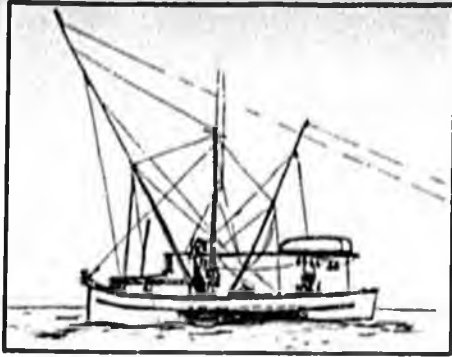


ALASKA LEGISLATURE COMMITTEE FILES 1991-1992 8672
7205 HOUSE RESOURCES



Alaska Trollers Association

RECEIVED MAY 7 1992

REPRESENTING ALASKA TROLLERS

130 Seward St., No. 213
Juneau, Alaska 99801
(907) 586-9400

May 5, 1992

Representative Cliff Davidson, Chairman
House Resources Committee
State Capitol
Juneau, AK 99801-1182

Dear Representative Davidson,

The Alaska Trollers Association watches with dismay as SB423 seems to breeze through every obstacle between it and legislative approval. The measure passed the Senate with no opposition, despite an almost uniform show of no support from the Senate Special Committee on Domestic and International Commercial Fisheries.

The criteria laid out in SB423 leaves the practice of temporary permit transfers open to abuse, and it sets a serious precedent. ATA opposes any bill that sets a precedent for permit leasing. Permit leasing has the potential to place increased pressure on Alaska's salmon stocks by encouraging more people to fish permits which have been inactive. Although the limited entry program set a maximum on the number of permits issued in the salmon fisheries, optimum numbers have never been determined, and many fisheries are already troubled with too many participants to maintain viability. The troll fleet is a prime example.

Alaska is currently seeing a high abundance of chinook, but the US/Canada Treaty has our trollers squirming under a restrictive quota. There are less summer chinook than ever to go around, and the troll fleet simply cannot support any additional effort. Yet, this measure could add an additional 63 active boats to the troll fishery. Lower 48 fishermen are in the midst of a complete crisis, which will disrupt troll fisheries from California to the Canadian border this season. The chinook abundance here could make it worthwhile for southern fishermen to lease a permit in Alaska until their fisheries stabilize. This spring the Board of Fisheries allocated chinook salmon between troll and sport fishermen, with trollers receiving an 8% cut from their historic harvest share. A decreased allocation, coupled with increased effort, could be disastrous for our fleet.

ATA empathizes with seniors who have legitimate health problems. A fisherman's lifestyle is physically demanding, and it can take its toll, especially in later years. However, a temporary transfer system could be exploited by healthy seniors. What criteria will be used to determine which illness or disability is appropriate to trigger a lease arrangement?

Finally, this measure is the foothold permit brokers need to wrench open our closed permit system. Left alone, it's plausible many seniors who meet the criteria would choose not to lease their permits. However, we share the concerns of CFEC that permit brokers would launch an aggressive campaign to urge leasing by seniors who may be enticed by the income earning potential of their dormant permits.

We urge you to consider this measure carefully. While this appears to be a bill that gives senior citizens a break, it may in fact represent a new and revolutionary chapter in the way Alaska manages its permit system.

Sincerely,

Dale A. Kelley
Executive Director

TO: Hon. Bill Hudson
House of Representatives
State of Alaska
M/S: 3100

DATE: May 6, 1992

FAX NO: 789-6170

TELEPHONE NO: 789-6160

ATTN: Landa B. Holtan

SUBJECT: CSSB 423

FROM: Commercial Fisheries
Entry Commission R.F.I.
Rich Listowski, Commissioner
M/S: 0302

CSSB 423 will allow only permanent permit holders 65 years of age and older the right to lease a permit year-to-year without supervision from the CFEC for reasons of illness or disability. The bill may have the following impacts on the commercial fisheries:

1. Increase in the cost of permits as the supply of permits decreases while the demand for permits rises or remains constant.
2. Increase in the amount of gear being fished as retired elderly permit holders lease their permits to the highest bidder.
3. Marginal permit holders over 65 years of age presently engaged in the fishery will be encouraged to retire and lease their permits to younger and more aggressive fishers thereby increasing effort.
4. Inflation of permit prices caused by leasing will add to the already high cost of permits and further prevent young rural people from entering a local fishery.
5. Leasing of permits will create a absentee landlord class of permit holders. In 5 years, approximately 13% of the total permits issued could fall under the leasing provision. This could become a public relations problem when the fishing industry becomes involved in legal disputes or resource allocation controversies with other industry or user groups.
6. Seattle permit brokers will benefit from a relaxation of anti-leasing provisions now in the statute as they expand their businesses from brokering of permit transfers to include brokering of leased permits. They will be able to obtain a list of names and addresses from the Commission of permit holders over 65 years of age.
7. CSSB 423 may violate the equal protection clause in the State Constitution. The Attorney General Office has not rendered an opinion on the constitutionality of this leasing proposal.
8. Legislative intent at the passage of limited entry law intended for the permit holder to be an active participant in the fishery. The limited entry program was never calculated when passed into law in 1973 to become a social program or a retirement plan by its supporters in the administration, the Legislature, or the commercial fishing industry.

STATE OF ALASKA

COMMERCIAL FISHERIES ENTRY COMMISSION

WALTER J. HICKEL, GOVERNOR

8800 GLACIER HIGHWAY, #109
JUNEAU, ALASKA 99801
(907) 789-6150 Licensing Calls
(907) 789-6160 Other CFEC Calls
(907) 789-6170 FAX

May 1, 1992

The Honorable Jay Hammond
Lake Clark Lodge
Port Alsworth, AK 99853

Dear Governor Hammond:

You recall that, when we met earlier this year, you were concerned about older limited entry permit holders who suffered disabilities which prevented them from fishing. Some of them wanted to obtain medical emergency transfers for more than one year in a row. They did not want to be forced into an untimely and improvident permanent transfer of their entry permits. As you know, under our statute the general rule is that an individual can be granted a medical emergency transfer for only one season for a given medical condition, unless extraordinary circumstances can be found in subsequent years.

We advised you that we had been able to help a number of such people based on a case from the Bristol Bay area. There was a grandfather who held a permit which he was no longer capable of fishing. He wanted to permanently transfer the permit to his grandson. However, the grandson had not yet reached an age where the grandfather could reasonably transfer the permit to him. The grandfather wanted to be able to obtain emergency transfers of his permit until his grandson reached a suitable age to hold and fish the permit. Because the transfer of a permit to a member of one's family is an intended purpose of the Limited Entry Act, we were pleased to find an exception to the one-year requirement for the grandfather. We have ruled the same way on a number of similar cases.

You indicated that this commission practice would help people you were concerned about and would obviate the need for legislation on this subject. You indicated, however, that the commission's practice was not sufficiently known to people who might benefit, and you asked the commission to make this information more widely available. We agreed to do so.

I wanted you to know that we have begun to make good on that commitment. I was given 45 minutes on the agenda of the Bristol Bay Native Association's Bristol Bay Fisheries Conference this spring in Dillingham. A principal part of my presentation consisted of explaining our practice. I urged those in attendance to take the information back to their villages for the benefit of individuals in this situation. (I also made some

The Honorable Jay Hammond

-2-

May 1, 1992

other practical suggestions to help people get and keep limited entry permits in local communities, which I would be happy to discuss with you in detail, when we next have a chance to talk.)

In any event, I wanted you to know that we had begun to spread the information about how, under the existing program, the commission could help older individuals prevented from fishing their permits. We are sharing this letter with a number of interested legislators for the same purpose.

Cordially,

COMMERCIAL FISHERIES ENTRY COMMISSION

Bruce Twomley, Chairman
Rich Listowski, Commissioner
Frank Homan, Commissioner

by: 

cc: Bristol Bay Native Association
The Honorable Fred Zharoff
The Honorable Dick Eliason
The Honorable Lloyd Jones
The Honorable Lyman Hoffman
The Honorable Sam Cotten
The Honorable Cliff Davidson
The Honorable George Jacko

Re: SB 423 Temporary Transfer of Entry Permits

May 9, 1992

Hearing before House Resource Committee

I am Randy Briggs from Ugashik. I have been a commercial fisherman for 31 years. Chairman of the Lower Bristol Bay Advisory Committee for 20 years. I am speaking for myself and my family.

When Limited Entry came into being in 1973, no fisherman then fishing nor any legislators writing the law invisioned the fact that some provision also be made for temporary transfers for long time fishermen--where this was their only source of income, in fact--their way of life!

Provisions were made in statue after death and for minors, but no provision was made to cover the decline of physical activity of a fisherman who still wishes to stay involved in fishing, but physically can not be out in the vessel every minute the gear was being fished.

Now, 19 years later, a fisherman finds he can no longer continue as he or she has in the past. He doesn't wish to cut off his lifeline, but he can only get a temporary transfer for one or two years at most following a serious illness or accident. The following year the fisherman has to sell or sign over the permit or find another medical reason why he needs to transfer the permit. It is expensive to travel from remote villages to a medical facility to do this when needed.

This bill, SB 423 provides another option for the elder fisherman who may have days when he can't physically be on that boat. If a temporary transfer could be made to a family member, or a crewman, the boat could continue without the elder fisherman aboard.

Some argue "absentee ownership, that the person who owns the permit will make money off another person's labor." Fishing is a business. Show me a business today which doesn't make money off its employees.

There will be pressure on elder fishermen to keep the local permits in the local areas. In case of in-family transfers, the elder fisherman will still own the permit. Thus, the transferee will not be able to sell or mortgage the permit without permission.

I do not believe this bill is unconstitutional. Permit holders are now treated differently for temporary transfers.

1. Permanent permit holders can obtain temp. transfer for one year.
2. Interim use permit holders need only show hardship to transfer each year.
3. Permanent mobile gear holders must be on board at all times when fishing.
4. Fixed gear operators need only be in the general beach area.

Alaska already has other senior citizen benefits no one else has.

1. Longivity bonus is based in part on age.
2. Free hunting, fishing and trapping licenses--the 60-30 club.
3. Free automobile licenses for those over 60.
4. Senior citizens do not have to pay property tax in cities and buroughs.

It is unfortunate that so called bureaucratic agencies, bound by statue, are forced to make it so difficult for our senior fishermen to temporarily transfer their permit when needed on a year to year basis.

I urge you to pass this bill on for full house consideration.

Randy Briggs

SENATE BILL 423

Committee substitute for SB 423 addresses the concerns of commercial fishermen 65 years of age and over who suffer from age related physical disabilities.

CURRENT LAW A permanent permit holder fishing mobile gear must be present at all times when the gear is fished.

The emergency transfer of a permanent permit may be made only in case of illness or disability of a temporary, unexpected, and unforeseen nature, usually for one year, unless a different disability of unexpected nature occurs the following year.

EXCEPTIONS TO THE ABOVE L. Estates may emergency transfer the permit from year to year until the estate is settled.

2. Trustees of minors who inherit permits, may emergency transfer the permit year to year until the minor is 16 years of age.

3. The Limited Entry Commission tells us, interim use permit holders may emergency transfer the permit at any age because of illness or disability, or to simply alleviate a hardship on a year to year basis.

4. Fixed gear permit holders need only be in the general area when their gear is being fished. They are not required to actually participate physically.

CURRENT OPTION If a permanent permit holder suffers a disability which lasts more than a year the option is, sell the permit or give it away. In either case the permit holder must sign the permit over to the transferee with no recourse to repossess if agreement falls thru.

SENIOR FISHERMEN, ESPECIALLY MOBILE GEAR OPERATORS This bill is an attempt to cover by statute the senior fisherman, who, because of illness or disability, may need to slow down, not be present at all times or at best only part of the time when the gear is being fished.

Total Limited Entry Permits Issued (Excludes non transferable permits)		12,230
Total permit holders 65 and over (Incl. 109 permits not currently fished)	1062	8.7%
Total permit holders 60 to 64 (Incl. 75 permits not currently fished)	760	6.3%

A long time fisherman takes a great deal of pride in his fishing ability and in the ownership of a permit. It may be the only thing of great value which he or she owns. For many, fishing is a lifestyle. Most senior fishermen will wish to continue to be active even in a less physical manner. This bill will provide an opportunity for elder fishermen to impart their long term knowledge and still be involved in the fishing effort.

Because of the social structures in rural areas, it is believe this bill will help keep local permits in the local areas.

In case of in-family transfers, the elder fisherman will be provided time to make certain the family member appreciated the value of the permit and will not be able to sell or mortgage the permit immediately without permission.

S B

4 4 0

Alaska State Legislature

STEVE FRANK

119 N. Cushman, Rm. 213
Fairbanks, Alaska 99701
(907) 452-3421



Senate

White in Juneau
P.O. Box V
Juneau, Alaska 99811
(907) 465-3709
Capitol Rm. 417

SPONSOR STATEMENT

SB440

Senate Bill 440 would prohibit an individual from receiving an Alaska hunting, fishing, or trapping license (and appropriate permits or tags), or a guide-outfitting license if that person's right to obtain a hunting, fishing, trapping or guide-outfitting license is suspended or revoked in another state. Once the period of suspension or revocation on the out-of-state license expires, the individual is then eligible to receive the desired license in Alaska.

In practice this provision would be applied by adding a statement to the existing Alaska hunting/fishing/trapping license form requiring the applicant's signature verifying that his or her right to obtain a hunting, fishing or trapping license in another state has not been suspended or revoked. Guide-outfitters would sign a document required by the Big Game Commercial Services Board verifying that his or her right to obtain a hunting, fishing, trapping or guide-outfitting license is not suspended or revoked in another state.

Clearly, our state law enforcement officials and the courts take fish and game violations seriously. I believe Alaskans take pride in holding in high regard the value of our fish and game resources and in respecting the laws that apply to fishing, hunting and trapping. Adoption of Senate Bill 440 will further demonstrate our commitment to protecting Alaska's fish and game resources for the benefit of all law-abiding consumptive and non-consumptive users.

FISCAL NOTE

No. 1

Bill Version: SB440

(S) Publish Date: 4-1-92

STATE OF ALASKA
1992 LEGISLATIVE SESSION

Revision Date: 2/18/92

Department Affected: Fish and Game

Title: Issuance of Hunting and Fishing

BRU: Administration and Support

Licenses

Component: Administrative Services

Sponsor: Senator Frank

Requestor: Senate Resources
Expenditures/Revenues: (Thousands of Dollars)

COMPONENT SERIAL NO.

4	7	9
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OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL	0	0	0	0	0	0
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REVENUE FUND SOURCE:	0	0	0	0	0	0
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FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER FUND SOURCE:	0	0	0	0	0	0
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

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

Estimate of current year impact: None

ANALYSIS: (Attach a separate page if necessary.)

This fiscal note assumes that the Department of Fish and Game will not be expected to do any enforcement of this statute.

Prepared By: Geron Bruce

Phone: 465-4100

Division: Commissioner's Office

Date: 3/30/92

Approved by Commissioner: Carl Z. Rusini

Agency: Department of Fish and Game

Changes in CSSB440 (RES) have no fiscal impact. This fiscal note is appropriate.

Distribution (by Changes in CSSB440 (JUD) aster. CMB/D
have no fiscal impact. This fiscal note is appropriate.
date 4-15-92 JK
Comte Aide (initial)

3-31-92 TCO
date Comte Aide (initial)

FISCAL NOTE

Bill Version: CS5B 440 (TUD)

(S) Publish Date: 4-15-92

STATE OF ALASKA
1992 LEGISLATIVE SESSION

Revision Date: _____ Department Affected: Public Safety

Title: "An Act relating to the issuance of BRU: Fish and Wildlife Protection

sport fishing, hunting, or trapping licenses. " Component: Enforcement and ISU

Sponsor: Senator Frank

Requestor: Senator Frank COMPONENT SERIAL NO.

	4	9	0
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EXPENDITURES/REVENUES: (Thousands of Dollars) (inflation not included)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	-0-

CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
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REVENUE	-0-	-0-	-0-	-0-	-0-	-0-
FUND SOURCE:						

FUNDING: (Thousands of Dollars)

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

POSITIONS:

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

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

No impact upon the Division of Fish and Wildlife Protection is anticipated.

Prepared By: Captain C. Seibel Phone: 269-5682

Division: Fish and Wildlife Protection Date: 4/2/92

Approved by Commissioner: *Richard L. Burton* Richard L. Burton

Agency: Department of Public Safety Date: 4/2/92

STEVE FRANK

19 N. Cushman, Rm. 213
Fairbanks, Alaska 99701
(907) 452-3421

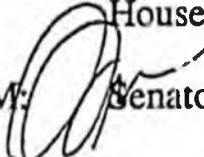
Alaska State Legislature



Senate

While in Juneau
P.O. Box V
Juneau, Alaska 99811
(907) 465-3709
Capitol Rm. 417

TO: Representative Cliff Davidson, Chairman
House Resources Committee

FROM:  Senator Steve Frank

RE: Senate Bill 440 - Issuance of hunting, fishing,
trapping or guide-outfitting licenses

DATE: April 24, 1992

I would like to request that a hearing be scheduled on CSSB 440 (Jud) in the House Resources Committee at your earliest convenience.

Senate Bill 440 would prohibit an individual from receiving an Alaska hunting, fishing, or trapping license (and appropriate permits or tags), or a guide-outfitting license if that person's right to obtain a hunting, fishing, trapping or guide-outfitting license is suspended or revoked in another state. Once the period of suspension or revocation on the out-of-state license expires, the individual is then eligible to receive the desired license in Alaska.

Clearly, our state law enforcement officials and the courts take fish and game violations seriously. Alaskans take pride in holding in high regard the value of our fish and game resources and in respecting the laws that apply to fishing, hunting and trapping. Adoption of Senate Bill 440 will further demonstrate our commitment to protecting Alaska's fish and game resources for the benefit of all law-abiding consumptive and non-consumptive users.

FISCAL NOTE

**STATE OF ALASKA
1992 LEGISLATIVE SESSION**

BILL NO. CSSB 440(RES)

Revision Date: _____ Department Affected: Public Safety
 Title: "An Act relating to the issuance of BRU: Fish and Wildlife Protection
sport fishing, hunting, or trapping licenses. . ." Component: Enforcement and ISU
 Sponsor: Senator Frank
 Requestor: Senator Frank COMPONENT SERIAL NO.

4	9	0
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EXPENDITURES/REVENUES: (Thousands of Dollars) (inflation not included)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	-0-

CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
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REVENUE FUND SOURCE:	-0-	-0-	-0-	-0-	-0-	-0-
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FUNDING: (Thousands of Dollars)

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

POSITIONS:

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

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

No impact upon the Division of Fish and Wildlife Protection is anticipated.

Prepared By: Captain C. Seibel Phone: 269-5682
 Division: Fish and Wildlife Protection Date: 4/2/92
 Approved by Commissioner: *Richard L. Burton* Richard L. Burton
 Agency: Department of Public Safety Date: 4/2/92

BILL NO: CSSB 440(RES)

DATE: April 9, 1992

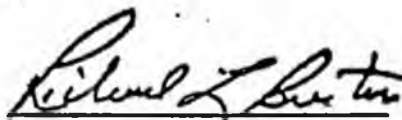
TITLE: "An Act relating to the issuance of sport fishing hunting, or trapping licenses. . ."

CONTACT: Gayle A. Horetski
Deputy Commissioner
465-4322

POSITION PAPER - Department of Public Safety

Passage of CSSB 440(RES) would prevent the issuance of a sport fishing, hunting, or trapping license or other permit or tag issued under AS 16.05.330 - 16.05.430, if the person's right to obtain, or exercise the privileges granted by, a sport fishing, hunting, or trapping license has been suspended or revoked in another state. This bill would require that any person applying for such a license, permit or tag sign a statement that the person's right to obtain, or exercise the privileges granted by a sport fishing, hunting, or trapping license is not suspended or revoked in another state.

Under current law a serious fish and game resource offender from another state may apply for and be issued a sport fishing, hunting, or trapping license, or a big game guide-outfitter related license, in Alaska. Serious resource violators frequently travel freely between states to illegally harvest fish and game. The Department of Public Safety supports preventing those resource violators whose fishing and hunting privileges have been suspended or revoked in another state from obtaining a license or permit to take wildlife in Alaska, and supports CSSB 440(RES).



Richard L. Burton
Commissioner

FISCAL NOTE

STATE OF ALASKA
1992 LEGISLATIVE SESSION

BILL NO. CSSB 440

Revision Date: 4/1/92

Department Affected: Fish and Game

Title: Issuance of Hunting and Fishing

BRU: Administration and Support

Licenses

Component: Administrative Services

Sponsor: Senator Frank

Requestor: Senate Judiciary
Expenditures/Revenues: (Thousands of Dollars)

COMPONENT SERIAL NO.

4	7	9
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OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL	0	0	0	0	0	0
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REVENUE FUND SOURCE:	0	0	0	0	0	0
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FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER FUND SOURCE:	0	0	0	0	0	0
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

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

Estimate of current year impact: None

ANALYSIS: (Attach a separate page if necessary.)

This fiscal note assumes that the Department of Fish and Game will not be expected to do any enforcement of this statute.

Prepared By: Geron Bruce G.B.

Phone: 465-4100

Division: Commissioner's Office

Date: 4/5/92

Approved by Commissioner: [Signature]

Agency: Department of Fish and Game

Date: 4/1/92

Distribution (by preparer): Leg. Fin., Legislative Sponsor, Requestor, OMB/DBR, Gov. Legis. OSC., & Impacted Agency(ies).

DEPARTMENT OF FISH AND GAME

POSITION PAPER

Bill Number: CSSB 440

Sponsor: Senator Frank

Bill Title: "An act relating to the issuance of sport fishing, hunting, or trapping licenses, permits, or tags to a person whose sport fishing, hunting, trapping, license is suspended or revoked in another state; and providing for an effective date."

Department Position: Support

Legislative Intent: This legislation would make it illegal for someone to apply for an Alaskan hunting, trapping, fishing license, or tag or permit, if that person's sport fishing, hunting or trapping license is currently revoked or suspended in another state.

Effects of legislation on department programs: This legislation would require the department to add a statement to the hunting, trapping and sport fishing license application, stating that the individual applying for the Alaska license does not currently have his fishing, hunting, or trapping license revoked or suspended in another state.

This legislation would add very little to the cost of the printing of sport fishing, trapping, and hunting licenses. The effective date of January 1, 1993 would give the department adequate time to revise its existing license forms, and add the appropriate statement to the form.

The department assumes that no investigation or enforcement activities by the department would be required by this legislation.

Commissioner's Signature

Paul Somerville Jr

Date

4/6/92

FISH & GAME POSITION PAPER

1-800-478-3377



**ALASKA FISH & WILDLIFE
SAFEGUARD**

5700 East Tudor Road, Anchorage, Alaska 99507
(907) 269-5540

March 30, 1992

Sen. Steve Frank
Alaska State Legislature
P.O. Box V
Juneau, AK 99811

Dear Sen. Frank:

As vice chairman of the statewide Alaska Fish and Wildlife Safeguard board, I'm writing today to convey the full support of our three regional boards for Senate Bill No. 440. We believe this legislation prohibiting persons with suspended fishing, hunting or trapping licenses in other states from obtaining such licenses here is long overdue and will serve as a further deterrent to violations of our laws.

We appreciate your efforts in sponsoring this valuable legislation.

Sincerely,

A handwritten signature in cursive script that reads "Fred E. Chase".

Fred E. Chase
State Vice Chairman
Alaska Fish and Wildlife Safeguard

TAKE AIM ON VIOLATIONS

S B

4 4 8

WALTER J. HICKEL
GOVERNOR



JVI

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

March 11, 1992

The Honorable Richard I. Eliason
President of the Senate
Alaska State Legislature
State Capitol
Juneau, AK 99801-1182

Dear President Eliason:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a bill that provides for legislative approval of a royalty oil contract between the state and Petro Star Valdez Refinery Joint Venture for the sale of Kuparuk River Unit royalty oil. Also transmitted with this bill is a copy of the resolution of the Alaska Royalty Oil and Gas Development Advisory Board recommending approval of that contract in accordance with AS 38.06.040(a)(3) and 38.06.050(a), and providing the report required by AS 38.06.070(c).

The contract is also described in the finding issued by the Commissioner of Department of Natural Resources on March 4, 1992. Copies of the Commissioner's preliminary finding and the draft contract have been sent to the Legislature and made available to the public for review. The Commissioner's final finding and the signed contract are attached.

A bill approving the contract is being introduced for legislative approval for two reasons. First, as a matter of comity, I respect the Legislature's desire to have a direct voice in major disposals of royalty oil. Therefore, although this and previous Administrations have consistently taken the position that the statutory requirement of legislative approval of royalty oil contracts (AS 38.06.055) is unconstitutional, the contract itself contains provisions requiring approval by the Legislature before it takes effect.

Second, this legislation would ratify the royalty oil contract. This ratification would cure any procedural defect that might have occurred in the process of entering into this contract.

I urge your prompt consideration and passage of this bill.

Sincerely,

A handwritten signature in cursive script that reads "Walter J. Hickel".

Walter J. Hickel
Governor

FISCAL NOTE

No. 2

Bill Version: SB 448

(S) Publish Date: 3-11-92

STATE OF ALASKA
1992 LEGISLATIVE SESSION

Revision Date: _____
Title: Approving the Sale of Kuparuk River Unit Royalty
Oil by the State of Alaska to Petro Star Valdez Refinery

Department Affected: Revenue
BRU: Revenue Operations
Component: Oil & Gas Audit

Sponsor: _____
Requestor: _____

Component Serial No.

0	1	1	5
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Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

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

REVENUE FUND SOURCE						
---------------------	--	--	--	--	--	--

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER FUND SOURCE						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS:

Prepared by: Robert L. Doss, Director

Phone: 276-1363 ext. 225

Division: Oil & Gas Audit Division

Date: Feb. 27, 1992

Approved by Commissioner: *David Axelrod*

Agency: Revenue

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

FISCAL NOTE

No. 1
 Bill Version: SR 448
 (S) Publish Date: 3-11-92

STATE OF ALASKA
 1992 LEGISLATIVE SESSION

Revision Date: _____ Department Affected: Natural Resources
 Title: Petro Star Royalty Oil Contract BRU: Petroleum Management
 Component: Petroleum Management
 Sponsor: Rules Committee for Governor
 Requestor: _____ COMPONENT SERIAL NO.

	1	3	9
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EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	-0-	-0-	-0-	-0-	-0-	-0-
TRAVEL	-0-	-0-	0	0	0	-0-
CONTRACTUAL	-0-	-0-	-0-	-0-	-0-	-0-
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	-0-

CAPITAL						
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REVENUE						
FUND SOURCE:						

FUNDING: (Thousands of Dollars)

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

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

Division of Oil and Gas staff handles a number of royalty-in-kind contracts. Existing staff will handle the proposed contract with Petro Star Valdez Refinery Joint Venture.

Prepared By: Bob Loeffler Phone: 762-2578
 Division: Oil and Gas Date: 2-27-92
 Approved by Commissioner: Harold C. Heinze Date: 2-27-92
 Agency: Natural Resources

Handwritten signature and date:
 HC
 2/27/92

Resolution 92-1

On January 23, 1992, the director of the division of oil and gas ("director") provided the Alaska Royalty Oil and Gas Development Advisory Board ("board") with preliminary findings and proposed contract for a long-term sale of up to about 30,000 barrels per day of Kuparuk River Unit royalty oil to Petro Star Valdez Refinery Joint Venture, a joint venture comprised of Petro Star Valdez, Inc., (a subsidiary of Arctic Slope Regional Corporation), Harbor Enterprises, Inc., and Alaska Refining, Inc. (collectively "joint venture"). The joint venture will process the oil in a refinery proposed for Valdez.

The proposed contract was discussed between representatives of the division of oil and gas (DOG) and the joint venture over the past year culminating in a draft contract. On January 23, 1992, the director made public the proposed contract and the Preliminary Finding and determination of the Commissioner of the Department of Natural Resources. The director notified the public that the proposed sale would be discussed at the board's meeting on February 6, 1992 and invited them to attend.

On February 6, 1992, the board met to discuss the sale and to take public comment on it. The meeting was attended by representatives of the DOG, representatives of the joint venture, and members of the public. The board received a presentation from the DOG staff regarding the proposed sale and contract, questioned the staff about them, and made several suggestions. The staff will implement those suggestions. At the conclusion of the discussion, the voting members of the board, who attended the meeting, unanimously approved the proposed sale and recommended that the proposed contract be approved by the legislature.

Based on the board's review of the contract for the sale and purchase of royalty oil between the State of Alaska and the joint venture, the Commissioner's findings and determinations regarding the proposed sale, and the information presented at public meeting of the board, the board is of the opinion that the proposed disposition of Kuparuk River Unit royalty oil to the joint venture meets the requirements of AS 38.06 and 11 AAC 26. The board adopts the Commissioner's finding and determinations, and recommends that the Seventeenth Alaska Legislature approve the agreement for the sale and purchase of royalty oil from the Kuparuk River Unit to Petro Star Valdez Refinery Joint Venture.

L. Frank DeLong
L. Frank DeLong

Charles Logsdon

Glenn A. Gids

The Alaska Royalty Oil and Gas Development Advisory Board

Resolution 92-1

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L. Frank DeLong



Charles Logsdon

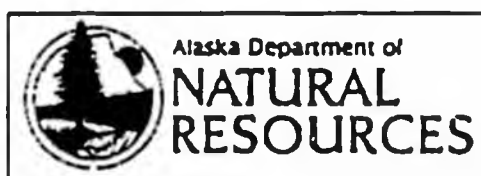
Glenn A. Olds

Final Finding and Determination

To Sell Royalty Oil

to

Petro Star Valdez Refinery Joint Venture



**Division of Oil and Gas
3601 "C" Street; Suite 1360
Box 107034
Anchorage, Alaska 99510-7034**

March 4, 1992

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Appendices

- Appendix A: AS 38.05.183(e) and AS 38.06.070(a)
- Appendix B: Comments and Responses on the Preliminary Finding and Draft Contract
- Appendix C: Changes to the Preliminary Finding and Draft Contract

CORRECTION

**THIS DOCUMENT
HAS BEEN REPHOTOGRAPHED
TO ASSURE LEGIBILITY**

Final Finding and Determination
To Sell Royalty Oil
to
Petro Star Valdez Refinery Joint Venture



Division of Oil and Gas
3601 "C" Street; Suite 1380
Box 107034
Anchorage, Alaska 99510-7034

March 4, 1992

**Final Finding and Determination
To Sell Royalty Oil
to
Petro Star Valdez Refinery Joint Venture
March 4, 1992**

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- Appendix A: AS 38.05.183(e) and AS 38.06.070(a)
- Appendix B: Comments and Responses on the Preliminary Finding and Draft Contract
- Appendix C: Changes to the Preliminary Finding and Draft Contract

Summary

The Commissioner of the Department of Natural Resources, on behalf of the state, proposes a long-term sale of 30,000 barrels per day of the state's royalty oil to Petro Star Valdez Refinery Joint Venture ("Petro Star JV"). Petro Star JV proposes to build and operate a refinery in Valdez. This document provides the finding and recommendation required under AS 38.05.183 for the proposed sale.

The department distributed the preliminary finding and draft contract on January 23, 1992. The public comment period ended one month later on February 24, 1992. The department advertised the finding and contract by sending a notice or copies to a 450-person mailing list, and through display advertisements in the Anchorage Times, Anchorage Daily News, Juneau Empire, Fairbanks News-Miner, and the Valdez Vanguard. The mailing and advertisements also notified the public of the Alaska Royalty Oil and Gas Development Advisory Board meeting on February 6, 1992 in Anchorage which discussed the proposed sale.

Though approximately 50 people attended the Alaska Royalty Oil and Gas Development Advisory Board meeting, no one chose to testify. The department received four letters commenting on the finding and contract. The letters and the department's responses are included as Appendix C to this finding.

This finding and the signed contract are being forwarded to the legislature. The sale will not take effect unless it is approved by the legislature; nor will oil be delivered to Petro Star JV before the refinery is ready to process the oil.

Background

The State of Alaska receives as royalty 12-1/2% of the oil and gas sold from the Kuparuk River oil field. The state may take its royalty either in-kind or in-value. When the state takes its royalty share of oil production in-kind, it takes ownership of the oil, and the commissioner acting on behalf of the state, disposes of the oil through either competitive or non-competitive sales. When royalties are taken in money (in-value), the state's lessees that produce the oil also market the state's share of production, and they are obligated to pay the state the value of its royalty share. The commissioner administers the state's oil and gas lands and royalty program.

In mid-1991, Petro Star JV contacted the Department of Natural Resources with a request to purchase a portion of the state's royalty production. In response to that request and after negotiation with the company, the department proposes the contract which accompanies this finding.

Petro Star JV is a joint venture of three Alaskan companies: Petro Star Valdez, Inc., a subsidiary of the Arctic Slope Regional Corporation; Alaska Refinery, wholly-owned subsidiary of Neil Bergt Trust; and Harbor Enterprises. The joint venture proposes to build a facility to refine

30,000 barrels per day of north slope crude oil into jet fuel, marine diesel, and heating fuel. The refinery will be constructed on private land purchased by Petro Star JV. The land is located adjacent to Dayville Road east of the Trans Alaska Pipeline terminal in Valdez.

The refinery expects to produce approximately 110 million gallons per year of the products listed in Table 1. One hundred and ten million gallons per year is equal to 7,200 barrels per day, or approximately one-quarter of the amount being delivered. The remaining three-fourths will be returned to the Trans-Alaska Pipeline System and sold by Petro Star JV.

Table 1. Expected Refinery Products

<u>Product</u>	<u>Approximate Volume</u>
Jet A	105,00 gallons per day
Heating Fuel #1	20,000 gallons per day
Marine Diesel (summer weight)	130,000 gallons per day
Marine Diesel (winter weight)	45,000 gallons per day

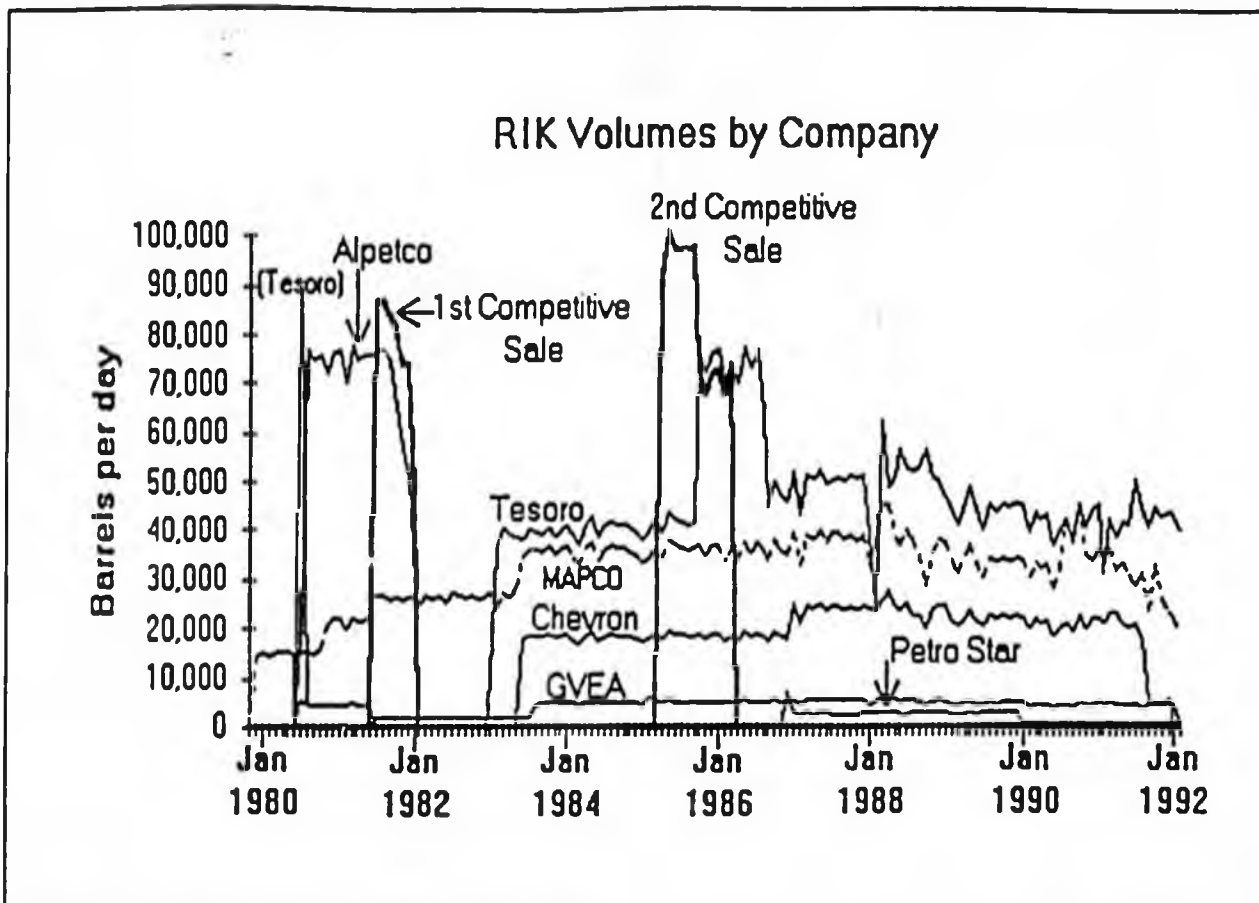
Total (approximate)	300 thousand gallons per day (110 million gallons per year)

The product mix outlined in Table 1 is expected to change after the refinery begins operation and the demand becomes clear. Petro Star JV has executed two sales contracts for its products. The joint venture will sell jet fuel to MarkAir Inc., an Alaska-based airline. It will sell 20 - 40 million gallons per year of jet fuel, depending on the outcome of the airline's current expansion. Approximately 10 million gallons per year of heating and marine diesel fuels will be available locally in Valdez for Prince William Sound communities. The balance of the products will be sold to Petro Marine Services, a subsidiary of Harbor Enterprises and a marine fuel distributor servicing southcentral Alaska. Petro Marine Services is expected to use most of the purchased fuel in Seward, Kodiak, and Dutch Harbor.

Petro Star JV has purchased private land for the facility, has received a conditional use permit from the City of Valdez, and has initiated the required air quality permitting process. Construction may begin as early as April 1992, and the refinery may be ready to begin operation as early as October 1992.

This finding and best interest determination *does not* decide whether construction and operation of the proposed refinery is in the best interests of the state. The refinery is a private facility built on private land. The refinery is not dependent on this proposed royalty oil sale. The proposed refinery, like others operating in the state, has the option of purchasing north slope crude oil directly from the north slope producers. While the proposed royalty oil sale may help the financial viability of the refinery by providing a long-term source of crude oil at a competitive price, the decision on whether to construct the proposed refinery is rightly made by the private owners, and not by the state. This best interest determination decides whether the proposed royalty oil sale is in the state's best interest.

Summary of Previous North Slope Royalty Oil Sales

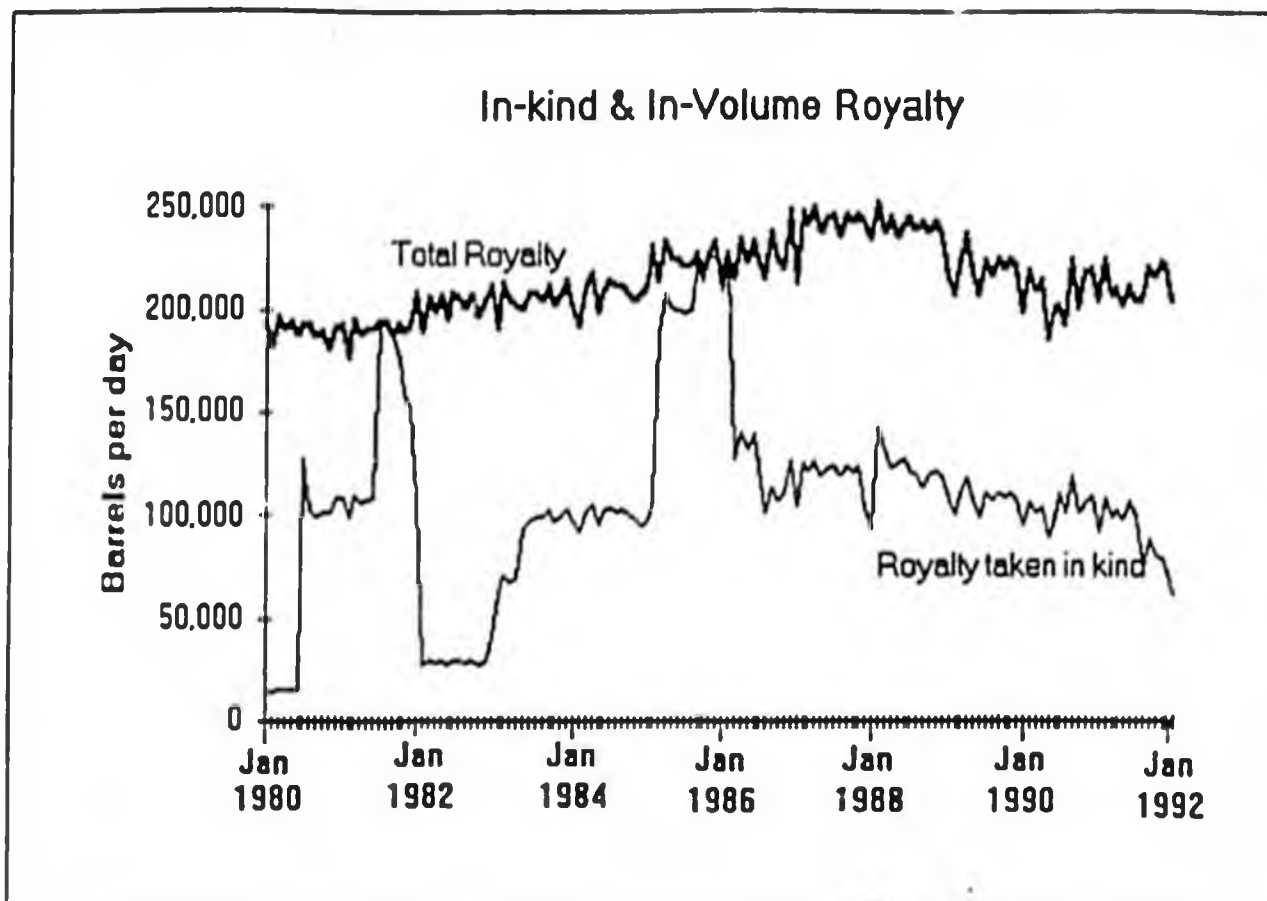


Volumes. Beginning in November 1979 and continuing to the present, the state has delivered royalty-in-kind north slope crude oil to fourteen companies in sixteen negotiated contracts, two competitive sales, and one quasi-competitive sale. Through September 1991, the state had delivered 475 million barrels or approximately 50% of its north slope royalty oil in these sales.

Figure 1 shows the amount of royalty oil sold to each company since the north slope production began. The graph shows that the amount of oil sold to each company has varied over the years, but that Tesoro and MAPCO have been the state's two most consistent customers. Most crude purchased by Tesoro is refined at its facility in Nikiski (capacity 30,000 barrels per day). Chevron's in-state refining was at its 18,000 barrel-per-day plant in Kenai, which ceased production in June 1991. The MAPCO and GVEA purchases are refined at the MAPCO refinery in North Pole (capacity 113,000 barrels per day). The Petro Star purchase is refined at its 7,000 barrel-per-day plant in North Pole. (Capacity figures are taken from *Historical and Projected Oil and Gas Consumption, June 1991* published by DNR, Division of Oil and Gas.)

The competitive and quasi-competitive sales were purchased by a mixture of companies. Some of the crude purchased in these sales was refined at the in-state refiners, some was exported from Alaska. The Alpetco purchases were also exported.

Figure 2 shows the total amount of royalty oil due the state, and the amount of that oil taken in-kind and sold by the state. The volumes of royalty sales have remained approximately constant since 1986 until the recent decline.



Price. Since the first royalty oil sale, the state's policy has been that it would not necessarily maximize revenues from royalty in-kind sales, but that it would not receive less for the people's royalty when taken in-kind and sold than the state would otherwise have received had it left the oil with the lessees and taken its royalty in-value. Consistent with this policy, each of the state's previous non-competitive royalty contracts have had a similar conceptual price: the value that the state would have received if it had left the oil in-value (plus field costs, and in some cases plus a premium). However, the value that the state receives for its in-value royalty has been in litigation as part of the ANS Royalty Litigation (1-JU-77-847 Civil, Superior Court for the State of Alaska, First Judicial District at Juneau)¹. Thus, the price term for former royalty in-kind contracts have included interim pricing formulae to be used until the final monthly values are known, and a mechanism for retroactive adjustment of the interim price based on the outcome

¹ This case was originally titled State of Alaska, et al v. Amerada Hess Corp., et al and has been frequently been referred to as the Amerada Hess litigation.

of the litigation. The price term for every former negotiated state royalty-in-kind contract has had essentially this form. The substantive differences have been in the interim payment method, and sometimes the addition of a premium.

During the last two years, seven companies representing approximately 80% of north slope oil production have settled their ANS Royalty Litigation obligations with the state. Two of these companies, ARCO and BP, own leases in the Kuparuk River Unit. These two companies represent 94.5% of production from the Kuparuk River Unit. These settlements provide an agreed-upon valuation method that did not exist when any of the previous royalty oil contracts were signed. As a result, the price term in the proposed contract to Petro Star JV differs from previous royalty in-kind contracts. This contract relies upon the agreed-upon valuation methods in the ARCO and BP settlements to establish a contract price. Except for certain related adjustments contemplated under the settlement agreements with ARCO and BP, the Petro Star JV contract will not require a retroactive adjustment or an interim pricing method.

Competitive and quasi-competitive contracts have been priced differently. The department felt that strong bidder aversion to retroactive ANS Royalty Litigation adjustments would depress bids, and the competitive sales have required bidders to offer premiums over a base price without retroactive ANS Royalty Litigation adjustments.

Recent Development - Canceled Contracts. In the first half of 1991, the state's in-kind deliveries of north slope crude averaged approximately half of the state's total royalties, or approximately 103,000 barrels per day. The state delivered north slope crude to five companies under six contracts. Recently, however, the state's purchasers have canceled four of the six contracts. By March 1992, in-kind deliveries of north slope crude are expected to decline to less than 60,000 barrels per day (less than 30% of the state's royalty share of north slope production). Table 2 shows the average volume delivered from January through June 1991 to each company. It also shows the last delivery date for the four canceled contracts.

Table 2. Current Royalty Contracts

<u>Company</u>	<u>Average Deliver Volume</u> (barrels per day) <u>January -- June, 1991</u>	<u>Date of Last Delivery</u>
GVEA ¹	4,730	January 31, 1992
Chevron ²	22,148	December 31, 1991
Petro Star ³	1,104	December 31, 1991
MAPCO	34,283	Continuing
Tesoro	40,567	Continuing

¹ GVEA will continue to pay the state its 30¢ per barrel premium through June 30, 1992.

² Chevron had two contracts. The last delivery under the larger contract occurred August 31, 1991.

³ Petro Star continued to pay its 35¢ per barrel premium through February 29, 1992.

As a result of the cancellations, the state is taking less of its oil in-kind than it has at any time since early 1983. Beginning in February 1992, the state will be taking less than 29% of its royalty in-kind. Except for Chevron which shut down its Kenai refinery last June, the state's former in-kind customers are still refining north slope oil, but they are buying less oil from the state. While the crude supplier(s) for each company is confidential (and not known by the department), it appears that the companies are now purchasing more of their oil directly from north slope producers.

Summary of Proposed Contract Terms

1. **Price.** The state will receive a total price per barrel that is the sum of two components: netback value and field cost.
 - (a) *Netback Component.* The netback component is the volume-weighted-average netback value at the delivery point (the inlet of the Kuparuk Pipeline) of royalty barrels produced by ARCO and BP from the Kuparuk River Unit. These two lessees have settled their ANS Royalty Litigation obligation with the state, and together they produce 94.5% of the oil from Kuparuk. Production volumes of companies for which the state is still in litigation under ANS Royalty Litigation will not be included in the volume-weighted average netback.
 - (b) *Field Cost Component.* Per barrel Kuparuk River field costs as described in the agreement that is Appendix I to the December 1981 Kuparuk River Unit Agreement.
2. **Point of Delivery.** The state will deliver the oil to Petro Star JV at the time and place when it receives its royalty oil from its lessees. At present, that is the custody transfer meters into the Kuparuk Pipeline at the Kuparuk Central Production Facility.
3. **Purchase-price Reopener.** At any time after two years following the date oil is first delivered under the contract, the state or Petro Star JV may reopen the contract to begin negotiations to establish a new purchase price. If, after negotiating, the state and Petro Star JV do not reach agreement, either party may cancel the contract, subject to notice requirements. If agreement is reached, either party may re-open after a further two years.
4. **Quantity and Source.** The contract allows Petro Star JV to purchase a maximum quantity of 30,000 barrels per day expressed as a percentage of daily royalty oil from the Kuparuk River Unit. Because the maximum quantity is expressed as a percentage of the Kuparuk River Unit production, it will decline as production from the Kuparuk River Unit declines. Petro Star JV may elect to purchase less oil, subject to notice requirements (required by the Kuparuk River Unit Agreement). Petro Star JV may make a permanent decrease in the maximum quantity (subject to notice requirements) before the first delivery of oil, and at one time after that date. Petro Star may also elect to purchase less than the maximum quantity, but it must pay a per-barrel reservation fee on each barrel less than the maximum quantity that it elects not to purchase. The per-barrel reservation

fee is 0.75% of the full purchase price.

5. **Term.** Delivery of the oil will begin the first day of the first month that is the later of:
1) seven months after the contract is approved by the Legislature and the Governor, or
2) seven months after Petro Star Valdez Refinery certifies that within seven months it will be ready to accept oil. The contract terminates on December 31, 2003. The contract is expected to be approved during the 1992 legislative session, and the first oil delivery is expected to occur at the end of 1992 or the beginning of 1993. Thus, the contract term is expected to be approximately 10 years.
6. **In-state Processing.** Petro Star JV agrees to process at least 80% of the royalty oil delivered under this contract at the proposed refinery in Valdez. The state may waive this requirement if it is satisfied that Petro Star JV is using its best efforts to process the royalty oil and that the waiver would not be contrary to the underlying intent of other provisions of the contract.
7. **Security.** Beginning 190 days before oil is first delivered, Petro Star JV will provide an irrevocable letter of credit equal to the Commissioner's estimate of the value of 90-days delivery of oil. The term of the letter of credit must be renewed 90-days before it expires (so that the letter of credit is continuously valid for 90-days beyond any date oil is delivered). In addition, Arctic Slope Regional Corporation, an Alaskan Native corporation with significant in-state assets, is a signatory to the contract.

Discussion of Specific Contract Provisions

This section of the finding explains differences between this and typical provisions in recent royalty-in-kind contracts. The most recent contract was signed in December 1985. That was a two-company sale from the state to Petro Star, Inc. and Chevron (differences due to the unique two-company sale of that contract are not discussed). The most recent one-company contract, the GVEA-3 contract, was signed in October 1985.

Price: *No Retro Active ANS Royalty Litigation price readjustment; no escrow.* Previous non-competitive contracts have been designed to net the state no less than the value it would have received had it left the oil with the lessees and taken its royalty in value. (Sometimes with the addition of a premium). However, implementing this design has had a practical problem. Until the recent settlements, the state and the north slope lessees have not agreed on how to compute the lessees' royalty in-value liability, and there has been no accepted methodology to compute a dollars-and-cents price-per-barrel for a royalty in-kind sale. Thus, every negotiated contract has included provisions for retroactive price adjustments based on the outcome of the ANS Royalty Litigation.

The requirement for ANS Royalty Litigation retroactive price adjustments provided significant problems both for the purchaser and for the state. It meant the purchaser is buying oil (and must

price its refined oil) based on an alternative purchase price for the crude that may not be known for years. The state is only now nearing completion of its first ANS Royalty Litigation adjustment for royalty-in-kind oil though the first oil was delivered in 1979.

The amount of the price readjustment and the potentially long time lag may result in a large liability. The state's first ANS Royalty Litigation rebilling will total significantly more than \$100 million to five companies. The large rebillings also provide problems for the state. The delay in providing a final bill means that disputes over the final bill may not be identified until long after the oil is delivered. It may be difficult for some companies to pay a potentially large amount long after the refined products have been sold. And at least one in-kind purchaser, Alpetco, has gone bankrupt.

To avoid these problems, the 1985 Petro Star contract required the company to escrow \$1.12 per barrel of royalty oil purchased as a deposit against its ultimate ANS Royalty Litigation liability. Although Petro Star's ultimate liability has not been determined, Petro Star has assured the department it will pay its retroactive ANS Royalty Litigation obligation.

As mentioned previously, based on recent settlements of ANS Royalty Litigation price litigation with seven companies, there is now an agreed-upon price method for 94.5% of the state's royalty production from Kuparuk River. Agreed-to methods for valuing the vast majority of the state's in-value production from the Kuparuk River Unit now exist.

The proposed contract requires Petro Star JV to pay the volume-weighted average netback value for those Kuparuk lessees that have settled: ARCO and BP. As 94.5% of Kuparuk's production is accounted for by the ARCO and BP ANS Royalty Litigation settlements, there is no need for a retroactive price adjustment based on royalty settlement for the remaining production. The value of the 94.5% should be an adequate proxy for the remaining 5.5%.

By establishing a firm value based on agreed-to methodologies, there is no need for an escrow, and no need for retroactive ANS Royalty Litigation adjustments. Petro Star JV has a firm purchase price, subject to certain subsequent adjustments which may be occasioned by the mechanics of the settlement agreements between the state, and ARCO and BP, and the state is certain of being paid the final value.

Price Premium. Many of the previous royalty-in-kind contracts have included a premium above the average netback value for in-value royalty oil. This premium was intended to compensate the state for the so-called "displacement effect" and "competitive effect."

The "displacement effect" theorizes that in-kind sales by the state replace west-coast sales by the lessees. For example, once the sale is in place, a west-coast refiner in California or Washington may no longer purchase crude to make jet fuel to sell in Alaska. While the amount of west-coast sales (including Alaska) would remain the same, some of these sales would be state in-kind sales and less would be made by the lessees. If this occurs, the lessees' average monthly netback value would reflect a lower proportion of west-coast sales and a higher proportion of gulf-coast

sales. The effect is diminished by the fact that the state's royalty share is only one-eighth of the lessees' production. Therefore, only one-eighth of the displacement effect is borne by the state. The displacement effect was much larger a few years ago when half of Alaska's crude oil was transported to the U.S. Gulf Coast.

In 1985, almost half of the state's royalty in-value oil was sold to refiners in the US Gulf (including the Virgin Islands). That amount has been decreasing. Between May and August of this year, it had decreased to 11%, and according to the Department of Revenue's Spring 1991 Revenue Forecast, it will continue to decrease until 1996, when the last gulf sale is projected to occur.

The "competitive effect" is more difficult to explain than the "displacement effect." At the risk of oversimplification, one can maintain that the actual market price on the west coast is above the competitive market-price due to the decision of producers, primarily BP, to transport oil to the gulf coast that might be sold on the west coast, but at a lower price. If the state were to sell significant oil in competitive sales, it might undermine the market power of the producers and lower the market price.

This effect was a larger concern during 1985 and 1986 than it has been after that time because of the large negotiated and competitive in-kind sales that were then occurring. Between May 1985 and April 1986, the state sold approximately 90% of its royalty oil in-kind, up to an average of approximately 210,000 barrels per day during January 1986. There was some concern that this amount of state sales would affect the west-coast market power of the lessees.

The proposed sale to Petro Star JV will not generate this effect. Thirty thousand barrels per day is less than 2% of the north slope production and will not affect operation of the west-coast oil markets.

The small and decreasing proportion of gulf sales, and the small volume proposed to be sold to Petro Star JV mean that the proposed contract will not noticeably displace the lessees' west-coast sales nor generate competitive effects on the west-coast oil markets. For these reasons, and to encourage the jobs, income, tax, and consumption benefits from in-state refining, the proposed contract does not include a premium.

Purchase-price Reopener. The two-year purchase-price reopener is a standard component of most in-kind royalty contracts. Day-to-day fluctuations in the netback value are built into the state's royalty oil settlements and are a part of the contract price to Petro Star JV. The reopener provides additional flexibility to respond to unforeseen changes.

Field Cost. Previous royalty-in-kind contracts do not specify a separate field cost for Natural Gas Liquids (NGLs). While the field cost for crude oil was established in a 1980 field cost agreement (that was made part of the Kuparuk River Unit Agreement), the NGL field cost is still in dispute with the lessees of the Kuparuk River and Prudhoe Bay Units.

NGLs are approximately 3% of the total oil volume produced from the north slope. Some lessees recognize NGLs as part of the crude oil stream and report the agreed-upon crude-oil field cost. Others report a separate field cost for NGLs. That cost varies considerably by lessee and by field -- up to \$13.60 per barrel from one Prudhoe Bay lessee.

Between April 1985 and March 1988, lessees from Kuparuk River oil field sold NGLs with the remainder of Kuparuk's crude oil stream. The field cost for those NGLs is still in dispute. Since March 1988, the lessees have re-injected all NGLs as part of Kuparuk's enhanced oil recovery program. At present, Kuparuk lessees do not take a field cost deduction for NGLs, and disputed NGL field costs are not a problem for the proposed contract. However, NGLs may be sold from the field in the future, and the proposed contract provides a method for resolving the problem, should it occur.

The contract requires that if NGLs are sold from the Kuparuk River Unit, Petro Star JV will pay the full producer-reported field cost for NGLs (or for any other field cost in dispute). It also requires a retroactive adjustment for over- or underpayment after a final, field cost has been determined. Specifically, the contract provides that if a field cost different from the existing field cost agreement is established, the state will rebill (or provide a credit) for field costs not covered by the existing agreement. This provision was added to ensure that Petro Star JV would pay the state's liability for the full NGL field costs if the Kuparuk River lessees begin selling NGLs, and if NGLs are ultimately determined to have a different field cost than that of the remaining crude.

Quality. The 1985 contracts did not distinguish between crude oil, condensate, or natural gas liquids. In the proposed contract, Petro Star JV waives any claim that either condensate or NGLs blended with the crude by the lessees and tendered to the state as royalty oil is not oil for the purpose of the contract. If NGLs are once again sold from the Kuparuk River Unit, this waiver will protect the state against a future claim that Petro Star JV did not receive its full volume of crude oil or more oil than it contracted for by asserting that condensate or NGLs are not crude oil under the contract.

Best Efforts. In its 1985 contract, Petro Star agreed to use its "best efforts" to market its refined products in Alaska. It agreed to its "best efforts" to market a volume of at least 23% of the royalty oil sold under the contract.

This "best efforts" provision is not included in the draft contract. The contract requires that 80% of the royalty oil be processed at the proposed Valdez refinery; it no longer requires "best efforts" in-state marketing of the product.

The provision is omitted because assessing "best efforts" is difficult if not impossible to enforce. In addition, given the incentives to market refined product in Alaska, the history of in-state refiners marketing in Alaska, and contractual provisions of the joint-venture owners of the refinery to market the refined product to MarkAir and to Petro Marine Services, the "best efforts" requirement is unnecessary.

Late Payment Penalty. The 1985 Petro Star contract required a monthly 1% penalty fee to all late royalty payments except for those caused by unintentional clerical errors. This contract changes the fee to 5% per month to be more in line with current commercial practices.

Interest. This contract uses a different interest rate for under- and over-payments than previous contracts. It uses the statutory rate that the legislature established during its last session. Chapter 23 SLA 91 establishes the interest rate to be "five percentage points above the annual rate charged member banks for advances by the 12th Federal Reserve District as of the first day of that calendar quarter, compounded quarterly as of the last day of that quarter." It is important to recognize that if Petro Star JV overpays, the state will have to credit back the amount of the overpayment plus interest to Petro Star JV, just as Petro Star JV will have to pay the amount of any underpayment plus interest to the state.

Security. The proposed contract requires an irrevocable letter of credit equal to 90 days' worth of oil deliveries. The letter of credit is intended to protect the state from any inability of Petro Star JV to pay its bills to the state or to take delivery of the oil. The 90-day requirement has been a feature of all royalty oil disposals since the competitive sale of December 11, 1984 with two exceptions. The Prudhoe Bay royalty oil offered in that competitive sale included a "put call" option which enabled the letter of credit requirement of that oil to be reduced to 60 days (see The Findings and Determination to Conduct a Competitive Sale of Prudhoe Bay and Kuparuk River Royalty Oil, of October 17, 1984). In addition, in the 1985 Petro Star-Chevron sale, Chevron agreed to a "backup" arrangement to accept delivery of any volume of royalty oil upon which Petro Star might default. That "backup" agreement allowed Petro Star's letter of credit requirement to be reduced to 60 days.

The 90-day requirement provides protection for the state. Understanding the risk, however, requires an understanding of the "denomination" process.

The Kuparuk River Unit Agreement and the recent ANS Royalty Litigation settlements effectively give the state the ability to "denominate" most of its oil (change its take of royalty oil from in-kind to in-value) with specified notice to the producers. In the Kuparuk River Unit, there is what amounts to a 90-day notice requirement for 95% of production, and a six-month notice requirement for the remaining 5%. Thus, if the state were notified that Petro Star JV was unable to meet its obligations under the contract -- either that the joint venture was unable to process the oil or unable to pay for it -- the state would have to dispose of the equivalent of 93½-days worth of ~~in-kind~~ deliveries before it could return to taking its royalty in-value. (The 93½ days equals 95% of in-kind deliveries with 90-days notice plus 5% with a six month notice.)

In the unlikely event that Petro Star JV were to become bankrupt, the state may not receive notice until it fails to receive timely payment. By that time, the joint venture may have received approximately 70 days worth of oil:

- 30 days for the production month
- + 10 days for billing (the state bills 10 days after the end of each month)
- + 7 days for Petro Star to receive the bill
- + 10 days for payment (payment is required 10 days day after the bill is received)
- + 13 days for decision (a decision to declare the contract in default and denominate the oil would undoubtedly take some time)

70 days of oil

The letter of credit would have to make the state whole for non-payment for 70-days worth of oil, and to make up the discount in selling the additional 93½-days worth of oil that would be the state's responsibility before the state's royalty reverted to in-value production. The 90-day letter of credit would make up the difference to the state as long as the state received 80% of its royalty-in-value revenue for the 93½-days of in-kind oil it was forced to sell. That is, neglecting fluctuations in oil prices, the value of a 90-day letter of credit is approximately equal to the value of 70-days in-kind deliveries plus 80% of the value of 93½-days of in-kind oil.

In the two cases where the state was forced to dispose of in-kind production because of bankruptcy, it sold the oil to ARCO and Sohio for only a slight discount from the full price. These experiences and knowledge of the oil markets indicate that the state would be able to sell as an "emergency sale" three months of production at more than 80% of the in-value revenue.

In addition to the 90-day letter of credit, additional security is provided by the fact that Arctic Slope Regional Corporation is a signatory to the contract. Arctic Slope Regional Corporation is a regional Native Corporation representing the north slope. The corporation is and will remain an Alaska corporation with significant assets in Alaska. The corporation's assets provide security for the state in case of bankruptcy by Petro Star JV, and if retroactive billings exceed the value of the 90-day letter of credit or if billings occur after the last delivery of oil. The corporation's commitment to the contract along with the 90-day letter of credit should provide adequate protection for the state.

Local Hire. Like the state's other long-term royalty oil contracts with in-state refiners, the proposed contract contains a provision concerning local hire. The preferential hiring clause states in part that Petro Star JV "agrees to employ Alaska residents and Alaska companies to the extent they are available, willing and qualified for all work performed in Alaska in connection with the Agreement." An "Alaska resident" is defined as an "individual who has resided in the state for one year at the time of employment." If this provision is determined to be unconstitutional, then, Petro Star JV agrees to employ Alaskan residents and Alaska companies to the extent such preferential hiring is determined to be constitutional.

In-state Benefit Analysis

The primary bases for this long-term negotiated sale are: 1) to receive a fair market value for royalty oil; and 2) to encourage in-state processing of royalty oil and the attendant benefits (primarily jobs, taxes, and competition between refined product suppliers that may lead to lower product prices for consumers.)

Construction and Operation Benefits. Even without this contract, the Petro Star Valdez Refinery may build and operate the refinery with crude oil purchased from the north slope lessees rather than from the state. Therefore, most or all of the benefits of constructing and operating the refinery cannot be ascribed to the proposed contract. It is possible, however, that this proposed royalty oil contract may increase the financial viability of the refinery. If so, an unknown portion of these benefits should be ascribed to the contract.

The direct benefits from refinery construction and operation occur through payroll, property taxes, state corporate taxes, and profits if held in-state. All of the joint venture profits are expected to be held in state. These cash infusions are multiplied as they are spent and recycled throughout the economy. However, actual project specific multiplier effects can only be ascertained by extensive surveys or actual development.

Table 3. Direct Construction and Operation Benefits
(thousand dollars; figures are approximate)

<u>Construction Benefits</u>		<u>Operation Benefits</u>	
Capital Investment	\$30,000	Payroll	\$1,700 (16-20 jobs)
Capital Investment in Alaska	\$25,000	Property Taxes	\$ 400
		Profits	Unknown
		State Income Tax	Unknown

		Known Total	\$2,100

Table 3 provides some measures of in-state benefits for the Petro Star JV. The table shows estimates of potential direct benefits from operation and construction of the refinery. The direct operation-benefits to the state are approximately \$2.1 million dollars per year plus whatever benefits exist from in-state profits and state income taxes and from multiplier effects. The facility will also provide approximately 100 construction jobs and 16-20 permanent jobs once the refinery begins operation. In addition, it will pay approximately \$400,000 in taxes to the City of Valdez. (The jobs and taxes do not include any created by downstream employment such as additional dock workers.)

The addition of another in-state refinery might have the effect of decreasing a small proportion of production at an existing refinery -- either the existing Tesoro facility at Nikiski (capacity of 80,000 barrels per day), or at MAPCO facility at North Pole (capacity of 113,000 barrels per day). If this decrease occurs, then the tables may overstate the operation benefits of the refinery.

All of the products that Petro Star Valdez Refinery expects to produce are also produced in-state by other refiners. The current in-state refining output does not provide all of Alaska's needs for these products. A portion of Alaska's supply of these fuels is imported from outside the state, and that proportion appears to be larger than the expected output of the refinery. While pricing and supply patterns may change in the state, there appears to be in-state demand to accommodate the proposed production from Valdez without provoking idle refining capacity elsewhere in Alaska.

According to the Army Corps of Engineers publication "Waterborne Commerce of the United States, 1989" (the most recent year published), approximately 52 million gallons of jet fuel and 60 million gallons of kerosene was imported into Anchorage from outside the region. It appears that the amount of jet fuel imported by Alaskans is in excess of the amount that the Valdez refinery will produce. Similar figures are not easily available for marine diesel, but it is expected that the proposed refinery output will not displace all marine diesel imports into Alaska.

Consumption Benefits. Consumers may benefit from the proposed sale through lower product prices. Oil products refined in Alaska may be priced lower than those imported from outside the state. In addition, an increase in competition resulting from the addition of another refinery may result in lower product prices. If either of these situations occur, consumers will benefit through lower prices. There is certainly no reason to believe that construction or operation of the refinery could have the effect of increasing overall consumer prices.

The proposed Petro Star JV has sales agreement to sell most of its Jet Fuel to MarkAir Inc., and most of the remaining product to Petro Marine Services. MarkAir Inc., is an airline company based and operated in Alaska. Presumably, MarkAir will purchase the fuel for less than its current cost. The extent to which the lower prices result in lower airline fares is unknown.

Petro Marine Services, is a fuel distributor which markets its products throughout coastal southcentral Alaska, though mostly in Kodiak, Dutch Harbor, and Seward. Presumably, it has signed the purchase agreement to decrease costs, though the extent, if any, to which consumer fuel prices will be lowered in those communities is unknown.

Environmental Impacts. The impacts of the royalty sale itself are expected to be minimal. The impacts of constructing and operating the refinery may be somewhat greater. Previous analysis indicated that the economic benefits of constructing and operating the refinery cannot be ascribed to the state's royalty sale. The same is true of the environmental impacts.

The Petro Star JV has received a conditional use permit from the City of Valdez. The City of Valdez is the appropriate authority to consider whether such a facility is compatible with the land use requirements of the city. Approval by the City of Valdez indicates that the conversion of the vacant land to a refinery will cause no unacceptable land-use impacts. Similarly, the refinery has begun the process to apply for an air quality permit from the Department of Environmental Conservation. Air quality impacts are best considered by the Department of Environmental Conservation in that process. Operation of the refinery requires compliance with the applicable

permits. That compliance will be evidence of acceptable environmental impacts.

Social Impacts. The refinery will pay property taxes to the City of Valdez, and its employees will use city services. The tax base in the City of Valdez is decreasing approximately \$90 million per year (as depreciation lowers the assessed value of the Trans Alaska Pipeline System). This decrease has severe impacts on the city's tax receipts. This year's property tax rate is expected to increase by three mills to make up for the smaller tax base. The \$30-million refinery is expected to pay approximately \$400,000 in property taxes. It will be a welcome addition to the city's tax base.

The additional employment may also affect services in the City of Valdez. The Community Development Director for the City of Valdez reports that while vacancy rates in Valdez are currently low, there is an ample supply of vacant land suitable for residential housing. In addition, he reports that the addition of children to the Valdez school system brought by new employment is unlikely to overtax the school system; in any case it will not cause any unacceptable social impacts.

Findings and Determinations

Competitive Bidding is Waived. I have determined in accordance with AS 38.05.183(a) and 11 AAC 03.030 that the best interest of the state does not require competitive bidding, and that competition does not exist for state in-kind royalty oil. During the last few years, the state has been delivering royalty oil to in-state refiners under six contracts. Four of the six contracts have been canceled over the last few months. Contracts were canceled by Chevron (two contracts), GVEA, and Petro Star. Once all of the deliveries under the canceled contracts cease, the state will be taking less than 30% of its royalty oil as in-kind deliveries. This is the lowest percentage of royalty oil taken in-kind since February 1983. The only in-state refiners who are being supplied with royalty oil are MAPCO and Tesoro, both of which purchase additional fuel from north slope producers. As the state has more royalty oil available than it has purchasers, a competitive bid would not result in a higher value to the state. The state retains enough royalty oil to be able to sell to future in-state purchasers should they become interested.

The Sale is in the Best Interest of the State. Under AS 38.05.183(e), a non-competitive sale, exchange, or other disposal of royalty oil or gas taken in-kind by the state may be awarded by the commissioner to the prospective buyer whose proposal offers maximum benefits to the citizens of the state.

In accordance with AS 38.05.183(a),(c), and (e), and 11 AAC 03.010(b) and (d), I find that taking royalty oil in-kind and selling that oil to Petro Star Valdez Refinery Joint Venture ("Petro Star JV") for use at the proposed refinery in Valdez is in the best interests of the state and that it will maximize benefits to state citizens. According to AS 38.05.183(e) and AS 38.06.070(a), before making a non-competitive sale of state royalty oil, the commissioner must consider the criteria listed in AS 38.05.183(e) and AS 38.06.070(a) and listed in the appendix to this finding.

1. The state is now highly dependent on oil revenues and will continue to depend on oil revenues in the future. The price term of the sale protects the state's interest by ensuring that revenues from this sale will equal the in-value alternative.
2. Petro Star JV will make an initial investment of approximately \$25 million dollars within Alaska. The direct annual benefits to local payroll and to the purchase of local goods and services is more than \$2.1 million. While the proposed sale may increase the financial viability of the refinery, the extent to which these benefits can be ascribed to the proposed contract is unknown.
3. The existence of the refinery may increase competition in fuel sales in the state and may provide for lower consumer product prices. A one cent decrease in the price of each gallon of refined product that could be made from 1,000 barrels per day translates to an annual consumer saving of approximately \$153,000. The two companies that will purchase most of the refinery's products are MarkAir Inc., and Petro Marine Services which will almost certainly benefit from lower prices.

4. The proposed refinery would add 16-20 permanent, new jobs in the City of Valdez, and pay property taxes of approximately \$400,000 per year to the city. The addition of new employment and a larger tax base for Valdez are expected to be welcome benefits to that city's declining property tax revenues and outweigh whatever additional social costs and responsibilities, if any, that they impose. As with construction and operation benefits, however, the extent to which these benefits can be ascribed to the proposed sale contract is unknown.
5. Any environmental effects will result from construction and operation of the refinery, not from the proposed royalty sale. The sale itself has little or no environmental effects. The major permanent construction and operation impacts are the land-use and air-quality impacts. The fact that the refinery has received a conditional use permit from the City of Valdez and is consistent with that city's coastal zone plan shows that the land-use impacts are acceptable. Similarly, the proposed refinery will not operate without receiving an air quality permit from DEC. Those impacts are best considered by the Department of Environmental Conservation during that process.
6. To the extent that the sale helps provide a long-term crude oil supply to the proposed Petro Star JV, the sale will help provide new in-state investments. It will provide increased competition for existing in-state refineries.

Criteria Weights. According to 11 AAC 03.060(b), "In considering the criteria described in AS 38.05.183(e), the commissioner will state which criteria apply to the proposed disposition, and discuss the weight given to the applicable criteria in determining the maximum benefit to the state..."

In making this finding, the department first determined that the state would not lower the total royalty oil revenue due the state by making a disposal to Petro Star JV. The department next looked at whether the disposal would increase the amount of in-state refining and has the potential to lower product prices. Finally, the department examined the criteria to determine that the sale would not create any unacceptable environmental or social impacts.

Contract Prices Are Acceptable. Under 11 AAC 03.091(b), I find that in establishing the price of this royalty oil contract, the department has obtained a price that is equal to the volume-weighted average of settled royalty netback value applicable to the oil that is being sold, plus field costs incurred by the royalty share. The 94.5% of Kuparuk production that is based on settled claims with the state under ANS Royalty Litigation provide the agreed-upon values and methodology for the in-kind sale of Kuparuk River oil. A price based on the volume-weighted average netback of that production is an acceptable benchmark for final value due the state. Therefore, I find there is no need for a retroactive adjustment upon resolution of further ANS Royalty Litigation claims.

Conclusion. Under the terms of the proposed contract, the state would receive a market price for the royalty oil, while fostering in-state processing, potentially lowering product prices, and providing attendant benefits. The satisfactory price terms, coupled with the associated direct and secondary benefits for Alaska citizens, supports the decision to waive competitive bidding.

The foregoing facts and analysis support the finding that this disposal is in the best interest of the state and that it maximizes the benefits to Alaska citizens.

Harold C. Heinze
Harold C. Heinze, Commissioner

3/4/92
Date

Appendix A: AS 38.05.183(e) and AS 38.06.070(a)

AS 38.05.183(e) When a sale, exchange or other disposal of oil or gas taken in kind by the state as its royalty share, or a sale, exchange or other disposal in whole or in part of a right to receive future royalty oil or gas, under a state lease under this chapter is made other than by competitive bid, the sale, exchange or other disposal shall be awarded by the commissioner to the prospective buyer whose proposal offers the maximum benefits to citizens of the state. The commissioner shall consider:

- (1) the cash value offered;
- (2) the projected effects of the sale, exchange or other disposal on the economy of the state;
- (3) the projected benefits of refining or processing the oil or gas in the state;
- (4) the ability of the prospective buyer to provide refined products or by-products for distribution and sale in the state with price or supply benefits to the citizens of the state; and
- (5) the criteria listed in AS 38.06.070(a).

AS 38.06.070. Criteria. (a) In the exercise of its powers under AS 38.06.040(a) and 38.06.050 the board shall consider

- (1) the revenue needs and projected fiscal condition of the state;
- (2) the existence and extent of present and projected local and regional needs for oil and gas products and by-products, the effect of state of federal commodity allocation requirements which might be applicable to those products and by-products, and the priorities among competing needs;
- (3) the desirability of localized capital investment, increased payroll, secondary development and other possible effects of the sale, exchange or other disposition of oil and gas or both;
- (4) the projected social impacts of the transaction;
- (5) the projected additional costs and responsibilities which could be imposed on the state and affected political subdivisions by development related to the transaction;
- (6) the existence of specific local or regional labor or consumption markets or both which should be met by the transaction;
- (7) the projected positive and negative environmental effects related to the transaction; and
- (8) the projected effects of the proposed transaction upon existing private commercial enterprise and patterns of investments.

Appendix B: Comments and Responses on the Preliminary Finding and Draft Contract

The department sent either a copy of the preliminary finding and draft contract, or a notice announcing its availability to a 450-person mailing list. In addition, display advertisements were published in the Anchorage Times, Anchorage Daily News, Juneau Empire, Fairbanks News-Miner, and the Valdez Vanguard.

The department received four letters commenting on the proposed sale. Two letters were received from one respondent (Prince William Sound Conservation Alliance). These two letters are answered together. The letters and responses follow.

ALASKA LEGAL RESEARCH

Joseph A. Sonneman, B.S., M.A., Ph.D., J.D., Esq.

324 Willoughby, Juneau, Alaska 99801

PH: (907) 463-2624 FAX: (907) 463-3802

Director
Division of Oil & Gas
Box 107034
Anchorage, AK 99510

February 15, 1992

Dear Director Eason:

re: Royalty Oil Sales

Here are my comments on the proposed sale of royalty oil to Petro Star Valdez Refinery (or to anyone else, for that matter).

1. During the ALPETCO (a Hammond-era refinery project) days, I was a cab driver and once took to their private jet a trio of ALPETCO executives or lawyers or lobbyists (one was Cathy Chandler, now Sen. Stevens' wife). They talked about their legislative game plan en route: it was to delay and do nothing. Nothing is what they did. ALPETCO built no refinery, but I think ALPETCO did make substantial profits off the State's royalty oil until its contract was finally canceled.

2. Therefore, in any other royalty oil sale:

- a. The refinery must be built BEFORE the oil is sold to it!
(OR, FORWARDED BY REFINERY)
- b. There must be a COMPLETION BOND to ensure that the refinery is indeed built.

3. Refineries--and their following petrochemical industries--are wonderful examples of value-added processing that Alaska should do much more of. Great!

4. However, the State of Alaska should keep at least 50% of the oil that is run through such a refinery and petrochemical plant, just BECAUSE of the value added by that processing. At the time of ALPETCO, the value of plastics from one barrel of oil was said to be about \$3500. I don't know what it is now, but if Alaska sells the oil for \$15-20 and the products made from that oil sell for \$3500 or more, Alaska is getting the short end of the stick!

Much better for Alaska to CONTRACT with Petro Star or other refineries and petrochemical operators to PROCESS State of Alaska oil, than for Alaska to SELL the oil outright and let other folks make all the profit off resources that belong to all Alaskans. In other words, **THE STATE OF ALASKA SHOULD SELL PETROCHEMICAL PRODUCTS, NOT CRUDE OIL.** The terms of trade favor producers of manufactured goods, not extractors of natural resources.

Thank you for your attention.

Sincerely & cordially,


Joe Sonneman

RECEIVED

FEB 2, 1992

DIV. OF OIL & GAS

WALTER J. HICKEL, GOVERNOR

DEPT. OF NATURAL RESOURCES

P.O. BOX 107034
ANCHORAGE, ALASKA 99510-7034
PHONE: (907) 782-2553

DIVISION OF OIL AND GAS

March 3, 1992

Joseph A. Sonneman
324 Willoughby
Juneau, Alaska 99801

Dear Mr. Sonneman:

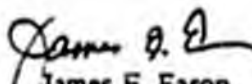
Thank you for your letter concerning the proposed royalty oil sale to Petro Star Valdez Refinery Joint Venture. We received only four comments on the proposed sale and so we have the luxury to respond to the comments individually.

Your letter asked that we ensure that the refinery is built before the state sells its oil. The proposed contract has this insurance. The contract does not take effect until Petro Star certifies that the refinery will be ready to accept and process oil within seven months. The seven month lead time is included because under the Kuparuk River Unit agreement, the state is required to give lead time to alert the producers that it wishes to take its oil in-kind rather than leave it for the producers to market. In addition, the proposed contract includes an 80% in-state processing requirement. Thus, Petro Star is not permitted to take the oil with building a refinery.

Your letter also suggests that the state retain title to half of the produced high-value petrochemical products such as plastics. You mention that some chemicals made from one-barrel of oil may sell for \$3,500. The proposed refinery does not produce these products. Rather, it will produce lower-value fuels such as jet-fuel, and marine diesel. The large profits that you foresee are unlikely to exist. During the last year, the Chevron refinery in Kenai closed and three other companies canceled their royalty oil contracts with the state. Rather than the possibility of large profits, there is now lower demand for in-state royalty oil purchases than at any time since 1983.

Under separate cover we will be sending you a copy of the Final Finding and Determination and the final contract for the royalty oil sale. The contract will not take effect unless approved by the legislature (and unless the Petro Star builds the refinery). Thank you for your comments. If you have questions, please let me know.

Sincerely,


James E. Eason
Director

WALTER J. HICKEL, GOVERNOR

DEPARTMENT OF LABOR
OFFICE OF THE COMMISSIONER

P.O. BOX 21149
JUNEAU, ALASKA 99802-1149
PHONE: (907) 465-2700

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February 14, 1992

James E. Eason, Director
Alaska Department of Natural Resources
Division of Oil and Gas
P.O. Box 107034
Anchorage, AK 99510

RECEIVED
FEB 24 1992
DIV. OF OIL & GAS

Dear Mr. Eason:

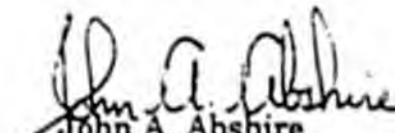
Re: Proposed Royalty Oil Sale to Petro Valdez Refinery Joint Venture

We have received and reviewed the Preliminary Finding and Determination regarding the above referenced royalty oil sale proposal. While we have no recommended corrections or additions to the report, we applaud your efforts to maintain the State's revenue while simultaneously promoting in-state processing of our natural resources. We understand from your report that the refinery project is not dependent on the proposed sale, but that a long-term source may be attractive to the joint venture from a business planning perspective.

Success in your efforts will lead to increased direct and indirect employment and a better life style for our citizens. As we pointed out in our January 17, 1992, news release, the December unemployment rate in Alaska was 10.1% compared to 7.5% a year earlier. In the Valdez-Cordova census area, the December unemployment rate was 12.2%, up from 11.2% in December 1990. It is our hope that projects such as this will successfully lead to increased employment of Alaska residents who will benefit from greater in-state processing of our natural resources.

Thank you for giving us the opportunity to comment on the proposed royalty oil sale.

Sincerely,


John A. Abshire
Acting Commissioner

WALTER J. HICKEL, GOVERNOR

DEPT. OF NATURAL RESOURCES

P.O. BOX 107004
ANCHORAGE, ALASKA 99510-7034
PHONE: (907) 782-2553

DIVISION OF OIL AND GAS

March 3, 1992

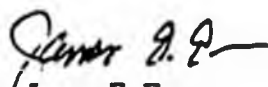
John A. Abshire, Acting Commissioner
Department of Labor
P.O. Box 21149
Juneau, Alaska 99802

Dear Mr. Abshire:

Thank you for your letter supporting the Preliminary Finding and Determination for the proposed royalty oil sale to Petro Star Valdez Refinery Joint Venture. We received only four comments on the proposed sale and so we have the luxury to respond to the comments individually.

Under separate cover we will be sending you a copy of the Final Finding and Determination and the final contract. The contract will not take effect unless approved by the legislature.

Sincerely,


James E. Eason
Director



Prince William Sound Conservation Alliance

P.O. Box 1697
 Valdez, AK 99686
 (907) 835-2799
 Fax (907) 835-5395

February 24, 1992

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DIV. OF OIL & GAS

Board Members	James E. Eason, Director Alaska Dept. of Natural Resources Division of Oil and Gas Box 107034
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Nancy R. Leticoe Vice-President	Ted Moninski, Project Review Coordinator Alaska Division of Governmental Coordination Southcentral Regional Office 3601 C Street, Suite 370 Anchorage, Alaska 99503-5930
JoAnn Lundfelt Secretary/Treasurer	Svend Brandt-Erichsen, Regional Administrator Alaska Dept. of Environmental Conservation Southcentral Regional Office 3601 C Street, Suite 1334 Anchorage, Alaska 99503-5930
Kim McCarty	
Sun Stephens	Re: Petro Star Refinery JV; State of Alaska Royalty Oil Contract. Air Control Permit. Coastal Consistency.
Executive Director	
David P. Janka	Prince William Sound Conservation Alliance (PWSCA) has concern that your agencies are failing to take the problems related to the Petro Star Refinery JV (Petro Star) project as described in our comments dated January 15, 1992 seriously. State and Local Coastal Management Program (CMP) as well as state and federal permit requirements are being undermined with the result being a loss of safety to workers, the public and the environment. The problems we cited are still unresolved, despite the fact that the Alaska Department of Environmental Conservation (ADEC) has issued their air permit and the Alaska Division of Governmental Coordination has issued a ruling in favor of coastal consistency. The proposed sale contract for Alaska royalty oil should not proceed.
Administrative Assistant	
Nancy Phelps	

COASTAL CONSISTENCY:

Zoning decisions and permits were made by the City of Valdez on October 7, 1991 without any site specific geological/seismic studies at hand. Now the State Division of Governmental Coordination is using those city decisions to support their coastal consistency findings.

Nearly 3 months after the City of Valdez made those decisions and after the end of the public comment period (which itself was flawed—see PWSCA comments of 1/15/92), Dow Engineers of Anchorage under contract with Petro Star released nothing more

than a summary of what they have stated are their "findings and opinions regarding the seismic stability of the planned refinery in Valdez, as well as our assessment of the potential for other natural hazards to impact the site."

Findings, opinions and assessments fall far short of a site specific geotechnical/seismic study. Without such a study, no credibility can be given to the siting of this facility. In fact, when PWSCA did a literature search and contacted experts in the field of geological hazards related to the area in question, we found nothing but extreme and obvious problems related to ground stability, seismic wave runup and river flooding. The full study (if there is one), and not a press release, on the geotechnical and seismic hazard aspects of this project must be issued and made available for review. Until this is done, neither the public nor the government agencies whose responsibility it is to protect the public and the environment can be sure what is fact and what is the opinion of a paid contractor.

PWSCA discovered errors in calculations done by CH2M Hill, the company contracted to work out Petro Star's Air Permit Application. Possible errors or omissions in Dowl Engineers' work cannot be known, as there are no calculations or study available for review. However, there are statements made in their summary which contradict our findings, although both were taken from many of the same sources. (see PWSCA comments 1/15/92)

NPDES PERMIT:

There is no City wastewater system for Petro Star to connect into in the vicinity of the proposed refinery site for disposition of stormwater discharges. There has been nothing to date that has shown that Petro Star will not be discharging into waters of the United States. This would require them to obtain a National Pollution Discharge Elimination System (NPDES) Permit. PWSCA wonders how many times this fact must be stated before someone catches on that Petro Star is trying to undermine the permitting process. Or are we again seeing agencies and government following some hidden agenda?

AIR PERMIT:

When PWSCA discovered errors in CH2M Hill's calculations in Petro Star's Air Permit, there were additional errors discovered by the Alaska Department of Environmental Conservation (ADEC) and/or CH2M Hill within that particular part of the permit. The additional errors were worked into the calculations by CH2M Hill and it turned out that they still had not brought emissions over a 100 tons/year permit threshold. These errors, and the manner in which paid contractors are left to their own reviewing and editing, put the reliability of the permit calculations in question. PWSCA had requested that an independent review of the application be initiated by ADEC or the City of Valdez. No such review has taken place. Until such a review takes place and proves that Petro Star is meeting all permit requirements this project should not be allowed to proceed. This review must also take into account parts of this project which are being left out.

INCOMPLETE PLANS:

Petro Star has failed to give full information on the distribution of their product. PWSCA is still adamant that all aspects of this project be taken into consideration when permits and rulings are being made. Petro Star already has plans for additional tank farms and very different plans for transportation of their product than those stated in their permit applications. (see PWSCA comments 1/15/92)

SPILL CONTINGENCY PLAN:

At this time PWSCA asks that an Oil Spill Contingency Plan (C-Plan) be formulated for this project as soon as possible. Before State Royalty Contracts are signed or any other aspect of this project is allowed to proceed, the C-Plan must be put together and approved. PWSCA feels that this is important in that the site for this facility lies within a rich biological area and that because of the expansive tidal flats, river

deltas, salmon spawning and rearing habitat and wetlands that lie adjacent to the site, a responsible and effective C-Plan is not likely to be achievable. To wait until Petro Star is ready to start up their refinery for an approved C-Plan again fails to adequately protect the environment. (see PWSCA comments 1/15/92)

Prince William Sound Conservation Alliance wishes to again stress our concern over the complacency to earthquake hazards that is pervasive throughout state and local government as well as industry. Of any place on the face of this Earth, Alaska should be the most aware and prepared for the inevitable occurrence of a major earthquake. Unfortunately, this is not so. The responsibility for the safety of the public and the environment falls into your hands. We hope that you will take our concerns seriously, back up a few steps, and reconsider this project as presented.

Thank you. Please feel free to contact us with any questions or for any further information.

Sincerely,



David P. Janka
Executive Director

cc: ADEC Valdez; ADF&G; ADNR; EPA; USF&WS; Army Corps of Engineers; City of Valdez; Petro Star; Alaska Representative Gene Kubina; State Senators Jay Kertula and Curt Menard; House and Senate Resource Committee; Regional Citizens Advisory Council; Valdez Fisheries Development Association; Jeff Sauer, attorney & Sierra Club Legal Defense Fund; Trustees for Alaska; Alaska Center for the Environment; KCHU radio; *Valdez Vanguard*; KVAK radio and *The Pioneer*; *Anchorage Daily News*; *Anchorage Times*



Prince William Sound Conservation Alliance

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James E. Eason
Director
ADNR/Division of Oil and Gas
Box 107034
Anchorage, Alaska 99501

January 30, 1992

Dear Mr. Eason,


I received information concerning the sale of state royalty oil to Petrol Star Valdez Refinery JV today. Prince William Sound Conservation Alliance (PWSCA) will submit comments on the proposed sale before the February 24, 1992 deadline. At this time though we wish to share with you our comments concerning this project submitted earlier this month to ADEC and ADGC in reference to the air permit and coastal consistency review. (Document attached)

To summarize our comments at this time: PWSCA with a membership of nearly 300, with approximately 100 of those living here in Valdez, feel strongly that this project has been misrepresented, poorly engineered, and shows a lack of responsibility to the safety and well being of the community and the environment. In short this project should not be allowed to proceed.

Also at this time PWSCA wishes to request that the February 6, 1992 meeting of the Alaska Royalty Oil and Gas Advisory Board be teleconferenced through the Legislative Information Office system to at least Valdez or Juneau.

Thank you and please feel free to contact PWSCA for any further information or questions.

Sincerely,


David P. Janka
Executive Director

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JAN 5 1992
DIV. OF OIL & GAS



Prince William Sound Conservation Alliance

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January 15, 1991

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Kim McCarty

Stan Stephens

Re: Public Comment for Air Quality Control Permit Application (ADEC File No. 9124-AA(X)1) and Consistency with the Alaska/Valdez Coastal Management Program (State I.D. No. AK 011223-12A) from Petro Star Refinery JV.

To whom it may concern:

The Prince William Sound Conservation Alliance (PWSCA) will provide arguments that the Petro Star Valdez Refinery JV (Petro Star) has submitted incomplete plans for their project including insufficient data on which to base a determination of airborne particulates and incomplete plans for the total project. In particular, we will argue that this is an inappropriate activity for placement directly in a coastal habitat which is susceptible to a number of geophysical hazards. For the reasons explained below and supported by the Appendices and accompanying bibliography, we strongly urge you to refuse Petro Star's application for an Air Quality Control Permit to Operate, ADEC File No. 9124-AA(X)1, and rule on the projects inconsistency with the Alaska/Valdez Coastal Management Programs State I.D. No. AK 011223-12A.

INCOMPLETE PLANS:

Failure to include plans for distribution of product: The project as it is presented primarily covers the facility itself and not the transportation of its

product or other plans discussed by Petro Star. These excluded elements include both immediate and future additions of off-site storage, product loading facilities and product pipelines. Without this information, neither the total impacts of the project on the area nor the total air emissions can be adequately reviewed or assessed as required by the Coastal Zone Consistency review process and the Alaska Department of Environmental Conservation's (ADEC) permit review process.

Petro Star's application is incomplete, because it does not discuss product transportation, but attempts to separate permitting for the facility from permitting for the distribution system. For example, Petro Star's application does not mention locating a tank farm on Mineral Creek Loop Road (Loop Rd.), product pipelines from there to the Valdez Container Terminal Dock, oil product loading facilities on the Container Dock, or product pipelines running the approximately 11 km. (7 mi.) from the refinery site to the proposed Loop Rd. tank farm. These facilities would cross and/or be adjacent to wetlands, salmon spawning/rearing habitats, three major waterways and the Valdez Old Town site (condemned because of earthquake hazards after the March 27, 1964 Earthquake). They would also create additional emissions in respect to the air permit.

However, Petro Star has described its distribution plans in local newspapers, and they were discussed at meetings on the Valdez Duck Flats Area Meriting Special Attention (AMSA) and at a joint meeting sponsored by the City of Valdez to address concerns about the proposed Petro Star Refinery project held November 5, 1991 (Joint Meeting). They are detailed further in a City of Valdez memo of December 2, 1991 (Appendix 1). It is the position of the Prince William Sound Conservation Alliance that the Coastal Zone Consistency Review Process requires the applicant to provide complete information both on the facility and on the proposed distribution process or on alternative distribution plans, if no final plan has been selected.

At the Joint Meeting Mr. Al Ewing of the United States Environmental Protection Agency (EPA) indicated that the EPA was concerned that the project did not consider how the product would be transported noting that the EPA would prefer to see the project as a whole, that is, from the time product leaves the Trans-Alaska Pipeline System until it is delivered to the market. Mr. Ewing indicated that an Army Corps of Engineers permit might be necessary depending on the method of transportation (Joint Meeting, tapes). PWSCA encourages the EPA, ADEC and Coastal Zone Consistency review to require consideration of the Petro Star project as a whole.

Incomplete information on the total cumulative effects from project: The cumulative impact upon the air quality of Port Valdez air containment area from the total Petro Star Project must also be addressed. The Petro Star permit application provides incomplete information on the cumulative effects of emissions from trucks, tankers, tugs or barges themselves and on the safety concerns of additional truck traffic on the Richardson Highway and the narrow, residential Loop Road. If the proposed Loop Road tank farm is used, there would be three transfers of product creating additional emissions during loading as well as additional tank losses. It is the position of PWSCA that all emissions and aspects of this project must be taken into consideration during the Coastal Zone review process and ADEC Air Quality Permit.

Incomplete information on the total air emissions in the Valdez Air Containment District: Air pollution has been a major problem with the Alyeska Pipeline Service Company (Alyeska) facility operations that has taken ADEC and EPA too many years to resolve. PWSCA is very concerned about the health and environmental effects of the total air emissions from Alyeska, Petro Star, municipal and other sources.

Incomplete information on the disposal of wastewater: Petro Star's permit application is also incomplete in that it fails to address what will become of the facility's stormwater runoff following preliminary on-site treatment. At the Joint Meeting Mr. Ewing stated that no National Pollution Discharge Elimination System (NPDES) permit would be required as long as the stormwater runoff does not enter waters of Port Valdez. Petro Star had informally indicated an intention to use the Valdez Municipal Sewer System. There are three major problems with this proposal:

1) There is no municipal system in the area, so a 9.5 km. (6 mi.) extension to the Valdez wastewater treatment system would need to be constructed. No funds are allocated in the City of Valdez budget for either a feasibility or engineering study for the extension or for its construction.

2) Even if the sewer system were constructed in time, according to Mr. Ewing there is a legal question concerning whether stipulations associated with a federal grant to the City of Valdez for construction of its sewer treatment plant will permit it to process stormwater runoff from Petro Star. The system was not constructed to handle this type of waste and it is questionable whether it can handle the additional volume (Joint Meeting, tapes).

3) The other possibility is to treat the stormwater runoff on site. Although the applicant expressed a possible intention to treat all wastewater on site (Joint Meeting, tapes), no design plans have been presented demonstrating that this is either possible or feasible.

Petro Star indicated at the Joint Meeting that they would not be discharging waste water to surface waters. However, the facility clearly possesses the possibility of discharging stormwater runoff to adjacent surface waters. It is PWSCA's understanding that EPA regulations state that any facility that may discharge wastes into surface waters, regardless of its design, must undergo an NPDES permit review. At this time Petro Star has not demonstrated that wastewater will not be entering U.S. surface waters and has not applied for an NPDES permit. PWSCA believes there is sufficient evidence to indicate that an NPDES review is required and that it should be a part of the Coastal Zone Constituency Review process. If Petro Star fails to obtain a permit, EPA has the power to delay startup of the refinery, to shut it down until compliance is obtained or to issue a waiver. Issuing a waiver would mean water based resources on which Valdez's existing fisheries and tourism industries depend could be jeopardized. This is a scenario that would be difficult on Petro Star, the EPA and the community of Valdez. If Petro Star wishes to show their ability to be an environmentally responsible Alaskan business and a good addition to the Valdez business community, then PWSCA encourages Petro Star to apply for all permits in a timely manner.

Incomplete information on compliance to the National Emissions Standards for Hazardous Air Pollutants requirements for refineries: Mr. Ewing indicated at the Joint Meeting that the Na-

national Emissions Standards for Hazardous Air Pollutants (section on refineries) might apply to Petro Star's activities and suggested they look at pertinent sections of the law (Joint Meeting, tapes). The application does not address this question.

ADEC AIR QUALITY PERMIT APPLICATION

PWSCA found the Air Quality Permit Application to contain gross errors in the calculations for emission tank losses for the fixed-roof tanks. The calculations for product throughput used a barrel size of 5.6 gallons per barrel. This should be 42 gallons per barrel. PWSCA figured that these errors put Petro Star's figure for Volatile Organic Compounds (VOC) emissions off by a factor of 7.5. This it seemed would have brought their VOC losses from their fixed roof tanks alone to 90 tons per year, which when added to the product loading losses of 2.8 tons/year and the internal floating-roof tank losses of 15.6 tons/year brings the total VOC losses of 108.4 tons/year. These errors were brought to the attention of ADEC and others in a letter from PWSCA dated January 7, 1992. An additional 4 errors were discovered by ADEC and/or CH2M Hill (Petro Star's contractor) but the new total VOC emission figure is not what PWSCA expected. At this time it appears that no one has done or is planning on doing a detailed independent review of this application. PWSCA wonders what other errors of this nature are yet to be found in the document? Therefore PWSCA strongly requests an independent review be initiated by ADEC and made available for public review before a decision is made on Petro Star's permit.

PSD review required: According to federal law, if Petro Star emits more than 100 tons per year or has the capability of emitting more than 100 tons per year, it is required to undertake a Point Source Determination (PSD) review. PWSCA believes Petro Star's application when corrected as indicated in the proceeding comment, requires a PSD review under federal law.

Alaska State regulations are more stringent than federal law and require any facility that processes more than five tons per hour of any material to complete a PSD review. It is PWSCA's position that DEC is required by law to evaluate Petro Star's permit application using both the federal and state standards. It is uncertain at this time whether this has been done.

Modelling for the dispersion of air pollutants and field-testing of models: PWSCA remains concerned about where pollutants will go after they leave the stack. PWSCA encourages ADEC to model the dispersion and field test their modelling against actual conditions in Port Valdez.

GEOPHYSICAL HAZARDS:

The siting of the refinery is of concern to the residents of Valdez because it lies within the 100 year flood plain on the outwash delta of the Lowe River, which raises unanswered questions concerning the site's geological suitability for this type of use. In brief, the site is unsuitable for the following eight reasons:

- 1) It is on unconsolidated sediments in a known mass wasting zone (downslope movement

of rock, soil and other debris). (cf. Valdez Coastal Zone Management Plan).

2) It is on the flood fringe of a braided outwash plain of the glacier fed Lowe River system. (cf. Valdez Coastal Zone Management Plan) which has been, and may in the future continue to be subject to catastrophic floods from the breakage of ice dammed lakes.

3) It is within 0.8 km (0.5 mi.) of a lineament (i.e., a linear surface feature that may be an indicator of earthquake faulting) (1972, Seismology and Geodesy).

4) It is within an area that has experienced seiches (seismic induced sea waves) caused by the sliding of the unconsolidated sediments into Port Valdez during at least four earthquakes in the past 90 years (Coulter, 1966, pp. C7-C9).

5) It is in an area that subsided during the 1964 Earthquake (Tectonics).

6) There are no publicly available core samples and geotechnic engineering analysis showing the nature of the underlying sediments and their ability to bear the weight of the proposed structures in the event of subsidence induced by either erosion from flooding or lateral movement from mass wasting of adjacent areas during an earthquake.

7) The site is within an Alaska Department of Natural Resources (DNR) recognized crucial rated habitat area and adjacent to a Valdez Coastal Zone AMSA area which is highly productive of salmon, bird, and marine life that would be adversely affected in the event of an oil spill (DNR, *Prince William Sound Area Plan*, Unit 21, Map 1: 3-175).

8) The shoreline adjacent to the proposed site is mudflats and salt marsh. At this time, NOAA and other oil spill cleanup authorities do not recommend any oil spill cleanup technologies for use on mudflats or in salt marshes (*Prince William Sound Area Plan: ISCC Shoreline Cleanup Manual*). A spill on these low energy mudflats would have long-term adverse biological effects on the Port's primary and secondary productivity and on commercial enterprises dependent upon fisheries, wildlife viewing and scenic qualities.

IMPORTANCE OF THE LACK OF DETAILED GEOTECHNICAL ENGINEERING STUDY FOR SITE:

The Valdez Coastal Management Program section on geophysical hazards was not followed by the Valdez City Council when the area was rezoned and a conditional use permit issued, because the required detailed geotechnical analysis did not accompany the permit request, was not available to the Valdez Planning and Zoning Commission when they recommended approval of a Conditional Use Permit on September 11, 1991 and was not available on October 7, 1991 when the Valdez City Council rezoned the area from Unclassified to Heavy Industrial and approved the permit. At the Joint Meeting, Mayor Pro Tempore Lynn Chrystal requested Petro Star's geotechnical study be made available to the City. Petro Star's attorney indicated he would provide this (Joint Meeting, tapes). However, no study has been received by the City of Valdez or made available for public review as of January 7, 1992. In a phone conversation on January 6, 1992 Petro Star indicated that the engineering study was not yet complete. The Petro Star spokesperson indicated that when the study was completed that for the most part only the results and not the body of the study would be released. It is PWSCA's position that the results plus supporting data must be made available for peer and public review before a Coastal Consistency review can commence. This position is based on the statement at the Joint Meeting made by Ms. Bens-

from the Division of Governmental Coordination (DGC) that the geological suitability of the site would be considered as part of the Coastal Consistency Review. (Joint Meeting, tapes and p. 10).

PWSCA Literature Search: In the absence of a formal geotechnical study that is available for peer review, PWSCA conducted a literature search for information pertinent to the site's geophysical suitability for a refinery. The following comments are based on this literature search as indicated by references and supported by the professional judgements of recognized authorities.

The permit application and previous public and written comments by Petro Star indicate a lack of information regarding the load bearing capacity of the soils and their stability during a seismic event. Bedrock is the best local substrate for construction purposes (Combellick and Updike, 1987 passim.). The Alyeska Marine Terminal site was blasted out of bedrock and the proposed Trans-Alaska Gas Pipeline facility at Anderson Bay in Port Valdez would be located on bedrock. These sites were chosen for their stability during an earthquake and for protection from seismic induced waves as the elevation gained reduces the risk from wave damage.

Pros and cons of siting the refinery on an alluvial fan: The proposed site lies on an alluvial fan which may overlay Lowe River delta sediments and finer grained marine sediments. PWSCA found some disagreement between geologists on the suitability of the site for construction.

Suitability of surface soils: Combellick maps surface deposits on the site as alluvial fan material consisting of 57.5% gravel, 42.4% sand and 0.1% silt (Combellick, 1987). No borings were taken. However, estimated thickness is less than 20 m; the water table depth is estimated at less than 20 m.; permeability is rated at low to moderate; and susceptibility to frost is considered moderate. Combellick rates the susceptibility to an earthquake induced ground failure for alluvial fan material in general as low and its suitability as foundation material as very good. The map is a general surface geological map for the Valdez area and does not discuss other characteristics of specific sites.

Disadvantages of specific site: According to Coulter (1966), unconsolidated alluvial fan sediments are an acceptable alternative *when held in place by bedrock islands* as in the case of new town Valdez (Coulter, 1966, p. C35). Coulter and other US Geological Survey scientists and engineers consulted by PWSCA indicated that because of the area's seismic activity, there is a significant risk that substantial marine landslides of the adjacent delta material would permit a lateral movement of the unconsolidated alluvial fan sediments, creating significant ground breakage as occurred in the old Valdez town site. Map 16 in the Earthquake Tectonic Studies indicates that this area moved laterally 16 to 19 feet in 1964.

Summary: The difference between Combellick and Coulter lies in their scope: Combellick is discussing only the suitability of the surface soils in general without regard to their specific location and other factors; Coulter is considering the soils plus their location and other geological factors. Since the question is not whether the soils at the proposed site are suitable in general for foundations, but whether the soils in this specific location adjacent to an overly steepened delta are suitable, PWSCA believes that Coulter's observation on the importance of the bedrock

islands as a restraining wall is significant. There is no such restraining bedrock formation to hold the alluvial fan in place at the proposed Petro Star site.

Risks associated with fine-grained sediments: Soils with the greatest risk of instability and potential liquefaction are fine grained sediments, such as those at the eastern end of Port Valdez (Coulter, p. C 14ff. C 35). The risk is also substantially increased in areas where a high water table exists. Soils in the vicinity of old town and between Old Town and the Lowe River are known to belong to this high risk from surveys and core samples taken immediately after the 1964 Earthquake (Coulter, p. C14-15). No core samples were taken on the south side of the Lowe River following the earthquake, nor were visual investigations made according to geologists who participated in the survey, because the Mineral Creek Alluvial Fan with its restraining bedrock formation was clearly a better site for the City of Valdez. However, as indicated above, USGS scientists did determine that mass wasting at the Valdez Old Town site caused some local subsidence due to lateral movement (16 to 19 ft. lateral movement). USGS surveys show subsidence at the east end of Port Valdez ranging from 0.6 ft. near the Petro Star site to 3.5 ft. at the Old Town site (Ferrans, personal communication).

Because information on the proposed site is limited, PWSCA consulted several geologists concerning the possibility of ground breakage associated with either subsidence or lateral movement in the event of a major earthquake. Studies of similar alluvial fans and deltas in the Copper River Basin following the Earthquake indicated that almost every active flood plain had ground breakage. Thus, the geologists PWSCA consulted believed ground breakage probably would have been found on the south side of the Lowe River if a geologist had been available to look for it in 1964.

Possibility of subsurface fine-grained sediments at the Petro Star site: Although no core samples were taken along the delta on the south side of the Lowe River (proposed Petro Star site), Coulter noted: "Inasmuch as materials carried by the Lowe River have been transported much farther than those on the rest of the delta, presumably they would generally have a finer grain or particle size." (Coulter, p. C15). Because subsurface soils at the proposed Petro Star site may have a greater portion of fine grain sediments, the risk of potential liquefaction may be even higher. The Valdez Coastal Zone Management Plan probably did not classify this as a potential liquefaction area because of the lack of specific geotechnical information. Absence of information cannot be used as an argument for or against the area's susceptibility to liquefaction; however, it is a good reason to require that geotechnical information be provided for review prior to permitting the construction of the proposed facility. There is clearly sufficient evidence of potential geological hazards to require that the applicant complete a geotechnical engineering study and release it for peer and public review prior to receiving a Coastal Zone Consistency determination.

Absence of site-specific information on subsurface sediments: Although Coulter thought there might be more fine grained sediments near the Lowe River than at Old Town, no subsurface studies have been done of the area. PWSCA has been unable to find any State or Federal agency which has taken core samples on the Petro Star site. No cores have been taken by the U.S. Geological Survey's Alaska Geological Survey Branch or by the Menlo Park Branch. The State

of Alaska's Division of Geology has not taken any core samples. Furthermore, despite requests for information, Petro Star has not released any information regarding private surveys or core samples they may have taken. United States Geological Survey (USGS) seismologists warn that without these site specific core samples a shaking amplification model for a non-bedrock area would also be impossible (Page, personal communication).

Risks from tsunamis: The Petro Star alluvial fan, unlike the Valdez City location, has no bedrock outcroppings to hold the unconsolidated alluvial sediments in place or to protect the site from being devastated by a tsunami. At least five times in the last 90 years, unconsolidated sediments at the east end of Port Valdez have undergone mass wasting during earthquakes (Coulter, p. C7-C18) creating turbidity currents. Some of these have generated local tsunamis or seiches as happened in 1964. According to USGS reports, the 1964 seiches generated a water surge of 6-9 m. (20-30 ft.) in the eastern end of Port Valdez. The Petro Star site is located only 13 ft. above mean sea level. According to the USGS, this is a normal, not abnormal, event: "Thus, the record shows that on at least five occasions in the past 70 years, submarine slides — and associated turbidity currents — have accompanied earthquakes at Valdez. To this extent, the combined effects of the earthquake of March 27 were in no way abnormal. Instead, they typify a reaction pattern under seismic conditions that may be expected in the prism of saturated fine-grained deposits that make up the Valdez delta (Coulter, p. C9)."

Risk of earthquake during lifetime of refinery: The U.S.G.S. predicts that a major earthquake will occur in the Yakataga fault sometime within the next 25 years. The last time a large Earthquake occurred in the Yakataga area, unconsolidated sediments on the Valdez Delta (including those adjacent to the proposed Petro Star site) slid into Port Valdez (Coulter, C7-9).

Risks from streambank erosion and flooding: In addition to earthquake associated risks, the site is also exposed to the risks of meanderings of the Lowe River and from a 100 year flood. According to the Federal Emergency Management Agency (1983), "The risk of experiencing a rare flood increases when periods greater than one year are considered. For example, the risk of having a flood which equals or exceeds the 100-year flood (one-percent chance of annual occurrence) in any 50-year periods is about 40 percent (four in ten) and, for any 90-year period, the risk increases to about 60 percent (six in ten). The analyses reported here reflect flooding potentials based on conditions existing in the community at the time of completion of this study. (p. 6)." The areas in Texas that have been flooded for the past month were in the 100 year flood plain. This is the second time in three years that some of these communities have been flooded. Let us not now create a problem similar to those in Texas or those that occurred at the Drift River oil facility in Cook Inlet.

Recently, the Lowe River, a braided glacial stream, has moved from along the northern edge of the valley to the southern side and is causing erosion of alluvial fans upstream from the Petro Star site. If the river continues its present course, there is a possibility that river bank erosion will become a problem in the vicinity of the Dayville Road bridges near the Petro Star alluvial fan. Such activity is normal for a braided stream. It can be controlled to a limited degree by in-stream gravel mining and placement of riprap, but according to a hydrologist consulted by the City of

Valdez "there is no practical way to obtain stable streams in those areas where glacial sediment loading is occurring (GEOMAX, 1989, p. 19).

Risk from breakage of an ice-dammed lake: In the past, the Lowe River has experienced catastrophic floods from the breakage of ice-dammed lakes that have caused sudden and dramatic changes in the river's course. At the present, there are no ice-dammed lakes in the Lowe River drainage. However, during conversations with glaciologists of the USGS, the current absence of ice-dammed lakes does not mean they will not reappear in the future, since the glaciers, themselves, are still active (Post, personal communication).

Risk of flooding from mass wasting of slopes as a result of logging: The City of Valdez has requested that DNR offer state land on tributaries feeding the Lowe River for timber harvest. Experience in Southeast Alaska and other areas throughout the world show that logging on steep slopes in areas of high precipitation can lead to serious mass wasting and flooding when streams are blocked and temporary lakes form.

As our testimony indicates, various branches of the State and Federal government and the City of Valdez have conducted surveys and studies indicating the multiple geological hazards of the proposed site. In conclusion, we quote again from the U.S. Geological Survey's "Lessons and Conclusions," which was written after the 1964 Earthquake.

Provision of good geologic maps alone is not enough, of course, to insure that the facts they show will be used effectively in reducing earthquake hazards. This lesson was forcefully taught by the Alaska experience of 1964. Modern geologic maps of Anchorage were available, and geologists had warned in print that one of the map units, the Bootlegger Cove Clay, would be unstable in the event of future earthquakes. The warnings went unheeded, however, because civic authorities, builders and others either were unaware of the existence of the geologic information or ignored its implications.

Disastrous translatory landslides initiated by the earthquake of 1964 amply proved the correctness of the warnings.

Obviously, means must be sought to acquaint city planners, engineers, builders and the populace with the existence of useful geologic information and with its implications in terms of earthquake hazards and land use. (Eckler, p. 39).

What the writer did not mention is that five people died in the Bootlegger Cove slides, because City and State planners did not heed the geologists' warnings. As residents of Valdez whose lives and livelihoods will be adversely affected by the environmental and economic consequences of a major containment failure and spill at the Petro Star refinery, we urge you as planners and regulators to heed the warnings of geologists. Complacency was at the root of the EXXON-VALDEZ Oil Spill. The information and concerns presented here go beyond this project and this community and need to be in the forefront of planning throughout Southcentral Alaska. Let us not now become complacent about the realities of earthquake hazards and then learn the hard way as we did in 1989 about the transportation of North Slope Crude oil through Alaska's waters.

Following the 1964 Earthquake, the U.S. Geological Survey stated:

"Ports, docks, and canneries obviously have to be built close to the shore. But the Alaskan experience indicates that *the hazards are enormously compounded if such facilities are built on steep-faced deltas or other deposits of unconsolidated materials that are marginally stable under seismic conditions.* At many places, such deposits offer the only level surfaces near tidewater for easy or economical construction. If they must be utilized, advance knowledge that they are vulnerable to future earthquakes may stimulate planning to minimize the hazards. (Eckel, p. 38, italics added)."

Since the proposed refinery has not submitted a plan to utilize the waterfront for docks, it is not an economic development that requires positioning on a hazardous site and does not meet the requirements of the Valdez Coastal Zone Plan. The only reason justifying the site's selection appears to be that it is owned by one of the applicants. This is a good reason for the applicant, but it is not a good reason for the City of Valdez or the Coastal Zone Planning Commission to permit siting of the refinery in an area of known geological and hence, economic and environmental risk.

With the exception of some losses experienced by commercial fishermen, U.S. courts do not hold companies responsible for the economic losses caused by their oil spills (Gibbon, 1991). Processors, canneries, cannery workers, suppliers, tour and charter boat operators and many others are excluded from making economic claims against a spiller. Although construction of the Petro Star refinery on this site has a high risk of a major oil spill, the economic costs of that risk will be borne by those who have no economic interest in Petro Star. It is important to note here that Mapco stations sell fuel at higher prices in Fairbanks than in Anchorage despite the fact that a Mapco refinery is located in the Fairbanks area. Location of a refinery in Valdez does not necessarily mean that fuel prices will be lower in the Valdez area. Thus, unless there is a contractual agreement with Petro Star guaranteeing lower price fuels to the Valdez area, it is premature to count on increased business in the transportation and tourism sectors as a result of the availability lower priced fuels in Valdez.

In the event of an earthquake damaging the Petro Star refinery, the City of Valdez through its issuance of a Conditional Use Permit and rezoning of the area and the State of Alaska if it issues a Coastal Zone Consistency determination could be liable for damages to Petro Star for property losses and for compensation to the survivors of any victims. Although the decision to deny or issue Petro Star a permit or consistency determination should be based on a commitment by governments to protect the lives, property and environment within their jurisdictions, PWSCA recognizes that legal obligations are often a stronger argument. Recently, courts in California have held that cities which issue building permits for sites with known geologic hazards are liable for damages to property and life resulting from structural failure during an earthquake.

FAILURE TO FOLLOW ADMINISTRATIVE PROCEDURES ACT:

Inadequate and insufficient public notice for comment period: There has also been an inadequate and insufficient notice for the public comment announcements about this proposed project. The first notice in the local Valdez paper was in the January 9, 1992 issue of the *Valdez Vanguard* for the Air Permit. This was just 8 days from the original deadline date and the incorrect date for the new deadline. A second notice published in the *Valdez Vanguard* appeared after the deadline for comments that appeared in the ad. Additionally, there has been no notice on the request for public comment on the Coastal Consistency review from the Division of Governmental Coordination for this project.

PWSCA has been informed that the deadline has been extended to January 30, 1992. However, this does not meet the requirements of the Administrative Procedures Act for public notice. PWSCA has been told that lawyers are holding that publication of a notice in the *Anchorage Daily News* fulfills the requirement for public notification. The *Anchorage Daily News* is not a local Valdez paper. According to a spokesperson at the *Anchorage Daily News*, they have a circulation in Valdez of 325 households. The *Valdez Vanguard*, a weekly, reaches approximately 1000 households. Most Valdez residents do not look for public notices regarding local Valdez events in the *Anchorage Daily News*. They look for them in the *Valdez Vanguard*. Failure to publish the notification in the *Valdez Vanguard* with complete information about the public comment period for both the Air Quality Permit and the Coastal Zone Consistency determination with the correct comment dates constitutes inadequate notification of the affected publics. PWSCA requests that the comment period be restarted when proper public notice has been given to the people of Valdez.

CONCLUSIONS

The potential risk of loss of life and an oil spill occurring as the result of structural failure during an earthquake, tsunami or flooding appears high. PWSCA recommends that before a Coastal Consistency determination is made that the applicant be required to do a detailed geophysical analysis, seismic engineering study including borings to 100 feet (as DOT does for bridges and should also include a shaking amplification model), do an oil spill risk assessment, and make all studies available for peer and public review.

PWSCA requests that Petro Star be required to undergo a PSD review as we feel this would settle many of the air quality concerns we have. Without a PSD review Petro Star would not be required to utilize best available pollution prevention technology in their facility. Petro Star has indicated that they have been purchasing pieces of refineries over the past 10 years and that this is what they would use to construct a refinery here in Valdez. The EPA requires the best available technology.

The time table publicized by Petro Star for the facility to come on line (fall 1992) with the above mentioned design and engineering aspects either missing or misrepresented, makes it evident that Petro Star cannot be expected to construct and operate a refinery in Valdez in a safe and responsible manner. PWSCA therefore urges you to refuse Petro Star's Air Quality Control Permit to Operate (ADEC File No. 9124-AA001) and rule that this project is inconsistent with the Alaska/Valdez Coastal Management Program and Consistency review (State I.D. No. AK911223-12A).

If it has not become obvious that this project should not be allowed to proceed, then PWSCA requests that public hearings be held in Valdez before a final decision on their permit application and coastal consistency is made.

OBSERVATION:

There is a recognized value in having industry and environmental organizations work together. PWSCA believes that the problems that have accumulated with this proposed project could have been minimized if Petro Star had tried to involve the public in a constructive pre-planning role. For example, in March of 1991, Yukon Pacific Corporation agreed to make a special grant to the Alaska Conservation Foundation to administer the Trans-Alaska Gas System Environmental Review Committee. PWSCA is a participant on this Committee which brings together a sharing of concerns, issues, plans and knowledge. The goal is to save time and money by minimizing such things as lawsuits and re-engineering costs that result from the confrontational approach that too often characterizes the relationship between industry and environmental groups. PWSCA suggested the Joint Meeting that was sponsored by the City of Valdez as an attempt to begin a constructive dialog with Petro Star. Unfortunately, Petro Star did not follow up on concerns raised at the meeting.

At this point in time, the Yukon Pacific Review Committee is working out well, although it is still too early to tell how well the environmental community's input will be utilized. The Yukon Pacific approach does not necessarily guarantee that a project will receive full support from the environmental community nor does it mean that input from the environmental community will be used in a meaningful manner. However, PWSCA is committed to the idea of working together with industry to try to constructively identify potential problem areas in a project at an early stage, so that the company has the opportunity to respond in a timely manner and the risk of litigation delaying a project is reduced. We regret that Petro Star did not wish to pursue such an approach. We expect that the experience with Yukon Pacific will continue to be positive and productive and hope that in the future other companies will follow Yukon Pacific's lead (Appendix II).

Thank you for this opportunity to comment and feel free to contact us with any questions or for any further information.

Respectfully submitted by,



David P. Janka
Executive Director

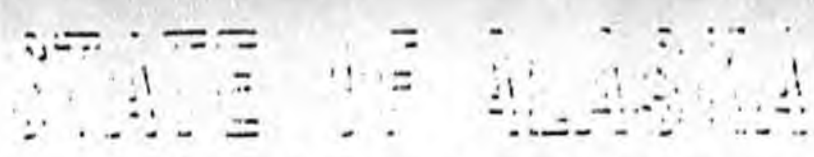
Attached:
Bibliography.
Appendices 1&2 (addressee only).

cc: ADEC Valdez; Alaska Dept. of Fish and Game; ADNR; EPA; Army Corps of Engineers; City of Valdez; Petro Star; Alaska Representatives: Gene Kubina; State Senators Jay Kerttula and Curt Menard; Regional Citizens Advisory Council; Valdez Fisheries Development Association; Jeff Sauer, attorney & Sierra Club Legal Defense Fund; Trustees for Alaska; Alaska Center for the Environment; Northern Alaska Environmental Center; Alaska Conservation Foundation; Cordova District Fisherman United; Oil Reform Alliance; Marine Advisory Program; Public Awareness Committee for the Environment; Greenpeace, Anchorage; Sierra Club, Anchorage; KCHU radio; APRN radio; *Valdez Vanguard*; KVAK radio and *The Pioneer*; *Anchorage Daily News*; *Anchorage Times*.

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DIVISION OF OIL AND GAS

March 3, 1992

David P. Janka, Executive Director
Prince William Sound Conservation Alliance
P.O. Box 1697
Valdez, Alaska 99686

Dear Mr. Janka:

Thank you for your letter concerning the proposed royalty oil sale to Petro Star Valdez Refinery Joint Venture. We received only four comments on the proposed sale (including your two letters) and so we have the luxury to respond to the comments individually.

Your letters are addressed jointly to this department concerning the proposed royalty oil sale; to the Department of Environmental Conservation concerning the air quality permit; and to the Division of Governmental Coordination concerning the Coastal Consistency Permit. However, the concerns outlined in your letters are within the jurisdiction of other agencies, not of DNR.

For example, your letters include concerns with the spill contingency plans (the authority of DEC), air quality permits (DEC), NPDES permits (DEC and EPA). The Department of Natural Resources has neither the expertise nor the statutory authority to rule on those concerns. They are rightfully under the jurisdiction of other agencies. This department takes no positions on the deliberations of those agencies, and we do not expect that the proposed contract will bias their decisions. The decision on the proposed royalty oil sale should not be used to review or appeal the decisions of other agencies. If you wish to appeal their decisions, you should do so directly using the processes that exist in those agencies.

Your concerns are focused on whether the refinery is constructed and if so how it will operate. They do not focus on whether the oil used by the refinery is purchased from the state or from another source. This latter question, along with the question of whether the state is receiving a price is equal to the in-value alternative is the main focus of the finding.

Under separate cover we will be sending you a copy of the Final Finding and Determination and the final contract for the royalty oil sale. The contract, however, will not become effective until approved by the legislature and until the refinery certifies that it will be ready to process the oil. Without the required permits, the refinery cannot operate (and the contract will not take effect).

Thank you for your comments. If you have any further questions, please let me know.

Sincerely,

James E. Eason
Director

Appendix C: Changes to the Preliminary Finding and Draft Contract

The draft contract was changed in response to a request made by the Alaska Royalty Oil and Gas Development Advisory Board. The board pointed out that the draft contract may have been ambiguous with respect to when late payment penalties are due. To clarify the due date for late payment penalties, the following sentence was added to Section 5.7: "The late payment penalty is due at the time of the next Month's payment."

Section 2.1 of the draft contract was changed to simply and clarify the process by which Petro Star JV could change the amount of oil to be tendered under the contract. It standardized the notice requirements (to at least six months and ten days written notice unless the increase or decrease is less than ten percent of the then current nomination, then at least 100 Days written notice). In addition, it clarified the process to ensure that the new tendering will take effect on the first day of the first month after the applicable notice period expires (i.e., the state will not change nominations in mid-month).

No comments requested changes to individual provisions of the preliminary finding and none of the individual provisions were significantly changed.

AGREEMENT FOR THE SALE AND PURCHASE

OF

STATE ROYALTY OIL

to

PETRO STAR VALDEZ REFINERY JOINT VENTURE
PETRO STAR VALDEZ, INC.
ARCTIC SLOPE REGIONAL CORPORATION
HARBOR ENTERPRISES, INC.
ALASKA REFINING, INC.

THE STATE OF ALASKA
Department of Natural Resources

March 4, 1992

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AGREEMENT FOR THE SALE AND
PURCHASE OF ROYALTY OIL

THIS AGREEMENT is entered into as of March 4, 1992 by and between the State Of Alaska ("the State") and Petro Star Valdez Refinery Joint Venture, Petro Star Valdez, Inc., Alaska Refining, Inc., Arctic Slope Regional Corporation, and Harbor Enterprises, Inc. (collectively hereinafter referred to as "Petro Star JV").

ARTICLE I

DEFINITIONS

As used in this Agreement, the following terms shall have the following respective meanings:

1.1 "Commissioner" means the Commissioner of the Alaska Department of Natural Resources or his designee.

1.2 "Daily Royalty Oil" means the quantity of Royalty Oil available from the Lessees of the Kuparuk River Unit each day.

1.3 "Day" means a period of twenty-four (24) consecutive hours, beginning at 12:01 a.m., Alaska Standard Time.

1.4 "Effective Date" shall have the meaning set out in Article VI.

1.5 "Field Cost Agreement" means the Agreement for Settlement of Cleaning, Dehydration and Transportation Charges Applicable to Royalty Oil Taken from the Kuparuk River Unit,

effective as of December 13, 1981, and attached to the Kuparuk River Unit Agreement of December 1, 1981 as Appendix I.

1.6 "Leases" means the Oil and Gas Leases which are subject to the terms of the Kuparuk River Unit Agreement.

1.7 "Lessee" means any person owning a working interest in any of the Leases.

1.8 "Month" means the period beginning at 12:01 a.m., Alaska Standard Time, on the first Day of the calendar Month and ending at the same time on the first Day of the next succeeding calendar Month.

1.9 "Oil" shall have the same meaning as the word "Oil" under the Leases and the Kuparuk River Unit Agreement, except where inconsistent with Section 2.2 of this Agreement, in which case Section 2.2 shall control.

1.10 "Point of Delivery" shall have the meaning set out in Section 2.5.

1.11 "Royalty Oil" means the Oil which the State may take in-kind (in amount) as its royalty under the Leases whether or not the State has elected to take or is taking that royalty in-kind.

1.12 "Royalty Settlement Agreement" means the written royalty settlement agreements between the State and BP Exploration (Alaska) Inc. ("BP") dated December 31, 1991, and the State and Atlantic Richfield Company and Arco Alaska, Inc., ("ARCO") dated September 12, 1990.

1.13 "Royalty Value" means, with respect to each

Royalty Settlement Agreement, the royalty value calculated in accordance with BP's and Arco's Royalty Settlement Agreement for Kuparuk River Oil.

1.14 "TAPS" means the Trans Alaska Pipeline System.

1.15 "Unit Agreement" means the Kuparuk River Unit Agreement effective December 1, 1981, by and between the Lessees, as amended from time to time.

ARTICLE II

SALE OF ROYALTY OIL

2.1 Quantity. The State agrees to sell to Petro Star JV and Petro Star JV agrees to buy from the State that amount of Oil equal to 76.18% of the Daily Royalty Oil ("Maximum Quantity"). Petro Star JV may permanently decrease the Maximum Quantity only twice: (1) once by giving the State written notice seven months before the date of first delivery and (2) once thereafter by giving the State six Months and ten Days written notice.

Petro Star JV may at any time decrease or increase the amount of Oil to be tendered but not the Maximum Quantity except as provided above. To increase or decrease the amount of oil to be tendered, Petro Star JV must give the State at least six Months and ten Days written notice. If, however, the increase or decrease is less than ten percent of the then current nomination, Petro Star JV must give at least one hundred Days written notice. In addition, the new tendering will take effect on the first day

of the first month after the applicable notice period expires.

It is understood and agreed that the volume of Daily Royalty Oil available to the State will vary and may be interrupted from time to time, and depends upon a variety of factors, including the rate of production from the Leases. The State disclaims and Petro Star JV waives any representation, covenant or warranty, expressed or implied, as to the specific quantity or the total or daily, Monthly, average, or aggregate volume of Royalty Oil to be sold or tendered under this Agreement. The State warrants that it has good title to the Oil tendered under this Agreement.

If the State underlifts or stores Royalty Oil at Kuparuk River Unit, or if the State recovers underlifted or stored Royalty Oil, the quantity of Oil tendered under this Agreement shall be calculated as if no Royalty Oil was underlifted or stored or recovered.

2.2 Quality. The Oil sold shall be the same quality as the Royalty Oil delivered by the Lessees to the State at the Point of Delivery. It is understood and agreed that the quality of the Oil sold may vary from time to time. The State disclaims, and Petro Star JV waives, any guarantee, representation, or warranty, either expressed or implied, of the merchantability, fitness for use, or suitability for any particular use or purpose, or otherwise, of any of the Oil delivered under this Agreement or as to any specific, average, or overall quality or characteristic of Oil to be sold or tendered under this

Agreement. Petro Star JV expressly waives any claim that any liquid hydrocarbons made available to the State by the Lessees, including such substances as crude oil, condensate, natural gas liquids, or return oil from the Kuparuk River Unit Crude Oil Topping Plant, that may be blended with crude by the Lessees before the Point of Delivery and tendered as a common stream by the Lessees to the State as Royalty Oil are not Oil, for purposes of this Agreement.

2.3 Price of the Royalty Oil. The price each Month for Oil purchased under this Agreement shall be the average Royalty Value (weighted by production volume) for that Month of all Oil delivered from the Kuparuk River Unit production for which the Royalty Value is determined by the Royalty Settlement Agreements plus field costs. See examples attached as Exhibits A and B.

Field costs are those costs as defined in the Field Cost Agreement. If a field cost different from that in the existing Field Cost Agreement is established through future written agreement, or settlement or final resolution of any litigation, then that new field cost shall apply to the portion of the liquid hydrocarbons deemed not to be covered by the now existing Field Cost Agreement. In the interim, Petro Star JV agrees to pay the State the field costs claimed by the Lessees for any Royalty Oil taken by Petro Star JV. Any future field cost adjustments shall bear interest as provided in Section 5.6.

If any applicable law of the United States of America or any rule or regulation promulgated by a federal agency will,

in the judgment of the State, operate to prohibit or prevent the State from receiving the full amount due under the above provision, Petro Star JV's obligation to pay the amount of the purchase price in excess of the amount permitted will be suspended or adjusted to the minimum extent required for the State to comply with that law, rule or regulation.

2.4 Purchase Price Reopener. The State and Petro Star JV shall have the right to reopen this Agreement as to purchase price only. At any time after Petro Star JV receives Oil for two years from the Date of First Delivery (as defined in Section 2.11), the State or Petro Star JV may exercise the right to reopen by giving the other party one Month prior written notice. Upon issuance and receipt of a notice to reopen, Petro Star JV and the State will promptly commence good faith negotiations in an attempt to establish a new purchase price. If a new purchase price is not agreed to by Petro Star JV and the State within three Months after giving the notice to reopen, either Petro Star JV or the State may terminate this Agreement upon nine Months written notice to the other. The purchase price for Oil tendered during any period pending termination shall be determined in accordance with the price term in effect immediately before giving the notice of intent to reopen. If a new purchase-price provision is agreed to by Petro Star JV and the State, the new purchase-price provision shall become effective for Oil tendered in the Month following the written Agreement on the new purchase-price provision. Not less than two years after the conclusion of

the purchase-price reopener process described above, either Petro Star JV or the State again may reopen this Agreement, as to purchase price only, by giving notice of intent to exercise the right to reopen. At that time, the purchase-price reopener process described above may again be followed and every two years thereafter.

2.5 No Third-Party Intervention. Petro Star JV shall not voluntarily intervene or otherwise participate in any way regarding litigation, styled State of Alaska v. Exxon, et.al., Case No. 1-JU-77-847, ("ANS Royalty Litigation"), any future Royalty Settlement Agreements, or any reopeners or other discussions under or pertaining to Royalty Settlement Agreements. Any judgment resulting from the ANS Royalty Litigation, any future Royalty Settlement Agreements, or any reopener under any Royalty Settlement Agreement shall be conclusively binding upon Petro Star JV whether or not Petro Star JV agrees with or consents to the terms of any such judgment, settlement, or reopener. Furthermore, Petro Star JV has no independent right to invoke any of the provisions of any Royalty Settlement Agreement. If the Royalty Value is modified in the future as a result of a modification of any Royalty Settlement Agreement, a corresponding retroactive modification will be made to the price term of this Agreement and interest will apply to the modification, whether resulting in an overpayment or underpayment, as set forth in Section 5.6. Petro Star JV agrees to be conclusively bound by any such modification agreed to by