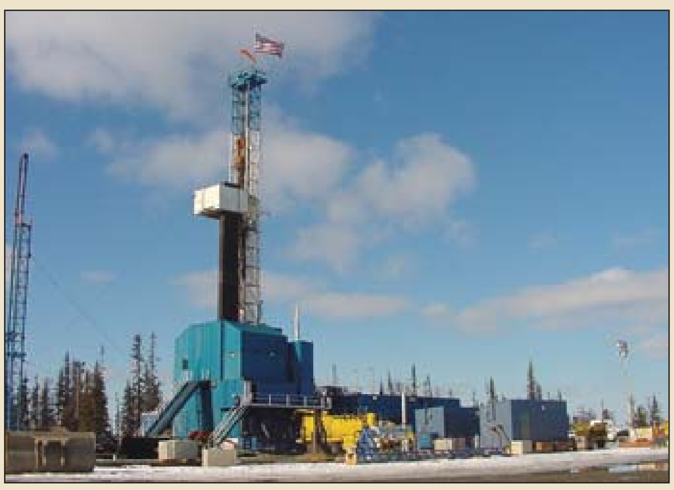
Petroleum news

page 9 Mounties ride into thick of election with criminal probe

Vol. 11, No. 2 • www.PetroleumNews.com — *A weekly oil & gas newspaper based in Anchorage, Alaska* — Week of January 8, 2006 • $1.50

Headed to Northern Dancer



COURTESY KUUKPIK DRILLING LLC

The Kuukpik rig no. 5 that will drill the Storm Cat well

Storm Cat mobilizes Kuukpik rig for Mat-Su gas drilling

Storm Cat Energy Corp. has contracted Kuukpik Drilling LLC to mobilize a rig to drill a well near Big Lake in Alaska's Matanuska-Susitna Borough, north of Anchorage, Scott Zimmerman, president and CEO of Storm Cat told Petroleum News on Jan. 4. Drill site construction will start some time next week, with a spud date in mid to late January — the spud date will depend on Storm Cat obtaining permits that are currently being processed, Zimmerman said.

Conventional natural gas

If all goes according to plan the Kuukpik No. 5 rig will drill the well to a conventional gas prospect in the Tyonek formation at a depth of about 7,500 feet. The well will be on an Alaska Mental Health Trust lease. Zimmerman hopes to have results

see **STORM CAT** *page 15*

Shell game sets off rumors

SHARES OF SHELL CANADA hit record heights at the end of 2005, fueled by rumors that Royal Dutch Shell might buy out the 22 percent it doesn't already own.

Neither company would comment on market speculation, leaving analysts to conjecture on the validity of the chatter.

The consensus thinking points to a number of options should the parent company attempt to absorb its Canadian unit including a share-exchange offer worth about C$7.6 billion, taking advantage of the recent unification of its previously dual corporate structure.

Other possibilities include capital investment and external acquisitions, using Royal Dutch Shell's surplus cash.

see **INSIDER** *page 15*

BREAKING NEWS

4 Oil found at Big Foot: Chevron, Anadarko, Plains hit 300 feet of net oil pay in deepwater Gulf prospect 225 miles south of New Orleans

4 Eminent domain draws six pre-files: Four House bills, two Senate bills; all restrict use of power; one bill extends it for O&G resources

7 North Slope output down: ANS oil production dropped 3.6 percent in December, to 859,838 bpd, Prudhoe has biggest drop

CANADA

Hearings on grand scale

On brink of dual reg processes for Mac project; Arctic gas future on the line

By GARY PARK
For Petroleum News

Ready or not, residents of northern Canada — along with regulators, lawyers, consultants, engineers, politicians, environmentalists and others — are about to be plunged into an epic round of hearings that are unprecedented for any capital undertaking in Canadian history.

On the line is a decades-long dream of turnings vast Arctic natural gas resources into a commercial venture that could eventually carry 1.9 billion cubic feet per day to Canadian and U.S. markets.

Before 2006 is over it should be clear whether the Mackenzie Gas Project is on track for completion in 2011, or whether Canada's northern petroleum riches will be shouldered aside by the much larger Alaska Highway gasline.

Sierra Club directors Elizabeth May and Carl Pope have made a case to ExxonMobil (parent of Imperial Oil, the Mackenzie's lead partner) to abandon their Canadian plans "in favor of advancing" Alaska.

By the middle of February, parallel hearings are due to start rolling across the Northwest Territories and extending into Alberta.

NEB begins Jan. 25

The National Energy Board has set Jan. 25 —

see **HEARINGS** *page 16*

COOK INLET

New contract sparks debate

Cook Inlet explorers, state, individuals challenge Marathon-Enstar gas deal

By ALAN BAILEY
Petroleum News

STEVEN MERRITT

The skyline of Anchorage, Alaska

Ask residents of Anchorage, Alaska, about natural gas and most will probably cite escalating price levels as a prime concern. But with gas supplies from the neighboring Cook Inlet basin set to decline, people are also becoming increasingly aware of the possibility of gas shortages.

Ensuring continuity of future gas supplies has become a major focus for Enstar Natural Gas Co., the main gas utility serving the Anchorage area. And in November 2005 Enstar agreed to a new gas supply contract with Marathon Oil Corp. That contract would assure sufficient gas to meet Enstar's needs through at least 2016, by which time there may be a spur pipeline delivering North Slope gas to the Anchorage area.

"The good news is that we've finally been able to negotiate supply for that period of serious uncertainty between now and … when we might see North Slope gas," Tony Izzo, president and CEO of

see **CONTRACT** *page 14*

JUNEAU

Old, new bills on agenda

House Ways to hear gas, oil tax bills; another proposes uniform permit app

By KRISTEN NELSON
Petroleum News

Rep. Berta Gardner

Sen. Gretchen Guess

The 24th Alaska Legislature reconvenes for its second session Jan. 9, and while it is waiting, along with the rest of the state, for a gas pipeline fiscal contract to review, it has other oil and gas issues on its agenda.

House Ways and Means has already scheduled hearings on two oil and gas tax measures introduced last session: House Bill 63, by Rep. Les Gara, D-Anchorage, an oil severance tax bill and HB 223, a natural gas pipeline incentive/gas tax, by Rep. Eric Croft, D-Anchorage, bills designed to garner more revenue for the state under high oil prices and to tax gas if a gas line is not built.

Other legislators have pre-filed matching House-Senate bills which address oil and gas permitting issues.

Rep. Berta Gardner and Sen. Gretchen Guess, both Anchorage Democrats, pre-filed bills requiring adoption of a "unified permit application form by the natural resource agencies; and providing for online per-

see **AGENDA** *page 15*

contents

Petroleum News | *A weekly oil & gas newspaper based in Anchorage, Alaska*

Alaska - Mackenzie Rig Report

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status

Alaska Rig Status

North Slope - Onshore

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
Doyon Drilling			
Dreco 1250 UE	14 (SCR/TD)	Milne Point H-pad MPC-28a	BP
Sky Top Brewster NE-12	15 (SCR/TD)	Kuparuk 1C-20	ConocoPhillips
Dreco 1000 UE	16 (SCR)	Workover well DS11-38a	BP
Dreco D2000 UEBD	19 (SCR/TD)	Alpine CD4-318	ConocoPhillips
OIME 2000	141 (SCR/TD)	Kuparuk 1J-101	ConocoPhillips
TSM 7000	Arctic Fox #1	Rigging up on Hailstorm #1	Pioneer Natural Resources
Nabors Alaska Drilling			
Trans-ocean rig	CDR-1 (CT)	Stacked, Prudhoe Bay	Available
Dreco 1000 UE	2-ES (SCR)	Prudhoe Bay 01-08Ai	BP
Mid-Continental U36A	3-S	Kuparuk 1D-134	ConocoPhillips
Oilwell 700 E	4-ES (SCR)	WGI-08	BP
Dreco 1000 UE	7-ES (SCR/TD)	Prudhoe Bay V-46	BP
Dreco 1000 UE	9-ES (SCR/TD)	L-123i	BP
Oilwell 2000 Hercules	14-E (SCR)	Staged at Cape Simpson	FEX
Oilwell 2000 Hercules	16-E (SCR/TD)	Stacked, Prudhoe Bay	Available
Oilwell 2000	17-E (SCR/TD)	Stacked, Point McIntyre	Available
Emsco Electro-hoist -2	18-E (SCR)	Stacked, Deadhorse	Available
OIME 1000	19-E (SCR)	Stacked, Deadhorse	Available
Emsco Electro-hoist Varco TDS3	22-E (SCR/TD)	Stacked, Milne Point	Available
Emsco Electro-hoist	28-E (SCR)	Stacked, Deadhorse	Available
OIME 2000	245-E	Stacked, Kuparuk	Available
Emsco Electro-hoist Canrig 1050E	27-E (SCR-TD)	Stacked on 12-acre pad	Available
Nordic Calista Services			
Superior 700 UE	1 (SCR/CTD)	1D-27, Prudhoe Bay	BP
Superior 700 UE	2 (SCR/CTD)	Well 3H-14 Kuparuk	BP
Ideco 900	3 (SCR/TD)	Kuparuk, 2T-208	ConocoPhillips

North Slope - Offshore

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
Nabors Alaska Drilling			
Oilwell 2000	33-E	NorthStar NS-10	BP

Cook Inlet Basin – Onshore

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
Aurora Well Service			
Franks 300 Srs. Explorer III	AWS 1	Stacked in Nikiski	Available
Kuukpik	5	Mobilized for Northern Dancer #1	Storm Cat
Marathon Oil Co.			
Taylor	Glacier 1	KBU 24-6 RD	Marathon
Nabors Alaska Drilling			
National 110 UE	160 (SCR)	Stacked, Kenai	Available
Continental Emsco E3000	273	Stacked, Kenai	Sold
Franks	26	Stacked	Available
IDECO 2100 E	429E (SCR)	Stacked, removed from Osprey platform	Available
Rigmaster 850	129	Middle Lake Unit #1	Forest Oil

Cook Inlet Basin – Offshore

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
Unocal (Nabors Alaska Drilling labor contractor)			
Not Available			
XTO Energy			
National 1320	A	Rig move on platform A	XTO
National 110	C (TD)	Idle	XTO

Mackenzie Rig Status

Canadian Beaufort Sea

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
Seatankers (AKITA Equtak labor contract)			
SSDC CANMAR Island Rig #2	SDC	Paktoa C-60	Devon ARL Corp.

Mackenzie Delta-Onshore

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
AKITA Equtak			
Dreco 1250 UE	62 (SCR/TD)	Stacked in Tuktoyaktuk, NT	Available
National 370	64	On barges moving to Hay River & then on trucks to Alberta.	Available

Central Mackenzie Valley

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
AKITA Equtak			
Rigmaster 850	40	Expects to move to Summit Creek K-44 on 1/10	Husky Oil
Dreco 1250 UE	63 (SCR/TD)	Moving to Stewart D-57 location. Est. spud 1/19	Husky Oil
AKITA/SAHTU			
Oilwell 500	51	Working in Alberta	Apache

Yukon Territories Rig Status

Yukon

Rig Owner/Rig Type	Rig No.	Rig Location/Activity	Operator or Status
AKITA/Kaska			
National 80UE	58	Stacked in Fort Liard, NT. Move to Beaver River mid Jan.	Talisman Energy
Ensign Resources Svc. Grp.			
Jackknife Double	55	Racked in Ft. Nelson	

The Alaska - Mackenzie Rig Report is sponsored by:

ConocoPhillips

The Alaska - Mackenzie Rig Report as of January 4, 2006. Active drilling companies only listed.

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

This rig report was prepared by Alan Bailey

JUDY PATRICK

Baker Hughes North America rotary rig counts*

	Dec. 30	Dec. 22	Year Ago
US	1,471	1, 475	1,243
Canada	364	532	346
Gulf	75	75	100

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

GULF OF MEXICO

Oil found at Big Foot in deepwater Gulf

Operator Chevron said Jan. 4 that 300 feet of net oil pay has been found at the Gulf of Mexico deepwater Big Foot prospect in Walker Ridge block 29 some 225 miles south of New Orleans.

The Big Foot No. 2 discovery well is in approximately 5,000 feet of water and was drilled to a total depth of 25,127 feet, encountering as much as 300 feet or more of net oil pay, Chevron said.

Drilling is under way at a sidetrack well and Chevron said further appraisal drilling will be required to determine commercial potential of the discovery.

Chevron, which owns a 60 percent working interest in Big Foot, is the operator; Anadarko Petroleum Corp. has 15 percent, Plains Exploration and Production Co. 12.5 percent and Shell 12.5 percent.

Big Foot follows Knotty Head

Ray Wilcox, president of Chevron North American Exploration and Production Co. called Big Foot the company's "latest success in the deepwater Gulf of Mexico," and said the discovery should "ultimately provide the country with much needed crude oil and natural gas."

"Big Foot follows our earlier success at the Knotty Head discovery and is confirmation of further potential of our exploration acreage," said Paul Siegele, vice president of Chevron's Gulf of Mexico deepwater business unit. Chevron is the largest overall leaseholder in the Gulf of Mexico, the company said.

Bob Daniels, Anadarko senior vice president, exploration and production, said the Big Foot discovery, following the December announcement of the Knotty Head discovery (see story in Dec. 25, 2005, issue of Petroleum News), "further validates the extensive middle-to-lower Miocene play we are aggressively pursuing within the foldbelt area." He said that including Anadarko's wholly owned Genghis Khan discovery, the company was "successful in three out of four foldbelt exploration wells during 2005." Daniels said Anadarko expects to participate in five delineation and exploration wells in the first quarter of 2006. "The deepwater Gulf of Mexico will be a major piece of our overall growth plan in the coming years," he said.

—PETROLEUM NEWS

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● ALASKA

Eminent domain issue draws six pre-files

Four bills in House, two in Senate; all restrict use of power; one bill also would extend it for developing O&G resources

By KRISTEN NELSON
Petroleum News

Bills pre-filed for the second session of the 24th Alaska Legislature include six prohibiting exercise of eminent domain for economic development. Eminent domain is the power to take private property for public use by government with just compensation.

HB 319, by Rep. Eric Croft, D-Anchorage, while it would prohibit "the exercise of eminent domain to acquire property for transfer to a private person" would specifically authorize "the exercise of the power of eminent domain for the purpose of developing the state's oil and gas resources."

Four of the eminent domain bills are in the House and two are in the Senate.

One of the bills, however, would make a specific exception for development of the state's oil and gas resources.

Current state law provides that right of eminent domain may be exercised for public uses including uses authorized by the U.S. government, public buildings and grounds for state use and other public uses authorized by the Legislature, public buildings and grounds for the use of organized or unorganized boroughs, cities, towns, villages, school districts or other municipal divisions. Eminent domain may also be exercised for canals, aqueducts, flumes, ditches or pipes conducting water, heat or gas for the use of local inhabitants, for raising the banks of streams, removing obstructions and widening, deepening or straightening channels, and for roads, streets and alleys.

Eminent domain may be exercised for facilities such as wharves, docks, piers, ferries, bridges, private roads, railroads, canals and pipes for public transportation or for supplying mines and farming neighborhoods with water, draining and reclaiming land, for floating logs and lumber on non-navigable streams and for reservoirs to collect and store water.

There is an extensive list of mine-related uses of eminent domain, which can also be exercised for private roads leading to highways, for telephone and telegraph lines, sewerage, tramway lines, electric power lines and for "location of pipelines for gathering, transmitting, transporting, storing, or delivering natural or artificial gas or oil or any liquid or gaseous hydrocarbons, including, but not limited to, pumping stations, terminals, storage tanks, or reservoirs, and related installations."

Economic development prohibited

The bills pre-filed for this session would

see DOMAIN page 5

NORTH AMERICA

New U.S. outlets for Canadian heavy crude

Aside from the welter of major new crude pipeline projects out of Alberta, smaller gains are under way in the United States, with new pipeline and refinery projects being announced Jan. 3.

Minnesota Pipe Line, operated by Koch, has launched plans to absorb more Canadian crude at the Minneapolis and St. Paul refineries, while a Kansas refinery is boosting capacity to process Canadian heavy crudes.

Minnesota Pipe Line said it is seeking regulatory approval to spend $300 million building 300 miles of new 24-inch diameter line from Clearbrook, Minn., where it takes crude off the Enbridge network, to the St. Paul area.

The initial expansion, due for completion by early 2008, will add 160,000 barrels per day of capacity to the Minnesota system, which is currently running at its 300,000 bpd capacity.

But the expansion project is being designed to eventually handle 350,000 bpd.

Minnesota project manager Larry Van Horn said the undertaking will “provide another outlet for Canadian producers to get their barrels to growing markets,” while providing an option to transport condensate to Canada’s heavy crude producers at some later date.

The refineries are Flint Hill’s 280,000 bpd Pipe Bend facility and Marathon Oil’s 70,000 bpd plant at St. Paul.

Meanwhile, Coffeyville Resources is spending $92 million to raise capacity at its Kansas refinery by 15 percent to 115,000 bpd by year’s end.

The additions will result in more heavy crudes run through the plant, which is due to process its first barrel of Canadian crude in March.

Until now the refinery has processed light sweet grades gathered from Kansas and Oklahoma and some crudes from Latin America.

—GARY PARK

continued from page 4

DOMAIN

all prohibit use of eminent domain for “economic development,” an issue of concern since private property in the Lower 48 has been condemned to allow private development which benefits the tax rolls of the entity condemning the property.

House Bill 317, by Rep. Bob Lynn, R-Anchorage, would prohibit “the exercise of eminent domain by the state and by its home rule and general law municipalities for the purpose of economic development” and would also repeal “the authority of the Alaska Housing Finance Corporation under the Slum Clearance and Redevelopment Act to exercise the power of eminent domain to acquire real property.”

Lynn’s bill provides that “eminent domain may not be exercised for the purpose of promoting economic development or to acquire land as part of an economic development project.” Economic development is defined as “an activity intended primarily to increase a municipality’s tax revenue, expand a municipality’s property tax base, create new jobs or retain existing jobs in a municipality, or improve the overall economic vitality of a municipality.”

One proposal excludes parks

HB 318, by Rep. Lesil McGuire, R-Anchorage, and co-sponsored by Reps. Mike Hawker, R-Anchorage, Bill Stoltze, R-Chugiak/MatSu, Carl Gatto, R-Palmer, Peggy Wilson, R-Wrangell, Vic Kohring, R-Wasilla, Gabrielle LeDoux, R-Kodiak, Nancy Dahlstrom, R-Anchorage and Mike Kelly, R-Fairbanks, broadens the restriction by specifying that “the right of eminent domain may not be exercised for the purpose of promoting economic development or to acquire land as part of an economic development project,” but also says that if property is the “primary residence of the owner of the property, the right of eminent domain may not be exercised for the purpose of developing a recreational facility or project, including a park, natural resource use area, trail or pedestrian pathway, greenbelt, access to a wilderness area, amusement park, small boat facility, personal use fishery, sports facility, playground, or infrastructure or other facility related to or in support of an indoor or outdoor recreational facility or project.”

HB 337, by Rep. Jim Holm, R-Fairbanks, specifies that the right of eminent domain may not be exercised to acquire land for the purpose of “transferring the land to a private landowner; ... increasing property tax income or other revenue to the state or a municipality; ... creating jobs; or ... creating or expanding economic development.”

Senate Bill 221, by Sen. Ralph Seekins, R-Fairbanks, is the Senate version of HB 337.

SB 205, by Sen. Con Bunde, R-Anchorage, specifies that “the right of eminent domain may not be exercised for the purpose of promoting economic development or to acquire land as part of an economic development project.”

Croft proposes use for oil and gas

HB 319, by Rep. Eric Croft, D-Anchorage, while it would prohibit “the exercise of eminent domain to acquire property for transfer to a private person” would specifically authorize “the exercise of the power of eminent domain for the purpose of developing the state’s oil and gas resources.”

Croft’s bill proposes that gas and oil be added to existing rights for entry “and the right to take from the earth, gravel, stones, trees and timber as may be necessary for a public use.” ●

QUEBEC

Quebec renews search for hydrocarbons

Talisman, Questerre to drill for gas this year; juniors partner with provincial utility, hoping for first commercial oil find

By GARY PARK

For Petroleum News

From shaky beginnings, Quebec is staging a renewed push to join Canada's hydrocarbon producing provinces.

Talisman Energy has linked up with Calgary-based junior Questerre Energy to drill a gas well this year and two other juniors — partners with Hydro-Quebec, the provincially owned utility giant — have raised hopes of Quebec's first commercial oil find.

Talisman and Questerre plan to drill their well in the St. Lawrence Lowlands between Montreal and Quebec City, targeting a structure that is an extension of Talisman's highly successful Trenton Black River play in the U.S. Appalachian region where the big Canadian independent is investing heavily and producing about 115 million cubic feet per day.

Other targets identified by the partnership are a deeper sandstone structure and a tight gas play.

Each holds the prospect of yielding gas in the billions of cubic feet, supported by Quebec government fiscal terms that Questerre Chief Executive Officer Michael Binnion rates as some of the best anywhere.

Talisman, which could spend up to C$6 million in Quebec this year, has a farm-in arrangement with Questerre to pay for the cost of drilling up to four wells to earn an interest in Questerre's land holdings.

Two wells with potential

Hydro-Quebec was an early partner with Questerre before dropping out, but is partnered with Junex and Gestion Bernard Lemaire in drilling three wells on the Gaspésie Peninsula.

Of the three wells on the Galt block, two have shown some potential, according to Jean-Sebastien Marcil, exploration chief for Junex. They were drilled to depths of 7,700 feet and 8,850 feet and indicated the presence of oil, gas and condensate without any water from depths of 2,600-9,800 feet.

Initial production tests in fall 2004 yielded about 185 barrels of clean light oil from one well, prompting the partners to undertake a "stimulation" job at a depth of 7,200 feet.

Depending on results of the extended production test, Junex hopes to raise as much as C$10 million to support the drilling of at least two more wells, a company spokesman said.

Junex will also continue work on a prospect west of Montreal and is preparing to drill three to six new shallow wells in partnership with Petrolia.

Exploration in the Gaspésie Peninsula started over a century ago with the drilling of 100 shallow wells along oil seepage areas, while companies such as Shell Canada and Husky Energy explored for hydrocarbons 50 years ago. Two commercial gas finds in the 1970s have since been produced.

Junex has spent the last 10 years working in the Gaspésie Peninsula, starting with the development of an oil well drilled in the 1980s and, in partnership with Petrolia, has accumulated 3.5 million acres of exploration land, identifying prospective zones that the company says are "considered favorable for hydrocarbon discovery."

As with major oil and gas producing areas, the latest hunt in Quebec is buoyed by advances in exploration technology.

Binnion is emphatic that there is gas to be found, noting that 90 percent of wells in Quebec have encountered gas, but the challenge is to find a pool that is big enough to support a commercial undertaking. ●

CALGARY

Producer fades away in sour gas case

Compton Petroleum will continue to produce from two wells on outskirts of Calgary, Alberta board denies request for extension of filing to August, January filing deadline passes

By GARY PARK

For Petroleum News

It is back to square one in a test case involving trillions of cubic feet of Alberta's gas future.

A showdown between gas producer Compton Petroleum and a formidable array of local government, health, environmental and community organizations — already the most protracted well license hearing in the province's history — may have to start from scratch if Compton hopes to develop sour gas on Calgary's outskirts.

The company passed up the chance to file an emergency response plan with the Alberta Energy and Utilities Board by a Jan. 3 deadline.

That, in turn, could scuttle any hopes by other producers to start developing sour gas resources close to major population centers.

In a surprise pre-Christmas ruling, the board denied Compton's request to extend to Aug. 1 the deadline for submitting its response plan tied to plans for drilling four sour gas wells southeast of the Calgary city limits.

However, Compton said it will continue to produce gas from two previously approved wells in the area.

Future of 40% of remaining gas in doubt

What is now in some doubt is the future of 40 percent of Alberta's remaining gas reserves, as operators and rapidly growing cities reach a crossroads.

The energy board has estimated that 6,000 "significant" sour gas wells are producing close to settlements in Alberta, including 105 in the vicinity of Calgary, pumping C$1.5 billion a year into government revenues and accounting for 37,000 jobs.

The cost has been equally high, with 37 industry workers killed by exposure to sour gas over the past 30 years.

But, other than a 68-day blow out in 1982 that killed two workers and spread a rotten-egg smell over a wide swath of Alberta, sour gas has been slow to register on the minds of most Albertans until more recent years.

Plans unveiled in 2001

That changed in 2001 when Compton unveiled plans to drill wells near Calgary to tap a reservoir of 68 billion cubic feet, with a hydrogen sulfide content of 35.6 percent that could affect 250,000 residents — 25 percent of Calgary's population — in the event of a blowout or leak.

Community fears dominated a 30-day board hearing that culminated June 22 when the regulator approved four of Compton's proposed six wells, but underscored its own concerns by requiring Compton to develop an improved emergency response plan after rejecting the initial plan as inadequate.

The City of Calgary and the Calgary Health Region were in the forefront of those objecting to Compton's wells.

They have appealed the board's decision and declined to cooperate with Compton in developing a response plan.

Board: Compton didn't complete all tasks

But the board said Compton had failed to demonstrate that it had completed all of the tasks that didn't require cooperation with other organizations and had failed to demonstrate that it was prevented from meeting the Jan. 3 deadline as a result of circumstances beyond its control.

Missing the deadline has been deemed by the board as an abandonment of the applications and will result in the file being closed.

That is a serious blow to industry proponents such as the Canadian Association of Petroleum Producers who argue that the expertise has been developed to safely drill for and develop sour gas and Energy Minister Greg Melchin, who argues that driving a car is a "far greater hazard" than developing sour gas.

With the board taking a hard line and community opposition at such a high level, it is expected that other companies hoping to follow a successful Compton application and drill close to Calgary will quietly fade from the scene. ●

● ALASKA

North Slope output down 4 percent

By KRISTEN NELSON
Petroleum News

Alaska North Slope production dropped 3.6 percent in December, averaging 859,838 barrels per day compared to 892,192 bpd in November, a 12.4 percent drop from December 2004, when North Slope production averaged 981,072 bpd.

With the exception of Milne Point, all North Slope fields declined in production from November to December.

The Alaska Department of Revenue estimated ANS production for the current 2006 fiscal year (July 2005 through June 2006) at 865,000 bpd, compared to 917,000 bpd for FY '05.

Prudhoe Bay had the largest per-barrel drop (23,428 bpd) and the second-highest percentage drop, 5.5 percent, averaging 400,965 bpd in December compared to 424,393 bpd in November. BP Exploration (Alaska)-operated Prudhoe includes the western Prudhoe satellites: Midnight Sun, Aurora, Polaris, Borealis and Orion.

The highest percentage drop, 8.33 percent, was at BP's Northstar field, which averaged 54,990 bpd in December down from 59,984 bpd in November. Revenue said the field had compressor problems Dec. 2-4 which appeared to be resolved by Dec. 5. Northstar production, which began the month at 60,740 barrels, dropped to 22,873 barrels Dec. 2, and only reached the 60,000 barrel level again Dec. 6; production dropped into the 40,000 bpd range Dec. 25-26, recovering into the 56,000-57,000 bpd range at the end of the month.

Milne only field with increase

Production from BP-operated Lisburne (which includes Point McIntyre and Niakuk) averaged 38,894 bpd in December, down 4.7 percent from a November average of 40,799 bpd.

BP-operated Endicott averaged 21,072 bpd, down 2.8 percent from a November average of 21,673 bpd.

The ConocoPhillips Alaska-operated Kuparuk River field (including production from West Sak, Tabasco, Tarn, Meltwater and Palm) averaged 169,348 bpd in December, down 1.5 percent from a November average of 171,998 bpd.

Alpine, also operated by ConocoPhillips Alaska, averaged 129,910 bpd down 0.5 percent from a November average of 130,597 bpd.

JUDY PATRICK

Prudhoe Bay had the largest per-barrel drop (23,428 bpd) and the second-highest percentage drop, 5.5 percent, averaging 400,965 bpd in December compared to 424,393 bpd in November.

BP's Milne Point field was the only one with a month-to-month increase in production, averaging 44,659 bpd, up 4.8 percent from a November average of 42,748 bpd.

The temperature at Pump Station No. 1 on the North Slope averaged minus 2.5 degrees Fahrenheit in December, up from a November average of minus 9.6 degrees F. The three-year December average is minus 3.9 degrees F.

Cook Inlet production averaged 18,893 bpd in December, up 0.6 percent from a November average of 18,790 bpd. ●

ALASKA

BLM OKs TAPS plans with requirements

The Joint Pipeline Office said Jan. 4 that the Bureau of Land Management has given its annual approval for the trans-Alaska pipeline system oil spill contingency plan, but with approval requirements.

Alyeska Pipeline Service Co., the trans-Alaska oil pipeline operator, was told to prepare a summary report upon completion of improvements at the Gulkana and Copper rivers, and to work through the response planning group (Alyeska and agency representatives) to develop a maintenance program addressing periodic vegetation clearing at culverts. Alyeska is also to develop and adopt a method for documenting hands-on training through the response planning group, establish minimum training requirements and standardize duty rosters by June 30.

Alyeska is also required to develop and conduct oil spill exercises using terrorist attack scenarios along the pipeline right of way or at the pump stations, involving appropriate security agencies.

—PETROLEUM NEWS

● NEW YORK

Oil prices end 2005 above $61 a barrel

Oil prices up 40% from start of year, natural gas surged 80%; U.S., Chinese demand expected to keep prices up, in $50 range

By BRAD FOSS
Associated Press Business Writer

Oil futures settled above $61 a barrel Dec. 30 and finished 40 percent higher than they started in 2005, capping a tough year for energy consumers but a great one for the petroleum industry as prices soared amid strong demand and tight supplies.

For similar reasons, there was an even sharper advance in 2005 in the price of natural gas, which surged more than 80 percent, making it extra expensive to produce electricity, manufacture goods and heat homes.

Many analysts believe the average price of oil will be below $60 in 2006, though not by much as U.S. and Chinese economic growth continues and hawkish members of OPEC, such as Venezuela and Iran, express growing interest in a production cut as early as the first quarter.

"Because of China, oil is never going to go to the $18 to $22 level again in our lifetime," said Mike Fitzpatrick, a broker at Fimat USA in New York. "But it certainly doesn't have to be $60."

Fitzpatrick believes average oil prices will be closer to $50 a barrel in 2006, an outlook predicated on a slowdown in economic growth in the second half of the year — because of high energy prices. "At some point, this has to have a deleterious economic effect," said Fitzpatrick, whose price outlook is more bearish than many of his peers.

$50 would be welcome news

While unthinkable just a few years ago, a price near $50 a barrel would actually be welcome news to energy-intensive industries such as airlines and trucking companies, who have retooled their operations to use fuel more efficiently.

There are signs that some homeowners and motorists are also making small changes to keep their energy consumption in check, though analysts say demand is still on the rise and that the tight supply of refining capacity in the United States is likely to boost the country's dependence on imports and keep pump prices high.

Average retail gasoline prices in the United States surged to record territory above $3 a gallon after Hurricane Katrina, which knocked out refineries and caused power outages that disabled pipelines that carry motor fuel from the Gulf Coast to the Northeast and Midwest. Now, the average retail price of gasoline nationwide is $2.19 a gallon, or 41 cents higher than a year ago.

Little excess capacity

One thing that all oil analysts agree on is that the world's largest petroleum producers are pumping almost as much as they can, with little excess production capacity available in the event of a prolonged supply disruption. The mere threat of lost output, whether because of geopolitical strife or a natural disaster, will be enough to keep the market on edge in 2006.

"It won't take much to up the price again next year," said London-based oil analyst John Hall of John Hall Associates.

"My guess is that OPEC is quote committed to holding up the price" at present levels, Hall said.

Hall also focused on Iraq, Iran and Nigeria as potential problem countries, saying output snags and increasing political tensions could drive prices upward.

We're in a post-Christmas lull, but "things will start to warm up when OPEC ministers start talking about what to do," ahead of their January meeting, Hall said. Even now, "they're all saying the same thing — 'we're going to cut.'"

On Dec. 30, light sweet crude for February delivery dropped 46 cents to $59.83 a barrel on the New York Mercantile Exchange by midday in Europe, reversing much of its 50-cent surge the previous day.

Traders focused on U.S. weather

With the Northern Hemisphere winter only a week old, traders remain focused on the weather in the United States, the world's largest energy market.

For that reason, natural gas, which briefly topped $15 per 1,000 cubic feet earlier in December, has been under pressure lately amid forecasts of mild weather in much of the United States.

On Dec. 30, natural gas futures inched 0.2 cent higher to settle at $11.225, up 83 percent on the year. On Dec. 29, the Energy Department said domestic storage of natural gas stood at 2.64 trillion cubic feet on Dec. 23. That is 8 percent below year-ago levels and 1 percent above the five-year average for this time of year.

Heating oil dropped marginally to $1.6925 per gallon, while gasoline futures slipped to $1.6403 a gallon.

On the ICE Futures exchange in London, Brent crude eased 40 cents, to $57.67 a barrel.

The price of Nymex crude is about 14 percent below its Aug. 30 high of $70.85. Oil prices remained above $60 a barrel for months after Katrina disrupted Gulf of Mexico oil and natural-gas output. About one-quarter of the region's daily oil production, and one-fifth of its natural gas production, remains offline, because of damage to offshore platforms, underwater pipelines and onshore processing plants. ●

● CANADA

Mounties ride into thick of election

Start criminal investigation into allegations by left-wingers that investors profited from insider information on income trust ruling

By GARY PARK
For Petroleum News

In its desperate struggle to retain power in Canada, the Liberal party government of Prime Minister Paul Martin has been dealt what many observers think could be a knock-out blow.

The Royal Canadian Mounted Police announced Dec. 28 it has started a criminal investigation into whether anyone in government leaked advance notice of Finance Minister Ralph Goodale's decision on the taxation of income trusts before the official announcement on Nov. 23.

But the national police force emphasized it had seen no evidence of "wrongdoing or illegal activity on the part of anyone associated with this investigation," including Goodale.

In the hours before Goodale removed the threat of a tax on the trusts, while deciding to enact a politically popular cut in corporate dividend taxes to reduce the advantage held by trusts in the market, the value of trusts and related stocks —especially those in the energy sector — rose sharply.

Although it is not clear whether the heavy trading was anything more than informed guesswork by investors, the Mounties said they intended to probe an allegation by the left-wing New Democratic Party "regarding a possible breach of security or illegal transfer of information."

The investigation will involve a special unit of Mounties and securities regulators which was created in 2003 to concentrate on capital market fraud.

But the national police force emphasized it had seen no evidence of "wrongdoing or illegal activity on the part of anyone associated with this investigation," including Goodale.

What is unusual is for such a high-profile, politically charged investigation to be started in the midst of a federal election campaign, leading to a vote on Jan. 23, while early polls showed the Liberals and Conservatives in a virtual tie for the first time in the campaign.

Political clamor follows

It set off an immediate clamor by the New Democratic, Conservative and Bloc Quebecois parties for Goodale's resignation.

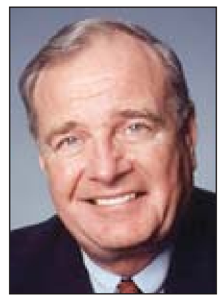
New Democratic finance spokesman Judy Wasylycia-Leis said that even though there was no indication Goodale was personally involved in the alleged leak as minister he was responsible for the actions of his staff and the civil servants in his department and should resign until the matter was resolved.

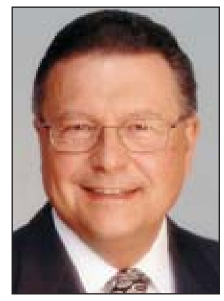
Conservative finance spokesman Monte Solberg said the confirmation of a policy investigation "highlights that the Martin government continues to operate under an ethical cloud."

Goodale said he was "absolutely confident about my conduct in this matter and I do not see any basis on which to resign."

He got the unreserved backing of Martin, who said Goodale is a "person of the highest integrity and he will not be stepping down."

Editorial opinions on most of Canada's largest newspapers agreed there was no reason for Goodale to quit his cabinet post.


Prime Minister Paul Martin


Finance Minister Ralph Goodale

However, Martin confirmed that he and some members of his staff were aware of Goodale's income trust decision in advance.

"I knew and I'm one of them," Martin said. "The fact is the people who would be on a need-to-know basis would have that kind of information."

Columnist: investigation unprecedented

Although the trust probe could last well beyond the election date, it provides further ammunition for the opposition parties in their attack on scandals and corruption that have undermined the Liberals.

John Ibbitson, a columnist in the Globe and Mail, suggested the criminal investigation "may have cost the Liberals this election."

He said the investigation is stunning and unprecedented.

"In the past police forces have deliberately delayed announcing criminal investigations or the laying of charges during election campaigns, for fear of influencing the outcome of those campaigns," Ibbitson wrote.

Tom Caldwell, chairman of Caldwell Securities, was among those who doubted any criminal impropriety will be uncovered.

"My gut feeling is that by the time the smoke clears and a lot of money is wasted, I don't think you're going to find any clear villains."

Trust under further scrutiny

Aside from the political fallout, the trusts — which carry a combined market value of C$170 billion — have come under further scrutiny by the C.D. Howe Institute, a national, independent research organization.

Jack Mintz, president of the think-tank, said more reforms are needed over and above those announced by Goodale to reduce the market distortions created by the investment vehicles.

He said the tax regime still encourages trusts to pay excessive cash distributions to investors because trusts that retain taxable profits are subject to heavy taxation.

An institute brief also cautioned that the dividend tax decrease does not affect foreign shareholders, who pay little or no tax on investment income earned in Canada.

Non-resident investors, as well as pension funds and retirement savings plans "prefer companies to convert business assets into income trusts since they can avoid paying corporate taxes at a 35 percent rate," Mintz said.

To help remove the tax discrepancies between trusts and corporations, Mintz suggested:

- Making the dividend tax credit refundable to owners of pension and retirement savings plans so they would be indifferent between corporation and trust assets.
- Levying a corporate distribution tax to ensure that the refundable dividend tax is covered by corporate tax payments.
- Increasing the level of tax on non-residents receiving income trust distributions so that they pay a similar tax on corporate dividends and income trust distributions. ●

● ANCHORAGE

Ethics complaint dismissed against Alaska AG Marquez

Independent counsel said Alaska attorney general does not own shares in BP or ConocoPhillips, not a lead player in negotiations

By MARK THIESSEN

Associated Press Writer

The state Personnel Board on Dec. 30 dismissed an ethics complaint which requested Alaska Attorney General David Marquez, a former oil industry lawyer and executive, recuse himself from Alaska natural gas pipeline negotiations.

"I accepted this appointment as attorney general with my pledge to serve to the utmost limits of my abilities the best interests of this state," Marquez said Dec. 30 in a prepared statement. "I will continue to honor this commitment as long as I serve in this capacity."

JUDY PATRICK

DAVID MARQUEZ

The complaint filed Aug. 4 by former U.S. Attorney Wev Shea alleged Marquez was in violation of the Alaska Executive Branch Ethics Act because his role in the pipeline negotiations could alter the value of his deferred compensation plan from two oils companies, which Shea said was valued at more than $1 million.

In dismissing the complaint, the Personnel Board's independent counsel found Marquez does not own shares in either BP or ConocoPhillips, and he does not control the rate of return on either compensation plan. In fact, the ConocoPhillips package is held in mutual funds.

It also noted he worked for neither company involved in the negotiations but for their predecessors, ARCO and Phillips Petroleum Co.

Decision: Marquez not a lead player

The decision also discounted the allegation that Marquez is a lead player in the state's negotiations with BP, ConocoPhillips and ExxonMobil to build a $20 billion pipeline to take natural gas from the North Slope, through Canada to markets in the Midwest.

Instead, the decision says Marquez only serves in an advisory role to the state negotiating team. It found he would have little influence on any deal, whose final terms must be approved by Gov. Frank Murkowski, the Commissioner of Revenue and the Alaska State Legislature.

"I respect the initial decision, and I have 15 days to file a response, and I'll file a response," Shea said Dec. 30.

Shea has another complaint pending against Marquez with the Personnel Board. In it, he claims Marquez broke attorney-client privileges by publicly commenting on a memo written to him by former Natural Resources Commissioner Tom Irwin.

Irwin was dismissed last fall after criticizing the state's negotiations with oil producers on the natural gas pipeline in the memo, which Murkowski publicly released.

Marquez with ARCO for 21 years

Marquez worked for ARCO Alaska Inc. for about 21 years, first as an attorney and later as a vice president and chief counsel. He also was Alyeska Pipeline Service Co.'s general counsel from 1991-1993. He retired from the industry in 2001 after a brief stint as vice president and chief counsel for Phillips Alaska Inc. He practiced law part time until being hired by the Department of Law in 2003.

Marquez became the state's attorney general on March 31. He replaced Gregg Renkes, who resigned in February amid conflict of interest allegations for his role in a trade agreement between Alaska and Taiwan.

Renkes helped shape the agreement to export Beluga coal to Taiwan. The deal mentioned the use of coal-drying technology patented by Denver-based KFx Inc., a company in which Renkes owned stock valued at more than $126,000 at its peak.

An outside investigator concluded the amount of stock Renkes owned was not enough to be considered legally significant. Renkes said he resigned to distance his family from continued personal attacks over the deal. ●

LONDON

Gas price drops amid Russia-Ukraine tift

Natural-gas prices fell Jan. 3 in electronic European trading as traders seemingly brushed off a pricing dispute between Russia and Ukraine that had threatened European gas supplies.

Natural gas prices fell 42.5 cents to $10.80 per 1,000 cubic feet in electronic trading on the New York Mercantile Exchange by morning in Europe.

One analyst said Russian state-controlled OAO Gazprom's efforts to restore gas flow had helped ease upward pressure on prices.

"The price that Gazprom wants is more or less the price today, it's just that all the former Soviet surrogate states have been receiving reduced prices over the years," said Victor Shum, a Singapore-based analyst at energy consultants Purvin & Gertz. "So that's why in the interim, you don't see too much price movement."

Light, sweet crude oil for February delivery was up 10 cents to $61.14 a barrel.

The price of Nymex crude is about 15 percent below its Aug. 30 high of $70.85. Oil prices remained above $60 a barrel for months after Hurricane Katrina disrupted Gulf of Mexico oil and gas output and dipped below $60 recently amid mild winter weather in the United States.

Heating oil gained slightly to $1.7634 a gallon, while gasoline was at $1.7230 a gallon.

Supplies back to Europe

European buyers of Gazprom's natural gas said Jan. 3 they had started receiving full supplies after the Russian monopoly increased shipments through Ukraine following a chorus of protest over its decision to cut off supplies to its neighbor.

The resumption of normal flows was reported by Hungary, Austria and Slovakia, among others, and came as officials with Gazprom and its Ukrainian counterpart, Naftogaz, were scheduled to resume talks over the pricing dispute later Jan. 3.

Gazprom halted deliveries to Ukraine Jan. 1 because Kiev had refused to meet its demands for a fourfold price increase. The state-controlled company said then that it would continue shipping full supplies to its European customers, about 80 percent of which goes through pipelines crossing Ukraine.

About one-quarter of Europe's gas comes from Russia, and the standoff raised fears of serious gas shortages as Europe suffers through a particularly cold winter.

—THE ASSOCIATED PRESS

● NOVA SCOTIA

Nova Scotia woes keep piling up

EnCana-Marauder wildcat unsuccessful, sidetrack well under way at Deep Panuke; more exploration licenses abandoned; no wells scheduled for 2006; Marauder shares drop by 50%

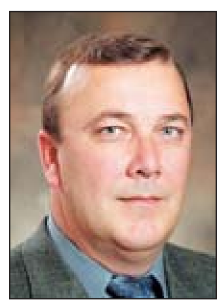
By GARY PARK

For Petroleum News

Any northeastern United States markets counting on Nova Scotia natural gas as a vital source of support would be well advised to check out other prospects.

A year marked by inactivity ended with the only exploration well turning into a flop and another bunch of exploration permits being abandoned.

What that amounts to over the near term is a brief turnaround in production from the Sable field, with output rising close to capacity of 530 million cubic feet per day, then receding back to current volumes of 400 million cubic feet per day and less.



EnCana's new CEO Randy Eresman

Those counting heavily on EnCana's Deep Panuke discovery becoming the basin's second commercial development were dealt a setback Dec. 28 when the big independent and its partner, Marauder Resources East Coast, reported that Dominion J-14 failed to encounter a gas-bearing reservoir.

Those counting heavily on EnCana's Deep Panuke discovery becoming the basin's second commercial development were dealt a setback Dec. 28 when the big independent and its partner, Marauder Resources East Coast, reported that Dominion J-14 failed to encounter a gas-bearing reservoir.

It was drilled to 12,100 feet at a cost of C$30 million by the Rowan Gorilla VI rig.

Shares of Marauder, which has no other assets, were immediately slashed by 50 percent. The junior paid 40 percent of the cost to earn a 20 percent stake in the Grand Pre block.

But Marauder Chief Executive Officer Robert Shields did not concede final defeat.

"I am disappointed that the original target didn't show up, but this isn't dead yet," he said, referring to the sidetrack EnCana and Marauder expect to complete by mid-January.

The sidetrack will follow the same vertical hole into the Abenaki reef formation to determine whether gas is located near the Dominion J-14 target.

"It's a big reservoir (and) it's very complex," Shields said, noting that two of the original four wells at Deep Panuke had to be sidetracked and both were successful.

EnCana: 'more work to do'

A spokesman for EnCana said there is "more work to do" before decisions can be made on how the J-14 well will affect the future of Deep Panuke.

When EnCana stalled the regulatory process on Deep Panuke three years ago it estimated reserves at 930 billion cubic feet — not enough in its view to make a C$1.3 billion project economically viable.

It opted to continue exploring for additional reserves, while negotiating more favorable fiscal terms with the Nova Scotia government and determining whether there might be a way to share infrastructure with the Sable field, which had watched its reserve estimates tumble from 3.6 trillion cubic feet to 1.4 tcf.

The last two months have produced a couple of glimmers of good news for Deep Panuke, with Nova Scotia Premier John Hamm reporting progress in the fiscal negotiations and EnCana's new Chief Executive Officer Randy Eresman telling reporters before the J-14 results that he was "reasonably certain" the field would be developed in the "reasonable future," without tying that forecast to J-14.

Some analysts, who rate Deep Panuke's prospects close to 1.5 tcf, suggested J-14 could double those reserves, opening the door to a new producing basin.

"We have been continuously working to try to find a way to make (Deep Panuke) economically viable," Eresman told the Calgary Herald. "Our chief concern is the downside risk.

"On a high-side case, this is a tremendous asset, but on the downside, it wouldn't compete for capital. So we are very sensitive about making sure we do the right kind of deal here."

Eresman reiterated the thoughts of his predecessor Gwyn Morgan who had indicated EnCana might bring Deep Panuke to a certain point, then dilute its role.

"Certainly, we don't want to be the operator," because EnCana does not have the internal expertise to take on such a project, Eresman said.

Some assume the obvious buyer would be ExxonMobil, which is operator of the nearby Sable field.

Exploration licenses lapse

While Deep Panuke remains in doubt, further clouds spread over Nova Scotia when holders of six exploration permits allowed the licenses to lapse Dec. 31, wiping another C$156 million in work commitments off the books.

Since mid-2004 more than 30 permits carrying more than C$500 million in work pledges have been abandoned, taking such key operators as ExxonMobil, Imperial Oil, Shell Canada and Kerr-McGee with them.

In addition, companies have invested in the region of C$1 billion drilling a string of dry holes over the past seven years.

That history is making it difficult for Nova Scotia boosters to make their case that the region is still an immature play and has logged only a fraction of the wells completed in the Gulf of Mexico and other major offshore basins.

But a spokesman for the Canada-Nova Scotia Offshore Petroleum Board told the Financial Post that, although no wells are planned for 2006, Nova Scotia remains a "very frontier area."

He said the regulator understands there is the potential for 40 tcf, but hitting "the right spot" through exploratory drilling is a complex process. ●

VENEZUELA

Venezuela: Three firms owe $224M

Venezuelan tax authorities have told three foreign oil firms they owe a total of $223.7 million in back taxes.

Spain's Repsol YPF SA was billed $113 million, while France's Total SA was charged $107.4 million, said tax agency official Diana Vargas. Japan's Teikoku Oil owes $3.3 million.

The Venezuelan government has sought to claim a greater share of revenues from private oil companies amid high oil prices, including increasing tax collection. As part of an industry-wide review, Venezuela has claimed it is owed much as $3 billion in unpaid taxes from private oil firms, which it plans to collect by March 2006 at the latest.

Vargas said four more companies will receive tax bills in late January, including Chevron and BP.

—THE ASSOCIATED PRESS

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Petroleum news

Business Spotlight

By PAULA EASLEY

FORREST CRANE

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Lifelong Alaskan Robert Fairbanks has been in the heavy equipment field 21 years, six with CMI. He is active in Associated General Contractors, the Anchorage Petroleum Club and the Alaska Miners Association. Working on his hotrod, attending hockey games and spending time with the family at Big Lake are his favorite activities. He and Mary, his wife of 29 years, have two children, Chris and Emily, and a grandson.

continued from page 1

CONTRACT

Enstar told an Anchorage Chamber of Commerce audience on Nov. 14.

But in focusing on continuity of supplies has Enstar conceded future price levels that are too high? And will the new contract stifle future gas exploration in the Cook Inlet basin? These are a couple of the questions that the State of Alaska, companies linked to the Cook Inlet gas industry and private individuals have raised with the Regulatory Commission of Alaska prior to an RCA decision on whether to investigate the contract.

Guaranteed delivery

At the core of the new contract are guaranteed volumes of natural gas that Marathon will supply to Enstar from 2009 onwards from known Cook Inlet gas reserves that Marathon owns. The guaranteed volumes increase until 2016 and decline thereafter. Without additional gas sources, volumes would decline to zero at some time after 2018.

When added to Enstar's other contracted supplies (primarily from Chevron and another Marathon contract) Enstar should obtain sufficient gas to meet projected demand through 2016. Without the contract, Enstar could start to run short of gas as soon as 2009, Enstar has said.

And, according to Enstar's contract approval request to RCA, "Marathon was the only gas producer that offered to meet Enstar's unmet requirements beginning in 2009 and continuing for a reasonable period."

Under the contract, the price that Enstar will pay for the gas will be based on a 12-month trailing average of gas prices at the Henry Hub gas market in the Lower 48, with discounts if that index price climbs above $6 per thousand cubic feet. The price will have a floor of $4.25 per mcf and a cap of $15 per mcf (the Henry Hub price was about $13.5 at the end of December). There is an additional charge for peak gas volumes supplied at volume rates in excess of contracted peak volumes.

Also under the terms of the contract Marathon will have an unlimited ability to meet its supply commitments by buying and reselling gas from third party producers.

Rather than adding variable gas pipeline tariff rates to Enstar's cost for the gas, the contract specifies a fixed transportation rate of 25 cents per mcf for all gas supplied.

Questions of price

Much of the criticism of the contract revolves around the price levels on which Marathon and Enstar have agreed. And the state attorney general has said that because Enstar passes the gas prices that it pays directly through to its customers, the utility has little incentive to ensure low prices in its gas supply contracts.

Questions by the attorney general have particularly focused on price indexing to Henry Hub price levels. Earlier Enstar contracts with Unocal (now Chevron), in 2001, and NorthStar, in 2004, already use the Henry Hub price as an index, although both of those contracts used a 36-month trailing average price rather than the 12-month trailing average of the new contract.

The linkage to Lower 48 prices results from a need to attract new investment into Cook Inlet gas exploration — there's little or no incentive for companies to explore for gas in the Cook Inlet basin if those same companies can explore for gas at higher prices elsewhere in the United States (or overseas). And without new Cook Inlet gas exploration, gas supplies in the Anchorage area will surely run dry before too long.

Earlier contracts specified exploration

But the earlier contracts with Enstar were exploration contracts that incorporated a need to find new gas reserves to satisfy the supply agreements. The new contract only depends on known Marathon gas reserves; commitments in the contract do not depend on exploring for further gas.

"Most notable for the purposes of the Commission's review of this Marathon GSA (gas supply agreement) is that both the Unocal and NorthStar GSAs purported to be 'exploration' contracts and each company relied on this characterization as a justification to use HHI (Henry Hub) as a pricing index," the attorney general said in his comments to RCA on the new contract.

Marathon has, however, commented that it has already "invested significant amounts of capital to prove up and develop gas reserves that can serve Enstar and other Cook Inlet markets" and "as a result, Marathon can now offer proven reserves to Enstar that will provide strong security of supply to Enstar and its customers."

The attorney general and others have also pointed out that Henry Hub prices have been subject to recent spikes as a result of events such as hurricane Katrina. Why should Alaska residents have to suffer from price shocks that result from events that don't impact Alaska gas supplies, these people ask.

Giard dissented to 2004 order

And in a dissenting statement to the 2004 RCA order approving the NorthStar/Enstar contract RCA Commissioner Kate Giard expressed a concern that by linking Cook Inlet gas prices to Henry Hub "captive (gas) ratepayers are at the mercy of a spot market in the Lower 48 that bears no relation to gas market conditions in Alaska."

The attorney general also criticized the use of a 12-month trailing average price, rather than a 36-month trailing average: the 12-month average will increase price volatility and the possibility of rate shocks, the attorney general said. Marathon and Enstar have justified the use of a 12-month moving average on the grounds that it will provide diversification from the price formula in the 2001 Unocal contract and that it will buffer the Unocal price by "more quickly reflecting falling prices."

And the attorney general has questioned the use of a fixed transportation fee, saying that this fee is "arbitrary, potentially discriminatory and unsupported."

Aurora Gas LLC, an active explorer in the Cook Inlet basin and operator of five gas fields on the west side of the Inlet, supports gas price increases as necessary incentives for new Cook Inlet basin exploration but has expressed concern about the impact of the new contract on the taxes and royalties on production from its Moquawkie field. Aurora sells gas from Moquawkie at a lower price than that in the Marathon-Enstar contract, while production taxes and royalties are calculated from "prevailing value," a weighted average of prices paid by utilities in the region.

"The scenario creates a situation whereby the smallest company, with the highest development costs per unit, is receiving the lowest net price for its gas," Scott Pfoff, president of Aurora Power said in a letter to RCA about the new contract.

Market access

And companies such as Aurora feel particularly concerned about the way in which gas supply agreements such as the new Marathon-Enstar contract can close the gas market to new companies that want to explore the Cook Inlet basin.

"Having pounded the pavements in downtown Houston, downtown New York and in Calgary in search of private equity capital … we never had any problem selling anybody on the technical merits of looking for oil and gas in the Cook Inlet basin," Pfoff said at the Resource Development Council annual conference in mid-November. "… The problem came when I got up and tried to talk about the market. There is no spot market up here — you don't just find gas, hook it up to the nearest pipeline and start selling it. You've got to have contracts; you've got to have a way to sell your gas."

Enstar and Marathon have pointed out that the new contract runs for a relatively short term compared with other Cook Inlet contracts. However, the new contract would, together with existing contracts, account for gas sales to Enstar until at least 2016.

So, Aurora and Trading Bay Oil and Gas LLC, another Cook Inlet lease owner, have requested that RCA requires a set-aside of about 10 percent of purchased gas for producers other than Marathon.

"If new companies fail to show up with new supply, then the existing producer community can compete for the set aside portion of the utility's requirements," Pfoff said.

Marathon can purchase from others

The attorney general and others have also criticized another aspect of the contract that they think limits competition in the Cook Inlet gas market: the contract allows Marathon an unlimited ability to meet its supply commitments by purchasing gas from third party producers. That would enable Marathon to resell the gas to Enstar at a profit, using the contract price.

"Under this GSA Marathon … could, if approved, enhance its windfall opportuni-

see **CONTRACT** *page 16*

continued from page 1

INSIDER

But it is also expected to take several months of legal work before the parent company makes a decision to avoid the financial, legal and regulatory pitfalls that have plagued previous Shell buyouts.

Bringing the two units together would reduce the complexities of decision-making, which were reportedly outlined to senior managers by Linda Cook, chief executive officer of Shell Canada for 12 months in 2003-2004 and now Shell's global executive director for gas and power.

She apparently talked about the difficulties of dealing with minority shareholders and the seven independent directors on Shell Canada's 10-person board.

Giving the parent company 100 percent control could give a lift to future profits and a boost to the company's reserves.

Shell Canada is in the front lines of most of Canada's oil and gas frontier projects.

It is 60 percent operator of the 155,000 barrel per day Athabasca oil sands project which is chasing a goal of 500,000 bpd; becoming a major player in the deep gas plays of Western Canada; one of four anchor gas owners in the Mackenzie Gas Project; and a partner in Nova Scotia's Sable gas field.

—GARY PARK

Loeffler joins Jade North

BOB LOEFFLER, formerly director of the Division of Mining, Land and Water in the Alaska Department of Natural Resources, has joined Jade North LLC, the firm said Jan. 3.

Jade North said Loeffler will represent clients with natural resource extraction and transport issues and assist clients with land management projects and issues with government, Native and other private land owners.

COURTESY JADE NORTH

BOB LOEFFLER

Loeffler, who has spent some 25 years working for the State of Alaska, was one of six Department of Natural Resources officials who resigned Oct. 27 following the dismissal of Commissioner Tom Irwin in a dispute within the administration over how the gas pipeline fiscal contract negotiations with the North Slope producers were proceeding.

Jade North, an Anchorage-based firm founded in 2000, provides consulting services in the natural resource, Alaska Native and government sectors.

—KRISTEN NELSON

AAEP to hear talk on FERC gas line review

AT THE NEXT Alaska Association of Environmental Professionals' brown bag lunch meeting Joe Reinermann of Natural Resource Group Inc. will talk about the Federal Energy Regulatory Commission review process for natural gas pipelines.

The meeting will take place at 11:45 a.m. on Wednesday Jan. 18 in the BP Energy Center in Anchorage. Contact Denise Saigh at (907) 562-8738 for more information.

—PETROLEUM NEWS

continued from page 1

STORM CAT

from the well in late February or early March, following drilling, testing and evaluation.

"Northern Dancer No. 1 is the well name," Zimmerman said. "… It's close to the Big Lake No. 1 well."

Pan American Petroleum Corp. drilled the (USA) Big Lake No. 1 well in 1968 to a depth of 6,026 feet at section 1, township 15 north, range 4 west of the Seward meridian. The Alaska Oil and Gas Commission records for that well do not appear to indicate any oil or gas shows, although at that time Pan American would have been exploring for oil.

Zimmerman said that Storm Cat's well will be located about 6 miles from the Enstar gas pipeline that transports gas into the Mat-Su Borough and Anchorage.

Alaska-based consultants Arlen Ehm, Corri Feigi and Mike Belowich helped Storm Cat identify the prospect using 2D seismic data, Zimmerman said.

Although the focus of the Northern Dancer No 1 well will be conventional natural gas, Storm Cat will evaluate any coalbed methane potential.

"We will be going through coal formations and, while we won't be testing them, we'll be able to evaluate them through log characteristics and gas shows," Zimmerman said.

Canadian company

Storm Cat is registered in British Columbia and has offices in Denver, Calgary and Ulaanbaatar, Mongolia. According to the company's web site "Storm Cat Energy is a rapidly growing exploration company focusing on developing unconventional natural gas reserves globally."

The company first entered the Alaska oil and gas scene when it purchased two leases near Big Lake in the Alaska Mental Health Trust Land Office November 2004 lease sale. The company went on to purchase eight nearby leases in the State of Alaska's May 2005 Cook Inlet areawide lease sale.

"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," Zimmerman said after the state lease sale. "… 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."

Although Storm Cat has been using a team of Alaska consultants, the establishment of a company office in Alaska will depend on drilling success at this "or the next couple of wells," Zimmerman said. Meanwhile the company is making use of Alaska services and personnel.

"We are using local Big Lake area contractors and services from Alaska," Zimmerman said.

—ALAN BAILEY

continued from page 1

AGENDA

mit applications."

HB 336 and Senate Bill 203 give the state's resource agencies — the departments of Environmental Conservation, Fish and Game and Natural Resources — until July 1, 2007, to adopt a unified permit application form. Following the adoption of the form, "the unified permit application shall be the only application required for any permitting action by the resource agencies when a project requires permits from two or more resource agencies." The bills also provide that the resource agencies will make the uniform forms available in both electronic and printed formats.

Natural resource agencies would be required to provide permit application information on the Internet by July 1, 2007, and by July 1, 2008, to have an interactive application on the Internet, "or other means for an applicant to determine what permit or permits" the applicant must obtain from each resource agency, along with "information concerning the procedure for each agency's review of a unified permit application."

By July 1, 2008, each agency must also have in place the process for submitting the unified permit application on the Internet.

Permitting an issue

Industry has complained about the number of different permit applications required by different departments.

John Barnes, Marathon Oil's Alaska manager, has tabulated and talked about the number of permits required for work on the Kenai Peninsula, where Marathon is a major natural gas producer and explorer.

Geological consultant Arlen Ehm raised the issue of multiple, and different, forms at a House Special Committee on Oil and Gas hearing in November. The committee had asked what the Legislature could do to encourage independent activity in the state. Gardner is a member of the committee.

Ehm told the committee that Lower 48 independents aren't interested in coming to Alaska because of high entry costs, high operating costs, high risk, permitting problems, excessive bureaucracy, excessive environmental constraints, long lead time, remote exploration targets, seasonal operational restrictions, lack of infrastructure and seasonal access.

Ehm said the state can't do anything about most of those problems, but it can address permitting problems. He said companies looking at Alaska have all heard "horror stories about the permitting process."

He recommended cataloguing existing regulations for permitting, developing "a unified integrated information gathering system covering all agencies thereby avoiding duplication," putting this online where applicants can access it and where all the agencies can retrieve applications filed online.

Ways & Means hearings

The House Special Committee on Ways and Means has scheduled a hearing on HB 223 for Jan. 11 and on HB 63 for Jan. 13.

This will be the first hearing for the bills. HB 63 was introduced in January 2005; HB 223 was introduced in March 2005.

In his sponsor's statement Gara said HB 63 recognizes that smaller and older fields need some severance tax relief, but provides for a minimum production tax of 5 percent, a "modestly" higher tax at higher oil prices and a lower tax at lower oil prices.

Gara characterized HB 63 as the "Alaska fair share bill."

While the state is still negotiating with the North Slope producers for gas pipeline fiscal terms, those negotiations have been expanded to include oil taxes. Changes in the state's oil taxation would require legislation.

Gara has also pre-filed HB 332 and HB 333, which would provide what he describes as a "modest increase in oil taxes" to fund education enhancements. HB 332 would provide schools with funds to hire parental involvement coordinators as well as funding financial incentives for teachers to obtain masters degrees, Gara said in a Jan. 4 statement. HB 333 would create a

see AGENDA page 16

continued from page 15

AGENDA

fund to reinstitute public pre-school for parents who want their children to attend school before Kindergarten. Gara and Rep. David Guttenberg, D-Fairbanks, are the sponsors of HB 340, which would levy a supplemental income tax on oil revenue for postsecondary and vocational education and create grant programs for postsecondary and vocational education students.

Croft's gasline now act

Croft said in his sponsor statement that HB 233 "is a useful tool for guaranteeing construction of a gas pipeline from the North Slope, encouraging exploration for natural gas, and for filling the state's structural budget deficit until that pipeline gets built." Croft's proposal is to charge "a fee for storing Alaska's gas in the largest gas fields," a fee which would go away once a gas pipeline is completed.

Croft is also gathering signatures to put this proposal on the ballot as an initiative.

The annual tax would be 3 cents per thousand cubic feet of gas at Prudhoe Bay and Point Thomson; once a pipeline is built and gas is flowing, Croft said, a company could get the amount of the tax back as a credit against severance tax on natural gas shipped in the line.

Energy studies, energy reimbursements

Rep. Ethan Berkowitz, D-Anchorage, has introduced a bill to create the Alaska energy research and development program in the Alaska Energy Authority, with a Committee on Alaska Energy Research and Development to assist in program development.

The goal of the program would be to "improve the development and application of reliable and cost-efficient alternative energy sources in the state to reduce the cost of energy paid by Alaska communities and make them less dependent on nonrenewable fuels and costly energy supplies."

Senators Gene Therriault, D-North Pole, and Al Kookesh, D-Angoon, co-sponsored two bills, SB 214 and SB 215, proposing to use some of the state's oil tax revenues for energy assistance and weatherization and as an energy dividend for 2005.

Therriault said in mid-December that the proposals would give back a portion of the state's current budget surplus to Alaska by a $250 energy rebate, additional funds for Power Cost Equalization and $10 million for the Low Income Weatherization Program (see story in Dec. 18, 2005, issue of Petroleum News). ●

continued from page 1

HEARINGS

two days after Canada's federal election campaign — to start its proceeding in Inuvik on the Mackenzie Delta.

A Joint Review Panel has also set Inuvik to begin probing environmental and socio-economic issues on Feb. 14.

It is expected the process will involve stops at 20 Northwest Territories locations, plus Whitehorse, Edmonton and Calgary and will wrap up in December.

But the schedule could be thrown off track by any one of several unresolved aboriginal issues.

A case has been filed before the Federal Court of Canada by the Dene Tha' First Nation, which has land claims pending in northern Alberta and the southern Northwest Territories, and argues that Joint Review Panel hearings should be delayed until their concerns are resolved.

Talks are also continuing with the Deh Cho First Nations, whose land covers about 40 percent of the pipeline route, and who have been a persistent wild card by refusing to join northern native regions in settling benefits and access agreements.

Complicating matters, the K'asho, Gotine and Tulita/Deline communities have requested additional time to conclude their agreements.

Key players in the Mac regulatory process

• National Energy Board: Canada's federal energy regulator has assigned a three-member panel consisting of chairman Ken Vollman and members Gaetan Caron and David Hamilton to conduct the main review and decide whether to approve or reject the project. That finding will also draw on the Joint Review Panel report. That review has 120 registered interveners.

• Joint Review Panel: A seven-person panel, including four aboriginal and Northwest Territories residents, will examine the potential social, environmental and economic impacts of the project and decide what, if any, conditions should be imposed on the licenses and permits. It has 99 individuals and organizations registered as interveners.

• Mackenzie Valley Land and Water Board: It has a mandate to regulate the use of land, water and waste deposits in the Mackenzie Valley. It is drawn from the Gwich'in Land and Water Board and the Sahtu Land and Water Board, with other board members nominated by First Nations, the Northwest Territories government and a chair appointed by the federal Indian and Northern Affairs Minister Andy Scott.

• Northwest Territories Water Board: Its function is to monitor the conservation, development and utilization of the water resources in the Inuvialuit region of the Northwest Territories.

Apart from the main applications, more than 4,000 licenses, permits and agreements are needed during the planning, construction and start-up phases of the project, covering benefits and access, wildlife compensation, land use, surface tenure, water use, quarry, bird sanctuary access and fisheries approvals.

Among the logistical challenges, apart from coordinating the two hearing streams, the Northwest Territories uses English and French — Canada's two official languages — and nine aboriginal tongues, all of which the National Energy Board and Joint Review Panel said it welcomes in statements, evidence and verbal presentations.

Concern that Alaska could go first

On the larger front, John Duncan, a Canadian Member of Parliament and a natural resources spokesman for the Conservative Party, says the Mackenzie supplies are needed and the economics are right.

But he shares the concerns of many others in government and the industry that if the Mackenzie plan stumbles, the Alaska project will surge ahead.

Alaska has support from an unlikely source that is expected to figure large in the Mackenzie hearings.

Sierra Club directors Elizabeth May and Carl Pope have made a case to ExxonMobil (parent of Imperial Oil, the Mackenzie's lead partner) to abandon their Canadian plans "in favor of advancing" Alaska.

They say an Alaska pipeline would cause less ecological damage than a Mackenzie route through boreal forest and taiga and the associated spin-off resource development along the right of way.

May and Pope also argue the Mackenzie gas would be exclusively used as an energy source to increase oil sands production in Alberta, adding to Canada's greenhouse gas. Also under way are critical negotiations between the Mackenzie proponents and the Canadian government on the federal offer to assume a "greater share of the project downside risks provided it is able to increase its share of the potential rewards" — the breakthrough that made it possible for the project consortium to notify the National Energy Board it was ready to proceed to public hearings.●

continued from page 14

CONTRACT

ties by simply acting as a middle-man to provide all or some of its commitments," the attorney general said.

"It is highly improbable that the party selling gas to Marathon would be able to negotiate a gas sales price and related terms sufficient to encourage the level of exploration and production activity needed on a sustained basis between now and 2018," said Paul Craig, manager of Trading Bay Oil and Gas.

Enstar, in its submission to RCA, justified the unrestricted ability of Marathon to purchase gas on the grounds that "when gas is scarce it is not desirable to make it more difficult to discover, produce or deliver or to otherwise limit the sellers alternatives to procure gas to meet Enstar's requirements." Enstar also pointed out that Marathon may want to develop gas storage facilities and then purchase gas, typically in the summer, to store to meet peak winter demand.

So, what will be the upshot of the debate regarding the new Marathon-Enstar contract? The RCA will at some stage rule on whether to investigate the contract. And Giard has said in the past that "the test for approving gas supply contracts is whether the contract provides a reliable source of gas at a reasonable price."

But maintaining a Cook Inlet gas market that assures future supplies at reasonable prices clearly presents something of a challenge.●