Petroleum news

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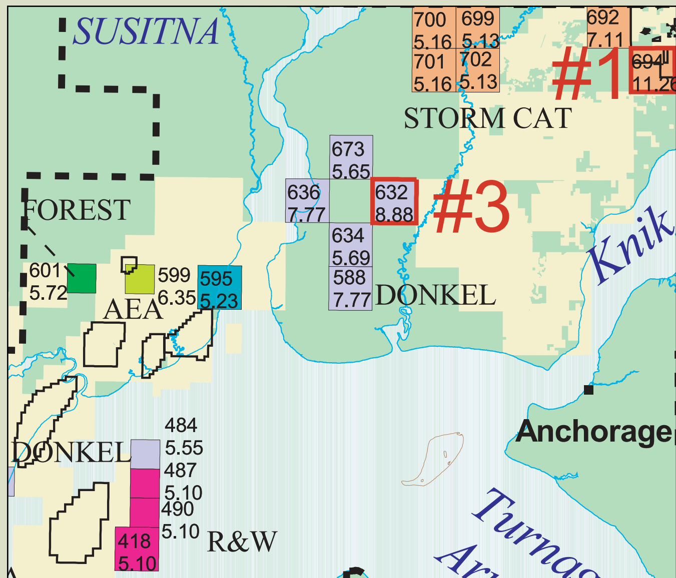
Week of June 12, 2005 • $1.50

page 14 TransCanada chief visits Alaska; gas pipeline contract in fall

New players outline strategies



Storm Cat and Alaska Energy Alliance talk about their plans for leases won in the May Cook Inlet lease sale in story on page 9.

Chinese company still looking at making an offer for Unocal

CNOOC, the Chinese offshore oil company, is still pondering a competing bid for Unocal, CNOOC said in a statement to the Hong Kong Stock Exchange June 7. Unocal has agreed to be acquired by Chevron for about $16 billion in cash and stock.

CNOOC's statement was in response to an article on the Bloomberg news wire June 6, saying it was not considering a Unocal offer.

"The company announces that it is continuing to examine its options with respect to Unocal," the CNOOC statement said. "These options include a possible offer by the company for Unocal, but no decision has been made in this respect."

see **BID** *page 16*

Bass Boys raise Nova Scotia's hopes; Parnell leaves division

THE TIGHT-LIPPED BASS BILLIONAIRES of Texas are putting themselves in the spotlight – like it or not.

Through Bass Enterprises Production of Fort Worth they are moving ahead with plans for a wildcat well offshore Nova Scotia in early 2006.

In the process they are switching the focus in the Nova Scotia waters from natural gas, which has yielded little other than dry holes in recent years, to oil.

But the gamble isn't likely to cause heart beats to skip in the Bass family, led by patriarch Perry 90 and comprising four brothers – all five of whom have accumulated fortunes through real estate, news media and technological investments.

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ALBERTA

Techies lead the way

Research speeds ahead in hunt to replace gas for Alberta oil sands development

By GARY PARK

Petroleum News Canadian Correspondent

It's a veritable alphabet soup that may contain the ingredients of economic health in the Alberta oil sands.

What, for instance, do you make of SAGD, MSAR, VAPEX, SAP and THAI?

Try steam-assisted gravity drainage, multi-phase superfine atomized residue, vapor extraction, solvent aided process and toe-to-heel air injection.

They're just part of the latest batch of advances that have turned what some might have viewed as pure science fiction into a profitable business.

Whether it is drilling, pumping, engineering, shipping or refining, Canadian innovators have figured out ways to turn sludge into liquid gold.

Through skill and risk-taking, they have developed methods to extract bitumen that is buried too deep in the Alberta muskeg to be removed by open-pit mining. Now technology lets operators pump steam into the ground, forcing the molasses-like bitumen to the surface where it can be refined into a wide range of petroleum products from gasoline to diesel fuel.

It all started in 1893

Getting to this point has been a long,

see **OIL SANDS** *page 19*

"If we are going to exploit and properly develop the oil sands, we have to find a way that involves something more than truck and shovel or conventional mining techniques." –John Richels, president of Devon Energy

NORTH SLOPE

Pioneer wants a break

Without lease royalties reduced, independent will not 'vigorously pursue' Oooguruk

By KAY CASHMAN

Petroleum News Publisher & Managing Editor

The Alaska subsidiary of Pioneer Natural Resources has formally applied for a royalty reduction for four leases adjacent to its proposed Oooguruk oil development offshore the North Slope. All four leases will be included in a unit expansion request that Pioneer expects to file around June 15, the company said in a letter sent in late May to Tom Irwin, commissioner of the Alaska Department of Natural Resources.

Located in Harrison Bay near Thetis Island, the Oooguruk discovery includes "potentially commercial reserves" within the Kuparuk and Nuiqsut

see **PIONEER** *page 18*

Wells drilled by others in expansion area

Three exploratory wells were drilled by Pioneer Natural Resources Alaska in 2002 in what is now called the Oooguruk unit – Oooguruk No. 1, Ivik No. 1 and Natchiq No. 1.

In its application to the state of Alaska for royalty relief on four leases that will be included in an upcoming unit expansion, Pioneer said eight additional wells have been drilled within the expansion area, six of which fall in the boundaries of the four leases.

see **WELLS** *page 18*

HOUSTON, TEXAS

Weatherford pumps up

Oilfield services company to buy two divisions from Canada's Precision Drilling

By RAY TYSON

Petroleum News Houston Correspondent

Weatherford International, in what analysts called a bold move for the big U.S.-based oil-field services company, has agreed to buy two of Precision Drilling's major divisions for $2.28 billion in stock and cash, signifying further consolidation of a once floundering industry now revived by the unprecedented strength in worldwide oil and gas prices.

Wall Street immediately warmed up to the deal as investors stepped in with their wallets to push Weatherford shares higher on announcement of the transaction June 6.

Investment bank Jefferies & Co. raised Weatherford's target price to $70 per share from $65 per share. The stock closed June 6 at $56.27 per share, up 4.2 percent from the previous close.

Weatherford's CEO, Bernard Duroc-Danner, said that in large part industry's increasing move toward directional and horizontal drilling prompted the deal with Precision Drilling.

"Weatherford's new product introductions, acquired assets from (Precision Drilling) and its cost-cutting measures combined with our bullish outlook for the oil service sector should drive strong earnings

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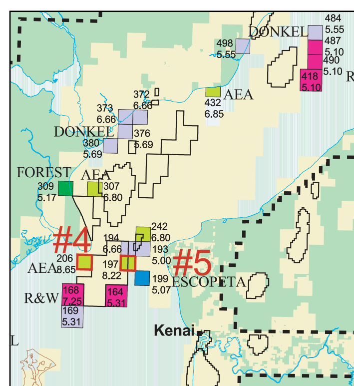

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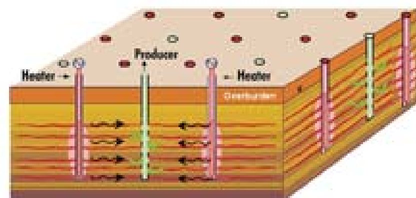

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Gulf of Mexico Activity Report

Current Deepwater Activity

Operator	Area/ Block	OCS Lease	Rig Name	Prospect Name	Water Depth (ft)
Anadarko Petroleum	AT 305	G18556	T.O. DEEPWATER MILLENNIUM	Jubilee West	8,750
BHP Billiton Petroleum (GOM)	WR 206	G16965	GSF C.R. LUIGS	Casade	8,160
Spinnaker Exploration L.L.C.	MC 961	G26281	T.O. CAJUN EXPRESS	Q	7,928
Chevron U.S.A. Inc.	WR 758	G17015	T.O. DISCOVERER DEEP SEAS	Jack	6,959
BP E&P	GC 826	G09982	DIAMOND OCEAN CONFIDENCE	Mad Dog	6,736
BP E&P	MC 822	G14658	T.O. DISCOVERER ENTERPRISE	Thunder Horse South	6,262
ConocoPhillips	GB 783	G11574	NABORS MODS 201	Magnolia	4,674
BP E&P	GC 782	G15610	PRIDE MAD DOG SPAR RIG	Mad Dog	4,430
BP E&P	GC 645	G11081	HOLSTEIN SPAR RIG	Holstein	4,344
Murphy E&P	MC 734	G21778	T.O. MARIANAS	Thunderhawk	5,710
Dominion E&P	MC 773	G16647	NABORS POOL 140	Devil's Tower	5,610
ConocoPhillips	GB 783	G11574	NABORS MODS 201	Magnolia	4,674
BP E&P	GC 782	G15610	PRIDE MAD DOG SPAR RIG	Mad Dog	4,426
BP E&P	GC 645	G11081	HOLSTEIN SPAR RIG	Holstein	4,344
BHP Billiton Petroleum (GOM)	GC 654	G20085	T.O. DEEPWATER HORIZON	Shenzi	4,342
Anadarko Petroleum	GC 652	G21810	ENSCO 7500	Genghis Khan	4,331
Anadarko Petroleum	GC 518	G21801	NOBLE PAUL ROMANO	K2 North	4,047
Eni Petroleum Co. Inc.	GC 562	G11075	GSF CELTIC SEA	K2	3,934
Kerr-McGee Oil & Gas	EB 646	G20725	DIAMOND OCEAN VALIANT	Northwest Navajo	3,905
Shell Offshore Inc.	MC 934	G07969	NOBLE JIM THOMPSON	Europa	3,875
Union Oil of California	GC 512	G26315	T.O. DISCOVERER SPIRIT	Knotty Head	3,570
Pioneer Natural Resources	GC 299	G15571	DIAMOND OCEAN AMERICA	Clipper	3,452
Shell Offshore Inc.	GB 516	G11528	DIAMOND OCEAN VICTORY	Serrano	3,392
Shell Offshore Inc.	AT 267	G18537	T.O. DEEPWATER NAUTILUS	Vrede	3,341
Murphy E&P	GC 338	G22950	NABORS MODS 200	Front Runner	3,328
Kerr-McGee Oil & Gas	EB 599	G19028	DIAMOND OCEAN VOYAGER	Hack Wilson	3,220
Shell Offshore Inc.	VK 956	G06896	H&P 205	Ram-Powell	3,214
Kerr-McGee Oil & Gas	GB 667	G17407	DIAMOND OCEAN STAR	Gunnison/Durango	3,103
Shell Offshore Inc.	GC 158	G07995	H&P 202	Brutus	2,985
Shell Offshore Inc.	MC 807	G07962	H&P 201	Mars	2,945
Shell Offshore Inc.	GB 426	G08241	AUGER	Auger	2,862
Kerr-McGee Oil & Gas	GC 320	G25139	NOBLE AMOS RUNNER	Chilkoot	2,450
BHP Billiton Petroleum (GOM)	GC 282	G26302	NOBLE MAX SMITH	Boris North(GC)	2,346
Murphy E&P	MC 582	G16623	NABORS S.D. XVI	Medusa	2,223
Noble Energy, Inc.	GC 199	G24160	DIAMOND OCEAN QUEST	Lorien	2,200
Chevron U.S.A. Inc.	GC 236	G15562	THERALD MARTIN	Typhoon	1,987
Chevron U.S.A. Inc.	VK 786	G12119	ENSCO 25	Petronius	1,754
Amerada Hess Corporation	GB 200	G17307	DIAMOND OCEAN CONCORD	Northwestern	1,736
Eni US Operating Co. Inc.	EW 965	G12145	T.O. AMIRANTE	Morpeth	1,694
BP E&P	VK 989	G06898	NABORS POOL 143	Pompano I	1,290
Apache Corporation	MC 400	G21754	NOBLE LORRIS BOUZIGARD	Ben	1,139

Total Deep Water Prospects with Drilling/WO Activity: 38

New Deepwater Activity

Operator	Area/ Block	OCS Lease	Rig Name	Prospect Name	Water Depth (ft)
Anadarko Petroleum	AT 305	G18556		Jubilee West	8,750
Spinnaker Exploration	MC 961	G26281		Q	7,928
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Kerr-McGee Oil & Gas	EB 599	G19028		Hack Wilson	3,220
Amerada Hess Corporation	GB 200	G17307		Northwestern	1,736

Baker Hughes North America rotary rig counts*

	June 3	May 27	Year Ago
US	1,353	1,331	1,168
Canada	375	271	256
Gulf	94	91	90

Highest/Lowest

US/Highest	4530	December 1981
US/Lowest	488	April 1999
Canada/Highest	558	January 2000
Canada/Lowest	29	April 1992

*Issued by Baker Hughes since 1944

The Gulf of Mexico Activity Report as of June 6, 2005. Active drilling companies only listed.

TD = rigs equipped with top drive units WO = workover operations CT = coiled tubing operation SCR = electric rig

This platform report was prepared by Tom Kearney

COURTESY BP

BP's Holstein Spar rig

COURTESY TRANSOCEAN INC.

Transocean's Deepwater Millennium

● NORTH SLOPE

Weeks heading back into North Slope facility-sharing negotiations with producers

By KAY CASHMAN

Petroleum News Publisher & Managing Editor

At this time only one facility-sharing agreement for production exists between North Slope producers and a non-facility owner and that was negotiated between Kuparuk River unit operator ConocoPhillips and Jim Weeks, managing member of Winstar Petroleum, for his company's Oliktok Point State No. 1 well. The well, which turned out to be a duster, was drilled in 2003 from onshore drill site 3-R on the northern edge of the Kuparuk River unit to an offshore target was that part of Winstar's lease.

Weeks, who believes in getting a facility-sharing agreement for production in place before drilling exploration wells, is headed back into negotiations with North Slope producers. This time he is hoping to get an agreement put together for the exploration and development of leases west of the Point McIntyre operating area – leases that are owned by Winstar's sister company, UltraStar Exploration LLC.

Jim Weeks, managing member of Winstar Petroleum

At Prudhoe Bay, where some Point McIntyre oil is processed, it will "only take the Big 3 to make it happen," Weeks said, because the Prudhoe Point McIntyre Participating Area owners require only 90 percent approval of a facility-sharing agreement.

"The structure of the Point McIntyre deal will probably need to be different than the one at Kuparuk, but the substance shouldn't be much different since the same three companies have already agreed once to a deal for us non-unit participants. At least there is precedent out there," Weeks said.

The KPA owners require 100 percent agreement for all non-owner use of Kuparuk River unit facilities and pipelines, which meant Weeks had to win the approval of ConocoPhillips, BP, Unocal, ChevronTexaco and ExxonMobil.

Only two of the owners — ConocoPhillips and BP — were bound by a charter agreement with the state of Alaska that required them to provide reasonable access to their North Slope infrastructure.

"It was a tiny deal for the big guys. Not a lot of money in it for them; more headaches and dilution of their attention away from more leveraging issues," Weeks said, quick to point out that the intentions on the part of the KPA owners were always to make the deal happen.

"They're clearly willing to put agreements together to enable a little guy like us to do something up there. It just took us a long time to put the deal together at Kuparuk," Weeks said, crediting that to the fact it was the first deal of its kind with a non-facility owner.

Backouts the biggest hurdle

The biggest economic challenge in North Slope facility-sharing agreements, Weeks said, is the cost of the backouts, which can "make or break an independent's economics."

Backouts represent the amount of oil (owned by the facility owners) from mature fields that must be deferred in order to make room for new oil. The oil from mature fields often has a high water and/or gas content, which can push a processing facility's water and gas handling capability to the max and so oil from those wells often has to be backed out to make room for new wells.

North Slope facility owners want to be compensated for the amount of their own oil that they have to back out of the system in order to free up capacity to process the new oil.

At Kuparuk, ConocoPhillips uses a computer simulation program to model the day to day processing operations at the facilities which has resulted in a "detailed dynamic plant model," from which a complex backout methodology is created. Non-facility owners are not allowed access to the model and so have to trust in what the facility operator tells them.

This resulted in non-facility owners stressing the need for a more transparent methodology; perhaps simpler models to be built which were accessible by all, Weeks said.

But after working with the North Slope producers, Weeks is no longer as concerned about transparency.

"One of my objections to backout was it was a giant 'trust me,' but I got beyond that. I don't think they (major North Slope producers) will purposely rig the numbers. I think they will model it straight up the way they see it."

Backout costs can be 30-50% per barrel

Weeks said if a non-facility owner is looking at testing what he thinks will be a small North Slope field – 50 million barrels or less – he should "get somewhat of an understanding of which facility it's going to have to go into and what constraints that facility has in terms of backouts and fees. You can't firm up the costs – but the costs can be staggering."

Backout costs alone for going into the Kuparuk unit, he said, can be as high as 30 to 50 percent of your per barrel development cost.

"In our case (with Oliktok Point State No. 1 well), we could drill from an existing pad on the road system so we didn't have the expense of an ice road and ice island to deal with. … (and) CPF3, which we were going into, wasn't as heavily loaded."

One of the biggest hurdles with backouts is that the North Slope facility owners do not include in their backout calculation the possibility of being able to produce the backed oil at a later date. It's calculated as lost forever, which is not what state officials and Petroleum News' oil industry sources say happens in other parts of the world.

Weeks agreed it was a problem. "That was my biggest objection, but they (North Slope facility owners) argued that on a present value basis we would get it back so late that is would be worthless; plus they have concerns that their field may not have enough life in it to ever allow for the deferred oil to be produced." ●

Editor's note: Pioneer Natural Resources is in the process of negotiating a production facility-sharing agreement for Kuparuk facilities for development of its Oooguruk unit. See related story in this issue.

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● CALGARY

Fear itself carries a price, says CERI

Canadian research institute estimates "fear premium" at 45-50 percent of world oil price; sees no change through 2006

By GARY PARK

Petroleum News Canadian Correspondent

The price of fear will likely continue to pump an extra US$22 per barrel into world oil prices through 2006, says the Canadian Energy Research Institute.

Otherwise CERI estimates that the price of oil based solely on market fundamentals would be only $21.50-$25.50 per barrel.

The Calgary-based agency expects that rising geopolitical uncertainty will "act as an upward force" on what it describes as the "fear premium," although improving supply flexibility should have an offsetting effect, barring any major and sustained disruptions.

CERI said the War on Terror, including the war in Iraq, have added to political instability in the Middle East, heightening concerns about security of supply, especially among major oil importing countries.

That has spawned a revival of geopolitical competition among major powers (the United States, Europe, China, Russia and Japan) and a scramble to secure access to foreign oil.

Civil unrest in Venezuela, Nigeria

In addition to the Middle East conflict, CERI said the civil unrest in Venezuela and Nigeria has curtailed production in both countries, while Hurricane Ivan removed 2 million barrels per day of U.S. Gulf Coast production in the third and fourth quarters of 2004.

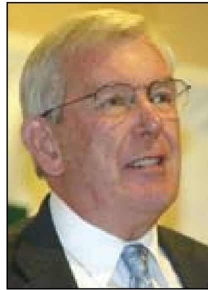
The lack of supply flexibility shows up in several ways, including low levels of OPEC spare production capacity, a shortage of global facilities to process lower quality crude and low commercial inventories.

A surge in oil demand in 2004 caused OPEC spare capacity to dwindle to around 1 million bpd in the latter part of the year from 4 million bpd, 5.5 million and 3 million in 2001, 2002 and 2003, respectively, the study said.

Herrera: $24 oil will increase the 'fear factor'

"We should all hope that the Canadian Energy Research Institute is wrong in its estimate that a non-fearful world would reduce the price of a barrel of oil to about $24. If, in fact, we can forget that the Middle Eastern producer nations contain most of the world's oil reserves and that those producing nations have not been exactly politically stable over the past generation or two, then we can perhaps reduce our concern about future reliable supplies from that region and look forward to low priced oil," Petroleum News' favorite oil price guru, Anchorage-based oil and gas consultant Roger Herrera, said about CERI's analysis.

The problem, he said, is that $24 for a barrel of oil is "not an incentive to explore for new oil anywhere else in the world. Despite great new technology, oil is proving more and more difficult to find and the cost of successful exploration is increasing.


JUDY PATRICK

ROGER HERRERA

"Therefore $24 oil will only increase our reliance on the Middle East and thereby inevitably increase the 'fear factor.'

"When one looks carefully at the CERI logic," Herrera said, "it is difficult not to conclude that world demand has been largely responsible for the increase in the price of oil."

CERI figures, he said, show that world demand for oil has led to the "effective elimination of any spare OPEC capacity. However, it then goes on to say that the International Energy Agency forecasts that plenty of new oil will be found in the near future so everything will be hunky-dory. Such a forecast is obviously designed to eliminate fear, but the widespread lack of success in finding significant large new reserves of oil over the past decade or so would suggest that a logical concern about our future supplies of oil might be a healthy reaction."

Herrera said it is "worth remembering that even if the world is close to its peak oil output (a theory CERI does not mention), it only indicates that about half the world's oil has been used. That is hardly a fearful prognosis." On the other hand the "various political misfortunes that CERI mentions as contributing to its 'fear premium,' are not unique to this time. World wars, cold wars, dictators etc have characterized the whole of the Oil Era. It would be naive not to expect similar influences during the second and final half of the oil era. We will undoubtedly have to pay for them even if we are not afraid of them," Herrera said.

—PETROLEUM NEWS

Uncertainty regarding OPEC decline rates

CERI said that OPEC countries have started investing heavily to increase production capacity and attempt to regain control over the world market.

Although there is uncertainty over both existing field decline rates and the timing of new additions, the International Energy Agency has projected an increase in OPEC production capacity of 1 million bpd in 2005 and 700,000 bpd in 2006, raising spare production capacity from 1.9 million bpd in 2004 to 2.6 million bpd this year and 3.6 million bpd in 2006.

CERI is also counting on two major advances to ease constraints on the global refining system – an improving crude slate, notably from Saudi Arabia and Nigeria, and additions of desulfurization capacity to refineries to take advantage of large price differentials between various crude qualities.

In the realm of geopolitical uncertainty, CERI believes Iraq and Nigeria are the "most likely to suffer a major supply disruption," while Saudi Arabia and Venezuela have quelled local opposition to their regimes, making them less likely candidates.

Heightening concerns about security of supply, especially among major oil importing countries … have spawned a revival of geopolitical competition among major powers (the United States, Europe, China, Russia and Japan) and a scramble to secure access to foreign oil.

Iran and nuclear weapons

Next on the list of potential sources of the "fear premium" is Iran, which CERI says could change the dynamic in the Middle East if it develops nuclear weapons, which could occur in another two years.

"Unfortunately, Western options to discourage Iran from developing nuclear weapons are limited," with an invasion by the U.S. unlikely, leaving "surgical" air strikes as the most likely choice, the institute said.

It said the "war drums might grow louder through 2006 … although the Iranian nuclear situation likely will not lead to a supply disruption until at least 2007, if at all."

CERI excludes traders and speculators from its list of "fear premium" contributors.

It said speculators on the NYMEX futures exchange decreased their bets on higher prices for most of the year when the price of WTI closed at US$55.17 per barrel in October 2004.

Refiners concerned about the availability of crude oil to meet winter demands were responsible for driving up prices, CERI said.

In contrast, when WTI hit US$57.27 per barrel on April 1, speculators were moving into the market on the upside, despite expectations of lower spring and summer demand.●

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● WASHINGTON

Crude futures climb back above $55 a barrel

Oil prices 40% higher than year ago; EIA official says demand growth will be there, inventory surpluses going to disappear

By BRAD FOSS
The Associated Press

Crude futures climbed 3 percent to settle above $55 a barrel June 3 as traders' supply fears were bolstered by an Energy Department official who predicted new record highs for oil prices because of "paltry" domestic inventory levels.

Analysts have noted a variety of factors putting upward pressure on oil prices in recent days — from U.S. refinery snags to the hospitalization of Saudi Arabia's King Fahd — though the most prominent has been concern that as refiners strive to meet today's strong demand for gasoline and diesel, they could end up having difficulty producing enough heating oil later in the year.

As a result, heating oil futures have surged more than 10 percent in the past week, climbing 5.73 cents to $1.5595 a gallon June 3 on the New York Mercantile Exchange.

John Cook, director of the petroleum division at the agency's Energy Information Administration, helped justify the oil market's nervousness, telling Dow Jones Newswires "I think we'll see new records, not necessarily by much, but I think we may even average $60 for a month."

Cook says might see $60 oil

John Cook, director of the petroleum division at the agency's Energy Information Administration, helped justify the oil market's nervousness, telling Dow Jones Newswires "I think we'll see new records, not necessarily by much, but I think we may even average $60 for a month."

"The demand growth is going to be there, and the inventory surpluses we have are pretty paltry to begin with and they are going to disappear," Cook was quoted as saying.

Light sweet crude for July delivery climbed $1.40 to $55.03 a barrel June 3 on Nymex, rising eight out of the nine past trading sessions. On June 2, prices finished 97 cents lower at $53.63.

Gasoline futures increased by 4.17 cents to $1.5571 per gallon.

Oil analyst Tim Evans of IFR Energy Services in New York said he considered Cook's comments to be irresponsible, given the climate of fear already permeating the market.

"He's acting more like a cheerleader for the rally than he is an analyst, or a keeper of the numbers," said Evans, whose own analysis has led him to conclude that hype and speculation — not genuinely tight supplies — have pushed oil prices to record levels.

"There is this ingrained belief that even if the market's not tight today, it's going to be tomorrow," Evans said.

But broker Tom Bentz of BNP Paribas Commodity Futures in New York said Cook's comments merely confirmed what many traders have been saying for months. Still, Bentz said he was "a little surprised that he would make those comments ... It just sparks fear."

Jonathan Cogan, a spokesman for the EIA, said he spoke with Cook after the publication of the Dow Jones story and that Cook emphasized to him that the prediction of $60 a barrel oil was not considered "our most likely scenario, though it was certainly a possible scenario."

On June 2, the EIA said inventories of crude oil rose last week by 1.4 million barrels to 333.8 million barrels, or 11 percent above last year, while gasoline inventories grew by 1.3 million barrels to 216.7 million barrels, up 6 percent from a year ago.

But distillate fuel supplies rose by only 700,000 barrels to 106.4 million barrels, or roughly equal to year-ago levels. That added to worries that there might not be enough heating oil and diesel output for the next winter season in the Northern Hemisphere.

Xie: Growing inventories should lower prices

But Morgan Stanley economist Andy Xie said "the market is making a mistake in assuming linkages between distillate prices and crude prices," adding that the growing crude inventories should lower prices. "With higher inventory numbers and a substantial number of investors backing off in the summer, declining price levels to $40 is possible."

At the moment, oil prices are 40 percent higher than a year ago.

The Organization of Petroleum Exporting Countries meets June 15. Analysts believe the 11-member group will not reduce its current output of 30 million barrels daily.

On June 1, OPEC President Sheik Ahmed Fahd Al Ahmed al-Sabah said the group would maintain its current production ceiling until the third quarter of 2005. ●

EIA forecasts oil above $50 through 2006

As predicted last week by John Cook, director of the petroleum division at the U.S. Energy Information Administration, on June 7 EIA revised its estimate for the average U.S. oil price in the third quarter to $52.83 a barrel from its previous estimate of $51.58.

In its monthly forecast, EIA said it expects the price for U.S. crude to average $55 a barrel during the fourth quarter, up from its previous estimate of $53.

The agency also said it expects the average monthly U.S. oil price to stay above $50 through 2006. Gasoline prices were forecast to stay above $2 a gallon through 2006.

"Oil prices remain sensitive to any incremental oil market tightness. Imbalances (real or perceived) in light product markets could cause light crude oil prices to rise above $55," the agency said in a release.

—PETROLEUM NEWS

JUNEAU

Murkowski signs permitting bills

In early June, Alaska Gov. Frank Murkowski signed two bills into law intended to streamline the permitting process for oil and gas development.

Senate Bill 103, introduced at the request of the governor, gives the Alaska Oil and Gas Conservation Commission the authority to regulate all underground injection wells used in the oil and gas industry. Currently, the state regulates Class II wells while the EPA regulates Class I wells.

"This change will result in quicker action on permit applications and create a single, uniform process for regulating underground injection to improve efficiency and reduce confusion in the permitting process," the governor's office said in a press release.

Senate Bill 144, sponsored by Senate Resources Committee, is part of the Murkowski administration's efforts to streamline permitting. The bill updates state statutes to mirror federal definitions relating to air quality permits, making it easier to issue and enforce air permit compliance more effectively, Murkowski's office said.

—PETROLEUM NEWS

LONDON

G8 to look at tax breaks to spur refinery investment

Next month the Group of Eight industrialized nations will consider tax breaks for oil companies to stimulate investment in new refineries in the United States and other western countries, the Financial Times reported June 7.

The information, garnered from an unnamed senior energy official by the FT, follows International Monetary Fund warnings about the lack of spare refinery capacity. The issue is expected to be on the agenda for the G8 meeting in Scotland in July.

The G8 consists of leaders from the United States, Japan, Germany, Britain, France, Italy, Canada and Russia.

News reports said the proposal would likely encounter opposition from environmentalists and advocates of poverty relief.

No new oil refineries have been built in the United States since the 1970s due to poor financial returns for their owners and strong local and environmental opposition.

The Bush administration is also looking to encourage new refineries, possibly on military bases, but oil companies say it makes more financial sense to expand capacity at existing facilities.

—PETROLEUM NEWS

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● NEWFOUNDLAND

Province's firebrand leader at it again

Newfoundland premier threatens to leave resources in the ground unless companies agree to cough up more in royalties

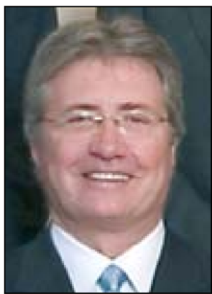
By GARY PARK

Petroleum News Canadian Correspondent

Remember Danny Williams? He's the blustering, bare-knuckles, no-holds-barred premier of Newfoundland who ordered Canadian flags removed from government offices earlier this year when he wasn't getting his way with Prime Minister Paul Martin in his demands for a larger share of offshore royalties.

With the Martin government in a precarious state, Williams went straight for the throat, squeezing out a commitment to keep all of its royalty revenues, without penalty.

For Newfoundland, the deal is worth C$2.6 billion, not including any new projects.



DANNY WILLIAMS

Seems determined to punish industry

Fresh from that triumph, Williams is back – only now he seems determined to punish the industry that has been responsible for almost half his province's economic growth since 1997.

He warned energy industry executives that Newfoundland wants to extract even greater royalties from its natural resources.

If tough talk doesn't work, Williams said he is ready to leave oil, natural gas, minerals and hydro-electric projects on the shelf rather than see them proceed under what he views as bargain-basement arrangements.

"We have sought and achieved a greater return from the federal government based on arguments of fairness and equity and we hope to accomplish the same with the industry," he told the Atlantic Oil and Gas Summit in Halifax.

"Our oil and gas, our hydro, our minerals are all extremely valuable assets. We should not be of the mindset that developers are doing us all a favor by utilizing them."

His pledge is to "negotiate fearlessly with the goal of getting a great deal for the province. We are fully prepared to do no deal at all. That was our approach with the federal government and that will be our approach for the industry."

First target: Hebron-Ben Nevis-West Ben Nevis oil project

The first venture to put this commitment to the test could be the Hebron-Ben Nevis-West Ben Nevis oil project, which is just coming back to life, more than three years after being halted because of shaky economics, complex geology and the heavy nature of the field's 400-700 million barrels.

Project operator Chevron Canada Resources, with a 28 percent stake, announced two months ago that it had reached a joint utilization and operating agreement with its three partners (ExxonMobil Canada 37.9 percent, Petro-Canada 23.9 percent and Norsk Hydro Canada Oil & Gas 10.2 percent) to restart evaluation of the resource.

Chevron Canada said it has found ways to improve the value of the Hebron-Ben Nevis-West Ben Nevis crude.

If the partners can keep the project moving forward, the first oil could flow as early as 2011, a spokesman said.

But Chevron Canada president Alex Archila said a "significant amount of work" must be completed before regulatory applications can be filed.

If Hebron-Ben Nevis-West Ben Nevis is to join Hibernia, Terra Nova and White Rose as Newfoundland producing fields, the partners have insisted on a "preferred royalty regime."

That's a non-starter for Williams. "We don't see that," he told reporters.

He said royalties negotiated from Hibernia, which has been producing since 1997 and is now pumping 200,000 barrels per day, were "on the low end … we had to give something in order to get something. I see that as money well spent."

That overlooked the deal struck with the Hibernia consortium to build a production platform anchored to the sea floor that created hundreds of construction jobs in Newfoundland and pushed capital costs to C$6.2 billion.

By opting for a floating producing, storage and offloading vessel, rather than Hibernia's gravity base system, the Terra Nova partners incurred capital costs of C$2.5 billion for a slightly smaller project.

Now Williams wants a better return on Newfoundland's assets by not allowing future projects to proceed at what he views as bargain basement prices.

He even suggested that jurisdictions like Russia and Venezuela are obtaining greater returns through taxation, increased royalties and equity.

"It is time for industry to treat Newfoundland … as partners, not merely suppliers of their needs," Williams said, declaring that his province is embracing the concept of "share the wealth … as our mantra."

Uneasy about this new direction, industry spokesmen note that Newfoundland is an expensive area in which to operate, because of its harsh climate and offshore environment, and tougher royalties would have it even less competitive at a time when a lack of exploration success has hurt activity.

In addition to Hebron-Ben Nevis, a partnership of Chevron Canada, Imperial Oil and ExxonMobil has been quietly laying the groundwork for possible exploration of the Orphan Basin after making work commitments of C$673 million for 5.25 million acres which hold four pools each with possible reserves greater than Hibernia's 884 million barrels.

Other plays on the horizon are the Labrador Shelf, with about 123 million barrels of natural gas liquids and 4.2 trillion cubic feet of gas; the deepwater Flemish Pass, where Petro-Canada has identified five targets each in the 500 million barrel range; and the potential for opening up 50 tcf of gas in the Grand banks area where the producing oil fields are located. ●

ALASKA

State to back Arctic shuttle study to study route from Alaska to Iceland

Marine transportation in the Arctic Ocean could become a reality in the next few decades as climate change thins Arctic sea ice, allowing icebreaker ships to plow through, scientists say.

Now Adak, a fishing town of about 120 on the far eastern tip of the Aleutian Islands, is set to begin plowing through the political and logistical waters of establishing the route.

This year's state capital budget, which still awaits the governor's signature, sends $50,000 to Adak to study the social and economic returns of an Arctic Ocean cargo shuttle to Iceland. The passage would be a competitive route to the Panama Canal.

"The question that needs to be addressed is what are the economics that would drive an arctic shuttle concept," said Ben Ellis of the Anchorage-based research group Institute of the North.

The group has worked closely with Adak officials to study the shuttle concept. Ellis said it likely would be at least a couple of decades before the ice melts enough to open the Arctic passages, but other countries such as Russia, Canada, Iceland and Greenland already are working toward utilizing the routes once they are available.

"Experts from Alaska and Iceland will work with Finnish icebreaker technologists, Russian administrators of the Northern Sea Route and other appropriate sources of information in completing the study," the budget proposal states. "The study will determine what further public and private investment might initiate service this decade."

Ellis said the study could aim to answer questions such as whether a seasonal or year-round route would be more economical.

"If the economics says it has to be year-round, you are looking at a different scenario," he said.

It also would examine the political landscape of operating in international waters, he said.

Lamar Cotton, a project manager for the city of Adak, said the route could provide alternative passages between Europe and the Northern Pacific, allowing ships a route quicker than the Panama Canal.

"We recognize this is a long-term look at things," Cotton said.

According to the project proposal, the money would help establish an agreement between the Aleutian and Icelandic ports to share information and pursue gathering other logistical information to establish the route.

The study would likely be commissioned by the Institute of the North, the city of Adak and the Aleut Corp.

—TIMOTHY INKLEBARGER, Associated Press writer

● ALASKA

Trans-Alaska pipeline worth $3 billion

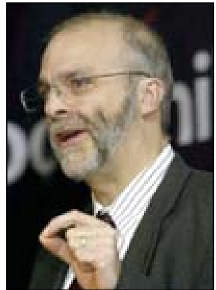
State review board upholds Revenue's decision regarding value of TAPS, keeps line's value at about same level as last four years

By MATT VOLZ
Associated Press Writer

It's pumping half the oil it did in its prime, and tariffs could drop sharply in the coming years, but the Trans-Alaska Pipeline System is still worth $3 billion, according to a state review board.

The five oil companies that own the 800-mile pipeline had appealed that assessment by the Alaska Department of Revenue, which this year changed the way it values the pipeline in figuring the property tax owed.

The owners say under the method used previously — basing the assessment on tariff income — the pipeline's value is actually $1.5 billion.



AL GRILLO

"The last time it went to a hearing was four years ago. All the parties agreed looking at it, the revenue stream was the way to go. This year when we looked at it, we said there is a good chance for a reduction in tariffs." —Dan Dickinson, Tax Division director

The local governments through whose land the pipeline runs also appealed the state's assessment, but took the opposite line: The state's price tag is as much as $11 billion short of the real value.

The Department of Revenue's number was upheld recently by the State Assessment Review Board, keeping the pipeline's value at about the same level as it has the past four years.

JUDY PATRICK

The 800 mile trans-Alaska oil pipeline stretches from Prudhoe Bay in the north to the port of Valdez in southern Alaska.

Taxes the reason for dispute

The reason for the dispute is taxes. Upholding the $3 billion assessment for 2005 means the pipeline owners will have to pay $60 million in property taxes to be split between the state, five municipalities and the North Slope Borough.

"The last time it went to a hearing was four years ago," said Dan Dickinson, Tax Division director. "All the parties agreed looking at it, the revenue stream was the way to go.

"This year when we looked at it, we said there is a good chance for a reduction in tariffs."

If tariffs are reduced in 2009, when a settlement expires in calculating those fees, the property tax would go down using that method of calculation, Dickinson said.

Because of that possibility, the division used a new way of calculating the pipeline's value. Using that method, the value is based on how much it would take to replace the entire pipeline system, minus the cost of depreciation.

The division figures the oil pipeline is about halfway through its life, and is expected to last until 2034, according to Randy Hoffbeck, state petroleum property assessor.

The review board said continuing to use tariff income as the basis for the assessments would "understate the full value of the TAPS."

"The board agreed with the division that valuation of the TAPS based on its tariff income stream is likely to become less and less reliable as an indicator of the TAPS' full and true value," wrote board chairman Steven Van Sant in the May 26 decision.

Appeal possible

Daren Beaudo, spokesman for BP Exploration (Alaska), said since 2001, there has been depreciation and a reduction in oil flowing through the pipeline, pointing to a lower overall value of the pipeline. He said the company stands by its $1.5 billion assessment, but has not decided whether to pursue the appeal in court.

"We're challenging the appraised value just as homeowners have the right to challenge the appraised value of their homes," Beaudo said.

Dawn Patience, spokeswoman for ConocoPhillips Alaska, said ConocoPhillips also believes the $1.5 billion is the appropriate appraisal, but declined to go into details, saying it was "an ongoing dispute."

The municipalities' assessments, which ranged from $8.9 billion to $13.9 billion, includes costs the state kept out of its assessment — road and bridge construction, legal fees, program management and other costs. The municipalities also argued that the pipeline's life is through 2040, not 2034.

The review board said the state did nothing wrong in excluding those costs, but the division should review the 2040 date in future assessments. ●

ALBERTA

Alberta regulator kept busy; sulfur emissions down by 26 percent

It's all in the numbers for Alberta's energy regulator, which conducted more field inspections, found a higher industry compliance rate and logged fewer pipeline failures through the energy boom of 2004.

The Energy and Utilities Board is also brushing off criticisms that it is not equipped to handle such unparalleled activity.

Employee numbers now stand at 845, compared with 675 in 2000, and the board's funding has soared 85 percent over the same period to C$130 million.

Statistical highlights for 2004, showed:

• A compliance rate with major EUB regulations at 98 percent, up from 97 percent in 2003 and 96.5 percent in 2000.

• Initial field inspections rose to 10,167 from 7,910 the previous year.

• Public complaints about upstream operations were up 4 percent year-over-year at 850, but down 8 percent from 2000.

• The pipeline failure rate has shrunk by 27 percent since 2000, with failures for every 1,000 kilometers (600 miles) of pipeline at 2.4 last year against 3.3 in 2000.

• Sulfur emissions from Alberta gas plants have been slashed by 26 percent since 2000 – 58,000 metric tons compared with 78,000 – and by 75 percent since the 229,000 metric tons in 1974.

• The regulator suspended 118 energy facilities and operations in 2004, raising the total this century to 734.

—GARY PARK

● COOK INLET

New inlet players outline strategies

Storm Cat and Alaska Energy Alliance talk about their plans for leases won in the May Cook Inlet lease sale

By ALAN BAILEY
Petroleum News Staff Writer

Storm Cat Energy Corporation and Alaska Energy Alliance Inc. adopted distinctly different strategies in buying leases at the state of Alaska's Cook Inlet areawide sale in May. Both companies are new to Alaska, although Storm Cat had already bought some leases near Big Lake, northeast of Anchorage, in the November 2004 Mental Health Trust lease sale.

Storm Cat's state leases all lie in the Mat-Su Valley at the northern end of the state's lease sale area.

"The recent (state) acreage we picked up complements the Mental Health Trust acreage, so we're putting together the acreage position for both conventional gas and coalbed methane," Scott Zimmerman, president of Storm Cat, told Petroleum News. "… Storm Cat believes in the potential of north Cook Inlet and that we'll be able to (work) in an environmentally safe and sound manner."

SCOTT ZIMMERMAN

Storm Cat is registered in British Columbia and has offices in Denver, Calgary and Ulaanbaatar, Mongolia. Zimmerman used to be vice president of Evergreen Resources, a Denver-based company that had been working a coalbed methane prospect in the Matanuska-Susitna Borough. Pioneer Natural Resources bought out Evergreen and subsequently dropped the Mat-Su acreage, to focus on the North Slope.

Conventional gas first

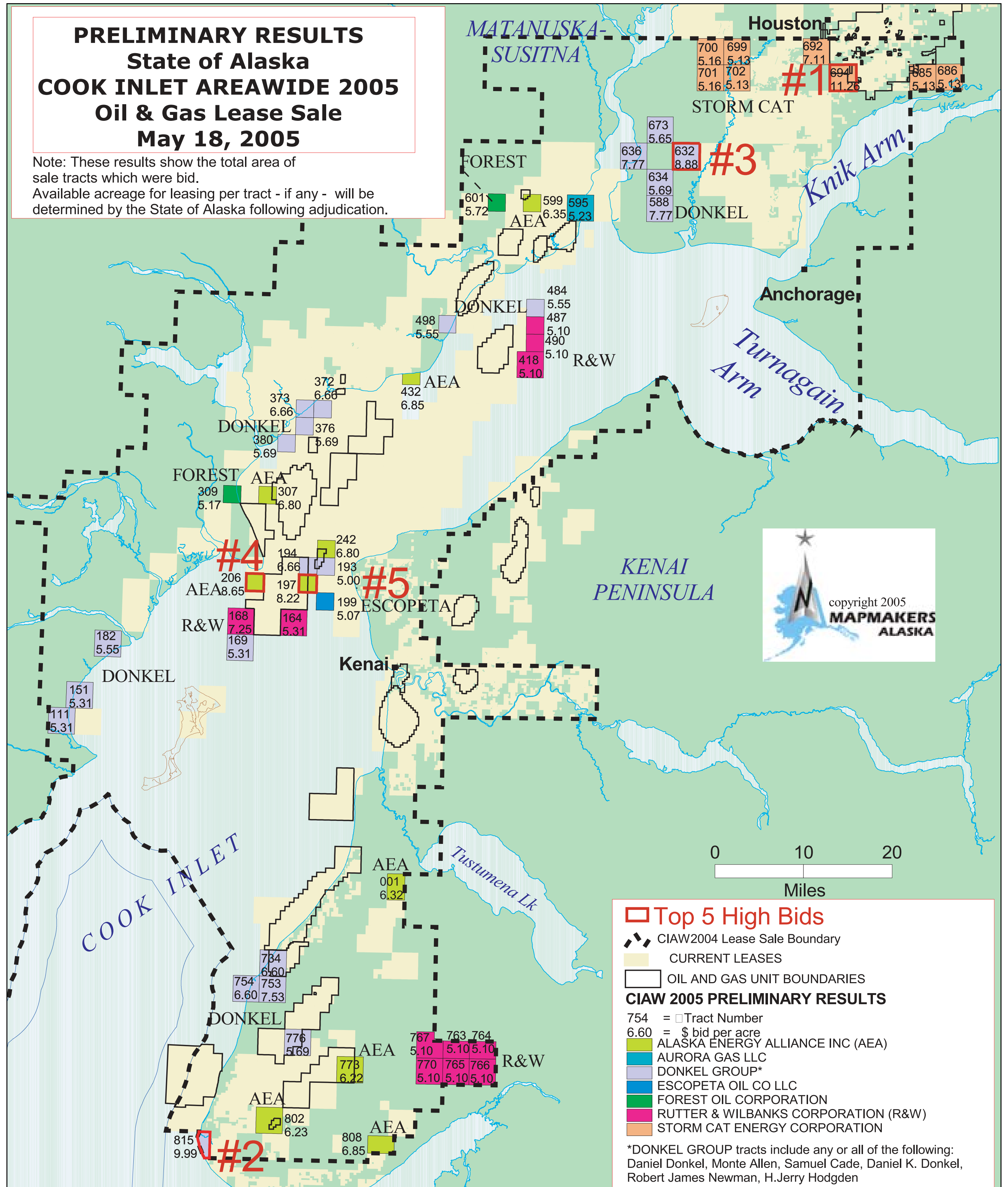
Storm Cat's new venture in the Mat-Su Valley will initially focus on finding conventional gas.

"We will probably look first at the conventional possibilities," Zimmerman said. However, the company expects to be able to evaluate coalbed methane potential using the same well that it drills for conventional gas, he said.

The company's preliminary geological evaluation has identified some promising structures in the area of the leases. And the nearby ARCO BLT well, drilled near Big Lake in 1992, has caught Storm Cat's attention.

"The old BLT well has a lot of interesting gas shows within it," Zimmerman said. That's one of the key wells that we're looking at, he said.

However, coalbed methane development is a future possibility. Zimmerman is familiar with the recent controversy surrounding this type of development. He thinks that the regulatory framework for coalbed methane in the Matanuska Susitna Borough is inappropriate.



see LEASES page 10

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UNITED STATES

Executives blame oil price for slow growth

Executives of leading U.S. corporations expect their growth to slow over the next year, and many think rising oil prices are part of the reason. That's among the conclusions of a quarterly survey of 147 chief financial officers and other top managers of U.S.-based multinationals.

The PricewaterhouseCoopers survey says the executives expect revenue growth of 8.1 percent during this calendar year, compared with an increase of 10.1 percent in 2004. A third of the survey participants, and nearly half of those in the manufacturing sector, cited rising oil prices as a factor.

For the first quarter, 47 percent of executives reported increased costs at their companies, compared with 21 percent who said their costs went down. Meanwhile, 46 percent of the companies boosted their own prices, compared with just 12 percent who cut prices for their products.

"The economy appears to be stuck in neutral, waiting for oil prices to stabilize," said John O'Connor, vice chairman of PriceWaterhouseCoopers LLP. "Companies that are vulnerable to rising oil prices expect notably slower growth, and report weaker margins and considerably more cost increases."

But the executives still see the glass as half-full, with 77 percent optimistic about the U.S. economy and 67 percent bullish on the world economy. Only 3 percent are pessimistic on each of those issues. And 57 percent expect their company's workforce to grow, compared with 10 percent who expect to have few workers at the end of the year.

More information on the survey and others by the firm is available at www.barometersurveys.com

—ALLEN BAKER

continued from page 9

LEASES

"The borough has not fully understood and has not really done the proper work and the regulations are inappropriate and improper," he said.

Storm Cat is using existing seismic data and has assembled a geological team, with a view to start drilling in the winter of 2005/2006.

Drilling next winter

Storm Cat is using existing seismic data and has assembled a geological team, with a view to start drilling in the winter of 2005/2006.

"We've put together our geological team and they're putting together an evaluation to pick a location to drill some time late third quarter or early fourth quarter (2005)," Zimmerman said.

A consulting firm in Anchorage is doing the geological investigation and Storm Cat may itself establish an office in Alaska.

"We do not have an office but we have some consultants working for us and we're looking at possibly getting an office up there soon," Zimmerman said.

Alaska Energy Alliance

Alaska Energy Alliance is based in Newport Beach, California, and was formed by Stan Snyder and his wife Alexis Snyder to enter the Alaska oil and gas business, Stan Snyder told Petroleum News. The Snyders have been in the oil and gas business for nearly 30 years, primarily with gas interests in Colorado, Snyder said.

"We're primarily land speculators … that's the primary focus of our business although we are involved in some exploration," Snyder said. "We would like to be involved in Cook Inlet exploration."

Alaska Energy Alliance bought 10 leases scattered across the lease sale area. Four leases are on the Kenai Peninsula, four are in the Cook Inlet near Trading Bay, one is near Granite Point and one is onshore west of the mouth of the Susitna River.

"The strategy is in our first year of bidding on tracts in Alaska is to take more of a scattered or shotgun approach," he said.

But Snyder said that his company had not expected to win so many tracts.

"In most of our bidding … we're lucky enough if we put in 10 or 12 bids to come out with three or four tracts," he said. " I feel very, very fortunate that we were able to do as well as we did but I had no idea … that we would acquire what was basically 10 out of 11 applications we put in."

Some of the leases are near Alliance Energy Group LLC's North Fork Unit at the southern end of the Kenai Peninsula. However, Snyder said that there is no connection between Alaska Energy Alliance and Alliance Energy Group, despite the similarity in the names.

Snyder said that there is no connection between Alaska Energy Alliance and Alliance Energy Group, despite the similarity in the names.

Exploration plans

The company did some preliminary geological evaluations when determining which tracts to bid for and now plans to hire a consulting geologist to do a detailed evaluation of each tract.

"What we'll do now that we've acquired the tracts is … some extensive geology on the areas and (determine) what we might do with them at some point in the future," Snyder said.

The company is primarily interested in gas plays.

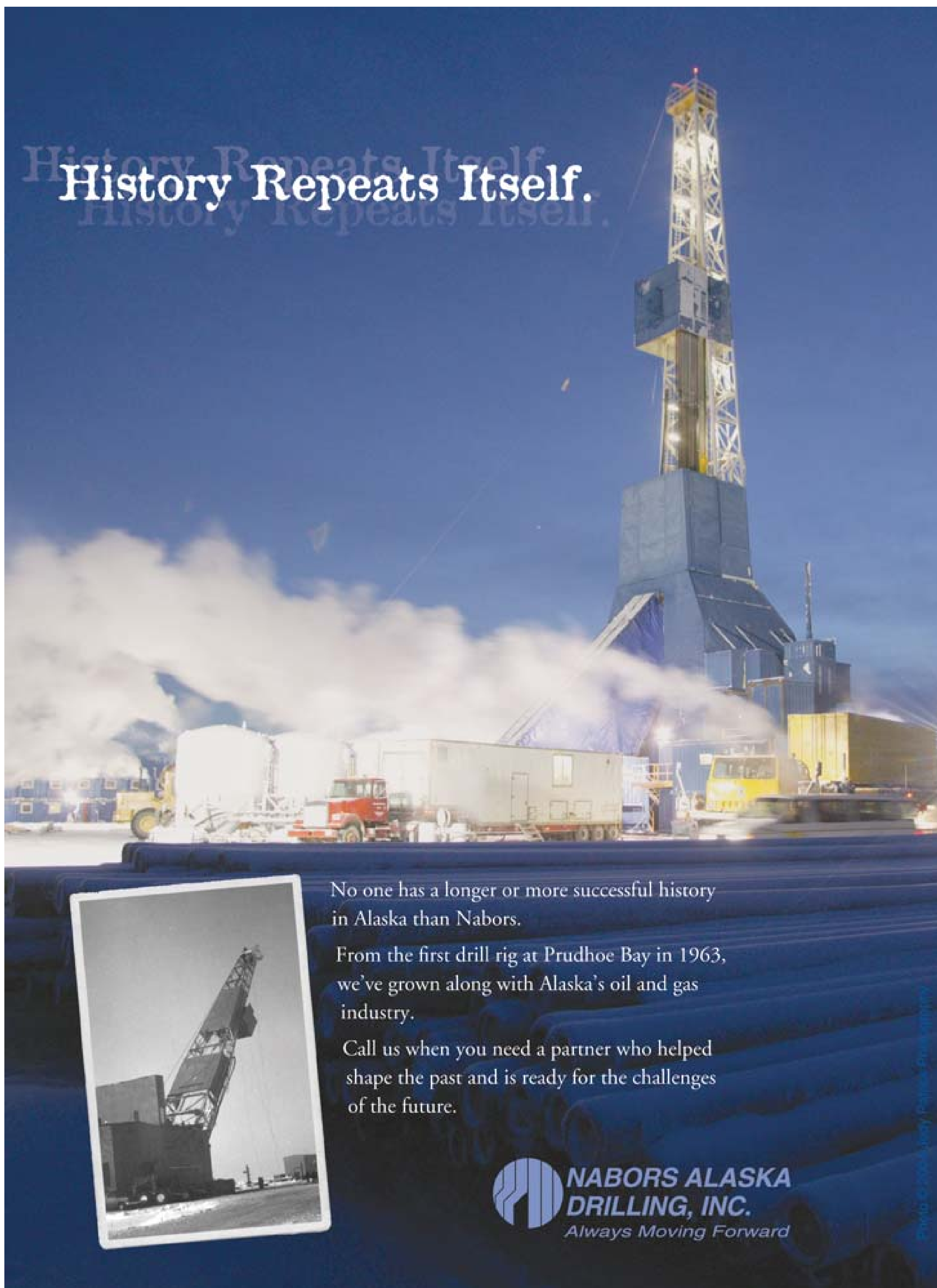
"I understand there's … a contract on the table for any gas that's produced that will be sold at prevailing prices, so that certainly is intriguing for us," Snyder said.

He emphasized how pleased his company was to be entering the Alaska oil and gas business and how welcome it felt in the state.

"We found everybody to be very, very friendly and very to receptive — the attitude seems to be if you do it right and you do it clean we're more than welcome to have to you up here," he said.

And Snyder thinks that the new leases provide a good starting point for his company.

"We are certainly delighted that we have our holdings now covering all quadrants of the Cook Inlet — it will give us quite a bit of insight as to the specific areas that we want to focus on in future acquisitions," he said. ●



● UNITED STATES

U.S. oil shale: Real, or just a mirage?

New processes might turn the mirage of future oil shale development into a viable source of vast quantities of petroleum products

By F. JAY SCHEMPF

Petroleum News Contributing Writer

The federal government is taking another serious look-see at whether U.S. shale oil reserves can be tapped economically and in an environmentally friendly way.

So what's new? After all, government and industry have searched over more than a century for a way to coax oil economically from the vast U.S. oil shale deposits — the largest in the world — most of which are lodged in a 16,500-square-mile area encompassing the Green River, Uinta and Piceance basins in southwestern Wyoming, northeastern Utah and northwestern Colorado.

It's also well known that the hydrocarbons in western oil shale reserves are the equivalent of 1.2 to 1.8 trillion barrels of crude oil. Of that, according to U.S. Department of Energy figures, anywhere from 130 billion to 1 trillion barrels ultimately may be recoverable. A trillion barrels is roughly equivalent to all the combined proven conventional oil reserves in the world today.

Rock that burns

What is oil shale, anyway, this "rock that burns?"

For one thing, it isn't shale. For another, it doesn't contain crude oil. Instead, it's hard, black or dark brown marl that's richly infused with bituminous material. It was formed eons ago by the simultaneous deposition of silt and organic debris on the sea bottom that once covered the western U.S. As these deposits piled up, heat and pressure transformed them into a stable mixture of inorganic minerals and solidified organic sludge. However, the heat and pressure did not reach high enough levels to form crude oil.

Although solid at ambient temperatures, super-heated oil shale yields a hydrocarbon vapor called kerogen that, when condensed, can be captured and refined into gasoline, diesel and jet fuel.

You can dig it

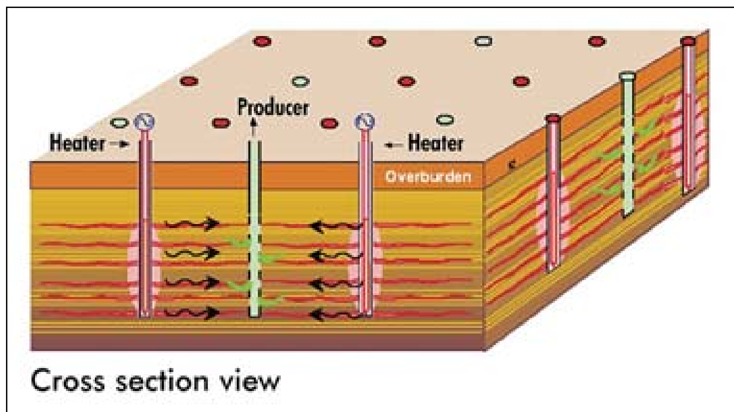
The oil shale recovery and kerogen extraction technology that has been most widely employed combines subsurface mining with surface retorting. Producers extract the shale using explosives or draglines at the surface and by burrowing deeper with mining equipment. The chunks of extracted oil shale are broken up and then introduced into retort ovens where, aided by steam, the entrained kerogen and gases are condensed. The next step, refining, cracks the kerogen molecule and adds hydrogen to yield a high-grade synthetic crude oil known as syncrude.

When heated, the oil shale expands much like popcorn, so that even after product removal, the volume may be as large or larger than it was originally. Producers must move this spent material to a proper disposal site and stabilize it — the remnants hold a variety of undesirable mineral compounds that can leach out with rain. What's more, shale retorts historically have released vile-smelling vapors, some of which may be harmful.

And, of course, producers still have to seal up the excavated area, filling it with soil, reshaping surface contours and then planting it with trees, native grasses, etc.

Not viable

Even if the mine/report method were to be environmentally friendly, the method has not proved to be financially viable and several attempts at exploiting oil shales in the United States have failed.



Simplified here, Shell's In-Situ Conversion Process (ICP) heats oil shale kerogen below ground. The resulting light, gaseous compounds are claimed via conventional production wells and are condensed into a light oil ideal for refining into motor fuels.

In one notable episode, the Middle East oil embargo and several Middle East wars spurred the federal government to create a new shale oil business in the west in the late 1970s. Several companies — confident that oil prices would remain high — placed orders for large mining/retorting operations in the area around the communities of Rifle and Parachute, Colo.. The resulting economic boom burst on May 2, 1982 – a few months into construction – when the biggest shale operator, Exxon Corp., abruptly shut down its Colony mine/retort project near Parachute. The company cited construction cost overruns, but the truth was, crude oil prices had returned to pre-embargo levels. Unocal and Tosco (The Oil Shale Corp.), among others, kept smaller projects on track for a while longer, but by 1991, all Colorado oil shale development had petered out.

Rebirth of the industry

Currently, however, in virtually the same geographic area, the hint of a quiet, measured rebirth of oil shale exploitation is again being debated in local government offices, civic clubs, cafes and beauty parlors. The difference now is that one company, Shell Exploration and Production, thinks it has extraction technology to develop shale oil efficiently without surface retorts, crushers or landfills. In fact, Shell's new process leaves a footprint no larger than that of conventional oil field development.

But mindful of the earlier oil shale bust, Shell has done everything possible to forestall any local — or national — perception that another oil shale 'boom' is in the offing.

And Shell isn't flying solo. Several other companies, including ExxonMobil, Chevron and others, still hold large blocks of acreage in all three oil shale states, and have themselves continued their oil shale research. And while Shell is the only major company talking about shale oil extraction these days, a few smaller — much smaller — companies are either retorting shale already or soon plan to do so.

New shale bill 'Hatched'

Utah Sen. Orrin Hatch hopes to amend the omnibus energy bill now pending in the Senate, with proposed legislation to open Rocky Mountain oil shale and oil sands for leasing and to promote new extraction technologies — all by 2010

Meanwhile, the industry says oil shale development needs federal government interest. Such interest already exists — DOE, for example, has conducted oil shale research for decades. What's more, the U.S. Department of the Interior Bureau of Land Management, which oversees federal shale properties, is now working on a new leasing policy.

And recently, powerful government lawmakers from the three western states

see **OIL SHALE** page 12

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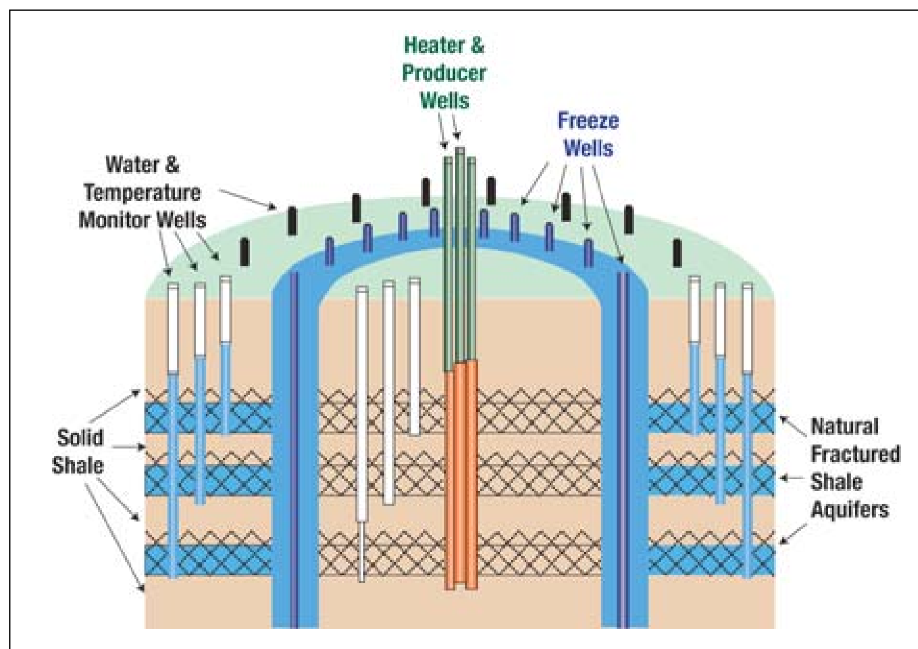
continued from page 11

OIL SHALE

with oil shale deposits have seen U.S. oil shale exploitation as a way to stave off perceived crude and products shortfalls and perhaps lower the unprecedented motor fuel price hikes seen in recent months. They also view shale development as a major boon to their states' economies.

Concern about domestic supplies of conventional oil and gas is also prompting some action inside the Washington Beltway to look at supplies from oil shale, oil sands and heavy oil deposits.

On May 19, Utah Republican Senator Orrin Hatch introduced the Oil Shale and Tar Sands Development Act. Hatch and fellow western state lawmakers hope to tack the bill — or at least its main points — on as an amendment to the Senate version of the omnibus energy bill, which its Energy & Natural Resources Committee reported out May 26 to be brought soon to the floor for a vote. The House already has passed its version, and President Bush wants a final bill for his signature by Aug. 1.



To isolate the useful and waste products of its ICP system from intruding into surrounding formations, Shell circulates water to absorb heat around injection/production wells to create an "ice barrier."

The Hatch bill would create a Strategic Fuels Task Force to accelerate and integrate a five-year commercial development of fuels from shale and oil sands. The bill also directs DOI to kick off a comprehensive public lands leasing program (the one BLM already is working on), and calls for a DOE cost-sharing program to demonstrate promising extraction technologies.

Finally, the bill would allow producers immediate expensing of new technology outlays for shale and oil sands development. The bill also suggests sliding-scale federal royalty reductions for initial production.

Backing the Hatch bill are fellow Utah Republican Sen. Bob Bennett, as well as Sens. Wayne Allard, R-Colo., and Ken Salazar, D-Colo., among others.

"Who would have guessed that in just Colorado and Utah, there is more recoverable oil than in the Middle East?" Hatch asked recently. "We just don't count it among our nation's oil reserves because it's not yet being developed commercially."

Shell's downhole heater

Though Shell is loath to say that it has a commercial process, the company is blazing a trail to just the kind of oil shale development Hatch envisages. The company has conducted numerous field tests in Colorado during the last five years that indicate its In-situ Conversion Process, known as ICP, actually works.

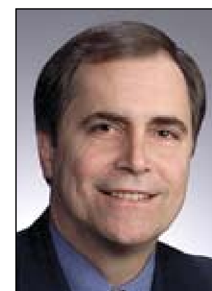
With the ICP, the company inserts electric resistance heaters into cased holes in the shale, and then heats the subsurface around each bore hole gradually over a three to four-year period until the surrounding zone reaches a temperature of around 650 F, driving vaporized kerogen into offset producers. This leaves the spent shale, or "char" — heavier hydrocarbons and all those nasty mineral compounds — in the formation.

Testifying at an April 12 Energy & Natural Resource Committee hearing on oil shale potential, Steve Mut, chief executive officer of Shell's Unconventional Resources unit, said the latest ICP test, performed over several months, produced more than 1,200 barrels of light oil and gas liquids. Some 32 downhole heaters have been placed in wells spaced 10 to 20 feet apart over a five-acre parcel at the company's 20,000-acre Cathedral Bluffs property in Rio Blanco County, near Rifle, about 200 miles west of Denver.

Heating the shale source rock to release kerogen, said Mut, "…accelerates the natural process of oil and gas maturation by literally tens of millions of years."

The process produces about 65 percent to 70 percent of the original subsurface "carbon" in place, he noted. The remaining carbon products, if brought to the surface, would require broad, energy intensive upgrading and hydrogen saturation. So, he inferred, these products are best left in place.

The method of keeping the heated shale products from escaping into groundwater flows forms a unique feature of Shell's ICP process. Mut said that engineers can isolate the ICP-affected underground area by adapting 100 year-old mining and construction technology that freezes groundwater to form an ice barrier or to reduce water flow.



Steve Mut, CEO of Shell E&P's Unconventional Resources unit, says the company's In-Situ Conversion Process (ICP) for producing oil from shale, still under development in Colorado, "…accelerates the natural process of oil and gas maturation by literally tens of millions of years."

According to Mut, Shell use a refrigeration system, based on the same principle as a residential air conditioner. The system circulates cold fluid through a series of wells, so that ice grows around the wells to connect into a solid ice wall.

The new process uses a lot of electrical energy, said Mut. However, each unit of energy used to generate electricity yields about 3.5 units of energy to be treated and sold, he said, adding that the process compares favorably with steam injection in conventional heavy oil reservoirs.

The ICP produces a different hydrocarbon mix than traditional crude oils — it's much lighter, with almost no heavy ends, Mut said. However, the process can control product quality by using changes in heating time, temperatures and pressures, he said.

Much to be done

But don't bet the farm on the ICP just

see **OIL SHALE** *page 13*

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Glennallen gas well looks promising

By STEVE SUTHERLIN

Petroleum News Publisher & Managing Editor

Rutter and Wilbanks Corp. has completed its gas exploration well near Glennallen in Alaska's undeveloped Copper River basin. The results are encouraging enough to test the well, Bill Rutter III told Petroleum News June 7.

The Midland, Texas-based independent will know if Ahtna No.119 contains commercial potential by July 4, Rutter said.

The company started drilling the well in February, but encountered high geologic pressures at a depth of 1,200 feet — earlier than expected, company officials told Petroleum News in early March.

Later, Rutter and Wilbanks had to switch from winter operations and using an ice drilling pad to summer operations with a gravel pad system.

Forest Oil and Anschutz Exploration are partners in the prospect, part of an exploration license obtained from the state of Alaska. The drill site was on land owned by Native regional corporation Ahtna Inc.

Hoping for 100 bcf and spur line

Rutter and Wilbanks hopes a major gas discovery will stimulate the North Slope spur line concept and convince the state to build a section of the line from Glennallen to Palmer, to get the company's gas into the Enstar system for Southcentral Alaska consumers to help replace dwindling Cook Inlet basin production.

Eleven wells have been drilled in Alaska's undeveloped Copper River basin, but there have been none since Copper Valley Machine Works drilled Alicia No. 1 in 1983.

Rutter and Wilbanks hopes to find 100 billion cubic feet or more natural gas to justify building a pipeline to more populous areas, Rutter said. If the field proves considerably smaller, the company is eyeing the local market, supplying Glennallen and the Copper Valley Electric Association, a Glennallen-based rural electric cooperative with 3,600 customers in the Copper River basin and Valdez. ●

Shell's ICP shale oil layout resembles an oilfield production complex typical of those found in Colorado's conventional "oil patch." Some piping carries condensed shale kerogen from heated well bores to processing facilities, while others are used to surround underground well bores with an "ice barrier."

continued from page 12

OIL SHALE

yet. Mut said that while Shell has spent many millions of dollars on the process and has eliminated a great deal of risk and uncertainty, "much work and expenditure still remain before the ICP process can be commercialized."

Recent reports, however, say Shell plans to expand ICP research during the next two to three years as a next step toward commercialization, drilling more wells, and taking them deeper. But among other technical needs, the company reportedly is still looking for a heater efficient enough to hold a constant downhole temperature of 600 F for months or years.

Shell officials hope the ICP will be commercial by about 2010, although that may not lead to a major ICP-based project, at least in the U.S.

But while industry observers have long maintained that crude oil prices would have to be at least $40 a barrel to make extracting shale oil profitable, Shell officials say the ICP could make kerogen production profitable at world oil prices of $30 per barrel. With today's price bouncing around $50, the decision to go ahead seems to be a 'no-brainer.' ●

CALGARY

First Calgary seeks pact with Repsol

First Calgary Petroleums has signed an agreement in principle with Spain's Repsol to jointly develop its large natural gas finds in Algeria.

If a final pact is signed it will see the Calgary-based junior grow into a production company from a pure explorer.

But First Calgary President and Chief Executive Officer Richard Anderson has cautioned that there are major obstacles still to be cleared in resolving how quickly the reserves can be developed.

Repsol is eager to participate in a liquefied natural gas terminal to open up development of the Berkine Basin, which is believed to hold 13 trillion cubic feet of reserves.

In the meantime, First Calgary is no longer reviewing strategic options, which many investors had hoped for more than six months would result in an outright sale.

—GARY PARK

Enbridge takes ownership of U.S. pipeline

Enbridge has locked up total ownership of a U.S. pipeline that forms a vital link in its plans for eventually delivering oil sands production to Gulf Coast refineries.

The Calgary-based pipeline company paid US$12.4 million to BP for the final 10 percent it did not already own of what is now the Spearhead pipeline.

The majority stake cost Enbridge US$112 million in 2003, leaving it with an option to acquire the remainder.

Earlier this year the company obtained approval from the U.S. Federal Energy Regulatory Commission to reverse the flow of the now unused 650-mile pipeline from Cushing, Okla. to Chicago.

It is aiming to complete the reconfiguring work in the first quarter of 2006, offering initial capacity of 125,000 barrels per day to offer a "more varied grade mix of crudes with physical characteristics that will be available for the first time to refineries in Kansas, Texas and Oklahoma."

It is aiming to complete the reconfiguring work in the first quarter of 2006, offering initial capacity of 125,000 barrels per day to offer a "more varied grade mix of crudes with physical characteristics that will be available for the first time to refineries in Kansas, Texas and Oklahoma."

Enbridge has said the line could be expanded to 160,000 bpd.

It also has FERC permission to offer discounted shipping rates to help offset "dwindling U.S. oil supplies and … increase refineries' security of supply."

—GARY PARK

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● ALASKA

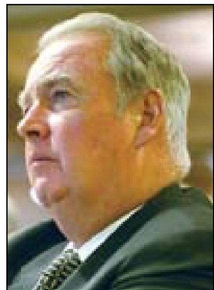
TransCanada chief visits Alaska

Gov. Murkowski says a natural gas pipeline contract should go to a special session of the state legislature for approval in the fall

By **ALAN BAILEY**
Petroleum News Staff Writer

On June 6 Gov. Murkowski held a press conference to report on the status of negotiations regarding an Alaska gas pipeline and to introduce Hal Kvisle, chief executive officer and chairman of TransCanada. TransCanada executives were in Alaska for discussions with the state negotiators.

"We had an interesting and fruitful discussion and as you know we are looking forward to presenting this fall (a contract) to the mandatory 30-day hearing process … after that … (we'll present) a submission to the legislature in a special session," Murkowski said.


JUDY PATRICK
Alaska Gov. Frank Murkowski

TransCanada and the North Slope gas producers have both submitted gas pipeline proposals to the state. A third proposal by the Alaska Pipeline Port Authority has until Aug. 5 to show the state it has access to natural gas for its project or to provide a financial guarantee of its performance in order to be eligible to negotiate with the state for a gas project under the under the Alaska Stranded Gas Development Act.

When quizzed about the length of time that the negotiations were taking, Murkowski pointed out the complexity of the issues and the amount of detail that needs to be sorted out. There are benefits and risks associated with different options and we have an obligation to flush that out and determine what's in the best interests of the state, he said.

Hal Kvisle, CEO and chairman of TransCanada

"We're moving quite well on the two proposals that we have before us," Murkowski said.

And, at a time when the state has three gas pipeline applications, the governor dismissed as premature any threats to force gas production by imposing a gas reserves tax or retracting leases.

TransCanada's position

Kvisle said that TransCanada had conducted many discussions with both the state and the producers. He said that the Alaska and Canada portions of the project are quite distinct and by not objecting to U.S. enabling legislation for the pipeline, TransCanada had "effectively opened the door for a variety of different ways that the project could go ahead within the state of Alaska."

But, "We've shown no such flexibility on the Canadian side," Kvisle added, referring to his company's adamant position that it owns legal rights to build the Canadian portion of the Alaska pipeline, under the terms of Canada's Northern Pipeline Act.

And with many of the right-of-way arrangements in the Yukon already in place Kvisle said that TransCanada can deliver the right of way on the Alaska project more predictably than other proposals.

Expanded system

Kvisle characterized the Canadian segment of the Alaska pipeline as an expansion to TransCanada's existing pipeline infrastructure.

"We would have to augment our Canadian system by about 20 percent in order to accommodate the Alaska gas at the Yukon-Alaska border and that is our intention and that is what we're proposing to do," he said.

In the 1990s TransCanada built more miles of pipeline than would be required in the Alaska pipeline project, Kvisle said.

When asked about the potential for a partnership between TransCanada and the gas producers Kvisle said that he didn't know what the producers wanted as a final outcome and that at least two of the producers had challenged TransCanada's rights to build the Canadian portion of the project. However, Kvisle sees TransCanada as an essential player in getting Alaska gas to market.

"We'll continue to work towards that," he said. ●

● INTERNATIONAL

Shell wins 3 more Sakhalin LNG sales

New agreements with Japanese utilities give Sakhalin 2 commitments for 75 percent of initial output capacity; BP-led Tangguh LNG project gets $1.4 billion; Conoco plans more Timor drilling this year for big Darwin liquefied natural gas plant

By **ALLEN BAKER**
Petroleum News Contributing Writer

FAR EAST report

Shell Gas & Power has announced three new deals with Japanese companies for LNG shipments from the Sakhalin 2 project. The agreements give the $12 billion project an outlet for 75 percent of the 9.6 million tonnes of liquefied natural gas that will be produced annually, starting in 2007. Sakhalin 2 will also produce oil.

Shell says it now has eight LNG sales agreements with Japanese utilities, removing many of the potential customers for an undersea pipeline that had earlier been planed for gas from the ExxonMobil-led Sakhalin 1 project.

Shell said June 6 that Toho Gas Co. Ltd. had signed a full sales and purchase agreement for 200,000 tonnes annually for 20 years. Earlier this month, Tohoku Electric Power Co. signed a Heads of Agreement for 420,000 tonnes annually, and in late May Hiroshima Gas Co. Ltd. signed a similar Heads of Agreement for 210,000 tonnes annually. A metric tonne of LNG converts to about 50,000 cubic feet of natural gas, so the Hiroshima deal would yield about 10 billion cubic feet a year.

The Sakhalin project also has long-term sales agreements to supply up to 2 million tonnes annually to Korea and nearly 2 million tonnes annually to Sempra's Baja California terminal. More than 3.4 million tonnes annually is slated for Japan.

Shell holds 55 percent of Sakhalin 2, with Mitsui & Co. at 25 percent and Mitsubishi Corp. at 20 percent. There have been reports that Russia's Gazprom will take a stake in the project by trading gas reserves to Shell for a 25 percent stake.

$1.4 billion for Tangguh

Meanwhile, eight Japanese companies have committed to invest $1.4 billion in gas fields that will provide the fuel for the BP-led Tangguh LNG project in Indonesia, set to begin exporting 7.6 million tonnes annually starting in 2008, according to the Japan's Asahi Shimbun newspaper.

The paper said total development cost for the project is now estimated at $6 billion. Proven reserves total more than 14 trillion cubic feet of gas. A unit of Halliburton Co. and JGC Corp. of Japan won $1.8 billion contract in March to build the LNG facilities.

BP, which has a 37 percent stake in the Tangguh field, signed the construction deal after getting lease extensions on the three fields that will supply the LNG plant 1,900 miles east of Jakarta in Papua province. CNOOC has nearly 17 percent of the Tangguh project and various Japanese entities, including Mitsubishi, Sumitomo and Kanematsu, hold the rest.

Up to half of the Tangguh LNG will go to Sempra's Baja facility, with 2.6 million tonnes set to go to China and about half that slated for Korea.

see **FAR EAST** page 15

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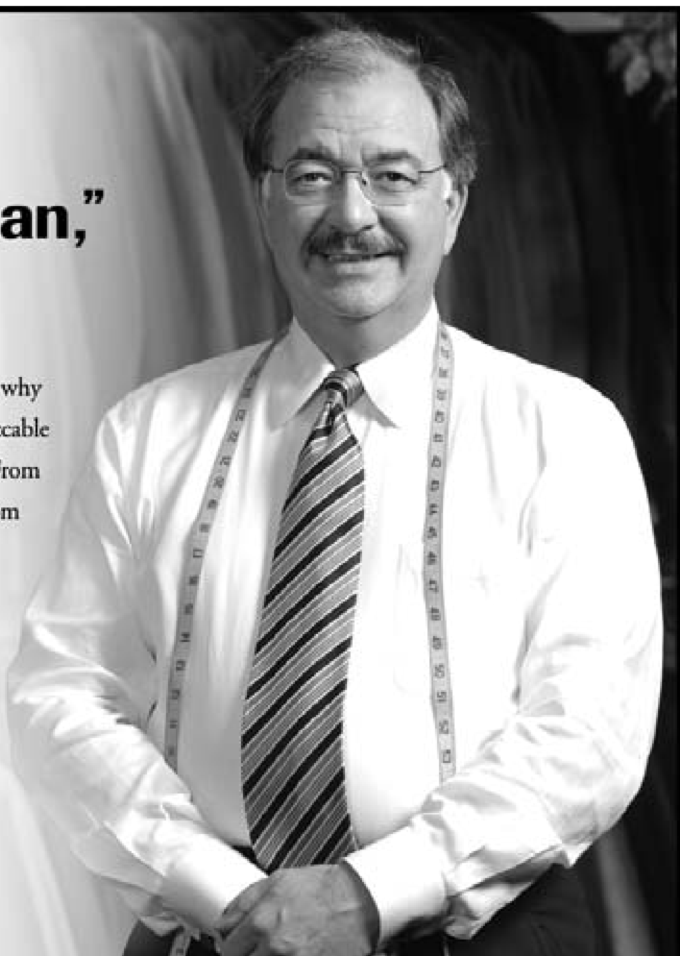

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● NEW BRUNSWICK

Irving, Repsol sign New Brunswick LNG pact

THE ASSOCIATED PRESS

Encouraged by a 25-year freeze on property taxes, Irving Oil Ltd. and Madrid-based Repsol YPF have signed definitive agreements to develop a $750-million liquefied natural gas terminal in Saint John, New Brunswick.

The agreements create a new company, Canaport LNG, which will construct own and operate the terminal by 2008, the firms said June 7.

The terminal will initially be capable of delivering one billion cubic feet per day of regasified LNG, as provided in an existing permit. Repsol will be responsible for providing all of the LNG while Irving will market the regasified LNG in Atlantic Canada, and Repsol will sell it elsewhere in Canada and in the United States.

"The parties have nearly completed front-end engineering design for the terminal, and plan to request proposals for engineering, procurement and construction contracts during July of this year," the companies said in a release.

In May, people opposed to a lucrative tax break by the City of Saint John presented a petition at the New Brunswick legislature that called for the deal to be revoked. It's estimated the tax concessions will cost the city as much as $125 million.

Eyeing spin-off benefits, Saint John common council voted to freeze property taxes for the terminal at $500,000 a year for 25 years, with no adjustment for inflation. ●

continued from page 14

FAR EAST

ConocoPhillips plans Timor drilling

Another source for both Japan and the U.S. West Coast is Australia, where ConocoPhillips is planning new drilling this year in the Timor Sea to provide gas for the big LNG plant it's building Wickham Point, near Darwin, Australia, according to Bloomberg.

Drilling with partner Santos Ltd. will be at the Caldita prospect near Evans Shoal. Another well is planned at Firebird, near the Bayu-Undan field.

The $1 billion Wickham Point liquefaction plant is expected to go into operation early next year with an initial capacity to ship out 3.5 million tons a year and potential expansion possibilities. Feed gas will come initially from the 57 percent owned Bayu-Undan development, now producing condensate and reinjecting the dry gas.

ConocoPhillips has contracts to supply LNG from Australia to Tokyo Electric Power Co. and Tokyo Gas Co., and has said it may send some of the gas to the Long Beach, Calif., terminal it is planning with Mitsubishi Corp.

Another potential source of additional gas for Wickham Point is the Greater Sunrise field, where Woodside Petroleum (33 percent) is the operator and ConocoPhillips has a 30 percent interest.

But that field is in a murky border area and development has been stalled as Australia and East Timor work out an arrangement on splitting royalties. ●

continued from page 1

WEATHERFORD

growth over the next several years," Jefferies analyst Stephen Gengaro said in a note to clients.

Money-making deal

Weatherford's acquisition of the Canadian-based company's Energy Services Division and International Contract Drilling Division was done for no other reason than to make money, said Bernard Duroc-Danner, Weatherford's chief executive officer.

"It's really all we're after," Duroc-Danner told analysts in a conference call explaining the deal. "This is not an exercise in industry aesthetics. It's not an exercise in some sort of crusade. This is just money."

Investors were not as kind to Precision Drilling, Canada's largest contract drilling company, as Precision's share price fell three percent on news of the transaction. Moreover, Standard & Poor's Ratings Services put the company on its Credit Watch with negative implications. S&P noted that while the pending sale likely would not affect Precision's dominant position in Canada, it would remove about half of the company's assets.

Under terms of the agreement, Weatherford agreed to pay Precision Drilling $900 million in cash plus 26 million Weatherford shares for Precision's two divisions. The acquired net book value is about $1.63 billion, according to Weatherford.

Weatherford is already a strong player in drilling services. But the inclusion of the Precision Drilling business would significantly improve Weatherford's directional drilling and wireline capabilities, as well as add more "underbalanced" drilling capabilities, according to Weatherford. Underbalanced maintains wellbore pressure below formation pressure while drilling.

Precision's international division a carrot

The odd part of the deal is Precision Drilling's international contract drilling division, consisting of 48 land rigs with a strong presence in the Middle East-North Africa region. While Weatherford already has a strong position in the region, actually operating rigs in the area would be a first for Weatherford. However, the company plans to target national oil companies that desire "one-stop shop" services, Weatherford's Duroc-Danner said.

"They are showing a keen interest in having engineering planning, logistic coordination, drilling efficiencies … managed with as few contractors or vendors as possible," he added. Duroc-Danner said Precision also has developed innovative technologies which Weatherford is anxious to harvest. He said Weatherford intends to accelerate the growth of the technologies with the full support of its worldwide infrastructure.

"And that's why I am very grateful that we were able to pick up Precision, which has done a wonderful job at developing those technologies," Duroc-Danner said. "Frankly, we could not duplicate what they did, and we need it."

He said that Weatherford brings its vast worldwide infrastructure to the deal, while Precision brings technology and the product and service lines that Weatherford lacks.

"So for us it's very much a harvesting of their product and service lines and the technology work they've done," Duroc-Danner added. "For them it's harvesting our infrastructure. It consolidates what we have. It broadens what we have and gives us what we want."

5,300 employees in 25 countries

In the 12 months ending December 2004, Precision Energy Services and International Drilling had combined revenues of C$1.1 billion. The combined divisions have about 5,300 employees operating in 25 countries.

"After careful consideration of various strategic alternatives, the board determined this opportunity to be the best for our shareholders and for employees of the respective divisions," said Hank Swartout, Precision Drilling's chief executive officer.

The transaction is expected to be completed during the third quarter of 2005 and is subject to regulatory approvals, including U.S. and Canadian competition filings.

Weatherford's Duroc-Danner said that in large part industry's increasing move toward directional and horizontal drilling prompted the deal with Precision Drilling.

"One thing we found out is how very successful the underbalanced business is (and) that pretty much all the wells that we are getting involved in are either directional or horizontal," he said.

"We also found out that in much of our market the client wants us to coordinate closely with the directional people. We also found out that we did not have a substantive directional competency. Directional was the missing link. And that (acquisition) to us is sort of being able to get all the right arrows in our quiver." ●

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LONG BEACH, CALIF.

Long Beach votes to continue LNG talks

The Long Beach City Council has voted to continue talks on a proposed LNG terminal at its port, the Los Angeles Times reported. The 5-4 vote early June 8 was a defeat for residents who wanted to stop the facility planned by a joint venture of Mitsubishi Corp. and ConocoPhillips.

About 400 people came to hear the debate over the proposed terminal, which could handle 5 million tons of liquefied natural gas annually, turning it into 700 million cubic feet of gas each day.

Some council members said they had concerns about the project, but the council decided to go ahead with an environmental impact report and consider the matter again once that is completed next spring. Council members opposing the project cited concerns about terrorist attacks at the site, about two miles from downtown Long Beach.

The $450 million terminal had supporters as well as opponents at the packed hearing, with some union leaders saying the use of LNG for terminal vehicles would clean the air, and the project would provide jobs.

Three other terminals are proposed in California, two to be sited far offshore. One terminal just across the border in Ensenada, Mexico, is already under construction and another in Baja California is planned. California's current natural gas consumption is about 6.5 billion cubic feet daily, and even the relatively small Long Beach terminal could supply more than 10 percent of that. So it's unlikely that all of the terminals will go forward.

—ALLEN BAKER

LOUISIANA

Meridian logs another gas discovery

Meridian Resources Corp. has another significant gas find with the Avoca 6-1 well in the N.W. Bayou Chene area of Louisiana. The well was drilled to 11,500 feet, and logged more than 40 feet of pay in the Big Hum 2 sands at 10,748 to 10,791 feet, the company said June 7.

A test of the well through 40 feet of perforations showed a gross daily flow rate of 6.5 million cubic feet of gas and 214 barrels of condensate with no water production at a flowing tubing pressure of 3,608 pounds per square inch through an 18/64th-inch choke. The successful well follows another nearby discovery May 16 in the Avoca 5-2 well at Bayou Chene, in the coastal area south of Baton Rouge. That well showed a gross daily flow rate of 2.3 million cubic feet, also from the Big Hum 2 sands but at a depth of more than 11,000 feet.

Meridian, based in Houston but exploring and producing mostly in the marshlands of Louisiana, has a 92 percent working interest in both wells, and expects to build a pipeline and facilities to put the wells into production during the early part of the third quarter.

The rig used for both of those wells was moved to the company's nearby Turtle Bay prospect to drill the CL&F D-1 well. The company is expecting to keep three or four rigs busy for the rest of the year as part of a $139 million capital budget.

—ALLEN BAKER

Vacancy Announcement
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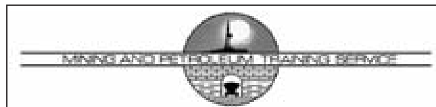

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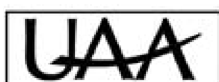

JUNEAU

DEC proposes financial responsibility increases for pollution response regulations

The Alaska Department of Environmental Conservation is proposing increases to the dollar amounts of financial responsibility required for pollution response from a wide range of oil facilities in Alaska. DEC periodically increases the dollar amounts in line with inflation, as measured by the Anchorage consumer price index.

"We do this regulatory process every three years," Christopher Pace, environmental specialist with DEC, told Petroleum News in early June. The original dollar amounts were set in 1990 and the amounts have increased to 1.435 times the 1990 levels, Pace said. The dollar amounts are specified by regulation and details of the proposed changes can be obtained from DEC. Comments on the changes must be submitted by July 6.

Facility operators are responsible for ensuring compliance with the regulations but, once the regulations change, DEC will try to contact companies whose proofs of financial responsibility fall below the new levels, Pace said.

—ALAN BAILEY

continued from page 1

INSIDER

Since obtaining an exploration license in 2002, Bass Enterprises has gathered enough 3-D seismic through modern digital projections to stir optimism.

The well, named Mon Cherie, will be drilled in 4,800 feet of water to a total depth of about 10,700 feet.

It is in the same vicinity as a well plugged and abandoned 20 years ago by Petro-Canada and Texaco.

For the Nova Scotia government and industry, the results could be crucial to the region's chances of reviving hope after years of setbacks.

Parnell leaves Division of Oil and Gas

SEAN PARNELL, DEPUTY DIRECTOR of the state of Alaska's Division of Oil and Gas, has left the agency, Mark Myers, director of the division told Petroleum News June 6.

SEAN PARNELL

Parnell received "an offer he couldn't refuse" from the Anchorage office of Patton Boggs, an international law firm, Myers said, where Parnell will be a partner.

Parnell, a former state senator, also was a member of the state's gas pipeline negotiating team.

In the interim, the division's petroleum manager, Bill Van Dyke, will be acting deputy director. Myers said no decision has been made on a long-term replacement.

Sempra's investment in Alaska LNG hit $6.3M

THE SAN DIEGO UNION TRIBUNE picked up a tidbit concerning Sempra's withdrawal from its alliance with the Alaska Gasline Port Authority's proposed LNG project that as of June 9 (Petroleum News' press date) no other publication had reported.

The Tribune reported that at the time of its withdrawal, San Diego-based Sempra had invested $6.3 million in the port authority's LNG project, which will be recovered only if the project is successfully completed. The company had been paying $750,000 per month under its deal with Sempra.

Editor's note: Oil Patch Insider is written by Gary Park and Kay Cashman. Please send news leads to publisher@petroleumnews.com or call 907 770-3505.

continued from page 1

BID

CNOOC, which is controlled by the Chinese government, has hired the investment bank Rothschild to provide an independent assessment of the deal, according to S&P Equity Research.

Going after Chevron on its own U.S. turf would be a difficult battle for CNOOC, which had considered a bid earlier this year. But the firm held back as Unocal's board accepted Chevron's April offer, which includes a $500 million breakup fee to Chevron if anyone else buys Unocal.

When asked to comment on CNOOC's statement, Chevron spokesman Don Campbell told the Los Angeles Times, "It's inappropriate for us to comment on the possible actions of others." But, he said, "We believe our offer, accepted by the Unocal board, is attractive and has a high degree of certainty as to completion." Unocal had no comment.

Some analysts doubted if CNOOC would make an offer for Unocal.

"The Unocal shareholders are perfectly happy to hold Chevron paper (stock) and take some of it in cash. But Unocal's shareholders would be less inclined to hold CNOOC paper, so CNOOC would have to top Chevron with an all-cash bid," said Derek Butter, head of corporate analysis at the Edinburgh, Scotland, office of Wood Mackenzie.

To trump Chevron's offer for Unocal, CNOOC would have to pay at least US$18 billion, which represents 80 percent of its market capital, said DBS Vickers June 9.

It went onto say, "In our view, the financial risks are very high for CNOOC to pay such a price for Unocal at cycle peak;" also, Unocal's U.S. assets offer little synergy, presenting higher operating risk for CNOOC as it lacks experience in United States. "We expect that CNOOC is only interested in acquiring Unocal's assets in Asia either from Unocal or Chevron."

Meanwhile, Chevron and Unocal are moving forward on their merger. On June 8, the companies reached an agreement with Federal Trade Commission staff on a proposed settlement that would allow their merger to close.

But it remains to be seen whether FTC's commissioners will approve the companies' proposal, said Joe Simons, an attorney for Paul Weiss Rifkind Wharton & Garrison, and former director of the FTC's Bureau of Competition. "I don't know if the commission will approve it or not. They might send it back to adjudication. … The commissioners may ask for additional conditions that Unocal may or may not agree to."

CNOOC now produces about 380,000 barrels of oil equivalent daily; Unocal about 430,000 BOE.

—Allen Baker and AP contributed to this Petroleum News report

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Business Spotlight

By PAULA EASLEY

FORREST CRANE

Erling Young, PE, PMP

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Erling Young is a longtime Alaskan whose career has centered on North Slope oil field development, from TAPS construction to Alpine. He received his master's degree in civil engineering from UAF. For 15 years Erling worked for ARCO and has been with NANA/Colt five years. Married to Lynn, the couple has three grown children (and multiple foster children).

FORREST CRANE

Stephanie Holthaus, Vice President, Cargo

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Stephanie Holthaus has worked in every aspect of service, sales, operations and management during her 18 years with NAC. She loves challenges. In May she finished her first-ever triathlon at the 2005 Nugget. Other rewarding challenges have been being a Big Sister and supporting youth organizations. Husband Ken Acton consults on aviation issues, and when time allows, they're hopping on a jet plane.

continued from page 1

PIONEER

(Jurassic) formations; however, the economics of … the project are marginal," Pioneer told the state.

If it doesn't get its royalties on the four leases dropped from 12.5 percent to 5 percent, the Dallas-based independent said it "cannot vigorously pursue" development of the Oooguruk unit.

Pioneer has been working with the state for the last six months, reviewing data and trying to find ways to modify the existing lease terms to "encourage timely development" of Oooguruk, a development Pioneer is quick to point out, that has not yet been sanctioned by its board of directors.

The company has said Oooguruk would produce less than 20,000 barrels per day and would be developed in four feet of water from a five-acre drill site. Pioneer hopes to commence construction activities in the first quarter of 2006 and begin production near the end of 2007.

State can make big bucks

Once part of ARCO Alaska's Kuukpik unit, which has since expired, the four leases in the royalty reduction application bear a lower royalty than the leases currently in the Oooguruk unit, which carry a 16.67 percent royalty. But unlike those in the unit, the four leases are subject to a net profit share interest that allows the state to collect an additional 30 percent once the costs of development have been recovered by Pioneer.

In its royalty relief request, received by the state May 25, Pioneer noted that because of the net profit share provision the state will be able to participate "at a large and significant level in all the project success which results from favorable changes in the price of oil or gas, production rates, projected ultimate recovery, development costs, and operating costs, lower cost performance or production rate upside."

At Alaska North Slope West Coast oil prices of greater than $40 per barrel, the "expected financial benefits to the state" under the royalty reduction regime proposed by Pioneer "will exceed the benefits associated with a flat one sixth royalty," which has become the state's standard royalty in and around existing infrastructure, the company told the state.

$80 million in development costs

In its application Pioneer also asked the state to lump the four leases into a single development account, treating them as one lease. (A state statute establishes an accounting system for the administration of net profit sharing leases which consists of three separate accounts — development, production revenue, and net profit payment.)

The company wants the aggregated development account balance to be formally set at $80 million as of Jan. 1, 2005, which Pioneer said will save audit and accounting expenses — and give investors in the project "relative fiscal certainty."

Royalty reductions can be a challenge

According to Tim Ryherd of the state Division of Oil and Gas, no applications for royalty relief have been approved by the state to date.

"There is a fairly high hurdle" to qualify, he said.

The applicant has to prove its project needs relief; that without it the project can't go forward, the division's senior commercial analyst Kevin Banks told Petroleum News June 7.

"To prove that often requires information that the company may not have or considers confidential, (including) … delineation, a fair amount of information about the resource and pretty good information about the cost of developing the field," Banks said.

"What we have found in the past is that this kind of information is not available at the time they come in and apply for royalty relief. … They haven't done the work yet.

"It's a chicken and egg kind of problem for producers," Banks said, explaining that producers are often loathe to commit to the amount of investment it takes to obtain the information needed to qualify for the relief until they can be sure they will get the relief.

When asked what kind of investment would be needed, he said to adequately delineate a prospect an applicant might have to drill additional wells, etc.

"It's a major hurdle for them," Banks said.

Setting a standard with Pioneer's royalty relief

"We're going to work with Pioneer and see if we can thread the needle with this project." The division will be working under new legislation that streamlined the process for applying for and determining royalty relief – a process that was severely hampered by legislation passed in the mid-1990s, Banks said.

"We have enough tools available to us now," he said. "For example, a sliding scale royalty could be designed to allow for changes in costs and oil prices."

Although Banks had not yet reviewed Pioneer's application, he said if "there is some uncertainty about the resource, we can craft the royalty provision so that the state will get its full royalty if it turns out the resource is bigger than expected. We're going to look at that and other things with Pioneer."

Although Pioneer clearly states in its application that it is looking for fiscal certainty for investors and therefore wants development costs fixed at $80 million and a flat royalty reduction to 5 percent, the company also refers to the part of the statute that requires the state to modify the royalty for an increase or decrease in the price of oil or gas by using a sliding scale royalty or other mechanism. That portion of the statute also says a sliding scale royalty "may be based on other relevant factors such as a change in production rates, projected ultimate recovery, development costs, and operating costs," Pioneer wrote.

Phillips, Unocal, BP once asked for royalty relief

Prior to the 2002 legislative change in the royalty relief statute, the most recent royalty relief request came from Phillips for its Tyonek Deep prospect in Cook Inlet, Banks said.

"My understanding is they backed out because they got caught up in the merger with Conoco," he said, but there were also problems because of a lack of information to make the determination, he said.

"Before that, an application came in from Unocal for royalty relief on all of their Cook Inlet platforms and through the course of the evaluation the state put together a proposal to provide relief for some of the platforms but not all; some were fine, some were beyond rescue, such as Spark which is shut-in now, and some would have qualified for relief.

"Before a final determination could be reached," Banks said Unocal "began pursuing a legislative fix and got it."

The new law allows a platform to "automatically get royalty relief when production falls to a certain amount," he said.

Before Unocal's application, BP applied for royalty relief at Milne Point, "but fairly quickly withdrew their application … they elected not to pursue it."

On fast track to get decision for Pioneer

Banks said the division has "no timetable for making a decision on Pioneer's (royalty relief) application other than to say that the company undoubtedly needs a decision fairly quickly."

Whatever is decided, he said, has to be approved by the governor.

"We're going to try to work on this as fast as we can," Banks said.

The application for royalty relief was made on behalf of Pioneer and its working interest partner Armstrong Alaska, an affiliate of Denver-based Armstrong Oil & Gas. Armstrong originally assembled the prospect, which was initially called Northwest Kuparuk.

In addition to the four leases, Pioneer said the June 15 unit expansion request will include other state leases adjacent to the Oooguruk unit.●

continued from page 1

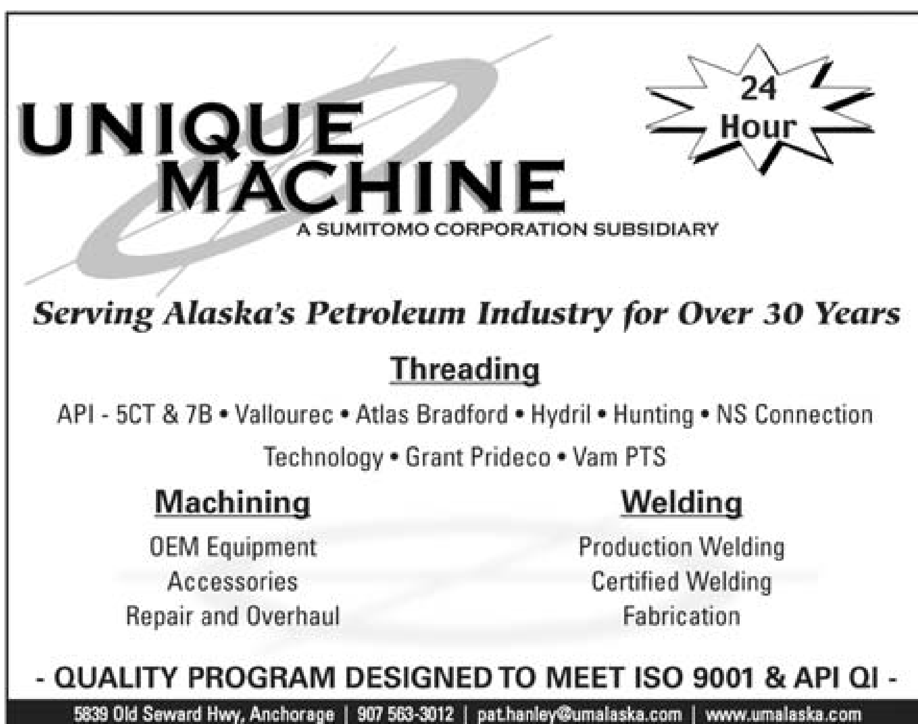
WELLS

Following is the information Pioneer provided about the wells with its application, beginning with the lease number, well driller and name, and the year the well was drilled. Those with an astrix were certified to be capable of production in paying quantities.

- ADL 355036 ARCO Kalubik No. 1 1992*
- ARCO Kalubik No. 2 1998
- ADL 355037 Texaco Colville Delta No. 1 1985*
- Texaco Colville Delta No. 1A 1985
- ADL 355038 Texaco Colville Delta No. 2 1986*
- ADL 355039 Texaco Colville Delta No. 3 1986*
- ADL 379301 Exxon Thetis Island No. 1 1993*
- ADL 389959 ARCO Kalubik No. 3 1998

The four state leases included in Pioneer's royalty relief application have gone through several transfers of ownership over the years. As a result, current working interest owners include a number of companies. Pioneer and Armstrong have the largest chunks, but OXY and Herbaly LLC also hold substantial portions. Anadarko, Hunt, and Joyce hold 2-4 percent pieces, depending on the lease and the interval.

—KAY CASHMAN



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OIL SANDS

often agonizing struggle since the Parliament of Canada passed legislation in 1893 approving funds for the Geological Survey of Canada to probe the oil sands as a source of energy.

There was even a time when the Alberta government was ready to approve the use of atomic bombs almost on the scale of those that destroyed Hiroshima and Nagasaki to trigger an underground nuclear inferno to turn bitumen into a liquid that would eventually be brought to the surface.

Canadian atomic energy and defense authorities had given preliminary approval to the idea, but some suspect the government deliberately avoided controversy by never completing a necessary technical report.

It wasn't until 1967 that the first modern oil sands project, now owned by Suncor Energy, started commercial production near the tiny river town of Fort McMurray.

Science drops costs by $25 per barrel

Since then, the technological improvements have seen the cost of separating the bitumen from a mixture of sand, water and clay fall from more than C$25 per barrel to less than half that – savings that afford companies a "safety net" for a time when oil prices fall.

"It's technology that got us where we are today and it's going to be technology that gets us where we need to go," says Eric Newell, who retired after 14 years as chief executive officer of Syncrude Canada, the consortium that will soon pump 350,000 barrels per day from the oil sands.

Scorning those who question the economics of the oil sands, he says there's a wave of new technology being developed that makes him very bullish about the resource.

Advances needed

The need for advances is critical.

Natural gas is a vital element in the extraction and processing of raw bitumen. In simple terms, you need energy to produce energy.

To achieve the ambitious target of five million barrels per day of oil sands output would consume an "unthinkable" 60 percent of all the natural gas from Western Canada and the Arctic, the Alberta Chamber of Resources warns.

But the chamber acknowledges that many areas of fundamental science have brought the oil sands to their current advanced stage and new science has the potential to provide long-term answers.

The need for breakthroughs is emphasized by John Richels, president of Devon Energy, who says that "if we are going to exploit and properly develop the oil sands, we have to find a way that involves something more than truck and shovel or conventional mining techniques."

What are the possibilities?

So what answers might lie in the alphabet soup?

SAGD – Developed in 1978 by Roger Butler at Imperial Oil, it involves drilling twin wells to bitumen deposits that are buried too deep to scoop out with mechanical shovels.

One well injects steam that breaks down the bitumen and forces it to the surface through the second well. EnCana and Petro-Canada have advanced to using SAGD for full-scale production.

Because SAGD projects can be developed in phases, construction costs are easier to manage than the massive mining ventures.

But there are drawbacks. SAGD requires natural gas to produce steam and needs water – two commodities that are expensive and limited.

MSAR – A possible fuel alternative to natural gas that is made from a mixture of bitumen, water and detergent and has combustion characteristics matching that of gas.

It was first developed by BP and PDVSA, Venezuela's state-owned oil company, in the 1980s for the heavy oil fields of Venezuela.

MSAR is now being tested in a pilot project involving Petro-Canada, ConocoPhillips, Deer Creek Energy and Paramount Resources.

Quadrise Canada Fuel Systems, a private Calgary-based firm, has assembled a 14-member team to promote the use of MSAR in oil sands in-situ projects over the next few years, projecting the fuel will lower the costs of bitumen production by US$2.50 per barrel compared with natural gas, although it will require the reinjection of carbon dioxide emissions.

VAPEX – It's a technology that is being tested, using a vaporized solvent such as propane, to reduce the stickiness of bitumen. VAPEX proponents believe their technology will use less steam and water than SAGD, thus lowering costs. VAPEX is thought to be a couple of years away from commercial application.

SAP – A pilot project in Saskatchewan that added a small amount of solvent to steam indicated the flow rate of oil was increased by more than 50 percent. More tests are underway in Alberta.

THAI – Yet another revolutionary technology, this involves pumping air to ignite the bitumen, allowing the oil to flow almost immediately through a second well – thus from the "toe" of the well to the "heel" using air injection, or THAI.

Proponents estimate the method can recover 80 percent of the original oil in place and partially upgrade the crude at the same time. ●

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GULF OF MEXICO

Pioneer begins production from new Gulf well

Exploration and production independent Pioneer Natural Resources said June 8 that it has begun production from a new gas well at the company's deepwater Gulf of Mexico Raptor field in the Falcon Corridor, located in the East Breaks area. The Raptor well tested at about 30 million cubic feet of natural gas per day, Pioneer said, adding that system pressure will limit the incremental production impact. But the new Raptor well is expected to extend the productive life of the Falcon Corridor system and generate a return on investment in excess of 100 percent, the company said.Pioneer holds a 100 percent interest and operates the three fields which are tied into the Falcon facilities. Over the remainder of 2005, Pioneer said it plans to drill and operate two additional wells in the deepwater U.S. Gulf of Mexico.

They are the Clipper prospect, an amplitude play located in the Green Canyon area in which Pioneer has a 55 percent interest, is currently drilling. The Paladin prospect, a sub-salt well located in the Garden Banks area in which Pioneer expects to own about a 40 percent interest, is expected to spud during the third quarter.

The company said it also plans to drill three to four wells on the Gulf's continental shelf before year-end.

—RAY TYSON

NORTH AMERICA

Canada's rig count up by 104, U.S. up by 22

The number of rotary drilling rigs operating in the United States and Canada during the week ending June 3 totaled 1,728 rigs, up by a combined 128 rigs from the previous week and up by 304 rigs from the same period last year, according to rig monitor Baker Hughes. The rig count in Canada alone surged by 104 to 375 rigs from the previous week and was up by 119 rigs compared to the year-ago period.

The number of rigs operating in the United States stood at 1,353, an increase of 22 rigs from the prior week and an increase of 185 rigs from last year. The number of land rigs increased by 18 to 1,231 rigs, while offshore rigs increased by four to 98 rigs. Inland water rigs were unchanged with 24 rigs.

Of the total number of rigs operating in the United States during the recent week, 1,206 rigs were drilling for gas and 146 rigs for oil; one rig was being used for miscellaneous uses. Of the total, 844 wells were vertical, 333 directional and 176 horizontal.

Among the leading U.S. producing states during the recent week, Texas gained 12 rigs for a total of 611, Louisiana picked up six for a total of 187; Colorado increased by three to 70; Oklahoma increased by three to 154; and California increased by one to 24. Alaska's rig count was unchanged with nine rigs.

—RAY TYSON

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WYOMING

BLM sale fetches over $6.5 million

Receipts totaling $6,586,982 were received for leasing rights on parcels offered by the Bureau of Land Management at the bi-monthly federal oil and gas lease oral auction held in Cheyenne, Wyo. on June 7, BLM said in a press release.

Bids totaling $6,330,437 ranged from the federally mandated minimum of $2 per acre to $500 per acre. That bid was for a 241 acre parcel in Carbon County that was won by Marshall and Winston Inc., of Midland, Texas.

The highest bonus bid of $478,400 was for a 1,195 acre parcel in Carbon County, which was won by Baseline Minerals Inc., of Denver, Colo. Successful bidders also pay a $75 per parcel administrative fee and yearly rental of $1.50 per acre.

In addition to the bids, the sale netted $243,570 in first year rental fees, and $12,975 in administrative fees. Half of bid and rental receipts go to the state of Wyoming.

A total of 175,311.740 acres in 189 parcels were offered at the sale. A total of 162,339.320 acres in 173 parcels were sold. Average bid per acre for each acre sold was $39 and the average parcel sold netted $36,592.12 from bidding.

The next auction will be held on Aug. 2 in Cheyenne.

—PETROLEUM NEWS

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