

HOUSE / SENATE FINANCE COMMITTEE MINUTES - 1967-1982 2717

*Section 1. FINDINGS AND INTENT. The legislature finds that the abuse of intoxicating liquor is inflicting very deleterious effects on individuals, families, and the public at large. The legislature intends that the manufacture, distribution, and sale of intoxicating liquor be controlled and regulated under the police power of the state in such a manner as to mitigate the deleterious effects of intoxicating liquor on the health, safety and welfare of the people of the state. The legislature finds, in furtherance of that intention, that the health, safety and welfare of the public will be well served by placing a person on the Alcoholic Beverage Control Board who is trained to recognize the deleterious effect of alcohol in society and who will be in a position to influence the development of a state policy competent to mitigate or neutralize those effects.

Sec. 04.06.020 is amended to read:

APPOINTMENT AND QUALIFICATIONS. The board consists of six (FIVE) members appointed by the governor and confirmed by a majority of the members of the legislature in joint session. A member of the board may not hold any other state or federal office, either elective or appointive. Two members of the board shall be persons actively engaged in the alcoholic beverage industry, except that no member may hold a wholesale license or be an officer, agent, or employee of a wholesale alcoholic beverage enterprise. One member of the board must have training or experience in the epidemiology of alcoholism. No three members of the board may be engaged in the same business, occupation, or profession. -1044-5-31-80

PAGE 1, DELETE LINES 19 - 21

REPLACE WITH

~~ALTER~~ LINE 22 delete "(b)" insert "Sec 19.40.120"

* Sec. 3, AS 19.40 is amended by adding new sections to read:

ARTICLE 2. USE OF THE HIGHWAY.

Sec. 19.40.⁰⁷⁴~~100~~. USE OF THE HIGHWAY BY INDUSTRIAL OR COMMERCIAL TRAFFIC. (a) The department shall maintain the highway and keep it open to industrial or commercial traffic throughout the year.

(b) "industrial or commercial traffic" means

(1) travel necessary and related to resource exploration and development or to support of those activities, if the individual engage

in those activities has all necessary permits; or

(2) travel necessary and related to access by local residents to their property; or

(3) motor carriers engaged in commerce which are common carriers or contract carriers regulated by the Alaska Transportation Commission under AS 42.10.

Sec. 19.40.⁰⁷⁵~~100~~. CLOSURE OF THE HIGHWAY TO TRAFFIC. The provisions of AS 19.10.100 apply to the closure of the highway by the department.

HOUSE FINANCE COMMITTEE

June 5, 1980

8:40 a.m.

All Members of the Committee were present except Representatives Schaeffer and Smith. Other Legislators present: Representatives Carney, Parker, Osterback, Hurlbert, Phillips, Branson, Cotten, Halford, Eliason, Malone and Metcalfe.

PRESENT

Testifying before the Committee: Commissioner Robert E. LeResche, Department of Natural Resources; Attorney General Avrum Gross; John Hedland, Attorney, Hedland, Fleischer & Friedman; Dudley Parker, General Manager, Alpetco; and Jamie Love, Alaska Public Interest Research Group.

Chairman Meekins called the meeting to order. He said the purpose of the meeting was to receive information on the Alpetco Contract.

ALPETCO
CONTRACT

Tape HFC 80-76, Side 2

475 ROBERT LERESCHE, Commissioner, Department of Natural Resources testimony.

Robert
LeResche
Testimony

618 Moss question - teapot dome crude. LeResche response.

639 Meekins question - determining price. LeResche response.

720 Moss question - pricing & selling oil. LeResche response.

749 Meekins comments on contract. LeResche comments.

757 Carney question - selling oil at competitive bid. LeResche response.

776 Meekins questions on contract & best available price. LeResche response.

820 Rogers questions on not approving contract.

Tape HFC 80-77, Side 1

001 Rogers continues questions. LeResche response.

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198 Osterback question on not approving contract. Hedland response.
243 Meekins question - lawsuit. Hedland response.
266 Hurlbert question - contract vaguely written. Hedland response.
299 Meekins questions - original contract/litigation. Hedland response.
359 Carney comment - 75,000 barrels per day.
366 Halford comments on contract. Hedland response.
393 Meekins questions benefits. Hedland response.
400 Carney/Hedland comments on contract.

419 AVRUM GROSS, Attorney General, State of Alaska testimony.

Avrum
Gross
Testimony

463 Meekins question - Alpetco 95% in compliance. Gross response. Further questions from Meekins and Gross response.

573 Rogers question and Gross response.

582 McKinnon comments and response from Hedland and Gross.

[Technical Problems with Tape Recorder for approximately 3 minutes.]

679 Metcalfe comments on financing. Meekins comments.

720 Gross comments.

736 Halford question on contract. Hedland response.

792 Rogers - kind of financing for petrochemicals & trends for future under amendment #2. Gross response and discussion between Meekins, Gross and Rogers.

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822 Eliason question - bank financing on contract.
Gross response - proceeding in good faith under
original contract.

Tape Change HFC 80-78, Side 1

001 Discussion between Gross and Eliason.

032 Metcalf question - Alpteco in compliance with
contract.

065 Hedland response. Comments between Metcalfe and
Hedland.

150 Meekins and Rogers comments.

179 Meekins comment contract not just for one year.
LeResche response - federal government changing.

193 Hurlbert question - could legislature be sued.
Gross response.

226 Moss question - what is being built in Valdez.
Hedland and Gross response.

259 LeResche comments - site in Valdez. Moss questions
and LeResche response.

284 Gross comments - difference between old/new contracts.

293 Rogers question - turning down amendment. Gross
response.

342 Carney question - uncertainties on financing.
Gross response and Carney comments.

385 Metcalf question - legislative approval. Gross
comment. Metcalfe question on liability and
Gross response.

513 McKinnon comments - Alpetco benefits. Meekins
comments.

544 Halford question - definition of petrochemical plant.

550 Rogers moved to report HR 26 ("Urging the commissioner
of natural resources to sell a portion of state
royalty oil by competitive bid.") out of Committee.
There being no objection, it was so ordered.

HR 26
REPORTED
OUT

6/5/80

621 Halford question answered.

624 Meekins question/Gross response - petrochemical plant.

652 Discussion between Meekins/Metcalfe - conditionally approving contract.

673 Hedland response to conditional approval. Gross response.

690 Hedland comments on A.L.I.V.E. case.

698 Rogers comment on administration amending contracts. Gross response.

721 Halford question - production of Napa. Gross response.

Dudley
Parker
Testimony

010 JAMIE LOVE, AkPIRG testimony.
124 Meekins question. Love response.
374 Meeting Adjourned. 12:30 p.m.

Adjourn

Tape	HFC 80-76,	Side 2	#470	to	end
	HFC 80-77,	Side 1	#001	to	end
		Side 2	#001	to	end
	HFC 80-78,	Side 1	#001	to	end
		Side 2	#001	to	end
	HFC 80-79,	Side 1	#001	to	374

MR. DUDLEY PARKER, GENERAL MANAGER, ALPETCO. TESTIMONY

PARKER: It is not Charter's desire to initiate or defend (inaudible)
That is one of the reasons why we came to you. We have our own
opinion as far as what --

GUY: Mr. Chairman, before he continues with his main testimony,
I believe he was present when I was asking about the makeup
of ALPETCO, Charter Oil, and who they are?

PARKER: In order to put that to rest. Charter owns approximately
at ^{this} ~~that~~ point in time 85%, E. F. Hutton owns approximately 8%,
SeaTrain 7%, and the Alaskan Regional Native Corporation owns
.7. Now that represents a 3% carried interest in Alaska
Petrochemical, .7 for the overall project. Now the individual
native corporations involved, we can give you that if you
want it.

GUY: Mr. Chairman, I'm not particularly interested in the part
of the Native interests concerned, but much more concerned about
the makeup of Charter, the subsidiaries and affiliates.

PARKER: Charter Oil company, well let's start with the Charter Company.
The Charter Company is a public held corporation, it's trade
on New York Stock Exchange is in the top 100 corporations in
the Country. It operates its business through a series of
subsideraries. The oil portion of the business is basically
Charter Oil Company. With that we also have established a
Charter Oil of Alaska, and I don't know exactly which ones
in Alaska is the actual entity that is part of the Alpetco.

But that is a wholly owned sub through the various chains of the charter company.

GUY: Of each Charter Company?

PARKER: Of the Charter Company, which is the parent company.

GUY: Oh, of the.

PARKER: The Charter Company is broken down into not only oil, but it is broken down into insurance and communications. You may not be aware of it, but Charter owns Ladies Home Journal, it owns Redbook. We've got several newspapers, TV stations, radio stations and etc. That's referred to as the communications segment of our business. Then of course the oil business is primarily the major portion. Then it is also involved in insurance. It owns various insurance companies. Of the three segments of the Charter company, I represent only that portion (inaudible) of oil.

GUY: Thank you Mr. Chairman.

(inaudible)

PARKER: O.K., again, as I said we have not come either to defend or initiate. I would like to give you, based on our figures of what the difference between the two contracts really represents. First of all, in existing contract, there is no date for start up. In the amendment, without a doubt, the date is there, March 1, 1986. One could conclude, if you wanted to, that you didn't have to start up under the existing facility that, well you could spend 1.5 billion dollars in doing that, you would start some facility. I think that in the reading of the contract as far as must expend such and such dollars, as time goes on, if one will read it, it merely says must commit,

and there's a lot of difference between committing to spend and the actual expenditure. It says commit or expend. From that standpoint, the only actual commitment to spend is the \$100 million commitment that must be expended by July the 18th. We have made an agreement that that money will be spent prior to June 30th in order to give the Commissioner's staff a chance to audit and to verify the fact that \$100 million has actually been expended.

MEEKINS: What does that mean? We had a question here before that somebody could loan you money and you could spend it back to them, and then they could give it back to you and you could give it back to them, or some kind of game like that, and nothing would have every really been spent, but it would look like it had been spent.

PARKER: I am not an attorney and I think the contract says you must expend the money. Now, it does not specify what the money should be spent on, it could be spent on steel, it could be spent on platinumum, which is used (inaudible) within the facility. There are no specifications as to what it is to be spent on. There is merely the obligation to expend \$100 million.

MEEKINS: In connection with the facility? Does that mean you could spend a \$100 million buying oil for somebody?

PARKER: No sir. We can testify that that is not (inaudible). There is no completion date in the existing contract. There is a completion date in the amendment. The type of facility in the existing contract is vague, and as was testified, the definition of a petrochemical facility and/or a refinery depends on whether you call for the attorney general's last comments, is expected in wording in that contract, it says that configuration can be

changed depending on market conditions as time goes on. So within the existing contract you have the ability to change to whatever you deem as being as reasonable under the economic conditions that prevail.

MEEKINS: Change what?

PARKER: Change what you will build. Under the proposal you will be given

(Tape change HFC 80-78, Side 2)

at what will be built before we proceed forward.

MEEKINS: Let me back you up a bit. Did you say that there was a complication under the proposal here for start up?

PARKER: Under the amendment.

MEEKINS: Under the amendment to the old contract?

PARKER: Yes sir.

MEEKINS: Let's call it the proposal. It's getting confused with the amendments to the amendments. Under the proposal that we're discussing.--

PARKER: There is a start-up.

MEEKINS: When is that?

PARKER: It's March 1, 1986.
And how is

MEEKINS: ~~YXXXXXX~~ A start-up defined. What does that mean?

PARKER: When you are --

MEEKINS: March the first, what?

PARKER: 1986.

MEEKINS. Start-up? Oh, o.k., I don't mean that. I mean construction. I don't mean start up the plant, I mean when do you start construction. Your completion date is '86. Is there a date when you have to start to build?

PARKER: That would be covered at the time we are allowed to go forward. In other words, when that total package is put there, it will be based on a completion by March 1st. Included in there will be a time at which it will be started.

MEEKINS. O.k. but it's not in the contract?

PARKER: It is not in the contract. Let me bring, when we came up here a week and a half, ten days ago, we were proceeding under the original contract. We have tendered ~~xxxPxxndxxx~~ ^{the crude oil} 150,000 barrels a day of crude oil has been tendered to the pipeline. It has been accepted by the pipeline. We postponed meetings in order to finalize the \$100 million expenditure. That meeting was set for Monday. It has been rescheduled for Friday. So that we will spend the \$100 million, and we will meet the July 18th bench mark.

MEEKINS: Well how do you get it expended if you are postponing. How are you going to expend it?

PARKER: Well, we have been working for several weeks and months to come up with a list. We have gone out to vendors. We have gotten bids. From a list that contains more money than \$100 million we will set down and make a determination of which ones of those do we actually go ahead and set up to be expended.

MEEKINS: That didn't answer my question though. Do you know what is going to be, how you're going to spend the money. Can it be for things like steel or is it going to be for something else.

PARKER: It's going to be for tangible items. I do not know the exact items. I'm sorry.

MEEKINS: Well, I don't mind that. I mean if you're talking about buying things that are physical things that are in the plant, that's what I have in my mind as something that --

PARKER: And that's what will come in on the \$100 million (unclear) will be items that we have told the commissioner and I think we've given him a list of the type of items and the companies of which we're dealing with, people such as G.E., Chicago Bridge and Iron, U. S. Steel. Companies that are not going to get involved in mickey-mousing arrangements as far as you proceeding forward in the contract.

MEEKINS: Mr. Randolph?

RANDOLPH: Mr. Chairman I have just one question to follow up on you question. If you buy steel, or whatever product you are going to buy, allegedly to produce at the Valdez plant, what's the guarantee that's what's going to happen to the steel and so forth?

PARKER: Well, if the procedure goes forward, what we buy is being specked at as part of the construction contract and what is needed. It's actually being placed, and the order is being placed. We are looking at them to build and handle the construction (unclear) on this project. We are not going to go ahead and go out there and order something that is not a part of their plan as far as the actual construction is.

RANDOLPH: I guess my question is how liquid are those commodities likely to be. So that if you have a million dollars in the Valdez plant, and the Valdez plant doesn't go ahead, you obviously are going to be thinking what are we going to do with these materials we've bought.

PARKER: The obligation is not from the standpoint that we spend \$100 million and we leave it on the ground in Valdez. If there is a salvage bag, I'd expect any court or anybody would say it reasonable that you were able to claim you salvage value.

RANDOLPH: Oh, (unclear) on the ground in Valdez?

PARKER: No sir, it will not. And let me explain some of the reason for that. In a facility such as is currently under configuration to be designed, there are some very, very, very large vessels that have to be run through a shop and in many cases it required 18-24 months lag time between the time that is ordered and the time that vessel is actually shipped out there. One of the keys in building any type of facility of this nature is the critical path as to when certain items must be put on the site. The manner on which they are put on the site, because you don't move them around. In other words, when they come in, they've got to come in in a sequence where it is a logical construction that takes place.

MEEKINS: Mr. Metcalfe?

METCALFE: How much difficulty do you perceive in obtaining financing? Do you know that you've only got an 18 month (unclear).

PARKER: You're confusing. That's under the proposal. And there's no question, when you came in with that financing you would have your total package and it would be subject to the approval of the commissioner and the longterm (unclear). So you're not getting financing with only 18 months of crude oil. You're getting a proposal that, if it goes forward, is tied into the 20 some odd years crude contract.

MEEKINS: Yea, but the question is, they can opt out.

PARKER: And if you opt out than the project doesn't go forward.

Somewhere along the line we're mixing the proposal and the existing contract. The proposal does not require an expenditure of \$100 million.

METCALFE: I've got two basic concerns before I'm willing to go ahead with the amendments. From what I've seen the possibility of Charter Oil basically using this as (unclear) and they're buying ours (unclear) in the meantime, to show some demonstration of compliance, you're buying materials (unclear). My understanding at this point that you have to go out and you have to spend money. (unclear)

PARKER: By the way, we're committed to (unclear) and we're not going to buy platinum.

METCALFE: Right, but what I'm saying is that you can go out and buy a lot of materials that are useful elsewhere, and thereby make some effort to establish that you have made a good faith effort, and then at the end of '81, have a project that gets turned down, and assets were liquid (unclear). You have basically spent maybe 70% of what you have made off of the (unclear) for the resale of oil and you'd walk away with that profit. And you'd also walk away with your original assets. And, ahh, so I've got two concerns. I want an accountability of where the money is being, of what is going on and what is being spent from you so that we can assess, we have the good records to assess whether or not there has been a good faith effort, number one, and two I don't believe the Charter is in compliance with its original contract at this time and I see that the commissioner has said that has. So how objectional would you be, what problems would Charter have, if we were to add to this some accountability and disclosure requirements?

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PARKER: Add to what?

METCALFE: To the existing contracts, so that we have adequate records. As well as an additional method to require that not only the commissioner has to approve. That is the commissioner makes his recommendation and submits it to the legislature.

PARKER: Well, you're asking me if we want to set out and add additional renegotiations of the current contract.

METCALFE: What I'm saying is we have some amendments you would like to see get through, the administration would like to see get through, and if they're going to get through they are going to have to satisfy at least 21 members of the House and that's (unclear).

PARKER: O.K., I think we're talking about two separate things.

To spend the \$100 million is under the existing contract, and there are means in there whereby the commissioner has the right to audit and get a report from Peat, Marwick and Mitchell, in complete detail of what that \$100 has been spend for and how it has been spent. So that's already in there. If you accept the amendment there is no obligation to spend the \$100 million.

METCALFE: So, ... I have to think about that. Now it is my understanding that there was (unclear) of how or what you have to do between and '81, and why is it to our interest to allow you to play the stockmarket with (unclear).

PARKER: Well, what we have to do between now and 1981, the first thing is you must approve the amendment. Because if you don't approve the amendment 1981 is not the trigger date. O.K.? What did you ask we're going to do between now and 1981, number one you cut the volume that we were counting on to run through

that facility by 1/3. And on that basis, that facility has to be redesigned. So, from that standpoint is what we will be doing -- will be the redesigning of the facility. To say o.k., here is what we now will fill, we'll actually construct, say here's where it will be financed, here's what it will produce, and there is the completion date. That's what we will be doing between now and December 31st, 1981.

METCALFE: Would you have a problem amending one thing or another? What we have before us now is something that requires you to come back to us, the legislature, not the commissioner, for approval in '81.

PARKER: I tell you, I speak for Charter and Alpetco, and do not want to get into the battle that apparently may surface between the division of powers within the state of Alaska. I think that's not fair to ask us to do that.

METCALFE: What I'm asking you is would that, I'm not asking you to be in the battle, I'm saying would that change your attitude, because ultimately you have to accept any amendments we approve.

PARKER: But so does the administration. My point being if you do that, and the administration says no, then you've put us right in the middle of negotiations of what the administration wants and what the legislature wants.

METCALFE: If you'll go along with me, I don't see any reason why the administration wouldn't go along with it. If we amend ~~it~~ it and it is acceptable to you, I don't see any reason why administration wouldn't also find it also acceptable. So, what I'm asking you is is it going to make it unacceptable to you if we do those things?

PARKER: I don't know. Probably, based on the time frame. The clock is ticking as far as us taking the 150,000 barrels a day of crude oil. The clock is ticking for us to meet the June 18th benchmark. We've been up here 10 days working on an amendment, at the same time preceeding forward with the existing contract.

METCALFE: If the House agrees on something today, it will be done by the 7th, and when you have to come back in '81 we can always put a provision in there that the Legislature has x-number of days to comply or not comply.

PARKER: I think that is something the law you need to enact in the State of Alaska to decide how you want the administration to (unclear) contracts.

METCALFE: So you would basically not have a problem if we put in a --

PARKER: I didn't say that. I would say I probably would have a problem.

METCALFE: But, what I'm saying is, if the Commissioner makes a determination and the Legislature had authority to look at that determination of a period of 15 days and if they hadn't made a decision within x-number of days, --

PARKER: What I don't understand (METCALFE & PARKER talking at once) I have no way of knowing what powers the legislature has between now and the time in which I show up. I don't intend to try and control that. I'm trying to build a facility. And rather than me getting tied up into trying to fight any changes in the laws which might make what we agreed to impossible for me to meet, I can't afford to take that risk.

METCALFE: This wouldn't affect the basic contract.

PARKER: But I don't know whether next year's Legislature would say

well, we don't like it and we're going to change another law.

MEEKINS: I think your answer is no Mr. Metcalfe. Well, let me ask you a question. What is the capacity of all the refineries that are operated by Charter and its affiliates?

PARKER: At this point in time, Houston has the capacity of approximately 70,000 barrels a day. we own half interest in (unclear) a refinery that has a capacity of 500,000 barrels a day.

MEEKINS: Those are the only two you have?

PARKER: That's the only two we have. We are in the throes of negotiating of trying to take a third refinery out of bankruptcy. It has been in bankruptcy for I guess, a couple of years. It is a facility that two or three years we also tried to acquire.

MEEKINS: Is it London based?

PARKER: No, it's in Puerto Rico. It's a common --

MEEKINS: What's its capacity?

PARKER: I really can't answer because the capacity, I've given you crude capacities in this case, and that facility is not necessarily geared for a lower crude capacity. That's basically is down stream processing. In other words, we currently sell out of our Bohemian refinery the Napa that goes on into there for further processing. So depending on whether they are running maximum Napa, or whether they are running crude oil, will determine that.

MEEKINS: Is that one currently operating, the one you're trying to take over?

PARKER: It's, as I understand, it is operating at a very reduced crude rate, and they of course are buying (unclear)

MEEKINS: Whatever its capacity is, it is operating, but it is below capacity?

PARKER: That's correct.

MEEKINS: And what about the other two that you mentioned. Are they at peak capacity or do they --

PARKER: The Houston refinery is operating full, the domestic refinery is operating full, the other one has averaged 130,000-140,000 barrels a day. We only own half of it, and the actual capacity of any plant depends on the crude its designed for, so there could be some crude's running in there, that we are currently running, that you could not run a full 500,000 barrels a day.

MEEKINS: The point I'm getting to though is that you've got at least 570,000 capacity, right?

PARKER: We only half of the 500.

MEEKINS: oh, yea. But, the capacity that you are affiliated with is 570,000 barrels a day and, at least potentially another 1, of which we don't know what the capacity is, so and what you're saying about what you're running is about 200,000 -- with the caveat that to some extent it runs below capacity because of the kind of crude that you're using, the conclusion I'm leading to is that it seems inconsistent when you have two refineries that aren't running full, and you're trying to get a third one, which isn't running full, that you would want to build a forth one. It seems to me more likely that what you'd want to do is go find some oil.

ROGERS: Mr. Chairman.

MEEKINS: Mr. Rogers,

ROGERS: There are a couple of points on that though. One is, to my knowledge they could not shift the oil to the Hama refinery without getting a waiver from congress because that oil would be in international commerce. They could run it from Huston, ^a ^{of} and I'm not sure if you run ~~xxxx~~ domestic form/ crude there and displace other. The interesting one though would be the commonwealth oil facility. Did you say you couldn't run Alaska crude (unclear).

PARKER: (unclear). We don't own that one yet.

ROGERS: O.K., but the point is , now if you do acquire it then ship from Alaska to the commonwealth refinery and process (unclear) you don't have to use Jones Act tankers. That's one of the few places in the world --

PARKER: That's not true. The only exception to Jones Act tankers to my knowledge is on the Hess that goes into the Persian Islands.

ROGERS: And you saying a commonwealth --

PARKER: You cannot use foreign planked tankers to go to Puerto Rico.

ROGERS: That's considered interstate commerce.

PARKER: That's right.

ROGERS: Can I ask then Mr. Chairman, o.k. if you are going to take on July 18th, what are going to do with the oil. Can you tell us, I mean, Alpetco's going to sell some to Charter obviously, and take that 30¢ profit and --

PARKER: We do that as an internal (unclear)

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ROGERS: And then where's the oil going to go

PARKER: It's going to go to the gulf coast.

ROGERS: O.K., so it's going to your Houston refinery or be sold to other processors.

PARKER: Well, you keep saying sold to somebody else. If the only profitability in moving of crude oil is by reselling it, then ^{es it} you've drawn a conclusion that the refiner process~~xxxx~~for nothing. We are in the process of (unclear) of product, and you've got to get that crude oil into product⁺. So our desire is from the stand-point to convert either 50 or 75,000 into product and sell the product. So, we are not looking at (unclear) of crude oil.

ROGERS: O.k., so instead you would be contracting for the refining to the extent that you can't refine it yourself?

PARKER: That's correct.

ROGERS: o.k. Mr. Chairman, I've got one other question

MEEKINS: Let me interrupt you, the Speaker is asking us to come to the Session and we do have a number of witnesses who have asked to testify. Perhaps it would be appropriate to thank Mr. Parker for his testimony and allow other witness to testify.

PARKER; Would you let me make one statement before leaving?

McKINNON: I have a number of questions for Mr. Parker

-- --

ROGERS: Can I follow up?

MEEKINS: Mr. Rogers

ROGERS: O.k. this is a quick one. and it involves Mr. Parker and the Commissioner. The new section 4.2.3 requires reports, a quarterly report, (unclear) confidential as requested by buyers and permitted by law. Does that mean that we can say they are not confidential by law and that they will not be confidential, that's number one.

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Number two, if they are confidential is it the opinion of Alpetco and the commissioner that those would be available to the legislative budget and audit committee?

LERESCHE: The answer to your second question is no. They are confidential and (unclear). The pragmatic answer is virtually everything here will be available because the law is very (unclear) regarding what is confidential, and that applies mostly to trade secrets.

ROGERS: Thank you Mr. Chairman.

LERESCHE: There may be an exception to confidentiality to the Budget and Audit Committee, but I'm not positive (unclear).

MOSS: I've asked this question to a number of other people. Let's talk about \$100 million for tangible items and so forth. You've talked about building, and I still don't have an answer just what in blue-blazes we're going to build out there. I'd like to know. We talked about a petro chem. plant, are we talking about a refinery, and how many Alaskan jobs are going to be involved in it. Now it is my understanding under a chemical processor, we would have many jobs, but under a refinery we will have less. Can you tell me how many Alaskans we are talking about or how many jobs are going to be available, and just exactly what are we building?

PARKER: Under the current configuration that is under the original contract, the number of permanent jobs, I think ranged somewhere between 500 and 700 jobs.

MOSS: That's under the original.

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PARKER: That's under the existing contract that's in effect right now.

MOSS: What are we talking about under the one we are doing now, and what are we going to be employing those people --

PARKER: Are you talking about the proposed amendments?

MOSS: The proposed amendments.

PARKER: Well, when we came up here ten days ago, we didn't have the idea of changing the configurations of that facility. So we have not within a ten day of time redesigned and redetermined what units will be put in there. It's not whether its a petro-chemical facility or a refinery that determines the number of jobs. Its the sophistication of that facility in a number of units that are built. Let me give you an example, it doesn't have to do with size, take a unit that runs 150,000 barrels a day of crude oil, 5 operators. They operate three shifts. That's fifteen people. And there's four-five people off at all times. That's 20 people. If all you build was a (unclear) plant. That's what you'd have. But you don't do that. You go down and strain each unit that you add and you add additional operators, with that you end up with your maintenance people, so size has nothing to do with in. In fact a scale down is not there. That's another item before preceed on under the amendment that the commissioner will look at and we will say here are the units and there is our best estimate of the number of people it takes to operate that. And there is no way anybody can give you that since last Monday a week ago when we came up here.

MOSS: Then I assume we are talking about basically a refinery, and

my next question would be, if we do have a refinery, are we going to have a practical first choice on that fuel and stuff, diesel and heating oil and so forth in Alaska before it goes outside? Or are we going to end up having to ship that stuff back or are we going to get the opportunity to use it within the state?

PARKER: We would hope from the standpoint that our product as much as possibly can be utilized in the State of Alaska that we would sell it. (unclear) your competitors and people at Tesoro, Chevron and etc. that we're going to compete with them. So, and answer from the standpoint of whether of you get all of ours, is going to be depending on what handle the pricing structure takes throughout the state. You won't be able to utilize I don't think the total output. But we had rather sell that product in a market in the state of Alaska rather than us having to ship it some other market. That again will be a function of the demand in the state of Alaska not only for this facility, but all the facilities.

MOSS: Thank you Mr. Chairman.

OSTERBACK: Mr. Parker, when you testified at the Resource Committee talking about the 75,000 barrels a day to build a refinery, figure it would be more economic or feasible to come down to 75,000 barrels in case the oil started dropping from Prudhoe Bay. When a required 50% (unclear) is that right? Let's put it this way, if you were going to build a bigger plant, and you didn't get enough oil, it wouldn't be feasible. That's what I understood.

PARKER: I think from the standpoint that the size of plant, of course its got to be looked at in reference to the guaranteed supply for whatever timeframe you have. Probably it's a little more difficult to finance a larger facility where you show a gap where production is below what you were able to run, and convince them that there will be other discoveries of which you have call on. And it would be if the facility was a lesser size, and you showed you had that all for x-number of years longer. I do think that in scaling the facility down you showed an assured crude supply for a longer period of time, which should aid in the financing of that facility. One other thing that you can do in the building of that facility is the way in which it's constructed, is that you can design it in such a manner that you can continue to turn the unit down. In other words, just because it's designed to run 150,000 barrels a day doesn't mean that you don't have limitation that you can run a lesser amount. I'm sure we do a combination of both of them.

MCKINNON: I'm still not clear on the taking of the oil and the refining of the oil. Alpetco is apparently taking the oil, transports it to Valdez, at that point what happens with it?

PARKER: Under the existing contract?

MCKINNON: Under, well what are you going to do if you start taking oil, (unclear) who's going to refine it, Alpetco, Charter, what company takes it?

PARKER: Alpetco. The contract is with Alpetco.

MCKINNON: Alright. Alpetco will ship the oil to where? (unclear)

PARKER: Well, it will go to the gulf coast. Some of it may go in (unclear) refinery, some of it may go in other refineries (unclear) that process for us, which is not unusual in the oil industry.

MCKINNON: It will be processed for Alpetco. Alpetco will retain the title for the oil as it's processed (unclear) or the refining?

PARKER: I don't know that it will stay in the Alpetco, or whether each individual partner will want to call on their own oil. I say that because for instance, Seatrain is a refinery, and they have a refinery in Abeline, Texas, so they may want to take their crude oil and in some form or fashion go to Abeline, Texas.

MCKINNON: (unclear) Using Seatrain, Seatrain takes it to Abeline, refines it, at what point is the profit made on the oil that's going to be reinvested in the project?

PARKER: Well, hopefully, you could take it all the way through and the profit is going to be made when the product that's produced is sold.

MCKINNON: From the refinery?

PARKER: From the refinery. Now, I'm not saying that all of the oil will be refined, some of it may be refined in our existing refineries, some may be processed for others; some of it may be sold.

MCKINNON: Assuming Seatrain is paying a higher price on the stock market (unclear) and it takes this crude at a lower price, would that differential be included ~~xxxxxxx~~ or do you envision reinvesting that differential in part of the project?

PARKER: I think when you look at the project you can answer the reinvestment in anyway you want to. There's a certain amount of equity that has to be and will be contributed to that project. Whether it comes out

of the profit of this one, the selling of that, or whether it comes out of the profit of an existing crude that's produced in Houston, doesn't really make any difference. You're going to have put certain amount of equity, because if you said you'll take all the profit on this, and that's not enough money to come up with your equity, then you're going to take additional profit out of other facilities, and put in there. So, to me to isolate whether that profits in or out, doesn't really make any difference. It's from the standpoint that all of the companies listed there will come up with their equity share and continue to go forward with this project.

MCKINNON: One of the amendments that was offered yesterday, well you already answered that. You indicated the profits were really irrelevant. Ah, if you are prepared to comply with the original contract as you have indicated, and the Commissioner has indicated he doesn't intend to cancel the contract, I can't really understand why you would agree to an amendment that first of all is going to cut in half the supplies available to you, and secondly give the commissioner authority to veto this project even if you are acting in good faith and in compliance with the contract.

PARKER: Well, I think from the evidence of the last ten days up here this is not the most friendly and pleasurable atmosphere towards Alpetco, which we would hope could finally be achieved. Charter was not a part of the original Alpetco. We are part of it now. Our mode of operation is to become a good corporate citizen. We intend from a standpoint to do that. Some of those concessions

were made, which we thought were legitimate concerns, by members of the Legislature, to solve existing problems. They were concerned about in state refineries. One way in which we did that was to give up part of this crude oil. Now, we had rather have a facility that is smaller, but under a friendly atmosphere, rather than to try to fight this thing from now on, at every turn and every move, either at hearings or in the courts. And there is our basic reason.

McKINNON: My concern is that the reason is simply it eliminates the provisions that -- some people anyway are in the opinion that you're in breach of.

PARKER: Well, and again, I told you I was not an attorney. You heard the testimony of your Attorney General. We don't think that we are out of compliance.

McKINNON: Assuming there were no time frame problems, would you have any objection to amendments to the contract that would one, eliminate the confidentiality provision on your progress reports so that members of the Legislature could have access to them.

PARKER: Ah, my first inclination is to say probably I wouldn't, but I'd like to ask my attorney on that. And, again, one of the concerns that I've always had, and have expressed several times, we can't run, nor can anybody else run a business in a fishbowl. We're out there competing in a very, very competitive marketplace. And people that have testified here of their needs for proof, and their needs of

why we shouldn't be there, are our competitors. And they don't want us to be their competition against them. So, what you're saying is that if we tell you exactly everything we do, make it public, that's fine. But we don't get to see the other side of the coin. We don't get to see their business day by day. So, from that standpoint, I think that's an unfair request. We talked in reference to the use of the (unclear) our partner in that facility is Chevron, who would like to have crude oil in the State of Alaska. Tesoro is the largest stock holder of Commonwealth Oil Company, the one that's in bankruptcy that we're trying to buy. Now, all I'm trying to do, again, is come forward as Charter Oil Company, sincerely saying what we have negotiated here, we think is a better agreement for the State, as given State's some additional proof, and for that we're asking, let us build you a facility in the State of Alaska.

McKINNON: What (unclear)?

PARKER: It will vary. Right now the spot market price of crude oil, we probably wouldn't buy any of it. And the reason why you won't is that the price of crude in the spot market is worth more than the product it produces. And you can't build a big enough refinery or a big enough bulk to overcome that.

McKINNON: You don't currently purchase any (unclear) on the spot market?

PARKER: Very little.

McKINNON: What are your systems for supply (unclear)?

PARKER: Again, I'd rather not tell you from the standpoint our business, and how we do that, who we deal with, and what are contracts are. In some of those contracts are with foreign governments which we are obligated not to reveal the conditions of the contract.

McKINNON: I'm not asking you to reveal the conditions.

PARKER: Some of it's foreign, some of it's domestic.

McKINNON. I guess that answers my questions.

HURLBERT: I guess Joe covered part of it, I just, is is true, in its simplest form, that this amendment voids other major hoops you have to jump through, it sets up a new ball game based on the Commissioner's veto up or down on a ne facility.

PARKER: I don't know what you mean by hoops that we have to jump through.

HURLBERT: Benchmarks.

PARKER: The benchmark, the current benchmark that we're looking at is the July 18th benchmark.

HURLBERT: It knocks that off?

PARKER: It knocks that off.

HURLBERT: Basically, you don't have any measurability, other than the design of the facility.

PARKER: Well, it would be pretty hard for me to spend \$100 million if all of a sudden I am designing a new facility. I could go buy platinum or something, but I can't go out there now and take the orders that are being prepared to be issued, because they may not fit in the existing facility.

HURLBERT: You don't have to spend the \$100 million, right?

PARKER: I don't have to spend \$100 million if the amendment is approved.

Then

HURLBERT: ~~Can~~ you get a complete obligation free contract, basically, is that correct?

PARKER: I get, ah, to proceed with diligence between now and December 31, 1981, and I am willing to give up a 20-some odd year supply of crude oil. And you think the company, our size, that has been in the oil business for 25 years is willing to take 75,000 barrels a day, for 18 months, and throw away a long term food supply, is just unconceivable as far as I'm concerned.

HURLBERT: O.k., then what I stated is true, right? You have reduced it, (unclear) and it basically takes any obligation away from your part, other than then, you're saying you're going to design a facility, the commissioner can go up or down on it?

PARKER: That's right.

HURLBERT: Thank you.

MEEKINS: O.k., if there are no further questions. You have a closing statement?

PARKER: Could I make just one comment please? Again, I'm not an attorney, and neither am I a financier, but we've talked about the need of benchmarks in reference to financing, and they read an item where we were (unclear), there's also another paragraph that pertains to the financing, which is the first one was an 18 month benchmark, the second one is a 30-month

benchmark. And that 30-month benchmark says within 30 months after the effective date, execute definitive documents relating to the long term loan for the petrochemical facility. So I think it was contemplated that even though you have a commitment now, that you do not issue bonds and put the rate on those bonds, until the day before they hit the market. But when you start talking about that should be there, that's why that year was put in place. And we will meet that December 30, 1980 benchmark.

(Inaudible question).

PARKER: No, this is under the existing contract. So, there was a time frame of a year contemplated to put all of the final dotting of the i's and crossing of the t's under this contract relating to financing.

RANDOLPH: One of the questions, I think the Attorney General stated that basically you folks came to town because there was questions from the Legislature (unclear). Do you mean you'd rather prefer to have the existing contract or the amended one.

PARKER: I'd rather have the amended contract.

RANDOLPH: Why?

PARKER: Because I hope and sincerely believe that if I don't leave town doing that, I haven't succeeded in creating a friendlier atmosphere for us to proceed with this project.

RANDOLPH: Let's assume that you've made us all happy, and we're all friendly with the old contract, and there is no hints of problems. Then which contract would you prefer?

PARKER: I don't know.

RANDOLPH: Can you comply with the old contract?

PARKER: Yessir. But I guess the problem that I have with the old contract, there is a lot of verbage in there that's vague, and our compliance, and our definition within how we comply is probably not going to be the same thing as people said, that's not what was said, that's not what was agreed to. But it is what's in that contract. And that's why we were trying to come in with something that there isn't any question on. They are specific time flags. That gets back to the point, when you start talking, you must spend 1.458, and it's spent in various time frames. It says that you must commit or spend. And I don't want to argue with every word within that contract and what the intent was. I want to build a facility.

RANDOLPH: You are obviously reducing the size of the complex?

PARKER: Yes sir.

RANDOLPH: And, many of us think the intent of the contract (unclear) could argue about, but is the size of the complex that was contemplated in the old contract feasible, economically feasible, in Alaska; or is that one of (unclear)?

PARKER: Well, a 150,000 barrel a day facility, assuming there is crude supply to run through it, you do get the economics of size, there's no question about that. In today's oil industry the economics of size is just not as critical as it used to be. It used to be crude oil cost \$2 or \$3 per barrel, and the refinery spent 70/80¢. Now your crude oil costs you

\$30 a barrel, and your refinery expense is probably \$2. So you can see, size is not necessarily the determining factor as such. Ah, I, you know when you say, o.k., is it economically feasible, ah, it probably would be if we could size a facility and sell all the product in the state of Alaska, would be much more feasible than it would be to size it from the standpoint where we're forced in to have just the reverse, try to ship our product into another market. --

[Tape Change -- HFC 80-79, Side 1.]

-- I thank you very much.

MEEKINS: Mr. Love?

[End of Parker Testimony.]

The Bonding Proposal. The \$600 million bond issue to be made by the City of Valdez is to be underwritten by E.F. Hutton & Company. Obviously, until the bonds are in fact offered for sale and purchased, or commitments to purchase them have been made, there are no "commitments to lend or invest" within any possible interpretation of Subsection (d). Although the arrangement contemplates a purchase by E.F. Hutton of the bond issue, and a subsequent reoffering by Hutton of the bonds to the public, Hutton's commitment to purchase the bonds likewise does not suffice to comply with Subsection (d).

The terms of the undertaking by Hutton are set out in its letter of November 19, 1979 to Mayor Walker. Condition five to Hutton's undertaking is that the bonds receive a Standard & Poor's "investment grade rating". An investment grade rating will be issued by Standard & Poor's only in the event that it determines that the prospective revenues from the project will be sufficient to repay the bond holders, and Hutton's commitment is therefore, in effect, that it will purchase the bonds only if there is a public market for the bonds, which has not yet been determined.

Accordingly, the situation is no different, in substance, than if Alpetco were now proposing to float the bonds itself it an attempt to raise the necessary revenue, since the terms of the bonds provide that they will be paid for only out of the revenues of the project. Thus, there is no "commitment" on the part of Hutton to purchase the bonds and, in reality, Alpetco has produced nothing more than an offer to attempt to sell bonds.

Condition seven of Hutton's undertaking provides that its obligation is subject to an agreement by Alpetco to "maturity schedules, interest rates and other terms which are commercially reasonable given all the facts and circumstances prevailing at the time the Bonds are available for reoffering." [Emphasis added]. In other words, any obligation on Hutton's part to purchase the bonds would arise only at the time that Hutton attempted to reoffer them to the public, and only to the extent that Alpetco agrees to terms that are satisfactory to Hutton at that time, given the financial soundness of the project. Not only does this condition impose a conceptually impossible term, i.e., that the purchase price of the bonds is to be determined after their purchase, but it effectively permits Hutton to opt out of the entire arrangement by permitting it to impose onerous and impossible terms upon their purchase in the event that the project appears to be a high risk one. Thus, Hutton's "commitment" at this time can hardly be regarded as evidence of the project's financial feasibility or an assurance that Alpetco has the necessary financing to carry it through.

Finally, the second paragraph of Hutton's "commitment" letter provides that the price of the bonds to be paid by Hutton to the city of Valdez, and the price at which they

that it would later arrange for a loan. By the same token, it cannot satisfy the requirement through a statement by a third party that it will later obtain a loan for Alpetco. In either case, the requirement is satisfied if, and only if, a commitment to loan money is made on or before the benchmark date -- December 18, 1979.

Moreover, even the limited undertaking by Thyssen to arrange for financing through some other party is subject to the prior requirement that the balance of the 1.5 billion dollars be committed. Since this obligation is conditioned upon an event that has not occurred, it cannot logically be argued that its own "commitment" was made on or before the effective date, albeit that the "commitment" would not satisfy the requirement of Subsection (d) in any event.

Even if it could somehow be argued that even though Alpetco has not obtained a commitment to lend to or invest money in its project, it has nevertheless, by virtue of its arrangement with Thyssen, "cause[d] contractually bound third parties to obtain written commitments to lend or invest...." Clearly, the obvious import of this language is that the "contractually bound" third party must obtain the commitment within the benchmark period, not that it merely have undertaken to do so within the benchmark period.

However, even if an agreement with a third party made within the allowable time period to obtain a loan commitment after the deadline is sufficient, it is probable that Thyssen is not "contractually bound" to do so, since the essential terms and conditions of the loan, including interest rate, repayment schedule, security, and all of the ordinary and customary provisions of a loan agreement are not set out in Thyssen's letter. This fact caused Mr. Bonness to conclude that the "lack of specificity most likely would result in a court concluding the commitment is not enforceable against Thyssen." See page 9 of the memorandum to Commissioner LeResche dated February 21, 1980. Consequently, the Thyssen arrangement is deficient under subsection (d) in two respects, and it is highly questionable whether Thyssen is a "contractually bound" third party, even if the nature of its undertaking is otherwise sufficient.

Somehow, Mr. Bonness concluded that even though the undertaking of Thyssen was probably not enforceable, it was sufficient to comply with subsection (d). Insofar as the nature, as opposed to the enforceability, of Thyssen's undertaking is concerned, Mr. Bonness stated only that

"I believe that a commitment 'to arrange' is satisfaction of Alpetco's requirement 'to obtain' if the commitment is otherwise adequate. It is not surprising to find a lead company willing to take on the obligation to come up with the financing without knowing a year in advance exactly who will provide the funds."

CORRECTION

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

ALASKA STATE LEGISLATURE - HOUSE OF REPRESENTATIVES



REPRESENTATIVE JOE MCKINNON

POUCH V, JUNEAU, ALASKA 99811

April 28, 1980

MEMORANDUM

TO: Joe McKinnon
FROM: James Grandjean *J6*
RE: Alpetco Contract

The question addressed in this memorandum is whether or not Alpetco has complied with Section 10.2(3)(d) of its contract with the State. This provision provides, in substance, that the contract is terminated unless, within 18 months of the effective date (i.e., by December 18, 1979) Alpetco shall

"[o]btain or cause contractually bound third parties to obtain written commitments to lend or invest at least One Billion Five Hundred Million (\$1,500,000,000.00) in the aggregate for payment of Total Project Cost."

Alpetco proposes to meet this provision through (a) the issuance of \$600 million in tax exempt revenue bonds by the City of Valdez to be loaned to Alpetco; (b) a purported commitment by Thyssen to "arrange for" \$750 million in additional financing; and (c) \$350 million in direct financing by the member companies of the Alpetco consortium. Since the commitments by the Alpetco members are conditioned upon the other financing, the focus of this memorandum is on items (a) and (b) above.

In my view, a defensible argument that Alpetco's performance complies with Paragraph 10.2(3)(d) cannot be made. The manifest purpose and effect of subsection (d) is that Alpetco must, to retain its rights under the contract, obtain commitments from lenders or investors by December 18, 1979 that demonstrate the financial feasibility of the project. It can meet its obligations in one of two ways: through a commitment directly from the lender or investor to lend or invest the requisite amount, or through a commitment made to a "contractually bound" finder on behalf of Alpetco by the lender or investor.

Attachment 6/5/80

- 1079 -

The Bonding Proposal. The \$600 million bond issue to be made by the City of Valdez is to be underwritten by E.F. Hutton & Company. Obviously, until the bonds are in fact offered for sale and purchased, or commitments to purchase them have been made, there are no "commitments to lend or invest" within any possible interpretation of Subsection (d). Although the arrangement contemplates a purchase by E.F. Hutton of the bond issue, and a subsequent reoffering by Hutton of the bonds to the public, Hutton's commitment to purchase the bonds likewise does not suffice to comply with Subsection (d).

The terms of the undertaking by Hutton are set out in its letter of November 19, 1979 to Mayor Walker. Condition five to Hutton's undertaking is that the bonds receive a Standard & Poor's "investment grade rating". An investment grade rating will be issued by Standard & Poor's only in the event that it determines that the prospective revenues from the project will be sufficient to repay the bond holders, and Hutton's commitment is therefore, in effect, that it will purchase the bonds only if there is a public market for the bonds, which has not yet been determined.

Accordingly, the situation is no different, in substance, than if Alpetco were now proposing to float the bonds itself in an attempt to raise the necessary revenue, since the terms of the bonds provide that they will be paid for only out of the revenues of the project. Thus, there is no "commitment" on the part of Hutton to purchase the bonds and, in reality, Alpetco has produced nothing more than an offer to attempt to sell bonds.

Condition seven of Hutton's undertaking provides that its obligation is subject to an agreement by Alpetco to "maturity schedules, interest rates and other terms which are commercially reasonable given all the facts and circumstances prevailing at the time the Bonds are available for reoffering." [Emphasis added]. In other words, any obligation on Hutton's part to purchase the bonds would arise only at the time that Hutton attempted to reoffer them to the public, and only to the extent that Alpetco agrees to terms that are satisfactory to Hutton at that time, given the financial soundness of the project. Not only does this condition impose a conceptually impossible term, i.e., that the purchase price of the bonds is to be determined after their purchase, but it effectively permits Hutton to opt out of the entire arrangement by permitting it to impose onerous and impossible terms upon their purchase in the event that the project appears to be a high risk one. Thus, Hutton's "commitment" at this time can hardly be regarded as evidence of the project's financial feasibility or an assurance that Alpetco has the necessary financing to carry it through.

Finally, the second paragraph of Hutton's "commitment" letter provides that the price of the bonds to be paid by Hutton to the city of Valdez, and the price at which they

will be reoffered to the public, as well as other essential terms such as maturity dates, "will be fixed and agreed upon between E.F. Hutton and [Alpetco] at such times as the bonds are available for reoffering" and that the material terms will be subject to approval by the city. Once again, this provision obviously gives both the City of Valdez and E.F. Hutton the practical ability to opt out of the arrangement at any time, and negates any intention that the arrangement constitutes "commitments to lend or invest".

Moreover, the Hutton/Valdez arrangement is not an orthodox one. Normally, an underwriter agrees to purchase bonds and takes its chances on its ability to resell them on the open market, which it will hopefully do at a profit to itself. The arrangement contemplated in this case hedges Hutton's obligation to purchase the bonds and conditions it, for all practical purposes, upon a market for reoffering them, and pegs the terms of its purchase of the bonds upon market conditions that prevail at the time of reoffering.

In effect, Hutton's status as an underwriter, aside from administrative matters, does little or nothing to differentiate this arrangement from one in which the bonds were offered directly by Alpetco and/or the City of Valdez to the public. Therefore, since it is far from clear that the public will purchase the bonds, the arrangement cannot reasonably be regarded as a commitment to lend or invest at the present time.

The Thyssen Proposal. The second major component of Alpetco's purported compliance with the 1.5 billion dollar financing benchmark is its arrangement with Thyssen. Thyssen is a German corporation that is primarily in the construction business and which Alpetco expects to build the facility if it is built. Thyssen's "commitment" is set out in a letter dated December 7, 1979 to Alpetco, and a telegram dated December 17, 1979 that amplifies the December 7th letter. The letter provides that Thyssen does thereby "commit to arrange financing up to" \$750 million subject to Alpetco's acquisition of an additional \$750 million in financing. Definitive agreements for the financing "shall be entered into by December 18, 1980, on such terms and conditions as are customarily required for similar financings by lenders at such time. If such definitive agreements are not entered into by such date, we reserve the right to terminate our commitment hereunder without any liability on our part." The telegram substantially restates the above terms insofar as permanent financing is concerned.

On its face, this undertaking by Thyssen does not purport to be a commitment by it to lend or invest, nor a commitment by a third party to Thyssen to lend or invest to Alpetco. Clearly, Alpetco could not satisfy the requirement that it obtain a commitment to loan it money through a statement

that it would later arrange for a loan. By the same token, it cannot satisfy the requirement through a statement by a third party that it will later obtain a loan for Alpetco. In either case, the requirement is satisfied if, and only if, a commitment to loan money is made on or before the benchmark date -- December 18, 1979.

Moreover, even the limited undertaking by Thyssen to arrange for financing through some other party is subject to the prior requirement that the balance of the 1.5 billion dollars be committed. Since this obligation is conditioned upon an event that has not occurred, it cannot logically be argued that its own "commitment" was made on or before the effective date, albeit that the "commitment" would not satisfy the requirement of Subsection (d) in any event.

Even if it could somehow be argued that even though Alpetco has not obtained a commitment to lend to or invest money in its project, it has nevertheless, by virtue of its arrangement with Thyssen, "cause[d] contractually bound third parties to obtain written commitments to lend or invest...." Clearly, the obvious import of this language is that the "contractually bound" third party must obtain the commitment within the benchmark period, not that it merely have undertaken to do so within the benchmark period.

However, even if an agreement with a third party made within the allowable time period to obtain a loan commitment after the deadline is sufficient, it is probable that Thyssen is not "contractually bound" to do so, since the essential terms and conditions of the loan, including interest rate, repayment schedule, security, and all of the ordinary and customary provisions of a loan agreement are not set out in Thyssen's letter. This fact caused Mr. Bonness to conclude that the "lack of specificity most likely would result in a court concluding the commitment is not enforceable against Thyssen." See page 9 of the memorandum to Commissioner LeResche dated February 21, 1980. Consequently, the Thyssen arrangement is deficient under subsection (d) in two respects, and it is highly questionable whether Thyssen is a "contractually bound" third party, even if the nature of its undertaking is otherwise sufficient.

Somehow, Mr. Bonness concluded that even though the undertaking of Thyssen was probably not enforceable, it was sufficient to comply with subsection (d). Insofar as the nature, as opposed to the enforceability, of Thyssen's undertaking is concerned, Mr. Bonness stated only that

"I believe that a commitment 'to arrange' is satisfaction of Alpetco's requirement 'to obtain' if the commitment is otherwise adequate. It is not surprising to find a lead company willing to take on the obligation to come up with the financing without knowing a year in advance exactly who will provide the funds."

With all due respect, for the reasons set out above, I think this conclusion is erroneous. A "commitment" by a construction company of undetermined financial position to "arrange" that another party make a loan on unspecified terms, a "commitment" which is in itself of dubious enforceability, can hardly be equated with a commitment by a lender to lend money. The fact that Alpetco is having difficulty in obtaining financing and does not know at this point who its ultimate lenders will be (if any can be found) does not detract from this conclusion.

The precise purpose of subsection (d) was to ensure that the State not be committed to the Alpetco project unless Alpetco could demonstrate its feasibility by obtaining the necessary financing commitments within the 18-month period designated. It would be an exercise in totally circular reasoning to conclude that Alpetco's inability to obtain the financing relieves it from the obligation to do so, and that it is therefore entitled to the fruits of the contract without performing its own obligation.

Letter to Members of the
Royalty Oil and Gas Advisory Board
from
Robert E. LeResche, Chairman
and Commissioner of the Department of Natural Resources

At our meeting of Wednesday, June 4, 1980, we will have before us a proposed Second Amendment to the Alpetco contract. Events of the past months, and particularly the last few weeks, have necessitated this meeting. The reason for this communication is to further inform the members, prior to the meeting, of the circumstances surrounding this Amendment and matters I believe you should consider in the upcoming meeting. This letter is also to be considered as expressing at least part of any findings and conclusions that I may be required to make under AS 38, and as such is a public document, not to be considered confidential under the statutes and regulations of the Board.

I recognize that the proposed amendment is being consummated with great speed. But, unfortunately, there are no satisfactory alternatives available to the state. A review of the events of the past months will illustrate the present bind.

Under the existing contract, Alpetco submitted certain items by December 18, 1979. That December 18th benchmark, specifically 10.2(3), however, was open to varying interpretations. Unlike a statutory or regulatory review, my approval or disapproval was subject to contractual standards -- standards that apply to any individual business decision by private parties. Simply, there was a wide zone in which it was reasonable to conclude that Alpetco had complied with the December 18, 1979 benchmark. As I have stated publicly, although I concluded that Alpetco's submissions were near the lower edge of the zone of compliance, I did conclude that they had met the benchmark.

A significant number of legislators, however, disagreed. Within the past month, extensive, and sometimes bitter, public hearings were held by the legislature - hearings which received public attention not only locally, but also in wider circles including domestic and foreign financial markets. In addition, litigation was threatened to prevent Alpetco from receiving the oil on July 18th and to declare the contract terminated.

The result of this legislative oversight, which I am convinced was well-intended by the vast majority of legislators, was serious jeopardy of the ability of Alpetco to perform in the future. For example, one partner dropped

out, citing, in part, the legislative criticism. Also, the bond counsel for the proposed Valdez bond issue expressed doubts because of the rumored litigation. Overall, the business climate for Alpetco to perform was seriously jeopardized by the public criticism, which, if not alleviated, would continue to hurt the project.

I am convinced, however, that Alpetco under its present ownership has made tremendous efforts in good faith toward the existing project. I am persuaded that without the present climate Alpetco probably would have continued to meet the benchmarks and would have constructed the required facility.

I believe, however, that the present climate will not just go away. The feelings generated two years ago have continued unabated and, in fact, have grown even stronger. Although I believe that even under the present climate Alpetco could, and would, meet the \$100 million benchmarks so as to be entitled to receive 150,000 barrels per day on July 18, 1980, the longer-term future of the project is now in serious jeopardy. Future benchmarks will continue to raise controversy, financial circles will be made even more wary, and litigation, however well intended, would impossibly confuse the situation more -- with potentially disastrous results to all concerned.

Even under the circumstances, however, I was prepared to fully support the project if Alpetco was willing. But, as will be explained, Alpetco decided that it was in their and the project's best interest to attempt to alleviate the legislative concerns. In large part, as expressed to me, they desired to gain the support of the state and thereby build a conducive business atmosphere.

After their public hearings, the Joint Gas Pipeline Committee, on May 21, 1980, sent a letter to me concerning the project. Since this letter is the genesis of the Amendment you have before you, it is repeated here in its entirety:

May 21, 1980

Commissioner Robert LeResche
Department of Natural Resources

Dear Commissioner LeResche:

Recently the Legislature concluded a two-day oversight review of the Alpetco project, and Alpetco's compliance with the contractual intent and provisions. On the basis of this review, the Joint Gas Pipeline Committee has reached several conclusions:

(1) The project today differs markedly from the project as described to the Legislature in 1978, with Alaskans receiving substantially reduced benefits. We are not receiving in any way what we expected when the Legislature ratified the contract two years ago.

(2) In addition, it appears very doubtful that Alpetco has complied with its contractual obligations under arts. 10.2.3 and 4.2.1. It is clear that Alpetco has failed to comply with the intent of these provisions, and considerable evidence exists that they have failed to comply with the letter of the contract.

(3) Even as the project is described today, its economic viability remains very much in doubt, as is evidenced by Alaska Interstate's dropping out suddenly without recovering a significant capital investment.

(4) Existing instate refiners indicate both current and projected crude oil deficits which may curtail present operations and impede future expansion.

(5) The State risks not receiving full value, wise development and associated benefits from the in-kind use of its royalty oil.

These and other findings are presented at length in the Committee's report of May 15, 1980 (copy attached). Based on these findings, we have concluded that to allow Alpetco to take early delivery of royalty crude on an interim basis beginning July 18, 1980, is unacceptable.

We further conclude that the current contract between the State and Alpetco should be renegotiated. In renegotiation sessions between Alpetco and the State, the following areas should be discussed:

(1) Redefinition of the project, with the goal of establishing an instate facility which is economically sound and strong, not a "bootstrap" operation.

(2) No provisions for early taking of crude if that crude is to be exported from the [s]tate, unless existing instate refiners have sufficient crude supplies to maintain their current instate operations.

(3) Modification of the future options[sic] provisions so that Alpetco does not have an exclusive option to future sales of royalty oil.

(4) Insertion into the contractual procedures of adequate administrative review time of Alpetco's submissions for benchmark requirements, before compliance is approved or disapproved.

(5) Removal or redefinition of ambiguous language in the contract.

We would ask you to contact Alpetco officials immediately to open this renegotiation effort. With the shift in Alpetco ownership, we feel an obligation to Charter Oil to leave the door open for possible renegotiation of the contract as Charter had no role in creating the original expectations of a substantially different project and an apparently limited role in the subsequent defaults in contractual obligations. We would expect a reply from you within three days as to your evaluation of the possibility of opening the renegotiations and Alpetco's response to this request.

However, if there is no indication that renegotiations can be undertaken and if Charter continues to call for early delivery of royalty crude, we will, of necessity, take stronger action to minimize the risks to the State and to protect its resources.

Sincerely yours,

/s/

/s/

Mike Colletta
Co-Chairman

Bill Miles
Co-Chairman

Upon receipt, I transmitted the letter to Alpetco and requested their response.

As an aside, the present amendments address each of the five areas of concern, except that the option on future discoveries is substantially reduced, but not eliminated.

After receipt of the letter, and well within one week, key Alpetco officials, with full authority to act, came to Juneau. On the morning of May 27, Alpetco officials met in my office with the legislators, with myself and Avrum Gross present, to discuss the present situation. The legislators present at the initial meeting were Senators Sackett, Colletta and Kerttula, and Representatives Branson, Miles, Gardiner, ~~Malone~~ and Malone.

On the afternoon of May 27th, I, along with my staff, met with Alpetco officials. At that time, Alpetco made the following oral proposal to amend the contract.

First, Alpetco would reduce its ceiling volumes beginning July 18 and for the term of the contract (27 years) from 150,000 barrels per day to 100,000 barrels per day. In return for reducing Alpetco's supply, the State would pay Alpetco 35 million dollars, the present benchmarks would be eliminated, and Alpetco would come back in 24 months with a complete project ready to go with all financing, construction contracts, permits, etc. in place. At that time, the State would approve or disapprove the facility proposed. The remaining provisions of the contract, including the existing calls on future state royalty oil, would remain in place.

After oral negotiation, Alpetco presented in writing another, modified proposal which stated:

ALPETCO ROYALTY OIL CONTRACT

SALIENT FEATURES OF PROPOSED AMENDMENT

This document sets forth the salient features of a proposed amendment (the "Amendment") to the Agreement for Sale and Purchase of State Royalty Crude Oil (the "Agreement") dated February 22, 1978, between the State of Alaska and Alaska Petrochemical Company and its successor The Alpetco Company ("Alpetco"). The State and Alpetco propose the Amendment so as to satisfy various concerns over provisions in the Agreement and to clarify the obligations of the parties.

1. In-State Needs. The parties propose that the maximum volume of crude oil to be supplied by the State to Alpetco will be reduced from 150,000 barrels per day to 100,000 barrels per day so that the State can use the remaining barrels to satisfy the needs of in-state refiners, to develop other projects for the State and to generate additional revenues for the State. The reduction will require Alpetco to (a) forego future profitability associated with the additional crude oil, (b) forego economies of scale associated with a larger facility and (c) incur substantial costs due to the necessity of redesigning the facility to be constructed to process the crude oil. The reduction will provide the State crude oil which it can sell for in-state refining or in markets which may generate additional revenues for the State and which it can use to develop other projects in the State. The parties agree that Alpetco should receive \$30 million from the State to compensate it for the reduction of the supply obligation.

2. Economic Viability of Alpetco Facility.

The parties propose that Alpetco be required promptly to redesign the facility to accommodate the reduced supply of crude oil and to insure economic viability. In this regard the State desires that proof that the facility will be constructed and will be economically viable be provided to the State as a condition to the supply of State royalty crude oil to the facility. The Amendment, therefore, will provide for a substituted benchmark which requires Alpetco on or before December 31, 1981, to have in place and executed all financing documents, construction contracts, permits, and licenses necessary for the facility to be completed. At such time the State may, in its sole discretion, approve or disapprove the facility. Upon approval, Alpetco will be required to diligently proceed to construct the facility in compliance with the documents and contracts presented to the State, and the State will be required to continue the supply of crude oil for the remaining term of the Agreement. Disapproval will permit the State to terminate the Agreement. The supply of crude oil will commence on July 18, 1980, at the reduced quantity and will continue after the approval for the entire term of the Agreement unless there is earlier termination because of disapproval by the State. Alpetco shall provide the State on at least a quarterly basis with such documents and information as the State may reasonably request to enable the State to review the facility. In any event, Alpetco shall provide the State with all documentation by December 31, 1981, and the State shall use its best efforts to evaluate the facility within 60 days of submission by Alpetco.

3. Commitment of Undiscovered Reserves.

The parties propose that provisions of the Agreement which refer to undiscovered crude oil reserves of the State be clarified to the extent necessary that the future discoveries are available to Alpetco only to maintain the supply to Alpetco and to provide Alpetco with the flexibility in Article 2.3 of the Agreement.

After further intense discussion, both before and after the written document was presented, Alpetco agreed to modify their above proposal as follows. First, Alpetco would initially lift only 75,000 barrels a day until approval or disapproval of the proposed facility. Upon approval, the amount would increase to 100,000 barrels per day. Second, the 24 month period was reduced to the period ending December 31, 1981 (about 19 months). Third, the cash reimbursement was reduced to \$20 million. Fourth, the call on future royalties was reduced from 90% to 60% for "cheaper" oil, and 70% to 50% for "other future" royalty oil.

After that meeting, I met with key legislators and discussed the revised Alpetco offer. I asked them to respond to me as soon as possible, which response occurred on the morning of May 28, 1980.

The legislators, through Representative Miles, asked for some basic changes. They requested that no money would be reimbursed. In addition two contracts would be signed. The first contract would be for a period of 48 months for 75,000 barrels per day with a December 31, 1981 benchmark for submission and approval of the redesigned facility. The second contract would be for 100,000 barrels per day beginning after the expiration of the first contract, and be conditioned upon the facility being in place and operating.

I then met with Alpetco, explained the legislators' position and asked for their response. The next meeting occurred on the afternoon of May 28th, where Alpetco returned to their modified offer except that they reduced their cash request from \$20 million to \$5 million.

After reviewing both proposals, I called both sides to my office and stated that unless both sides were agreeable to what I considered a reasonable amendment that protected the State, there would be no amendment at all and the contract as it presently existed would remain in force. The amendment I proposed contained previous features as well as other items.

The terms that I presented at that time to both parties, for their acceptance or rejection (and if rejected the existing contract to remain in force), were as follows. First, there would only be one contract. The reasons given to me for having two contracts appeared, in my analysis, to be simply cosmetic. Further, I believe the current concerns expressed by the legislators concerning a desire to assure that a facility would be constructed in order for Alpetco to continue to receive 100,000 barrels per day could be accomplished in one contract. In addition, I wanted all the provisions of the present contract that were not amended to remain in force, which would have been difficult to accomplish in two

contracts. Finally, I was worried that the execution of two new contracts might affect the waiver of supplier/purchaser relationship granted by the Department of Energy in 1978.

Second, Alpetco would receive 75,000 barrels a day of crude oil beginning on July 18, 1980 until December 31, 1981. I believe that under the circumstances of the present situation, Alpetco would have been able to lift 150,000 barrels a day of oil for at least five months, and, in all probability, for a considerable period of time in excess of five months. Instead of 150,000 barrels for a period of five to twelve months, and possibly longer, Alpetco would, under the new amendment, be entitled to 75,000 barrels for nineteen months.

Third, on or before December 31, 1981, Alpetco was to submit complete plans for a 100,000 barrel per day facility; to obtain all financing necessary to pay for the construction of the facility, including signed definitive documents relating to the loan of funds; to enter into all construction contracts necessary to provide for the construction of the facility; to provide a construction schedule and completion date for the construction of the facility; and to obtain all material permits and licenses relating to the facility necessary for its completion. At that time, December 31, 1981, if such documents were not submitted, the Commissioner would have the absolute right to terminate.

Fourth, even if all documents were submitted, the State would have the absolute right to approve or disapprove the proposed facility. In addition, I required that the approval authority was not limited by the reasonableness standard of the present article 26.7. In other words, that the approval or disapproval could be arbitrary and that Alpetco would have no recourse from any decision that might be made concerning their proposed facility at that time. If the facility were disapproved, Alpetco's right to take oil would terminate.

Fifth, there would be a specific requirement of due diligence both in Alpetco's activities towards accomplishing all that was required between now and December 31, 1981, and also to apply to the subsequent construction, if approval was given. The present contract contains a provision allowing the state to have complete access to all documents, records and other materials of Alpetco. That provision will remain unchanged. In addition, one of the reasons for requesting a construction timetable and completion date, along with complete loan documents, including drawdown schedules and construction contracts, was to allow the State, in monitoring the construction of the facility, to have a standard by which to measure the due diligence of Alpetco.

Sixth, Alpetco would be entitled to receive 100,000 barrels per day or the design capacity of the proposed facility, following the approval of the plans submitted December 31, 1981. My main concern was that the production curve at Prudhoe Bay will decline rapidly beginning approximately 1988-1992. Alpetco stated that their intention was to take the 100,000 barrels per day and "time-trade" (forward exchange) the oil so as to receive oil at a later date when the Prudhoe production curve was declining. Thus, the proposed facility, when constructed, could run at full capacity for a longer period of time, thus improving its economics and benefits to the state. For the same reason, the 85% provision of the present contract remained in force, since that would also give approximately one to two years more deliveries at 100,000 barrels per day when Prudhoe production declines.

Seventh, Alpetco's call on future royalties would be reduced from 90% to 60% for "cheaper oil" and from 70% to 50% for "other oil," both of which were limited by the ceiling of 100,000 barrels per day.

Eighth, there would be no payment by the State to Alpetco.

Ninth, there would be some time certain by which Alpetco would have completed the facility, or the state would have the unilateral option to terminate.

Finally, I required that the amendment must be consummated this legislative session. The main reason is that any delays would severely jeopardize Alpetco's continued performance under the existing agreement. On June 18, 1980 Alpetco must expend or commit to expend \$100,000,000. By July 18, 1980, prior to receiving the oil, Alpetco must have actually expended \$100,000,000. Any delay beyond this session would eliminate any possibility of timely compliance under the existing contract. Further, one of the major financing commitments obtained by Alpetco is expressly conditioned upon Alpetco being able to receive oil on or before July 18, 1980. For these, and other reasons, delay beyond this session was unacceptable.

I then stated that because of the short time frame available, I required that both parties accept those terms by 9:00 a.m. the next day or I would break off all negotiations and demand compliance under the existing contract.

Later that evening I had a meeting with Representative Miles, after Representative Miles and Dudley Parker (from Alpetco) had apparently discussed my terms.

Miles indicated that he, and he thought the Legislature, and Alpetco, would be agreeable if two changes were made. One change was to delay the increase from 75,000 to 100,000 barrels until the facility was complete and actually processing oil. In exchange, Alpetco's call on future "other" oil would be raised to 85% of future royalty supplies. I stated that the increase in Alpetco's call on future supplies to 85% was unacceptable, but that I would consider delaying the increase from 75,000 barrels per day until actual startup. After some discussion, I stated that if both Alpetco and the Legislature were agreeable to that change, it would be acceptable to me.

Late that night, Representative Miles reported back to me that he had reviewed the terms with concerned legislators and that the terms were acceptable. Alpetco also indicated their acceptance. Staff for all parties worked throughout the night drafting the language for the amendments, which was reviewed by all parties the next morning. The result is the Amendment before you today.

After review of the proposal, it appeared that there was agreement. Unfortunately, during the afternoon of Friday, May 30th, a misunderstanding threatened the Amendment. The Amendment provides that in order to receive 100,000 barrels per day, the facility must be complete and

processing crude oil. The legislators assumed that this also meant that in order to continue to receive 100,000 barrels per day, the facility must continue to process the oil. This is not in the Amendment, for a number of reasons, two of which are as follows. First, "down time," both normal and exceptional, will occur. But second, and more important, the crude oil delivered will probably be used as security for the loans to finance the refinery. The lenders will demand that they, through Alpetco, be able to take the oil if the facility goes bankrupt or is destroyed. But if Alpetco cannot take oil if the facility is shut down, then the lenders will be unable to secure the loans. This misunderstanding delayed legislative acceptance another day, until the morning of Saturday, May 31. At that time, the contract Amendment was signed. The Governor then submitted the Amendments to the Legislature for its approval. Public hearings were held on the amendment before the House Resources Committee late that afternoon. The rest of the legislative process between May 31 and today is a matter of public record and will not be repeated here.

On Saturday afternoon, I had hand delivered to Board members the documents and a summary of the proposed Amendment.

What is before the Board is an Amendment to Alpetco's existing contract dated February 22, 1978. The Amendment is being submitted for approval pursuant to Article XXII of the Alpetco contract. It is not, therefore, a sale, exchange, or other disposition of crude oil within the meaning of AS 38. AS 38 contemplates and intends that where the State is giving up a right to deal with or otherwise initially obligate a quantity of royalty oil, approval is required by both the Royalty Board and the Legislature. Here, however, oil has already been committed under an existing contract and, under the Amendment, the State is gaining quantities of oil to be sold, exchanged, or otherwise disposed of in the future.

Approval for amending an existing contract is not required by the statute. For example, AS 38.06.050(c) speaks of competitive bidding for the dispositions covered by AS 38.06. It is impossible, however, to competitively amend an existing contract since only the original buyer qualifies for the amendment. Therefore, the Board is meeting as a contract requirement, not pursuant to a statute.

In evaluating the amendment, however, it is appropriate for the Board to consider the various statutory criteria and adopt resolutions as if the amendment were a "sale" within the meaning of AS 38.06.050. This will at least focus the discussion of the proposed amendment.

Discussion of Criteria Contained in AS 38.06.070(a).

AS 38.06.070(a) sets forth considerations that the Board shall have in mind when it reviews initial proposals for the sale of royalty oil. Subsection(1) states that the Board shall consider "the revenue needs and projected fiscal condition of the State." The proposed sale, in my belief, will have minor impact, if any, upon the state's revenue needs. In essence, the state is reducing its obligation to deliver royalty oil to a buyer. The question is whether or not such a reduced obligation will impact upon the state's revenue needs. As a general matter, the state is projected to have tremendous cash surpluses for at least the remainder of this decade. Further, the sale to Alpetco, in essence, required that they pay us for oil at the same price that we would have received for the oil from the producers if we would have taken in value. Ultimately, the amount to be received will be the same whether we sell this oil to Alpetco or whether we retain the oil in value. Further, since at least 75,000 barrels a day will be released for approximately four years, and 50,000 barrels a day when the facility comes on stream, we always have the option of disposing of the remaining oil if we can get better terms than we would by taking in value or under a sale to Alpetco. There is, however, an affect on the interim payments to be made from

Alpetco to the State. The method of calculating royalty in value at pump station number 1 is presently a matter of litigation. During the course of litigation, Alpetco has agreed to pay under Exhibit B of their contract, which represents a favorable result of the litigation. At the present time, the producers are not obligated to pay us the value at pump station number 1 during the lawsuit -- thus, for the interim, Alpetco will be paying the State a higher price than would otherwise have been received had we taken the oil in value. Of course, when litigation is concluded, refunds will be made if that result occurs; so ultimately, the price received will be the same as the true in-value price. The effect of this interim payment is problematic, and is in any case minor considering the present and projected surpluses in the state budget.

AS 38.06.070(a)(2) provides that the Board shall consider "the existence and extent of present and projected local and regional needs for oil and gas products and by-products, the effect of state or federal commodity allocation requirements which might be applicable to those products and by-products, and the priorities among competing needs." Under the proposed amendment, we are gaining the flexibility to deal with an additional 50,000 to 75,000 barrels per day.

AS 38.06.070(a) (4) provides that the Board shall consider "the projected social impacts of the transaction." Subsection (5) requires consideration of "the projected additional costs and responsibilities which could be imposed upon the state and affected political subdivisions by development related to the transaction;" subsection (6) requires a consideration of "the existence of specific local or regional labor or consumption markets or both which should be met by the transaction;" subsection (7) provides for consideration of "the projected positive and negative environmental effects related to the transaction;" and (8) provides that the board should consider "the projected effects of the proposed transaction upon existing private commercial enterprise and patterns of investment." In considering all of these criteria, the salient feature of the new amendment is that the facility will be down-sized, and that the state has the arbitrary right to approve or disapprove all the plans submitted to the state on December 31, 1981. Thus, at this time, it would be expected that both negative and positive impacts will be decreased to some extent by the downsizing of the facility. But it should be emphasized that if that downsizing does not maximize benefits to the state while limiting possible detrimental effects, the state again has the arbitrary right to cancel the project.

CORRECTION

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

Testimony before the recent legislative hearings indicated that there might be some additional in-state needs that are not presently being met. The 50,000 to 75,000 barrels per day freed by the proposed amendment would be available to satisfy such in-state needs for oil and gas products and by-products if in fact such needs are found to exist. Further, I believe that this Amendment will make it more likely that the facility will be built, thus making substantially more products available for in-state use.

AS 38.06.070(a)(3) provides that the Board shall consider "the desirability of localized capital investment, increased payroll, secondary development and other possible effects of the sale, exchange or other disposition of oil and gas or both." Both the old and present Agreement contemplate that the site of the plant will be at Valdez. Of course, under the existing agreement, there is a specific commitment to expend \$1.5 billion, which may or may not be achieved under the Amendment. However, as explained previously, under the present circumstances, that greater investment is very problematic. It should also be noted that the state has the arbitrary right to cancel the agreement in 1982 if it believes that the down-sized refinery is not in the state's best interest.

AS 38.06.070(a)(4) provides that the Board shall consider "the projected social impacts of the transaction." Subsection (5) requires consideration of "the projected additional costs and responsibilities which could be imposed upon the state and affected political subdivisions by development related to the transaction;" subsection (6) requires a consideration of "the existence of specific local or regional labor or consumption markets or both which should be met by the transaction;" subsection (7) provides for consideration of "the projected positive and negative environmental effects related to the transaction;" and (8) provides that the board should consider "the projected effects of the proposed transaction upon existing private commercial enterprise and patterns of investment." In considering all of these criteria, the salient feature of the new amendment is that the facility will be down-sized, and that the state has the arbitrary right to approve or disapprove all the plans submitted to the state on December 31, 1981. Thus, at this time, it would be expected that both negative and positive impacts will be decreased to some extent by the downsizing of the facility. But it should be emphasized that if that downsizing does not maximize benefits to the state while limiting possible detrimental effects, the state again has the arbitrary right to cancel the project.

Thus any detailed consideration of the projected impacts of the transaction are at best problematic; however, the state has the greatest possible protection in its complete freedom to approve or disapprove the facility when its exact nature becomes known.

Waiver of Competitive Bid.

The document you will be considering is, as the title implies, an amendment to the existing Alpetco contract. It reduces the quantity of oil to be sold to Alpetco and reduces the size and requirements for the facility that Alpetco is required to build in Valdez. The oil Alpetco would receive under the proposed amendment is the same oil it would receive under the present contract. I do not believe that the proposed amendment constitutes a sale, exchange or other disposition for purposes of the requirements of AS 38.05.183 or AS 38.06 and therefore I do not believe that I need make a finding waiving competitive bidding even though there has been no competitive bid process, or that I need to determine that the oil sold under the amended contract is surplus to intrastate domestic and industrial needs even though some of the oil is to be exported from the state. If, as others may believe, those determinations should be made with regard to the amendment, I offer the following reasons for the determinations.

The reasons the competitive bidding was waived in the existing contract was basically that the criteria set out in AS 38.06.070, upon which award of the contract was based, are very complex criteria. If absolutes, mainly price, are the only considerations, which by definition they are in a competitive bid situation, none of the criteria in AS 38.06.070 could be compared by the Board in a development contract such as this. Thus, a sale or disposition of this type which takes into account the .070 criteria cannot be done by competitive bid. It therefore was determined that it was in the best interest of the state not to require competitive bids for the original contract. Those reasons still apply fully.

In the particular situation in which we find ourselves regarding this amendment, competitive bidding is precluded by the fact that there is only one entity which could bid on oil which is already committed. That entity is, of course, the party to whom the oil is presently committed. Therefore, with regard to the oil covered by the amendment, there is no competition possible.

Not Surplus to In-state Needs.

As I have stated above, I do not believe that a finding that the oil which would be sold to Alpetco under the amended contract and exported by Alpetco from the state is surplus to intrastate domestic and industrial needs.

That finding was made by me for the original contract and was approved by the Royalty Board. If the finding were to be made again at this time, I believe it could be supported even more strongly with regard to this amended contract as it would for the original. The finding was based primarily on a report entitled "Oil and Gas Consumption in Alaska 1976-2000." The conclusions reached in that report are still applicable.

In addition, we have a very good idea what the projected intrastate domestic and industrial needs will be from testimony of instate refiners given at the April 28, 1980 hearing conducted by the Joint Gas Pipeline Committee of the Alaska State Legislature. These refiners testified that they expected shortfalls in crude oil supplies to their refineries both presently and in the coming years.

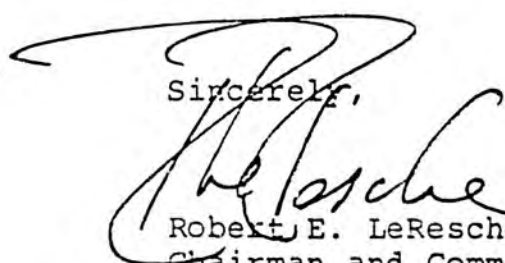
The amended contract allows the state to have oil which it may use to fulfill the requirements of current instate refiners if it so chooses while at the same time fully supplying a downsized processing facility in Valdez. It should be emphasized that these 75,000 barrels per day are supplies which, under the present contract, are otherwise unavailable for in-state disposition. Since the 75,000 barrels (later, 50,000 barrels) which will be returned to the state can be used to fulfill the needs of current in-state

refiners, the 75,000 barrels which will be exported from the state during the period prior to completion of the Valdez facility is surplus to intrastate domestic and industrial needs.

I realize that the time-frame for consideration of this Amendment is an imposition on most members, and I sincerely regret it. Circumstances, however, make it absolutely necessary and I sincerely appreciate your continued forbearance and contributions to the State beyond the call of duty.

Dated June 4, 1980.

Sincerely,



Robert E. LeResche
Chairman and Commissioner of
the Department of Natural
Resources

REL:cb:RMM

SECOND AMENDMENT

Dated May 30, 1980

to the

AGREEMENT FOR THE SALE AND
PURCHASE OF STATE ROYALTY OIL

THIS SECOND AMENDMENT entered into as of the 30th day of May, 1980, by and between THE STATE OF ALASKA, hereinafter called the "Seller," acting by and through its Commissioner of Natural Resources, and THE ALPETCO COMPANY, a Florida general partnership, hereinafter called the "Buyer", and being the Second Amendment to the Agreement between Seller and Alaska Petrochemical Company entered into February 22, 1978, and assigned by Alaska Petrochemical Company to Buyer by an assignment executed December 13, 1979, and approved by Seller on February 4, 1980.

WITNESSETH:

WHEREAS, an Agreement for the Sale and Purchase of State Royalty Oil was duly executed on February 22, 1978, was amended on May 17, 1978, and was assigned to Buyer pursuant to an assignment executed December 13, 1979, and approved by Seller on February 4, 1980 (the "Agreement"); and

WHEREAS, the Agreement may be amended under Article XXII thereof; and

WHEREAS, Seller and Buyer desire to reduce the amount of crude oil that Seller must sell to Buyer under the Agreement; and

WHEREAS, Seller and Buyer desire that certain provisions of the Agreement be amended to clarify the obligations of Seller and Buyer thereunder;

NOW THEREFORE, in consideration of the mutual agreements and undertakings provided herein, Seller and Buyer hereby agree as follows:

1. The first Whereas clause on page 1 of the Agreement is hereby amended to read in its entirety as follows:

"WHEREAS, it is in the mutual best interests of Seller and Buyer that Buyer construct and operate a facility in Alaska to process oil sold hereunder, said facility to have the capacity to process approximately 100,000 barrels of crude oil per stream day and to produce at least approximately 30,000 barrels per day of energy fuels for in-state distribution and sale; and"

2. Article I is hereby amended by deleting Articles 1.12, 1.13 and 1.14, renumbering Articles 1.6 through 1.11 to be Articles 1.7 through 1.12 and adding the following new Article 1.6:

"1.6 'Facility' shall have the meaning defined in Article 4.2.1."

3. Each reference in the Agreement to "Petrochemical Facility" is hereby changed to "Facility."

4. Article 2.1 is hereby amended and restated in its entirety to read as follows:

"2.1 Sale of Prudhoe Bay Royalty

Oil. Subject to the terms and conditions hereinafter provided, and subject to the prior obligations of Seller to deliver 5,000 barrels of crude oil per day under its contract with Golden Valley Electric Association, Inc. ("Golden Valley"), for the term and in the quantity now stated therein, Seller agrees to sell to Buyer, and Buyer agrees to buy from Seller, on the average, determined on an annual basis, approximately 75,000 barrels per day from Seller's royalty oil out of the crude oil production removed or sold from the Leases which the Seller has the right to take and is available to the Seller for taking in kind. However, in the event that 75,000 barrels per day of royalty oil is greater than 85% of Seller's royalty oil, then Seller shall be obligated to deliver said lesser quantity. Seller shall nominate that

percentage of its royalty oil from the Leases which shall equal approximately 75,000 barrels per day on the average, except as provided in the preceding sentence. If total production from the Leases changes such that Seller's nomination results in Seller receiving from the Leases less than 75,000 barrels per day determined on an annual basis, then Seller, as expeditiously as possible (and subject to the terms of the Prudhoe Bay Unit Agreement if applicable), shall adjust its nomination to equal 75,000 barrels per day (except that Seller shall not be required to nominate more than 85% of Seller's royalty oil for sale to Buyer). Subject to the further provisions of this Article 2.1, Seller reserves the right to use or dispose of the remaining royalty oil. After the completion of the Facility, Seller's obligations to Golden Valley, if any, shall first be satisfied out of the royalty oil from the Leases not being sold to Buyer hereunder. In addition to the crude oil deliverable under the other provisions of this Article 2.1,

Buyer shall also possess the option to purchase an additional five percent (5%) of the total amount of Seller's royalty oil out of the Leases:

(a) in the event Seller enters into a contract with North Pole Refining Company ("NPR") granting NPR an option to purchase part or all of the fifteen percent (15%) portion of the oil out of the Leases not sold to Buyer under other provisions of this Article 2.1 and NPR does not exercise its option in full to purchase the oil on which it has an option, but Buyer's option to purchase shall extend only to the purchase of that quantity of oil from time to time not purchased by NPR: or

(b) in the event Seller does not enter into or have in effect a contract with NPR as recited in Article 2.1(a).

In the event it exercises its option under Article 2.1(a) or 2.1(b) above, Buyer agrees to give Seller an additional thirty (30) days notice of any

nominations under this Article in addition to the time for notice specified in the Prudhoe Bay Unit Agreement. In the event under any agreement with NPR Seller obtains a right to purchase from NPR any oil returned to the Trans Alaska Pipeline System by NPR, Seller shall assign all such rights to Buyer for the term of such NPR agreement.

Seller represents to Buyer that it has obtained sufficient advance written consents to termination and an agreement from Lessees (which to Seller's knowledge has been performed) to require similar consents from all subsequent purchasers agreeing to waive or terminate any supplier-purchaser relationship as to sufficient quantities of Seller's royalty crude oil out of the Leases to enable Seller to perform its delivery obligations under this Agreement.

Notwithstanding the foregoing provisions of this Article 2.1, Seller shall sell to Buyer approximately 100,000 barrels per day on the average, determined on an annual basis, after Buyer has begun processing crude oil in

the Facility, except that if 85% of Seller's royalty oil is less than 100,000 barrels per day then Seller shall be obligated to sell to Buyer only said lesser amount."

5. Article 2.2 is hereby amended and restated in its entirety to read as follows:

"2.2 Initiation of First Delivery.

Buyer shall take delivery of crude oil under this Agreement beginning July 18, 1980. Buyer agrees that it shall fully comply with its obligations under Article 26.6."

6. Article 2.3 is hereby amended by replacing the words "ninety percent (90%)" in the first sentence thereof with the words "sixty percent (60%)," replacing the words "ten percent (10%)" in the fourth sentence thereof with the words "forty percent (40%)" and replacing the number "150,000" with the number "100,000" in the third from the last sentence thereof.

7. Article 2.4 is hereby amended by replacing the numbers "145,000" and "150,000" with the numbers "95,000" and "100,000," respectively, in each place that they appear in such Article, and replacing the words "seventy percent (70%)" in the first and third sentences thereof with the words "fifty percent (50%)."

8. Article 2.5 is hereby amended by replacing the number "150,000" with the words "75,000 or 100,000, as the case may be," in the first sentence thereof.

9. Article 2.6 is hereby amended by replacing the words "on or prior to" in the third line thereof with the words "commencing on" and inserting after the words "Date of First Delivery" in the fourth line thereof the following words:

", and shall maintain at all times
thereafter,"

10. Article 2.7 is hereby amended and restated to read in its entirety as follows:

"2.7 Reduction of Quantity of Oil Deliverable to Buyer. Notwithstanding any provision of Article II requiring Seller to deliver to Buyer quantities of crude oil up to 100,000 barrels per day, in the event that on or before December 31, 1985, the designed capacity of the Facility is less than 100,000 barrels per stream day, the maximum quantities deliverable by Seller for the remaining term of this Agreement shall be reduced to that quantity equal to the designed capacity of the Facility at such time. Coincident with such reduction, the figure '95,000 barrels' appearing

several places in Article 2.4 shall be reduced by a like amount."

11. A new Article 2.8 is hereby added as follows:

"2.8 Nomination of Crude Oil. It is expressly recognized that as to royalty oil out of the Leases, and perhaps to royalty oil on future production, the Seller may only nominate its royalty oil by percentage, and not by a fixed amount of barrels. Therefore, whenever the Seller is to deliver, and Buyer is to receive, a fixed number of barrels, either "75,000" or "100,000", it is understood that Seller can only nominate a percentage of its royalty share that, upon the best information available to Seller, will equate approximately to the fixed number of barrels to be delivered. For example, it is recognized that fluctuation in production may sometimes cause the existing percentage nomination to differ substantially from the fixed number of barrels required herein. If there is a significant change in production, Seller shall be obligated only to increase or decrease its royalty percentage pursuant to Lease

or Prudhoe Bay Unit procedures so as to again approximately equate to the fixed number of barrels required. In addition, and as another example, it is also expected that temporary increases or decreases in production will result in deliveries hereunder to fluctuate around the fixed number of barrels set forth herein."

12. Article 4.2.1 is hereby amended and restated in its entirety to read as follows:

"4.2.1 Construction Obligations.

In consideration of the obligations assumed by each party herein, upon approval by the Commissioner pursuant to Article 10.2 hereof Buyer will proceed with diligence to construct, start up and thereafter initiate operation of a facility in the State of Alaska with capacity to process approximately 100,000 barrels of crude oil per stream day substantially in accordance with the schedule presented to the Commissioner pursuant to Article 10.2 hereof. Such facility shall include substantially all of the facilities approved by the Commissioner pursuant to Article 10.2

hereof. Incidental changes and modifications of the facilities prior to start-up may be made without the consent of the Commissioner, but any major changes in the facilities prior to start-up must be approved by the Commissioner. Final process configuration and production rates from the facility will be determined by (i) marketing considerations and (ii) process optimization of the overall facility design to produce the desired products in the most effective manner. Variations in design, configuration and process optimization will occur throughout the anticipated life of the facility. Such facilities shall be hereinafter referred to as the 'Facility.'"

13. Article 4.2.3 is hereby amended and restated in its entirety to read as follows:

"4.2.3 Progress Reports by Buyer.

From the date of the Second Amendment and until December 31, 1981 (and thereafter until the start-up of the Facility if the Commissioner gives his approval pursuant to Article 10.2 hereof) on or before the twentieth (20th) day after

each calendar quarter, Buyer shall furnish the Commissioner a written progress report as of the end of such calendar quarter describing its progress on the engineering, design and construction activities of Buyer with respect to the Facility, progress in the marketing of the products therefrom and the proposed financings. Such reports, or portions thereof, shall be held confidential as requested by Buyer to the extent permitted by law."

14. Article 4.4 is hereby amended by deleting the words "fuels and petrochemical" from the fourth sentence thereof.

15. Article 10.2 is hereby amended and restated in its entirety to read as follows:

"10.2 Termination by Seller.

Notwithstanding anything else to the contrary in this Agreement, this Agreement shall terminate and Seller shall have no further obligation to deliver any further crude oil to Buyer (i) upon failure of Buyer to proceed with reasonable diligence pursuant to the provisions of Article 4.2.1 or Article 10.2.1 or

(ii) 30 days after the disapproval by the Commissioner of the Facility pursuant to the provisions of this Article 10.2.2, except that Buyer pursuant to Article 14.2 shall have the obligation to purchase royalty oil if Seller elects to sell such oil to Buyer.

10.2.1 Buyer's Obligations.

Buyer promptly after the date of the Second Amendment shall proceed with reasonable diligence to do the following:

(a) configure, engineer and design the Facility, which shall have a capacity to process at least 100,000 barrels of crude oil per stream day;

(b) obtain all financing necessary to pay for the construction of the Facility including entering into all definitive documents relating to the loan of funds that are necessary to finance the costs of construction of the Facility;

(c) enter into all construction contracts that