



THE STATE
of **ALASKA**
GOVERNOR BILL WALKER

Department of Natural Resources

DIVISION OF OIL & GAS

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CERTIFIED MAIL
RETURN SERVICE REQUESTED

Cory E. Quarles
Vice President
ExxonMobil Alaska Production Inc.
P.O. Box 196601
Anchorage, AK 99519-6601

Re: PTU IPS POD Approval and Expansion Project Planning POD Denial

Dear Mr. Quarles:

ExxonMobil Alaska Production Inc. (Exxon) submitted to the Department of Natural Resources, Division of Oil and Gas (Division), a Point Thomson Unit (PTU) Plan of Development (POD) on June 30, 2017 to (1) provide a new POD for the Initial Production System (IPS), which expires September 29, 2017; and (2) provide an Expansion Project Planning POD, as required by Paragraph 4.6.2 of the March 29, 2012 PTU Settlement Agreement. Exxon provided additional information during a July 12, 2017 technical meeting with the Division. Exxon also submitted an earlier update on the IPS on March 1, 2017. As discussed below, the Division approves the IPS POD but finds that the Expansion Project Planning POD is inconsistent with the Settlement Agreement and on that basis denies it. If Exxon submits a revised Expansion Project Planning POD on or before October 13, 2017, the Division will review it and determine if it is consistent with the Settlement Agreement.

IPS POD

The current IPS POD is set forth in Paragraphs 4.1.1 through 4.1.4 of the Settlement Agreement, with an expiration date of May 1, 2017. The Division extended the POD until September 29, 2017. The POD period thus ran from March 29, 2012 until September 29, 2017. During this POD period The PTU working interest owners (WIOs) agreed to:

- Bring the PTU 15 and PTU 16 wells into production and “Continuous Operation” by May 1, 2016 using the IPS. The Settlement Agreement defines Continuous Operation as continuing operation of wells and facilities except for maintenance or repairs, operational upsets, or circumstances beyond the WIOs’ control.
- Sustain production of at least 10,000 barrels of condensate per day and drill and place additional wells on production as necessary to maintain this rate of production.
- Identify and pursue debottlenecking work to increase capacity at the facilities.
- Drill a well from the West Pad targeting Thomson Sand by May 1, 2016.

- Continue obtaining permits for the East Pad, an East Pad well targeting Thomson Sand, and one additional well targeting Thomson Sand.

The State interprets the Settlement Agreement as setting forth the existing POD only. The Settlement Agreement further describes specific Future PODs for Major Gas Sale Sanction, Expansion Project Planning, and Expansion Project Commitment. For the IPS, though, the Settlement Agreement does not address PODs after the expiration of the 2012–2017 POD. The agreement allows for the IPS POD to be included in the same document as a future POD, but does not otherwise address subsequent IPS PODs. Thus, this portion of the proposed POD is governed by the unit agreement and the regulations, not the Settlement Agreement. This is significant because 11 AAC 83.343(c) provides for an operator to deviate from a prior POD; the Settlement Agreement, as a contract, does not. Thus, the Division considered Exxon's failure to satisfy exact terms of this portion of the Settlement Agreement as POD deviations under 11 AAC 83.343(c) rather than contractual breaches.

Exxon drilled the wells identified in the Settlement Agreement, but did not meet its production obligations. Exxon reports that it drilled PTU 17 from the West Pad and brought PTU 15, PTU 16, and PTU 17 into production and Continuous Operation. Exxon further states that production has reached or exceeded a rate of 10,000 barrels of condensate. Production data shows, however, that while there have been individual days that have reached this rate, the average daily production rate has fallen short of the agreed 10,000 barrels per day. Exxon stated in its POD that production was impacted by difficulties with its gas injection compressor. During the technical meeting, Exxon provided additional detail about the compressor and its design flaws and difficulties in relation to this reservoir. By Exxon's account, it was conducting maintenance or repairs on the compressor during periods when production ceased or decreased. Thus, the interruptions in production do not appear to be breaks in "Continuous Operations," as defined by the Settlement Agreement. Exxon has struggled to sustain production of at least 10,000 barrels per day, as specified in Paragraph 4.1.1.2 of the Settlement Agreement. The Division is hopeful that Exxon will belatedly achieve the 10,000 barrels per day after further refinement of the compressor system.

Exxon acknowledged that the Settlement Agreement required it to identify and pursue debottlenecking work, but did not identify any such work completed during the prior POD period. Exxon's efforts to resolve issues with its compressor could be considered debottlenecking, but the Settlement Agreement requires Exxon to identify and pursue debottlenecking work that would increase capacity at its facilities. Exxon described its efforts to use existing capacity by fixing its compressor, not work to increase the facility's capacity. Thus, based on the information Exxon provided in the POD and at the technical meeting, Exxon did not "identify and pursue debottlenecking work to increase the capacity of the installed facilities," as specified in Paragraph 4.1.1.4 of the Settlement Agreement.

The proposed POD does not address permitting for the East Pad, an East Pad well, or any additional wells. Exxon had already applied for an EIS at the time of the Settlement Agreement, and shortly thereafter submitted a Plan of Operations that included the East Pad. But the Division is unaware of any efforts by Exxon to further permit the East Pad, an East Pad well, or an additional well. The 2012 Plan of Operations alone does not constitute a continued effort to permit during the 2012–2017 POD period. Thus, based on the information it provided, Exxon

has not fulfilled its obligation to continue permitting the East Pad, an East Pad well and an additional well, as specified in Paragraph 4.1.3 of the Settlement Agreement.

For the next POD period, Exxon states that it plans to continue operating the IPS facilities and that it will evaluate opportunities to optimize operating variables. Exxon does not plan any additional drilling for the POD period. In addition, the February IPS update represented that Exxon has completed all drilling for the IPS and included no mention of an East Pad well or additional well. The proposed POD also states that Exxon will consider debottlenecking work in the 2017–2019 POD period.

With the IPS POD set forth in the Settlement Agreement expiring, this IPS POD is governed by the PTU Unit Agreement and applicable regulations. When considering a POD, the Division considers the public interest, conservation of natural resources, prevention of economic and physical waste, protection of all interested parties, including the State, environmental costs and benefits, geological and engineering characteristics or reservoirs or potential hydrocarbon accumulations, prior exploration activities, plans for exploration or development, economic costs and benefits to the state, and any other relevant factors, including mitigation measures. 11 AAC 83.303(a), (b).

Continued operation of the IPS facilities benefits the State through production of the State's resources. This production has so far been minimal and sporadic. Exxon's explanation of difficulties with its compressor, however, suggest that it may have resolved many of those issues.

The Division is concerned about the Settlement Agreement requirements for the 2012–2017 POD period that Exxon did not fulfill: sustaining 10,000 barrel per day production, identifying and pursuing debottlenecking work to increase capacity, and continuing to permit the East Pad, an East Pad well, and an additional well. The Division is additionally concerned that while the proposed IPS POD does not include any plans to complete the permitting obligation. Exxon did provide an extensive explanation of its problems with the compressor and the Division remains hopeful that those problems are now resolved and that Exxon will soon meet its production rate obligation. The Division also appreciates that Exxon included consideration of debottlenecking work in the proposed POD.

While the Division remains concerned about the future of the IPS, the proposed POD does provide for continued production, which is a benefit to the State. Unitized production like this generally conserves resources, minimizes environmental impacts, and prevents waste. The proposed POD does not create additional impacts to the land. Thus, despite the Division's continued concerns, the Division hereby approves the IPS POD for the period September 30, 2017 through December 31, 2019. The next POD is due 90 days before this POD expires, on or before October 2, 2019.

The Settlement Agreement deviates from the administrative appeal process set forth in statute and regulations for disputes regarding a "Future POD," but does not specify an alternative process for an IPS POD. Even though Exxon submitted its IPS POD and Expansion Project Planning POD in the same document, the IPS and Expansion Project are separate projects with separate plans. Thus, the State interprets the Settlement Agreement as being silent as to the administrative appeal process for an IPS POD, leaving it governed by DNR statutes and

regulations. An appeal by a party who is not subject to the Settlement Agreement would also be governed by the jurisdictional statute and procedural regulations for DNR appeals.

Per the regulations, 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 Andrew T. Mack, 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@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.

Expansion Project Planning POD

Paragraph 4.6.2 of the Settlement Agreement states that the WIOs “must begin engineering and permitting of a Point Thomson Expansion Project” and submit an Expansion Project Planning POD “that includes work plans for evaluation and selection of an option for development of the Point Thomson Reservoir through a Point Thomson Expansion Project.” This POD must include plans to address (1) data acquisition and technical evaluations and qualifications to support the development plan; (2) well planning, including identification of the number, location, and completion plans for wells; (3) the project design basis and engineering plans for infrastructure, pads, and processing facilities; (4) acquisition of permits and other approvals; (5) operation and maintenance considerations; (6) construction and start-up, including estimated completion times; (7) logistics; and (8) safety, security, health, and environmental considerations.

Exxon’s Expansion Project Planning POD discusses a potential expansion to the IPS facilities and infrastructure to increase production to more than 50,000 barrels per day of condensate to transport through TAPS and 920 million standard cubic feet per day of gas to inject into the Prudhoe Bay Unit (PBU). As part of this project, Exxon would drill two new production wells from the Central Pad, drill a disposal well, and convert PTU 15 and PTU 16 from injectors to producers. Exxon set forth five activities for the 2017–2019 Expansion Project Planning POD period:

- Negotiate a commercial agreement to inject gas into PBU.
- Discuss technical alignment and scope with the PBU WIOs.
- Front End Engineering Design (FEED) planning and execution.
- Develop applications for federal and state permits.
- Prepare unspecified “deliverables.”

The proposed POD further states that until the WIOs enter a commercial agreement with the PBU WIOs, there will be no funding for any planning work. Exxon reiterated during the technical meeting that it will not move forward with any expansion planning work until the PTU WIOs enter an agreement with the PBU WIOs. Exxon further explained that it has not even approached the Prudhoe WIOs to begin these discussions, but surmised that the PBU WIOs were

aware of the need for an agreement. Exxon, BP Exploration (Alaska) Inc., and ConocoPhillips Alaska, Inc. collectively own 99 percent of the working interest in both PTU and PBU. These entities do not own the same interest in both units, but, by and large, the PBU WIOs are the PTU WIOs. More importantly, this potential commercial agreement is not part of the Settlement Agreement obligations for the Expansion Project Planning POD, nor would the lack of an agreement prohibit Exxon from moving forward with planning work. The Division understands that a commercial agreement is important to the PTU WIOs, but it is not itself an impediment to Exxon fulfilling its obligations under the Settlement Agreement.

An agreement to inject gas into PBU is not Exxon's only condition. The POD conditions all FEED work—the work that the Settlement Agreement requires the PTU WIOs to conduct during this POD period—on whether the WIOs decide to fund the work. Exxon prefaces its discussion of FEED by stating, “[i]f funded, FEED would progress...” and then proceeds to refer to activities it “would” do, rather than activities it *will* do. The Division questioned Exxon about this language to determine if it was intentional or merely inartful drafting. Exxon confirmed at the technical meeting that the WIOs did not intend to proceed with any Expansion Project Planning work unless they both decide to fund the work and enter a commercial agreement for PBU injection. Again, the Division understands the importance the commercial agreement, but it is not an impediment to complying with the Settlement Agreement.

Conditioning the planning work on commercial negotiations and a decision to fund is directly contrary to the WIOs contractual obligations under the Settlement Agreement. Paragraph 4.6.2 obligates the WIOs to “begin engineering and permitting” during this POD period and to submit a POD that “includes work plans for evaluation and selection of an option for development.” Instead, Exxon submitted a POD that vaguely refers to generalized categories of tasks and commits to completing none of them. This proposed POD would allow the WIOs to decide that they would rather not pay for planning, and then Exxon would perform no work. This proposed POD would also allow the WIOs to not enter an agreement with themselves for PBU injection, and then Exxon would perform no work. In other words, after agreeing to conduct and complete planning work now, the WIOs submitted a POD that would allow them to unilaterally decide to do nothing. Because of the conditions, the POD is inconsistent with the Settlement Agreement and the best interests of the State.

Exxon's proposed POD is also inconsistent with the Settlement Agreement because it lacks the level of detail the WIOs committed to provide with this POD. For example, Paragraph 4.6.4(b) requires the POD to include “the number of drill wells, well locations, and completion plans.” The proposed POD states only that “[t]wo new production wells and one new disposal well would be drilled at Central Pad.” Exxon failed to include the bottomhole locations of these potential wells or any detail about its plans for completing the wells.

Similarly, Paragraph 4.6.4(d) requires this POD to “include plans to address... acquisition of permits and other approvals to accommodate drilling, construction, production transportation, and operations.” The proposed POD merely states that Exxon's schedule includes time to prepare and file permit applications and cites one example of a permit. Scheduling time to apply for permits is not a plan for acquiring them.

Overall, the proposed POD fails to paint even the most impressionistic picture of what Exxon will do over the next year and a half to engineer and permit an expansion project. It is thus inconsistent with the Settlement Agreement.

A POD in general needs to specify an operator's plans for the coming POD period. Not work it might consider if certain events occur. Not work it might consider if it decides to fund the work. A POD needs to sets forth what an operator plans to do. Because of the Settlement Agreement, this Expansion Project Planning POD is not just a regulatory obligation, but a contractual one. To settle the PTU litigation and retain the unit, the WIOs agreed to conduct the planning work for an expansion project, starting now and completing by the end of 2019. The proposed Expansion Project Planning POD fails to provide for Exxon to fulfill this contractual obligation. The proposed POD includes conditions that would give the PTU WIOs control to avoid doing any planning work, effectively nullifying this portion of the Settlement Agreement. And even taking away these conditions, the proposed POD is so vague, it is unclear what planning work Exxon is committing to do. Thus the Division finds that this POD is inconsistent with the Settlement Agreement and contrary to the State and public interests that the Division considers when reviewing a POD. Accordingly, the Expansion Project Planning POD is denied.

It is the Division's understanding that the Settlement Agreement sought to alter DNR's administrative appeal procedures and superior court jurisdiction over challenges to DNR decisions by making a challenge to an Expansion Project Planning POD denial subject to review in the first instance in superior court. To the extent this understanding is incorrect or a person who is not party to the Settlement Agreement seeks to challenge this decision, 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 Andrew T. Mack, 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@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.

The Division interprets the Settlement Agreement as not prohibiting Exxon from submitting a revised Expansion Project Planning POD for consideration. The Division will review a revised POD if Exxon submits it on or before October 13, 2017. Per the Settlement Agreement, the Division would then have 60 days to determine if the revised POD is consistent with the Settlement Agreement and, if found consistent, the POD would have an effective date of April 2, 2017.

Sincerely,



Chantal Walsh
Director