

Findings and Decision of the Director
of the Division of Oil and Gas

DENYING AN APPLICATION TO EXPAND THE DEEP CREEK UNIT AREA
TO INCLUDE OIL AND GAS LEASE ADL 390511

Under a Delegation of Authority
from the Commissioner of the State Of Alaska
Department of Natural Resources

December 21, 2004

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I. Summary

Alliance Energy LLC (Alliance) applied to the State of Alaska, Department of Natural Resources, Division of Oil and Gas (the State, the DNR, or the Division, as appropriate) to expand the Deep Creek Unit area to include oil and gas lease ADL 390511, which abuts the unit's eastern boundary (the Application). ADL 390511 is currently held by Alliance and Northstar Energy Group (Northstar) (jointly referred to as Alliance or the Applicants) with 99.275% and .725% working interest ownership, respectively. In addition, five parties own a total of 5.18% overriding royalty interest in ADL 390511. The Division finds that the proposed expansion of the Deep Creek Unit area is not supported by the available geological, geophysical, or engineering data, and the Applicants have not committed to acquire additional technical data that would justify approval of the Application.

II. Background

The Deep Creek Unit is located on the Kenai Peninsula, approximately five miles inland from the nearest communities of Ninilchik and Happy Valley. The Deep Creek Unit encompasses 22,656.90 acres. Approximately 40.37% of the unit area lies within three State leases and 59.45% lies within five CIRI leases. The remaining .18% of the Deep Creek Unit (39.99 acres) is unleased federal acreage managed by the Bureau of Land Management (BLM). The State and CIRI jointly administer the Deep Creek Unit Agreement (the Agreement). Union Oil Company of California (Unocal) is the Deep Creek Unit Operator and the sole working interest owner in the unit. The Division and Cook Inlet Region Inc. (CIRI) approved the formation of the Deep Creek Unit and Unocal's initial plan of exploration effective December 31, 2001.

The Division issued oil and gas lease ADL 388199 effective February 1, 1997, with a seven-year primary term. ADL 388199 was a noncontiguous lease with approximately two miles between the two lease segments. The eastern portion of ADL 388199, Segment 1, contained 1,920 acres and the western portion, Segment 2, encompassed 1,115.68 acres for a total leased area of approximately 3,035.68 acres.

Alliance owned ADL 388199 in 2001, when Unocal applied to form the Deep Creek Unit. However, Alliance neither responded to the Division's public notice requesting comments on Unocal's unit application nor requested that its lease be included in the initial unit area.

In September 2003, Sam Nappi, President of Alliance and Northstar, contacted the Division contending that Segment 2 of ADL 388199 should be included in the Deep Creek Unit. The Division received a map of the Applicants' seismic interpretation of the Deep Creek Unit area as it related to their lease on October 3, 2003. On November 4, 2003, Alliance submitted three seismic dip sections and a two-way time map of the Upper Tyonek Sandstone in the lease area.

On October 30, 2003, Alliance submitted an application to form the Nikolaevsk Unit southeast of the Deep Creek Unit that included Segment 1 of ADL 388199. The Division issued a public notice of Alliance's Nikolaevsk Unit application on November 2, 2003. On the last day of the public comment period, December 8, 2003, Alliance informed the Division that it was assigning its interest in the acreage proposed for inclusion in the Nikolaevsk Unit to Unocal. Unocal submitted an amended

application to form the Nikolaevsk Unit with a slightly modified unit area, and informed the Division that it had acquired 100% working interest ownership from Alliance and all of the other lessees in the proposed Nikolaevsk Unit area, including Segment 1 of ADL 388199. However, Unocal did not acquire any working interest ownership in Segment 2 of ADL 388199.

The Division approved the formation of the Nikolaevsk Unit to include Segment 1 of ADL 388199, effective January 30, 2004. The Division severed ADL 388199, and assigned lease number ADL 390511 to the non-unitized acreage in Segment 2 of ADL 388199. With the same effective date and term as the original lease, ADL 390511 was due to expire on January 31, 2004.¹

On November 4, 2004, the Division and CIRI approved Unocal's application for formation of the Happy Valley Participating Area (the Happy Valley PA) within the Deep Creek Unit. The Happy Valley PA encompasses approximately 1,239.99 acres, including 145.84 acres within a State lease and 1,094.15 acres within three CIRI leases. Gas produced from the Happy Valley PA is allocated to the individual leases based on their surface acreage within the participating area as a percentage of the total acreage in the Happy Valley PA.

III. Application for Expansion of the Deep Creek Unit Area

On January 30, 2004, the DNR granted a six-month extension of the lease term until July 30, 2004, to allow Alliance time to present its geologic interpretation and file a formal application to expand the Deep Creek Unit to include ADL 390511.² On July 16, 2004, Alliance submitted an application to expand the Deep Creek Unit. The Division deemed Alliance's application incomplete, and by letter dated July 28, 2004, specified the additional information needed for a complete unit expansion application and granted a further extension of the lease term, until September 30, 2004, to allow Alliance time to complete the application.

On September 1, 2004, Alliance submitted a new Deep Creek Unit Expansion Application. The Application included the Deep Creek Unit Agreement, executed by the Applicants; Exhibit A, a schedule describing the expanded unit area; and Exhibit B, a map depicting the expanded unit area. The Applicants also submitted executed documents stating that they

adopt, ratify, confirm and approve all of the terms and provisions of the Deep Creek Unit Operating Agreement and the Deep Creek Unit Agreement, including all attachments and exhibits thereto and all Plans of Development and other appropriate filings approved by the DOG, and does hereby approve

¹AAC 11.83.373. SEVERENCE. (a) Except as otherwise provided in this section and 11 AAC 83.356, where only a portion of a lease is committed to a unit agreement approved or prescribed by the commissioner, the commitment constitutes a severance of the lease as to the unitized and nonunitized portions of the lease. The portion of the lease not committed to the unit will be treated as a separate and distinct lease having the same effective date and term as the original lease and may be maintained thereafter only in accordance with the terms and conditions of the original lease, statutes, and regulations. Any portion of the lease not committed to the unit agreement will not be affected by the unitization or pooling of any other portion of the lease by operations in the unit, or by suspension approved or ordered for the unit under 11 AAC 83.336(b).

² AAC 11.83.373. SEVERENCE. (b) The commissioner will, in his discretion, grant up to a two-year extension of the lease term for that portion of a lease not committed to the unit agreement under this section.

and fully support Union Oil Company of California (“Unocal”) as the Deep Creek Unit operator.

The overriding royalty interest owners also submitted ballots supporting the Application. Technical data submitted in support of the Application included a report prepared by Sproule International, Ltd. (the Sproule Report) and a time structure map on the Upper Tyonek.

On September 16, 2004, the Division deemed the Application complete and published a notice on September 19, 2004, which invited interested parties and members of the public to submit comments by October 22, 2004. Under 11 AAC 83.316, the Division has sixty-days following the close of the public comment period to issue a findings and decision approving or disapproving a unit expansion application. On September 28, 2004, the DNR extended ADL 390511 until December 21, 2004, to allow the Division time to process the Application.

The Division received only one response to the public notice. On October 1, 2004, Unocal, the Deep Creek Unit Operator, submitted comments on the Application including confidential technical data and interpretations. Unocal asserted that the Division should reject the Application.

Unocal believes DO&G has proceeded improperly in this matter. No extension of the lease was appropriate in the absence of either new geological or geophysical information or the commitment by Alliance to obtain such additional information or, better yet, drill a well to support the application. Unocal believes that DO&G’s extension of the primary term of the lease in the absence of either new data or a work commitment is unprecedented and inappropriate.

In addition, if the Division continued to process the Application, Unocal requested that the Division deny Alliance’s request to expand the Deep Creek Unit due to lack of technical merit.

We encourage you to evaluate the new attached confidential information in conjunction with previously submitted information supplied by Unocal and conclude that a Deep Creek Unit expansion is not warranted at this time and deny Alliance’s unit expansion application.

IV. Analysis of the Application for Expansion of the Deep Creek Unit Area

The Commissioner of DNR (the Commissioner) reviews unit-related applications, including unit expansions and the formation of participating areas, under AS 38.05.180(p) and 11 AAC 83.301—11 AAC 83.395. The statute and DNR regulations set out the standards and criteria for expansion of a unit area.

UNIT AREA; CONTRACTION AND EXPANSION. (a) A unit must encompass the minimum area required to include all or part of one or more oil or gas reservoirs, or all or part of one of more potential hydrocarbon accumulations.³

³ 11 AAC 83.356.

APPLICATION FOR UNIT APPROVAL. Any person owning an interest in a lease which is proposed to be committed to a unit which would include a state oil and gas lease may propose a unit agreement by applying to the commissioner for approval of the agreement. The following items constitute a complete application for approval: ... (4) all pertinent geological, geophysical, engineering, and well data, and interpretations of those data, directly supporting the application.⁴

The Commissioner or his designee⁵ may approve a unit expansion application if he determines it is necessary or advisable in the public interest.⁶ This Finding and Decision evaluates the Application based on the six factors set out in 11 AAC 83.303 (b).

1. Prior Exploration and Development Activities and the Geological and Engineering Characteristics of the Reservoir

The Deep Creek anticline is the main feature in the Deep Creek Unit area, and a structural saddle separates it from the Happy Valley anticline. The Happy Valley reservoir consists of Tertiary (Kenai Group) Tyonek and Beluga formation sandstones and interbedded coals. The reservoir is defined by a four-way dip closure along a northeast-southwest trending anticline, with possible fault containment on the east.

In 1958, Standard Oil of California (SOCAL) drilled the first well to test the Deep Creek anticlinal trend, the SOCAL Deep Creek 1 well (SDC 1). SOCAL's primary exploration objective was oil in the Hemlock Formation, with gas in the Tyonek Formation as a secondary target. Subsequent to logging the initial borehole, problems forced the operator to re-drill the well before testing the Hemlock Formation (SDC 1-RD). SOCAL completed two drill stem tests (DSTs), one in the Tyonek Formation and one in the Hemlock Formation that showed minor indications of gas. SOCAL plugged and abandoned the SDC 1-RD as a dry hole.

In 1963, Superior Oil Company drilled the Happy Valley Unit #31-22 well (HVU 31-22) approximately one mile south of SDC 1-RD and within the current Happy Valley PA. Superior did not perform any reservoir tests on the HVU 31-22 well before plugging and abandoning it as a dry hole.

Effective December 31, 2001, the State and CIRI approved Unocal's application to form the Deep Creek Unit. The initial Plan of Exploration contained a commitment to drill one exploratory well in the first year, and if successful, Unocal was prepared to drill a second well in the unit area. The State

⁴ 11 AAC 83.306 (4)

⁵ By memorandum dated September 30, 1999, the Commissioner approved a revision of Department Order 003 that delegated this authority to the Director of the Division of Oil and Gas.

⁶ The proposed unit action must be necessary or advisable in the public interest: "To conserve the natural resources of all or part of an oil or gas pool, field, or like area, the lessees and their representatives may unite with each other, or jointly or separately with others, in collectively adopting or operating under a cooperative or unit plan of development or operation of the pool, field, or like area, or part of it, when determined and certified by the commissioner to be necessary or advisable in the public interest." AS 38.05.180(p).

and federal agencies approved the necessary permits to spud the first well prior to formation of the Deep Creek Unit, and Unocal drilled the NNA #1 well as a straight hole on CIRC acreage north of the SDC 1-RD. Unocal completed NNA #1 on January 27, 2002, and tested several intervals which were wet or tight.

After drilling the NNA #1 well, Unocal constructed a gravel pad nearly two miles south of the first well location and drilled the Happy Valley #1 well (HV-1) to a bottom-hole location about a mile west of the pad. HV-1 produced gas from two Lower Tyonek intervals at test rates of 4.1 million cubic feet per day (MMCFPD) at 1,122 pounds per square inch gage fluid tubing pressure (psig FTP). Encouraged by the HV-1 well's success, Unocal continued to drill Happy Valley delineation wells in 2003 and 2004.

Unocal drilled six more wells in the Deep Creek Unit and converted NNA #1 to a disposal well before submitting an application to form the Happy Valley PA. Unocal tested gas production from the HV-1 and HV-2 wells in the Tyonek formation and the HV-8 well in both the Tyonek and Beluga formations. No test rate was established for HV-3, HV-4, HV-6, or HV-7 wells. Unocal drilled the HV-5 well to the target objective, but it was unproductive.

Unocal also committed to acquire new proprietary 2D or 3D seismic data within the proposed unit area to enable mapping of the adjacent structures during the second year of the Initial POE. Unocal fulfilled the commitment by acquiring 105 line miles of 2D seismic over the Deep Creek Unit area.

Unocal proceeded with its plan of exploration, established gas production in commercial quantities, and applied to form the Happy Valley PA. The Happy Valley PA is stratigraphically limited to the Beluga and Tyonek Formation Sands from -1,547 feet True Vertical Depth Sub Sea (TVDSS) (2,176 feet Measured Depth) in the Happy Valley Unit No. 31-22 well to -9,368 feet TVDSS (10,678 feet Measured Depth) in the HV-3 well. Unocal mapped the depth of the lowest known gas for each producible interval based on seismic and well control and overlaid them on an aliquot part map grid to determine the Happy Valley PA boundary, which is based on 40-acre aliquot parts.⁷ The unit boundary, the Happy Valley PA boundary, and well locations are depicted on Figure 1 below.

Unocal's initial interpretation indicated that the unit area may encompass several potential hydrocarbon accumulations and exploration to date has confirmed the presence of the Happy Valley reservoir in the northern unit area. Alliance based its interpretation of one large accumulation extending over the entire Deep Creek Unit on five seismic lines acquired by ConocoPhillips, which is a subset of the data Unocal relied on to establish the original unit boundary.

Alliance has not acquired any new geologic, geophysical, or well data over the lease area, while Unocal drilled ten wells since forming the Deep Creek Unit and acquired 105 miles of proprietary seismic data in addition to ConocoPhillips' data. Unocal's interpretation of the Deep Creek Unit boundary remains unchanged, as set out in its comments on the Application.

⁷ 11 AAC 88.185(11) "legal subdivision" means an aliquot part of a section of land according to the public land rectangular survey system, not smaller than one-quarter of one-quarter of one section of land, containing approximately 40 acres; where a section of land contains section lots, "legal subdivision" also means those section lots; "legal subdivision" also means a protracted legal subdivision according to any protracted public land rectangular survey prepared by the division or Bureau of Land Management of the Department of the Interior, and made available to prospective applicants for leases;

All data acquisition to date continues to confirm and support Unocal's original interpretation of the current Deep Creek Unit boundary. No other new and available information is known to suggest any other interpretation, nor warrant a change in the Unit boundary at this time.

In addition to Unocal's Happy Valley well data, the Division has access to approximately three times as much seismic data over the proposed expansion area than Alliance. The Division agrees with Unocal's assessment that the Deep Creek Unit may contain multiple accumulations but the only confirmed commercial production is from the Happy Valley reservoir, which does not extend onto the Applicants' lease.

However, Unocal's interpretation of the data also indicates a potential accumulation south of the Happy Valley reservoir that Unocal refers to as the Middle Happy Valley Prospect. Unocal planned to drill two wells, Middle Well #1 and Saddle Well #1, from a new pad to evaluate this prospect. In March 2004, Unocal requested approval of a Plan of Operations to build a road and construct the Happy Valley Middle Saddle Pad. The Plan of Operations states: "Currently only Middle Well #1 is on the drilling schedule, with an expected spud date of July 1, 2004." The Office of Project Management and Permitting issued a determination that Unocal's Plan of Operations was consistent with the Alaska Coastal Management Plan, and the Division issued Lease/Unit Operations Approval LOCI 04-06 on May 24, 2004. However, Unocal neither constructed the road or pad nor drilled a well to evaluate the Middle Happy Valley prospect. The Divisions approval will expire if Unocal does not begin operations within three years.

An exploration well would be needed to confirm whether the Middle Happy Valley Prospect is commercially viable and if the accumulation extends onto the proposed expansion area. However, the well and geophysical data provided in support of the Application, and otherwise available to the Division, suggest that the lease may lie within the structural saddle that separates the Deep Creek anticline from the Happy Valley anticline, in which case it would not contribute to production. The data is currently insufficient to conclude if the land within ADL 390511 is underlain by hydrocarbons.

The prior exploration activities and the geological and engineering characteristics of the proposed expansion area do not support approval of the Application under 11 AAC 83.303(b)(2) and (3).

2. The Applicants' Plan of Development for the Proposed Expansion Area

The Application states:

Interest owners in the Expansion Area have executed a ratification document, thereby ratifying the plan of development provided by the unit operator, pursuant to the Unit Agreement, and subject to the Commissioner's approval of the expansion of the DCU.

On November 4, 2004, the Division and CIRI approved the Unit Operator's First Plan of Development for the Deep Creek Unit (First POD) for the period September 1, 2004 to August 31, 2005. The First POD includes plans to develop the reserves underlying the Happy Valley PA and to explore the unit area outside of the participating area. Unocal completed construction of gas handling facilities on the Happy Valley pad and gathering lines that connect it to the Kenai Peninsula pipeline network. Sustained production from the Happy Valley PA commenced in November 2004. Unocal commingles gas production from multiple zones in the Tyonek and Beluga sandstones, processes the hydrocarbon stream in the gas processing facility located on the Happy Valley pad, and ships pipeline quality gas through the pipeline that connects the Deep Creek Unit to the Kenai-Kachemak Pipeline.

Unocal's First POD also includes plans to drill two or more additional development wells in the Deep Creek Unit from the Happy Valley pad. Unocal has approved permits and is currently drilling HV-9 and HV-10. Unocal may also establish a second drill pad to develop the reserves in the western portion of the Happy Valley PA. Primary gas treatment facilities may be located on the second development pad and a gathering line installed to ship the gas to the Happy Valley pad where it will be processed for sale.

Exploration activities outside of the Happy Valley PA include both exploration drilling and seismic evaluation. Unocal installed the Star pad in the southern end of the Deep Creek Unit in 2004, and drilled the Star #1 well, which bottom-holed outside of the unit area. A flow test of the Star #1 well produced gas from the Tyonek formation at a rate of 0.5 MMCFPD at 413 psig FTP. Unocal plans to recomplete and test uphole zones in the Star #1 well during the term of the First POD. Further delineation of this southern accumulation may justify forming another participating area and expanding the unit area.

During the term of the First POD, Unocal will process and evaluate the seismic data acquired over the Deep Creek Unit area, which should improve Unocal's understanding of the underlying hydrocarbon accumulations.

The First POD does not contemplate any exploration wells that would evaluate whether hydrocarbons are present in the proposed expansion area, and the Applicants did not propose any additions or amendments to the approved unit plan. Therefore, the Applicants' plans for exploration of the unit area do not support approval of the Application under the section .303(b)(4) criteria.

3. The Economic Costs and Benefits to the State

There are no plans to confirm if a potential hydrocarbon accumulation exists within the proposed expansion area. Therefore, approval of the Application would provide no economic benefits from exploration, delineation, or production from ADL 390511. In addition, approving an expansion of the Deep Creek Unit to include ADL 390511 would extend the lease term for as long as the lease remained committed to the Unit Agreement. Unitization would extend the lease for nearly ten years even if exploration confirmed that the expansion area was not underlain by hydrocarbons. And, the entire lease would be held indefinitely if even a portion of the lease was included in a participating area.

Ten years after Sustained Unit Production begins, the unit area must be contracted to include only those lands then included in an approved Participating Area and lands that facilitate production including the immediately adjacent lands necessary for secondary or tertiary recovery, pressure maintenance, reinjection, or cycling operations. The Commissioner and the President may delay contraction of the Unit Area if the circumstances so warrant. If any portion of a lease is included in the Participating Area, the portion of the lease outside the Participating Area will neither be severed nor will it continue to be subject to the terms and conditions of the unit. The portion of the lease outside the Participating Area will continue in full force and effect so long as production is allocated to the unitized portion of the lease and the lessee satisfies the remaining terms and conditions of the lease.⁸

However, if the Division denies the Application, the lease will expire and the acreage will be available for bid in the next Cook Inlet Areawide lease sale.

In summary, the economic costs of approving the Application outweigh the benefits. The Applicants made no commitment to explore and develop the expansion area and the State would lose the opportunity to receive bonus bids on the available acreage. Therefore, the Division's evaluation of the section .303(b)(5) economic criteria does not support approval of the Application.

4. The Environmental Costs and Benefits

Unitization allows the unit operator to explore and develop the resources under a single unit plan rather than on a lease-by-lease basis. The benefits of consolidated exploration and development, application of the State's Areawide mitigation measures, and the use of existing roads, can balance the potential costs to the surrounding environment. In addition, Article 8.2 of the Agreement requires that a Unit Plan of Operations must be consistent with the leases, mitigation measures, and lessee advisories developed by the DNR for the State's most recent Cook Inlet Areawide lease sale. Exploration and development within the Deep Creek Unit is subject to these provisions, if proposed operations involve State surface or subsurface. Approval of the Application would reduce the environmental costs that would occur if Alliance were to explore and develop the proposed expansion area on a lease basis.

⁸ Deep Creek Unit Agreement, Article 14.2.

Unitized operations would reduce environmental impacts, which supports approval of the Application under the section .303(b)(1) criteria.

V. Findings

1. Promote the Conservation of all Natural Resources

The proposed expansion of the Deep Creek Unit area would not promote the conservation of surface or subsurface resources. A comprehensive operating agreement and plan of development governing the expansion area could help avoid duplicative development efforts on and beneath the surface of the area if the potential accumulations with the Deep Creek Unit extend onto the lease. But, the existence of such a reservoir is unconfirmed. Unocal is proceeding with delineation and development of the Happy Valley PA and exploration of the remaining unit area. However, extending the lease term by unitization without a commitment to explore the expansion area is not in the public interest.

Approval of the Application could help minimize negative impacts on the environment and other natural resources that would occur if the Applicants planned operations on the expansion area. However, approval of the Application would not help maximize oil and gas recovery given that there is no evidence of hydrocarbons within ADL 390511.

2. Promote the Prevention of Economic and Physical Waste

The available data is insufficient to determine whether a potential hydrocarbon accumulation exists within the Deep Creek Unit that extends onto the proposed expansion area. Even Alliance's interpretation suggests that only a small portion of the lease, if any, could be underlain by hydrocarbons. However, a prudent operator would not drill a well on ADL 390511 to confirm the prospect, because, even in the most optimistic case, it lies on the lower edge of the structure. An exploration well drilled within the unit area to the southwest of the lease could confirm if a reservoir exists, but additional well tests would be necessary to determine if it was a commercial discovery and if the lease could contribute to production.

3. Provide for the Protection of all Parties of Interest, Including the State

If the proposed expansion area was capable of contributing to production from the Happy Valley reservoir, it would justify approval of the Application and an expansion of the Happy Valley PA.⁹ However, the data indicate that the Happy Valley reservoir does not extend southeast of the current Happy Valley PA boundary. Therefore, approval of the Application is not needed to protect the Applicant's rights to any of that reservoir's production.

Although the Applicants agreed to support the Unit Operator's plan of development, the First POD does not include any plans to explore or develop the proposed expansion area. The Application does not protect the State's interest in having its hydrocarbon resources explored and developed in a timely manner. It is unfortunate, however, that Alliance and Unocal could not agree on a plan to evaluate

⁹ 11 AAC 83.350. PARTICIPATING AREA. "(c) A participating area must be expanded to include acreage reasonably estimated through use of geological, geophysical, or engineering data to be capable of producing or contributing to the production of hydrocarbons in paying quantities, ..."

the expansion acreage and submit a joint unit expansion application. In essence, the Application requests the Division approve involuntary unitization of the lease. It may have been in the State's interest to approve the Application if Alliance had supplemented the First POD with a commitment to drill a well within the unit area to evaluate its acreage. That, however, would have put Unocal in an unreasonable position as the Unit Operator who is required to fulfill a commitment that it did not make.

Alliance took no action during the seven-year primary term of the lease to evaluate its hydrocarbon potential. Further, Unocal claims the Division acted inconsistently by granting Alliance lease extensions to prepare, submit, and evaluate the Application.

In searching our records, we are unable to come up with any past lease extension request granted to Unocal by the DO&G wherein a work commitment, nonperformance payment or well commitment was not a condition of extension. The favorable treatment of Alliance in this matter is inconsistent with the treatment Unocal has experienced under similar yet different instances.

While I do not agree with Unocal's assessment in this case, I am concerned about any perception that the Division's actions were unfair or unreasonable. Alliance first approached the Division about expanding the Deep Creek Unit four months prior to expiration of the lease's primary term. It was in the State's interest to grant the extension, if Alliance could provide technical data and an appropriate plan of exploration supporting commitment of the lease to the Deep Creek Unit. If we allowed the lease to expire, the State may receive bonus bids when it re-offered the acreage, but the acreage may not be explored within the primary term of the new lease. However, it would be in the State's interest to have a commitment to explore and develop the acreage sooner under the Deep Creek Unit Agreement. The State's interest is best served by ongoing production under State oil and gas leases.

The Agreement provides for future expansions and contractions of the unit area as warranted by data obtained by exploration or otherwise. The Agreement thereby protects the public interest, the rights of the parties, and the correlative rights of adjacent landowners. It is possible that as Unocal continues to explore the Deep Creek Unit area, it may find a reservoir that extends onto the proposed expansion area. If so, at that time, Unocal will be required to apply to expand the unit area and form a participating area to allocate production. However, there is insufficient data at this time to justify expanding the Deep Creek Unit to include ADL 390511.

VI. Decision

The Division reviewed the statutes, oil and gas unitization regulations, the Deep Creek Unit Agreement and Operating Agreement, and materials supplied by Alliance in support of the Application. I find that the proposed expansion of the Deep Creek Unit would not promote the conservation of natural resources, promote the prevention of economic and physical waste, or provide for the protection of all parties in interest including the State. The Application provides inadequate protection of the public interest, is not in the State's best interest, and fails to meet the requirements of AS 38.05.180(p) and 11 AAC 83.303. Therefore, the Application is denied.

A person affected by this decision may appeal it, in accordance with 11 AAC 02. Any appeal must be received within 20 calendar days after the date of "issuance" of this decision, as defined in 11 AAC 02.040 (c) and (d), and may be mailed or delivered to Thomas E. Irwin, Commissioner, Department of Natural Resources, 550 W. 7th Avenue, Suite 1400, Anchorage, Alaska 99501; faxed to 1-907-269-8918; or sent by electronic mail to dnr_appeals@dnr.state.ak.us. This decision takes effect immediately. If no appeal is filed by the appeal deadline, this decision becomes a final administrative order and decision of the department on the 31st day after issuance. An eligible person must first appeal this decision in accordance with 11 AAC 02 before appealing this decision to Superior Court. A copy of 11 AAC 02 may be obtained from any regional information office of the Department of Natural Resources.

Original signed by Mark D. Myers, Director
Mark D Myers
Division of Oil and Gas

December 21, 2004
Date

cc: Kirk McGee, CIRI
Kevin Tabler, Unocal
Jeff Landry, Assistant Attorney General