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Nothing New in Obama Plan for Offshore Drilling

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In early April, the Obama Administration announced that it will expand offshore exploration and development to reduce dependence on foreign oil. The plan that was announced is, in fact, more restrictive than what was already in place, and will have no near- or mid-term impact on our need to import oil. It maintains the status quo by allowing leasing in the eastern Gulf of Mexico and offshore Virginia, and by allowing drilling in certain areas offshore Northern Alaska, but it closes the Bristol Bay area offshore southern Alaska. All areas in the Pacific Ocean off the coasts of California, Oregon and Washington remain closed.

The portion of the eastern Gulf of Mexico that is offered for leasing in the government's plan is limited to areas more than 125 miles offshore that are mostly in water depths of 6,000 feet or greater (Figure 1). While the administration describes this as a development area, it is a high-risk, ultra deep-water wildcat province. Sixty-two wells were drilled in shallower areas of the eastern Gulf before the drilling moratorium, and the only prospective area found so far is the shallow-water Destin Dome region off the Alabama coast where reserves are estimated to be 2.7 trillion cubic feet of gas (equal to about 1.5 months of US natural gas consumption). The geology of the eastern Gulf of Mexico is different from the traditional producing area of the central and western Gulf. While it contains legitimate petroleum systems, it is a relatively high-cost, high-risk area.

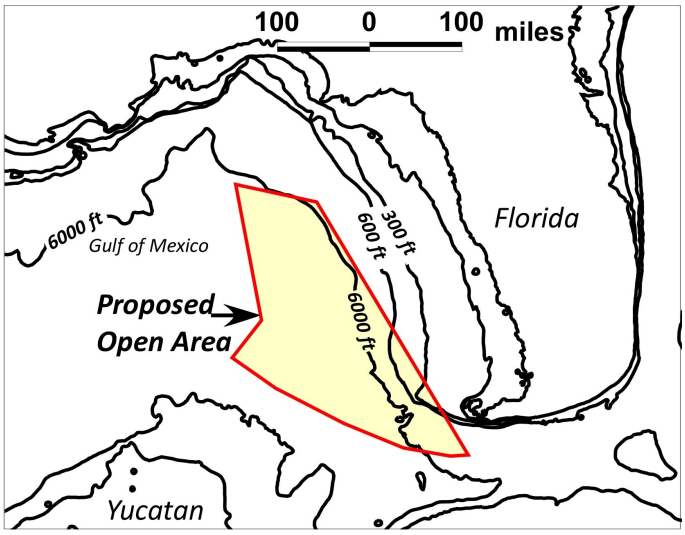

Figure 1. Gulf of Mexico bathymetric map showing proposed area for oil and gas leasing.

The area of the Atlantic coast that is included in the government plan is offshore Virginia (Figure 2). The Atlantic margin of the U.S. was drilled and evaluated before the area was closed to exploration in the 1980s, and the results were dismal. More than 50 wells were drilled, and only a

few wells in the Baltimore Canyon area off the coasts of New Jersey, Maryland and Virginia had any indications of petroleum. A few wells tested showed that natural gas could be produced at rates that would probably be commercial onshore today, but not 100 miles offshore.

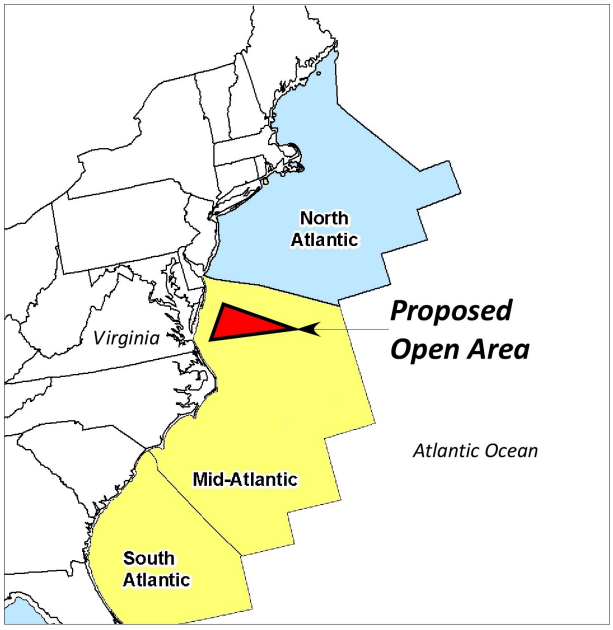

Figure 2. Offshore Atlantic Margin showing area proposed for offshore leasing. Modified from Minerals Management Services map.

In frontier areas like the Atlantic Margin and Eastern Gulf of Mexico, big fields are commonly discovered early in the exploration cycle because industry identifies and drills the largest, most obvious features first. The fact that approximately 50 largely unsuccessful wells have been drilled in each of these areas is discouraging. The Atlantic Margin seems to be an area where any hydrocarbons that are found will be natural gas rather than crude oil, based on geochemical analysis to date. While that is not a completely negative factor, further exploration there does little to change our dependence on foreign crude oil, and we currently have abundant supplies of onshore natural gas that can be found and developed at considerably lower cost.

On the positive side, the Atlantic Margin and eastern Gulf of Mexico are huge areas where important discoveries may have eluded early exploration efforts. Neither of these regions has been evaluated using modern seismic methods that could yield a different view of its potential for producing natural gas or oil.

As someone who works in the exploration and production business, I am in favor of opening these areas and letting industry decide if they have merit. At the same time, it is important to be objective. Under the most favorable scenario, it will take many years to acquire and interpret the necessary seismic and geochemical surveys that precede drilling. If discoveries are made, appraisal drilling, economic analysis, and development planning will require more time. Infrastructure adds yet another layer of time and complexity. Evaluation of large oil and gas projects worldwide commonly takes at least six years from discovery to first production. High-risk, capital intensive oil and gas exploration cannot be expected to produce quick results.