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HRES

HB

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(FILE 1)

1 I. INTRODUCTION

2 The litigation between the State of Alaska ("State")
3 and Alaska Oil Company ("AOC") arises from AOC's failure to
4 pay approximately \$62.6 million of the full invoiced price
5 for royalty oil purchased by AOC from the State in 1981 and
6 1982. The State has insisted from the beginning of the dis-
7 pute that the price invoiced by the State was calculated in
8 accordance with the contract between the State and AOC, and
9 that the full invoiced price must be paid. But AOC claims
10 that the price invoiced by the State exceeds the "market
11 price" which AOC asserts was agreed to in the contract, and
12 AOC has therefore paid the State a lower price in accordance
13 with AOC's unilateral calculations of the "market value" of
14 the oil.

15 Section II of this memorandum briefly discusses
16 the State's right to and its options for the disposition
17 of royalty oil from Prudhoe Bay. Then, in Section III, the
18 negotiation and amendment of the AOC contract will be con-
19 sidered, and the price terms will be examined. AOC's with-
20 holding from payments to the State, and AOC's claimed reasons
21 for such withholding, are described in Section IV. Finally,
22 in Section V, the ongoing litigation between the State and
23 AOC is reviewed.

24 II. ROYALTY OIL FROM PRUDHOE BAY LEASES

25 During the 1960s, the State sold leasehold interests
26 at Prudhoe Bay to various oil companies. Each lease reserves
27 for the State a one-eighth (12.5%) royalty share, to be taken
28

1 "in kind" or "in value," in any production which might occur
2 after the leases are explored and developed.

3 Under the lease terms, if the State opts to take
4 all or part of its royalty share "inkind," the State takes
5 possession of the royalty oil at Pump Station No. 1 after
6 giving the North Slope Producers six months notice of the
7 volume of oil desired. Traditionally, the State does not
8 take physical custody of the oil, but rather resells it at
9 Pump Station No. 1.

10 Under the "in value" alternative in the Prudhoe Bay
11 leases, the State can receive cash payments from the North
12 Slope Producers for the value of some or all of the State's
13 12.5% of Prudhoe Bay oil. Although in this case the State
14 has no control of how the oil is marketed, the State is em-
15 powered to audit the Producers to insure that proper value is
16 received for the State's royalty oil.

17 Disposition of the royalty oil to which the State
18 is entitled under the Prudhoe Bay leases is governed by AS
19 38.05.182-183. Section 182(a) requires the Commissioner of
20 Natural Resources to take royalty oil "in-kind" unless the
21 Commissioner finds that "in value" taking is in the best
22 interest of the State. Section 183(e) requires the
23 Commissioner to evaluate royalty oil purchase proposals
24 (where sale is other than by competitive bid) in light of,
25 among other things, the cash value offered, the benefits of
26 refining or processing in the State, and the ability of the
27 purchaser to supply refined products in-state with price or
28

1 supply benefits. These statutory directives imply a prefer-
2 ence for taking royalty oil "in kind" rather than "in value,"
3 and a preference for in-state processing over purely export
4 sales.

5 In 1974 the Alaska Legislature established the
6 Alaska Royalty Oil and Gas Development Advisory Board, and
7 invested it with authority to approve or disapprove any
8 royalty oil disposition contracts submitted by the
9 Commissioner of Natural Resources. Under the 1974 legis-
10 lation, proposals for the sale of royalty oil first had to be
11 approved by the Royalty Board, and then submitted to the
12 Alaska Legislature for its concurrence.

13 III. ALPETCO AOC CONTRACT

14 A. Negotiations

15 In the summer of 1977, the Department of Natural
16 Resources formally solicited bids for the sale of the State's
17 royalty oil from Prudhoe Bay. The solicitation required each
18 bid to provide for the use in Alaska of "some or all" of the
19 purchased royalty oil. Concurrently, the Royalty Board supple-
20 mented the existing statutory guidelines with several policies
21 to guide the disposition of the State's royalty oil. Among
22 the policies was the requirement that the price at which the
23 State sold royalty oil should be no less than the amount the
24 State would have received had the State opted for "in value"
25 cash payments from the Producers instead of taking the oil
26 "in kind."

27 Ten preliminary proposals responding to the State's
28 solicitation were received by August 1, 1977. After the

1 Commissioner of Natural Resources evaluated the proposals,
2 the list of bidders was reduced to four companies who sub-
3 mitted final proposed contracts for large-volume purchases of
4 royalty oil. Following intensive negotiations with the final
5 four bidders, on February 22, 1978 the Commissioner signed,
6 and the Royalty Board approved, an Agreement for the Sale and
7 Purchase of State Royalty Oil (the "Contract") between the
8 State and Alaska Petrochemical Company ("APC"). The initial
9 Contract was for a term of 27 years and authorized the pur-
10 chase of up to 150,000 barrels per day of royalty oil for
11 processing in a world-scale petrochemical plant APC agreed to
12 construct in Alaska.

13 B. Amendments to APC Contract

14 The APC Contract was amended twice. The first
15 amendment occurred as a result of the legislative approval
16 process for the initial Contract; changes were mandated by
17 the Legislature in some of the terms of the Contract relating
18 to required expenditures and construction obligations. The
19 amended Contract required Alpecto to expend certain amounts
20 in furtherance of the project at specified intervals, to
21 enter into arrangements for construction and financing by
22 December of 1979. The amended Contract was approved by the
23 Legislature on June 13, 1978.

24 The second amendment stemmed from three events.
25 First, the project sponsors indicated that the petrochemical
26 portion of the project was not immediately feasible, and that
27 the facility constructed would in fact be a refinery (although
28 a highly sophisticated refinery using state of the art technology).

1 Second, the State's determination in December 1979 that Alpetco
2 had met required conditions regarding construction and financing
3 arrangements, entitling them to interim taking of royalty
4 oil, met with substantial public criticism. Third, the owner-
5 ship of the project changed substantially in 1979 when APC
6 assigned its interest in the Contract to the Alpetco Company,
7 which later changed its name to Alaska Oil Company ("AOC").
8 AOC is a general partnership presently consisting of Charter
9 Oil (Alaska) Inc. (85.31%), Valdez Oil, Inc. (8.04%) and
10 Barbour Oil Company (6.65%). Charter Oil (Alaska), Inc. and
11 Valdez Oil, Inc. are both wholly owned subsidiaries of The
12 Charter Company, which therefore has an indirect 93.35% inter-
13 est in AOC.

14 The second amendment, entered into in May 1980,
15 reduced the volume of oil to be purchased by AOC beginning in
16 July 1980 from 150,000 to 75,000 barrels per day. Only when
17 the promised refinery was operational would AOC be permitted
18 to purchase up to 100,000 barrels per day. To ensure that
19 AOC constructed the refinery in an expeditious manner, the
20 amended Contract also required AOC to meet specific project
21 development criteria by December 31, 1981, before the
22 Commissioner would approve further sales of North Slope
23 crude to AOC.

24 c. Contract-Price Provisions

25 The price provisions of the Contract were not
26 altered by either amendment. Since price is at the center of
27 the State's dispute with AOC, the price provisions are des-
28 cribed below in some detail.

1 The State had insisted from the outset that the
2 minimum acceptable price for its royalty oil would be the
3 equivalent of the "in value" price the State would have re-
4 ceivsd from the Producers had the State not opted to take its
5 oil "in kind." In keeping with the State's unwavering posi-
6 tion on price, the Contract expressly provides that the final
7 price to be paid by APC/AOC "shall be equal to the sum the
8 [State] would have received from the [Producers] had [the
9 State] received its royalty in value instead of . . . in
10 kind." (Article 8.1.1.) This provision reflects the simple
11 fact that the State had no intention of diminishing its
12 royalty income as a result of taking its royalty oil "in
13 kind" (for sale to AOC) instead of "in value" (i.e., cash).

14 At the time the Contract was signed, the method of
15 determining the "in-value" price of royalty oil was the sub-
16 ject of a still unresolved lawsuit entitled State of Alaska,
17 et al. vs. Amerada Hess Corporation, et al. Since the
18 "in value" price had yet to be determined in the Amerada Hess
19 litigation, the Contract provided for two prices: a final
20 price to be paid once Amerada Hess establishes the "in value"
21 price, and an interim price to charged pending the resolu-
22 tion of Amerada Hess.

23 Article 8.1.1 of the Contract provides that the
24 final price under the Contract will equal the "in value"
25 price to be judicially determined in Amerada Hess.

26 After such time as [Amerada Hess] shall
27 be resolved among Seller and [the Produ-
28 cers], the parties hereto will be bound
by the terms of such resolution, judicial
or otherwise. Seller and Buyer expressly

1 recognize that adjustments in prices
2 previously paid may be necessary follow-
3 ing said resolution . . .

4 Article 8.1.1 of the Contract also specifies the
5 interim price to be used until Amerada Hess is decided:

6 Pending resolution of said dispute among
7 Seller and [Producers], by judicial deci-
8 sion or settlement in the [Amerada Hess]
9 case, the in value royalty under the
Leases, and therefore the price here-
under, shall be computed in accordance
with Exhibit "B", attached [to the Con-
tract.]

10 Exhibit B was designed to yield a price akin
11 to what the State believes the Court in Amerada Hess will
12 eventually determine is the proper "in value" price. The
13 Exhibit B price is calculated each month in two steps. First,
14 a per barrel royalty oil "value" is determined for each Pro-
15 ducer, by taking the higher of the weighted average of the
16 actual prices received by that Producer or the weighted aver-
17 age of the actual prices received by all other Producers.
18 The "values" for each Producer are then used in the second
19 step of the Exhibit B calculation, which computes the weighted
20 average of the "values" of all the Producers. The effect of
21 this method of price calculation is to disregard, for purposes
22 of the final weighted average, the lower prices received by
23 some Producers, and unless all Producers report exactly the
24 same prices, the Exhibit B price will always exceed the weighted
25 average of all Producers' prices for that month.

26 The fact that neither the final price nor the Ex-
27 hibit B price under Contract would necessarily equal "market"
28

1 value was repeatedly recognized during negotiation of the
2 Contract, and on at least three occasions the parties re-
3 jected use of "market price" as a price standard. APC's
4 original contract proposal called for a "market price" tied
5 to the price of Saudi crude oil. But the State insisted on
6 receiving an "in value" price pegged to the price the Pro-
7 ducers would have paid the State had the State's royalty been
8 taken "in value" rather than "in kind," and Alpetco eventually
9 agreed.

10 Later in the negotiations, discussion turned to the
11 interim price to be paid by APC pending resolution of Amerada
12 Hess. Until Amerada Hess is decided, royalty payments by the
13 Producers are based on a weighted average of all Producers'
14 actual sales, a formula which yields a price lower than the
15 "in value" price which the State in Amerada Hess claims is
16 appropriate, and which Exhibit B approximates. APC objected
17 to paying a higher interim price than the interim price the
18 Producers were paying, and sought to base its interim price
19 on the weighted average of the prices reported to the State
20 by all the Producers. The State, however, was unwilling to
21 allow APC to follow the Producers in paying less than the
22 price the State expects Amerada Hess to establish since APC
23 had no security in Alaska comparable to the Producers' leases.
24 APC eventually agreed to base the interim price (Exhibit B)
25 on the State's position in Amerada Hess, and thus agreed to a
26 price higher than the weighted average of the Producers'
27 prices.
28

1 Thereafter, during the detailed negotiation on
2 using the State's position in Amerada Hess as a basis for the
3 interim price, market price was once again rejected, this
4 time by APC. In Amerada Hess, the State asserts that each
5 Producer should pay the highest of three price standards, one
6 of them being "market price." The State proposed using the
7 same three-part standard for APC's interim price, but APC
8 objected that "market price" is too subjective to use in
9 computing price. The parties then agreed to exclude "market
10 price" from Exhibit B calculations, a decision reflected in
11 Footnote 5 to Exhibit B:

12 "Market" . . . value shall not be used in
13 calculating the "In Value Price to Buyer"
14 unless and until the methodology of deter-
 mining same is judicially decided.

15 Thus, during negotiation of the Contract, the subject of
16 using "market price" as a standard arose three times. On
17 each occasion, its use was rejected.

18 IV. THE PRICE DISPUTE

19 A. AOC Cancellation of Refinery Project

20 By meeting certain "benchmark" requirements of the
21 Contract pertaining to progress on the refinery project, AOC
22 became entitled to and began receiving 75,000 barrels per day
23 of royalty oil in July 1980. Each month thereafter, the
24 State rendered an invoice to AOC for the oil purchased the
25 previous month. The price used in each invoice was computed
26 by applying the formula in Exhibit B of the Contract to data
27 reported by Producers for royalty purposes. The State also
28 provided AOC with certain data from the Producers' royalty

1 reports which were used to calculate the Exhibit B price.

2 For almost one year, AOC paid each monthly invoice, based on
3 the interim Exhibit B price, in full.

4 On May 21, 1981, AOC announced the cancellation of
5 the refinery project, claiming that they had determined that
6 they would be unable to obtain adequate project financing
7 before the Contract deadline of December 31, 1981. The State
8 and AOC thereafter mutually agreed to terminate the Contract.
9 But because of the notice requirement in the Prudhoe Bay Unit
10 Agreement for denominating royalty oil, the Contract provided
11 that AOC had to continue taking royalty oil for seven months
12 after notice of termination unless the State could make alter-
13 nate sales arrangements. The State was unable to place the
14 oil elsewhere under satisfactory terms, and AOC therefore
15 continued to take 75,000 barrels per day until January 12,
16 1982, when the Contract was officially terminated.

17 B. AOC Withholding from Payments to State

18 In mid-1981, shortly after AOC's cancellation of
19 the refinery project, AOC became dissatisfied with the interim
20 Exhibit B price established by the Contract and decided to
21 set the price unilaterally. Thereafter, during the remaining
22 months of the Contract, AOC paid about \$62.6 million less for
23 the State's royalty oil than the amount invoiced by the State
24 pursuant to Exhibit B. ~

25 In underpaying the State for oil delivered from
26 June 1981 to January 1982, AOC not only unilaterally "ad-
27 justed" the Exhibit B price to a lower price arbitrarily set
28

1 by AOC; it also subtracted a portion of its payments previously
2 made at the Exhibit B price for the months of February through
3 May 1981. For example, for the month of November 1981, AOC
4 underpaid the State approximately \$3 million on the basis of
5 its unilateral price adjustment for the month of November,
6 and withheld an additional \$7.5 million as a "retroactive
7 adjustment" for February 1981 -- even though AOC had previously
8 paid the February 1981 invoice in full.

9 By this device of "retroactive adjustment," AOC
10 attempted to disguise the magnitude of its unilateral price
11 revisions. For example, AOC purported to reduce the price it
12 paid for oil in November 1981 by \$1.92 per barrel and attri-
13 buted the remainder of its November underpayment to a "retro-
14 active adjustment" of \$3.53 per barrel for the month of
15 February, 1981; the combined effect of these "adjustments,"
16 however, was a price reduction of more than \$6 a barrel below
17 the \$22.91 invoiced price calculated pursuant to Exhibit B
18 for oil delivered in November.

19 The oil for which AOC had underpaid the State was
20 re-sold by AOC, through an affiliate, for a profit which has
21 been estimated at between \$32 million and \$38 million. The
22 disposition of this profit by AOC is difficult to trace with
23 precision, but it is clear that AOC itself retained virtually
24 none of the profit. Instead, the profit was transferred to,
25 AOC's partners and to other affiliates of The Charter Company
26 (which indirectly owns 93.35% of AOC).

1 C. AOC's Claimed Justification for Withholding

2 AOC claims that the Contract price for the oil
3 should represent a "market price," and that AOC does not have
4 to pay any price higher than the "market price" calculated by
5 AOC. The basis for AOC's claim that it should pay only a
6 "market price" (rather than the invoice price computed pur-
7 suant to Exhibit B of the Contract) has never been thoroughly
8 explained. But AOC argues that the invoiced Exhibit B price
9 was too high because the prices reported by the Producers, on
10 which the Exhibit B calculation is based, were too high.
11 Despite repeated requests from the State for evidence support-
12 ing AOC's claim that the Producer reported prices were too
13 high, AOC's only evidence to date consists of theoretical
14 calculations by AOC of what the true "market price" for
15 Prudhoe Bay oil should be. AOC's claim of inflated price
16 reports from the Producers is especially implausible since
17 the severance tax paid to the State by the Producers is based
18 on the prices they report. In other words, if, as AOC claims,
19 the Producers are reporting prices which are too high, then
20 the Producers are thereby deliberately increasing the amount
21 of severance tax they must pay to the State.

22 Although the factual basis for AOC's withholding
23 remains murky, the claimed legal basis for that withholding
24 is more focused. Article 9.3 of the Contract provides in its
25 entirety:

26 Billing Disputes. Should any portion of
27 the account furnished to Buyer by Seller
28 be disputed in good faith, Buyer and
Seller agree to mutually arrive at a fair
and equitable resolution of such dispute,

1 if possible, and Buyer agrees to pay the
2 amount so determined to be due to Seller
3 within fifteen (15) days after such resolu-
4 tion. Buyer shall pay for such amounts
as it does not in good faith dispute in
accordance with the provisions of this
Article IX.

5 The State's position is that this Contract provision is designed
6 to cover routine and relatively minor billing disputes, and
7 that, in any event, AOC's price dispute is not in "good faith."
8 But AOC interprets the provision much more broadly, arguing
9 that it covers matters as fundamental as the method of calcula-
10 ting the price, and that AOC has no obligation to pay amounts
11 it unilaterally disputes until fifteen days after the resolu-
12 tion of such dispute.

13 V. LITIGATION BETWEEN THE STATE AND AOC

14 The State met on numerous occasions with AOC and
15 its lawyers in an attempt to determine if AOC had any valid
16 grounds for claiming the existence of a pricing dispute within
17 the meaning of the Contract, and to hear various presentations
18 made by AOC in support of their claim. On December 14, 1981,
19 a letter was sent by the State to AOC setting forth the State's
20 determination that no cause for a price dispute existed, and
21 demanding payment of the full amount due to the State under
22 the Contract. The day following receipt of this letter, AOC
23 filed a Complaint for declaratory judgment against the State
24 in Fairbanks Superior Court. The State answered, alleging
25 that the Contract price term controls, and that AOC had en-
26 gaged in various fraudulent conveyances and other transactions
27 which had depleted its assets. That case is currently pending,
28 but has been stayed by the petition filed by the State in the

1 United States Bankruptcy Court in Anchorage seeking to have
2 AOC declared an involuntary bankrupt.

3 The decision to proceed against AOC in the Bankruptcy
4 Court rather than in Fairbanks Superior Court reflected the fact
5 that AOC itself has virtually no assets, having transferred them
6 to its affiliates. In order to recover any substantial portion
7 of the money owed to the State by AOC, it will be necessary for
8 the State to collect from AOC's parent (The Charter Company) and
9 its affiliates -- a process which is far easier in the Bank-
10 ruptcy Court than in State Court. Moreover, the Bankruptcy
11 Court has broader jurisdiction over witnesses and documents
12 outside of Alaska, and Bankruptcy proceedings tend to be re-
13 solved more quickly than State Court actions.

14 The bankruptcy proceeding was commenced by the
15 State in February 1982 and the matter was tried in January
16 1983. During the intervening months, nine separate hearings
17 were held, dozens of briefs and memoranda were filed by both
18 sides, thirty-one depositions were taken in four states, and
19 tens of thousands of pages of documents were exchanged and
20 reviewed.

21 Trial commenced in Anchorage on January 17, 1983,
22 and continued for five very full trial days. At the conclu-
23 sion of the trial, the Bankruptcy Judge denied the State's
24 petition to have AOC placed in involuntary bankruptcy. This
25 ruling does not, however, prevent the State from now proceeding
26 against AOC in the Alaska State Courts.

27 The Findings of Fact and Conclusions of Law which
28 the Bankruptcy Judge must issue to conclude the bankruptcy

1 proceedings are still the subject of memoranda and argument
2 before the Court, and are not expected to be issued before
3 the end of April. But even in the absence of a definitive
4 statement from the Court, the oral ruling by the Judge at the
5 close of the trial in Anchorage gives a fair indication of
6 the basis for his ruling.

7 The Bankruptcy Judge stated that, based solely on the
8 price provisions of the Contract, AOC has a debt to the State
9 for at least some portion of the amount withheld from AOC's pay-
10 ments for royalty oil. But the Judge also concluded that AOC's
11 price dispute is in good faith within the meaning of Article
12 9.3, and that Article 9.3 of the Contract gives AOC the right
13 to withhold payment of any amounts disputed in good faith until
14 such time as the dispute is resolved. Therefore, the Court con-
15 cluded, AOC's debt to the State is not yet "due" to be paid
16 because of the good faith price dispute, and AOC could not be
17 judged to be bankrupt for failing to pay that debt. Counsel for
18 the State believe that the Court's ruling is not consistent with
19 existing law, and the prospects for an appeal of the Bankruptcy
20 Court's decision are now being evaluated.

21 The State is also considering the extent to which
22 it will be fruitful to pursue the State Court action against
23 AOC to recover the \$62.6 million withheld by AOC from its
24 payments for royalty oil. Among the factors to be considered
25 in connection with that decision is the fact that Article
26 9.3, which proved to be the major stumbling block in the
27 Bankruptcy Court proceeding, would have little bearing on an
28 action in Alaskan Courts. AOC was able to avoid involuntary

1 bankruptcy by convincing the Bankruptcy Court that its dispute
2 with the State was in good faith, and that (because of Article
3 9.3) AOC's debt was not yet "due" to be paid. But in State
4 Court, the central issue would be simply whether or not AOC
5 has paid the price called for by the Contract, and AOC's good
6 faith (or lack thereof) would not control whether AOC must
7 pay the State the amount withheld. Another important consi-
8 deration bearing on the decision whether to pursue the
9 State Court case is the fact that much of the research and
10 discovery already conducted in the bankruptcy proceeding
11 could be used in a State Court action.

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STATE OF ALASKA
THE LEGISLATURE

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

LEGISLATIVE AFFAIRS AGENCY

MEMORANDUM

May 5, 1983

SUBJECT: Royalty oil sales under AS 38.06.055
(Work Order No. 13-1361)

TO: Representative John Cowdery

FROM: Richard C. Folta *RF*
Legislative Counsel

You have asked if the legislature does not approve a royalty oil sale under the above statute, may the commissioner of natural resources sell the oil without legislative approval to the same company on a negotiated short term contract substantially different from the original sale.

The answer is yes, if the sale is determined by the commissioner to be needed to "relieve storage and market conditions". AS 38.06.055(b)(1) provides that legislative approval is not required when the sale, exchange, or other disposition of oil or gas for one year or less if the sale, exchange, or other disposition is entered into to relieve storage or market conditions. The commissioner may also forego competitive bidding if in the "best interest of the state" after notice to the Royalty Board (AS 38.05.183(a)).

The transaction may be viewed with suspicion by the legislature, who after disapproving a sale of royalty oil sees the commissioner finding a sudden storage and market crisis and proceeding with a sale under AS 38.06.055(b)(1). If there was litigation over the sale the standard of review by the courts would be as set out in National Bank of Alaska v. Department of Revenue, 642 p.2d 811 (1982).

The reasonable basis standard is used where the question at issue, i.e., determination of "relieve storage or market conditions" implicates special agency expertise or the determination of fundamental policies within the scope of the agency's statutory functions. The second test or independent judgment standard is when the court makes its own determination of the meaning of the statute and need not

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Representative John Cowdery
Page 2
May 5, 1983

follow the agency's construction even if it is one of several reasonable readings. Very likely the court would invoke the former rule in coming to a decision.

RCF:ljb
17/031

Introduced by: Mayor
Date: May 3, 1983
Vote:
Action:

KENAI PENINSULA BOROUGH

RESOLUTION 83-119

SUPPORTING APPROVAL OF STATE ROYALTY OIL CONTRACTS TO CHEVRON USA AND TESORO ALASKA.

WHEREAS, contracts for the supply of the State's royalty oil for Chevron USA and Tesoro Alaska are currently pending the approval of the State Legislature; and

WHEREAS, the supplies of crude oil from Cook Inlet and Peninsula fields have been dwindling annually since 1970 necessitating the companies to look to the State for assured supplies; and

WHEREAS, it has been the expressed interest of the State to pledge its royalty oil for in-State processing and to trigger new industrial investment and employment; and

WHEREAS, the contracts call for an eleven-year supply of 18,000 barrels per day to the Chevron refinery, and 26,000 barrels per day to the Tesoro refinery for in-State processing of products for Alaska markets; and

WHEREAS, the supply of the royalty oil will add measurably to the economic well-being of the State of Alaska and the Kenai Peninsula assuring the continuing operation for the Chevron refinery and the further expansion of the Tesoro refinery; and

WHEREAS, the Chevron and Tesoro refineries are annual contributors to the economy with a combined payroll of \$4 million from the 105 year-round jobs, operations impacting another 100 jobs and \$2.5 million in wages in the service and supply sector, \$1.5 million in local purchases, and sizeable tax contributions from a combined \$125 million in assessed valuations; and

WHEREAS, such contributions to the economy would be increased by an \$80-\$90 million expansion of the Tesoro refinery, a 250-member construction work force, and the addition of 20-30 new year-round jobs for the expanded operations of the plant; and

WHEREAS, it has been determined by the State Commissioner of Natural Resources, and the State's Royalty Oil and Gas Advisory Board that the approval of contracts to provide long-term supplies of the State's North Slope crude to the two companies is in

the best interest of the State of Alaska, and a wise and expedient use of the State's oil resources;

NOW THEREFORE, BE IT RESOLVED BY THE ASSEMBLY OF THE KENAI PENINSULA BOROUGH:

Section 1. That the Assembly recommends that the State Legislature approve contracts for the supply of the State's royalty oil from the North Slope to the in-State refining facilities of Chevron USA and Tesoro Alaska.

Section 2. That the Kenai Peninsula Borough Assembly supports the concept of approval and ratification of those contracts as provided in HB 320; HB 370; HB 371; SB 268, and SB 269.

Section 3. That the Borough Clerk shall distribute a copy of this resolution to Governor William J. Sheffield; to Senate President Jalmar Kerttula; to House Speaker Joe L. Hayes; to the Chairmen of the Senate and House Resources Committees; to Senators Don Gilman and Paul Fischer; and to Representatives Hugh Malone, Bette Cato, Milo Fritz, and Vern Hurlbert.

Section 4. That this resolution takes effect immediately on the date of its adoption.

ADOPTED BY THE ASSEMBLY OF THE KENAI PENINSULA BOROUGH ON THIS _____ DAY OF _____, 1983.

Donald L. McCloud, Assembly President

ATTEST:

Borough Clerk



Chevron U.S.A. Inc.

P.O. Box 7-839, Anchorage, AK 99510 • Phone (907) 273-9666

J. E. Day
Public Affairs Manager

May 11, 1983

Honorable John Ringstad
Honorable Richard Shultz
Co-Chairmen
House Resources Committee

Gentlemen:

At the House Resource Committee hearing on May 5, 1983 there were questions raised for which we had incomplete answers at the time. This letter will provide more complete responses to the specific questions listed.

1. What is the total petroleum product demand in Alaska, and what is the individual refiner market share?

It is difficult to provide a precise and up-to-date summary of product demands and refiner market share within the time frame needed for your deliberations. However, we feel that the data presented in the Alaska Petroleum Product Pricing Report (L. F. DeLong and L. M. Pernela, February 1, 1983) is reasonably accurate and does report figures that approximate our own estimates that were made in 1979. Therefore, we summarize them on Attachment A, giving you the source pages in the Pricing Study Report. For a separate break-out of "Railbelt" demand Page 34 of that report is enclosed as Attachment B.

Our own 1979 study anticipated Alaska's demand for product to increase over a 1980 base of 1 by the following factors:

	<u>1980</u>	<u>1985</u>	<u>1990</u>	<u>2000</u>
AV GAS	1	1.00	1.18	1.36
MO GAS	1	.98	.95	.93
JET FUEL	1	1.18	1.35	1.41
DISTILLABLE FUELS	1	1.13	1.21	1.31

2. What is the price of Cook Inlet Crude?

This crude is priced by the individual producers and the most recent price posting we have is by ARCO dated February 17, 1983. That posting was at \$25.00/Bbl. for crude at a gravity between 34.0 and 34.9 °API. For every gravity increase of 1° API the price goes up 10¢; e.g., 36.5° API crude would be \$25.20/Bbl.

We also should point out that this is a premium crude; it is low sulfur and contains a much higher percent of light products (in the order of magnitude of 55% vs. 35% from ANS).

3. How much Jet Fuel does Chevron import? How much Jet Fuel is imported at Anchorage International Airport?

It might help to first provide a brief description of the airport consortium. It is currently a consortium of ten (10) airline members operated by Butler Aviation. Each airline purchases its own fuel from various suppliers for delivery to common tankage. The fuel is comingled but each airline maintains its own inventory. The consortium itself does not purchase fuel, it only operates the facility.

Chevron supplies fuel to various airlines and during the year of 1982 supplied approximately 2.8 million Bbls. (7.7 MBD). The source of this fuel was as follows:

	<u>%</u>	<u>MBD</u>
Imported via tanker	43	3.3
Produced at Nikiski Refinery	24	1.9
Exchange or purchase agreement from other in-state refiners	<u>33</u>	<u>2.5</u>
	100	7.7

The total thru-put for the Anchorage terminal for 1982 is in the order of magnitude of 5,000,000 Bbls. or about 13.7 MBD.

4. What is Chevron's distribution system for Western Alaska?

This can be best described by use of a map (see Attachment C). The map gives general routes, but some additional detail is provided to help in understanding the magnitude of the handling costs.

In the summer time, tankers deliver product to Dutch Harbor and since the wharf is too small to accommodate them, a barge lightering operation is required. Large barges then move the product from Dutch Harbor up to Kotzebue, Nome and St. Michael, but again, because of shallow water, the fuel is lightered to shore on smaller barges.

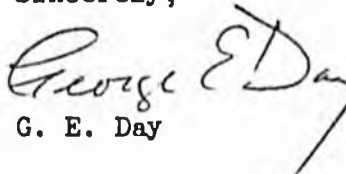
Because product resupply can only be accomplished during summer months these terminals are much larger than those that can be resupplied year around. Also, for this same reason average annual inventory at these terminals is much higher than the average which adds a higher than normal inventory cost to the ultimate fuel price.

For the use of the committee only we have also provided some dollar values of ice locked terminal inventories and plant facilities. We ask that this particular information because of its proprietary nature not be released to the press or made available to our competitors.

<u>PLANT</u>	<u>ESTIMATED MARKET VALUE OF PLANT</u>	<u>ESTIMATED VALUE OF AVERAGE INVENTORY</u>
Bethel	\$ 2,739,000	\$ 4,681,000
St. Michael	809,000	1,474,000
Nome	1,159,000	5,582,000
Kotzebue	2,587,000	5,726,000
Dillingham	1,582,000	1,374,000
Fort Yukon	557,000	670,000
Galena	971,000	1,198,000
Naknek	875,000	1,206,000

We hope that this information is the complete response to your questions. If there is other information that would be desired, please let Mr. Ray Plummer know and we'll try and respond.

Sincerely,


G. E. Day

SUMMARY OF SELECTED PRODUCT DEMANDS IN
ALASKA AND IN-STATE REFINERY PRODUCTIONS

ATTACHMENT A

	CHEVRON		TESORO		NPR		(6) Alaska Demand -	Product 1982
	(1) 1982 (Adjusted)	(3) Capacity	(1) 1982	(4) Capacity	(1) 1982	(5) Capacity		
	(7) BPCD	BPSD	BPCD	BPSD	BPCD	BPSD	BPCD	
MO GAS			11.5	12.28	-	-	14.4	
JP-4	.9	1.1	1.0	1.07	2.7	3.72	29.1	
JET A-1	2.3	2.8	12.6	12.2	5.4	8.37(3)		
#1 OIL			} 3.9	} 4.3	} 4.4	} 2.42	31.6	
#2 OIL	2.2	2.8						
CRUDE FUEL	(2) 14.5	18.0	45.2	48.5	43.0	46.5		
	(7)	BPCD = Bbls per calendar day (Average annual production that allows for some down time.)						
		BPSD = Bbls per stream day (Capacity on any given single day.)						
	(1)	Source is Page 54 of Pricing Report. Chevron's numbers have been adjusted to reflect anticipated operation at 18 MBSD.						
	(2)	BPCD adjusted for refinery maintenance and asphalt production. (Pg. 7 of "Agreement for Sale and Purchase of Royalty Oil" between State of Alaska and Chevron U.S.A. Inc.) Also yield of Jet A-1 in winter is less as that product is used to produce low pour diesel.						
	(3)	Source is Pg. 39 of Pricing Study with yields corrected to reflect current operation.						
	(4)	Source is Pg. 46 of Pricing Study. The split between Mo Gas and JP-4 is an estimate because the Pricing Study lumps them together.						
	(5)	Source is Pg. 42 of Pricing Study.						
	(6)	Source is Pg. 27 of Pricing Study.						

AGO 786476

D. RAILBELT DEMAND

The demand for petroleum products in the Railbelt was determined from a number of data sources, including but not limited to: the volumes and types of petroleum products moved thru the ports of Anchorage, Whittier, and Nikiski; the production of products at the Alaska refineries and the product/crude oil movements through the GVEA, Nikiski, and Whittier pipelines. Utilizing the above data and formulating an input/output model, the 1981 and 1982 Railbelt demand on a BPCD basis was determined as outlined below:

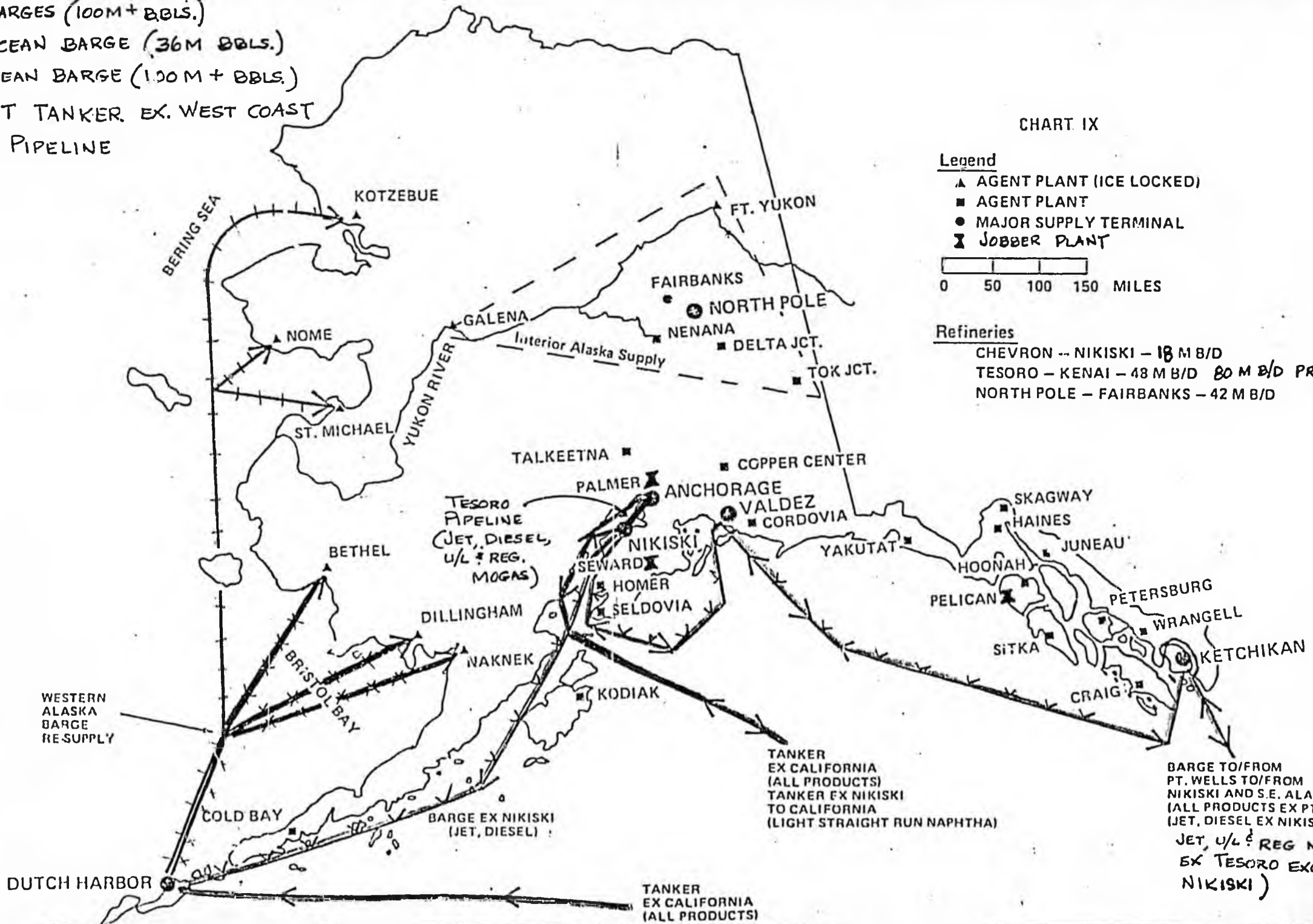
RAILBELT PRODUCT DEMAND

<u>Product.</u>	<u>MPBCD</u>	
	<u>1981</u>	<u>1982</u>
MoGas	10.2	10.8
JP-4	4.6	4.6
JET B	1.7	.5
AVGas	.9	.7
Jet A-1	20.1	23.0
#1 HO/diesel/DFA	1.6	1.8
#2 HO/diesel	4.4	4.3
#4 FO	.6	.8
Asphalt	<u>.6</u>	<u>.9</u>
Total	44.0	46.5

The Railbelt volumes shown above reflect actual purchases and deliveries by refiners and wholesalers. Not included in the above figures are the TAPS turbine fuel manufactured and used exclusively by TAPS. Also year to year inventory changes would modify some of the above numbers in a minor way. For example, the changes in yearly inventory of the asphalt mix used in the manufacture of asphalt by Union at their topping plant at their Anchorage terminal is a clear indication of the types of problems encountered when interpreting data. In this example the numbers presented above do not reflect inventory carry-overs or drawdowns, yet in 1981 Union used 1980 asphalt in their plant, whereas in 1982 they imported asphalt mix and used it all in that year. The apparant "increase" in asphalt demand

Alaska Primary Distribution

- PSTB
- ++ OCEAN BARGES (100M+ BBLs.)
- X FOSS OCEAN BARGE (36M BBLs.)
- V-V PSTB OCEAN BARGE (1,00M+ BBLs.)
- 35MDWT TANKER, EX. WEST COAST
- TESORO PIPELINE



AGD 785478

WESTERN ALASKA BARGE RE-SUPPLY

TANKER EX CALIFORNIA (ALL PRODUCTS)
TANKER EX NIKISKI TO CALIFORNIA (LIGHT STRAIGHT RUN NAPHTHA)

BARGE TO/FROM PT. WELLS TO/FROM NIKISKI AND S.E. ALASKA (ALL PRODUCTS EX PT. WELLS) (JET, DIESEL EX NIKISKI CUSA JET, U/L & REG MOGAS EX TESORO EXCHANGE NIKISKI)

TANKER EX CALIFORNIA (ALL PRODUCTS)

San Francisco, CA
May 11, 1983

ALASKA PRODUCT STUDY

J. C. LEUTWYLER:

have developed the following responses to the questions raised in Mr. J. F. Mayer's May 9 letter to you on the above subject:

Q. What is the cost to produce Nikiiski jet fuel versus West Coast jet fuel?

We have never attempted to allocate refinery costs to individual product yields at our refineries and, therefore, these data are not available. We do maintain refinery optimization programs at most of our refineries to determine cost to produce incremental products based on assumed incremental raw material supply. However, these data would not be applicable to determine average costs.

Q. What is the in-state refinery output versus capacity?

Total in-state refinery capacity reflected on page 36 of the study is 130.5 MBPCD. Total output reflected in the refinery yield data incorporated in the study and assuming that Arco is operating its North Slope Refinery at capacity (14.0 MBPCD) totals 84.5 MBPCD.

Q. With the Tesoro expansion what will be the total in-state refinery output?

Based on a February 7, 1983 Oil and Gas Journal article indicating that Tesoro plans to expand its refinery to 80.0 MBD by mid-84, total in-state refinery output would be increased about 30 MBPCD to a total of about 114.5 MBPCD if Tesoro operated that increment at capacity.

Q. What products are imported into the state? From where?

All premium unleaded mogas and avgas must be imported because local refineries are unable to manufacture these premium products. This coupled with the deficits of jet and diesel oil are all imported from the West Coast with the exception of a small amount of foreign jet fuel as discussed in the next question. Asphalt charge stock is also imported from the West Coast for further processing at our Nikiski Refinery to manufacture finished asphalt.

Q. Does the consortium in Anchorage import jet fuel into the state? From where?

It is our understanding that essentially all imported jet into Anchorage flows through the consortium. On page 31 of the study, the import of jet fuel is indicated as follows:

3490 BPCD is imported from the West Coast

540 BPCD from foreign sources

However, we believe the import of foreign-source jet has now been switched to the West Coast.

Please advise if you have any questions regarding the above.

W. T. DANKER

ATD

WTD:jh

6/14/83

Tesoro Stake Lowered To 28.9% by Charter Co.

By a WALL STREET JOURNAL Staff Reporter
WASHINGTON—Charter Co. said it lowered to 28.9% its stake in Tesoro Petroleum Corp.

In a filing with the Securities and Exchange Commission, Charter said a subsidiary, Charter Security Life Insurance Co., New York, sold 250,000 shares of Tesoro common stock from May 16 through May 20 at prices ranging from \$14.875 to \$15.25 a share on the open market. The filing also said that 36,800 shares were purchased on April 15 at prices ranging from \$14.875 to \$15 a share.

The filing also said that on May 23 Charter Security of New York sold 1,276,685 Tesoro common shares to another Charter subsidiary, Charter Security Life Insurance Co., Louisiana, for \$14 a share. It also sold all of the Tesoro preferred shares it held to Charter Security of Louisiana for \$17.60 apiece. Charter said that its New York unit sold all of its voting stock of Tesoro after New York state Insurance Department representatives indicated that its stake might be violating New York law governing stock ownership by insurance companies.

As a result of the purchases and sales, the filing said that Charter Co. holds 2,184,085 common shares and 2,875,000 preferred shares convertible into 2,500,100 common shares.

As of Dec. 31, Tesoro had 13.7 million common shares outstanding.

In Jacksonville, Fla., a spokeswoman for Charter, an oil, insurance and communications concern, said the company didn't have any comment about the filing. "It's just a regular 13D," she said.

In San Antonio, Texas, Tesoro officials couldn't be reached for comment.



ALASKA RURAL ELECTRIC COOPERATIVE
ASSOCIATION, INC.

237 E. FIREWEED LANE • SUITE 301
ANCHORAGE, ALASKA 99503 • (907) 276-3235

Hon. Frank Ferguson
Alaska State Legislature
Pouch V
Juneau, AK 99811

June 14, 1983

Dear Sen. Ferguson,

Several weeks ago, I had the opportunity to testify before the House and Senate Resources Committees regarding pending state royalty oil contracts with Tesoro Petroleum and Chevron USA.

Our support of these contracts was voiced in an effort to create a condition where competition and free market forces would force lower fuel prices in Western Alaska, both for our member electric utilities and consumers who must now pay more than 50% of their total household income for heat and light.

In the intervening weeks, we have been able to obtain some fuel prices which reinforce our position and should, we feel, be taken into consideration as these contracts are acted upon.

As you know, Western Alaska is supplied exclusively by Chevron USA from bulk shipments of fuel that originate on the West Coast. We have met with the company three times in an effort to negotiate lower prices but these talks have been singularly unproductive. Their prices are their prices and we don't like them; that's too bad. Their prices are also set community by community and are not effected by decreases in prices in Anchorage where Chevron must compete against other suppliers.

Tesoro, on the other hand, has been more than willing to assist our efforts at obtaining lower prices. And the president of Tesoro, Mr. Dennis Jurens, has made good faith commitments to us regarding a continuation of their pricing policies for this year and for the years to come. His company, he says, is interested in moving its products and to do that, it must have additional sales points and a more widespread

distribution system.

The savings that Tesoro can give our member utilities right now are substantial. In the case of Naknek, Tesoro will sell us fuel at their Nikiski price of \$.79 a gallon. We can barge this fuel into Naknek for \$.10 a gallon with a landed price of \$.89. This compares to \$1.1425 per gallon from Chevron. The savings for the co-op in Naknek amount to \$256,000 this year.

At Unalakleet, we are looking forward to saving a proportionate amount since Chevron's landed price is \$1.38 while we can get supplied from a delivery point outside of St. Michael's at less than \$1.16. Instead of prices in excess of \$1.40 at Kotzebue, deliveries from competitive markets at Dutch Harbor will come in for just over \$1.16.

Tesoro's Nikiski price, by the way, is lower than the jobber prices in Puget Sound. So much lower, in fact, that even piggybacking major shipments to the North Slope on already hired barges is more expensive than buying in-state and shipping from Cook Inlet.

Chevron's comments to us indicate that their prices will only respond to actual competition in the marketplace. None of the other major oil companies in Alaska we have contacted have expressed willingness to market products in Western Alaska in the immediate future. Lower fuel prices in the Western Alaska district are directly tied to Tesoro's ability to process more crude in-state and sell it here to existing markets. We feel that this opportunity to see Alaskans directly benefit from Alaska's oil resource should not be passed up since competition will result in lower prices for home heating fuel as well.

The state has a direct financial interest in these fuel prices, not only as a user of fuels but as a subsidizer of energy costs through the Power Cost Assistance Program and the Energy Cost Assistance Program. The lower the retail price of fuel, the less state money will have to be committed to support these programs.

As an aside, our fuel purchasing efforts are not being confined only to electric co-ops. We are in the process of contacting canneries and other major users who can take deliveries of large quantities to help us achieve an economy of scale. Mr. Jurens has indicated Tesoro's willingness to help us in this effort by arranging trades with other suppliers to provide the

quantities necessary in the event that there is a delay
in their refinery expansion.

We feel strongly that it is in the best interests of the
state, particularly Western Alaska, to approve these
contracts and we would ask your support in this matter.

Regards,

Bill Blessington
Information Director

cc Dennis Jurens

Alaska State Legislature



ANCHORAGE

P.O. BOX 10-1623
ANCHORAGE, AK 99511
(907) 344 0950

JUNEAU

POUCH V
JUNEAU, AK 99811
(907) 465-4905
465-4906

House of Representatives

REPRESENTATIVE
JOHN J. COWDERY
DISTRICT EIGHT

COMMITTEES
OIL & GAS—(CO-CHAIR)
STATE OF AFFAIRS—(VICE-CHAIR)
LABOR & COMMERCE
RESOURCES

June 15, 1983

The Honorable Bill Sheffield
Governor
State of Alaska
Juneau, Alaska 99811

Dear Governor Sheffield:

I am seriously concerned by your recent statements regarding the proposed royalty oil contracts for Tesoro and Chevron. I note that, at your cabinet meeting this week, you accused several "large oil companies" of interfering with your attempts to seek legislative approval of the royalty oil contract legislation. Yet you declined to mention any of these "interferers" by name.

In a free enterprise system it seems quite appropriate to me that competition be allowed to flourish. You evidently disagree as evidenced by your statements. Further, if you intend to make such accusations, I would think you would have the courtesy to specifically name your detractors rather than brand the oil industry wholesale for what you perceive to be improper actions. I would request that you name the "large oil companies" which you are accusing so that the public will not be led to believe that the State's Chief Executive is dealing in rumor spreading or plain gossip.

I also am concerned that you are urging legislative ratification of these contracts and that you feel they deserve to be voted on. Yet, much of the information requested of Tesoro and Chevron by the House and Senate committees has not been forthcoming. Am I to assume by your statements that you wish the Legislature to vote on these contracts while many important questions about the financial feasibility of these long term contracts remain unanswered? I certainly hope not. You recently forced some legislators to vote on another matter without allowing questions to be answered via the committee process, and we have seen the less than ideal results of that debacle.

AGD 786485

Governor Bill Sheffield
June 15, 1983
Page 2

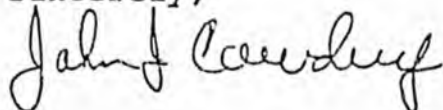
The committee process is in place to ask the questions that, perhaps, your Administration would rather not ask. We owe that obligation to Alaskans. The people of Alaska trust that their representatives will vote only after they are properly informed on the issues. Some of us respect the Constitutional duties we have been elected to uphold.

The contracts before us deserve critical and prolonged examination. I, personally, do not believe, at this time, they should be entered into. If the questions I have asked of the oil companies are satisfactorily answered, I might change that opinion.

Finally, I would note that House and Senate priorities were agreed upon during the time you were out of state attending a zoo opening in Oregon. If these contracts were so vital to you, it seems to me you would have been present in Juneau during the critical negotiations between the House and Senate to bring this session to a close.

I urge that you give greater consideration to these contracts and the unanswered questions. I further urge that you refrain from negatively branding the oil industry on which this state depends so greatly without adequate justification.

Sincerely,



Representative John Cowdery
Chairman
Joint Legislative Committee on Oil and Gas



THE ALLIANCE

P.O. Box 100100 / Anchorage, Alaska 99510 / (907) 562-0100

RESOLUTION IN SUPPORT OF
ENACTMENT OF MEASURES
WHICH ALLOW THE STATE TO
PROCEED WITH THE SALE OF
ROYALTY OIL TO BOTH TESORO
ALASKA PETROLEUM CO. AND
CHEVRON U.S.A.

Whereas, the Alaska Support Industry Alliance has reviewed the complicated issues attendant to the contracts between the State of Alaska and the Tesoro Alaska Petroleum Co. and Chevron U.S.A. and,

Whereas, after such review, it appears to be in the best interest of the State to proceed to enter into these agreements.

Now Therefore Be It Resolved that the Alaska Support Industry Alliance hereby does call upon the Legislature of the State of Alaska to expeditiously proceed with passage of those bills which are required to ratify both of the agreements executed by the Commissioner of Natural Resources and the in-state refiners.

Dated this 2nd day of June, 1983

Milton Byrd
Milton Byrd, President

Alaska Support Industry Alliance...for responsible economic development

Milton Byrd — President
Frontier Companies of Alaska
Ann Curtis — Vice President
Crowley Maritime
Paul Harding — Secretary
Universal Services, Inc., Int'l

Joe Mathis — Treasurer
Universal Services, Inc., Int'l
Virgil Gillespie
Alaska International
Construction, Inc.
Len Kelley
Greyhound Support Services, Inc

John Martin
Dresser Atlas
Val Molyneux
VECO
Roger Spencer
Alaska Bussell Electric, Inc.

Bill Webb
Arctic Hosts, Inc.
Chuck Becker
Executive Director

AGO 786487



Alaska State Legislature

HOUSE OF REPRESENTATIVES
COMMITTEE ON RESOURCES

JOHN RINGSTAD, CO-CHAIRMAN
RICHARD SHULTZ, CO-CHAIRMAN
POUCH V
JUNEAU, ALASKA 99811
(907) 465-3715

April 20, 1983

TO: All Members, House & Senate Resources Committee
Joint Oil & Gas Committee

FROM: Committee Staff

RE: Royalty Oil Sales to Tesoro and Chevron
Petroleum Companies

The Senate Resources Committee and members of the Joint Oil & Gas Committee will join the House Resources Committee on Wednesday, April 20, to hear testimony on the proposed State royalty oil sales to Tesoro and Chevron Petroleum Companies. These hearings will be held at 3:00 p.m. in the Senate Finance Committee room.

There are three different contracts before the Legislature for the sale of royalty oil. The first contract is for the sale of approximately 8,200 b/d of Cook Inlet crude to Tesoro Petroleum Company. The contract would commence January 1984, with a term of eleven years. The price term is the weighted average price which the State would have received had the State taken the oil in-value. Tesoro has committed to manufacture the Cook Inlet crude in their Nikiski refinery.

The second contract is between Chevron, USA, and the State. This agreement is for 18,000 b/d of ANS royalty crude which will be run at Chevron's Nikiski refinery. Chevron has agreed to pay \$.30 over the producers weighted average field price which the Department of Natural Resources claims will offset and avoid creating any significant downward trend in the oil market. The term of this contract is twelve years.

The third contract before the Committee is an agreement between Tesoro Petroleum Company and the State for the sale of approximately 26,000 b/d of ANS royalty crude. In consideration for the royalty crude, Tesoro has agreed to pay \$.30 over the producers weighted average field price to diminish the possible displacement of ANS on the West Coast. Tesoro has further agreed to refine this crude in their Nikiski refinery, which they plan to expand to refine additional petroleum products for sale in Alaska. Because of the concern over Tesoro's agreement with Charter Security Life Insurance Company, which is a subsidiary of Charter Company, this contract provides that if a third party acquires control of Tesoro, the State may cancel the contract at its sole discretion.

Additional information on these three contracts has been attached.

AGD 786488

ROYALTY OIL INFORMATION

I. Existing Agreements

A. Cook Inlet - Tesoro takes all royalty oil under 1969 contract; expires in 1983; a ten-year renewal is now before the Legislature (HB 320).

B. Prudhoe Bay

1. Golden Valley Electric Association - may take up to 5,000 barrels a day (b/d) under their 1977 agreement which expires in 1984. Currently working with Department on renewal.
2. North Pole Refining (Mapco) - entitled to 15 percent, or up to 35,000 b/d under their 1978 agreement, which expires in 2003.
3. Tesoro - entitled to 24.5 percent, or up to 46,000 b/d under their 1982 agreement, which expires in 1994..

All of the existing Prudhoe Bay agreements were approved by the Alaska Legislature. Two other long-term proposals, by Alpetco and Doyon, were approved by the Legislature in 1978 and 1982, respectively, but have since been terminated.

The basic provisions of the pending long-term Prudhoe Bay Unit (PBU) agreement,

Tesoro

- an 11-year contract for almost 14 percent of PBU production (about 26,000 b/d at current levels);
- for every barrel, a 30-cent premium over the in-value price;
- special provisions to avert control of Tesoro by Charter;
- enables \$90 million expansion of Nikiski refinery by Tesoro; entire quantity must be processed in-state.

Chevron

- an 11-year contract for about 9½ percent of PBU production (about 18,000 b/d at current levels);
- as with Tesoro, a 30-cent premium for each barrel over the in-value price;
- will avert the closure of the Kenai refinery;

- will require the in-state production of specified petroleum products, including asphalt (which is in high demand).

Major benefits of the agreements:

In-state processing of more than 23 percent of Alaska's royalty oil promising

- adequate supplies of gasoline, asphalt, and other petroleum products for Alaskans;
- over \$4 3/4 million annually above the amount that would have been received in-value;
- continuation of Chevron's Kenai refinery; nearly \$90 million expansion of Tesoro's Nikiski refinery;
- attendant tax base and employment benefits.



Tesoro Alaska Petroleum Company

March 15, 1983

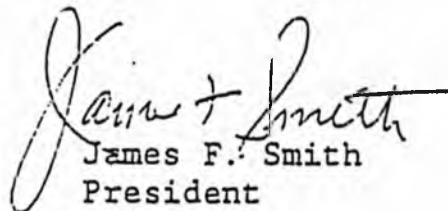
Ms. Esther C. Wunnicke,
Commissioner
State of Alaska
Department of Natural Resources
Pouch M
Juneau, Alaska 99811

Dear Commissioner Wunnicke:

Please find enclosed a fully executed original of the Letter Agreement between the State of Alaska and Tesoro Alaska Petroleum Company concerning third party control of Tesoro.

A copy of this letter has been retained for our records.

Yours very truly,


James F. Smith
President

JFS:pw

AGO 786492 X

STATE OF ALASKA

BILL SHEFFIELD, GOVERNOR

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

POUCH M
JUNEAU, ALASKA 99811
PHONE: (907) 465-2400

March 12, 1983

Mr. James F. Smith
President
Tesoro Alaska Petroleum
Company
8700 Tesoro Drive
San Antonio, Texas 78286

Dear Mr. Smith:

On March 12, 1983, the State of Alaska and Tesoro Alaska Petroleum Company ("Tesoro Alaska") entered into an Agreement for the Sale and Purchase of Royalty Oil (the "Agreement"). Article 7.5 of the Agreement provides that the State may elect to terminate the Agreement in the event that a "third party" obtains "control" (as such terms are defined therein) of Tesoro Alaska or its parent, Tesoro Petroleum Corporation ("Tesoro").

During the negotiations which led to the execution of the Agreement, you informed the State that, on January 26, 1983, two Charter Security Life Insurance Companies, subsidiaries of The Charter Company ("Charter"), had entered into a Purchase Agreement, a Stockholders Agreement, a Registration Rights Agreement and a Certificate of Designation Establishing A Series of \$2.20 Cumulative Convertible Preferred Stock (the "agreements") with Tesoro to purchase 2,875,000 shares of a new series of Cumulative Convertible Preferred Stock of Tesoro. Furthermore, those agreements contemplate that the Charter Security Life Insurance Companies or other companies affiliated with The Charter Company may purchase additional shares of Tesoro so that The Charter Company and companies affiliated with The Charter Company may own up to 30 percent of the voting interest in Tesoro. You also informed us that the Charter Security Life Insurance Companies will be entitled to up to three seats on Tesoro's Board of Directors, depending upon the size of Tesoro's Board.

AGO 706493

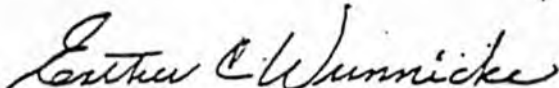
Mr. James F. Smith

-2-

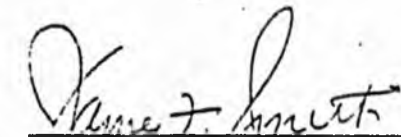
March 12, 1983

The purpose of this letter is to set forth the understanding and intent of the State and Tesoro Alaska with respect to the application of Article 7.5 of the Agreement to the contemplated relationship between Charter and Tesoro. If the arrangements described in the preceding paragraph are effected, it is the understanding and intent of the parties that Charter and/or its affiliates will not control Tesoro or Tesoro Alaska within the meaning of Article 7.5 of the Agreement. If, however, Charter and/or its affiliates materially increases its or their ability to direct or cause direction of the management and policies of Tesoro or Tesoro Alaska over that contemplated in the agreements, Article 7.5 will be applicable.

Sincerely,


Esther C. Wunnicke
Commissioner

ACCEPTED AND AGREED TO:


James F. Smith, President
Tesoro Alaska Petroleum Company

WFS
LAW

AGO 786494



STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

HB 326

March 31, 1983

The Honorable Joe L. Hayes
Speaker of the House
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Mr. Speaker:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill which provides for legislative approval of a royalty oil contract between the state and Tesoro Alaska Petroleum Company for the sale of Cook Inlet royalty oil.

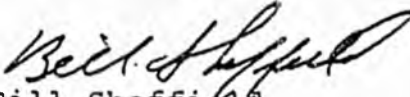
This contract is described in the findings entitled "Proposed Disposition of Royalty Oil, Tesoro Alaska Petroleum Company" issued by the Department of Natural Resources on February 22, 1983. Copies of these findings have been made available to the legislature and the public for review.

This contract is being submitted for legislative approval for two reasons. First, although this and the previous administration have consistently taken the position that the statutory requirement of legislative approval of royalty oil contracts is unconstitutional (AS 38.06.055), as a matter of comity I respect the legislature's desire to have a direct voice in major disposals of royalty oil. Therefore, this contract contains provisions requiring approval by the legislature before it becomes effective. Second, this bill would ratify the agreement for the sale of oil. This ratification would cure any procedural defect that may have occurred in the process of entering into this contract.

Although we believe that all necessary steps have been taken, the statutes and regulations governing the disposal of royalty oil represent often conflicting desires and goals, both procedural and substantive. For example, even if statutorily requiring legislative approval were constitutional, the present statutes provide, on the one hand, that the legislature is to approve the contract by enacting legislation (AS 38.06.055(a)), but, on the other hand, they also provide that a report of the Royalty Board

"shall be submitted for legislative review at the time of [sic] resolution for legislative approval of a proposed disposition of royalty oil and gas is introduced in the legislature" (AS 38.06.070(c)). Since legislative approval is required anyway as a matter of contract, I believe it only prudent to present this contract for legislative approval and ratification at this time.

Sincerely,


Bill Sheffield
Governor

STATE OF ALASKA
FISCAL NOTE

Revision Date , 1983

I. REQUEST

Bill/Resolution No.: HB 320
 Title: Approving Cook Inlet royalty oil agreement
 Sponsor: Governor
 Requestor: Governor

II. FISCAL DETAIL

Agency Affected: Natural Resources
 Program Category Affected: Mgmt. of Enerc
 BRU, Program of Subprogram(s) Affected: Oil & Gas Mgmt.

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 COMMODITIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL OPERATING	0	0	0			
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER (Specify Source)						
	0	0	0			

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						
	0	0	0			

III. SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

IV. ANALYSIS: Attach a separate page for any Analysis

Prepared By: Mark Wittow *Mark Wittow* Phone: 465-2400
 Division: Commissioner's Office, DNR Date: 3/30/83
 Approved by Commissioner: Maureen Holleran Date: 3/30/83
 Department: Natural Resources

Distribution:

Original to Legislative Finance
 Copy to Office of Management and Budget (for Legislature introduced bills)
 Copy to Department (for Governor introduced bills)
 Copy to Sponsor



HE 370

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

April 19, 1983

The Honorable Joe L. Hayes
Speaker of the House
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Mr. Speaker:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill which provides for legislative approval of a royalty oil contract between the state and Chevron, U.S.A., Inc. for the sale of Prudhoe Bay royalty oil.

This contract is described in the findings entitled "Proposed Disposition of Royalty Oil, Chevron, U.S.A." issued by the Department of Natural Resources on March 16, 1983. Copies of these findings have been made available to the legislature and the public for review.

This contract is being submitted for legislative approval for two reasons. First, although this and the previous administration have consistently taken the position that the statutory requirement of legislative approval of royalty oil contracts is unconstitutional (AS 38.06.055), as a matter of comity I respect the legislature's desire to have a direct voice in major disposals of royalty oil. Therefore, this contract contains provisions requiring approval by the legislature before it becomes effective. Second, this bill would ratify the agreement for the sale of oil. This ratification would cure any procedural defect that may have occurred in the process of entering into this contract.

Although we believe that all necessary steps have been taken, the statutes and regulations governing the disposal of royalty oil represent often conflicting desires and goals, both procedural and substantive. For example, even if statutorily requiring legislative approval were constitutional, the present statutes provide, on the one hand, that the legislature is to approve the contract by enacting legislation (AS 38.06.055(a)), but, on the other

hand, they also provide that a report of the Royalty Board "shall be submitted for legislative review at the time of [sic] resolution for legislative approval of a proposed disposition of royalty oil and gas is introduced in the legislature" (AS 38.06.070(c)). Since legislative approval is required anyway as a matter of contract, I believe it only prudent to present this contract for legislative approval and ratification at this time.

Sincerely,



Bill Sheffield
Governor

STATE OF ALASKA
FISCAL NOTE

Revision Date _____, 1983

I. REQUEST

Bill/Resolution No.: HB 370
 Title: Chevron Prudhoe Bay Unit Royalty
 Sponsor: Governor Oil Agreement
 Requestor: Governor

II. FISCAL DETAIL

Agency Affected: Natural Resource Mgmt
 Program Category Affected: Mgmt of Energy
 BRU, Program of Subprogram(s) Affected: Oil and Gas Management

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 COMMODITIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL OPERATING	0	0	0	0		
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER (Specify Source)	0	0	0	0		

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						
	0	0	0	0		

III. SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

IV. ANALYSIS: Attach a separate page for any Analysis

Prepared By: Mark Wittow *Mark Wittow* Phone: 465-2400
 Division: Commissioner's Office, DNR Date: 4/8/83
 Approved ^{for} Commissioner: Maughallera Date: 4/18/83
 Department: Natural Resources

Distribution:

Original to Legislative Finance
 Copy to Office of Management and Budget (for Legislature introduced bills)
 Copy to Department (for Governor introduced bills)
 Copy to Sponsor
 Copy to Requestor (if different from Sponsor)

AGO 786502



116371

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

April 19, 1983

The Honorable Joe L. Hayes
Speaker of the House
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Mr. Speaker:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill which provides for legislative approval of a royalty oil contract between the state and Tesoro Alaska Petroleum Company for the sale of Prudhoe Bay royalty oil.

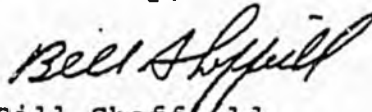
This contract is described in the findings entitled "Proposed Disposition of Royalty Oil, Tesoro Alaska Petroleum Company" issued by the Department of Natural Resources on March 16, 1983. Copies of these findings have been made available to the legislature and the public for review.

This contract is being submitted for legislative approval for two reasons. First, although this and the previous administration have consistently taken the position that the statutory requirement of legislative approval of royalty oil contracts is unconstitutional (AS 38.06.055), as a matter of comity I respect the legislature's desire to have a direct voice in major disposals of royalty oil. Therefore, this contract contains provisions requiring approval by the legislature before it becomes effective. Second, this bill would ratify the agreement for the sale of oil. This ratification would cure any procedural defect that may have occurred in the process of entering into this contract.

Although we believe that all necessary steps have been taken, the statutes and regulations governing the disposal of royalty oil represent often conflicting desires and goals, both procedural and substantive. For example, even if statutorily requiring legislative approval were constitutional, the present statutes provide, on the one hand, that the legislature is to approve the contract by enacting legislation (AS 38.06.055(a)), but, on the other

hand, they also provide that a report of the Royalty Board "shall be submitted for legislative review at the time of [sic] resolution for legislative approval of a proposed disposition of royalty oil and gas is introduced in the legislature" (AS 38.06.070(c)). Since legislative approval is required anyway as a matter of contract, I believe it only prudent to present this contract for legislative approval and ratification at this time.

Sincerely,

A handwritten signature in cursive script that reads "Bill Sheffield".

Bill Sheffield
Governor

STATE OF ALASKA
FISCAL NOTE

Revision Date _____, 1983

I. REQUEST

Bill/Resolution No.: HB 371
 Title: Tesoro Prudhoe Bay Unit Royalty Oil Agreement
 Sponsor: Governor
 Requestor: Governor

II. FISCAL DETAIL

Agency Affected: Natural Resource Mgmt.
 Program Category Affected: Mgmt. of Energy
 BRU, Program of Subprogram(s) Affected: Oil and Gas Management

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 COMMODITIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL OPERATING	0	0	0	0		
CAPITAL						
REVENUE						

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER (Specify Source)	0	0	0	0		

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						
	0	0	0	0		

III. SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

IV. ANALYSIS: Attach a separate page for any Analysis

Prepared By: Mark Wittow *Mark Wittow* Phone: 465-2400
 Division: Commissioner's Office, DNR Date: 4/8/83
 Approved by Commissioner: *Mark Wittow* Date: 4/8/83
 Department: Natural Resources

Distribution:

- Original to Legislative Finance
- Copy to Office of Management and Budget (for Legislature introduced bills)
- Copy to Department (for Governor introduced bills)
- Copy to Sponsor
- Copy to Requestor (if different from Sponsor)

AGO 786506

RECEIVED
JAN 5 1983

EXHIBIT C

Department of STOCKHOLDERS AGREEMENT
Natural Resources

This Stockholders Agreement is entered into this 26th day of January, 1983, between CHARTER SECURITY LIFE INSURANCE COMPANY, a New Jersey corporation, and CHARTER SECURITY LIFE INSURANCE COMPANY (NEW YORK), a New York corporation (collectively "Charter" and individually "the Purchasers") and TESORO PETROLEUM CORPORATION, a Delaware corporation ("Tesoro").

W I T N E S S E T H:

WHEREAS, Charter has agreed to purchase from Tesoro and Tesoro has agreed to sell to Charter 2,875,000 shares of Tesoro's \$2.20 Cumulative Convertible Preferred Stock (the "Preferred Stock") pursuant to, and in accordance with, a Purchase Agreement (the "Purchase Agreement") dated January 26, 1983 between Tesoro and Charter; and

WHEREAS, as contemplated by the Purchase Agreement, Tesoro and Charter wish to provide for certain arrangements with respect to the Preferred Stock and any shares of common stock (the "Common Stock") of Tesoro which Charter may receive upon conversion of the Preferred Stock or may otherwise acquire from time to time, including the 504,000 shares of Common Stock owned by Charter on the date hereof (such shares of Common Stock and the Preferred Stock are hereinafter referred to as the "Stock") and with respect to certain relationships between Tesoro and Charter;

NOW, THEREFORE, Tesoro and Charter agree as follows:

Section 1. Representations and Warranties.

1.1 Representations and Warranties of Tesoro.
Tesoro hereby represents and warrants to Charter as follows:

(a) Tesoro is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware.

(b) The authorized capital stock of Tesoro consists of (i) 50,000,000 shares of Tesoro common stock, of which at January 1, 1983, 13,708,403 shares were validly issued and outstanding, fully paid and nonassessable and no shares were held in Tesoro's treasury and (ii) 5,000,000 series preferred shares, with no par value, of which, at January 1, 1983, 40,000 were designated 8% Convertible Preferred Stock, of which 1,000 were validly issued and outstanding, 4,600,000 were designated \$2.16 Cumulative Convertible Preferred Stock, of which 1,323,862 were validly issued and outstanding. In addition, at January 1, 1983, an aggregate of 1,620,619 shares of Tesoro common stock and 200,000 shares of \$2.16 Cumulative Preferred Stock (including authorized but unissued shares and treasury shares) were reserved for issuance pursuant to currently existing and future stock incentives, under currently existing stock incentive plans and an aggregate of 2,473,902 shares were reserved for issuance upon conversion of Tesoro's preferred shares and convertible debentures. There are outstanding no other options, warrants, rights or convertible securities providing for the issuance of Tesoro capital stock.

(c) Tesoro has full legal right, power and authority to enter into and perform this Agreement, and the execution and delivery of this Agreement by Tesoro and the consummation of the transactions contemplated hereby have been duly authorized by the Board of Directors of Tesoro and require no other action by the Board of Directors or stockholders of Tesoro. This Agreement constitutes a valid and binding agreement of Tesoro.

1.2 Representations and Warranties of Charter.
Charter hereby represents and warrants to Tesoro as follows:

(a) Each of the Purchasers is a corporation duly organized, validly existing and in good standing under the laws of their respective states of incorporation as set forth above.

(b) Charter has full legal right, power and authority to enter into and perform this Agreement, and the execution and delivery of this Agreement by Charter and the consummation of the transactions contemplated hereby have been duly authorized by the Board of Directors of Charter and require no other action by the Board of Directors or stockholders of Charter. This Agreement constitutes a valid and binding agreement of Charter, except that no representation or warranty is made that the restrictions contained in Sections 3.1, 3.2 and 3.3 of this Agreement will be enforceable.

Section 2. Covenants of Charter with Respect to the Stock and Other Matters.

2.1 Restrictions on Resale or Other Disposition.

Until the Expiration Date (as defined in Section 4.1) or the early termination of this Agreement pursuant to Section 4.2 or Section 4.4. Charter covenants and agrees that for so long as it or any of its affiliates owns, directly or indirectly, any Stock or any voting securities of Tesoro (any and all voting securities of Tesoro, including the Stock, are hereinafter referred to as the "Tesoro Voting Securities"), or any other Tesoro securities convertible into or exchangeable or exercisable for the purchase of Tesoro Voting Securities (all such other Tesoro securities and the Tesoro Voting Securities are hereinafter referred to as the "Tesoro Restricted Securities"), Charter and its affiliates will not sell, transfer, pledge, hypothecate or otherwise dispose of any Tesoro Restricted Securities, or any beneficial interest therein, except with the prior written consent of Tesoro. Such consent shall be conclusively presumed and may not be withdrawn by Tesoro, if the proposed sale, transfer, pledge, hypothecation or other disposition is to occur pursuant to:

(a) a public offering of Stock pursuant to the registration rights granted under the Registration Rights Agreement between Tesoro and Charter dated January 26, 1983 (the "Registration Rights Agreement") made in accordance with Section 2.2; or

(b) sales of Stock made in accordance with Rule 144 of the General Rules and Regulations of the Securities and Exchange Commission under the Securities Act of 1933, as amended (the "Securities Act") or sales in conventional brokerage transactions made in compliance with all applicable securities laws, provided that such sales are made in accordance with Section 2.2 and further provided that Charter shall notify Tesoro at least two days prior to the date of entering any such sale or transfer order by Charter, and provided further that, if Tesoro shall thereupon notify Charter of the pendency of a sale under any public offering by it of any Tesoro Voting Securities, and if the managing underwriter of such public offering shall advise Charter that in its good faith judgment sales by Charter pursuant to this paragraph (b) would make it impracticable to conduct Tesoro's public offering at the price at which the securities to be sold in such public offering could be sold without such sales by Charter pursuant to this paragraph (b), neither Charter nor any of its affiliates shall effect any sales pursuant to this paragraph (b) within 10 days prior to the commencement of or during such offering; or

(c) sales of Stock pursuant to a tender offer or exchange offer which the Board of Directors of Tesoro does not oppose; or

(d) sales of Stock which are exempt from the registration provisions of the Securities Act, provided that no sales of Stock shall be made to any person or group (within the meaning of the Securities Exchange Act of 1934, as amended (the "Exchange Act")), if Charter knows, or upon the exercise of its best efforts, should have known, that the person or group purchasing such Stock owns, or will own, directly or indirectly, following such sale, Tesoro Voting Securities having an aggregate of 5% or more of the voting power of all of the then outstanding Tesoro Voting Securities (assuming for the purposes of such calculation that all Tesoro securities which may, by their terms, be converted into Tesoro Voting Securities without the payment to Tesoro of any consideration, have been so converted) and provided that, prior to making such sales, Charter and its affiliates comply with the provisions of Section 2.3 hereof; or

(e) sales of Stock which are exempt from the registration provisions of the Securities Act, provided that each person purchasing such Stock executes and is bound by an agreement with Tesoro which contains the provisions and restrictions of this Stockholders Agreement and provided that, prior to making such sales, Charter and its affiliates comply with the provisions of Section 2.3 hereof.

2.2 Covenant with Respect to Distribution of Shares. In any transaction or transactions described in Section 2.1(a) or (b), the seller of Stock will use its best efforts to effect the sale or transfer of such Stock in a manner which will effect the broadest possible distribution, with no sales or transfers of Stock to any one person or group (within the meaning of the Exchange Act) in excess of 3% of the then outstanding Tesoro Voting Securities.

2.3 Right of First Refusal. Prior to any sale of shares of Stock pursuant to Sections 2.1(d) or (e), Charter or its affiliates shall notify Tesoro, in writing (the "Purchase Notice"), of their intention to sell such Stock, stating the identity of the purchaser, the price at which the shares of Stock are to be sold, the proposed manner in which sales will be made, the number of shares of Stock to be sold, the proposed closing date for such sales (which closing date may be set by Charter irrespective of any time periods relating to actions to be taken by Tesoro as set forth in Section 2.4) and the other terms and conditions of the sale. In the event that sales are to be made to more than one purchaser, a separate Purchase Notice shall be given with respect to each purchaser. Tesoro shall have, during the periods specified in Section 2.4, the right and option to purchase all, but not less than all, of the shares

of Stock covered by any Purchase Notice in the manner set forth in Section 2.4. In the event that Tesoro notifies Charter that it does not intend to exercise its option or if it does not exercise its option within the periods specified in Section 2.4, Charter and its affiliates may sell the shares covered by the Purchase Notice, at no less than the price, in substantially the manner and to the purchaser specified in the Purchase Notice, provided that such sales are consummated within 120 days of the written notification to Charter by Tesoro that Tesoro does not intend to exercise its option or the failure by Tesoro to exercise its option within the time periods specified in Section 2.4.

2.4 Exercise of First Refusal Right. Tesoro may exercise its right and option arising under Sections 2.3, 4.3(a), 4.3(b) and 4.5 by giving Charter notice in writing ("Notice of Exercise"), within the 15 day period following receipt by Tesoro of the Purchase Notice, of Tesoro's election, subject, if Tesoro so desires, to obtaining financing for the purchase, to exercise its option to purchase all, but not less than all, of the shares covered by the Purchase Notice. The Notice of Exercise shall state the amount and terms of the financing, if any, which Tesoro shall require in connection with its purchase. Tesoro shall use its best efforts during the period ending 60 days after the receipt by Tesoro of the Purchase Notice, to obtain financing in the amount and on the terms specified in the Notice of Exercise. If Tesoro shall arrange financing within such period on terms at least as favorable to Tesoro as those specified in the Notice of Exercise, Tesoro shall, or if Tesoro has not been able within such period to arrange such financing, Tesoro may, at its option, notify Charter of its irrevocable election to purchase the shares covered by the Purchase Notice and shall specify the closing date for the purchase, which shall be a date not more than 90 days after the date on which the Purchase Notice was delivered to Tesoro. On such closing date, Charter shall deliver or cause to be delivered the certificate or certificates representing the appropriate number of shares, endorsed in blank or with appropriate stock powers attached, to Tesoro, or to such other purchaser as Tesoro shall designate to Charter, in writing, against payment of the purchase price by certified or official bank check payable in New York Clearing House funds. The purchase price payable for any shares purchased pursuant to this Section 2.4(c) shall be an amount in cash equal in value to the price set forth in the Purchase Notice, with any property, notes, securities or other non-cash consideration included in the price set forth in the Purchase Notice being valued by agreement between Tesoro and Charter or, in lieu of such agreement, by a nationally recognized investment banking firm agreeable to Tesoro and Charter, plus, with respect to shares of Preferred Stock, the dividends which have accrued and remained unpaid on the shares of Preferred Stock to be purchased during the period

between the proposed closing date specified in the Purchase Notice and the actual closing date for the purchase of such shares by Tesoro. With respect to shares of Common Stock purchased by Tesoro, Tesoro shall pay to Charter, at the end of the fiscal quarter in which the actual closing date occurred, the pro rata (based on the number of days such shares of Common Stock were owned by Charter during such fiscal quarter) amount of the dividends, if any, that would have been paid on the shares of Common Stock purchased by Tesoro had they been owned by Charter during all of such fiscal quarter. In the event that Tesoro shall fail to give a Notice of Exercise within the 15 day period set forth above, or having given such Notice of Exercise, shall fail to notify Charter of its irrevocable election to purchase the shares covered by the Purchase Notice within the 60 day period from the receipt by Tesoro of the Purchase Notice as set forth above, then Charter may sell the shares covered by the Purchase Notice in the manners specified in Sections 2.3, 4.3(a) and 4.3(b).

Section 3. Voting, Ownership and Other Restrictions.

3.1 Obligation to be Counted for Quorum. Charter agrees, as a stockholder, to be present, and to use its best efforts to cause its affiliates who are stockholders of Tesoro to be present, in person or to be represented by proxy, at all stockholder meetings of Tesoro so that all shares of Tesoro Restricted Securities beneficially owned by Charter or its affiliates may be counted for the purpose of determining the presence of a quorum at such meetings.

3.2 Voting by Charter. Charter and its affiliates agree, as stockholders, if so requested by the Board of Directors of Tesoro, to vote or cause to be voted all Tesoro Restricted Securities beneficially owned by them in the same proportion as the votes cast by or on behalf of all other holders of Tesoro Voting Securities, except that Charter and its affiliates may vote at all times in their discretion with respect to any matter that would materially and adversely affect Charter if it did not own Tesoro securities and with respect to any amendment of the Certificate of Incorporation or By-Laws of Tesoro which imposes limitations on the legal rights of Charter as a Tesoro stockholder, other than those imposed pursuant to the terms hereof, based on the size of security holdings or other considerations applicable to Charter and not to security holders of Tesoro generally.

3.3 Certain Agreements of Charter. Charter and its affiliates shall not, unless the prior written consent of the Board of Directors of Tesoro has been obtained (and then only to the extent such written consent has been obtained):

AGO 786512

(a) solicit proxies or become a "participant" in a "solicitation" (as such terms are defined in Regulation 14A under the Exchange Act) in opposition to the recommendation of the Board of Directors of Tesoro with respect to any matter; or

(b) deposit any Tesoro Voting Securities in a voting trust or subject them to a voting agreement or other arrangement of similar effect; or

(c) acquire or offer to acquire or agree to acquire, directly or indirectly, by purchase or otherwise, any Tesoro Restricted Securities, if after such acquisition Charter and its affiliates would own, directly or indirectly, Tesoro Voting Securities representing more than 30% of the combined voting power of all Tesoro Voting Securities (assuming for the purposes of such calculation that all Tesoro securities which may, by their terms, be converted into Tesoro Voting Securities without the payment to Tesoro of any consideration, have been so converted); or

(d) join or permit any affiliate of Charter to join a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding or disposing of Tesoro Voting Securities within the meaning of Section 13(d) of the Act unless such partnership, limited partnership, syndicate, or other group consists solely of Charter and its affiliates; or

(e) initiate, propose or otherwise solicit stockholders for any matter at any time, or induce or attempt to induce any other person to initiate any stockholder proposal or a tender offer for shares of Tesoro securities or any change of directors or control of Tesoro, or for the purpose of convening a stockholders' meeting of Tesoro; or

(f) acquire, other than for investment purposes, by purchase or otherwise, shares representing more than 5% of the voting power of all of the voting securities of any entity, if Charter or its affiliates know, or in the exercise of their best efforts, should have known, that such entity and its affiliates are the beneficial owner of Tesoro Voting Securities having an aggregate of 5% or more of the voting power of all of the then outstanding Tesoro Voting Securities; or

(g) take any action as a Tesoro stockholder by written consent in lieu of a meeting.

3.4 Legend and Stop Transfer Order. To assist in effectuating the provisions of this Agreement, Charter and its affiliates hereby consent:

(a) to the placement of the following legend on all certificates representing ownership of Tesoro Restricted Securities beneficially owned by Charter or its affiliates until such shares have been sold, transferred or disposed of pursuant to the requirements of Section 2 hereof, at which time Tesoro will promptly remove such legend:

The shares represented by this certificate are subject to the provisions of an Agreement among Tesoro Petroleum Corporation, Charter Security Life Insurance Company and Charter Security Life Insurance Company (New York), and may not be sold, transferred, pledged, hypothecated or otherwise disposed of except in accordance therewith. A copy of said Agreement is on file at the office of the Secretary of Tesoro Petroleum Corporation.

(b) to the entry of a stop transfer order with the transfer agent or agents of Tesoro securities against the transfer of the Tesoro Restricted Securities except in compliance with the requirements of this Agreement, which stop transfer order shall be removed promptly from the shares being transferred upon transfer in compliance with the requirements of this Agreement, or if Tesoro is its own transfer agent with respect to any Tesoro Restricted Securities, to the refusal by Tesoro to transfer any such securities except in compliance with the requirements of this Agreement.

3.5 Certain Agreements of Tesoro. Tesoro agrees that it will not, at any time prior to the earlier of the Expiration Date (as defined in Section 4.1 hereof) or any early termination of this Agreement pursuant to Section 4.2 or Section 4.4 hereof, unless the prior written consent of Charter has been obtained, acquire or offer to acquire or agree to acquire, directly or indirectly, by purchase or otherwise, any voting securities of The Charter Company.

Section 4. Term of Agreement; Certain Provisions Regarding Termination.

4.1 Term of Agreement. Except as otherwise provided in Section 4.2 or Section 4.4, the respective covenants and agreements of Charter and its affiliates and Tesoro contained in this Agreement will continue in full force and effect from the date first above written until January 25, 1993 (such date being referred to herein as the "Expiration Date"). Upon the Expiration Date, unless there is an early termination of this Agreement pursuant to Section 4.2 (in which case the continuing rights and obliga-

tions of Charter and its affiliates and Tesoro shall be governed by Section 4.3) or Section 4.4 (in which case the continuing rights and obligations of Charter and its affiliates and Tesoro shall be governed by that Section), all rights and obligations of Charter and its affiliates and Tesoro shall terminate except as specifically provided in Section 4.5.

4.2 Early Termination. Charter may, at its sole option, 10 days after written notice (the "Termination Notice") has been received by Tesoro, terminate this Agreement prior to the Expiration Date, if one of the following events has occurred:

(i) if, in Charter's opinion, there is a change in the members of Tesoro's senior officer group which significantly affects the business strategy or prospects of Tesoro;

(ii) if, at any time, in the opinion of Charter's independent public accountants, Charter may no longer account for its ownership of Tesoro Common Stock using the equity method (Charter's accountants shall assume, for the purpose of making this determination, that the number of shares of Tesoro Voting Securities held by Charter is the number that would be obtained if it were assumed that Charter initially purchased 2,875,000 shares of Preferred Stock and 1,625,000 shares of Common Stock and that Charter made no transfers or other dispositions (other than conversions of Preferred Stock to Common Stock) of any Tesoro Restricted Securities held by it from the time of such initial purchase to the time of the determination);

(iii) if any one of the individuals designated by Charter and accepted by Tesoro, pursuant to Section 5 below, for election to the Board of Directors of Tesoro, is not nominated for election as a director or is not elected as a director of Tesoro (other than by reason of such individual's incapacity or unwillingness to serve);

(iv) if, at any time, Tesoro shall be in default in the payment of dividends on the Preferred Stock in an amount equivalent to or exceeding four quarterly dividends (whether or not consecutive) and Charter shall, at such time, own any shares of Preferred Stock;

(v) if, at any time, Tesoro shall be adjudicated as bankrupt or insolvent, or admit in writing its inability to pay its debts as they mature, or make an assignment for the benefit of creditors, or shall apply for or consent to the appointment of any receiver, trustee, or similar officer for it or for all or any

substantial part of its property, or such receiver, trustee or similar officer shall be appointed without the application or consent of Tesoro or Tesoro shall institute any bankruptcy, insolvency, readjustment of debt or similar proceeding relating to the rights of creditors or if any such proceedings shall be commenced against Tesoro and shall remain undismissed for 60 days; or

(vi) if, at any time, indebtedness of Tesoro (except indebtedness as to which there is no recourse against Tesoro or any of its subsidiaries and except an amount of purchase money mortgage indebtedness not exceeding in the aggregate the lesser of (i) 5% of the total assets of Tesoro and its subsidiaries on a consolidated basis or (ii) \$50 million, which indebtedness was incurred with respect to special project financings and with respect to which the only recourse is against subsidiaries of Tesoro formed specifically to accommodate such financings) in an amount in excess of \$10 million shall become due and payable, by reason of a default, prior to the date on which such indebtedness was, by its terms, to become due and payable or if, at any time, Tesoro shall receive a notice that such an amount of indebtedness will become due and payable, by reason of a default, prior to the date on which such indebtedness was, by its terms, to become due and payable, and such notice shall not be properly waived or withdrawn within 30 days of its receipt by Tesoro.

Ten days after receipt by Tesoro of the written notice by Charter pursuant to this Section 4.2 electing to terminate this Agreement, unless such notice shall have been rescinded by Charter in writing, all rights and obligations of Tesoro and Charter under this Agreement shall terminate except as shall be provided in Section 4.3. hereof. For purposes of clause (i), "senior officer group" shall mean executives at or above the level currently designated as group vice president; also, the retirement or other loss of members of senior management who at the date of this Agreement are age 63 or older shall not be the basis for a Termination Notice.

4.3 Rights of Tesoro and Charter Upon Early Termination. If, at any time prior to the Expiration Date, Charter shall terminate this Agreement pursuant to Section 4.2 above, the following provisions shall apply:

(a) Right of First Refusal. Prior to any sale by Charter or its affiliates of shares of Common Stock pursuant to Sections 2.1(d) or (e) or pursuant to a bona fide offer by a person unaffiliated with Charter to purchase shares of Common Stock, other than sales pursuant to Sec-

tions 2.1(a), (b) or (c), which sale is to occur during the two year period following the effective date of the early termination of this Agreement pursuant to Section 4.2 but in no event later than the Expiration Date (the "Common Stock Restricted Period") and prior to any sale by Charter or its affiliates of shares of Preferred Stock pursuant to Sections 2.1(d) or (e) or pursuant to a bona fide offer by a person unaffiliated with Charter to purchase shares of Preferred Stock, other than sales pursuant to Sections 2.1(a), (b) or (c), which sale is to occur during the five year no call period of the Preferred Stock (the "Preferred Stock Restricted Period"), Charter or its affiliates shall notify Tesoro in writing (the "Purchase Notice") of such proposed sale, naming the prospective purchaser, stating the price at which the shares are to be sold, the number of shares sought to be purchased and the other terms and conditions of the proposed sale. In the event that sales are to be made to more than one prospective purchaser, a separate Purchase Notice shall be given with respect to each prospective purchaser. Tesoro shall have, during the periods specified in Section 2.4, the right and option to purchase all, but not less than all, of the shares covered by any Purchase Notice in the manner set forth in Section 2.4. In the event that Tesoro notifies Charter that it does not intend to exercise its option or if it does not exercise its option within the periods specified in Section 2.4, Charter or its affiliates may sell the shares covered by the Purchase Notice to the purchaser at no less than the price and in substantially the manner specified in the Purchase Notice, provided that such sale is consummated within 120 days of the written notification to Charter by Tesoro that Tesoro does not intend to exercise its option or the failure by Tesoro to exercise its option within the time periods specified in Section 2.4.

(b) Right of Repurchase. Tesoro shall have the right, during the Common Stock Restricted Period, to repurchase any or all shares of Common Stock of Tesoro owned by Charter or its affiliates on the effective date of the early termination of this Agreement or received thereafter upon conversion of Preferred Stock. Tesoro may exercise this right of repurchase by notifying Charter in writing (the "Repurchase Notice") of such intention, which Repurchase Notice shall set a closing date for the repurchase of the shares covered by such Repurchase Notice, which closing date shall be a date not less than 120 days or more than 180 days after the date of the Repurchase Notice. If during the 90 day period following the receipt by Charter of the Repurchase Notice Charter or its affiliates shall receive a bona fide offer by a person unaffiliated with Charter to purchase any or all of the shares covered by the Repurchase Notice, which offer Charter or its affiliates intends to accept, then Charter shall notify Tesoro of such offer by means of a Purchase Notice in the manner provided in subparagraph (a) above and Tesoro shall have the right and

option to purchase all, but not less than all of the shares covered by such offer as provided in subparagraph (a) above. Tesoro may purchase at the closing date specified in the Repurchase Notice any or all shares covered by the Repurchase Notice for which no bona fide offer is received by Charter or its affiliates during the 90 day period following receipt by Charter of the Repurchase Notice at a price per share which shall equal 110% of the average closing price for a share of Tesoro Common Stock on the New York Stock Exchange for the 10 trading days immediately preceding such purchase. On the closing date specified in the Repurchase Notice, Charter or its affiliates shall deliver or cause to be delivered the certificate or certificates representing the appropriate number of shares, endorsed in blank or with appropriate stock powers attached, to Tesoro, or to such purchaser as Tesoro shall designate to Charter, in writing, against payment of the purchase price by certified or official bank check payable in New York Clearing House funds.

(c) Restrictions on Transfer. Charter or its affiliates shall not sell, assign or otherwise transfer any shares of Common Stock during the Common Stock Restricted Period or any shares of Preferred Stock during the Preferred Stock Restricted Period except in the manner provided in paragraphs (a), (b), (c), (d) and (e) of Section 2.1 or pursuant to bona fide offers by persons unaffiliated with Charter after complying with the provisions of this Section 4.3.

(d) Restrictions on Purchase. During the Preferred Stock Restricted Period, so long as Charter or its affiliates shall own any shares of Preferred Stock, Charter and its affiliates shall continue to be subject to the restrictions contained in Section 3 hereof. If Charter or its affiliates shall desire that such restrictions shall no longer apply, Charter shall notify Tesoro in writing (the "Restrictions Notice") of such desire. Tesoro shall have the right and option, for a period of 60 days following the receipt of the Restrictions Notice, to purchase any or all of the shares of Preferred Stock owned by Charter or its affiliates at the price of \$20 per share plus accrued and unpaid dividends, if any. Tesoro may exercise this right and option by giving Charter notice in writing of Tesoro's election, which notice shall specify the number of shares of Preferred Stock to be purchased and the closing date for the purchase, which shall be a date not more than 90 days after the receipt by Tesoro of the Restrictions Notice. Tesoro may pay the purchase price of the shares of Preferred Stock, by delivery to Charter at the closing of, (i) a certified or official bank check (the "Check") payable in New York Clearing House funds for at least 20% of the aggregate purchase price and (ii) a note (the "Note") for the remaining amount of the aggregate purchase price. The Note shall bear interest at the rate that Charter would charge in a loan to a

company with a credit rating comparable to Tesoro at the date the Restrictions Notice is received by Tesoro. The principal amount of the Note shall be payable in equal annual installments, plus all accrued and unpaid interest, on each succeeding anniversary of the closing date, provided that Tesoro shall pay any unpaid principal amount and all accrued and unpaid interest on the last day of the Preferred Stock Restricted Period and provided that the principal amount of the Note, or any portion thereof, may be prepaid without penalty at any time. Upon delivery to Charter of the Check and the Note, if applicable, on the closing date, Charter and its affiliates shall deliver or cause to be delivered the certificate or certificates representing the appropriate number of shares, endorsed in blank or with stock powers attached, to Tesoro or to such other person as Tesoro shall designate to Charter, in writing. If Tesoro shall have assigned its right to purchase any of the shares covered by the Restrictions Notice to any other purchaser, Tesoro shall unconditionally guaranty all the obligations of such purchaser under the Note, if any, delivered to Charter at the closing. Upon such a closing, or if Tesoro shall have not elected to purchase any shares of Preferred Stock, on the date 61 days after the receipt by Tesoro of the Restrictions Notice, Charter and its affiliates shall cease to be subject to the restrictions contained in Section 3 hereof.

4.4 Other Termination. If, at any time, the Tesoro Voting Securities held by Charter or its affiliates shall represent less than 5% of the voting power of all the then outstanding Tesoro Voting Securities, both Tesoro and Charter shall have the option, during such time as Charter or its affiliates shall continue to own Tesoro Voting Securities representing less than 5% of the voting power of all the then outstanding Tesoro Voting Securities, to terminate this Agreement by written notification to the other party. Ten days after the receipt of such written notice by the other party all rights and obligations of Tesoro and Charter under this Agreement shall terminate.

4.5 Rights of Tesoro and Charter Upon Expiration. After the Expiration Date, for so long as Charter or its affiliates own any of the shares of Stock that were owned by them on the Expiration Date, unless this Agreement has been terminated prior to the Expiration Date pursuant to Section 4.2 (in which case the continuing rights and obligations of Charter and its affiliates and Tesoro shall be governed by Section 4.3) or Section 4.4 (in which case the continuing rights and obligations of Charter and its affiliates and Tesoro shall be governed by that Section), Charter and its affiliates shall not transfer any shares of Stock that were owned by Charter or its affiliates on the Expiration Date, or any interest therein, except pursuant to a bona fide sale. Tesoro shall have a right of first refusal with re-

spect to any such bona fide sales ("Restricted Transfers") except sales of Stock made by Charter or its affiliates in the manner specified in Sections 2.1(a), (b), (c) or (d); provided that with respect to any sale of stock in the manner specified in Section 2.1(d), such sale need not comply with Section 2.3. Prior to any Restricted Transfer, Charter or its affiliates shall notify Tesoro, in writing (the "Purchase Notice") of their intention to sell such Stock, stating the identity of the purchaser, the price at which the shares of Stock are to be sold, the proposed manner in which sales will be made, the number of shares of Stock to be sold, the proposed closing date for such sales (which closing date may be set by Charter irrespective of any time periods relating to actions to be taken by Tesoro as set forth in Section 2.4) and the other terms and conditions of the sale. In the event that sales are to be made to more than one purchaser, a separate Purchase Notice shall be given with respect to each purchaser. Tesoro shall have, during the periods specified in Section 2.4, the right and option to purchase all, but not less than all, of the shares of Stock covered by any Purchase Notice in the manner set forth in Section 2.4. In the event that Tesoro notifies Charter that it does not intend to exercise its option or if it does not exercise its option within the periods specified in Section 2.4, Charter and its affiliates may sell the shares covered by the Purchase Notice, at no less than the price, in substantially the manner and to the purchaser specified in the Purchase Notice, provided that such sales are consummated within 120 days of the written notification to Charter by Tesoro that Tesoro does not intend to exercise its option or the failure by Tesoro to exercise its option within the time periods specified in Section 2.4.

Section 5. Election of Directors. Tesoro agrees that it will nominate and use its best efforts to the end that two individuals (or, if the total number of directors of Tesoro other than those designated by Charter shall equal or exceed 15, three individuals) designated by Charter and reasonably acceptable to Tesoro shall be, at all times, members of the Board of Directors of Tesoro; provided, however, that at any time when Charter and its affiliates beneficially own shares of Tesoro Voting Securities with less than an aggregate of 1,850,000 votes but more than an aggregate of 925,000 votes, Charter shall have the right to designate one such individual (or, if the total number of directors of Tesoro other than those designated by Charter shall equal or exceed 15, two individuals) and Charter shall use its best efforts to cause one of its designees on the Tesoro Board of Directors to resign forthwith; and provided, further, however, that at any time when Charter and its affiliates beneficially own shares of Tesoro Voting Securities with an aggregate of 925,000 votes or less, Charter shall not have the right to designate any such person and Charter shall use its best efforts to cause its designee or

designees on the Tesoro Board of Directors to resign forthwith. Charter's rights under this Section 5 shall be in addition to any rights which Charter may have as a holder of Preferred Stock.

Section 6. General

6.1 Specific Enforcement; Other Remedies. (a) Charter acknowledges and agrees that Tesoro would be irreparably damaged in the event any of the provisions of this Agreement were not performed by Charter and its affiliates in accordance with their specific terms or were otherwise breached. It is accordingly agreed that Tesoro shall be entitled to an injunction or injunctions to prevent breaches of the provisions of this Agreement and to enforce specifically the terms and provisions hereof in any court of the United States or any state thereof having jurisdiction, in addition to any other remedy to which Tesoro may be entitled at law or equity.

(b) In the event any of the provisions of this Agreement are not performed by Tesoro in accordance with their specific terms or are otherwise breached, Charter and its affiliates shall be entitled to an injunction or injunctions to prevent breaches of the provisions of this Agreement and to enforce specifically the terms and provisions thereof or seek recovery of money damages in any court of the United States or any state thereof having jurisdiction, in addition to any other remedy to which Charter and its affiliates may be entitled at law or equity, provided that any such nonperformance or breach shall not entitle Charter to terminate this Agreement prior to the Expiration Date unless such non-performance or breach was willful and material and further provided that no action taken by Tesoro which constitutes an event specified in Section 4.2 or which causes an event specified in Section 4.2 to occur, shall entitle Charter to terminate this Agreement except in the manner specified in Section 4.2.

6.2 Severability. If any term, provision, covenant or restriction of this Agreement is held by a court of competent jurisdiction to be invalid, void, or unenforceable, the remainder of the terms, provisions, covenants and restrictions shall remain in full force and effect and shall in no way be affected, impaired or invalidated. It is hereby stipulated and declared to be the intention of the parties that they would have executed the remaining terms, provisions, covenants and restrictions without including any of such which may be hereafter declared invalid, void or unenforceable.

6.3 Definitions. As used herein the term "affiliate" shall have the meaning set forth in Rule 12b-2 under the Exchange Act and shall also include any person

acting on behalf of a person or its affiliate, the term "person" shall mean any individual, partnership, corporation, trust or other entity and the term "voting power" shall refer to the ordinary right of the holder of a security to vote for the election of directors (without reference to any special rights which may arise with respect to defaults in the payment of dividends or defaults under any other terms of preferred stock).

6.4 Amendments. This Agreement may be amended only by an agreement in writing.

6.5 Descriptive Headings. Descriptive headings are for convenience only and shall not control or affect the meaning or construction of any provision of this Agreement.

6.6 Counterparts. For the convenience of the parties, any number of counterparts of this Agreement may be executed by either party hereto and each such executed counterpart shall be, and shall be deemed to be, an original instrument.

6.7 Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of and be enforceable by the successors and assigns of the parties hereto except that Tesoro may only assign its rights of repurchase and first refusal set forth in Sections 2.3, 4.3 and 4.5 in the manner provided in those Sections.

6.8 Transfers. Nothing in this Agreement shall prohibit transfers of Tesoro Voting Securities among Charter and controlled affiliates of Charter, so long as all limitations and covenants herein on the part of Charter shall apply to such controlled affiliates to the same extent as they apply to Charter.

6.9 Accounting Matters. Tesoro will, and will cause its employees, independent public accountants and other representatives to, provide all information and any certificates or documents to, and otherwise cooperate with, Charter so as to enable Charter to (i) account for its investment in Tesoro pursuant to the equity method, (ii) prepare financial statements and related information in accordance with generally accepted accounting principles and with statutory accounting principles applicable to insurance companies and (iii) to comply with its reporting requirements and other disclosure obligations under applicable laws and regulations. In that regard, Tesoro acknowledges and agrees not to dispute that Charter has the ability, by virtue of its ownership of Stock or its representation on Tesoro's Board of Directors, to influence the management of Tesoro. Nothing in this Section 6.9 shall restrict the right of Tesoro to issue its securities at any time.

6.10 Redemption of Preferred Stock. Until the Expiration Date or the effective date of any early termination of this Agreement, Tesoro will not, so long as Charter or its affiliates own any shares of Preferred Stock, redeem any shares of Preferred Stock without the prior written consent of Charter.

6.11 Effect of Stock Splits, etc. Whenever any rights under this Agreement are available only when at least a specified minimum number of Tesoro Voting Securities or votes is involved, such specified number shall be appropriately adjusted to reflect any stock split, stock dividend, combination of securities into a smaller number of securities or reclassification of stock.

6.12 Notices. Any notice to be given hereunder shall be deemed sufficiently given when in writing and delivered to an officer of Tesoro or Charter, transmitted by tested telecopier, telex or TWX, or deposited in the United States mail, postage prepaid and registered or certified and addressed as set forth below in this Section 6.12 or to such other address for a party as may be specified in a notice. Tested telecopier, telex and TWX notices shall be effective upon transmission and notices delivered personally to an officer of Charter or Tesoro shall be effective when given. Notices that are mailed shall be effective upon receipt or upon rejection by the party to whom addressed:

To Tesoro:

Tesoro Petroleum Corporation
8700 Tesoro Drive
San Antonio, Texas 78286
Attn: Chairman of the Board

To Charter:

Charter Security Life Insurance Company
21 West Church Street
Jacksonville, Florida 32202
Attn: President

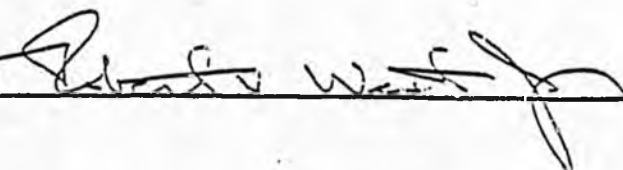
with a copy to:

Smith & Hulsey
500 Barnett Bank Building
Jacksonville, Florida 32202
Attn: E. Ellis Zahra, Jr., Esq.

6.13 Counterparts. This Agreement may be executed simultaneously in one or more counterparts, each of which shall be deemed an original.

IN WITNESS WHEREOF, Tesoro and Charter have caused this Agreement to be duly executed by their respective officers, each of whom is duly and validly authorized and empowered, all as of the day and year first above written.

TESORO PETROLEUM CORPORATION

By 

CHARTER SECURITY LIFE INSURANCE
COMPANY

By _____

CHARTER SECURITY LIFE INSURANCE
COMPANY (NEW YORK)

By _____

The Charter Company agrees that it and its affiliates who are not otherwise parties to this agreement will be bound by the restrictions placed upon them as set forth in this agreement.

THE CHARTER COMPANY

By: _____

ALASKA ROYALTY OIL AND GAS DEVELOPMENT ADVISORY BOARD

Resolution 83-3

WHEREAS, the State of Alaska, through the Commissioner of the Alaska Department of Natural Resources, and Chevron U.S.A. Inc. have entered into an "Agreement for the Sale and Purchase of Royalty Oil" dated the 16th day of March 1983; and

WHEREAS, in accordance with AS 38.06.055(a) "... the Commissioner of Natural Resources may not enter into a sale, exchange, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas under AS 38.05.183 without the prior approval of the Legislature ..."; and

WHEREAS, according to AS 38.06.055(a), "... a sale, exchange, encumbrance, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas may not be made by the Commissioner of Natural Resources under AS 38.05.183 without prior review of the proposed sale, exchange, encumbrance or other disposition by the Board. A written recommendation of the Board on the proposed sale, exchange, encumbrance or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas shall be submitted to the Legislature at the time a resolution approving the proposed sale, exchange, encumbrance, or other disposition is introduced in the Legislature"; and

WHEREAS, in accordance with AS 38.06.040(a), the Board shall

"(2) hold public hearings on proposed sales, exchanges, or other disposals of royalty oil or gas to determine whether the proposals comply with AS 38.06.070;

(3) examine proposed sales, exchanges or other disposal or, and recommend to the Legislature that it approve or disapprove a proposed sale, exchange or other disposal of

(A) the oil or gas that is obtained by the State as royalty under AS 38.05.183; or

(B) the rights to receive future oil or gas production under State Leases"; and

WHEREAS, the Board did on March 17, 1983 receive from the Commissioner of Natural Resources the above-mentioned agreement with Tesoro as well as a document entitled "Proposed Disposition of Royalty Oil, Tesoro Alaska Petroleum Company, Findings and Determinations Required for Disposals of Royalty Oil", dated March 16, 1983 and the Board did act and call public hearings, in accordance with the regulations outlined in 3 ACC 56, in Juneau and by teleconference in Fairbanks, Anchorage, and Kenai on April 5, 1983 and received public comment pertinent to this agreement; and

WHEREAS, in accordance with AS 38.06 and AS 38.05, the Commissioner of Natural Resources is required to submit to the Board, in writing, certain Findings or Determinations relating to the disposal of oil and gas royalty interests and the Board has received the required Findings and Determinations; and

WHEREAS, the board members had the opportunity to review the agreement, related Findings and Determinations and Public Testimony during the period March 17, 1983 until April 20, 1983; and

WHEREAS, the Board did, on April 20, 1983, meet to discuss the agreement, related Findings and Determinations, and Public Testimony to insure that this disposal is in accordance with the statutory purpose and criteria set forth in AS 38.06 as well as the Board's "Basic Principles and Policies" as outlined in the Board's development plan.

THEREFORE, the Board finds as follows:

1. that the Commissioner of Natural Resources has followed the board policies, applicable statutes, and regulations relating to the disposal of oil and gas royalty interests.
2. that the sale of the royalty oil interests to Chevron U.S.A. Inc., as per the agreement, was made because:
 - (a) the oil is to be refined or processed in the existing Chevron refinery near Kenai, Alaska.
 - (b) Chevron is an in-state refiner which supplies products to the Alaska market with supply benefits to state citizens.
 - (c) the price the State will receive for this royalty interest appears to be substantially equivalent to or greater than the price the State would receive by taking this royalty in-value.
 - (d) that Chevron is a qualified company which has been operating its refinery to produce products for the Alaska market for many years.
 - (e) Chevron has advised the State that its refining system is short of crude and without additional crude supplies the closure of the Nikiski refinery might be imminent. It is in the State's interest to have the refinery continue to operate.
 - (f) Chevron is the State's only road asphalt producer and closure of the refinery would eliminate the State's only local supplier.
 - (g) that this agreement is consistent with the criteria outlined in AS 38.06.070.

Resolution 83-2

WHEREAS, the State of Alaska, through the Commissioner of the Alaska Department of Natural Resources, and the Tesoro Alaska Petroleum Company have entered into an "Agreement for the Sale and Purchase of Royalty Oil" dated the 16th day of March, 1983; and

WHEREAS, in accordance with AS 38.06.055(a) "... the Commissioner of Natural Resources may not enter into a sale, exchange, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas under AS 38.05.183 without the prior approval of the Legislature ..."; and

WHEREAS, according to AS 38.06.055(a), "... a sale, exchange, encumbrance, or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas may not be made by the Commissioner of Natural Resources under AS 38.05.183 without prior review of the proposed sale, exchange, encumbrance or other disposition of oil or gas or of the rights or waiver of the rights to receive future production of royalty oil or gas shall be submitted to the Legislature at the time a resolution approving the proposed sale, exchange, encumbrance, or other disposition is introduced in the Legislature"; and

WHEREAS, in accordance with AS 38.06.040(a), the Board shall

"(2) hold public hearings on proposed sales, exchanges, or other disposals of royalty oil or gas to determine whether the proposals comply with AS 38.06.070;

(3) examine proposed sales, exchanges or other disposal of, and recommend to the Legislature that it approve or disapprove a proposed sale, exchange or other disposal of

(A) the oil or gas that is obtained by the State as royalty under AS 38.05.182; or

(B) the rights to receive future oil or gas production under State leases"; and

WHEREAS, the Board did, on March 17, 1983 receive from the Commissioner of Natural Resources the above-mentioned agreement with Tesoro as well as a document entitled "Proposed Disposition of Royalty Oil, Tesoro Alaska Petroleum Company, Findings and Determinations Required for Disposals of Royalty Oil", dated March 16, 1983 and the Board did act and call public hearings, in accordance with the regulations outlined in 3 ACC 56, in Juneau and by teleconference in Fairbanks, Anchorage, and Kenai on April 5, 1983 and received public comment pertinent to this agreement; and

WHEREAS, in accordance with AS 38.06 and AS 38.05, the Commissioner of Natural Resources is required to submit to the Board, in writing, certain Findings or Determinations relating to the disposal of oil and gas royalty interests and the Board has received the required Findings and Determinations; and

WHEREAS, the board members had the opportunity to review the agreement, related Findings and Determinations and Public Testimony during the period March 17, 1983 until April 20, 1982; and

WHEREAS, the Board did, on April 20, 1983, meet to discuss the agreement, related Findings and Determinations, and Public Testimony to insure that this disposal is in accordance with the statutory purpose and criteria set forth in AS 38.06 as well as the Board's "Basic Principles and Policies" as outlined in the Board's development plan.

THEREFORE, the Board finds as follows:

1. that the Commissioner of Natural Resources has followed the Board policies, applicable statutes, and regulations relating to the disposal of oil and gas royalty interests.
2. that the sale of the royalty oil interests to Tesoro Alaska Petroleum Company, as per the agreement, was made because:
 - (a) the oil is to be refined or processed in the Tesoro refinery near Kenai, Alaska.
 - (b) Tesoro-Alaska is an in-state refiner which supplies products to the Alaska market with supply benefits to State citizens.
 - (c) the sale is made to support Tesoro-Alaska's refinery expansion plans to increase the capacity from the current 48,500 BPD to approximately 80,000 BPD. The construction program is expected to include a new crude distillation tower, expansion of the hydrocracker from 7,500 to 9,000 BPD, a hydrogen plant to produce 14 million cubic feet of hydrogen from natural gas, and a sulfur plant to recover and produce 14.2 tons per day of sulfur. Necessary offsite facilities, such as tankage, pipelines, etc., to support the expansion also are to be constructed. The expansion has an announced cost of \$80-90 million and is to be completed to mid-1984.
 - (d) the price the State will receive for this royalty interest appears to be substantially equivalent to or greater than the price the State would receive by taking this royalty in value.
 - (e) that Tesoro-Alaska is a qualified company which has been operating its refinery to produce products for the Alaska market for over 13 years.
 - (f) that this agreement is consistent with the criteria outlined in AS 38.06.070.

AND THEREFORE BE IT RESOLVED THAT the Alaska Royalty Oil and Gas Development Advisory Board recommends to the Thirteenth Alaska Legislature that the "Agreement for the Sale and Purchase of Royalty Oil" between the State of Alaska and Tesoro-Alaska Petroleum Company, dated March 16, 1983 be approved.

Board Member Jack Roderick moved the adoption of the Resolution. Board Member Richard Lyon seconded. The vote was as follows:

APPROVE

DISAPPROVE

<u>Don Tringali</u>	_____
<u>Joseph K. Donohue</u>	_____
<u>John R. Roderick</u>	_____
_____	_____
_____	_____
_____	_____

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH M
JUNEAU, ALASKA 99811
PHONE: 907/465-2400

Pursuant to the Alaska Statutes and the recommendations of the Alaska Royalty Oil and Gas Development Advisory Board, the Commissioner of the Alaska Department of Natural Resources intends to sell the State's royalty oil from Cook Inlet. The Commissioner desires to sell the oil competitively to someone able to process the crude within the State of Alaska or supply products in-state from crude processed elsewhere. Preference will be given to companies capable of processing the crude in Alaska. Only in the case of an exceptional premium would he consider selling it for export from the State.

The amount of crude oil available over the term of the contract will vary with production. The Cook Inlet field is in decline, and it is anticipated that the volume of oil that will be available for sale on January 1, 1984, will be approximately 6,900 barrels per day (b/d). The volume will decline to approximately 2,700 b/d by 1990.

At the present time, the Cook Inlet royalty crude oil is committed by contract to Tesoro Alaska Petroleum. The Tesoro contract, which expires on December 31, 1983, has been in effect since 1970. Tesoro currently processes the crude in its refinery at Kenai, Alaska.

The price of the oil, if sold, will be no less than in-value. The sale is being considered under Title 38 of the Alaska statutes and the regulations contained in 11 AAC 03, and potential buyers should be aware of those provisions.

In addition to the statutory criteria, the financial responsibility of the bidders will be considered and initial information relating to such responsibility should be submitted with the proposal.

It is anticipated that negotiations may begin with the qualified respondents shortly after the close of the solicitation period and that a contract will be finalized in February, 1983, for submittal to the 13th Alaska Legislature. Because of the short timeframe for negotiations and submittal of a contract to the Legislature, proposals must be as specific as possible and should include price, volume and term of

contract. The purchaser of the royalty oil must be able to process or begin supplying products in-state by January 1, 1984.

The Commissioner may reject submitted proposals at any time after receipt of the proposals, and may not hold negotiating sessions with every prospective buyer who submits a proposal. To the extent possible provisions of the Prudhoe Bay standard form contract will be included in any contract negotiated. The State's policy regarding royalty oil is discussed in the document prepared in February, 1982, entitled "Review of Alaska Royalty Oil Policy and Findings for Proposed Disposition of Royalty Oil." Copies of this document and further information can be obtained by contacting:

Lennie Boston
Special Assistant to the Commissioner
Department of Natural Resources
Pouch M
Juneau, Alaska 99811
(907) 465-2400

Responses to this solicitation must be received by the Commissioner of Natural Resources at the above address by close of business on December 17, 1982.

John W. Katz
John W. Katz, Commissioner
Department of Natural Resources

11/16/82
Date

Union 76 Division

Union Oil Company of California
Union Oil Center, Box 7600, Los Angeles, California 90051
Telephone (213) 977-6560



R. C. Beach
Vice President
76 Division Crude Supply

December 10, 1982

Commissioner Esther C. Wunnicke
Department of Natural Resources
State of Alaska
Pouch M
Juneau, Alaska 99811

Dear Commissioner Wunnicke:

This letter is in response to your department's solicitation of November 16, 1982, for the sale and purchase of Alaska Cook Inlet area royalty oil commencing January 1, 1984.

Union Oil Company is a major supplier of petroleum products throughout the State of Alaska. Although we will not be able to process the royalty oil within the State, we believe the proposal below will help provide a secure supply of petroleum products to our customers in Alaska.

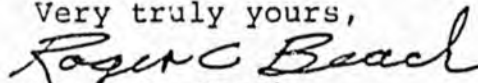
Proposal

1. The State of Alaska will sell and Union will purchase the full volume of the State's Cook Inlet area royalty oil commencing January 1, 1984.
2. Contract term will be firm for a period of five years.
3. Price paid by Union for the royalty oil will be Union's posted price.

If this response to your solicitation is of interest to the State, Union is prepared to meet with you and pursue the matter further.

Thank you for your consideration. We look forward to meeting with you in Juneau at an early date.

Very truly yours,


Roger C. Beach

RCB:jv

AGO 786535

Shell Oil Company



Two Shell Plaza
P.O. Box 2099
Houston, Texas 77001

December 10, 1982

Mr. John W. Katz, Commissioner
Department of Natural Resources
State of Alaska
Pouch M
Juneau, Alaska 99811

Dear Mr. Katz:

This responds to your solicitation letter of November 16, 1982, for proposals to purchase Cook Inlet royalty crude oil beginning January 1, 1984. Shell has carefully considered this matter and has decided not to make a proposal.

Even though Shell could physically transport this crude to its West Coast refineries and process it, it is a higher quality crude than we will require in 1984 and beyond. It is better suited to the Alaskan refineries designed to run it, while Shell's West Coast refineries are more economically suited to heavier crudes - especially California and Alaskan North Slope (ANS) crudes. In addition, unit transportation costs for the relatively low volumes of Cook Inlet royalty crude would be high.

We take this opportunity, however, to re-state our continuing interest in purchasing ANS royalty crude from the State of Alaska. We stand behind our proposal of October 7, 1982, to purchase 20 MB/D of ANS crude and to supply products, as needed, on a one-year term, and stand ready to negotiate a longer-term arrangement. We have been encouraged by recent discussions with you and your staff, and are especially interested in pursuing an arrangement whereby Shell would enter the Alaskan asphalt market in a substantial way.

We appreciate your inclusion of Shell in your solicitation of potential Cook Inlet crude purchasers and we look forward to an opportunity to further develop Shell's ANS crude purchases/product sales proposal to you and the incoming administration.

Most sincerely,

W. L. Kreps, Manager
Trading & Scheduling
Domestic Raw Materials Supply

AGO 786536

Mr. John W. Katz, Commissioner
State of Alaska

2

bc: M. J. Nevill
R. C. McMahan
O. Runnels
A. J. McNemar
C. G. Chew
R. T. Klope
R. A. Broderick
T. C. Moody
R. J. Bertus
D. R. Salzman
G. R. Nemetz
A. M. Raymond
J. F. Hall



Chevron U.S.A. Inc.
575 Market Street, San Francisco, CA 94105

Robert F. Walsh
Vice-President
Supply and Distribution

December 13, 1982

Commissioner John W. Katz
Department of Natural Resources
State of Alaska
Pouch "M"
Juneau, AK 99811

Dear Commissioner Katz:

This is in response to your November 16, 1982 solicitation for proposals to purchase Cook Inlet royalty oil starting January 1, 1984.

Chevron's proposal to purchase the Cook Inlet royalty oil is briefly summarized below:

Volume: Entire volume of royalty oil estimated to be about 6,900 BPD in January 1984 and declining to about 2,700 BPD by 1990.

Term: Six (6) years ending December 31, 1989 but Chevron is open to consider other periods.

Price: Chevron will pay the same price the State would have received if the State had taken the oil in value from the producers. This would be a weight average producer in-value price.

Additional Consideration: Chevron will commit to make available for sale in Alaska our historic level of aviation gasoline during the term we are purchasing the Cook Inlet royalty oil.

Chevron has been awarded 18,000 BPD of ANS royalty oil for processing at our Nikiski Alaska refinery under a one year contract starting about May 30, 1983. Consequently, we could not process the Cook Inlet royalty oil in-state for a short period of time between January 1, 1984 and May 30, 1984. Chevron is both an in-state-refiner as well as a large in-state supplier of refined products that are produced in our California refineries and shipped to Alaska. As the Alaskan demand for products has increased, Chevron has shipped to Alaska as much as 15,000 BPD of gasoline, heating fuels and aviation gasoline. We currently supply about 40% of the motor gasoline, 30% of the heating and distillate fuels and 80% of the aviation gasoline used in Alaska.

Chevron was the first company to market petroleum products in Alaska starting in 1889 and has served Alaska continuously since that time. We are the only statewide marketer in Alaska and are the sole supplier of petroleum products in eighteen (18) Alaskan communities.

AGO 786538

December 13, 1982

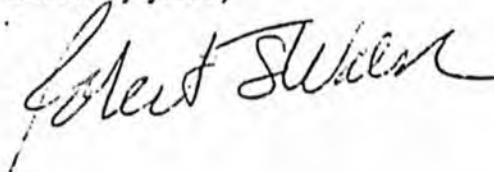
In support of our consideration to continue to make aviation gasoline available for sale in Alaska, we offer the following comments. None of the Alaskan refineries produce aviation gasoline. Consequently, in-state processing of Cook Inlet royalty oil to produce the Alaskan requirements for aviation gasoline cannot be achieved and aviation gasoline will have to be imported to Alaska from California. At least one historic supplier has already withdrawn from some of the aviation gasoline market in Alaska, leaving a greater responsibility on the remaining marketers. Chevron sincerely believes aviation gasoline is essential to the growth and economy in Alaska -- particularly in the Bush communities -- and a commitment by Chevron to meet these requirements is of great value to the State of Alaska. We hope the State will give this aviation gasoline commitment the proper consideration.

Chevron and the State spent considerable time during the past couple of years negotiating a long term agreement to purchase 38,000 BPD of ANS royalty oil. Although an agreement was not finalized, it is still of considerable interest to us. There may be some inter-relationship between a long term agreement for ANS royalty oil and the present solicitation for Cook Inlet royalty oil. Accordingly, Chevron would like the opportunity to discuss this overall royalty oil subject with the appropriate Department of Natural Resources representatives. We would appreciate a meeting in early January 1983 before any decision is made on the Cook Inlet royalty oil disposition.

Attached is a copy of the 1981 annual Report for Standard Oil Company of California (parent company of Chevron U.S.A.). We believe this will meet the request for initial information on the financial responsibility of bidders for Cook Inlet royalty oil.

Please contact Messrs. R. J. Alfrey or R. J. Engelhart at (415) 944-6204 regarding any questions on this proposal for Cook Inlet royalty oil and to set a meeting date in Juneau for discussions on the overall royalty oil subject.

Sincerely yours,



RJA:dw
Attachment