Petroleum news

page 4 Fairclough on all three Senate committees that worked tax bill

Vol. 18, No. 11 • www.PetroleumNews.com | *A weekly oil & gas newspaper based in Anchorage, Alaska* | Week of March 17, 2013 • $2

Latest Petroleum News Bakken

Petroleum News Bakken

page 5 ND House energy, resources committee chair on O&G politics

Vol. 1, No. 24 • www.PetroleumNewsBakken.com | *A weekly newspaper for industry and government* | March 17, 2013

Continental shooting for zero

PETROLEUM NEWS FILE

The largest oil producer in North Dakota's Bakken play, Continental Resources, says it is aiming to bring its gas flaring down to as close as possible to zero. Currently it's under 10 percent, as compared to the rest of the oil and gas producers in the Williston Basin, where the average is 29 percent. See story on page 3 of this issue. (This photo is not of a Continental operation. Can you guess where it was taken? Email publisher@petroleumnewsbakken.com with your answer.)

Slawson's upper shale project yields Northern Oil's highest IRR

JOHN MOWERS

MICHAEL REGER

In Northern Oil and Gas's fourth quarter earnings call on March 1, Chairman and Chief Executive Officer Michael Reger updated investors on the company's joint venture with Slawson Exploration in Upper Bakken shale development in Richland County, Mont. Thanks to innovations by Slawson, the NW Big Sky prospect, he said, is now Northern's area of highest internal rate of return.

"This is not a huge deal for us, but it will be among many of the drivers of production and value in 2013, similar to the

see UPPER SHALE page 11

Top three Bakken wells by IP rate

While ConocoPhillips brought in what appears to be the best initial production rate, or IP, for oil produced in a 24-hour period of any well in North Dakota to date with its McKenzie County Brazos 24-34H well in 2012, Whiting Oil and Gas appears to be running a close second — and third — based on limited research of the North Dakota Oil and Gas Division's data base by Petroleum News Bakken.

Whiting has three wells in the Twin Valley field in northern McKenzie County called the Tarpon wells. Two of those Tarpon wells rank second and third behind ConocoPhillips' Brazos 23-34H well in terms of oil IP rates.

In December 2012, Whiting's Tarpon Federal 21-4-3H

see IP RATE WELLS page 11

COMPANY UPDATE

Best Bakken well

A record well, highest liquids; COP earmarks $4B for Bakken through 2017

By MIKE ELLERD

For Petroleum News Bakken

RYAN LANCE

In a liquids-rich play, oil is paramount, and nowhere was that more evident than for ConocoPhillips in the Williston Basin in 2012. Not only did the company's 2012 Bakken production yield the highest liquids percentage in its product mix of all of its Lower 48 plays, but the company also came in with what is believed to be the highest initial oil producing well ever in the Bakken.

That well, the company's Brazos 24-34H well, is in the Charlson field in northeast McKenzie County and had a total depth 10,582 feet with a single lateral extending 4,256 feet into the Middle Bakken formation. It was completed with a 10-stage frack in May 2012, and during the initial 24-hour test in June, the well produced 5,130 barrels of oil, 9.75 million cubic feet of gas and only 206 barrels of water under a flowing pressure of 1,325 pounds per square inch.

According to Alison Ritter, public information officer for the North Dakota Industrial Commission's Department of Mineral Resources Oil and Gas Division, that 24-hour oil initial production or IP of 5,130 barrels of oil per

see RECORD WELL page 12

COMPANY UPDATE

New Bakken formation

Whiting to drill up to 15 wells to test Lower Bakken Silt oil zone at Hidden Bench

By RAY TYSON

Petroleum News Bakken

JAMES VOLKER

Williston Basin powerhouse Whiting Petroleum plans to test an untapped and highly prospective oil formation within the Bakken petroleum system known as the Lower Bakken Silt.

Sandwiched between the already producing Middle Bakken and Three Forks formations, Whiting says the "Silt" is situated in the central portion of the Williston Basin, and is "primarily present" at the company's Hidden Bench prospect in North Dakota's McKenzie County, James Volker, Whiting's chairman and chief executive officer, said in a recent presentation to analysts.

Whiting said it identified the zone through extensive core sampling, which "demonstrated high oil in place and may significantly increase reserves in this area."

The company is so confident about transforming the Silt into production that it plans to invest millions of dollars "bracketing" the formation with as many as eight wells above and seven wells below the Silt. The wells, to be drilled on 160-acre spacing, might even improve current production from the Middle Bakken zone, the company said.

see NEW FORMATION page 13

LAND & LEASING

MT flirts with records

Elm Coulee tracts top Montana auction, leading to 2nd highest ever average price

By MIKE ELLERD

For Petroleum News Bakken

While Montana oil and gas lease auction prices softened in 2012, the Minerals Management division of the Montana Department of Natural Resources and Conservation, or DNRC, saw an upswing in its March oil and gas lease auction. The agency sold 10-year leases this month on nearly twice as many acres as in its December auction for an average price per acre of more than three times that in December, nearly setting a new record.

In the March 5 auction, the division sold mineral leases on 12,596 acres in 25 separate tracts bringing in a total of $1,011,287 for an average price of $80.28 per acre, the second highest ever average price per acre received in a DNRC lease auction. In the

see MONTANA RECORDS page 15

Upcoming auctions

The next North Dakota Department of Trust Lands Minerals Management Division lease auction is scheduled for May 7. The location and time are yet to be announced. The nomination period for the North Dakota sale closes at 5:00 p.m. Central Daylight Time on March 22.

The Bureau of Land Management's Montana/Dakotas office will hold its next oil and gas lease auction on May 8 at the Montana BLM office in Billings, beginning at 9:00 a.m. Mountain Daylight Time. A total of 93,731 acres will be offered in 198

see UPCOMING AUCTIONS page 16

Petroleum News Bakken, a sister publication to Petroleum News, went to a weekly publishing schedule with its March 3 issue and, at the same time, became a standalone newspaper, which means it is no longer mailed with Petroleum News. But Petroleum News subscribers still receive the online version of the Bakken newspaper each week. Page 1 stories this week include news about ConocoPhillips' Bakken operations, including a 2012 ConocoPhillips well with an initial production (first 24 hours) of 5,130 barrels of oil, setting what appears to be a record IP rate for the petroleum system.

BP sees a drop sales and taxes; pair of odd items impacts profits

A pair of unique items on the BP plc balance sheet is making it difficult to tell exactly how well the company performed in Alaska in 2012, but the financial figures make one thing clear: continued production declines ate into revenues for the company last year.

BP Exploration (Alaska) Inc. earned more than $3.7 billion in 2012. The subsidiary of the London-based oil giant earned just $1.4 billion in 2011, but the huge jump from year-

see **BP REVENUES** *page 17*

Statoil Alaska strategy unchanged; Hess update; airship; big hearing?

A RECENT REPORT FROM A FINANCIAL news service indicated that Statoil has backed off its exploration program in the Alaska's Chukchi Sea as a consequence of Shell's February decision not to drill in the Chukchi in 2013. However, Statoil's Alaska strategy did not change following Shell's February decision, Jim Schwartz, Statoil's head of communications in Houston, told Petroleum News March 11.

"Our view is still the same. We take a very long-term

see **INSIDER** *page 17*

EXPLORATION & PRODUCTION

Planning ahead

ConocoPhillips' strategy for Chukchi Sea drilling in 2014 takes shape

By ALAN BAILEY

Petroleum News

ConocoPhillips is moving ahead with plans for exploration drilling in Alaska's Chukchi Sea in the summer of 2014, Mike Faust, the company's Chukchi Sea exploration project manager, told the National Marine Fisheries Service's annual Arctic Open Water Meeting on March 7.

"Our goal is to drill one well," Faust said, adding that, although it might be possible to drill two wells during the summer open water season, the drilling of one well would meet the company's expectations.

ConocoPhillips' drilling target is its Devil's Paw prospect, a 200,000-acre structure about 120 miles west of the coastal village of Wainwright. Devil's Paw was previously penetrated by the Klondike well, drilled by Shell in 1989. And although that well did not encounter commercial quantities of oil and gas, ConocoPhillips clearly views the prospect as holding promise for a major oil find — the

> *Faust said that ConocoPhillips is contracting a brand-new, state-of-the-art jack-up rig from Noble Corp. for the drilling.*

see **CHUKCHI PLANNING** *page 19*

EXPLORATION & PRODUCTION

Linc spuds, defers

Company starts first well at Umiat in 34 years, but delayed much of program

By ERIC LIDJI

For Petroleum News

Linc Energy Ltd. recently spud the first well at the Umiat prospect in 34 years, but weather delays have forced the company to cut back on its previous plans for this season.

The Australian independent spud the Umiat No. 18 well on a federal lease in the foothills of the Brooks Range some 100 miles west of Pump Station 2 using Kuukpik No. 5 rig.

Linc originally outlined a four-to-six well program at Umiat this winter, but following a period of light snowfall early in the season combined with extreme cold snaps, the company is now planning to drill just two wells this winter and cold-stack its rig on location to get a head start on mobilization for the 2013-14 winter exploration season.

Among the work being deferred is Umiat DSP No. 1, a Class II disposal well. Now, Linc plans to dispose of cuttings and drilling fluids using existing North Slope infrastructure.

Other previously mentioned well locations being deferred include the side-by-side Umiat No. 16 vertical and Umiat No. 16H horizontal wells, and the Umiat No. 19 vertical well.

Two wells this winter

The two wells now planned for this winter — Umiat No. 18 and Umiat No. 23H — would still

see **LINC UMIAT WELL** *page 18*

FINANCE & ECONOMY

Northstar's high stakes

Murphy case concerns production allocation in BP-operated Alaska field

By WESLEY LOY

For Petroleum News

The state and Murphy Oil Corp. are locking horns over the Northstar oil field along Alaska's North Slope.

The offshore field is on state and federal leases, producing from an artificial island located in the Beaufort Sea about six miles northwest of Prudhoe Bay. The field started production in 2001.

BP is the operator and major owner of the field, with Murphy, based in El Dorado, Ark., holding a small minority stake.

The dispute between the state and Murphy concerns how production from the Northstar "participating area" is allocated between the state and federal leases.

> *A weeklong evidentiary hearing was held before a DNR hearing officer in March 2012. The matter now sits before DNR Commissioner Dan Sullivan.*

The allocation makes a big difference to the state in terms of royalty and tax collections. Basically, state revenue is greater if more of Northstar's production comes from the state leases.

Confidential proceedings

During a Feb. 7 legislative hearing, attorneys with the Alaska Department of Law submitted a

see **NORTHSTAR FIELD** *page 17*

contents

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Alaska - Mackenzie Rig Report

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

Alaska Rig Status

North Slope - Onshore

Doyon Drilling			
Dreco 1000 UE	16 (SCR/TD)	Milne Point MPL-14, workover	BP
Dreco D2000 UEBD	19 (SCR/TD)	Alpine CD3-127	ConocoPhillips
AC Mobile	25	Prudhoe Bay Z-66	BP
OIME 2000	141 (SCR/TD)	Bear Tooth Unit Cassin 1	ConocoPhillips
Kuukpik	5	Umiat #18, drilling	Linc Energy Operations Inc.
Nabors Alaska Drilling			
Trans-ocean rig	CDR-1 (CT)	Prudhoe Bay	Stacked
AC Coil Hybrid	CDR-2	Kuparuk 1H-19	ConocoPhillips
Dreco 1000 UE	2-ES	Prudhoe Bay	Available
Mid-Continental U36A	3-S	Prudhoe Bay	Available
Oilwell 700 E	4-ES (SCR)	Prudhoe Bay	Available
Dreco 1000 UE	7-ES (SCR/TD)	Colville River Q3	Repsol
Dreco 1000 UE	9-ES (SCR/TD)	Prudhoe Bay	Available
Oilwell 2000 Hercules	14-E (SCR)	Prudhoe Bay	Available
Oilwell 2000 Hercules	16-E (SCR/TD)	Prudhoe Bay	Available
Oilwell 2000	17-E (SCR/TD)	Prudhoe Bay	Stacked
Emsco Electro-hoist -2	18-E (SCR)	Prudhoe Bay	Stacked
Emsco Electro-hoist Varco TDS3	22-E (SCR/TD)	Prudhoe Bay	Stacked
Emsco Electro-hoist	28-E (SCR)	Prudhoe Bay	Stacked
Emsco Electro-hoist Canrig 1050E	27-E (SCR-TD)	Kuparuk NDST-2	Pioneer Natural Resources
Oilwell 2000	33-E	Prudhoe Bay	Available
Academy AC Electric CANRIG	99AC	Colville River Q6	Repsol
Academy AC electric Canrig	105-E (SCR-TD)	Colville River Q1	Repsol
Nordic Calista Services			
Superior 700 UE	1 (SCR/CTD)	Prudhoe Bay Drill Site K-06B	BP
Superior 700 UE	2 (SCR/CTD)	Prudhoe Bay Well Drill Site 6-24B	BP
Ideco 900	3 (SCR/TD)	Kuparuk Well 2K-02	ConocoPhillips
Parker Drilling Arctic Operating Inc.			
NOV ADS-10SD	272	Prudhoe Bay F-13B	BP
NOV ADS-10SD	273	Prudhoe Bay 02-15B	BP

North Slope - Offshore

BP			
Top drive, supersized	Liberty rig	Inactive	BP
Nabors Alaska Drilling			
Dreco 1250 UE	14 (SCR/TD)	Endicott 3-19/OH, workover	BP
Commander 1500 HP	19-E (AC)	Oooguruk ODSN-24	Pioneer Natural Resources
OIME 2000	245-E	Oliktok Point	ENI
Doyon Drilling			
Dreco 1250 UE	14 (SCR/TD)	Prudhoe Bay DS-07-34	BP
Sky Top Brewster NE-12	15	Spy Island SP22-FN1	ENI

Cook Inlet Basin – Onshore

Kenai Land Ventures LLC (All American Consultants, labor Contract)			
Taylor	Glacier 1	Kenai Loop Drilling Pad #1	Buccaneer Energy Ltd
Aurora Well Service			
Franks 300 Srs. Explorer III	AWS 1	In winter maintenance mode, Do not expect to be done until April 1	Hilcorp Alaska
Doyon Drilling			
TSM 7000	Arctic Fox #1	Swanson River SRU 13-27	Hilcorp Alaska LLC
Nabors Alaska Drilling			
Continental Emsco E3000	273E	Kenai	Available
Franks	26	Kenai	Stacked
IDECO 2100 E	429E (SCR)	Stacked in Kenai	Available
Rigmaster 850	129	Kenai	Available
Academy AC electric Heli-Rig	106-E (SCR/TD)	Kenai	Available

Cook Inlet Basin – Offshore

XTO Energy			
National 110	C (TD)	Idle	XTO
Spartan Drilling			
Baker Marine ILC-Skidoff, jack-up		Spartan 151 Upper Cook Inlet KLU#1	Furie
Cook Inlet Energy			
National 1320	35	Osprey Platform RU-1, workover	Cook Inlet Energy
Hilcorp Alaska LLC (Kuukpik, labor contract)			
		Steelhead Platform M-25 Workover KD Management contract	Hilcorp Alaska LLC
		Monopod Platform, Preparing for workovers, KD Management Contract	Hilcorp Alaska LLC

Mackenzie Rig Status

Canadian Beaufort Sea

SDC Drilling Inc.			
SSDC CANMAR Island Rig #2	SDC	Set down at Roland Bay	Available

Central Mackenzie Valley

Akita/SAHTU			
Oilwell 500	51	Still out of the NWT, but is again available	Available
TSM 7000	34	On the move to East Mackay I-78 in the Sahtu	MGM Energy Corp.
Cook Inlet Energy			
Atlas Copco RD20	37	Racked in Norman Wells, NT	Available

The Alaska - Mackenzie Rig Report as of March 14, 2013. 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 Marti Reeve


JUDY PATRICK

Baker Hughes North America rotary rig counts*

	March 8	March 1	Year Ago
US	1,752	1, 757	1,973
Canada	580	655	655
Gulf	49	50	41

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

● GOVERNMENT

Fairclough: tax bill process thorough

Senator on all three committees that have seen SB 21; working concern gross revenue exclusion might eventually cover all production

By STEVE QUINN
For Petroleum News

Sen. Anna Fairclough has never backed down from a heavy workload since joining the Alaska Legislature in 2007.

As a freshman member of the House, the Eagle River Republican served on seven committees.

Now as a newly elected Senator she is the only member to serve on the TAPS Throughput, Resources and Finance committees.

That places her on the front lines of the highest profile bill this session: Gov. Sean Parnell's oil tax reform proposal.

Before the Senate Finance Committee approved of a committee substitute and forwarded the bill to the entire Senate, Fairclough sat down with Petroleum News to discuss oil and gas issues.

Petroleum News: Having sat on all three Senate committees hearing SB 21, how do you think the process went?

SEN. ANNA FAIRCLOUGH

Fairclough: I think it's been very fair. It's been methodical. It's been slow. The chairmen of the TAPS Throughput Committee as well as the Resource Committee has tried to make sure that all perspectives were allowed at the table and that methodologies could be changed. You could ask your chairman anything you wanted. Now if you've chosen to remain quiet until the very end, that creates, maybe in some people's minds, the perception of not being inclusive. But both chairmen have been wanting to hear what the general public had to say about the proposed changes and secondary to the committee, what each committee member wants to talk about.

Petroleum News: What provisions of the bill right now do you think can help?

Fairclough: Well, the gross revenue exclusion is trying to provide that incentive and that connection between actual production and what Alaskans receive in a benefit in the form of a credit. So, I believe the governor's proposal for gross revenue exclusions is trying to incorporate all that we've heard in the last two years, if not three years, on how we can tie production to credits.

Petroleum News: Now that's still being worked out, the formula, and could be when it gets to the House as well.

Fairclough: Exactly. In the Senate Resource Committee, a concern was raised, would all oil eventually become gross revenue exclusion oil. In other words would all oil, production North Slope, or otherwise, start to receive that gross revenue exclusion and Alaskans would see a credit become a norm.

So again, there was conversation in the Resource Committee of whether there should be a time limit on that, and I support that. I assured the member who raised that issue that I would carry that forward in the Finance Committee. Again, when people drop amendments and don't talk to people about those amendments, it's hard to say yes, I support it or no I don't until you have an opportunity to think about it for a little while.

It's like the bill. In the TAPS Committee, I want to hear line-by-line, section-by-section and hear what the administration is proposing from their perspective. Sometimes the language doesn't match the proposal. So when someone just lays an amendment on the table, whether it's on the Senate floor or in a committee, and they haven't had the courtesy to tell me why they are proposing it, versus just in the public forum, I don't have a lot of opportunity to say that's a good idea or no that's not.

Petroleum News: Why did you set yourself up for TAPS, Resources and Finance; that's quite a workload?

Fairclough: During organization, I wanted to be involved in TAPS because of the whole throughput issues, wanting to make sure that there was quality maintenance going on for the trans Alaska pipeline; wanting to make sure people took the time to understand the viscosity issue, the water issue in the line; pigging and why cleaning is important; the feeder lines; the agreements inside of who controls how much oil can be in there and who can put that oil in the pipeline. Those are all important things for Alaska. It's our backbone. We need to ensure that backbone is functioning properly. That it allows appropriate access and that it's maintained well.

Q AND A

Resources was an opportunity to learn and understand more about all different facets of our state, whether it's fishing that might be important to medium size communities to rural communities that depends on our rivers and stream or the hunting aspects that are very controversial. As you know, when I served in the House for my first term, I replaced a member and was able to serve for one year on Resources. So this is a chance to expand that statewide perspective on issues really important to Alaskans.

House Finance works differently than Senate Finance, and I've always wanted to understand the economics of Alaska, to make sure Alaska has a vibrant economy so people can go to work, that there is quality education and one way to do that is make sure our fiscal picture looks healthy,

see **FAIRCLOUGH Q&A** page 15

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CLARIFICATION

Base case budget

An article in the March 10, 2013, issue of Petroleum News regarding plans by ConocoPhillips to spend some $2.5 billion on its existing properties in Alaska over the next five years ("Sending AK tech abroad") included the sentence, "It's unclear whether the investment is any different than normal fieldwork." ConocoPhillips has since confirmed that the proposed $2.5 billion in spending would come from its "base case" budget for Alaska through 2017 and does not represent plans for additional spending.

● PIPELINES & DOWNSTREAM

Clearing one major hurdle

Proponent of BC refinery says he has debt financing for C$25B venture; needs producer, customer, aboriginals, government backing

By GARY PARK
For Petroleum News

A Canadian newspaper publisher is gradually attracting some believers from the ranks of many skeptics, seven months after publicly disclosing his dream of building a 550,000 barrel-per-day refinery at Kitimat on the British Columbia coast.

With no previous background in the petroleum industry and faced with the reality that a new refinery has not been built in Canada since the 1980s, David Black says he is now less than two months from making a final decision to proceed with a C$25 billion project — C$16 billion for the refinery itself, C$6 billion for a crude oil pipeline, C$2 billion for a gas pipeline and C$1 billion for ocean-going tankers.

Black said he is personally prepared to pay the estimated C$2 million cost of steering the proposal through the government regulatory process.

More importantly, he claims to have debt financing arranged and be on the verge of signing a memorandum of understanding to finance the project, although the obstacles ahead are considerable — lining up offtake customers, winning over First Nations and gaining the support of oil sands producers and governments, notably the British Columbia administration.

Investors interested

But few expected him to reach the point where he and Richard Cooke, senior managing director of Oppenheimer Investments Group for the Americas and Asia, reported the Swiss-based financing company has enough investors interested in the venture to fund the total cost through a debt-financing model.

Cooke said interest in the refinery is strong, adding "we have the funding committed to do this whole project."

Black said the financiers have an interest in products the refinery would produce, including diesel and jet fuel.

He said "there are huge pools of money that are looking for infrastructure investment that is safe and (the refinery) is safe. We will be the lowest-cost provider, there is a 100-year supply of oil and a 100-year supply of gas. That is a perfect situation."

While working on the financing issues, Black has also opened exploratory talks with First Nations on a possible ownership stake in Kitimat Clean, the private company he has established to develop the refinery.

Pressure on Northern Gateway

Both Black and Cooke expect the proposal will put pressure on Enbridge's proposed Northern Gateway pipeline, which has encountered stiff opposition from aboriginal communities, environmentalists and local residents to the plan for shipping 525,000 bpd of oil sands bitumen from Alberta to the deepwater port at Kitimat.

Todd Nogier, a spokesman for Enbridge, said his company is "neutral" on the refinery proposal, leaving the decision on how Northern Gateway is used over to shippers.

Black said "very good progress" is being made on all fronts, including the completion of preliminary design work for the plant.

Refined fuels from the refinery would be transported to markets around the Pacific Rim, he said, adding that potential Chinese customers have indicated they would sooner buy refined products than bitumen.

He told the British Columbia Chamber of Commerce that the projected refinery cost is up C$3 billion from his initial estimate last summer, largely because of changes to technology he plans to use to reduce greenhouse gas emissions.

He said the refinery will consume about 1.25 billion cubic feet per day of British Columbia gas and process Alberta crude bitumen that is otherwise "in danger of being landlocked."

"By changing the North American supply/demand situation this will have the additional positive effect of reducing the C$25 billion per year of existing sales discounts on all Canadian oil exported to U.S. refineries," Black said.

He said that by eliminating coking equipment from the original design in favor of gasification and using Fischer-Tropsch equipment, GHGs per barrel of refined products would be lowered by 50 percent. The Fischer-Tropsch process converts bitumen into lighter fuels by injecting large quantities of natural gas rather than breaking down heavy crude molecules through a coking process.

New processing approach

Black also announced that Calgary-based Expander Energy has recently patented a new approach for processing heavy oil and the Kitimat refinery would be the first to use the technology, which he estimated would be "roughly equivalent to running 40 diesel trucks or buses."

He argued that turning bitumen into gasoline or diesel, which would evaporate if spilled, should remove a major worry for British Columbia residents about the risks to their coastal waters.

To support that view, he commissioned a poll through the Mustel organization, conducting 800 interviews between February 18 and 24 and discovered that 80 percent of British Columbians were aware of the proposal.

The respondents, after being told the project would create 3,000 permanent jobs and 6,000 construction jobs, generate tax revenues and use technology that would minimize pollution and greenhouse gas emissions, indicated strong support for the venture.

While 70 percent of British Columbia residents are opposed to Northern Gateway, that number was almost reversed when the refinery component was included.

Economic benefits cited

The reasons most cited for support were economic benefits for British Columbia (20 percent) and job creation (17 percent), while those opposed cited environmental concerns (21 percent), concerns about oil spills (9 percent) and distrust about the information provided (9 percent).

If an environmentally sound method could be demonstrated for shipping crude bitumen from Alberta to the refinery, the poll indicated backing for the proposal increased to 66 percent and opposition dropped to 24 percent.

Among the doubters, University of Alberta business professor Richard Dixon said the idea is a gamble given that bitumen prices would have to remain at today's levels — C$40 per barrel below world oil prices — to make economic sense.

"What (Black) is gambling on is that the price differential will hold for five years" and that's unlikely, Dixon said.

He said the industry is cautious about new refineries when it is cheaper to retool existing plants to handle heavy crude.

Suncor Energy, the largest oil sands producer, and the Canadian Fuels Association say it is premature to comment on Black's proposal.

But Suncor has recently signaled its own unease about building upgrader to convert bitumen into synthetic crude for refining into transportation fuels by shelving plans for its C$21 billion Voyageur upgrader.

Aboriginal criticism

Art Sterritt, a spokesman for Coastal First Nations, an umbrella group representing some of the largest aboriginal communities on British Columbia's north and central coasts, criticized Black for "making the same mistakes as Enbridge by going public and trying to jam people on the project" before talking to First Nations.

Black endorsed as "commonsense" the five conditions British Columbia Premier Christy Clark has attached to Northern Gateway: Full environmental approvals, the best possible marine spill protection for the coast, enhanced spill cleanup systems along the pipeline route, meeting First Nations' concerns and guaranteeing British Columbia s share of the economic benefits for taking the bulk of environmental risks.

Clark told the British Columbia legislature her government, which faces defeat in a May 14 election, "wants to use every tool at our disposal to move the proposal forward where it can be judged on its merits by a robust, rigorous and, most importantly, independent environmental process (free) from political interference."

She put the refinery in the same league as her government`s support for LNG projects, calling for a cooperative effort to address the legitimate environmental and safety concerns and find a way to get to "Yes" on projects that will grow our economy." ●

Contact Gary Park through publisher@petroleumnews.com

● FINANCE & ECONOMY

Independents: SB 21 better than ACES

Armstrong's Kerr tells Senate Finance development puts oil in the pipeline, not exploration; Pioneer says issue competitiveness

By KRISTEN NELSON
Petroleum News

Is the Resources Committee substitute for Senate Bill 21 a perfect change to Alaska's current oil and gas production taxation system?

It's not, three of the smaller players on the North Slope told the Senate Finances Committee March 5, but they all said it's preferable to what's in place now — ACES, Alaska's Clear and Equitable Share.

1 2 SERIES

Todd Abbott, president of Pioneer Natural Resources Alaska, said negatives on the proposed changes include the loss of capital credits, the increased base tax rate and a complicated carry-forward loss calculation.

Those factors, he said, are disadvantages to new entrants.

Pioneer is a net investor in the state, Abbott told legislators, spending more money than it makes in Alaska, and that means benefits under the committee substitute, the CS, don't come to the company until out in the future. That means near-term costs under the CS have increased, he said, and more important, the long-term benefits haven't increased enough to offset the near-term costs for Pioneer.


TODD ABBOTT

Capital credits have been removed, in response to concerns that if oil prices fall in the future, the state wouldn't have enough income to pay out on credits.

Abbott said Pioneer favors credits. They directly encourage activity in Alaska, he said, and reduce investor risk. He told legislators that credits create activity by definition — for Pioneer to gain credits the company has to be doing a project. Abbott said he understood legislators' caution about the cost to the state of credits, but thinks the answer lies in the totality of the fiscal structure. The credits in the existing system are a good thing, he said, while a lot of other things in ACES inhibit growth.

No simplification

The proposal does not simplify tax calculations because of the carry-forward loss calculations and does not strongly motivate additional investment, Abbott said.

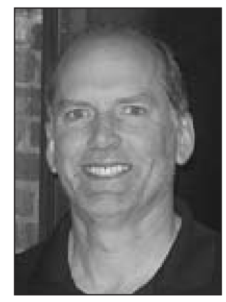
Proposed changes which Pioneer favors include the elimination of progressivity. That allows producers to share the upside potential and improves competitiveness, he said. Pioneer also finds positive the gross revenue exclusion, or GRE, a tax reduction for new oil, and the extension of the small producer credit.

Abbott said Pioneer recommends targeted credits for new facilities and well-related costs; allowing those targeted credits to be redeemable or transferable; and allowing credits to be taken against any payment to the state.

He said he understood the issues with blanket credits and suggested that allowing credits for new wells would be one way to start with credit changes. But, Abbott said, new facilities are also required to produce new oil, and cited the Nuna prospect Pioneer is working on now.

On the issue of exploration and new oil, Abbott said it isn't exploration that puts new oil in the line: it's development. Exploration credits without development credits get you only partway there, he said.

Armstrong: Better than ACES


ED KERR

Ed Kerr, vice president land with Denver-based Armstrong Oil & Gas, told legislators that to the extent the state's tax policy gets better, production will get better.

We're all trying to get the most equitable deal, he said, but the concern is that nothing happens.

While ACES has provided increased revenue to the state, production decline continues and Alaska isn't seeing the benefit of investment, Kerr said.

He cited the increase in production in Texas and North Dakota, while Alaska production has declined, and said that something needs to be done in the legacy fields, noting that Armstrong doesn't "have a horse in that race." The company operates in Cook Inlet, but not on the North Slope, where its current partner, Repsol, is the operator.

Alaska's geology is "fantastic," he said, comparing the state to "the pros" while North Dakota is "a junior-high team."

Rig count

Kerr said Alaska's rig count — some 14 in all of the state, split half and half between the North Slope and Cook Inlet — is "anemic." Last year 79 new producing wells were brought online in Alaska, he said, compared to more than 9,000 in Texas, calling it a direct corollary to the rig count.

More drilling is needed, he said, and the current tax system isn't going to promote that.

Kerr said Armstrong Oil & Gas supports SB 21, although the company doesn't believe it's enough, but "if we have to live with it, we'll take that over ACES," he said.

The rocks on the North Slope are fantastic, he said, and a lot of companies would like to work there, but the tax policy has got to motivate them.

While ACES is the biggest thing keeping people away, other negative factors are the North Slope climate, the expense of working in the state and regulatory issues.

There is a lot of interest in the state, Kerr said, but if nothing happens on the tax regime, that interest will go away.

The biggest improvement in the CS, he said, is that progressivity is gone.

The explorer

Alaska Venture Capital Group, through its operator Brooks Range Petroleum, does not yet have production in the state.

Ken Thompson, AVCG co-owner and investor, reviewed the company's work at its Mustang development project and its experience in bringing other independents to the state and in raising capital for Alaska work and said the biggest hurdles AVCG has heard keeping others out of Alaska are the complex and high government take of Alaska's fiscal system, resulting in a flow of capital to Lower 48 projects.

Thompson said positives in the CS include the increase of the carry forward loss credit from 25 percent to 35 percent and interest on unused credits, because it will provide more future cash flow for facilities and drilling in the state.

The extension of the small producers' credit to 2022 is also a positive.

The elimination of the 20 percent qualified capital credit is a negative for AVCG, Thompson said, and requested that it at least be extended through 2014 to cover Mustang development and drilling. The Mustang project, he noted, was approved when those capital credits existed, requiring less owners' funding for Mustang.

Elimination of progressivity

The elimination of progressivity is positive, Thompson said, as it both simplifies tax calculations and will be "a public relations" plus for the state.

But the increase of the base tax rate from 25 percent to 35 percent was not expected, and when AVCG runs economics, the $5 per barrel credit for produced oil only partially offsets the increase, helping at low oil prices.


KEN THOMPSON

The increase in the CS from 20 percent to 30 percent on the GRE should incentivize new oil production and also helps at low oil prices, he said.

Thompson cited as a "huge positive" the removal of the old distance limitations for exploration wells. The improvement allows the credit for exploration wells targeting new oil, regardless of location.

He said that overall the tax changes should help in attracting new capital and leveling oil production.

Proposed changes

In addition to eliminating progressivity, the CS from Senate Resources would raise the base tax rate from 25 percent to 35 percent balanced with $5 per taxable barrel allowance for produced oil.

Credits which remain under the proposed changes would only be redeemable against future production.

The goal is to make Alaska more competitive for investment.

ACES, the current production tax system, has resulted in very high production taxes, driven by progressivity — a boon to the state but not to producers.

The elimination of qualified capital credits addresses two concerns: those credits have not stemmed production decline and because of the volume of credits and the fact

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● FINANCE & ECONOMY

ISER forecasts rise in oil spending

Annual outlook of construction industry sees large growth from the oil and gas sector, but warns about plans falling through

By ERIC LIDJI
For Petroleum News

A big boost from the oil and gas sector is expected to drive growth in the construction industry this year, according to an annual forecast from the University of Alaska.

The construction industry is expected to see an 8 percent increase in spending this year to nearly $8.4 billion, with the largest share, $3.6 billion, coming from the exploration and production of oil and gas, according to the Institute of Social and Economic Research.

The forecast is a 13 percent increase in oil and gas construction spending over 2011.

"The growth is being driven by the continuing high prices of oil and gas, the increase in the cost of inputs to all phases of oil and gas operations, the growing need to maintain the aging infrastructure and facilities on the North Slope and in Cook Inlet, and last but not least, the tax credits available to companies as part of Alaska's Clear and Equitable Share production tax," ISER's Scott Goldsmith and Mouhcine Guettabi wrote in the report.

While oil and gas is the dominant sector driving spending, ISER threw some cold water on its forecast by noting that weather, logistics, commodity prices, state tax policy and potential federal energy initiatives always have the potential to impact company plans.

Additionally, ISER noted, "Some companies new to Alaska have tended to be overly optimistic in the last couple of years" when it comes to announcing proposed activities.

Excluding oil and gas, construction spending is expected to rise some 4 percent this year.

Work detailed

In terms of spending, the North Slope dominates the forecast.

The "most significant" spending from the majors will go toward increasing production from existing fields, but includes some additional programs. ConocoPhillips is starting its CD-5 development, preparing for Chukchi Sea exploration and potentially drilling in the National Petroleum Reserve-Alaska. Exxon is continuing its work at Point Thomson.

The forecast also includes ongoing developments from the two other producer-operators on the North Slope: Pioneer Natural Resources and Eni Petroleum. And it covers exploration by Brooks Range Petroleum Corp., Repsol USA E&P and Linc Energy Ltd.

It also includes work on the trans-Alaska oil pipeline.

While the majority of the spending appears to be on the North Slope, the majority of the growth appears to come from the ongoing renaissance of activity

see **ISER FORECAST** *page 9*

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INDEPENDENTS

that they are redeemable by the state, they are a liability of the state which could be difficult to meet should oil prices drop.

Lawmakers have also been concerned about the impact on investment of frequent changes in the state's fiscal system, and want to put in place a system which will be durable, providing assurance for companies considering investments in the state.

While increased investment — ultimately leading to more production — is a goal fiscal system changes, the short-term result will be lower oil tax revenues.

There appears to be some agreement across party lines that progressivity at high oil prices is too high, but there is not agreement on the short-term decrease in state revenues aimed at long-term increase, or at least flattening, of North Slope production. ●

Note: Part 1 of this story, reaction of major North Slope producers to the CS for SB 21, appeared in the March 10 issue of Petroleum News.

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ENVIRONMENT & SAFETY

Sen. Begich pushes BLM on legacy wells

U.S. Sen. Mark Begich, D-Alaska, is calling on the Obama administration to promptly clean up so-called legacy wells on the North Slope.

In a March 7 letter, Begich asked Bud Cribley, Alaska director for the Bureau of Land Management, to "formally and personally reassure Alaskans" that the agency "has a workable plan to properly plug and abandon these wells."

The legacy wells, predominantly within the BLM-managed National Petroleum Reserve-Alaska, were drilled decades ago by federal departments or their contractors to assess the reserve's oil and gas potential.

State drilling regulators and other elected officials including Alaska's senior senator, Republican Lisa Murkowski, have said dozens of well sites are in poor and junky condition, and that the BLM needs to get busy with a cleanup.

SEN. MARK BEGICH

Draft inventory submitted

BLM officials have cited the remote location of the wells and the enormous costs to plug and abandon them. Recently, the BLM submitted a draft inventory of the wells to the Alaska Oil and Gas Conservation Commission, which regulates drilling in the state. The inventory will help the BLM develop a five-year strategic plan for dealing with the legacy wells, an agency spokeswoman said.

State drilling regulators and other elected officials including Alaska's senior senator, Republican Lisa Murkowski, have said dozens of well sites are in poor and junky condition, and that the BLM needs to get busy with a cleanup.

Begich, in his letter, also asked Cribley to explain how the BLM will satisfy terms of the National Historic Preservation Act without slowing down the cleanup process.

The BLM has said legacy wells 50 years old or older are subject to a mandatory process to document their historic value.

Begich also said he understood BLM representatives had "rather unhelpfully," though perhaps accurately, stated at a hearing the AOGCC convened Jan. 10 on legacy wells that the BLM was not bound by state law and state well standards.

The senator noted the AOGCC had "done an admirable job" ensuring maximum resource utilization while protecting the public and groundwater. He concluded his letter by saying, "Alaskans expect better results on the legacy well issue than they have seen to date."

—WESLEY LOY

● FINANCE & ECONOMY

EIA expects 2013 Brent average of $108

Net oil imports projected to continue to fall, reaching 32% in 2013, lowest since 1985; China poised to become largest importer

By KRISTEN NELSON

Petroleum News

The U.S. Energy Information Administration said in its March Short-Term Energy Outlook that it expects the Brent crude oil spot price to average $108 per barrel this year and $101 per barrel in 2014, down from an average of $112 per barrel in 2012, reflecting an increasing supply of liquid fuels from non-OPEC countries.

EIA said members of OPEC, the Organization of the Petroleum Exporting Countries, cut production heavily in the fourth quarter of 2012, contributing to a rise in crude oil prices at the start of 2013. This was particularly true of Saudi Arabia: the agency said estimates are that country's production dropped by some 900,000 barrels per day between the third quarter of 2012 and February, from an average of 9.9 million bpd to 9 million bpd.

Non-OPEC production is projected to increase by 1.2 million bpd this year and by another 1.4 million bpd in 2014, EIA said, with North America accounting for almost three-quarters of the non-OPEC growth over the next two years "because of continued production growth from U.S. tight oil formations and Canadian oil sands."

Rapid US growth projected

EIA said it expects U.S. crude oil production to continue to grow rapidly over the next two years, from a 2012 average of 6.5 million bpd to 7.3 million bpd this year and 7.9 million bpd in 2014.

"Drilling in tight oil plays in the onshore Williston, Western Gulf, and Permian basins is expected to account for the bulk of forecast production growth over the next two years," EIA said.

The agency is projecting Alaska production to decline from an average of 530,000 bpd last year to 500,000 bpd this year and 470,000 bpd in 2014. U.S. federal Gulf of Mexico production averaged some 1.3 million bpd last year, down some 50,000 bpd from 2011 and is expected to increase to an average of 1.4 million bpd this year and 1.5 million bpd in 2014, the agency said.

"After reaching a record 60 percent of domestic oil demand in 2005, net oil imports next year are forecast to fall to 32 percent of consumption, the lowest level since 1985."
—EIA Administrator Adam Sieminski

"Higher U.S. oil production means America will need less imported oil. After reaching a record 60 percent of domestic oil demand in 2005, net oil imports next year are forecast to fall to 32 percent of consumption, the lowest level since 1985," EIA Administrator Adam Sieminski said in a March 12 statement.

He also said that with falling U.S. oil imports and rising Chinese demand, China is moving "closer to passing the United States as the largest global net oil importer. Net oil imports for the United States and China were on par at 6 million barrels per day in December 2012, according to the most recent trade data from EIA and China's General Administration of Customs."

Natural gas

"U.S. natural gas production should level off from the growth seen in recent years, and natural gas consumption is expected to remain around 70 billion cubic feet per day for 2013 and 2014," Sieminski said.

The agency noted that as natural gas production in the U.S. shifts inland, "well freeze-offs have become a greater supply disruption risk during the winter," with a 3.5 percent decline between November and December in New Mexico the largest of any state or region, "as operators reported shut-ins resulting from freeze-offs," with freeze-offs continuing to affect production in western U.S. states in January.

EIA said working gas stocks totaled 2.083 trillion cubic feet on March 1, 361 bcf less than at that time last year, but 269 bcf greater than the five-year (2008-12) average. EIA said it expects an end-of-March level of just under 2 tcf, less than the unusually high 2.477 tcf at the end of March last year, but well above the five-year average of 1.726 tcf.

Natural gas spot prices averaged $3.33 per million British thermal units at the Henry Hub in February, "relatively unchanged from the previous two months," EIA said. The agency said it expects the Henry Hub price to increase from a 2012 average of $2.75 per million Btu to $3.41 per million Btu this year, and $3.63 per million Btu in 2014.

Economic assumptions

Economic assumptions in the EIA's energy price forecasts incorporate recent tax changes in the American Taxpayer Relief Act of 2012 and assume that spending cuts mandated in the Budget Control Act of 2011 will be replaced by a combination of income tax increases and spending cuts implemented in 2014. The assumptions also include an agreement to increase the debt ceiling in the near term, EIA said.

"Recent economic indicators suggest that growth may be picking up, particularly in the manufacturing sector," the agency said.

A real GDP growth of 1.8 percent is assumed for the year, rising to 2.7 percent in 2014, with relatively slower growth in the beginning of the year following the expiration of the payroll tax cut. ●

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● LAND & LEASING

State approves lease deals in February

Assignments cover leases at Oooguruk, Nikaitchuq, Southern Miluveach, Point Thomson and other regions across the state

By ERIC LIDJI

For Petroleum News

The state approved and announced several lease-related deals in February.

Stuart W. Gustafson requested to transfer a small royalty interest — all in values of less than one-tenth of 1 percent — in 34 leases in the Pioneer Natural Resources-operated Oooguruk unit, the Eni Petroleum-operated Nikaitchuq unit and the Brooks Range Petroleum Corp-operated Southern Miluveach unit to the Maeco Family Trust.

The Armstrong Resources subsidiary 70 & 148 LLC transferred 11 North Slope leases outright to Repsol E&P USA Inc, and transferred a 70 percent working interest and a royalty interest between 58.33 and 61.25 percent royalty interest in 11 other North Slope leases to Repsol. The two companies are partnering on North Slope exploration work.

And Pioneer Natural Resources transferred 100 percent working interest and an 83.33 percent royalty interest in ADL 391459 to 70 & 148 LLC. The lease is adjacent to the southwest corner of the Oooguruk unit and contiguous with a block of 70 & 148 leases.

Finally, the state issued six Beaufort Sea leases to investor Daniel K. Donkel.

Shuffles at Point Thomson

At the Point Thomson unit, several small investors transferred interests in two leases.

At ADL 47560, the Estate of Mary Lou Holbrook transferred a 0.757318 percent working interest and a 0.6475068 royalty interest to the Eastland Oil Co. but retained a 0.0515464 percent overriding royalty interest; the George A. Donnelly III 1991 Irrevocable Trust transferred a 0.504878 percent working interest and a 0.4417682 royalty interest to G. Arthur Donnelly III; and Peggy D. McConnell transferred a 1.514635 percent working interest and a 1.3253056 percent royalty interest to Eastland Properties and Minerals.

At ADL 51667, the Estate of Mary Lou Holbrook requested to transfer a 0.05154 percent royalty interest to the Eastland Oil Co; the George A. Donnelly III 1991 Irrevocable Trust requested to transfer a 0.035061 percent royalty interest to G. Arthur Donnelly III; and Peggy D. McConnell requested to transfer a 0.105183 percent royalty interest to Eastland Properties and Minerals.

Cook Inlet dealmaking

In Cook Inlet, NordAq transferred royalty interests in three leases to four investors.

At ADL 391838, NordAq transferred a 2 percent royalty interest to Tekram LLC and a 1 percent royalty interest each to Hugh North, Tramlaw LLC and Robert Warthen. The lease is located just north of Port Nikiski.

At ADL 391596 NordAq transferred a 1 percent royalty interest each to Hugh North, Robert Warthen, Tekram LLC and Tramlaw LLC. The lease is adjacent to the northwest corner of the NordAq-operated Shadura unit.

At ADL 391278, NordAq transferred a 1 percent royalty interest each to Hugh North, Robert Warthen, Tekram LLC and Tramlaw LLC. The lease is in the southern Kenai Peninsula, northeast of the Hilcorp-operated Nikolaevsk unit.

Additionally, at ADL 391057, John Kidd transferred a 3 percent royalty interest to Tekram LLC and a 1 percent royalty interest to NordAq Energy Inc; and Paul L. Devine transferred a 1 percent royalty interest to Tramlaw LLC. NordAq operates the lease, located just north of Nikiski, adjacent to ADL 391838.

Also in Cook Inlet, the WTF Distribution Trust transferred a 2.5 percent working interest and a royalty interest between 1.875 and 2.1875 percent in 37 leases at the Kitchen Lights unit to Cornucopia Oil & Gas LLC. ●

—A copyrighted oil and gas lease map from Mapmakers Alaska was a research tool used in preparing this story.

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ISER FORECAST

in the Cook Inlet.

The Cook Inlet forecast is led by Hilcorp's ongoing program to develop and expand the assets it acquired from Chevron/Unocal and Marathon, but also includes work connected to the two jack-up rigs currently in the basin for Furie and Buccaneer; exploration from Apache Corp., Cook Inlet Energy, NordAq and Linc Energy; and ongoing development from Armstrong, Aurora, ConocoPhillips, and Anchorage Municipal Light and Power.

Finally, the forecast includes Doyons Limited's work in the Nenana basin. ●

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NATURAL GAS

BC offers LNG terminal site

The British Columbia government plans to hold a land auction to establish a third cluster of LNG export terminals after the Kitimat and Prince Rupert sites.

Grassy Point sits on a narrow peninsula about 18 miles north of Prince Rupert and was once the site for planned LNG exports by Dome Petroleum before the company collapsed under the weight of its debt in 1984.

Dome chose the site because of its proximity to open water and its hard-rock topography.

That project would have supplied 2.35 million metric tons a year of LNG to Japan over a 20-year period. A C$2 million liquefaction plant, C$500 million pipeline and C$1 billion fleet of Japanese-built LNG tankers were all key elements of the plan.

But Mobil Oil, on behalf of its Canadian subsidiary, said at the time that potential buyers and sellers of the LNG were unable to reach an agreement.

Submissions until March 18

Submissions for Grassy Point will be received until March 18 from proponents who will be required to identify what land they need and provide a description of their project.

The government said the land is being advertised because of some preliminary interest in the area.

No decisions have been made on how much land will be made available or whether it will be sold or leased.

ExxonMobil, 69.6 percent owner of Imperial Oil; Nexen, now owned by China National Offshore Oil Corp; and AltaGas in partnership with Japan's Idemitsu have been exploring Canadian LNG projects, although they have yet to choose a terminal site.

Grassy Point is seen as having some drawbacks, largely its lack of road and rail connections, while the nearby Lax Kw'alaams First Nation does not have amenities to serve a large construction project and industrial site.

However, Dome did reach a benefits deal with the First Nation, which has since opened a trade office in Beijing and sold lumber to China.

—GARY PARK

ENVIRONMENT & SAFETY

Cook Inlet maritime risk ideas ranked

An advisory team examining ways to reduce the risk of oil spills from vessels transiting through or near Alaska's Cook Inlet recently prioritized its list of ideas.

The team is part of the Cook Inlet Risk Assessment project, which involves the Kenai-based Cook Inlet Regional Citizens Advisory Council, the Alaska Department of Environmental Conservation and the U.S. Coast Guard.

Tesoro, which operates a refinery at Nikiski and receives shipments of crude oil via tanker, is among the sources of funding for the risk assessment.

The Cook Inlet Risk Assessment Advisory Team met Feb. 22 in Anchorage and recommended eight measures for immediate implementation, or continuation. Among them: improve vessel crew training; improve winter rules for navigating in Cook Inlet ice; improve spill response equipment appropriate for Cook Inlet conditions; maintain depth through dredging, especially at Knik Arm Shoal; and expand cell phone coverage in the inlet.

The team determined eight other ideas merit further evaluation, such as enhanced vessel monitoring and communication; improved ice monitoring capabilities; increased rescue towing capability; and construction of a cross-inlet oil pipeline, which could eliminate tanker shipments.

The team also recommended dropping several ideas from further consideration, such as removing out-of-service oil and gas platforms and subsea pipelines. "Removal cannot be required until leases expire," the team noted.

The Cook Inlet Risk Assessment project next will refine its list of priority risk reduction options and establish a plan for further evaluation, a March 6 press release said.

More information is available at www.cookinletriskassessment.com.

—WESLEY LOY

PIPELINES & DOWNSTREAM

Idle pump station revived as oil heater

A pump station once relegated to standby status is now playing an important role in keeping the trans-Alaska oil pipeline running safely in winter, says operator Alyeska Pipeline Service Co.

Pump Station 7, located about 50 miles north of Fairbanks, is not needed to pump oil under normal operating conditions. But during cold stretches, the station is being used to heat crude oil.

Oil enters the pipeline on the North Slope at about 110 degrees. In years gone by, the oil stayed plenty warm on its 800-mile journey down the line. But with the Slope's steep decline in production, the crude is traveling slower, allowing the oil to chill. This invites serious problems, such as potentially damaging ice formation in the line.

Teams have installed additional piping and new values at Pump Station 7, as well as Pump Station 4, to conduct recirculation of oil, Alyeska reports in the January edition of its newsletter, The Line. With recirculation, oil is looped back through the pumps several times, which adds energy to the flow of oil and thus heat.

The newsletter explains: "During recirculation, a portion of the crude stream passes through drag valves that produce a pressure drop to develop heat. That same crude oil then flows through a full head pump that adds more heat with friction and increases the pressure. The crude oil goes through yet another drag valve, dropping the pressure again and producing additional heat before the oil re-enters the pipeline."

Alyeska says it's been doing oil recirculation at several pump stations for two years.

Creating friction actually means the pipeline system "is running less efficiently, but what the pipeline loses in efficiency, it gains in heat."

Some pump stations have been overhauled in recent years. Pump Station 7 is using an existing "legacy" pump to heat oil, Alyeska says.

—WESLEY LOY

● GOVERNMENT

Alberta feeling the budgetary pain

Province floundering in budget deficits not seen in 20 years; faces return to debt; critics call government price forecasts misguided

By GARY PARK
For Petroleum News

Alberta, the engine of Canada's petroleum industry, faces a "lot of pain" in its next fiscal year, warns Finance Minister Doug Horner.

The province is already floundering in budget deficits not seen in 20 years and faces the specter of a return to debt, most of the downfall blamed on what the government calls a "bitumen bubble" and what critics say are its own misguided forecasts.

When the province released its 2013-14 budget, Jack Mintz, who holds the chair of public policy at the University of Calgary, said the document contained "no plan except for hope — hope that (oil and natural gas) prices come back."

Premier Alison Redford described the budget as a "once-in-a-generation" opportunity to change Alberta's financial course.

In the meantime, financing the government's capital spending plans will require borrowing C$12.7 billion by 2015-16.

Opposition leader Danielle Smith said it took a generation from the early 1990s to wipe out Alberta's C$23 billion debt and predicted a debt of C$17 billion in time for the next election in 2016, suggesting it will take another generation to pay off the debt accumulated under Redford.

The government attempted to soften the deficit and debt blow by promising a law ensuring debt-payment costs never exceed 3 percent of the operating budget.

Plunge in resource revenues

Horner said the plunge in natural resource revenues, dragged down by weak natural gas prices and the "bitumen bubble" resulting from the price differential between Alberta's mainstay heavy crude and West Texas Intermediate light crude.

Resource royalties are forecast at C$7.25 billion for the year which starts April 1, compared with the C$11.67 billion it had earlier projected.

"Despite challenging conditions in the marketplace due to restricted crude oil pipeline capacity that resulted in favorable heavy oil prices and growing US oil production, the industry continues to invest," Horner told reporters.

"The 'bitumen bubble' seems to have a severe impact on our total earnings and has led to a drop of C$6.2 billion in revenues from our oil and gas sector. We need better market access as that will fetch our producers an international price," he said.

Despite unchanged spending from the current budget year that ends March 31, Alberta will post a C$2 billion deficit, about half the current year's estimated C$3.9 billion.

Bitumen revenues down

Royalties from oil sands bitumen are estimated at C$3.37 billion for 2013-14, down from the current year's C$3.8 billion, but the government is targeting C$6.69 billion in 2015-16.

Crude oil royalties are estimated at C$1.62 billion, down C$290 million from the year ending March 31, reflecting an increase in production from horizontal wells, which are eligible for a special royalty rate of 5 percent in the first year and 5 percent for an additional one to three years depending on well depths.

The budget is based on an average WTI price of $92.50 per barrel, while Western Canada Select at Hardisty, Alberta, is expected to average C$68.21, down slightly from the C$68.91 per barrel for 2012-13.

The Western Canada Select/WTI price differential for the new budget year is expected to be 27 percent compared with 26 percent in 2012-13, a spread the government expects will narrow to 22 percent in 2014-15 and 19 percent in 2015-16 as North American pipeline capacity, upgrading capacity in the U.S. and access to Gulf Coast refineries all increase.

Conventional crude steady

Alberta's conventional crude output is expected to remain steady at 550,000 barrels per day, while raw bitumen production is forecast to climb to 2.14 million bpd from 1.92 million bpd in 2012-13.

Natural gas revenue, once the government's revenue windfall, is expected to generate C$965 million in the upcoming year, compared with C$554 million in the 2012-13 year.

The government expects natural gas prices to average C$3.07 per gigajoule at the AECO Hub, compared with its revised forecast of C$2.26 for 2012-13, down from its budget target of C$3.

Gas production is forecast to drop to 3.87 trillion cubic feet, a sharp decline from the current year's 4.18 tcf.

Returns from government land auctions are expected to reach C$1.15 billion, compared with C$1.06 billion for 2012-13, barely half the original budget forecast. ●

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● EXPLORATION & PRODUCTION

Shell remains intent on Alaska program

Company not drilling this year but plans ice gouge survey and continuing environmental studies; reflects on 2012 activities

By ALAN BAILEY
Petroleum News

Shell remains committed to its exploration program in the Alaska Arctic offshore, Michael Macrander, Shell's science team lead in Alaska, assured the National Marine Fisheries Service's Arctic Open Water Meeting on March 7.

"We, Shell, have not lost our appetite for exploration in the Alaska offshore," Macrander said.

Company officials have previously commented that, with potentially huge oil and gas resources under Alaska's Arctic seas, Shell sees exploration of the region as strategic to the company's search for new petroleum reserves. But the company has experienced a series of setbacks in its Alaska program, culminating in the grounding in the Gulf of Alaska of its Arctic floating drilling platform, the Kulluk.

Ice-gouge surveys

With the Kulluk refloated and now bound for Asia for repairs, and with the Noble Discoverer, the drillship that Shell is using in the Chukchi Sea, also heading to Asia for repair work, Shell has already decided not to drill in Alaska waters in 2013. But the company does plan to conduct surveys in the Chukchi Sea this summer, using sonar equipment to map ice-gouge patterns in the seafloor, Macrander said.

"It's essentially surveying the sea bottom to look for the typical scars or gouges that ice keels make in the seafloor," he said.

The purpose of the ice-gouge surveys is to determine the patterns and depths of the gouges, to enable the design of subsea pipelines, ensuring pipeline protection that will prevent pipeline damage from sea ice. Shell has already conducted surveys of this type in previous years but the company needs several years' worth of data in order to assess the relative frequency and depths of new gouges, Macrander explained.

This year's surveys will take place over Shell's Chukchi Sea Burger prospect and over areas to the south and east of that prospect, Macrander said.

Pauline Ruddy from Shell said that the surveys would likely amount to about 600 line miles, taking two to three weeks to accomplish, depending on the weather.

Other activities

Macrander said that Shell is also considering some other possible offshore activities for this year's open-water season, although time is now running short to put in place the permitting and other arrangements needed for the activities to happen.

"There are numbers of operations and activities that we have been pushing off into future years in order to be able to focus on drilling in 2012 and 2013, so … there are conversations going on about other activities that we might be able to do this year," he said.

Shell has been considering doing some geotechnical borings in the seafloor, but that activity is now unlikely to happen, Macrander said.

This year there will be a continuing full implementation of the offshore acoustic monitoring systems that Shell, ConocoPhillips and Statoil are funding to monitor marine mammal activities. And all Shell vessels will carry protected species observers. Shell will also operate a nearshore aerial survey program in the summer of 2013, watching for and recording marine mammal activity. Macrander said that sound from the sonar equipment used for ice-gouge surveys is unlikely to impact marine mammals because the sound frequency will be higher than the hearing range of the animals.

And Shell will continue to operate a data acquisition and management system that enables the real-time overlaying of ice maps derived from satellite data with weather forecasts, vessel movements and other information pertinent to offshore activities, Macrander said.

Activities in 2012

Macrander also reviewed Shell's activities in the Arctic during the 2012 open water season, the season during which the company drilled a top-hole well section in the Burger prospect in the Chukchi Sea and a top-hole well section in the Sivulliq prospect in the Beaufort Sea.

A drilling support vessel laid drillship anchors at the Burger prospect between Aug. 8 and 10, with the drillship Noble Discoverer then anchoring on location on Sept. 7, Macrander said. The drillship subsequently had to move off location because of an encroaching ice floe but returned on Sept. 21 to commence drilling on Sept. 23. Drilling ended on Oct. 26, with the drilling vessel departing south on Oct. 28.

In the Beaufort Sea, anchor setting at the Sivulliq prospect took place between Aug. 18 and 22. The Kulluk arrived on location on Sept. 25 after the end of the Cross Island subsistence whale hunt. The start of drilling was delayed until Oct. 3 because of a late start to the Kaktovik whale hunt. Drilling ended in the Beaufort Sea on Oct. 27.

Macrander said that the delay in the Kaktovik hunt had resulted from some issues in the community and that, following negotiations, Shell had been able to move its rig into position while the hunt was still in progress. However, the drilling did not start until the villagers

see **SHELL PROGRAM** *page 12*

Noble Discoverer on its way to Asia

The Noble Discoverer drilling vessel is en-route for an Asian shipyard, having been picked up from the Alaska port of Seward by heavy-lift vessel, the Xiang Yun Kou, Shell spokesman Curtis Smith confirmed to Petroleum News in a March 13 email. According to a report in the Alaska Dispatch the Xiang Yun Kou loaded the drilling vessel on March 2 at Seward by submerging its cargo deck under the Discoverer and then refloating.

The Noble Discoverer is heading for Asia for repairs, following problems with its propulsion system.

The Kulluk, Shell's floating drilling platform that ran aground on the south side of Kodiak Island during a storm on Dec. 31, has now been towed to Dutch Harbor. Another heavy-lift vessel, the Xiang Rui Kou, sister ship to the Xiang Yun Kou, is on its way to Dutch Harbor to carry the Kulluk to an Asian yard for the repair of damage caused by the grounding.

The Kulluk should be picked up from Dutch Harbor around March 18 to 20, Smith said.

—ALAN BAILEY

COURTESY SHELL

The heavy-lift vessel, the Xiang Yun Kou, submerges its cargo deck under the drilling vessel, Noble Discoverer, in Seward, prior to refloating with the drilling vessel on board.

9th Circuit Court upholds Greenpeace injunction

The U.S. Court of Appeals for the 9th Circuit has upheld an injunction issued by the federal District Court in Alaska in May 2012, banning environmental activist organization Greenpeace from interfering with Shell's offshore Alaska drilling operations. Greenpeace had appealed the District Court decision to the 9th Circuit.

"We conclude that, in light of the serious risk to human life and property posed by the conduct that the preliminary injunction enjoins, and given the narrow tailoring of the order, the district court did not abuse its discretion in finding that the scales of equity tip in Shell's favor," the 9th Circuit court said in a majority opinion of a panel of three judges.

One judge in the panel presented a dissenting opinion, arguing that the reasoning behind the injunction was based in large part on the actions of people from outside the U.S., who the U.S. Greenpeace organization had no control over.

—ALAN BAILEY

● GOVERNMENT

Northwest Territories on verge of resource control

By GARY PARK

For Petroleum News

Canada's Northwest Territories has ended a quest stretching over decades by negotiating the basis for what Prime Minister Stephen Harper said will be "the power to make resource management decisions ... and the power to collect royalties."

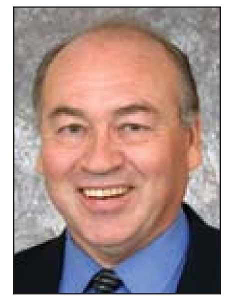
Speaking in Yellowknife, he said an agreement-in-principle transferring those rights from the Canadian government to the NWT is a key element of his desire to establish a northern strategy that places the destiny of the NWT in the hands of its residents and builds a "strong and prosperous north."

STEPHEN HARPER

In the process, Harper praised the dedication of NWT Premier Bob McLeod in achieving the agreement that is targeted for a final settlement in April 2014.

The Canadian government "believes the opportunities and challenges (in the NWT) would be better handled by the people who understand them best ... that is to say you who live here in the Northwest Territories, wherever possible, should make decisions about regional matters."

Some of the revenues from resource projects will go directly to the five NWT aboriginal governments that have signed on to the devolution agreement.



BOB MCLEOD

The Canadian government will keep ownership of offshore resources, notably the Beaufort Sea, but will open negotiations on revenue-sharing within 60 days of a final agreement.

Harper noted that a decade-old agreement with the Yukon Territory has seen unemployment rates drop and investment rise.

McLeod said the final pact is expected to be signed after his government has held community information sessions.

50% up to C$60 million

He said the agreement would allow the NWT to keep 50 percent of resource revenue up to an annual limit of C$60 million, with 25 percent of that amount going to native governments.

McLeod has long argued that the NWT, one of Canada's three territorial governments, should have the same rights as Canada's 10 provinces to "develop and market our natural resources without being held up in a regulatory logjam. The irony is that the NWT has vast oil and gas resources, but still has to import fuel."

He said the NWT is poised to take a leap, take on more province-like responsibilities and became less dependent on federal bureaucrats.

High on his action list is the Imperial Oil-operated Mackenzie Gas Project to develop an established 6 trillion cubic feet of Mackenzie Delta gas for southern Canadian and United States markets, but a venture that got bogged down through years of regulatory delays and has since been overtaken by the development of shale gas that has saturated continental markets.

McLeod said previously that if there is no North American market for the Mackenzie gas, the NWT should have the right to explore other options, including the export of that gas as LNG to Asia.

Former NWT premier Stephen Kakfwi, speaking for the two aboriginal governments that are holding out against devolution, said they fear that the NWT government will give greater priority to oil and gas activity than the socio-economic and environmental impacts of those projects.

He questioned whether consultation could be meaningful when the terms of devolution have already been negotiated. ●

Contact Gary Park through publisher@petroleumnews.com

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SHELL PROGRAM

had obtained their last whale, he said.

"We want to express our appreciation for all of the willingness to talk and to work together, to make things work for everybody," Macrander said.

Animal monitoring

All of the vessels involved in Shell's Arctic operations carried protected species observers, keeping watch for marine mammals. And, with as many as 57 observers deployed, the observers completed in total nearly 26,000 hours of watch-time, Macrander said.

Arrays of offshore acoustic recorders in the Beaufort Sea detected many bowhead whale calls, with the pattern of call locations indicating that the axis of the annual whale migration lay a little further offshore than normal early in the season. Curiously, however, there was a shoreward movement of the migration axis after Shell's operations started, Macrander said. And there were some whale calls detected within a couple of kilometers of Shell's Beaufort Sea drilling operation, he said.

Shell placed subsea acoustic recorders at a series of distances from the drilling operations in both the Chukchi and Beaufort seas, to gain insights into the types and levels of sound propagated through the water from a variety of different drilling activities. However, an attempt to characterize the Sivulliq drilling operation as a sound source ended after about 10 days when a storm broke the in-water sound recording system, Macrander said.

In addition to participating in communications centers in all coastal villages, to help achieve coordination between subsistence hunting and industrial activities, Shell worked with local subsistence advisors, embedded in the communities.

"Their job is to keep a finger on the pulse of what hunting activities are going on, what animal movements are going on, so that we can get that information and we can adjust our programs, such that we avoid impacts to hunting," Macrander said. ●

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● FINANCE & ECONOMY

Finance discussing committee substitute

Resources CS for SB 21 has been tweaked; focus remains increase in production; as with original bill, immediate revenues down

By **KRISTEN NELSON**
Petroleum News

More revenue now or the potential of more production and more revenue in the future?

That's the tradeoff facing legislators as they discuss changes in Alaska's oil and gas production tax.

Senate Finance's committee substitute for Senate Bill 21, the governor's oil tax changes, retains most of the features of the Resources CS, while turning a few knobs a little differently, Finance Co-Chair Kevin Meyer said March 12 when the Finance CS was introduced.

The base tax rate, set at 35 percent in the Resources CS, was dropped to 30 percent in the Finance version, with the offsetting $5 per taxable barrel allowance retained. The Finance CS drops the gross revenue exclusion from 30 percent to 20 percent, corresponding to the drop in the base rate, and expands definitions of applicable new oil to include oil from legacy fields which has not been in production, an area of the CS where work continues with the departments of Natural Resources, Revenue and Law. Application of the GRE is also limited to the first 10 years of production under the Finance CS.

The net operating loss carry forward can be monetized under the Finance CS, but only in exchange for investment in the state.

As the committee's vice chair, Anna Fairclough, put it in discussing monetizing the NOL — it's Alaska's money and Alaskans should benefit.

The Finance CS also adds a provision reducing what industry has called a punitive interest rate for delinquent payments, currently the fed rate plus 5 percent or 11 percent, whichever is greater, compounded quarterly, to the lesser of the fed rate plus 3 percent or 11 percent, compounded quarterly.

As with the governor's bill as introduced, progressivity is eliminated and qualified capital credits are eliminated.

Government take leveled

The combined government take — all applicable state and federal taxes — which ranges from 69 percent to 77 percent at oil prices from $80 to $140 per barrel for new entrants currently (under ACES, Alaska's Clear and Equitable Share) drops to 60 percent across that price range under the Finance CS. The government take for existing producers, which ranges from 66 percent to 75 percent from $80 to $140 per barrel under ACES, drops to an even 63 percent under the Finance CS.

Under the bill as originally proposed, those rates were 55 to 58 percent across those price ranges for new entrants, and a range from 56 percent to 60 percent under the Resources CS; and 62 to 64 percent for existing producers under the original bill, compared to 64 to 65 percent under the Resources CS.

The manufacturing tax credit added in the Resources CS doesn't change under the Finance CS, nor do exploration areas and extension of the small producer credit to 2022 is retained.

Meyer complemented the work the Resources Committee did on the bill.

The goal of the Finance CS was to be competitive, to get more oil in the pipeline, he said, noting that the GRE and $5 per barrel allowance are only applicable when oil is produced.

Revenue consequences

The divergence in committee views on the proposal were captured in comments from two of the members.

If these changes resulted in no more production than under ACES the fiscal impact — the reduction to state revenues — would vary from $1 billion to $1.3 billion in fiscal 2014, to as much as $1.4 billion to $1.8 billion in FY 2019.

Sen. Lyman Hoffman, D-Bethel, called

see **OIL TAXES** *page 14*

EXPLORATION & PRODUCTION

Plan for seismic survey off Colville Delta

A joint venture between SA Exploration and Kuukpik Corp., the Native corporation for the village of Nuiqsut, is planning to conduct a 3-D seismic survey in the shallow waters of the Beaufort Sea offshore the Colville River delta this summer, Rick Trupp, general manager of SA Exploration, told the National Marine Fisheries Service's Arctic Open Water Meeting on March 6. The survey, which would use state-of-the-art wireless nodal technology, with seismic receiver nodes placed on the seafloor, will be a non-exclusive program for multiple oil and gas leaseholders in the area, Trupp said.

The involvement of Kuukpik in the operation brings the benefit of local knowledge when planning and conducting the survey while also bringing economic benefits to the North Slope, Trupp said. In addition, most of the management team from SA Exploration has worked for a number years on Alaska seismic programs, he said. And, the company has established a strong group of local people to work as Inupiat communicators, subsistence advisors and marine mammal observers.

The plan is to mobilize the vessels needed for the survey in early July and conduct the survey between July 25 and Sept. 15, he said. The survey would involve a the use two seismic source vessels, two vessels for laying the seismic nodes, and a couple of bow-pickers to pick up equipment in the nearshore environment; a mitigation vessel would operate around the margins of the survey area, helping with a marine mammal monitoring program; a supply vessel would operate from the nearby Oliktok Point.

Protected species observers on the source vessels and the mitigation vessel would provide a continuous 24-hour watch for marine mammals.

—ALAN BAILEY

EXPLORATION & PRODUCTION

TGS plans Chukchi Sea seismic survey

Seismic company TGS proposes to conduct a 2-D seismic survey in the Chukchi Sea during the 2013 open water season, Steve Whidden, the company's project development and sales manager, told the National Marine Fisheries Service's annual Arctic Open Water Meeting on March 6.

The survey would involve a grid of widely spaced seismic lines covering a large part of the central and northern sections of the U.S Chukchi Sea, with a few lines extending into international waters in the extreme north of the sea, beyond the 200-mile limit of the U.S. exclusive economic zone.

The company wants to shoot the seismic to take advantage of the high quality of seismic imagery that can be obtained using modern seismic technology, Whidden said. High-quality 2-D seismic data can help a company make exploration decisions, perhaps determining where to shoot a high-resolution 3-D survey, he said.

Whidden told Petroleum News that TGS does not have any specific client for the survey and would make the survey data available for license.

TGS hopes to start its survey at some time between mid-July and mid-August, with the survey taking around 35 days to shoot — the total operational period, including some necessary down time, would be 45 to 60 days, Whidden said. The intention would be to complete the survey lines closest to the Alaska coast in July or August and move to international waters in mid to late September, or early October, he said. TGS anticipates being able to complete all of its seismic lines in U.S. waters, but completion of the international component of the survey might not be possible, depending on the ice conditions, Whidden said.

The survey would involve the towing of an eight-kilometer seismic receiver cable, he said. The seismic survey vessel would be accompanied by a scouting vessel for wildlife monitoring. If completed, the entire survey would gather about 9,500 kilometers of seismic data.

—ALAN BAILEY

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OIL TAXES

those numbers "truly staggering" and said that moving "this much cash across the table" would have detrimental effects on the state's operating budget and called any drilling resulting from the change "hypothetical."

Finance Co-Chair Pete Kelly, R-Fairbanks, asked whether it was the role of legislators to protect the interests of government or the interests of the people of Alaska. He said the interests of Alaskans include jobs and the ability to have a future in the state.

Too much is already being spent on government, Kelly said.

The state has too much government because it probably took too much from investors and now has to look at giving some back so they'll invest in the state, he said, urging that the proposed changes be measured not against what government wants but against what people want.

Competitiveness issue

Consultant Barry Pulliam of Econ One, for the administration, and Janak Mayer of PFC Energy and independent consultant Roger Marks, both under contract to Legislative Budget and Audit, all said the changes would make the state's fiscal system more competitive.

Pulliam said that compared to ACES all iterations of SB 21 made the state more competitive.

The net present value for a $20 a barrel capex development gets progressively better for the investor from SB 21 through the Resources CS to the Finance CS, Pulliam said. He said government take numbers from the Econ One model run for the administration were close to those of the Legislature's consultants.

He also said that under the CS numbers for new entrants are almost identical to those for incumbents, unlike under ACES where economics weren't as good for new participants. The small difference between incumbents and new producers under the Finance CS, with the new producer slightly better off, are driven by the small producer credit, Pulliam said.

Overall the changes put the new participant on a level playing field with the incumbent, he said.

Pulliam discussed the 10-year cutoff on the GRE, telling legislators it would raise the tax on new production just as wells become less economic, and could result in early shutdown. He said reducing the 20 percent GRE to 15 percent and allowing it to run to the end of well life would have about the same economic value for the producer.

Government take competitiveness analysis by PFC's Mayer showed the state more competitive at modeled price ranges from $80 a barrel to $140 a barrel, with the 60 percent government take for a new entrant falling between take rates for Texas and Australia under the Finance CS, and between Louisiana and Egypt at about 62 percent for incumbents.

Marks addressed the revenue implications of reducing taxes to make the state more competitive.

Alaska got where it's at today, he said, as the result of a large tax increase in 2007.

Marks said North Slope infrastructure — which he valued at some $60 billion including the trans-Alaska oil pipeline — couldn't go anywhere; he called it "captive investment" and compared that to Alberta which increased its royalty at about the same time, but without "captive investment." Drillers there simply moved their rigs, he said; production in Alberta fell; royalties were subsequently reduced and production came back.

On the North Slope, however, production continued and the state made a lot of money.

But, with lots of opportunities to produce oil around the world, corporations chose to invest their finite capital where they could make more money and Marks said that between 2007 and now there was a worldwide increase of about 50 percent in upstream capital, while in Alaska capital has stayed about the same as when oil prices were $60 a barrel.

And production dropped, he said, from some 850,000 barrels per day to 550,000 bpd.

He said that in taking the state from non-competitive to competitive you can't compare revenues using the same number of barrels, because with a competitive regime there will be more barrels produced. But, he said, there will be lead time before there is more production.

Marks said he looked at increasing production in 10,000-bpd increments to see what it would take to make more money over a 20-year period under the Finance CS. The crossover point, he said, is 70,000 bpd.

He noted that's not a lot — production dropped 300,000 bpd over six years and there are about 4 billion barrels of proved reserves on the North Slope, so producing 5 percent of that would be 70,000 bpd.

The tradeoff, he said, is a certain amount of ACES revenue now versus more-or-less non-ACES revenue down the road. ●

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● ENVIRONMENT & SAFETY

Cook Inlet discharge permits proposed

DEC and EPA permits would cover state, federal waters; drillers would be allowed to dump pollutants such as drilling fluids, cuttings

By WESLEY LOY

For Petroleum News

Government regulators are proposing to issue five-year "general permits" to oil and gas explorers to discharge certain pollutants into Alaska's Cook Inlet.

The Alaska Department of Environmental Conservation is proposing to issue a permit for state waters, while the U.S. Environmental Protection Agency is proposing a permit for federal waters.

The federal waters are defined as three nautical miles beyond the shoreline.

The general permits would allow exploratory drillers to discharge a range of pollutants, including drilling fluids and drill cuttings, into the inlet.

Other authorized discharges would include deck drainage, domestic wastewater, desalination unit wastes, blowout preventer fluid, boiler blowdown, fire control system test water, non-contact cooling water, uncontaminated ballast water, bilge water, excess cement slurry, and mud, cuttings and cement at the seafloor.

The permits would last five years, and would not cover discharges from development wells on Cook Inlet's established production platforms.

Regulators say they have the legal authority to issue general permits, as opposed to individual permits to drillers.

General permits have drawn some controversy and even legal challenge in the past.

Cook Inlet is a highly dynamic water body, noted for its large and strong tides, extensive mudflats, drifting winter ice floes, high turbidity, and fluctuations in salinity due to large glacial and freshwater inputs from surrounding drainages.

The inlet also is famed for its migrating salmon, and marine mammals such as beluga whales.

Cook Inlet is about 215 miles long and narrows to 10 miles wide between the East and West Forelands. The water is generally 120 feet deep north of the forelands, increasing to 480 feet to the south.

see **DISCHARGE PERMITS** *page 18*

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FAIRCLOUGH Q&A

so as you know for three years I've been trying to establish a fiscal plan. Finance would be my best opportunity to do that.

In the House, that's the only committee you have. In the Senate, because there is a smaller group of people, you are a partner on a whole bunch of different committees. The time also affects what you can ask to serve on. Finance can meet mornings and afternoons, so I have to be careful on where those other committees position themselves. TAPS, Resources and Finance wound up that, for most of the time, I can manage all of them.

Petroleum News: Go back to TAPS for a second. You detailed a lot of what you want to be involved with and what you want to learn. What have you learned that maybe you didn't in other hearings?

Fairclough: Well, people are saying there are more people at work on the North Slope than ever. That's a true story, but what are they doing? People allude that it's because of maintenance. That's what seems to be true. There's not a lot of well work in the form of new exploration. There is some exploration going that ACES contributed to. ACES is doing its work in some manner, in some functions. We have more, smaller explorers up on the North Slope, but they are not dropping those wells into the ground; they are not able, like the legacy fields, to produce oil in the short term. So Alaska's best hope if we want to stem the decline, is to get that oil from the legacy fields.

So with TAPS I'm learning more. We've had presentations from Admiral (Tom) Barrett before on TAPS and talking about the waxing issues. In the last year, I know they thought a ball of wax was a pig coming at the station where it would have been discharged, so they have to go back and find it. That's just new challenges that are happening because of the waxing situation. People may not know that Alyeska is currently exploring whether we can change this pipe to a cold line pipe in some way, and totally extract all water out of the oil and continue to move it without any freezing difficulties. It's new technology to see if the trans Alaska pipeline can migrate toward new equipment, new technology. I believe they have Alaskans best interests at heart when it comes to the environment. They want to have a reliable line for the investment group, the producers who put oil into the pipeline. They are trying to be responsible to people who utilize the line and the people of Alaska.

Petroleum News: You mentioned a feature of ACES that's working. What part of ACES is holding the state back?

Fairclough: The progressivity is a huge portion of that. I was OK with raising taxes on oil from 22.5 to 25 percent. But what was happening on the House floor and the Senate floor was what I consider a feeding frenzy. We just started turning knobs. We didn't know what the unintended consequences were those last 24 hours. I went to the speaker (John Harris) being a freshman serving on the House and said, 'I need a fiscal note. What happened here?'

We had just removed the ability for the legacy fields to monetize their expenses. Until they could get more information about what was qualifying as expenses, they wouldn't allow them for a certain period. I had no idea what the fiscal consequence of those knobs that they were turning on the House floor. It turns out it was over a billion dollars more in take that was unanticipated that was coming in that we didn't know we were going to get.

On progressivity, that was a concept the Palin administration had originally started at .2 percent, but in the end we took it to .4 above $92.50 a barrel. It was never modeled to the Legislature above $80 a barrel. So we had no idea of the consequences that night on the floor. So now the take is incredible. Alaskans are benefitting from that take, but industry is having a hard time from a global perspective competing for capital in those board rooms for Alaska, so there is less investment happening I think because of the progressivity take.

Petroleum News: Let's switch to natural gas. HB 4 could be coming your way soon and pipeline discussions will replace oil taxes. What are your thoughts on the status of the state advancing a pipeline project?

Fairclough: It's an incremental conversation in that Alaskans are most important to me. Whether you live in rural Alaska along the Kuskokwim or you live in Delta Junction or North Pole and the energy costs that are breaking economic opportunities for the people of Alaska. If we don't have a resource that can keep people warm and keep the lights on, Alaska will eventually whither and different pieces of Alaska will die off. I hope in all scenarios that the fuel whether it's propane or natural gas, that it can break off a backbone structure and make it to smaller communities so they can heat their families and keep their livelihoods whether its subsistence living or a refinery in North Pole that those economic opportunities are available at a reasonable cost. So with reasonable cost, another increment is what size should that pipeline be.

An argument and what I believe brought the bill (then HB 9) to its end last year was because the opposition was able to provide fear that the rates would be too high. We have to have that conversation, but coming from the Cook Inlet region, we had that conversation where the RCA told us the rates Marathon Oil were offering to Enstar were too high. RCA, in an attempt to protect the consumer, said no to those higher gas rates. Let me tell you, Marathon was right. RCA was wrong.

The consumers would have been better off today if we would have accepted those rates. Because it was something what we considered out of the norm, we said no, now we've invested huge dollars in a storage facility to try to keep the spikes down so we continue to supply Eagle River, East Anchorage and municipality of Anchorage.

So going back to the incremental, I don't know if a 36-inch line is right or a 24 or something smaller. But I do know Alaskans are starving for those energy molecules. We need to quit arguing about how we get there and find the best way forward to accomplish the goal.

Another increment we need to look at is our window. Right now the Asian market is still looking for natural gas in the form of contracts. If Alaska isn't on the board — now — this year, I think we miss our window for the long term. Then all we can look at is a state-funded, very small-diameter pipe to meet our needs, and I don't know then what the cost is on the North Slope to those who hold the leases and whether it would be cost prohibitive to bring our gas online.

Petroleum News: So what do you think can be done to get on the board for the Asian markets?

Fairclough: I think we need to bring all Alaskans together. I understand why Valdez wants a gas pipeline to their terminus. I understand why Nikiski wants a terminus to their point. As an Alaskan, I don't care. I want a cost-effective project that provides low transportation or at least reasonable transportation costs and puts those molecules into a market that Alaskans can benefit and I want a rate of return from somewhere outside of Alaska to help offset those prices for Alaskans. I don't know where the right point is. I think the private sector needs to determine that. Nikiski has its pluses in that it has a plant established there. Can we retrofit it so that it can last? Can we extend the life of that facility? Creating a new whole one at two different points is going to be expensive. In the end, I don't have a vested interest in whether it's Valdez or whether it's Nikiski. I have a vested interest that we just move forward.

For me, I would get it to North Pole, and then argue. We just need to get it across Alaska and coming. But we have to have the terminus point determined so we can actually establish the contracts. I would say to the naysayers, for those who don't want Nikiski, I wish they would put Alaskans first and quit arguing for their own personal benefits; for those who want to naysay on the Valdez terminus point, put Alaskans first and stop it.

Let's talk about a reasonable sized pipe that provides reasonable transportation. Alaskans in general have expectations that a 48-inch pipe is somehow normal. So anything lower than 48 inches may seem small. One of my questions to people who have been providing us information, is: is 24 inches standard for the rest of the world, or is it 36? I think it's 24. We are comparing it to the Trans Alaska pipeline sometimes when we really need to think differently. Alaskans are used to elephant pools of oil and large construction. We need to make sure our glasses on right when looking at what a natural gas pipeline should look like. ●

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Petroleum news

Oil Patch Bits

Homer Pratt Museum displays gray whale skeleton

COURTESY PRATT MUSEUM

The Homer Pratt Museum said Jan. 7 that the skeleton of a gray whale found across Kachemak Bay has found its home as the centerpiece of "Encounters: Whales in Our Waters" which opened Feb. 1.

With the backbone weighing nearly 600 pounds, a lot of heavy lifting was involved, as nearly 25 volunteers spent the morning of Jan. 5 moving pieces of the skeleton from the storage room into the special exhibits gallery.

The move was orchestrated by Lee Post, Homer's own whale skeleton articulation expert and director of last summer's Pratt Museum Community Gray Whale Project.

The whale was found across Kachemak Bay in June of 1999, and in July of 2012 more than 50 people took part in the project to repair the bones and get the skeleton ready for the exhibit.

For more information visit www.prattmuseum.org.

Tom Crowley honored for contributions to the USMMA

Crowley Maritime Corp. said March 4 that Tom Crowley, its president, chairman and CEO, became an honorary alumnus of the United States Merchant Marine Academy during a special banquet recently held in his honor. The USMMA Alumni Association and Foundation, along with its affiliated Jacksonville Chapter, recognized Crowley for his years of unstinting support of the academy and its cadets in front of more than 130 guests, including past and present Crowley employees and USMMA graduates, at the University Club in Jacksonville, Fla.

Several USMMA Alumni Association and Foundation members, including President James Tobin and Chairman of the Board of Directors Charlie Hill, thanked Crowley and his company, and presented him with a special portrait of a racing sailboat on Long Island Sound painted by fellow alumni.

"This is an immense honor for me, not just because this is one of the most important and outstanding institutions of higher learning, but because one of our company's core values is our people, and many of our people have their roots with this academy," said Crowley. "It's because of them, and those who will come after, that I will always support the U.S. Merchant Marine and its mission to develop maritime leaders."

Crowley has supported the USMMA through the establishment of the USMMA Scholarship Program funded by the Thomas B. Crowley Sr. Memorial Scholarship, which since 1994 has provided $10,000 in scholarship funds annually to deserving USMMA cadets.

Companies involved in Alaska and northern Canada's oil and gas industry

All of the companies listed above advertise on a regular basis with Petroleum News

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BP REVENUES

to-year is almost entirely attributable to a $3.5 billion item on the balance sheet reporting "gains on sale of businesses and fixed assets" outside Alaska, according to the company.

While the parent company BP plc usually breaks out financial information for BP Exploration (Alaska) in its annual 20F filing, the numbers also includes information from BP Exploration (Alaska) subsidiaries, some of which conduct business outside the state.

Even accounting for the sale, the 2012 balance sheet is further obscured by a nearly $1 billion impairment BP took in the second quarter after suspending its Liberty project.

Production, sales, taxes

For a better sense of how development activities, commodity prices and the Alaska fiscal regime impacted BP in 2012, it is better to look at production levels, sales and taxes.

BP produced some 139,000 barrels of oil per day in Alaska in 2012, down 9.1 percent from some 153,000 bpd in 2011 after dropping 7.8 percent between 2010 and 2011.

The declines came largely from smaller properties, though. The Prudhoe Bay field produced 77,000 bpd in 2012, down only 1.3 percent from 2011, while Milne Point produced 15,000 bpd in 2012, down more than 21 percent from 2011, and "other fields" including Northstar and Endicott produced 11,000 bpd, down 35 percent from 2011.

BP also produced some 18 million cubic feet of natural gas per day in Alaska last year, down from 22 million cubic feet per day in 2011 and 46 million cubic feet per day in 2010. With operations limited to the North Slope, BP's natural gas operations are limited to industrial uses.

The operator of the Prudhoe Bay field reported some $5.5 billion in sales and operating revenues in 2012, down from $6.1 billion in 2011 but up from $4.8 billion in 2010.

As would be expected with a drop in sales, taxes also fell year-over-year. BP Exploration (Alaska) paid some $1.5 billion in taxes in 2012, down from some $2.4 billion in 2011.

—ERIC LIDJI

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NORTHSTAR FIELD

brief case summary indicating "$160 million plus" is at stake in the Northstar dispute.

The summary indicates the dispute began in late 2009.

The dispute hasn't yet reached the courts. Rather, Murphy is pursuing an administrative appeal through the Alaska Department of Natural Resources.

A weeklong evidentiary hearing was held before a DNR hearing officer in March 2012.

The matter now sits before DNR Commissioner Dan Sullivan.

The appeal proceedings are confidential, and the hearing was closed. Petroleum News requested certain documents, but the state denied the request.

Martin Schultz, supervisor of the Department of Law's Oil, Gas and Mining Section, said the case is confidential due to provisions in state law protecting company tax, engineering and geological information.

However, Schultz was able to discuss a few details.

He described the case as a complex engineering and science case, with certain experts involved on both sides.

It's essentially "a battle over competing reservoir models" of the Northstar field, he said.

The state believes more of the field's production should be allocated to the state leases, with such production subject to state royalty and tax collections. Murphy, on the other hand, is arguing that more of the production should be allocated to the federal leases.

BP's status

The dispute reaches back to the field startup in 2001, Schultz said.

Northstar hit peak production of about 85,000 barrels per day soon after startup. State records show the field has produced about 156 million barrels of crude oil.

The $160 million the Department of Law estimates is at stake in the dispute seems enormous, given that Murphy Oil's ownership in Northstar is very small at about 1.4 percent.

But Schultz explained that the figure includes royalty and tax impact not only to Murphy but also to the field's major owner, BP.

BP is not a litigant, however, as only Murphy appealed the Northstar allocation issue, Schultz said.

Depending on the DNR commissioner's decision, an appeal to state Superior Court could follow.

"I have no way to predict when the commissioner's office might issue a decision," Schultz said.

DNR spokeswoman Elizabeth Bluemink indicated no decision was imminent. ●

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INSIDER

view with regards to Alaska," Schwartz said.

In September Statoil announced that it was deferring its planned Chukchi Sea exploration drilling from 2014 to 2015 at the earliest, as a result of challenges "experienced by others," in clear reference to the problems that Shell had encountered during its 2012 Arctic offshore drilling season. Statoil's position has not changed since then, Schwartz said.

"We're still evaluating the situation," he said.

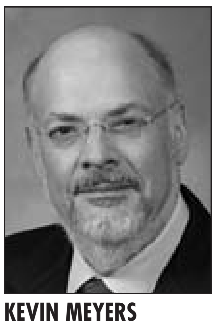
—ALAN BAILEY

Hess to focus on E&P, names ex-Alaska exec Meyers as a director

HESS CORP. IS GOING THROUGH a transformation, and a former Alaska oil and gas executive has been named to help lead the recast company.

On March 4, Hess announced several initiatives to become "a pure play exploration and production company."

Hess also named five new independent directors for election at the company's May 16 annual shareholders meeting. Among the five is Kevin Meyers, former president of ConocoPhillips Alaska Inc.



KEVIN MEYERS

Hess, headquartered in New York City, said its future production growth is expected to be driven largely by six core assets: the Bakken shale (North Dakota), the Valhall field (Norway), Tubular Bells (deepwater Gulf of Mexico), the North Malay basin (Malaysia), the Utica shale (Ohio), and Ghana.

The company said it would focus its portfolio by divesting Indonesia and Thailand, and is "pursuing monetization of Bakken midstream assets, expected in 2015."

Hess also said it is fully exiting its downstream businesses including retail fuel stations, energy marketing and energy trading.

"Once complete, the transformed Hess will have a focused portfolio of higher growth and lower risk E&P assets," Hess said in a March 4 press release.

Hess once had a substantial presence in Alaska.

Its website says that in 1969, Hess Oil & Chemical Corp. merged with Amerada Petroleum Corp. to become Amerada Hess.

"By May the following year the company drills its first successful wildcat well in Prudhoe Bay on Alaska's North Slope," the website says.

In 2003, Amerada Hess completed a sale of its 1.5 percent stake in the trans-Alaska pipeline system to ConocoPhillips.

In 2006, the company changed its name from Amerada Hess to Hess Corp.

The company is perhaps best remembered in Alaska for the so-called Amerada Hess royalty case.

This was an epic legal battle between the state and North Slope oil producers that wrapped up in 1995 and resulted in about $1 billion in total settlements from Arco, BP, Exxon and other companies. The state had accused the companies of undervaluing their oil and gas, thus denying the state the full value of its 12.5 percent royalty share.

The dispute became known as the Amerada Hess case because that was the first company listed alphabetically in the state's lawsuit. Amerada Hess actually was a bit player in the case, settling with the state in 1989 for $319,000.

—WESLEY LOY

An airship for Alaska

IF YOU'RE OUT AND ABOUT IN ALASKA this summer, don't be too surprised if you see a large and colorful airship floating above the muskeg or tundra. Skyship Services Inc. is bringing its Skyship 600 airship, the largest certified non-rigid airship in operation, to the state to demonstrate how a lighter-than-air vehicle of this type could be used for tasks such as aerial prospecting for minerals, geophysical surveys or environmental monitoring, according to a press release from Sen. Lesil McGuire, co-chair of the Alaska Arctic Policy Commission. This type of airship, filled with helium rather than inflammable hydrogen and powered by engines with directional control, can take off and land vertically; can cruise at 40 miles per hour; and can remain airborne for up to 18 hours, the press release said.

And, with an ability to move slowly coupled with no requirement to pitch or roll during operation, an airship can provide a stable observation or survey platform, with no dependence on roads or other means of surface travel.

"Alaska's limited road system … limits the ability to efficiently survey our resource rich lands," McGuire said. "It makes perfect sense for Alaska to have an airship to open up access to opportunities in resource development that will help secure Alaska's financial future."

The Skyship 600, which is 200 feet long and can carry up to 15 people, should arrive in Anchorage around July 4, remaining in Alaska until sometime in September, the press release said.

—ALAN BAILEY

Apparently anticipating considerable public interest, the Alaska Oil and Gas Conservation Commission said March 11 that its April 4 hearing on proposed changes to its fracking regulations has been moved.

AOGCC fracking hearing moved

APPARENTLY ANTICIPATING CONSIDERABLE public interest, the Alaska Oil and Gas Conservation Commission said March 11 that its April 4 hearing on proposed changes to its fracking regulations has been moved.

Originally scheduled for the commission's Anchorage offices, the hearing has been moved to the Hilton Hotel Anchorage at 500 W. Third Avenue, Anchorage.

The hearing will be held from 9 a.m. to noon and may be extended to accommodate those present before 9:30 who did not have an opportunity to comment.

The commission said it proposes to add regulations governing hydraulic fracturing applications, operations and reporting, including requirements for notification of landowners, surface owners and operators within one-quarter mile of the wellbore trajectory; pre and post hydraulic fracturing water well water sampling and analysis; disclosure of the chemical makeup of hydraulic fracturing fluids; wellbore integrity; containment of hydraulic fracturing fluids; casing and cementing; and disclosure of the intent to use a well for hydraulic fracturing on an application for a permit to drill.

The proposed regulations are available at www.aogcc.alaska.gov.

—PETROLEUM NEWS

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DISCHARGE PERMITS

The agencies are imposing certain restrictions on industry discharges. For instance, the proposed permits would prohibit discharges in shallow waters, and in the area of coastal marshes, river deltas, state game refuges, and critical habitat areas such as Kachemak Bay near Homer.

In documents prepared in support of the proposed permits, DEC and the EPA briefly discuss the history of industry activity in Cook Inlet, which is the state's junior, but elder, oil and gas province.

Generally, Cook Inlet's heydays are long past, with oil production peaking in 1970 and its sizeable natural gas reserves fast depleting.

Southcentral Alaska, where much of the state's population lives, depends on Cook Inlet gas as a critical fuel for making electricity and heating homes and businesses.

"The present supply-demand condition for Cook Inlet gas presents a renewed incentive for exploration and development," says a fact sheet prepared in support of the DEC discharge permit. "New gas exploration and development projects are underway and other projects are anticipated in the near future."

The regulators note that two companies, Furie and Buccaneer, have brought jack-up drilling rigs into the inlet. Furie already has drilled two exploratory wells in its Kitchen Lights unit.

Furie and Buccaneer have coverage for exploration-related discharges under a general permit issued by the EPA in 2007. The permit expired in July 2012, but has been extended.

The DEC is taking public comment until March 11. More information is available at www.dec.state.ak.us/water/wwdp/index.htm ●

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LINC ENERGY LTD.

The Australian independent spud the Umiat No. 18 well on a federal lease in the foothills of the Brooks Range some 100 miles west of Pump Station 2 using Kuukpik No. 5 rig.

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LINC UMIAT WELL

allow Linc to meet "key objectives" for the season, according to the company.

The Umiat No. 18 well will be drilled vertically into the Lower Grandstand formation to collect five 60-foot sections and then continued down below the Lower Grandstand "to assess the deeper resource potential," according to the company. After reaching its target depth, Linc plans to plug the well back to the Lower Grandstand to conduct a flow test.

Later in the season, Linc plans to drill the Umiat No. 23H well directionally into the same Lower Grandstand interval to provide "comparative flow testing" for economic purposes.

Linc already has a drilling permit from the U.S. Bureau of Land Management for Umiat 23H, but still needs a permit from the Alaska Oil and Gas Conservation Commission.

"It has been a huge team effort to get this first well spudded and I thank all of my team in Alaska and our contractors for the incredible effort it has taken," Linc Energy CEO Peter Bond said in a statement. "With the first Linc Energy well spudded at Umiat, I am now eagerly awaiting the results from the horizontal well, as that oil flow result will effectively confirm the 50,000-plus barrel per day plan Linc Energy has for the Umiat field."

The contracted program is a continuation of delays Linc experienced last winter, but could be seen as a mere blip when considered against the entire history of the prospect.

Even though the U.S. Navy discovered the Umiat oil field in 1946 and drilled 12 wells altogether in the vicinity, the field has remained undeveloped because of its remoteness and because the reservoir is shallow, partially frozen in permafrost and of low pressure.

With increasing oil prices and improved technologies, a string of independents eyed the prospect in the 2000s, but none of the companies were able to put a drill bit in the ground.

After Linc acquired Umiat from the small independent Renaissance Umiat LLC in mid-2011, it immediately planned a five-well program for the coming winter, but ultimately delayed the entire program by one year because of "logistical and weather issues."

First Umiat well since 1979

Still, Umiat No. 18 is the first well at Umiat since the U.S. Navy drilled the Seabee No. 1 deep test in the region in 1979, and the first exploration well in the National Petroleum Reserve-Alaska since 2009, when Anadarko Petroleum Corp. drilled Wolf Creek No. 4 to the west and ConocoPhillips drilled Pioneer No. 1 and Grandview No. 1 to the north.

The Umiat field is generally believed to have around 1 billion barrels of oil in place.

The consulting firm Ryder Scott Co. LP recently estimated that the field contains reserves of 154.5 million barrels of proved and probable (P2) oil equivalent and 194 million barrels of proved, probable and possible (P3) oil equivalent. For the purposes of the report, "probable" means there is at least a 50 percent chance of the actual recovered volumes meeting or exceeding the P2 estimate, and "possible" means there is at least a 10 percent chance of the actual recovered volumes meeting or exceeding the P3 estimate.

"It's not every day that one is able to tap into a billion barrel oil field and we have now done just that," Scott Broussard, head of Linc's oil and gas division, said. "The next significant milestone will be the results of the flow tests and the evaluation of the deep well. We are all very excited about the first step in a world class oil development." ●

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CHUKCHI PLANNING

Devil's Paw feature is similar in size to the huge Kuparuk River field in the central North Slope, Faust said.

Jack-up rig

Faust said that ConocoPhillips is contracting a brand-new, state-of-the-art jack-up rig from Noble Corp. for the drilling.

"They're building six of them and we're getting one of the rigs fresh out of the yard," Faust said. "We're not going to bring up a 30-year-old piece of equipment. We're bringing up state-of-the art new stuff that is meant to work in the Arctic."

The rig will have the latest features for safety and environmental protection, he said.

A jack-up rig is a floating structure that is towed into position at a drilling site, where tall legs are lowered into the water to the seafloor to lift the rig's drilling platform above the sea surface, thus creating a rigid, fixed structure from which to drill. And because the bulk of the structure is above the water, the drilling operation transmits less sound into the sea than a similar operation in a floating drillship, Faust explained.

The new rig will be extremely strong; it is designed for use in the North Sea where wave heights can be significantly higher than anything seen in the Chukchi Sea, with the drilling platform typically 40 to 60 feet above the water, Faust said. And, while the rig is designed for use in water depths of 400 to 500 feet, the water at the Devil's Paw drilling location will only be about 140 feet deep, he said.

One advantage of using a fixed jack-up platform for the drilling will be the ability to install a strong, heavy-duty steel riser pipe from the seafloor to the platform, rather than the more flexible type of pipe required for a floating drilling structure, Faust said. And that, in turn, enables the placement of the well's blowout preventer on the platform, where it can be accessed easily, rather than in a mud-line well cellar on the seafloor.

As a further line of defense against a well blowout, should the surface blowout preventer fail, ConocoPhillips is placing a well capping device on the seafloor, to close off the well if necessary.

"That cap is in place before we start drilling the well and we drill through that," Faust said.

Accommodating sea ice

The rig is not designed to operate in sea-ice conditions. But, although ConocoPhillips will use the rig at a time of year when sea at the drilling site should be clear of ice, there is the ever-present possibility of an unfavorable wind blowing ice floes into the area of the drilling operation.

To allow for the possibility of a threat from ice encroachment, ConocoPhillips has developed an ice alerts program, using satellite synthetic radar data showing sea-ice images that enable the plotting of sea-ice movements. This type of satellite technology can see through cloud, works in the darkness and images ice very effectively, Faust said.

Ice-alert circles

Essentially, the drilling team will plot three concentric ice-alert circles around the drilling location. Ice management vessels will investigate any ice that enters the outermost circle, about 50 kilometers from the drilling rig. If ice crosses the middle circle, no new drilling operations will start and the rig crew will begin preparations for a possible move from the drilling site. Once ice enters the inner circle, drilling operations will stop, the rig will jack down into the water and support vessels will tow the rig to safety, well away from the ice.

If the jack-up rig has to move off site, the well would be comprehensively sealed at the sea floor and the riser pipe removed, Faust told Petroleum News.

The diameters of the ice-alert circles may vary from day-to-day, and even within a day, depending on the observed speed of ice movement and the nature of the drilling operation being conducted — the longer the anticipated time taken to finish an operation, jack the rig down and tow it from the site, the larger the circles become.

If uninterrupted, the complete drilling of a single well, from rig-up to rig-down, should take about 40 days, 30 days of which would involve the actual drilling operations, Faust said. So, with the Chukchi Sea open water season lasting on average 100 to 120 days, there should be more than enough time to drill one well, with the possibility of a second well, he said.

Heavy-lift vessel

ConocoPhillips will use a heavy-lift vessel to transport the drilling rig from Singapore, hopefully all the way to the Chukchi Sea drilling site, Faust said. However, given the vagaries of the ice conditions, it may be necessary to stage the rig near the coast to the south, with tugs towing the rig into position once the ice has cleared, he said.

According to a Federal Register notice for an application for a marine mammal incidental harassment authorization that ConocoPhillips has submitted to the National Marine Fisheries Service vessels involved in the drilling operation will not arrive at the drill site until July 1 at the earliest, with drilling operations potentially taking place between July and October. A heavy-lift vessel will remove the jack-up rig from the drilling arena at the end of the drilling season, the notice says.

Staging location

The Federal Register notice also says that the location where ConocoPhillips may stage the drilling rig at the beginning of the drilling season, should ice conditions prevent the heavy-lift vessel delivering the rig all the way to the Chukchi Sea drilling site, is six miles offshore the Chukchi Sea coast, about 20 miles south of the village of Kivalina.

This choice of staging area location was based on proximity to infrastructure and the likelihood of ice-free conditions at the time when staging might be required, the notice says.

It became evident during the open water meeting that some Kivalina residents, presumably concerned about potential disturbance to subsistence hunting, are less than enthusiastic about the idea of having a jack-up rig parked near their village.

"We're certainly listening to that and tying that into our plans as much as we can," Faust said, commenting that, depending on ice conditions, one option might be to keep the rig on the heavy-lift vessel, rather than stage it.

Support fleet

ConocoPhillips anticipates needing nine vessels to support the drilling operation, with three vessels providing oil spill response support and the other vessels performing multiple roles, Faust said. Other than when used for shipping supplies, the support vessels will remain within five-an-a-half miles of the drilling rig, he said.

Wainwright will act as a supply base for the operation, with personnel being transferred to and from the offshore by helicopter, and with a landing craft carrying perishable supplies to a supply vessel. After hearing worries about possible noise and disturbance in Wainwright, ConocoPhillips has built a road to an out-of-town helipad and is in discussion with people from the community about appropriate helicopter routes, Faust said. And, to minimize the number of crew changes required, the company is using a drilling rig with large crew quarters, he said.

Faust said that in working with local North Slope communities ConocoPhillips has been addressing concerns and taking advice based on traditional knowledge.

"Over the past four years the plan has changed pretty significantly, in many ways because of the feedback we've gotten in the communities and the kinds of observation that the hunters and whalers have told us about," Faust said. ●

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Drilling some virtual Chukchi Sea wells

As part of its planning for exploration drilling in the Chukchi Sea in 2014, ConocoPhillips has been simulating its drilling project, drilling "virtual wells" during summer open water seasons, Mike Faust, the company's Chukchi Sea exploration project manager, told the National Marine Fisheries Service's annual Arctic Open Water Meeting on March 7. Each summer for the past three years the exploration team has gone through an exercise of drilling wells on paper, using actual weather and ice conditions to envisage how a real drilling operation might have progressed, Faust said.

"We've sat in a room every morning and pretended … we were really drilling the well," Faust said. "So we looked at every operation, every step. We took the ice conditions into effect … we took the weather conditions into effect that day and made operational decisions as if we were really drilling the well."

Lessons learned

The outcome has been a lengthy list of lessons learned that feed into revisions to ConocoPhillips' drilling plans — in the last year alone, the virtual drilling exercise generated about 200 lesson-learned items, Faust said.

One lesson learned from the first virtual drilling season related to the synthetic radar satellite imagery that the company plans to use to track the movement of sea ice, to enable the company to move the drilling rig out of the way of any ice floes that might encroach the drilling area. Subsistence hunters had correctly pointed out that ice can move and change very rapidly, Faust said. And, having realized that it would be necessary to obtain satellite data much more frequently than every three days, the frequency that the company had originally assumed, ConocoPhillips now buys satellite imagery twice a day — during actual drilling operations it may become necessary purchase imagery even more frequently than that, Faust said.

Operations center

Another lesson learned from virtual drilling has been the need for a state-of-the-art operations center, where sea-ice imagery, vessel locations, aircraft locations, personnel deployment data and other information about the drilling project can be displayed real-time in graphic form, Faust said.

"So we've built a really nice operations center across the street from the ConocoPhillips building (in Anchorage), and that will be manned 24/7 when we're out there actually operating," he said.

For this year's virtual drilling exercise ConocoPhillips is involving all of its contractors, to enable the contractors to practice with the company, simulating the anticipated plan for 2014, Faust said. Caryn Rae, manager of the ConocoPhillips environmental studies program for the Chukchi Sea, said that this summer's virtual drilling program will also reach out to the North Slope communities, enabling the practicing of daily reporting, for example.

Rae said the company is still figuring out the specifics of community involvement in the drilling simulation but that the company has been gathering information from the communities about their subsistence hunting activities.

"We will have that information at our disposal as we go through our virtual drill," she said.

—ALAN BAILEY