From: Jim Dodson [mailto:jdodson@investfairbanks.com]
Sent: Monday, August 02, 2010 10:02 AM
To: Jim Dodson; Ali Knabe (ali.knabe@alaska.edu); Andrew Niemiec (andrew_niemiec@dot.state.ak.us); Andrew P. Garrigus P.E. (agarrigus@myeterra.com); Andy Warwick (warwick@gci.net); B.B. Allen (Bill_Allen@commerce.state.ak.us); Bill Satterberg (bill@satterberg.net); Bob Hajdukovich (info@frontierflying.com); Bob Hajdukovich (bob@frontierflying.com); Brian Rogers (chancellor@uaf.edu); hbfate@gci.net; buz@jackovich.com; croberts@ci.fairbanks.ak.us; d_westlake@hotmail.com; Jim Dodson; Gary Wilken (garywilken@me.com); Gene Therriault (genet@gci.net); Jeffry J Cook (jeff.cook@fhr.com); John Binkley (jbinkley@alaska.net); Michael K. Henry; Mike Kelly (representative_mike_kelly@legis.state.ak.us); rwien@florcraft.nu; Tim Beck (tbeck@ptialaska.net); Tim Beck (tbeck@ptialaska.net); Bill Sackinger; Chris Storhok (cstorhok@co.fairbanks.ak.us); Dave Hoffman; DeLaina Storhok; Doug Smith; Frank Abegg; Jim Whitaker (jwhitaker@acsalaska.net); Luke Hopkins (mayor@co.fairbanks.ak.us); Therriault, Gene (GOV); Paul M Park; Paul Martz; Paul Metz (ffpam@uaf.edu); William Sackinger; Amy Cook (acook@carlile.biz); Bob Shefchik; Carol E. Lewis (celewis@alaska.edu); Cynthia Henry (hops@gci.net); Damian Thomas (damian_ak@hotmail.com); Dan Britton (dwbritton@fngas.com); Dan Gavora (dgavora@doyonutilities.com); Jack Hebert (jack@cchrc.org); Jesse VanderZanden (jesse.vanderzanden@alaska.gov); Kathryn Dodge (kdodge@co.fairbanks.ak.us); Luke Hopkins; Matt Want; Steve Lundgren (slundgren@denalistatebank.com); Terry Strle; Tony Johansen; (scott.v.bell@gmail.com); Buzz Otis; Buzz Otis; James M. Collins; Jerry Sadler (AERINC4@alaska.net); Jim Haselberger (jimh@alaskatent.com); Jim Johnsen (johnsenj@doyon.com); Joe Faulhaber (hellojoe02@gmail.com); Paul McCarthy; Paul Robinson; Ralph Seekins; Reinhard Neuhauser; Tim Cerny (tcerny@fdifairbanks.com)
Subject: Gene Therriault response to my distribution of the Alaska Digest article

Please find below Gene Therriault response to my distribution of the Alaska Digest article. Following Gene's response is my reply to Gene (in blue)

Jim

Dear Jim:

On July 12 you e-mailed a copy of a column written by Brad Keithley with the following comment from yourself:

> "I have attached, for your information, an article I copied from the Alaska Dispatch. After reading this article I hope you question, as I do, the focus that some of Alaska's political leaders have on building a gas line for the purpose of

exporting Alaska gas. State gas revenue is not going to replace the revenue the state receives from oil production. Business as usual is not working".

I believe Mr. Keithley's column suffers from a fundamental lack of understanding of the geology, engineering and economics of energy production on the North Slope of Alaska. In order to provide a more complete picture of what the administration is doing to encourage oil and gas development in Alaska, I offer the following information.

Despite the suggestion to the contrary, Governor Parnell is focused on future oil and gas development in Alaska. However unlike oil, North Slope natural gas requires a new pipeline to be constructed in order for the reserves to be commercialized. This infrastructure is critical for development of our gas reserves and for long term production of oil on the North Slope.

Like many world class basins, the North Slope has a large endowment of both oil and natural gas. In basins of this magnitude, production of oil is typically initiated first because it generates a higher rate of return on investment than gas. Over time natural gas becomes a more important economic component of the field as the easiest and least costly oil is produced. Finally, when the gas is monetized, it benefits from the infrastructure investments that have already been amortized and helps to carry a portion of the ongoing operation and maintenance costs of the fields. This sharing of infrastructure lowers the exploration and development risk for additional oil and gas to be produced from the field. This increases the economic value of marginal oil fields and extends the life of existing but declining oil fields. Two examples of this trend are the Gulf of Mexico Shelf and the Western Canadian Sedimentary Basin

The suggestion that Governor Parnell is backing efforts to access our natural gas resources on the North Slope just to fill the state treasury and in doing so has miscalculated the revenue that gas will produce is false. A natural gas pipeline benefits all Alaskans as well as the North Slope producers. In addition to state revenue, the pipeline will provide residents with access to a long term supply of reasonably priced energy as well as employment opportunities. The revenue stream from a large diameter pipeline was modeled three years ago and determined to be significant. Under expected prices scenarios, a North Slope gasline delivering 4.5 BCF of natural gas and natural gas liquids per day is projected to produce an average total annual revenue after tariffs of more than $10 billion for the state, producers, and the federal government to split. The states revenue share alone will be in the billions of dollars per year.

The volumetric component of this operation is critical to keep in mind not only for the potential revenue stream but perhaps more importantly because shipping costs per unit drop significantly as the volume transported goes up. In addition, as gas production increases, it will carry a larger portion of the existing operating costs relieving the economic pressure on remaining oil that exists in harder to produce formations and smaller less economic fields. In order to maximize the economics of a gasline project to the upstream owners (highest wellhead value), the transportation tariffs and processing costs need to be minimized. This is done in large part by maximizing the volume and BTU value of the gas transported which creates very beneficial economies of scale and much lower tariffs.

The beneficiaries of increased gas production and lower transportation costs will not only be the producers and the state treasury. Individual Alaskans will also benefit as the cost of the providing natural gas energy in-state goes down delivering more affordable fuel and a lower cost feed stock for value added processing. Decreasing the cost of transportation and processing through creation of a high volume operation will also lower the barrier to entry for natural gas production from new discoveries and previously discovered but undeveloped fields. If companies know they will be able to get either resource to market, they are more likely to drill wells.

Today, companies put off drilling certain exploration wells if they believe they are more likely to find natural gas than oil. Extending the life of older oil fields and improving the economics for new developments and discoveries including viscous oil means that more oil will flow through TAPS, slowing or reversing oil decline and extending the life of the pipeline. All of this activity will result in trucking jobs, maintenance jobs, exploration jobs and countless other jobs associated with expansion of activity on the North Slope. These are the economics Governor Parnell is striving to achieve by linking our world class natural gas resources to the market. In short, development of natural gas means development of more oil.

It appears that one of the main objectives of Mr. Keithley's piece is to strike at the validity of the ACES oil and gas tax. He mounts this challenge by suggesting that as a result of passing the ACES tax in 2007 ConocoPhillips has now experienced its first summer season in 40 years with no active onshore exploration. What Keithley fails to disclose is that ConocoPhillips did have onshore activity planned for the 2010 summer season; however, this activity was curtailed when the US Army Corps of Engineers failed to issue the necessary permits for a new river crossing of the Colville River. This permit difficulty has been widely reported in the press including the August 1, 2010 Petroleum News which carried the following statement:

> ConocoPhillips next planned step-out from Alpine, the CD5 or Alpine West development, lies in the extreme east of the National Petroleum Reserve-Alaska. This development has been stymied by a refusal by the U.S. Army Corps of

Engineers to allow the construction of a bridge across the Nigliq Channel of the Colville River.

Mr. Keithley also fails to acknowledge that as a net profit tax mechanism coupled with investment credits, ACES taxes less profitable fields at a lower rate and provides incentives for encouraging their development. The article also does not mention the increased tax credits and deductions that Governor Parnell won in legislation he proposed this year (nor the ones he proposed that the Legislature did not approve) that have increased the incentives to invest in new development in Alaska.

Major producers like ConocoPhillips and BP have reported strong profits from their Alaskan operations under the ACES system. For example, in 2009, ConocoPhillip's Alaska activity accounted for 12% of its worldwide production but 29% of its corporate profits. In addition, the August 1, 2010 edition of the Petroleum News recently detailed ConocoPhillip's current year earnings and concluded that "ConocoPhillips' exploration and production activities continue to be more profitable in Alaska than across the Lower 48".

Keithley also makes the assertion that smaller, more nimble oil and gas exploration and production companies do not have the resources, financial, technical or managerial strength to develop projects in Alaska. However, he does not address the success of companies like Pioneer Resources, Armstrong or Anadarko Petroleum in our state.

Finally, the Chukchi and Beaufort Sea portions of the OCS have both proven large oil and gas discoveries and significant potential for world class discoveries. Governor Parnell has been and remains a strong and vocal advocate in Washington DC for increased access to these areas for exploration and development. It was the unfortunate spill in the Gulf that has lead to a deferral of this activity by the Secretary of Interior. This deferral has delayed multibillion dollars of planned investments offshore of the North Slope by Shell and others.

I hope this message provides useful information as you engage in discussions on Alaska's oil and gas future. Having previously worked as a Deputy Director for the Alaska Division of Oil and Gas as well as past employment with ConocoPhillips Alaska, I believe Governor Parnell understands the balance that must be struck to encourage full development of North Slope's potential while protecting the shareholder rights of the Alaska citizens.

Please consider forwarding this message to the distribution list that you sent the Brad Keithley column to. If you would like a clean copy as a word document, please let me know and I will send it to you.

Gene Therriault
Senior Policy Advisor on In-state Energy

Dear Gene and Gary,

The reason I sent out the AD article was to demonstrate that Alaska's natural gas is not going to replace the value, to state government, of Alaska's crude oil production. The simple truth is that natural gas has a dollar value of on a btu equivalent basis of 1/8 or less of that of crude. In other words Gary's old "Bridging the Gap" model does not work. The discussion we are having and the political leaders (McGuire, Ramras and company) I am talking are those that are proposing to build a in-state bullet line from the North Slope to Cook Inlet for the purpose of reducing Anchorage's energy shortage and exporting the balance. That is business as usual and in case you haven't notice, business as usual is not working. I would be more than happy to discuss this in more detail and if I had your distribution list I would include them on my reply.

Jim

Jim Dodson
President & CEO

FAIRBANKS
Economic Development
CORPORATION
907-452-2185
jdodson@investfairbanks.com
www.investfairbanks.com

From: Jim Dodson
Sent: Monday, July 12, 2010 9:15 AM
To: Ali Knabe (ali.knabe@alaska.edu); Andrew Niemiec (andrew_niemiec@dot.state.ak.us); Andrew P. Garrigus P.E. (agarrigus@myeterra.com); Andy Warwick (warwick@gci.net); B.B. Allen (Bill_Allen@commerce.state.ak.us); Bill Satterberg (bill@satterberg.net); Bob Hajdukovich (info@frontierflying.com); Bob Hajdukovich (bob@frontierflying.com); Brian Rogers (chancellor@uaf.edu); hbfate@gci.net; buz@jackovich.com; (croberts@acsalaska.net); d_westlake@hotmail.com; Jim Dodson; Gary Wilken (garywilken@me.com); Gene Therriault (genet@gci.net); Jeffry J Cook (jeff.cook@fhr.com); John Binkley (jbinkley@alaska.net); Michael K. Henry; Mike Kelly (representative_mike_kelly@legis.state.ak.us); rwien@florcraft.nu; Tim Beck (tbeck@ptialaska.net); Tim Beck (tbeck@ptialaska.net); 'Bill Sackinger'; 'Chris Storhok (cstorhok@co.fairbanks.ak.us)'; 'Dave Hoffman'; DeLaina Storhok; 'Doug Smith'; 'Frank Abegg'; Jim Dodson; 'Jim Whitaker (jwhitaker@acsalaska.net)'; 'Luke Hopkins

(mayor@co.fairbanks.ak.us)'; 'Paul M Park'; Paul Martz; 'Paul Metz (ffpam@uaf.edu)'; 'William Sackinger'; 'Amy Cook (acook@carlile.biz)'; 'Bob Shefchik'; 'Carol E. Lewis (celewis@alaska.edu)'; 'Cynthia Henry (hops@gci.net)'; 'Damian Thomas (damian_ak@hotmail.com)'; 'Dan Britton (dwbritton@fngas.com)'; 'Dan Gavora (dgavora@doyonutilities.com)'; 'Jack Hebert (jack@cchrc.org)'; 'Jesse VanderZanden (jesse.vanderzanden@alaska.gov)'; 'Kathryn Dodge (kdodge@co.fairbanks.ak.us)'; 'Luke Hopkins'; 'Matt Want'; 'Steve Lundgren (slundgren@denalistatebank.com)'; 'Terry Strle'; 'Tony Johansen'; (scott.v.bell@gmail.com); 'Buzz Otis'; 'Buzz Otis'; James M. Collins; Jerry Sadler (AERINC4@alaska.net); 'Jim Haselberger (jimh@alaskatent.com)'; Jim Johnsen (johnsenj@doyon.com); Joe Faulhaber (hellojoe02@gmail.com); 'Paul McCarthy'; 'Paul Robinson'; Ralph Seekins; Reinhard Neuhauser; Tim Cerny (tcerny@fdifairbanks.com)
Subject: Document1

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907-452-2185
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