

November 30, 1999

The Honorable Tony Knowles, Governor
State of Alaska
State Capitol, 3rd Floor
Juneau, Alaska 99811

Dear Governor Knowles:

I write to report the results of the public comment and hearing process on the draft Charter for the Development of the North Slope ("draft Charter") and to suggest certain changes to the draft Charter in response to that process. We heard a broad cross-section of Alaskan views on issues of utmost importance to the State and to its economic future. While there is no solution that all Alaskans would embrace, my fellow cabinet members on the merger review team and I believe that the draft Charter, with our recommended changes, will achieve the two objectives you established at the outset of this process: increased competition in Alaska's oil patch and an enhanced corporate commitment by BP to Alaskans.

This report is divided into two parts. First, to provide appropriate context, the report will set forth the path that we traveled from late March when the merger was announced through the negotiation of the draft Charter and ending with the public comment process. Second, the report will summarize the critical comments that were received and recommend changes to the Charter. At your direction and with your involvement, negotiations with BP Amoco have been ongoing during and after the public comment period.

This report recommends the following substantive changes to the Charter. First, I believe the Charter provisions related to the environment should be revised. The proposed changes would establish (1) a floor, not a ceiling, of \$10 million to be spent cleaning up orphan sites, (2) a cap of an extra \$5 million to be spent for extra orphan site clean-up, spill research, or corrosion experts as requested by the Alaska Department of Environmental Conservation Commissioner, (3) an agreement to repudiate any trade association effort to weaken Oil Pollution Act of 1990 (OPA 90) standards, (4) continued support for the ship escort response vessel system in Prince William Sound, (5) a requirement for BP to report annually on environmental issues, and (6) a reconsideration of the enforceability of the environmental commitments.

Second, the focus of the gas commercialization provision in the draft Charter should be changed. Specifically, the price target provision should be removed and replaced with a commitment to nondiscriminatory open negotiations with prospective project sponsors for the purpose of making available sufficient gas to support a qualified treatment and transmission project. In addition, as specified below, other language of the draft Charter should be clarified to better reflect the parties' intent.

I. The State's Review of the Merger and Negotiation of the Charter
A. The Review Process

On April 1, 1999, after receiving the news of BP Amoco, p.l.c.'s proposed acquisition of the Atlantic Richfield Company, you announced the appointment of a cabinet-level team to review the merger and its consequences for Alaskans. Named to the review team were Commissioner

of Natural Resources John Shively, Commissioner of Revenue Wilson Condon, Special Counsel to the Governor John Katz, who also serves as director of the State's Washington, D.C., office, and me as Attorney General.

You stated your concern that the proposed merger "could have significant impacts on Alaska jobs and families" but expressed the hope that the merger would present an "opportunity to build on the accomplishments we have made with industry over the past four years." In your remarks, you announced four principles for evaluation of the merger. The merger must:

1. continue to strengthen Alaska's economy through Alaska hire, use of Alaska businesses, and support of community organizations and causes;
2. continue improvements for environmental protection and the safe transportation of oil;
3. maintain competitive opportunities for other companies to enter the oil industry in Alaska; and
4. continue to provide a stable source of revenues to the State of Alaska.

You asked your cabinet team to evaluate the impact of the proposed merger in six areas:

1. valuation of North Slope crude;
2. marine transportation;
3. operation of the Trans Alaska Pipeline;
4. development of other North Slope facilities and fields;
5. natural gas development; and
6. current and future leasing of acreage for oil and gas development.

To better understand the legal and economic implications of the proposed merger, the State retained nationally and internationally recognized experts in petroleum economics, antitrust law, pipeline transportation, and oil and gas industry development. Staff from the Alaska Departments of Natural Resources, Revenue, Environmental Conservation, Labor, and Law with many years of experience also formed a task force to assist in the review process.

We recognized that Alaska's policy should be developed in consultation with federal antitrust officials who had the responsibility to review and approve the merger under parallel federal laws. In mid-April we invited staff of the Federal Trade Commission (FTC) to participate in a briefing on North Slope development. And, in early June, the cabinet team traveled to Washington, D.C., to meet with top FTC officials in order to establish full communication with the FTC staff and the FTC chairman. The State and the FTC agreed to work cooperatively in reviewing the merger and established a pattern of constructive dialogue.

In response to FTC and state requests, BP and ARCO produced more than 2,000 boxes of documents during the summer and fall. In early October, the cabinet team returned to Washington, D.C., to discuss the proposed acquisition with top FTC staff members and appropriately coordinate the state and federal review processes.

My department coordinated its antitrust investigation with those of the states of California, Oregon, and Washington. The antitrust attorneys and experts of the states developed a framework for analysis of the issues, reviewed the documents produced by the parties, deposed BP and ARCO officials, and conducted third party interviews of other petroleum industry

companies. The same state parties were also working together on the issues posed by the parallel Exxon-Mobil merger.

You, members of the cabinet team, and others from the administration personally interviewed a number of major oil companies about their possible participation in the exploration, development, and recovery of Alaska's oil and gas resources. These interviews included meetings across the country by you and members of the team.

Following extensive discussions among state officials and the Alaska public, you laid out the Administration's position on the proposed merger in a speech to the Anchorage Chamber of Commerce on August 23, 1999. The "bottom line" was that Alaskan control of "our resources requires a competitive free market environment." Recognizing there had been a "structural consolidation of unprecedented proportion" in the oil industry, driven in part by low oil prices, you emphasized that it was critically important to maintain a competitive environment in Alaska. Appropriately, our focus was on the merger's potential impact on Alaska; potential competitive impacts on retail markets in California and the acquisition of foreign interests were not our concern.

You also felt that BP had to demonstrate a renewed sense of corporate commitment to the State, and you set forth specific elements of an appropriate solution.

The first element of a competitive solution was for BP to divest itself of sufficient North Slope production and leases to guarantee that another major oil company would be an active competitor in exploration and production on the North Slope.

The second element was "open access to our oil transportation and production facilities at a published fair price." You called for a tariff reduction, not to increase state revenues, but to guarantee a price that would not be an obstacle to competition. Fair access to production facilities also had to be guaranteed.

The third element of your competitive solution was to make available adequate natural gas reserves at fair market rates for any sponsor of a natural gas project. No single company, you insisted, should be able to lock up economically recoverable reserves and prevent their production.

In Anchorage, you also called for BP to demonstrate its heightened commitment to Alaska by achieving a higher standard in environmental protection and participation in the community. You asked BP to make a substantial contribution to the University of Alaska endowment for the technical training of young Alaskans and to build upon the State's internationally recognized expertise in arctic engineering. You also called for renewed commitments to Alaskan hire and use of Alaskan businesses. In the environmental area, you asked BP to take responsibility for the clean-up of contaminated sites on the North Slope, even those that were of unknown or "orphan" origins. You also asked for BP to commit to ARCO's plans to build new millennium class, double-hulled tankers.

The Anchorage speech set forth the substantive framework for the negotiations with BP. On September 20, before the negotiations began, you also committed to a public process for taking testimony on any proposed agreement with BP. The terms of any proposed agreement would be

made public and public town meetings would be held on the agreement over a two-week period. BP signaled its willingness to proceed and participate in this process.

As the State entered the negotiations, it became clear that the two announced goals, competition and community commitment, had different foundations. The State's competition objectives were driven by the antitrust laws, whose purpose is to protect competition. Applying standard analysis, the State sought to fashion remedies that addressed the barriers to competition produced by the merger and to create a binding structure for enforcement of these remedies. The objectives for community commitment did not arise from antitrust concerns, but from the State's view that an enlarged BP should have expanded corporate citizenship obligations. For these reasons and because of the adequacy of existing state environmental law, the State did not enter the negotiations with the expectation that the community commitment remedies should be contractually enforceable.

As the Task Force gathered advice from the State's expert consultants and from industry, it focused on what solutions would maintain and enhance competition on the North Slope. The key issue was what would it take to attract new players to Alaska to participate aggressively in leasing, exploration and development. Because participants in Alaska's oil industry compete in a world market both for commitment of capital to new exploration and development and as marketers of Alaska's oil, it was important that the new participants be large and experienced enough to be effective players in Alaska. As the Task Force explored this issue, it was clear that there was a limited set of companies that could meet the State's needs.

Any solution also required that new entrants obtain sufficient resources to achieve the "critical mass" necessary to be an effective participant on the North Slope. ARCO has been an active and aggressive competitor in the development of the North Slope and Alaska's petroleum economy. The goal was not to recreate ARCO as such but to attract new companies that could be effective competitors to BP in leasing, exploration and development. At the same time, it was important for BP to be able to achieve savings in operating costs, particularly within the Prudhoe Bay field, to make it a more cost efficient competitor in the world petroleum market. The key to attracting new players was a package of opportunities ³/₄ giving them a foundation in existing production, particularly in newer fields, forcing BP/ARCO to divest substantial promising acreage on State lands and on federal lands in the National Petroleum Reserve, ensuring competitive access to transportation facilities by requiring the divestiture of pipeline space on TAPS and its feeder lines to the owners of divested production so that they could carry their production on their "own" pipeline capacity, and ensuring a remedy if access to existing field facilities became an issue. As the antitrust analysis advanced, it became clear that a pro-competitive solution demanded a multi-front approach.

We began comprehensive negotiations with BP and ARCO in late September. The cabinet team conducted these negotiations in a series of lengthy meetings in Anchorage and Juneau. However, because of certain BP actions, on October 31, 1999, you instructed me to halt negotiations. At that time, substantial progress had been made but many issues were unresolved.

The cause for the suspension of negotiations was BP's unilateral action in triggering the FTC's 20-day time limit for completing its review of the merger under federal law. BP's notice was delivered to the FTC late on Friday, October 29, and it would have forced the FTC to make a decision within 20 days whether to approve or oppose the merger. Your October 31 letter to

FTC Chairman Robert Pitofsky stated that the companies' action was inconsistent with both the spirit and content of the negotiations with the State. Unless the companies lifted the deadline, your letter urged the FTC to proceed with litigation to enjoin the merger, litigation that the State promised to join.

Immediately responding to the October 31 letter, BP and ARCO rescinded their action and agreed not to trigger the 20-day time limit until negotiations had resulted in a proposed charter with the State or had broken down.

The cabinet team resumed negotiations on November 3. BP dispatched Rodney Chase, its second-highest-ranking executive from London, with instructions to attempt to finalize an agreement with Alaska. For the final session of negotiations, you led the team personally, and the draft Charter was agreed upon on Friday, November 5, 1999. That afternoon, you announced the draft Charter at a statewide press conference and promised to start immediately a process for receiving public comment.

B. The Charter's Rationale

The draft Charter is intended to provide the foundation for continued competitive development of Alaska's North Slope petroleum resources by creating a more competitive environment for the future than presently exists on the North Slope. The following features of the draft Charter are intended to ensure that the North Slope competitive environment is revitalized:

At least 175,000 barrels a day of production will be divested to other companies.

There will be new operators for Kuparuk and Alpine

One of the new operators of Kuparuk or Alpine will gain leases on at least 100,000 acres in the NPRA

At least 220,000 acres of NPRA leases and at least 400,000 acres of states leases will be sold to other companies.

The draft Charter adds two new exploration operators on the North Slope

Any company seeking to explore the North Slope will have timely access to BP Amoco's and ARCO's proprietary seismic data

Minor producers on the North Slope will have guaranteed access to market for their production. BP Amoco will be required to purchase up to 5,000 barrels per day of petroleum from small producers, up to a maximum of 25,000 barrels per day.

The draft Charter gives owners of satellite fields the right to take BP into binding arbitration if they are denied access to production or other lease facilities.

The new operators of Kuparuk and Alpine will receive shares of TAPS and all relevant intermediate pipelines.

Other producers on the North Slope will have an opportunity to purchase a share of TAPS. BP and ARCO will be required to offer any surplus marine tankers to other North Slope producers.

The draft Charter commits BP to negotiate in good faith for the next four years to make available sufficient gas to support a qualified treatment and transmission project with full and fair consideration of all competing proposals.

For the foreseeable future, development of the North Slope will be concentrated in the West, including the NPRA. The divestitures of NPRA lands are structured so that the purchasers will have both the incentives and the means to aggressively develop these lands. Moreover, one

purchaser will not just get NPRA leases, but it will also obtain the production base and infrastructure of Alpine and/or Kuparuk to support its operations. In addition, the draft Charter opens State lands to further competition. Under the draft Charter, the divestitures of State lands must be done in a manner that will result in two play fairways operated by another company or companies. I believe that the draft Charter enhances the competitive dynamics on the North Slope and is superior to alternative remedies that could have been employed, including simply blocking the merger in its entirety. Under the draft Charter, ARCO will be replaced on the North Slope by a number of new players. Therefore, competition in leasing, exploration, and development of the North Slope will be greater than it is today. Moreover, BP will achieve significant efficiencies in the Prudhoe Bay unit $\frac{3}{4}$ making it a strong competitor in the marketing of Alaskan oil. The draft Charter also lays out specific steps that BP will take to enhance its commitment to Alaska.

II. The Public Comment Process and the State's Response to Those Comments

Testimony from the public was taken in a variety of ways. The Department of Law received comments via e-mail and in writing through November 26. Hearings were held in Juneau, Fairbanks, and Anchorage, and teleconferences reached all regions of the state, including the legislative information offices in Kenai, Valdez, Kodiak, Seward, Homer, Barrow, Kotzebue, Bethel, Nome, Ketchikan, Delta, Palmer, Glennallen, Tok, and Sitka and other locations from which people called. More than 1,200 written communications were received and more than 300 individuals or representatives of organizations spoke on the Charter. The hearings were held during the week of November 15 thru November 20, 1999.

A clear majority of the comments received were supportive of the draft Charter. However, many thoughtful commenters questioned both the process and substantive provisions of the draft Charter. What follows is a summary of these comments and a brief discussion of them.

A. Comments on the Process

Urgency on concluding the agreement. A clear majority of the comments received were supportive of the draft charter and emphasized an urgency in concluding the agreement expeditiously. Commenters noted a slowdown in oil field activity due to the uncertainty of North Slope ownership.

Sue first, negotiate later. As the draft Charter demonstrates, Alaska's concerns were much broader than what an antitrust suit would cover and what remedies it could offer. Litigation is costly, time consuming, and confrontational. It entails time and risk. Moreover, pursuing antitrust litigation in the merger context generally signals an inability to reach compromise. Because the market knows this, the point of greatest leverage is before, rather than after, the initiation of litigation. Once litigation has been filed, and the market has reacted, the leverage attributable to the willingness to forbear filing a lawsuit has been lost. In addition, because the stakes are so large and the timelines so short, reaching compromise after initiating litigation is unlikely, simply because the litigation becomes all-consuming and there is no time for anything else. For these reasons, it was my judgment that litigation in this instance would have been appropriate only if it was apparent that we could not achieve our objectives through negotiation.

Secrecy of the negotiations. Under state and federal antitrust laws, my investigation had to be conducted confidentially. The negotiations consummating that investigation also had to be in private because they involved extensive use of sensitive business information obtained pursuant to those laws.

Adequacy of the information available. The terms of the draft Charter were made widely available (the draft Charter was published on the State website, copies were distributed at public hearings and by Department of Law and the Governor's office as requests were received, and copies were distributed by BP in newspapers around Alaska). In addition, substantial background information was made available to the public. Two classes of information were not made available: documents subpoenaed from the companies and certain expert reports. Both of these kinds of documents are confidential by law. At both the federal and state levels throughout the U.S., these two types of material are generally not made available. They represent materials collected by the Attorney General as he performs his responsibilities to investigate possible violations of and to enforce the State's antitrust laws. The courts have recognized that these materials are privileged because disclosure of confidential materials gathered in a law enforcement investigation would impede and interfere with the ability of the Attorney General to gather critical documents and receive candid views from experts and industry.

Adequacy of the public hearings. Given our prior statements to the FTC and our continuing information that the FTC was working aggressively toward deciding its own position, we placed hearings on a compressed schedule, in keeping with your announcement in August. We established open forums throughout the State, for comment in person or electronically at a variety of locations. We also invited comments in writing by both regular mail and e-mail to reach the widest possible audience. We received approximately 1,200 written comments on the merger. A number of persons repeated their comments in multiple forums and by multiple means.

The facility for the first Anchorage hearing was inadequate. The space could not accommodate all who wished to attend, leaving hundreds outside the meeting room and unable to hear the proceedings. Even with the three-minute time period allotted to each speaker (a subject of criticism by some), testimony ran until 1 a.m. Consequently, we scheduled additional hearings on Saturday, November 20, 1999, which corrected the shortcomings of the earlier session.

I believe that the public comment process has yielded an unprecedented amount and diversity of public comment in the time available. I also believe there has never been this degree of public input into a proposed settlement of an antitrust case. My recommendations for changes to the draft Charter are in direct response to the public comments.

The existence of a deadline. There has been much press coverage about whether the State was working against an FTC "deadline." While I was constantly mindful of your view that it was important that we complete the process as quickly as possible, consistent with the public interest, I believed that we were working against what was for all practical purposes an FTC "deadline"; that is, a limit on the time in which we could provide effective input to the FTC. Let me provide some background.

At the same time that the State was conducting its investigation and analysis of the merger, the FTC was conducting its own investigation and analysis. In our discussions with the FTC, we

established an objective of synchronizing our efforts with the FTC process. It made great sense that both the State and Federal investigations proceed on parallel tracks because both agencies were focusing on many of the same issues. Our goal was simple: to be able to present a final Alaska position to the FTC before that agency was called upon to take action.

When was FTC planning to act? There was no set date, though both the FTC and we were aware of BP's public pronouncements that it expected the merger to be closed by the end of the year and its privately stated objectives to wrap the matter up in September, then October, and so on. As early as August, BP was intimating to the FTC that it might trigger the 20-day rule at any time. This rolling threat persisted throughout the fall. Our imperative was to complete our investigation and any discussions with BP and present the result thereof to the FTC, after a public comment process, to allow the FTC sufficient time to review our analysis before they would need to make any enforcement decisions. Consequently, the public comment process, which was part of the overall state process of analysis, decision, negotiation, and resolution, needed to be conducted on an expedited basis.

In fact, BP ultimately took the unilateral step of triggering the 20-day deadline for decision on October 29, 1999. This meant that the Commission was required to decide whether the merger was acceptable under federal antitrust laws by November 19, 1999. What neither BP nor the FTC anticipated was your intervention. You directed me to stop negotiations with BP until the effect of this action was rescinded. BP rescinded the action almost immediately, and promised in writing not to trigger the 20-day deadline again until agreement was reached with the State or negotiations were terminated.

Thus, your decision stopped the clock. It did not, however, stop progress on the FTC's internal deliberations. I would note that the FTC does not publicly announce a deadline for completing its process although it is well known that it establishes an internal schedule for completing its work. This internal schedule, of course, adjusts as the FTC staff continues its discussions with the parties to the merger and others and as issues are resolved or enlarged. It was my judgment, supported by our expert antitrust counsel, who are very experienced in the FTC merger review process, that any agreement with BP resolving the State's concerns would need to be concluded by late November or early December in order for the FTC to have sufficient time to determine whether such an agreement resolved its concerns, if any.

Shouldn't the State have waited until the FTC finished its investigation?

The draft Charter that was negotiated resolves the State's competitive concerns. There was no reason to wait. However, in the event that BP Amoco and ARCO reach an agreement with the FTC that differs from the draft Charter, I note that the Charter includes a provision that the State will receive any additional concessions given to the FTC.

B. Substance

1. MONOPOLY

- a. Questions were asked about why BP was being allowed to increase its monopoly interest in the North Slope, why should BP be allowed to dominate the political and economic life of the State, why a foreign company was allowed to buy out ARCO, and whether there were any secret understandings with BP about taxes or any other issues.

Preserving competition on the North Slope for bidding and leasing of State lands in the future is critical to the financial health of the State. No amount of competition in the future will affect lease sales that have already occurred because those deals have already been done. Consequently, allowing BP to acquire an additional share of the Prudhoe Bay Unit will not have any impact on the leasing revenues the State can derive from the leases in that unit; the State has already received all the leasing revenue that will be derived from that Unit. Thus, we focused our efforts on preserving competition in the future for North Slope bidding, leasing, and development.

The draft Charter ensures there will be robust competition at every level. The draft Charter address competition in leasing by transferring ownership of huge quantities of State lands and NPRA acreage that were previously controlled by BP and ARCO. BP and ARCO also have committed to a timetable to release seismic and other data needed for bidders to evaluate the potential of undeveloped acreage. In addition, competition for exploration will be bolstered by the fact that the draft Charter creates three new exploration play fairway opportunities -- at least one in the NPRA and at least two on State lands.

Moreover, BP will relinquish control of the Kuparuk and Alpine fields. Forty percent or more of BP Amoco/ARCO's ownership in these fields will be divested to new owners who will then have the opportunity to operate those fields. The State also has asserted its ability to resolve issues of access to field facilities by new owners through the authority of the Commissioner of Natural Resources.

The competitive safeguards imposed by the draft Charter do not stop at the borders of the North Slope. The new owners in the Kuparuk and Alpine fields will be entitled to purchase a matching share of the TAPS, Kuparuk, and Alpine pipelines to transport oil on their own "space." In addition, the remaining share of ARCO's interest in TAPS will be available for purchase by other North Slope producers for the life of the agreement. BP has also agreed to divest surplus ANS-suited tankers.

Some parties questioned why a foreign company was being permitted to take over so much of Alaska's resources. Absent an antitrust violation, there is no law that prevents any person from buying or selling property. Under fundamental principles of the U.S. Constitution, no State is permitted to discriminate against or prohibit foreign investment in its economy. BP has owned a majority share of the Prudhoe Bay field for more than a decade and has been subject equally with the other large petroleum companies operating in Alaska to the requirements of Alaska law. All companies, foreign or domestic, must obey and abide by Alaska state and federal laws.

Unquestionably, BP is able to exercise political, social, and economic influence within the Alaska body politic. Alaska's antitrust laws do not prohibit such influence. Nor do the antitrust laws provide the occasion to renegotiate Alaska's tax regime, as some have suggested. We will be providing a fiscal note to the legislature detailing our assessment of the fiscal impacts of the merger. Modifications, if any, to the tax regime should be accomplished industry-wide and should be undertaken by the legislative, not the executive, branch.

- b. Questions were asked about whether the proposed Charter reduced or eliminated the operating cost efficiencies that the combination of BP and ARCO sought to achieve. Others asked whether the State had received less through negotiation and the Charter than BP had offered when it announced the acquisition.

We have not lost many of the efficiencies initially anticipated with the merger. Most of these savings in Alaska come from the consolidation of BP's and ARCO's interests and operations in the Prudhoe Bay field. Indeed, BP's Chief Executive Officer Sir John Browne acknowledged that BP will retain more than 70 percent of the efficiencies it had targeted. BP Amoco Press Release, Nov. 5, 1999. By opening up the newer fields and acreage to the West, by requiring BP to sell matching pipeline interests and establishing new operators in fields BP has operated, and by allowing BP to consolidate all or nearly all of ARCO's interest in Prudhoe Bay, a fair balance was struck. A more competitive environment for future development was created without sacrificing most of the efficiencies BP sought to gain from the more established fields.

- c. Questions were asked about whether BP would lock up seismic and well data needed to make informed leasing and exploration decisions.

The draft Charter addresses concerns about BP having exclusive access to seismic and well data by requiring BP and ARCO to make publicly available for purchase proprietary North Slope seismic and well data, provided they have the right to do so. If they do not currently have such rights, they will diligently seek permission from other owners to release this data. A third party will act as marketing agent for the data at prices it determines, except that pre-1975 data will be released without charge. The data will be made available within three months of the completion of the merger.

2. TRANS ALASKA PIPELINE (TAPS)

- a. Questions were asked why the TAPS tariff wasn't being lowered, why BP was being allowed to retain any share of the pipeline, and why the 1985 TAPS settlement was not being renegotiated.

The focus of the State's effort was on encouraging competition on the North Slope. The State looked closely at the issue of what influence TAPS might have on that competition. The State believes that the divestiture of major shares of TAPS and the Kuparuk and Alpine pipelines to new and existing producers on the North Slope is the right competitive solution. The new operators of the Kuparuk and Alpine fields will be in a comparable position to BP in terms of having matching interests in the pipeline and production. In addition, the draft Charter provides independent producers on the North Slope with an opportunity to purchase a share of TAPS. They too can match their production with pipeline ownership if they so desire.

A reduction in the TAPS tariff was an alternative method at achieving a pro-competitive result. However, as I noted earlier, we were advised that the FTC would view a reduction in the TAPS tariff as an inappropriate non-structural remedy to any competitive problems associated with TAPS.

The State's first objective was to ensure that TAPS was opened up to the new operators so that they could carry their production on their own pipeline space. The draft Charter guarantees this. After that, the State wanted to enable independent producers to buy the remaining portion of ARCO's TAPS space.

Under the state's antitrust law, the issue is what are the consequences of the proposed merger. If the proposed merger is substantially likely to lessen competition, then the appropriate remedy is to ensure that the prospect of those anti-competitive effects is eliminated. Thus, the State set out to ensure that competition would continue at the level it would have been absent the merger. The draft Charter provides that BP must offer to divest ARCO's share of TAPS to either the new production operators or other independent North Slope producers. There was no basis for asking for greater pipeline divestiture than ARCO's share in the context of the other remedies contained in the draft Charter.

- b. Questions were asked about why BP was not asked to segregate the amounts collected for the eventual dismantling and removal of TAPS and the restoration of its environment (DRR).

The issues concerning DRR do not relate to an antitrust analysis. The obligations to dismantle and remove TAPS and restore the environment arise from the federal and state right-of-way leases and affect all TAPS carriers, not just BP and ARCO. The TAPS owners have collected nearly all of the funds they can collect from shippers through the TAPS tariff under the TAPS settlement. There will be opportunities to address DRR issues, which are not competition issues, in the context of the renewal of the right-of-way leases, in pending proceedings before the Regulatory Commission of Alaska, and in future FERC proceedings.

3. GAS

- a. Many comments were directed at the gas clause of the draft Charter. Questions were asked why the draft Charter fixed the price of gas at so high a level or at all, why the State allowed BP to control gas commercialization, whether the gas provisions would block the Mayors' project, and why BP wasn't being forced to sell the gas. Other comments suggested that the Mayors' project set too low a price for gas or was otherwise unrealistic.

To solve the problem of ensuring the availability of BP's and ARCO's North Slope gas to any project that could prove itself viable, the draft Charter adopted an option approach. A project that demonstrated (a) sufficient financial backing, (b) the ability to acquire the required approvals and permits, and (c) a schedule resulting in full ramp-up by 2010 would have qualified for the option. Because both LNG and overland projects are being discussed, the draft Charter announced minimum price goals for both to ensure that there is a balance of benefits between producers, project sponsors, and the State. The draft Charter also created an objective standard to select a project to receive the gas if more than one project qualified.

Substantial comment was received on the gas provisions of the draft Charter. Commenters objected to the price set in the draft Charter for BP's gas supply obligation

as being too high and to the volume commitment as being too low. In response to these comments, I recommend that the draft Charter be amended to follow a different approach. The suggested amendments would obligate BP to negotiate in a fair and nondiscriminatory process with qualifying treatment and transmission projects to ensure them sufficient gas to support a project. To qualify, a project would have to demonstrate that it was able to obtain construction financing, provide reasonable financial security with respect to a long-term 100 percent take-or-pay arrangement, and obtain necessary approvals from field interest owners. BP will commit to meeting on request with project sponsors, and to giving fair consideration to all reasonable approaches including LNG proposals, the port authority project, and gas-to-liquids proposals. The period of good faith negotiations will last until the end of the year 2003. The State will receive reports and information to enable it to monitor the process. BP and ARCO may proceed with their own projects at the same time. The new provisions meet the concerns that a level playing field be established to enable the competing proposals for development of North Slope gas to negotiate the needed gas supplies for their projects. The new provisions avoid the problems of the provisions of the draft Charter, particularly the perception that the price provisions were unworkable.

4.ENFORCEABILITY

- a Many commenters asked why the community commitments, including the environmental requirements, were enforceable only in the "court of public opinion."

The Charter is divided, broadly speaking, between issues that are based upon antitrust or competition concerns and issues that arise outside of the antitrust law. The State insisted that the draft Charter terms dealing with competition issues such as divestiture of land, pipeline shares, and production be enforceable in court. This was comparable to the standard consent decree approach that federal and state agencies employ in resolving merger issues. Thus, the draft Charter is enforceable as a contract for the competition commitments.

For non-competition issues, the State adopted a different approach. For environmental issues, the State relied upon its strong powers under existing environmental laws supplemented by specific promises. For community issues, the State thought that a contractual approach was inappropriate to deal with pledges of a charitable nature, just as individual charitable pledges are not commonly made in binding contractual form. A failure by BP to live by its community pledges would be very visible to Alaskans throughout the State and quite damaging to its ability to be a responsible corporate citizen in Alaska.

However, many public commenters believed that the environmental obligation in the draft Charter should be enforceable as a contractual obligation. In response to those comments, I recommend that we revisit the environmental section of the draft Charter, and include a provision that ensures that the State may bring an action to enforce each of the specific funding commitments BP and ARCO have made related to environmental protection.

- b. Commenters asked whether the draft Charter waived or modified existing environmental laws in the "non-enforceable" environmental clauses.

The environmental obligations in the draft Charter are in addition to existing environmental laws and regulations. There is no waiver of any of BP's existing legal obligations. Given the public comments, however, I propose the draft Charter be amended so that it explicitly states that the draft Charter does not waive any other legal obligation.

- c. Commenters asked whether the commitment of funds to the University of Alaska and other community causes was an improper subject of negotiation.

The Administration has always taken the position that the State's partnership with Alaskan businesses is a two-way street. Given BP's increased presence, you believed it was obligated to demonstrate a level of corporate commitment to the State that befitted its new status.

- d. Commenters asked whether the provisions for enforcing the agreement through the courts were slow and ineffective.

The State has taken steps in the draft Charter to expedite any needed court action. BP recognizes the jurisdiction of the Alaska court to enforce the charter. BP also agrees in the draft Charter that the applicable charter provisions may be specifically enforced by the court through injunctive relief, a more expeditious remedy. In addition, the draft Charter provides that a trustee may be appointed by the court to carry out any divestiture contemplated by the draft Charter if BP fails to do so on the stated timetable.

5. OTHER ISSUES

- a. Commenters asked whether the environmental provisions were sufficient.

BP committed to a number of environmental obligations in addition to existing contractual, statutory, and regulatory requirements. However, I recommend the following proposed changes to the draft Charter:

- a. establish a floor, not a ceiling, of \$10 million to be spent cleaning up orphan sites,
 - b. establish a cap of an extra \$5 million to be spent for extra orphan site clean-up, spill research, or corrosion experts as directed by the ADEC Commissioner,
 - c. require an agreement to repudiate any trade association effort to weaken OPA 90 standards,
 - d. require continued support for the ship escort response vessel system in Prince William Sound,
 - e. require BP to report annually on environmental issues, and
 - f. reconsider the enforceability of the environmental commitments.
- b. Commenters asked why the State did not resolve issues involving potential age discrimination, outstanding OSHA litigation and ongoing tax litigation through the Charter.

Some commenters asked why the State had not taken measures to prevent BP from discriminating against older workers in the upcoming layoffs, to require BP to remedy

outstanding OSHA violations and allegations of OSHA violations, and to pay outstanding tax liabilities. The State's ability to effectively review the merger was based upon its antitrust enforcement powers. The antitrust laws are designed to prevent effects on competition. These issues relating to potential age discrimination, OSHA, and tax claims have no connection to the competition issues raised by the merger. Instead each is governed by specific statutes, regulations, and procedures that provide appropriate remedies to resolve these very fact-intensive issues on a case-by-case basis. I would note that BP and the State are pursuing a resolution of outstanding tax controversies in the confidential tax dispute process established under existing law.

- c. Commenters asked whether the Charter would have any impact on State revenues.

Some have asked whether the merger will be revenue neutral to the State. The State of Alaska has agreed to different calculations of transportation costs by BP and ARCO. There is nothing inherently more or less favorable to the state in either method. In addition, ARCO's oil shipping is more efficient and less costly than BP's. These efficiencies should be realized by BP after the acquisition. The administration and legislature will want to closely monitor this issue.

III. Conclusion

The proposed merger of BP-Amoco and ARCO presents fundamental issues of public policy to the State of Alaska and to your administration. There are no easy choices. We cannot go back to the petroleum industry that existed prior to the Exxon-Mobil and BP-Amoco-ARCO mergers. You have set as the Administration's objectives the twin goals of ensuring competition on the North Slope and requiring BP to enhance its community commitments to reflect its larger role in the state. After listening to public comment, consulting with experts, and hearing the views of the legislature and industry, I believe the draft Charter with the revisions I recommend achieves your goals.

In the core areas of competitive concern the draft Charter lays a foundation for attracting new oil industry players to Alaska through land, production, and pipeline divestitures and by creating a framework for ensuring access to field facilities and seismic and well data. The draft Charter also establishes a level playing field with visible rules for obtaining sufficient gas to support viable gas treatment and transmission projects. This solution was a result that antitrust litigation would not have gained.

The draft Charter also contains environmental commitments over and above what our environmental laws require, including a commitment to clean up orphan sites, to spend additional millions on a variety of clean-up and corrosion issues, and to refrain from lobbying for relaxation of strict tanker safety requirements. BP's plans for substantial charitable and community contributions reflect its recognition of its larger role in Alaska.

For all of these reasons, I recommend that you sign the revised draft Charter.

Sincerely yours,

Bruce Botelho
Attorney General