

State of Alaska
Department of Natural Resources

COMMISSIONER'S FINDINGS and DECISION
REGARDING

Alaskan Crude Corporation (AAC) April 14, 2008, Appeal of Director's March 24, 2008, Decision denying request to toll Arctic Fortitude Unit (AFU) amended initial Plan of Exploration (POE) work obligation deadlines because of alleged force majeure; and

ACC's failure to meet May 15, 2008, POE work obligation, AFU Default, and Demand to Cure Default.

July 16, 2008

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ATTACHMENTS

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1. Introduction

On April 14, 2008, Alaskan Crude Corporation (ACC) appealed the State of Alaska Department of Natural Resources (DNR) Division of Oil and Gas (Division) Director's (Director) March 24, 2008 Decision denying ACC's request to toll its obligation, under the amended initial Plan of Exploration (POE), to move a drilling or workover rig onto the Burglin #33-1 well pad by May 15, 2008. The appeal included requests that the DNR Commissioner (Commissioner): 1) determine that AFU leases are subject to a force majeure, and; 2) grant a suspension of operations under Paragraphs 4(f) and 4(e) of the AFU leases, respectively. ACC stated that this appeal and requests were based on ACC's appeal of an Alaska Oil and Gas Conservation Commission (AOGCC) order.

On April 24, 2008 and May 5, 2008, ACC requested permission to delay its May 15, 2008 work obligation under the amended initial POE to March 31, 2009. ACC stated that it needed the delay to use its own Ideco HD 35 drilling rig and to resolve its appeal at the AOGCC.

On May 15, 2008, ACC failed to meet its work obligation under the amended initial POE. ACC did not move a drilling or workover rig onto the Burglin #33-1 well pad.

This document sets out my findings and decision on the appeal, gives notice of default for ACC's failure to meet its work obligation, and demands that ACC cure the default.

2. Summary of Decision

ACC's April 14, 2008 appeal is denied. Based on my review of this record, I find that ACC has provided no basis to change the Director's March 24, 2008, Decision. I also find no basis to determine that a force majeure exists under Paragraph 4(f) of the AFU leases or the AFU Agreement or to grant a suspension of operations under Paragraph 4(e) of the AFU leases. Thus, I affirm the Director's March 24, 2008, Decision.

ACC's submitted the April 24, 2008 and May 5, 2008 requests to defer its amended initial POE work obligations as additional material in support of the appeal under 11 AAC 02.030(d). See April 24, 2008 letter from the Commissioner to ACC acknowledging ACC's right to submit this material. The default cure set out below has the practical effect of granting ACC's requests to delay its work obligations under the amended initial POE.

This is notice of a default of the AFU under 11 AAC 83.374(b) because ACC has failed to meet its work obligation to move on rig onto the Burglin #33-1 well pad by May 15, 2008 as required under the amended initial POE. To cure the default, ACC shall complete the attached Second Plan of Exploration and Default Cure (Attachment #1 to this Findings and Decision), which is substantively identical to ACC's April 24, 2008 proposed "Second Amended Initial Plan of Exploration." If ACC fails to complete any of the obligations in the attached Second Plan of Exploration and Default Cure, then I may terminate the AFU under 11 AAC 83.374(c).

1. Background

On April 8, 2006, ACC submitted an Application to form the AFU. The Application included: 1) the AFU Agreement; 2) Exhibit A to the Agreement legally describing the AFU, its leases, and ownership interests; 3) Exhibit B to the Agreement, a map of the AFU, and; 4) Exhibit G to the AFU Agreement, a proposed initial POE, which proposed re-entry and workover of the Burglin #33-1 well to the Ivishak formation by June 30, 2007 and automatic AFU termination for non-performance of work obligations. ACC waived its procedural rights under 11 AAC 83.374.

On May 3, 2006, ACC's geology consultant submitted a letter regarding oil shows from the cored intervals in the Burglin #33-1 well. The consultant stated that there was "evidence from mud log and core material that demonstrate ample evidence that liquid hydrocarbons are present in the Burglin #33-1 well," and more specifically discussed the geology of the various formations that the well had previously penetrated.

On June 29, 2006, the Division issued a decision approving formation of the AFU, which consisted of three leases covering approximately 6,363 acres. The leases and their corresponding lease numbers, acreages, state royalty interests, lease issue dates, and lease expiration dates are shown below in Table 1.

Table 1 – AFU Lease Information

ADL	Acres	State Royalty Interest %	Lease Effective Date	Lease Expiration Date
389178	1280	12.5	7-01-1999	6-30-2006
389179	2523	12.5	7-01-1999	6-30-2006
389177	2560	12.5	7-01-1999	6-30-2006

The Division approved an initial POE, which set out a timely sequence of well testing, drilling, and exploration activities to facilitate development of and production of the AFU. ACC's first work obligation was to move a drilling or workover rig onto the Burglin #33-1 well pad and re-enter and workover the well by October 1, 2007, three months later than proposed by ACC. The initial POE work obligations also included drilling two additional wells and shooting 3-D seismic, with drilling

due to be completed by November 1, 2009. ACC agreed to the initial POE work obligations, which also provided for automatic AFU termination, and did not appeal that decision.

One year later, on June 26, 2007, ACC requested a modification of the initial POE work obligation deadline. ACC asserted that it could not meet the October 1, 2007, work obligation deadline because, “[w]inter tundra travel equipment shortages and summer tundra travel restrictions specific to my well location will not allow me to get the required work completed by October 1, 2007.” ACC requested a one-year delay, to October 1, 2008, of its obligation to move a drill rig onto the Burglin #33-1 well pad and re-enter and workover the well.

Also on June 26, 2007, the AOGCC issued a determination that “the Ugnu and West Sak formations in the Burglin #33-1 well . . . are highly unlikely to produce liquid hydrocarbons in amounts greater than 825 bopd.” The AOGCC also confirmed that the Burglin #33-1 well could not be classified as a “gas-only” well.

On June 28, 2007, the Division denied ACC’s request to modify the initial POE stating that “the initial POE was contingent on completion of an explicit development timeline because no drilling or workovers occurred during the seven-year primary term[s] of the AFU leases Failure to timely submit the appropriate application or requests to DMLW [Division of Land, Mining, and Water] does not justify relief . . . [and] the AFU was approved on June 29, 2006, which provided adequate time for scheduling winter equipment deliveries”

ACC appealed the Division’s June 28, 2007, decision to the Commissioner on July 17, 2007. ACC asserted that “the unavailability of appropriate rolligons for use by ACC this past winter season to stage its equipment at the Burglin #33-1 well pad was unprecedented It was circumstances in the rolligon market beyond the operator’s reasonable ability to foresee or control that prohibited the operator from moving equipment to the well site this past winter Summer tundra travel is not the preferred mode of operations on the North Slope. It is not the operator’s intent . . . to damage the tundra this summer.” ACC requested an oral hearing, a stay of the Director’s decision and that the Commissioner grant the modification to the initial POE to stay any effort to terminate the AFU leases during the appeal as long as rentals are paid, and that the AFU not be placed in default or terminated. The appeal alternatively requested that the Commissioner declare that a force majeure situation existed and “toll the dates” in the initial POE, or grant a suspension of operations under the leases and unit agreement with the dates to resume operations consistent with ACC’s request to the Director to modify the initial POE.

On September 28, 2007, DNR conducted a hearing on ACC’s appeal of the Division’s June 28, 2007 decision. ACC did not appear at the hearing.

On October 1, 2007, the AOGCC affirmed its June 26, 2007, determination that the Burglin #33-1 well could not be classified as a "gas-only" well and indicated that the strata above a maximum depth of 6196' are highly unlikely to produce liquid hydrocarbons to the surface in amounts greater than 600 bopd.

On October 29, 2007, the AOGCC recommended to the Alaska Department of Environmental Conservation (ADEC) a Response Planning Standard (RPS) of 115 bopd for an Ugnu formation only project.

ACC, on November 6, 2007, submitted an amended initial POE that proposed to deliver a workover rig to the Burglin #33-1 well pad by May 15, 2008 and to re-enter and workover the well by October 1, 2008. This amended initial POE would defer ACC's rig delivery work obligation from October 1, 2007 to May 15, 2008, and other work obligations commensurately. It also provided for automatic AFU termination if ACC failed to perform specific obligations. On November 7, 2007, more than four months after the AOGCC determined that the Burglin #33-1 well was not a "gas-only" well, after ACC did not meet the October 1, 2007 work obligation, and as a settlement of the ACC appeal, the Division approved the amended initial POE.

On January 4, 2008, ACC sent an e-mail to Mr. Art Copoulos, a unit manager on the Division staff responsible for the AFU, seeking advice on ACC's consultant's alleged inability to communicate with the AOGCC regarding an oil discharge prevention and contingency plan (C-Plan) for the Burglin #33-1 well in the AFU. ACC stated, in part, that this alleged inability is "delaying my ability to obtain a C-Plan and forcing work into a force majeure [sic] situation. Your thoughts please."

On January 16, 2008, Mr. Copoulos responded to ACC's e-mail stating, in part, that "[t]he Division sees no cause for delays in ACC's work obligations under the Arctic Fortitude Unit Amended initial Plan of Exploration. Your claim . . . is incorrect. ACC is in control of the process"

On February 2, 2008, ACC sent a letter to the Division captioned as an "Appeal" of Mr. Copoulos' "Decision" regarding ACC's request that the POE work obligations be tolled because of the alleged AOGCC delays.

On February 15, 2008, in response to ACC's February 2, 2008, letter, the Division indicated it could not process ACC's letter as an appeal. The Division indicated it would consider ACC's letter as an original request to toll the AFU POE work obligations, subject to ACC providing information about 1) the specific nature of the alleged force majeure and whether it is ongoing, and 2) which work obligations it wanted tolled and for how long. The Division reminded ACC that "[u]nder the current AFU Amended Initial Plan of Exploration (POE), ACC is required to move a drilling rig or

workover rig onto the Burglin #33-1 Well pad by May 15, 2008, and drill or workover the Well by October 1, 2008.”

On February 27, 2008, ACC sent a fax transmittal to the Division requesting a “declaration of force majeure for an extension of the Arctic Fortitude Unit work commitment deadlines commensurate with the period of the force majeure caused by AOGCC actions.”

On March 24, 2008, the Division denied ACC’s February 27, 2008, request and set out the following key findings and decisions.

- I simply don’t understand, from what you have submitted to me, how the AOGCC has delayed your consultant’s ability to prepare and submit a C-Plan for ADEC approval and why any additional post-appeal communication between ACC and AOGCC staff about the well would facilitate approval of a C-Plan.
- It appears to me that ACC is requesting to delay its POE work obligations solely because it is dissatisfied with the AOGCC’s determination that the Burglin #33-1 well is not a gas-only well. This determination will require ACC to obtain a C-Plan approval from ADEC, which it must pay to prepare, submit, and execute by moving appropriate oil spill response tankage and equipment to the lease.
- Based on what you have submitted to me, I find for the following reasons that your asserted AOGCC delay, AOGCC’s gas-only determination, and resulting appeal are not force majeure events under the terms of the AFU leases, which require that a cause must be “beyond the lessee’s reasonable ability to foresee or control”
- Thus, I further find that the dispute and litigation with the AOGCC is not preventing ACC from complying with the requirement to move a rig on the lease by May 15, 2008. ACC does not need a C-Plan to meet this work obligation deadline.

On April 14, 2008, the Commissioner received a 51-page appeal from ACC of the Director’s March 24, 2008 Decision, which denied ACC’s request to toll its obligation, under the amended initial POE, to move a drilling or workover rig onto the Burglin #33-1 well pad by May 15, 2008. ACC renewed the force majeure assertion and suspension of operations request that it had made to the Director. ACC indicated that its appeal and requests were based on its appeal of the AOGCC’s determination that the Burglin well is not a “gas-only” well.

On April 24, 2008, the Commissioner informed ACC that “. . . under the POE, ACC is required to move a drilling or workover rig onto the Burglin #33-1 Well pad by May 15, 2008 and re-enter or workover the Burglin #33-1 Well by October 1, 2008. ACC’s April 14, 2008 appeal and request

does not stay the Director's March 24, 2008 Decision 11 AAC 02.060. Pending my decision on the appeal, the POE remains in effect and AAC is obligated to move a rig onto the pad by May 15, 2008. As stated in the Director's Decision, if ACC fails to meet its current obligation, the AFU will be in default and subject to termination under Article 20 of the AFU Agreement."

On April 24, 2008, ACC submitted a proposed second amendment to the amended initial POE ("Second Amended Initial Plan of Exploration") that included a request to defer ACC's work obligations and to extend the amended initial POE another 16 months to November 1, 2011. ACC provided a number of reasons for this request that were mainly related to rig procurement. Notwithstanding its pending force majeure assertion, ACC now asserted that had to "make the decision to ship the little rig from New Mexico to Deadhorse, Alaska: no later than Saturday, April 26, 2008." ACC's proposed amendment also provides for automatic AFU termination.

On April 25, 2008, the Director, on behalf of the Commissioner, responded by e-mail to ACC indicating that the materials submitted on April 24, 2008, would be added to the materials considered in support of ACC's appeal of the Director's March 24, 2008, Decision. The response indicated that DNR would not make a decision on ACC's appeal until ACC had had the opportunity it requested to add materials to the record.

On April 28, 2008, the Director and the Commissioner received a fax transmittal from ACC again requesting a decision to amend the amended initial POE and issue a force majeure decision as soon as possible. ACC also filed additional materials to supplement its April 14, 2008, appeal and confirmed that its appeal filings were complete.

On May 5, 2008, the Director and the Commissioner received another fax transmittal from ACC making a second request to defer the amended initial POE work obligation from May 15, 2008 to March 31, 2009 and to extend the amended initial POE for another 16 months to November 1, 2011. ACC provided a number of reasons for this request including rig procurement, and its AOGCC appeal.

On May 15, 2008, ACC failed to meet its work obligation under the amended initial POE, which was to move a drilling or workover rig onto the Burglin #33-1 by that date.

2. DISCUSSION OF DECISION CRITERIA

I reviewed the criteria set out in 11 AAC 83.303(a) and (b) when evaluating requested authorizations or approvals under 11 AAC 83.301 – 11 AAC 83.395. A discussion of the subsection (b) criteria, as applied to this decision, 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 Unitized Exploration and Development

When ACC did not deliver any equipment to the Burglin #33-1 well pad location in the winter of 2006/2007, ACC asserted that the summer operations needed to complete its initial POE work obligation by October 1, 2007 might damage the tundra and that another winter drilling season was needed to fulfill its work obligations.¹ In acknowledgement of the environmental risks associated with summer tundra travel, the default cure set out in this decision allows for winter operations to move the drilling/workover rig onto the Burglin #33-1 well pad to be completed by March 31, 2009, as requested by ACC in its appeal.

2. The Geological and Engineering Characteristics of the AFU, and Prior Exploration Activities in the Proposed Unit Area

Notwithstanding ACC's litigation with the AOGCC over whether the Burglin well is a "gas-only" well, ACC has not provided any new geological or engineering data with the appeal to support a finding that the Burglin #33-1 well is a "gas-only" well.

¹In its June 26, 2007, letter to the Division seeking modification of the initial POE, ACC asserted that "[a] few trips with light loads would be allowed in the summer, but not repetitive trips with heavy loads." In an August 6, 2007, letter to the Division, ACC asserted that "[a]llowing excessive summer tundra travel is not in the best interest of the state, and the travel should be postponed until the winter season, when the fragile ecosystem can be adequately protected." And, in an August 29, 2007, letter to the Division, ACC indicated that "ACC is concerned by at least 26 trips to and 26 trips from the well pad just for the presently required C-Plan (15% RPS) all across the tundra by rolligon, even using a variety of routes is not good for the tundra plus the DNR would not approve summer access thereby stalling the ability to do the Unit Plan of Exploration this work season."

The information ACC submitted in support of its Application to form the AFU does not support its current assertion that this is a gas-only well. ACC's own consultant states that there is "ample evidence that liquid hydrocarbons are present in the Burglin #33-1 well."

The Division's June 29, 2006, Decision approving the AFU formation described the AFU's geologic and engineering characteristics and prior exploration activities in the proposed unit area; that description is incorporated into this decision by reference.

3. Plans for Exploration or Development

The initial POE set out a timely sequence of well testing, drilling, and exploration activities to facilitate development and production of the AFU. ACC's first work obligation was to move a drilling or workover rig onto the Burglin #33-1 well pad and re-enter and workover the well by October 1, 2007. ACC agreed to the initial POE work obligations and did not appeal the Division Decision setting those terms.

After the first year of the initial POE, ACC was unable to provide any substantive evidence of efforts to deliver equipment to the Burglin #33-1 well location during the winter of 2006-2007. ACC asserted that winter tundra travel equipment shortages (rolligon availability) prevented ACC from delivering equipment to the Burglin #33-1 well location during the winter of 2006-2007, but provided no substantive communication with rolligon or other equipment suppliers to support that assertion.

The Division extended ACC's work obligation deadlines in the amended initial POE on November 7, 2007 after ACC did not meet the October 1, 2007 work obligation in settlement of ACC's appeal to the Commissioner of the Division's Decision denying ACC's request to modify the initial POE. Under that POE, ACC was required to deliver a workover rig to the Burglin #33-1 well pad by May 15, 2008 and to re-enter and workover the well by October 1, 2008. This deferred ACC's first work obligation from October 1, 2007 to May 15, 2008. This deferral provided ACC almost two years to move a rig to location. ACC agreed to the amended initial POE on November 6, 2007, several months after the AOGCC first determined that the Burglin #33-1 well was not a gas-only well.

ACC's initial POE work obligations were reasonable. The Division provided ACC 15 months to complete the first work obligation and the opportunity to complete both winter and summer operations. After ACC's first work obligation was deferred until May 15, 2008, ACC had almost two years just to bring equipment to the Burglin #33-1 well pad. Approximately one year after unit formation on June 26, 2007, ACC began providing excuses for not meeting its work obligations.

During the history of this unit ACC has repeatedly agreed to work obligations, provided excuses to try to justify a work obligation deferral, requested a deferral of its work obligations, and then appealed any decision denying the deferral request.

In the present appeal, ACC again requests that DNR defer its obligation to move a drilling rig onto the Burglin #33-1 well pad—an obligation that ACC has had two years to fulfill. ACC's current excuse is that it is prevented by force majeure from delivery a drilling rig to the pad because of its dispute with the AOGCC regarding its determination that the well is not a gas-only well. I agree with the Director that the alleged reason for the delay, AOGCC gas-only determination, and resulting litigation are not force majeure events under the terms of the AFU leases. This litigation does not prevent ACC from moving a rig onto the well pad. See Director's March 24, 2008, Decision denying request to toll amended initial POE work obligation deadlines. Furthermore, ACC knew on November 7, 2007, when the Division approved the agreed-to amended initial POE, that the AOGCC had determined that the Burglin #33-1 well was not a gas-only well.

4. The Economic Costs and Benefits to the State

One of the costs to the State and of deferring ACC's work obligations again is that the AFU will not be timely explored and potential underlying hydrocarbons will not be timely delineated and produced. There are also administrative burdens associated with continuing the AFU based on ACC's history of non-compliance with approved POEs. The administrative costs of managing a unit with no oil or gas production are generally incommensurate to the value received by the State. The State is primarily interested in timely oil and gas production from its leases. A majority of the State's general fund revenue is derived from North Slope oil and gas operations in the form of royalty, net profit shares, production tax, property tax, and corporate income tax. Failure to complete required work obligations and develop and produce possible oil and gas accumulations deprives the State of potential incremental revenue, economic activity and jobs.

On the other hand, ACC has paid the State lease rental payments and \$180,000 in security payments and asserts that "it would seem the state would be overjoyed in having a risk capital investor (ACC) ready and willing to risk its capital to prove up such a low potential prospect." The State recognized this low potential when it approved the AFU in 2006. See June 29, 2006, Director's Decision approving the AFU formation. But the State believed there was some benefit to allowing ACC "the opportunity to explore . . . given the constraints and conditions . . . in [the] decision." Id. at p. 6. ACC has failed to take advantage of that opportunity.

ACC must continue to pay lease rentals and made an additional security payment to the State on July 1, 2008, to avoid AFU termination. Lease rental payments and security payments do not, by themselves, justify a lease or unit extension. Lease rental payments are required as a condition of the AFU leases. Security payments are required under the initial and amended initial POEs and are

refundable upon successful completion of work obligations. These payments are not in lieu of completing work obligations nor do they justify deferring a work obligation.

5. Other Relevant Factors

Timing of Division response: In its April 24, 2008, and May 5, 2008 requests to amend the amended initial POE, ACC sought an immediate response so it can decide which rig to use. ACC asserted that it had a rig in Kenai that could test as deep as 9400' and sidetrack and that this rig needs to remain on location in Kenai until the mud road was re-frozen, or until approximately December, 2008, and that it had another rig available in New Mexico but it can only test to 5000'. ACC asserted that it "[had to] make the decision to ship the little rig from New Mexico to Deadhorse, Alaska no later than Saturday, April 26, 2008 due to the pending North Slope coastal plain tundra travel closure and the current AFU POE work commitment date [of] May 15, 2008."

After owning the AFU leases for approximately nine years, ACC was still pondering which rig to deliver to the well pad approximately three weeks before its work obligation deadline and suggested its decision was based on a last minute DNR determination. ACC assured that it was prepared to move a rig onto the lease, notwithstanding its argument that it was prevented by force majeure from doing so. ACC never moved a rig onto the lease. ACC must make its own business decision about which rig to move to the lease. It is ACC's responsibility to complete its work obligations. The work obligation deadlines are no surprise to ACC. The Division has cooperated with ACC by extending the work obligation deadline and by repeatedly providing ACC notice that work obligations under the POEs need to be timely completed. See Background section, above.

Prior ACC investment: ACC has cited a \$7.5 million investment in the AFU to demonstrate its level of work commitment.

The \$7.5 million investment refers to the original cost of drilling of the Burglin #33-1 well, which was done in 1985--long before the current leases were issued.

ACC permitting and other efforts: ACC cites its efforts to complete permitting, contact suppliers, and work with various state agencies to demonstrate its level of work commitment.

ACC's efforts are noted, but these efforts have not resulted in completion of ACC's work obligations under either the initial POE or the amended initial POE.

Alaska's competitiveness: ACC asserts that there are no individual Alaskans producing and selling oil, that ACC is Alaska's first "homegrown independent," that there are only about eight producing companies in Alaska, and that existing state statutes and regulations do not adequately provide for small operators of ACC's size.

Alaska's competitiveness and any perceived need to modify existing state statutes and regulations are outside the scope of this decision. ACC's size and position as a small independent were recognized in the Division's June 29, 2006, Decision approving the AFU, but size and position is not a basis for a work obligation deferral.

ACC's request to extend or modify the AFU POE "is not unusual." In its May 5, 2008, letter, ACC asserts that "the request to extend or modify the AFU POE is not unusual or inordinate. It is prudent for the State Division of Oil and Gas to approve this request for modification, as it has done for several other operators with similar circumstances."

I agree. The State does defer work obligations and has deferred the ACC's obligations in the AFU, based on the decision criteria set out in 11 AAC 83.303 (a) and (b). In this appeal, although I am defaulting the unit, the cure demand set out here defers the previously-existing May 15, 2008, work obligation to March 31, 2009. If ACC does not meet this work obligation or meet any of its other work obligations in the attached Second Plan of Exploration and Default Cure, the AFU is subject to termination.

Applicability of June 29, 2006, AFU Decision: ACC argued in its April 14, 2008, appeal that "the findings and decision of the Director approving the AFU remain sound and applicable today."

The Division approved the AFU, in part, based on ACC's firm commitments to timely develop the AFU. However, ACC has not timely developed the unit under any of the approved POEs. I agree with the Director that "ACC is requesting to delay its POE work commitments solely because it is dissatisfied with the AOGCC's determination that the Burglin #33-1 well is not a gas-only well." See March 24, 2008, Director's Decision.

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

1. Promote the Conservation of All Natural Resources

Unitization provides a practical and efficient method for maximizing oil and gas recovery, while minimizing the use of materials and equipment, and protecting surface and subsurface resources. There can be no argument here that whatever oil and gas there is in the Burglin #33-1 well has been conserved because ACC has not undertaken the rig placement and drilling obligations set out in the AFU POEs.

2. Prevention of Economic and Physical Waste

The State has received very little economic benefit from the AFU, other than the rentals and security payments ACC has paid. Whatever oil and gas there is in the Burglin #33-1 well has not been physically wasted because ACC has not undertaken the rig placement and drilling obligations set out in the AFU POEs.

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

ACC's interest

Overturing the Director's March 24, 2008, Decision, and expressly granting ACC's deferral requests, provides ACC with more time to deliver a rig to the well pad and pursue its current litigation with the AOGCC over that agency's gas-only determination. This default decision and cure demand also gives ACC additional time to deliver a rig to the well pad, but does not recognize the AOGCC litigation as a force majeure event. Given my decision, I believe that ACC should dismiss that appeal, accept the modest RPS suggested by the AOGCC, get a C-Plan approved by the ADEC, and explore for and develop whatever oil and gas exists in the formations under the Burglin #33-1 well.

State's interest

ACC has not met its work obligation under the initial and amended initial POE. Therefore, the State has not realized the potential economic or other unitization benefits associated with development of the AFU leases. Additional, unconditional deferral of ACC's obligations risks further delay these potential benefits.

It is not necessarily in the State's interest to grant an owner an extension on development without completion of work obligations. Oil and gas units and leases give lessees the right to explore for, develop, and produce oil and gas. ACC has not reasonably or diligently exercised its rights in the AFU. The State has an interest in orderly and reasonably prompt development. The State's interest is best served by promoting competition for the right to develop state lands, not by allowing repeated deferral of work obligations in exchange for an unconditional promise to complete work obligations when the state has no reasonable basis to believe that granting those requests will result in well testing, drilling, and exploration.

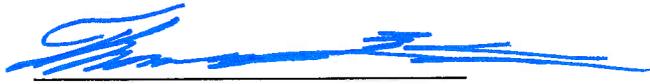
Unconditionally granting ACC's requests or overturning the Director's March 24, 2008 Decision, would allow ACC to hold state oil and gas leases without completing any work obligations and renders POE work obligations meaningless. Timely completion of work obligations is essential to ensure the timely development of state land and continued receipt of royalties from oil and gas produced from state lands.

3. FINDINGS AND DECISION

1. ACC has failed to meet its work obligation under the amended initial POE, which is to move a drilling or workover rig onto the Burglin #33-1 well pad by May 15, 2008. The cost to the State of deferring ACC's work obligations is that the AFU will not be timely explored and potential underlying hydrocarbons will not be timely delineated and produced.
2. ACC provided no substantive evidence of its efforts to complete its work obligations under the initial POE during the winter months of 2006-2007.
3. The Division deferred the initial POE work obligations and has provided ACC with adequate notice that its work obligations must be completed.
4. ACC's initial work obligations were reasonable. ACC was provided 15 months to complete the first work obligation and the opportunity to complete both winter and summer operations. ACC's first work obligation was deferred until May 15, 2008. Thus, ACC had almost two years to bring equipment to the Burglin #33-1 well pad. ACC knew when it agreed to the amended initial POE that the Burglin #33-1 well was not, by its own Application and assertions, and under the AOGCC determination, a gas-only well.
5. I have no reasonable basis to believe that expressly granting any of ACC's requests or overturning the Director's March 24, 2008, Decision will result in well testing, drilling, and exploration within the AFU.
6. I affirm the Director's March 24, 2008, Decision in all respects. I find no basis to determine a force majeure exists under Paragraph 4(f) of the AFU leases or to the AFU Agreement, or to grant a suspension of operations under Paragraph 4(e) of the AFU leases and these requests are also denied. ACC agreed to the amended initial POE, and has again proposed, delivering a rig to the Burglin #33-1 well pad by March 31, 2009, knowing the AOGCC had determined that the well was not a gas-only well.
7. This is an AFU default notice under 11 AAC 83.374(b) because ACC has failed to meet its work obligation under the amended initial POE. To cure the default, ACC shall complete the attached Second Plan of Exploration and Default Cure.
8. If AAC fails to complete any of the obligations in the attached Second Plan of Exploration and Default Cure, then I may initiate AFU termination under 11 AAC 83.374(c).

9. I am providing ACC an opportunity to cure the rig delivery default consistent with the provisions of 11 AAC 83.374. The default cure provides ACC with another winter to complete delivery of equipment to the Burglin #33-1 well pad.

This is a final administrative order and decision for purposes of an appeal to Superior Court. An appellant affected by this final order and decision may appeal to Superior Court within 30 days in accordance with the rules of the court, and to the extent permitted by applicable law.



Thomas E. Irwin
Commissioner, Dept. of Natural Resources

Date: July 16, 2008

Attachment 1

Arctic Fortitude Unit Agreement Second Plan of Exploration and Default Cure¹

The Unit Operator, Alaskan Crude Corporation (ACC), **shall** [WILL] complete an amended initial plan of exploration for the Arctic Fortitude Unit (AFU), effective May 1, 2008 – NOVEMBER 1, 2011.

Stage 1 and 2 Security Provisions

1. The Stage #1 and Stage #2 Security Payments and Provisions, which are referred to in this document are described in the AFU initial Plan of Exploration. ACC has made the Stage #1- payment #1, and the Stage #2- payment #2. The payments remain on deposit with the State of Alaska and shall be handled according to terms set out in this document.
2. By 5 p.m., Alaska time, on July 1, 2008, ACC shall submit an additional \$60,000 to the Division in the form of a bond acceptable to the state, certificate of deposit, or wire transfer of cash funds (Stage 2 Security – payment #3).
3. If ACC fails to submit the Stage 2 Security – payment #3 as set out in this document:
 - a. the AFU will automatically terminate at 5:01 p.m., Alaska time, on July 1, 2008; and
 - b. ACC shall forfeit all \$60,000 of the Stage 1 Security – payment #1, and the \$60,000 of the Stage 2 Security – payment #2 to the Division upon termination of the AFU.

Stage 2 Work Obligations

1. By 5 p.m., Alaska time, on March 31, 2009, ACC shall complete delivery to the Burglin #33-1 well pad the major heavy drilling-equipment necessary to complete the work described below in step #3. This includes spotting a drilling or workover rig on the Burglin #33-1 well pad that is suitable to re-enter and workover the Burglin #33-1 well as required in step #2.
2. By 5 p.m., Alaska time, on October 1, 2009, ACC shall complete the following additional Stage 2 work obligations:

¹See ACC's April 24, 2008, Second Amended Initial Plan of Exploration. Language added under this Decision is underlined and bolded, and language deleted under this Decision is bracketed and capitalized.

[a. MOVE A DRILLING RIG OR WORKOVER RIG ONTO THE BURGLIN #33-1 WELL PAD;]

- a. re-enter and workover the well, which means to perform onsite well operations in an effort to cause production of oil or gas in paying quantities where there was none from the West Sak, Ugnu, Sag River, or Ivishak formation, but does not include bleeding the well or the well annulus;
 - b. attempt to flow, pump, or circulate reservoir fluids to a surface tank or surface facility;
 - c. acquire flow test data for certification of the well as capable of production in paying quantities, as those terms are defined in 11 AAC 83.361;
 - d. submit the flow test results, supporting geologic data, and cost data to the Division as an application for certification under 11 AAC 83.361, which the Division will approve or disapprove, in its sole discretion;
 - e. provide a written statement to the Division describing all the onsite activities conducted by ACC under its Stage 2 work obligations; and
 - f. provide a second written statement to the Division whether or not it elects to complete all of the Stage 3 work obligations, as set out in this document.
3. If ACC satisfactorily completes, as determined in the Division's sole discretion, all of the Stage 2 work obligations, as set out in this document, and submits the Stage 2 Security payment-payment #3:
- a. AFU will remain in effect, subject to Stage 3 work commitments;
 - c. The Division will release or refund \$20,000 of the Stage 1 Security-payment #1 to ACC, without interest, upon ACC's request.
4. If ACC does not complete, as determined in the Division's sole discretion, all of the Stage 2 work obligations:
- a. the AFU will automatically terminate at 5:01 p.m., Alaska time, on **October 1, 2009** [NOVEMBER 1, 2009]; and
 - b. ACC shall forfeit all \$60,000 of the Stage 1 Security and \$120,000 of the Stage 2 Security (payment #2 and #3) to the Division upon termination of the AFU.
5. If, however, ACC satisfactorily completes, as determined in the Division's sole discretion, all of the Stage 2 work obligations, as set out in this document, but ACC elects to not complete all of the Stage 3 work obligations, as set out below, then:
- a. The AFU will automatically terminate at 5:01 p.m., Alaska time, on **October 1, 2009** [NOVEMBER 1, 2009];

- b. the Division will release or refund \$20,000 of the Stage 2 Security-payment #2 to ACC, without interest, upon ACC's request; and
- c. ACC shall forfeit the remaining \$40,000 of the Stage 1 Security-payment #1, and the remaining \$100,000 of the Stage 2 Security - payment #2 and #3 to the Division upon termination of the AFU.

Stage 3 Work Obligations

1. By 5 p.m., Alaska time, on November 1, 2010, ACC shall complete the following Stage 3 work obligations:
 - a. drill one exploratory well [FROM EITHER THE ACC F-2 GRAVEL PAD] to a bottom-hole location within ADL 389177 or [FROM THE ACC F-3 GRAVEL PAD] to a bottom-hole location within ADL 389179, to a total depth sufficient to penetrate the Ivishak formation and acquire and submit to the Division open-hole formation log data from the well; or
 - b. acquire and submit to the Division 3-D seismic data shot over the entire AFU acreage sufficient to determine the extent of any reservoirs under the acreage.
2. If ACC does not complete all of the Step 1, Stage 3 work obligations, as determined in the Division's sole discretion, and as set out in this document, then:
 - a. The AFU will automatically terminate at 5:01 p.m., Alaska time, on November 1, 2010; and
 - b. ACC shall forfeit all the remaining \$160,000 of the Stage 1 and 2 Securities to the Division.
3. If ACC does complete all of the Step 1, Stage 3 work obligations, then by 5 p.m., Alaska time, on NOVEMBER 1, 2011[10], ACC shall complete the following additional Stage 3 work obligations:
 - a. If a well was drilled as set out in Step 1 of Stage 3, drill a second exploratory well [FROM EITHER THE ACC F-2 GRAVEL PAD OR FROM THE ACC F-3 GRAVEL PAD] to a bottom-hole location within either ADL 389179 or ADL 389177, whichever one was not drilled to in Step 1 of Stage 3, and drill to a total depth sufficient to penetrate the Ivishak formation;
 - b. acquire and submit to the Division 3-D seismic data shot over the entire AFU acreage sufficient to determine the extent of any reservoirs under the acreage;
 - c. if 3-D seismic was shot as set out in Step 1 of Stage 3, drill one exploratory well [FROM THE ACC F-2 GRAVEL PAD] to a bottom-hole location within ADL 389177 and drill a second exploration well [FROM THE ACC F-3 GRAVEL PAD] to a bottom-hole location within ADL 389179, both to a total depth sufficient to penetrate the Ivishak formation;
 - d. acquire and submit to the Division open-hole formation log data from the well or wells identified above;

- e. provide a written statement to the Division describing all the onsite activities conducted by ACC under all Stage 3 work obligations.
4. If ACC satisfactorily completes, as determined in the Division's sole discretion, all of the Stage 3 work obligations, as set out in this document, by 5 p.m., Alaska time, on NOVEMBER 1, 2011, the Division will release or refund, without interest, the remaining \$160,000 of the Stage 1 and 2 Securities to ACC, upon ACC's request.
 5. If ACC does not complete all of the Stage 3 work obligations, as determined in the Division's sole discretion, and as set out in this document, then
 - a. the AFU will automatically terminate at 5:01 p.m., Alaska time, on NOVEMBER 1, 2011; and
 - b. ACC shall forfeit all the remaining \$160,000 of the Stage 1 and 2 Securities to the Division.

Additional Provisions:

1. ACC waives the extension provisions of 11 AAC 83.140 and Article 15.02 of the AFU Agreement.
2. ACC waives the notice and hearing provisions of 11 AAC 83.374, applicable to default and termination of the AFU.
3. ACC shall provide written quarterly reports to the Division documenting all progress and work activities toward completing this Plan of Exploration, effective January 31, 2008 for the prior quarter October 1, 2007 through December 31, 2007, and every three months subsequent to January 31, 2008 for the prior quarters, as long as this Plan of Exploration is in effect.