

CONTINUED PRODUCTION OF THE NAVAL
PETROLEUM RESERVES BEYOND APRIL 5, 2009

MESSAGE

FROM

THE PRESIDENT OF THE UNITED STATES

TRANSMITTING

NOTIFICATION OF HIS DECISION TO EXTEND THE PERIOD OF PRODUCTION OF THE NAVAL PETROLEUM RESERVES FOR A PERIOD OF THREE YEARS FROM APRIL 5, 2009, THE EXPIRATION DATE OF THE CURRENTLY AUTHORIZED PERIOD OF PRODUCTION, PURSUANT TO 10 U.S.C. 7422(e)(2)(B)



OCTOBER 3, 2008.—Message and accompanying papers referred to the Committee on Armed Services and ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE

To the Congress of the United States:

Consistent with section 7422(c)(2) of title 10, United States Code, I am informing you of my decision to extend the period of production of the Naval Petroleum Reserves for a period of 3 years from April 5, 2009, the expiration date of the currently authorized period of production.

Attached is a copy of the report investigating continued production of the Reserves, consistent with section 7422(c)(2)(B) of title 10. In light of the findings contained in the report, I certify that continued production from the Naval Petroleum Reserves is in the national interest.

GEORGE W. BUSH.

THE WHITE HOUSE, *October 2, 2008.*

CONTINUED PRODUCTION OF THE NAVAL PETROLEUM RESERVES
BEYOND APRIL 5, 2009

BACKGROUND

The Naval Petroleum Reserves Production Act of 1976 (Pub. L. 94–258) directed that the Naval Petroleum Reserves be developed and produced at their maximum efficient rates for an initial 6–year period beginning in April 1976. Pub. L. 94–258 authorizes the President to extend production in increments of up to three years provided that he first requires an investigation of the necessity for continued production; that he submits to the Congress, at least 180 days prior to the expiration of the current production period, a copy of the report on the investigation, along with a Presidential certification that continued production is in the national interest; and that neither House of Congress adopts a resolution, within 90 days of receiving the report and certification, disapproving further production.

President Reagan exercised his authority to continue production on three occasions; President George H. W. Bush exercised his authority once; President Clinton, three times; and President George W. Bush, twice, in 2002 and most recently in 2005. As a result, production from the Reserves has been continuously authorized since 1976 and is currently authorized through April 5, 2009.

Under Pub. L. 94–258 the President may:

- Continue production at the maximum efficient rate for up to three years beyond April 5, 2009, or
- Shut in production at a level that would protect the reservoirs from ultimately losing oil reserves, perhaps indefinitely or until a national defense emergency required activation of the Reserves.

This report addresses the continuation of production operations at Naval Petroleum Reserve No. 3 (NPR–3, Teapot Dome) a small, mature stripper field located near Casper, Wyoming. NPR–3 is the

only remaining Naval Petroleum Reserve administered by the Department of Energy under the Naval Petroleum Reserves Production Act of 1976.¹ The Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub. L. 105–261, authorizes DOE to dispose of NPR–3 by sale, lease, or transfer to another Federal agency, after abandoning oil and gas operations in accordance with commercial operating practices.

CONTINUED PRODUCTION OF NPR–3

Economics and assumptions

NPR–3 is a mature crude oil stripper field (i.e., production averages under 10 barrels per day per well). It is nearing the end of its economic life (the time during which revenues from the sale of produced oil exceed the costs of production to yield a positive net cash flow). Estimated average production from all wells during FY 2008 is projected to be 230 barrels of oil per day (BOPD).

With a projected average crude oil sales price of \$95.79 per barrel, FY 2008 revenues from the sale of the produced oil would exceed \$8.0 million. The crude oil sale price for June 2008 exceeded \$120 per barrel, thereby making the projected revenue stream somewhat conservative. In FY 2008, direct and overhead operational costs will be about \$5.0 million, thereby resulting in estimated net revenues to the U.S. Treasury of \$3.0 million.

NPR–3 will generate revenues that exceed the operational costs through the period of this report and for several years beyond. The primary assumptions of this forecast are:

- Straight-line funding consistent with the 2009 budget request, which allows production of about 60 percent of the economically producible wells at NPR–3;
- The average sales price for crude oil for FY 2009 is equal to the average projected price for FY 2008, estimated to be \$95.79 per barrel. Projected oil prices for FY 2010 and beyond are adjusted per the Energy Information Administration (EIA) crude oil price forecast found in its FY 2008 Annual Energy Outlook;
- No capital investment projects are undertaken;
- Overhead is, allocated between the Rocky Mountain Oilfield Testing Center (RMOTC), production operations, and environmental restoration proportional to costs, consistent with standard accounting practices;
- An annual production decline rate of 11% throughout the projection period with the exception of FY 2010 in which there will be no decline from FY 2009 as a result of wells which had been temporarily been shut-in being returned to production. Beginning in FY 2011, the decline rate will return to 11%, which is based on recent production history from 2004 to the present; and

¹The Department of Energy (DOE) divested its interest in Naval Petroleum Reserve No. 1 (NPR–1, Elk Hills, in Kern County, California) in 1997. In addition, section 331 of the Energy Policy Act of 2005 transferred administrative jurisdiction and control over all public domain lands in Naval Petroleum Reserve No. 2 (NPR–2, Buena Vista Hills, in Kern County, California) (with certain limited exceptions) from DOE to the Department of the Interior for management in accordance with laws governing management of the public lands. Therefore, continued production from NPR–1 and NPR–2 is not analyzed in this report.

- All costs are in current year dollars.

Profitable operations are projected to continue through at least FY 2012. Cash flow projections for continued operations of NPR-3 for the four fiscal years which encompass the three-year continued production period that is the focus of this report indicate that profits from the oil production will average \$1.3 million per year.

The cash flow calculation for NPR-3 reflects an allocation of overhead costs proportional to direct operating costs. The other activities supported by NPR-3 overhead are environmental restoration and RMOTC. Some overhead costs will shift between production operations, environmental restoration, and testing as the level of effort shifts between these programs.

Co-located at NPR-3, and utilizing the same production and processing facilities, is RMOTC, a program initiated by DOE in 1994. Conducted largely in cooperation with private industry and academic institutions through cost-shared projects, RMOTC provides for the development and demonstration of enhanced oil recovery techniques, production tools and processes, and environmental compliance technologies that can be transferred to and utilized by the domestic oil and gas industry. An additional benefit to NPR-3 is that testing successful technologies provides increased production and reduced operating costs directly to NPR-3, thus positively impacting the economic performance of the field.

Impacts

While the revenues from production operations at NPR-3 are not significant in the context of the overall federal budget, crude oil sales nonetheless provide income to the U.S. Treasury. Discontinuing production at NPR-3 would result in the loss of revenue from oil sales. Similarly, discontinuation would accelerate the government's cost obligations associated with the abandonment, restoration, and reclamation of the field which are estimated at \$112.7 million over a 6.5 year period to comply with state and federal regulations. However, discontinuing production and accelerating environmental restoration at NPR-3 would accelerate realization of environmental benefits.

Given the nature of its crude oil reservoirs, production at NPR-3 is unlikely to resume if its wells are plugged and abandoned and the field restored. Environmental regulations require wells that are shut-in for more than a short, fixed amount of time must be permanently abandoned. At that point, the reserves can be recovered only through drilling new wells. Drilling new wells or re-drilling cemented wells in a stripper oilfield is uneconomic for the foreseeable future. Once shut-in, the field would remain closed, and more than 400,000 of barrels of economically recoverable oil will become much less economic. Closing the field also significantly increases the cost to produce some of NPR-3's remaining 200 million barrels of presently non-recoverable oil resources. The amount of this resource that could be economically recovered either before or after shut-in varies as the economics continue to change based on the price of oil and the cost of recovery.

Emergency preparedness

NPR-3 provides less than 0.002 percent of daily domestic crude oil consumption and would have no measureable effect on mitigating supply interruptions. Although NPR-3 production rates are so small that there is no defense value or other national benefit in conserving the oil field for future use, it is important in the local, state, and regional context.

CONCLUSION

Given that the revenues generated and deposited into the U.S. Treasury exceed the cost to operate the Teapot Dome Field, continued production of Naval Petroleum Reserve No. 3 beyond April 5, 2009, is in the national interest.

