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December 29, 2016

VIA ELECTRONIC MAIL

Chantal Walsh, Director
Division of Oil and Gas
Alaska Department of Natural Resources
550 West 7th Avenue, Suite 1100
Anchorage, AK 99501-3560

Andrew T. Mack, Commissioner
Alaska Department of Natural Resources
550 W. 7th Avenue, Suite 1400
Anchorage, Alaska 99501-3561

Re: Approval of Kitchen Lights Unit 4th Plan of Development – Response/Appeal

Dear Director Walsh and Commissioner Mack:

On behalf of Furie Operating Alaska, LLC (“Furie”), we express our appreciation for your timely approval of the Plan of Development (“POD”) for the Kitchen Lights Unit (“KLU”) as submitted. Furie values the Division’s willingness to work with Furie to promote the public interest.

Clarification and Correction of the Record/Appeal

Furie is writing this letter to clarify two statements in the December 8, 2016, approval of the 4th POD. The first statement indicates the Director’s belief that she may exercise authority under 11 AAC 83.356(e) to contract the KLU as early as February 1, 2017. Although Furie disagrees with that position, it is unclear if the Division intended the last paragraph on page 2 to be an official finding of the POD approval decision or simply a statement of the Division’s opinion. If it is the latter, Furie would appreciate either the withdrawal of the paragraph from the approval letter or written confirmation that the paragraph is not part of the approval decision subject to appeal. We believe that this is likely what the Division intended, since 11 AAC 83.356(e) is not relevant to the proposed 4th POD or its approval. Nor does it appear that the paragraph is intended to serve as the notice or opportunity to be heard required by 11 AAC 83.356(e) since it does not meet the regulation’s prerequisites. Finally, prior to receiving the December 8 letter, Furie had no indication that the POD approval would include any finding regarding the Division’s authority under 11 AAC 83.356(e), and no opportunity to provide pertinent information on the issue.

We would also like to clarify the intent of the first sentence on the second page of the approval that the POD “covers development activities in the Corsair block, with a possibility for exploration activities in the North block.” As noted in the first paragraph of the approval, and

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consistent with 11 AAC 83.343(a), the POD covers the entire KLU. Furie believes the sentence is a description of the work commitments for 2017 rather than a limitation on the scope of the geographic area covered by the POD. If so, Furie would appreciate the Division confirming that the sentence only describes the work commitments contained in the POD, or, if it chooses to reissue the decision, substituting another word like “includes” for “covers.”

If Furie has misunderstood the Division’s intent regarding either the first sentence or the last paragraph on page 2 of the approval, or both, then and to that extent, please consider this letter an appeal of those statements pursuant to 11 AAC 02.010 - 11 AAC 02.900.

Furie believes that the history of the unit demonstrates that discretionary contraction of the KLU is not available until 2019, ten years after formation of the KLU. This letter also contains an explanation of the POD’s coverage, as well as a proposed amendment to the POD if deemed necessary by the Division or the Commissioner.

KLU Formation and History

The KLU was formed effective June 30, 2009. Immediately prior to formation of the KLU:

- No jack-up rig had been in Cook Inlet in over 15 years;
- The Kitchen Unit was in default for failure to drill and the default was under appeal;
- The Kitchen Unit POE denial was on appeal;
- The Corsair Unit was in default and on appeal;
- The Corsair Expansion Application had been denied and timely appealed to Superior Court;
- A stay from default of the Corsair Unit had been denied and appealed to Superior Court; and
- The decision that the Northern Lights Unit application was incomplete was under appeal.

In light of these circumstances, the State took certain actions which it describes as follows:

On December 18, 2008, in an effort to settle these multiple administrative and superior court appeals, deliver a jack-up rig to the Cook Inlet, and begin oil and gas exploration and production from these properties, the Division submitted a proposal (Attachment 10) designed to encourage Escopeta, PERL, ConocoPhillips (operator of the North Cook Inlet Unit) and Renaissance to align their lease interests and form a new unit to include some or all of the non-performing properties—the Kitchen Unit, the Corsair Unit and expansion leases, and the proposed Northern Lights Unit leases. The Division’s intent was to

encourage these lessees to work together under a single operator, align timelines in all units and leases, avoid involuntary unit terminations, and deliver a jack-up rig to the Cook Inlet to find and develop oil and gas in the area.

[T]he Division's intent was for all the lessees to voluntarily aggregate their individual interests, form a single unit overlying all identified potential hydrocarbon accumulations and designate one of the parties as the Unit Operator

Kitchen Lights Unit, Findings and Decision of the Director, Division of Oil and Gas under Delegation of Authority from the Commissioner, Department of Natural Resources, State of Alaska dated June 30, 2009.

Three of the parties, the lessees of the Kitchen and Corsair Units, and of the proposed Northern Lights Unit, did exactly as the State suggested: voluntarily aggregating their interests to form a single unit overlying several potential hydrocarbon accumulations under one operator and delivering a jack-up rig to Cook Inlet. The application requested an expansion and renaming of the existing Kitchen Unit only for expediency. The State approved the new Kitchen Lights Unit effective June 30, 2009. In exchange, the parties dismissed all of the pending administrative and superior court appeals.

Activities Subsequent to Unit Formation

Since the KLU was formed in 2009, the operator has:

- Delivered two jack-up rigs to Cook Inlet;
- Drilled 5 exploration wells and a sidetrack;
- Installed a gas production platform, 15-mile subsea pipeline, and onshore processing facilities;
- Drilled and completed two development wells;
- Drilled one additional development well (to be completed in 2017);
- Produced almost 4 bcf of natural gas for use in Southcentral Alaska;
- Paid almost \$1.7 million in royalties to the State; and
- Acquired 3D seismic over the entire unit.

In 2011, ownership and management of the KLU operator changed and the company was renamed Furie Operating Alaska, LLC. From the time Furie assumed management authority, the KLU has never been in default. Furie has diligently and safely conducted exploration and development activities across the KLU. In short, Furie has done what it promised to do and what the State has asked it to do, as well as meeting the State's aspirational goals stated in the KLU

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Decision. Despite this track record, the State has signaled its intent to contract the unit and deprive Furie and the working interest owners of a significant portion of the value of their investments, including the considerable expense incurred in acquiring the 3D seismic over the entire unit that the State required Furie to obtain in 2015.

Unit Contraction Issues

Under 11 AAC 83.356(e), the Director may contract the unit no sooner than ten years after the effective date to include only that land covered by an approved POE/POD, or that area underlain by oil or gas reservoirs or potential hydrocarbon accumulations and lands that facilitate production.

The effective date of the decision approving the Kitchen Lights Unit is June 30, 2009. Although denominated as an expansion and renaming of the Kitchen Unit, the action created a new unit as requested by the State and a foundation on which to build an exploration and development program; it did not simply add peripheral leases to an existing unit. The KLU combined three separate units or proposed units, encompassing at least four separate prospects. For many of the leases, it was the first time they were unitized. The working interest owners of the affected leases surrendered significant legal rights at the time the unit was formed, including withdrawal of the pending appeals and termination of existing units. The formation of all these prospects into a single unit was suggested by the State. The State cannot now complain that the unit is too large and attempt to contract it sooner than ten years from its creation in its current form. The State has never before used 11 AAC 83.356(e) to contract a unit that has met all state requirements. In fact, we can find only one instance of the State ever contracting a unit pursuant to that regulation. In that case, the State contracted the Redoubt Unit after the operator failed to comply with POD requirements and failed to respond to numerous requests from the State. The operator of the Redoubt Unit did not object to the contraction. By contrast, Furie has been fully responsive to State requests, satisfied its POD commitments, and strongly objects to any unit contraction.

The proper application of 11 AAC 83.356(e) to the KLU does not allow the Director to exercise discretion to contract the unit before June 30, 2019, at the earliest. Even at that time, discretionary contraction of the unit would not be justified unless there is a history of noncompliance and nonresponsiveness.

POD Coverage

The POD submitted by Furie covers the entire unit as demonstrated by the first paragraph of the POD and acknowledged in the first paragraph of the POD approval letter. The statement in the approval letter that the POD "covers development activities in the Corsair block, with a possibility for exploration activities in the North Block" is a description of the work

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commitments for 2017 rather than a limitation on the scope of the geographic area covered by the POD. By regulation, the POD covers “the proposed development activities for the unit” for a single year of activities and must be renewed every year. The approved work commitments are a function of what can practically and safely be accomplished in a single drilling season rather than a limitation of the geographic area covered by the POD. Generally, it would not be safe nor prudent for Furie to drill more than two wells in the unit over the summer season. Moreover, Furie is simultaneously pursuing additional development of the known reserves while continuing safe, appropriate, and prudent exploration activities. It would be imprudent to undertake additional exploration and development activities during a single drilling season.

Furie’s intent to continue diligent exploration throughout the unit is demonstrated by the various permits it has obtained which span several years, authorize multiple exploration wells, and cover the entire unit area. Most significantly, on May 20, 2016, DNR approved the KLU Plan of Operations for exploration activities which includes wells throughout the KLU to be drilled through 2021. As stated in the Plan of Operations:

This Plan of Operations describes oil and natural gas exploration activities that are planned for the KLU, as initially described in the Plan of Development submitted to the department on 7 October 2015. The KLU covers approximately 130 square miles in Cook Inlet. Over the next few years, Furie plans to return to the KLU#4 exploration well to continue exploration as well as drill up to 9 new exploration wells in the KLU. Furie anticipates drilling 2 exploration wells each year. Goals for KLU#4 exploration include commercially reasonable efforts to drill and acquire sufficient logs and data to properly evaluate the KLU #4 well to a depth sufficient to test for gas and oil through the Tyonek and Hemlock formations and into the Jurassic formation. Goals for additional drilling of exploration or delineation wells within the KLU include testing through the Tyonek, Beluga, and Hemlock formations for oil and gas in the Southwest Block, testing the Hemlock formation for oil in the North Block, and testing through the Sterling, Beluga, Tyonek, Hemlock, and Upper Jurassic formations for oil and gas in the Central and Corsair Blocks. Exploration activities in this Plan of Operations are proposed to continue through 2021.

In addition to the approved Plan of Operations, Furie has obtained authorization from the U.S. Army Corps of Engineers for these exploration wells. At considerable expense and as requested by the State, Furie also acquired 3D seismic data over the entire KLU to facilitate its future operations in the unit.

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Early unit contraction would be unfair and highly prejudicial to the lessees who have done what the State has asked of them. In particular, in 2015, Furie brought a new jack-up rig to Cook Inlet in reliance on the State's approval of the multi-year Plan of Operations and acquired 3D seismic over the entire unit at the State's insistence. Furie has also obtained multi-year exploration permits covering the entire KLU. Each of these investments was made with the expectation that the unit would remain intact for many years to come so that the lessees could realize the benefits of these investments.

Amendment to Approved POD

To the extent the Department considers the POD to be limited to only those areas in which drilling activities are proposed in 2017, Furie submits the above information as an amendment to the POD.

Conclusion

We hope that this summary is helpful to you in considering any position that DNR may take regarding contraction of the KLU. This letter highlights certain pertinent facts regarding these issues but is in no way an exhaustive explanation of the relevant facts and arguments. Furie reserves the right to appeal any future contraction decision and to make any and all arguments in challenging any contraction decision. Nothing contained in this letter, or omitted from this letter, waives any rights or arguments Furie may have with respect to future actions of the Department.

As described above, Furie considers both the date for potential unit contraction and the statement regarding POD coverage to be dicta and not a binding part of the POD approval. However, in the event the Division disagrees, Furie submits this letter as an appeal pursuant to 11 AAC 02.010 - 11 AAC 02.900. In the event this letter is considered an appeal, Furie requests the following relief:

- a determination that the POD covers the entire KLU; and
- a determination that either
 - the statements in the last paragraph of page 2 of the approval are not findings in the POD approval decision and do not bind Furie (thus preserving Furie's right to challenge any action the Division or Department might take in the future under 11 AAC 83.356(e)), or
 - discretionary contraction of the KLU under 11 AAC 83.356(e) is not available until June 30, 2019, at the earliest.

Because we do not know whether you will consider this as an appeal, and recognizing the deadline to submit all supporting evidence and argument within 20 days pursuant to 11 AAC

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02.030(d),¹ we respectfully request that you inform us within five days whether you consider this to be an appeal. Understanding that the holidays may make this impossible, in the event you require additional time to consider this matter, we request an extension of time to submit additional information commensurate with the time required to make such decision.

Please contact me if you have any questions or would like to discuss these matters further. If this is considered an appeal, please direct all communications to me using the Anchorage address set forth below or the contact information provided on the first page of this letter.

Sincerely,



Ramona L. Monroe

cc: Becky Kruse, DNR
David Elder, Furie
Bruce Webb, Furie
Tony Nunes, Cogan & Partners
Jon Iversen
dnr.appeals@alaska.gov

¹ In the event this is considered an appeal, we also provide notice of our intent to file additional written material pursuant to 11 AAC 02.030(d). Also, a list of the leases in the Kitchen Lights Unit is attached to comply with 11 AAC 83.030(a)(12).