

12024 SENATE RESOURCES

Sale Oil for any Month to not more than 85 percent of the total Royalty Oil for the Month or not more than 95 percent of the Royalty Oil for the Month from any single Unit.

2.1.2 Buyer's Elective Reduction of Quantity. Buyer may elect to reduce the initial Sale Oil quantity by giving Notice. The initial Sale Oil quantity shall remain as stated in Section 2.1.1 for 12 Months after the Day of First Delivery. Notice of a reduction shall be delivered to the State at least six Months before the effective date of the reduction. The reduced maximum quantity shall be 137.5 percent of the reduced minimum quantity. For example, if the reduced minimum quantity is 40,000 barrels per Day, the reduced maximum quantity shall be 55,000 barrels per Day (40,000 times 1.375=55,000.)

Buyer may elect additional reductions to the Sale Oil quantity following a reduction to the initial Sale Oil quantity. A reduction cannot be effective until at least 12 Months after the effective date of the most recent reduction in quantity. Notice of an additional reduction shall be delivered to the State at least six Months before the effective date of the additional reduction. The reduced maximum quantity shall be 137.5 percent of the reduced minimum quantity.

The minimum Sale Oil quantity shall not be reduced below 24,000 barrels per day, except (1) in the case of a temporary quantity reduction in the event of a Force Majeure under section 2.1.4, (2) in the event that the North Pole refinery is shut down, or (3) during the second five years of the contract term if the Sale Oil quantity is reduced to zero.

2.1.3 Increase in Quantity Following Elective Reduction. Following a reduction of Sale Oil quantity under Section 2.1.2, Buyer may request an increase in the Sale Oil quantity to an amount that does not exceed the initial Sale Oil quantity. The increased maximum quantity must be 137.5 percent of the increased minimum quantity, and the minimum quantity shall not

be increased to less than 24,000 barrels per day. An increase cannot be effective until at least 12 Months after the effective date of the most recent change in quantity (*i.e.*, a decrease under Section 2.1.2 or an increase under Section 2.1.3). The Commissioner may approve or deny a request for an increase in Sale Oil quantity.

2.1.4 Temporary Quantity Reduction in Event of Force Majeure. In the event of a Force Majeure, Buyer may temporarily reduce the Sale Oil quantity by an amount equal to the reduction in Buyer's requirements that is a direct result of the Force Majeure event. Buyer shall include a notice of temporary reduction in Sale Oil quantity under this Section with each of Buyer's monthly nominations of Sale Oil made in accordance with Section 2.1.5. Each notice of temporary reduction shall include documentation of the nature of the event and quantification of the direct impact of the event on Buyer's Sale Oil requirements for the affected Month of nomination. Temporary reductions in Sale Oil quantity under this Section shall be effective to the extent that the State is able to reduce the volume of Royalty Oil that it actually receives through the nomination process set out in Section 2.1. Buyer shall accept delivery of the total volume of Royalty Oil delivered to the State in accordance with the State's nominations. Buyer acknowledges that some of the Leases from which the State must nominate Royalty Oil require six Months notice to the Lessee prior to decreasing the State's nomination of Royalty Oil to be taken in-kind in any Month.

2.1.5 Monthly Nomination. Buyer shall nominate the total monthly Sale Oil quantity by giving Notice. Except when the additional notice provisions of Section 2.1.6 are invoked by Lessees, a monthly nomination shall be effective on the first Day of the Month following expiration of a minimum of one hundred Days after the Notice of Buyer's nomination. The State will make commercially reasonable efforts to nominate, in accordance with applicable

Unit Agreements, percentages of the State's estimated Royalty Oil volume from one or more Units, at the State's discretion, that will equal the Sale Oil quantity nominated by the Buyer. Buyer agrees to accept the volume of Royalty Oil delivered in accordance with the State's nomination. See Appendix 1 for an illustration of the State's nomination procedure for Sale Oil nominated from the Prudhoe Bay Unit for July 2004.

2.1.6 Additional Notice Provisions. Buyer acknowledges that if a Lessee invokes the Force Majeure provisions of its Royalty Settlement Agreement, the State may be required to give up to 180 Days (*i.e.*, an additional 90 Days) notice to the Lessee prior to decreasing the State's nomination of Royalty Oil to be taken in-kind in any Month. If a Lessee invokes the Force Majeure terms of its Royalty Settlement Agreement as a result of a reduction in Buyer's nomination, Buyer's reduced nomination shall not become effective until the end of the additional 90 Day notice period. If a Lessee invokes the Force Majeure terms of its Royalty Settlement Agreement and extends the notice period an additional 90 Days, the State agrees to make commercially reasonable efforts to reduce its Royalty Oil nominations to other Lessees that have not invoked Force Majeure in order to limit Buyer's obligation to purchase Sale Oil.

2.1.7 No Guarantee of Quantity. The State shall exercise its rights under the Leases and Royalty Settlement Agreements to request that Royalty Oil be delivered as Sale Oil. The State can deliver Sale Oil only to the extent it receives Royalty Oil from the Lessees. The quantity of Royalty Oil available to the State may vary and may be interrupted from time to time depending on a variety of factors, including the rate of production from the Leases. The State disclaims and Buyer waives, any guarantee, representation, or warranty, either express or implied, that a specific quantity of the total, daily, monthly, average, or aggregate Royalty Oil will be delivered as Sale Oil.

2.1.8 Source of Sale Oil. The State will deliver, as Sale Oil, Royalty Oil produced from the Leases and delivered to the State as Royalty Oil in-kind. The availability to the State of Royalty Oil in-kind in any Month may vary depending on a variety of factors, including the rate of production from the Leases. The State disclaims and Buyer waives, any guarantee, representation, or warranty, either express or implied, that Sale Oil delivered and sold by the State in any Month is from a certain Lease, Unit, or other area.

2.1.9 State's Warranty of Title. The State warrants that it has good and marketable title to the Royalty Oil delivered and sold as Sale Oil.

2.2 Quality.

2.2.1 Quality of Sale Oil. The Royalty Oil the State delivers to Buyer as Sale Oil shall be of the same quality as the Royalty Oil delivered to the State at the Point of Delivery. The quality of the Royalty Oil delivered to the State may vary from time to time. The State disclaims, and Buyer waives, any guarantee, representation, or warranty, either expressed or implied, of merchantability, fitness for use, or suitability for any particular use or purpose, or otherwise, and of any specific, average, or overall quality or characteristic of Sale Oil. Buyer specifically waives any claim that any liquid hydrocarbons, including such substances as crude oil, condensate, natural gas liquids, or return oil from the crude oil topping plant, delivered with the Sale Oil, are not Sale Oil for purposes of this Agreement.

2.3 Price of the Sale Oil. The price per barrel of Sale Oil delivered from each Unit by the State to the Buyer each Month shall be equal to

ANS Spot Price - \$1.55 - Tariff Allowance + Quality Bank Adjustment - Line Loss.

"ANS Spot Price" means the monthly average of the daily high and low assessments for the Month for ANS oil traded at the United States West Coast as reported by Platts' Oilgram Price Report, Telerate online data reporting service, and Reuters online data reporting service. The ANS Spot Price calculation will not include days on which prices are not reported, such as weekends or holidays. If one or two of these publications ceases to report daily assessments for ANS oil traded at the United States West Coast, the Parties agree to calculate the ANS Spot Price using the data from the remaining reporting service or services. If either Buyer or Seller makes a good faith determination that the ANS Spot Price no longer accurately represents the price for ANS oil traded at the United States West Coast, Buyer and Seller will attempt in good faith to arrive at a mutually agreeable alternative source to establish, or substitute for, the ANS Spot Price. If the Buyer and Seller arrive at a mutually agreeable alternative source, that source shall be used to determine the ANS Spot Price beginning the Month following the Month in which the alternative source was determined. If Buyer and the State are unable to agree on an alternative source, either may provide written notice of dispute to the other Party, and the dispute shall be administered in accordance with Section 13.1.

"Tariff Allowance" means the sum of (1) the average, weighted by ownership, of the Minimum Interstate TAPS Tariff (Pump Station No. 1 to Valdez Marine Terminal) for each owner in effect on the Day the Sale Oil is tendered by the State to Buyer; and (2) any tariffs paid by Buyer for shipment of Sale Oil upstream of Pump Station No. 1. "Minimum Interstate TAPS Tariff" means the effective TAPS tariff on file with the Federal Energy Regulatory Commission ("FERC") for each carrier on a given Day, excluding incentive tariffs. If a tariff which has been used in the calculation of a Tariff Allowance is changed or subject to a refund order by the FERC, the Tariff Allowance will be recalculated using the changed FERC-ordered tariff, the

Sale Oil Price will be adjusted accordingly, and the resulting refund to the State (or credit to Buyer) will be made in accordance with Article III. If a FERC-ordered tariff is suspended or enjoined from implementation, the Tariff Allowance shall not be recalculated until the suspension or injunction is lifted and the FERC order is implemented and goes into effect.

The "Quality Bank Adjustment" is a per-barrel amount, positive or negative, that accounts for the difference in quality between the oil produced from the units on the North Slope and the co-mingled ANS TAPS stream downstream of the PSVR connection. The Quality Bank Adjustment for a Unit's stream will be calculated each Month as the difference between the stream value for the PSVR Reference Stream and the stream value for each Unit. The stream value and PSVR Reference Stream are reported by the TAPS quality bank administrator. If the stream value or the PSVR Reference Stream is recalculated by the Quality Bank administrator, the Quality Bank Adjustment shall be recalculated and the Price shall be adjusted as follows: (1) a recalculation of a Quality Bank Adjustment that is not the direct result of an order issued by the FERC shall apply to Sale Oil that has been delivered to Buyer from and after the effective date of the adjustment, but any retroactive application of the adjustment shall be limited to Sale Oil that has been delivered to Buyer in the six calendar Months immediately prior to the Month of invoice of the recalculation, and the Price shall be adjusted in accordance with Article III; and (2) a recalculation of a Quality Bank Adjustment that is the direct result of an order issued by the FERC, including but not limited to any and all orders issued in Docket No. OR89-2-016 et al., shall apply to all Sale Oil deliveries that occur within the time frames affected by the FERC order(s), and any resulting liability for retroactive adjustments shall be payable by the State or Buyer in equal monthly installments over the same number of Months as the number of Months of Sale Oil deliveries to which the recalculation of the Quality Bank Adjustment applied. The

payments (or credit) of retroactive adjustments shall begin in the Month following the Month in which the Quality Bank administrator issues an invoice that implements a retroactive adjustment required by the FERC and shall be subject to the billing and payment (or credit) provisions of Article III. If monthly payments are owed at termination, the amount owed (i.e., the monthly payment times the number of months remaining for payments to be made) shall be paid as an adjustment under Article III as follows: (a) the first \$1 million of the amount owed shall be paid in full; and (b) the remainder of the amount owed, if any, shall be discounted to its net present value and the discounted amount shall be paid in full. The discount rate used in this calculation shall be the Bank of America prime rate plus 2 percentage points and the term for discount shall be the number of months of payments remaining at termination. An adjustment under subsection (2) of this paragraph will not be implemented until the relevant FERC order is final and not subject to further appeal.

"Line Loss" is a per barrel amount equal to  $(.0009) \times (\text{ANS Spot Price} - \$1.55 - \text{Tariff Allowance} + \text{Quality Bank Adjustment})$ .

Appendix 2 is an illustrative example of the calculation of the Price of Sale Oil. If there is a conflict between Appendix 2 and Section 2.3, Section 2.3 shall control. The \$1.55 component used in calculation of the Price shall be adjusted one time for Sale Oil deliveries on and after April 1, 2009, according to the terms of Appendix 5.

#### 2.4 Delivery of Sale Oil.

2.4.1 Day of First Delivery. The State will make first delivery of the Sale Oil to Buyer at the Point of Delivery on the first Day of the Month following the Month of Closing ("Day of First Delivery"). "Closing" means the transfer from Williams to Buyer of legal title to

all of Williams' Alaska Properties. All nominations made by Williams prior to Closing that provide for the deliveries of Royalty Oil by the State on and after the Day of First Delivery shall be deemed to be nominations by Buyer under this Agreement and shall be subject to all terms of this Agreement, including Price.

2.4.2 Later Deliveries. After the first delivery, the State shall tender the Sale Oil to Buyer at the Point of Delivery immediately upon the receipt of the Royalty Oil from the Lessees at the Point of Delivery.

2.5 Passage of Title and Risk of Loss. Title to, and risk of loss of, the Sale Oil shall pass from the State to Buyer for all purposes when the State tenders delivery of the Sale Oil to Buyer at the Point of Delivery. Buyer shall bear all risk and responsibility for the Sale Oil after passage of title.

2.6 Indemnification After Passage of Title. Buyer shall indemnify and hold the State harmless from and against any and all claims, costs, damages (including reasonably foreseeable consequential damages), expenses, or causes of action arising from or related to any transaction or event in any way related to the Sale Oil after title has passed to Buyer. If Buyer suffers damages or losses caused by third parties and related to the Sale Oil, the State agrees to cooperate with the Buyer to permit Buyer to attempt to recover such damages or losses. The State will, on request, assign the State's claims to Buyer and cooperate in Buyer's pursuit of State assigned claims.

2.7 Transportation Arrangements. Buyer shall make all arrangements for transportation of the Sale Oil from the Point of Delivery, to, through and away from the TAPS, and all pipelines upstream from Pump Station No. 1, and shall be responsible for meeting any linefill and storage tank bottom requirements related to transportation of the Sale Oil after

passage of title, except that the State shall be responsible for meeting any linefill requirements for pipelines upstream of Pump Station No. 1. If Buyer provides the necessary data, the State shall meet its linefill requirements by passing title to Sale Oil to Buyer at the Point of Delivery but not invoicing Buyer for the portion of Sale Oil required for linefill until that portion of Sale Oil has been delivered to Buyer at Pump Station No. 1. For purposes of invoicing, Buyer and State agree that the linefill upstream of Pump Station 1 that has not been invoiced will be deemed to be the last barrels injected at the Point of Delivery. On the State's request, Buyer shall provide the State with evidence of the arrangements for transportation of the Sale Oil from the Point of Delivery, through and away from TAPS, and all pipelines upstream from Pump Station No. 1, and evidence of arrangements for resale, exchange, or other disposal of the Sale Oil. Buyer's failure to provide information, evidence, or assurances requested by the State shall, at the State's election and after Notice to Buyer, constitute a material default under this Agreement.

### **ARTICLE III INVOICING AND PAYMENT**

3.1 Invoices. On or before the twentieth calendar Day of each Month after the first Month of delivery of Sale Oil, the State shall send to Buyer via facsimile a statement of account with an invoice for the total amount due for the estimated quantity of Sale Oil delivered to Buyer during the immediately preceding Month and the estimated Price applicable to those deliveries. The State will base its estimates on the best information reasonably available to the State. The State shall adjust invoices as provided in Section 3.3.

3.2 Payment of Invoices. Buyer shall pay the total amount of each invoice, in full, on or before the later of (1) the third Business Day after the date of the statement of account in which the invoice is included; or (2) the twentieth calendar Day of the Month. Any amount that

Buyer does not pay in full on or before the payment due date calculated in accordance with this section shall accrue interest as provided in Section 3.5, and become subject to the late payment provisions of Section 3.7, and any other remedies available to the State under this Agreement and at law.

3.3 Adjustments. Buyer acknowledges that any time after an invoice is sent, the State may receive more accurate information concerning the ANS Spot Price, actual quantity of Sale Oil delivered to Buyer, the proper calculation of Tariff Allowance, and Quality Bank Adjustments that affect the Price of the Sale Oil. Buyer agrees that any time such information becomes available to the State, the State shall make adjustments and invoice or credit Buyer the amount of the adjustment in accordance with the process and retroactivity limits described in Section 2.3. The State shall invoice or credit Buyer in a statement of account for the adjustments as promptly as reasonably possible. All adjustments shall be paid within 30 Days of the end of the term.

3.4 Payment of Adjustments. The Buyer shall pay the total amount of each adjustment invoice in full, on or before the later of (1) the third Business Day after the date of the statement of account that includes the adjustment invoice; or (2) the twentieth calendar Day of the Month. If an adjustment is due to Buyer for an overpayment, the State shall credit to Buyer the amount of the overpayment on the following Month's invoice or, if no following Month invoice is provided, the State shall refund to Buyer the amount of the overpayment by the twentieth calendar Day of the following Month. Any amount the Buyer does not pay in full when due shall bear interest at the rate provided in Section 3.5 and become subject to the late payment provisions of Section 3.7, and any other remedies available to the State under this Agreement and at law.

3.5 Interest. All amounts under this Agreement that Buyer does not pay in full when due, or that the State does not credit Buyer or pay in full when due, shall bear interest from the date payment is due, calculated in accordance with Section 3.4, at the rate provided by Alaska Statute 38.05.135(d) or as that statutory provision may later be amended.

3.6 Adjustments After Termination. Buyer and State agree that the State shall continue to make adjustments after termination of this Agreement, and agree that the provisions of Articles III, VI, VII, and IX shall survive termination of this Agreement for any reason. If following termination of this Agreement an adjustment is determined to be due to Buyer for overpayment in an amount that exceeds the amount of all sums remaining due from Buyer to the State, the State shall credit the overpayment against any sums due from Buyer to the State, and shall refund to Buyer the remaining amount of the adjustment. Any adjustments made after termination must be paid within thirty Days after the date of the invoice.

3.7 Late Payment Penalty. In addition to all other remedies available to the State, if Buyer fails to make timely payment in full of any amount due, including adjustments, Buyer shall pay the State as a late payment penalty an amount equal to five percent of the total amount not timely paid, in addition to the amount not timely paid. The Commissioner shall waive imposition of the late payment penalty if the Buyer provides evidence that the failure to make timely payment was not willful and was not due to one mistake in a chronic pattern of mistakes. Appendix 3 contains an illustrative example of interest and late payment penalties.

3.8 Disputed Payments. If a dispute arises concerning the amount of an invoice, Buyer agrees to pay in full all amounts not in dispute, and to explain in writing with particularity the basis for and calculation of any disputed amounts withheld.

3.9 Confidential Information. The State and Buyer agree that the State may invoice Buyer for, and Buyer agrees to pay, amounts that are based upon confidential information held or received by the State. If confidential information is used as the basis for an invoice, upon receipt of a written request from Buyer, the State shall furnish to Buyer a certified statement of the Commissioner to the effect that, based upon the best information available to the State, the invoiced amounts are correct. At the request and expense of Buyer, the Commissioner's certified statement will be based on an audit by an independent third party.

3.10 Manner of Payment. Except as provided in Section 3.8, Buyer shall pay all invoices in full within the times specified and without any deduction, set off, or withholding. Buyer shall pay all invoices by either Automated Clearinghouse or by Federal Reserve Wire Transfer (immediate funds available) procedure to the following State account and address:

State Street Bank & Trust Company  
Boston, Massachusetts  
ABA #011000028  
For Credit to the State of Alaska  
General Investment Fund – AY01  
Account No. 00657189 (Federal Reserve Wire Transfer)  
Account No. 00653220-10000 (Automated Clearinghouse)

Buyer may pay an invoice in such other manner or to such other address the State has specified in an invoice or by written notice. All other payments due shall be paid in the same manner and according to the same time schedule provided in this Article. If payment falls due on a Saturday, Sunday, or federal bank holiday, payment shall be made on the next Business Day.

#### **ARTICLE IV** **IN-STATE PROCESSING**

4.1 In-State Processing. Buyer shall use all commercially reasonable efforts to insure that Sale Oil will be processed at its Alaska refinery or be exchanged for other crude oil that will

be processed at its Alaska refinery. "Process" means the manufacture of refined petroleum products.

**ARTICLE V**  
**BUYER'S SPECIAL COMMITMENTS**

5.1 Buyer agrees to comply with and perform the list of "Special Commitments" contained in Appendix 4 to this agreement.

**ARTICLE VI**  
**BUYER'S AND GUARANTOR'S REPRESENTATIONS AND OBLIGATIONS**

6.1 Good Standing and Due Authorization of Buyer. Buyer warrants that it is, and shall remain at all times during the term of this Agreement: (1) qualified to do business in Alaska; and (2) in good standing with the State. Buyer warrants that it has all company power and authority necessary, and has performed all company action required, to enter into and fulfill its obligations under this Agreement.

6.2 Good Standing and Due Authorization of Guarantor. Guarantor warrants that it is, and shall remain at all times during the term of this Agreement: (1) qualified to do business in Alaska; and (2) in good standing with the State. Buyer warrants that it has all company power and authority necessary, and has performed all company action required, to enter into and fulfill its obligations under this Agreement.

6.3 Financial Information. As soon as practicable after the execution of this Agreement, and annually as soon as practicable after March 31 but no later than June 30, Guarantor shall cause a financial analyst (the "Financial Analyst") to submit an opinion to the Commissioner in the form of a letter (the "Opinion Letter") about Guarantor's current and expected future credit rating by Standard and Poor's and Moody's. The Financial Analyst shall be qualified to render an opinion as to the creditworthiness of the Guarantor and shall be in the

business of understanding complex financial matters and financial statements to the extent required to render such opinion. Buyer shall have the right to designate the Financial Analyst, subject to approval by the State. The Financial Analyst shall be a contractor to Guarantor, and Guarantor shall be responsible for entering into any necessary contractual arrangements with the Financial Analyst and paying the fees and expenses of the Financial Analyst.

The contract between Guarantor and the Financial Analyst and each Opinion Letter must recite that the Financial Analyst (1) has been provided a copy of this Agreement, (2) understands the significance of the Opinion Letter in the administration of this Agreement, (3) understands that the State will rely on the Opinion Letter, and (4) understands that the Opinion Letter is for the benefit of the State. The contract between Guarantor and the Financial Analyst shall be subject to approval by the State, and the State shall be given a copy of the contract and all amendments to it.

The Opinion Letter shall (i) identify all documents reviewed in forming the opinion, (ii) identify people interviewed in forming the opinion and discuss the nature of the interview, (iii) state the current long term (and short term, if available) credit ratings of Guarantor by Standard and Poor's and Moody's and (iv) express an opinion whether those ratings are reasonably likely to fall to or below BBB+ (Standard and Poor's) and Baa1 (Moody's) at any time during the following twelve Months. Guarantor shall cause the Financial Analyst to review evidence of the most current ratings by Standard and Poor's and Moody's of Guarantor's long and short term debt, all bank presentations provided to Guarantor's lenders, all reports on Guarantor prepared by Standard and Poor's or Moody's, any assessment (if available to the Guarantor) of Guarantor's financial condition conducted on behalf of the Port Commission of the Port of Corpus Christi Authority, concerning the Port of Corpus Christi Authority of Nueces County.

Texas Solid Waste Disposal Revenue Bonds, all documents filed by Guarantor with the Securities and Exchange Commission, if any, any other documents reasonably necessary to deliver the Opinion Letter, and a complete set of year-to-year comparative, independently audited financial statements, including footnotes, prepared in accordance with generally accepted accounting principles.

Guarantor's contract with the Financial Analyst may require the Financial Analyst to protect the confidentiality of the information supplied to it under Section 6.3. The State may review the information supplied to the Financial Analyst under Section 6.3 by executing a confidentiality agreement with Guarantor but will not take any action that will make the information part of the State's public records.

6.4 Financial Condition. Guarantor warrants (1) that all financial information submitted to the Financial Analyst or reviewed by the State under Section 6.3 is complete and accurate at the time of preparation, and fairly represents Guarantor's financial condition at the time of submission; and (2) that there has been no material change in Guarantor's financial condition, business operations, or properties since the financial information was prepared. Guarantor warrants that the financial statements were prepared in accordance with generally accepted accounting principles. Guarantor and Buyer shall immediately inform the State of any material change in Guarantor's ownership or ownership of Buyer, ownership of parent companies, or financial condition, business operations, agreements, or property that is likely to affect their ability to perform their obligations under this Agreement.

6.5 Absolute Obligations. Buyer's and Guarantor's obligations to pay amounts due, provide assurances of performance in accordance with Article VII, accept, and dispose of and pay for Sale Oil, are absolute. These obligations shall not be excused or discharged by the

operation of any disability of Buyer or Guarantor, event of Force Majeure, impracticability of performance, change in conditions, or other reason or cause.

6.6 Guaranty. Buyer was formed to purchase the refinery at North Pole, Alaska now owned by Williams Alaska Petroleum, Inc. Buyer is an indirect, wholly-owned subsidiary of Guarantor. Buyer does not have any operating history, does not have public financial statements, and does not have debt rated by Moody's or Standard and Poor's. The State is not willing to make this Agreement based solely on the credit worthiness of Buyer. Guarantor therefore agrees that it guarantees performance of all of Buyer's obligations under this Agreement as if Guarantor were the Buyer and legally indistinguishable from Buyer. The State may require Guarantor at any time to satisfy any unsatisfied obligation of Buyer.

#### **ARTICLE VII** **ASSURANCE OF PERFORMANCE**

7.1 Credit Review. If Guarantor fails to timely submit its financial statements and other documents and information required under Article VI such that the Financial Analyst is unable to timely submit the Opinion Letter; or if, in the opinion of the Financial Analyst, Guarantor's credit ratings have fallen to or below, or are reasonably likely in the twelve Months following the Opinion Letter, to fall to or below (a) "BBB+" (Standard and Poor's "Long term issuer"), or (b) "Baa1" (Moody's Investor Services "Issuer Ratings/Long Term Obligation Ratings"); or Guarantor is not rated by Standard and Poor's and Moody's, Guarantor shall immediately deliver to the State a one year irrevocable stand-by letter of credit (the "Letter") meeting the requirements of Sections 7.2 through 7.5.

Guarantor shall annually renew and continuously maintain the Letter in effect until such time as, in the opinion of the Financial Analyst, Guarantor's credit rating is no longer reasonably likely to fall to or remain below (a) "BBB+" (Standard and Poor's "Long term issuer"); or (b)

"Baal" (Moody's Investor Services "Issuer Ratings/Long Term Obligation Ratings") at any time during the twelve Months following the Opinion Letter.

7.2 Letter of Credit. In the event that Guarantor is required to deliver a letter of credit to the State in accordance with Section 7.1, the Letter shall be in a form satisfactory to the Commissioner and shall be in effect no later than five Business Days after the effective date of Notice from the State to the Guarantor ("Letter Effective Date"). The State's Notice shall include a description of the circumstances that trigger the Letter requirement in accordance with Section 7.1. The Letter shall be issued for the benefit of the State by a state or national banking institution of the United States that is insured by the Federal Deposit Insurance Corporation and has an aggregate capital and surplus amount of not less than One Hundred Million Dollars (\$100,000,000) ("Issuer"), or other banking institution approved by the Commissioner, such approval not to be unreasonably withheld. The principal face amount of the Letter shall be an amount reasonably estimated by the Commissioner to be equal to the Price of all Sale Oil to be delivered by the State to Buyer during the 90 Days immediately following the Letter Effective Date. The Letter shall not require the State to submit any documentation in support of drafts drawn against it other than a certified statement by the Commissioner and the State's Attorney General that Guarantor is liable to the State for an amount of money equal to the amount of the draft, that the amount of money is due and payable in full, and it has not been timely paid.

7.3 Performance Assurance After Termination. If in accordance with the terms of Section 7.1, a Letter is in effect immediately prior to Termination of the Agreement, the Commissioner may require that, after Termination, the Letter be maintained in an amount estimated by the Commissioner to be equal to the value of all adjustments which may be made under Article III. As an alternative to maintaining a Letter after Termination, the Guarantor may

establish and maintain an interest-bearing escrow account in the same amount and including the same payment terms as the Letter requirements of Section 7.2. on commercial terms acceptable to the Commissioner.

7.4 Other Performance Assurance. The Commissioner may allow Guarantor to provide security other than the Letter if the Commissioner determines other security is adequate to protect the State's interest.

7.5 Correction of Defects in Letter. Guarantor shall have five Business Days to correct any defect in the Letter beginning on the Business Day Guarantor first learns of the defect whether through Notice from the State or otherwise. A defect is any failure to comply with the terms and conditions of Article VII.

#### **ARTICLE VIII** **MEASUREMENTS**

8.1 Measurements. The quantity and quality of Sale Oil the State delivers under this Agreement shall be determined by measurement at the Point of Delivery. Procedures used for metering and measuring the Sale Oil shall be in accordance with the procedures in effect at the Point of Delivery.

#### **ARTICLE IX** **EFFECTIVE DATE AND TERM**

9.1 Effective Date. This Agreement shall be effective when it is signed by all parties ("Effective Date")

9.2 Initial Term. The Initial Term of this Agreement shall begin on the Day of First Delivery and terminate at the end of the last Day of the 12th Month after the Day of First Delivery, including the Month in which the Day of First Delivery occurs.

9.3 Extension of Term. Under Alaska Statute 38.06.055, this Agreement is limited to a term of no longer than one year unless a longer term is approved by the Alaska legislature. The Commissioner shall have legislation to approve the extension of the term of this Agreement for an additional nine years following the last Day of the Initial Term prepared for introduction to the 23rd Legislature in 2004. The Commissioner and Buyer agree to use their best efforts to support the passage of the legislation.

9.4 Termination Prior to Legislative Approval. Buyer, Guarantor, or the State may terminate this Agreement, with no further obligation or liability to each other, if Enactment has not occurred on or before March 17, 2004. Notice of termination shall be in writing, and shall be effective if delivered to the other Party in accordance with Section 16.1 before Enactment. "Enactment" means the Governor's signing of a bill passed by the 23rd Legislature that approves the extension of the term of this Agreement for an additional nine years following the last Day of the Initial Term.

9.5 Closing on Williams' Alaska Properties. Buyer, Guarantor, or the State may terminate this Agreement, with no further obligation or liability to each other, if Closing has not been completed before April 1, 2004. Notice of termination shall be in writing, and shall be effective if delivered to the other Party in accordance with Section 16.1 before Closing.

9.6 Continuation of Obligations. Except as provided in Sections 9.4 and 9.5, termination of this Agreement shall not relieve either Party from any expense, liability, or other obligation or any remedy that has accrued or attached prior to the date of termination. For Sale Oil actually delivered under this Agreement, termination of this Agreement shall not relieve Buyer of its obligation to pay all production Month invoices, initial adjustments, subsequent

adjustments, and interest, and, where applicable, penalties, costs, attorney fees, and any other charges related to the Sale Oil actually delivered.

**ARTICLE X**  
**DEFAULT OR TERMINATION**

10.1 Default.

10.1.1 Events of Default. The Commissioner may suspend or terminate the State's obligations to tender, deliver and sell Sale Oil to Buyer, and may exercise any one or more of the rights and remedies provided in this Agreement, or at law, if any one or more of the following events of default occur:

(i) Buyer or Guarantor fails to pay in full any sum of money owed under this Agreement within five Business Days after the State gives Buyer Notice that payment is past due:

(ii) Within five Business Days after Notice from the State, Buyer or Guarantor fails to provide written assurances satisfactory to the State of Buyer's or Guarantor's intention to perform its obligations under this Agreement and evidence or assurances of transportation arrangements under Section 2.7:

(iii) There is a material change in Buyer' or Guarantor's financial condition, business operations, agreements, or property or ownership that is likely to affect Buyer's or Guarantor's ability to perform its obligations under this Agreement, and within five Business Days after Notice from the State, Buyer or Guarantor is unable or unwilling to provide a Letter meeting the requirements of Sections 7.1 and 7.2:

(iv) Buyer or Guarantor fails to perform any of its obligations under this Agreement, and cannot cure the non-performance or the non-performance continues for more than 30 Days after the State has given Notice to Buyer or Guarantor of its non-performance:

(v) Any representation or warranty made by Buyer or Guarantor in this

Agreement is found to have been materially false or incorrect when made; or

(vi) Guarantor fails, or is unable for any reason (including reasons beyond Guarantor's control), to maintain the Letter required under Article VII, regardless of Guarantor's willingness or ability to perform any other obligations under this Agreement.

10.1.2 Default by Inability to Pay. Buyer or Guarantor shall immediately provide the State with Notice if Buyer or Guarantor is unable to pay any of its debts when due, makes an arrangement for the benefit of creditors, files a bankruptcy petition, or is otherwise insolvent. Upon Notice from Buyer or Guarantor, or if the State independently determines that Buyer or Guarantor is unable to pay any of its debts when due or is otherwise insolvent, the State's obligations to deliver and sell Sale Oil to Buyer shall automatically and immediately terminate without any requirement of Notice to Buyer or Guarantor or other action by the State. Within 30 Days after termination under this Article 10.1.2, the State shall have the right, upon consent of Buyer or Guarantor, to reinstate all of the State's, Buyer's and Guarantor's obligations under this Agreement retroactive to the date of termination.

10.2 State's Remedies. If Buyer or Guarantor defaults under this Agreement, in addition to all other remedies available to the State under this Agreement or at law, the following remedies shall be available to the State:

10.2.1 Buyer's and Guarantor's Obligations Become Due. All monetary obligations Buyer or Guarantor has accrued under this Agreement, even if not yet due and payable, shall immediately be due and payable in full.

10.2.2 State May Dispose of Sale Oil. The State may dispose of some or all of the Sale Oil to third parties. If the State exercises this remedy, regardless whether this Agreement is terminated, Buyer and Guarantor shall be and shall remain liable to the State for the amount of the difference between the Price for the Sale Oil under Article II and the actual price the State receives from disposition of the Sale Oil to third parties.

10.2.3 Indemnification for Loss. Buyer and Guarantor shall hold the State harmless and indemnify it against all its liability, damages, expenses, attorney's fees and costs, and losses directly arising out of Buyer's or Guarantor's default, termination of the State's obligations, and disposal of the Sale Oil to third parties. Additionally, if Buyer or Guarantor defaults in the payment of any monetary amounts due to the State for Sale Oil tendered or delivered under this Agreement, Buyer or Guarantor shall pay the State 100 percent of reasonable actual costs and attorney fees incurred by the State in pursuing payment of the monetary amounts due, regardless of whether litigation is commenced and regardless of whether legal services are provided by the Attorney General's office or private counsel.

10.2.4 Other Rights and Remedies. The State shall have the right cumulatively to exercise all rights and remedies provided in this Agreement and by law, and obtain all other relief available under law or at equity, including mandatory injunction and specific performance.

10.3 Limitation of Buyer's and Guarantor's Remedies. If Buyer or Guarantor breaches or defaults in any of its obligations under this Agreement, Buyer or Guarantor shall not obtain a temporary restraining order or preliminary injunction preventing the State from disposing of the Sale Oil in accordance with Section 10.2.2.

10.4 Article Survives Termination. This Article survives termination of the Agreement.

#### **ARTICLE XI** **DISPOSITION OF OIL UPON DEFAULT OR TERMINATION**

11.1 Disposition of Oil Upon Default or Termination. Buyer and Guarantor acknowledge that the State may be required to provide six Months notice to the Lessees before the State may decrease its in-kind nomination of Royalty Oil in any Month. The Commissioner may request a waiver of any notice provision, condition, or requirement of a Lease, Unit Agreement, Royalty Settlement Agreement or other agreement. If this Agreement terminates for default or any other reason after Buyer has nominated or is deemed to have nominated Sale Oil,

Buyer shall continue to accept and pay for Sale Oil through the first Day of the Month following expiration of a minimum of 100 Days after the date of termination, if the Commissioner so requires. Under no circumstances will Buyer be deemed to have nominated Sale Oil if Closing does not occur. If, however, the additional notice provisions of Article 2.1.6 are invoked, Buyer shall continue to accept and pay for Sale Oil until the expiration of six Months and ten Days after the Date of default or notice of termination.

11.2 Security for Disposal of Sale Oil. To secure the Buyer's obligations to purchase and dispose of Sale Oil, upon the Commissioner's request, if Buyer refuses to accept or receive Sale Oil under this Agreement, Buyer shall assign or otherwise transfer to the State, or its designee, Buyer's right to transport the Sale Oil through and away from the TAPS, and all pipelines upstream from Pump Station No. 1, whether such rights are under nominations, leases, contracts, tariffs, charter parties, or other agreements. The State shall not incur liability or obligations unless the State actually exercises its rights under this Section.

#### **ARTICLE XII** **NONWAIVER**

12.1 Nonwaiver. The failure of a Party to insist upon strict or a certain performance, or acceptance by a Party of a certain performance or course of performance under this Agreement shall not: (1) constitute a waiver or estoppel of the right to require certain performance or claim breach by similar performance in the future; (2) affect the right of another Party to enforce any provision; or (3) affect the validity of any part of this Agreement.

#### **ARTICLE XIII** **DISPUTE RESOLUTION**

13.1 Dispute Resolution. Any disagreement or dispute about the meaning or application of a word, term, condition, right, or obligation in this Agreement shall be decided

according to the dispute resolution procedure set forth in this Article. The procedure set forth in this Article shall be initiated by a Party by providing written Notice of the disagreement or dispute to the other Parties. No later than sixty Days after a Party provides written Notice, the Parties shall each present any arguments and evidence supporting its view of the disputed term, condition, right, or obligation in writing to the Commissioner for consideration. The State, Buyer and Guarantor shall not have the right to civil litigation-type discovery or a civil litigation-type trial with the right to call or cross-examine witnesses unless granted by the Commissioner, after request. Within thirty Days after the Parties submit their arguments and evidence, the Commissioner shall issue a finding interpreting the meaning or application of the disputed word, term, condition, right, or obligation and shall set forth the basis for the conclusions. The Parties agree to accept findings of the Commissioner under this Article that are supported by substantial evidence in light of the whole record.

#### **ARTICLE XIV** **SEVERABILITY**

14.1 Severability. If a court decrees any provision of this Agreement to be invalid, all other provisions of this Agreement shall remain valid. If, however, invalidation of a provision impairs a material right or remedy under this Agreement, the Parties will negotiate in good faith to maintain the original intent and benefits of this Agreement. If the Parties cannot restore the original intent and benefits of this Agreement, then either Party may terminate this Agreement by giving Notice.

#### **ARTICLE XV** **FORCE MAJEURE**

15.1 Effect of Force Majeure. Except for Buyer's and Guarantor's obligations to pay amounts due, provide assurance of performance in accordance with Article VI, and to accept,

dispose of, and pay for Sale Oil, no Party shall be liable for failure to perform if performance is substantially prevented by Force Majeure after commercially reasonable efforts to perform.

15.2 Force Majeure. The term "Force Majeure" means an event or condition not within the reasonable control of the Party claiming "Force Majeure." Force Majeure Events include, but are not limited to, the following events:

i. act of God, fire, lightning, landslide, earthquake, storm, hurricane, hurricane warning, flood, high water, washout, explosion, well blowout, failure of plant, pipe or equipment, or:

ii. strike, lockout, or other industrial disturbance, act of the public enemy, war, military operation, blockade, insurrection, riot, epidemic, arrest or restraint by government of people, terrorist act, civil disturbance, or national emergency;

iii. act, order, or requisition of any governmental agency or acting governmental authority or any governmental proration, regulation, or priority.

15.3 Notice and Remedy of Force Majeure. If a Party believes that Force Majeure has occurred, the Party shall immediately notify the other Parties of its claim of Force Majeure. Except for Buyer's and Guarantor's absolute obligations to pay amounts due, provide assurances of performance in accordance with Article VII, and accept, dispose of and pay for Sale Oil, the disabled Party's obligations to perform that are affected by the Force Majeure shall be suspended from the Notice Effective Date until the disability caused by the Force Majeure should have been remedied with reasonable diligence. If Buyer or Guarantor is prevented by Force Majeure from performing any material obligation for 180 successive Days or more, the Commissioner may terminate this Agreement on sixty Days Notice.

**ARTICLE XVI**  
**NOTICE**

16.1 Method. All notices, consents, requests, demands, instructions, approvals, and other communications permitted or required ("Notice") shall be made in writing and delivered by any two of the following methods: (a) personally delivered, (b) delivered and confirmed by facsimile transmission, (c) delivered by Federal Express, DHL, or other reputable overnight courier delivery service, (d) e-mail, or (e) deposited in the United States mail, first class, postage prepaid, certified or registered, return receipt requested, addressed as follows:

State of Alaska  
Commissioner of Natural Resources  
400 Willoughby Avenue  
Juneau, Alaska 99801  
Facsimile Number: (907) 465-3886  
e-mail: commissioner@dnr.state.ak.us

and

Director, Division of Oil and Gas  
550 West 7th Street, Suite 800  
Anchorage, Alaska 99501-3510  
Facsimile Number: (907) 269-8938  
e-mail: director\_dog@dnr.state.ak.us

the Buyer:

Flint Hills Resources Alaska, LLC  
4111 E. 37<sup>th</sup> St. N.  
Wichita, KS 67220  
Facsimile Number: (316) 828-8245  
Attention: President  
e-mail: allen.lasater@flhr.com

the Guarantor:

Flint Hills Resources, LLC  
4111 E. 37<sup>th</sup> St. N.  
Wichita, KS 67220  
Facsimile Number: (316) 828-8245  
Attention: President  
e-mail: david.robertson@flhr.com

or to any other place within the United States of America designated in writing by the State, Buyer or Guarantor.

16.2 Notice Effective Date. Notice given by personal delivery, overnight courier, or mail shall be effective on the date of actual receipt at the appropriate address. Notice given by facsimile or e-mail shall be effective on the date of actual receipt if received during recipient's normal business hours, or at the beginning of the next business Day after receipt if received after recipient's normal business hours. The Notice Effective Date is the effective date of the first of the two Notices received.

16.3 Change of Address. A Party may notify the other Parties of changes in its address by giving Notice.

#### **ARTICLE XVII RULES AND REGULATIONS**

17.1 Rules and Regulations. This Agreement is subject to all applicable laws of the State of Alaska, and orders, rules and regulations of the United States, the State of Alaska, and any duly constituted agency of the State of Alaska.

#### **ARTICLE XVIII SOVEREIGN POWER OF THE STATE**

18.1 Sovereign Power of the State. This Agreement shall not be interpreted to limit in any way the State's ability to exercise any sovereign or regulatory powers, whether conferred by constitution, statute or regulation. The State's exercise of any sovereign or regulatory power shall not be deemed to enlarge any of Buyer's or Guarantor's rights, or limit any of Buyer's or Guarantor's obligations or liabilities under this Agreement.

**ARTICLE XIX**  
**APPLICABLE LAW**

19.1 Governing Law. This Agreement, and all matters arising from or related to this Agreement, shall be governed, construed and determined by the laws of the State of Alaska.

19.2 Jurisdiction. After exhaustion of the dispute resolution provisions in Article XIII, any legal action or proceeding arising out of or related to this Agreement shall be brought in a State court, and Buyer and Guarantor irrevocably submit to the jurisdiction of the State court in any action or proceeding.

**ARTICLE XX**  
**WARRANTIES**

20.1 Warranties. The purchase and sale of Royalty Oil under this Agreement are subject only to the warranties the State has expressly set forth in this Agreement. The State disclaims and Buyer and Guarantor waive all other warranties, express or implied in law.

**ARTICLE XXI**  
**AMENDMENT**

21.1 Amendment. This Agreement may be supplemented, amended, or modified only by written instrument duly executed by the Parties, and, where required, only on approval under Alaska Statute 38.06.055.

**ARTICLE XXII**  
**SUCCESSORS AND ASSIGNS**

22.1 Assignments and Other Transfers. Buyer may freely assign its rights and obligations to an Affiliate formed under the laws of a state in the United States of America. An "Affiliate" shall mean an entity that is directly or indirectly controlled by Guarantor or Guarantor's permitted assigns, or is directly or indirectly controlled by an entity that directly or

indirectly controls Guarantor or Guarantor's permitted assigns, where control means the right to vote more than fifty percent of the voting interest in the entity.

Buyer and Guarantor may, without consent of the State, collectively assign their rights and obligations under this Agreement to a Person that acquires all or substantially all of the Alaska refining assets of Buyer and Guarantor (the "Assignee"), provided that at least 45 Days before the effective date of the assignment the Assignee provides to the State (a) all of the financial information and warranties Guarantor is required to provide under Article VI and (b) a copy of the form of the assignment, including Assignee's obligation to assume and discharge all of Buyer's and Guarantor's obligations under this Agreement. If, based on the financial information supplied under Article VI, Assignee is required to supply a Letter under Article VII, the Letter in the form and amount required by Article VII must be provided to the State at least 30 Days before the effective date of the assignment. No assignment can be made to an Assignee with long term credit ratings of less than BBB- (Standard and Poor's) or Baa3 (Moody's). From and after the effective date of the Assignment, Buyer and Guarantor shall be relieved of their rights and obligations under this Agreement. No assignment shall be effective until after 45 Days Notice to the State.

Buyer and Guarantor may not otherwise assign their rights or obligations under this Agreement without first obtaining the written consent of the Commissioner, which may not be unreasonably withheld.

22.2 Binding on Successors. This Agreement shall be binding upon and inure to the benefit of the legal representatives, successors, and assigns of the Parties.

**ARTICLE XXIII**  
**RECORDS**

23.1 Inspection of Records. Buyer and Guarantor and the State shall each accord to the other and the other's authorized agents, attorneys, and auditors access during reasonable business hours to any and all property, records, books, documents, or indices related to Buyer's, Guarantor's or the State's performance under this Agreement, and which are under possession or control of the Party from which access is sought, so the other Party may inspect, photograph, and make copies of the property, records, books, documents, or indices except: (1) the State shall not be required to disclose any information, data, or records that it is required by state or federal law or regulation, or by agreement with the Person supplying the record, to be held confidential; (2) the State's access to and treatment of Guarantor's financial records shall be limited by Section 6.3; and (3) no party shall be required to produce documents that are protected by the attorney-client privilege. If information the State obtains from Buyer or Guarantor may be held confidential under state or federal law or regulation, Buyer may request in writing that the State hold the information confidential, and the State shall keep the information confidential to the extent and for the term provided by law.

**ARTICLE XXIV**  
**EMPLOYMENT OF ALASKA RESIDENTS**

24.1 Employment of Alaska Residents. Buyer shall comply with all valid federal, state, and local laws in hiring Alaska residents and companies, and shall not discriminate against Alaska residents and companies. Within the constraints of law, Buyer voluntarily agrees to employ Alaska residents and Alaska companies to the extent they are available, willing, and at least as qualified as other candidates for work performed in Alaska in connection with this Agreement. "Alaska resident" means an individual who is physically present in Alaska with the

intent to remain in the state indefinitely. An individual may demonstrate an intent to remain in the state by maintaining a residence in the state, possessing a resident fishing, trapping or hunting license, or receiving a permanent fund dividend. "Alaska companies" means companies incorporated in Alaska or whose principal place of business is in Alaska. If a court invalidates any portion of this provision, Buyer agrees to employ Alaska residents and Alaska companies to the extent permitted by law.

#### **ARTICLE XXV COUNTERPARTS**

25.1 Counterparts. This Agreement may be executed in multiple counterparts. It is not necessary for the Parties to sign the same counterpart. Each duly executed counterpart shall be deemed to be an original and all executed counterparts taken together shall be considered to be one and the same instrument.

#### **ARTICLE XXVI MISCELLANEOUS**

26.1 Agreement Not to Be Construed Against Any Party as Drafter. The Parties recognize that this Agreement is the product of the joint efforts of the Parties and agree that it shall not be construed against any Party as drafter.

26.2 Entire Agreement. This Agreement constitutes the entire agreement and understanding between the Parties about the subject matter of this transaction and all prior agreements, understandings, and representations, whether oral or written, about this subject matter are merged into and superseded by this written Agreement.

26.3 Headings. The headings throughout this Agreement are for reference purposes only and shall not be construed or considered in interpreting the terms and provisions of this Agreement.

26.4 Authority to Sign. Each Person signing this Agreement warrants that he or she has authority to sign the Agreement.

26.5 Further Assurances. The Parties agree to do such further acts or execute such further documents as may reasonably be required to implement this Agreement.

26.6 Currency. All dollar amounts are U.S. dollars.

**SIGNATURES:**

the State:

THE STATE OF ALASKA

\_\_\_\_\_  
Commissioner  
Department of Natural Resources

Date:

FLINT HILLS RESOURCES ALASKA, LLC

\_\_\_\_\_  
Printed Name:

Title:

Date:

FLINT HILLS RESOURCES, LLC

\_\_\_\_\_  
Printed Name:

Title:

Date:

**APPENDIX 1  
NOMINATION PROCEDURE EXAMPLE  
For Sale Oil Delivered in July 2004**

	PBU IPA & Satellites	Greater Pt McIntyre Area	Total
<b>March 15, 2004</b>			
State receives preliminary barrel per day (bpd) production forecasts from the unit operator 105 days prior to the start of the production month	456,000	63,200	519,200
<b>Not later than March 19, 2004</b>			
RIK purchaser notifies state of monthly bpd nomination (a)			56,362
<b>Not later than March 31, 2004</b>			
State computes RIK percent of Royalty Oil based on Buyer's Sale Oil nomination			
Estimated royalty rates	12.50%	13.34%	
Total state estimated royalty bpd (bpd * royalty rate)	57,000	8,431	65,431
State's RIK nomination percentage (Purchaser RIK bpd/estimated royalty bpd)			86.14%
<b>March 31, 2004</b>			
State notifies unit operator of state's RIK nomination percentage	86.14%	86.14%	86.14%
<b>May 24, 2004</b>			
Unit operator notifies state and working interest owners of updated production forecast			
Production forecast (bpd) for May production month	441,752	62,600	504,352
State calculates RIK bpd			
Royalty rates based on updated estimates (b)	12.50%	13.391158%	
State's RIK nomination percentage	86.14%	86.14%	
RIK bpd (bpd production forecast * Royalty rate * nomination %)	47,566	7,221	54,787
<b>May 31, 2004</b>			
State notifies RIK purchaser of bpd volume available for July production month	47,566	7,221	54,787
<b>August 2, 2004</b>			
State invoices RIK purchaser for July production			
Alaska meter volume for July 1-31, 2003	14,392,425	2,045,163	16,437,588
State's RIK nomination percentage	86.14%	86.14%	86.14%
Royalty rate	12.50%	13.391158%	
Total RIK bbls	1,549,704.36	235,912.49	1,785,616.85
bpd volume (Total RIK/31) (varies from forecast)	49,990.46	7,610.08	57,600.54

**Table notes**

- (a) The state determines from which units to nominate RIK volumes (Section 2.1.5 of the Agreement)  
 (b) The estimated royalty percentage for Greater Pt McIntyre is a composite royalty rate from several fields and will vary with production

**APPENDIX 2:  
EXAMPLE OF CALCULATION OF PRICE OF SALE OIL**

The Price of the Sale Oil delivered by the State to the Buyer each Month for each Unit from which the Sale Oil is nominated is:

$$\text{Price} = \text{ANS Spot Price} - \$1.55 - \text{Tariff Allowance} + \text{Quality Bank Allowance} - \text{Line Loss}$$

**ANS Spot Price**

Table 2-1 illustrates the calculation of the ANS Spot Price for July 2004.

**Table 2-1: Calculation of ANS Spot Price**

Effective Date	Platt's Oilgram Price Report			Telerate On-line Data Reporting Service			Reuters On-line Data Reporting Service		
	ANS Daily Low	ANS Daily High	ANS Daily Midpoint Average	ANS Daily Low	ANS Daily High	ANS Daily Midpoint Average	ANS Daily Low	ANS Daily High	ANS Daily Midpoint Average
07/01/04	\$24.01	\$24.05	\$24.03000	\$24.03	\$24.08	\$24.05500	\$23.81	\$23.98	\$23.89500
07/02/04	\$23.62	\$23.66	\$23.64000	\$23.67	\$23.72	\$23.69500	\$23.50	\$23.67	\$23.58500
07/06/04	\$24.55	\$24.58	\$24.56500	\$24.49	\$24.54	\$24.51500	\$24.19	\$24.36	\$24.27500
07/07/04	\$23.70	\$23.74	\$23.72000	\$23.72	\$23.77	\$23.74500	\$23.61	\$23.78	\$23.69500
07/08/04	\$24.27	\$24.31	\$24.29000	\$24.23	\$24.28	\$24.25500	\$23.61	\$24.37	\$23.99000
07/09/04	\$25.04	\$25.08	\$25.06000	\$24.98	\$25.03	\$25.00500	\$24.20	\$25.07	\$24.63500
07/12/04	\$25.77	\$25.81	\$25.79000	\$25.72	\$25.77	\$25.74500	\$25.61	\$25.78	\$25.69500
07/13/04	\$25.42	\$25.46	\$25.44000	\$25.35	\$25.40	\$25.37500	\$25.30	\$25.47	\$25.38500
07/14/04	\$26.63	\$26.67	\$26.65000	\$26.50	\$26.60	\$26.55000	\$26.47	\$26.64	\$26.55500
07/15/04	\$27.33	\$27.36	\$27.34500	\$27.17	\$27.27	\$27.22000	\$27.17	\$27.34	\$27.25500
07/16/04	\$26.71	\$26.75	\$26.73000	\$26.94	\$27.04	\$26.99000	\$26.53	\$26.70	\$26.61000
07/19/04	\$27.16	\$27.20	\$27.18000	\$27.34	\$27.44	\$27.39000	\$27.03	\$27.20	\$27.11500
07/20/04	\$26.83	\$26.87	\$26.85000	\$27.03	\$27.13	\$27.08000	\$26.80	\$26.97	\$26.88500
07/21/04	\$27.11	\$27.15	\$27.13000	\$27.48	\$27.58	\$27.53000	\$27.25	\$27.42	\$27.33500
07/22/04	\$27.49	\$27.53	\$27.51000	\$27.58	\$27.68	\$27.63000	\$27.33	\$27.78	\$27.55500
07/23/04	\$27.31	\$27.35	\$27.33000	\$27.30	\$27.40	\$27.35000	\$27.01	\$27.26	\$27.13500
07/26/04	\$28.14	\$28.18	\$28.16000	\$27.66	\$27.91	\$27.78500	\$27.56	\$28.01	\$27.78500
07/27/04	\$27.25	\$27.29	\$27.27000	\$27.60	\$27.85	\$27.72500	\$27.20	\$27.37	\$27.28500
07/28/04	\$26.53	\$26.56	\$26.54500	\$26.83	\$27.08	\$26.95500	\$26.42	\$26.59	\$26.50500
07/29/04	\$27.09	\$27.12	\$27.10500	\$27.65	\$27.75	\$27.70000	\$27.66	\$27.83	\$27.74500
07/30/04	\$27.59	\$27.63	\$27.61000	\$28.21	\$28.31	\$28.26000	\$28.17	\$28.34	\$28.25500
	Platt's Monthly Avg =		\$26.18810	Telerate Monthly Avg =		\$26.31214	Reuters Monthly Avg =		\$26.15143

$$\text{ANS Spot Price}_{\text{July 2004}} = \frac{\text{Platt's Monthly Average} + \text{Telerate Monthly Average} + \text{Reuters Monthly Average}}{3} = \$26.21722$$

## Tariff Allowance

The Tariff Allowance (TA) is the sum of (1) the average, weighted by ownership, of the Minimum Interstate TAPS Tariff for each owner in effect on the Day the Sale Oil is tendered by the State to the Buyer; and (2) any tariffs paid by Buyer for shipment of Sale Oil upstream of Pump Station No. 1. Table 2-2, 2-3, and 2-4 illustrate how the state will calculate the TA for each of the Units from which Sale Oil may be offered.

**Table 2-2: Calculation of TAPS Portion of Tariff Allowance**

Ownership-Weighted Average Minimum Interstate TAPS Tariff – July 2004				
Pipeline Company	FERC No.	Percent Pipeline Company Ownership	Minimum Interstate TAPS Tariff (Pump Station No. 1 to Valdez Marine Terminal) by Pipeline Company	TAPS Tariff times Company Ownership Percentage
Phillips Transportation Alaska, Inc.		28.2953%	\$3.32	\$0.93940
ExxonMobil Pipeline Company		20.3378%	\$3.34	\$0.67928
Williams Alaska Pipeline Company		3.0845%	\$3.28	\$0.10117
BP Pipelines (Alaska) Inc.		46.9263%	\$3.28	\$1.53918
Unocal Pipeline Company		1.3561%	\$2.83	\$0.03638
		100.0000%		
Ownership-Weighted Average Minimum Interstate TAPS Tariff				\$3.29741

**Table 2-3: Calculation of Portion of Tariff Allowance Upstream of Pump Station No. 1**

Minimum Tariff on Pipelines Upstream of Pump Station No. 1 – July 2004				
Pipeline Company	FERC No.	RCA Tariff Advice Letter No.	Pipeline	Tariff
Kuparuk Transportation Company			Kuparuk River Unit to TAPS Pump Station No. 1	\$0.20000
Endicott Pipeline Company			Endicott Main Production Island to TAPS Pump Station No. 1	\$0.36000
Kuparuk Transportation Company			Milne Point Pipeline Connection to TAPS Pump Station No. 1	\$0.14400
Milne Point Pipeline Company			Milne Point Central Facilities to Kuparuk Transportation Company Tie-in	\$0.28000
			Total MPU Upstream Tariff Allowance	\$0.42400
Kuparuk Transportation Company			Kuparuk River Unit to TAPS Pump Station No. 1	\$0.20000
Alpine Transportation Company			Colville, Alaska Alpine Field to Kuparuk River Unit	\$0.78000
			Total CRU Upstream Tariff Allowance	\$0.98000
BP Transportation (Alaska) Inc.			Northstar Unit Seal Island to TAPS Pump Station No. 1	\$2.02000

## Table 2-4: Calculation of Tariff Allowance for Each Unit

### Calculation of TA for Prudhoe Bay Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
Upstream Tariff: \$0.00000  
TA<sub>PBU</sub>: \$3.29741

### Calculation of TA for Kuparuk River Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
Kuparuk Transportation Co. Tariff: \$0.20000  
TA<sub>KRU</sub>: \$3.49741

### Calculation of TA for Duck Island Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
Endicott Pipeline Co. Tariff: \$0.36000  
TA<sub>DIU</sub>: \$3.65741

### Calculation of TA for Milne Point Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
Kuparuk Transportation Co. Tariff: \$0.14400<sup>1</sup>  
Milne Point Pipeline Co. Tariff: \$0.28000  
TA<sub>MPCU</sub>: \$3.72141

### Calculation of TA for Colville River Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
Kuparuk Transportation Co. Tariff: \$0.20000  
Alpine Transportation Company Tariff: \$0.78000  
TA<sub>CRU</sub>: \$4.27741

### Calculation of TA for Northstar Unit

Ownership-Weighted Average Minimum Interstate TAPS Tariff: \$3.29741  
BP Transportation (Alaska) Inc. Tariff: \$2.02000  
TA<sub>NU</sub>: \$5.31741

<sup>1</sup>Kuparuk Pipeline/Milne Point Pipeline connection to TAPS Pump Station No. 1

## Quality Bank Adjustment (QBA)

The TAPS Quality Bank compensates shippers of a high-value crude oil stream when a lower-value crude oil stream is blended in the common stream.<sup>1</sup> To calculate the Price of the Sale Oil at the Point of Delivery an adjustment must be made for the impact that the sale oil will have on the value of the commingled crude oil stream when it enters the TAPS Valdez terminal.

<sup>1</sup> Mitchell & Mitchell, 8300 Douglas Avenue, #800, Dallas, TX 75225, administers the TAPS Quality Bank. Anyone who ships oil on TAPS must make prior arrangements with Mitchell & Mitchell to participate in the TAPS Quality Bank.

The QBA is a per-barrel value, either positive or negative, and will be calculated each Month by the State for Sale Oil from each Unit. The State will estimate a QBA for each applicable Unit for the initial billing. Typically, the State receives the data to calculate the actual QBA for the Month about two Months after the Month the Sale Oil is delivered. For this reason the QBA will be subject to a routine true-up in a subsequent adjustment.

**Table 2-5: Hypothetical TAPS Quality Bank Data**

TAPS Quality Bank Stream Values and Total Stream Volume Shipped July 2004				
Sample Location	Stream	Volume (BBL)	Stream Value (\$/BBL)	Total Stream Value (\$)
PBU IPA	PBU IPA	19,000,000	\$27.9380000000	\$530,822,000.00
LISBURNE	LISBURNE	3,500,000	\$27.5372400000	\$96,380,340.00
ENDICOTT	ENDICOTT	1,250,000	\$27.2598000000	\$34,074,750.00
KUPARUK	KUPARUK	12,000,000	\$27.4418300000	\$329,301,960.00
NORTHSTAR	NORTHSTAR	2,000,000	\$28.0000000000	\$56,000,000.00
PS #1	PS #1 REFERENCE	37,750,000	\$27.7239483444	\$1,046,579,050.00
GVEA OFFTAKE	GVEA PASSING	28,000,000	\$27.6546500000	\$774,330,200.00
GVEA RETURN	GVEA RETURN	3,500,000	\$26.6753800000	\$93,363,830.00
GVEA	GVEA REFERENCE	31,500,000	\$27.5458422222	\$867,694,030.00
PSVR OFFTAKE	PSVR PASSING	30,000,000	\$27.5517600000	\$826,552,800.00
PSVR RETURN	PSVR RETURN	1,000,000	\$26.8450200000	\$26,845,020.00
PSVR	PSVR REFERENCE	31,000,000	\$27.5289619355	\$853,397,820.00

EPC Quality Bank Stream Values and Total Stream Volume Shipped July 2004				
Sample Location	Stream	Volume (BBL)	Stream Value (\$/BBL)	Total Stream Value (\$)
BADAMI	BADAMI	80,000	\$27.4526400000	\$2,196,211.20
ENDICOTT REFERENCE	ENDICOTT REFERENCE	1,250,000	\$27.2598000000	\$34,074,750.00
ENDICOTT MAIN PROD	ENDICOTT MAIN PROD	1,170,000	\$27.2466143590	\$31,878,538.80

KTC Quality Bank Stream Values and Total Stream Volume Shipped July 2004				
Sample Location	Stream	Volume (BBL)	Stream Value (\$/BBL)	Total Stream Value (\$)
ALPINE	ALPINE	3,000,000	\$27.8000000000	\$83,400,000.00
MILNE POINT	MILNE POINT	1,500,000	\$27.1352300000	\$40,702,845.00
KUPARUK REFERENCE	KUPARUK REFERENCE	12,000,000	\$27.4418300000	\$329,301,960.00
KUPARUK RIVER UNIT	KUPARUK RIVER UNIT	7,500,000	\$27.3598820000	\$205,199,115.00

Table 2-5 shows the kind of information supplied by the TAPS quality bank administrator that will be used to calculate the quality bank differential for Sale Oil produced from each Unit. The TAPS quality bank administrator provides this information to the State, pipeline owners, and shippers. As a shipper on TAPS, the Buyer will also receive this information. In the column titled "Stream Value (\$/BBL)" are the different per-barrel values of each stream produced from the Units from which Sale Oil may be delivered. The PSVR Reference Stream value is labeled

“PSVR Reference” and is the stream value of the blended TAPS stream immediately downstream of the Petro Star Valdez Refinery return stream. The Quality Bank Adjustment is calculated as the difference between the stream value of each Unit and the PSVR Reference Stream.

For example, assume that the Month is July 2004 and the Sale Oil is produced from the Duck Island Unit. The QBA for Sale Oil from the Duck Island Unit ( $QBA_{DIU}$ ) is calculated as the per-barrel difference between the Stream value for the Duck Island Unit, indicated as the “Endicott Main Prod” in Table 2.5, and the PSVR Reference Stream Value. In this example Sale Oil from the Duck Island Unit lowers the value of the stream of oil measured at Valdez. Therefore, \$0.2823475765 per barrel is the QBA incorporated in the calculation of Price for Sale Oil from the Duck Island Unit.

Quality Bank Adjustment for the Duck Island Unit = the stream value for Endicott Main Production minus the stream value of PSVR Reference (from Table 2-5)

$$QBA_{DIU} = 27.2466143590 - 27.5289619355$$

$$QBA_{DIU} = -\$0.28235$$

Note: The Price of Sale Oil from the PBU IPA and Lisburne are invoiced separately.

#### Line Loss

Using the results of the example calculations above, Line Loss for Sale Oil delivered from the Duck Island Unit in July 2004 equals

$$\text{Line Loss}_{DIU} = (.0009) \times (\$26.21722 - \$1.55000 - \$3.65741 + -\$0.28235) = \$0.01865.$$

#### Calculating the Price of Sale Oil

The Price of Sale Oil delivered from the Duck Island Unit in July 2004 is

$$\text{Price}_{DIU} = \$26.21722 - \$1.55000 - \$3.65741 + -\$0.28235 - \$0.01865 = \$20.70881$$

Note that the each number in the equation is rounded to five decimal places. If a number's sixth decimal is 0, 1, 2, 3, or 4, the number shall be truncated to the fifth decimal. If a number's sixth decimal is 5, 6, 7, 8, or 9, the number shall be truncated to the fifth decimal and the fifth decimal shall be increased by 1.

**APPENDIX 3**  
**EXAMPLE OF CALCULATION OF INTEREST AND LATE PAYMENT PENALTIES**

**Sample Calculation of an Invoice for July 2004 Deliveries**

Assumptions:

1. Month is August 2004.
2. Sale Oil delivered to the Buyer from the Duck Island Unit in July 2004 = 2,170,000 barrels (70,000 bpd).
3. July 2004 Price of the Sale Oil for the Duck Island Unit as initially estimated by the State = \$21.00000 per barrel.
4. Statement of account, with July 2004 invoice, sent to the Buyer on August 3, 2004.
5. July 2004 invoice payment due to the State = August 20, 2004.
6. Buyer pays State only \$10,000,000 on the due date, August 20, and pays the outstanding balance on August 25, 2004.
7. Annual interest rate provided by Alaska Statute 38.05.135(d) for August 2004 is 11 percent.

Method for calculating Buyer's invoice payment for July 2004 deliveries:

$$\begin{aligned} \text{Invoice Amount} &= \text{Quantity of Sale Oil} \times \text{Buyer's Price of Sale Oil} \\ &= 2,170,000 \times \$21.00000 = \$45,570,000.00 \end{aligned}$$

Because payment in full was not received by the State on or before August 20, 2004, interest will accrue on the unpaid balance from August 20, 2004 through the date the payment is received, and a late payment penalty will be assessed.

Below is a sample calculation of late payment penalty fee (assuming that it is not waived under Section 3.7) and interest. This sample calculation shows what will happen if the Buyer makes a partial payment on August 20 and the balance on August 25.

Late Payment Penalty Fee:

Statement of Account amount	=	\$45,570,000.00
Amount paid on August 20	=	<u>10,000,000.00</u>
Outstanding balance (8/20/04)	=	\$35,570,000.00
Late Payment Penalty Fee (\$35,570,000 x 5%) =	=	\$1,778,500.00

Interest:

\$35,570,000 x (11%/366) x 5 Days	=	<u>\$53,452.19</u>
Amount Buyer owes on August 20, 2004	=	\$37,401,952.19

Note: As more accurate data is received by the State, the State may adjust the Price and/or the actual quantity of Sale Oil and invoice the Buyer in the initial adjustment invoice submitted with the following Month's (August 2004) statement of account.

### Sample Calculation of an Adjustment Invoice in September 2004

#### Assumptions:

1. Month is September 2004.
2. Sale Oil delivered in July 2004 has been revised to 2,169,0000 barrels.
3. July 2004's price for Sale Oil is unchanged at \$21.00000 per barrel.
4. Date of the statement of account that contains the adjustment invoice is September 2, 2004.
5. Date the adjustment invoice payment is due to the State = September 20, 2004.

#### Method for calculating the Buyer's adjustment invoice amount for July 2004:

$$\begin{aligned}\text{Invoice Amount} &= \text{Quantity of Sale Oil} \times \text{Buyer's Price of Sale Oil} \\ &= 2,169,000 \times \$21.00000 \\ &= \$45,549,000.00\end{aligned}$$

Adjusted Invoice Amount for July 2004	= \$45,549,000.00
Amount previously paid by the Buyer for July 2004	= <u>\$45,570,000.00</u>
Overpayment for July 2004	= (\$21,000.00)

Credit due the Buyer against statement of account amount dated September 2 due September 20, 2004.

Note: As more accurate data is received by the State, the State may adjust the Price and/or the actual quantity of Sale Oil and invoice the Buyer in the adjustment invoice submitted with the following Month's (October 2004) statement of account.

### Sample Calculation of an Adjustment Invoice in October 2004

#### Assumptions:

1. Month is October 2004.
2. July 2004's price for Sale Oil is changed to \$21.05000 per barrel due to a change in the quality bank.
3. The statement of account that contains the adjustment invoice is October 1, 2004.
4. The adjusted invoice payment is due to the State = October 20, 2004.

#### Method for calculating the Buyer's adjustment invoice amount for July 2004:

$$\begin{aligned}\text{Production Month Invoice Amount} &= \text{Quantity of Sale Oil} \times \text{Buyer's Price of Sale Oil} \\ &= 2,169,000 \times \$21.05000 \\ &= \$45,657,450.00\end{aligned}$$

#### APPENDIX 4 SPECIAL COMMITMENTS

Buyer agrees to the following list of Special Commitments:

**A. Clean Fuels Processing.** After performing an engineering study, Buyer will install necessary equipment and complete such modifications to its North Pole Refinery or will participate in the modification of other refinery facilities in Alaska as required to produce gasoline and on-road, off-road, marine, and rail diesel fuels that meet or exceed all EPA low sulfur fuel requirements ("Clean Fuels"). Buyer will make commercially reasonable efforts to complete necessary installations and modifications on or before the effective dates of the Clean Fuels requirements of the EPA regulations.

Total project costs are expected to exceed \$100,000,000.00 and will likely include the construction of processing units, including hydrotreating, a hydrogen plant and sulfur removal equipment. These projects will result in a significant reduction in gasoline and diesel sulfur levels.

**B. Anchorage Tank Farm Evaluation.** Buyer agrees to discharge the commitments previously made by Williams in the "Memorandum of Agreement between Williams Alaska Petroleum, Inc. and The Government Hill Community Council" attached as Appendix 6 to this agreement. The key requirements are as follows:

- Removal of three (3) tanks from east of the Ocean Dock Road with a total capacity of over 5,500 barrels
- Refrain from installing additional tanks east of the Ocean Dock Road
- Evaluation of all remaining tanks east of the Ocean Dock Road to determine whether they comply with all State and Federal requirements viz. overfill protection, fire protection, tank seal monitoring, potential for change of product service, and possible removal of additional tanks, and prompt remediation of any violations of these requirements.
- Installation of new tanks west of the Ocean Dock Road will occur provided that existing tanks on the east side of Ocean Dock Road are retired and removed on a tank-for-tank basis.
- FHR agrees to continue cooperative efforts in connection with the ongoing Bulk Fuel Hazard Study currently underway through the Municipality of Anchorage.

**C. Shipment by Rail.** Williams currently ships refined products by rail under an Agreement with Alaska Railroad Corporation (an Agreement originally entered by MAPCO Alaska Petroleum Inc. in May of 1993). As part of Buyer's refinery acquisition from Williams, Buyer will assume the rights and obligations of Williams under the rail agreement and continue to ship refined products to Anchorage.

**D. Air Traffic Marketing and Structural Improvement Study.** Buyer and the State shall jointly explore commercially reasonable options for increasing passenger and cargo air traffic through the Fairbanks International Airport. Buyer shall work with the Fairbanks International Airport to concentrate on promoting the Fairbanks International Airport to cargo carriers operating between Asia and Europe and otherwise; shall evaluate, and possibly upgrade, the airport's fuel distribution facilities, including the feasibility of using or

# CORRECTION

THE FOLLOWING DOCUMENT(S)  
HAVE BEEN REFILMED TO  
ASSURE LEGIBILITY OR PAGINATION



Central Microfilm Services  
Department of Education & Early Development  
State of Alaska

### Sample Calculation of an Adjustment Invoice in September 2004

Assumptions:

1. Month is September 2004.
2. Sale Oil delivered in July 2004 has been revised to 2,169,0000 barrels.
3. July 2004's price for Sale Oil is unchanged at \$21.00000 per barrel.
4. Date of the statement of account that contains the adjustment invoice is September 2, 2004.
5. Date the adjustment invoice payment is due to the State = September 20, 2004.

Method for calculating the Buyer's adjustment invoice amount for July 2004:

$$\begin{aligned} \text{Invoice Amount} &= \text{Quantity of Sale Oil} \times \text{Buyer's Price of Sale Oil} \\ &= 2,169,000 \times \$21.00000 \\ &= \$45,549,000.00 \end{aligned}$$

Adjusted Invoice Amount for July 2004	= \$45,549,000.00
Amount previously paid by the Buyer for July 2004	= <u>\$45,570,000.00</u>
Overpayment for July 2004	= (\$21,000.00)

Credit due the Buyer against statement of account amount dated September 2 due September 20, 2004.

Note: As more accurate data is received by the State, the State may adjust the Price and/or the actual quantity of Sale Oil and invoice the Buyer in the adjustment invoice submitted with the following Month's (October 2004) statement of account.

### Sample Calculation of an Adjustment Invoice in October 2004

Assumptions:

1. Month is October 2004.
2. July 2004's price for Sale Oil is changed to \$21.05000 per barrel due to a change in the quality bank.
3. The statement of account that contains the adjustment invoice is October 1, 2004.
4. The adjusted invoice payment is due to the State = October 20, 2004.

Method for calculating the Buyer's adjustment invoice amount for July 2004:

$$\begin{aligned} \text{Production Month Invoice Amount} &= \text{Quantity of Sale Oil} \times \text{Buyer's Price of Sale Oil} \\ &= 2,169,000 \times \$21.05000 \\ &= \$45,657,450.00 \end{aligned}$$

Adjusted Invoice Amount for July 2004	= \$45,657,450.00
Amount previously paid by the Buyer for July 2004	= <u>\$45,549,000.00</u>
Underpayment for July 2004	= \$108,450.00

The underpayment is due the State on October 20, 2004

upgrading the hydrant fueling system; and shall charge a jet fuel customer in Fairbanks the same or a lower price as Buyer charges that same customer in Anchorage.

**E. Wholesale Rack Price Parity.** Buyer agrees, for the term of the Agreement, to maintain the Buyer wholesale truck rack posted price for gasoline in Fairbanks at a price not to exceed the Buyer wholesale truck rack posted price for gasoline in Anchorage on an annual simple average basis (within a tolerance/variation of 1 cent per gallon (cpg)). Buyer makes no guarantee of the price parity for Buyer's wholesale truck rack posted prices for gasoline in Fairbanks and Anchorage on a daily basis. If the annual average variation of the aforementioned posted prices exceeds 1 cpg, Buyer shall have ninety (90) days to reduce the variation below 1 cpg, averaged over an all-inclusive timeframe, including the ninety (90) day period and the previous annual period. This provision shall not apply to any gasoline exchanges. An example of the calculations appears in Table 4-1.

**Table 4-1 Wholesale Truck Rack Posted Price True-Up**

Wholesale Rack Price Parity	Scenario 1			Scenario 2		
	Buyer Fairbanks Posting (cpg)	Buyer Anchorage Posting (cpg)	Fairbanks minus Anchorage (cpg)	Buyer Fairbanks Posting (cpg)	Buyer Anchorage Posting (cpg)	Fairbanks minus Anchorage (cpg)
January	104.00	102.44	1.56	106.00	102.44	3.56
February	103.00	100.76	2.25	103.00	100.76	2.25
March	100.00	103.01	(3.01)	105.00	103.01	1.99
April	108.00	110.02	(2.02)	112.00	110.02	1.98
May	112.00	110.07	1.93	112.00	110.07	1.93
June	111.00	109.40	1.60	111.00	109.40	1.60
July	106.00	108.38	(2.38)	108.00	108.38	(0.38)
August	107.00	109.77	(2.77)	109.00	109.77	(0.77)
September	112.00	114.02	(2.02)	115.00	114.02	0.98
October	115.00	114.02	0.98	115.00	114.02	0.98
November	115.00	113.38	1.62	113.00	113.38	(0.38)
December	112.00	113.70	(1.70)	113.00	113.70	(0.70)
Annual Average	108.75	109.08	(0.33)	110.17	109.08	1.09
January	Not Applicable			119.00	119.95	(0.95)
February				125.00	126.19	(1.19)
March				133.00	134.13	(1.13)
15 Month Average				113.27	112.61	0.65

## APPENDIX 4 SPECIAL COMMITMENTS

Buyer agrees to the following list of Special Commitments:

**A. Clean Fuels Processing.** After performing an engineering study, Buyer will install necessary equipment and complete such modifications to its North Pole Refinery or will participate in the modification of other refinery facilities in Alaska as required to produce gasoline and on-road, off-road, marine, and rail diesel fuels that meet or exceed all EPA low sulfur fuel requirements ("Clean Fuels"). Buyer will make commercially reasonable efforts to complete necessary installations and modifications on or before the effective dates of the Clean Fuels requirements of the EPA regulations.

Total project costs are expected to exceed \$100,000,000.00 and will likely include the construction of processing units, including hydrotreating, a hydrogen plant and sulfur removal equipment. These projects will result in a significant reduction in gasoline and diesel sulfur levels.

**B. Anchorage Tank Farm Evaluation.** Buyer agrees to discharge the commitments previously made by Williams in the "Memorandum of Agreement between Williams Alaska Petroleum, Inc. and The Government Hill Community Council" attached as Appendix 6 to this agreement. The key requirements are as follows:

- Removal of three (3) tanks from east of the Ocean Dock Road with a total capacity of over 5,500 barrels
- Refrain from installing additional tanks east of the Ocean Dock Road
- Evaluation of all remaining tanks east of the Ocean Dock Road to determine whether they comply with all State and Federal requirements viz. overfill protection, fire protection, tank seal monitoring, potential for change of product service, and possible removal of additional tanks, and prompt remediation of any violations of these requirements.
- Installation of new tanks west of the Ocean Dock Road will occur provided that existing tanks on the east side of Ocean Dock Road are retired and removed on a tank-for-tank basis.
- FHR agrees to continue cooperative efforts in connection with the ongoing Bulk Fuel Hazard Study currently underway through the Municipality of Anchorage.

**C. Shipment by Rail.** Williams currently ships refined products by rail under an Agreement with Alaska Railroad Corporation (an Agreement originally entered by MAPCO Alaska Petroleum Inc. in May of 1993). As part of Buyer's refinery acquisition from Williams, Buyer will assume the rights and obligations of Williams under the rail agreement and continue to ship refined products to Anchorage.

**D. Air Traffic Marketing and Structural Improvement Study.** Buyer and the State shall jointly explore commercially reasonable options for increasing passenger and cargo air traffic through the Fairbanks International Airport. Buyer shall work with the Fairbanks International Airport to concentrate on promoting the Fairbanks International Airport to cargo carriers operating between Asia and Europe and otherwise; shall evaluate, and possibly upgrade, the airport's fuel distribution facilities, including the feasibility of using or

**APPENDIX 5  
PROCEDURE FOR ADJUSTING THE FORMULA  
FOR CALCULATIONS OF PRICE**

- Step 1:** Calculate the volume-weighted average cost of marine transportation reported on the royalty returns of BP, ExxonMobil, and CPAI for the production Months January 2006 through December 2008. Adjustments through March 31, 2009 shall be used in the calculation. For example, the royalty returns for December 2008 productions are due in January 2009. The marine transportation cost reported in January can be adjusted through March 31, 2009, but not later. The amount calculated is defined as "RIV Marine Cost."
- Step 2:** Subtract from the RIV Marine Cost the amount \$0.30. The answer shall be substituted for the \$1.55 used in the calculation of the Price (as defined in Section 2.3) subject to the following limitations:
1. if the answer is less than \$1.45, substitute \$1.45 for the \$1.55 used in the calculation of the Price;
  2. if the answer is greater than \$1.65, substitute \$1.65 for the \$1.55 used in the calculation of the Price.
- Step 3:** For Sale Oil deliveries beginning April 1, 2009, the \$1.55 that had been used in the calculation of the Price shall be replaced with the number determined in Step 2, above. That number used in the calculation of the Price shall remain in effect through the end of the term of the Agreement.

**APPENDIX 6  
MEMORANDUM OF AGREEMENT  
BETWEEN  
WILLIAMS ALASKA PETROLEUM, INC.  
AND  
THE GOVERNMENT HILL COMMUNITY COUNCIL**

**MEMORANDUM OF AGREEMENT**

between

**Williams Alaska Petroleum, Inc.,**

and

**the Government Hill Community Council,**

**an unincorporated association**

WHEREAS, Williams operates bulk fuel storage and distribution facilities including storage tanks, loading racks, and related industrial structures in the vicinity of Government Hill and the Port of Anchorage and wishes to build a double track rail loop (the Loop Track Project) on its property and on certain islands it will acquire from the Alaska Railroad; and;

WHEREAS, construction of the Loop Track project will reduce traffic congestion in the Port area, allow for more efficient transfer of fuel from rail cars to storage and transmission facilities and enable Williams to build additional storage tanks west of Ocean Dock Road should the need arise in the future, and

WHEREAS, the Government Hill Community Council (the Council) desires to allow Williams to proceed with the orderly development of its Loop Track project while also reducing risks associated with the continued presence of fuel storage facilities near Government Hill,

NOW THEREFORE, THE PARTIES AGREE AS FOLLOWS:

1. **Non Opposition to Loop Track project** The Council and its officers agree not to oppose the Loop Track project proposed by Williams and will not, officially or unofficially continue efforts to convince public and private entities to take a position or other action adverse to construction of the Loop Track project. The Council will also take reasonable efforts to inform the residents of Government Hill of this agreement and its official position on the Loop Track project.

2. **Letters stating the Official Position of the Council on the Loop Track project** Upon execution of this Agreement, the Council president shall sign several letters setting forth the official position of the Council on the Loop Track project. The letters shall be substantially

in the same form as those contained in Exhibit B and may be presented by Williams to any public or private entity in connection with the Loop Track project as Williams determines. The letters include:

1. A letter from the Council's executive committee recommending the Council withdraw its support for Resolution AR 2001-146 now before the Anchorage Assembly and that the Council request the Resolution be withdrawn from the Assembly agenda. The parties have been advised that upon approval of this Agreement, the sponsor of that Resolution will request that the Assembly table that resolution indefinitely.
2. A letter to the Anchorage Assembly supporting the Alaska Railroad's efforts to lease back the small portion of tidelands from the Municipality required to complete the Loop Track Project.
3. A letter supporting Williams' efforts to build the Loop Track project throughout the permitting and construction process. Specifically, the Council will advise the Division of Governmental Coordination that it has withdrawn its opposition to the Loop Track project. The Council will also send a letter to the Corps of Engineers stating it has withdrawn its opposition to Williams's Fill Permit application currently under review by the Corps and withdrawing the Council's request for a public hearing.
4. A letter to the municipality stating the Council's non-objection to the extraction and use of the railroad's gravel deposit on the Hollywood Vista for the Loop Track project consistent with this agreement.
5. A letter supporting Williams's efforts to build future tanks on the west side of Ocean Dock road consistent with this agreement.

3. Construction of New Tanks East of Ocean Dock Road Williams agrees not to construct any new fuel storage tanks on property it owns or leases which is located east of Ocean Dock Road.

4. **Construction of New Tanks West of Ocean Dock Road** The Council agrees that Williams may build new fuel storage tanks on property it owns or leases west of Ocean Dock Road provided that existing tanks on the east side of Ocean Dock Road are retired and removed on a tank-for-tank basis, after the conditions specified in Section 5 below are met.

5. **Removal of Three Existing Tanks East of Ocean Dock Road** If the Loop Track project is constructed, Williams agrees that the tanks shown on the site plan attached as Exhibit A will be removed at its own expense no later than the dates specified below:

Tank # 3296	Built 1950	December 31, 2002
Tank # 3578	Built 1950	December 31, 2003
Tank # 3577	Built 1950	December 31, 2004

After removing those three tanks, the parties agree that Williams will have banked a "credit" to build one tank on the west side of Ocean Dock Road, without the requirement to remove an additional tank as defined under the provision of Section 4 above.

6. **Mineral Resource (gravel) extraction operations** To build the Loop Track project Williams may acquire gravel from a pit owned by the Alaska Railroad in the vicinity of the former Hollywood Vista apartments. The Municipality of Anchorage has provisionally taken the position that a conditional use permit granted by the Planning and Zoning Commission on 2/05/96 for gravel extraction in that area remains in effect until 12/31/01. If Williams acquires gravel from that area for its project, Williams will comply with applicable terms and conditions of that conditional use permit and will complete gravel extraction for the Loop Track project from the Railroad Property by no later than 12/31/01 unless extended by mutual consent of the parties. Subject to this agreement, the Council does not object to gravel extraction from the railroad site necessary for construction of the Loop Track project.

#### 7. **Port of Anchorage Bulk Fuel Hazard Study**

1. The parties agree to continue cooperative efforts in connection with the ongoing Bulk Fuel Hazard Study currently underway through the Municipality of Anchorage. Williams agrees to ensure that the study includes an assessment of alternatives for reducing the

likelihood and/or consequence of risks associated with the presence of bulk fuel storage facilities in the Government Hill Area. Mitigative alternatives to be considered will include development of a buffer zone between fuel storage facilities and residential areas.

2. Upon completion of the Bulk Fuel Hazard Study, the parties will work cooperatively in obtaining public approval(s) of municipal and state legislation, including bond propositions to fund implementation of the Study.

8. **Compliance with all laws** Nothing in this agreement shall excuse Williams from its continuing obligation to comply with all local ordinances and regulations, together with all state and federal laws and administrative regulations that apply to the Loop Track project.

9. **Integration.**

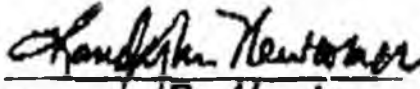
- A. This Memorandum and its attached exhibits contain the entire agreement of the parties. There are no other promises, terms, conditions, or representations binding on any party to this agreement which are not expressed herein.
2. The following are incorporated into this agreement by reference:

Exhibit A: Site Plan


Exhibit B: Letters stating Council's position on Loop Track project

DATED THIS 2<sup>d</sup> DAY OF JUNE, 2001 AT ANCHORAGE, ALASKA

Williams Alaska Petroleum Co. Inc.

  
\_\_\_\_\_  
its President

The Government Hill Community  
Council

  
\_\_\_\_\_  
its President



Dear Mr. Newcomer,

This letter conveys the Government Hill Community Council's position of support for the construction of new bulk fuel storage tanks by Williams Alaska Petroleum, Inc., on lands west of Ocean Dock Road, subject to the terms of an agreement between the Council and Williams concerning the removal of tanks from the east side of Ocean Dock Road. This letter is directed to the attention of anyone it may concern.

Government Hill Community Council has for many years advocated for the creation of a safety buffer area to separate bulk fuel storage tanks from residences and other sensitive land uses in our area. In May, 2001, the Council and Williams negotiated an agreement to begin implementation of a buffer zone at Williams' fuel terminal along Ocean Dock Road. Under this agreement, Williams committed to removal of three tanks from the east side of Ocean Dock Road in 2002, 2003, and 2004, and to future removal of additional tanks from the east side of Ocean Dock Road whenever new tanks are built west of Ocean Dock Road, according to a formula that was arrived at mutually by the parties.

In consideration for Williams' agreement to removal of these tanks and staged creation of the safety buffer area, Government Hill Community Council supports construction of the new tanks west of Ocean Dock Road required to continue and expand Williams' operations. The council commits to continued support of new tank construction so long as such new tanks contribute to the establishment of the safety buffer as explained in the agreement.

Thank you for your continued communication with the council and your participation in our joint negotiations and agreement.

Sincerely,

*GC*  
C.  
Stuart Hall  
President,  
Government Hill Community Council

" B "

Dear Mr. Newcomer

Pursuant to the agreement between Williams Alaska Petroleum Inc. and the Government Hill Community Council, this letter states, for anyone it may concern, the council's official position of non-objection to extraction of gravel from Alaska Railroad Corp. land adjacent to the Hollywood Vista property on Government Hill for the purpose of construction of your Loop Rail Project, subject to the understandings contained herein.

The council is of the understanding that the Municipality of Anchorage has provisionally taken the position that a conditional use permit granted by the Planning and Zoning Commission on February 4, 1996, remains in effect until December 31, 2001, for gravel extraction from certain Alaska Railroad Corp. land near Government Hill. Subject to compliance with the provisions of that permit, the Council does not object to removal of gravel from that site for the Loop Rail Project prior to the last day of 2001.

This letter and the Council's position of non-objection is offered to Williams in consideration for Williams' agreement to remove three bulk fuel storage tanks from near the Government Hill neighborhood and for the further future removal of other tanks as new tanks are built west of Ocean Dock Road. This letter does not apply to other lands than those covered in the February 4, 1996, conditional use permit, nor to any project Williams or the Alaska Railroad may contemplate subsequent to the end of 2001.

Thank you for your continued communication with the council and participation in our negotiation process and agreement.

Sincerely,

 Stuart Hall  
President,  
Government Hill Community Council



**GOVERNMENT HILL COMMUNITY COUNCIL**

Post Office Box 100018 · Anchorage, Alaska 99510-0018

Wednesday, 30 May 2001

Honorable Dick Traini, Chair  
Anchorage Municipal Assembly  
P.O. Box 196650  
Anchorage, Alaska 99519-6650

RE: Lease-back, Tidelands, Port of Anchorage (ARRC/Williams  
Petroleum, Inc.)

Dear Mr. Chairman and Members of the Assembly:

In light of recent negotiations between Williams Petroleum, Inc, members of the Assembly and representatives of the Government Hill Community Council, the Executive Committee of the Council convened this date agrees to support the efforts of the Alaska Railroad Corporation to lease back a small portion of tidelands in the Port of Anchorage from the Municipality of Anchorage to permit completion of a loop track railroad project by Williams Petroleum, Inc.

Very truly yours,

STUART C. HALL, President



## GOVERNMENT HILL COMMUNITY COUNCIL

Post Office Box 100018 · Anchorage, Alaska 99510-0018

Wednesday, 30 May 2001

District Engineer  
U.S. Army Corps of Engineers, Alaska District  
Post Office Box 898  
Anchorage, Alaska 99506-0898

Att'n: David C. Casey, Regulatory Branch

RE: M-920000, Knik Arm 119/Williams Petroleum, Inc.

Dear Mr. Casey:

In light of recent negotiations between Williams Petroleum, Inc., members of the Anchorage Municipal Assembly and representatives of the Government Hill Community Council, the Executive Committee of the Council convened this date withdraws its opposition to the application of Williams Petroleum, Inc., for a fill permit and withdraws the Council's request for a public hearing on this application.

Very truly yours,

STUART C. HALL, President

# Flint Hills Response to DNR MEMO.

## What will SB 314 do?

- SB 314 proposes the enactment of a statutory prohibition on "retroactive price adjustment" terms in existing and future RIK contracts. It will cause an amendment of the price term in the existing RIK contract between the State and Flint Hills Resources.

## How will FHR's RIK Contract Change?

- FHR's Price Term is defined in Article 2.3 as:

ANS Spot Price - \$1.55 - Tariff Allowance + Quality Bank Adjustment - Line Loss.

- The contract defines the "Tariff Allowance" as:

"Tariff Allowance" means the sum of (1) the average, weighted by ownership, of the Minimum Interstate TAPS Tariff (Pump Station No. 1 to Valdez Marine Terminal) for each owner in effect on the Day the Sale Oil is tendered by the State to Buyer; and (2) any tariffs paid by Buyer for shipment of Sale Oil upstream of Pump Station No. 1. "Minimum Interstate TAPS Tariff" means the effective TAPS tariff on file with the Federal Energy Regulatory Commission ("FERC") for each carrier on a given Day, excluding incentive tariffs."

- On February 13, 2005, FHR asked DNR to amend the retroactive requirement. SB 314 would require that such an amendment be adopted by the commissioner.

~~"If a tariff which has been used in the calculation of a Tariff Allowance is changed or subject to a refund order by the FERC, the Tariff Allowance will be recalculated using the changed FERC ordered tariff, the Sale Oil Price will be adjusted accordingly, and the resulting refund to the State (or credit to Buyer) will be made in accordance with Article III. The changed FERC ordered tariff shall be used in the calculation of the price of Sale Oil delivered to Buyer on and after the date of the FERC order, but not before. If a FERC-ordered tariff is suspended or enjoined from implementation, the Tariff Allowance shall not be recalculated until the suspension or injunction is lifted and the FERC order is implemented and goes into effect."~~  
[Deletions are indicated in strikeout; additions are underlined.]

- *This is terribly misleading. FHR began this conversation March 2005 by proposing several alternative solutions to the issue. The DNR did not respond to any of those.*
- The retroactive provision in the FHR contract was agreed to at the expense of other considerations for the State. The retroactive provision is just one part of a larger deal in which the state agreed to the \$1.55 per barrel discount on ANS spot price, provided

FHR with an option to reduce volumes purchased, added a built in automatic reopener to lower FHR's price after five years.

- *"The retroactive provision in the FHR contract was agreed to at the expense of other considerations..."*
  - *What are these other expenses? The FHR crude contract results in a premium of about \$0.30/bbl to the State's alternative royalty-in-value (RIV) contracts.*
  - *The \$1.55 "discount on ANS" is in reality recognition of the marine cost to ship ANS to the W. Coast. Marine costs are also included in the State's RIV contracts.*
  - *The retroactive language was vigorously challenged by FHR during the crude contract negotiations and only accepted by FHR because FHR understood that the State, being a signatory to the TAPS Settlement Methodology (TSM) was bound by a joint defense agreement in that settlement to defend the TAPS tariff. Understanding the State had agreed to defend TSM reassured FHR that TSM tariffs would be in-place at least until 2009. Ultimately, FHR agreed to the retroactive language because the State insisted it was required to match the retroactivity provisions of its RIV contracts in this Royalty-in-Kind (RIK) contract and with the understanding that a retroactive reduction in tariff was remote given the State's commitment to TSM.*
- *"... added a built in automatic re-opener to lower FHR's price after five years."*
  - *This is inaccurate. The re-opener was at the request of the State and FHR did not want to accept the re-opener preferring the certainty of fixed pricing relationships.*

#### How does FHR's retroactive obligation arise?

- When FHR and the state negotiated the RIK contract in 2004, both were well aware that the Regulatory Commission of Alaska had two years before determined that the methodology used to calculate the TAPS intrastate tariff exceeded the "just and reasonable" rate standard required by law. (The RCA's decision has been affirmed in Alaska superior court.) The state and FHR agreed that, should the interstate TAPS tariff be changed by a ruling of the FERC so that refunds to shippers would be required, then FHR would pay the state the difference between the temporary and the new permanent tariffs. (Similarly, if the permanent FERC tariff were higher, the contract requires that the state will refund the difference to FHR.)
- *Since the State is a signatory to the TSM, it apparently agreed that TSM is "just and reasonable". In its decision to accept retroactivity in the crude contract, FHR placed a great deal of importance on the state's commitment to TSM and the joint defense provisions the State committed to in signing that settlement.*
- An independent (i.e., non-TAPS owner) ANS oil producer challenged the 2005 TAPS interstate tariffs submitted to the FERC by the TAPS owners on the grounds that the interstate tariffs failed to meet the Interstate Commerce Act's requirement that tariffs be "just and reasonable." The FERC, pending a full hearing, suspended the 2005 and 2006 proposed tariffs, making them temporary and refundable. The state joined the complaint charging that the interstate TAPS tariffs were discriminatory when compared to the intrastate rates for essentially the same transportation service.

- *"The state joined the complaint charging the TAPS tariffs were discriminatory when compared to the intrastate rates for essentially the same transportation service." Apparently, the State did not feel TSM was discriminatory nor unjust or unreasonable when it chose to enter the TSM settlement. Joining the tariff complaint is a complete reversal from the commitment the State made to defend TSM when it entered into that settlement and beyond any eventuality FHR could have reasonably foreseen at the time it entered into the crude contract with the state.*

#### **How much State revenue is at stake?**

- The 2005 and 2006 proposed interstate tariffs are \$3.71 and \$3.96 per barrel, respectively. The RCA ordered for this same service is \$1.96. FHR has purchased an average of about 55,000 barrels per day of RIK oil from the state in 2005-06. Using the RCA tariff as an indicator of what the FERC may do in January 2007, FHR could owe the state approximately \$100 million for the 2005-07 period. Twenty-five percent of these amounts, i.e., \$25 million, will be paid to the Permanent Fund.
- According to the "fact sheet" accompanying SB 314, the total amount that FHR may owe the State could be \$200 million depending on the extent of FERC appeals.
- If FHR's contract is changed, FHR will be given a benefit that the ANS lessees do not have. According to the lease contracts and the royalty settlement agreements, the lessees will have to adjust retroactive that amount they owe the state for taking royalty in-value. This means that RIK will be less than RIV if SB 314 passes. The State would have been better off, i.e., received higher royalty revenues, if it had chosen not to sell to FHR.
- *"This means that RIK will be less than RIV if SB 314 passes." This statement is only true if the tariff is retroactively lowered. If the tariff is not retroactively lowered, the RIK value will continue to exceed that of the RIV as it does today. "The State would have been better off, i.e., received higher royalty revenues, if it had chosen not to sell to FHR." This statement is only true if one ignores the other sources of value the State receives by supplying the N. Pole refinery with crude oil.*
- SB 314 does not require that the State receive anything in return for relieving FHR of its retroactive obligation. This lack of an enforceable and measurable commitment jeopardizes the constitutionality of SB314.
- *FHR's obligation was entered into under circumstances that have changed dramatically and in a way that FHR could not have reasonably foreseen. Simply put, the State has joined a complaint against the very same TSM that they are a party to and, as part of the TSM settlement, had agreed to defend. In contrast to the DNR's position, the State's federal delegation has taken a stance against the inherent unfairness of retroactivity as it relates to the Quality Bank. FHR can not "retroactively" adjust its operations to reflect a retroactive change in its cost of crude oil whether those costs accrue from changes in the Quality Bank or tariff.*

### Constitutional Issues:

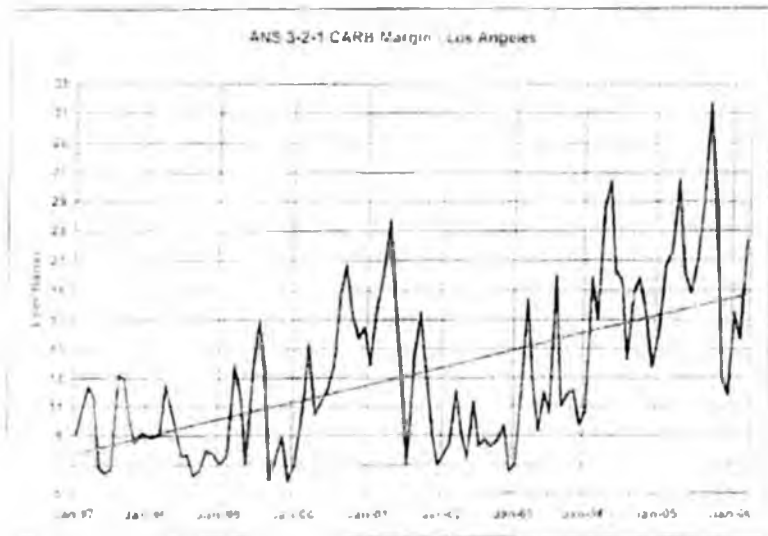
- The Department of Law has identified three potential constitutional problems with SB 314: impairment of contracts; separation of powers; and a violation of Article VIII, Section 2.
- DNR can comment on this last item. Article VIII, Section 2 states  

"The legislature shall provide for the utilization, development, and conservation of all natural resources belonging to the State, including land and waters, for the maximum benefit of the people."
- In the ANS Royalty Litigation, Alaska Superior Court Judge Compton ruled that the "maximum benefit" requirement prohibits the commissioner of DNR from collecting royalties "in kind" if the amount realized would be less than if taken "in value." For the reasons stated above and assuming as FHR, the legislative "fact sheet," and DNR's own modeling of the FHR's potential liability, RIK will be less than RIV if the FERC rules to lower the interstate tariff as the RCA did in 2002.
- *Currently FHR pays approximately \$0.30/bbl premium over the RIV the State would otherwise receive. In addition, there are other benefits that accrue to the people of Alaska from having refined products produced in the State rather than simply exporting ANS and receiving RIV. In any event, the Judge's ruling does not limit the power of the Alaska legislature to enact as law the draft legislation.*
- If SB 314 were to require that the commissioner negotiate a trade from FHR such that at FHR would provide some compensating non-price benefit in return for the relieving FHR of its retroactive obligation, the "maximum benefit" might be achieved. This non-price benefit would have to have a definite commitment required of FHR and that the benefit would have to be measurable and sufficiently balance what the State gives up. This assumes that there may be more latitude to amend the FHR contract than Judge Compton ruling requires.

### FHR Economics

- Consider that FHR can acquire crude oil at a substantially lower price than West Coast refineries (at the RIK netback price plus the intrastate tariff between Pump Station No. 1 and North Pole) and sells its products at a price only slightly less than West Coast refineries (after accounting for FHR's cost of railroading its products from Fairbanks to Anchorage).
- DNR hired Baker & O'Brien to review information supplied by FHR. In the two years that FHR has owned the North Pole refinery, it has very favorable margins.

Even considering the margins of the last five years, the North Pole refinery has experienced positive earnings.



**FHR Economics:**

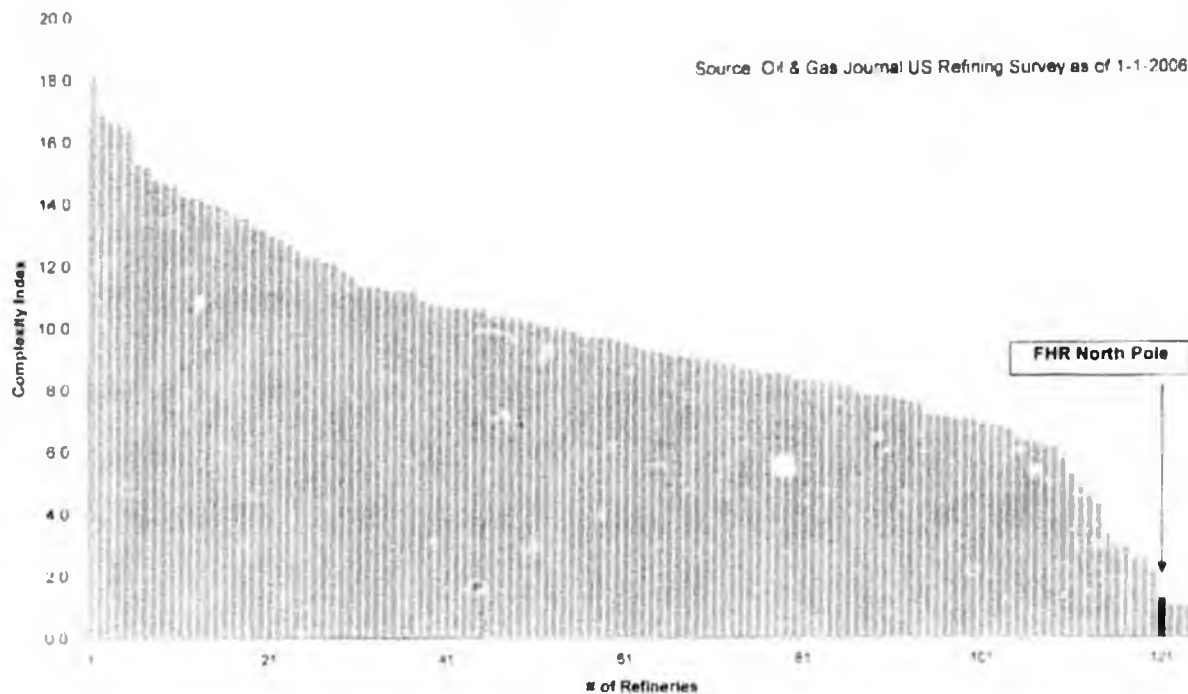
- *The graph the DNR provides above is a "CARB 3-2-1 Margin" representing a product slate that is 67% CARB gasoline and 33% CARB diesel and without deduction for operating costs. First, CARB quality products command a premium price to conventional quality products. FHR does not make CARB products. Second, FHR's produces less than 10% gasoline, less than 10% diesel, with jet fuel being the major portion of the refinery's yield. A closer approximation is shown below, still on a gross margin basis (i.e., operating costs have not been deducted). As can be seen, this gross margin is much lower than the 3-2-1 CARB Margin provided by the DNR, approaching and even falling below \$0/bbl from time-to-time, and this before subtracting operating costs.*

ANS Quality Bank Topping Margin



*The reason for this very dramatic difference between these two margin estimates is the very low complexity of FHR's refinery. Very few refineries in the U.S. have such a low complexity.*

#### U.S. Refinery Complexity



- FHR has very limited opportunities to invest in the refinery as evidenced by FHR's decision to buy, instead of producing clean diesel, from Tesoro. FHR indicated to DNR that the uncertainty caused by the retroactive tariff allowance provision in its RIK price contributed to this decision but a doubling of anticipated project costs contributed to this decision.
- *The clean diesel project at North Pole was canceled because of retroactivity, not rising costs. Costs are rising at our other refineries also, but we are investing hundreds of millions of dollars at those refineries. We are accustomed to making investments for the future in the face of rising costs and changing market conditions. We are not investing at North Pole because we can not forecast the outcome of a high stakes, winner-takes-all lawsuit.*
- FHR has indicated that a prospective rise in the RIK price will mean that FHR will try to maximize cash flow by reducing costs by reducing throughput and avoiding new investment.

### FHR North Pole Refinery Throughput



- *The preceding chart shows how FHR's production is expected to decline. This trend reflects the unfavorable result of the recent Quality Bank decision by the Administrative Law Judge which has rendered some of FHR's historic production uneconomic, in FHR's view. This declining volume also illustrates how the complexity of the Quality Bank can make specific products uneconomic even if some macro refining margins (e.g., ANS 3-2-1 CARB Margin) may indicate refining is profitable in general.*
- Relieving FHR of its retroactive obligations will not likely contribute to lower product prices. To assume that FHR can influence prices downward or upward because of its costs is to assume that FHR has market power in what should be a fairly competitive market.
- The question for policy makers is what will (can?) FHR do if the retroactive provision of its contract is changed.

#### Future RIK Contracts

- If SB 314 passes, and the constitutional "maximum benefit" requirement is resolved, DNR will have to draft conforming regulations. Today the commissioner is prohibited from selling RIK for less than RIV under 11 AAC 03.030.

Kevin Banks  
Department of Natural Resources  
April 2006

# GVEA

Golden Valley Electric Association

PO Box 71249, Fairbanks, AK 99707-1249 • (907) 452-1151 • www.gvea.com

Your Touchstone Energy Cooperative 

April 21, 2006

The Honorable Thomas Wagner  
Alaska State Senate  
Chair, Resources Committee  
State Capitol, Room 427  
Juneau, AK 99801-1182

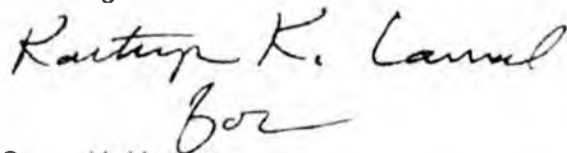
Subject: SB 314

Dear Senator Wagner:

I would like to express my support for the concept of SB 314 because it would help reduce pricing uncertainty for oil to be used in the State. As a utility that purchases large quantities of oil processed within the State, we are concerned with retroactive impacts that may or may not be allowed in our rates by the Regulatory Commission of Alaska.

Thank you for your consideration.

Best regards,



Steve H. Haagenson  
President and Chief Executive Officer

SCR

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# ALASKA STATE LEGISLATURE



Official Business

## SENATE RESOURCES COMMITTEE

**Senator Tom Wagoner, Chair**

State Capitol, Room 427

Juneau, AK 99801-1182

Phone: (907) 465-4907 Fax: (907) 465-4779

Senator Ralph Seekins, Vice-Chair

Senator Ben Stevens

Senator Kim Elton

Senator Fred Dyson

Senator Bert Stedman

Senator Gretchen Guess

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### Sponsor Statement

#### SCR 6: COOK INLET OIL & GAS PLATFORM ABANDONMENT

The Senate and House Resources Committees held a joint committee meeting in Kenai in February 2005. The purpose of the meeting was to receive testimony from individuals and companies doing oil and/or natural gas business in the Cook Inlet basin.

The committee heard comments and suggestions on methods to improve the business conditions in the oil and natural gas industry. One of those suggestions was the need to provide for regulations on the abandonment of the platforms in the Cook Inlet.

Production in the Cook Inlet has declined since the date the platforms were in place in the 1960's. Four of the sixteen platforms are "lighthoused" and inactive. However, it is possible that the platforms could be instrumental in reversing the declining production trend. The platforms could be used to drill new, deeper wells and might tap into larger fields than have been developed to date.

In 1996, the Alaska Oil and Gas Conservation Commission (AOGCC) proposed implementation of revised platform abandonment regulations. However, a decision by the attorney general indicated that the Department of Natural Resources (DNR) and not the AOGCC was responsible for developing regulations.

This resolution urges the Governor to direct the DNR to undertake a comprehensive review of the platform abandonment.

**SCR**

**7**

# ALASKA STATE LEGISLATURE



Official Business

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Juneau, AK 99801-1182

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Senator Ralph Seekins, Vice-Chair

Senator Ben Stevens

Senator Kim Elton

Senator Fred Dyson

Senator Bert Stedman

Senator Gretchen Guess

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### **SCR 7: Oil and Gas Regulatory Revisions** **Sponsor Statement**

The Senate and House Resources Committees held a joint committee meeting in Kenai in February 2005.

The purpose of the meeting was to receive testimony from individuals and companies doing oil and/or natural gas business in the Cook Inlet basin. The committee heard comments and suggestions on methods to improve the business conditions in the oil and natural gas industry.

One of those suggestions was the need to continue to streamline the regulatory process for oil and gas exploration.

Exploration is critical to the development and production of new fields and attention to the permitting processes and the efforts and costs of those processes is necessary in order to assure continued exploration efforts.

This resolution recognizes the efforts undertaken by Governor Murkowski since his administration took office in December 2002 and endorses ongoing efforts to continue to review and revise regulations to streamline the exploratory oil and gas process.

# ALASKA STATE LEGISLATURE



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This resolution urges the Governor to direct the DNR to undertake a comprehensive review of the platform abandonment.

**SJR**

**2**

# FISCAL NOTE

**STATE OF ALASKA**  
**2005 LEGISLATIVE SESSION**

Fiscal Note Number: \_\_\_\_\_  
 Bill Version: S:R002-DNR-O&G-01-2  
 ( ) Publish Date: \_\_\_\_\_

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: Natural Resources  
 Title Endorsing ANWR Leasing RDU Resource Development  
 Component Oil and Gas Development  
 Sponsor Senate Resources Committee  
 Requester Senate Resources Committee Component No. 439

**Expenditures/Revenues** (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
<b>TOTAL OPERATING</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>						
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<b>CHANGE IN REVENUES ( )</b>						
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
<b>TOTAL</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Estimate of any current year (FY2005) cost: 00  
 Mark this box (X) if funding for this bill is included in the Governor's FY 2006 budget proposal:

**POSITIONS**

Full-time						
Part-time						
Temporary						

**ANALYSIS.** (Attach a separate page if necessary)  
 No fiscal impact anticipated with passage of this resolution.

Prepared by: Mark D. Myers, Director Phone 269-8800  
 Division Oil and Gas Date/Time 1/21/2005  
 Approved by: Tom Irwin, Commissioner Date 1/21/2005  
 Agency Natural Resources

# SJR 2

**Headquarters:**  
217 2nd Street, Suite 201  
Juneau, Alaska 99801  
(907) 586-2323 FAX 463-5515  
www.alaskachamber.com



**Regional Office:**  
601 W. 5th Ave., Suite 700  
Anchorage, Alaska 99501  
(907) 278-2722 FAX 278-6643

January 25, 2005

Senator Tom Wagoner  
Chair  
Senate Resource Committee  
State Capitol Room 427  
Juneau, Alaska 99801-1182

The Honorable Chairman and Members of the Senate Resource Committee,

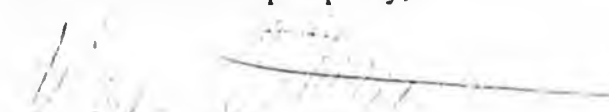
The Board of Directors of the Alaska State Chamber of Commerce supports and endorses passage of Senate Joint Resolution 2 (SJR 2). The resolution urging the United States Congress to pass legislation to open the coastal plain of the Arctic National Wildlife Refuge, Alaska, to oil and gas exploration, development, and production is in line with one of our legislative priorities urging the opening of the ANWR to oil exploration.

The Alaska State Chamber of Commerce supports Alaska's role in providing this nation with a major portion of its domestic oil and encourages the United States Congress to pass a bill opening the coastal plain of the Arctic National Wildlife Refuge to responsible exploration, development, and production of its oil and gas resources. We believe that oil exploration and development activity can be conducted in a manner that protects the wildlife and the environment. Additionally, the Alaska State Chamber of Commerce opposes any efforts to declare the coastal plain of ANWR a wilderness area.

The Alaska State Chamber of Commerce urges the Senate Resources Committee and Legislature to continue to support and actively participate in efforts to open the Coastal Plain of ANWR to environmentally responsible oil and gas development and to appropriate the necessary resources to attain congressional approval of environmentally responsible development within the 1002 area of ANWR. We believe adoption of SJR 2 sends a strong message of support for opening ANWR.

Thank you for your support and consideration of this resolution.

Yours in economic prosperity,

  
Wayne A. Stevens  
President

# ALASKA STATE LEGISLATURE



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### Sponsor Statement

#### SJR 2 – ENDORSING ANWR LEASING

The need for expanding Alaska's resource based industries is imperative if we want to maintain or increase the State's economic base. Development of our oil and gas reserves is our most viable option to increase the revenue stream and supply new jobs for those entering the workforce.

North Slope production peaked in 1988 at 2,005 million barrels per day and has declined steadily since. Current production is approximately half of the peak production. Development of the Coastal Plain will allow Alaska to derive economic benefits and at the same time provide stability to our national energy demands during the ongoing turmoil in the Middle East and Venezuela.

This resolution is not a new piece of legislation. It has been introduced on several occasions and has always enjoyed overwhelming support from the Governor and Legislature, as well as the citizens of Alaska.

With the recent changes in the United States Senate and support from the leadership in both the Senate and the House of Representatives, it is quite likely that Congress will act favorably this year. We can be assured that President Bush will not veto it, like his predecessor, President Clinton, did in 1995.