the Secretary to result in a reasonable allowance under subsection (a), oth-

er than (i) a declining balance method, (ii) the sum of the years-digits method, or (iii) any other method allowable solely by reason of the application of subsection (b)(4) or (j)(1)(C).

(G) Normalization method of accounting.—In order to use a normalization method of accounting with respect to any public utility property—

(i) the taxpayer must use the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account, and

(ii) if, to compute its allowance for depreciation under this section, it uses a method of depreciation other than the method it used for the purposes described in clause (i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from the use of such different methods of depreciation.

(H) Flow-through method of accounting.—The taxpayer used a "flow-through method of accounting" with respect to any public utility property if it used the same method of depreciation (other than a subsection (I) method) to compute its allowance for depreciation under this section and to compute its tax expense for purposes of reflecting operating results in its regulated books of account.

(I) July 1969 accounting period.—The term "July 1969 accounting period" means the taxpayer's latest accounting period ending before August 1, 1969, for which it computed its tax expense for purposes of reflecting operating results in its regulated books of account.

For purposes of this paragraph, different declining balance rates shall be treated as different methods of depreciation.

(4) Special rules as to flow-through method.—

(A) Election as to new property representing growth in capacity.—If the taxpayer makes an election under this subparagraph before June 29, 1970, in the manner prescribed by the Secretary, in the case of taxable years beginning after December 31, 1970, paragraph (2)(C) shall not apply with respect to any post-1969 public utility property, to the extent that such property constitutes property which increases the productive or operational capacity of the taxpayer with respect to the goods or services described in paragraph (3)(A) and does not represent the replacement of existing capacity.

(B) Certain pending applications for changes in method.—In applying paragraph (1)(B), the taxpayer shall be

deemed to have used a flow-through for its July 1969 accounting period pre-1970 public utility property for application for change of accounting 1, 1969, if with respect to public same (or similar) kind most recent used a flow-through method of accounting period.

(5) Reorganizations, assets acquisition.—In the case of a corporate reorganization, by reason of the assets of one taxpayer by another the fact that any trade or business of the ratemaking by more than one body, or circumstances, the application of any provision to any public utility property does not apply. This subsection, the Secretary shall provide the application of such provisions in a the purposes of this subsection.

(m) Class lives.—

(1) In general.—In the case of a taxpayer election under this subsection for the "reasonable allowance" as used in subsection respect to property which is placed in service in a taxable year and which is included in any class life has been prescribed) only an allowance life prescribed by the Secretary which anticipated useful life of that class of property or other group. The allowance so prescribed (unless otherwise prescribed by the Secretary) per class life by not more than 20 percent (or half year) of such life.

(2) Certain first-year conventions not permitted.—No convention with respect to the time at which property is placed in service shall be permitted unless the convention generally would provide greater depreciation in the taxable year in which the assets are placed in service than would be permitted if all assets were placed in service throughout the year and if depreciation was computed without regard to any convention.

(3) Making of election.—An election for any taxable year shall be made at the beginning of the year, and subject to such conditions as the Secretary by regulations.

(n) Straight line method in certain cases.—

(1) In general.—In the case of any property which is part constructed, reconstructed, erected,

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seemed to have used a flow-through method of accounting for its July 1969 accounting period with respect to any pre-1970 public utility property for which it filed a timely application for change of accounting method before August 1, 1969, if with respect to public utility property of the same (or similar) kind most recently placed in service, it used a flow-through method of accounting for its July 1969 accounting period.

(5) **Reorganizations, assets acquisitions, etc.**—If by reason of a corporate reorganization, by reason of any other acquisition of the assets of one taxpayer by another taxpayer, by reason of the fact that any trade or business of the taxpayer is subject to jointmaking by more than one body, or by reason of other circumstances, the application of any provisions of this subsection to any public utility property does not carry out the purposes of this subsection, the Secretary shall provide by regulations for the application of such provisions in a manner consistent with the purposes of this subsection.

(6) **Class lives.**—

(1) **In general.**—In the case of a taxpayer who has made an election under this subsection for the taxable year, the term "reasonable allowance" as used in subsection (a) means (with respect to property which is placed in service during the taxable year and which is included in any class for which a class life has been prescribed) only an allowance based on the class life prescribed by the Secretary which reasonably reflects the anticipated useful life of that class of property to the industry or other group. The allowance so prescribed may (under regulations prescribed by the Secretary) permit a variance from any class life by not more than 20 percent (rounded to the nearest half year) of such life.

(2) **Certain first-year conventions not permitted.**—No convention with respect to the time at which assets are deemed placed in service shall be permitted under this section which generally would provide greater depreciation allowances during the taxable year in which the assets are placed in service than would be permitted if all assets were placed in service ratably throughout the year and if depreciation allowances were computed without regard to any convention.

(3) **Making of election.**—An election under this subsection for any taxable year shall be made at such time, in such manner, and subject to such conditions as may be prescribed by the Secretary by regulations.

(4) **Straight line method in certain cases.**—

(1) **In general.**—In the case of any property in whole or in part constructed, reconstructed, erected, or used on a site which

was, on or after June 30, 1976, occupied by a certified historic structure (as defined in section 191(d)(1)) which is demolished or substantially altered (other than by virtue of a certified rehabilitation as defined in section 191(d)(3)) after such date—

(A) subsections (b), (j), (k), and (l) shall not apply,

(B) the term "reasonable allowance" as used in subsection (a) shall mean only an allowance computed under the straight line method.

(2) **Exception.**—The limitations imposed by this subsection shall not apply to personal property.

(c) **Substantially rehabilitated historic property.**—

(1) **General rule.**—Pursuant to regulations prescribed by the Secretary, the taxpayer may elect to compute the depreciation deduction attributable to substantially rehabilitated historic property as though the original use of such property commenced with him. The election shall be effective with respect to the taxable year referred to in paragraph (2) and all succeeding taxable years.

(2) **Substantially rehabilitated property.**—For purposes of paragraph (1), the term "substantially rehabilitated historic property" means any certified historic structure (as defined in section 191(d)(1)) with respect to which the additions to capital account for any certified rehabilitation (as defined in section 191(d)(3)) during the 24-month period ending on the last day of any taxable year, reduced by any amounts allowed or allowable as depreciation or amortization with respect thereto, exceeds the greater of—

(A) the adjusted basis of such property, or

(B) \$5,000.

The adjusted basis of the property shall be determined as of the beginning of the first day of such 24-month period, or of the holding period of the property (within the meaning of section 1250(e)), whichever is later.

(p) **Depreciation of improvements in the case of mines, etc.—**

For additional rule applicable to depreciation of improvements in the case of mines, oil and gas wells, other natural deposits, and timber, see section 611.

Aug. 16, 1954, c. 736, 68A Stat. 51; Sept. 2, 1958, Pub.L. 85-866, Title I, § 89(b), 72 Stat. 1665; Oct. 16, 1962, Pub.L. 87-834, § 13(b), (c)(1), 76 Stat. 1034; Nov. 8, 1966, Pub.L. 89-800, § 2, 80 Stat. 1513; June 13, 1967, Pub.L. 90-26, §§ 1, 2(b), 81 Stat. 57, 58; Dec. 30, 1969, Pub.L. 91-172, Title IV, § 441(a), Title V, § 521(a), (d), 83 Stat. 625, 649, 653; Dec. 10, 1971, Pub.L. 92-178, Title I, § 109(a), 85 Stat. 508; Jan. 3, 1975, Pub.L. 93-625, § 3(c), 88 Stat. 2109; Oct. 4, 1976, Pub.L. 94-455, Title II, §§ 202(c)(3), 203(a), Title XIX, §§

201(a)(27), 1906(b)(13)(A), Title XX
§ 1530, 1768, 1834, 1918; Nov. 12, 19
§ 1555.

Historical Note

Internal Revenue Code. Similar provisions to this section were contained in section 23(D), (n), 114(a) of the 1939 Internal Revenue Code.

Derivation and Similar Provisions. For derivation and similar provisions to section 23, I.R.C.1939, see Historical Note to section 161 of this title.

Section 114, I.R.C.1939, was derived from Act May 28, 1938, c. 289, § 114, 52 Stat. 494.

Provisions similar to those in section 114, I.R.C.1939, were contained in the following prior Revenue Acts:

1906—June 22, 1936, c. 690, § 114, 49 Stat. 1086.

1934—May 10, 1934, c. 277, § 114, 48 Stat. 710.

1932—June 6, 1932, c. 209, § 114, 47 Stat. 202.

1928—May 29, 1928, c. 852, § 114, 45 Stat. 821.

1926—Feb. 26, 1926, c. 27, § 204, 44 Stat. 11, as amended by Act June 29, 1939, c. 247, Title II, § 213(i), 53 Stat. 872.

1924—June 2, 1924, c. 234, § 204, 43 Stat. 258, as amended by Act June 29, 1939, c. 247, Title II, § 213(i), 53 Stat. 872.

References in Text. Section 8 of the United States Housing Act of 1937, referred to in subsec. (k)(3)(B), is classified to section 1437 of Title 42, The Public Health and Welfare.

The Communications Satellite Act of 1962 (47 U.S.C. 701), referred to in subsec. 204(A)(iii), is Pub.L. 87-624, Aug. 31, 1962, 76 Stat. 419, which is classified generally to chapter 6 (section 701 et seq.) of Title 47, Telegraphs, Telephones, and Radiotelegraphs. For complete classification of this Act to the Code, see Short Title note under section 701 of Title 47 and Tables volume.

1977 Amendment. Subsec. (k). Pub.L. 95-171, substituted "January 1, 1979" for "January 1, 1978" wherever appearing in (1), (2), and (3)(D).

1976 Amendment. Subsec. (b). Pub.L. 94-455, § 1906(b)(13)(A), struck out "or 'delegate' following 'Secretary'".

Subsec. (d). Pub.L. 94-455, § 1906(b)(27)(A), 1906(b)(13)(A), substituted his

1901(a)(27), 1906(b)(13)(A), Title XXI, § 2124(c)(1), (d)(1), 90 Stat. 1540, 1768, 1834, 1918; Nov. 12, 1977, Pub.L. 95-171, § 4(a), 91 Stat. 1075.

Historical Note

Internal Revenue Code. Similar provisions in this section were contained in section 212(b), (a), 114(a) of the 1939 Internal Revenue Code.

Derivation and Similar Provisions. For derivation and similar provisions to section 167, see Historical Note preceding section 161 of this title.

Section 167 of I.R.C. 1939, was derived from Act July 28, 1938, c. 289, § 114, 52 Stat. 111.

Provisions similar to those in section 167 of 1939, were contained in the following Revenue Acts:

- June 22, 1936, c. 690, § 114, 49 Stat. 1690.
- May 10, 1934, c. 277, § 114, 48 Stat. 710.
- June 6, 1932, c. 209, § 114, 47 Stat. 202.
- May 29, 1928, c. 852, § 114, 45 Stat. 821.
- Feb. 26, 1926, c. 27, § 204, 44 Stat. 14, as amended by Act June 29, 1939, c. 247, Title II, § 213(i), 53 Stat. 872.
- June 2, 1924, c. 234, § 204, 43 Stat. 258, as amended by Act June 29, 1939, c. 247, Title II, § 213(i), 53 Stat. 872.

References in Text. Section 8 of the United States Housing Act of 1937, referred to in subsec. (k)(3)(B), is classified to section 1437f of Title 42, The Public Health and Welfare.

The Communications Satellite Act of 1962 (U.S.C. 701), referred to in subsec. (d)(3)(F), is Pub.L. 87-624, Aug. 31, 1962, 76 Stat. 419, which is classified generally to chapter 6 (section 701 et seq.) of Title 47, Telegraphs, Telephones, and Radiotelegraphs. For complete classification of this Act to the Code, see Short Title table under section 701 of Title 47 and Tables volume.

1974 Amendment. Subsec. (k). Pub.L. 93-415 substituted "January 1, 1979" for "January 1, 1978" wherever appearing in subsec. (k)(3)(D).

1974 Amendment. Subsec. (b). Pub.L. 93-415 substituted "1906(b)(13)(A), struck out "or his delegate" following "Secretary".

1977 Amendment. Pub.L. 95-171, § 4(a), substituted "1906(b)(13)(A), struck out

ed "after August 16, 1954" for "after the date of enactment of this title" and struck out "or his delegate" following "Secretary" in first sentence preceding "shall be binding".

Subsec. (e). Pub.L. 94-455, §§ 202(c)(3), 1906(b)(13)(A), substituted in par. (3) "beginning after December 31, 1975" for "beginning after July 24, 1969" and in pars. (1) to (3) struck out "or his delegate" following "Secretary".

Subsec. (f)(1). Pub.L. 94-455, § 1906(b)(13)(A), struck out "or his delegate" following "Secretary".

Subsec. (f)(2). Pub.L. 94-455, § 1901(a)(27)(B), substituted "October 16, 1962" for "the date of enactment of the Revenue Act of 1962".

Subsec. (i). Pub.L. 94-455, § 1906(b)(13)(A), struck out in pars. (1) and (2) "or his delegate" following "Secretary".

Subsec. (j). Pub.L. 94-455, § 1906(b)(13)(A), struck out in pars. (1), (4)(B), (5)(C), and (6)(A) "or his delegate" following "Secretary".

Subsec. (k)(1). Pub.L. 94-455, §§ 203(a)(1), 1906(b)(13)(A), substituted reference to January 1, 1978 for reference to January 1, 1976 and struck out "or his delegate" following "Secretary".

Subsec. (k)(2)(A). Pub.L. 94-455, § 203(a)(2), substituted "\$20,000" for "\$15,000".

Subsec. (k)(3)(B). Pub.L. 94-455, §§ 203(a)(3), 1906(b)(13)(A), substituted "the Leased Housing Program under section 8 of the United States Housing Act of 1937" for "the policies of the Housing and Urban Development Act of 1968" and struck out "or his delegate" following "Secretary".

Subsec. (k)(3)(D). Pub.L. 94-455, § 203(a)(4), added subsec. (k)(3)(D).

Subsec. (d)(3)(F). Pub.L. 94-455, § 1906(b)(13)(A), struck out "or his delegate" following "Secretary".

Subsec. (d)(4)(A). Pub.L. 94-455, §§ 1901(a)(27)(C), 1906(b)(13)(A), substituted "before June 29, 1970," for "within 180 days after the date of the enactment of this subparagraph" and struck out "or his delegate" following "Secretary".

Even if tax court had duty to consider income taxpayer's uncontroverted and self-serving trial testimony given as establishing that his dominant motivation for loans was to make profit in his own land development business, tax court was also entitled to consider contemporaneous objective circumstances surrounding the loans, which permitted reasonable inference inconsistent with such testimony. *Id.*

141. Findings

Tax Court did not err in determining that dominant motivation of shareholders in guaranteeing third party's loan was investment-related and not business related, and, thus, that bad debt was nonbusiness, where only evidence of dominant motivation was size of shareholders' investment in third party. *Tennessee Securities Inc. v. C.I.R.*, C.A.6, 1982, 674 F.2d 570.

Tax Court properly found that obligation with respect to which income taxpayer suffered loss was worthless where at time of payments principal debtor's estate was insolvent, but where there were two principal debtors on the bond, income taxpayer, seeking deduction for payment made on his guaranty, was bound to show that obligation of other debtor, on performance bond funded by surety in favor of county and water district, was also worthless to county or to surety, and same was true despite Tax Court's finding that second debtor was principal in name only to comply with local law and that liability thus fell upon taxpayer when his father, first-mentioned debtor, became insolvent. *Hunsaker v. Commissioner of Internal Revenue Service*, C.A.9, 1980, 615 F.2d 1253.

Where Tax Court found that income taxpayer's purpose in becoming actively involved in development corporation was to protect his father's very substantial investments and his own, not as shareholder but as creditor and perhaps also as future joint venturer, not to enter trade or business of managing corporations or with intent of becoming employee of corporation or of insuring development projects for his own businesses, Tax Court could find that taxpayer's payments made as guarantor on performance bonds were not result of connection with, nor were the losses incurred in, taxpayer's real estate and land development businesses. *Id.*

142. Review

For purposes of review of Commissioner's determination as to whether taxpayer is entitled to deduction for partially worthless debt, facts must be considered as they existed at time deduction was taken; of course, Commissioner's denial of partially worthless debt deduction does not preclude taxpayer from attempting to establish deduction for later years. *Brimberry v. C.I.R.*, C.A.5, 1979, 588 F.2d 975.

Given church's consistently healthy operating revenues in 1968 and 1969 and prospect of successful reorganization in 1968, neither insolvency of church, Securities and Exchange Commission's complaint against church in 1967, nor church's institution of chapter X reorganization proceeding in 1968 necessarily demonstrated partial worthlessness of debt owed taxpayer by church and thus Commissioner's disallowance of taxpayer's claimed partially worthless debt deductions for 1967 and 1968 was neither arbitrary nor erroneous. *Id.*

§ 167. Depreciation

(a) **General rule.**—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

- (1) of property used in the trade or business, or
- (2) of property held for the production of income.

In the case of recovery property (within the meaning of section 168), the deduction allowable under section 168 shall be deemed to constitute the reasonable allowance provided by this section, except with respect to that portion of the basis of such property to which subsection (k) applies.

[See main volume for text of (b) and (c)]

(d) **Agreement as to useful life on which depreciation rate is based.**—Where, under regulations prescribed by the Secretary, the taxpayer and the Secretary have, after August 16, 1954, entered into an agreement in writing specifically dealing with the useful life and rate of depreciation of any property, the rate so agreed upon shall be binding on both the taxpayer and the Secretary in the absence of facts or circumstances not taken into consideration in the adoption of such agreement. The responsibility of establishing the existence of such facts and circumstances shall rest with the party initiating the modification. Any change in the agreed rate and useful life specified in the agreement shall not be effective for taxable years before the taxable year in which notice in writing by certified mail or registered mail is served by the party to the agreement initiating such change. This subsection shall not apply with respect to recovery property defined in section 168.

[See main volume for text of (e) to (h)]

(i) **Repealed.** Pub.L. 95-600, Title III, § 312(c) (4), Nov. 6, 1978, 92 Stat. 2826]

[See main volume for text of (j)]

(k) **Depreciation of expenditures to rehabilitate low-income rental housing.**—

(1) **60-month rule.**—The taxpayer may elect, in accordance with regulations prescribed by the Secretary, to compute the depreciation deduction provided by subsection (a) attributable to rehabilitation expenditures incurred with respect to low-income rental housing after July 24, 1969, and before January 1, 1984, under the straight line method using a useful life of 60 months and no salvage value. Such method shall be in lieu of any other method of computing the depreciation deduction under subsection (a), and in lieu of any deduction for amortization, for such expenditures.

(2) **Limitations.**—

(A) Except as provided in subparagraph (B), the aggregate amount of rehabilitation expenditures paid or incurred by the taxpayer with respect to any dwelling unit in any low-income rental housing which may be taken into account under paragraph (1) shall not exceed \$20,000.

(B) The aggregate amount of rehabilitation expenditures paid or incurred by the taxpayer with respect to any dwelling unit in any low-income rental housing which may be taken into account under paragraph (1) may exceed \$20,000, but shall not exceed \$40,000, if the rehabilitation is conducted pursuant to a program certified by the Secretary of Housing and Urban Development, or his delegate, or by the government of a State or political subdivision of the United States and if:

- (i) the certification of development costs is required;
- (ii) the tenants occupy units in the property as their principal residence and the program provides for sale of the units to tenants demonstrating home ownership responsibility; and
- (iii) the leasing and sale of such units are pursuant to a program in which the sum of the taxable income, if any, from leasing of each such unit, for the entire period of such leasing, and the amount realized from sale or other disposition of a unit, if sold, normally does not exceed the excess of the taxpayer's cost basis for such unit of property, before adjustment under section 1016 for deductions under section 167, over the net tax benefits realized by the taxpayer, consisting of the tax