RESOURCE review

akrdc.org

A periodic publication of the Resource Development Council for Alaska, Inc.

March 2011

Alaska's economy trumped by ACES?

The oil industry is the foundation of Alaska's economy. North Slope oil production built the $39 billion Permanent Fund, accounts for at least a third of all jobs in the state, and provides 80 to 90 percent of Alaska's unrestricted general fund revenues that pay for state government.

On the surface, the state's current fiscal position appears strong, especially compared to the other 49 states. Alaska is only one of four states with a surplus. In addition to the $39 billion Permanent Fund, Alaska has over $11 billion in its savings accounts.

Yet not all is well. In fact, across Alaska's private sector, there is growing concern – even outright alarm – about where the state's economy is heading. Fiscal analysts warn those huge reserves and the high price of oil sweep a chronic oil production decline under the rug. That decline has accelerated and could usher in the premature shut down of the Trans-Alaska Pipeline System (TAPS), leading to a catastrophic drop in state revenues.

Higher oil taxes have kept state coffers overflowing, but oil production is declining faster than anticipated and there are no new fields on the horizon beyond Eni Petroleum's 10,000 barrels per day (bpd) Nikaitchuq project which just came on line and BP's Liberty field, expected in 2013.

In an effort to attract major industry investment back to Alaska to stimulate new exploration, promote infield drilling, and stem the production decline, RDC is encouraging legislators to pass Governor Sean Parnell's HB 110, a bill that would make major revisions to the state's oil tax structure. The debate on the governor's bill is the biggest issue of the session. It has support from House leaders, but faces resistance in the Senate.

"Obviously, oil production is critical to our state's future and provides the bulk of funding for our infrastructure, education system and vital services," said Parnell. "Alaska must compete for jobs in the global context and we need to act this session to keep ourselves in the game."

With investment leaving the state for other areas, Governor Parnell warned that Alaska is close to slipping from being the country's second largest oil producing state to its fourth largest. "The more you tax, the less you get,"

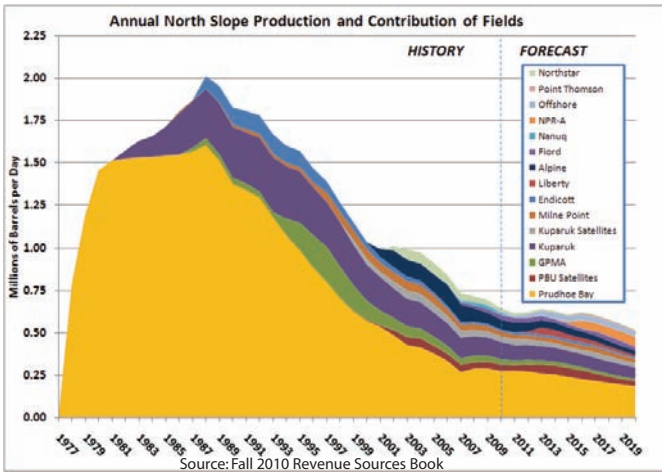
(Continued to page 4)

In this issue

Trumped by ACES	1, 4-6
Alaska Business Report Card	3
Polar bear habitat challenged	6
'Wild Land' policy denounced	7-8
Women in Resources reception	7
Shell delays Alaska OCS drilling	9
From the President	10
Industry digest	11

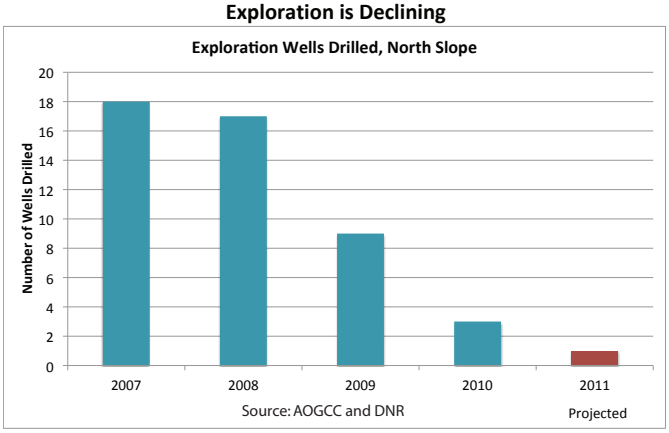
Troubling Indicators

Production is Declining



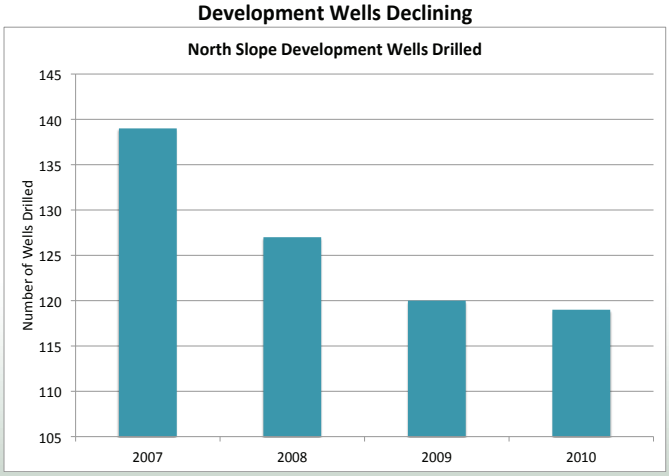
Source: Fall 2010 Revenue Sources Book

Exploration is Declining



Source: AOGCC and DNR

Development Wells Declining



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Workforce Development in Action

CH2M HILL students at the King Salmon training facility - April 2010
2009 Employer of the Year by Alaska Department of Labor and Workforce Development

Through Workforce Development CH2M HILL has been able to recruit and retain skilled labor for our North Slope jobsites, establish relationships with future clients and strengthen our alliance with our current business partners.

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The Resource Review is the official periodic publication of the Resource Development Council (RDC), Alaska's largest privately funded nonprofit economic development organization working to develop Alaska's natural resources in a responsible manner and to create a broad-based, diversified economy.

Past issues of the Resource Review (1978-2010) are available at akrdc.org.

Editor's Note: The business associations listed below will once again be developing the Alaska Business Report Card. The report card was launched last year to measure our legislators and governor on issues important to Alaska's business community. The letter was delivered to all 60 members of the Alaska Legislature last month.

The 2011 Alaska Business Report Card

alaskabusinessreportcard.com

Last year, the ***Alaska Business Report Card*** was launched. The following groups will once again be developing the report card to give their collective memberships a clear sense of how each legislator, as well as the Governor, stand up for Alaskan business:

- Alaska State Chamber of Commerce *http://www.alaskachamber.com/*
- Alaska Support Industry Alliance *http://alaskaalliance.com/*
- Associated Builders and Contractors of Alaska, Inc. *http://www.abcalaska.org/*
- Prosperity Alaska *http://www.prosperityalaska.org*
- Resource Development Council for Alaska, Inc. *http://www.akrdc.org*

Each of the participating organizations, who represent companies that employ tens of thousands of Alaskans, actively works to build a strong economy in Alaska and to ensure the state develops a policy regime that supports jobs and business. Each of our organizations will continue to work with all of our policy makers to make Alaska an attractive place for private sector investment, jobs, and economic growth.

Admittedly, the ***Alaska Business Report Card*** participants did not do a sufficient job last year of informing legislators of our process. We aim to improve our communication with legislators and at the same time, commit to disseminating the 2011 and 2012 grades to an even wider audience to ensure it is known how legislators are/are not advocating for the business community.

We will evaluate members of the 2011 Alaska State Legislature and the Governor based on their respective performances related to the priorities of Alaska's business community. Legislators will be evaluated on the following broad policy areas:

1. Fiscal Responsibility
2. Oil Tax Reform
3. Regulatory Streamlining
4. Litigation Reform
5. General Business Climate
6. Strategic Infrastructure

Letter grades will be given to legislators following the legislative session, computed through an average of each participating organization's input. Each organization will grade based upon its own specific priorities and issues. Individual grades from each organization will **not** be released.

Specific legislation considered in the grading process will be posted throughout the legislative session to *www.alaskabusinessreportcard.com* as well as on each participating organization's website. Grading will be based on:

1. Bill sponsorships
2. Committee votes
3. Floor votes
4. Actions taken in committee when applicable
5. Overall leadership in and out of the Legislature

We would be happy to discuss additional details or answer questions with you or your staff. Please contact us at info@alaskabusinessreportcard.com to set up a meeting. We look forward to working with you this session to make Alaska a better place to invest.

New investment, production trumped by ACES

(Continued from page 1)

Parnell said. "The more we tax companies for producing a commodity, the less they will produce here, and the more they will produce elsewhere."

With the highest energy taxes in the U.S. since the implementation of Alaska's Clear and Equitable Share (ACES) in November 2007, Alaska trails most of North America as an attractive place to invest capital, according to the Fraser Institute's annual study of 133 oil and gas jurisdictions worldwide. For North America, Alaska ranked 31 of 38 in overall attractiveness. Globally, Alaska ranked 68 of 133 overall. In the area of fiscal terms, a key element the state can control, Alaska ranked 34 of 38 in North America, and in a Wood MacKenzie study, Alaska's fiscal terms ranked 117 of 129 globally.

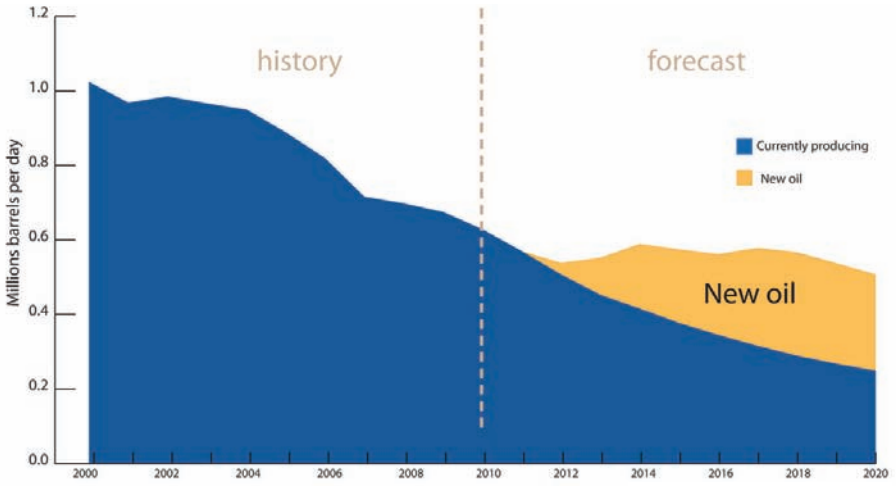
The current tax is onerous and a disincentive to invest here, investors warn, especially when oil prices are high, given the progressive surcharge which captures nearly all the upside. For example, at $100 a barrel, the government takes 71 percent of every dollar earned after operating costs. In Alberta, it's 55 percent, in the Gulf of Mexico, it's 43 percent. As a result, Alaska becomes less competitive at high oil prices, and investors turn indifferent to investing here at $70 or $120 oil.

Parnell's bill sets a lower base tax rate for areas outside of current fields to encourage new development. It also caps production taxes at 50 percent and proposes tax credits for drilling wells.

The governor said there is no denying that lower tax rates could reduce revenue flowing into state coffers in the short term, but he said it is clear Alaska is competing in a global market and in the long term this reduction will make the state a more desirable place to invest. Parnell said his objective is to grow the economy and not necessarily the state's savings accounts. "With the energy industry providing over 85 percent of our annual budget, cutting taxes will not just create jobs but, by increasing exploration and investment, will lead to greater revenue. That means money for schools, troopers, roads, and ferries," Parnell said.

Industry executives say Parnell's bill is a positive step toward encouraging the investment needed to boost oil production.

Without New Investment, Oil Production Falls More Than 50% By 2020



Source: Department of Revenue

More than 50% of total North Slope production in 2020 is forecasted to come from new oil, but most of that production will require huge investment from industry that is currently not occurring, despite high oil prices.

They warned that increased investment is flowing into other states and countries with more favorable tax regimes.

As the debate on the issue heats up in Juneau, the industry is citing new data on declining production, exploration, and well activity on the North Slope. In a presentation to RDC February 3 in Anchorage, Marilyn Crockett, Executive Director of the Alaska Oil and Gas Association, pointed out that only 119 development wells were drilled on the North Slope in 2010, compared to 142 in 2005. Development drilling is critical to sustaining production from existing fields.

Crockett also noted exploration activity has fallen sharply. According to the Alaska Department of Revenue, only three exploration wells were drilled on the North Slope in 2010, compared to 18 in 2007. Crockett noted of the three wells drilled in 2010, two were delineation wells within existing discoveries. As a result, there was only one true exploration well drilled in 2010 aimed at finding new oil, she said. Despite high oil prices, only one exploration well is anticipated for 2011 on the North Slope while nearly 170 drill rigs are active in North Dakota. ConocoPhillips, Alaska's most prolific explorer, did not drill an exploration well last year for the first time in 45 years and does not plan to drill this year.

Crockett warned the production decline on the North Slope is accelerating and reached seven percent over the last year. In Fiscal Year 2008, production fell 18,000 bpd over 2007; in 2009 the decline increased to 24,000 bpd, and in 2010 the decline accelerated to 48,000 bpd.

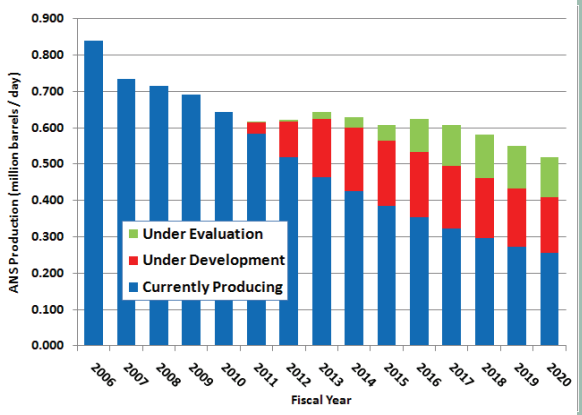
Crockett pointed out that it takes five to seven years to bring even a modest-size North Slope field on line, and with no fields in the lineup after Nikaitchuq, Liberty and the ConocoPhillips CD-5 project, which has been delayed by federal permitting issues, the state will ultimately face formidable challenges later in this decade in sustaining TAPS, Alaska's economic lifeline.

The state is projecting that more than 50 percent of total production in 2020 will come from new oil, but most of that production will require significant investment from industry that is currently not occurring.

Depending on the level of industry investment going forward, the state is forecasting oil production will fall to a range of 386,000 to 680,000 bpd in 2015 and 255,000 to 520,000 bpd in 2020.

"It is imperative the Legislature pass

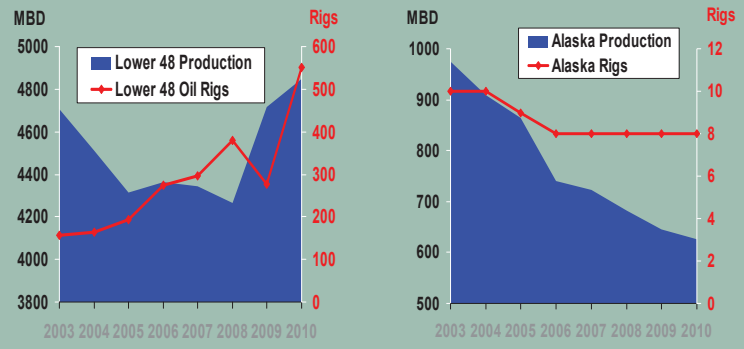
Investment Needed In New & Old Fields Alike



Source: Fall 2010 Revenue Sources Book

The state is forecasting oil production could fall to 386,000 barrels per day in 2015 and 255,000 bpd in 2020 without new investment. Significant investment is needed to stem the current and forecasted decline.

Lower 48 Oil Production Up, Alaska Down



Increased production follows increased drilling

Source: Energy Information Administration and Baker Hughes

Despite high oil prices, Alaska oil production has declined 36 percent since 2003 while Lower 48 production has increased. The rig count in the Lower 48 has risen sharply in recent years of high oil prices, but in Alaska the count has stagnated. Lower 48 production is up 3 percent since 2003 and 12 percent from 2005.

See more charts on page 6

meaningful changes this year to the petroleum tax structure," Crockett said. "The sooner the legislature acts, the earlier a recovery will take place in exploration and development activity."

RDC President Tom Maloney warned Alaska simply can't afford for the Legislature to do nothing in this session on oil production taxes. "Alaska is no longer competitive and it cannot prosper with a tax regime that hinders growth," Maloney said. "Alaskans are very concerned about the decline in production and they see taxes as too high to encourage new exploration or development in existing core fields. We must take a leap of faith now to make Alaska a compelling place for industry to invest."

Maloney emphasized there is an urgent need to slow the decline in TAPS, citing the 2010 decline of 48,000 barrels per day, which was much steeper than the state had anticipated in earlier forecasts. "The accelerated decline in throughput will turn into a terminal illness for Alaska's economy without the right medicine," Maloney said. He noted the pipeline is now running at two-thirds empty and could become uneconomic to operate within ten years.

Maloney warned that a premature shut down of TAPS would not only devastate Alaska's economy, it would also strand billions of dollars in state royalty payments, which exceeded $2 billion in 2010 alone and $46 billion over the past 50 years. "If we leave two billion barrels of oil on state land stranded, Alaska loses $22.5 billion in royalties at $90 oil. When other revenue flows are considered, Alaska could lose $90 billion in lost royalties and taxes. Without production, the state gets no royalties."

Critics of the governor's bill claim investment in the form of capital expenditures has increased since the implementation of ACES in November 2007. However, industry executives note that most of those capital expenditures went for maintenance and repairs, not projects that put new oil into the pipeline.

"There is no denying Alaskan exploration and development activity is down while other mature energy basins in the U.S. have mitigated their decline," said RDC Executive Director Jason Brune. He noted investment, exploration and development activity in North Dakota is booming and the state is on track to surpass Alaska production in several years. He also pointed out that the Lower 48 led the world in production growth in 2009, while Alaska production continued to slide.

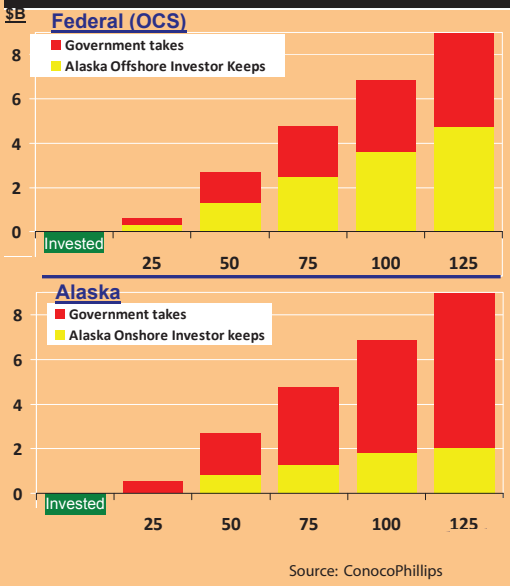
"There are still billions of barrels of oil waiting to be developed on the North Slope and offshore," Brune said. "Eni brought Nikaitchuq online in February and expects the field to produce for 30 years, peaking at 28,000 barrels per day. Alaska needs two to three fields like Nikaitchuq to come online each year just to stem the ongoing annual production decline of six to eight percent. Governor Parnell's HB110 will help encourage more exploration so more fields like Nikaitchuq are in Alaska's future."

Marc Langland, Chairman and CEO of Northrim Bank and a founding member of the Make Alaska Competitive Coalition, noted, "Alaska used to be the top oil producer in the nation and now we're number two, and soon will drop to fourth as investment dollars are bypassing Alaska for North Dakota, Alberta, Australia, and Russia." Langland added, "We don't have a lack of oil in Alaska, we have a lack of investment. We must reverse the trend and get more oil in the pipeline. Alaska is simply not competitive under ACES."

It is vital that RDC members contact their legislators in support of HB 110. See akrdc.org for a contact list of legislators, as well as member comments on HB 110.

ACES is driving away investment in new oil production

$1 Billion Investment Success Case



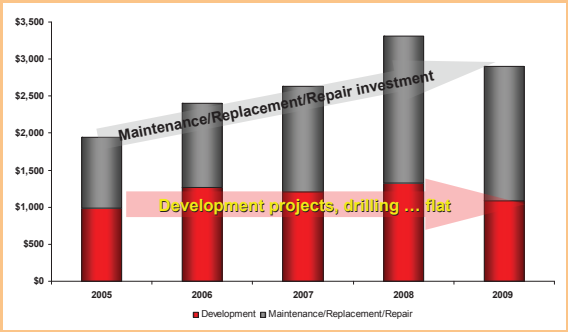
Adequate returns in success case justify up front investment risk

Alaska onshore fiscal terms: Risk / reward is out of balance

Source: ConocoPhillips

Spending on Maintenance Dominates

Prudhoe, Kuparuk, Alpine (Core fields) gross investments include capital/operating expense, $MM



At left, ACES has left the risk/reward profile for new industry investment in Alaska out of balance. Alaska's fiscal terms capture nearly all the upside at high oil prices. As a result, Alaska becomes less competitive at high oil prices, and investors turn indifferent to investing here at $70 or $120 oil. Above, most of industy's spending in recent years has been for maintenance and ongoing operations, while development projects and drilling have been flat.

Native groups may file suit over polar bear habitat

Arctic Slope Regional Corporation (ASRC), the North Slope Borough and a coalition of Alaska Native groups from the North Slope, Northwest, and Southwest Alaska have notified the Department of the Interior of their intent to sue the federal government over its decision to designate more than 187,000 square miles of land and sea ice as critical habitat for polar bears.

The plaintiffs believe the federal government broke the law when it ignored concerns of the Alaska Native community and designated an area larger than California as critical habitat for polar bears.

The letter, signed by Arctic Slope Regional Corporation, the North Slope Borough, Bering Straits Native Corporation, NANA Regional Corporation, Calista Corporation, and a number of other Native corporations was sent to the Department of the Interior last month. Federal law requires a 60-day notification before a lawsuit is officially filed. It is the coalition's hope that the Secretary of the Interior will use this time to address the plaintiffs' concerns.

"This is a poor attempt to legislate climate change through regulation," said Rex Rock, Sr., President and CEO of ASRC. "The Department has recognized that the designation will not have any impact on the primary threat to polar bears – the loss of sea ice habitat – but it could cripple our communities."

Worldwide populations of polar bears have gone from around 5,000 in the late 1960s to between 20,000 to 25,000 today.

An independent economic analysis into the critical babitat designations found the financial burden to the State of Alaska, North Slope Borough and ASRC could reach into the billions of dollars. As an example, a 1% reduction in oil production within critical habitat could lead to a loss of more than 200 jobs and nearly $100 million in output statewide. Over the past five years, an average of 85 percent of Alaska's revenue – outside of federal and investment income – has come from the oil and gas industry. Almost half of the North Slope oil production comes from an area within the critical habitat designations.

Polar bears frequently roam across the North Slope and are often seen in or near villages and towns such as Kaktovik and Barrow.

"The critical habitat designation does not get at the problem of melting sea ice, so it won't help the polar bear," said North Slope Borough Mayor Edward S. Itta. "It will only restrict normal community growth in our villages and threaten access to our traditional subsistence hunting areas. As a solution, this completely misses the mark."

Governor Sean Parnell welcomed the effort from the Native community to fight critical habitat designations. "I share the concerns of ASRC and the many other corporations that realize this designation was overreaching and improper," Governor Parnell said. "The designation will have a negative economic impact and would delay jobs, increase the costs of, or even prevent resource development projects that are crucial to Alaskans."

Last month the State of Alaska notified U.S. Interior Secretary Ken Salazar of its intent to sue over the critical habitat designation.

Governor denounces decision on Alaska 'Wild Lands'

Governor Sean Parnell expressed grave concerns about a recent decision by U.S. Interior Secretary Ken Salazar to evaluate 87 million acres of federal land in Alaska as potential 'Wild Lands.' That designation would effectively allow the federal government to create more wilderness in Alaska without congressional oversight.

In comments submitted to Salazar, Governor Parnell said Interior's wild lands designation will diminish access to federal lands and cost jobs.

"Putting such a sweeping initiative in place overnight, with no congressional direction and no advance consultation with affected states or the public, is unfathomable," Governor Parnell said. He noted that Alaska lands have been repeatedly studied, with large areas placed off-limits to resource development.

"Congress passed the Alaska National Interest Lands Conservation Act (ANILCA) of 1980, which studied public lands in Alaska and set aside 57 million acres as wilderness. Nearly every Interior secretary since ANILCA was passed has chosen not to conduct further discretionary wilderness inventories in Alaska, and has recognized the importance of a public process and discussion with state leaders. I will not allow such disregard for Alaska and its citizens to stand unchallenged."

In addition to the flawed process, the governor noted specific concerns:

• "By designating 'Wild Lands,' Order 3310 usurps congressional authority where Interior improperly acted as an administrative surrogate for congressional designations of wilderness;

See related Guest Opinion column on page 8

• "In Alaska, where most of BLM's 86 million acres retain their wilderness values, the heavily weighted default protection of wilderness characteristics could easily render most BLM lands de facto wilderness areas, absent BLM's multiple-use direction. This would have a devastating effect on Alaska's people, economy, and land use and access. Thus, the order directly conflicts with the 'no more' clauses in ANILCA and the Federal Land Policy and Management Act (FLPMA);

• "The order is, for all practical purposes, an end-run around ANILCA, which I predict will lead to egregious social and economic consequences for Alaskans. Without the explicit provisions of ANILCA that apply to conservation system units, BLM Wild Lands will likely be managed more restrictively in Alaska than ANILCA-designated wilderness managed by the National Park Service, Fish and Wildlife Service, or Forest Service;

• "The order purports to seek 'balance' between responsible resource development and protection of wilderness characteristics; yet there is a strong presumption in favor of wilderness-style protection. For that reason, this order will have a severe chilling effect on future proposals designed to create jobs in resource development once an area is designated Wild Lands. This approach also contradicts BLM's multiple-use mandate under FLPMA;

• "BLM managers' discretion to determine where and when 'impairment' of wilderness characteristics is 'appropriate' is subject to undue scrutiny and approval in Washington D.C., where decisions tend to be political and knowledge of local conditions, issues, and needs is diluted, at best; and

• "BLM has no authority whatsoever to apply this policy to the National Petroleum Reserve-Alaska because it is not subject to FLPMA."

RDC submitted comments on the Wild Lands Policy to the U.S. House Committee on Natural Resources, which held a hearing on the issue last month. See akrdc.org.

More than 50 attend Women in Resources reception in Juneau

Over 50 women attended the 7th Annual Women in Resources Reception in Juneau on February 9th. The event, hosted annually by RDC's women Board members, recognizes the women legislators and policy makers in a unique, private setting where attendees may get to know each other and talk about the issues. At top left, (from left to right) are Josie Hickel, Pebble Partnership; Senator Cathy Giessel; Lindsay Williams, Office of Senator Giessel, and Lisa Parker, Parker Horn Company. In photo at right, Representative Lindsey Holmes; Linda Leary, Carlile Transportation Systems, and Wendy Lindskoog, Alaska Railroad Corporation. The reception was sponsored by Anglo American US LLC, ARAMARK, Arctic Slope Regional Corporation, Carlile Transportation Systems, CH2M HILL, ConocoPhillips Alaska, Inc., ExxonMobil, Jade North LLC, Kinross - Ft. Knox, Lynden, Parker Horn Company, Pebble Limited Partnership, Pioneer Natural Resources Alaska, and Usibelli Coal Mine, Inc.

A 'wild' surprise from Secretary Ken Salazar

Editor's Note: This editorial originally appeared in the Fairbanks Daily News-Miner last month.

"My administration is committed to creating an unprecedented level of openness in government. We will work together to ensure the public trust and establish a system of transparency, public participation, and collaboration."

This is the opening paragraph of a memorandum signed Jan. 21, 2009, by President Barrack Obama, one day after his inauguration.

The memorandum goes on to state: "Executive departments and agencies should offer Americans increased opportunities to participate in policymaking and to provide their government with the benefits of their collective expertise and information." Many Americans applauded this as proof that "hope and change" wasn't just a beguiling campaign slogan.

Some 23 months later, on Dec. 23, 2010, Secretary of the Interior Ken Salazar unveiled a secretarial order establishing a new policy for lands managed by the Bureau of Land Management. This policy directs the BLM to inventory all lands it manages for their wilderness characteristics and creates a new classification of lands known as 'Wild Lands.'

Salazar's announcement was the first anyone outside the Department of the Interior knew about the Wild Lands policy, even though it was nearly two years in the making.

Governor Parnell's office was informed of the program only hours before it was announced. Utah Gov. Gary Herbert, whose state in 2003 reached a settlement with Interior on new wilderness study areas, was afforded a similar courtesy.

In a letter to Salazar, Governor C.L. "Butch" Otter of Idaho declared: "Without any state or public input, the Interior Department has circumvented the sovereignty of the states and the will of the public by shifting from the normal planning process of the Federal Lands Policy and Management Act (FLPMA) to one that places significant authority in the hands of non-elected federal bureaucrats."

Secretary Salazar's decision to unilaterally create and implement this policy contradicts both the President's memorandum and the Department of the Interior's own "Open Government Plan." That June 2010 plan is chock full of terms such as "citizen engagement," "collaboration," "cooperation" and "stakeholder involvement." Detailed flow charts sprinkled throughout show how the principles in the president's memorandum flow into the core mission objective of the department.

Salazar's failure to allow the American public and the governments of the 43 states in which the BLM manages lands to participate in developing this policy or provide "their collective expertise and information" calls into question the department's commitment to an open and transparent government.

One doubts Salazar would have ignored such a snub during his tenure as a U.S. senator or, prior to that, as Colorado's attorney general.

> **"If President Obama's directive calling for an open and transparent government is to be anything more than empty words, Salazar's order must be rescinded."**

The BLM manages 253 million surface acres in the United States. In Alaska, once all land conveyances are completed, the agency will manage some 75 million acres.

Under the new policy, BLM lands in Alaska will be inventoried for wilderness characteristics, even though they were withdrawn, inventoried, studied and classified during the years between the passage of the Alaska Native Claims Settlement Act in 1971 and enactment of the Alaska National Interest Lands Conservation Act in 1980.

While BLM manages none, there are 57 million acres of congressionally-designated wilderness in Alaska.

The BLM Wild Lands Policy has drawn strong reactions from all quarters. Several governors and members of Congress have questioned whether the secretary has the authority to implement the policy with its new land classification. Committee hearings are being planned. Many have proposed withholding funding for implementing the policy.

Ranchers, the oil and gas industry, the mineral industry, local governments and motorized recreational users have voiced strong objections. While many organizations applaud the policy, others feel it doesn't go far enough to protect BLM lands. Certainly, it raises an abundance of questions about the future of BLM-managed lands in Alaska.

It might be naïve, but it is not unreasonable, to believe that every substantive policy or program adopted by a federal department or agency should be subjected to some level of public review and input during its development, not afterward. What constitutes substantive is open for debate.

What is not debatable, however, is that the manner in which the BLM Wild Lands policy was conceived and put into place with no input from the affected states or the American public is insulting and unacceptable.

If President Obama's directive calling for an open and transparent government is to be anything more than empty words, Salazar's order must be rescinded.

Stan Leaphart is the executive director of the 12-member Citizens Advisory Commission on Federal Areas, which monitors federal land management actions and assists Alaskans affected by them. Administratively, the commission lies within the state Department of Natural Resources. Its website is http://dnr.alaska.gov/commis/cacfa/

Shell defers Alaska offshore exploration

While Russia is fully embracing drilling offshore in its Arctic region, exploration off Alaska's northern coast was dealt yet another set back when federal permitting uncertainty forced Shell to defer its 2011 Beaufort Sea drilling program.

The recent remand of air permits issued by the Environmental Protection Agency (EPA) was the final driver behind Shell's decision to defer drilling to the 2012 summer season.

"This is not an environmental issue," said Pete Slaiby, Vice President for Shell in Alaska, during a press briefing February 3 in Anchorage. "We have made significant and voluntary capital improvements in the air emissions technology we have applied to the entire program that will allow us to have almost no material impact on the Arctic air shed. It is an issue of processing a permit application in a timely way, now for five years."

Shell receives award for Arctic science (See page 11)

Slaiby said that as a result of Shell's inability to get needed permits from the federal government, it expects to release most of the vessels earmarked for the drilling program to other projects abroad, costing Alaskan jobs and lost economic opportunities.

The 2011 drilling program would have created about 800 jobs in Alaska alone. In addition, deferral of the program will further delay the opportunity to bring more domestic oil into production.

The EPA issued the air permit, but the agency's review board granted an appeal because of what it deemed a limited analysis by the agency of the effects of emissions from drilling ships and support vessels.

Slaiby noted Shell's program will have no impact on Alaska villages. He also pointed out that Shell has invested $15 million in its Arctic drilling assets "to put together what's really a world-class program."

Shell has invested more than $3.5 billion in exploration off Alaska's northern coast since 2005. More than $2 billion was spent on buying leases in the Chukchi Sea and over $1 billion has been spent on assets and other preparations for drilling.

Although a number of wells were drilled in the Chukchi Sea in the 1980s, proposed drilling programs under current lease planning areas have faced multi-year delays in obtaining federal permits. The Obama administration has dropped the North Aleutian Planning Area from future lease sales.

The company had hoped to drill exploration wells last year in the Chukchi Sea, but Interior Secretary Ken Salazar put a hold on all permitting in the Arctic following the Deepwater Horizon incident in the Gulf of Mexico. In October, Shell said it would focus on drilling one or two exploration wells in the Beaufort Sea during next summer's open water season, but that sharply scaled back plan was ultimately extinguished by the EPA appeals board.

Shell has stressed that Arctic drilling would be in shallow water and that the risk of a spill is minimal. It also agreed to position a second drill ship in Alaska as a safety measure, as well as having spill response vessels, equipment and personnel on site during drilling operations.

Shell's primary drilling ship has now been moved to New Zealand.

Alaska officials were furious over federal permitting delays and are concerned with declining throughput in the Trans-Alaska Pipeline, which is now running at less than one-third capacity. Alaska Governor Sean Parnell said it is unfathomable that a company could spend billions of dollars in federal leases but years later still be struggling to obtain permits.

"It's unfathomable that they cannot get an air permit after five years when they can get one in the Gulf of Mexico within months," Parnell said. "This is just another delay resulting from the federal government dragging its feet, killing jobs and making us even more reliant on oil from the Middle East and elsewhere."

Republican Senator Lisa Murkowski said the multi-year permitting delays and litigation against drilling will result in higher gasoline prices and a loss of jobs and revenue. "We talk a lot about the economy, but rarely do our actions match our rhetoric," she said. "That's unfortunate."

Democratic Senator Mark Begich also blamed the federal government for the most recent delay. "I put the blame for this squarely on the EPA and the Obama administration who have taken virtually every opportunity to block responsible development of Alaska's resources. Their foot dragging means the loss of another exploration season in Alaska, the loss of nearly 800 direct jobs, and many more indirect jobs. That doesn't count the millions of dollars in contracting that won't happen either at a time when our economy needs the investment," Begich said. "Shell has been working diligently for five years and has invested billions of dollars to meet the regulatory and permitting requirements of the federal agencies. It is shameful to see another season lost."

Begich also said that the President's own Oil Spill Commission, in its final report released last month, found a moratorium on development in the Arctic is not justified and recommended moving forward on an Arctic energy development plan.

Republican Congressman Don Young blamed the decision on "bureaucracy and an overabundance of unnecessary regulations." Young called the administration's talk about jobs as lip service and said, "Any attempt at project development is shut down by the EPA. They won't be happy until we've run all business out of the country and we're back to traveling on dirt roads in covered wagons."

Production and drilling drops significantly since ACES

Alaska enacted a huge tax increase on the oil industry in November 2007 called Alaska's Clear and Equitable Share (ACES). Although my professional background and certifications are in accounting and finance, there are tax provisions in ACES – including retroactivity and accelerating progressivity – that I have never heard of before.

The multi-billion dollar tax hike increased production taxes by 50 percent from 2007 and 350 percent from 2006, based on an oil price of $80 a barrel, and even more at $90 oil. How is North Slope production responding to Alaska's current fiscal regime?

Year	Production Decline, barrels per day (bpd)	Average Daily Production	Annual Decline
2008	-18,000	716,000 bpd	-2.5%
2009	-24,000	692,000	-3.4%
2010	-48,000	644,000	-6.9%

Could you even begin to imagine this significant decline of your personal finances?

The next question: Why is production declining? The answer is simple. Drilling is down, and one cannot get to new oil, gas or water without drilling.

Year	North Slope Exploration Wells	North Slope Development Wells	Total North Slope Wells Drilled
2007	18	139	157
2008	17	127	144
2009	9	120	129
2010	3*	119	122

**Includes two wells drilled at Point Thomson gas field. These were only considered exploration wells since the gas field is not yet in production.*

How does one stop the decline in drilling? There is only one answer and that is to DRILL! However, in my view, it is difficult to see how the punitive tax structure of ACES will encourage the oil industry to ramp up drilling in Alaska – when the government takes almost 80 cents of each additional dollar of profit earned at $90 oil.

Wall Street and other analysts have raised red flags about steadily declining oil production and its impact on the Trans-Alaska Pipeline System (TAPS), the lifeblood of Alaska's economy. The recent temporary shut down of TAPS in January sent shock waves across the nation and gave Alaskans a preview of what the future may hold. A CNBC story used the shut down to highlight the impact of declining throughput on TAPS, Alaska, and the nation.

The challenges of restarting the pipeline in extreme cold at reduced flow clearly foreshadow the line's future. Studies show that ice can form in the pipeline at a flow of 500,000 barrels a day or less, a threshold that may be breached within five years. While new investment in TAPS could help mitigate low-flow challenges, less oil in the line will hasten the day when the pipeline may be forced to shut down.

Analysts warn an accelerating TAPS throughput decline could lead to the premature shut-down of the pipeline, stranding billions of dollars in state royalty payments, which exceeded $2 billion in 2010 alone.

With a production decline of seven percent annually, TAPS could be non-functional before this decade ends. With no pipeline, Alaska would lose 90 percent of its revenue base and one-third of its private sector jobs. Considering a large portion of government jobs are supported by oil revenues, actual job losses statewide could be much higher. The ramifications to our economy would be absolutely devastating. How would the state pay for essential public services and honor long-term pension, medical, and other obligations?

The only way to keep the pipeline operating far enough into the future until potential offshore production kicks in sometime in the next decade is to encourage more development onshore. The only way to do that is to make Alaska a compelling place for industry to invest, and that is done by cutting taxes to sharply improve Alaska's competitive position, which now ranks near the bottom of the pack on a national and global basis when it comes to fiscal terms.

Governor Parnell and some members of the legislature have proposed changing ACES to boost industry investment and create jobs. The governor clearly recognizes the current tax is onerous and a disincentive to invest here, especially when oil prices are high, given the high progressive surcharge.

Some legislators want to grow the state's savings accounts as quickly as possible, convinced the production decline is irreversible. I respectfully disagree, believing the decline can be reversed. There is still a lot of oil to be produced from existing core fields on state lands on the North Slope. However, much of the remaining oil will be challenging and expensive to develop. Over the long-term, new offshore and ANWR production each have the potential to reverse the decline – if TAPS is still operating. Since 2003, the decline in production in Texas has been virtually arrested, demonstrating that mature energy regions can mitigate decline.

We need to do more than just grow the state's savings accounts because it's not about growing government, it's about growing the private sector economy. A strong private sector will do more over the long term to sustain Alaska than a fat savings account, which will never replace the oil industry. The best way to grow the economy and create new jobs is to grow the pie, rather than government cutting a bigger piece for itself of a shrinking pie. More drilling will equal more jobs and production, which in turn will extend the life of TAPS and yield additional tax and royalty revenues to the state.

Critics of the governor's plan claim capital expenditures, employment, and exploration are up since 2007. But investments primarily went up because of needed maintenance and repairs, as well as TAPS reconfiguration, Shell's offshore activities, Point Thomson, and pre-ACES sanctioned exploration and development.

With regard to employment, the January 2011 issue of Alaska Economic Trends reported average monthly employment in the oil and gas industry fell to 11,800 jobs in 2010, a loss of 1,000 over the 2009 monthly average. This represented a 7.8 percent decline, the largest drop in employment of any sector. To compound the problem, these jobs were some of the highest paying in the state. Alaska Economic Trends pointed out that industry employment leveled off in 2009 and has been drifting downward, and this decline will likely continue in 2011. It said "the outlook for the oil patch in 2011 is unclear, though it appears maintenance such as replacing pipe and old infrastructure will dominate."

Clearly, there are red flags everywhere. Consider these troubling indicators:

- Lower 48 oil production and drilling rigs have increased during recent years of high oil prices, but the number of Alaska rigs stayed about the same while production declined 36% since 2003.
- As shown in the table above, the number of exploration and development wells drilled on the North Slope have fallen since ACES.

(Continued to page 11)

Industry digest

Shell gets award for science

The Alaska SeaLife Center honored Shell Alaska with an Alaska Ocean Leadership Award during its Marine Gala, held January 16. The award was established as an annual opportunity to recognize outstanding achievements related to ocean sciences, education and resource management in Alaska.

Shell Alaska was presented the "Stewardship and Sustainability Award" – highlighting an industry initiative that demonstrates the highest commitment to sustainability of ocean resources.

"Through the efforts of Shell and its many partners, a better understanding of the Alaskan Arctic offshore is emerging, further enabling critical decision-making and responsible management of this critical resource," said Michael Macrander, Environmental Team Leader, Shell Alaska.

Since returning to Alaska in 2005, Shell has engaged in a comprehensive environmental studies program in the Arctic offshore. Shell has worked in a collaborative manner with a wide range of stakeholders, including industry partners, local, state, and federal governments, universities, and non-government organizations to share resources and facilitate a better understanding of the Arctic marine ecosystem.

Shell has taken the lead in the development and implementation of new technologies, including unmanned aerial systems, acoustic recorders, and integrated ecosystem studies to advance capacities to work in the challenging offshore environment. Shell fosters and funds such diverse research as computer assisted identification of marine mammal calls, greatly enhancing the capacity to utilize acoustic sampling technologies, satellite tagging, ice and weather forecasting and physical oceanography.

"It's an honor to be recognized by the Alaska SeaLife Center for our efforts to further our understanding of Alaska's ocean resources," said Pete Slaiby, Vice President, Shell Alaska. "Recently, Shell entered into a five-year collaborative science agreement with the North Slope Borough Mayor's office that will enable local stakeholders to pursue robust scientific programs," Slaiby said. "Shell's program of scientific study in the Arctic is far-reaching and diverse in scope and we are proud to be recognized as one of the scientific leaders in the Alaska offshore," Slaiby added.

The Alaska SeaLife Center, known for generating and sharing scientific knowledge to promote understanding of Alaska's marine ecosystems, is considered one of the most prominent cold-water rehabilitation and research centers in the world.

Eni brings Nikaitchuq online

Eni Petroleum has started production from its Nikaitchuq unit on the North Slope. Eni anticipates that the nearshore field will produce for 30 years, peaking at 28,000 barrels per day. The field is estimated to contain 220 million barrels of recoverable reserves.

Eni is in the early stages of a 52-well development project at Nikaitchuq. Twelve wells have been drilled to date with the remaining to be drilled between now and 2014. The wells are being drilled from a combination of onshore and offshore sites. Some of the extended reach wells are designed to run 4,000 feet vertically and up to 20,000 feet horizontally.

With Nikaitchuq online, Eni joins BP, ConocoPhillips and Pioneer Natural Resources as a North Slope operator.

Alaska Resource Education events set

Alaska Resource Education is currently accepting prizes for the biennial raffle and silent auction at the Alaska Miners Association convention in Juneau. The grand prize drawing of two round-trip tickets on Alaska Airlines will be March 18, 2011. To donate a prize or to view a current list of prizes, please visit akresource.org.

Save the date: The 19th Annual Coal Classic Golf Tournament will be on Wednesday, June 15, 2011. For more information, please email golf@akresource.org or call 907-276-5487.

Governor's bill will move needle and draw major investment back to Alaska...

(Continued from page 10)

• Beyond Nikaitchuq and the federal Liberty project, there are no new fields coming online in the foreseeable future to offset declining production.

• Alaska forecasts production will fall to a range of 386,000 to 680,000 bpd in 2015 and 255,000 to 520,000 bpd in 2020, depending on industry investment.

• By 2020, more than 50% of total production forecasted by the State of Alaska will come from new oil, which will require significant new investment that has not yet been committed.

• Using the historical decline trend of 7% for North Slope production, TAPS will reach a critically-low flow range by 2015, triggering operational issues.

• Acreage under lease on the North Slope has been in steady decline in recent years with the industry surrendering 1.8 million acres in 2008, 2 million acres in 2009, and 1.5 million acres in 2010.

• In North Dakota exploration is booming and oil production is up 138% since 2008. The state is expected to surpass Alaska in production later this decade.

Investors are warning us Alaska is no longer competitive. Alaska has to compete with Lower 48 opportunities, yet we have the highest energy taxes in the nation, as well as the highest capital costs.

If declining production in Alaska continues to accelerate and the state loses most, if not all, of its revenue flow from oil before this decade is out, it would have no choice but to turn to Alaska's other industries to help pay the bills. Alaskans would likely face a new state income and sales tax and much higher user fees. The state would also be forced to raid the Permanent Fund, and spend its savings accounts to meet its obligations.

We simply cannot afford to do nothing. Alaska cannot prosper with a tax regime that strangles growth. We must take a leap of faith to make Alaska a compelling place for industry to invest. It is imperative our lawmakers act now. If they do, the governor's bill, which if enacted, will move the needle and draw major investment back to our state.

Tom Maloney is a Certified Public Accountant, a Certified Management Accountant, and a Certified Financial Planner.

RESOURCE DEVELOPMENT COUNCIL

Growing Alaska Through Responsible Resource Development

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