(3) Finally, a few words about what I think is the most important aspect of taxation which is available to the State, that is your State income tax.

I think the Legislature, in due course, its certainly not required at this Special Session of the Legislature, must review its legislation to insure that incomes earned in the State are within reach of the State's income taxing power. This does not imply anything about the way you levy income tax, or whether there are any changes, but it does imply that you will scrutinize your income tax legislation very carefully.

In the end the income taxing power of the State is the means by which the State can insure that there is in the future a reasonable partition, or sharing, of what are the ultimate economic benefits of resource production in the State. I'm not only talking about crude oil but I'm talking about what hopefully will be a major exploratory and development program now that lands are beginning to be available for the reopening of leasing operations. Through your income taxing power you have the final means by which the State can decide, but not arbitrarily, never by itself, because its all subject to the essential incentives of investment by private companies in exploration and development. But within these limits the State has a means to participate in a reasonable and equitable way in the benefits that will come from Alaskan resource development.

MILTON
LIPTON
10/22/1973

STATE OF ALASKA
THE LEGISLATURE
LEGISLATIVE AFFAIRS AGENCY

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99801

October 31, 1973

The attached transcript contains the remarks made by Mr. Milton Lipton on October 22, 1973 before the Senate Resources Committee. It is a verbatim transcript of Mr. Lipton's remarks. There is occasionally a word missing or other minor gaps in certain places, which are due to the speaker's testimony being indecipherable at that point. However, it is believed that these occasions are rare and the transcript presents a fair picture of the thoughts expressed by the witness before the committee.

Senator John Sackett
Chairman
Resources Committee

SENATE RESOURCES COMMITTEE

October 22, 1973 Hearing

TESTIMONY OF MR. MILTON LIPTON

The legislation that's directly before you is the Right of Way Leasing Act but before I address myself to that specifically, I would like to say something about the entire package of legislation. It has been stated by industry, of course, that it is a package and they will review whatever decisions come out of the Legislature as a whole. I think it's true even more so for the state than for industry that the whole complex of oil legislation that's before you determines the extent to which the interests of the state are protected or the extent to which the interests of the state are yielded.

I don't want to take too much time on other aspects of it and get to the Right of Way Leasing Act as quickly as possible. So let me start out by saying that, in our opinion, having looked at all the legislation carefully, having listened to a great deal of the testimony that was made before the various committees, we now feel that the pivotal piece of legislation which determines the extent to which any compromise is satisfactory to the interest of the state, is the Alaska Pipeline Commission Act. This is your regulatory bill, a strong bill that was enacted in the 1972 session of the legislature, a bill for which the government and industry have submitted proposed amendments which largely convert what had been intended by the legislature in the first instance as a regulatory bill into an entirely different instrument for

the state, namely a device whereby a commission of the state simply represents the state in hearings before the Interstate Commerce Commission. The amendment to the bill as proposed and as pointed out by Professor Witherspoon yesterday afternoon, in effect, specifically denies (if the amendment is passed) by act of the Alaska legislature any and all jurisdiction which the state of Alaska might in the normal course of events, exercise over pipeline activities in this state, if only a pipeline such as transAlaska subjects itself to or is subjected to the jurisdiction of the ICC.

Now let me explain the reasons for our thinking that this particular act, as it now stands, the Alaska Pipeline Commission, is one of the most important tools available to the state of Alaska in protecting its interest. First of all, the act that's on the books claims very extensive jurisdiction for the pipeline commission which is being established. The jurisdiction extends to various aspects of regulation extensions of services, connections, expansion of capacity, potential abandonments --- so that with respect to these various aspects of pipeline operations the state of Alaska claims jurisdiction for its pipeline commission. Secondly, it vests in this pipeline commission wide authority to pass upon the validity of tariffs which are set by the pipeline. There is no claim made in the existing act, which is on your books, that the state of Alaska can regulate tariffs for the movement of oil in interstate commerce. This falls within the jurisdiction of the ICC. But there will undoubtedly be movement of oil in intrastate commerce, as for example from the northslope

to Fairbanks. There will probably be movement of oil in intrastate commerce from the north slope to Valdez which will remain within the state, for example, if the state should contract to take royalty oil and sell it for a year or two years or five years to the Tesoro Refinery or any other refinery which may be then or in the future be constructed within the state. So the state need only claim jurisdiction over the operations of the pipeline which affect intrastate commerce and jurisdiction over tariffs which involve the movement of oil in intrastate commerce.

Now what's the value of this? Insofar as there may be in the future an issue over the tariff set by the pipeline and this has been pivotal to your deliberations for two years now, insofar as there should be an issue over the tariff, there has really to be two things -- one, a determination as to what the appropriate tariff is, and secondly, a decision by the state as to what it will do to try to enforce what it believes is an appropriate tariff. How does one go about determining what is an appropriate tariff for the pipeline? I don't believe that the legislature in its deliberation is going to want to tackle the job -- that fantastically difficult and complicated job -- of determining what is fair value on a pipeline -- what goes into the capital base and what is not allowed in the capital base, and of what rate of depreciation is appropriate, and everything else --. Or what is a fair return -- this is an incredibly involved problem which the ICC struggles with or avoids by not doing anything about it,

as the case may be. In any case this is really not a problem of the legislature.

But you have established in the existing legislation a pipeline commission which has jurisdiction to determine the fairness and adequacy of tariffs insofar as it involves intrastate commerce. It would do so by holding hearings. If a rate is filed for the intrastate movement of oil, your pipeline commission may accept that rate as it's filed, or it may protest that rate in which case it has administrative processes by which it holds hearings, by which if it renders a decision it must support and justify why that particular decision was issued. And it provides opportunity for the pipeline companies to protest any tariff decision, or any other decision of the pipeline commission, insofar as the pipeline companies believe that it runs counter to due process of law, which means that the administrative decision of your pipeline commission will be tested in your state courts, or if necessary in a federal court.

But if in fact, your own adminitrative and judicial process has come up with a tariff which is lower than the tariff set by the pipeline companies it can be then enforced upon the intrastate movements, and the legislature and the state of Alaska is in a position to expect that the companies will apply an equivalent tariff to interstate movements also. Now that may not be enforced but I put it to you that on the day that it is determined by the state of Alaska, through its administrative and judicial processes, that a tariff is appropriate

for the intrastate movement of oil from the north slope to Valdez -- if on that day the companies refuse to reduce the tariff, which means to increase the well head value on all the oil that moves in interstate commerce, then the problem of the legislature in recapturing the interest of the state is a simple one, at that point you have the taxing power and know exactly at what level and what rate to exercise it, because you have through the instrumentalities of your own legislation already created the means and device by which an appropriate tariff can be determined; by which your own courts will reject the findings of the pipeline commission if they are arbitrary, confiscatory o. capricious, but if administratively and judiciously that tariff is upheld, then the legislature has the guidelines precisely how to go about recapturing the interest in the state through its incontrovertible sovereign powers - that is to say the power of taxation.

It's for this reason that we feel the regulatory bill is absolutely the heart of the entire package. Furthermore, it is our feeling, and here of course it's difficult to speak for companies because, as they said, they would go back and review the whole package, but insofar as the companies feel that there is a claim of jurisdiction by the state which is unconstitutional because it involves interstate commerce or insofar as they feel that there's a decision by your pipeline commission in an area where it has jurisdiction but which decision goes against the law because it violates due process, they always have recourse to the courts. They need not litigate this issue in

advance because the mere fact that this law is on your statute books and I'm referring to the 1972 pipeline commission act, the mere fact that this law is on the statute books does not impose in advance the kind of disabilities upon their intentions to construct the pipeline that will require extensive litigation at this state of the game. Furthermore, as we have pointed out at the previous sessions of the legislature where regulatory bills were before you, there is legislation to this effect on the books of other major producing states and these have never involved extensive constitutional issues so far as we know. Well then, this pipeline commission act we feel is the guts of any compromise which the legislature may wish to substitute in lieu of the compromise package which has been put before you by the executive department.

Now let me pass on then to the Right of Way, but before I do, let me say a few words about the other bills and then come to the guts of the legislation which is before you which is the Right of Way Leasing Act. There are three different tax measures before you and I don't believe that any of them are in any respect crucial to the willingness of the companies to abandoning litigation or to going ahead with the construction of the pipeline. The severance tax, of course is in the course of litigation and it's in course of litigation because the 1972 amendment to your severance tax law contains a royalty credit feature which the companies feel would establish a very unacceptable precedent if it were, first of all applied here, and secondly if it were emulated in other states. I think they're misguided in their concerns; I think the state of Alaska has very little interest, really, in maintaining the

royalty offset provision. It's applied actually by the state of Alaska in a very generous way so that the relatively high cents per barrel tax, which was imposed in your 72 legislation is evaded and reduced by virtue of the royalty credit. You could settle the legal issue in five minutes by repealing the royalty credit and leaving everything else stand, in which case the companies would be subjected to considerably higher taxation than they were previously and that they are in the governor's proposal. So that the removal of the royalty credit feature in your severance tax which the companies are so eager to obtain, we would surely recommend that the legislature give to them. Perhaps the easiest way of doing it is to give it to them by accepting the severance tax amendment which is before you. But I caution one thing: I don't believe that this is the time for the Alaskan legislature to enact a severance tax schedule, whether it's a percent of value at the wellhead or cents per barrel or a combination of both with the idea that what is enacted today is going to be appropriate to whatever the volumes and values of oil may be that are going to be produced in 1977 and 1978. So if you prepare to accept the proposed severance tax amendment as part of a compromise package, I would strongly suggest that it is part of the legislative record in your committee hearings and in your debate that in no sense does this represent a commitment on the part of the legislature that these particular tax rates are the rates which will obtain five and six and seven and eight years from today. We will have time to review that. So that in a sense what you are giving by accepting the proposed amendment to the severance tax is a willingness

on the part of the legislature to avoid extensive litigation on the royalty offset feature which we think is of very little interest to the state of Alaska, in any case.

Now, the severance tax of course is one of your important weapons. I mentioned in previous hearings before this committee and elsewhere, that eventually your income tax is an important thing but that's not up for discussion. It's not an appropriate time for the legislature to review your state income tax legislation although I strongly urge that at one of your sessions you review with your commissioner of revenue your entire concept of corporate income taxation here in the state. The conservation tax bill which is before you, I think is unncessary. We had recommended that the conservation tax which had been on your statute books in the past be eliminated and simply subsumed within your severance tax. It's an added piece of legislation that we don't feel strongly about one way or the other, but it complicates the whole process of paying and collecting monies as between the state and the industry. On the ad valorem tax, as we see it, this is a revenue measure designed largely to yield income to the state over interim years before Prudhoe Bay production begins, before the pipeline is completed. It falls within the province of the legislature to decide how, when and under what conditions it wants to raise that amount of money.

It's the combination then of a strong regulatory bill and the fact that you have continuing flexibility and authority

to tax via your severance tax or eventually through your income tax that we believe yields the greatest control by the state over the operations and the tariff determinations of the pipeline so as to protect the interest of the state.

Now let me get on the Right-of-Way Leasing Bill. We have gone through this bill chapter, book and verse, section, sub-section and paragraph and I think we are prepared to sit down with this committee and other committees of the legislature to discuss it in detail. I don't believe we have time to go through each and every aspect of this here, but I will report on those which we feel are most critical to whatever compromise package comes out. The first issue, as we see it, involving any amendments to the Right-of-Way Leasing Act is how much of the regulatory power that the state wants to exercise shall be done by indirection in the form of stipulations and agreements as conditions of leasing. The industry is challenging the 1972 Right-of-Way Leasing Act in the courts on constitutional grounds, claiming that in effect regulation achieved by indirection which cannot be exercised by the state directly is an illegal exercise of the leasing powers of the state of Alaska. This is one of the major issues under litigation. We obviously are not in a position to pass any judgment whatsoever on the merits of the case in litigation. I think there is a spirit of compromise abroad, I see it very much in the proposals of the Governor's Office, I'm not quite sure I see that much spirit of compromise

in what the companies are proposing in their package, but nevertheless, there is a spirit of compromise abroad and certainly we would feel strongly, and I hope the legislature does also, that it is desirable to avoid unnecessary prolongation of litigation, and the possibility that such continuing litigation may delay the start of construction. So if it is possible to avoid litigation without unduly sapping the legislative enactments that are vital to the state interest, we would feel that there is some merit in the legislature going ahead with the executive departments decision that a compromise is now in order. So on then to the question of the regulatory items which are introduced into the Right-of-Way Leasing Act by virtue of stipulations as a conditions of lease. One, the most important one in our opinion, which is largely eliminated is in section 120 (a) (3) that's the common carrier section. For many reasons it is of importance to this state that it is understood beyond any doubt that the transAlaska pipeline is a common carrier; a common carrier not only for purposes of regulation of interstate oil movements by ICC but a common carrier also for purposes of regulation by your pipeline commission. There is merit, that as a condition of the lease the pipeline stipulates that it is a common carrier period --without reservations, without qualifications, or anything else. Now this is so common, this is so common in state and federal regulation, that it is really surprising to me that any amendment to the existing Right-of-Way Leasing Act should in effect qualify the common carrier status here. It says first of all, that there will be common carrier if the

the commission so determines at the time the lease is issued. I don't think this should require a determination by the commissioner. Under these circumstances the pipeline is a common carrier -- without hearing, without determination, or anything else. Secondly, I don't think it is necessary in the Right-of-Way Leasing Act to stipulate what obligations fall upon a common carrier and certainly not to qualify the obligations incumbent upon a common carrier. 120 (a) (3) says that it will accept, convey, transport without discrimination, crude oil. This is something which will be covered by your pipeline commission in the course of regulation if it is a common carrier. Certainly not in advance to limit the jurisdiction over a common carrier by your own pipeline commission by saying that the imposition of common carrier status does not require the lessee to accept tenders of crude oil, except at points where there exists public, etc. etc. Do not c 'y the obligations of a common carrier. This is a function of your regulatory agency and insofar as your regulatory agency in its individual decision from month to month or year to year may either deny rights to a common carrier or impose obligations upon a common carrier which the pipeline owning companies feel are unduly onerous, they have recourse to the courts. So I don't think that one should qualify the obligations of a common carrier. I think that your 120 (a) (3) should simply stipulate that as a condition of obtaining a right-of-way over state lands, the lease for the right-of-way over state lands, the pipeline carrier itself, submits itself as a common carrier. Not only for the ICC

jurisdictional purposes but for the purposes of the exercise of jurisdiction by your pipeline commission.

120 (a) (4) in the recommended legislation removes the common purchaser provision from your 1972 legislation. At that time it was a permissible feature of your law. In place of the removal of the common purchaser status as a condition of leasing, the Governor has sent down a special bill that would make it possible to establish under certain conditions and subject to certain provisos, common purchaser status for companies owning the transAlaska pipeline. We do not feel now and we felt for a long time that there is real doubt as to how important common purchaser provision is in the state of Alaska, under the conditions where your oil is being produced and transported. Common carrier, yes, because it provides access to transportation and an equitable basis for everybody who is able to achieve production in the new state. Common purchaser for many reasons we have reservations about whether to leave it or not. The bill which is proposed to you we think is a weak and rather attenuated version of a common purchaser act, as it is applied in other states in the United States. Our recommendation at this stage of the game would be that you can afford and should yield the common purchaser provision as a condition of right-of-way leasing and probably simply pass over this special piece of legislation which establishes a common purchaser provision and hold that over to future sessions of the legislature as not being important at this time. When and as common purchaser provisions become meaningful in the conditions of the state of Alaska, at that

time to enact not the legislation that's proposed by the Governor, but a strong common purchaser act which is appropriate to the circumstances at such time. You will have ability and time to do that in the future. I don't think it's an essential point of the compromise, either from the companies' standpoint or from the State's standpoint.

I'm bringing before you here only major things or illustrative aspects of it. 030 - 040 -- these are repealed in the proposed amendment. In the proposed amendment to the Right of Way Leasing Act 1972, section 2 repeals 030-040. Now, 030-040 in the act that is now on the books governs the abandonment of or reduction or impairment of service and temporary emergencies services, and so on. It has to do with the authority that the state claims for itself and buttresses that authority by virtue of this being a condition of the lease. I would think that it might be appropriate, again in the spirit of compromise, that 030 and 040 be retained but that the language be rewritten to say that insofar as these are imposed upon the carrier, that they are in accordance with the jurisdiction and orders of the Interstate Commerce Commission or the Alaska Pipeline Commission, as is appropriate to the case. Which means in effect that the companies, although they are governed by these two clauses, nonetheless know that these two clauses are in accordance -- what is obligatory upon them is in accordance with the regulations that may be promulgated, either by the ICC if it involves interstate commerce or by the Alaska Pipeline Commission if it involves intrastate commerce. I put these out only as illustrative of the

aspects of regulation within the Right of Way Leasing Act which is at issue in the courts -- where we think either the state should stand firm, such as in the matter of common carrier, or where we think the state may very well yield. In general I would think that insofar as the state can achieve a right of way leasing act which avoids litigation but does not give up essential rights which the state still retains through, and I repeat, the combination of a strong regulatory bill and the ultimate enforcement of state regulation through its taxing power, that the legislature can yield on certain of these items in the Right of Way Leasing Act.

This by no means exhausts the regulatory aspects, but in the interest of time I want to move on to other things and as I said we're prepared to go through section by section with our specific recommendations to you.

The second major issue in the Right of Way Leasing Act is the percentage lease rental formula. There are two different impressions abroad as to the purpose of the percentage lease rental formula. Prof. Witherspoon yesterday afternoon suggested that he looked upon it as a revenue measure for the state. That if, in fact, the value of state lands were to be appreciated by the construction of the pipeline then the state like any other owner of land should be in a position to bargain for a fair share of the value of the land when it is being put to a superior use. I have no quarrel with this in principle; however, our position always has been that the leasing of state lands for pipeline right of way should not be regarded as a revenue device by the state of Alaska. We have always recommended that the interest of the state of Alaska is in the lowest possible cost transporta-

tion and the state of Alaska should not in and of itself undertake measures which inherently tend to increase costs of transportation, insofar as producing operation in the development of Alaska's resources provide the base for state taxation. It should be other than through the rentals of the right of way leasing of state land. So we have always urged the lowest reasonable rental for the commitment of state land to right of way. I would point out, for example, that even private property insofar as it's condemned by eminent domain for public utility or pipeline purposes does not convey even to a private owner any right or any entitlement to the enhanced value of land if it's put to other use. So we would recommend that however one looks at the rental for right of way lease that this not be regarded by the legislature as an aspect of its taxing power or as a means of gaining state revenues. That comes from other taxing devices in the state.

The other aspect of the percentage lease rental provision in the right of way leasing bill was that it was to be looked upon as an alternative -- either pain of paying or inducement to the companies to bring their tariffs down to a level which is compatible with the interests of the state; that is to say, a tariff that is lower than the maximum it might obtain under the ICC rate-making rule, certainly high enough to be rewarding for their investment and their risks but a level which is appropriate to the circumstances of pipeline operation in the state. And insofar as they increased their tariffs above a certain level, they were in effect subjecting themselves to the pains of progressively higher lease rental.

This was the percentage lease rental formula. This is one of the major items under litigation. For very obvious reasons the companies regard this as not only as something which is onerous to their circumstances in the state of Alaska but a precedent that if it were followed could lead to all kinds of things in their operation elsewhere. We have reservations about the effectiveness with which the percentage lease rental formula would operate for its major purpose, that is to say, in and of itself to induce the companies to bring the tariff down. It might for some companies, it might not for others. The extent to which it does for any of them would be largely contingent upon their respective equities in the pipeline as sellers of transportation services and in production as buyers of pipeline transportation services. There is an element of unpredictability in the operation of it. And while it was from the beginning, in our opinion, an imaginative and constructive approach and we're not saying even today that if properly effective it might not be a useful tool in right of way leasing legislation; but in the context of the violent litigation associated with this aspect of the right of way leasing bill, with the chances that continued litigation over this aspect of the bill may delay construction of the line, and on the presumption that what you have is not an emasculative regulatory bill but a strong regulatory bill, then we would feel that the legislature could give on the percentage lease rental and adopt the alternative to it as is proposed in the amendment to the Right of Way Leasing Act of 1972 by the Governor's amendments. Again, I say

that there are questions about how effectively it would operate in practice. Notwithstanding, there might be reasons for the state to hold to its case, to fight through the issue of litigation, if there weren't such a sense of urgency about getting the pipeline built, if there might not be such a large cost to the state in litigating. And whatever is done by way of amending the Right of Way Leasing Act in order to assuage the fears and concerns of the pipeline companies, either because of what it does or the precedent that it sets, I would say that what the legislature may do in terms of amending the Right of Way Leasing Act, in our opinion should be contingent first upon the retention of a strong and effective regulatory bill, that is to say Alaska Pipeline Commission Act. A strong regulatory bill which is backed then also by the state's taxing power and so that although you yield another tool in the entire package of legislation which was designed in 1972 to effect and enforce the state interest, really yielding to industry concerns, you do so here in the interest of avoiding undue litigation and the danger of delay on the pipeline.

The third aspect of the Right of Way Leasing Act to which I'd like to refer is the option to buy a percentage interest in the pipeline. The option to buy a percentage interest in the pipeline. I will not take time now to review the reasons why we have supported the insertion of the option to buy in the 1972 legislation. I think they're fairly familiar and

they've been reviewed I believe in previous sessions of this committee. We still feel that the option to buy a percentage interest is an important feature of right of way leasing. I think that insofar as the companies have allowed the purchase by the state of an interest in the pipeline to appear as a condition of the lease, even in the proposed amendment by the Governor, suggests that it is not a disabling aspect of the legislation from the standpoint of constitutionality of the legislation -- I don't know. But certainly the alternative which appears in the legislation which is section 120 (a) (7), the alternative which is substituted in the proposed legislation in our opinion represents nothing whatsoever for the state.

I think to amend the Right of Way Leasing Act to include the amended 120 (a) (7) would be to retain nothing for the state in this respect. I certainly would not recommend that part of the amendment. An opportunity to negotiate for an equity in the pipeline under highly qualified conditions, means that the state has an opportunity to negotiate when it serves the interests and purpose of the companies, which is really not what is intended in the option to buy as contained in the existing law. We do feel, however, that the legislature should give very serious consideration to the advice laid before it by Mr. Spahr of Standard of Ohio, that the option as it stands in the

legislation today may pose difficulty to the financing, or at least the financing at attractive terms, of the pipeline. Because of the uncertainty in the minds of prospective lenders as to what the capacity of the state as a possible future owner of a share of the pipeline may be to carry out obligations for the debt that is incurred at the time of construction which carries over and then may have to be shouldered by the state if the state buys the pipeline. I can appreciate that concern. But I would like to point out first of all -- and I have said this in general and I like to be very specific -- that there are precedents for this. The illustrations that I have made before various committees of this legislature the last two days, I would like to refer to very specifically here. There is the agreement between a consortium of oil companies called Syncrude and the province of Alberta in Canada which determines the basis upon which they get the lease to produce oil from the Athabasca tar sands and transport that oil via pipeline from Athabasca to Edmonton where the oil would enter into the major pipeline systems that traverse Canada and enter the United States. First of all, this has to do with ownership of the pipeline. This synthetic crude pipeline shall be constructed and owned as to an undivided 80 percent thereof by Her Majesty and/or an entity or entities hereafter formed by Her Majesty.

So that from the start, the province of Alberta is being given 80 percent participation in the pipeline. Now, an eighty percent participation in the pipeline--where is the oil going to come from? The province of Alberta is going to finance its 80 percent share of the pipeline just as a private company would. But how do you finance construction of a pipeline if you are not sure you are going to have the oil to put through? The lessees, and her Majesty, and the respective assignees of any interests in the Syncrude projects will dedicate their respective shares of the Syncrude oil recovered from the project to the Syncrude pipelines. That is to say, where the oil being produced by that project is committed to the pipeline irrespective of the fact that Her Majesty's government, that is to say in the province of Alberta, has 80 percent interest in the pipeline. So the percent of interest in the pipeline is there, the difference, of course, being that the state of Alaska in its Right-of-Way Leasing Act had wanted an option.

Now the issue of an option comes up. In this same agreement between the Syncrude consortium and the province of Alberta, the lessees, the Syncrude group including Exxon through Imperial Oil Canada, Atlantic Richfield (these are familiar names to you), Cities Service, and Gulf Oil--these lessees hereby grant Her Majesty an irrevocable option to acquire an interest in the Syncrude project. This is in the producing operation including the project sites, the leases and rights granted thereby, and all facilities acquired or constructed as part of the Syncrude project, which interest may equal undivided percentage interest of not less than 5 percent and up to and

including 20 percent. The option may be exercised at any time during the period from the date hereof and up to and including that date which is 6 months after the date of start of production or the 31st day of December 1982, whichever is the earliest.

Now as to how this is paid for, the payment by the government of Alberta to the members, the private companies, that make up Syncrude: Such costs shall be computed (in accordance with the accounting manual) on the basis of all of the costs which they, the companies, have incurred up to the date of the exercise of the option and shall include interest compounded annually at 8 percent. No portion of such costs shall be attributed to the reserves of leased substances. The province of Alberta could thus be buying in at what is the investment costs of the company plus the payment of 8 percent interest for all time that is elapsed. An interest in the producing operation of between 5 and 20 percent.

Why do I introduce this? Simply because I'm trying to suggest that there is precedence where the companies are prepared to undertake both to accept government participation in the pipeline and whereby companies are prepared to accept an option for governments to participate in what is essentially private operation. That the financing of this project does not seem to be inhibited whether by the government's participation in the pipeline or by the government's option to acquire an interest even in producing operations. Now I grant you that there is a very significant difference in the capital costs of the two projects. The TransAlaska pipeline will probably involve an aggregate initial investment on the order of ten times as much as the Syncrude operation. But that doesn't mean that

individual bond holders are lending ten times as much money. The problem of the bondholder, whatever the number of dollars, always is what security lies behind; what security is there which insures that the viability of the operation will provide for interest and sinking fund contributions. To get back to the crucial point, if the option is retained in the Right-of Way Leasing Act, the existing legislation may be amended so as to stipulate in advance, first of all, what the basis of compensation will be so that there is clear protection that no member of the Trans Alaska group will in effect suffer deterioration of its capital position by virtue of the exercise of the option by the state. And that in negotiating that option, the commissioner shall be prepared to enter into such stipulations by the state as provides the assurance necessary for the indebtedness that bondholders will be entering into prior to any possible exercise of the state's option. We feel that the right of the option to obtain an equity is a useful aspect of the entire package of legislation which you enacted in 1972. We think there may be a question about the way it is now written, whether or not the companies have as much, what shall I say, protection for their borrowing capacity as they would like to have. This protection can probably be provided both in the legislation where it refers to the terms at which the price will be paid and in the lease negotiation itself where the commissioner is authorized to give certain commitments on the part of the state of Alaska. Existing legislation also requires considerable other steps before an option can ever be exercised, including the positive act by the legislature and a referendum by the people of the

state of Alaska if there is to be debt financing. So I think there can be fair protection all around.

This again, represents in our judgment an approach to the issues which confront the state of Alaska. The issues being, must you continue litigation and risk the fact that prolonged litigation may result in delay in the pipeline? Or must you accept a negotiated package of legislation such as submitted to the legislature by the Governor? Or is there an alternative package of legislation which in your judgment represents the protection of the vital interests of the state of Alaska insofar as resource development and pipeline development is concerned, and probably represents a package which the industry can accept? It may pose uncertainties for industry but insofar as they may be obliged or feel they want to litigate, they need not do it in advance but can start construction of the pipeline and be prepared to litigate specific aspects of it as they become relevant. For example, if your pipeline commission, sometime in the future, issues an order which is deemed to be an unreasonable, in violation of due process, the companies can protest such order in the courts, and upset it if their protest is upheld. I think that what we are suggesting here is in the spirit of the negotiations between the Governor and the companies. It certainly represents a yielding on the part of the legislature, if our recommendations are followed, which go a considerable way to meet the issues posed in litigation by the companies. But I do believe it retains for the state of Alaska in two critical areas--namely the regulatory bill and the ultimate ability to enforce the intentions of regulation by the state's taxing

powers. Plus the retention in the Right-of-Way Leasing Act of certain conditions including the common carrier provision. It means yielding on what had been one of the most provocative and imaginative aspects of the legislation which is percentage lease rental. It means compromise on the option to buy so as to provide certain added protection for the companies. In our judgment, I think that this combination of action by the legislature would secure the interests of the state, and in our judgment (of course we are not in a position to speak for the companies) might not be wholly attractive to the companies, but we would think that they would not litigate to the extent that it would involve delay in the construction of the pipeline.

ARLO TUSSING
10/17/1973

STATE OF ALASKA
THE LEGISLATURE
LEGISLATIVE AFFAIRS AGENCY

POUCH Y STATE CAPITOL
JUNEAU, ALASKA 99801

October 31, 1973

The attached transcript contains the remarks made by Mr. Arlon Tussing on October 17, 1973 before the Senate Resources Committee. It is a verbatim transcript of Mr. Tussing's remarks. There is occasionally a word missing or other minor gaps in certain places, which are due to the speaker's testimony being indecipherable at that point. However, it is believed that these occasions are rare and the transcript presents a fair picture of the thoughts expressed by the witness before the committee.

Senator John Sackett
Chairman
Resources Committee

Memorandum
October 17, 1973 CONFIDENTIAL

To: John Sackett

From: Arlon Tussing

These remarks are based upon a first reading of the pipeline legislation proposed by the Governor and do not reflect any presentation by the administration or other witnesses.

General Remarks

The Legislature should be aware that the Middle East fighting, together with the new price increase imposed by the Persian Gulf nations, have put the State of Alaska in an absolutely invincible bargaining position with respect to the oil companies. The expected profits of the companies from their North Slope holdings have probably doubled over the last year, and will continue to spiral upward as the domestic crude oil deficit grows and with the expected rise in prices of Middle East imports. There is not the slightest possibility that the companies would refuse to build the pipeline because of the State's failure to enact the Governor's legislative package or any part of it. You should also know that Senator Jackson has prepared, and has promised to introduce a bill to nationalize the Trans-Alaska pipeline if

litigation between the State and the companies delays construction. There is no warrant for the State of Alaska to make any economic concessions to the companies at this time; indeed, an opposite approach might well be considered.

The emphasis on economic measures is an important one. Where there are legal flaws in the existing State statutes dealing with pipelines, they ought to be remedied. Where there is even a possibility that such flaws could stand in the way of early pipeline construction, amendments ought to be considered. If there is to be further bargaining between the State and the companies (economic, political or legal), it is important to put the full onus for any postponement of construction on the backs of the companies and not upon State law or upon that popular whipping boy, the courts.

The state stands in two rather distinct legal relationships to the companies which are operating on the North Slope and which propose to build the pipeline. The State is, firstly, the sovereign, with taxing authority and the police power. As such it can tax and regulate oil and gas production and pipelines (to the extent that the latter power over pipelines is not preempted by the federal government), whether they are on State lands, federal lands or private lands. Secondly, the State is the landlord and royalty owner with respect to the producing properties on the North Slope and

the landlord with respect to pipeline rights-of-way across State lands. Different principles govern what the State may and may not do in these two capacities. Although the State as landlord is not necessarily on an equal footing in every respect with (say) a private landlord, it is among other things bound by the sanctity of contracts, including that of oil and gas leases.

The existing right-of-way bill asks for trouble because it confuses the State's two roles and attempts to use the State's sovereign power to achieve for the State as landholder privileges which are not available to other landholders. I do not have the legal expertise to say whether or not the State would prevail in a court test of the existing right-of-way leasing act, but as long as there are more straightforward ways to achieve the State's economic ends - ways that clearly respect the distinction between the State's two kinds of legal personae - there is no reason to resort to complex and novel formulas as laden with legal controversy as is the current law.

An often expressed objective of the original pipeline package was for the State to maintain control of its own destiny and to limit the ability of the major oil companies to control the State's economy and (implicitly) its politics. Many Alaskans would be willing to sacrifice substantial oil and gas revenues to advance this objective. The most

important elements in preventing company domination, however, are (1) an informed population, (2) a high level of integrity and detachment on the part of the State's elected and appointed officials and (3) an expert, professional and well-funded Division of Oil and Gas. The third we now definitely have. The second - integrity and independence of public officials - is probably most important because the information received by the public and the maintenance of an independent analytical and regulatory capacity depend upon it. If the Legislature wants to guarantee its own political independence and that of the State government, it might consider some very tough public disclosure, conflict of interest, and campaign financing statutes.

The Ad Valorem Property Tax

I see no problem with the general principle of an ad valorem tax. The arguments for the State's preemption of taxing authority over this kind of property are compelling, and need not be repeated here. The division of tax revenues between the State and its subdivisions is a purely political question which is outside my terms of reference as a consultant.

One question that might be asked about this proposed legislation is the reason for exempting the so-called intangible drilling and development expenses. This item is made up primarily of the labor employed in drilling of wells and is not different in principle from the labor employed in

building a pipeline or any other structure. These outlays could be valued on a depreciated historical cost basis, on the same principles as other outlays for producing properties. Is the exemption proposed because the companies do not want to disclose their intangible expenses (which get special treatment under federal tax law), or are they just anxious that the principle of treating them like other investment costs never be established anywhere, lest the expensing of intangibles in federal income tax law be jeopardized? In either case the Legislature ought to know the reason and view it on its merits.

Right-of-Way Leasing

My preliminary remarks dealt with some of the objections to using right-of-way leases as a roundabout way --- a hostage, in effect --- to influence the State's combined royalty and tax revenues from oil and gas production. It confuses the State's roles as sovereign and as a quasi-private party to a commercial transaction - roles which ought to be kept distinct for a number of reasons. Whether or not the approach in the present Act would stand up in the courts, it is sufficiently questionable that it ought to be avoided if there are equally effective alternatives that are more conventional or more straightforward. The proposed amendment, however, goes out of its way to abdicate any authority of the State, in either its capacity as sovereign or as landowner, to regulate operation of the pipeline.

Page 4 of my copy of the Governor's proposal was missing, so I cannot refer accurately to sections and subsections on pages 5 to 11. The language of subsection (3) on page 5, which begins, "the imposition of common carrier status does not require . . . ", is not necessary to protect owners and operators from unreasonable and uneconomic demands by shippers, and appears to go far beyond the common law in permitting pipeline operators to evade their common carrier obligations.

Some modification of language or punctuation is necessary to make it clear that the word "which" at the beginning of line 7, page 6, refers to "pipeline" rather than to "lessee."

I shall comment on the common purchaser provisions, which the Governor proposes to remove from the right-of-way leasing act, separately under the heading of common purchasers.

The State's option in existing law to buy 20 percent of the pipeline is probably unworkable in view of the way in which the pipeline is to be organized, financed and owned. Once the line was built, transfer of a share to the State would be extremely complicated and would generate horrendous Lawsuits. The proposed substitute language (subsection 7 on page 7), however, is almost meaningless. Its only force is to establish instances in which the State would not have "an opportunity to negotiate." It is not clear what is the purpose of this provision.

There are still arguable grounds for the State to own a share of the pipeline, both (1) to protect its own royalty and tax interest against tariff manipulations, and (2) to provide a vehicle for shipment of oil by independent producers if the companies operating the pipeline are unwilling or unable to provide transportation on a nondiscriminatory basis. If this is the State's approach, however, the decision ought to be made positively now to buy into the pipeline on a specified proportion, before pipeline construction is started, and this decision ought to be coupled with the necessary organization, bonding authority, etc. to carry out the project. The option to buy in its present form is understandibly objectionable to the companies because of its potential use simply for harrassment.

It ought to be kept in mind that the State does have the ultimate power regardless of this legislation to condemn pipeline property for public purposes (provided it does so subject to law and pays the owners fair compensation), and to operate the pipeline as a state-owned public utility. It is not clear what benefits there would be in state ownership, but its possibility might be as much of a deterrent to abuse of private pipeline ownership as the option in statute to buy a part of the line. I am not sure that there is any point in raising the state ownership issue in any legislative form today, however, unless the State definitely intends to own

and/or operate all or part of the pipeline.

The Production Tax

Collection of a production tax, whether "cents per barrel" or a percentage of wellhead value is unquestionably within the authority of the State. There are no obvious legal difficulties in coupling a minimum cents-per-barrel tax with a proportional or graduated tax above this minimum.

Much higher prices can be expected for crude oil in the near future, and these prices will not be offset by higher development costs or additional exploration risks. The result will be vast windfalls for the operating companies. There is no economic reason the State could not levy a highly progressive severance tax --- one which takes 25, 40 or even 90 percent of wellhead revenues above a given level, for example $4.00 per barrel. I am not proposing such a tax, but in view of the quite successful demands of a similar magnitude by the OPEC countries, it would be surprising if Alaska did not reconsider its oil and gas taxation levels in the context of the new conditions.

One recurring problem with respect to severance taxes (or royalties) levied as a proportion of wellhead value is the valuation of oil or gas at the wellhead, where arms-length sales are lacking or rare. In general, the operators will be carrying their own oil through their own pipeline and selling it to their own refining divisions. In such a case the declared

wellhead value or transfer price is not a real price but is an accounting fiction chosen to minimize the company's consolidated liability for taxes and royalties. Where the sum of production tax and royalty rates is low at the margin, the depletion allowance (which is applicable only to income from production) encourages the integrated companies to take their profits in production rather than in transportation or refining. This tendency means that the companies will declare relatively high wellhead prices, which are in the State's interest.

It is not always in the companies' interest to maximize wellhead values, however. As the sum of royalties and production tax rates is increased, it is increasingly important that wellhead values not be unilaterally set by the companies and uncritically accepted by the State. Recognition of this problem was of course one rationale for the existing right of way leasing law. Some remedy to this situation seems to be available in existing and proposed state law, but the Administration ought to be able to explain carefully and completely how any remedies will or do work, and how the State expects to combat any unrealistically low transfer pricing.

One question that ought to be explored thoroughly is whether it is in the State's interest to imitate federal tax law in every respect --- particularly whether the percentage depletion allowance, the expensing of intangible drilling costs, etc. This Session is not the time for such a new and

complicated issue, but a study Senator Jackson has requested from the Library of Congress in behalf of the U.S. Senate's Energy Study will be the most complete consideration of the tax preferences for oil and gas yet published. This study will be available early in 1974, and will be of considerable value to Alaska's Legislature.

Conservation Tax

There are no apparent problems with the oil and gas regulation and conservation tax. Because its revenue would go into the general fund and is not earmarked for these specific activities, however, the segregation of this tax in a separate bill with a special name is just semantics.

Common Purchasers

The kindest thing to say about this bill is that its provisions will never be used. It does not cope with the problem that created the demand for common purchaser legislation in the first place, and addresses a problem which is unlikely ever to arise. The bill, in essence, forbids a petroleum purchaser to discriminate among sellers. The problem however, is that pipeline owners, by virtue of their monopoly over transportation, are alleged to compel independent producers to sell to them in the field at prices less than the value of their oil. The discrimination at issue is not among sellers, but between the oil of the pipeline owner's affiliate (which is not sold in the field), and that of independents (who must sell in order to dispose of their oil).

The existing law at least recognizes and addresses itself to the real problem though perhaps not effectively.

In any event, a civil penalty of $100 to $1,000 can simply be regarded as a cost of doing business. If the conduct in question would bring a disruptive outsider to heel, it could well be a rewarding investment. If either common carrier or common purchaser legislation is to have any effect, the Legislature ought to consider at least creating (1) a private cause of action for recovery of triple damages, and (2) the possibility of injunctive relief.

Perhaps the problem is one that can never really be solved under a regime of shipper-owned pipelines. Even if common carrier requirements are strictly complied with, it is always cheaper for the pipeline owner to ship an additional barrel of his own oil through his own pipeline than it is for an independent to ship his oil through a pipeline he does not own. The outsider pays the tariff (which is always higher than the cost of shipment) and the owner pays the cost (even though his books say he paid the tariff. He paid it to himself!) So, given equal prices at the downstream end of the pipeline, the pipeline owner can always offer to buy the independent's oil in the field for a better price than the owner can get by selling it at the other end of the pipeline and paying the transportation tariff. If the common carrier requirement can be evaded, of course, the pipeline owner can get by with a

lower price than the independent could have got by selling at the pipeline outlet.

Pipeline Commission Act

Whether the State has concurrent regulatory jurisdiction with the federal government over oil pipelines is a serious legal question, and I am at a loss to know why the Administration would not want this issue to be litigated. If the State lost the case, its remaining authority would be no less than provided in this bill, and might well be greater.

There is no way in which litigation over the regulatory authority of the Pipeline Commission could hold up pipeline construction; it is difficult to conceive of a cause of action the companies could advance until the Commission issued an order which conflicted with federal jurisdiction, and such orders would not commence until the pipeline began operation.

The assertion that new attention in Congress to anti-trust and common carrier problems assures an effective ICC surveillance of pipelines is at best naive.

Concluding Remarks

I want to reemphasize that these are first reactions upon a first reading of the proposed legislation. Despite occasional strong language, my remarks are provisional, and my conclusions may change as I am exposed to advocates of the legislation and have an opportunity to study the proposals

more carefully. There is one conclusion that I do not expect to change, however. These bills need not be considered as an inseparable package; they each ought to be examined on its own merits.

CHARLES SPAHR
10/19/1973

STATE OF ALASKA
THE LEGISLATURE

LEGISLATIVE AFFAIRS AGENCY

POUCH Y | STATE CAPITOL
JUNEAU, ALASKA 99801

October 31, 1973

The attached transcript contains the remarks made by Mr. Charles Spahr on October 19, 1973 before the Senate Resources Committee. It is a verbatim transcript of Mr. Spahr's remarks. There is occasionally a word missing or other minor gaps in certain places, which are due to the speaker's testimony being indecipherable at that point. However, it is believed that these occasions are rare and the transcript presents a fair picture of the thoughts expressed by the witness before the committee.

John O. Sackett

Senator John Sackett
Chairman
Resources Committee

TRANSCRIPT OF SENATE RESOURCES HEARING

October 19, 1973

SPAHR: For the record I should identify myself. As most of you know, I am the Chairman of the Standard Oil Company of Ohio. I have been involved in the oil business all of my working, earning life and am getting to the point where my seniority might entitle me to some respect in my actions and correspondence--in other words, I am getting to feel rather old these days. I feel that in the Committee's best interests, it would behoove me to position myself in the very beginning to answer questions, since I did make a statement this morning of an all encompassing nature, which I believe all of you heard. I believe we can use that as a reference and begin in whatever way you gentlemen would prefer.

SACKETT: Very good. Are there any questions from Committee members? Senator Thomas?

THOMAS: I won't hesitate to jump in now, because I know if I don't it will be about two hours before I get a chance. Mr. Spahr, maybe if I could just preface it by saying that I, at least, and I know a few others also, several years ago were much persuaded by the arguments about the ICC being a paper-tiger really and would not, because of its past performance, really protect our best interests up here. And, what we were fearful of was that the wellhead value would go down to a point

that our taxes would not amount to what they otherwise would and that is one reason, I am sure, that the cents-per-barrel tax came through; but primarily that was my reason, at least, in voting for the right-of-way leasing act--to give us some kind of handle on this thing and hopefully to persuade the owner companies of the pipeline to not recoup their investment as quickly as they could legally under the ICC rulings. And, at the same time we had no assurance that a maximum take would not be made by the companies involved--no assurance that this would not happen--driving down the value of the wellhead. Out of this, I think you can see what my question is--how are we going to be protected against this sort of thing?

SPAHR: Senator Thomas, I will try to be responsive to your concern. At the time you considered these questions and expressed these concerns, all of which are related, circumstances were somewhat different than they are today. I really believe that the things that have happened are one of the bases for your concern of these matters being litigated somewhat. Let me proceed to explain. I refer mainly to the way things are going in the world of oil production and purchasing and the relationship of supply and demand and the effects of all these things on the value of oil. A very decided upward pressure on the price. That prospect was not apparent several years ago when first considering the measures that are now law and your calculations have indicated that then current prices, backing off transportation charges, terminaling charges and all those kinds

of things, allowed for 7% return on the ICC evaluation on the pipeline on a low volume, that the value would be minimal, if existant at all. At that time we tried to point out that we were not interested in producing oil for no profit, just having all our profit given to a pipeline return, but I realize we just weren't very convincing. Let me proceed to the ICC. This morning in the House Resources Meeting, the question about the ICC arose and I think the implication was strong that there was still concern that there might be a paper-tiger. The question posed to me was--what has my company's experience been in working insofar as its transportation operations were concerned under ICC jurisdiction. And, I will give you the same kind of answer as I gave those gentlemen. My company, as far as operating pipelines in the Lower 48--we have one that we own entirely which is rather old now, which connects the tri-state, that is, the Illinois, Indiana and Kentucky oilfields, to our Ohio refinery--was built in 1939. It has connections to other carriers that serve it from more distant fields and it, in turn, has connections at this terminus that allow oil to be moved on to other carriers to destination. So, it is involved in both establishing rates and working out divisions of rate with other carriers, all of which have to be approved by the ICC. It has transported oil for other shippers who were the sole owner. At the same time, we have used pipelines operated by others that parallel and serve this line that I mentioned--Marathon's pipeline being one--various carriers who deliver into central

Illinois being others. We also participate in the Capline Project through our ownership in the Mid-Valley Pipeline. This latter company, Mid-Valley, built a consortium in 1950, connecting the East Texas oil fields to the Ohio refineries and pipelines which originate there. This was owned by the Sun Oil Company and my company in the beginning--we originated the line as we are attempting to share in the origination of this one because we needed the new carrier and a capacity that would be sufficient, and at the right place to satisfy our needs. Later, Gulf became a partial owner. That line operated continuously since 1950--it has served other shippers such as Ashland, other companies that I could name--it goes through the same proceedings in filings its tariffs and getting approval of the ICC as SOHIO Pipe. I could name others--the Colonial Pipeline, a product carrier, is one in which we have an interest, and the Harbor Pipeline is another, on the East Coast, in which we have a small interest. We have other wholly owned interests and much more restricted--restricted in terms of volume--but in all instances we have to file and get approval on our terms--terms of receipt, minimum volumes, conditions under which we receive, we have to specify the carrier's responsibility, the custodial law, the obligation to return it in kind, or substantial kind--and in all these operations, to my recollection, while we have had inquiries for clarification and some suggestions on improvements of our tariffs from the ICC, we have really quite apparently done nothing to trigger their criticism in terms of penalities that might have been applied--in other words, I think

we have conducted our operations well. Now I think our experience is typical of that in the Lower 48. We have used other people's pipelines before and they have used ours. We, or most major companies in the Lower 48, have operated for sometime and have been in transportation operations for sometime and parties to the rather well remembered Madison Consent Decree, which was the basis of establishing the limitatio.. on pipeline earnings and related earnings to a percentage of the valuation. So you have that restriction, and an effective one, to be concerned about in our operation, and, of course, we are subject to the Interstate Commerce Act, which Act carries some interesting penalties among other things, failing to observe the law. The potential difficulty that arises out of malfeasance or misfeasance, or plain bad operation, or illegal operations, are so potentially severe that the ICC, in my view--an operator that has had to work under the jurisdiction--is a very effective regulator. Now, I believe it is a very fair thing for me to add that their concern about their regulation varies almost directly in relation to the size of the facilities, complexity of facilities, they have to be concerned about. A small line operating for a long time with a reliable record of performance gets their attention, but very little concern, let us say. They can easily tell if the tariffs are being developed in accordance with their regulations and if there are differences of any substantial nature from what they expect. Larger lines, such as Capline, which is a still growing line, having capacity added

almost every year, and which has an ultimate potential capacity of around 900,000 barrels a day, being in the state of development and growth, gets more of their attention than do the older, smaller lines. Thus, the operators get more inquiries; but again, the performance requirements have been so well established and the availability of the systems have been so general that the ICC's requirement to police and penalize is not great. Now I have the firm impression, however, that comments about ICC being a paper-tiger, concerns expressed in this State, general concerns expressed in Washington and elsewhere about the possible need of making sure that regulatory effort is good--all are going to have the result of making the Interstate Commerce Commission very, very aware of this pipeline and of the need to inspect, to study, to regulate, and to be sure that we don't do anything that we should not do. That's all a very lengthy way of saying--my own experience with them is that they will do an effective job. And, my belief is that this likelihood, coupled with the provision that we are going to keep our records for Alaskan operations separate from all of our other records--coupled with the willingness I expressed this morning to have our records--my own company's records with respect to Alaska--independently audited, with the auditor one that would be acceptable to the State--ought to give you some substantial assurance that we are going to operate within the law rather than outside it. Now, with respect to costs and tariffs and the value of Prudhoe Bay oil. We now expect to schedule our construction in such a way that the second increment of volume capacity will be available

as soon as the pipeline is done. In other words, we expect to install the stations needed to operate at 1,200,000 barrels a day and have them ready as soon as the line is commissioned. We will have to undergo a short period of commissioning time--it's variously estimated at four to six months, depending upon the weather prevailing at the time we are doing this--when we have to test everything, make sure it works right, fill the line, make sure we have vessels scheduled in Vald to take the oil away, make sure we don't encounter difficulty that would cause the pipeline to shut down and allow the jelling of the oil in severe winter--during which time the--according to Alyeska's operating people, we'll be operating at rates varying from 200,000 to 1,200,000 barrels per day. During that period of commissioning, the average rate's going to be less than 1,200,000, but as soon as it is over, there is nothing that we can visualize that would prevent us from operating practically at the 1,200,000 barrel per day rate. So, we no longer visualize the possibility of an extended period of time going by, like a year, during which low rates where, if the choice were calculated on the basis of a 7% return of low rate, it would go sky-high. We do want to have the privilege and we are counting on having the privilege of establishing our rates in accordance with the ICC limits, but we believe and we think it can be demonstrated by our people, as well as by the State Administration, that the use of tariffs that will allow a return on investment approximating 7% of valuation will not result in a valued oil at the wellhead that would be anywhere close to nothing or nominal. So, the combination of

expected initial volume at a high rate, with the advances and prices of world oil which will effect the value of Alaskan oil are the principal things that I see that tend to completely eliminate the concern that you have. I will try to be more brief on other answers.

SACKETT: Are there other questions? Senator Rader.

RADER: I am interested in the nature of the understanding that you have with the Governor. If we pass a 20 mil tax this session--ad valorem tax--and an additional 5 mils next session, would that be a violation of your understanding with the Governor?

SPAHR: We have absolutely no understanding what the Legislature should, could, or would do in the future. I didn't presume to try and establish that. I feel if I had, the Governor would probably have kicked me out of his office. We simply tried to develop together--after listening to one another, a set of revised laws that would eliminate our concerns by being able to finance and really operate without undue restrictions and regulation. Now we recognize that the State must have revenues to meet its budgetary requirements and it has that power to do this at any time it wishes to, but as I said to the Governor in the very beginning--I believe that a philosophy we could use as a foundation for our discussion which would lead to a negotiation would be this--we recognize that with the State's power, and the realism of its working out tax laws that would provide it with the revenue it needs to do the jobs it wants to do for the State of Alaska. On the other hand, we hope that we can convince the

State as to the needs we must have for relief in the regulatory and financing areas that will allow us to do this job the way the State really wants us to do it with minimal cost and, you might say, with maximum speed. And, if this can be the basis of examination for changes that could be made to the laws about which we have been so concerned, it would seem to us that we should find a way for us to solve our problems, accomplish our objectives, and eliminate the waste of time that is bound to continue to occur by pleading the process through the courts.

RADER: Now if the imposition of a 25 mil ad valorem tax in January would not be a violation of your understanding, would the imposition of that tax now be a violation of your understanding with the Governor?

SPAHR: Well, sir, I really think the imposition of such a tax by you couldn't be conceived to be a violation of the understanding that I have with the Governor; however, the understanding I believe I have with the Governor is that the total content, including the tax amounts of these legislative proposals that are before you now, represents in combine a solution to the problems that we have. And, my understanding is that it represents an adequate taxation base and contemplated take for the part of the State. The Governor understands, and I want to be sure you do too, that if you decide to change this now, then I have the problem of going back to all of the companies involved, whom I have represented here as a spokesman, as well as the obligation of

re-examining from our own point of view, any changes that you make in order to determine whether we want to accept them, or whether we feel it would be best to go ahead and use the facilities of the court. My point is that if you do not choose now to approve what has been put before you, substantially in the way it has been put to you, then we just simply have to take the risk of use of time to find out who wants to do what--whether the lawsuit stays in effect, or whether we can accept what you do. Now, insofar as January is concerned, while it is only a few months away, I think you are no more restricted there than you would be at any other legislative session, which is to say you are not restricted at all; however, I would feel that, frankly, you would be taking advantage of a technicality to move that fast on a change in the tax base--I wouldn't really understand it.

RADER: Our standard maximum in the State is 30% on ad valorem for our subdivisions at this time. If we went to 30 mils right now, you state the reason for the negotiations is so you would not have to go to court and have protracted hearings or for financing. Of course, there would be no court hearing involved in that--nor would that affect your financing, would it? If it was just a matter of our judgment what the fair tax would be?

SPAHR: It's a matter of your judgment, but here you begin to affect the economic considerations of the people involved in this pipeline project, and you bring me to the point where I would like to expand a little bit on what I said in the general

session this morning. While you have a right to do this, it changes our economics. Every participant in TAPS could evaluate it again. Some might conclude that, well--if the tax burdens are going to be this way--they are going to apply to the pipeline this heavily--maybe there is no real incentive to us anymore --they might reason-- to participate in the line so we would like to get out. My conjecture is that this kind of reasoning is very likely to arise among the small owners. Thus, we would be involved in TAPS in a reorganization--a rearrangement of ownership. I think it is fair to say that nobody wants to take any more of this ownership burden, in spite of your thoughts, that you may have had in the past, about the lucrative ownership of the pipeline--nobody wants any more of the burden than they have to take proportionately to the utilization made and so there will have to be some time spent in working out the rearrangement of ownership and investment responsibility and then there would be, as a consequence of that, the disappearance of some if it should take place, a going concern that I would have, and I think would be shared by others, that the elimination of small owners would serve to enhance the curiosity of the Department of Justice about whether or not we are getting involved in something that is a violation of anti-trust laws. We wouldn't be, but it is one thing to feel, you might say honest and pure, and another thing to convince those who might be inclined to think just the opposite of you. So these are the kinds of things that I think would arise out of such an action.

PADER: As I understand it, you are saying that some of the owners, if you raise the tax, might consider it so unprofitable that they would not any longer be interested in participating?

SPAHR: Undesirable--I don't think I said unprofitable. Maybe I did, and if I did I want to correct that.

RADER: Undesirable--unprofitable--aren't you talking about profitability?

SPAHR: Profitability is always related, but you see, every company involved, I think, has the theoretical choice at least, and I think it's a practical choice, of deciding where he is going to put his money for investment. He doesn't have to put it in Alaska in a pipeline when he could put it in a chemical plant, or motel, or invest it at 10% in short-term governments, or there are a lot of things that would perhaps be attractive by comparison, so he might decide that he can rely upon somebody else taking care of his obligation in the pipeline, including perhaps the Federal Government, finally, as I mentioned this morning--let them do it, produce his oil, he won't have to worry about the risk of the pipeline, he won't have to hire lawyers to take care of his obligations, he won't have to do a lot of things that are involved here--he can do the simpler job of making money elsewhere, and rely upon a service provided by somebody else.

RADER: Let me preface my next question with a statement. A lot of us are concerned about the ICC matter, because we view the pipeline as being in the nature of a public utility--a

monopoly, which is different than in the Lower 48. Pipelines have other competive methods, but we have only one exit from the North Slope. It has to go through this pipeline, and if we did consider it in the nature of a public utility, then you would be assured as a public utility is, with a certificate of convenience and necessity, and the rest of it, and under ordinary and standard public utility law, a reasonable return on your investment, and bankers are accustomed to lending money under those circumstances. Don't you think they would finance you if you were under the same constraints?

SPAHR: I doubt it, but let me answer you in a broader context than you posed the question to me--I want to refer to some of your observations. You apparently think there is a difference in the situation you are involved in because there aren't other transportation facilities available to compete with the pipeline. As a practical matter, in the Lower 48 states there are no other transportation facilities that are available to compete either. It is not physically attractive, desirable, or economically feasible to transport oil by truck or by railroad, or by anything other than by pipelines down there. In the normal course of development of pipelines, there aren't duplicate facilities that serve the same source, the same destination, so while this is the first development up here--and it is the biggest one ever--it seems to me that the situation is relatively the same as those operating in the Lower 48--your State situation as well as Texas or anywhere else, so I really don't understand the concern. Now it really isn't a public utility--as public

utilities are defined as I understand them--it's a private business, regulated, serving a limited amount of interested shippers and those who at destination would like to have the oil. And the public as such isn't involved at all, so to regulate us and restrict us and require certificates of convenience and necessity to get in and out, as I see it, would serve no purpose except to be restrictive and ready to provide jobs for others--it wouldn't protect the public--it would severly limit us in the flexibility we would like to exercise as time goes by, but none of us present in the room, for example, may be in the same position to be influenced as we are now. So, that's the objectionable feature to me.

RADER: Of course, you say it is not a public utility, but that may be a question. If we have only one, it's a monopoly situation--everybody has to use it. It has all the earmarks of a public utility where you want only one waterworks, one telephone system, or one power company; we don't want two pipelines, and we don't want alternate methods for economic reasons, ecological reasons, and other reasons, and it's hard for me--and I think others have the same problem here--to think that the public doesn't have an interest in that rate, and what the rates are that other corporate citizens, who are not owners of the pipeline, have to pay to get their oil to market. It is because of our concern in that sense--and again, assuring to you--what if we put you under our Public Service Commission, no owner's forfeiture provisions or anything else--you would be under the same provisions as the Alaska Juneau Light Company or Alaska Pipeline from Kenai on up to Anchorage up north--the same position, same

control, same regulation--that will guarantee a rate of return. They have no trouble financing themselves, its a method of financing that is well known throughout the country--a certificate of convenience of necessity enhances the financability of most utility projects--why wouldn't it operate in the same way for you?

SPAHR: I repeat, this is not a utility project, so I can't see that it would enhance our capabilities at all--I see that I haven't been convincing to you, although I still contend with great conviction, that it would hamper us. I have complete difficulty in understanding your concern since we are regulated by the Interstate Commerce Commission on the one hand, by the Madison Consent Decree on the other, which limits how we can establish our tariffs. We have to make the pipeline available to any and all who meet the tariff requirements--we have to be reasonable in the first place and satisfy the ICC as to the reasonablness. It seems to me that all you are suggesting, frankly, is double regulation which requires more attention to detail, more expense, and in the end less profit, and it seems to me it's less rewarding to you.

RADER: But that's not a reason for not building the pipeline--for double regulation, is it? Isn't there a lot more involved in this than that? Isn't there a great difference in the type of regulation I am talking about and what you are talking about?

SPAHR: Would you mind telling me specifically what you think might be involved? Are you concerned about the profits we will make on the pipeline?

RADER: I think you must make a profit. I want you to make a profit, but I think the public has an interest, aside from that profit, in the same way they have an interest in the profit of the local utility company here. They have a monopoly situation. They are serving the greatest resource we have--there is no other way to extract the resource.

SPAHR: Do you think a return of 7% on the approximate investment involved in the pipeline is unreasonable?

RADER: As I understand it, that could be a 50 or 100% return on your invested equity. We have had testimony from others that that could well be a 100% return on your invested equity.

SPAHR: Alright, now we are getting very much to the point. Our borrowing capacity--anybody's borrowing capacity--is limited finitely, dependent upon the resources we have available to cover the borrowing. If we are going to remain in business, then every investment we make has to be a reasonably constructive one or we ought to take the alternates that are available to us. Therefore, if we are going to be limited severly on the return on the borrowed capital we have to employ up here, we are employing the capital and withdrawing the ability to use it elsewhere for a better rate of return with the rest of our capital employed. If we only use 15% equity up here, we will probably use more elsewhere. We can take advantage of the high borrowing ability up here to finance a project that is very, very costly, which couldn't be financed otherwise if we had to use more equity. This particularly applies to my company and it has very similar appeal to all the rest, so when you are looking at our problems and our finan-

cing and our returns on investment, you have to consider our whole company and its problems. We have to--just to talk about my company a bit more--in addition to building our share of the pipeline, comparing our share of the North Slope, which is rather substantial, we have to buy ships for the Valdez operation --a 120,000 ton ship costs $50 million each at this time-- in order to meet all the requirements and specifications that are designed into it now--we have to revise our refineries in the mid-continent so that they can run Slope crude, whereas they have been running Mid-East crude before--this takes millions of dollars; we have investments in expansion in the market place to make, as well as refining facilities to support them. Because of the very rapid shifting and supply situation in the world we have to commit ourselves to the financing of large capacity tankers of foreign flag nature to bring oil from the foreign lands to this land of ours--we have many, many things to do-- this is multiplied many times by the total industry. It is not remotely possible that we can do all these things with our own funds, and the problems facing the oil companies, as well as other industries in raising adequate amounts of money to do the kinds of things that are projected that we are going to need to do in this country, are nothing short of appaling, so we have to look at what we do in Alaska as part of the total, realizing that we have choices to make if the opportunities in one place aren't as good as in another, and this is why I have said, as strongly as I could say--hopefully without appearing to be combative or unreasonable--that if we cannot have the opportunity to work under ICC regulations with the realibility that I think

they provide for everybody--if we have to be restricted substantially in our earning capacity here--I am one who would much prefer to see somebody else do it. And, I am...

PALMER: You have just said we have to consider the entire situation, not as an isolated case. I think we do, so I think we have to figure the pipeline and its profit--not in its own relationship, but also in relationto the fact that it provides you a means of extracting and marketing the North Slope oil and, therefore, should be a much higher profit than might be gained in many other places, so it is not an end result, but only a means to an end, and can't be considered by itself in isolation.

SPAHR: It's a component of a total and I don't think you can necessarily conclude that its going to enable us to make an unconscionable profit on the oil that would not otherwise be moved. This oil is going to be moved anyway. If we don't build the pipeline, somebody else will. I am confident we will get that oil out of there--sometime.

KERTTULA: John's question wasn't entirely answered...

RADER: I have a couple more if I could follow for just a minute here...

KERTTULA: The answer is you can't earn over 7%--you can earn over 7% on your equity, that is....

SPAHR: Well, you can earn 7% on the evaluation which, in the very beginning, would be an approximation of the total investment

involved. Borrowed money, as well as equity money.

RADER: It is my understanding that it is your position that the TAPS consortium cannot finance this pipeline on a public utility basis--would not want to--is that what you are telling me?

SPAHR: I did not say that it could not be done. I do want you to understand that I think it would be more difficult. I do want you to understand it would be far less attractive to me--I am not talking now about the consortium of the other oil companies because I haven't discussed this problem you are raising with them. We have only discussed feasible solutions we felt we could accept.

RADER: Now if you feel you would not want to build it on a utility basis, with a utility profitability, and if we felt we had to have that sort of a show, would your position then be to favor a Federal line?

SPAHR: My position would be that we would have to go home and re-examine the whole problem by ourselves and with our associates and reach a conclusion and my position is that that will take time. If we have to do it, we will have to do it, but I do feel it is not in the interests of anybody involved to spend time unnecessarily. This may be necessary as a consequence of what you do, but I am trying to say that it poses enough of a different question from any that we have considered that I do not have an answer.

SACKETT: Before anyone asks a question--while we are still on the same subject--I kind of like your idea of a Federal pipeline, built by the Federal government.

SPAHR: That's not my idea! It is a suggestion of a way to solve the problem.

SACKETT: Well, I like the suggestion you made this morning, as another alternative. I would assume that under Federal ownership the regulation would be with the Federal government and that regulation might take care of the same problem we have now, which is the concern over tariffs being charged at the wellhead value. Would you care to comment more on this concept?

SPAHR: The Federal government is another business--the Tennessee Valley Authority being a prime example--anyone who wishes to can evaluate that operation to their full satisfaction and speculate on this one. I don't think it would be a very good solution to ask the Federal government to build the line. I start from the premise that I simply can't accept your concern about the possibility that we are going to milk everybody in sight out of all the money they have for our pipeline service. I am concerned that Federal building of the pipeline would probably be the most expensive way to build it, and that it won't necessarily be the quickest way either, because the profit motive is not there, as it is with us. The desire to minimize the cost is not there, as it is with us. I could cite many, many instances on this latter business. For example, we attempted to persuade the Conference Committee that just brought out the pipeline bill to insert the

word "reasonable" in the phrase that requires us to compensate the government for all its expense in the past, now, or in the future, for investigating the line, inspecting during construction and during operation. We wanted "reasonable" in there so that we would only have to reimburse for reasonable expenses and that the charges might be subject to some examination. We didn't succeed in getting it in there and we have no control over what will be done. And, I don't think--and this is a personal opinion--that those who were responsible for putting that in there in the first place have much concern over what those costs will be. Now I want the pipeline inspected. I want it built well. I don't want trouble out of it, and we are determined we won't have it, but I do think that we need to do just as good a job on planning how to insure its inspection will get the job done well as by the kinds of materials we select. So, I think if the Federal government builds the line it will be more expensive, it will take longer and maybe the problems arising out of operation will be more difficult and time consuming to solve. That's it.

BUTROVICH: Mr. Spahr, you and Senator Rader had quite an exchange on whether the pipeline should be a public utility. Are pipelines public utilities anywhere? Are they handled as public utilities anywhere to your knowledge?

SPAHR: To my knowledge, no crude oil carrier or oil product carrier is treated as a public utility anywhere in the United States, I am not knowledgable about the European countries, although I believe the same to be true over there.

BUTROVICH: If they are not a public utility, then as far as earnings are concerned, if they are not treated as a public utility, you agree then they should not be treated as a public utility for any other reason? Would that be a fair statement?

SPAHR: I think that would be a fair statement. In other words, they shouldn't be protected from competition or anything like that? Yes, that's correct.

BUTROVICH: All embracing--anything--they should not be considered a public utility for...

SPAHR: With a very important exception which I wish to make. The right of eminent domain is an important thing.

BUTROVICH: That is what I was thinking about.

SPAHR: I thought you might be. Railroads have had that right in the past. The pipeline has to -- the pipelines are already regulated in a very effective way, but if they don't have the right of eminent domain, perhaps then they can't be built.

BUTROVICH: Is that inherent or by a specific law?

SPAHR: I am not---is it inherent? I think you will have to ask Mr. Heard, who will be up here soon and who is a lawyer, to comment upon that.

SACKETT: Senator Palmer.

PALMER: Mr. Spahr, you talked earlier about your pipeline operations in the lower states---mentioning some of those. What is the percent profit earned at this time, or for the

recent past years, as calculated under the ICC? We hear about 5% and wondered if that was correct.

SPAHR: Depending upon the abilities to operate at the volumes that were contemplated when the tariff was set, theyhave ranged from 5 to 5-1/2, up to 7 at times.

PALMER: Well, if there is no competition down there, and I felt that was what you said awhile ago, then why are the tariffs....

TAPE TURNED OVER--SOME TESTIMONY MISSED.

SPAHR: ....their geology and the rest of their exploration indicates is available. That's been proven time and again.

PALMER: But given that geology, they can only bid what their economic....(couldn't hear rest of his sentence.)

SPAHR: That's right, but think of the differences that sometimes exist on the bids on the same tract of land because of differing evaluation in any circumstance---they are far more important, I think, than the cost of transportation.

PALMER: If production capacity increases, as we hope it will, markedly, with some of thenew lands up there, a market of course exists, what plans do you have for looping the line?

SPAHR: The plans have not been developed yet. They will be, I think, when it becomes apparent that they are getting close to the time. For example, once the line is built, and operating

at 1,200,000, it will be time, if not before then, to start developing, perfecting the plans for looping. There has been some projecting of looping plans already so that we are aware of what can generally be done, but nothing has been finalized in detail. I don't--I plead with you really to be somewhat confident that the companies are going to be quite timely in planning for that kind of thing.

PALMER: Even if it's not your own oil--even if it is someone else's oil that you will be carrying?

SPAHR: Yes, because among other things, you know, if somebody else discovers oil and puts it to us, and we don't have the capacity, everybody gets prorated and our oil gets backed up, and that gets pretty costly, so we will make the investments alright.

SACKETT: Are there other questions of committee members? Senator Rader.

RADER: On this problem of public utility regulation type of thing. We regulate as a public utility a gas line that exists --a single gas line that crosses the Inlet and serves Anchorage from the Kenai Peninsula--limiting their rate of return. Is that an unusual situation, or an unfair situation in your view?

SPAHR: I am really not competent to talk about that. The Natural Gas Act is quite an act in itself and has quite a lot of influence upon thinking pertaining to gas matters, and I am not as knowledgable about those things as many others are. We are not gas producers in any substantial degree, nor are we gas

transmission operators.

RADER: Part of your pipeline package here is the sale to you of lands with the dock in Valdez and for other facilities, not at a competitive sale. And, of course, we would have to justify that because there was a very substantial broad public interest in the pipeline and in your expeditiously getting that land--that it not be handled with somebody in between, making a very large profit or something like that. It seems to me that if we were to consider you in the light of a public utility; if you had a guaranteed rate of return, and a certificate of public convenience and necessity where you couldn't be competed with by any other consumer facility that it would make it much easier for us to make that land available to you.

SPAHR: Well, let me...I think it has been pointed out up here that we have offered to pay the appraised value of the lands. All those lands we specified that we want, for $10 million or whatever is higher. I think that is public knowledge up here. Our own appraisals of the land indicate that that $10 million is better than twice a realistic appraisal at the present time. So, we felt that we had demonstrated a considerable responsibility in assuring you that even with this deviation from your normal procedure of selling land, that we assured you of substantially more than might otherwise come out of a sale, even with public bidding. So, I think we have handled the problem really.

RADER: I think you are right, but we have the philosophical thing and it's really the public interest in this pipeline is different than other bidders of land and other people we are dealing with. Let me ask you this. We have attempted through our right-of-way leasing thing to increase the right-of-way fees, as your profits increase--as a contractual matter--that is the theory we have proceeded on there. Would it be totally unacceptable to you, or your people, if we entered into an agreement with you as a contractual matter, and instead of that fee schedule that we have in the right-of-way lease, merely that you agreed to submit to public utility--standard public utility--type of regulation with a standard return on invested capital? I mean the whole public utility thing--get away from all this forfeiture stuff.

SPAHR: I dislike it myself. I don't know...I dislike it myself because of the things I have already said and because I don't think it is necessary to protect your interests; however, I cannot speak for the other oil companies involved. This would have to be put to them and they would have to consider it and answer for themselves, either directly or through me. I would be willing to be a conveyor, but that's not a question that is going to be answered in a few hours.

RADER: Let me carry it a little further--you don't really have to worry about ad valorem taxes of 30 mils if you are a public utility and have a guaranteed rate of return which is going to let you pay that 30 mil tax. You have, in a lot of ways, the things you are objecting too and the things you are concerned

participation, much as I dislike some of the features of it, and so on.

CROFT: You indicated that you might encourage others to take a percentage of the present participation. Are there arrangements between the owner companies at this time regarding that?

SPAHR: There is a provision in an agreement that exists among the owner companies that provides for a means of reallocating ownership as the pipeline capacity is enlarged, that provides for their nominating capacity for determination of what the new capacity allocations will be up to 100% and that's all that we have. But this provision was put into the contract because the contract was prepared at a time when the potential of Prudhoe Bay wasn't very definite. People thought they had certain interest in the field, but they weren't sure, and, of course, as it has turned out, there have been differences from expectations.

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END OF TAPE.

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END OF TAPE.

MILLER: My impression from your talk this morning was that basically the eight bills, substantially as written, which would indicate to me that that would include the distribution of the tax within the State of Alaska to local governments and this type of thing, also perhaps may have been part of your agreement with the Governor.

SPAHR: No, that was the Governor's determination. I am only--we agreed we wouldn't fight a 20 mil tax--an all inclusive tax--now by some formula (there is one in there) which would allow for distribution. We are not concerned about that. I don't see how we could possibly be, or should be. I didn't mean to imply that at all.

MILLER: With that particular bill then, perhaps we have more leeway than your talk indicated, and perhaps maybe some of the other bills could be construed the same way.

SPAHR: No, I think you have more leeway than you might have assumed this morning on that 20 mil bill, but I don't think my talk indicated that you would have less than I am indicating to you now. I was talking about the total amount of the tax this morning--if it were changed upward, then the total combination of things which we view as all inter-related would have to be reviewed because the cost would be higher.

MILLER: But I assume...

SPAHR: But, the distribution of the 20 mils, or of any figure, the distribution would be of no concern to us. It is the total that matters.

MILLER: But, that is a rather major portion of that bill that could be altered from the way it was written as far as you are concerned?

SPAHR: Distribution?

MILLER: Yes.

SPAHR: As long as the total doesn't change.

MILLER: Thank you, Mr. Chairman.

SACKETT: Mr. Spahr, Senator Silides has to leave for another meeting and has a question for you.

SILIDES: Mr. Spahr, there seems to be some difference of opinion as to whether you will be required to purchase oil which is brought to you. I was under the impression that you would have the option of buying it and that the prorating would begin only if you did indeed begin, or commence buying such oil.

SPAHR: I think I can straighten that out. I think there is a little confusion on several different facts. If the pipeline is full with oil from Prudhoe Bay put to it by all of the producers up there, including us, and some other oil field is developed and connected to the pipeline, then those producers--let's say they exclude us--have the right to make tenders in accordance with the tariffs. If the pipeline does not have the capacity for handling everything, oil from Prudhoe Bay is going to have to be backed down so that the new producers and the old producers get transportation prorata to their total needs equitably.

SILIDES: Then ycu are indeed a common purchaser?

SPAHR: No, there is no purchasing involved here at all. Now if in this---you see, we are only producers here along with other producers, so we are an owner of oil that we want to ship, along with others who might have bought it or who produced it and, because of a restriction in transportation capacity, we are all restricted from moving all the oil we would like--it's a pro-rata restriction--nobody gets favored. Now, however, if in this field (we are talking about this second field) we choose to go in as a buyer from one producer there; then this proposal requires us to become a common purchaser in that field and to take prorata from everybody, as I understand it. We still could then turn around and find we are restricted as an owner of that purchased oil from moving all that we want to move, because the pipeline doesn't have the capacity.

SILIDES: My basic concern, which I think you have answered, but I want to be sure I understand---if someone connects with you, then you do have to back up the Prudhoe Oil and take oil....

SPAHR: Or provide the additional capacity so that nobody gets on the prorata purchase.

TUSSING: Both this morning and this afternoon you have said that the company could, or would not, go on with construction unless the proposed legislation were adopted, substantially as is. Now these bills contain a very large and complicated selection of propositions, some of which are considerably more important than others to the State and some which are considerably more important than others to the companies. We realize

that you are privileged to speak for the other companies. I think it would be useful to go through the bills and their main disposition and indicate some order of priority; that is, which of these things do you think are really indispensable. Specifically, which of them are things without which you would not go on with construction. Secondly, which are things which would not necessarily be an obstacle to initiating construction, but in the absence of which you would continue to litigate. And, then thirdly, those things which you think would be wise for the State to do and you would urge the State to do, but might not be either an obstacle to construction or a cause of action in a law suit.

SPAHR: If I might respond to you for the moment...this morning I indicated not that the pipeline companies or the oil companies could not or would not proceed with pipeline construction if you alter the legislation. What I tried to say was that if you do alter it substantially, then there will be an element of delay, compared with the situation that will prevail if you do not alter it substantially, because new evaluations of the total affect of the altered legislation will have to be made by everybody concerned, so that each person will be able to make his own individual decision as to whether the changes are acceptable or not. That takes time and the point was that the risk we face, therefore, was time in the very beginning. And the secondary risk, of course, is whether or not the changes made will result in any alteration of the TAPS consortium, etc. I pose those to you as possibilities that I think are real and should not be overlooked. Now, in response to your suggestion

that we ought to go through this legislation bit by bit--I'd like to repeat what I indicated this morning--that in our negotiations with the Governor, we made it clear--as we finally made clear by accepting the results--that we were looking at all of our problems and trying to solve them all as a package and that in our view, what has been presented to you will solve our problems in a way--and we believe from what the Governor said, would solve yours--in a way that would permit us to go ahead and permit you to let us go ahead. Now if you are going to examine these laws bit by bit--we have the people available who will do this with you--but I really don't propose to try to dismember or do surgery to all this stuff. What has been presented to you is something we can buy. If you choose to change it, that will be your decision and then we will look at it.

TUSSING: You are saying then, take it or leave it?

SPAHR: No, I am not really saying that. I am saying that a bit by bit examination with me of this legislation is not going to be productive because I am in no position to bargain with you at this time on alterations to this--speaking for seven oil companies--I do not have that commission and I don't presume to be presumptous about it.

TUSSING: On the same basis, I can't pretend to speak for the committee members, but it seems unrealistic to come in here and expect to get the entire package, every jot and tilt, passed in its form--it's proposed form--and I think it would be worthwhile to pick out some of these things and to ask questions. Which of these things from your own point of view you could not live with.

SPAHR: Well, I have already said, this morning, and I will say it now voluntarily. Any very substantial change in taxes, in regulatory arrangements, is going to require a review on our part and on the part of the other oil companies. I had hoped when I came here that the Legislature would eventually conclude that the total content of the tax package was adequate. Now if you are going to raise some things and lower others so that the consequence for us is about the same, I'd have to predict that that would probably work out, but it would still have to be examined.

TUSSING: May I ask the Chairman here whether he wants to pursue this line of reasoning, because I do think it would be useful to ask specific questions about specific items, but I think that is up to you and whether the other members want to travel along that road.

SACKETT: Since we do have other people available who could probably answer these specific questions....

SPAHR: I doubt that they will be able to answer those...

SACKETT: The people tomorrow?

SPAHR: I doubt that.

SACKETT: Well, obviously they won't be answered, but then perhaps through the Attorney General's office and the Governor's office we may be able to determine exactly the priority....

TUSSING: In that case, let me ask one other question. The circumstances of the world energy picture has changed very radically in the last two years, and particularly in the last two weeks, and one of the consequences of that change is the vastly increased urgency of delivery of Alaskan oil to the Lower 48 markets, and the vastly increased value for that oil to its owners, both the State of Alaska and the operating companies. As far as I know, nobody has done the calculations and revised revenue projections in view of developments in the past two weeks. Perhaps it would not be unreasonable to project dollar values at the wellhead--in fact, values two or three times those that were projected (noise on tape...missed next couple of words)....Interior Department's tax statement 2-1/2 years ago.

SPAHR: I do have reason to believe that your State Administration is diligently working, and constantly, to keep such information updated.

TUSSING: Well, that really is not the point. In view of the immensely greater value and greater urgency of Alaskan oil, doesn't it seem that whatever difficulties or complications, either in financing or in the overall attractiveness of the overall project would be created by existing...(noise on tape--missed next word or two)...difficulties and burdens would be substantially less burdensome and substantially more bearable than there were in the time when the companies initiated their litigation against the State's laws.

SPAHR· I believe when you ask that question you are ignoring the realities of financing choices that holders of money and funds to invest have to make; particularly when those people can reason, as I believe they can, that they have a multiple of choices, all of which will be beneficial if chosen, to the country as well as to the owners of the money.

TUSSING: You think that this is one of the less desirable alternatives that is provided....

SPAHR: Would you say that again?

TUSSING: Well, I think you are implying that Alaska North Slope development and delivery of its oil to market would go down substantially...so substantially in the ranking of desirable investments that this project would no longer be of substantial interest to the government.

SPAHR: On the contrary....a different nuance...I want to remind you, for example, that one of the features of the present legislation is that the State has an option to buy 20% of the pipeline, at a time of its choosing under circumstances where it can negotiate. Now I submit that that option stays in there--in the first place the State is not going to exercise it except under what it considers to be the most opportune time. Now, I would like for this to be understood. When one goes to a prospective lender, and in this case it will be a substantial insurance institution or big pension fund, or something else similar, to propose that they lend us money---we are going to talk to people with substantial funds of knowledge in financing