ALASKA STATE LEGISLATURE
JOINT MEETING
HOUSE RESOURCES STANDING COMMITTEE
HOUSE JUDICIARY STANDING COMMITTEE
Anchorage, Alaska
December 1, 2008
2:31 p.m.

MEMBERS PRESENT

HOUSE RESOURCES

Representative Carl Gatto, Co-Chair
Representative Craig Johnson, Co-Chair
Representative Paul Seaton
Representative Peggy Wilson
Representative Scott Kawasaki

HOUSE JUDICIARY

Representative Jay Ramras, Chair
Representative Nancy Dahlstrom, Vice Chair
Representative John Coghill
Representative Bob Lynn
Representative Ralph Samuels
Representative Max Gruenberg

MEMBERS ABSENT

HOUSE RESOURCES

Representative Anna Fairclough
Representative Bob Roses
Representative Bryce Edgmon
Representative David Guttenberg

HOUSE JUDICIARY

Representative Lindsey Holmes

OTHER LEGISLATORS PRESENT

Representative Mike Chenault
Representative Kyle Johansen
Representative-Elect Charisse Millet
Representative-Elect Kathy Muñoz

COMMITTEE CALENDAR

DNR Permitting Process Testimony from Department of Natural Resources, DNR, Division of Oil & Gas, Aurora Power, Escopeta, Exxon Mobil Corp.

PREVIOUS COMMITTEE ACTION

No previous action to record

WITNESS REGISTER

DANNY DAVIS, President
Escopeta Oil Company ("Escopeta")
Houston, Texas
POSITION STATEMENT: Provided comments and answered questions during the presentation on matters pertaining to the DNR permitting process.

BRUCE WEBB, Operator
Web Petroleum Services;
Manager
Land and Regulatory Affairs
Aurora Gas
POSITION STATEMENT: Provided comments and answered questions during the presentation on matters pertaining to the DNR permitting process.

CRAIG HAYMES, Production Manager
ExxonMobil Corporation
Anchorage, Alaska
POSITION STATEMENT: Provided the committees with an update of the Point Thomson project.

JOE CAMPBELL, Senior Drilling Superintendant
ExxonMobil Corporation
(No address provided)
POSITION STATEMENT: During hearing regarding Point Thomson, offered comments.

TOM IRWIN, Commissioner
Department of Natural Resources
Anchorage, Alaska
POSITION STATEMENT: During hearing regarding Point Thomson, provided a prepared statement.

KEVIN BANKS, Director

Division of Oil & Gas
Department of Natural Resources (DNR)
Anchorage, Alaska
POSITION STATEMENT: During discussion of Point Thomson, answered questions.

MARTY RUTHERFORD, Deputy Commissioner
Office of the Commissioner
Department of Natural Resources (DNR)
Anchorage, Alaska
POSITION STATEMENT: During discussion of Point Thomson project, answered questions.

ACTION NARRATIVE

CHAIR JAY RAMRAS called the joint meeting of the House Resources Standing Committee and the House Judiciary Standing Committee to order at 2:31:43 PM. Representatives Seaton, Wilson, Gatto, Johnson, Coghill, Dahlstrom, Samuels, and Ramras were present at the call to order. Representatives Kawasaki, Gruenberg (via teleconference), and Lynn arrived as the meeting was in progress. Also present were Representatives Chenault and Johansen and Representatives-Elect Millet and Muñoz.

Overview(s): Matters pertaining to the DNR permitting process

CHAIR RAMRAS announced the only order of business would be the consideration of matters pertaining to the Department of Natural Resources (DNR) permitting process, with testimony from DNR's Division of Oil & Gas, Aurora Power, Escopeta Oil Company, and ExxonMobil Corporation.

CHAIR RAMRAS expressed his desire that this meeting would result in a better understanding of the relationship between the oil and gas industry, DNR, and the executive branch of Alaska.

2:35:50 PM

DANNY DAVIS, President, Escopeta Oil Company ("Escopeta"), noted that Escopeta has been doing business in Alaska since 1994. He spoke of a large lease block (ph) in the water with a large reservoir that Escopeta could develop, partly with Pacific Energy Resources, LTD (Pacific Energy), and partly on its own.

2:36:17 PM

BRUCE WEBB, Operator, Web Petroleum Services; Manager, Land and Regulatory Affairs, noted that Web Petroleum Services is a contracting company that assists Pacific Energy, Escopeta, and Fox Petroleum, while Aurora Gas is a small, independent gas producer in Cook Inlet. He mentioned his involvement with exploration and production and said he has three off-shore leases. Prior to that, he noted, he worked for the Division of Oil & Gas for 11 years in the Permitting and Compliance Section.

CHAIR RAMRAS asked Mr. Webb to confirm that he did the regulatory work for Escopeta and that Aurora Gas is at the root of a situation involving gas in Fairbanks, "cutting off 400 customers here in Anchorage, and turning them over to ENSTAR [Natural Gas Company]," and "the whole RCA problem that has ensued."

MR. WEBB answered that is correct.

2:37:56 PM

MR. DAVIS mentioned leases, part of which Escopeta shares 50:50 with Pacific Energy, and the other Escopeta owns itself as its Kitchen prospect, which he said Escopeta believes could hold 800 million barrels of oil and approximately 4 trillion cubic feet (tcf) of gas. The only way to know for certain is to drill, he remarked. Corsair and East Kitchen combined have an estimated 300 million barrels of oil and 2-2.5 tcf of gas to be developed. He explained that the structures were found in the mid '60s by Shell, but were never fully developed. In 2006, Mr. Davis said, Escopeta attempted to transport a jack-up rig to the Cook Inlet Basin; however, due to certain circumstances, that plan did not transpire. He related that last year he showed Kevin Banks of the Department of Natural Resources (DNR) how much money Escopeta had expended, and DNR worked with the company to perpetuate what leases it had for another year so that Escopeta could get the aforementioned rig to Cook Inlet.

MR. DAVIS said all the lease blocks "that are now in the water" and owned by Escopeta expire December 31, 2008, as do the lease blocks owned by Pacific Energy. The years of work that has been done thus far have resulted in Escopeta having a rig contract and heavy lift vessel contract and the ability to begin drilling wells in April or May of 2009, depending on when the aforementioned rig can be put in place.

MR. DAVIS said he has been working closely with Pacific Energy in the development of a shared reservoir. A drilling contract was made in Pacific Energy's name with the knowledge that Escopeta would have to "participate in half of it." He said there are some lease blocks in the middle of the acreage shared by Escopeta and Pacific Energy, which Forest Oil Company forgot to include in its unit before Pacific Energy took over. Pacific Energy subsequently requested to have those two leases in "that unit," and that was going to be "our original drill site." The state denied both leases. The case went to appeal, and the appeal has been "sitting there for six months." Mr. Davis indicated that the state required Escopeta and Pacific Energy to sign a contract for a heavy-lift vessel to move the rig in order to participate, and the contract was due November 1. Currently, there is no ruling on the appeal "to put the drill site in, in the middle of our leases," nor has there been a ruling "on the fact the fact that they were going to extend our leases." Mr. Davis said Escopeta has a $150 million commitment to Blake Drilling Company for a three-year drilling contract. He stated, "They wanted us to execute a $10 million contract with heavy lift vessel, but we didn't have any leases to drill on because we knew they were going to expire." He said he has asked the state for a two-year extension "on these blocks" so Escopeta can set up the rig.

MR. DAVIS predicted that upon discovery, in less than 18 months there could be gas flowing into the system, which would enable gas to be supplied in the Cook Inlet Basin. Development of oil would require building larger platforms, which would take extra time. He expressed confidence that the job can be done, and reiterated that Escopeta is staged to do it but remains in limbo because it cannot deliver to its partners who will drill the projects unless it knows where it stands. Mr. Davis stated that that is why he petitioned the state and Mr. Banks for an extension on the leases. He said it is confusing to be asked to sign a $10 million contract to bring a rig to Alaska without first having leases and a drill site. He said if the company could drill, an estimated 100,000 barrels a day of oil could be added to the Cook Inlet Basin, along with enough cubic feet of gas to take care of the homes in need.

2:43:30 PM

MR. DAVIS emphasized that Escopeta is not asking for money or a handout, just an opportunity.

CHAIR RAMRAS reminded members of the joint committee that currently the market in Alaska is only able to bring 25 percent of its oil out of the Cook Inlet at tide water, is bringing about 50 percent of its oil from Valdez, and is importing the other 25 percent of its oil from around the world; therefore, the ability to make significant discoveries flowing through the Cook Inlet would not only be a boon for the state treasury, but also for consumers statewide.

MR. DAVIS recollected that in the '60s, about 250,000 barrels a day were being moved in Cook Inlet.

CHAIR RAMRAS offered his understanding the amount was approximately 200,000 barrels a day, and now it is below 10,000 barrels a day.

MR. DAVIS said, "I truly believe we can make a difference to that. We just need the opportunity, and we're going to pay for the opportunity."

2:46:28 PM

MR. DAVIS, in response to Co-Chair Gatto, explained the steps that were taken during a seven-year period, including contracting with a jack-up rig, hiring a heavy-lift vessel to move it, a trip to Washington related to the Jones Act waiver, and losing the rig to a much more lucrative contract. With Pacific Energy's help, a new contract was executed with Blake Drilling Company and with a heavy-lift vessel. The contract only becomes valid if the leases are extended, a provision that Escopeta wrote into the contract to protect itself from a $10 million liability if the leases are not extended. Mr. Davis said there are partners willing to work with Escopeta on these projects; the company does not have the $50 million it will take to move the rig to Alaska and drill the wells. He offered to provide the necessary information to prove the funds are there and from where they are coming. The seven-year period, he said, is "the term of the oil and gas lease you sign with the State of Alaska."

MR. DAVIS, in response to a follow-up question from Co-Chair Gatto, assured him that there would not be a repeat situation wherein the rig ended up being transported somewhere else again. He said the reason is that the money has been paid and the Blake 151 hails from Louisiana and Texas and "they're not going anywhere else."

2:50:05 PM

MR. DAVIS, in response to a question from Representative Coghill, said Escopeta has asked for an extension only on its own leases. If Forest Oil Corporation is not granted an extension, he relayed, Escopeta will still be able to drill its prospects, even though the two companies share the same reservoir. In further response, Mr. Davis explained that when Escopeta knew the rig was not going to move, the company wrote to Secretary Churdal (ph), letting him know Escopeta had been put on hold, and that the company would notify him when it was ready to move. Mr. Davis said he notified the secretary two weeks ago that Escopeta would probably be "moving" next April and asked him to make known any problems with the plan. He said so far, Escopeta has not heard back. He concluded, "As far as I know, we're still in business."

2:52:01 PM

REPRESENTATIVE SAMUELS stated his assumption that DNR is going to want a commitment from Escopeta that if the lease is extended, the company would actually perform or pay a penalty.

MR. DAVIS answered, "That's the way it was written last year." He explained that Escopeta has not yet discussed the issue of a penalty. In response to Representative Samuels, he clarified that he meant a penalty related to an extension.

2:53:01 PM

REPRESENTATIVE GRUENBERG recollected that Mr. Davis had stated that the lease blocks had been forgotten to be included. He asked how that happened.

MR. DAVIS reiterated the information regarding the failed leases and pending appeal. To a follow-up question, he suggested Representative Gruenberg had probably misunderstood regarding lease blocks being forgotten. He said the chair of Pacific Energy discovered that the lease was going to expire and got Mr. Webb to petition the State of Alaska to see if it would reinstate those leases into the Corsair unit. He specified that they would be the southern-most leases in that unit.

REPRESENTATIVE GRUENBERG asked Mr. Davis if the state provided him with a written opinion or decision denying those leases, and if so, what did it say?

MR. DAVIS said the state did not provide anything to him, because the request was made by Pacific Energy. He deferred to Mr. Webb.

2:55:12 PM

MR. WEBB noted that he had provided to the committees the Corsair Unit extension appeal document.

CHAIR RAMRAS noted that it is in the committee packet.

2:57:05 PM

REPRESENTATIVE SEATON recalled that Mr. Davis had said that gas could be available fairly quickly, but that oil production takes longer. He asked if there are separate reservoirs or if the Alaska Oil & Gas Conservation Commission (AOGCC) has to determine whether gas can be "blown off" before the oil is recovered.

2:57:46 PM

MR. DAVIS responded that there are two separate reservoirs. He said it is believed that oil reservoirs, which start at about 13,000 feet, continue down to 18,000 feet. He mentioned a presentation made to AOGCC, which addressed the issue of satellite platforms used to develop gas reserves at a quicker rate, and he suggested Mr. Webb could provide the information from that presentation.

REPRESENTATIVE SEATON said he wants to know that there is agreement that the gas could be taken off rather than be held for enhanced oil recovery or anything like that.

MR. WEBB shared his understanding that there was not any such agreement. He said the presentation basically focused on single casson (ph) drilling platforms, and he stated his belief that it is generally acknowledged that the different reservoirs are separate and distinct and can be managed separately. He said he has not heard plans for enhanced oil recovery, although he said he assumes that would be water injection and gas.

MR. DAVIS, in response to a request, reiterated Escopeta's projected timeline.

3:00:33 PM

CHAIR RAMRAS asked Mr. Webb if he thinks DNR is more interested in getting lease bonuses and payments or in developing oil and gas prospects in the Cook Inlet.

MR. WEBB opined that DNR is more interested in lease bonuses and payments. He said the denial of the Corsair expansion made no sense and was not in the best interest of the state, Cook Inlet consumers, the company, or anyone. He said it seemed like DNR wished to warehouse the leases rather than let a willing and ready company explore the area.

3:01:33 PM

CHAIR RAMRAS referred to a letter to Governor Palin from Escopeta Oil, in which Mr. Davis wrote that if the governor decides to continue her work in Alaska, Escopeta and Pacific Energy, as well as others, could use her help in rebuilding the oil and gas industry in the Cook Inlet Basin to meet the need of all Americans. He asked Mr. Davis to expound on that idea.

3:02:22 PM

MR. DAVIS stated that the decisions that Commissioner Tom Irwin and Kevin Banks make will affect the future of the oil and gas industry. He expressed frustration with America's dependence on the Middle East and said Alaska has the ability to help the rest of the United States get back on its feet. In response to a follow-up question, he emphasized the necessity of getting help from DNR to make the drilling possible.

3:05:17 PM

MR. WEBB, in response to Representative Wilson, said the timeframe for a reconsideration is 30 days, while an appeal to the commissioner has no timeline.

3:06:26 PM

REPRESENTATIVE COGHILL said he wants to know if DNR is acting in Alaska's best interest or if "the combination of those two leases somehow creates a conundrum for us."

MR. DAVIS responded that Forest Oil Corporation no longer exists here; Pacific Energy owns the leases "to the north of us." He reviewed what has been done thus far in conjunction with those leases. He said other companies would also use the rig once it is moved up to Alaska, and the rig would be in Alaska for three

or four years. In response to a follow-up question, he said Pacific Energy inherited their leases from Forest Oil Corporation about a year and a half ago.

MR. WEBB noted it was August 2007.

MR. DAVIS, in response to a question regarding expansion, indicated that the leases in question hold the most oil and gas of any, and for some unknown reason, Forest Oil Corporation failed to include those leases in its Corsair Unit.

REPRESENTATIVE COGHILL recollected having heard some discussion about "them losing that and then having to go out to an open market bidding on that particular set."

MR. DAVIS replied that in about 30 days, the companies involved stand to lose everything. In response to Representative Coghill, he recalled that the prime lease area expired in May, but an extension was requested in order to "put it back into the unit" and "move that rig up there and drill that location." The lease area totals 11,364 acres. Mr. Davis said when he was asked to sign a contract for $10 million without a drilling lease, it made him feel like "the Wizard of Oz told me to go get the broomstick of the Wicked Witch of the West." Escopeta got the contract to the state in time, he added.

REPRESENTATIVE COGHILL said he appreciates Mr. Davis' tenacity, but he explained he is trying to figure out the legal conundrum in which the state might have put itself because of laws it has put in place or the policies that DNR must follow.

MR. DAVIS stated, "If these leases don't get extended and we're not going to have any legal action, I'll just go back to Texas and drill wells there." He explained that he is not here to fight the state, but rather to work with it to rebuild the industry.

REPRESENTATIVE COGHILL said he would like to overlay Mr. Davis' ideas onto regulatory code.

MR. DAVIS suggested that the rule to follow is a common sense one of asking whether something is right or not.

3:12:58 PM

MR. WEBB, regarding the timeline, said Forest Oil Corporation formed the Corsair Unit and included four leases, and it did so

under the geologic information it had. When Pacific Energy bought Forest Oil Corporation in 2007, it began cooperating with Escopeta, sharing seismic information and redefining the reservoir. That, he said, is when Pacific Energy saw that there were two leases "that were actually in common with the entire reservoir." He said Pacific Energy did not become the operator of the Corsair Unit until mid-November of 2007. What Pacific Energy inherited from Forest Oil Corporation, he said, was a drilling commitment to drill a well 34 days after becoming the operator, which is why the company applied for an expansion and an extension simultaneously. He said there is no legal conflict between the two; "the two companies, if they wanted to, could form one unit over the entire reservoir and then do an equalization of interest."

REPRESENTATIVE COGHILL surmised that the inheritance of the commitment to drill by the new partners could not be performed within the given timeline.

MR. WEBB answered that is correct. He said it was Pacific Energy's assumption that the state, in the past, had granted extensions to unit operating agreements, and that [getting an extension] would not be difficult if Pacific Energy could prove it could responsibly develop and meet future commitments, which it has done. He said Pacific Energy has "cured" a couple of default notices and has complied so far with every stipulation that DNR has given. He said, "As far as Pacific is concerned, they're ready to go except for losing those expansion acreages."

3:15:30 PM

MR. DAVIS shared an anecdote to illustrate how history repeats itself, concluding with an invitation to ExxonMobil Corporation to come help drill the Cook Inlet Basin. In response to Co-Chair Gatto, Mr. Davis said he thinks neither Mr. Banks nor Commissioner Irwin have been restrictive, but it is time to do something before the gas runs out, and Escopeta is ready for action.

3:19:20 PM

MR. WEBB noted that in December 1993, the Rowan Drilling Gilbert Road drilling rig left Cook Inlet, and for 15 years there has been no jack-up rig in the Cook Inlet. During those 15 years, he said, not one single major oil and gas company has bid on an offshore lease, yet every lease sale for 50 years has had bonus bids and lease payments made by individuals and independents.

He defined "offshore" as [a rig] that is not adjacent to land that can be reached "directionally" or adjacent to an existing platform that can be reached "directionally." He said, "And what that basically has been is nothing more than a charitable contribution to the state, because there's absolutely no way that you can develop an offshore lease without a jack-up drilling rig." Today, he emphasized, there are rising taxes, declining revenues, higher utility costs, and fiscal uncertainty, and there are two companies in Alaska, poised to drill, who keep meeting with resistance and onerous requirements. He said those companies are not asking for special consideration, "they just want some of the road blocks lowered a little bit so that they can drill."

The committee took an at-ease from 3:21:11 PM to 3:25:44 PM.

3:26:38 PM

CRAIG HAYMES, Production Manager, ExxonMobil Corporation, began by reminding the committee that ExxonMobil Corporation (ExxonMobil) has been working on the Point Thomson project for over a year. Mr. Haymes then introduced the project team members and some of the key contractors that were present. He highlighted that ExxonMobil has assembled a leadership team that has experience of 160 years between six individuals.

3:29:10 PM

MR. HAYMES turned the committee's attention to the PowerPoint entitled "Point Thomson Project - Progress Update," which shows a photograph of some of the first barges to arrive on the site in 2007. He informed the committee that over 150 people have been working on this project for quite some time and with the receipt of some permits will ramp up to over 200 people within the next three months. In fact, ExxonMobil will be ready to drill by February 2009. Mr. Haymes informed the committee that ExxonMobil has already spent and committed $125 million and no drilling has occurred. The initial phase of $1.3 billion will result in $250 million per year in expenditures. He mentioned that this project is a world class project that requires world class people and expertise, much of which can be provided by Alaska's contracting community. Point Thomson, he reminded the committees, contains 25 percent of the known gas resources on the North Slope. The gas of Point Thomson will be essential to the success of the gas pipeline. "It's in everybody's interest to drill, it's in everybody's interest to move forward with the development; it can only help all of us," he stated. He then

turned attention to slide 2 of the presentation, which illustrates that Point Thomson is about 60 miles east of Prudhoe Bay, which is a remote and environmentally sensitive area adjacent to the Arctic National Wildlife Refuge (ANWR) and 22 miles east of the nearest development, Badami. Point Thomson's reservoir is 12,000 feet beneath the surface and straddles the coast line. The pressure for Point Thomson is 10,200 pounds per square inch, which is over twice that elsewhere on the North Slope.

MR. HAYMES moved on to slide 3 entitled "Point Thomson - Initial Development Phase," which relates that production is targeted for the end of 2014 and the project is on schedule to meet that schedule. The base plan is to produce 10,000 barrels per day of condensate through two wells, drill three wells in oil, and tie in successful oil wells. He related that the facilities will be designed to the full development scenario of an export pipeline, which will be capable of 70,000 barrels per day of liquids and the gas pipeline will be built at a later date. He highlighted that this facility will have process facilities, liquids pipeline, an airstrip, and a camp. The facility is being designed such that it can be expanded rapidly.

3:32:59 PM

MR. HAYMES turned the committee's attention to the slide entitled "Point Thomson Project - Clear & Committed Timeline," which illustrates that ExxonMobil has moved forward on this project despite being in dispute with the state. For example, ExxonMobil has worked on its drilling permits, has secured a rig to which it has done significant upgrades, ordered long-lead time equipment, started engineering design, and procured materials. He pointed out that the activities go all the way to production by 2014, and therefore ExxonMobil and the 26 other owners have been doing everything on the critical path.

3:34:00 PM

REPRESENTATIVE WILSON asked if when Mr. Haymes refers to "production" whether he is speaking of oil or gas production.

MR. HAYMES answered both. The initial phase, he explained, will delineate and develop the oil, gas, and condensate. He said that ExxonMobil knows it can obtain a minimum of 10,000 barrels per day through the facility. The facility design, he reiterated, is being developed for more than the aforementioned minimum. The hope, he related, is that the oil wells will be

successful and can be tied in to produce the oil as well. How much will be produced is always a question.

REPRESENTATIVE WILSON inquired as to what ExxonMobil will do if it arrives at 2014 and there's no gas pipeline.

MR. HAYMES explained that at this phase, the gas will be cycled through the facilities and reinjected back into the ground. The resource is being conserved, which is important because every molecule of gas that leaves the reservoir results in the loss of condensate. Mr. Haymes clarified, "So, we're putting all of the gas back into the ground, saving that for eventually when there is a gas sales development.

REPRESENTATIVE WILSON related her understanding that the aforementioned is no different than what anyone else is currently doing.

MR. HAYMES noted his agreement, adding that the gas will be used to enhance liquids recovery.

3:35:54 PM

CHAIR GATTO recalled past discussion about development of Point Thomson and the oil rim. At that time, not much was known nor is much known about the oil rim, which means there is discussion about developing oil without knowing what there is. Therefore, he asked if ExxonMobil assumes that oil is available in quantities that are appropriate, or is there still a question as to how much oil is there and how long it will take to start exporting molecules of gas. He related his understanding from the AOGCC that a lot of oil won't be left behind just to draw down the gas well.

MR. HAYMES said ExxonMobil knows there is oil and gas present [at Point Thomson]. Furthermore, ExxonMobil has knowledge that there is more gas than oil. He explained that oil is heavy so that it sits at the bottom of the reservoir and the reservoir quality degrades the deeper one goes. Since the oil is heavy, it doesn't flow as easily and it's thin relative to the amount of gas. The oil sits between water and gas. Therefore, when the oil flows, water and gas will also flow because the gas in the water flows more easily than the oil. In doing the aforementioned, water and gas are being produced. The facility ExxonMobil is constructing can handle the aforementioned, the water and the gas as well as the reinjection of the gas into the reservoir. Three of the five wells that ExxonMobil will drill

target oil. Mr. Haymes related that the targets are at the extreme of the reservoir to prove-up and determine the productivity of the oil. Eventually, he explained, when the oil wells are depleted, they become gas wells. Therefore, these wells have dual utility. Mr. Haymes informed the committee that each well costs in excess of $100 million. In comparison, the Prudhoe Bay well costs $6-$8 million, which means that over 15 Prudhoe Bay wells amount to one of these wells. The aforementioned illustrates that when a well is drilled, the desire is to do so that they can be used.

3:38:52 PM

MR. HAYMES then moved on to slide 5 entitled "Point Thomson Project - Nabors 27E Drill Rig Upgrade," which relates that ExxonMobil has done $20 million in rig upgrades and Nabors is spending money on top of that for additional upgrades. The [rig upgrades] have been going on since March of 2008. He informed the committee that when the rig is complete it will have 1 million pounds of pulling strength, which means that it will be in the top 25 percent of the most powerful land rigs in the US. He further informed the committee that the mud system has to be overhauled and three mud pumps built to pump 1,600 gallons per unit of mud. This will be the heaviest drilling mud in the world, and therefore it poses some fairly significant challenges. Because such large pumps are necessary, a new mud pump module must be built. The module was built by Aurora [Gas LLC] in Anchorage. Also, the engines have had to be overhauled because of the need for more power. The derrick is being rebuilt and the draw works are being replaced. The aforementioned work is on schedule, and therefore the rig will be recommissioned by December 2008/January 2009 and will be ready to be mobilized to Point Thomson in February. He then turned the committee's attention to slide 6 entitled "Wells Required for High-Pressure Operations," which shows a photo of a typical wellhead that will be used at Point Thomson. He reviewed the details of the size and shape of the wellhead.

MR. HAYMES highlighted that this field is located in an environmentally sensitive area, a significant traffic area for whaling. He informed the committee that all of ExxonMobil's wells will be drilled from onshore, which means the wells will be long-reach wells under high pressure. Therefore, a lot of planning and due diligence is necessary to successfully drill such wells. ExxonMobil, he related, has significant expertise in high pressure drilling. In fact, every well ExxonMobil has drilled in Point Thomson has been successful. Moving on to

slide 7 entitled “Point Thomson Project - Site Activity,” which shows a photo of the site and highlights specific areas. ExxonMobil has laid out a plan specifying where the barge would land and where there would be an ice road. He noted that the ice road will be built from both the Endicott Causeway and Point Thomson. New tanks, camp facilities, etcetera are being installed. The intent was to do as much as could be done in the summer so that when the ice road is built and the rig is mobilized, drilling can begin. The aforementioned, he said, has been successfully accomplished by ExxonMobil.

3:44:49 PM

REPRESENTATIVE SAMUELS inquired as to how much of the aforementioned work was done since November 2006.

MR. HAYMES [referring to slide 7], said "All of this work, here, has been done this year and summer.” He mentioned that last year a lot of survey work and site visits were performed. This year, the bulk of the work was on-site activity.

3:45:30 PM

REPRESENTATIVE WILSON inquired as to how many successful wells ExxonMobil has drilled in Point Thomson.

MR. HAYMES recalled that of the 19 exploration wells drilled at Point Thomson, ExxonMobil, as an operator, has drilled 13 of those all of which were successful. However, two wells weren’t successful due to unique pressure issues.

MR. HAYMES, regarding permits, turned the committee’s attention to slide 8 entitled “Point Thomson Project - Permits.” He informed the committee that after the planning for the summer work, ExxonMobil applied for and received five permits, all of which were approved. Of the five permits, one permit was from DNR to provide access to operate on land to perform gravel work to set conductors at subsurface levels. ExxonMobil also received a permit from the Alaska Department of Fish & Game (ADF&G) to withdraw water from fish bearing lakes. ExxonMobil also received a permit from the North Slope Borough to conduct operations under their land management regulations. Furthermore, ExxonMobil received a conflict avoidance agreement from the Alaska Whaling Commission such that ExxonMobil agreed to shut down its barging operations so as not to interfere with subsistence activities. ExxonMobil also received a US Fish & Wildlife permit for the incidental taking of wildlife, if

necessary for the protection of human safety. Mr. Haymes relayed that ExxonMobil has been working collaboratively with all the permitting agencies. Slide 9 entitled "Point Thomson Project - Barge Route," shows the barge route utilized to move all the equipment to Point Thomson this summer. The barging route, he noted, was modified in consultation with the Alaska Eskimo Whaling Commission in order to avoid interference with whaling operations. The route is about 60 miles, which amounts to about 12 hours. During the summer, there were about 15-20 barge runs. At the request of the Alaska Eskimo Whaling Commission, ExxonMobil shut down on August 20th for three weeks. Mr. Haymes opined that ExxonMobil has worked positively with [Native] Alaska villagers and will continue to do so. He then highlighted slide 10, which is a photo of some of the first barges to arrive at the site while slide 11 shows photos of various equipment that has been offloaded from the barges. Furthermore, in accordance with the approved permits 700 tons of material and equipment has been delivered to the site. He then turned to slide 12, which highlights the gravel work performed at the site. In fact, ExxonMobil has constructed a helicopter landing site, including a camp facility that would allow people to stay overnight, a fuel tank farm utilized for winter drilling, as well as two well pad areas. He specified that the gravel pad is a 10 acre site. As slide 11 relates, ExxonMobil has drilled two well conductors down to 120 feet where they are cemented into the location. Mr. Haymes explained that a conductor is a large piece of pipe that is about three feet in diameter and offers a safe wall allowing a drill rig to drill. Drilling can't begin until the conductor is in place, otherwise the drilling mud would be invasive. Mr. Haymes relayed, "We have started drilling."

3:51:00 PM

REPRESENTATIVE SAMUELS asked if a specific permit is necessary to drill the well conductors.

MR. HAYMES answered yes, explaining that ExxonMobil needed approval of the land use permit, which specifically stated that it would install conductors and sellers on site. Therefore, all the work has been done in accordance with state laws, regulations, and approved permits. Installation of the first two wells was as much as could be accomplished this summer. He then informed the committee that the ice road requires knowledge of the water depth, and crews completed water depth surveys, bathymetry surveys, this September. Slide 15, he pointed out, is a recent overhead photo of the site. He then showed the

committees a short video clip of the Point Thomson project site in which he pointed out various aspects of significance. He emphasized the remoteness of the area.

3:53:41 PM

MR. HAYMES then directed the committees' attention to slide 17, which provides a list of contributing companies. There were over 40 Alaskan contractors that helped with this project. As mentioned earlier, over 150 people have worked at the site. He mentioned some of the contractors that aren't on the list, and said that every day the list of contributing companies/contractors grows. Slide 18 illustrates the 50-mile ice road along the coast line to Point Thomson. The ice road, he related, will employ 30-40 people for months to build it and maintain it. Slide 19 offers details regarding the construction of an ice road, which includes the construction of a mile-long runway that must be able to withstand the landing of large aircraft such as Hercules C-133 with a 155,000 pound payload. The ice road, he related will require 50 tons of equipment to build it. Furthermore, 51 million gallons of water will be used in the construction of the ice road. He explained that an ice road is built by drilling into the ocean, flooding, and letting it freeze. The aforementioned is done until the desired thickness is achieved. Since some of the modules that will travel on the ice road are 1 million pounds, the ice road will have to be a minimum of five feet thick or touching bottom. Mr. Haymes informed the committees that the ice road can't be built today because of the weather. As soon as the ice depth in the ocean is two feet deep, road construction can begin. Therefore, within two weeks, ExxonMobil will be waiting on permits [for the ice road].

3:56:08 PM

MR. HAYMES, moving on to slide 20 entitled "Point Thomson Project - Permits," pointed out 22 permits are necessary to build the ice road and drill. Of those 22 permits, 16 are in hand or on their way and 6 are of concern. He said that two permits are being denied, one of which is a land use permit and the other is the plan of operations. There are four other permits for which ExxonMobil doesn't know the status, including a temporary water use permit from DNR, a consistency review from DNR, a geophysical permit from DNR, and drilling permits from the AOGCC. The land use permit and temporary water use permit are necessary, otherwise the ice road can't be built. After construction of the ice road, permits for the plan of

operations, consistency review, geophysical, and drilling are necessary to actually drill. With regard to correspondence that ExxonMobil didn't want to build the ice road to do site remediation, Mr. Haymes said that's incorrect. The plan is to build the ice road to drill and perform site remediation. In fact, ExxonMobil has been working on site remediation with AOGCC since June of 2007 on 10 wells. Furthermore, funding is in place to do so. The intent is to build the ice road to drill, but also use that infrastructure to perform other work. A number of companies have called Exxon to ask to use the ice road and ExxonMobil has been working in confidence on commercial arrangements to do so. Mr. Haymes opined that it's in everybody's interest to drill.

3:58:31 PM

MR. HAYMES, referring to slide 21, highlighted that once this project is complete Point Thomson will be the world's highest pressure gas cycling project. The project is in its initial phase of development. Mr. Haymes pointed out that there are 27 owners at Point Thomson who have already spent $800 million plus $125 million. This phase will cost another $1.2 billion on top of that.

3:59:12 PM

REPRESENTATIVE SAMUELS inquired as to the cost per mile of the ice road.

MR. HAYMES responded that although the information is proprietary, it amounts to $10s and $10s of millions.

REPRESENTATIVE SAMUELS inquired as to what happens to all the information, body of work, the $800 million has purchased.

MR. HAYMES answered that the information is proprietary, and therefore would stay with the owners. However, he related that all of the data is being shared with the AOGCC through a confidentiality agreement, which has been the case since August of last year. The aforementioned has been done because "we" believe it's important to move forward with development of this field. Furthermore, [ExxonMobil] recognizes that the AOGCC will need to help ExxonMobil make decisions with regard to future development and offtakes for the field.

REPRESENTATIVE SAMUELS questioned, "Why would [ExxonMobil] spend the money and why would [the AOGCC] issue even one permit, if

they ... want to take the leases back and ... go to court and decide." He questioned why the parties are at the table today arguing over this project.

MR. HAYMES related that in the past there have been questions in terms of whether ExxonMobil can be trusted to execute this plan of development. In fact, from 1977-2005, there were 21 plans of development at Point Thomson, each of which was approved by DNR in consultation with the owners. At different times ExxonMobil has reviewed large scale cycles, large scale gas sales, but each time it has come together and agreed upon the next steps, and modified the plan of development accordingly. There have been surprises, or rather new information that has caused a change in course. He pointed out that change in course has been in consultation with DNR. The owners are all committed to develop Point Thomson, and furthermore it's in the best interest of everyone to move forward. ExxonMobil has kept the project schedule alive so that construction can begin by 2014. Mr. Haymes said, "We believe we can resolve the dispute. We are currently in good faith settlement discussions with the DNR; we're hopeful we can resolve this issue. I can't talk about those settlement discussions, they're confidential." He then related that ExxonMobil looks forward to working with the state to move forward with the development of Point Thomson, the gas pipeline, and any other resource that partners may wish to join ExxonMobil.

4:04:16 PM

JOE CAMPBELL, Senior Drilling Superintendant, ExxonMobil Corporation, began by informing the committee that on December 6 he will have been with ExxonMobil for 28 years and has worked in Alaska in 1981 and 1982. In response to Chair Ramras, Mr. Campbell recommended that the state proceed with the drilling. He explained that there is a 120-man camp at Point Thomson, of which part of it is for the construction and maintenance of the ice road. Mr. Campbell pointed out that he is the site supervisor and thus he would have some authority over those staff working in construction. He estimated that there would be a staff of 100-120 at a time and other staff would come out at various times. In response to Chair Ramras, Mr. Campbell confirmed that many of the staff would be Alaskans, trained in the state.

4:06:40 PM

CO-CHAIR JOHNSON asked if ExxonMobil, in its 21 plans to date, has ever been as far along as it is in this particular plan of development.

MR. HAYMES answered that it has never been as far along in a plan of development for Point Thomson as it is today. Not only is engineering work being done, ExxonMobil is two-and-a-half months away from starting development wells. ExxonMobil has never drilled a development well at Point Thomson, which means that although they will be capable of producing in the future, they're typically not set up for development.

CO-CHAIR JOHNSON surmised then that 21 times ExxonMobil has had a plan of development that was less developed than this plan of development and those were approved.

MR. HAYMES replied yes.

4:07:59 PM

REPRESENTATIVE SEATON, regarding leases and termination of leases, recalled that if a well is capable of production, the leases are extended, which cancels the termination of the unit. He asked if that's correct. He restated, "Is Exxon wanting to have a well so then they extend the leases and ... cancel the termination and DNR has made the determination to cancel these leases and cancel the unit. And if they permit you to drill a well, then you have legal rights to maintain the ownership for an extended period of time, whether you produce or not."

MR. HAYMES pointed out that there are different categories of leases. For example, under current regulations a lease can be retained for a certified well or a well capable of producing in payable quantities. ExxonMobil is interested in developing the resource, not leases, he clarified. The Point Thomson resource spans a number of leases, and therefore it wouldn't be prudent for ExxonMobil to focus on developing a lease. ExxonMobil, he relayed, is focused on the leases that link together to develop the resource. The resource under the ground doesn't follow lease boundaries. This plan is focused on the development of the resource, the heart of the reservoir for gas cycling, gas, and condensate while developing the flank of the oil to learn as much as possible. The aforementioned sets the stage for full field development for oil, cycling, gas or a combination of those. This plan of development, he said, is based on objective technical work from many owners. ExxonMobil, he reiterated, is focused on bringing the resource to production.

REPRESENTATIVE SEATON inquired as to unit termination. He posed a scenario in which there's a well capable of production at payable quantities, and asked if that would cancel the termination of the unit such that the entire unit is maintained.

MR. HAYMES specified that a unit holds a group of leases together. At this point, ExxonMobil is in court over whether there is a unit or not. The leases can be held through different means. He informed the committee that leases don't expire for 90 days after the unit was terminated. If there's a drilling operation underway on those leases, then those leases can be retained in accordance with regulations and lease conditions.

REPRESENTATIVE SEATON posed a scenario in which some leases in the center of the unit were held under those terms and the state succeeded in having the unit terminated and took other leases back. In such a scenario, how would the state be able to proceed with resale/reissuance of the unit or bid, he asked.

MR. HAYMES deferred to DNR. He then offered that if various owners own various leases that straddle the same resource, then that group of owners will have to come together to form a new unit and gather new information. After the litigation, which he estimated would take a decade plus, it would take another five years for the owners to create another unit. Therefore, it would be about 15 years before the point of starting is reached. Therefore, the result is a "real mixture," such that the current owners, even if there was litigation that was successful in terminating the unit, would still exist in the future unit.

4:13:37 PM

MR. CAMPBELL, in response to questions from Chair Ramras, confirmed that he has been to Point Thomson and the well conductors are in place and he is in place. Mr. Campbell offered that he has been working on modifying the rig to handle these wells and be prepared to drill.

REPRESENTATIVE SAMUELS asked if ExxonMobil owns any leases in the Beaufort [Sea].

MR. HAYMES answered not to his knowledge.

The committee took an at-ease from 4:15:30 PM to 4:15:53 PM.

4:17:02 PM

TOM IRWIN, Commissioner, Department of Natural Resources, began by noting that he wouldn't say much about the Kitchen, Corsair, or Pearl units because of court activity. With regard to Point Thomson, Commissioner Irwin read the following statement:

> The subject of today's hearing is how the Department of Natural Resources manages state oil and gas leases. Because of my role in resolving appeals filed by companies who have challenged the department's decisions, my comments today must be limited. I'm here to be respectful .... I want to explain the background for that decision. As you are all aware, the companies that once held leases to the land in the Point Thomson area have sued the state, challenging Commissioner Minge's 2006 decision to terminate the Point Thomson unit. The existence of that unit allowed the companies to hold on to leases beyond their primary term. Many of the leases in this area were acquired in the 1960s and had 10-year primary terms. Once the unit terminated, the leases, because they were beyond the primary term and not in production, expired. Thus, Director Banks ruled that 31 leases expired after the unit was terminated. And as required by our regulations, the Division of Oil & Gas sent lease termination notices. The former leaseholders appealed the director's decision to me this fall and that appeal is now pending. On January 12, 2009, the hearing will begin. The companies will have the opportunity to present factual evidence and make legal arguments challenging the lease determination decisions. Because I have the responsibility to hear the evidence and make a fair decision based on that record, I cannot testify today about the validity of the leases. That is an issue that I will resolve after hearing from the companies and looking carefully through the evidence they file. The director of the Division of Oil and Gas, Kevin Banks, is available to talk about the notices of termination he signed on August 4, 2008. Thirteen of the leases in this area terminated earlier. Under a 2001 agreement, DNR allowed ExxonMobil to expand the Point Thomson unit in exchange for their commitment to begin development. ExxonMobil gave DNR an unambiguous commitment to drill a well in 2003 and to begin development drilling by 2006 and have seven wells

producing by 2008. The expansion agreement also provided that ... if the drilling activities did not occur, the leases would be returned to the state without dispute, and ExxonMobil would pay a penalty of $20 million. None of the promised wells were drilled; the $20 million payment was made in the summer of 2007, but the leases were not returned. ExxonMobil has appealed my decision terminating those leases to superior court, where an appeal is pending.

There are several other legal actions pending. ExxonMobil has sued the state claiming damages based on funds they claim they spent trying to develop the Point Thomson unit. They sued after the unit was first terminated, the judge dismissed the case, and they appealed to the Supreme Court. Because of the pending litigation, the Supreme Court has stayed its consideration of this appeal. ExxonMobil sued again for damages after the April 2008 terminating the unit; the case has been consolidated with the appeal of the unit decision before Judge Gleason. Their brief is due at the end of January. They also filed a claim for damages before the Department of Administration that is pending before an administrative law judge. ExxonMobil has also filed legal actions at the AOGCC. In an attempt to circumvent DNR's decision to terminate the Point Thomson unit, they have asked the AOGCC to compulsory unitize leases that Director Banks has terminated. DNR has filed a motion to dismiss this unitization application. ExxonMobil has also applied for a drilling permit from the AOGCC and Chairman Seamount recently asked DNR and ExxonMobil whether a permit should be issued over the land owner's objections. I also have pending before me a request to reconsider three permit denials by the Department of Natural Resources. In addition to the ice road permit, DNR denied applications for plans of operations and for seismic activity on these lands earlier this year. I've been asked to reconsider those decisions and will issue my decisions after reviewing the agency record and allowing the appellants the opportunity to tell me why the decisions to deny the permits were wrong and provide any additional evidence they believe I should consider. As with the lease appeals, because I have the responsibility to make decisions in those cases, I

cannot comment further on those today. Respectfully, if there are questions ask Director Kevin Banks.

4:24:29 PM

REPRESENTATIVE SAMUELS, regarding [Escopeta Oil Company, LLC] ("Escopeta"), posed a scenario in which there was no litigation and the leases under discussion end on December 31, 2008. In such a situation, he inquired as to how long it would take to organize and release those leases.

KEVIN BANKS, Director, Division of Oil & Gas, Department of Natural Resources (DNR), said that under the scenario posed by Representative Samuels, those leases could be released in the next lease sale for the Cook Inlet, which would be in May [2009].

4:25:22 PM

REPRESENTATIVE SAMUELS asked if the price of oil would come into play when talking about whether or not to extend a lease. He then asked whether the lawyers make the decisions or the engineers and lawyers.

MR. BANKS answered that those decisions are made by DNR's resource evaluation staff and commercial staff, which includes geologists, geophysicists, and engineers. In the particular case with Escopeta, Mr. Banks explained that Escopeta was awarded the leases nine years ago. As a condition of forming the Kitchen unit around these 19 leases, Escopeta promised to drill a well in the Kitchen unit by the end of 2007. When Escopeta failed to meet the aforementioned drilling commitment, DNR placed the unit in default in order to provide the department more control in the next step in the process. A condition of the default specified that if Escopeta could drill a well by the end of 2008, it could proceed to the next step and keep the unit. He highlighted that Danny Davis is requesting that if [Escopeta] doesn't drill a well in two years from now that it will return the leases. Mr. Banks submitted that that's where the process is today and Mr. Davis has been unsuccessful in acquiring a rig. The aforementioned becomes mixed with the Corsair unit because of the relationship Mr. Davis is trying to foster between his investors and his firm and the investors of the Pacific Energy Firm. Mr. Banks opined that [the division] is faced with trying to make a decision based on the performance of the applicant and its capability to perform. Mr. Davis admitted that he was unsuccessful in getting a jack-up rig in

the later end of the seven-year term of the leases. At the 11th hour, Mr. Davis requested that a unit be formed in the Kitchen unit. The [division's] finding for that unit specified that the geological information submitted to the division was insufficient to define a unit. Mr. Banks reminded the committee that the process the division usually follows in awarding a unit is that a firm acquires a land position through a lease sale, the leases are drilled and delineated and form a unit in order to have the necessary land position to take care of the correlative rights of others that may own land in the same area. At that point, the firm can proceed to development.

4:29:57 PM

MR. BANKS related that in this case, geological information didn't indicate that there was a strong resource capability although the division was told that a jack-up rig would be brought in. On that promise, the division decided it would be in the state's interest to award the unit in the first place. Two years later, no drilling rig has been brought to the unit and the division is faced with the decision to default and as of December the unit will be terminated as will the leases.

4:30:44 PM

MR. BANKS then turned discussion to the Corsair unit. The Corsair unit formed at basically the same time as the Kitchen unit by Forest Oil Corporation. The Corsair unit included four leases. The justification of drilling on those four leases was based on geology that centered on those leases. After a year, Pearl took over the unit and the impending commitment for drilling. Mr. Banks opined that the division worked hard with Pacific Energy to establish deadlines for when a jack-up rig contract and a heavy-lift vessel would be required. After several of those interim milestones slipped, Pacific Energy requested an expansion of the unity. The division was faced with the decision as to whether to grant an expansion in a situation in which the applicant had performed no work and had missed several milestones. The division decided that the aforementioned wasn't in the best interest of the state because the acreage identified in the initial unitization process was found to be sufficient to support bringing in a drilling rig. The division believes that Pearl acknowledged that point through the process, and therefore the division decided not to expand the Crosair unit. If entities don't perform, he explained, the division has very limited options as to what it can make those

entities do. The leasing process is clear that leases must be offered competitively.

4:34:03 PM

CHAIR RAMRAS pointed out that if the division succeeds in the objectives before it; there won't be a jack-up rig and no drilling in the Cook Inlet, no construction of an ice road, or development of the Point Thomson unit.

MR. BANKS clarified that for Point Thomson the division isn't at the point Chair Ramras has described. For the Cook Inlet, Mr. Banks submitted that there isn't a jack-up rig on its way. The company doesn't have the funds to do so; Pacific Energy is on the verge of bankruptcy.

4:35:37 PM

MARTY RUTHERFORD, Deputy Commissioner, Office of the Commissioner, Department of Natural Resources (DNR), clarified that the department doesn't have a standing decision, as the Corsair unit is under appeal to the commissioner.

CHAIR RAMRAS surmised then that Mr. Davis lied to the committee about having a jack-up rig.

MR. BANKS explained that the only jack-up rig that's being offered is one by Pacific Energy. The contract for the heavy-lift vessel and the rig itself is Pacific Energy's contract.

CHAIR RAMRAS inquired as to the milestones that DNR is trying to accomplish at Point Thomson and Cook Inlet.

COMMISSIONER IRWIN said that he can't answer that question.

CO-CHAIR JOHNSON asked whether it can still be said that Alaska is open for business. He pointed out that Mr. Davis has offered to show [the committees] his financials that indicate there is the financing for the jack-up rig. Co-Chair Johnson opined that a year from now when his constituents have absorbed a 17 percent increase in gas prices, those constituents are going to be concerned with why they don't have gas and why they're paying more. He then highlighted that there has been testimony that in 12 months, the natural gas problems can be alleviated and shortly after that can prevent the importation of 25 percent of the state's gas. Co-Chair Johnson inquired as to who is in the queue that can get the job done quicker.

4:39:51 PM

MS. RUTHERFORD confirmed that the state is very much open for business. She then reminded the committees of the liquefied natural gas (LNG) export license, which this administration has supported as it moved through approval of a two-year extension. In the process, ConocoPhillips Alaska, Inc. and Marathon Oil provided commitments to drill additional wells in order to provide greater availability of gas for utilities as well as LNG export. Those two companies exceeded their commitments and made their LNG export facility available for third parties so that there is a market and an incentive for new investment in this state. Additionally, DNR is not sure that if a two-year extension was given to these units that there would be a drilling rig. In fact, there may be a two-year delay, she pointed out. Therefore, there's no certainty that there will be a delay but rather there's the hope that the timeline will be moved forward so that another entity can take the opportunities provided by the acreage.

4:41:59 PM

CO-CHAIR JOHNSON related his understanding that other oil companies, as part of the export license, agreed to drill additional wells.

MS. RUTHERFORD responded that ConocoPhillips Alaska, Inc. and Marathon Oil Company are drilling additional wells in response to the state's requirement for support in the LNG export license. That gas is to be made available primarily to the utilities as well as for their own LNG export facilities.

MR. BANKS, in further response to Co-Chair Johnson, informed the committees that ConocoPhillips Alaska, Inc. drilled wells in the Beluga River unit and is in the process of drilling a well off the tionic platform in the North Cook Inlet unit. Marathon Oil is drilling in the Kenai on Nikiski. Mr. Banks explained that the tionic wells are being drilled from existing tionic platforms. With regard to who is in the queue, Mr. Banks informed the committees that Armstrong [Cook Inlet, LLC] (Armstrong) is drilling at North Fork. Armstrong came forward with a rig contract that the division requested in an interim milestone for their unit applications and plans of development. When Armstrong realized it couldn't get the rig across the road at Anchor Point because of weight restrictions, the division could deal with such issues as long as there is some commitment

of funds. Mr. Banks said that a contract that says there is no contract unless DNR does certain things, including extending the term of lands that are onshore in order to get a jack-up rig suggests there's not a contract.

MS. RUTHERFORD added that the way the legislature structured the entire leasing and plan of development program is to ensure that the companies holding the land position are making commitments for exploration and development. As companies are held responsible for the commitments they've made and negotiated with the state, it's about getting drilling. When commitments aren't honored, the department has to be a good land manager and recognize that sometimes the competition provides for a greater opportunity for that exploration and development.

4:45:55 PM

COMMISSIONER IRWIN characterized Co-Chair Johnson's question as really important, noting that DNR has been asked if it is a proponent of development. Commissioner Irwin reviewed the work and commitment of various companies and the significant work being done in this state. Therefore, Commissioner Irwin emphasized that the department is a proponent of development.

4:47:21 PM

CO-CHAIR GATTO suggested that the department feels like an apartment landlord who faces a renter who wants a lease but when asked for the money says that he/she is expecting some money some time in the future. In such a case, would the landlord deny the renter the opportunity to rent an apartment, he asked.

MR. BANKS answered that the aforementioned is a fair characterization, adding that the state should think of itself as landlords. He then reminded the committees that the department awards "apartments" in a competitive bidding process. The lease has an obligation to develop and produce from that lease. If the department decides to extend leases rather than offer them in competitive lease sales, it would seem that the department is offering a lottery ticket to come to the state and negotiate a better deal. The aforementioned can't be right, he opined, as it's not fair to those who compete in the lease sale process.

4:49:42 PM

CO-CHAIR GATTO, regarding the jack-up rig, pointed out that Alaska is a fairly remote location and he would be nervous about sending it to Alaska in the hope it would work. He inquired as to the condition of the rig, the likelihood that rig would be destined to come to Alaska, and questioned whether it is more of a wish.

MR. BANKS related that although Blake 151 is currently under an obligation to ExxonMobil, with a certain amount of notice Blake 151 can give the rig to someone else. Therefore, ExxonMobil has a rig on hand that's potentially an interruptible service. On the other hand, Blake 151 has an option for others. He related that the Blake can drill in water depths up to 150 feet, is suitable for functioning in the Cook Inlet in the summer months when there is no ice. The commitment to bring it up to mobilize it and demobilize it is on the customer's nickel.

4:52:43 PM

REPRESENTATIVE WILSON posed a scenario in which "all this" is denied and the process stops until the lease sales, and then asked can the process be expedited.

MR. BANKS replied no, specifying that the dates set for the lease sales are set in the five-year plan and are updated yearly.

REPRESENTATIVE WILSON asked if the lease sales schedule is set in regulation or statute. She also asked whether there would be a reason to change that schedule.

MR. BANKS answered that the five-year plan is set ahead of time per statute. The actual lease sale date is schedule because there are notice requirements. Mr. Banks added that the aforementioned was a response to a fairly hypothetical question and that whether the department receives full and complete title to those leases on December 31 is another question.

REPRESENTATIVE WILSON inquired as to whether it would be possible to move the schedule up one month, for example.

MR. BANKS offered to review that possibility, and added that there is some possibility to move the schedule.

4:55:26 PM

REPRESENTATIVE SAMUELS pointed out that DNR keeps issuing permits to ExxonMobil. He asked, “Is there a legal reason for this particular permit that you’re protecting the lease with this particular permit?”

MR. BANKS pointed out that the ice road permit is one of others that DNR has denied. He agreed that having heard ExxonMobil speak, it would seem the situation is one of “Alice in Wonderland.” He then opined that DNR didn't permit anyone to place conductors in the pad. There are land use permits that have been granted in situations in which a lease hold right isn’t required to have the ability to move about on the North Slope. He highlighted that DNR has denied the ice road and ExxonMobil’s plan of operation. The later brings into question the Alaska Coastal Zone Management Plan permits that go along [with the plan of operation]. Mr. Banks said, “If a permit requires a leasehold right, in other words want to drill on our land, that would not be allowed.”

4:57:18 PM

MS. RUTHERFORD clarified that the distinction is general use permits and permits that require a leasehold interest. The previously issued permits are general use permits. Those permits being denied are ones requiring [ExxonMobil] have a leasehold position.

REPRESENTATIVE SAMUELS recalled that hearing during the Alaska Gasline Inducement Act (AGIA) that Point Thomson isn’t necessary to have the gas pipeline. He opined that the argument that someone is going to risk $40 billion to build a gas pipeline without having Point Thomson available is a silly argument. He further opined that everyone should recognize the need for Point Thomson gas. He then inquired as to how far the terms of the lease can [be changed]. He asked if it’s possible to propose that all the litigation be dropped if all the leaseholders placed their gas in TransCanada’s pipeline. Representative Samuels said, “You want Exxon, and Chevron, and BP, and all of the rest of them to put that gas into that AGIA pipeline; and that’s the new leverage point that’s going on right there.” He further asked whether that’s the “end-game” in this situation.

5:00:39 PM

MS. RUTHERFORD noted that the attorney general has been provided a tremendous amount of authority with regard to settling disputes. Currently, DNR is involved in court ordered

settlement discussions with the previous leaseholders. She recalled that in a public filing at least one of the leaseholders indicated that talking about a particular gas pipeline wasn't something with which they were comfortable.

5:01:51 PM

MR. BANKS pointed out that when people are knowledgeable of one's plans, the leverage can evaporate.

CO-CHAIR JOHNSON asked if there is any linkage in granting an extension in Cook Inlet as it might set a precedence that isn't desirable at Point Thomson.

MR. BANKS confirmed that there is no linkage. The department wants to treat every lessee fairly and consistently. He remarked that concerns regarding the state's behavior in the Cook Inlet haven't entered his mind in regard to the impact it may have with regard to the state's dispute with ExxonMobil.

CO-CHAIR JOHNSON posed a scenario in which the department granted a lease extension in Cook Inlet, and asked if it could jeopardize the potential settlement or retraction of leases with ExxonMobil. He further asked if such a scenario would set a precedent that the state may have to live with for an extended period of time.

MR. BANKS highlighted that the department has already extended, through unitization, the lease terms for both Pacific Energy and Escopeta. The department has done similar things for ExxonMobil through 21 plans of development (PODs) over the last 30 years at Point Thomson. There comes a time, he said, when the state has to say no. Mr. Banks opined, "It's easy to approve a plan of development; it's hard not to." Furthermore, it's difficult to exercise the leverage or the rights incorporated in awarding a plan of development because this sort of discussion will always occur in the public arena. Therefore, pressure is put on the department to make decisions that may not, in the long run, be good for the state because the state would lose control of how its lands are developed.

5:05:36 PM

REPRESENTATIVE SEATON, returning to the North Fork unit, recalled that the requirement for Gas-Pro Alaska was to drill a second well or the unit would run out. The aforementioned forced the sale [of the unit] to Armstrong, with a short

extension with the promise to drill once a rig could be brought onsite. If Gas-Pro Alaska requested [and was granted] an extension for a couple of years for the North Fork unit, would the drilling and production have taken place or would the unit have remained in a holding pattern.

MR. BANKS pointed out that Gas-Pro Alaska was in fairly difficult straights to pull together the drilling program to which Armstrong eventually committed. Although Armstrong had a bit more time, it wasn't a lot more time. He related his belief that Armstrong was still within the window to move forward on the promises of Gas-Pro Alaska. Mr. Banks opined that had the leases been extended to Gas-Pro Alaska, it's likely that the state could have had no activity in the North Fork unit. He then reminded the committees that the state had experience with Armstrong, an aggressive and well-funded company, in the Cook Inlet as well as on the North Slope. Armstrong organized the land position, the exploration wells, and activities that ultimately led to Oooguruk and Nakaitchuq oil fields now under development by others.

5:10:17 PM

REPRESENTATIVE DAHLSTROM asked Mr. Davis if in his earlier testimony he was lying.

MR. DAVIS answered, "No, I wasn't lying." Mr. Davis noted that he has never shared with Mr. Banks, who has never asked, who his partners will be. He offered to share that information when the "time comes." However, he said at this point Escopeta has no leases to drill. Mr. Davis said:

> To rebuild an industry, sometimes you need a helping hand. I'm not asking for a helping hand, I'm asking for an opportunity. He's right, my leases expired. I think I'd like to be treated like Exxon. I've got one plan of development, they've had 21; so, I guess I got 10-20 years to go before I need to give my leases back.

MR. DAVIS opined that it's hard to get the funds together to come to Alaska. He acknowledged that Armstrong is more well financed that Escopeta. Mr. Davis then opined that ExxonMobil should be allowed to drill Point Thomson.

REPRESENTATIVE DAHLSTROM asked if Mr. Davis is able and willing to have a face-to-face discussion with Mr. Banks regarding confidential information.

MR. DAVIS replied yes. In response to Co-Chair Johnson, Mr. Davis said that he would be able to share letters and such.

5:13:15 PM

REPRESENTATIVE GRUENBERG related his understanding of Commissioner Irwin's previous testimony that there's no statutory, regulatory, or policy setting forth a time for the decision once the appeal has been submitted.

COMMISSIONER IRWIN said that's correct.

REPRESENTATIVE GRUENBERG then pointed out that under statutes at the trial and appellate court level, the judiciary has six months after a matter is submitted within which it must render a decision or the judiciary isn't paid. Furthermore, each time the judiciary is paid he/she must sign an affidavit specifying that there are no pending motions or other matters for longer than six months. Representative Gruenberg inquired as to Commissioner Irwin's thoughts regarding such a statutory requirement for [DNR].

COMMISSIONER IRWIN opined that such a change could have unintended consequences. The department, he related, works very hard with the companies to try to make something work out. However, if the legislature determines a specific date is necessary, the department will make the decision.

REPRESENTATIVE GRUENBERG inquired as to whether the appeal regarding the failure to extend leases is de novo, a new hearing, or is the appeal on the record.

COMMISSIONER IRWIN asked if Representative Gruenberg is referring to Point Thomson specifically or all leases in general.

REPRESENTATIVE GRUENBERG clarified that he was referring to "the other matter."

COMMISSIONER IRWIN explained that he reviews all the data and takes testimony upon appeal. Ultimately, the decision is his, he said.

REPRESENTATIVE GRUENBERG surmised then that it's discretionary and can be done on the record or via a de novo appeal. He asked if people can request the presentation of additional evidence.

COMMISSIONER IRWIN said that is correct.

REPRESENTATIVE GRUENBERG related his understanding that the times Mr. Banks provided regarding when leases would be available were the appeal to be denied are subject to the possibility that a stay may be granted. He asked if that's correct.

MR. BANKS said he wouldn't place a tract of land with a clouded title into a lease sale. It wouldn't be good to offer up a lease if there was a stay on the department's actions to terminate the leases in some form or another. "The value of that tract of land would be blemished by the proceedings before it," he pointed out.

REPRESENTATIVE GRUENBERG posed a scenario in which an appeal was filed, but no stay was sought or a stay was sought but denied. He asked if the tract would be offered for a lease nonetheless or would that be considered a cloud on the title.

MR. BANKS, drawing from his own experience, recalled that with leases that had not been formally terminated, but were well past the termination date, the [department] has [had difficulties] with other lessees in which the previous lessee and the current award winner both sue the state. In regard to earlier testimony, Mr. Banks clarified that he had not called Mr. Davis a liar, but merely specified that Mr. Davis is not on the contracts for the vessel or the jack-up rig. Therefore, Mr. Davis's financial picture isn't of issue in the particular scenario. At the moment, Pacific Energy has the commitment to bring up the jack-up rig.

5:19:49 PM

CHAIR RAMRAS inquired as to the milestones for DNR in the next 12 months, regarding Escopeta and Point Thomson and the ability to move forward to build an ice road.

5:20:29 PM

MR. BANKS answered that he is fairly reluctant to specify the path the state should take with regard to Point Thomson as these are very intense negotiations with all of the owners. Regarding

Escopeta, Mr. Banks said that Escopeta was given a December 31st date. In the two years Escopeta [has held the lease] no well has been drilled, and therefore it's time to do something. He opined that the [decision] with regard to Escopeta will be forthcoming soon.

CHAIR RAMRAS asked whether Mr. Banks appreciated how difficult it is for Alaskans to reconcile DNR's point of view with the philosophy exposed by the governor.

MR. BANKS pointed out that Chair Ramras' comments are based on the premise that if a decision was made to extend the leases for Escopeta to accommodate Pacific Energy that a well would be drilled. Mr. Banks said that he isn't convinced the aforementioned will happen.

5:22:30 PM

MS. RUTHERFORD added that the same could be said for the Point Thomson leases. As mentioned earlier, there were absolute commitments on drilling and development from the previous leaseholders at Point Thomson. However, many of those commitments were reneged upon. Therefore, she opined that the department is trying to ensure that development will occur throughout state land. At some point, one must look to the past to determine the future. If entities haven't honored their commitments, then other operators have to be considered as possible drillers to ensure the development of all the state's resources.

CHAIR RAMRAS remarked, "From my point of view, you're wrecking my state ... and it hurts .... From Flint Hills to Healy clean coal to Point Thomson to the Cook Inlet, government just doesn't seem to have any answers. And it just drives me nuts."

5:24:02 PM

MR. DAVIS began by mentioning that the package he has wasn't entirely submitted to the committees because there is a confidentiality agreement with Mr. Banks. The [idea] that the contract with the heavy lift vessel is made to Escopeta Oil Company and Pacific Energy Alaska and was executed by both entities and submitted to the state is wrong. The drilling contract is between Pacific Energy Alaska, as the operator, and Blake Offshore. The rig will work in about 300 feet of water, not 150 feet of water. Furthermore, Escopeta is not a party to this contract, but Escopeta does have a rig sharing agreement

with Pacific Energy Alaska that makes [Escopeta] half responsible for the use of this rig when it arrives. The aforementioned has also been submitted to Mr. Banks. Mr. Davis opined that Mr. Banks hasn't went through the paperwork he has been sent. He said he would provide this information to the committees.

CHAIR RAMRAS again expressed exasperation with the government's inability to [move forward with resource development] and said that the public is also exasperated. Chair Ramras highlighted that the throughput in the Trans-Alaska Pipeline System (TAPS) is declining by 6 percent per year while the state budget is growing by 15 percent a year, which doesn't make for a happy picture going forward.

5:28:18 PM

MR. HAYMES acknowledged Chair Ramras' frustration, and related the desire to move to production with Point Thomson. Mr. Haymes then read from the July 7 DNR permit that was issued to ExxonMobil pertaining to conductors, as follows: "The permit was approved based on this attached document titled 'Point Thomson Drilling Program, Equipment Staging and Pad Preparation Project Description June 11, 2008." He read from the second paragraph on page 1, as follows:

> The proposed work includes facilitating removal of equipment currently stored on the pad by another operator, placement of ice road construction equipment, a 30-man construction camp, fuel storage tanks, and fuel associated with ice road construction and for use in other operations, and maintenance and site preparation of the existing pad. The maintenance and site preparation work will include grading, placing gravel from the Prudhoe Bay area and installation of cellars (ph) and conductors. Following site preparation work a small staff may be maintained on site for maintenance and security until ice road construction personnel mobilize to the Point Thomson 3 gravel pit area ... in November or December.

5:30:23 PM

REPRESENTATIVE SAMUELS asked if that language comes from the state permit.

MR. HAYMES clarified that ExxonMobil submitted a Point Thomson drilling program, site staging description, which was approved with the permit approval.

REPRESENTATIVE SAMUELS surmised then that the conductors are included in the plan for which ExxonMobil obtained a permit.

MR. HAYMES replied yes.

CHAIR RAMRAS related the following from an article by Dermott Cole (ph) titled "State will struggle with new financial realities created by falling oil prices." The aforementioned article says: "Just as the nation will struggle to adapt to new economic realities, so will the state. Facing lower oil prices and declining North Slope oil production, now about one-third of what it was two decades ago; it takes more than chanting 'Drill baby drill.' to address this problem."

REPRESENTATIVE SAMUELS related his understanding from the earlier testimony of Mr. Banks and Ms. Rutherford that ExxonMobil didn't have permits for the subsurface conductors.

MR. BANKS explained that was the permit from which Mr. Haymes read. It was a general use permit issued by the Division of Mining, Land, and Water. The permit would have been issued to any entity that had to perform remediation work or work on the pad that would've been required upon the termination of a lease. Regarding the language about conductors, it wasn't part of the permit he saw as it was issued by another division.

REPRESENTATIVE SAMUELS related his understanding then that the state gave ExxonMobil a permit to build a staging area for equipment and fuel to build an ice road. ExxonMobil spent money to do so. The state also gave ExxonMobil a permit for subsurface conductors, although testimony today related that ExxonMobil wasn't given such a permit. He questioned why the one permit was denied.

MS. RUTHERFORD clarified that the permit was a general use permit for surface activity. Although the permit may have made a reference to conductors, it doesn't mean that the Division of Mining, Land, and Water understood [the conductors] would be used as a subsurface device. General use permits, she explained, are issued to entities that don't have to have land use control of the oil and gas properties prior to issuance. The division has been very aggressive about not denying general

use permits as well as denying permits for the Point Thomson area, since the state is in litigation over that unit.

REPRESENTATIVE SAMUELS said that he understands giving leverage, but this is an “Alice in Wonderland” situation. "If this state does not get a gas pipeline, we are all so screwed. This economy is so screwed," he stressed.

5:36:08 PM

CO-CHAIR JOHNSON opined that the state has permitted drilling in so much as there is 125 feet of pipe in the ground to prevent mud from coming up at Point Thomson.

MS. RUTHERFORD relayed that she was recently in a conversation with Mr. Haymes, who clearly stated ExxonMobil wouldn’t do any drilling not permitted by DNR. She then opined that ExxonMobil doesn't perceive that as drilling and they truly understand that it is a general use permit and that ExxonMobil’s leases in the unit have defaulted. ExxonMobil, she pointed out, is trying to settle the matter as it is in good faith negotiations with the state. Ms. Rutherford emphasized that [DNR] issues many types of permits to entities without any land use rights; the permit under discussion is one such permit. “A word buried at the end of a document as an attachment will not change the dynamic of the litigation,” she stated. Ms. Rutherford opined that it’s extremely unfortunate that 25 years after the last activity at Point Thomson, the [state] doesn't know whether Point Thomson is an oil field that should be developed for 20 years prior to gas development or a gas field in which the gas can go into the pipeline at the initial open season.

5:37:53 PM

CO-CHAIR GATTO related that a conductor is a piece of wire that takes electricity from point A to be bled off at point B. If the division gives a permit that allows for someone to operate a conductor, is [the term conductor] defined or is the rationale that it means something different to the division than to Point Thomson, he asked.

MS. RUTHERFORD said that she hasn’t seen the attachment, and therefore doesn't know if [conductor] is a defined term. She said she guessed that [conductor] isn’t a defined term.

REPRESENTATIVE SEATON said he wanted to be sure that Alaskans don’t have the impression that there is no activity taking

place. He then highlighted that on the Lower Kenai Peninsula, Cosmopolitan has scheduled 20 wells and a rail system to extend three miles underneath Cook Inlet to develop an oil field. The exploratory wells have been drilled and now [Cosmopolitan] is moving into the production drilling phase. He also reminded members that Armstrong has drilled a second well at the North Fork field. He then expressed the hope for more drilling in the future.

CHAIR RAMRAS remarked, “Representative Seaton, just like the constituents I serve, you have communities that have no gas. We should be awash in gas. It’s just inexcusable.”

5:41:11 PM

REPRESENTATIVE GRUENBERG recalled earlier testimony from Mr. Banks in which he said that "Pacific Energy was close to bankruptcy." He further recalled Mr. Banks’ testimony relating that the department is unsure whether the project would ever be built or the drilling take place if the permit was given to Pacific Energy, Escopeta Oil, et cetera. If the condition of Pacific Energy is crucial to the decision, Representative Gruenberg requested discussion with regard to the financial status of Pacific Energy and how that is impacting DNR’s decision in the Escopeta Oil and Pacific Energy matter.

MR. BANKS informed the committees that Pacific Energy is a publicly traded company in the Canadian Stock Exchange. Pacific Energy is reporting that a $430 million loan has been converted from a long-term to a current debt. Pacific Energy has admitted that its debt to revenue ratio is fairly steep. Pacific Energy’s September 30th quarterly report indicates these are issues that need to be sorted out before moving forward. In fact, one of Pacific Energy’s employees describes the company as externally financed, a company with a small revenue stream from a few of its leases in Cook Inlet and properties in Southern California. Mr. Banks opined that Pacific Energy is out of balance in terms of carrying the kind of debt they have.

5:44:23 PM

MR. DAVIS responded that he finds it amazing that Pacific Energy is the only company in the US that’s in trouble. He highlighted some of the large companies in the US that are going broke. Mr. Davis then related that he is going to call Vladimir Kadik (ph) in the morning to determine if he will farm out the Corsair project, if the appeal and leases are approved. Therefore,

everything would be put under Escopeta and be unitized and drill. If [Pacific Energy] then goes into bankruptcy, it wouldn't impact any of the operations on the leases as [Pacific Energy] would retain overriding royalties. The aforementioned can be done, he stressed.

5:45:48 PM

MR. HAYMES clarified that the comment he read before was located on page 1 of the plan in the second main paragraph. He then pointed out that he wasn't aware that the ice road ExxonMobil is proposing to construct is on any of the leases currently under dispute. The ice road goes from the Endicott Causeway along the ocean and then arrives at the Point Thomson site.

MR. DAVIS shared that in Texas when one owns the land, sometimes people own the surface and the minerals underneath. He then inquired as to the ownership in Alaska and questioned where the surface stops and the minerals start. If ExxonMobil has drilled 160 feet deep and set conductors, it's considered drilling in Texas, he related.

5:47:55 PM

CHAIR RAMRAS commented that the upcoming legislature has interesting tasks before it.

5:49:00 PM

ADJOURNMENT

There being no further business before the committees, the joint meeting of the House Resources Standing Committee and House Judiciary Standing Committee was adjourned at 5:49:12 PM.