

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL AND GAS

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**Interim Decision of the Director of the Division of Oil and Gas
Application for Formation of the Polaris Participating Area**

This interim decision concerns the formation and appropriate size of the Polaris Participating Area.

On December 22, 2000, BP Exploration (Alaska) Inc., on behalf of itself and Phillips Alaska Inc., ExxonMobil Corporation, and Forest Oil Company (collectively referred to herein as “the Applicant”), submitted to the Department of Natural Resources, Division of Oil and Gas (“the Division”) an incomplete application for approval of the formation of the Polaris Participating Area (Polaris PA) within the Prudhoe Bay Unit. The Applicant requested that the Polaris PA be limited to the sands within the Mc, N, and O intervals of the Schrader Bluff Formation in the vicinity of S and M Pads.

On January 19, 2001, Chevron USA Production Company objected to the incomplete application, claiming that the sands within the Mc, N, and O intervals of the Schrader Bluff Formation in the vicinity of W Pad also should be included in the Polaris PA. The Applicant subsequently completed its application, then, on April 2, 2001, both the Applicant and Chevron submitted additional data and written arguments to the Division. On May 4, 2001, the Division conducted a hearing on the application during which the Division asked questions of the Applicant’s and Chevron’s geologists, geophysicists, petrophysicists, engineers, managers, and commercial personnel. Additionally, at hearing Chevron posed questions for the Applicant’s personnel; the Applicant declined to question Chevron personnel.

Because of the complex and technical nature of the dispute, a final decision may not be ready for issuance for several months. However, the parties to the dispute have expressed interest in a rapid decision to facilitate immediate development of the area at issue. Moreover, the Applicant’s authority to produce certain wells at S-Pad and W-Pad expires May 21, 2001, unless a participating area is approved prior to that date (or tract operations are extended). Thus, as an accommodation to the parties, the Division issues this interim decision, which provides for formation of the Polaris PA, effective on one of three dates: May 1, 2001, June 1, 2001, or the first of the month following issuance of a final decision. BP, as unit operator, may choose any one of these three effective dates; however, if BP does not notify the Division of its preferred effective date within thirty days of the date of this interim decision, the effective date will be the first of the month following issuance of the final decision.

The crux of the dispute revolves around whether the S and M Pad areas, or “Northern Area,” and the adjacent W Pad area, or “Southern Area,” are part of the same reservoir. Chevron argues that the Schrader Bluff Formation sands in the Northern and Southern Areas constitute a single continuous multi-layered

reservoir with localized compartmentalization in some but not all zones, and therefore, as a single reservoir, should be included in a single participating area. The Applicant argues that the Schrader Bluff Formation sands in the Northern and Southern Areas constitute multiple reservoirs separated by one or more impermeable faults, and that the Division cannot require the combination of multiple reservoirs into a single participating area over the objection of the Applicant. In fact, at hearing the Applicant claimed that the Northern Area consisted of three or more segments, each with up to ten separate sands, and therefore could contain thirty or more separate reservoirs. The same reasoning would have the Southern Area's four segments containing up to forty reservoirs. The Applicant offers its consent to the combination of multiple northern "reservoirs" into a single participating area, but would not extend its consent to any of the southern "reservoirs."

The Division's final decision will evaluate the application under the controlling statutes, regulations, agreements, and conditions. It will conclude that a single participating area covering the Northern and Southern Areas is appropriate for at least seven reasons. First, the Applicant has failed to prove that there is more than one reservoir. Second, the Applicant's proposed interpretation of the word "reservoir" is inconsistent with its definition of the Polaris Schrader Bluff reservoir at hearing,¹ inconsistent with its prior use of the word "reservoir" when communicating with the State about the area at issue, inconsistent with the intent and meaning of the Prudhoe Bay Unit Agreement, inconsistent with the unitization regulations, and inconsistent with North Slope and industry usage and practices.² Third, the Applicant's proposed interpretation of the word "reservoir" would mean that a number of the "reservoirs" in the Northern Area could not be included in the participating area because they lack production from even one well, a consequence surely not intended by the Applicant. Fourth, even if the Division accepted the Applicant's proposed interpretation of the word "reservoir," the Applicant failed to prove that one or more of the multiple "reservoirs" did not extend across the Northern and Southern Areas. Fifth, if the Division restricted the Polaris PA to the Northern Area, the Applicant would be in violation of Article 5.3 of the Prudhoe Bay Unit Agreement, which requires that every reservoir proven capable of sustained commercial production in sufficient quantities to justify development and production must be in a participating area; the Applicant has conceded that the W-200 well in the Southern Area produces from such a reservoir. Sixth, if the Polaris PA was restricted to the Northern Area, the Applicant would be in violation of conditions similar to those set forth in Article 5.3 of the Prudhoe Bay Unit Agreement, which conditions were explicitly imposed at the time of approval of tract operations for wells S-200 and W-200; the Applicant accepted the benefit of those tract operations and must now abide by the conditions for their approval. And, seventh, restricting the Polaris PA to the Northern Area would hinder optimal reservoir management.

The Division's final decision will reach these conclusions, whether it takes into account only the data shared by the Applicant and Chevron, or both the shared data and the Applicant's confidential, non-shared data.

Boundaries: The boundaries of the Polaris PA will not be as large as proposed by Chevron, but limited to those quarter-quarter sections where the parties' subsurface team by consensus mapped oil in the Schrader

¹ See hearing transcript, pp. 4-6.

² Regarding industry practice see, *e.g.*, discussions in *Railroad Commission of Texas v. Pend Oreille Oil & Gas Company, Inc.*, 817 S.W.2d 36 (Texas 1991) and *Amarillo Oil Company v. Energy-Agri Products, Inc.*, 794 S.W.2d 20 (Texas 1990).

Bluff Formation. No acreage outside the boundaries proposed by Chevron in hearing Exhibit 3 will be included in the Polaris PA at this time. Additionally, acreage outside the Applicant's proposed boundaries and north of the southern three-fourths of Sections 33 and 34, T12N, R12E, U.M. shall be excluded from the Polaris PA. Within thirty days of the date of this interim decision the parties shall submit to the Division the legal descriptions for the Polaris PA using the criteria set forth in this paragraph.

Allocation of Production and Expense: Unless the parties unanimously agree otherwise, for five years from the date of approval of the formation of the Polaris PA, participating area expenses and production shall be allocated on the basis of oil originally in place, using the most likely case volumes in the consensus subsurface report. These allocations shall be interim allocations, with final allocations and any retroactive reallocations either unanimously agreed to by all parties, or, if not unanimously agreed to by all parties, then as determined by the Division after the end of the five year period and following notice and an opportunity to be heard. Within thirty days of the date of this interim decision the parties shall submit to the Division the interim allocations for the Polaris PA using the criteria set forth in this paragraph.

Facility Access Fees: Unless the parties unanimously agree otherwise, for two years from the date of approval of the formation of the Polaris PA, the existing Schrader Bluff Interim Facility Sharing Agreement terms shall be applied to all Polaris reservoir production, except to the extent inconsistent with the preceding paragraph. The facility access fees for this two-year period shall be interim fees, with a final methodology for facility access fees and any retroactive adjustment to facility access fees either unanimously agreed to by all parties, or if not unanimously agreed to by all parties, then determined by the Division after the end of the two year period and following notice and an opportunity to be heard.

Plan of Development: The first plan of development for the Polaris PA shall be for the one year period commencing on the effective date of formation of the Polaris PA. Under the first plan of development the Northern and Southern Areas shall be managed as one reservoir. The first plan of development shall be as proposed by the Applicant for the Northern Area, except to the extent inconsistent with this interim decision, or, after issuance of the final decision, inconsistent with the final decision, and except to the extent it permits a single test of each well per month; two tests of each well are required each month. The first plan of development shall be as set forth in Exhibit 304³ for the Southern Area, except to the extent inconsistent with this interim decision, or, after issuance of the final decision, inconsistent with the final decision; again two tests of each well are required each month. An application for approval of a second plan of development must be filed with the Division at least ninety days before the expiration date of the first year's plan of development; however, BP, as unit operator, may request approval for an amendment to the first plan of development at an earlier time.

This interim decision is intended only as an accommodation to the parties; it is not intended to be a final decision appealable to the Commissioner of the Department of Natural Resources. Regardless of whether the Applicant chooses May 1, 2001, June 1, 2001, or the first of the month following the final decision as the effective date for the Polaris PA, no party shall be deemed to have waived its appeal rights by accepting the

³ Exhibit 304, presented at hearing, is a draft plan of development for the Polaris PA prepared by BP; it addresses both the Northern and Southern Areas. Chevron has represented that its proposed plan of development for the Southern Area (Attachment 14A to Chevron's January 18, 2001 submission) was based on BP's draft plan.

benefits or consequences of this interim decision. Following issuance of a final decision, an appeal may be taken to the Commissioner.



Mark D. Myers, Director
Division of Oil and Gas
Department of Natural Resources
State of Alaska

May 11, 2001

Date

cc: Pat Pourchot, Commissioner, Department of Natural Resources
Bonnie Robson, Department of Law