

**ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILES 8672**

**2280 SCOMM 94: SENATE SPECIAL COMMITTEE ON OIL & GAS, 1993-94**

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Rec'd 8/31/69

#### ARTICLE XXIII

##### AMENDMENT

23.1 Amendment. This Agreement may be supplemented, amended or modified at any time, but only by written instrument duly executed by the parties hereto, and approved by the Royalty Oil and Gas Development Advisory Board and by the Alaska State Legislature by Concurrent Resolution by majority vote of the members of each house.

#### ARTICLE XXIV

##### SUCCESSOR AND ASSIGNS

24.1 Successors and Assigns. This Agreement shall extend to, be binding upon, and inure to the benefit of the parties hereto and their respective heirs, devisees, legal representatives, successors, and assigns, and shall constitute a covenant of equitable servitude running with the interests covered hereby.

24.2 Transfer of Title. Any conveyance of all or any part of any interest owned by any party hereto shall be made expressly subject to this agreement. No change of title shall be binding on the other party hereto until the receipt by the other party of a photocopy or a certified copy of the recorded instrument evidencing such change in ownership.

24.3 General Prohibition. No assignment of this Agreement shall be made by either party without first obtaining the written consent of the other party. The Commissioner of Natural Resources may grant such consent on behalf of the Seller.

#### ARTICLE XXV

##### HEADINGS

25.1 Headings. Article headings used in this Agreement are for

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convenience only and shall not affect in the construction of this Agreement.

#### ARTICLE XXVI

##### OIL SPILL CLEANUP AND CONTINGENCY PLANS

26.1 Oil Spill and Cleanup Contingency Plans. Purchaser shall be responsible for the detection, location, confinement, and cleanup of oil discharges occurring at the Purchaser's refinery after the oil purchased hereunder has been delivered to Purchaser at the outlet flange measuring device of TAPS at North Pole, Alaska; and during the time such oil and the products therefrom remain in the physical possession of the Purchaser at its refinery or in pipelines or other carrier owned and operated by the Purchaser. At least 180 days prior to scheduled first delivery of royalty oil Purchaser shall submit its contingency plans to the Department of Environmental Conservation for review and approval. The plans shall provide for immediate corrective action in the event of oil discharges, including confinement and cleanup, and restoration of the affected resource. The plans shall include separate and specific techniques and schedules for cleanup of petroleum discharges on land, lakes, rivers and streams.

#### ARTICLE XXVII

##### RECORDS

27.1 Preservation of Records. Purchaser and Seller 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 resale of the royalty oil and its refined products for a period of four (4) 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

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law or regulation. Purchaser shall either maintain its records within the State of Alaska or make such records available to Seller and Purchaser's principal office in the State of Alaska within thirty (30) days after written request therefore by Seller.

27.2 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 thereto directly relating to the 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 such property, records, books, documents and indexes thereto. Notwithstanding the foregoing, (i) Seller shall not be required to disclose any information, data or records which are required to be held confidential by applicable state law or regulation, and (ii) Purchaser shall not be required to disclose any information, data or records containing trade secrets which Purchaser or its Affiliates, contractors or subcontractors have agreed to hold confidential, or which Purchaser or its affiliates, contractors or sub-contractors by contract with unaffiliated third parties have agreed to hold confidential. Seller shall notify Purchaser of all information obtained, recorded or copied from Purchaser's records in order that Purchaser may evaluate the advisability of seeking that such information be held confidential by Seller under applicable law or regulation or under the provisions of this Article.

27.3 Financial Statements. Purchaser will provide Seller with year-end financial statements audited by an independent certified public accounting firm. Preparation of the financial statements shall be at Purchaser's cost. Said statements shall be communicated to Seller in the manner provided in Article XVI.

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IN WITNESS WHEREOF, the Seller has caused this Agreement to be executed by its Commissioner of Natural Resources and the Purchaser has caused this Agreement to be executed by its President, thereunto duly authorized by its Board of Directors in accordance with the certified seal, duly attested, to be affixed hereto, as of the day and year first above written.

ATTEST:

Ludwig H. Brown

THE STATE OF ALASKA

By: Walter E. Pascho

Commissioner, Department  
of Natural Resources

"SELLER"

APPROVED AS TO FORM:

\_\_\_\_\_

EARTH RESOURCES COMPANY OF ALASKA

ATTEST:

Angimio H. Shihus

By: Wm. F. Long

President

"PURCHASER"

I, Michael E. Craig, certify that I am the Secretary of the Corporation named as Purchaser in the above contract, that Louis Francis DeLong was then President of said corporation; that said Agreement was duly signed for and in behalf of said corporation by authority of its governing body, and is within the scope of its corporate powers.

Michael E. Craig  
Secretary

(CORPORATE SEAL)

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Sheet 6 of 69

## EXHIBIT "A"

Attached to and Made a Part of the Agreement for the Sale and Purchase of State Royalty Oil dated May 2, 1927 between EARTH RESOURCES COMPANY OF ALASKA, an Alaska corporation "Purchaser", and the COMMISSIONER OF NATURAL RESOURCES OF THE STATE OF ALASKA, acting pursuant to Alaska Statute 38.05.183, "Seller", With Respect To Certain Royalty Oil Owned and Taken In-Kind by Seller Under the leases Described Herein Covering Lands in the State of Alaska.

| Tract No. | Description<br>(United Meridian, Alaska)       | No. of Acres | ADL Bond No. | Rate Per Acre | Lease of Record                         | OPR Interest | Working Interest Ownership                |
|-----------|------------------------------------------------|--------------|--------------|---------------|-----------------------------------------|--------------|-------------------------------------------|
| 1         | TIEN-RHIE, Sec. 8, 10                          | 1,250        | 47413        | 1/8           | Mohd and Chavira                        |              | Mohd-77%<br>Chavira-23%                   |
| 2         | TIEN-RHIE, Sec. 11, 12                         | 1,250        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 3         | TIEN-RHIE, Sec. 7                              | 800          | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 4         | TIEN-RHIE, Sec. 21, 24                         | 1,250        | 47413        | 1/8           | So-Vo Petroleum Co.                     |              | So-Vo-100%                                |
| 5         | TIEN-RHIE, Sec. 21, 22                         | 1,250        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 6         | TIEN-RHIE, Sec. 19, 20                         | 1,250        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 7         | TIEN-RHIE, Sec. 23, 24                         | 1,250        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 8         | TIEN-RHIE, Sec. 24                             | 640          | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 9         | TIEN-RHIE, Sec. 19                             | 800          | 47413        | 1/8           | Mohd and Phillips                       |              | Mohd-50%<br>Phillips-50%                  |
| 10        | TIEN-RHIE, Sec. 23, 24                         | 1,250        | 47413        | 1/8           | Mohd and Phillips                       |              | Mohd-50%<br>Phillips-50%                  |
| 11        | TIEN-RHIE, Sec. 21, 22                         | 1,250        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 12        | TIEN-RHIE, Sec. 17, 18, 19, 20                 | 2,416        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 13        | TIEN-RHIE, Sec. 12, 14, 15, 21                 | 2,500        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 14        | TIEN-RHIE, Sec. 15, 16, 21, 22                 | 2,500        | 47413        | 1/8           | Mohd and Chavira                        |              | Mohd-50%<br>Chavira-50%                   |
| 15        | TIEN-RHIE, Sec. 17, 18, 19, 20                 | 2,416        | 47413        | 1/8           | Mohd and Chavira                        |              | Mohd-50%<br>Chavira-50%                   |
| 16        | TIEN-RHIE, Sec. 12, 21                         | 1,250        | 47413        | 1/8           | A.R.Co., BP Alaska, So-Vo Petroleum Co. |              | A.R.Co.-50%<br>BP Alaska-50%<br>So-Vo-50% |
| 17        | TIEN-RHIE, Sec. 27, 28, 29                     | 1,250        | 47413        | 1/8           | Mohd and Chavira                        |              | Mohd-50%<br>Chavira-50%                   |
| 18        | TIEN RHIE, Sec. 27, 28, 29, 30                 | 2,500        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 19        | TIEN-RHIE, Sec. 25, 26, 27, 28                 | 2,500        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 20        | TIEN-RHIE, Sec. 29, 30, 31, 32                 | 2,500        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 21        | TIEN-RHIE, Sec. 27, 28, 29, 30                 | 2,500        | 47413        | 1/8           | A.R.Co. and Eason                       |              | A.R.Co.-50%<br>Eason-50%                  |
| 22        | TIEN RHIE, Sec. 27, 28, 29, 30, 31, 32, 33, 34 | 2,416        | 47413        | 1/8           | Mohd and Phillips                       |              | Mohd-50%<br>Phillips-50%                  |

\*See enclosure on page A-5

Y-Y Acid 60 Mils = 500 mg.

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| Time<br>No.           | Company                                       | No. of<br>Aircraft | ADL<br>Serial<br>No. | Eng<br>Serial<br>No. | Power<br>Plant               | Other<br>Remarks             | Weight<br>Class              |
|-----------------------|-----------------------------------------------|--------------------|----------------------|----------------------|------------------------------|------------------------------|------------------------------|
| (United States, A-4s) |                                               |                    |                      |                      |                              |                              |                              |
| 80                    | TION-RITE, Ser. 27, 28, 29, 30                | 2,372              | 47412                | 1/8                  | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati |
| 81                    | TION-RITE, Ser. 29, 30, 31, 32                | 2,371              | 47413                | 1/8                  | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati |
| 82                    | TION-RITE, Ser. 33                            | 646                | 47414                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 83                    | TION-RITE, Ser. 1, 4, 10                      | 1,823              | 47414                | 1/8                  | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati |
| 84                    | TION-RITE, Ser. 1, 2, 11, 12                  | 2,370              | 47415                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 85                    | TION-RITE, Ser. 6, 7, 8, 9<br>and NL/4 Ser. 3 | 2,371              | 47416                | 1/8                  | Mohr and Phillips            | Mohr and Phillips            | Mohr and Phillips            |
| 86A                   | TION-RITE, NW/4 Ser. 3                        | 180                | 47416                | 1/8                  | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati | Mohr, P. & Co.<br>Cincinnati |
| 86                    | TION-RITE, Ser. 1, 4, 9, 10                   | 2,373              | 47417                | 1/8                  | American Motors, et al.      | American Motors, et al.      | American Motors, et al.      |
| 87                    | TION-RITE, Ser. 1, 2, 11, 12                  | 2,380              | 47418                | 1/8                  | American Motors and<br>Corry | American Motors and<br>Corry | American Motors and<br>Corry |
| 88                    | TION-RITE, Ser. 1, 4, 7, 8                    | 2,381              | 47419                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 89                    | TION-RITE, Ser. 1, 4, 9, 10                   | 2,382              | 47420                | 1/8                  | St. Louis Petroleum Co.      | St. Louis Petroleum Co.      | St. Louis Petroleum Co.      |
| 90                    | TION-RITE, Ser. 1, 2, 11, 12                  | 2,383              | 47421                | 1/8                  | St. Louis Petroleum Co.      | St. Louis Petroleum Co.      | St. Louis Petroleum Co.      |
| 91                    | TION-RITE, Ser. 1, 4, 7, 8                    | 2,384              | 47422                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 92                    | TION-RITE, Ser. 1, 4, 9, 10                   | 2,385              | 47423                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 93                    | TION-RITE, Ser. 1, 2, 11, 12                  | 2,386              | 47424                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 94                    | TION-RITE, Ser. 1, 4, 7, 8                    | 2,387              | 47425                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 95                    | TION-RITE, Ser. 4, 9                          | 2,388              | 47426                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |
| 96                    | TION-RITE, Ser. 10                            | 870                | 47427                | 1/8                  | A.R. Co. and Evans           | A.R. Co. and Evans           | A.R. Co. and Evans           |

\*See also serial on page A-5



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## EXHIBIT "B"

Calculation of monthly in value royalty under the Leases and leases (all calculations shall be rounded to the nearest \$0.001)

STEP 1: Calculate each producer's weighted average value per barrel at Point of Delivery for all oil sold by each producer during the month, as follows:

## Example, Producer Y

| (1)<br>Destination | (2)<br>Volume<br>Sold | (3)<br>Sales Price<br>at<br>Destination | (4)<br>Shipping<br>Costs | (5)<br>Pipeline<br>Tariff | (6)<br>Point of<br>Delivery<br>Value | (7)<br>Weighted<br>Average<br>Value |
|--------------------|-----------------------|-----------------------------------------|--------------------------|---------------------------|--------------------------------------|-------------------------------------|
| 1                  | 2,000,000             | \$12.500                                | \$ -0-                   | \$4.770                   | \$7.730                              | -                                   |
| 2                  | 4,000,000             | 13.370                                  | 1.110                    | 4.750                     | 7.510                                | -                                   |
| 3                  | 5,000,000             | 13.440                                  | 3.830                    | 4.750                     | 4.860                                | -                                   |
|                    |                       |                                         |                          |                           |                                      | <u>\$6.145</u>                      |

Columns 2, 3, 4 and 5 shall be computed from actual data as reported by each producer and filed with the State of Alaska for royalty purposes and severance tax purposes.

STEP 2: The "weighted average value" per barrel of each producer (column 7 above) at the Point of Delivery shall then be used in column (9) below in calculating the applicable in value price for each producer (column 11 below), the weighted average of which shall be the In Value Price to Buyer (column 12), as follows:

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-continued-

Example, all producers:

| (8)<br>Producer<br>and<br>Quantity | (9)<br>Wtd. Avg. Value<br>at Point of<br>Delivery (Col. 7) | (10)<br>Wtd. Avg. Price<br>Received by all<br>other Producers | (11)<br>Applicable<br>Price for In<br>Value Calculation | (12)<br>In Value<br>Price to<br>Buyer |
|------------------------------------|------------------------------------------------------------|---------------------------------------------------------------|---------------------------------------------------------|---------------------------------------|
| X:<br>4,200,000                    | \$6.920                                                    | \$6.404                                                       | \$6.920                                                 | -                                     |
| Y:<br>11,000,000                   | 6.343                                                      | 7.003                                                         | 7.003                                                   | -                                     |
| Z:<br>500,000                      | 7.700                                                      | 6.504                                                         | 7.700                                                   | -                                     |
| Weighted Avg.                      | \$6.542                                                    |                                                               |                                                         | \$7.003                               |

## Notes:

- 1) Values in column 10 are the weighted average of all producers other than the producer for which the calculation is being made.
- 2) Column 11 is the highest of the values in columns 9 or 10 for each producer.
- 3) Column 12 is the weighted average of values in column 11.
- 4) Buyer shall not pay any reimbursable costs under Article II until such costs are judicially determined as owing.
- 5) There is no posted price. "Market" or "field" value shall not be used in calculating the "In Value price to Buyer" unless and until the methodology of determining same is judicially decided.
- 6) Subject to later adjustment under Article VI.

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RANDALL J. POZDENA, PhD  
Managing Director

Monday, March 22, 1993

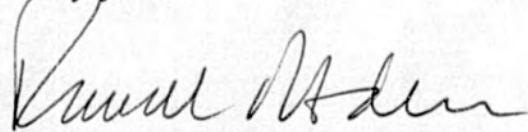
Ms. Annette Kreitzer  
Staff Assistant  
Office Of Senator Loren Leman  
State Capitol  
Juneau, AK 99801

Dear Annette:

Please find enclosed a copy of my slide presentation to Senator Leman's Committee last week, as per your request. Thank you for offering to distribute the attached to the committee members.

I appreciated the opportunity to present our work for Tesoro. Please let me know if I can be of further assistance.

Very truly yours,



Enclosure

PIONEER TOWER, SUITE 1460  
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RANDALL J. POZDENA, PhD  
Managing Director

Monday, March 22, 1993

Dear Committee Member:

The attached document is a copy of the slide presentation I made to your committee on Thursday, March 18, 1993. The presentation summarizes our analysis of the economic impact of an illustrative refinery capacity enhancement at the Kenai refinery of Tesoro Alaska Petroleum. As discussed in my presentation, such a refinery development and its on-going operation would generate over 2,700 jobs, and \$51.33 million in tax revenue.

I enjoyed the opportunity to share the results of our work for Tesoro. Please do not hesitate to contact us if we can be of further assistance.

Very truly yours,



### **Economic Impacts of Tesero's New Vacuum and Asphalt Units at Kenai, Alaska**

**Randall J. Pozdena**  
Managing Director  
ECO Northwest  
Portland, Oregon

ECO Northwest

### **ECO Northwest**

Economics, finance and planning  
consultants

- Founded by University of Oregon professors in 1974
- Offices in Eugene and Portland, Oregon
- Client base of public, private and litigation clients
- Specializing in quantitative valuation and analysis exercises

ECO Northwest

### **Selected Current Clients**

- Pacific Gas Transmission Company
- Peavey Grain Company
- Plaintiffs in the Exxon Valdez litigation
- Tri-Met (Portland-area transit agency)
- California Air Resources Board
- Plaintiffs in the SeaTac airport noise litigation
- Defending oil refiner, gas station litigation

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### **The Scale of the Project**

#### **Construction Phase:**

- \$46.5 m. for capital equipment, labor and materials
- 18 month period beginning 1993 and ending 1994

#### **Operational Phase:**

- \$5 m. annual operating expenditures
- Refine 15,000 barrels/day = \$82 m.

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### **The Economic Impacts**

- Direct impacts from spending on construction and operation
- Indirect impacts from the impact on other suppliers and vendors
- Induced impacts, as recipients of income spend their incomes on goods and services

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### **Modeling the Alaska Economy**

ECO developed custom Input-Output models

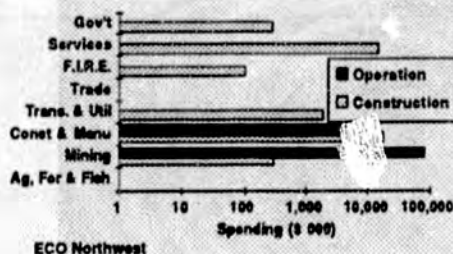
- Kenai Peninsula
- State of Alaska

ECO measured construction and operational spending

- by sector
- by year

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## Tesoro Spending by Sector



## Multiplier Effects

Multiplier effects are limited by "leakage" from the Alaska economy

But significant multiplier effects occur nonetheless:

- Each dollar of Tesoro spending generates 20 to 30 cents of spending elsewhere
- For each first-round job, another one-half job is created elsewhere

ECO Northwest

## Economic Impacts

The economic impacts are significant over the life of the Project:

|                    | Alaska     | Kenai      |
|--------------------|------------|------------|
| Business Output    | \$1,284 m. | \$1,188 m. |
| Labor Income       | \$126 m.   | \$107 m.   |
| Property Income    | \$632 m.   | \$591 m.   |
| Jobs (person-yrs.) | 2,787      | 2,357      |

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## Tax Revenue Impacts

Using the economic impacts, ECO calculated tax revenue over the life of the project

Historical ratios and relationships used for:

- Sales tax revenue
- Property tax revenue
- Corporate income tax revenue
- Fees and charges

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## Tax Rate Assumptions

### Sales Tax:

- 3% Kenai, 2% Borough, 1.18% elsewhere

### Property Tax:

- 1.261% of value in Kenai, 6.6% of income elsewhere

### Corporate Income Tax:

- 3.4% of "property income"

### Regulatory Cost Charges:

- 0.653% of gross pipeline revenue

### Workers Comp and Unemployment Insur.:

- 2.4% of employee compensation

ECO Northwest

## Tax Revenue Impacts

The tax revenue impacts over the life of the Project also are significant:

| Tax          | Statewide   | Kenai       |
|--------------|-------------|-------------|
| Sales        | \$ 0.74 m.  | \$ 0.67 m.  |
| Property     | \$ 22.76 m. | \$ 14.42 m. |
| Corp. Income | \$ 21.46 m. | NA          |
| Misc.        | \$ 6.35 m.  | NA          |
| TOTAL        | \$ 51.33 m. | \$ 15.09 m. |

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## **Distribution of Tax Burden**

Because Alaska relies on a corporate income tax:

- The tax revenues are collected from the sectors benefitting from the Project

Higher worker incomes:

- Lead to higher residential property spending and property tax revenues
- Effects will be confined to those areas benefitting from Project-stimulated jobs

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## **Conclusions**

Alaska economy would enjoy significant benefits from Tesoro Project

- Biggest effects come from on-going refining operations

Tax revenues also would increase significantly

- Corporate income tax and property tax revenues are the two biggest sources

ECO Northwest

# ANS ROYALTY RIK RETROACTIVE AMERADA HESS ADJUSTMENTS

(Millions of Dollars)

(Includes Interest through Fall 1992 Billing Date)

| Company                    | Billed            | Resolved,<br>Paid or Pending<br>Settlement | Paid<br>Under<br>Protest | Unpaid<br>or<br>Disputed | Comments                                                                                                                                                             |
|----------------------------|-------------------|--------------------------------------------|--------------------------|--------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Petrostar                  | \$ 2              | \$ 2                                       |                          | \$ 0                     |                                                                                                                                                                      |
| Tesoro<br>To Chevron       | 142<br>(45)<br>97 | 97                                         |                          | 0                        | \$45 M on bbls. sold to Chevron with an Amerada Hess Adjustment Clause. The rest would be covered under the Tesoro Settlement Agreement Payment Plan if consummated. |
| Chevron<br>From Tesoro     | 64<br>45<br>109   |                                            | \$47<br>—<br>47          | \$17<br>45<br>62         | \$47 M Payments under protest pending resolution of litigation. Scheduled for trial April 1995.                                                                      |
| Mapco<br>(GVEA)<br>(Mapco) | 18<br>101<br>119  |                                            |                          | 18<br>101<br>119         | Subject to two pending lawsuits -- one in Juneau and one in Anchorage.                                                                                               |
| <b>TOTALS</b>              | <b>\$327</b>      | <b>\$99</b>                                | <b>\$47</b>              | <b>\$181</b>             |                                                                                                                                                                      |

# **Mapco's 1991 10-K**

## **Item 3. Legal Proceedings**

**..... Based on information supplied to MAPI by State representatives, it appears that the potential claims asserted by the State might total between \$120 million and \$160 million, including interest on the retroactive amounts claimed by the State. The State's ultimate claim against MAPI would be based upon the difference between the volume weighted average of the royalty values reported by the producers in the past and the volume weighted average of the revised values the State succeeds in proving in the**

### **Amerada Hess litigation .....**

**After consideration of such legal, business and other factors it deems relevant, management believes that the outcome of such matters, including the matters specifically discussed above, will not have a material adverse effect on MAPCO's consolidated financial position.**

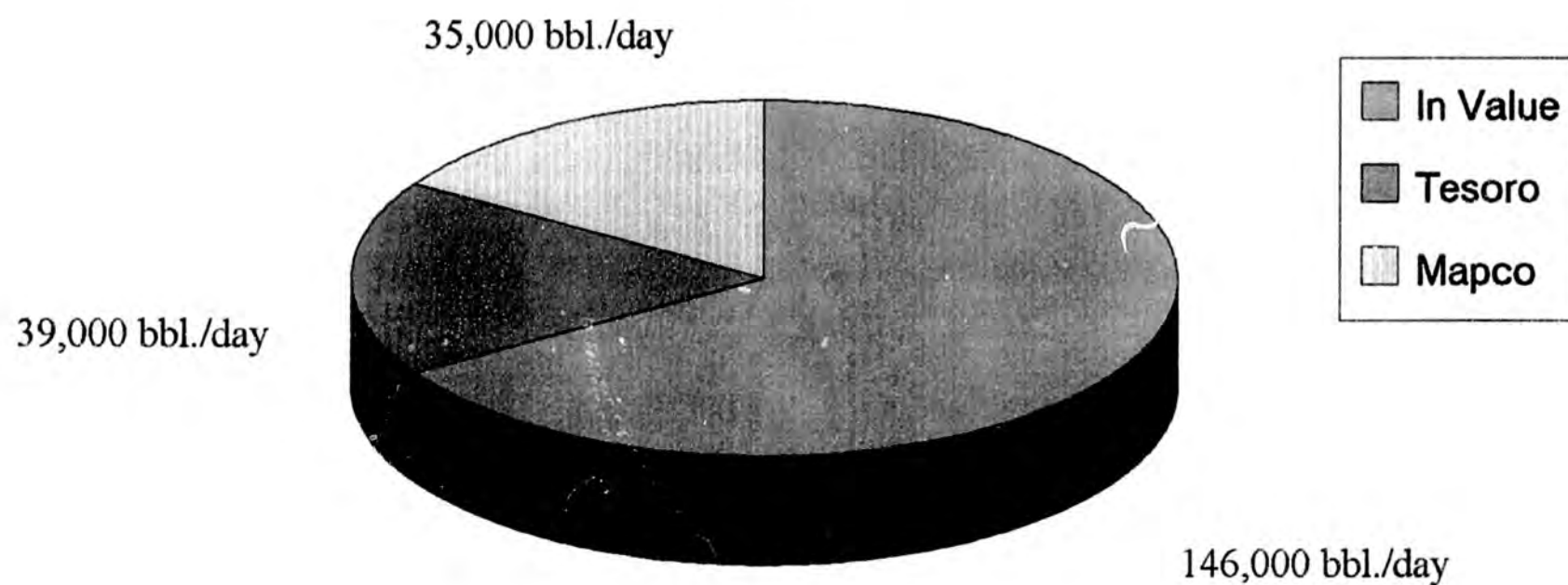
## **Section 6.4 Adjustments to Billings**

Royalty Oil Sales Agreement between ERCA and the State

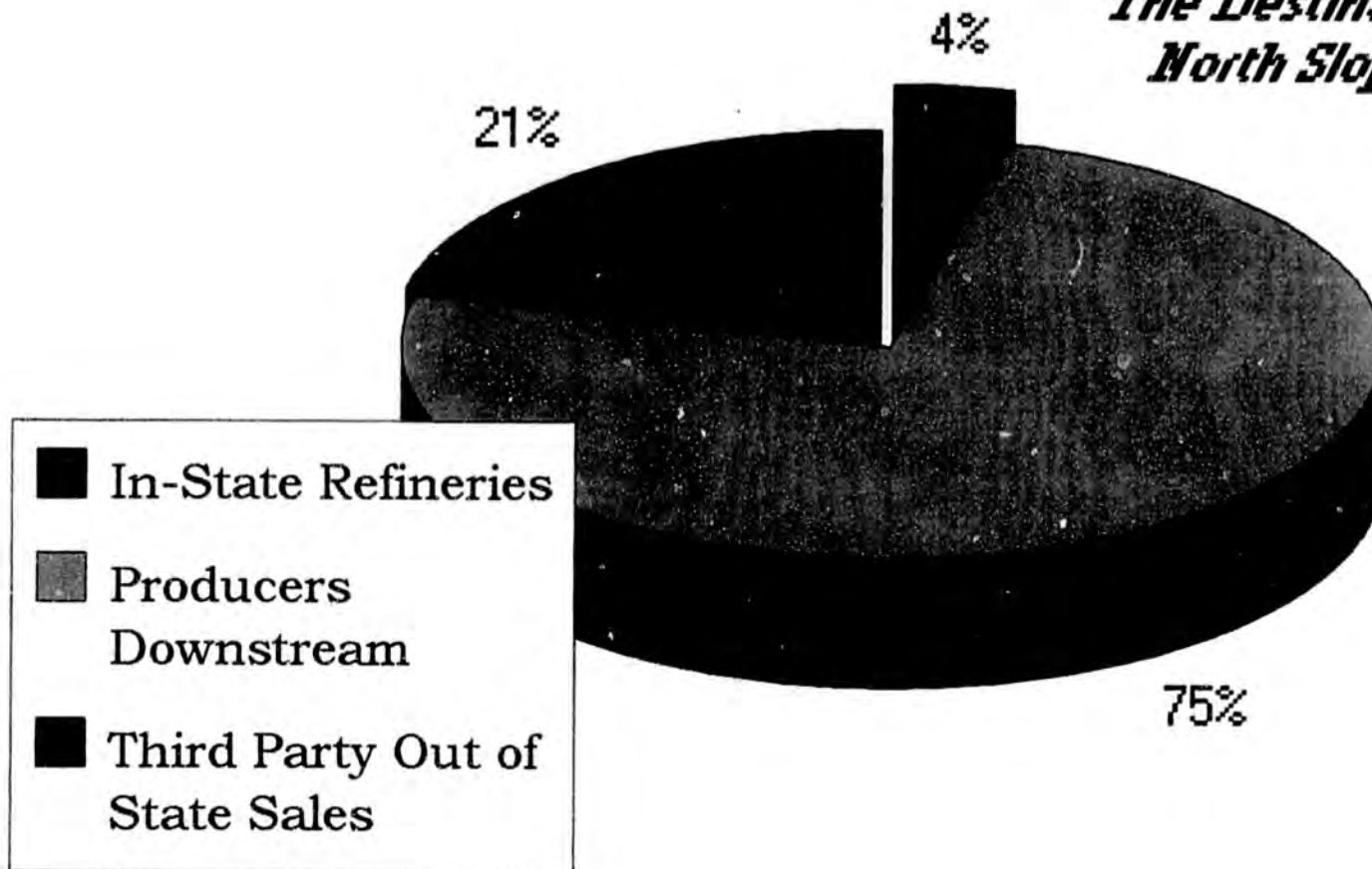
**. . . . Seller shall from time to time adjust its prior billings to reflect adjustments necessitated as a result of (i) a final judgment or settlement entered in certain pending litigation between Seller and the Lessees styled State of Alaska, et. al. vs. Amerada Hess Corporation, et. al., Ca No. 77-847, in the Superior Court of the State of Alaska, First Judicial District at Juneau; . . . .**

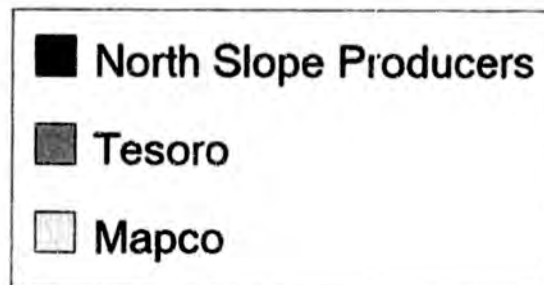
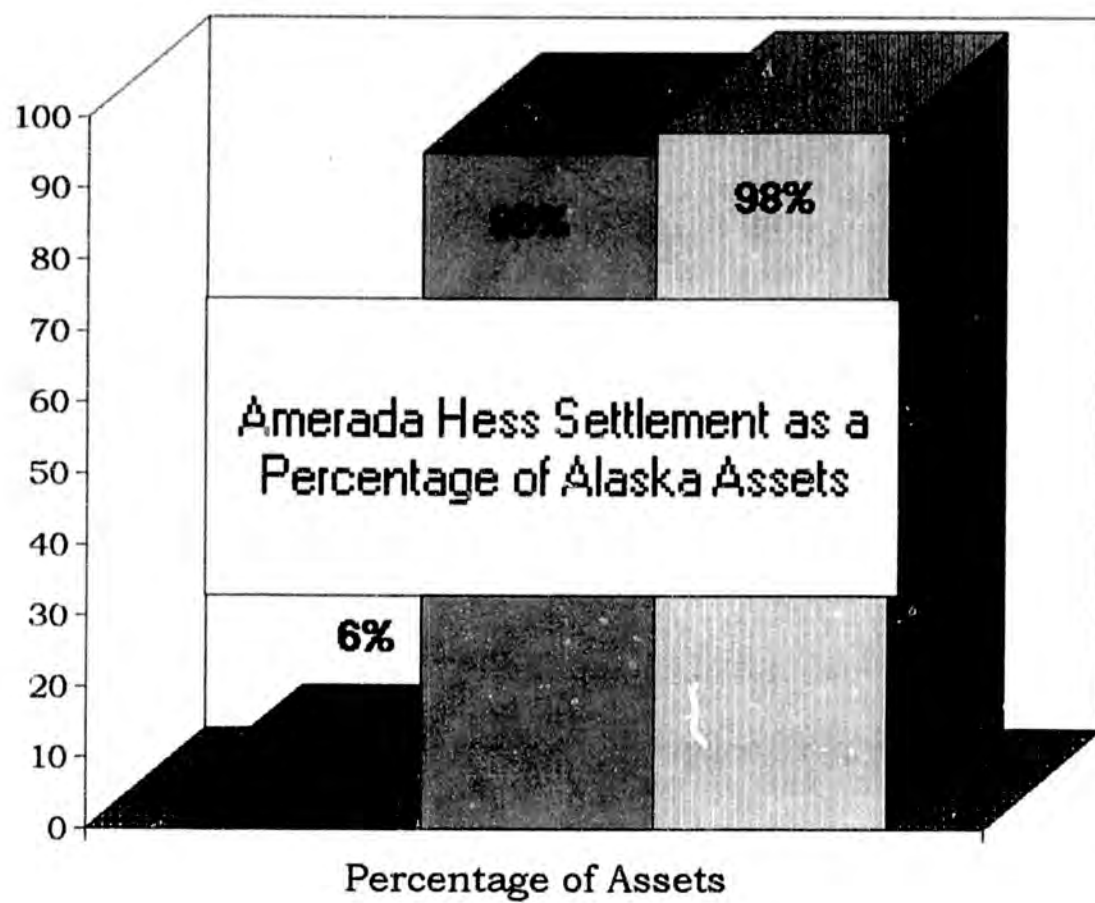
**Due to the potentially large sums of money involved, any adjustments to any billing under the provisions of this Article VI by Seller made more than sixty (60) days after such billing was initially rendered shall be paid to or refunded by Purchaser or Seller over the same period over which such adjustments accrued or thirty-six (36) months, whichever is longer. . . .**

***Disposition of State's North Slope Royalty  
Oil--1992***

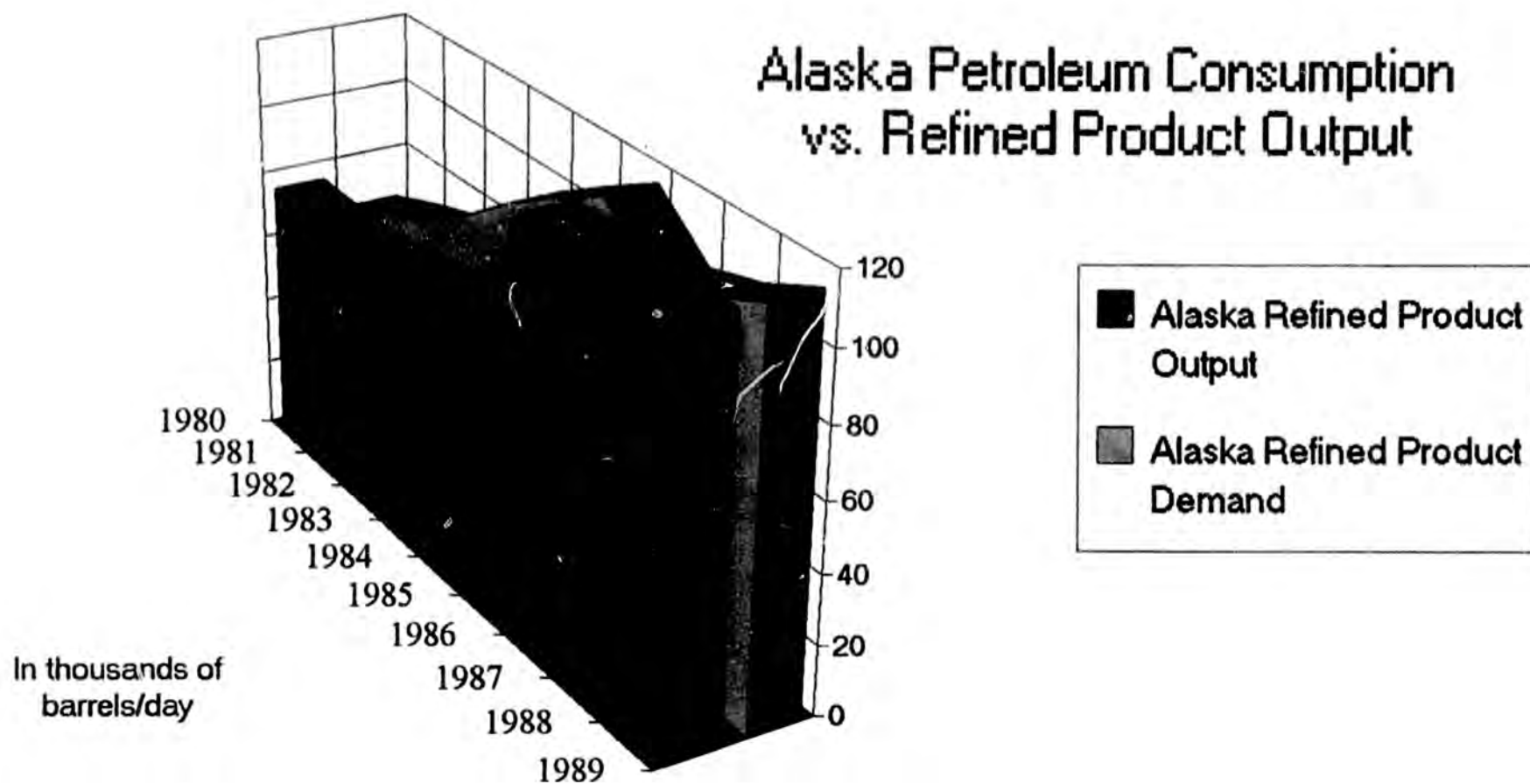


***The Destination of  
North Slope Oil***

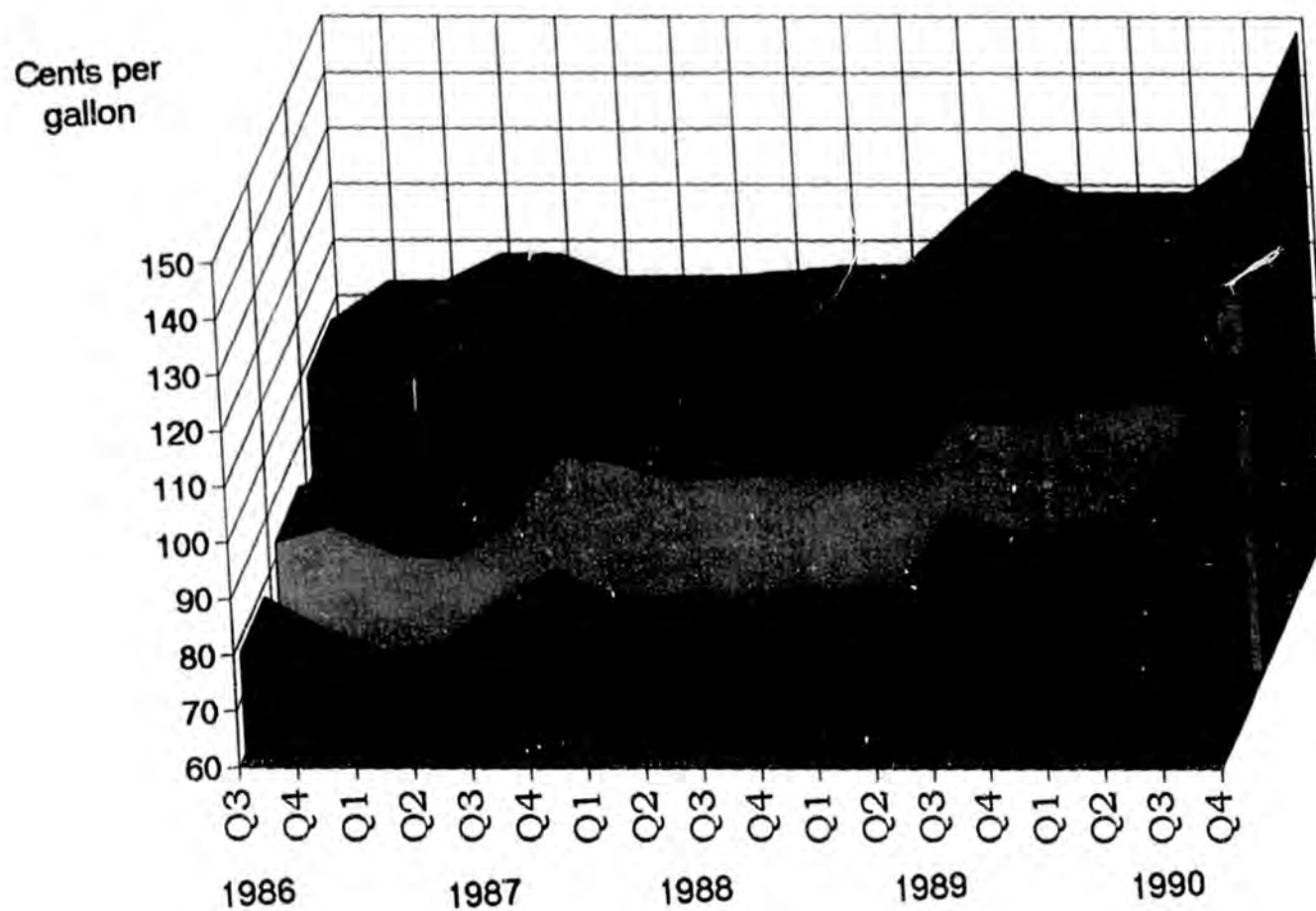




## Alaska Petroleum Consumption vs. Refined Product Output

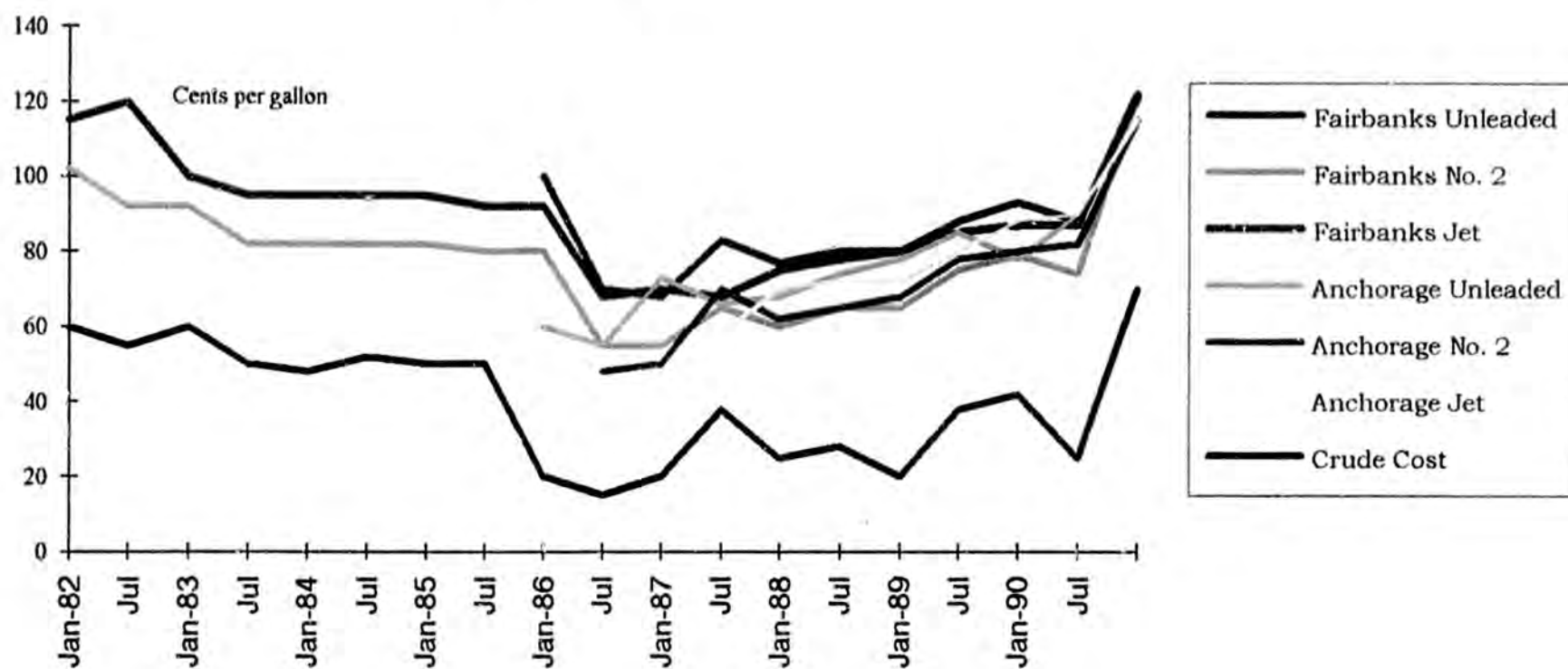


## Unleaded Gasoline Costs



- Anchorage
- Fairbanks
- Juneau

## MAPCO WHOLESALE PRODUCT PRICES AND CRUDE COST



## ***Other State Industrial Incentive/Credit Programs***



- ♦ **Fisheries Business Tax Credit.** AS 43.75.032. For five years (1987-91), fisheries businesses could reduce tax liability by up to 50% by taking credits for new processing ventures. ***Total cost to state over 5 years: \$68 million.***



- ♦ **Industrial Incentive Investment Tax Credit.** AS 43.20.042. As a credit against the corporate income and/or mining license taxes, taxpayers could take 40-100 percent of the full federal investment tax credit (on up to \$250,000,000 in investment) for new gas processing facilities and mineral exploration and development (normally only 18% of the federal credit was creditable against Alaska taxes). The Department of Revenue has not calculated the fiscal impact of this credit.



- ♦ **Mining License Tax Incentive for New Mines.** AS 43.65.010(a). As an incentive to open new mines, any new mine is exempt from the mining license tax for the first 3 1/2 years of production.



- ♦ **Oil and Gas Exploration Incentive Credit.** AS 38.05.180(i). DNR may allow credits of up to 50% of the cost of exploratory drilling or geophysical work against up to 50% of the lessees' liability for royalties and severance taxes. ***Total credits taken in past 10 years: \$40.9 million.***

## **The "Public Purpose Clause"**

*"No tax shall be levied, or appropriation of public money made, or public property transferred, nor shall the public credit be used, except for a public purpose."*

- ♦ *"Whether private entities receive a benefit from an expenditure of public money is not, in our view, the dispositive factor."*

**...The Attorney General's Office, April 10, 1992, in reviewing a \$1.2 million appropriation to assist an Arctic Slope Regional Corporation coal project.**

- ♦ *"The test instead is whether the expenditure will directly enhance the general welfare of the community." This is true even though the appropriation will "extend a substantial benefit to...private entities."*

**...From the same opinion.**

- ♦ *Appropriations aiding a private development project pass the "public purpose" test as long as they are intended to "resolve energy problems...provid[e] an abundant, stable-priced energy source, as well as provid[e] long-term, stable employment opportunities...and potential tax revenues."*

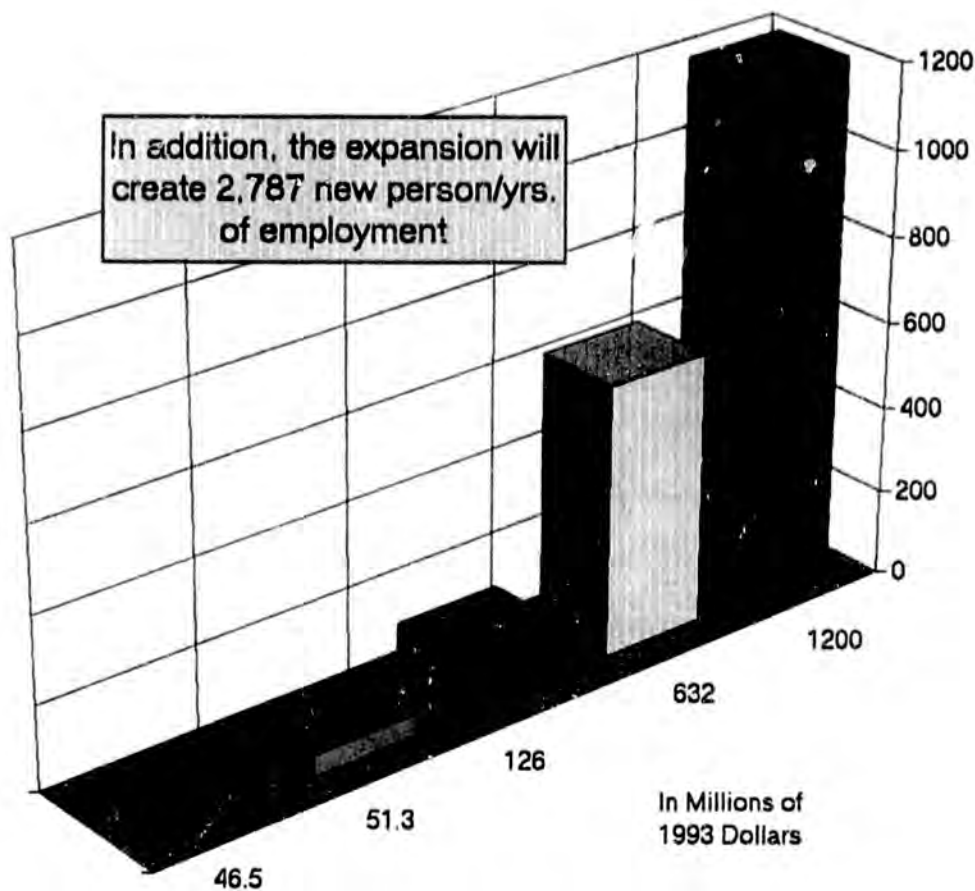
**...From the same opinion.**

- ♦ *"Substantial deference must be extended to the legislature's finding [that the program serves a public purpose]...[One] must therefore find that the legislative public purpose finding was arbitrary or without any reasonable basis in fact before concluding that the expenditure constitutes an impermissible expenditure of public funds."*

**...The Attorney General's Office, Sept. 13, 1984, in reviewing an appropriation in aid of the Red Dog Mine.**

- ♦ *For incentive programs, there need be no guarantee that the encouraged conduct would not occur anyway. It need only appear that the incentive is designed to "influence or affect private behavior."*

**...The Attorney General, March 8, 1983, in reviewing proposed assistance to a private ski area.**



### ***The Costs and Benefits of Tesoro's Expansion Proposal***

- Cost of Credit
- Increased State and Local Tax Revenues
- Increased Employee Compensation
- Increased Property Income
- Increased Industrial Output

## ***The "Special Legislation" Clause***

*"The Legislature shall pass no local or special act if a general act can be made applicable. Whether a general act can be made applicable shall be subject to judicial determination."*

### **The Test is Threefold:**

#### **♦ *Is the Act Special or Local?***

It is only "special or local" if, by its terms, it covers only an identified entity (e.g. the "Eagle River-Chugiak Borough"), geographic area (i.e. Prince William Sound or Delta) or event (i.e. Big Lake Ice Classic).

**SB 134 is therefore not "special legislation--it applies statewide to any royalty oil purchaser.**

#### **♦ *If it is "special," what is unique about the topic that prevents it from being adequately taken care of by general law?***

For example, there was no justification for a special law dealing with formation of the Eagle River-Chugiak Borough, because formation could be dealt with under Title 29. Laws treating the unique issues of oil spill cleanup in Prince William Sound or Delta agriculture, however, had to be limited to those areas. Only a "rational basis" for separate treatment is required.

**For reasons set out in Tesoro's White Paper, SB 134 treats issues unique to royalty oil purchasers. There are therefore several "rational reasons" for the legislation.**

#### **♦ *If the legislation is "special," is its overall goal a matter of "common concern" to Alaskans?***

This test relates to the law's goals, and not its reach or extent of impact.

**SB 134's goals are to promote the state's economy, generate tax revenues, and assure energy self-sufficiency. These are all matters of "common concern."**

## **The Permanent Fund Clause**

*"At least twenty-five percent of all mineral lease rentals, royalties, royalty sale proceeds...and bonuses **received by the state** shall be placed in a permanent fund..."*

- ♦ **The key word is "received," since the state has not RECEIVED the funds from the royalty oil purchasers that would be subject to the credit**
- ♦ **On April 24, 1992, the Attorney General ruled that the phrase "administrative proceeding" in the budget reserve clause must be given a strict reading, because:**

1. It is an "important right of the people..to have the constitution upheld as the people ratified it...Normally, such deference to the intent of the people requires 'adherence to the common understanding of words.' Applying this approach, the court **looked to a standard dictionary to determine the common understanding of the word at issue.**"

2. There are other constitutional policies that must be reconciled with the permanent fund clause. In the budget reserve case, this other policy was the constitution's general preference for the unrestricted receipt of funds.

### **Applying the Attorney General's analysis to this issue:**

- ♦ **The dictionary definition of "received" is "to come into possession of."**  
*...Webster's New Collegiate Dictionary (1981)*
- ♦ **The term "received" has always been carefully chosen when implementing the permanent fund clause. See: AS 37.13.010.**
- ♦ **There are also other constitutional policies that must be accomodated here--specifically, the policy of allowing the legislature the power to legislate to promote the public welfare. The permanent fund clause should not be interpreted to impliedly limit the legislature powers beyond its explicit scope--i.e., with respect to the disposition of funds that "it has come into possession of."**

*SB 134 and HB 185--A Sound  
Investment in Alaska's Economic Future*

Tesoro Alaska Petroleum Company

March 3, 1993

W. Gene Burden  
Vice President  
Administration & Government Relations

March 3, 1993

THE HONORABLE LOREN LEMAN  
The State Senate, State of Alaska  
Capitol Building, Room 113  
Juneau, Alaska 99801-1182

Subject: SB 134 Background and Analysis Material

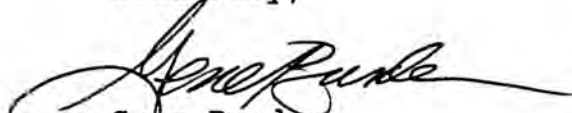
Dear Senator Leman:

Tesoro Alaska Petroleum Company supports the passage of SB 134 and looks forward to the opportunity for a full review of the benefits the legislation offers the state. Tesoro's support of the legislation is prompted by the obligations our company incurred as a result of the Amerada Hess settlements. In essence, Tesoro is now subject to payments over the next ten (10) years that are expected to be in excess of \$100 Million as a result of the state's retroactive price increases for crude oil we processed in the 1980's. We do not believe it likely that this obligation can be recouped from the 90% of the Alaska consumers who benefitted from fuel prices in effect during the years Tesoro paid the lower amount for royalty crude oil.

The legislation would offer a limited opportunity to obtain credit for qualifying capital investments made in the state which could be applied against our current obligations for the retroactive price increases. The benefits of such investments in terms of jobs, state and local tax income, and increased industrial output are substantial and are documented in the accompanying material. The concept presented is not unique and has been previously adopted by the Legislature for other industry and in related manners aimed at stimulating the economy. Examples of precedents are also presented in this package.

I look forward to meeting with you in the future and welcome any comments or suggestions you may have.

Sincerely,

  
Gene Burden

Enclosure

*SB 134 and HB 185--A Sound  
Investment in Alaska's Economic Future*

Tesoro Alaska Petroleum Company

March 3, 1993

## *SB 134 and HB 185--a Sound Investment in Alaska's Economic Future*

### ***I. Introduction and Executive Summary***

This paper discusses the background and rationale for SB 134 and HB 185-- legislation that would allow purchasers of state royalty oil to credit the value of future capital investment in the state against one-time retroactive claims made by the state under those purchasers' royalty oil sales contracts. That credit program would be: (1) a prudent investment of any benefits that the state might otherwise hope to receive from these claims, because ~~the capital investment resultantly encouraged would produce both tax revenues and private economic stimulus substantially in excess of the amount of the credit~~ (2) consistent with longstanding state royalty oil policy, which is to employ that oil to encourage Alaska energy self-sufficiency and provide refined products at a reasonable price; and (3) necessary to achieve equity in the sharing of burdens occasioned by the *Amerada Hess* litigation.

This paper is divided into six parts:

***Sec. II    The State of Alaska has long viewed its royalty oil as a critical tool in encouraging a competitive in-state refining industry, and that policy has enjoyed considerable success***

As a result of that policy, the state has achieved virtual energy self-sufficiency. Its three refineries provide a variety of refined products to 90% of Alaskans, at a resultant savings during the 1980's of at least \$450 million from the costs Alaskans would have had to bear if their refined products were still imported. Gasoline prices in areas served by these refineries have averaged \$.30/gallon less than in areas of Alaska still needing imported fuels.

**Sec. III** *The success of state royalty oil policy is jeopardized by \$300 million in retroactive purchase assessments now claimed against in-state refiners as a result of the Amerada Hess litigation settlement*

The state is now demanding over \$300 million in retroactive price increases from its in-state refiners, based on a formula developed in negotiations between the state and producers to which the refiners weren't invited. The result is a grossly inequitable burden on those refiners. The state's settlement with the producers represents only 6% of those companies' assets in Alaska, but the demands against the in-state refiners ~~represents nearly 100% of their Alaska assets.~~ The state's retroactive claims will result either in: (1) future inability to finance critical improvements and expansions to meet growing demand; and/or (2) higher fuel costs to consumers (crude costs account for 80% of product price fluctuations).

**Sec. IV** *SB 134 and HB 185 would allow the state to earn full value on its Amerada Hess claims without risking the continued health of the state's refining industry*

The legislation would allow in-state refiners to credit the cost of refinery expansion against the state's retroactive price increase claims, but only under safeguards not found in similar credit legislation--such as a requirement that the each investment yield commensurate returns; that the investment isn't otherwise required; and that the investment must occur within a finite period.

**Sec. V** *Available evidence indicates that the state could expect an exceptional return from its investment through SB 134*

As an example of how the legislation would work, ECO Northwest has analyzed the public benefits of a \$46.5 million expansion of the Tesoro refinery--an expansion that likely could not occur in the absence of the legislation. A \$46.5 credit investment would return \$51.3 million in tax revenues, \$126 million in new employee compensation, \$632 million in increased property income, and \$1.2 billion in increased industrial output, and would generate 2,787 new person/years of employment.

**Sec. VI** *SB 134 backed by ample precedent, and is consistent with long-established public policy*

SB 134 is simply a variant--and a more secure and prudent variant at that--of the investment tax credit. The state has established such credits for a number of industries, including a ~~fisheries tax credit~~ ~~under which \$10 million were credited over a five-year period for new fisheries ventures.~~ The state also has a number of existing programs for crediting royalty obligations for new industrial activity.

**Sec. VII** *SB 134 is constitutional*

A detailed legal analysis, enclosed as Appendix B, concludes that SB 134 serves two valid public purposes and is not "special" in nature. There is also no violation of the Permanent Fund clause.

OK was this 111?

**II. The State of Alaska has long viewed its royalty oil as a critical tool in encouraging a competitive in-state refining industry, and that policy has enjoyed considerable success**

For nearly two decades, the State of Alaska has successfully pursued a policy of taking part of its royalty oil "in kind," and then selling that oil to encourage the creation and expansion of in-state oil refining capability. In furtherance of that policy, and after Prudhoe Bay oil began flowing in the late 1970's, the Alaska Legislature approved sales of royalty oil to Tesoro Alaska Petroleum and Earth Resources Company (the

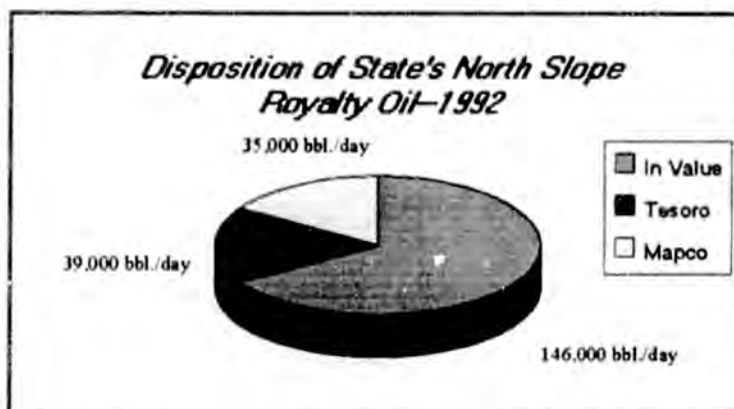


CHART 1. Source: Ak. Dept. of Natural Resources, *Historical and Projected Oil and Gas Consumption*, April 1992 at 6.

predecessor of Mapco Petroleum) of 39,000 bbl./day, and 35,000 bbl./day, respectively. See Chart 1. <sup>1/</sup> Both contracts required the oil to be processed at the companies' respective in-state refineries. <sup>2/</sup> At the time, the royalty oil sold by the state represented 100% of Earth Resources' throughput capacity, and enabled Tesoro to convert its refinery to operate with 100% ANS crude.

As a result of that policy, today three refineries--each fueled in part by state royalty oil--have made Alaska virtually self-sufficient in gasoline and other fuels.

<sup>3/</sup> These refineries provide product to every area of Alaska except Southeast, and

<sup>1/</sup> The Earth Resources contract was approved by HCR 130, Leg. Resolve 37 (1977), while Tesoro's contract was approved by §1, Ch. 105, SLA 1984. The Earth Resources contract (now assigned to Mapco) runs through 2003, while Tesoro's contract expires in 1995.

<sup>2/</sup> Tesoro's Kenai refinery began operation in the 1960's, supplied in part by royalty oil from Cook Inlet, which Tesoro began receiving in 1969. Earth Resources' North Pole refinery began operations in 1977 in anticipation of receiving state royalty oil as feedstock.

<sup>3/</sup> The three refineries are Tesoro's Kenai refinery (72,000 bbl./day capacity); Mapco's North Pole refinery (116,000 bbl./day); and Petro Star's North Pole refinery (7,000 bbl./day). A fourth refinery that once purchased royalty oil--Chevron's Nikiski refinery--closed for economic reasons in 1991.

have, throughout the 1980's, been able to expand their capacity to keep pace with rising consumer demand. Chart 2.

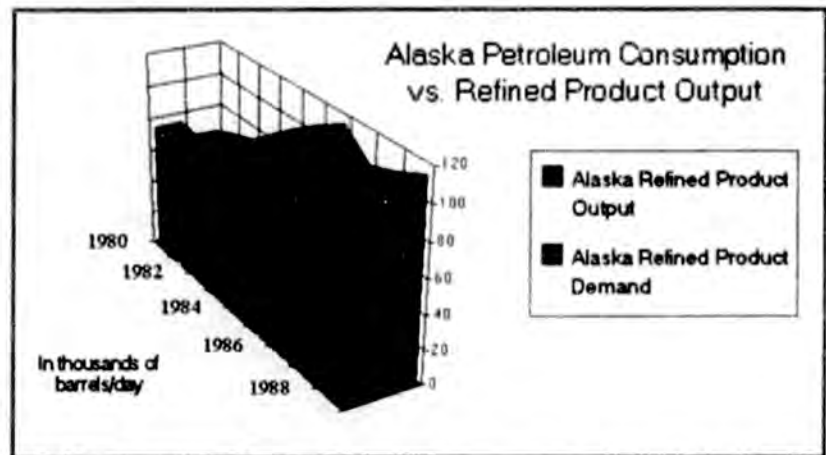


CHART 2.

Alaska's resultant energy self-sufficiency has brought with it considerable economic benefits. Aside

from the approximately 850 Alaskans directly employed by Tesoro, Mapco and Petro Star; the hundreds of Alaskans employed indirectly as a result of these refineries' operations; and the more than \$11 million in local and state tax revenues that these refineries generate annually, the state's royalty oil has fueled an intensively competitive product market, with considerable savings to the 90% of Alaskans within that market.

That fact can be seen clearly enough by comparing fuel prices in the markets served by these

refiners with the one Alaska market still dependent on lower-48 refined product--Southeast Alaska. As Chart 3 demonstrates, in recent years unleaded gasoline prices in Southeast

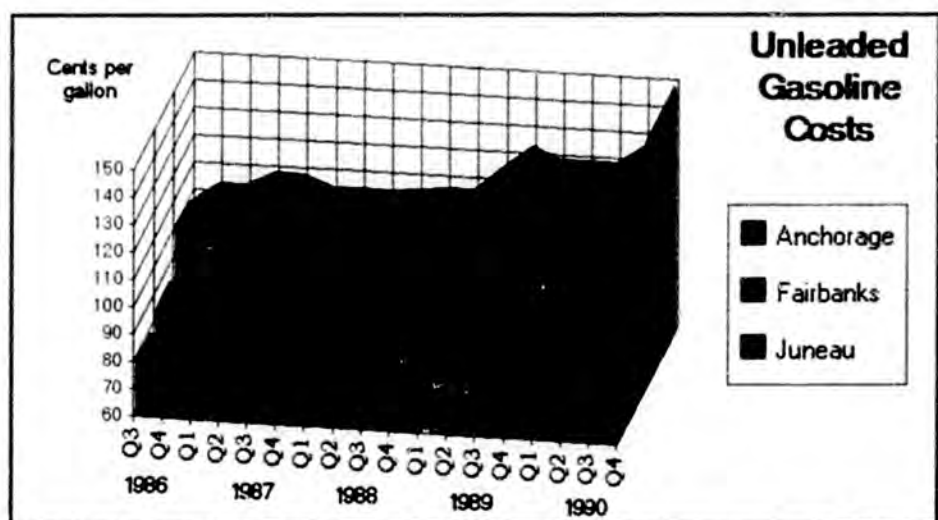


CHART 3. Source: Study by Purvin & Gertz, Inc. for Mapco Petroleum, 1992 at 4.

have averaged **30 cents per gallon** more than in Anchorage--a fact that experts

attribute in material part to the absence of refiner competition in the Panhandle.

<sup>4/</sup> As Purvin & Gertz explain, even if only one third of the price differential between Anchorage and Juneau were attributable to the keen competition encouraged by state royalty oil policy, that policy would still be responsible for a **\$450 million savings** to Alaska consumers in the 1980's. <sup>5/</sup>

**III. The success of state royalty oil policy is jeopardized by \$300 million in retroactive purchase assessments now claimed against in-state refiners as a result of the Amerada Hess litigation settlement**

The state's North Slope royalty oil sales occurred during a period of considerable controversy between the state and the North Slope producers over the "value" of royalty oil taken *in value* by the state. In 1977, the state filed suit over that dispute--the so-called *Amerada Hess* litigation. The suit languished for 15 years in its preliminary stages and, on the eve of trial in 1992, finally settled. Under the settlement, all the North Slope producers agreed to pay both past and future royalties under a complex new pricing formula. The cost of the retroactive payments by the producers totalled about \$700 million.

The in-state royalty oil purchasers paid for oil under their contracts in a different manner. DNR maintains, however, that those purchasers are obligated to also pay the state any additional money due by application of any formula agreed to by the state and the producers in the *Amerada Hess* litigation. Using the formula negotiated in the *Amerada Hess* litigation, and applying that formula to all royalty oil purchased by Mapco, Tesoro, Chevron and Petro Star over their contract periods, would yield retroactive payments approaching **\$300 million**.

<sup>4/</sup> Purvin & Gertz, Inc. report for Mapco Petroleum, 1992 at 1.

<sup>5/</sup> "If the competition brought on by the instate refineries didn't exist and the rest of Alaska were still supplied from outside the state, [and] even if the premium [resulting from lower instate refinery prices] were only 10 cents per gallon, Alaskan consumers would have paid \$450 million more for gasoline, heating fuel and diesel over the decade of the 1980s." *Id.*

The harshness of the state's position begins with the process it used to settle *Amerada Hess*. Remember that the *Amerada Hess* formula was developed in closed-door negotiations between the state and the North Slope producers. The state, however, maintained that the in-state refiners were precluded from participating in those negotiations. As a result, the refiners were not able to add their concerns to the deliberations--the final formula was served upon them as a *fait accompli*, without a thought given to the refiners' very different situation.

This is not to say that the North Slope producers won some painless deal from the *Amerada Hess* negotiations--the \$700 million settlement they must pay is a weighty one. However, by failing to have the refiners' voices at the negotiating table, it was inevitable that the ultimate settlement would fail to recognize the material differences between the producers' position and the

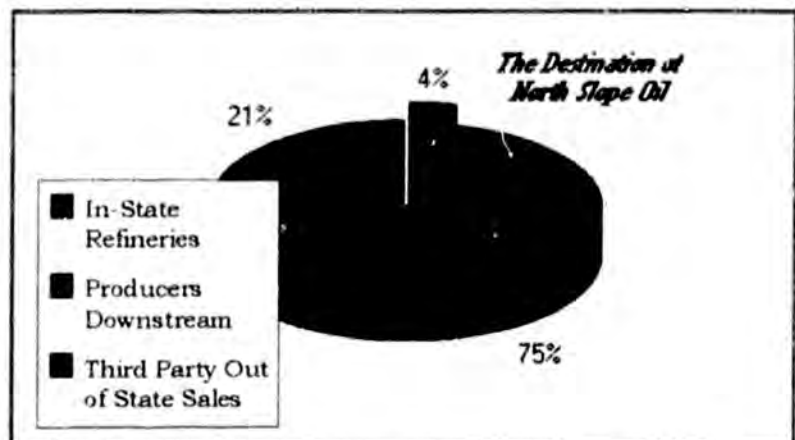


CHART 4

refiners'. For example, and as Chart 4 shows, three quarters of all North Slope oil is sent out of state to the producers' own refineries. Another 21% has been sold to out-of-state purchasers, including outside purchasers of royalty oil sold at auctions in the 1980's. Only 4% has been sold to in-state refiners, **but those refiners are being asked to shoulder 30%**-\$300 million out of a total \$1 billion--of all *Amerada Hess* payments.

And in this regard: of all the oil taken by North Slope producers, only 1/8th of that is royalty oil. What this means is that the producers are able to spread the *Amerada Hess* surcharge on one barrel of royalty oil over eight barrels of oil, while

the in-state refiners must bear that per-barrel surcharge undiluted. Thus, every \$1/bbl. *Amerada Hess* surcharge costs the in-state refiners \$1/bbl., while the same surcharge costs the producers 12.5 cents per barrel.

Moreover, the oil companies that purchased royalty oil at competitive bid in the 1980's, and shipped that crude outside for the benefit of lower-48 consumers (and conversely, without benefitting the Alaska economy at all), are not being asked to make *any* additional payments.

Additionally, the *Amerada Hess* settlement failed to account for the *relative* financial impact of the surcharge on the parties. As Chart 5 shows, while the producers' *Amerada Hess* settlements represent only six percent of the value of their Alaska holdings, the state's claim against Mapco virtually equals its entire Alaska asset base.

This kind of impact bodes ill for our in-state refiners' ability to continue to expand to meet growing market needs--a capability which, as we have seen, has heretofore been one of the principal dividends of state

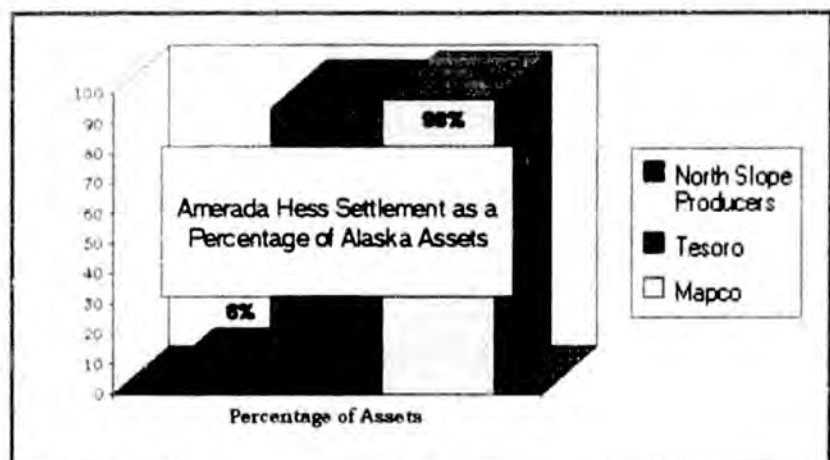


CHART 5 <sup>6/</sup>

royalty oil policy. Efforts to finance refinery expansion are impeded, or even barred, when a company faces extraordinary liability almost equal to its assets' value.

<sup>6/</sup> Source: For Mapco: Mapco Petroleum, "State of Alaska Royalty Oil Contracts; Retroactive Price Changes; "A Challenge...With Practical and Fair Solutions" (1992); For Tesoro: comparison of state's reported value of settlement against current assessed valuation.

Another potential adverse impact of these claims may be increased fuel prices throughout most of Alaska. A recent Mapco study indicates that variations in crude prices account for about 80% of all variations in wholesale product prices. Chart 6.

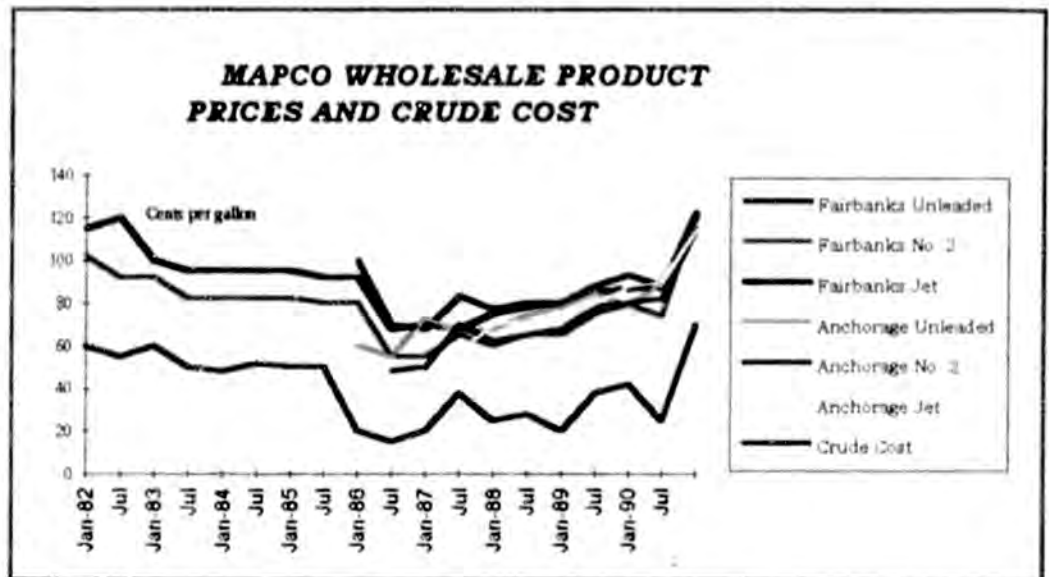


CHART 6

The sums now demanded by the state will be a cost of crude to the refiners, and there is no realistic mechanism available to recoup any *Amerada Hess* surcharges against customers who purchased the products that the state now claims were sold too cheaply. The unknown here is the extent to which the market will allow the in-state refiners to recover the surcharge costs through higher future product prices. The irony is that the intense competitiveness that the state has fostered through its royalty oil policy now threatens to work against the very businesses the state once encouraged, by forcing them to absorb a material part of these surcharges.

And if that occurs, the state could face the ultimate adverse consequence of its position. When Chevron's Nikiski refinery closed in 1991 for economic reasons, 22 Alaskans were unemployed; the Kenai Peninsula Borough lost considerable property tax revenues; the state lost considerable revenues through lost corporate income taxes; and the spinoff effects of that closure continue to reverberate throughout Southcentral Alaska.

In short:

***Whether the impacts of the state's claims manifest themselves in inability to expand refinery capacity; higher fuel prices or refiner insolvency, the result will be the same--state royalty oil policy will have undone itself.***

***IV. SB 134 and HB 185 would allow the state to earn full value on its Amerada Hess claims without risking the continued health of the state's refining industry***

The achievement of energy self-sufficiency through the state's refining industry has been one of Alaska's most impressive triumphs resulting from the discovery of oil in our state. And as we have just seen, the state's proposed retroactive price increases threaten to imperil those gains. If that were to happen, we would not have left to future Alaskans the kind of legacy from our discovery of oil that we had hoped.

SB 134 rejects the extremes of either zealous prosecution of full cash payment, or forgiveness. <sup>7/</sup> Rather, it tries to continue the business relationship between the state and the industry that, to this juncture, has proven so mutually beneficial. It does so by allowing the claims against in-state refiners for retroactive royalty oil price increases to be invested in the Alaska economy in a carefully targeted manner--one calculated to ensure that the considerable public benefits of

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<sup>7/</sup> SB 134 and HB 185 are identical companion bills. For brevity's sake, the legislation is referred to here only as "SB 134."

energy self-sufficiency continue to be enjoyed by Alaskans well into the 21st century.

The legislation allows royalty oil purchasers to credit the cost of future capital investment in Alaska against "liquidated purchase arrearage claims." That phrase is defined to mean claims for retroactive royalty oil price increases, the amount of which has been fixed either by a court judgment, a settlement agreement between the state and the purchaser, or a contract that resolves the claim.

As we'll see in Section VI, granting tax or liability credits for new investment is an historically proven tool for encouraging economic growth. Unlike its prior precedents, however, SB 134 incorporates special safeguards to ensure that the program earns a sound return on the public's investment. For example:

- The Commissioner of Commerce and Economic Development will disapprove any proposed credit that will not yield economic benefits to the state commensurate with the amount of the credit. This case-by-case cost/benefit analysis is unprecedented in credit legislation, and is intended to ensure that the legislation is administered as an investment program, and not simply a special interest grant;
- The credits must be taken within a finite period--10 years, or the period of any settlement agreement--to ensure that Alaska's economy benefits from the program in the short run; and
- To ensure that credits are granted as an incentive for economic activity that might otherwise not occur, credits cannot be taken for investments already committed to, or investments (like pollution control equipment) that may be required by law.

In short, SB 134 seeks to put the state's claims for retroactive price increases against its royalty oil purchasers to immediate productive public use,

creating jobs, new tax revenues and economic stimulus exceeding the cost of the credit itself.

The next section of this paper describes the magnitude of the state's potential return on investment through SB 134.

***V. Available evidence indicates that the state could expect an exceptional return from its investment through SB 134***

Tesoro has explored the possibility of adding new vacuum and asphalt units to its Kenai refinery, increasing its throughput capacity by 15,000 bbl./day. It is precisely the kind of investment that the state has long encouraged its in-state refiners to make--one that would allow it to keep pace with increasing consumer demand.

It is a considerable undertaking--\$46.5 million in capital investment. And, burdened with an extraordinary settlement liability to the state payable over 10 years, the prospects of Tesoro's obtaining conventional financing for the project are poor.

On Tesoro's behalf, the economic firm of ECO Northwest performed a study of the return to Alaskans from that investment. The results demonstrate that, if SB 134 were enacted, and its credit provisions allowed Tesoro to undertake the expansion, the increased tax revenues alone (to the state and the Kenai Borough) would exceed the amount of the credit, and with the addition of direct economic benefits, would dwarf the amount of that credit. Chart 7 sets out the results of that study graphically:

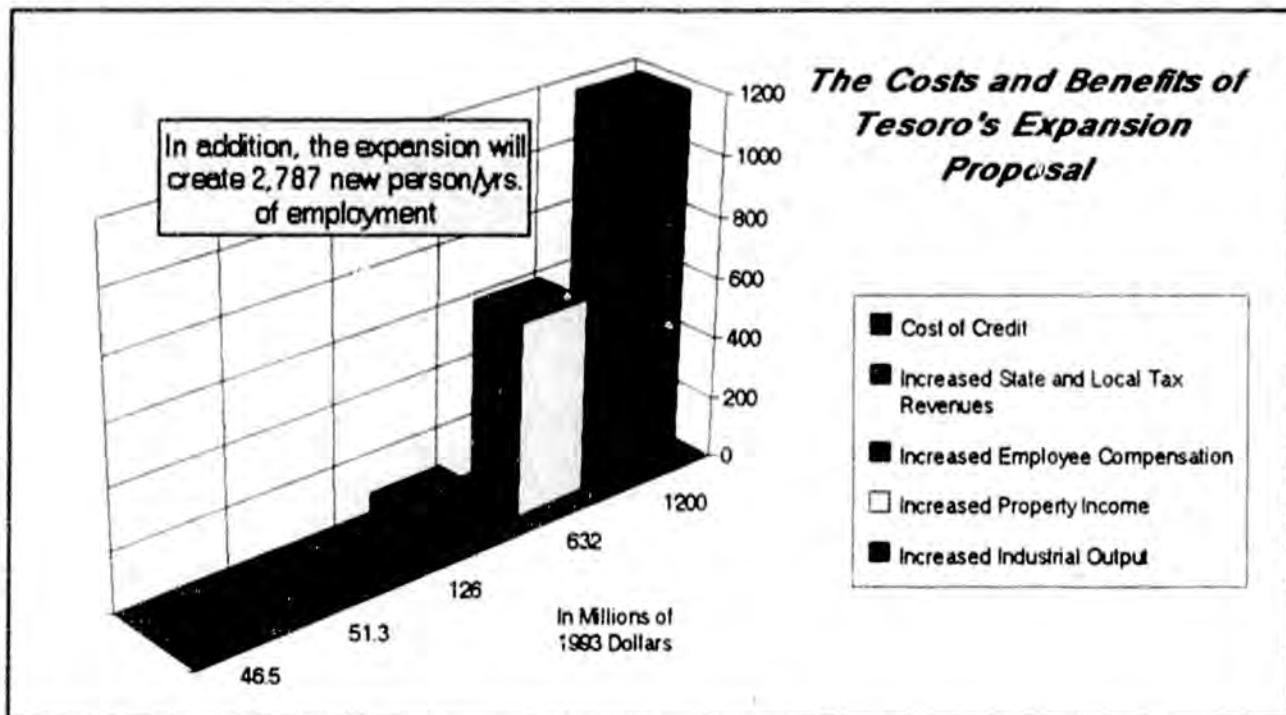


CHART 7. Source: ECO Northwest report, Appendix A.

The detailed executive summary of the ECO Northwest report is included as Appendix A to this paper. And there is nothing unique about the Tesoro proposal--investment in hard value-added assets can generally be expected to generate returns in healthy excess of the cost of investment.

Thus, viewed entirely from an economic perspective, SB 134 is an excellent investment and good public policy.

***VI. SB 134 is backed by ample precedent, and is consistent with long-established public policy***

The core purpose of government is to promote the well-being of the governed, and the ways in which government may act to achieve that purpose are virtually limitless, constrained only by organic restrictions <sup>8/</sup> on its powers, and by the creativity of the governing body.

<sup>8/</sup> "Organic restrictions" meaning, in the context of state action, those limitations imposed by the U.S. Constitution or the Alaska Constitution. The principal restrictions relevant to the legislation presently under consideration are probably the "Public Purpose" and "Special Legislation" clauses of the Alaska Constitution. Those clauses are discussed in the next section of this paper.

It's not the intent of this paper to offer a comprehensive catalogue of the many ways in which Alaska has spent or foregone money in order to stimulate its economy. The point here is only to put SB 134 in perspective. From power cost equalization in rural Alaska to highway funds and business loans in Anchorage, state government is properly in the business of aiding its economy, and that aid will often be targeted at quite discrete commercial sectors. In every case, the rationale is the same--the investment will yield a proper return to the public.

That's true whether the program involves expending state funds in support of a particular industry, or offering to credit obligations if that industry will invest in the state. With respect to the former, our statute books are rich with loan, grant and incentive programs that often directly inure to the benefit of a single industry, or a single business. <sup>9/</sup> Individual appropriations are frequently made in direct aid of even specific private ventures, when the legislature concludes that the public benefits of the investment outweigh its cost, and the examples here are simply too numerous to list completely. See 1984 *Inf. Op. Atty Gen.* (Sept. 13; 366-127-85) (review of appropriation for studies related to the Red Dog mine); 1992 *Inf. Op. Atty. Gen.* (April 10; 663-92-0379) (reviewing a \$1.2 million appropriation in aid of an Arctic Slope Regional Corporation coal project); and see Section VII and Appendix B, *post*.

In other cases, the legislature has simply decided to forego receipt of certain obligations to the state that would otherwise be payable. The legislature, for example, has provided for the disposal of state land at less than market value

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<sup>9/</sup> The forms of this kind of government support given by the Alaska Legislature over the years are myriad. They include, but are certainly not limited to: direct loans; grants; loan guarantees; tax credits and other concessions; access to revenue bonding; creation of venture capital initiatives (e.g. the former Alaska Renewable Resources Corporation (ARRC), the Alaska Science and Technology Foundation; and AIDEA); and creation and support of specialized financial institutions (e.g., AIDEA, AHFC, and CFAB). Another form of assistance is the creation of entire divisions (such as the Division of Tourism, and ASMI) to assist developing industries.

in order to meet a number of economic and social needs. <sup>10/</sup> Most germane are legislative grants to various taxpayers of credits for the cost of new investments against their state taxes or royalty obligations. The following are examples, by activity, of tax credits allowed by the Alaska Legislature:

1. Fisheries.

- a. former Fisheries Business Tax Credit, AS 43.75.032. Under this credit, businesses could take a credit of up to 50% of their tax liability for new fisheries ventures. In its five years of operation (1987-91), the state allowed **\$68 million** in tax credits under this program. <sup>11/</sup>
- b. Fisheries Business Education Tax Credit, AS 43.75.032; and
- c. Tax Credit for Scholarship Contributions, AS 43.75.032 (effective January 1, 1992).

2. General Business.

- a. Income Tax Education Credit, AS 43.20.014;
- b. Incorporation of general Federal Investment Tax Credit, AS 43.20.021(d);
- c. Special Industrial Incentive Investment Tax Credits, AS 43.20.042. Under this law, taxpayers may take a more generous credit than the general federal credit for new gas processing plants and in-state mineral exploration and development activities.

3. Mining.

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<sup>10/</sup> See AS 38.05.057 (disposing of land at less than market value where land is scarce); AS 38.05.082 (shore fisheries lease rentals to be set at level only to compensate for administrative costs); AS 38.05.940 (25% discount for land acquisition by veterans); AS 38.08 (state homesite program).

<sup>11/</sup> Ak. Dept. of Revenue, SB 27 Position Paper, 2/26/91.

- a. Mining License Tax, AS 43.65.010(a) (person subject to this tax is exempt from paying the tax for the first three and one-half years after starting production); <sup>12/</sup> and
  - b. Mining Business Education Credit, AS 43.65.018.
4. Oil and Gas.
- a. Exploration Incentive Credit, AS 38.05.180(i), allowing a credit for new exploratory wells drilled, based on the footage drilled; <sup>13/</sup>
  - b. Oil and Gas Producer Education Credit, AS 43.55.019;
  - c. Oil and Gas Property Education Credit, AS 43.56.018; and
  - d. Authorization to sell royalty gas at less than market value for utilities purposes, AS 38.05.133(h); and
  - e. Provisions to reduce lease royalties when necessary to prolong the life of the field. AS 38.05.180(j). <sup>14/</sup>

The preceding list is not intended to be exhaustive. Nonetheless, it does make it clear that credits against monetary obligations to the state are accepted mechanisms in Alaska for furthering various social or economic purposes. The credit against royalty oil price increases proposed by SB 134 is, by comparison, extremely appropriate.

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<sup>12/</sup> Although described as an exemption, this provision has the same effect and general purpose as a "credit" against taxes due during a start-up period.

<sup>13/</sup> When authorized in an oil and gas lease, the statute permits the lessee to apply the credit against either taxes payable under AS 43.55 or against royalty and rental payments payable to the state. This credit, in particular, provides a very direct parallel to the credit against retroactive royalty oil price increases proposed by SB 134.

<sup>14/</sup> In addition, throughout much of Alaska's history DNR inserted clauses in state oil and gas leases allowing a 10-year "discovery royalty"--one reducing the royalty from 12 1/2 to 5 percent--for the first production from a new geologic formation.

## **VII. SB 134 is constitutional**

### **A. The "Public Purpose" and "Special Legislation" clauses of the Alaska Constitution**

Appendix B to this paper analyzes SB 134 under Alaska Const., Art. IX, §6 (state funds must be expended for a public purpose) and Alaska Const., Art. II, §19 (prohibiting "local or special act[s] if a general act can be made applicable").

The appendix concludes that, under Alaska case law precedent and the consistent position of the Alaska Department of Law with respect to those provisions, SB 134 offends neither constitutional provision because:

- The legislation serves two "public purposes"--(1) encouraging new capital investment with its attendant direct and indirect economic benefits and tax revenues; and (2) helping ensure continued availability of refined petroleum products at reasonable prices throughout most of the state; and
- SB 134 isn't special or local in nature. It applies to any purchaser of royalty oil statewide, and it is motivated by a matter of common concern to all Alaskans--stimulating the Alaska economy.

### **B. The Permanent Fund and Budget Reserve Clauses**

Alaska Const., Art. IX, §15 provides:

*At least twenty five percent of all mineral lease rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments and bonuses **received** by the State shall be placed in a permanent fund, the principal of which shall be used only for those income-producing investments specifically designated by law as eligible for permanent fund investments.*

Similar, Alaska Const., Art. IX, §17 provides:

*There is established as a separate fund in the State treasury the budget reserve fund. Except for money deposited into the permanent fund under Section 15 of the article, all money **received** by the State after July 1, 1990, as a result of the termination, through settlement or otherwise, of an administrative proceeding or of litigation in a State or federal court involving mineral lease bonuses, rentals, royalties, royalty sale proceeds, federal mineral revenue sharing payments or bonuses, or involving taxes imposed on mineral income, production or property, shall be deposited in the budget reserve fund.*

The question has arisen whether, since at least 25% of any cash received by the state from its claims against the in-state refiners for retroactive royalty price increases would be deposited in the permanent fund, allowing in-state refiners to retire those claims through capital investment credits would violate either of those clauses.

The answer comes from the language of the clauses themselves. The key, and above-highlighted word is "**received**." By their terms, the two clauses impose obligations on the state to deposit funds **received** in a certain manner. They impose no obligation with regard to the stance that the state might take with respect to collection of those funds.

Were it otherwise--were the permanent fund and budget reserve clauses to obligate the state to collect the full amount from all its resource activities so that the fund and reserve might therefore be maximized--then much more than SB 134 would be at risk. For example, the state settled its *Amerada Hess* dispute with the North Slope producers for much less than it felt due through trial. The state forewent money that would have gone to the permanent fund. Did it violate the constitution?

Of course not. In fact, royalty and mineral tax disputes are often settled for less than the amount the state feels due. Other legitimate considerations always enter into the settlement equation, and there is nothing in either clause that

prohibits the state from continuing to factor all those considerations into any mineral settlement.<sup>15/</sup>

### **VIII. Conclusion**

The State of Alaska is an active player in the Alaska economy. And long ago it properly decided to use its North Slope wealth to become even more active--to help shape, through properly tailored investments and incentives, a self-sustaining economic infrastructure that would survive the boom. And nowhere was that policy more successful than in the encouragement of a healthy in-state refining industry.

Why, then, would Alaska want to reverse course, and use its considerable power as owner-state to imperil perhaps the most significant component of the value-added manufacturing base that it tried so hard to create? Surely there is a more creative use of the state's power here than simply to enter the bunkers, and bludgeon sums from this industry virtually equal to its entire Alaska worth. Higher fuel prices, insufficient future refining capacity, and lost jobs are not in anyone's interest. How the state chooses to use its considerable power here will help determine the kind of Alaska that enters the 21st century.

SB 134 is intended to give the state a prudent and creative path through this issue, by using its current claims against its refiners for sound investment, rather than mere submission.

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<sup>15/</sup> There are other, more technical reasons why these two clauses would not preclude the capital credit approach of SB 134. First, while Tesoro has entered into a settlement agreement with DNR, that agreement did not arise out of "an administrative proceeding or litigation," so the budget reserve clause of §17 would not be implicated. Second, most of the \$300 million allegedly due from these refiners is still very much in dispute.

The fundamental reason why these clauses aren't offended, however, lies in recognition of the common-sense fact that they impose **deposit** obligations, and not **collection** obligations.

Appendix A  
ECO Northwest Report

# The Fiscal and Economic Impact of New Vacuum and Asphalt Units at the Kenai Refinery of Tesoro Alaska Petroleum Company

## *Executive Summary*

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## Introduction and Impact Summary

Tesoro Alaska Petroleum Company ("Tesoro") analyzed the addition of a new Vacuum Unit and a new Asphalt Unit at its refinery in Kenai, Alaska. The total cost for developing these new facilities (the "Project") is estimated to be \$46.5 million, assuming construction over the years 1993 and 1994. The subsequent, annual operating costs are estimated to be approximately \$5 million per year. In addition, the new units would permit Tesoro to refine approximately 15,000 additional barrels of oil per day, with a current value of \$82 million per year.

Tesoro has no present plan to go forward with this Project; however Tesoro retained ECO Northwest to analyze the economic and tax revenue impacts of the addition of a project of this magnitude to their Kenai, Alaska, refinery. A special input-output model was constructed for the borough of Kenai Peninsula and the state of Alaska to analyze these impacts. From this modeling exercise, ECO estimates that the Project will have the following effects, in present value terms, on the economy of the state of Alaska:

- Industrial output will increase by \$1.2 billion
- Employment will increase by 2,787 person-years, or the equivalent of approximately 200 permanent jobs
- Employee compensation will increase by \$126 million
- Property income will increase by \$632 million

This activity will, in turn, stimulate significant increases in the tax revenue enjoyed by various governmental jurisdictions. In present value terms, the Project will increase total revenues by \$51.3 million. The sources of these increases are as follows:

- Corporate income taxes will increase by \$21.5 million
- Property tax revenues will increase by \$22.8 million
- Sales tax revenues will increase by \$741 thousand
- Fees collected for regulatory costs, worker's compensation, and unemployment insurance will increase by \$6.3 million.

ECO believes that these impacts represent a conservative estimate of the economic and tax revenue effects of the Project.

### The Modeling Process

ECO employed a special type of input-output modeling in the preparation of these impact estimates called IMPLAN modeling. IMPLAN is a set of computer programs and economic databases that permit estimation of the impacts of large scale projects such as Tesoro Project.

The use of input-output modeling is ideally suited to analysis of the Tesoro Project. The spending associated with the development and operation of the Project will *directly* stimulate output, employment, and personal and corporate income in the sectors affected by that spending. Those sectors, in turn, will *indirectly* stimulate other sectors with which they are linked in the Alaska economy. Finally, consumers and others that enjoy increases in income will *induce* additional economic activity through the spending of their incomes.

Input-output modeling permits tracing these direct, indirect, and induced effects. The IMPLAN modeling system, originally developed for the US Forest Service and other government agencies, is simply a cost-effective way of building an input-output model. ECO built separate models for the Kenai borough economy and the state of Alaska.

### Modeling the Tesoro Project

The engineers at Tesoro and the economists at ECO Northwest first calculated the direct spending impacts of the Tesoro Project, and allocated them to the 528 industrial sectors accommodated by the IMPLAN model. Since the Project would be built over a two-year period, and would operate for approximately 20 years

thereafter, separate spending estimates were made for each of these phases. Spending that was unlikely to be channeled through the Alaska economy was eliminated from the impact analysis. Table 1 displays the spending assumptions, aggregated to eight major industrial sectors.

The Project would have major effects, during its development phase, on the construction, manufacturing, and services sectors. In its operational phase, its primary effect is on the mining sector, because of the expenditures on additional crude petroleum that will be utilized by the new refinery units.

**TABLE 1: SPENDING IMPACTS OF THE TESORO PROJECT, BY SECTOR AND YEAR**

| Industry Sector                     | Year 1<br>(\$000) | Year 2<br>(\$000) | Annual<br>(\$000) |
|-------------------------------------|-------------------|-------------------|-------------------|
| Agriculture, forestry and fisheries | 0                 | 0                 | 0                 |
| Mining                              | 253               | 45                | 82,125            |
| Construction and manufacturing      | 14,916            | 2,632             | 4,967             |
| Transport, comm. and utilities      | 1,413             | 431               | 0                 |
| Wholesale and retail trade          | 0                 | 0                 | 0                 |
| FIRE                                | 66                | 34                | 0                 |
| Services                            | 10,895            | 4,033             | 0                 |
| Government enterprises              | 155               | 128               | 0                 |
| <b>Total, Alaska spending</b>       | <b>27,698</b>     | <b>7,303</b>      | <b>87,092</b>     |
| <b>Total, all spending</b>          | <b>37,711</b>     | <b>8,791</b>      | <b>87,092</b>     |

Source: Tesoro Alaska Petroleum, ECO Northwest

### Estimating Multiplier Effects of the Project

The spending impacts in Table 1 represent the first round, or direct effects of the Project. The size of any indirect, or induced effects depends upon the linkages in the economy. In an economy like Alaska, with relatively little indigenous equipment manufacturing and other heavy industry, some portion of the direct spending on refinery machinery and equipment "leak" out of the state, as purchases are made elsewhere. However, purchases of labor and other services are less likely to be fully dissipated, and generate indirect and induced activity in the Alaska economy.

In addition, the Project is particularly potent in the context of the Alaska economy because it does not come at the expense of

alternative expenditures within the state. Activities such as public infrastructure development or retail or wholesale trade, on the other hand, frequently divert spending from substitute activities or producers. On balance, such spending does not represent net new activity, and impact analysis will tend to overstate impacts. In contrast, in the Tesoro Project, both the development of the Project and the expenditures on operations represent spending that otherwise might not occur, rather than a diversion of spending from other activities.

The IMPLAN models built by ECO permit these effects to be traced throughout the Kenai and Alaska economies. On balance, the Tesoro Project has greater local effect on the Alaska economy than might otherwise be assumed. For each dollar of initial purchase of industrial output, the Project generates an additional 20 to 30 percent of output through indirect and induced effects. This "multiplier" of 1.2 to 1.3 is modest, but consistent with the special circumstances of the Alaska economy.

Job multipliers, which tend to be higher than spending multipliers, are as high as 1.5 —each job created directly by Project spending results in up to 0.5 jobs in other, independent sectors. The direct, indirect, and induced effects on jobs are summarized in Table 2.

**TABLE 2: EFFECTS OF THE PROJECT ON KENAI AND ALASKA JOBS, IN PERSON-YEARS**

| Study Area<br>(for all sectors)                             | Direct<br>Jobs | Indirect<br>Jobs | Induced<br>Jobs | Total Jobs |
|-------------------------------------------------------------|----------------|------------------|-----------------|------------|
| <b>Year 1 of Development Phase</b>                          |                |                  |                 |            |
| Alaska                                                      | 358.78         | 50.00            | 80.49           | 489.33     |
| Kenai                                                       | 233.00         | 33.04            | 53.40           | 319.53     |
| <b>Year 2 of Development Phase</b>                          |                |                  |                 |            |
| Alaska                                                      | 95.14          | 12.83            | 21.13           | 129.10     |
| Kenai                                                       | 55.02          | 8.04             | 12.63           | 75.84      |
| <b>Operating Phase, Annual</b>                              |                |                  |                 |            |
| Alaska                                                      | 114.52         | 31.58            | 28.63           | 174.79     |
| Kenai                                                       | 106.50         | 24.59            | 26.30           | 157.44     |
| Source: ECO Northwest. There may be errors due to rounding. |                |                  |                 |            |

Since the impacts of the Project are spread over a 22-year period (2 years of construction and 20 of operation), it is appropriate to calculate the present value, in 1993 dollars, of the impacts. As argued in the Technical Addendum, the use of a four percent real discount rate, coupled with no imputation of inflation to the annual impacts, represents a conservative means of estimating the present value of the Project impacts. These estimates, calculated separately for Kenai and the entire state of Alaska, are presented in Table 3.

**TABLE 3: ECONOMIC IMPACT SUMMARY, ALASKA AND KENAI, IN PRESENT VALUE**

| Study Area | Total Output (\$m) | Labor Income (\$m) | Property Income (\$m) | Jobs (person-years) |
|------------|--------------------|--------------------|-----------------------|---------------------|
| Alaska     | 1,283.74           | 126.02             | 632.20                | 2,787.26            |
| Kenai      | 1,188.18           | 106.57             | 591.12                | 2,356.56            |

Source: ECO Northwest. The various impacts are discounted at a 4 percent real rate, with no imputation of inflation. The construction phase lasts two years, and the operational life of the Project is 20 years. Dollar values are in 1993 dollars.

As summarized earlier, the Project has significant impacts in Kenai and in the State of Alaska.

### **Estimating the Effects on Tax Revenue**

The economic impact estimates, such as those presented in aggregated form in Table 3, are the basis for estimating the tax revenue effects. ECO constructed a tax module that links the economic impact estimates to the sales, corporate income, property and other taxes and fees levied in Alaska. The outcome of this part of the modeling process, summarized earlier, is presented in somewhat greater detail in Table 4.

The impact of the Project on property and corporate income tax revenues contributes significantly to the \$51.3 million of revenue (in present value terms) generated by the Project. These follow, in turn, from the significant stimulus that the Project provides to personal and business income.

The use of conservative assumptions in constructing the IMPLAN model and the tax module suggest that the revenue calculations in Table 4 are conservative, but realistic estimates of the impact of the Tesoro Project.

**TABLE 4: TAX REVENUES GENERATED BY TESORO  
PROJECT IMPACTS, IN PRESENT VALUE**

| <b>Tax Jurisdiction</b> | <b>Sales Tax<br/>(\$000)</b> | <b>Property<br/>Tax<br/>(\$000)</b> | <b>Corporate<br/>Income<br/>Tax<br/>(\$000)</b> | <b>Regulatory<br/>Cost<br/>Charge<br/>(\$000)</b> | <b>Workers<br/>Comp and<br/>Unemp.<br/>Insurance<br/>(\$000)</b> | <b>Total<br/>All Taxes<br/>(\$000)</b> |
|-------------------------|------------------------------|-------------------------------------|-------------------------------------------------|---------------------------------------------------|------------------------------------------------------------------|----------------------------------------|
| Alaska                  | 68.11                        | 8,339.16                            | 21,486.24                                       | 3,317.17                                          | 3,023.26                                                         | 36,233.94                              |
| Kenai                   | 673.15                       | 14,419.52                           |                                                 |                                                   |                                                                  | 15,092.68                              |
| All                     | 741.26                       | 22,758.68                           | 21,486.24                                       | 3,317.17                                          | 3,023.26                                                         | 51,326.61                              |

Source: ECO Northwest. There may be errors due to rounding. "Alaska" refers to Alaska other than the Borough of Kenai Peninsula area. The various impacts are discounted at a 4 percent real rate, with no imputation of inflation. The construction phase lasts two years, and the operational life of the Project is 20 years. Dollar values are in 1993 dollars.



***An Analysis of Capital Credit Legislation  
Under the "Public Purpose" and "Special  
Legislation" Clauses of the Alaska  
Constitution***

SB 134 and HB 185 would allow purchasers of state royalty oil to credit against certain retroactive payment assessments the value of new capital facilities constructed in the state. This paper analyzes that legislation under Alaska Const., Art. IX, §6 (state funds must be expended only for "a public purpose") and Alaska Const., Art. II, §19 (prohibiting "local or special act[s] if a general act can be made applicable").

This paper concludes that, under Alaska case law precedent and the consistent position of the Alaska Department of Law with respect to those provisions, the legislation offends neither constitutional constraint:

**First**, the legislation serves two "public purposes"--(1) encouraging new capital investment with its attendant direct and indirect economic benefits and tax revenues; and (2) helping to ensure continued availability of refined petroleum products at reasonable prices throughout much of the state. Legislative findings articulating those purposes should be prepared, and the courts will defer to those findings. The fact that private corporations will also benefit from the legislation does not diminish the significance of the public benefits that flow from it, and is legally irrelevant; and

**Second**, the legislation isn't special or local in nature. It applies to any purchaser of royalty oil statewide, and it is motivated by a matter of common interest to all Alaskans--stimulating the Alaska economy.

## ***I. The Public Purpose Clause***

Alaska Const., Art. IX, §6 provides:

*No tax shall be levied, or appropriation of public money made, or public property transferred, nor shall the public credit be used, except for a public purpose.*

That clause has been applied by the Alaska Supreme Court to a number of statutes; however, in no instance was the law invalidated on this ground. <sup>1/</sup> A good statement of the judiciary's deferential attitude towards this clause appears in Wright v. City of Palmer, 468 P2nd 326, 331 (Alaska 1970):

*The test...is whether the plan is so unreasonable as to transgress the limitations of our constitution. If the plan of action were plainly foolhardy, or if it amounted to the pledging of credit or the giving away of assets without any corresponding discernible benefit, we might be persuaded to strike down the plan.*

Our supreme court has accordingly afforded great deference to the legislature's findings of public purpose, and has indicated that those findings won't be disturbed unless they lack any reasonable basis in fact. DeArmond v. Alaska State Dev. Corp., 376 P2nd 717 (Alaska 1962).

The program created by SB 134 and HB 185 would be available to any purchaser of state royalty oil, of which four have encountered disputes of the type covered by the legislation--Tesoro, Mapco Petroleum, Chevron and Petrostar. In each case, the Alaska Department of Natural Resources has demanded additional payments under their purchase contracts above the price originally paid. The legislation calls these "purchase arrearages," and once that arrearage is "liquidated" (that is, reduced to a sum certain through judgment or settlement), the

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<sup>1/</sup> A good summary of Alaska's public purpose cases can be found in Comtec, Inc. v. Municipality of Anchorage, 710 P2nd 1004, 1005-6 and n. 1 (Alaska 1986); See also Levy, Constitutional Limitations on Appropriations, 11 U.C.L.A.-Alaska L. Rev. 189, 204-5 (1982).

law allows the purchaser to take a credit against that arrearage for new capital investment in Alaska.

There are limits on the credits that may be taken: (1) pre-existing investments don't qualify, nor do investments that must be made in any event because of legal requirements; (2) the credit will be disallowed if it doesn't result in benefits to the public commensurate with the credit taken; and (3) in order to ensure that investment occurs soon, the credit period is limited to 10 years, or the term of the settlement agreement.

The arrearages against which these credits can be taken are, for the most part, one-time windfall claims arising as an indirect result of favorable (to the state) settlement of the *Amerada Hess* litigation (a case not involving these purchasers).

The concept of government-funded incentives aimed at stimulating new economic activity in the state is hardly a new concept--the Alaska Legislature having often recognized that the public benefits of encouraging new economic enterprise may outweigh the costs of providing the requisite inducement. With respect to the capital credit legislation, the firm of ECO Northwest has performed a study of a particular Tesoro investment that would be eligible for a credit--a possible \$46.5 million refinery addition--and estimated the following direct and indirect public benefits that would flow from such an investment:

***Amount of Investment Credit***

*\$46.5 million*

***Resultant Public Benefit <sup>2/</sup>***

*New direct tax revenue to state  
and local governments...\$51.3 million*

*Employment increase...2,787 person/yr.*

*New employee compensation...\$126 million*

*Industrial output increase...\$1.2 billion*

*Property income increase...\$632 million*

In addition, the royalty oil purchasers affected by the legislation currently provide a majority of Alaskans with reasonably-priced refined products, using the royalty oil as feedstock. A retroactive assessment of arrearages against that royalty oil would adversely affect Railbelt energy prices, and resultantly impair the Railbelt economy. Indeed, in a recent Mapco study "Mapco's crude costs were found to explain over 80% of the variation in posted product prices." <sup>3/</sup>

Finally, receiving the revenue from the arrearage instead of allowing an investment credit would not be an unmixed blessing to the public. To the extent the market permitted, the costs of paying the arrearage may be passed on to Alaska consumers in the form of higher fuel prices. Conversely, to the extent that prices couldn't be passed through, Alaska refiners would be forced to absorb the cost--an event which, at a minimum, could impair their ability to expand operations and meet future market demand. Either way, the public would emerge the poorer. The capital credit legislation is intended to provide a third alternative--one allowing the public to benefit from the arrearages allegedly due while avoiding the damaging side-effects of demanding full direct payment.

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<sup>2/</sup> Expressed in 1993 dollars.

<sup>3/</sup> Mapco, *Royalty Oil and Refined Products: Supply and Pricing Impacts*, Sept., 1991 at 7.

The public benefits of the credit legislation, then, are considerable. There are three arguments that might nonetheless be advanced against the legislation; however, as both the courts and the Attorney General have often decided, the legislature here would be within its prerogative to conclude that the public benefits of the proposal outweighed these other considerations.

The possible arguments against the bill are these:

**(A) Private Businesses Will Also Benefit from the Legislation.**

Certainly that's true--any purchaser who takes a credit will see its arrearage balance reduced commensurately. But according to the Attorney General, "whether private entities receive a benefit from an expenditure of public money is not, in our view, the dispositive factor."<sup>4/</sup>

In a number of cases, the Attorney General has upheld appropriations clearly targeted at a specific private business, on the theory that the resultant spinoff benefits to the public gave the grant a "public purpose." In 1984 *Inf. Op. Atty. Gen* (Sept. 13; 366-127-85), the legislature had appropriated funds to the Alaska Industrial Development Authority (AIDA) for the purpose of certain port and road engineering studies. While the port and road would serve regional purposes, the particular transportation project was "inextricably linked to the development of the Red Dog mineral deposits"--a mining venture being undertaken by Cominco, Alaska and NANA Regional Corporation. The state was considering a role in the Red Dog project, through AIDA, which would include financial support for the transportation network.

Despite the private beneficiary of the legislation, the Attorney General found the expenditure was for a public purpose:

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<sup>4/</sup> 1992 *Inf. Op. Atty. Gen.* (April 10; 663-92-0379) at 3, citing *Wright v. City of Palmer*, 468 P2nd 326 and *Suber v. Alaska State Bond Commission*, 414 P2nd 546, 552 (Alaska 1966). The Alaska Supreme Court first reached this same conclusion in *Lien v. City of Ketchikan*, 383 P2nd 721, 722 (1963).

*The appropriation at issue is extended directly to AIDA, yet it is equally clear that expenditure of the funds will indirectly extend a substantial benefit to two private, for-profit corporations, Cominco, Alaska and NANA. Whether or not Cominco, Alaska receives a benefit is not the dispositive factor, however. **The test instead is whether the expenditure will directly enhance the general welfare of the community...**In undertaking this inquiry, substantial deference must be extended to the legislature's finding--as evidenced by the adoption of the appropriation--that the expenditure of public funds to assist in the development of preliminary site information for the DeLong Mountain Transportation Project serves a valid public purpose. AIDA, as would a court upon review of the appropriation, must therefore find that the legislative public purpose finding was arbitrary or without any reasonable basis in fact before concluding that the expenditure constitutes an impermissible expenditure of public funds.*

*Id.* at 2-3. Indeed, added the Attorney General, the intercession of AIDA in the funding process was not critical to the result. A public purpose would still exist, the Attorney General concluded, "[e]ven if the appropriation had been directly extended to Cominco, Alaska." *Id.* at 3.

The same result was reached in 1991 *Inf. Op. Atty. Gen.* (May 7; 661-91-0503), where the Attorney General upheld an appropriation to finance a drinking water filtration system for a privately-owned water utility. And most recently, in 1992 *Inf. Op. Atty. Gen.* (April 10; 663-92-0379), the Attorney General upheld an \$1.2 million appropriation to the North Slope Borough for use in funding a development study of a coal project owned by the Arctic Slope Regional Corporation.<sup>5/</sup> Although acknowledging that the appropriation would "extend a substantial benefit to two private entities, namely, the corporation that owns the mine site and the consulting group performing the study," the Attorney General ruled that the legislature could properly conclude that the regional benefits of facilitating coal-generated electricity nonetheless justified the appropriation:

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<sup>5/</sup> This was, in fact, the third legislative grant for this project--the prior two being for \$2 million, and \$200,000, respectively.

*According to documents accompanying the appropriation, the goal of the Project is to resolve energy problems that persist throughout rural Alaska by providing an abundant, stable-priced energy source, as well as providing long-term, permanent employment opportunities, development of an infrastructure in the region, and potential tax revenues...*

*Id.* at 3. The parallel between this opinion, and the purposes of the capital credit legislation--to foster employment and aid the provision of reasonably-priced energy on a regional basis--should not be missed on the reader.

Occasionally, when there is no discernible public benefit from the appropriation at all, the Attorney General will intervene. That happened, for example, in 1987 *Inf. Op. Atty. Gen.* (March 19; 663-87-0372), where the Attorney General rejected a proposed appropriation to a regional aquaculture association for use as mere investment funds. The idea was that earnings on these funds would be used for salmon enhancement projects in the future; however, there was nothing in law requiring use of those funds for any particular project. The absence of any linkage to particular projects, and the absence of any "guarantee that the funds will eventually be used for a public purpose," were fatal to the proposal.

And, in 1983 *Inf. Op. Atty. Gen.* (July 27; 366-036-84), a Juneau proposal to contribute state grant funds to a private, for-profit corporation to help build a parking garage was invalidated because of the absence of any safeguards designed to ensure that the public benefits received were commensurate with the amount of the city grant.

The capital credit legislation was consciously drafted to avoid both those shortcomings. First, unlike the aquaculture association's earnings, the credit here is linked to specific, concrete investment proposals, the asserted public benefits of which are subject to state review. And, unlike the Juneau parking garage, the state is empowered to disapprove the credit if it won't yield public benefits commensurate with the amount of the credit. The only remaining indictment on

this count, then, is that private businesses will benefit from the legislation--and, as we've seen, that isn't "dispositive." <sup>6/</sup>

**(b) The Public Won't Have Any Ownership Interest in the Facility Built With the Credit.** This particular claim has never troubled the Attorney General. It was specifically dealt with in the context of assisting the ASRC coal project (discussed *ante*). Even though "the borough does not own nor have control over the Project or the mine site," the Attorney General said, the public benefits of coal development justified the appropriation. *Id.* at 3; see also 366-127-85, *supra* (Red Dog Mine assistance); 1983 *Inf. Op. Atty. Gen.* (March 8; J66-463-82) (financial assistance for expansion of private ski area serves a "public purpose"); Lien v. City of Ketchikan, 383 P2nd 721.

**(c) There Isn't An Absolute Causal Link Between the Credit and the Investment--the Investment Might Occur Anyway.** This topic is included because of 1983 *Inf. Op. Atty. Gen.* (March 8, J66-463-82), which invalidated the proposed forgiveness of a loan to a private ski area. There was no public purpose served by the forgiveness, the Attorney General concluded, because the benefit provided by the private corporation--the provision of skiing facilities--had already occurred:

*[T]he behavior for which the money is spent has already occurred. The expenditure of money to 'reward' past behavior is clearly different from the expenditure of money to influence or affect private behavior so as to directly benefit the public.*

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<sup>6/</sup> In the cases and opinions cited above, it's often said that the private benefit should be "indirect," while the corresponding public advantages "direct." Each of the holdings, however, proves that distinction illusory. In the ASRC coal project case, for example, the direct benefits of the appropriation went to the corporation. If any benefits were "indirect," they were the energy and employment benefits that might ultimately flow to regional residents. Precisely the same is true for the Red Dog appropriation.

*Id.* at 2. The opinion, however, went on to uphold future assistance for ski area expansion, since that would plainly "influence or affect" the provision of future benefits.

In the ski area case, it was logically impossible for loan forgiveness to influence the provision of public benefits. Conversely, the Attorney General has never required an absolute certainty that the state-funded incentive be a necessary precondition to provision of future benefits. Obviously, the Attorney General could not know whether the Red Dog Mine or the ASRC coal project might be built anyway, even in the absence of state help. All that was needed was that the incentive appeared to "influence or affect" future investment decisions.

The capital credit legislation is structured to meet that standard by precluding a credit for any pre-existing investment, or for investments that must occur because of legal constraints. These, it should be noted, are safeguards present in neither the Red Dog nor ASRC appropriations. There is thus no court nor Attorney General precedent that could be used to invalidate the capital recovery legislation on this basis.

## **II. The "Special Legislation" Prohibition**

Art II, §19 of the Alaska Constitution provides:

*The Legislature shall pass no local or special act if a general act can be made applicable. Whether a general act can be made applicable shall be subject to judicial determination.*

The clause does not prohibit special legislation. It only prohibits special legislation when there is nothing in the nature of the specific area that justifies a departure from making the legislation applicable to all similar areas. Abrams v. State, 534 P2nd 91, 94 (Alaska 1975) (law creating a new Eagle-Chugiak Borough

held unconstitutional because nothing in the nature of the Eagle River-Chugiak area justified departing from the general law scheme for incorporating a new borough). <sup>7/</sup>

It is hard to fault the capital credit legislation under this clause, because it is not "special"--it applies to any purchaser of royalty oil. It is true that this class is quite small; however, the limited number within the affected class has never been a factor in "special legislation" analysis. In virtually every case in which the "special legislation" indictment has been raised, the legislation, *by its terms*, applied only to a particular geographic area, a particular individual or a particular event. <sup>8/</sup>

It is true that the principal direct public benefits of this "general" law will fall on Southcentral and Interior Alaska--through job creation, economic growth and continued reasonable fuel prices. However, as the Attorney General has often reminded, if the goals themselves are a matter of common interest (here, the common interest in economic growth), the fact that the benefits will flow regionally, rather than to every corner of the state, is irrelevant. 1992 *Inf. Op. Atty. Gen.* (June 8; 883-92-0088) (common goal was enhanced oil spill cleanup; benefits were felt most directly in Prince William Sound); 1986 *Inf. Op. Atty. Gen.* (May 28; 883-86-

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<sup>7/</sup> Conversely, if the subject matter is something that, by definition, can only be acted on specially, then a special law is appropriate. 1985 *Inf. Op. Atty. Gen.* (April 10; 166-337-85) (bill authorizing extension of royalty oil contract was addressed only to one particular contract, so "special" legislation was plainly required); see also *Boucher v. Engstrom*, 528 P2nd 456 (Alaska 1974). In that event, the only remaining test under the clause is whether the special treatment given in the legislation is "reasonably related to a matter of common interest to the whole state." *Abrams v. State*, 534 P2nd at 94. The Attorney General has been quite reluctant to substitute his views on what is a "common interest" to Alaskans--stopping short, for example, of recommending a veto of even legislation specially authorizing local gambling events. 1990 *Inf. Op. Atty. Gen.* (April 17; 883-90-022) (legislation specially authorizing Big Lake Ice Classic not "clearly unconstitutional").

<sup>8/</sup> See 1992 *Inf. Op. Atty. Gen.* (June 8; 883-92-0088) (legislation imposing special oil spill cleanup responsibilities only on Prince William Sound, and on holder of Trans Alaska Pipeline Right-of-Way, was subject to, but survived, "special legislation" analysis); 1986 *Inf. Op. Atty. Gen.* (May 28; 883-86-0104) (legislation relating to reorganization of the debt owed by Delta agricultural projects was geographically limited, but a rational reason existed for disparate treatment).

0104) (common goal was health of agricultural industry; benefits were most directly felt in Delta area).

There are, in fact, relatively few state laws whose direct blessings are spread equally statewide. And accordingly, the fact that the immediate impact of the legislation is limited to even a small geographic area is legally irrelevant. Abrams v. State, 534 P2nd at 94. The "matter of common interest" (see n. 7, *ante*) that must motivate any legislation refers, then, not to the breadth of the legislation's impact, but rather to the legislation's overall goals.

Here, the goal of the capital credit legislation is economic growth and wellbeing--plainly a matter of "common interest" to Alaskans. And even some of the direct, quantifiable impacts of the legislation will fall statewide--such as ECO's projected increase in state corporate income tax revenues from the studied Tesoro investment. Moreover, even to the extent that the benefits of the legislation might be termed only "regional," the regions most directly affected--Southcentral and Interior Alaska--subsume about three-quarters of Alaska's population, and Mapco and Tesoro provide fuel to every region of the state except the Panhandle.

Given that the legislation is thus founded on a "common interest," and that its reach is "general," the "special legislation" clause of the Alaska Constitution really isn't even germane.

### **III. Conclusion**

SB 134 and HB 185 are simply variants of the traditional investment tax credit--the lessening of a governmental obligation in return for the obligee's infusing the foregone debt into the economy. Viewed from that perspective, the legal propriety of the legislation seems apparent. The legislation is motivated by a desire to stimulate the Alaska economy through job creation, wealth generation,

additional tax revenues and reasonably-priced fuel. These are "public purposes," and matters in which all Alaskans have a "common interest."

The wisdom of the legislation, of course, will be debated in the legislative forum. As this paper has shown, however, that debate should proceed unclouded by any *legal* doubts.

We do recommend that the legislature prepare findings explaining the public purposes of the legislation. As the Attorney General has often reminded us, even though both the "public purpose" and "special legislation" clauses are judicially enforceable, it's the legislature that is entrusted with making the judgment call over whether the public benefits of this particular legislation outweigh the private advantages. Explicit findings will memorialize the legislature's conclusions, and those conclusions will be accorded extraordinary deference.

March 1, 1993.

BIRCH, HORTON, BITTNER and CHEROT

Jon K. Tillinghast

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# The Fiscal and Economic Impact of New Vacuum and Asphalt Units at the Kenai Refinery of Tesoro Alaska Petroleum Company

## *Executive Summary*

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## Introduction and Impact Summary

Tesoro Alaska Petroleum Company ("Tesoro") analyzed the addition of a new Vacuum Unit and a new Asphalt Unit at its refinery in Kenai, Alaska. The total cost for developing these new facilities (the "Project") is estimated to be \$46.5 million, assuming construction over the years 1993 and 1994. The subsequent, annual operating costs are estimated to be approximately \$5 million per year. In addition, the new units would permit Tesoro to refine approximately 15,000 additional barrels of oil per day, with a current value of \$82 million per year.

Tesoro has no present plan to go forward with this Project; however Tesoro retained ECO Northwest to analyze the economic and tax revenue impacts of the addition of a project of this magnitude to their Kenai, Alaska, refinery. A special input-output model was constructed for the borough of Kenai Peninsula and the state of Alaska to analyze these impacts. From this modeling exercise, ECO estimates that the Project will have the following effects, in present value terms, on the economy of the state of Alaska:

- Industrial output will increase by \$1.2 billion
- Employment will increase by 2,787 person-years, or the equivalent of approximately 200 permanent jobs
- Employee compensation will increase by \$126 million
- Property income will increase by \$632 million

This activity will, in turn, stimulate significant increases in the tax revenue enjoyed by various governmental jurisdictions. In present value terms, the Project will increase total revenues by \$51.3 million. The sources of these increases are as follows:

- Corporate income taxes will increase by \$21.5 million
- Property tax revenues will increase by \$22.8 million
- Sales tax revenues will increase by \$741 thousand
- Fees collected for regulatory costs, worker's compensation, and unemployment insurance will increase by \$6.3 million.

ECO believes that these impacts represent a conservative estimate of the economic and tax revenue effects of the Project.

### **The Modeling Process**

ECO employed a special type of input-output modeling in the preparation of these impact estimates called IMPLAN modeling. IMPLAN is a set of computer programs and economic databases that permit estimation of the impacts of large scale projects such as Tesoro Project.

The use of input-output modeling is ideally suited to analysis of the Tesoro Project. The spending associated with the development and operation of the Project will *directly* stimulate output, employment, and personal and corporate income in the sectors affected by that spending. Those sectors, in turn, will *indirectly* stimulate other sectors with which they are linked in the Alaska economy. Finally, consumers and others that enjoy increases in income will *induce* additional economic activity through the spending of their incomes.

Input-output modeling permits tracing these direct, indirect, and induced effects. The IMPLAN modeling system, originally developed for the US Forest Service and other government agencies, is simply a cost-effective way of building an input-output model. ECO built separate models for the Kenai borough economy and the state of Alaska.

### **Modeling the Tesoro Project**

The engineers at Tesoro and the economists at ECO Northwest first calculated the direct spending impacts of the Tesoro Project, and allocated them to the 528 industrial sectors accommodated by the IMPLAN model. Since the Project would be built over a two-year period, and would operate for approximately 20 years

thereafter, separate spending estimates were made for each of these phases. Spending that was unlikely to be channeled through the Alaska economy was eliminated from the impact analysis. Table 1 displays the spending assumptions, aggregated to eight major industrial sectors.

The Project would have major effects, during its development phase, on the construction, manufacturing, and services sectors. In its operational phase, its primary effect is on the mining sector, because of the expenditures on additional crude petroleum that will be utilized by the new refinery units.

**TABLE 1: SPENDING IMPACTS OF THE TESORO PROJECT, BY SECTOR AND YEAR**

| Industry Sector                     | Year 1<br>(\$000) | Year 2<br>(\$000) | Annual<br>(\$000) |
|-------------------------------------|-------------------|-------------------|-------------------|
| Agriculture, forestry and fisheries | 0                 | 0                 | 0                 |
| Mining                              | 253               | 45                | 82,125            |
| Construction and manufacturing      | 14,916            | 2,632             | 4,967             |
| Transport, comm. and utilities      | 1,413             | 431               | 0                 |
| Wholesale and retail trade          | 0                 | 0                 | 0                 |
| FIRE                                | 66                | 34                | 0                 |
| Services                            | 10,895            | 4,033             | 0                 |
| Government enterprises              | 155               | 128               | 0                 |
| <b>Total, Alaska spending</b>       | <b>27,698</b>     | <b>7,303</b>      | <b>87,092</b>     |
| <b>Total, all spending</b>          | <b>37,711</b>     | <b>8,791</b>      | <b>87,092</b>     |

Source: Tesoro Alaska Petroleum, ECO Northwest

### Estimating Multiplier Effects of the Project

The spending impacts in Table 1 represent the first round, or direct effects of the Project. The size of any indirect, or induced effects depends upon the linkages in the economy. In an economy like Alaska, with relatively little indigenous equipment manufacturing and other heavy industry, some portion of the direct spending on refinery machinery and equipment "leak" out of the state, as purchases are made elsewhere. However, purchases of labor and other services are less likely to be fully dissipated, and generate indirect and induced activity in the Alaska economy.

In addition, the Project is particularly potent in the context of the Alaska economy because it does not come at the expense of

alternative expenditures within the state. Activities such as public infrastructure development or retail or wholesale trade, on the other hand, frequently divert spending from substitute activities or producers. On balance, such spending does not represent net new activity, and impact analysis will tend to overstate impacts. In contrast, in the Tesoro Project, both the development of the Project and the expenditures on operations represent spending that otherwise might not occur, rather than a diversion of spending from other activities.

The IMPLAN models built by ECO permit these effects to be traced throughout the Kenai and Alaska economies. On balance, the Tesoro Project has greater local effect on the Alaska economy than might otherwise be assumed. For each dollar of initial purchase of industrial output, the Project generates an additional 20 to 30 percent of output through indirect and induced effects. This "multiplier" of 1.2 to 1.3 is modest, but consistent with the special circumstances of the Alaska economy.

Job multipliers, which tend to be higher than spending multipliers, are as high as 1.5 —each job created directly by Project spending results in up to 0.5 jobs in other, independent sectors. The direct, indirect, and induced effects on jobs are summarized in Table 2.

**TABLE 2: EFFECTS OF THE PROJECT ON KENAI AND ALASKA JOBS, IN PERSON-YEARS**

| Study Area<br>(for all sectors)                             | Direct<br>Jobs | Indirect<br>Jobs | Induced<br>Jobs | Total Jobs |
|-------------------------------------------------------------|----------------|------------------|-----------------|------------|
| <b>Year 1 of Development Phase</b>                          |                |                  |                 |            |
| Alaska                                                      | 358.78         | 50.00            | 80.49           | 489.33     |
| Kenai                                                       | 233.00         | 33.04            | 53.40           | 319.53     |
| <b>Year 2 of Development Phase</b>                          |                |                  |                 |            |
| Alaska                                                      | 95.14          | 12.83            | 21.13           | 129.10     |
| Kenai                                                       | 55.02          | 8.04             | 12.63           | 75.84      |
| <b>Operating Phase, Annual</b>                              |                |                  |                 |            |
| Alaska                                                      | 114.52         | 31.58            | 28.63           | 174.79     |
| Kenai                                                       | 106.50         | 24.59            | 26.30           | 157.44     |
| Source: ECO Northwest. There may be errors due to rounding. |                |                  |                 |            |

Since the impacts of the Project are spread over a 22-year period (2 years of construction and 20 of operation), it is appropriate to calculate the present value, in 1993 dollars, of the impacts. As argued in the Technical Addendum, the use of a four percent real discount rate, coupled with no imputation of inflation to the annual impacts, represents a conservative means of estimating the present value of the Project impacts. These estimates, calculated separately for Kenai and the entire state of Alaska, are presented in Table 3.

**TABLE 3: ECONOMIC IMPACT SUMMARY, ALASKA AND KENAI, IN PRESENT VALUE**

| Study Area | Total Output (\$m) | Labor Income (\$m) | Property Income (\$m) | Jobs (person-years) |
|------------|--------------------|--------------------|-----------------------|---------------------|
| Alaska     | 1,283.74           | 126.02             | 632.20                | 2,787.26            |
| Kenai      | 1,188.18           | 106.57             | 591.12                | 2,356.56            |

Source: ECO Northwest. The various impacts are discounted at a 4 percent real rate, with no imputation of inflation. The construction phase lasts two years, and the operational life of the Project is 20 years. Dollar values are in 1993 dollars.

As summarized earlier, the Project has significant impacts in Kenai and in the State of Alaska.

### **Estimating the Effects on Tax Revenue**

The economic impact estimates, such as those presented in aggregated form in Table 3, are the basis for estimating the tax revenue effects. ECO constructed a tax module that links the economic impact estimates to the sales, corporate income, property and other taxes and fees levied in Alaska. The outcome of this part of the modeling process, summarized earlier, is presented in somewhat greater detail in Table 4.

The impact of the Project on property and corporate income tax revenues contributes significantly to the \$51.3 million of revenue (in present value terms) generated by the Project. These follow, in turn, from the significant stimulus that the Project provides to personal and business income.

The use of conservative assumptions in constructing the IMPLAN model and the tax module suggest that the revenue calculations in Table 4 are conservative, but realistic estimates of the impact of the Tesoro Project.

**TABLE 4: TAX REVENUES GENERATED BY TESORO PROJECT IMPACTS, IN PRESENT VALUE**

| Tax Jurisdiction | Sales Tax (\$000) | Property Tax (\$000) | Corporate Income Tax (\$000) | Regulatory Cost Charge (\$000) | Workers Comp and Unemp. Insurance (\$000) | Total All Taxes (\$000) |
|------------------|-------------------|----------------------|------------------------------|--------------------------------|-------------------------------------------|-------------------------|
| Alaska           | 68.11             | 8,339.96             | 21,486.24                    | 3,317.17                       | 3,023.26                                  | 36,233.94               |
| Kenai            | 673.15            | 14,419.52            |                              |                                |                                           | 15,092.68               |
| All              | 741.26            | 22,758.68            | 21,486.24                    | 3,317.17                       | 3,023.26                                  | 51,326.61               |

Source: ECO Northwest. There may be errors due to rounding. "Alaska" refers to Alaska other than the Borough of Kenai Peninsula area. The various impacts are discounted at a 4 percent real rate, with no imputation of inflation. The construction phase lasts two years, and the operational life of the Project is 20 years. Dollar values are in 1993 dollars.

PROVIDED BY MAPCO  
OTG Committee 3/18/93

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## ROYALTY OIL AND REFINED PRODUCTS :

## SUPPLY AND PRICING IMPACTS

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March 1993

Robert A. Hermes  
Blake T. Eskew

PURVIN & GERTZ, INC.  
Dallas - Houston - London  
Los Angeles - Calgary

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## **KEY CONCLUSIONS**

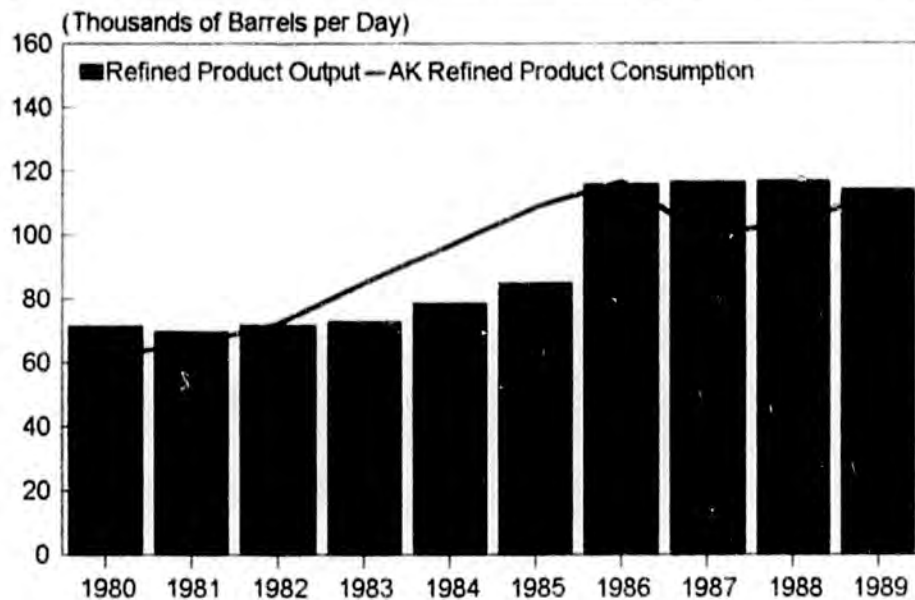
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- **The practice established by the State of Alaska of selling in-kind royalty oil for in-state processing has played a key role in developing a viable in-state refining industry.** As a result, those areas of Alaska served by in-state refineries have enjoyed higher competition and lower prices for refined petroleum products. The only area of the state not supplied by in-state refineries is Southeast Alaska, which still relies on West Coast suppliers for its fuel needs.

The disparity between Southeast fuel prices and prices in the Railbelt is immediately evident. Juneau's consumers, for example, pay a premium averaging 30¢ per gallon over the price paid in Anchorage for gasoline. If the competition brought on by the in-state refineries did not exist and the rest of Alaska were still supplied from outside the state, even if the premium were only 10¢ per gallon, Alaskan consumers would have paid over \$450 million more for gasoline, heating fuel and diesel over the decade of the 1980s.

- **Due to the close relationship between prices of Alaskan crude oil and refined products, any benefits of lower royalty oil prices have been passed on to Alaska's consumers.** If royalty oil prices were lower than they otherwise might have been, refined product prices were also lower. If historical royalty oil prices had been higher, refined product prices would also have been higher.

# ALASKA PETROLEUM CONSUMPTION AND REFINED PRODUCT OUTPUT



## REFINED PRODUCT OUTPUT AND ROYALTY OIL PURCHASES

