

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES

DIVISION OF OIL & GAS

SARAH PALIN, GOVERNOR

550 WEST 7TH AVENUE, SUITE 800
ANCHORAGE, ALASKA 99501-3560

PHONE: (907) 269-8800

FAX: (907) 269-8938

**CERTIFIED MAIL
RETURN RECEIPT REQUESTED**

February 12, 2008

Paul Wharton
Staff Landman
ConocoPhillips Alaska, Inc.
P.O. Box 100360 – Suite ATO 1482
Anchorage, Alaska 99501-0360

Re: Amended Approval of the Expansion of the Tarn Participating Area

Dear Mr. Wharton,

On January 23, 2008, the State of Alaska, Department of Natural Resources, Division of Oil and Gas (Division) issued the Findings and Decision of the Director of the Division of Oil and Gas “Approval of the Expansion of the Tarn Participating Area Kuparuk River Unit” (Tarn Expansion Decision). On January 28, 2008, by phone and email, the KRU Operator, ConocoPhillips Alaska, Inc. (CPAI) asked for clarification to the third sentence of Section III.2.c.: “For that reason, the TPA is limited to that area of the Bermuda interval deemed to be productive.”, email attached. By letter dated February 11, 2008, CPAI requested that the Division formally revise the sentence to read “The TPA development has thus far been limited to that area of the Bermuda interval deemed to be productive.” and issue an Amended Tarn Expansion Decision. The Division agrees to revise the sentence and to issue an Amended Approval of the Expansion of the Tarn Participating Area Kuparuk River Unit, attached to this letter.

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 Tom Irwin, Commissioner, DNR, 550 W. 7th Avenue, Suite 1400, Anchorage, Alaska 99501; faxed to 1-907-269-8918, or sent by electronic mail to dnr.appeals@alaska.gov. This decision takes effect immediately. An eligible person must first appeal this decision in accordance with 11 AAC 02 before appealing this decision

“Develop, Conserve, and Enhance Natural Resources for Present and Future Alaskans.”

to Superior Court. A copy of 11 AAC 02 may be obtained from any regional information office of the Department of Natural Resources.

If you have any questions regarding this decision, contact Temple Davidson with the Division at 907-269-8784.

Sincerely,

A handwritten signature in black ink, appearing to read "Kevin R. Banks", with a long horizontal flourish extending to the right.

Kevin R. Banks

Acting Director

Attachments

Cc: Jeff Landry

Davidson, Temple (DNR)

From: Wharton, Paul K [Paul.K.Wharton@conocophillips.com]
Sent: Monday, January 28, 2008 9:23 AM
To: Davidson, Temple (DNR)
Cc: Cunningham, Bryce; Isaacson, Lisa E.
Subject: Tarn PA modification language at p.7 par. c

Temple:

As we discussed a question has been raised as to a sentence which appears in the Tarn PA approval at page 7, paragraph c:

"TPA is limited to that area of the Bermuda interval deemed to be productive"

As we discussed, you interpret these words as descriptive only and not as words of limitation. Consequently future production from

Esker and Cairn intervals will be treated as production under the Tarn PA and future operations to these intervals within the extent of the Tarn PA need not have tract operations approval.

If we need to petition to have this issue clarified please notify me by February 1, 2008.

Thank you for your attention to this matter and please call me with any questions.

Paul

Paul K. Wharton
Staff Landman
ConocoPhillips Alaska, Inc.
ATO 1482
700 G. Street (zip for street address 99501)
P.O. Box 100360
Anchorage, Alaska 99510-0360
tel. (907) 263-4076
fax (907) 263-4966
email: Paul.K.Wharton@conocophillips.com

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

**AMENDED APPROVAL OF THE EXPANSION OF THE TARN
PARTICIPATING AREA
KUPARUK RIVER UNIT**

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

February 12, 2008

TABLE OF CONTENTS

I	BACKGROUND	Page 3
II.	APPLICATION	Page 4
III.	DISCUSSION OF DECISION CRITERIA	Page 5
	A. Decision Criteria considered under 11 AAC 83.303(b)	
	1. The Environmental Costs and Benefits of TPA expansion	
	2. The Geological and Engineering Characteristics of the TPA Expansion Area	
	3. Further Plans for Exploration or Development for the TPA	
	4. The Economic Costs and Benefits to the State and Other Relevant Factors	
	B. Decision Criteria considered under 11 AAC 83.303(a)	
	1. Promote the Conservation of All Natural Resources	
	2. The Prevention of Economic and Physical Waste	
	3. The Protection of All Parties of Interest, Including the State	
IV.	FINDINGS AND DECISION	Page 10
V.	ATTACHMENTS	
	1. July 2, 2003 Automatic Contraction of the TPA	
	2. May 2005, Extension request and Approval	
	3. June 2006 Extension request and Approval	
	4. June 2007 Kuparuk River Unit Tarn Participating Expansion Application	
	5. Kuparuk River Unit Tarn Participating Area Exhibit C	
	6. Kuparuk River Unit Tarn Participating Area Exhibit D	

I. BACKGROUND

Effective July 2, 1998, the Division approved the Sixth Expansion of the Kuparuk River Unit and Formation of the Tarn Participating Area, which required the inclusion of the expansion leases in a participating area within five years of the effective date of the expansion--July 2, 2003.

In a June 25, 2003, letter, the State of Alaska Department of Natural Resources (DNR), Division of Oil and Gas (Division), issued the Automatic Contraction of the Tarn Participating Area (TPA) and Associated Contraction of the Kuparuk River Unit (KRU), which contracted the KRU boundary and the TPA boundary, but deferred the contraction of portions of three of the TPA leases, designated as Expansion Areas 1, 2, & 3, described below.

That letter discussed the automatic contraction of the KRU, and ADLs 375073, 375077, 375078, 375079, 375080, 373111, which the KRU Operator, ConocoPhillips Alaska, Inc. (CPAI) had requested for continued inclusion in the KRU, but omitted reference to two other leases also subject to possible automatic contraction: ADLs 375074 and 375079. ADL 375074 was committed in part to the TPA. On July 2, 2003, the Division issued the Correction for the Automatic Contraction of the Tarn Participating Area and Associated Contraction of the Kuparuk River Unit (July 2, 2003, Correction), which included reference to the two leases (Attachment 1).

In that Correction, the Division deferred the automatic contraction of ADL 375074, as well as the other leases, until September 1, 2003, and in an August 27, 2003, letter, CPAI again requested extension. The Division deferred the contraction of the leases to January 29, 2004. Effective January 30, 2004, the portions of ADL 375074 not committed to the TPA contracted from the TPA and the KRU and the other leases contracted from the KRU.

The terms of the July 2, 2003, Correction required CPAI to drill two wells in Expansion Area 1 by July 1, 2005, and one well in both Expansion Area 2 and Expansion Area 3 by July 1, 2006. If the wells were not drilled by the commitment dates in the locations specified, the relevant Expansion Areas would contract from the TPA. Although the acreage would contract from the TPA, none of the acreage in the Expansion Areas would contract from the KRU because all the leases were already partially committed to the KRU Kuparuk Participating Area (KPA) and the TPA.

Expansion Area 1:

Tract 90	ADL 25603 (T10N, R8E, UM, Section 19)
Tract 95	ADL 25608 (T10N, R8E, UM, Section 30)

Expansion Area 2:

Tract 134	ADL 380053 (T10N, R7 E, UM, Secs 25, SE/4, 36 NE/4)
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Expansion Area 3:

Tract 134	ADL 380053 (T10N, R7 E, UM, Secs 35, SE/4, 36, SW/4,)
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On May 12, 2005, CPAI requested extension of the Expansion Area 1 well commitment deadline, from July 1, 2005 until July 1, 2006. The Division granted the extension as requested in a May 17, 2005, letter (Attachment 2).

In a June 13, 2006, letter, CPAI requested extension of the drilling commitment deadlines for Expansion Areas 1, 2, & 3. On June 28, 2006, the Division deferred the contraction to July 1, 2007, and, if submitted prior to July 1, 2007, allowed consideration of requests for portions of the Expansion Areas to remain committed to the TPA (Attachment 3).

II. APPLICATION

The Division received “The Application for the Modification of the Tarn Participating Area” (Application) on June 29, 2007. The Application (Attachment 4) requested a deferment of the automatic contraction, inclusion of a portion of the Expansion Areas (Deferment Acreage) in the TPA, and the expansion of the TPA to include additional acreage (Expansion Acreage). The Application does not address the eastern half of Expansion Area 1 and the southern half of Expansion Area 2, which are both subject to automatic contraction.

Deferment Acreage

Expansion Area 1:

Tract 90 ADL 25603 (T 10N, R 8E, UM, Section 19, W/2)

Tract 95 ADL 25608 (T 10N, R 8E, UM, Section 30, W/2)

Expansion Area 2:

Tract 134 ADL 380053 (T 10N, R 7E, UM, Section 25, SE/4)

Expansion Area 3:

Tract 134 ADL 380053 (T 10N, R 7E, UM, Sections 35,
SE/4 and 36, SW/4)

Expansion Acreage

Tract 131 ADL 380051 (T 10N, R 7E, UM, Section 13, S/2)

Tract 90 ADL 25603 (T 10N, R 8E, UM, Section 18, SW/4)

Although CPAI did not drill the wells required in the July 2, 2003, Correction, the Application requests that the Division include portions of the acreage due to automatically contract, (Deferment Acreage) and expand the TPA based upon Section 6.2 of the Kuparuk River Unit Agreement (KRUA)

a participating area may be expanded or contracted from time to time by the Unit Operator with the approval of the Working Interest Owners and of the Commissioner whenever expansion or contraction is warranted on the basis of further drilling or otherwise[.]

and 11 AAC. 351(c)

[a] participating area must be expanded to include acreage reasonably known to be underlain by hydrocarbons and known or 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.

For the purposes of this Decision, the Deferment Acreage and the Expansion Acreage will be collectively referred to as the TPA Expansion Acreage and this Decision considered an expansion of the TPA.

CPAI submitted confidential geotechnical, engineering, and economic data to support the Application. In a September 12, 2007, letter, the Division notified CPAI that the data submitted with the Application had been reviewed and that the Application warranted further discussion. The Division met with CPAI for a confidential technological work session on October 9, 2007, in order to discuss questions and better understand the work CPAI had completed in the TPA which formed the basis for the deferment and expansion request.

As a result of these discussions, the Division recommended a revision to the acreage for which CPAI had requested expansion. The Division recommended that the TPA expand to also include the southern half of Expansion Area 2. CPAI concurred and on November 27, 2007, submitted a revised Exhibit C for the Application. All of Expansion Area 2 would be included in the TPA.

Revised Expansion Area 2:

Tract 134 ADL 380053 (T 10N, R 7E, UM, Section 25, SE/4,
Section 36, NE/4)

III. DISCUSSION OF DECISION CRITERIA

The DNR Commissioner (Commissioner) reviews applications related to units, including unit contraction and participating area expansion, under 11 AAC 83.303-11 AAC 83.395. By memorandum dated September 30, 1999, the Commissioner approved a revision of Department Order 003 and delegated this authority to the Division Director. The Division's review of the Application is based on the criteria set out in 11 AAC 83.303 (a), (b) and (c). Subsection (c), paragraph (4), directs the Commissioner to consider the criteria in subsections (a) and (b) when evaluating a PA. A discussion of the subsection (b) criteria, as they apply to the Application, is set out directly below, followed by a discussion of the subsection (a) criteria.

A. Decision Criteria considered under 11 AAC 83.303(b)

1. The Environmental Costs and Benefits of the Expansion of the TPA

Approval of the TPA expansion has no direct environmental impact. This Decision is an administrative action and does not authorize any on-the-ground activity. Potential effects on the environment are analyzed when permits to conduct exploration or development in the unit area are reviewed. Approval of this expansion does not convey any authority to conduct any operations on the surface within the KRU. DNR considered environmental issues in the lease sale process, the initial KRU unitization and TPA formation process, and the unit plan of operations, exploration, and development approval processes. This Decision simply approves additional acreage for an existing PA for which there is an approved plan of operations and development and any environmental costs associated with this expansion are outweighed by the benefits of producing oil and gas from the existing TPA infrastructure.

2. The Geological and Engineering Characteristics of the TPA Expansion Area

a. Exploration History

Exploration activity in the area began with the drilling of the Bermuda #1 well (KRU 36 10-7/1) in 1991 followed by the Tarn 1 well in 1992. A 3-D seismic survey was acquired over the area in early 1996. Interpretation of the data led to the drilling of the Tarn 2, Tarn 3, Tarn 3a, and Tarn 4 delineation wells in the 1996/1997 winter drilling season. The 10-day cased-hole production test in the Tarn 2 well confirmed the discovery of a Brookian oil reservoir. This test yielded an average, post fracture-stimulated flow rate of 1900 bpd of 37 degree API gravity oil from the perforated interval between 5488 - 5572 feet measured depth (md). Additional 3-D seismic data was acquired to the north and south of the Tarn Discovery area during the winters of 1996/1997 and 1997/1998.

b. Characteristics of the Reservoir

The TPA is situated in the southwest part of the Kuparuk River Field. The Late Cretaceous Tarn Sands are comprised of five sequences of Cenomanian-aged marine sandstone of the Seabee Formation that contain inter-bedded sandstones, siltstones, and mudstones with similar lithologic and fluid characteristics. These five intervals are informally named from oldest (deepest) to youngest (shallowest): C- 30, Bermuda, Caim, Arete, and Iceberg. The type section of the Tarn field is defined in the AOGCC Pool Rules from the stratigraphic interval between 4376 feet and 5990 feet measured depth (md) in the Berumda #1 well (KRU 36 10-7/1). The sequences were deposited from mud-rich to mixed sediment and sand-rich Brookian sources as confined and unconfined deep-water slope-apron turbidite deposits along the base of slope in the Brooks Range foreland basin. At maximum sea level low-stand, slope gullies are thought to have fed multiple slope apron systems. Distribution of reservoir sand within the Tarn Sands is complex, with highly variable gross sand percentages within each interval. Hydrocarbon distribution is controlled by sand distribution.

Reservoir sandstones within the Bermuda interval consists of very fine, to fine-grained, moderately, to well-sorted litharenites with the average framework grain composition of Q₁₀F₁₀L₈₀. The lithic component is composed of sedimentary, igneous and metamorphic rock fragments L_{S40}L_{V20}L_{M40}. Significant amounts of zeolite in the form of analcime resulting from diagenetic alteration of pyroclastic volcanic glass is also present. Clay content is high, ranging between 15 and 25 percent, and occurs primarily within the lithic framework grains. Porosity ranges from 18 to 27 percent, averages 21 percent, with common microporosity. Air permeability ranges from 1 to 45 md and averages 10 md. The Tarn structure is a homocline, with easterly dip ranging up to four degrees. Few faults have been identified within the reservoir.

The lithic nature of the reservoir presents unique challenges to petrophysical log analysis and the identification of reservoir quality sands. The variable mineralogy and physical characteristics of the lithic fraction are complicating factors, as is the low density analcime. Grain densities vary from 2.52-2.78 g/cc and largely reflect the distribution of analcime and lithic grains. Petrologic data combined with routine core analyses has proven crucial for developing a petrophysical log model for estimating rock properties such as porosity, permeability and saturation, even then, limits in log resolution of thin, inter-bedded sands can make log analyses challenging.

c. Current TPA Production

Development and production from the Tarn oil pool has been limited to reservoir sands within the Bermuda interval. The other potential reservoir intervals in the pool have not yet been shown to be productive. The TPA development has thus far been limited to that area of the Bermuda interval deemed to be productive. In 1998, estimated original oil in place (OOIP) for the Bermuda interval was 80 – 250 million barrels of oil (MMBO), with an expected value of 136 MMBO. Recoverable reserves were estimated to be approximately 43 MMBO. As of December 31, 2006, CPAI had drilled 45 wells from two drillsites (DS 2L and 2N) in the Tarn PA. Production started in 1998. After a short period of primary depletion, water alternating miscible gas injection started in July 1999. A 20 percent pore volume of miscible injectant followed by lean gas to recover the mobilized oil and miscible products. Through November 2007, 107 MMSTB water and 150 MMSCF miscible gas have been injected. Production from Tarn has been better than originally anticipated. As of November 30, 2007, 85.5 MMBO has been produced from the Bermuda interval. Average daily production in November 2007 was 14,912 barrels of oil per day (BOPD). Peak production in 2003 averaged 33,842 BOPD. Estimated ultimate recovery as of 2007 will be 121 million STB based on production performance (2007 DOG Annual Report).

d. Recent Tarn Reservoir Development

In recent years CPAI has adopted a phased approach in stepping out to delineate the distal portions of the Bermuda interval. During the period January 1, 2006 through November 30, 2007, CPAI drilled 10 development wells in the Tarn reservoir. Many of the wells targeted thinner, distal lobes previously assessed to be uneconomic. This

included twinning of wellbores drilled during initial development, which were thought to be non-productive based upon the petrophysical logs and subsequently sidetracked back towards the core area of the field. By stepping out in a phased approach, CPAI was able to maximize production while gathering the data needed to calibrate the well results to their seismic data and reservoir models.

e. Conclusions

CPAI requested the inclusion of a portion of the Expansion Areas in the TPA, as well as additional acreage (Attachment 4). The portions of the Expansion Areas included in the Application consist of the western half of Area 1, the northern half of Area 2, and all of Area 3. The portions of the Expansion Areas not included in the application will be subject to automatic contraction.

Although CPAI did not drill the wells within the Expansion Areas required to avoid the automatic contraction of the Expansion Areas from the TPA, two wells, 2L-309 and 2N-310, were drilled within a few hundred feet of those areas. In a letter dated July 28, 2006, (Attachment 3), the Division stated that it would consider including all or portions of the Expansion Areas if information from existing adjacent wells justified the inclusion of those areas in the TPA.

The results of recent wells drilled by CPAI, including those adjacent to the Expansion Areas, demonstrate that thinner sands along the distal flanks of the field are capable of producing in payable quantities. In addition, during work sessions as part of the Plan of Development (POD) and Application process, CPAI shared confidential interpretive data with the Division that reasonably indicate that the productive sands extend onto the applied for expansion acreage. Based upon the data presented, the Division believes that the consistent application of the criteria used to define the areal extent of the TPA requires the inclusion of the southern half of Expansion Area 2 (Tract 134; ADL 380053, T10N, R7E, UM, Section 36, NE/4) in the TPA as part of the expansion.

3. The Further Plans of Development for the TPA

The Division approved the 2007 KRU POD for the period August 1, 2007 through July 31, 2008. As of December 31, 2006, CPAI had drilled 45 wells from two drillsites (DS 2L and 2N) in the TPA. During the period January 1, 2006 through November 30, 2007, CPAI drilled 10 development wells in the Tarn reservoir, including the 2L-309 and 2N-310 wells drilled within a ¼ mile of the expansion areas. Based upon the recent drilling results, CPAI is updating the Tarn geologic model to refine the history match of the reservoir model. CPAI acquired six leases adjacent to the TPA for evaluation. For the 2007 POD, CPAI plans to continue infill drilling with eight possible wells under consideration, contingent upon data obtained from current completions. Veritas DGC Land Inc. has applied for a permit from the State to acquire a 200 square mile 3-D seismic survey for CPAI over the Tarn Field and adjacent acreage during the 2007/2008 winter season.

The State will benefit from CPAI's further POD, which proposes to maximize the physical recovery of hydrocarbons from the Tarn. Increased hydrocarbon production will enhance the State's long-term royalty and tax revenues.

4. The Economic Costs and Benefits to the State and Other Relevant Factors

CPAI submitted tract participation schedules for the individual tracts in the TPA (Attachments 5 and 6) as required under 11 AAC 83.371. The proposed allocation distributes expenses and production among the tracts in the PA on a surface acreage basis. The PA is defined by the surface acreage covering the anticipated productive area. CPAI also submitted confidential paying quantities calculations demonstrating that the Expansion Acreage is reasonably capable of producing hydrocarbons in paying quantities, as required under 11 AAC 83.351(c).

The Division finds CPAI's tract participation schedules acceptable for allocating production and costs among the tracts in the TPA. CPAI shall work with the Division's Royalty Accounting Section to submit royalty and operator reports to properly allocate the production from the PA.

CPAI has allocated production from wells drilled to date within the TPA to the TPA. The 2L-319 was the only well drilled outside the existing TPA boundary and production from that well was assigned account code KU21. Account code KU21, approved for production from the 2L-319 tract operation, acreage now committed to the expanded TPA, will be discontinued and CPAI shall report all of the production from the TPA using the TPA production accounting code.

B. Decision Criteria considered under 11 AAC 83.303(a)

1. Promote the Conservation of All Natural Resources

The unitization of oil and gas reservoirs and the formation and expansion of participating areas within unit areas to develop hydrocarbon-bearing reservoirs are well-accepted means of hydrocarbon conservation. The TPA expansion conserves natural resources by increasing hydrocarbon production without substantially increasing the facilities required to accommodate that additional production. This expansion of an existing participating area promotes efficient evaluation and development of the State's resources, yet minimizes impacts to the area's cultural, biological, and environmental resources.

2. The Prevention of Economic and Physical Waste

This proposed expansion prevents economic and physical waste within the KRU. CPAI has submitted tract allocation schedules which allocate costs and revenues equitably between the Working Interest Owners (WIO). All of the leases retain a 12.5% royalty rate and the ownership of the Tarn interval within the expanded TPA is aligned as follows:

ConocoPhillips Alaska, Inc.	55.402367%
BP Exploration (Alaska) Inc.	39.282233%
Union Oil Company of California	4.95060%
ExxonMobil Alaska Production, Inc.	0.364800 %

Alignment of interest in a PA prevents competition amongst leases with differing ownership interests that may inhibit maximum efficiency in the development of the leases as a single reservoir. And, TPA expansion will contribute to the optimization of KRU processing facilities.

Approval of the TPA expansion and associated field development will provide economic benefits to the State. The long-term goal is to maximize the physical and economic recovery of hydrocarbons from each of the productive reservoirs. Maximum hydrocarbon recovery will enhance the State's long-term royalty and tax revenue stream. Any additional administrative burdens associated with the PA expansion are outweighed by the additional royalty and tax benefits derived from production.

3. The Protection of All Parties of Interest, Including the State

The TPA expansion protects the economic interests of the WIOs and the royalty owner. The expansion promotes the State's economic interests because hydrocarbon recovery will be maximized and additional production-based revenue will be derived from the increased production.

IV. FINDINGS AND DECISION

Considering the facts discussed in this Decision and the administrative record, I hereby make findings and impose conditions as follows.

1. The geological and engineering data that CPAI provided reasonably justify the inclusion of the TPA Expansion Acreage under the terms of the applicable regulations governing formation, expansion, and operation of oil and gas units and participating areas (11 AAC 83.301 – 11 AAC 83.395) and the terms and conditions under which these lands were leased from the State.
2. CPAI submitted confidential geotechnical, engineering, and economic data that justifies the TPA expansion and the resolution of the automatic contraction provisions. The TPA Expansion Acreage proposed for inclusion is underlain by hydrocarbons and reasonably estimated to be capable of production or contributing to production in sufficient quantities to justify the expansion of the TPA, retroactively effective July 1, 2007 .
3. The production of hydrocarbons through the existing production and processing facilities reduces the environmental impact of the additional production. Using

existing facilities will avoid unnecessary duplication of development efforts on and beneath the surface.

4. The TPA is stratigraphically limited to the Tarn Sands defined by the AOGCC in the Tarn Pool Rules as being from 4,376 MD to 5,990 MD in the ARCO Bermuda #1 Well.
5. The Accounting Unit Code KU21 is closed, effective July 1, 2007. TPA production will continue to be reported to the KUTR production Accounting Unit code.
6. This TPA expansion provides for the equitable division of costs and an equitable allocation of produced hydrocarbons under a POD designed to maximize physical and economic recovery from the reservoirs within the approved participating area.
7. The allocations of production and costs for the tracts within the TPA are approved, as submitted.
8. The aerial extent of the Tarn PA is revised as follows:

Acreage that automatically contracts from the Tarn PA under the July 2, 2003, Correction:

Tract 90	ADL 25603 (T 10N, R 8E, UM, Section 19, E/2)
Tract 95	ADL 25608 (T 10N, R 8E, UM, Section 30, E/2)

Acreage included in Expanded Tarn PA:

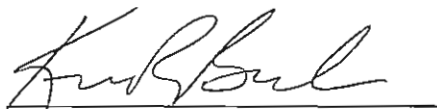
Tract 131	ADL 380051 (T 10N, R 7E, UM, Section 13, S/2)
Tract 90	ADL 25603 (T 10N, R 8E, UM, Section 18, SW/4)

9. CPAI shall submit revised KRUA Exhibits C and D within sixty days of the issuance of this Decision.

For the reasons discussed in this Findings and Decision, I hereby approve the TPA Expansion and the tract allocation schedules subject to the conditions set out above.

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 Tom Irwin, Commissioner, DNR, 550 W. 7th avenue, Suite 1400, Anchorage, Alaska 99501; faxed to 1-907-269-8918, or sent by electronic mail to dnr.appeals@alaska.gov. This decision takes effect immediately. 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.

If you have any questions regarding this decision, contact Temple Davidson with the Division at 907-269-8784.



Kevin R. Banks,
Acting Director
Division of Oil and Gas

7/12/08

Date

Cc: Jeff Landry, Department of Law

Attachments:

1. July 2, 2003 Automatic Contraction of the TPA
2. May 2005, Extension request and Approval
3. June 2006 Extension request and Approval
4. June 2007 Kuparuk River Unit Tarn Participating Expansion Application
5. Kuparuk River Unit Tarn Participating Area Exhibit C
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