Approved: March 24, 2009
Date

MINUTES OF THE HOUSE ENERGY AND UTILITIES COMMITTEE

The meeting was called to order by Chairman Carl Holmes at 9:00 a.m. on March 12, 2009, in Room 783 of the Docking State Office Building.

All members were present except:
Representative Annie Kuether-excused
Representative Don Myers-excused

Committee staff present:
Melissa Doeblin, Office of the Revisor of Statutes
Sean Ostrow, Office of the Revisor of Statutes
Mary Galligan, Kansas Legislative Research Department
Cindy Lash, Kansas Legislative Research Department
Renae Hansen, Committee Assistant

Conferees appearing before the Committee:
Andy Cockrell, Kansas Oil Producer
David Bleakly, Eastern Kansas Oil and Gas Association (EKOGA)
Doug Louis, Kansas Corporation Commission, (KCC)

Others attending:
Eighty-Seven including the attached list.

Background briefing on: Kansas Oil Production: Is supply and demand working?

Andy Cockrell, Kansas oil producers, presented testimony regarding Kansas Oil Production. Included in his testimony is a summary of his statement, (Attachment 1), and his testimony (Attachment 2), that includes exhibits A-K.

Those exhibits are as follows:

A- State Production and Historical Information
B- Kansas Department of Commerce: Circulation of the dollar
C- World Crude Oil Prices, from the official energy statistics of the US Government
D- Cross referencing the spot price with the day sold form Exhibit C
E- Reference to the dockage of oil run tickets
F- Environmental Integrity Project
G- Governor Schwarzenegger to ban Canadian Tar Sand Oil/EPA says no to Tar Sand
H- Section 526 of the Energy Independence and Security Act of 2007
I- Oklahoma Attorney General Investigation
J- Kansas historical references of Unfair Practices Act
K- Canadian Tax Subsidies

David Bleakly, EKOGA (Attachment 3), presented information about the typical process by which an oil producer drills for or acquires oil production. In sub-point 6 he noted the process by which a load of oil is sold and prices are determined for that oil. Included also were some factors that create demand or tight supplies.

Doug Louis, Director of Oil and Gas Division, KCC (Attachment 4), presented information on Kansas crude oil facts, and various charts and graphs pertaining to the supply and demand of oil and gas.

Other informational material was made available to committee members: Crude oil market infrastructure task force, Executive Summary, (Attachment 5), and WTI (Spot West Texas Intermediate): A broken benchmark, (Attachment 6).

Minutes of the House Energy and Utilities Committee at 9:00 a.m. on March 12, 2009, in Room 783 of the Docking State Office Building.

Questions were asked and comments made by Representatives: Cindy Neighbor, Rob Olson, Carl Holmes, Vern Swanson, Forrest Knox, Joe Seiwert, Josh Svaty, Tom Sloan, Vince Wetta, Tom Moxley, and Mike Burgess.

The next meeting is scheduled for March 17, 2009.

The meeting was adjourned at 10:24 a.m.

HOUSE ENERGY AND UTILITIES COMMITTEE
GUEST LIST

DATE: March 12, 2009

NAME	REPRESENTING
Tom Day	KCC
Ken Peterson	KS Petroleum Council
Bob Thomas	EKOGA
Scott Burkdoll	EKOGA
Jim O. [illegible]	EKOGA
[illegible]	Bailey Oil
Elsie K. Galmore	GV Oil
[illegible]	GV Oil
[illegible]	Jackson Oil
Julie Galmore	Galmore Oil
Rachel Galmore	Galmore Oil
Amanda Moyer	Yates Center NEWS
Brian Birk	Birk Petroleum
Ed Birk	Birk Oil Inc.
Alex Houdashelt	R+J Oil Co.
Bob Houdashelt	R&J Oil Co
Joe Green Jr.	Little Joe Oil Co.
[illegible]	Quest Dev. Co.
Craig Settle	Shawmar Oil + Gas Co, Inc.

HOUSE ENERGY AND UTILITIES COMMITTEE
GUEST LIST

DATE: March 12, 2009

NAME	REPRESENTING
Beau Cloutier	Shawmar Oil & Gas
Tom Baugher	B & B Oil Recovery
Charles Sheedy	SHEEDY ENERGY PRODUCTION CO.
Victor Hood	J.V. Oil
[illegible]	Kinsey Drilling
Roger Kent	R.J. Enterprises
JAY Leedy	L&B Crude
Jerry Bowen	Triple B Crude
Jim Loeffelbein	J & J Oil operating, LLC
Tom CRAIN	Venture Oil
JOHN Loeffelbein	J+J Oil Operating LLC.
Brent Newman	B + S Oil
[illegible]	S + K Oil
[illegible]	A + A Well Service
[illegible]	D & L Services
[illegible]	Dale Jackson Prod. Co.
Mike Cantrell	Cantrell Energy Corp
Dale Jackson	Dale Jackson Product.
Darrell Jackson	J + J production

HOUSE ENERGY AND UTILITIES COMMITTEE
GUEST LIST

DATE: March 12, 2009

NAME	REPRESENTING
Greg Brevel	Rolling Meadows Oil & Gas
Tom KEMPER	Bomber Oil Inc.
MARK DOUDNA	DOUDNA OIL INC.
Keith Crawford	Crawford Oil
Shane Lyle	KGS
Vern Leis	Victor Leis Oil Co.
Mari Tucker	Dept of Commerce
A.L. Ballard	Bulldog Oil
Tom Thompson	Sierra
Mark Hartell	CEP
LON STANTON	NORTHERN NATURAL GAS
Don Schmacke	TransCanada Pipeline Co.
GINA BOWMAN	CVR Energy
David Degrandt	KIOGA
Kelly Peterson	Rolling Meadows Oil & Gas
Wendy Sheedy	SHEEDY ENERGY PRODUCTION INC

Summary Sheet

Benefits

1. Big oil profits
2. Transporters
3. Refineries

Detriments

1. National Security
   - **More dependency on foreign oil**
2. Gouging
   - **Price to crude producer compared to gas price average from 1996 to 2009**
     - National average gas price in 1996 $1.15/gallon. Price paid to an oil producer in Kansas in 1996 was $18.05/barrel
     - National average gas price in 2009 $1.97/gallon. Price paid to an oil producer in Kansas in 2009 was $21.45/barrel
     - Net Result
       - ↑ 72% increase in a gallon of gas
       - ↑ 18.85% increase in a barrel of Kansas crude oil
3. Pollution
   - **Emission increase**
   - **Land devastation**
     - Tar sand land destruction is the size of Florida.
4. Loss of Wealth
   - **Government and Tax Base**
   - **Employment**
   - **Individual net per capita income**
   - **Independent oil industry**
   - **Service industry**
   - **Oil field suppliers**

HOUSE ENERGY AND UTILITIES
DATE: 3/12/2009
ATTACHMENT 1

KANSAS LOSES

The true title of this hearing should be "Kansas Loses." The facts we will discuss today in our testimony show that supply and demand factors have very little to do with our current situation and the problems we are facing. High and low commodity prices are an acceptable way of life for many of us who work with crops, cattle, oil and gas. The independent oil and gas producers are here today to demonstrate how the Sherman Act, passed in 1890, and other antitrust laws passed, since then, were designed to protect things such as: our people and businesses, the citizens of Kansas, and the prosperity of our cities, counties, state, and our way of life. This world we live in is not a slow world anymore. After hearing our testimony today, we will urge you to swiftly take action and help us keep what is being stolen from us on a daily basis, "OUR NATURAL RESOURCES".

A few years ago, the United States was faced with what we thought was a limited oil supply, high gas prices, and a booming healthy economy. In reality our situation is quite different. We now have a virtually unending supply of dirty oil from our Canadian neighbors to the north, high gas prices, but lower than what they were a year ago, and a contracting, almost collapsing economy with unemployment figures soon to be in the double digits. Market conditions have changed at the speed of light. As we talk about Canadian oil many of you may wonder what that has to do with any of us here today. Canada exports about 1.2 million barrels of oil everyday to the U.S. and is currently the largest exporter of oil to the U.S. Canada expects to increase its exports to 3 million barrels a day by 2018 if not sooner. Canada is a good neighbor and ally, but still a foreign nation. As a nation, we wanted to become more energy independent and less dependent on hostile foreign oil exporters from the Middle East. This has created a newer and bigger problem. Now we are importing tar sand oil that is produced using unconventional methods. It is environmentally dangerous and it creates a high cost to our communities. Other states such as California have already passed carbon reduction laws that will ultimately ban the imports of Canadian tar sand oil into their refineries. As a rule, heavier crude oil has a more severe environmental impact than lighter oil. President Bush signed into law The Energy Independence and Security Act of 2007, including section 526. This section was designed to keep any federal agency from procuring an alternative or synthetic fuel including a fuel produced from non-conventional petroleum sources, for any mobility-related use.

We are here today to ask you to stop the dirty oil that is subsidized by the Canadian government to the tune of 1.5 billion dollars a year, from heading to our refineries and ultimately the gas tanks of our Kansas citizens. Since the Canadian tar sand oil has been piped to our refineries, the dock on what we receive when we sell our oil has risen over the past several years. This cost of doing business has escalated out of control to the point where it is the single largest expense of every producer here today and represents what the antitrust laws were designed to protect. The dock on our oil is unfair and costs Kansas at a minimum, several hundred million dollars in taxable revenue. This unfair dock represents: loss of capital to reinvest into our businesses, loss to the landowners and royalty owners who depend on that money, loss of jobs for Kansas residents, loss of cash flow into our local economy, loss of tax revenue for our state, loss of free-trade and an un-fair market. Our industry needs a level playing field and some

HOUSE ENERGY AND UTILITIES
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ATTACHMENT 2-1

regulations to protect both the producers and the people of Kansas. If we do not stop tar sand oil from infiltrating our oil markets we will crush our domestic production capability and ultimately be at the mercy of foreign oil at an inflated level.

The Kansas oil industry is the second largest industry in the state. Kansas represents the eighth largest producer of oil in the U.S. In 2007, Kansas produced 36,589,409 barrels of oil. The minimum dock on our oil has been $10/barrel. Last month, I personally received a $17/barrel dock on the oil I sold. A 17 dollar a barrel dock with a 40 dollar a barrel market price represents $2,720 dock on 160 barrels of oil sold. I did not receive this revenue which would have helped my business nor did Kansas receive this revenue to help its economy. Actually no one locally was able to benefit in any way from this lost revenue. The oil we produce is a natural resource that comes from Kansas. We have no choice but to take the price we get for the oil we sell. This price is dictated by the hauling companies and the refineries. Market prices as listed on WTI or NYMEX are what most people associate with oil prices. Actually, this is the price we used to get. We will get into the rest of our handouts later that document what the dock has been in years past and how it has crept up over the years. The oil industry in Kansas is in serious jeopardy. Unlike crops in a field, once a barrel of oil is lost, it is gone forever.

You as a legislative body have two choices. Before Kansas purchasers buy Canadian oil and exchange their dirty oil for our cleaner oil. You can support local producers and act swiftly to help us get a fair market price for the natural resources produced by callused hands and hard working Kansas families. The other choice is to continue down the path of bringing in subsidized Canadian oil that is environmentally dangerous with three times the greenhouse gas emissions as our domestic oil. This choice will demolish our industry and cause ripple effects that ultimately destroy our way of life in Kansas. The producers and their employees will ultimately have to pack their bags and move to Canada to work in their oil fields BECAUSE the jobs in Kansas are going to vanish. We are for Kansas, our neighbors, our friends, and our families. We know you are too and you will do the right thing!

IN CONCLUSION

You cannot leave this dire subject in committee till the year 2010. You must act now. We need an emergency solution.

These are the things we need to happen:

1. We need to be able to sell our oil at a world market price without an unfair dock.
2. We need transparency on how we get paid. EQUAL PAY FOR EQUAL OIL!
3. We need to stop exchanging cleaner Kansas oil for dirty Canadian oil.

EXHIBITS

Exhibit A:

From the KGS Energy Resources, State Production and Historical Information

Exhibit B:

Kansas Department of Commerce: Circulation of the dollar. Over $1 billion in lost taxable revenue.

Exhibit C:

World Crude Oil Prices, From the Official Energy Statistics of the US Government.

Exhibit D:

Cross referencing the spot price with the day sold from Exhibit C.

Exhibit E:

Reference to Dock from oil run ticket.

1. Little Joe Oil
2. KAMC
3. JV Oil

Exhibit F:

Environmental Integrity Project

Exhibit G:

1. Governor Schwarzenegger to ban Canadian Tar Sand Oil.
2. EPA Says NO to Tar Sand

Exhibit H:

Section 526 of the Energy Independence and Security Act of 2007

Exhibit I:

Oklahoma Attorney General Investigation

Exhibit J:

Kansas Historical references of Unfair Practices Act

Exhibit K:

Canadian Tax Subsidies

State Production and Historical Info

Production data through November 2008. County production is also available online.

Year	Oil		
	Production (bbls)	Wells	Cumulative (bbls)
1995	45,381,023	42,827	5,802,691,000
1996	43,642,645	49,002	5,846,333,645
1997	41,289,345	47,037	5,887,622,990
1998	36,378,608	44,460	5,924,001,598
1999	33,905,125	41,404	5,957,906,723
2000	35,174,434	42,165	5,993,081,157
2001	34,124,322	41,545	6,027,205,479
2002	33,379,734	41,383	6,060,585,213
2003	33,972,047	41,206	6,094,557,260
2004	33,878,472	41,920	6,128,435,732
2005	33,619,258	43,012	6,162,054,990
2006	35,667,469	43,915	6,197,722,459
2007	36,589,409	43,396	6,234,311,868
2008*	36,154,331	44,843	6,270,466,199

*2008 data incomplete at this time.
Note: bbls is barrels.

From: scadoret@kansascommerce.com
To: whistlestop75@hotmail.com
Date: Mon, 9 Mar 2009 13:01:24 -0500
Subject: response to email - formula for dollar circulation

Gwen,
I do not know where to locate the actual formula for the dollar circulation, but the calculation uses 3 times on the conservative side and 7 on the generous side.

Susan NeuPoth Cadoret
Business Expansion & Retention Manager
Kansas Department of Commerce
1000 SW Jackson, Suite 100
Topeka, KS 66612-1354
785.296.7198 Voice
785.296.3490 FAX

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Energy Information Administration
Official Energy Statistics from the U.S. Government

World Crude Oil Prices

(Dollars per Barrel)

Period: Weekly

Crude Type	01/09/09	01/16/09	01/23/09	01/30/09	02/06/09	02/13/09
Total World	43.12	40.98	41.05	42.07	41.77	43.0
United States	39.84	38.24	38.21	40.60	39.42	40.4
OPEC* Average	43.76	41.21	41.21	41.86	41.89	42.9
Abu Dhabi, Murban 39°	48.99	46.81	44.76	44.76	44.81	46.7
Algeria, Saharan Blend 44°	45.99	44.04	44.50	45.02	45.25	46.6
Angola, Cabinda 32°	43.57	41.46	41.94	42.82	42.96	44.0
Dubai, Fateh 32°	46.62	44.34	42.43	42.46	43.59	45.0
Ecuador, Oriente 30°	37.50	32.94	32.13	37.28	37.50	37.3
Iran, Heavy 30°	41.57	40.60	40.07	40.49	40.22	42.0
Iran, Light 34°	43.72	42.05	41.52	41.94	41.67	43.2
Iraq, Kirkuk 36°	44.21	42.59	42.81	42.74	42.81	44.7
Kuwait, Kuwait 31°	43.33	41.07	39.14	39.21	41.44	43.1
Libya, Es Sider 37°	45.14	43.50	43.94	43.64	43.50	45.3
Neutral Zone, Khafji 28°	41.76	38.54	39.51	40.09	39.49	40.3
Nigeria, Bonny Light 37°	48.30	46.24	46.35	47.44	47.72	48.7
Nigeria, Forcados 31°	49.07	46.97	47.11	47.97	48.11	49.1
Qatar, Dukhan 40°	47.13	45.02	43.28	43.53	44.24	46.2
Saudi Arabia, Arabian Heavy 27°	38.11	34.89	35.86	36.44	36.64	37.4
Saudi Arabia, Arabian Light 34°	41.76	38.54	39.51	40.09	39.49	40.3
Saudi Arabia, Arabian Medium 31°	39.71	36.49	37.46	38.04	37.74	38.5
Venezeula, Bachaquero 17°	NA	NA	NA	NA	NA	N.
Venezeula, Bachaquero 24°	NA	NA	NA	NA	NA	N.
Venezuela, Tia Juana Light 31°	43.13	38.03	38.56	41.46	40.96	39.2
Non-OPEC* Average	42.29	40.69	40.84	42.35	41.62	43.0
Australia, Gippsland 42°	45.56	45.15	43.81	45.61	44.68	47.6
Brunei, Seria Light 37°						
Cameroon, Kole 34°	42.18	40.13	42.38	42.61	42.82	43.9
Canada, Canadian Par 40°	35.38	35.24	33.94	37.43	33.86	38.4
Canada, Heavy Hardisty 22°	30.72	32.92	31.61	36.94	33.56	35.6
Canada, Lloyd blend 22°						
China, Daqing 33°	41.50	41.29	39.36	39.84	41.86	43.4
Colombia, Cano Limon 30°	50.22	45.08	43.75	48.01	47.07	46.8
Egypt, Suez Blend 33°	41.32	39.68	39.51	39.70	39.93	41.7
Gabon, Mandji 30°	NA	NA	NA	NA	NA	N.
Indonesia, Minas 34°	45.18	45.28	44.89	44.58	45.02	47.5
Malaysia, Tapis Blend 44°	48.23	47.43	46.01	48.31	46.96	49.5
Mexico, Isthmus 33°	43.02	37.92	38.45	41.35	40.85	39.1

Notes: ...tries listed under OPEC and non-OPEC are based on current affiliations. OPEC and non-OPEC averages are based on affiliations for th...ed period ...which may differ from current affiliations. Indonesia withdrew from OPEC in January 2009, Angola joined OPEC in January 2007, Ecua... withdrew ...n OPEC in January 1993 and rejoined in November 2007, and Gabon withdrew from OPEC in July 1996. Estimated contract prices base... government-selling prices, netback values, or spot market quotations. All prices are f.o.b. at the foreign port of landing except where noted; 30 day payment plan except where noted. Iraq, Kirkuk 36° is the netback price at the U.S. Gulf. Total OPEC is the netback price at the U.S. Gulf. Total World, United States, OPEC, and Non-OPEC are average prices (f.o.b.) weighted by estimated export volume. Egypt, Suez Blend 33° is on 60 days credit. Effective with the week ending July 6, 2007, Llolyd Blend crude stream data are no longer available; a similar crude stream Heavy Hardisty has replaced this category. Brunei, Seria Light 37° contract prices are no longer available for use in weekly calculations. Russia, Urals 32° price (f.o.b.) to Mediterranean destinations; also called Urals. United States average price (f.o.b.) is weighted by estimated import volume. The Canadian crude prices have been changed to U.S. dollars. See Definitions, Sources, and Notes link above for more information on this table.

Release Date: 3/4/2009
Next Release Date: 3/11/2009

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Definitions, Sources and Explanatory Notes

Category: Petroleum Prices
Topic: World Crude Oil Prices

Definitions

Key Terms	Definition
API Gravity	An arbitrary scale expressing the gravity or density of liquid petroleum products. The measuring scale is calibrated in te as follows: Degrees API = (141.5 / (sp. gr. 60°F / 60°F)) - 131.5 The higher the API gravity, the lighter the compound. Light crudes generally exceed 38 degrees API and heavy crudes crudes with an API gravity of 22 degrees or below. Intermediate crudes fall in the range of 22 degrees to 38 degrees AI
Barrel	A unit of volume equal to 42 U.S. gallons.
Crude Oil	A mixture of hydrocarbons that exists in liquid phase in natural underground reservoirs and remains liquid at atmosphe surface separating facilities. Depending upon the characteristics of the crude stream, it may also include: • Small amounts of hydrocarbons that exist in gaseous phase in natural underground reservoirs but are liquid at atmo recovered from oil well (casinghead) gas in lease separators and are subsequently commingled with the crude stream measured. Lease condensate recovered as a liquid from natural gas wells in lease or field separation facilities and late also included; • Small amounts of nonhydrocarbons produced with the oil, such as sulfur and various metals; • Drip gases, and liquid hydrocarbons produced from tar sands, oil sands, gilsonite, and oil shale. Liquids produced at natural gas processing plants are excluded. Crude oil is refined to produce a wide array of petrole gasoline, diesel and jet fuels; lubricants; asphalt; ethane, propane, and butane; and many other products used for their
F.O.B. (Free on Board)	Pertains to a transaction whereby the seller makes the product available within an agreed on period at a given port at a of the buyer to arrange for the transportation and insurance.
OPEC	An intergovernmental organization whose stated objective is to coordinate and unify petroleum policies among membe Baghdad Conference on September 10-14, 1960, by Iran, Iraq, Kuwait, Saudi Arabia, and Venezuela. The five foundin nine other members: Qatar (1961); Indonesia (1962); Libya (1962); United Arab Emirates (1967); Algeria (1969); Niger 2007); Gabon (1975-1994), and Angola (2007).

For definitions of related energy terms, refer to the EIA Energy Glossary.

Sources

EIA, Office of Energy Markets and End Use, Integrated Energy Statistics Division; Platt's Oilgram Price Report; Petroleum Intelligence Weekl Journal; Oil Market Intelligence; Natural Resources Canada; Petroleum Place.

Explanatory Notes

- Countries listed under OPEC and non-OPEC are based on current affiliations. OPEC and non-OPEC averages are based on affiliations fo may differ from current affiliations. Indonesia withdrew from OPEC in January 2009, Angola joined OPEC in January 2007, Ecuador withdr and rejoined in November 2007, and Gabon withdrew from OPEC in July 1996.
- Estimated contract prices based on government-selling prices, netback values, or spot market quotations. All prices are f.o.b. at the foreig noted; 30 day payment plan except where noted.
- Iraq, Kirkuk 36° is the netback price at the U.S. Gulf.
- Total OPEC is the netback price at the U.S. Gulf.
- Total World, United States, OPEC, and Non-OPEC are average prices (f.o.b.) weighted by estimated export volume. For details, see "Calc Explanatory Notes of the Weekly Petroleum Status Report.
- Egypt, Suez Blend 33° is on 60 days credit.
- Effective with the week ending July 6, 2007, Lloyd Blend crude stream data are no longer available; a similar crude stream Heavy Hardist
- Brunei, Seria Light 37° contract prices are no longer available for use in weekly calculations.
- Russia, Urals 32° price (f.o.b.) to Mediterranean destinations; also called Urals.
- United States average price (f.o.b.) is weighted by estimated import volume.
- The Canadian crude prices have been changed to U.S. dollars.

2-8 C

Spot Prices

(Crude Oil in Dollars per Barrel, Products in Cents per Gallon)

Period: Daily

Product by Area	02/10/09	02/11/09	02/12/09	02/13/09	02/17/09	02/18/09
Crude Oil						
WTI - Cushing, Oklahoma	37.54	35.93	34.03	37.63	34.96	34.6
Brent - Europe	45.88	44.24	47.23	43.36	39.69	39.4

2-9 D

PACER ERGY MARKETING, LLC.

Questions on this Payment Call: (918) 585-6790

30640 LITTLE JOE OIL CO Tax Id: xx-xxx2803 Duplicate Cannot Be Furnished - Retain For Tax Purposes

---------Property----------				100% Lease Over Owner Amounts					---100% Net---
IT --Rev Int%--	$/Unit	----Volume---	--Gross Rev--	----Taxes----	--Other Exp--	-----JIB-----			---Your Net---
1546 NELSON			County/State: ALLEN ,KS		Prdn Pd: 02/2009	Product: Oil			
		170.55	3,658.30	15.52	1.60	0.00	3,641.18		
W 0.4375000000	21.450	74.61	1,600.50	6.79	0.80	0.00			1,592.91

PACER ENERGY MARKETING, LLC. 086570

Visit our website at
www.pacerenergymarketing.com

		----Gross----	---Sev Tax---	--Other Exp--	-----JIB-----	--Your Net---	-----W/H-----	--Check Amt--
	This Check:	1,600.50	6.79	0.80	0.00	1,592.91	0.00	1,592.91
Check Nbr: 086570	YTD WI:	1,600.50	6.79	0.80	0.00	1,592.91		
Date: 02/17/2009	YTD RI:	0.00	0.00	0.00		0.00		
	YTD Totals:	1,600.50	6.79	0.80	0.00	1,592.91	0.00	1,592.91

WTI PRICE ON 2-13-09

37.63
- 21.45 was paid
16.18 clock

2-10 E

Produ Period: 01/2009
Statement Date: 02/17/2009

Crude Oil Statement
PACER ENERGY MARKETING LLC
P O BOX 4470
TULSA OK 74159

KAMC OIL & GAS LLC
800 HENRY CIRCLE
FRUITA CO 81521

Field:
State: KANSAS
County: ALLEN
Property Operated By: KAMC OIL & GAS LLC
Lease: 2426 FUSSMAN STATE PRDN ID: 114235

Tank	Date	Ticket	Seal In	Seal Out	Adj Grav	Price	Barrels	$ Value	Taxes	Net $	Deductions	Final Net $
2426-1	01/02/09	150108			20.0	30.1000	8.84	266.08	12.32	253.76	0.11	253.65
							8.84	266.08	12.32	253.76	0.11	253.65

Owner Revenue Allocations

Owner		Int Type	Revenue Interest	Sales Volume	Gross Revenue	Taxes	Other Chg	JIB Chg	Net
13721	FUSSMAN, PHILLIP C	R	0.0312500000	0.28	8.32	0.39	0.00	0.00	7.93
13722	BURTON, KAY F	R	0.0937500000	0.83	24.95	1.16	0.00	0.00	23.79
23322	KAMC GAS & OIL LLC	W	0.8750000000	7.73	232.81	10.77	0.11	0.00	221.93

WTI PRICE on 1-2-09

46.34
- 30.10 was paid
16.24 dock

2-11 E

E
2-12

JV Oil LLC
PO Box 151
Chanute KS 66720

John Galemore (918)-629-1776
Victor Hood (620)-433-1692

PLAINS 1995-2002							
Date	BBLS	WTI	Paid	Difference	Percentage	Load Fee	Land Owner $ Lost
11/03/95	75.00	$17.93	$15.88	$2.05	11.43%	$153.75	$ 19.22
11/24/95	63.00	$17.93	$15.91	$2.02	11.27%	$127.26	$ 15.91
02/12/96	70.00	$18.01	$18.05	-$0.04	-0.22%	-$2.80	$ (0.35)
02/26/96	80.00	$19.45	$18.05	$1.40	7.20%	$112.00	$ 14.00
03/15/96	77.00	$21.99	$20.48	$1.51	6.87%	$116.27	$ 14.53
04/04/96	76.00	$22.75	$21.21	$1.54	6.77%	$117.04	$ 14.63
10/21/96	76.00	$25.85	$24.12	$1.73	6.69%	$131.48	$ 16.44
11/05/96	68.00	$22.65	$20.84	$1.81	7.99%	$123.08	$ 15.39
11/23/96	72.00	$24.15	$22.33	$1.82	7.54%	$131.04	$ 16.38
11/15/99	60.00	$25.31	$22.25	$3.06	12.09%	$183.60	$ 22.95
05/25/02	86.00	$26.69	$21.75	$4.94	18.51%	$ 424.84	$ 53.11
06/05/02	156.00	$25.02	$21.00	$4.02	16.07%	$ 627.12	$ 78.39
07/13/02	157.00	$27.48	$23.50	$3.98	14.48%	$ 624.86	$ 78.11
07/15/02	73.00	$27.23	$23.00	$4.23	15.53%	$ 308.79	$ 38.60
07/22/02	154.00	$26.61	$22.50	$4.11	15.45%	$ 632.94	$ 79.12
08/14/02	157.00	$28.19	$24.25	$3.94	13.98%	$ 618.58	$ 77.32
09/05/02	110.00	$29.06	$25.00	$4.06	13.97%	$ 446.60	$ 55.83
09/09/02	152.00	$29.80	$25.75	$4.05	13.59%	$ 615.60	$ 76.95
10/02/02	153.00	$30.59	$26.50	$4.09	13.37%	$ 625.77	$ 78.22
10/15/02	152.00	$29.73	$25.75	$3.98	13.39%	$ 604.96	$ 75.62
11/04/02	141.00	$26.89	$23.00	$3.89	14.47%	$ 548.49	$ 68.56
12/03/02	162.00	$27.34	$23.25	$4.09	14.96%	$ 662.58	$ 82.82
12/15/02	158.00	$28.39	$24.50	$3.89	13.70%	$ 614.62	$ 76.83
						$8,548.47	**$ 1,068.56**

EIP Releases Report on U.S. Refinery Expansions to Process Dirty Oil from Canadian Tar Sands

Tar Sands - Feeding U.S. Refinery Expansions with Dirty Fuel

Jun 4, 2008

Over two thirds of currently planned expansions of U.S. oil refining capacity are intended to accommodate heavier, dirtier crude oil from Canadian "tar sands," according to data on U.S. oil refinery permitting activity under the Clean Air Act ("CAA") recently compiled and analyzed by the Environmental Integrity Project. Out of the approximately 1.6 million barrels per day ("bpd") of increased refining capacity currently in the pipeline, about 1.1 million bpd will be devoted to refining tar sand oil. In addition, more than 800,000 bpd of existing conventional crude capacity is planned to be modified to process oil from tar sands, so that the total increase in tar sands capacity is over 1.9 million bpd, while conventional crude capacity is undergoing a net decrease of over 300,000 bpd. This is equivalent to constructing more than sixteen new refineries dedicated to tar sands. Refining tar sand oil will result in higher air emissions of harmful pollutants such as sulfur dioxide, hydrogen sulfide, sulfuric acid mist, and nitrogen oxides, as well as toxic metals such as lead and nickel compounds. The consequences of tar sand oil extraction include the clear-cutting and strip-mining of huge portions of intact boreal forest ecosystem, the creation of vast un-reclaimable toxic lakes of wastewater, the consumption of enormous amounts of water and energy, and the production of three times more greenhouse gas as extracting conventional crude oil.

Tar Sand's Biggest Customer Has Second Thoughts

OIL SANDS-PART 3:
Biggest Customer Has Second Thoughts

Chris Arsenault*

FT. MCMURRAY, Oct 20 (IPS) - As Canada's tar sands extraction expands full steam ahead, a perfect storm of internal and external opposition could derail some of the voracious growth at the world's largest energy project.

Together, skyrocketing construction costs, falling crude prices, increasingly vocal opposition from some native groups, and a little known section of the 2007 U.S. Energy Independence and Security Act all threaten growth projections in northern Alberta.

"If I was an investor, I wouldn't want to take the risk of putting money into the tar sands right now," said Liz Barratt-Brown, a senior attorney at the Natural Resources Defence Council, an NGO leading U.S. lobbying efforts against Canada's heavy oil industry.

Canada is the largest foreign exporter of oil to the United States, with Alberta's tar sands sending roughly 500,000 barrels to the U.S. every day. Losing access to the U.S. market would significantly affect expansion plans.

And Canadian oil industry lobbyists are concerned about section 526 of the U.S. Energy Independence and Security Act of 2007 which bars U.S. federal agencies such as the military and the postal service from buying synthetic or unconventional fuels if they create more greenhouse gases emissions than conventional fuels.

"It was just one of those funny stories in Washington where this section [526] was overlooked," Greg Stringham from the Canadian Association of Petroleum Producers told IPS. "I don't think Canadians or oil companies knew about this section."

Between January and September of this year, Canadian oil lobbyists pushed hard to have section 526 amended or repealed, Barratt-Brown told IPS. Unlike other provinces, Alberta maintains its own special interests office in Canada's embassy in Washington.

In February 2008, Canada's ambassador to the United States, Michael Wilson, wrote to the U.S. defence secretary arguing that Canadian tar sands oil should not be included in the interpretation of this section.

Then on Mar. 17, Democratic Senator Henry Waxman, chair of the House Oversight and Government Reform Committee and author of the legislation, wrote a letter to Chairman Jeff Bingaman of the Senate Energy and Natural Resources Committee clarifying the meaning of section 526.

Waxman said section 526 of the Act prohibits U.S. government agencies, including the military, from purchasing "fuels derived from tar sands".

Lobbying continued throughout the spring. Two Republicans from Texas, Reps. Jeb Hensarling and Mike Conaway, sent a letter in late March to other members of the House of Representatives stating: "Section 526 would be problematic enough if it were clear and straightforward, however, the language contains several ambiguities, causing a flurry of attempts at legislative interpretation by the Air Force, the Canadian government, [and] the Centre for Unconventional Fuels [an industry lobby group]."

To counter anti-tar sands campaigners, the Alberta government launched a 21-million-

dollar advertising campaign in April aimed at improving the province's brand.

Environmentalists claimed victory in late September, when the Defence Authorisation Bill passed without weakening or amending section 526. Oil industry lobbyists say environmentalists haven't won any victory and U.S. institutions will continue purchasing tar sands oil.

"This will be the first time government agencies have to look at greenhouse gas emissions for purchasing policies and that's positive," Barratt-Brown told IPS.

Oil from Canada's tar sands creates roughly three times the GHG emissions as conventional crude, according to environmentalists.

While environmentalists are claiming victory, plans in the U.S. are going ahead to retrofit old refineries to process tar sands synthetic crude, a sign that some industry players are not concerned about new legislation. U.S. drivers in Colorado, Ohio, and Indiana are already burning gasoline derived from tar sands oil.

"I was in Whiting, Indiana recently, where they are retrofitting one of the oldest refineries the U.S. to process tar sands crude," Thomas Clayton-Muller, with the Indigenous Environmental Network, told IPS. Much of his community in Alberta is opposed to the development because of local health effects and broader environmental concerns, according to Clayton-Muller.

In January 2007, Governor Arnold Schwarzenegger announced that California would require a 10-percent reduction in carbon content from all fuels sold in the state by 2020, which would effectively ban imports from the tar sands.

The U.S. Conference of Mayors passed a resolution in June calling for an end to unconventional oil imports. "Our cities are asking for environmentally sustainable energy and not fuels from dirty sources such as tar sands," said Eugene, Oregon Mayor Kitty Piercy, who submitted the resolution.

Despite the actions of individual cities and the California's state government, the military is the largest consumer of transportation fuel in the U.S., so its interpretation of Section 526 and future purchasing habits are crucial.

From the office tower of the Canadian Association of Petroleum Producers in downtown Calgary, Greg Stringham is within a 15-minute walk from 150 oil companies and "rumours spread fast".

Stringham doesn't seem overly concerned about anti-tar sands legislation in Washington. He wouldn't comment directly on what a Barack Obama-Joe Biden Democratic administration and increased concerns about global warming could mean for the industry except to tell IPS: "I'm not confident of anything."

"Clearly the oil sands is the most high-impact oil available," Simon Dyer of the Pembina Institute, an environmental watchdog, told IPS. "The oil sands are three times as greenhouse gas-intensive as regular oil," said Dyer, adding that roughly three barrels of water are required to process one barrel of heavy oil.

Tar sands production is set to increase from its current 1.2 million barrels of oil per day, to some 3.0 million barrels per day by 2018, most of which is slated for export to the United States.

U.S. EPA says NO to Tar Sands Refinery

Posted by mhudema on June 12, 2008

U.S. EPA Rejects ConocoPhillips Refinery Expansion

CHICAGO, Illinois, June 10, 2008 (ENS) - In a case that could affect oil refineries around the country, plans by ConocoPhillips to expand its refinery in Roxana, Illinois were sidelined on Friday when an appeal board of the U.S. Environmental Protection Agency upheld a challenge to the air permit required for the project.
The decision sends ConocoPhillips and the Illinois EPA, which had granted the permits for the Wood River refinery expansion, back to the drawing board.

The legal challenge mounted by environmental groups in August 2007 argued that harmful air pollution from the refinery's flares, which relieve pressure in the refining process, was not being sufficiently controlled.

The Natural Resources Defense Council led the challenge representing American Bottom Conservancy, a nonprofit organization based in the Metro East St. Louis area.

The Sierra Club was represented by the Environmental Integrity Project.

"This is a huge win for anyone living near a refinery, but especially the communities in the Metro East area and for St. Louis," said Ann Alexander, senior attorney for the Natural Resources Defense Council and lead litigator on the challenge.

"Excessive emissions from this expanded refinery would have harmed the health of everyone in the region," she said.

Worker at ConocoPhillips Wood River refinery (Photo courtesy ConocoPhillips)

The Wood River Refinery is ConocoPhillips' largest in the United States. The company seeks to invest an estimated $1 billion to add a second coker, or crude oil processor.

The refinery expansion is connected to ConocoPhillips' development with TransCanada Pipelines of a proposed 1,840 mile pipeline from Hardisty, Alberta.

ConocoPhillips wants to expand the refinery to process crude oil extracted from Canadian tar sands, an energy source that the environmentalists point out generates three times more greenhouse gases than gasoline made from conventional oils.

At issue are the burning columns of waste gas known as flares that can be seen for miles, and which emit dangerous pollutants. NRDC attorneys contend that refineries elsewhere have reduced flaring through better design and improved management practices.

The challengers claimed that state officials have hindered local community input on the ConocoPhillips Roxana project and ignored "readily available, proven safeguards used widely at similar facilities nationwide."

"At a time of record oil profits, this decision ensures ConocoPhillips will invest in protections for the surrounding communities, rather than pushing the cost of pollution onto taxpayers in the form of respiratory illness, hospital bills, and lost time at work," said Alexander. "We hope this will become the norm at all oil refineries in the United States."

"Illinois EPA ignored the simple rules required by law," said Kathy Andria, president of American Bottom Conservancy and a member of the Illinois Sierra Club Clean Air Campaign. "Citizens should not have to file legal appeals to see that the Clean Air Act is enforced or that a state agency does the job it is supposed to do to protect their communities."

Alexander points out that California refineries have been held to a higher standard than those elsewhere in the United States when it comes to cutting pollution from their flares.

"There is no reason that people in San Francisco or L.A. should have better protections than people elsewhere in the country. EPA is sending a message to oil refineries around the nation that it is time they clean up," she said.

"This expansion project would not do anything to bring down gas prices right now," said Alexander. "The ConocoPhillips refinery is expanding to process Canadian tar sands oil, which is profitable only if crude prices stay high."

"We are not asking for hugely complicated or costly measures," Alexander said. "Holding flare emissions down just requires sound engineering and responsible operating practices."

Without the expansion, the Wood River Refinery refines approximately 306,000 barrels of oil per day to produce gasoline, jet fuel, diesel, asphalt, propane and other products, and supplies part of the St. Louis region, Chicago, Indiana and Ohio.

SEC. 526. PROCUREMENT AND ACQUISITION OF ALTERNATIVE FUELS.

No Federal agency shall enter into a contract for procurement of an alternative or synthetic fuel, including a fuel produced from nonconventional petroleum sources, for any mobility-related use, other than for research or testing, unless the contract specifies that the lifecycle greenhouse gas emissions associated with the production and combustion of the fuel supplied under the contract must, on an ongoing basis, be less than or equal to such emissions from the equivalent conventional fuel produced from conventional petroleum sources.

Energy: Canadian oil in Cushing spurs antitrust inquiry

OFFICIALS SAY LOW PRICES ARE UNDERCUTTING LOCAL PRODUCERS

BY RANDY ELLIS
Published: March 4, 2009

The Oklahoma attorney general's office has opened a preliminary inquiry into concerns that oil from Canada possibly is being dumped on Oklahoma markets in potential violation of state and federal antitrust laws, Attorney General Drew Edmondson confirmed Tuesday.

"The situation is serious to begin with because it's impacting (Oklahoma) oil production," Edmondson said. "If it's both serious and a violation of law, then we will definitely take steps."

Edmondson said he became concerned about the situation last week after meeting with Oklahoma oilmen Harold Hamm, Mickey Thompson and Mike Cantrell.

Hamm is chairman and chief executive officer of Continental Resources Inc. of Enid, Thompson is former president of the Oklahoma Independent Petroleum Association, and Cantrell is an Ada independent oil and gas producer. Hamm and Cantrell also are both board members of the OIPA.

Edmondson said the three oilmen expressed concerns about oil coming into Oklahoma from Canada and "arriving at Cushing at a price they suggested was below actual and below market and, in essence, freezing out local producers from the Cushing supply area."

"They raised the possibility that this was an unfair trade practice that may be a violation of both state and federal anti-trust laws," Edmondson said.

What they discussed

Edmondson said he asked the men to suggest someone with expertise in petroleum pricing and markets to assist his anti-trust lawyers in determining whether an unfair trade practice exists.
"We're awaiting that and will take it from there once we get that information and that contact," Edmondson said.

Hamm and Thompson both told *The Oklahoman* they believe it costs about $60 a barrel to produce the Canadian oil that is being sold in Cushing on the New York Mercantile Exchange for about two-thirds that amount.

"The last I knew, it was illegal to bring materials in below the cost of production,"

Hamm said. "It's a ripe area for investigation."

What's the impact?

The effect on Oklahoma oil producers has been dramatic, Hamm said. Traditionally, Oklahoma sweet crude oil has brought about $2 more a barrel at Cushing than similar Brent Crude oil that comes from overseas, he said.

"Now we're at a severe discount ... recently as much as $10 a barrel ... (compared) to Brent," Hamm said.

On top of that, the companies that buy oil from Oklahoma producers are paying as much as $6 a barrel less than the price being paid at Cushing. As a result, Oklahoma oil producers are getting as much as $16 a barrel less for their oil than world oil prices, Hamm said.

Since gross production taxes are based on those prices, it's very costly to the state, he said.

Related Topics: Science and Technology, Technology, Political Policy, Politics, Business, Trade Policy, Corporate Crime, Antitrust Crime, Trade, Oil Production and Refining, Energy Technology, International Relations, Fair Trade

Is this drew running for governor? Seems they would keep this story quiet until they had evidence to back up the claim.

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and an Insurance Practices Act, [16] prohibiting statutorily defined or administratively determined unfair methods of competition in the business of insurance. [17]

2. Discrimination

As previously noted, Kansas statutes do not contain an analogue to the Robinson-Patman Act.

a. Price Discrimination

Kansas statutes contain no analogue to Section 2(a) of the Robinson-Patman Act.

b. Brokerage

Kansas statutes contain no analogue to Section 2(c) of the Robinson-Patman Act.

c. Payments for Services or Facilities

Kansas statutes contain no analogue to Section 2(d) of the Robinson-Patman Act.

d. Provision of Services or Facilities

Kansas statutes contain no analogue to Section 2(e) of the Robinson-Patman Act.

e. Buyer Liability

Kansas statutes contain no analogue to Section 2(f) of the Robinson-Patman Act.

f. Territorial or Locality Discrimination

Kansas statutes do contain a proscription against locality price discrimination. [18] The state statute prohibits underselling in particular localities for the purpose of destroying competition. The state statute applies only to entities or persons "doing business in the state of Kansas, and engaged in the production,

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[16] Kan. Stat. Ann. §§ 40-2401 to -2414 (1986 & Supp. 1989).

[17] The Kansas Fair Trade Act, Kan. Stat. Ann. §§ 50-301 to -310, passed in 1937 and repealed in 1963, and the Kansas Unfair Practices Act of 1941, Kan. Stat. Ann. §§ 50-401 to -408, repealed in 1961 (prohibiting sales below cost), were repealed after being declared unconstitutional and have not been replaced.

[18] Kan. Stat. Ann. § 50-149 (1983).

manufacture, distribution, sale or purchase of any commodity in general use," [18] and prohibits not only the selling at a lower rate, but also the buying at a higher rate, of any such commodity. The statute additionally provides that price discrimination is to be determined only "after equalizing the distance from the point of production to the factory, for distribution, and freight rates therefrom." [19] Unlike Section 3 of the Robinson-Patman Act, the state statute does not expressly prohibit acts taken for the purpose of "eliminating a competitor." [20] No reported decisions have construed the state statute.

g. The Meeting Competition Defense

Kansas statutes currently contain no analogue to the meeting competition defense set forth in Section 2(b) of the Robinson-Patman Act. From 1941 to 1961, Kansas had an Unfair Practices Act which contained a provision stating that the Act "shall not apply to sales . . . at wholesale . . . where the price of merchandise is made in good faith to meet the price of a competitor in the same locality . . . " [21] In one case, the Kansas Supreme Court found that sales of cigarettes at $1.605 per carton at less than cost to the wholesaler fell within that exemption, and reversed the trial court's finding to the contrary. [22] The Unfair Practices Act contained an exemption for grain and feed dealers, which was subsequently found to amount to an "arbitrary, fictitious and unreasonable statutory discrimination." [23] The court held this exemption was not severable from the remainder of the Act, and therefore held the entire Act unconstitutional. [24]

h. Other Defenses

Kansas statutes contain no analogues to the Robinson-Patman Act's defenses of cost justification, [25] selection of customers in *bona fide* transactions, [26] or changing conditions. [27] The sole defense set forth in the Kansas statutes regarding antitrust, discrimination in restraint of trade or unfair competition, and applicable to a charge of price discrimination, is for acts done in compliance with certain federal laws, codes, or regulations. [28] Specifically, proof that the act complained of was done "in compliance with the provisions of any code, agreement, license, rule or regulation in effect under the terms of the national industrial recovery act [long since

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[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] Kan. Stat. Ann. § 50-405 (G.S. 1947 Supp.).

[22] *State ex rel. Anderson v. Commercial Candy Co.*, 166 Kan. 432, 201 P.2d 1034 (1949).

[23] *State ex rel. Marshall v. Consumers Warehouse Mkt., Inc.*, 185 Kan. 363, 369, 343 P.2d 234, 240 (1959).

[24] *Id.*

[25] 15 U.S.C. § 13(a) (1988).

[26] *Id.*

[27] *Id.*

[28] Kan. Stat. Ann. § 50-157 (1983).

MEDIA RELEASE

KAIROS study reveals billions in Canadian tax subsidies to Big Oil come at the expense of conservation and climate

TORONTO Apr 15, 2008

TORONTO - The federal government has confirmed that it will spend $1.5 billion dollars in additional subsidies to tar sands companies as a result of its slow phase out of tax breaks for one of Canada's largest greenhouse gas emitting (GHG) industries. And ***Pumped Up***, a new KAIROS study, concludes that by 2012 GHG emissions from the tar sands alone may wipe out all anticipated reductions in GHG emissions from all federal government programs.

The government confirmed the tax break figures in its responses to a formal petition filed with the Auditor General of Canada by KAIROS: Canadian Ecumenical Justice Initiatives, a church-based social justice organization. KAIROS' analysis of likely GHG emission reductions is based on the federal government's own figures.

The petition was filed last November and the government was legally required to respond within 120 days. While the government provided answers to some questions, it failed to respond to the key question at the heart of the petition.

"Why does Canada spend millions of dollars on subsidizing oil and gas industries - a prime cause of climate change - and so little money on green alternatives when the majority of Canadians want action to reduce greenhouse gas emissions? That was the essential question we asked the government," says John Dillon, a KAIROS Program Coordinator and co-author of *Pumped Up: How Canada subsidizes fossil fuels at the expense of green alternatives*. "The government didn't answer that core question."

The KAIROS study calls for redirecting subsidies from fossil fuels to energy efficiency, conservation and renewable alternatives. In addition, Canada must put firm caps on emissions from large industries and mandate stricter vehicle emission standards and energy product efficiency standards. In letters from the ministers of finance, environment, foreign affairs, international trade, natural resources and international cooperation, the government gives no indication that it plans a major shift in spending away from tax breaks for big oil towards spending on green, renewable energy sources.

"The government seems to be taking a business as usual approach in terms of its energy policy," says Ian Thomson, of KAIROS and a co-author of Pumped Up. "What's revealing about these responses is how much the government was unable or unwilling to tell us. For instance, it failed to quantify the total size of subsidies in dollar amounts going to the oil and gas sector, as requested."

Ecojustice, the environmental law group formerly known as Sierra Legal Defence Fund, also filed a formal petition on the subsidies issue last November. It isn't satisfied with the government's responses either.

"The Harper government gives almost $1 million of taxpayer money to the tar sands industry every day

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with this single subsidy. Leaving aside the absurdity of this spending, imagine the great opportunities the federal government is squandering by not dedicating this money to renewable energy, mass transit, and energy conservation," says Albert Koehl, an Ecojustice staff lawyer.

Between 1996 and 2002 the federal government spent approximately $8 billion on tax subsidies for Canada's oil and gas industries. KAIROS and Ecojustice wanted the government to provide current figures, given the huge increase in tar sands developments. However, the government did not provide enough information to allow an assessment of the impact of subsidies on GHG emissions.

The Ministers did provide some useful information about some government activities. For example, the Department of Foreign Affairs is monitoring the negative impact of biofuel production on world agricultural production and access to food. However, given the significant gaps related to the petitions' key questions, KAIROS and Ecojustice are contacting the Commissioner of the Environment in the Auditor General's office to request that answers be provided.

The groups say they will continue to press government to redirect subsidies from the hugely profitable oil and gas companies into green alternatives. For KAIROS, the petition and Pumped Up are part of Re-energize, its public engagement and advocacy program aimed at getting individuals, communities and government to reduce their carbon footprint.

"The serious energy questions we are facing are, at their heart, spiritual in nature for the churches," says Dorothy McDougall, KAIROS Ecological Justice Program Coordinator. "We need to understand our deep interconnections with the rest of creation."

For further information about the KAIROS public engagement program on energy visit www.kairoscanada.org or go directly to the Re-energize site at www.re-energize.org.

For more information, please contact:

Adiat Junaid, KAIROS: Canadian Ecumenical Justice Initiatives (416) 463-5312 ext. 223
Albert Koehl, Ecojustice (formerly Sierra Legal Defence Fund) (416) 533- 1231

Related content

- Case Oil and Gas Subsidies Complaints
- Media Release Misdirected spending: Groups demand investigation into billions in federal subsidies to Canada's booming oil and gas industry
- Story Oil Subsidies: Finally, some light at the end of the funnel

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2-25

HOUSE UTILITY COMMITTEE
MARCH 12, 2009
RE: Kansas Oil Production: Is supply & demand working?

Testimony of David P. Bleakley - Legislative Chairman
Eastern Kansas Oil and Gas Association
&
Director of Acquisitions & Land Management
Colt Energy, Inc.

The Eastern Kansas Oil and Gas Association (EKOGA) association represents and supports eastern Kansas oil and gas producers, service companies, royalty owners and associated businesses along with the overall welfare of the Kansas oil and gas industry in this state.

MY BACKGROUND

For the past 20 years, I have served as the Director of Acquisitions and Land Management for Colt Energy, Inc., an independent oil and gas company with operations located throughout Eastern Kansas. I am currently and have been a Kansas royalty owner for over thirty years. For 10 years prior to my employment with Colt, I owned an oil and gas company operating and producing oil in three Eastern Kansas counties and I also farmed and co-managed a 5,000 acre family farm and oversaw 200 head of registered Angus cattle. I am a graduate of Kansas State University with a degree in Animal Science and Industry. For the past eleven years I have also served as the EKOGA representative to the Kansas Corporation Commission Oil and Gas Advisory Committee and the KCC Rules and Regulations Sub Committee.

Kansas Oil Production: Is supply & demand working? The following will outline the supply of Eastern Kansas oil and the factors that create demand as we know them.

SUPPLY OF EASTERN KANSAS OIL

Typical process by which an oil producer drills for or acquires oil production.

1. Geology and/or historic well information leading an oil company to believe oil production can be found and produced in a particular location on a particular property.

2. Contact the landowner that owns that particular property and attempt to negotiate an oil and gas lease (contract) laying out the terms and rights of the oil company to explore, drill and produce oil from that desired property.

3. If the oil company and landowner come to terms on a lease, then the oil company will drill a well on such property and if they are successful in finding oil, then they will build a pipeline from the well to a storage facility for handling and process oil for sale to a crude oil purchaser.

4. If an oil company acquires existing production, then the above exploring, drilling and finding oil has already occurred to the point of production.

5. The next step for the oil company in the process is to contact various crude oil purchasers to see who has the best price and service to pick up the oil from the oil companies storage facility.

6. Then once the oil company has produced enough oil in its storage facility to sell a "load" (approximately 150 bbls) to the crude oil purchaser they will call in for a pick up.

CRITERIA FOR CRUDE OIL PICK UP

a. The oil company must provide a good and safe access to the storage facility for the crude oil purchaser or the purchaser may elect not to pick up such oil.

b. The oil company must make sure the oil for sale in the storage facility meets the criteria set forth by the crude oil purchaser to have such purchaser accept such oil and transport from the storage facility to the refinery for sale. If the oil company's oil does not meet such criteria, then the crude oil purchaser will turn down such oil and not pick it up or some companies will elect to pick up such oil and discount it because it becomes off spec oil and will require further treatment at the crude oil purchaser's facility.

c. The oil company must provide proof of title for all interest owners including the landowners for the crude oil purchaser to make the proper payment to each interest owner in the well or lease.

d. The crude oil purchaser requests that the oil company build enough oil storage to allow for a one stop pickup so they do not have to make multiple stops to fill a tank truck.

COMMON DEDUCTIONS OR ADJUSTMENTS TO ARRIVE AT A CRUDE OIL PRICE PAID TO THE OIL COMPANY

a. The gravity (Quality) of the oil. The price of oil is based on 40° oil which has the visual appearance and physical consistency of the soft drink Coke. 20° oil has the visual appearance and physical consistency of dark molasses. For every 1° below 40° there is a $ .15 deduction.

b. All oil is adjusted to 60 degrees Fahrenheit.

c. BS&W (Basic sediment and water) i.e. sand, clay, limestone & formation water.

d. Split loads – multiple stops to pick up enough oil to fill up a crude oil transport. Negotiated between the Oil Company and crude oil purchaser.

e. Quick pay – settlement within seven days of oil pick up. Can result in $5.00 deduct per barrel. Most oil is purchased in one month and paid for by the crude oil purchaser by the 20th of the next month (normal settlement period).

f. The further away from the refinery the greater the transportation cost therefore, the larger the deduction of price paid.

7. Eastern Kansas which encompasses the eastern 1/4 to 1/3 of the state produces approximately 9,000 to 10,000 barrels of oil per day.

8. Supply or production from Eastern Kansas historically declines at approximately 12 % per year and tends to stabilizes or slightly increase during prolonged times of higher oil prices. Currently there are several counties in Eastern Kansas that are producing at the same rate they were producing at in1998.

FACTORS THAT CREATE DEMAND OR TIGHT SUPPLIES

1. Worldwide strong economies.

2. Wars or conflicts in major oil producing areas.

3. Unstable governments of major oil producing countries.

4. Supply disruptions due to oil embargos, natural disasters and terrorism.

5. Speculation in the commodities market that there is not enough world supply to meet world demand.

6. Significant declines in production of the major fields around the world.

7. Large areas of potential significant production ruled off limits by governments due to environmental or public concerns (not in my back yard).

8. The bulk of the world oil production and reserves are owned by Governments not private companies.

9. Alternative Energies not living up to expectations.

IN CONCLUSION: Eastern Kansas will continue to supply 8,000 to 10,000 barrels of crude oil per day for many years to come as long as the price per barrel doesn't stay below our lifting cost for a prolonged period of time. Additional technologies along with better efficiency and management practices should allow the oil companies for at least a period of time to keep pace with natural declines in production. Not only are the Eastern Kansas crude oil producers, but all Kansas crude oil producers are fortunate to have three refineries located in our state to help maintain a local market for our crude oil. Unfortunately the Kansas oil producers cannot supply all of the crude oil supply needs of the three refineries in Kansas but, we can continue to be an important part of their mix of local stable crude oil that is unaffected by events outside of this country.

Thank you for allowing me to speak today.

David P. Bleakley

Kansas Crude Oil Supply

Doug Louis, Director
KCC- Conservation Division
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316-337-6200
www.kcc.ks.gov

March 12, 2009
House Energy and Utilities Committee

HOUSE ENERGY AND UTILITIES
DATE: 3/12/2009
ATTACHMENT 4-1

Kansas Crude Oil Fact Sheet

- Oil was first discovered in 1860, Miami County

- Over 350,000 wells have been drilled in search of oil and gas

- Currently there are approximately:
  - 40,000 oil wells
  - 18,000 gas wells
  - 16,000 saltwater injection wells

Number of licensed Kansas operators: 2410

- Daily Crude Oil Production- 97,800 bbls/day
  - Approximately 36 million bbls/year
  - Vast majority of wells produce less than 5 bbls/day

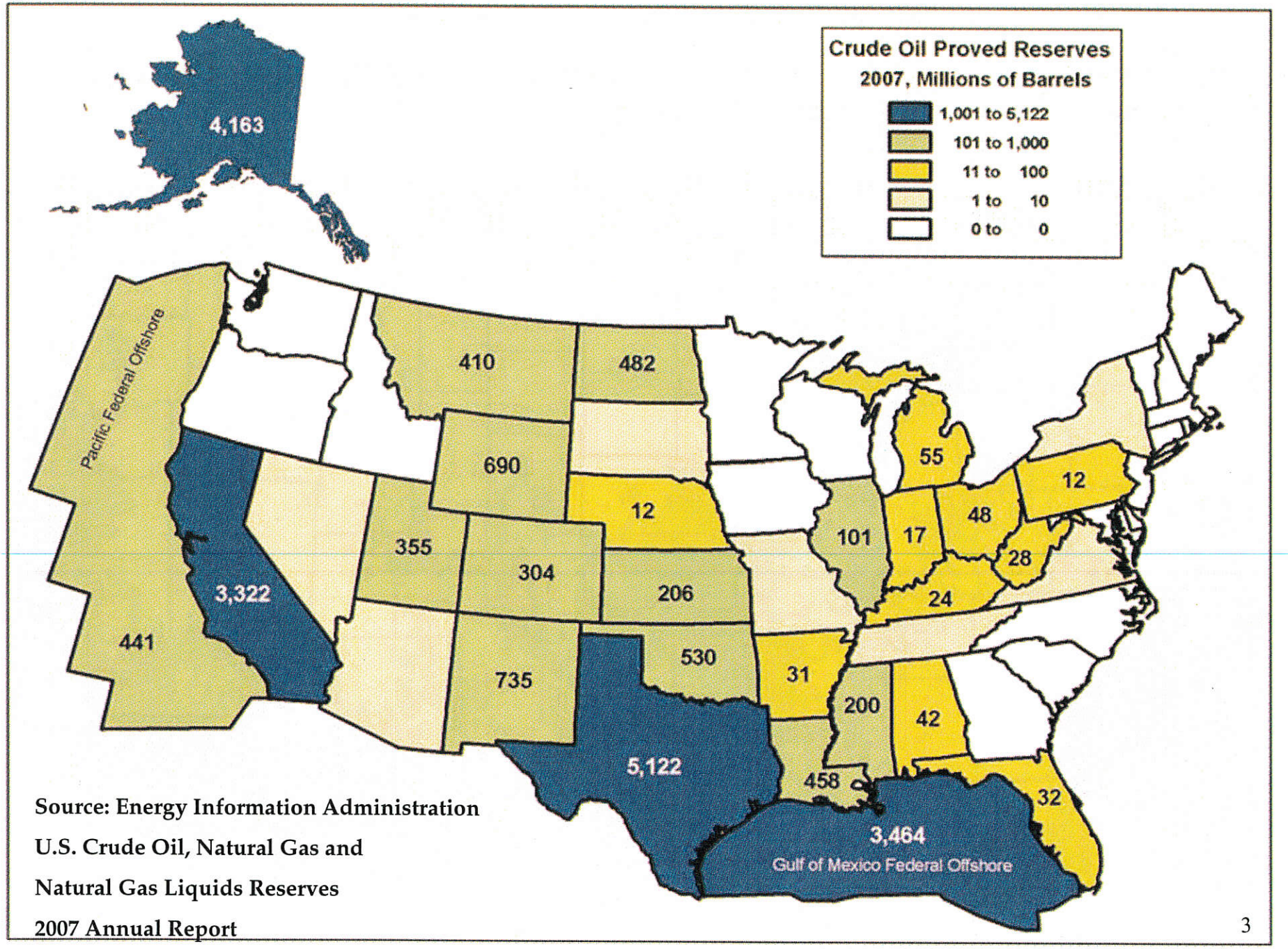
- Kansas ranks 8th in the nation for oil production

- 206 million bbls proved reserves

- Three refineries are located in Kansas

	Refinery Capability
• Coffeyville Resource Refinery & Marketing	115,000 bbls/day
• National Cooperative Refinery Association-McPherson	85,000 bbls/day
• Frontier El Dorado Refinery & Marketing	130,000 bbls/day
	330,000 bbls/day

4-2



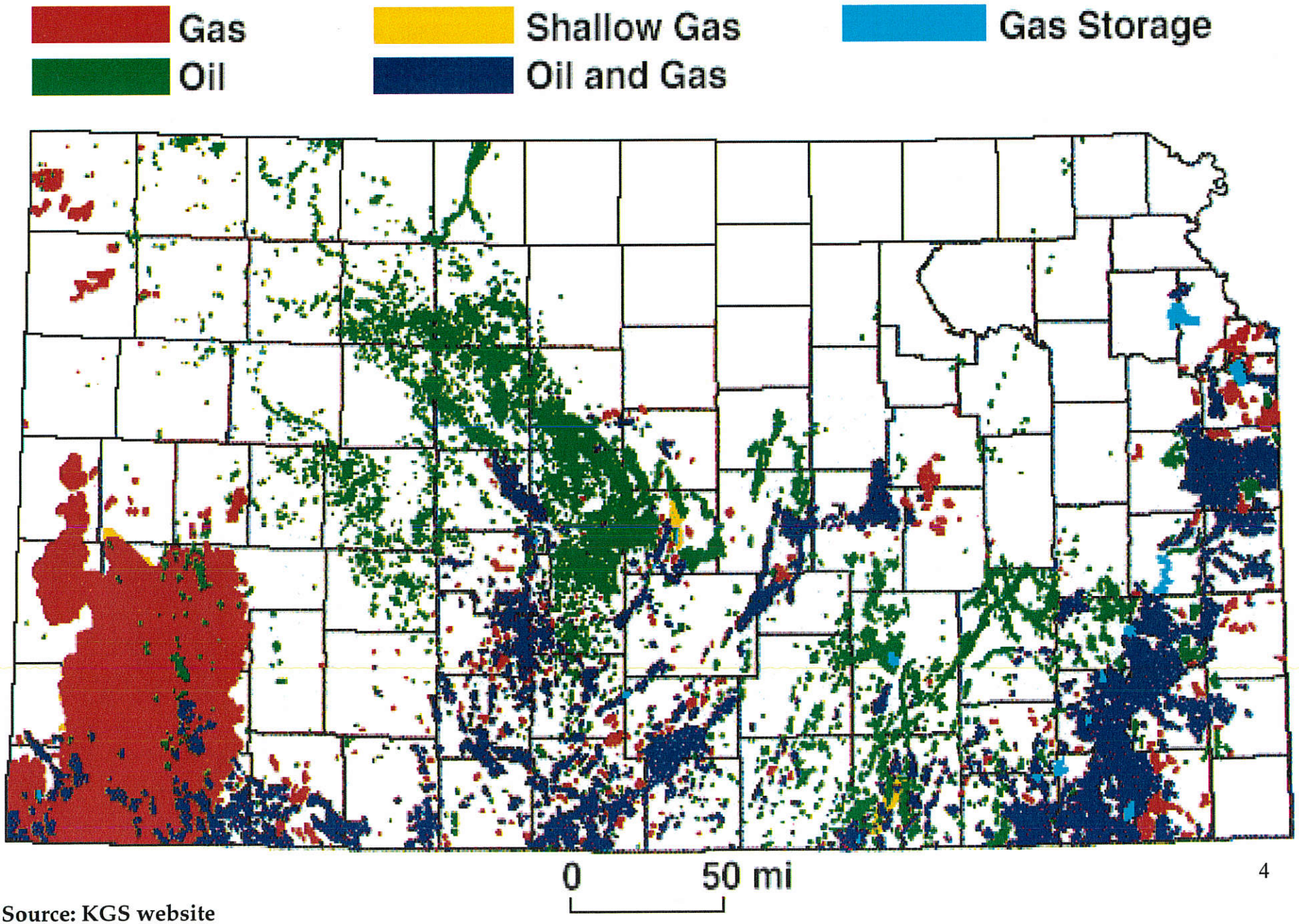
Source: Energy Information Administration

U.S. Crude Oil, Natural Gas and

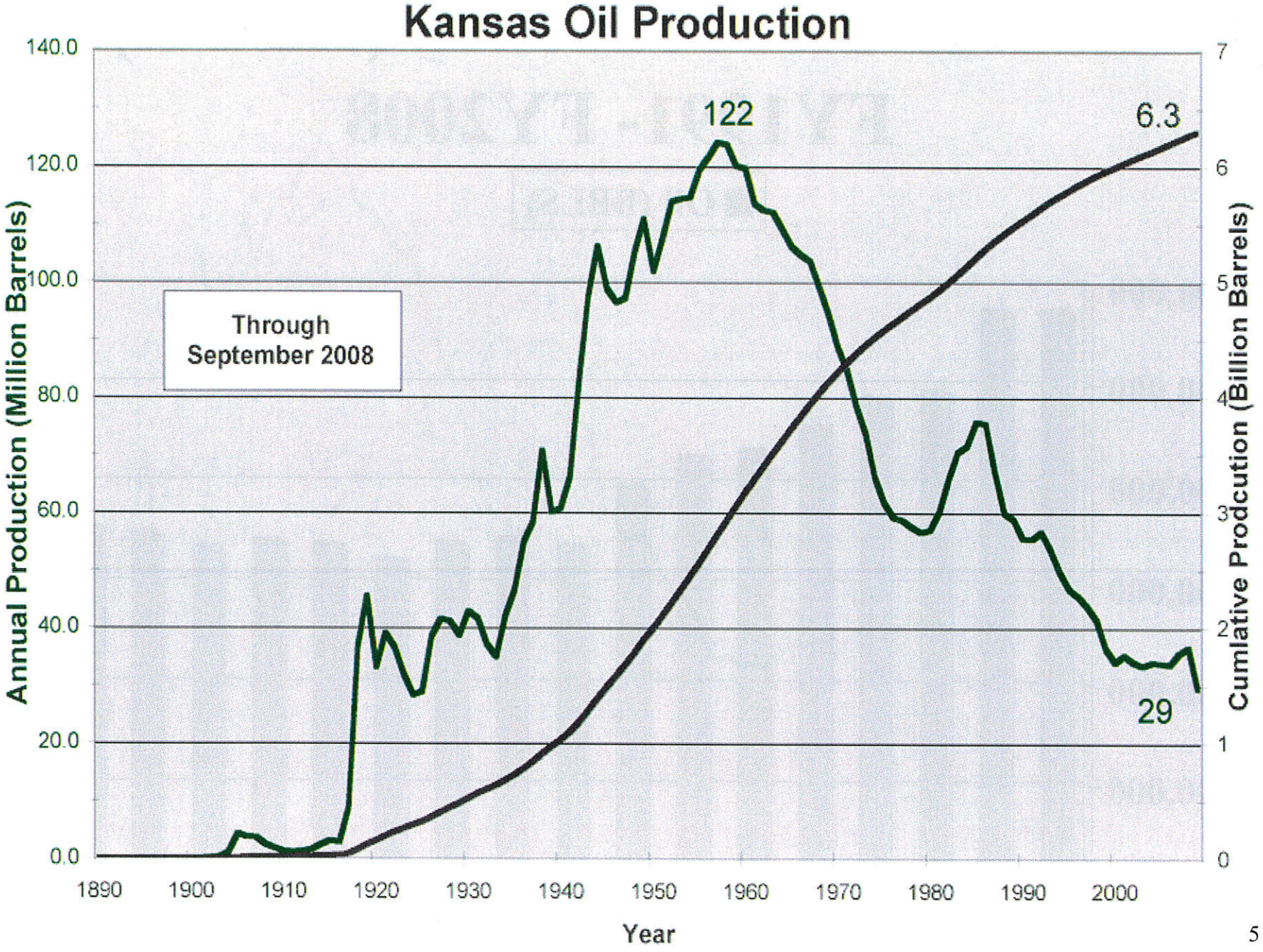
Natural Gas Liquids Reserves

2007 Annual Report

Oil and Gas Fields in Kansas

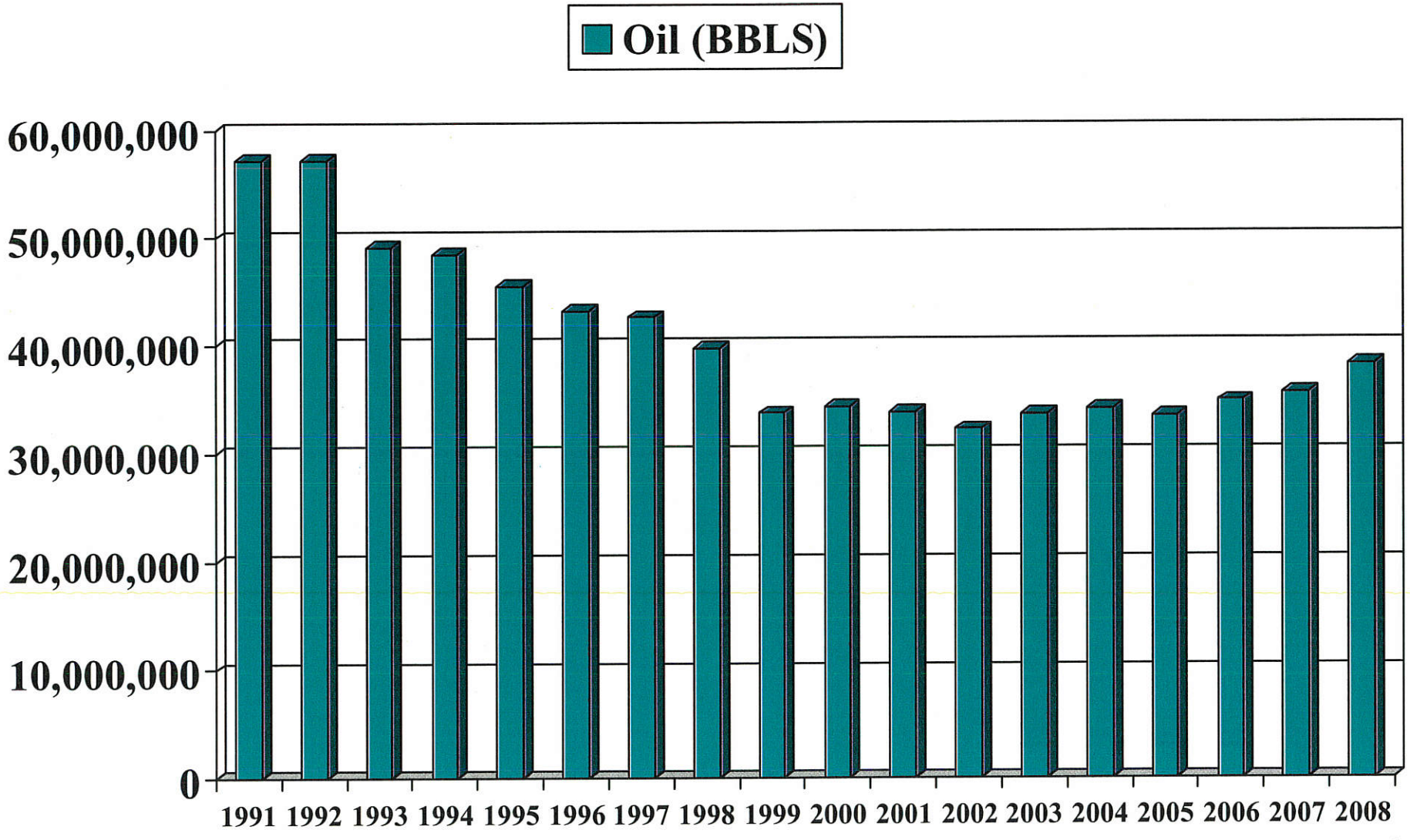


Source: KGS website

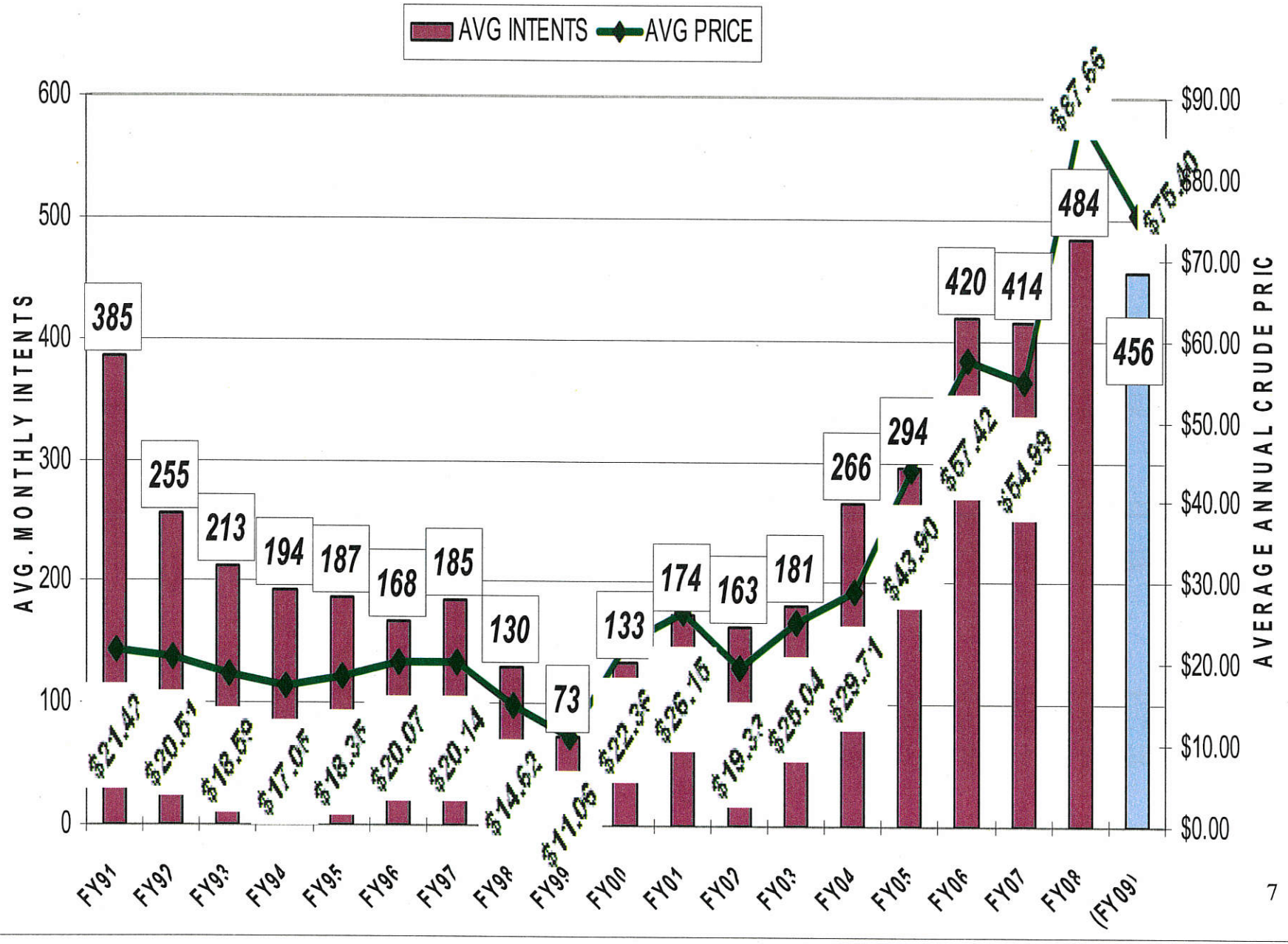


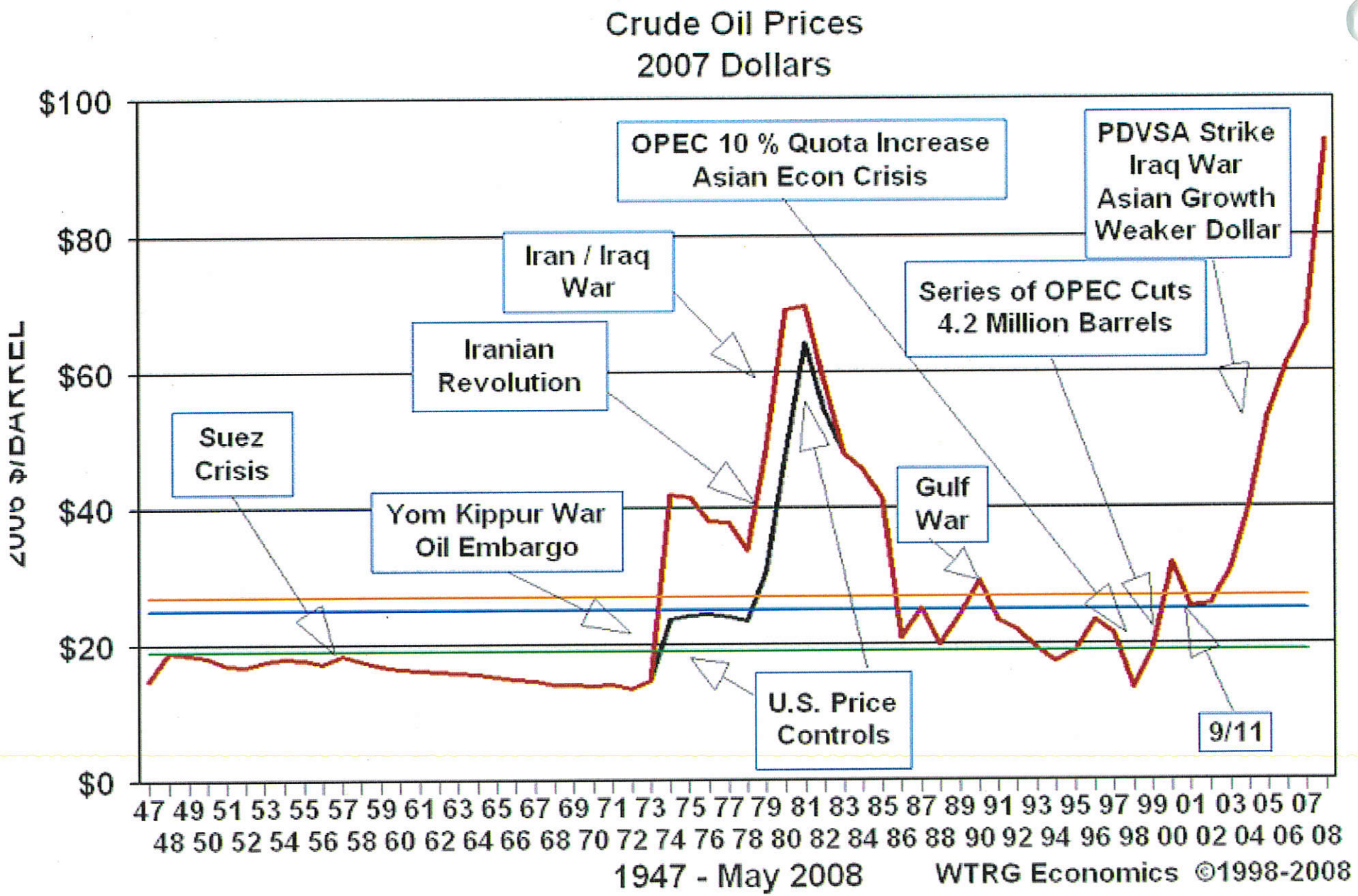
Source: KGS website

Kansas Oil Production (KDOR)
FY1991- FY2008



AVERAGE MONTHLY INTENTS-TO-DRILL
VS. AVERAGE FISCAL YEAR CRUDE OIL PRICE




Crude Oil Prices
2007 Dollars
$100
$80
$60
$40
$20
$0
2007 $/BARREL
OPEC 10 % Quota Increase
Asian Econ Crisis
PDVSA Strike
Iraq War
Asian Growth
Weaker Dollar
Iran / Iraq
War
Series of OPEC Cuts
4.2 Million Barrels
Iranian
Revolution
Suez
Crisis
Gulf
War
Yom Kippur War
Oil Embargo
U.S. Price
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9/11
47 49 51 53 55 57 59 61 63 65 67 69 71 73 75 77 79 81 83 85 87 89 91 93 95 97 99 01 03 05 07
48 50 52 54 56 58 60 62 64 66 68 70 72 74 76 78 80 82 84 86 88 90 92 94 96 98 00 02 04 06 08
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8 - 17

CONDITIONS THAT WILL INFLUENCE OIL PRODUCTION

FAVORABLE FACTORS

Improved Technology Including:

- Polymer treatments
- 3-D seismic
- CO2 injection for enhanced oil production
- Improved hydra-fracing treatments
- Horizontal drilling

ADVERSE FACTORS

- Lower crude oil prices
- Uncertainty of future price
- Reduced funding for research
- Possible stricter environmental laws (e.g. elimination of hydra-fracing exemption)
- Surface usage limitations

INTERSTATE Oil & Gas COMPACT COMMISSION

Crude Oil Market Infrastructure Task Force

EXECUTIVE SUMMARY

Introduction

At the beginning of 2006, domestic crude oil producers in the Rocky Mountain region began to receive much lower prices for their production than similar quality oil sold in other parts of the country. The lower prices resulted from crude oil supplies far exceeding demand. At the same time, a separate set of supply and demand market forces kept prices high for refined products in the region. While crude oil producers bore the brunt of the price collapse, governments at the federal, state and local levels were also impacted as a result of greatly reduced royalty payments, which are based on product sales value. In addition, state and local tax receipts suffered enormous revenue losses as well. The falling value of the crude oil itself could also result in a premature abandonment of the resource and a cutback in domestically produced petroleum –key concerns of the Interstate Oil and Gas Compact Commission (IOGCC).

As a result of these changing market conditions and the glut of crude oil in the Rocky Mountain states, during the first half of 2006 local domestic oil producers in those states were receiving as much as $25 to $30 per barrel less than what was paid for similar quality oil in other regions of the country. While these price differentials have declined to about $6 to $10 per barrel in the last half of 2006, the differentials remain much higher than the historical average of $1 to $3 per barrel. Furthermore, the imbalanced supply and demand conditions that caused the highest differentials in the early part of 2006 remain in place, and may cause further problems in the future.

In May 2006, IOGCC Chairman Dave Freudenthal, Governor of Wyoming, created a task force to specifically identify the reasons that domestically-produced crude oil within the Rocky Mountain region was receiving significantly lower well head prices than similar oil sold in the rest of the country. The task force included representatives from Colorado, Montana, North Dakota, South Dakota, Utah, Wyoming, the Province of Alberta, the U.S. Department of Energy and the Federal Energy Regulatory Commission (FERC). Gov. Freudenthal charged the task force to:

- *investigate the crude oil market dynamics in the Rockies*
- *identify the conditions causing the precipitous price drop, and the expected duration of these conditions*
- *recommend both near and long-term actions that could be taken to correct this situation*

Some of the factors evaluated by the Rocky Mountain task force included the impact of asphalt use, increased crude oil production in the Rockies, increased crude oil production in western Canada, refining capacity, pipeline capacity and crude oil quality variation. Some of the data considered by the task force included the number of new well permits, well completions, production quantities and trends, state tax information, forecasts for Canadian imports and Rockies regional production, existing pipeline and refinery capacities, plans for increasing pipeline and refinery capacities, and existing and proposed state and federal legislation.

This report is the result of the work of that task force.

Background

Prior to 2006, the crude oil markets in the Rocky Mountain states were generally in balance with supplies from local production and imports meeting the needs of the refineries in the region while any surplus production was exported out of the region to other areas of the country. Under these conditions, the price that local producers received for their crude oil was similar to prices throughout the country. However, these conditions changed drastically at the beginning of 2006. A confluence of supply and demand factors came together at that time resulting in a significant over-supply of crude oil in the Rocky Mountain states as compared to demand for that oil. As a result of this oil glut, local producers began to receive prices as much as $25 to $30 per barrel less than similar quality oil sold in other parts of the country. At the same time supply and demand for refined products in the region kept those prices high. While producers bore the bulk of the price collapse; federal, fee, and state royalties as well as state and local tax receipts suffered enormous revenue losses as well.

Factors that contributed to and may continue to contribute to market volatility in the Rocky Mountain region relative to other regions include the following:

- *Supply - Increasing Local Production*
  Crude oil production in the Rockies is no longer declining, and in some areas, dramatic growth in production has occurred. This growth is anticipated to continue over the course of the next five to ten years. Specifically, North Dakota and Montana production, primarily in the Williston Basin, is growing more rapidly than in any other State in the region.

  Twenty years of production decline in Wyoming has been reversed in 2006 as a result of successful enhanced oil recovery operations and condensate production increases in the Jonah/Pinedale area. Growth in the Uintah Basin of Utah and along the Utah Hinge Line area also continues and could accelerate.

- *Supply – Increasing Imports from Canada*
  In May 2005, the Express Pipeline bringing Canadian crude oil into the region expanded its capacity and actual imports of Canadian crude increased by an average 15,000 barrels of oil per day (bpd).

- *Demand – A Decline in Demand by Refineries*
  From January to March 2006 Rockies refinery consumption declined due to refiners reducing demand as they upgraded their facilities to Ultra Low-Sulfur Diesel (ULSD) specifications, shifted from heating oil to gasoline production, scheduled maintenance, and forced outages.

- *Demand - Pipelines Moving Crude Oil Out of the Region*
  The Enbridge Pipeline and the Platte Pipeline are the only two major crude oil pipelines that can move oil out of the region to other parts of the country. The Enbridge Pipeline became full in February 2005. The Platte Pipeline became full in December 2005. Having both pipelines at capacity created a bottleneck limiting the amount of oil that can be moved out of the region.

Conclusions

The task force concluded that extreme crude oil market volatility in several producing regions of the Rockies resulted when limited pipeline and refinery infrastructure was impacted by equipment failures and production growth. Factors that contributed to and may continue to contribute to market volatility in the Rocky Mountain region relative to other regions include the following:

1. While the supply and demand were closer to being in balance since the early summer, excess supplies are still causing significant price differentials, albeit at lower levels.

2. In the next few years, Canadian imports will continue to increase. Canadian imports are reliable supplies from a secure country – i.e., good for energy security. On the other hand, Canadian imports are a concern in the sense that they can overload regional take away

capacity and depress local prices. The key is to eliminate the bottlenecks that prevent oil in the Rockies from reaching destinations where it can maintain higher values.

3. Exporting pipeline capacity is expected to increase, although it is unclear if proposed capacity increases will be adequate.

4. There has been no significant change in refinery capacity in the region of study in the last 20 years. Although incremental expansions are being considered, none have been announced.

5. The production of Canadian heavy sour crude oil and Canadian synthetic crude oil has increased and refinery modifications have concentrated on processing sour crude. Regional U.S. production increases have been predominately sweet crude oil. With refinery demand staying constant, supply is now exceeding demand. The result is more crude oil needs to be exported out of the region; however, the export pipelines are already at full capacity.

6. Those who capitalized upon the changing market conditions and the glut of oil in the Rockies states did so at the expense of diverting supplies that they might otherwise have purchased under spot and term contracts.

7. Additional growth in regional production can be anticipated if prices and demand remain strong. In addition, growth in the Uintah Basin of Utah and along the Hinge Line area also continues and could accelerate. Additional growth can be anticipated in the 2012 to 2015 period if crude oil prices stay at current or higher levels and shale oil is developed.

Recommendations

The task force generally recognized that the underlying issues associated with market dynamics will not change over the short term. The group also concluded that crude oil imports from Canada are extremely important to the nation's energy mix, and the challenges of transportation of these resources to appropriate markets should be addressed.

Without the expansion of infrastructure (pipelines and refinery capacity) and a more coordinated regulatory framework, the continued growth in both Rocky Mountain region and Canadian production will lead to increased crude oil market volatility in the region.

Timing of refining and pipeline expansions is uncertain as market participants attempt to sort out who is going to commit to and pay for new infrastructure.

Ultimately, market forces will prevail and expanded and/or new refinery capacity and expanded and/or new pipeline facilities will be built to accommodate growing production from the region. An unsatisfactory outcome would be for market forces to stunt production growth in the region as market volatility reduces or eliminates the return on exploration and production investment. The ultimate effect of this scenario would be the loss of this resource to U.S. energy consumers.

The Task Force believes that during the time that market forces drive expansion of capacity or construction of new capacity that there are several things that can be done to better educate the marketplace on crude oil dynamics and that IOGCC participants can implement to provide market expansion sooner rather than later:

1. The IOGCC should commission an annual study of each critical pipeline hub within the United States. This study should examine the volume of incoming crude, including local production and imports, with the available takeaway capacity, including refining consumption and pipeline export capacity. These results should be used to proactively promote pipeline and refinery development or other solutions that ensure a "healthy" marketplace.

2. The IOGCC should provide a platform where crude oil pipelines serving major hubs post capacity and aggregated, nominated volumes on a monthly basis.

Recommendations Cont'd

This platform would include current and historical information in order to increase transparency to the marketplace and provide producers and marketers a useful tool from which to determine if they need to add capacity to their markets.

3. The FERC should continue to adopt policies that promote infrastructure development.

4. The IOGCC should form a task force comprised of one regulatory member from each State to develop a model regulatory framework under which pipeline companies desiring to build new projects can operate. This will eliminate state by state confusion and should accelerate permitting and construction of new pipeline and refining projects.

5. The IOGCC should form a task force directed at working with Tribal groups to develop a model regulatory framework under which pipelines can cross Tribal lands.

6. States and the federal government should consider offering cost-effective tax incentives or royalty relief to producers, pipelines, and refiners if they commit to new build or expansion projects. Developers should be provided incentives to build "slack" capacity into their systems.

7. The IOGCC should promote the understanding that it is important to U.S. energy security that additional pipelines be built to carry Canadian crude to major U.S. refining centers. New and existing pipelines carrying Canadian crude oil should work with domestic producers and marketers to create receipt points for domestic crude to be shipped on their pipelines. In addition, crude oil pipelines should be permitted to sell firm service to shippers – especially on new pipelines.

8. The IOGCC should promote the understanding that localized prices in each state may fall out of favor from time to time due to changes in market forces such as imports, local production, refining capacity, pipeline capacity, crude quality and maintenance issues. Producers should be encouraged to work together to develop solutions that will assist in moving their oil to better valued markets. Aggregation of crude will assure the most efficient and economic development of pipeline or refining upgrades to each situation.

9. The IOGCC should work to streamline the overly burdensome, inconsistent and time-consuming refinery permit process by improving state, local and federal coordination, ensuring adequate resources at permitting authorities to shorten review timeframes, and empowering the U.S. Department of Energy to serve as a facilitator for timely permit reviews. Such projects should be viewed as a high priority due to national energy, national security and economic considerations.

10. The IOGCC should encourage Congress to codify the U.S. Environmental Protection Agency's (EPA) comprehensive reform of the New Source Review (NSR) regulations, including those that prohibit states from developing patchwork variations of the NSR process, which are stymied in judicial appeals.

11. The IOGCC should work to align National Ambient Air Quality Standards (NAAQS) deadlines to take advantage of the significant emissions reduction benefits achieved by existing federal regulation. Changes to consider during the 2010 statutory review cycle include standards relating to ozone and fine particulate matter.

About the IOGCC

The IOGCC, representing the governors of 30 member and seven associate states, promotes the conservation and efficient recovery of the nation's oil and natural gas resources while protecting health, safety, and the environment. Established by the charter member states' governors in 1935, and approved by Congress, it is the oldest, largest, and most effective interstate compact in the nation.

WTI: A broken benchmark

April 13, 2007

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Spot WTI crude oil prices no longer reflect international market dynamics. Rather, they represent local fundamentals for crude oil in the US mid-continent, putting a question mark over the value of this inland US crude as a world marker for hedging or speculation.

Spot West Texas Intermediate (WTI) prices have become divorced from the international crude oil market. Last year, WTI prompt prices were distorted by the impact of passive index fund rolls, exaggerating the steepness of the curve's contango. Now, physical market factors are further distorting prices (Figure 1). Spot WTI prices at Cushing, Oklahoma, are being depressed by lack of storage capacity, oversupply from Canada, bottlenecks in moving crude oil out of mid-continent PADD 2 and unexpected refinery outages. Until more storage is built and pipelines from the Gulf Coast to the US mid-continent are reversed, the rate of Canadian oil sands flows to the US and refinery demand for crude oil should dictate the price of WTI relative to waterborne crudes. Distortions look unlikely to dissipate before 2009.

By contrast, we believe light sweet waterborne crude prices in the Atlantic basin better reflect the value of oil. On Thursday April 12, 2007, the price of US-based Louisiana Light Sweet (LLS) crude, which is comparable to WTI, closed at $71.08, while dated Brent closed at $68.60, reflecting traditional Atlantic Basin market differentials. Prompt WTI futures closed at $63.88. In addition to PADD 2 (US Mid-West) dynamics, reduced supply of light sweet Atlantic basin crudes has increased their price relative to landlocked WTI. Tighter markets for these crudes reflect three main factors: Chinese demand for West African oil; Nigerian production outages related to political violence; and North Sea production declines.

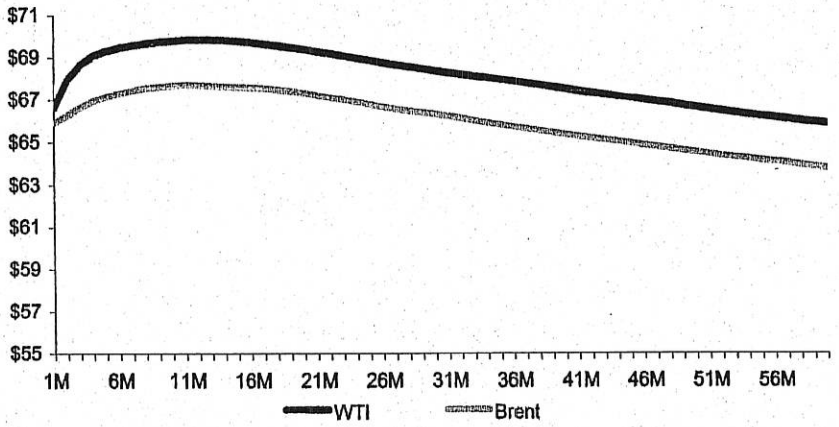
Substitution and arbitrage normally keep the prices of different crudes in parity

WTI and the failure of arbitrage economics

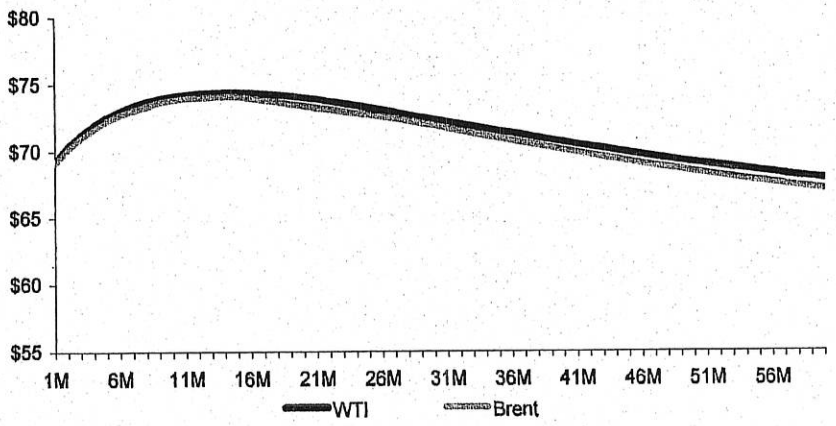
The US is the world's largest crude oil importer, taking in 10.1m b/d in 2006. As such the US market functions as the marginal consumer and price setter of any waterborne crude to which it has access at economic freight rates. In a world of accessible waterborne crude streams, price differentials between crudes should stem largely from crude quality and proximity to markets. If, for example, a 1m b/d supply disruption in the Gulf of Mexico made US Gulf Coast refiners willing to pay $10 more for crude than European or Asian refiners, and if the cost to ship crude oil from Africa were $1/bbl to Europe and $3/bbl to the US, African producers would quickly divert cargoes to the US. Demand pull from the US would then upset local supply-demand dynamics in other demand centers, causing the price of substitute crude oils to rise as well. This substitution and arbitrage process keeps the prices of different crudes in parity, even in crises affecting one region, assuming no dislocation of freight markets.

Figure 1: Breaking of the benchmark: WTI versus Brent over the past year

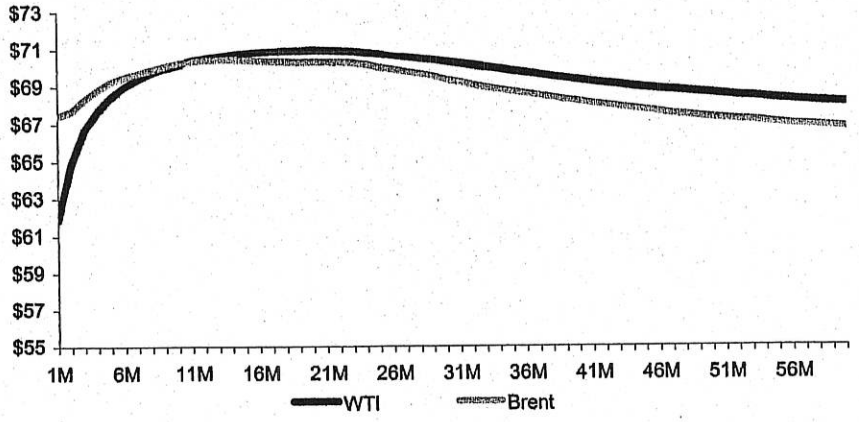
April 1, 2006: WTI enjoys traditional premium over Brent, but even last year the impact of index fund rolls started to slightly distort the front end of WTI relative to Brent.



September 1, 2006: WTI converges to Brent at the front end starting in mid-2006 as the Brent market tightens and the Cushing-Chicago Spearhead pipeline is reversed.



April 12, 2007: Currently, the front end of WTI lags that of Brent due to higher Canadian flows stuck at Cushing and refineries unable to sop up surplus crude.



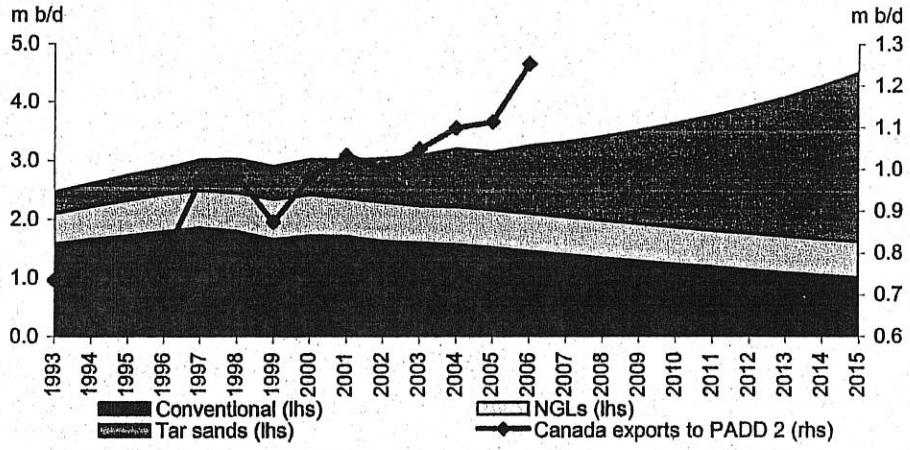
Source: Bloomberg

6-2

But because of a local supply glut, this dynamic is failing with respect to WTI

Today, this arbitrage dynamic is failing with respect to WTI. Until a local supply glut eases in Chicago and Cushing—the delivery point for NYMEX WTI—light sweet waterborne crude prices will likely act as a ceiling to US and Canadian light sweet inland crudes (ignoring freight). A floor to the price differential has disappeared because incremental Canadian flows have almost entirely displaced waterborne barrels in markets with access to both crude oil sources. As Canadian flows into the mid-continent continue rising — they are up 700k b/d over the past decade, and 140 k b/d (12.5%) in 2006 (Figure 2) — further discounting of inland crudes may well occur. Pipeline and storage constraints could translate into discounts big enough to encourage trucking oil out of the region or shut-ins of other inland PADD 2 supplies from Wyoming or Canada.

Figure 2. Canadian production to add 150k b/d annually with nowhere to go but PADD 2



**Includes exports through PADD 4.*
Source: EIA, Canadian Association of Petroleum Producers, Lehman Brothers Estimates.

Pipeline constraints keep inland crudes bottled up

Canadian crude has saturated PADD 2

Currently, Canadian oil enters PADD 2 from the West via PADD 4 (Rocky Mountains) and from the north, flowing to Chicago (Figure 3). As Canadian flows have increased, Chicago refineries have generally opted to consume discounted Canadian barrels rather than take waterborne barrels flowing up Capline, a 1.1m b/d capacity pipe running to Chicago from St. James, Louisiana. With large volumes of Canadian crude saturating the Chicago market, Enbridge bought and then reversed the 125k b/d Cushing-to-Chicago Spearhead pipeline in April 2006, sending Canadian barrels to the NYMEX WTI delivery point. Reducing flows from the Gulf Coast to PADD 2 on Capline and the 350k b/d capacity Seaway pipeline are one way the inland market has coped with higher Canadian oil exports (Figure 4). But substitution has not eliminated PADD 2 waterborne imports. In 4Q06 these imports averaged 1.4m b/d, versus Canadian imports of 1.2m b/d. One reason is that mid-continent pipeline constraints prevent those refiners still receiving waterborne crudes from accessing cheaper Canadian oil.

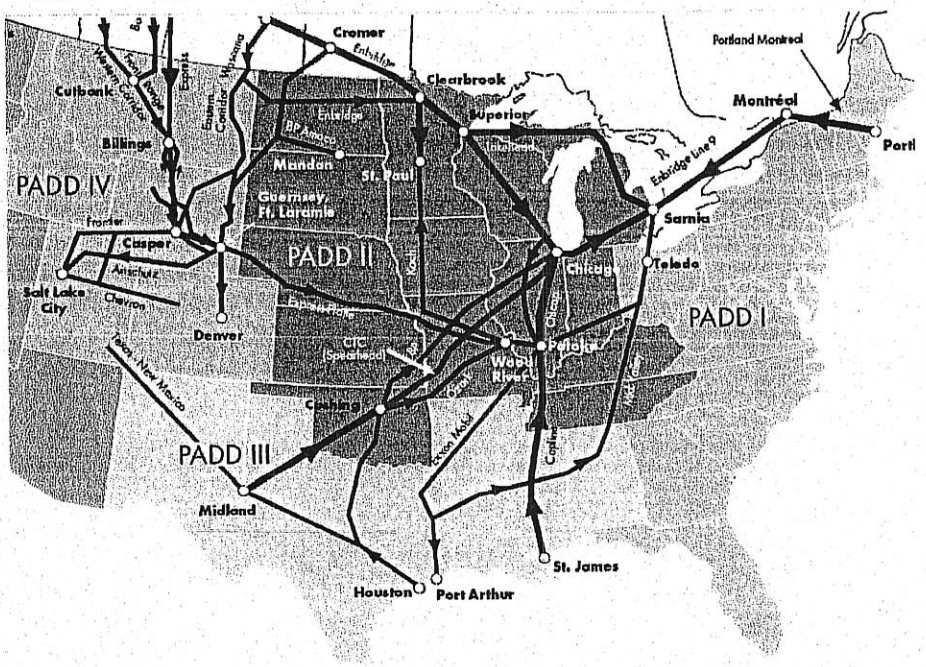
Canadian supplies sent on to Cushing have few export options

Cushing, traditionally a gathering point for mid-continent production for area refineries, has few export outlets to offload Canadian crude. The only major outlet—the 170k b/d Ozark pipeline from Cushing to Wood River, IL—has been full since shortly after Spearhead was reversed. For now, Cushing remains the end point for expanding Canadian exports. Until enough new pipeline takeaway capacity is built, WTI will likely

6-3

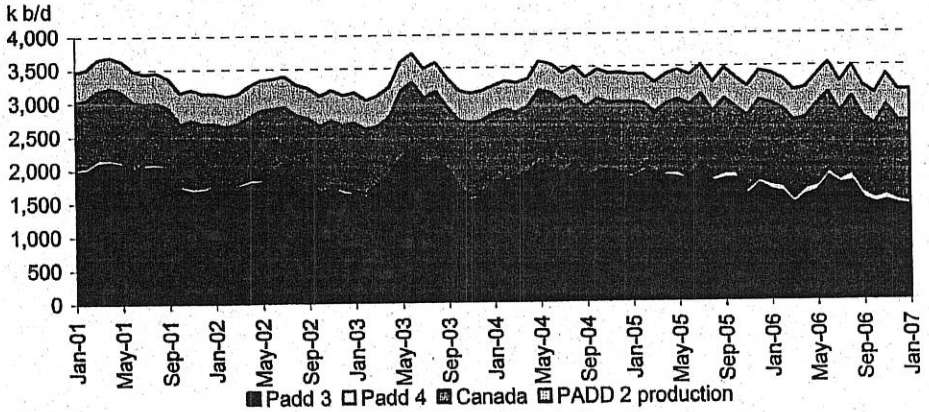
trade at a discount to waterborne crudes, ignoring freight, and Cushing is likely to be flush with inventory.

Figure 3. Major US oil pipelines



Source: Canadian National Energy Board.

Figure 4. PADD 2 crude oil sources: imports from Gulf Coast drop as they are replaced by Canadian barrels moving into Chicago and Cushing



Source: EIA.

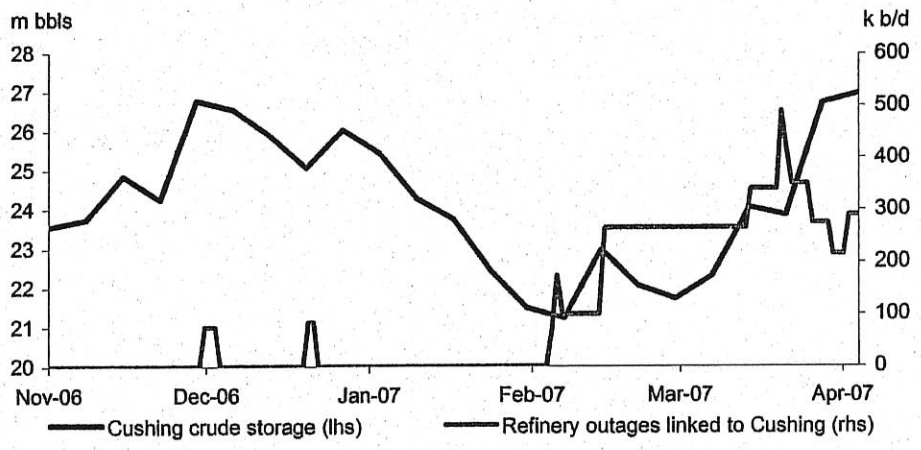
6-4

Unplanned refinery outages put downward pressure on the front end of WTI curve

WTI less flexible in handling demand swings from refinery outages

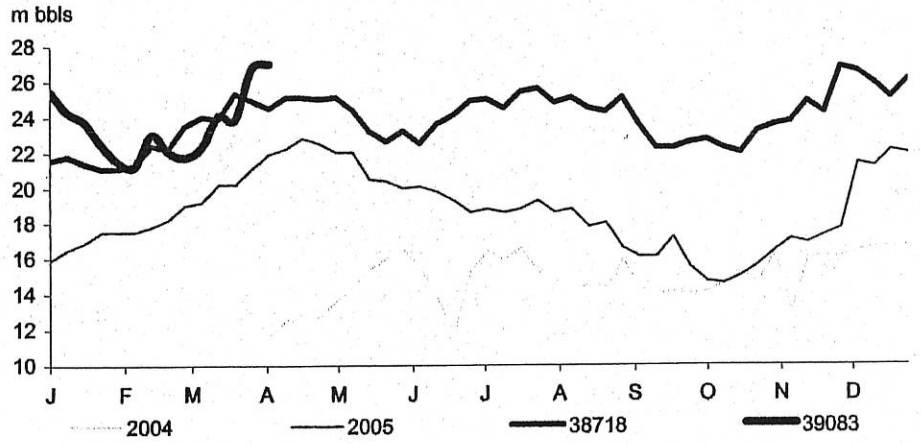
Depending on prevailing local supply-demand conditions in PADD 2, the effect of limited or unavailable storage at Cushing can be disastrous for WTI time spreads. This has been the case especially when refineries go offline for unplanned outages. In 2006, a power outage shut down the 306k b/d Wood River refinery and time spreads exploded. The recent McKee refinery outage has taken 165k b/d in crude refining capacity offline since February (slated for feed re-introduction to a 104k b/d crude unit on April 17), compounded by 100k b/d of turnarounds in Coffeeville, KS (recently back on line) and more recent maintenance turnaround at two 75k b/d crude units at Whiting. The price difference between the first and second month WTI prices grew from $0.85 (on a 30-day rolling average) in mid-February to $1.65 before the Whiting turnaround, to $2 this past week. These outages have backed up all crude supplies at Cushing (Figure 5).

Figure 5. Refinery outages pushing Cushing crude storage to its operational capacity



Source: EIA, Lehman Brothers Estimates

Figure 6. Cushing crude storage: Filled to the rim



Source: EIA

6-5

As storage at Cushing approaches its operational capacity of 27m bbls (Figure 6), these landlocked crudes are forced into spot sales, pressuring the front end of the WTI curve (latest US Department of Energy data shows that the Cushing crude storage for the week ending April 6, 2007 was at 26.986m bbls).

Atlantic basin crudes better represent world market conditions

While WTI suffers from a supply glut, an overall reduction in available light sweet crudes, such as North Sea Brent and Nigerian crudes in the Atlantic basin has increased their relative value. Three main factors have dictated this trend.

China continues consuming additional West African crudes at a strong pace

First, China continues to consume additional West African crudes at a strong pace, rising from 520k b/d in 2004 to some 750k b/d (25%, of total imports) today. With our forecast of 2007 Chinese demand growth of 500k b/d (7.2%) and flat domestic output, we expect China's 2007 imports to increase by 500k b/d (17.1%) y-o-y. With China's refining system requiring light sweet crude rather than Middle East grades, we expect China's appetite for West African crudes to remain a critical incremental demand source.

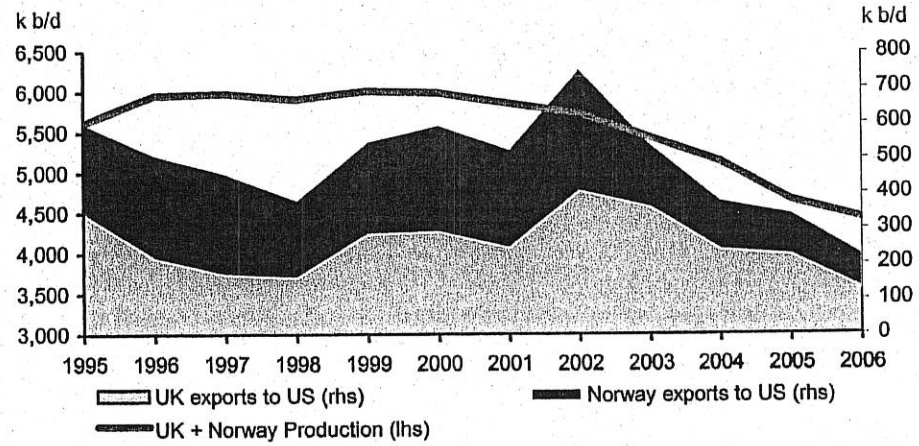
Outages in Nigeria place further strain on Atlantic Basin supplies

Second, outages in Nigeria related to political violence place a strain on Atlantic Basin supplies. The rise of Niger Delta militancy has taken about 700k b/d in crude supplies offline since February 2006. With more violence expected before the April 21 presidential elections—which may be postponed—Nigerian supply disruptions should damp Atlantic Basin output until at least 4Q07, when capacity may begin returning.

Declines in North Sea production are another major factor

Finally, declines in North Sea production have exacerbated the strain on light, sweet Atlantic basin crudes. Since its 1999 peak, UK and Norwegian output has declined by an annual average of 210k b/d, accelerating to 335k b/d since 2004 (Figure 7). About 40% of UK output and 60% of Norway's is from fields that have been declining by about 15% annually, with additions lagging mature basin declines. The UK's new Buzzard field, expected to peak at 200k b/d in mid-2007, should help moderate declines, but we still posit that 2007 UK plus Norway output will fall 170k b/d.

Figure 7. North Sea total oil production and exports to US, 1999-2006



Source: EIA, UK Dept of Trade and Industry, Norwegian Petroleum Directorate.

6-6

Has WTI outlived its usefulness?

Until reconnected with the global market, WTI could be a risky hedging instrument

The Cushing supply glut is worsening while the Atlantic basin market is tightening, underpinning our belief that WTI should continue trading between a discount to and on par with Brent and LLS, versus its traditional premium. Until WTI is reconnected to the global market, it could be substantially riskier to use WTI as a hedging instrument, except farther out on the curve, for production or for refining, unless the risks being managed are operationally within western PADD 2. That leaves ICE Brent, or markers derived from less liquid OTC markets, as benchmarks carrying less basis risk.

Broken arbitrages tend to fix themselves...

Ultimately, broken arbitrages tend to fix themselves. One million barrels of new Cushing storage capacity should come online by end-2Q07. Three million barrels more of capacity should come on in 2H07, adding more swing inventory cushion to cover sudden refinery demand drops. As refiners ramp up for gasoline season and asphalt plants prepare to start paving roads this spring and summer, more than 800k b/d of additional crude demand in PADDs 2 and 3 could start to draw down excess supplies and ease the current supply glut. Finally, producers may find it attractive to unwind their hedges in WTI and lock in still near-$70/bbl pricing in Brent, which could narrow the WTI/Brent price differential.

...if barriers to investment are overcome

A further obstacle to solving WTI's inland isolation stems from barriers to investment that could render WTI a risky and unrepresentative benchmark until at least 2009. Coordination problems exist between producers, pipeline companies, and consumers, stymieing efforts to build pipelines to bring Canadian barrels to the Pacific Ocean or the Gulf Coast. Teppco Partners, according to press reports, is considering reversing its 300k b/d Seaway pipeline connecting Cushing and the Texas Gulf, but that is unlikely before 2009.

Oil could be undergoing a major change with respect to crude oil benchmarks

Oil could be undergoing a major change with respect to crude oil benchmarks. WTI is landlocked and in the midst of a supply glut. Increased basis risk could push away natural hedgers while an increased contango because of spot oversupply and lack of storage could push away index investors losing money every month on bigger roll premiums. Meanwhile, both Brent and Dubai benchmarks are hurt by declining production and, in the case of Brent, uncertainty around quality and yields with the addition of Buzzard into the Forties system. If the Dubai Mercantile Exchange futures contract based on Omani crude takes off successfully this year, there could be a significant transfer of liquidity into this contract, which we think better reflects the world's crude oil supply. While WTI is likely to muddle through, it may already have moved past the peak of its usefulness as the preferred global benchmark for crude. ■