In the Supreme Court of the State of Alaska

STATE OF ALASKA, DEPARTMENT OF NATURAL RESOURCES, Petitioner, vs. EXXON MOBIL CORPORATION, OPERATOR OF THE POINT THOMSON UNIT; BP EXPLORATION (ALASKA) INC.; CHEVRON U.S.A. INC.; CONOCOPHILLIPS ALASKA, INC., Respondents.	**Supreme Court Case No. S-13730** Trial Court Case No. 3AN-06-13751 (Consolidated Appeals) Case No. 3AN-06-13760 CI Case No. 3AN-06-13773 CI Case No. 3AN-06-13799 CI Case No. 3AN-07-04634 CI Case No. 3AN-07-04620 CI Case No. 3AN-07-04621 CI

BRIEF OF RESPONDENTS EXXON MOBIL CORPORATION, BP EXPLORATION (ALASKA) INC., CHEVRON U.S.A. INC., AND CONOCOPHILLIPS ALASKA, INC.

PETITION FOR REVIEW FROM THE SUPERIOR COURT
THIRD JUDICIAL DISTRICT
HONORABLE SHARON GLEASON, SUPERIOR COURT JUDGE

Of Counsel:
M. Randall Oppenheimer
Charles C. Lifland
O'MELVENY & MYERS LLP
400 South Hope Street
Los Angeles, California 90071
Phone: (213) 430-6000

William B. Rozell
Alaska Bar No. 7210067
P.O. Box 20730
Juneau, Alaska 99802
Phone: (907) 463-5647

Douglas J. Serdahely
Alaska Bar No. 7210072
Barat M. LaPorte
Alaska Bar No. 9511064
PATTON BOGGS LLP
601 West 5th Avenue, Suite 700
Anchorage, Alaska 99501
Phone: (907) 263-6310

Attorneys for Respondent Exxon Mobil Corporation

George R. Lyle
Alaska Bar No. 8411126
GUESS & RUDD PC
510 L Street, Suite 700
Anchorage, Alaska 99501

Susan Orlansky
Alaska Bar No. 8106042
FELDMAN ORLANSKY & SANDERS
500 L Street, Suite 400
Anchorage, Alaska 99501

Bradford G. Keithley
Alaska Bar No. 1010054
PERKINS COIE LLP
1029 West 3rd Avenue, Suite 300
Anchorage, Alaska 99501

Attorneys for Respondent BP Exploration (Alaska) Inc.

Of Counsel:

P. Jefferson Ballew
G. Luke Ashley
THOMPSON & KNIGHT LLP
1722 Routh Street, Suite 1500
Dallas, Texas 75201-2533

Stephen M. Ellis
Alaska Bar No. 7510065
DELANEY WILES, INC.
1007 West 3rd Avenue, Suite 400
Anchorage, Alaska 99501

Attorneys for Respondent Chevron U.S.A. Inc.

Spencer C. Sneed
Alaska Bar No. 7811140
DORSEY & WHITNEY LLP
1031 West 4th Avenue, Suite 600
Anchorage, Alaska 99501

Attorneys for Respondent ConocoPhillips Alaska, Inc.

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CONSTITUTIONAL PROVISIONS

Alaska Const. art. I, § 7

Section 7. Due Process

No person shall be deprived of life, liberty, or property, without due process of law. The right of all persons to fair and just treatment in the course of legislative and executive investigations shall not be infringed.

Alaska Const. art. I, § 15

Section 15. Prohibited State Action

No bill of attainder or ex post facto law shall be passed. No law impairing the obligation of contracts, and no law making any irrevocable grant of special privileges or immunities shall be passed. No conviction shall work corruption of blood or forfeiture of estate.

Alaska Const. art. I, § 18

Section 18. Eminent Domain

Private property shall not be taken or damaged for public use without just compensation.

U.S. Const. art. I, § 10

Section 10. Powers Prohibited of States

No State shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Reprisal; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.

U.S. Const., 5th Amendment

5th Amendment. Trial and Punishment, Compensation for Takings

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall

any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

U.S. Const. 14th Amendment, § 1

14th Amendment. Citizenship Rights

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

STATUTES

AS 38.05.180(p), (q)

Oil and Gas and Gas Only Leasing

(p) To conserve the natural resources of all or a part of an oil or gas pool, field, or like area, the lessees and their representatives may unite with each other, or jointly or separately with others, in collectively adopting or operating under a cooperative or a unit plan of development or operation of the pool, field, or like area, or a part of it, when determined and certified by the commissioner to be necessary or advisable in the public interest. The commissioner may, with the consent of the holders of leases involved, establish, change, or revoke drilling, producing, and royalty requirements of the leases and adopt regulations with reference to the leases, with like consent on the part of the lessees, in connection with the institution and operation of a cooperative or unit plan as the commissioner determines necessary or proper to secure the proper protection of the public interest. The commissioner may not reduce royalty on leases in connection with a cooperative or unit plan except as provided in (j) of this section. The commissioner may require a lease issued under this section to contain a provision requiring the lessee to operate under a reasonable cooperative or unit plan, and may prescribe a plan under which the lessee must operate. The plan must adequately protect all parties in interest, including the state.

(q) A plan authorized by (p) of this section, which includes land owned by the state, may contain a provision vesting the commissioner, or a person, committee, or state agency, with authority to modify from time to time the rate of prospecting and development and the quantity and rate of production under the plan. All leases operated under a plan ap-

proved or prescribed by the commissioner are excepted in determining holdings or control under AS 38.05.140. The provisions of this section concerning cooperative or unit plans are in addition to and do not affect AS 31.05.

AS 44.64.050(b)

Hearing Officer Conduct

(b) The chief administrative law judge shall, subject to AS 39.52.920 and by regulation, adopt a code of hearing officer conduct. The code shall apply to the chief administrative law judge, administrative law judges of the office, and hearing officers of each other agency. The following fundamental canons of conduct shall be included in the code: in carrying out official duties, an administrative law judge or hearing officer shall

(1) uphold the integrity and independence of the office;
(2) avoid impropriety and the appearance of impropriety;
(3) perform the duties of the office impartially and diligently;
(4) conduct unofficial activities in ways that minimize the risk of conflict with the obligations of the office; and
(5) refrain from inappropriate activity in seeking employment with another agency or employer or in seeking reappointment.

REGULATIONS

2 AAC 64.040(a)

Conflicts

(a) A hearing officer or administrative law judge shall refrain from hearing or otherwise deciding a case presenting a conflict of interest. A conflict of interest may arise from a financial or other personal interest of the hearing officer or administrative law judge, or of an immediate family member. A conflict of interest exists if

(1) the financial or other personal interest reasonably could be perceived to influence the official action of the hearing officer or administrative law judge; or

(2) a hearing officer or administrative law judge previously represented or provided legal advice to a party on a specific subject before the hearing officer or administrative law judge.

11 AAC 83.180(a)-(b)

Default

(a) Whenever the lessee of a lease on which there is no well capable of producing oil or gas in paying quantities fails to comply with any provision of the lease or applicable regulations other than the payment of rental and the failure to comply continues for 60 days after receipt of notice to the lessee of the failure to comply, the director may terminate the lease by mailing notice of the termination to the lessee. Termination is effective upon giving the notice.

(b) Whenever the lessee of a lease on which there is a well capable of producing oil or gas in paying quantities fails to comply with any of the provisions of the lease or applicable regulations and the failure continues for a period of 60 days following notice to the lessee of the failure to comply, the lease may be cancelled by judicial proceedings instituted for that purpose in any court of competent jurisdiction having jurisdiction over the land covered by the lease or any part of it.

11 AAC 83.374(d)

Default

(d) If a default occurs with respect to a unit in which there is a well capable of producing oil or gas in paying quantities and the default is not cured by the date indicated in the demand, the commissioner will, in his discretion, seek to terminate the unit agreement by judicial proceedings.

Exxon Mobil Corporation, BP Exploration (Alaska), Inc., Chevron U.S.A. Inc., and ConocoPhillips Alaska, Inc., the respondent working interest owners ("WIOs") under the Point Thomson Unit Agreement ("PTUA"), submit this joint brief in opposition to the opening brief of petitioner State of Alaska Department of Natural Resources ("DNR").

I. ISSUES PRESENTED

1. Whether the superior court correctly held that DNR must comply with the procedures and protections specified in Section 21 of the PTUA when DNR seeks to unilaterally increase the rate of prospecting, development, or production under the PTUA.

2. Whether the superior court correctly held that DNR violated the WIOs' due process rights when it allowed attorneys and staff who had advocated in the first superior court appeal for affirmance of DNR's termination of the PTUA to provide *ex parte* advice to DNR's adjudicatory decisionmaker and officiate in remand proceedings where DNR again sought termination.

II. INTRODUCTION AND SUMMARY OF ARGUMENT

As framed by the Court's order granting DNR's petition, this interlocutory petition for review of Judge Gleason's January 2010 decision vacating DNR's second attempt to "administratively terminate" the PTUA presents two discrete questions.[1] The first is a straightforward issue of contract interpretation. Section 21 of the PTUA establishes procedures DNR must follow and protections it must accord the WIOs before it can unilaterally—that is, without the consent of the WIOs—require an increase in the rate of pros-

[1] By order dated June 24, 2011, the Court struck portions of DNR's brief that requested interlocutory review of a third issue not encompassed within DNR's petition. *See* 6/24/11 Order (striking Section III, issue 2 [p. 9] and Section VI.B [pp. 58-67]).

pecting, development, or production under the PTUA. The question presented is whether DNR can permissibly bypass those procedures and protections by the expedient of (1) declining to approve a proposed plan of development ("POD") that does not, in DNR's estimation, assure production on DNR's desired timetable, (2) declaring the WIOs to be in "default" under the PTUA for failure to propose a POD acceptable to DNR, and then (3) terminating the PTUA based on the WIOs' alleged default.

Judge Gleason unsurprisingly held the answer to be no. As she correctly reasoned, DNR's attempt to "administratively terminate" the PTUA for failure to propose a POD requiring production on DNR's desired timetable impermissibly reads Section 21 out of the contract. This Court should affirm Judge Gleason's decision. Contrary to DNR's argument, requiring DNR to comply with Section 21 does not contradict any other provisions of the PTUA or applicable Alaska statutes and regulations. Nor does it place an inappropriate or undue burden on DNR's ability to deal with "recalcitrant" lessees—a false description made possible here only by DNR's incomplete and misleading statement of the facts. And it certainly does not "subvert" DNR's authority to manage the State's natural resources in the public interest. It merely upholds the WIOs' contractual entitlement to the procedures and protections that DNR agreed to provide under the PTUA.

The second question under review is a straightforward question of procedural due process. Judge Gleason's 2007 decision held that DNR had not provided constitutionally sufficient notice of its intent to seek PTUA termination. The decision further held that DNR's rejection of the proposed 2005 POD, though within the agency's discretion, did not establish an act of default or a material breach of the PTUA by the WIOs. The court

remanded the matter to DNR for determination of the appropriate remedy following rejection of the proposed POD, with specific instructions for DNR to consider the import of Section 21.

On remand, DNR issued a formal notice that it still intended to seek termination. The WIOs in turn requested that the contested legal and factual issues be adjudicated in an evidentiary hearing before an impartial adjudicator, pointing out that DNR, as the contracting party, was the WIOs' direct adversary on the termination claim. The WIOs also requested assurances that, in the event DNR sought to adjudicate its own right to terminate the PTUA, persons who had acted and would be acting for DNR as a contracting party would be segregated from the DNR officials deciding the termination issue.

DNR declined both requests, allowing personnel responsible for contract administration and attorneys and staff who had represented DNR in the superior court appeal to attend the administrative hearing and provide *ex parte* input to the DNR Commissioner throughout the proceeding. DNR even appointed the person who was its internal "contact point for litigation" against the WIOs to act as the Commissioner's hearing officer. The question presented is whether DNR adequately separated its proprietary role as a contracting party advocating PTUA termination from its administrative role as the adjudicator of its own claimed contractual right to terminate.

Again unsurprisingly, Judge Gleason held the answer to be no, and again this Court should affirm. As Judge Gleason explained, under this Court's decision in *In re*

Robson,[2] due process required DNR to ensure that attorneys and staff who represented DNR in the contested Superior Court proceedings took no part in the agency's adjudicatory decisionmaking on remand.[3] DNR's argument that *Robson* does not apply because the agency proceedings were not "adversarial" is specious. Over the WIOs' strong objections, DNR sought to terminate a unit agreement covering leases on which the WIOs have made a valuable discovery and to date invested over $1.5 billion. Such a proceeding is inherently adversarial, triggering a due process obligation to keep adversarial and adjudicatory roles separate. Judge Gleason correctly concluded that the personnel in question had impermissibly served as advisors to DNR's supposedly neutral adjudicator after having advocated DNR's position in the superior court, and *Robson* itself repudiates DNR's suggestion that a due process violation occurs only when actual bias is shown.

III. STATEMENT OF THE CASE

DNR's argumentative and incomplete statement of "facts" attempts to create the impression that the Point Thomson Unit ("PTU") contains vast quantities of readily accessible oil and gas that the respondents have inexplicably refused to produce. The record below not only belies that characterization, but affirmatively demonstrates that DNR at all times controlled and acquiesced in the pace of development of the PTU from its inception in 1977 through 2005 by approving every POD under which the unit has been operated. And despite its purported termination of the PTUA, DNR has continued to approve

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[2] 575 P.2d 771 (Alaska 1978).

[3] *Id.* at 775.

extensive operations on the underlying leases in the PTU, including a $1.3 billion cycling project commenced in 2008 to produce gas condensate.

The Formation of the Point Thomson Unit

The State auctioned the first oil and gas leases at Point Thomson, a remote north coastal area with no infrastructure, in the mid-1960s.[4] The vast oil reserves 50 miles west at Prudhoe Bay had not yet been discovered, and the bidders did not know whether the leases would prove valuable.[5] Most of the leases had initial terms of 10 years, with provisions for automatic extension on completion of wells capable of producing hydrocarbons in paying quantities or inclusion with other leases in a unit.[6]

By the mid-1970s, the WIOs had completed sufficient exploration drilling and seismic testing to suggest that 18 of the leases might overlie a common oil and gas reservoir. In August 1977, DNR approved and consented to an agreement to "unitize" those leases under the PTUA.[7] The PTUA designated ExxonMobil as Operator and had an ini-

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[4] R. PTU 19959, 1865, 13965. ("R. PTU" refers to documents in the record on appeal with a "PTU Rec" prefixed number. "R. Appx" refers to documents in the record on appeal with an "Appx" prefixed number. "R." refer to documents in the court file using numbers assigned by a clerk of the Court.)

[5] R. PTU 7568.

[6] *E.g.*, Exc. 1-4; R. PTU 25381-88.

[7] Exc. 38-57, 376; R. PTU 774. Unitization enables common production of a reservoir underlying multiple leases and is favored under Alaska law because it provides for economically efficient oil and gas development and promotes conservation of natural resources. *See* AS 38.05.180(p); Exc. 38 (purpose of the Point Thomson Unit Agreement is "to conserve natural resources, prevent waste, and secure other benefits obtainable through development and operation of the area"); R. 15318-19; *ConocoPhillips Alaska, Inc. v. State*, 109 P.3d 914, 917 n.16 (Alaska 2005) (purpose of a unit agreement is "to

tial term of five years, subject to automatic extension on completion of a well capable of producing in paying quantities.[8] With expansions and contractions made over the years, the PTU now includes 31 leases.[9]

The Geology of the Point Thomson Unit

The PTU contains an estimated 8 trillion cubic feet of natural gas in the Thomson Sand Reservoir, together with a lesser volume of heavier hydrocarbons.[10] The liquid hydrocarbons in the reservoir consist of a thin layer of heavy oil plus "retrograde condensate," which is gaseous in the reservoir but becomes liquid at the surface.[11] If all hydrocarbons in the reservoir could be brought to the surface, over 90% of the total volume would be natural gas.[12] The PTU also contains some lighter oil in separate accumulations called Brookian sands.[13]

As the State has acknowledged, the geology of the PTU makes production of the gas, condensate, and oil located there technologically challenging.[14] The main gas reser-

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efficiently extract oil from a common reservoir that is the subject of multiple leases"). The PTUA, as amended, is found at Exc. 147-70.

[8] Exc. 41, 52-53.

[9] Exc. 762.

[10] Exc. 386-87; R. PTU 2580, 5611.

[11] R. PTU 15920, 16254.

[12] R. PTU 15920.

[13] T. 98.

[14] R. PTU 935, 941. *See* R. PTU 3135 (2006 statement by Commissioner of Internal Revenue recognizing the "highly challenging technical demands and uncertainties as-

voir, 12,000 feet below the surface, is under extreme pressure—over 10,000 pounds per square inch ("psi") compared to an average of 4,335 psi at Prudhoe Bay. [15] The very high pressures create both drilling risks and production safety issues.[16] In addition, because the condensate is "retrograde," some liquids will condense deep in the gas reservoir as pressure declines, rather than only at the surface. This presents problems for recovery of both condensate and gas.[17] Finally, the main gas reservoir may be compartmentalized, discontinuous, or poorly connected. Production of hydrocarbons from reservoirs of this nature requires more wells.[18]

The heavy oil is sandwiched between the gas cap and a layer of water.[19] Extraction is technically difficult both because the thin horizontal oil layer is difficult to target and because reservoir dynamics will produce the water and gas preferentially to the oil, meaning the quantity of producible oil will be small relative to the amount of water and gas.[20] The minor oil accumulations in the Brookian sands are less viscous than the heavy oil in the gas reservoir, but the accumulations are discontinuous, making recovery especially

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sociated with developing the Thomson Sand Reservoir in a safe and environmentally sound manner").

[15] R. PTU 30027. 10,000 psi would approximately equal the pressure of two 4x4 pickup trucks resting on a person's thumbnail.

[16] R. PTU 935, 941-44, 15404.

[17] R. PTU 15009, 15404, 16374.

[18] R. PTU 934, 936, 15930, 16353.

[19] Exc. 387.

[20] R. PTU 16046.

challenging.[21] Efforts to produce oil from similar Brookian reserves 20 miles away at the Badami unit have proved disappointing and uneconomic.[22]

The PTU's remoteness from any market and the lack of a gas pipeline to the North Slope has made commercial gas production impractical.[23] Construction of a 20-mile connection to the Badami pipeline, which connects to the TransAlaska Pipeline System, could provide a means to transport producible PTU liquid hydrocarbons to Lower 48 markets.[24] But no pipeline system exists for transporting PTU gas to market. Construction of a gas pipeline to Lower 48 markets is a multi-billion dollar proposition that, despite the ongoing efforts of many, still awaits a political and commercial solution. Because of the lack of transportation, gas is not commercially produced for non-local use anywhere on the North Slope, including Prudhoe Bay, which has estimated gas reserves triple PTU's.[25]

Operations and Development under the PTUA - 1977 to 2004

Under the PTUA, the WIOs continued exploration drilling as approved by DNR.[26] By 1984, they had expended over $700 million to drill 14 wells in and around the PTU.[27] DNR in turn had certified six of those wells as capable of producing in paying quanti-

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[21] R. PTU 16046, 16375-77.

[22] Exc. 610; T. 798-802; R. PTU 30024.

[23] Exc. PTU 607-08.

[24] T. 621-22.

[25] R. PTU 2538.

[26] Exc. 44.

[27] Exc. 121; R. PTU 650, 14081, 14090.

ties.[28] As originally drafted, the PTUA required the establishment of a "participating area" for production promptly upon making a valuable discovery.[29] But in 1982, before the end of the initial 5-year term of the PTUA, DNR agreed to modify Section 11 of the PTUA to provide that a participating area need only be established "prior to commencement of production of unitized substances into a pipeline or other means of transportation to market."[30] The amendment reflected DNR's understanding that construction of a North Slope gas pipeline could take many years and it would be unfair and unreasonable to expect production to begin potentially years before the produced oil or gas could reasonably be brought to market.[31]

DNR agreed to additional amendments of the PTUA in 1985. These amendments extended indefinitely the PTUA and underlying leases by deleting the reference to any participating area in the Section 20 *habendum* clause.[32] At the same time, DNR agreed to both procedural and substantive limitations on its authority under Section 21 to modify

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[28] R. PTU 20298, 21012-13, 21834, 23421, 24521-23, 25366-68. DNR certified a seventh well as so capable in the mid-1990s. R. 26200-04.

[29] Exc. 45-46. A "participating area" is the underlying area estimated to be capable of contributing to the well's production of hydrocarbons in paying quantities. *See* 11 AAC 83.351.

[30] *See* R. PTU 738, 1286-89, 1409-10, 1412-14.A, 1422. The form originally used for the PTUA was developed for the Lower 48 states, and conditions on Alaska's North Slope are quite different. R. PTU 1287. The amended PTUA is comparable to unit agreements for remote offshore units. R. PTU 1286-87; 53 FR 10770-71 (participating area provisions in former model offshore unit agreement, codified as 30 C.F.R. § 250.194 (1988)).

[31] R. PTU 738-40.

[32] R. PTU 1267-68, 10214, 13958-60.

the rate of prospecting, development, or production under the PTUA without the WIOs' consent. As discussed below, Alaska's unitization statute generally does not allow DNR, without the consent of the underlying lessees, to "establish, alter, change, or revoke" contractual requirements for drilling or producing.[33] In the case of unit agreements covering State-owned lands, however, the statute makes available a limited exception: The agreement "may contain a provision vesting [DNR] with authority to alter or modify from time to time the rate of prospecting and development and the quantity and rate of production."[34]

As originally drafted, Section 21 empowered DNR to exercise this authority after notice to the Operator and opportunity for a hearing to be held not less than 15 days from notice.[35] The 1985 amendment increased the notice period to 30 days, and further provided that DNR's authority under Section 21

> shall not be exercised in a manner that would (i) require any increase in the rate of prospecting, development or production in excess of that required under good and diligent oil and gas engineering and production practices; or (ii) alter or modify the rates of production from the rates provided in the approved plan of development and operations then in effect or, in any case, curtail rates of production to an unreasonable extent, considering unit productive capacity, transportation facilities available, and conservation objectives; or (iii) prevent this agreement from serving its purpose of adequately protecting all parties in interest hereunder, subject to applicable conservation laws and regulations.[36]

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[33] *See* former AS 38.05.180(m) (now AS 38.05.180(p)).

[34] *See* former AS 38.05.180(n) (now AS 38.05.180(q)).

[35] Exc. 53.

[36] Exc. 129.

Under the terms of this amendment, DNR retained the contractual authority permitted under the unitization statute to unilaterally require an increase in the rate of prospecting, development, or production, but bound itself to provide the agreed procedural and substantive protections in connection with any exercise of that authority.

In general, of course, the PTUA contemplated that the pace of development and production would be determined not by DNR unilaterally, but cooperatively under periodic PODs submitted by the Unit operator for DNR's approval.[37] Section 10 of the PTUA governs submission and approval of periodic PODs. Under Section 10, the operator expressly covenanted to "develop the unit area as a reasonably prudent operator in a reasonably prudent manner."[38] The reasonably prudent operator ("RPO") standard is an objective standard requiring the operator to do what, in the circumstances, "would be reasonably expected of operators of ordinary prudence, *having regard to the interests of both lessor and lessee.*"[39] The RPO standard also governs and is drawn from DNR's standard form leases unitized under the PTUA.[40] Section 10 also provides that PODs submitted

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[37] Exc. 45.

[38] *Id.*

[39] *In re ANS Royalty Litigation*, No. 1JU-77-847, at 41-42 (Alaska Super. Mar. 13, 1991) (Carpeneti, J.) (quoting *Brewster v. Lanyon Zinc Co.*, 140 F. 801 (8th Cir. 1905) (emphasis added)). *See* exhibit 1 to Affidavit of Barat M. LaPorte in Support of Respondents' Request for Judicial Notice (hereinafter "LaPorte Affid."), filed concurrently herewith.

[40] *See, e.g.*, DNR's DL-1 lease form, at ¶ 19 ("This lease contemplates the reasonable development of said land for oil and gas as the facts may justify. Upon discovery of oil or gas in paying quantities on said land, Lessee shall drill such wells as a reasonably prudent operator would drill having due regard for the interests of Lessor as well as the interests of Lessee."). Exc. 2. Section 18 of the PTUA provides that "[t]he terms ... of all

under this standard "shall be as complete and adequate as [DNR] may determine to be necessary for timely development and proper conservation of the oil and gas resources of the unitized area" and "shall be modified or supplemented when necessary to meet changed conditions, or to protect the interests of all parties to this agreement."[41]

From 1977 through 2004, the PTU was continuously developed and operated under PODs approved by DNR under Section 10. The first POD, calling for continued exploration drilling, was submitted and approved in 1977.[42] Updated PODs were submitted and approved most years thereafter, though some multi-year PODs were approved.[43] In conformance with these PODs, the WIOs completed substantial exploration and delineation drilling, seismic studies, computer modeling, and engineering work, all designed to

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leases ... are ... amended to the extent necessary to make the same conform to the provisions hereof, but otherwise to remain in full force and effect." Exc. 50. No provision of the PTUA conflicts with the RPO standard established in the unitized leases.

[41] Exc. 45.

[42] Exc. 69-70; R. PTU 11350, 11354-56.

[43] *See generally* Exc. 487-88, R. PTU 796-811 (summarizing PODs and development activities). For the complete set of approved PODs, *see* Exc. 69-70, 75-79, R. PTU 11350 (1st POD), Exc. 80-81, R. PTU 11333, 11342-48 (2nd POD), Exc. 82-83, R. 11300-01 (3rd POD), Exc. 101-102, R. 11289-91 (4th POD), Exc. 108-109, R. 11270-71 (5th POD), Exc. 111-113, 119, R. 11257 (6th POD), Exc. 120-24 (7th POD), R. PTU 11528, 11532-33 (8th POD), Exc. 143-44, R. 11422-25 (9th POD), R. PTU 11385-92 (10th POD), Exc. 145-46, R. PTU 14160-66 (11th POD), Exc. 179-85 (13th POD), R. PTU 11644-45, 11648-52 (14th POD), R. PTU 15345-51 (15th POD), Exc. 192-98, R.11757 (16th POD), R. PTU 1453-65 (17th POD), Exc. 225-26, R.11930-39 (18th POD), Exc. 277-87 (19th POD), Exc. 292-95, R. 4398-402 (20th POD), Exc. 296-305 (21st POD).

develop a detailed understanding of the reservoirs and to identify an economically viable way to develop the hydrocarbons within the PTU.[44]

This is not to suggest that DNR was never dissatisfied with a proposed POD or frustrated when development proposals studied under a series of PODs proved technically infeasible and uneconomic.[45] When issues arose, however, they were resolved by agreement. DNR never approved the 12th POD, for example, but extended the 11th POD and then approved a 13th POD to replace it.[46] DNR also initially rejected the 15th POD, but then approved a revised version in which the WIOs had incorporated changes that DNR suggested.[47]

Each time DNR approved a proposed POD under Section 10, it accepted the POD to be "as complete and adequate" as "necessary for timely development and proper conservation of the oil and gas resources of the unitized area."[48] DNR approved these PODs over the course of a series of administrations of varied political persuasions.[49] Before 2005, DNR never sought to invoke its authority under Section 21 to unilaterally impose a faster rate of development. On the contrary, DNR and the WIOs long agreed that the optimal way to develop the PTU's gas would be in conjunction with the commercial devel-

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[44] Exc. 969-91.

[45] DNR Brief at 5, 15-17; Exc. 178; R. PTU 5284-87.

[46] Exc. 178, 179-80, 184.

[47] Exc. 186-91, 836-49.

[48] Exc. 45.

[49] *See* R. PTU 3117.

opment and marketing of the gas at Prudhoe Bay.[50] In 1983, DNR approved a POD that described the PTU gas as capable of production *when* transportation became available.[51] DNR also agreed that drilling production wells before transportation options became available made little sense and would be wasteful.[52]

But the WIOs did not merely wait for someone to build a gas pipeline to the North Slope. For over thirty years, they invested millions of dollars and thousands of person hours in efforts to identify a prudent alternative that would enable commercial production of the PTU's resources without a gas pipeline. By 2005, the WIOs' investment in developing the PTU had increased to over $800 million.[53]

The most extensively studied option for developing PTU resources without a gas pipeline was the possibility of producing liquid condensate from the gas reservoir by gas cycling (also called gas injection).[54] Initial studies showed a gas cycling project to be clearly uneconomic.[55] But the WIOs continued to try to make a gas cycling project viable

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[50] *See* Exc. 79 (DNR-approved POD stated in 1977 that "development of a gas market outlet will be related to studies to market gas from the Prudhoe area").

[51] Exc. 120. *See also* R. 014053 (stating that lessees viewed the PTU as commercially developable "at such time as availability of Alaska North Slope gas transmission system is assured").

[52] Exc. 121; R. PTU 14065, 14104.

[53] Exc. 602.

[54] As the name implies, in a gas cycling project, gas is brought to the surface, where the commingled gaseous condensates liquefy and are recovered as light oil, after which the dry gas is injected back into the reservoir. *See* R. 3198-99.

[55] *E.g.*, R. PTU 14054, 14105-15 (1987-88), 14217 (1993).

with newer technologies. The 17th through 20th PODs, submitted in 2000-03, focused on a full-field gas cycling project on which the WIOs spent over $60 million for design, engineering, and reservoir work.[56] In 2003 and 2004, however, rising material and safety design costs increased the estimated production costs by 30%, while new indications of connectivity problems in the reservoir decreased the estimated condensate recoveries by 35%.[57] The resultant doubling of per barrel development costs rendered the project uneconomic, notwithstanding the WIOs' substantial investment.[58] When presented with this information, DNR accepted the WIOs' decision to discontinue the project.[59] In September 2004, DNR approved the 21st POD, which contained no further gas cycling plans and no immediate plans for further drilling.[60] Instead, the 21st POD focused on preparatory work necessary to commit the PTU's gas reserves to a gas pipeline construction project

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[56] R. PTU 934-37, 955, 3191-253.

[57] R. PTU 935-36, 3191-253.

[58] R. PTU 936, 955.

[59] R. PTU 3204, 3191-253.

[60] Exc. 297-305, 318. The approval was contingent on review of additional data concerning the then-suspended cycling project. Those data were supplied. Exc. 312; R. PTU 001943-44. DNR also noted that the approval did not relieve the WIOs of the conditions contained in a Unit expansion agreement providing that "[d]evelopment drilling in the PTU must begin by June 15, 2006, or all of the Expansion Acreage will automatically contract out of the PTU and the PTU Owners will pay $20 million to the State of Alaska." Exc. 304. After concluding that drilling additional wells on this schedule would not be prudent or economic and failing to obtain DNR's agreement to modify the terms of the expansion agreement, the WIOs ultimately satisfied their obligations under that agreement by paying the $20 million, plus interest, to the State and allowing the expansion acreage to contract out of the PTU. R. 3586.

for which negotiations had begun earlier in 2004 under the 2003 Amendments to the Alaska Stranded Gas Development Act ("SGDA").[61]

The economic viability of the proposed gas pipeline depended on access to the gas reserves at PTU as well as at Prudhoe Bay.[62] Three of the PTU WIOs (ExxonMobil, BPXA, and ConocoPhillips) participated as a "Sponsor Group" in the SGDA negotiations, which continued through 2005 and included the Governor and Commissioner of Revenue as well as DNR Commissioner Menge.[63] The State's commitment to allow PTU development to focus on gas sales was a key term in the group's proposal which became important to the State as well.[64] The proposed "Fiscal Contract" that emerged from these negotiations required full commitment of the PTU reserves.[65]

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[61] Exc. 297-301. *See* ch 4, SLA 2003 (enacting AS 43.82.100(1)(A) and related provisions). Also in 2004, Congress enacted the Alaska Natural Gas Pipeline Act to expedite construction of a pipeline to bring the North Slope gas to market. *See* 15 U.S.C. §§ 720-720m (2006).

[62] *See* R. PTU 1602 ("The project plan assumes the Alaska Gas Pipeline Project will be underpinned by gas supplied from leases within the Prudhoe Bay Unit (PBU) and Point Thomson Unit (PTU). Both of these resources would be necessary to support the pipeline project."). *See also* R. PTU 1594-95, 1602-04, 2504.

[63] R. PTU 1896-97. *See, e.g.,* November 16, 2006, Alaska Department of Revenue "Appendix T to Interim Fiscal Interest Finding dated November 16, 2006 Chronology of Negotiations" [hereinafter "Interim Findings"] at 36-43, attached as exhibit 2 to LaPorte Affid.

[64] *See* Interim Findings, *supra* n.63, at 49, 51.

[65] Recital 11 of the proposed Fiscal Contract states that "PTU Gas resources are essential to anchor the Project and achieve the economies of scale consistent with delivering ANS [Alaska North Slope] Gas to Canadian or United States markets at a competitive cost of supply." R. PTU 2024 (italics for defined terms omitted).

The 22nd POD and the First Purported Termination of the PTU

In July 2005, the WIOs sent DNR a draft 22nd POD designed to be a logical extension of the approved 21st POD.[66] Like the 21st POD, the draft 22nd POD did not call for new drilling or production operations, but focused on preparatory work for supplying gas to the contemplated pipeline. DNR Oil and Gas Division Director Myers responded that the draft was not acceptable to DNR but suggested changes that would make it acceptable.[67] The WIOs adopted all the changes but one—a requirement that the WIOs commit to drilling a new delineation well within one year—and formally submitted the proposed POD to DNR. The WIOs explained that the well, which would cost $60 million, was neither necessary nor economically justifiable and would be potentially unsafe to design and drill on such a short timetable given the risks of high-pressure drilling.[68]

Director Myers formally rejected the proposed 22nd POD in a written decision issued on September 30, 2005, the final day of the 21st POD.[69] Invoking Section 21 of the PTUA, he held that he had "authority to modify the rate of development to achieve the conservation objectives under the PTU Agreement, and ... increasing the rate of development in the PTU is necessary and advisable."[70] He also gave notice that under Section 21, subject to a hearing to be held within 30 days, DNR was requiring the WIOs to "initi-

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[66] Exc. 302-305, 325-333; R. PTU 956-57.

[67] Exc. 334-336.

[68] Exc. 337-349; R. PTU 941-45, 957.

[69] Exc. 350-73.

[70] Exc. 371.

ate development activities within the PTU by October 1, 2007."[71] No Section 21 hearing was held, however, because less than 30 days after issuing the September 2005 decision, Director Myers *sua sponte* issued an amended final decision disclaiming reliance on and deleting references to Section 21.[72]

Aside from the deletion of references to Section 21, the amended decision largely tracked the initial decision. It continued to hold that DNR had "authority to modify the rate of development to achieve the conservation objectives under the PTU Agreement, and ... [that] increasing the rate of development in the PTU is necessary and advisable."[73] It declared that the PTUA was in "default" and asserted that "[f]ailure to submit an acceptable plan of development is grounds for termination of the PTU."[74] The amended decision gave the WIOs 90 days to "cure" the default by submitting an acceptable POD.[75] The decision gave examples of commitments to accelerated timetables for further delineation drilling, development, and production that DNR would deem satisfactory.[76] The commitments stated to be sufficient—which included commitments to drill a well in less than a year, to commit funding for a specific development project within a year, and to

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[71] Exc. 351.

[72] Exc. 374-97, 853, 861, 864-65.

[73] Exc. 371, 873.

[74] Exc. 874.

[75] Exc. 874.

[76] Exc. 874-75.

begin commercial production within four years—were substantially more demanding than what the Director had previously requested.

Director Myers' decisions came as a surprise to the WIOs.[77] The DNR Commissioner and other State officials had been supporting the SGDA pipeline proposal. DNR had produced no evidence that drilling a well would make economic sense. And, having approved the suspension of progress toward a gas cycling project only a year before, DNR had no evidence that a reasonably prudent operator would now commit to having the PTU in production within four years.

The WIOs requested and received from DNR Commissioner Menge extensions of time to appeal from the Director's decision in order to permit the SGDA pipeline negotiations related to the PTU to continue.[78] The State representatives, including Commissioner Menge, adhered to the position that the State's interests would be best served if the PTU were developed in conjunction with the plans for a gas pipeline, and that there was no compelling technical reason to drill an additional well in the near term.[79] When the proposed Fiscal Contract for the pipeline was announced by the State in mid-2006, it did not require the WIOs to meet any of the deadlines that Director Myers had called for in rejecting the proposed 22nd POD. Instead, the Fiscal Contract allowed the WIOs to focus

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[77] R. PTU 957.

[78] Exc. 398-99, 402-404, 408-409; Appx. 124.

[79] Appx. 124-25. Commissioner Menge told the Legislature that "Point Thomson turns out to be the single crucial most key issue in building this pipeline," and testified that putting the PTU into default would be wrong for Alaska because "without Point Thomson there's no gas line." R. PTU 9228, 9231; *see generally* R. PTU 9225-48.

exclusively on gas production and entirely exempted the PTU from annual PODs pending construction of a gas pipeline.[80] The Commissioner of Revenue told critics of the proposed Fiscal Contract that there was no evidence that it would be profitable to develop the oil at PTU.[81]

By the fall of 2006, however, with legislative approval of the Fiscal Contract appearing doubtful, Commissioner Menge directed the WIOs to proceed with their appeal and to submit, if they chose, a modified 22nd POD.[82] Consistent with the plans the Commissioner himself had endorsed, the WIOs submitted a modified POD continuing to focus on preparing for gas sales.[83] But in recognition of the possibility that the Fiscal Contract might not be approved, the modified POD also included a commitment to re-examine, once again, the economic feasibility of a gas cycling plan, and to drill a well during the 2008-09 drilling season.[84] The WIOs supported the modified POD with evidence and expert opinion that the modified POD was consistent with what a reasonably prudent operator would do.[85] DNR presented no contrary evidence.

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[80] R. PTU 2194-96; Appx. 282-83.

[81] R. PTU 838.

[82] Exc. 403-404.

[83] Exc. 413-417.

[84] Exc. 412-428. *See* R. PTU 941-45, 948-50 (explaining why it was imprudent to plan for drilling a well sooner than the 2008-09 season).

[85] *See* R. PTU 905-11, 934-38, 941-50, 955-60; *see generally* R. 733-854 (ExxonMobil brief to Commissioner); Exc. 432-471 (BPXA brief to Commissioner, incorporating exhibits at R. 898-3715).

In November 2006, Commissioner Menge issued a decision upholding the Director's rejection of the 22nd POD and rejecting the modified 22nd POD.[86] Asserting that the PTUA did not require DNR to evaluate a proposed POD under the reasonably prudent operator standard, the decision took the view that any POD that did not commit the PTU to immediate production warranted disapproval. The decision ignored that DNR itself had approved each of the previous PODs that did not propose to bring the PTU into production.[87] The Commissioner concluded his decision by terminating the PTUA, effective immediately.[88] In giving his reasons for termination, he again emphasized that it did not matter, in his view, whether a reasonably prudent operator would have undertaken the drilling, development, and production activities demanded by DNR, or performed them on the schedule demanded by DNR.[89]

Like the earlier POD rejection, the termination of the PTUA came as a surprise to the WIOs. DNR had given no notice that it contemplated terminating the unit on appeal. Moreover, the WIOs believed (and still believe) that termination of a unit with DNR-certified wells or wells otherwise capable of producing in paying quantities may be pursued only via judicial rather than administrative proceedings.[90] Even the Commissioner

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[86] Exc. 499-518.

[87] Exc. 513-518.

[88] Exc. 518.

[89] Exc. 516.

[90] *See generally* Brief of Appellants ExxonMobil Corp., BPXA, and Chevron U.S.A. at R. 2868-78; Brief of Appellant ConocoPhillips Alaska, Inc. at R. 3115-37, and Reply Brief of ConocoPhillips at R. 3999-4042.

appeared to share this understanding: as part of his decision, he purported to "decertify" the PTU's seven certified wells.[91]

The First Appeal to the Superior Court

The WIOs appealed the Commissioner's decision to the superior court. Attorneys representing the State (from the Alaska Department of Law and outside counsel, Ashburn & Mason, P.C.) advocated for affirmance of the decision.[92] DNR employee G. Nanette Thompson acted as the agency representative seeking to uphold the Unit termination, making at least one appearance for DNR at a hearing before Judge Gleason.[93]

Judge Gleason affirmed in part, reversed in part, and remanded for further proceedings. She held that DNR was not obliged under Section 10 of the PTUA to approve a proposed POD that met the RPO standard, but could disapprove a POD based on the agency's evaluation of additional public interest factors.[94] She also held that DNR had jurisdiction, under the regulatory scheme in effect when it approved the PTUA in 1977, to adjudicate administratively whether the facts and law warranted termination of the

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[91]Exc. 510-11, 516-17. Judge Gleason initially ruled that the WIOs had made a "clear showing of probable success on the merits" of their claims that DNR had violated its own regulations in decertifying the wells and administratively terminating the PTUA, but in her 2007 Decision On Appeal she did not reach the propriety of the purported "decertification." Exc. 571; R. 1816. The issue will be reviewable as part of a plenary appeal after the superior court issues a final judgment.

[92] Exc. 1029 n.99; *See* Section V.B.1, *infra*.

[93] DNR Brief at 73.

[94] Exc. 555-59. The WIOs do not agree with this ruling and reserve the right to challenge it in a plenary appeal from any adverse judgment.

PTUA after the rejection of the original and modified 22nd PODs.[95] But Judge Gleason also held that DNR was not authorized to terminate the PTUA merely because the agency had rejected those proposed PODs. As her decision stated:

> [R]ejection of a proposed plan of development does not result in automatic termination under the PTUA. Rather, a separate administrative determination as to the appropriate remedy is required in such instance.... Nothing in the PTUA nor the regulatory framework in place in 1977 mandated or authorized automatic termination of the unit when DNR rejected the proposed POD.[96]

Judge Gleason made special note of PTUA Section 21, observing that "[t]his section may well have applicability when determining the appropriate remedy when DNR rejects a proposed plan of development."[97] But she stopped short of reaching the merits of DNR's purported termination order because she found, as a procedural matter, that DNR had violated the WIOs' due process rights by failing to provide adequate notice that termination was even under consideration.[98] Instead, she remanded the matter to DNR "for the purpose of according to the [WIOs] a hearing on the appropriate remedy ... upon DNR's rejection of the proposed 22nd Plan of Development."[99] Consistent with her

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[95] Exc. 562-63, 565-67. The WIOs do not agree with this ruling and reserve the right to challenge it in a plenary appeal from any adverse judgment. *See* n.146 *infra.*

[96] Exc. 574, 576.

[97] Exc. 559 n.7.

[98] Exc. 577.

[99] *Id.*

discussion of Section 21, she gave DNR specific instructions to "consider the import of § 21 of the PTUA, as amended in 1985, in determining the appropriate remedy."[100]

The 23rd POD and the Second Purported Termination of the PTUA

Two weeks after remand, DNR gave written notice that it was still considering termination of the PTU.[101] Commissioner Irwin informed the WIOs that Ms. Thompson, the DNR employee who had acted as DNR's representative in the superior court, would serve as Hearing Officer.[102] DNR granted the WIOs' request for an evidentiary hearing, but Ms. Thompson limited the evidence to the issues of (1) what remedy other than terminating the PTUA did the WIOs contend DNR should consider, and (2) what bases did the WIOs have for contending that DNR should accept any remedy other than terminating the PTUA.[103] DNR refused to take evidence on whether the WIOs had committed a material breach of the PTUA, and assigned the WIOs the burden of proving that termination was not appropriate.[104]

The WIOs submitted a 23rd POD, which they asked DNR to approve as the appropriate remedy upon DNR's rejection of the 22nd POD.[105] The 23rd POD contained

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[100] *Id.*

[101] Exc. 581-82.

[102] Exc. 590.

[103] T. 56-57, 64, 66-67; Exc. 590-91, 884.

[104] T. 56-57.

[105] Exc. 604-621, 887. Approving the proposed POD would moot the question whether there had been a material breach of the PTUA. *Id.*

detailed plans for delineating the PTU reservoirs by drilling five wells and for commencing commercial production by year-end 2014 through a modified cycling project.[106] These commitments were unconditional.[107] The 23rd POD met all the objectives DNR had articulated when it rejected prior, less ambitious PODs. The WIOs asked, if DNR did not accept this POD because DNR believed a different rate of development was appropriate, that DNR follow the procedural and substantive requirements of PTUA § 21.[108]

The WIOs also asked DNR for procedural protections to ensure that they received a fair adjudicatory hearing. Among other things, they asked that the Commissioner appoint an independent deciding officer to avoid the appearance (and reality) of the conflict of interest inherent in allowing the decision as to the PTUA's future to be made by the agency that most stood to benefit if the Unit were terminated.[109] If the Commissioner was to preside at the hearing, the WIOs requested that he have independent counsel so that the Alaska Department of Law was not representing both a party and the deciding officer.[110] When the Commissioner confirmed that he would be the decisionmaker, the WIOs also requested that the Commissioner institute procedures to protect himself against *ex parte*

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[106] In contrast to the prior full-field cycling projects studied by the WIOs which proved technically risky and uneconomic, the 23rd POD proposed a two-well cycling project with three additional delineation wells. Exc. 609-10. The proposal minimized technical risk by starting with a smaller cycling project, and designed the facilities to be expandable based on the results of the initial five-well drilling program. Exc. 609, 615.

[107] Exc. 609-611.

[108] Exc. 585-86, 881-82, 887-93, 897-904, 922.

[109] Tr. 51; Exc. 584, 881-83, 893-96, 922-24.

[110] *Id.*

contacts with his staff on the subject of the hearing, so that his decision would be independent and based on the record.[111] DNR denied all these requests.[112]

The WIOs demonstrated at the hearing that the 23rd POD met the objectives that DNR had defined.[113] In addition, all the wells to be drilled under the POD could later be used for gas production when a pipeline became available.[114] Costs of the 23rd POD were estimated to exceed $1.3 billion over seven years.[115] To dispel any concern that the WIOs did not really intend to drill, no optional payments in lieu of drilling were proposed.[116] Backing this up, the WIOs stipulated to allow entry of a proposed final judgment providing judicial enforcement of the POD milestones.[117]

The WIOs also made clear that they did not present the 23rd POD as a "take it or leave it" proposal. They repeatedly stated their willingness to discuss with DNR the terms of the POD, to consider changes that DNR might desire, and to consider adding additional consequences for not fulfilling all the commitments, if DNR believed such addi-

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[111] T. 49-50, 53-54; Exc. 592.

[112] Tr. 47, 50; Exc. 590-91, 884-85, 922-25; R. 30521-22.

[113] R. 30000-357, 30614-860; Tr. 88-1051. Because DNR limited the hearing time, the Commissioner allowed additional materials to be submitted after the hearing, and the WIOs did so. R. 30912-1077, Exc. 590.

[114] T. 105.

[115] R. PTU 30004.

[116] T. 864-65, 1016.

[117] Exc. 720-724.

tions were appropriate.[118] All the WIOs presented evidence of their financial commitment to fund the 23rd POD.[119]

Finally, the WIOs presented evidence that terminating the PTUA would delay production by many years. Among other reasons, new lessees would not have access to all the proprietary data the WIOs had amassed during their years of studying and planning for PTU production.[120] DNR presented no evidence at the hearing. As a result, the WIOs' evidentiary presentation about the quantity and producibility of the hydrocarbon resources, the feasibility of various development plans, and the viability of the POD's plan for commencing production by 2014 was entirely uncontradicted.

Commissioner Irwin issued his decision on April 22, 2008.[121] He assumed that prior proceedings had established a material breach and that the only issue he had to decide was the appropriate remedy.[122] He rejected the 23rd POD as an appropriate remedy, and then summarily rejected the applicability of Section 21.[123] He concluded his opinion by again terminating the PTUA.[124]

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[118] T. 33-34, 46-47, 866-67, 874, 1008, 1038, 1043-44.

[119] T. 166, 225-27, 862-63; R. PTU 30917, 31115, 31122.

[120] T. 211-12, 470-71, 903-07, 960-62; R. PTU 30978-79, 31061-63.

[121] Exc. 658-736.

[122] Exc. 689, 727-28.

[123] Exc. 723-25.

[124] Exc. 689-723.

Commissioner Irwin's decision suggests that no plan the WIOs could have presented would have persuaded him not to terminate the PTUA. The decision rested principally on his assertion that the WIOs had broken past development commitments and could not be trusted to fulfill the commitments in the 23rd POD:

> Despite the fact that the plan may present a technically reasonable first step for developing these lands from a conservation perspective, it is an inappropriate remedy because I can find no basis in this record to conclude that I can be assured that it will be completed as promised; or that if the 23rd POD is completed, that Appellants will continue to expand production as promised.... I cannot risk the continued delays in development of this valuable state resource by these WIOs with this history of unfulfilled commitments.[125]

The Purported Lease Terminations and Conditional Approval for Gas Cycling

After terminating the PTUA, DNR purported to terminate all the underlying leases in the PTU by notices titled "Lease Expiration Due To Elimination From Unit."[126] The WIOs appealed the notices to the Commissioner, who held a hearing in January and February 2009.[127] Notwithstanding his assertion in 2008 that the 23rd POD would not be carried out, on January 27, 2009, the Commissioner issued a Conditional Interim Decision conditionally reinstating two leases because the WIOs "have offered testimony and evidence that they are engaged in 'drilling operations' for the purpose of diligently working in good faith to bring [two leases] into production ...."[128] As promised in the 23d POD,

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[125] Exc. 691 (footnote omitted).

[126] R. PTU 31590-651.

[127] Exc. 762.

[128] Exc. 764.

two wells have been drilled thus far. Permitting and design work on the production facilities is now well advanced. More than 150 companies have been engaged to help with the work and more than $730 million has been expended on it since October 2008.[129]

The Second Appeal to the Superior Court

After carefully reviewing the WIOs' appeal of the Commissioner's second termination decision, Judge Gleason again reversed, on two independent grounds.[130] First, noting that DNR had repeatedly cited its dissatisfaction with the rate of development under the PTUA as the basis for the purported termination, she found that DNR erred by failing to apply Section 21 of the PTUA, the specific contractual provision that governs DNR's authority to unilaterally increase the rate of development.[131] She explained that her 2007 decision had already held that DNR's refusal to approve a proposed POD in these circumstances did not in itself establish a material breach of the PTUA. Rejecting DNR's arguments that Section 21 did not apply, she held that Section 21 by its terms applies even in the absence of an approved POD and even when the rate of prospecting, development, or production is zero.[132] She also rejected DNR's arguments that her 2007 decision somehow precluded a Section 21 hearing, that applying Section 21 after DNR rejects

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[129] *See* Exxon's October 27, 2010 news release "ExxonMobil Announces Successful Drilling of Point Thomson Wells," attached as exhibit 4 to LaPorte Affid.

[130] Exc. 765, 793.

[131] Exc. 786-87.

[132] Exc. 779-84.

a POD would undermine DNR's authority, and that applying Section 21 would impermissibly shift the burden of designing an adequate POD to DNR.[133]

Second, Judge Gleason found that participation in the Commissioner's deliberations by persons who were part of the DNR legal team in the prior appeal was a *per se* violation of due process under this Court's decision in *In re Robson*.[134] She correctly noted that it was "undisputed" that "the Commissioner, acting in an adjudicative role, was advised by the same attorneys and staff who had represented the agency in the first appeal to the Superior Court."[135] (To avoid discovery on this issue in earlier proceedings before Judge Gleason, DNR had admitted that litigation staff and personnel who defended DNR during the first appeal later advised the Commissioner during the remand proceedings.[136]) Judge Gleason also noted that the Commissioner had appointed Ms. Thompson as the hearing officer on remand even though she had previously acted as DNR's official representative in the superior court when the agency defended the first appeal. Under *Robson*, Judge Gleason found that the private interaction of DNR's attorneys and Ms. Thompson with the Commissioner violated DNR's constitutional obligation to "'assure both the fact and appearance of impartiality in the agency's decisional

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[133] Exc. 784-87.

[134] 575 P.2d 771 (Alaska 1978); Exc. 791-92.

[135] Exc. 789.

[136] Exc. 1029 n.99, 1096-97.

function.'"[137] This was so even in the absence of any evidence that the former advocates took an active part in the Commissioner's substantive deliberations.[138]

In light of her rulings on Section 21 and the *Robson* due process violation, Judge Gleason expressly declined to reach numerous other issues raised by the WIOs.[139] Accordingly, even if DNR were to prevail on the two discrete questions raised in this petition (which it should not), the case would have to be remanded to the superior court for consideration of these remaining issues, as DNR itself acknowledges.[140]

IV. STANDARD OF REVIEW

This Court should, as did Judge Gleason, review *de novo* the proper interpretation of Section 21 since it is a matter of contract interpretation and therefore does not involve

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[137] Exc. 791-92 (quoting *Robson*, 575 P.2d at 775).

[138] Exc. 792.

[139] These unresolved issues include: whether DNR breached its duties of good faith and cooperation by terminating the PTUA, whether there was any permissible basis for the Commissioner to find a material breach warranting termination, whether forfeiture could be avoided even if there were a material breach, whether the Commissioner committed legal error by evaluating the 23rd POD under a subjective rather than an objective standard, whether the Commissioner's decision rested on misunderstandings and misreadings of the 23rd POD, whether the Commissioner failed to apply the proper standard in determining whether the WIOs' assurances regarding future performance were reasonably adequate, whether other aspects of DNR's extraordinarily one-sided hearing procedures (which included, among many other due process violations raised by the WIOs, DNR's refusal to provide any pretrial discovery, its refusal to provide a neutral decisionmaker, and its shifting of the burden of proof to the WIOs) violated the WIOs' due process rights, and whether DNR's actions violated the constitutional prohibition against impairment of contracts. Exc. 775-76 (summarizing Brief of Appellants, dated January 30, 2009, at 1-2).

[140] *See, e.g.*, DNR Brief at 8.

agency expertise.[141] DNR asserts that a rational basis standard should apply because the PTUA is "is not just any contract."[142] DNR notes that it approved the PTUA and is responsible for managing state lands in the public interest, and that the PTUA generally incorporates then-in-effect or later-enacted-and-consistent statutes and regulations.

But this Court has squarely held that a unit agreement *is* to be construed like any other contract, the interpretation of which is subject to the Court's independent judgment.[143] The principle that deference may be owed to DNR's interpretation of oil and gas statutes and regulations does not mean that deference is likewise owed to DNR's interpretation of negotiated contract provisions.[144] DNR's case citations are inapposite be-

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[141] Exc. 776-77, citing *Quality Asphalt Paving, Inc. v. State, Dep't of Transp. & Pub. Facilities*, 71 P.3d 865, 872 n.10 (Alaska 2003) ("We will substitute our own judgment for questions of law not involving agency expertise, such as contract interpretation."), and *Alaska Hous. Fin. Corp. v. Salvucci*, 950 P.2d 1116, 1119 (Alaska 1997) ("Interpretation of a contract is a question of law on which this court substitutes its own judgment.").

[142] DNR Brief at 26.

[143] *Exxon Corp. v. State*, 40 P.3d 786, 788, 792 (Alaska 2001) (reviewing the interpretation of a unit agreement under the independent judgment standard, and stating that a "unit agreement is a contract between the department and lessees" and that its interpretation "is not within the department's special expertise or skill").

[144] When a contract adopts a specified regulatory standard as a measure of performance, deference may be owed to DNR's interpretation and application of the underlying standard. *See ConocoPhillips Alaska, Inc. v. State*, 109 P.3d 914, 920 (Alaska 2005). But that is not the situation here, where the question presented is the purely contractual one of whether DNR, if it wanted to mandate an increase in the rate of prospecting, development, or production on the Unit, was obliged to comply with the procedures specified in PTUA Section 21.

cause they concern the interpretation of laws or regulations and not contracts.[145] No legal principle or precedent allows one party, even the State, to demand that a court defer to its own interpretation of a contract in a dispute concerning that contract.[146]

Judge Gleason's due process ruling is reviewed *de novo*.[147]

V. ARGUMENT

A. DNR Was Required To Invoke Section 21 To Unilaterally Increase The Rate Of Prospecting, Development, Or Production.

Judge Gleason concluded that the WIOs were entitled to a hearing under PTUA Section 21 because (1) DNR sought to increase the rate of development and production

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[145] *See* DNR Brief at 26 n.135, 26 n.138, citing *Union Oil Co. v. State*, 804 P.2d 62, 64 (Alaska 1990) (interpretation of tax statutes and tax policy); *Dep't of Revenue v. Atlantic Richfield Co.*, 858 P.2d 307, 308 (Alaska 1993) (interpretation of an agency's own regulation); *Bd. of Trade, Inc. v. Dep't of Labor, Wage & Hour Admin.*, 968 P.2d 86, 89 (Alaska 1998) (same).

[146] This would be an especially inappropriate case to create a new rule of contractual deference given the significant uncertainty as to whether DNR had jurisdiction to administratively adjudicate the purported termination of the PTUA in the first place. The PTUA authorizes DNR to terminate the agreement by administrative proceedings only before a well capable of producing unitized substances in paying quantities is completed. To the same effect, 11 AAC 83.374(d) requires DNR to initiate *judicial* proceedings if it seeks to terminate a unit agreement governing a unit in which there is a well capable of producing oil or gas in paying quantities. Judge Gleason held in her 2007 decision that DNR has inherent authority to terminate unit agreements and that 11 AAC 83.374(d) did not bind DNR because it was adopted after the effective date of the PTUA. Exc. 568-71. But her ruling on these points will be reviewable in a plenary appeal after final judgment, and its correctness is seriously open to question. The requirement for judicial proceedings in these circumstances is both consistent with DNR's uniform prior practice and compelled by the nature of the interests at stake once a valuable discovery has been made. And regulations adopted to protect the rights of parties dealing with the government normally should be applied retroactively in any event. *Atlantic Richfield Co. v. State*, 705 P.2d 418, 424 n.17 (Alaska 1985).

[147] DNR Brief at 27. *E.g.*, *Calvert v. Dep't of Labor & Workforce Dev.*, 251 P.3d 990, 998 (Alaska 2011).

on the PTU (and, indeed, expressly rejected the proposed 22nd and 23rd PODs because they did not, according to DNR, assure that development and production would proceed on the timetable DNR desired); and (2) under Section 21, DNR may unilaterally alter or modify the rate of prospecting, development, or production only after providing notice and an opportunity for a hearing on whether the proposed alteration or modification comports with the agreed limitations on DNR's exercise of that right.[148] That reasoning was eminently sound, and the decision should be affirmed.

First, Judge Gleason correctly found that DNR's objective, since the beginning of the events leading to this litigation, has been to accelerate the rate of development under the PTUA so as to enable earlier commencement of production.[149] DNR does not challenge this factual finding. Indeed, DNR affirmatively asserts that it has been trying to increase the rate of development for many years.[150]

Second, Judge Gleason correctly found that Section 21 necessarily applies when DNR will not approve the rate of development or production contemplated by a proposed POD. As discussed below, under the plain language of the PTUA, DNR must comply with Section 21 before it can force an increase in the rate of prospecting, development, or production over the WIOs' objections. Section 21 so interpreted is fully consistent with Section 10, which under DNR's contrary reading would impermissibly nullify Section 21. DNR's various arguments that Section 21 was inapplicable in the circumstances—for

[148] Exc. 780-81, 787.

[149] Exc. 780.

[150] DNR Brief at 4-5.

example, because there was no ongoing production—are also meritless, as is DNR's contention that the parties' prior conduct precluded the section's application. And finally, enforcing Section 21 is fully consistent with public policy as expressed in Alaska's constitution, statutes, and regulations and does not undermine DNR's regulatory authority.

1. Section 21 Applies Whenever DNR Seeks Unilaterally To Alter The Rate Of Prospecting, Development, Or Production.

Section 21 expressly empowers DNR, without the consent of the signatory lessees, to "alter or modify from time to time at [its] discretion the rate of prospecting and development and the quantity and rate of production under this agreement."[151] Section 21 also expressly limits that authority as follows:

> Powers in this section vested in [DNR] shall only be exercised after notice to Unit Operator and opportunity for hearing ..., *and shall not be exercised in a manner that would (i) require any increase in the rate of prospecting, development or production in excess of that required under good and diligent oil and gas engineering and production practices; or (ii) alter or modify the rates of production from the rates provided in the approved plan of development and operations then in effect or, in any case, curtail rates of production to an unreasonable extent, considering unit productive capacity, transportation facilities available, and conservation objectives; or (iii) prevent this agreement from serving its purpose of adequately protecting all parties in interest hereunder, subject to applicable conservation laws and regulations.*[152]

The non-italicized language was part of the original PTUA as approved by DNR in 1977. As described earlier, the italicized language was added in a package of amendments

[151] Exc. 166.

[152] Exc. 167 (italics added).

requested by the WIOs and approved by DNR in 1985 after exploratory drilling had revealed the extraordinary development and production challenges at Point Thomson.[153]

The Court should favor a plain reading of a contract if it gives reasonable effect to all of its provisions.[154] The plain language of Section 21, which is consistent with the rest of the PTUA's provisions, authorizes DNR to unilaterally alter or modify the rate of prospecting, development, or production under the PTUA only if the change:

> (1) is in the interest of attaining the PTUA's stated conservation objectives (or alternatively, in the case of production, is in the public interest),[155]
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> (2) does not violate any applicable state law,
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> (3) does not "require an increase in the rate of prospecting, development or production in excess of that required under good and diligent oil and gas engineering and production practices,"
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> (4) does not "alter or modify the rates of production from the rates provided in the approved plan of development and operations then in effect or, in any case, curtail rates of production to an unreasonable extent," and

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[153] Exc. 53, 129.

[154] *E.g.*, *Norville v. Carr-Gottstein Foods Co.*, 84 P.3d 996, 1001 n.3 (Alaska 2004); *Grant v. Anchorage Police Dept.*, 20 P.3d 553, 556 (Alaska 2001).

[155] PTUA Section 16 states the conservation objectives: "Operations hereunder and production of unitized substances shall be conducted to provide for the most economical and efficient recovery of said substances without waste, as defined by or pursuant to state law or regulation." Exc. 162.

(5) does not "prevent [the PTUA] from serving its purpose of adequately protecting all parties in interest."[156]

In addition, DNR may order such an increase only after providing notice of its intent to do so and an opportunity for a hearing on DNR's proposed action.

DNR, in rejecting the 22nd and 23rd PODs, was attempting to force an increase in the rate of development and production under the PTUA. DNR's initial decision rejecting the proposed 22nd POD expressly invoked Section 21 to order such an increase.[157] DNR's amended decision, which purported to disclaim reliance on Section 21, continued to demand accelerated development and production as a condition of approval.[158] And DNR rejected the proposed 23rd POD on the ground that it was "not adequate to insure timely development."[159] Although DNR disputes the applicability of Section 21, it does not and cannot dispute that it rejected the proposed 22nd and 23rd PODs because DNR desired to increase the rate of development and production at Point Thomson.

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[156] As the Operator covenants in Section 10 "to develop the unit area as a reasonably prudent operator in a reasonably prudent manner," this condition protects the operator from being compelled to develop the unit in a way that a reasonably prudent operator acting in a reasonably prudent manner would not do. This protection is essential given that DNR obtains the benefits of royalties, but generally does not share the burdens and risks of development costs.

[157] Exc. 371 ("The Director has the authority to modify the rate of development to achieve the conservation objectives under the PTU Agreement, and I find that *increasing the rate of development* in the PTU is necessary and advisable.") (emphasis added).

[158] Exc. 515 (finding that the WIOs did not propose "to *adequately* explore, delineate, or *produce*" the Unit's hydrocarbons) (emphasis added). Exc. 873 ("...I find that increasing the rate of development in the PTU is necessary and advisable.").

[159] Exc. 734.

The only provision of the PTUA that authorizes DNR to alter the rates of development or production without the WIOs' consent is Section 21. It therefore applies here, as Director Myers acknowledged in his initial decision invoking Section 21.[160] Under the plain terms of the PTUA, if DNR is not satisfied with the rate of development and production in a proposed POD and cannot obtain the WIOs' agreement to submit a modified or replacement POD that DNR is willing to approve, DNR may impose its preferred rates unilaterally only if it complies with Section 21.

2. Section 21 Is Consistent With Section 10, Which Under DNR's Contrary Reading Would Nullify Section 21.

According to DNR, Judge Gleason held that DNR must invoke Section 21 whenever DNR rejects a POD.[161] And that conclusion, DNR argues, conflicts with the language and purpose of Section 10 which, along with 11 AAC 83.303, governs how DNR evaluates a proposed POD.[162] But that is not what Judge Gleason said, and what she did say is perfectly consistent with Section 10.

Judge Gleason did not say that DNR must invoke Section 21 *whenever* DNR rejects a POD. She said a Section 21 hearing is the "natural progression" from the rejection of a POD *when* the rejection, as here, was based on DNR's demand to accelerate development and production under the PTUA. In Judge Gleason's view, DNR was required to comply with Section 21 because DNR purported to hold the WIOs in default and sought

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[160] Exc. 351, 853, 864-65.

[161] DNR Brief at 42-44.

[162] *Id.*

to terminate the Unit for failure to submit a POD that satisfied DNR's demand for faster development and production.[163] That reasoning is unassailable. Allowing DNR to terminate the PTUA for failure to propose a POD that meets DNR's desired timetable for development and production is functionally the same as allowing DNR to impose that timetable unilaterally. But Section 21 expressly provides that DNR may unilaterally change the rate of development and production *only* after providing notice and the opportunity for a hearing on whether the agreed conditions for DNR's exercise of that authority have been met. To allow DNR to terminate the PTUA for failure to submit a POD that meets DNR's desired rate of development and production without complying with Section 21 would nullify Section 21's protections and effectively read Section 21 out of the contract.

DNR argues at length that, based on its language and history, Section 21 is an optional path for DNR, giving DNR a power and not placing a burden on it.[164] Judge Glea-

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[163] Exc. 780-82.

[164] DNR Brief at 33-41. DNR argues that Section 21 bestows a power on it based on its similarity to a 1931 amendment to the federal Mining Act of 1920. DNR Brief at 40. But Section 21 of the PTUA contains additional language—specifically, the language added to Section 21 in 1985—that is not present in the Mining Act. *Compare* 30 U.S.C. § 226(m) ("Any plan...may, in the discretion of the Secretary [of the Interior] contain a provision whereby authority is vested in the Secretary of the Interior, or any such person, committee, or State or Federal officer or agency as may be designated in the plan, to alter or modify from time to time the rate of prospecting and development and the quantity and rate of production under such plan.") *with* Exc. 166-67 ("Power in this section...shall not be exercised in a manner that would (i) require any increase in the rate of prospecting, development or production in excess of that required under good and diligent oil and gas engineering and production practices...or (iii) prevent this agreement from serving its purpose of adequately protecting all parties in interest hereunder"). It is this additional language, concerning the standard of good and diligent oil and gas engineering and production practices, the requirement to protect the interests of all parties, etc., that is at is-

son did not say anything different. She merely held that, if DNR seeks to exercise its option to unilaterally alter the rate of prospecting, development, or production, then it must comply with Section 21. What DNR may not do is avoid its obligations under Section 21 by terminating the Unit because the WIOs did not propose a POD that accelerates prospecting, development, or production to DNR's preferred rate.

Properly interpreted, therefore, Section 21 does not conflict with DNR's claim that Section 10, along with applicable statutes and regulations, governs the parties' rights and obligations in the POD-approval process. A cardinal principle of contract interpretation is to give meaningful effect to all provisions of a contract.[165] This is why DNR's purported reading of Section 10 as "trumping" Section 21 must be rejected. If DNR could employ Section 10 to alter the rate of development and production by rejecting any proposed POD that did not assure the agency's desired rate and then declaring a default for failure to submit a satisfactory POD, Section 21 would have no function and the protections it establishes for the WIOs—and the public—would be rendered meaningless.

DNR's reliance on Section 10 as a provision vesting the State with broad authority to terminate a unit in the public interest is likewise misplaced. The WIOs' obligation un-

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sue in this case. *See also* Section V.A.5, *infra*, agreeing with DNR that Section 21 gives DNR a power, albeit a power with limits.

[165] *Exxon Corp. v. State*, 40 P.3d 786, 794 (Alaska 2001) ("Moreover, we have repeatedly noted that '[a] court should not interpret an agreement in a manner which would give meaning to one part of an agreement at the cost of annulling another part.'") (quoting *Betz v. Chena Hot Springs Group*, 657 P.2d 831, 835 (Alaska 1982)).

der Section 10 is to submit a POD that meets the RPO standard.[166] Judge Gleason held in her 2007 Decision that Section 10 nevertheless confers on DNR the discretion to reject a proposed POD without regard to the RPO standard if DNR finds that the pace of development and production contemplated in the POD is not in the public interest as that standard is elucidated in applicable statutes and regulations.[167] "But," as Judge Gleason stated in her Decision After Remand, "when Section 10 is interpreted in that manner, it cannot be the basis for establishing a material breach of the PTUA by the Appellants."[168]

This interpretation reconciles and gives meaning to both Section 10 and Section 21. Under Section 10 as construed by Judge Gleason, DNR may reject a proposed POD if it finds that the proposed rate of development and production is inadequate to satisfy the public interest. But this does not give DNR *carte blanche* to ignore the interests of the WIOs. Section 10 itself makes this plain by providing that any POD approved by DNR "shall be modified or supplemented when necessary ... to protect the interests of *all parties to this agreement.*"[169] It follows that if DNR and the WIOs cannot agree to a POD

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[166] Under Section 10, the Unit Operator "expressly covenants to develop the unit area as a reasonably prudent operator in a reasonably prudent manner." Exc. 156. The RPO standard is part of the common law. *In re ANS Royalty Litigation*, No. 1JU-77-847, at 42 (Alaska Super. Mar. 13, 1991) (Carpeneti, J.) ("The court holds that the producers have an obligation to act as reasonably prudent operators in performing their duties under the DL-1 lease."). *See* exhibit 1 to LaPorte Affid.

[167] As already noted, the WIOs do not agree with this ruling—the correctness of which is assumed in DNR's petition but is not yet before this Court—and reserve the right to challenge it in a plenary appeal from any adverse judgment.

[168] Exc. 782.

[169] Exc. 157 (emphasis added).

containing a mutually acceptable rate of development and production, DNR may not simply declare a default and terminate the PTUA. Instead, DNR must invoke the procedures and satisfy the conditions established in Section 21 for unilaterally imposing an accelerated rate. If DNR's preferred rate of development and production satisfies those conditions—*i.e.*, it advances the conservation objectives of the agreement and the law, does not depart from good and diligent oil and gas engineering and production practices, and does not prevent the agreement from adequately protecting *all* parties in interest—then DNR may require the WIOs to comply with the accelerated rate. If the WIOs still refuse to develop or produce at that rate, then and only then would DNR have a claim, consistent with the PTUA and applicable statutes and regulations, to terminate the Unit.

3. DNR's Various Arguments That Section 21 Does Not Apply In The Present Circumstances Are Without Merit.

DNR claims that Section 21 by its terms does not apply when there is no approved POD.[170] Judge Gleason correctly rejected that contention.[171] Nothing in Section 21 limits its application to when an approved POD is in place. Subsection (i) of the second paragraph of Section 21 makes no mention of applying only to an approved POD. Instead, it provides that DNR shall not—without qualification—"require any increase in the rate of prospecting, development or production in excess of that required under good and diligent oil and gas engineering and production practices." Subsection (ii) of that paragraph, which addresses only rates of production, states that, when an approved POD establishing

[170] DNR Brief at 39.

[171] Exc. 779-82.

production rates is in place, DNR may not alter or modify those rates at all. And the same subsection goes on to state that "in any case"—*i.e.*, when no approved POD dictates the rates of production—DNR may not curtail them unreasonably. Under both subsections, Section 21 on its face can and does apply when there is no approved POD.

From a practical point of view, moreover, Section 21 would be rendered superfluous and would give the WIOs no meaningful protection if deemed to apply only when there was an approved POD. Most PODs by their terms last only one year.[172] DNR could avoid Section 21 entirely by waiting until a POD expired, refusing to approve the following year's proposed POD because it did not call for fast enough development or production, and then insisting, on threat of termination of the PTUA, that any new POD must meet the agency's demands without regard to the agreed standards and protections of Section 21. This too precludes DNR's interpretation.

DNR also wrongly contends that Section 21 applies only when there is ongoing production under the PTUA.[173] In its petition, DNR argued that ongoing production was required as a condition for application of Section 21 because otherwise the WIOs would have no infrastructure investment requiring Section 21's protection.[174] In its brief, DNR argues that ongoing production is required because otherwise the safety and conservation

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[172] T. 164-65.

[173] DNR Brief at 47-48.

[174] Exc. 800-01.

objectives that Section 21 was intended to protect would not be implicated.[175] These arguments fail for multiple reasons.

First, while DNR's argument speaks only of ongoing *production*, the text of Section 21 speaks of the "rate of prospecting and development" *in addition to* the "quantity and rate of production."[176] Under Section 21, "prospecting" and "development" are not the same thing as "production," so the Section must have been intended to apply to disputes about the rate of prospecting or development before production has begun. It follows that Section 21 cannot logically be limited to scenarios where there is ongoing production. Moreover, it is clear that in the present situation, DNR primarily seeks to alter the rate of *development*, which necessarily is antecedent to production.

Second, DNR's assertion that Section 21 is triggered only when there is *ongoing* production (or development or prospecting) likewise has no grounding in the text of Section 21, or for that matter the rest of the PTUA or the WIOs' Operating Agreement (under which prospecting, development, and production occur).[177] Section 21 applies when DNR seeks to alter "the rate" of prospecting, development, or production. The "rate" can be zero.[178] In interpreting the word "rate," the Court should look to the "ordi-

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[175] DNR Brief at 48.

[176] Exc. 166.

[177] DNR says ConocoPhillips previously argued that Section 21 does not apply to DNR's attempt to change the rate of production when production has not commenced. DNR Brief at 51. ConocoPhillips's argument was that, before production commences, DNR is seeking to increase the rate of prospecting or development. Exc. 534.

[178] Exc. 782-84.

nary, contemporary, common meaning."[179] As Judge Gleason explained, the word "rate" refers to the amount or speed of development or production; and a "rate" can, indeed, be zero.[180]

Third, DNR asserts that because "production" in the rest of the PTUA and the Operating Agreement refers to actual production, then Section 21 must mean actual production as well. But, even assuming that all of the instances of "production" that DNR cites refer to actual production (which is not the case),[181] DNR ignores the effect of the modifier "rate of...." Speaking of an object's "motion," for example, refers to its actual motion. But referring to an object's "rate of motion" does not: it has a zero rate of motion when it is at rest.

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[179] *Kay v. Danbar Inc.*, 132 P.3d 262, 269 (Alaska 2006).

[180] Exc. 783-84. *See also* the cases Judge Gleason cited: *Amara v. Cigna Corp.*, 534 F. Supp. 2d 288, 324 n.18 (D. Conn. 2008) (referencing Internal Revenue Service ruling mentioning "a period of zero annual rate of accrual"), *vacated and remanded on other grounds*, *Cigna Corp. v. Amara*, 131 S.Ct. 1866 (2011); *State Bd. of Health v. Godfrey*, 290 S.E.2d 875, 877 (Va. 1982) (referencing expert witness's testimony regarding "slow or nil rates of absorption"); *Nw. Pipeline Corp. v. Adams County*, 131 P.3d 958, 960 (Wash. Ct. App. 2006) (referencing possibility that a company would have a "zero growth rate").

[181] Some of DNR's examples use "production" to refer to that which is produced (oil or gas). *See* WILLIAMS & MEYERS, MANUAL OF OIL AND GAS TERMS, "Production" (Lexis 2011) (citing cases illustrating these fundamentally different uses of "production"). *See, e.g.*, DNR's Brief at 50 n.185 (citing Section 6.1B ("All Production from a participating area shall be allocated"); Section 6.2 ("the Production therefrom"); Section 10.2 ("the Production therefrom"); Section 12.3 ("the Production obtained from the well"); Section 20.2 ("entitled to receive the Production from a well"); Section 25.2 ("or otherwise treat Production").

Fourth, it is simply incorrect to assert that safety and conservation principles are not implicated when DNR seeks to increase the rate of development or production from zero, that is, when there has been no development or production.[182] Safety principles are patently implicated in that situation because requiring WIOs to promptly commence development and production requires physical activities on a leasehold; for example, wells need to be designed and drilled and facilities need to be constructed. Commencing development and production also implicates conservation principles, since the pace of development and production affects the volume of hydrocarbons recovered. Indeed, in its decisions below, DNR cited conservation as one of its primary rationales for demanding the production of liquid gas condensate via cycling before the availability of a pipeline for the natural gas sales. According to DNR, producing the condensate in advance of producing the gas may significantly increase the volume of condensate ultimately recoverable from the PTU.[183] In addition, increasing the rate of development (or production) from nothing to something directly implicates conservation because it has economic effects, which PTUA Section 16 explicitly includes among conservation considerations:

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[182] DNR Brief at 48.

[183] *See* Exc. 371 ("Gas cycling theoretically allows the recovery of significantly more liquids than would be recovered in a pure gas blow down project. In a gas blow down scenario, oil and gas condensates that remain in the field following gas sales may be largely unrecoverable."); Exc. 394 (same finding in amended DNR decision).

> CONSERVATION. Operations hereunder and production of unitized substances shall be conducted to provide for the *economical* and efficient recovery of said substances without waste, as defined by or pursuant to state law or regulation.[184]

Finally, DNR's conduct belies its new-found interpretation of Section 21. DNR initially rejected the 22nd POD *and invoked Section 21* on the ground that "increasing the rate of development in the PTU is necessary and advisable."[185] There was ongoing development under the PTUA, just not at the rate DNR desired. DNR later disclaimed Section 21, not on the ground that there was no rate of development under the PTUA, but rather on the assertion that Section 21 "[did] not apply to [DNR's] evaluation of the Unit Operator's proposed plans for development of the Point Thomson Unit."[186] DNR cannot square its new-found interpretation of Section 21 with its course of dealing in this very dispute.

4. The Parties' Past Conduct Does Not Undermine The WIOs' Interpretation Of Section 21.

DNR's argument that the parties' past conduct with regard to prior unapproved PODs undermines the WIOs' interpretation of Section 21 is equally wrong. DNR asserts that the WIOs never before claimed that Section 21 applied in the context of a POD rejection. But that is only because Section 21 operates as a last resort which may never need to be invoked. When DNR rejects a submitted POD, both sides have a duty to cooperate to

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[184] Exc. 50 (emphasis added); *see also* Exc. 371, 394 ("[D]elaying timely production also constitutes waste."); *see also* 11 AAC 83.303(a)(2) (in evaluating a POD, DNR must consider whether it "promotes the prevention of *economic* and physical waste") (emphasis added).

[185] Exc. 371.

[186] Exc. 852.

find a mutually agreeable resolution[187]—one that meets both the WIOs' obligations under the RPO standard and the public interest considerations advanced by DNR, and that adequately protects all parties' interests. That is precisely what happened with the 12th and 15th PODs, which are the *only* earlier PODs that DNR did not approve. In the case of 12th POD, DNR consulted informally with the WIOs and reviewed documents they submitted.[188] In light of that back-and-forth, DNR instructed the WIOs to submit a new 13th POD which DNR then accepted, determining that it was not reasonable to require the WIOs to engage in further exploration or to commit to producing hydrocarbons at that time.[189] Similarly, after DNR initially rejected the 15th POD, the WIOs engaged DNR in a dialogue and then submitted draft revisions for DNR's comment.[190] Based on DNR's feedback, the WIOs revised and resubmitted the 15th POD, which DNR then approved.[191]

Given this history of cooperation, which on every prior occasion resulted in agreement on an approved POD going forward, there was never any occasion or need for DNR to invoke its authority under Section 21 or for the WIOs to demand Section's 21's protections. But that obviously does not excuse DNR from complying with Section 21

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[187] *Trinidad Petroleum Corp. v. Pioneer Natural Gas Co.*, 416 So. 2d 290, 297-98 (La. App. 1982). *See also* Exc. 926, 930, 940-46 (affidavit of Patrick H. Martin, the current editor of the leading treatise on oil and gas law, containing a detailed description of the duty of cooperation in oil and gas law as it applies to the PTUA).

[188] Exc. 830-835.

[189] Exc. 184-85.

[190] Exc. 186-91, 836-49.

[191] Exc. 849.

when, as has now occurred for the first time, the parties could not reach a mutually agreeable resolution and DNR continued to insist that the rate of development and production be increased to meet DNR's desired timetable.

DNR also makes the spurious argument, for the first time in this appeal, that the WIOs have somehow conceded the inapplicability of Section 21 because Director Myers "conditioned approval [of the 21st POD] on [the WIOs'] committing to drill a well in the 22nd POD" and the WIOs did not argue in their administrative appeal of that decision that this directive violated Section 21.[192] DNR's argument leaves out the critical point that Director Myers did not unilaterally impose a new drilling obligation in the 21st POD, but merely specified that the approval of the POD "[did] not relieve the PTU Owners of any of the conditions under which the Division approved the Second Expansion of the PTU."[193] Those conditions included a proviso that, if development drilling did not begin by June 15, 2006, "all of the Expansion Acreage will automatically contract out of the PTU and the PTU Owners will pay $20 million to the State of Alaska."[194] Because this "drill or pay" proviso was part of the Second Expansion Agreement, DNR's enforcement of that proviso was not a unilateral change in the rate of development requiring compliance with Section 21 but rather an independent contractual obligation to which the WIOs

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[192] DNR Brief at 52-53.

[193] Exc. 304.

[194] Exc. 304; *see also* Exc. 248.

had already agreed (and which they ultimately satisfied by paying the $20 million and allowing the expansion leases to contract out of the Unit).[195]

The most telling evidence on the question of how the parties intended Section 21 to operate is DNR's own initial decision, which expressly invoked Section 21 as the agency's basis for requiring a faster rate of development than the WIOs had proposed:

> This decision provides notice under Article 21 of the PTU Agreement that Exxon must initiate development operations within the PTU by October 1, 2007. The Division will contact Exxon to schedule a hearing on this issue, which will be held not less than 30 days from the date of this decision.... The PTU Owners shall have an opportunity for hearing regarding this notice to modify the rate of PTU development.[196]

As described above, DNR later withdrew this decision, presumably for tactical reasons in support of the positions it seeks to advance now, and replaced it with a functionally identical decision disclaiming reliance on Section 21.[197] But the fact that DNR initially *invoked* Section 21 speaks volumes about DNR's current assertions that Section 21 can never apply in these circumstances or that the parties have somehow waived its applicability. DNR is attempting to circumvent the protections and requirements of Section 21 that the parties intended would apply, and Judge Gleason correctly held that DNR may not lawfully do so.

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[195] Exc. 248.

[196] Exc. 351, 372.

[197] Exc. 375, 853, 864-65.

5. Section 21 Is Consistent With The Statutes And Regulations In Effect In 1977 And Does Not Undermine DNR's Authority To Manage The State's Natural Resources In The Public Interest.

DNR repeatedly asserts that the "fundamental issue" for this Court's review is whether Judge Gleason's ruling "entirely undermines DNR's ability to carry out its constitutional mandate to protect the public interest ...,"[198] implying that the constitution somehow excuses DNR from compliance with normal statutory and contract principles so long as it is acting in the "public interest." But no such constitutional mandate exists. The Legislature, not DNR, has the "mandate" under the Alaska Constitution's Article VIII, Sections 2, 8 and 12 to provide for oil and gas leasing.[199] DNR's mandate derives from

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[198] DNR Brief at 4. DNR references this supposed "constitutional mandate" throughout its brief. *See id.* at 6, 9, 10, 29, 30, 31, 32, and 79.

[199] In another matter pending before this Court, DNR, arguing against having to make a best interests finding for each phase of development under its oil and gas leases, explains that although Article VIII delegates authority to the Legislature to administer the state's lands and resources, this constitutional source of legislative authority does *not* impose on DNR any Article VIII duty distinct from its statutorily prescribed duties:

> It is true that DNR's duty can be traced to Article VIII because Article VIII authorizes the legislature to establish the procedures for disposing of state lands, and the legislature chose to require a best interest finding as one of those procedures. However, the fact the duty can be traced to Article VIII does not mean that Article VIII requires it. Numerous provisions of the Alaska Statutes may be traced to Article VIII's delegation of authority to the legislature to administer the state's lands and resources, but not all of these provisions are required by Article VIII.
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> DNR's procedures likely satisfy the duty to produce a "best interest finding" that the superior court articulated. However, subjecting DNR to a constitutional duty which is distinct from what the legislature has prescribed has the potential to raise long-term uncertainty about the validity of DNR's procedures and to delay exploration activities. Given the importance of oil

Article III, Section 16, which requires "faithful execution" of the laws enacted by the Legislature. And of course both the Legislature and the Executive Branch are bound by the state and federal constitutional prohibitions against impairment of contracts.[200]

The Legislature since Statehood has implemented its constitutional mandate to manage natural resources for the benefit of the people by means of the Alaska Lands Act.[201] The Act encourages unitization of oil and gas leases when that is in the public interest, but defines and limits the powers of DNR with respect to unitization precisely to ensure that the public interest is served. The Act recognizes that the public interest includes an array of interests: providing revenue to the State, promoting conservation, preventing physical and economic waste, and protecting the interests of private parties to ensure that adequate investments are made in developing Alaska's natural resources.

The Act provides for written unitization agreements, like the PTUA, to establish the rights of all parties, including the public. If unit agreements could be terminated by DNR "in the public interest" without abiding by contractual constraints, or if additional

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> and gas production to state coffers, the uncertainty and resulting delay would be harmful to the public interest.

Petition for Review, at 12-13, Daniel S. Sullivan, Commissioner, State of Alaska, Department of Natural Resources v. Resisting Environmental Destruction on Indigenous Lands (REDOIL) et al., Case No. S-14216 (Alaska 2011), exhibit 5 to LaPorte Affid. Just as the Article VIII source of legislative authority to prescribe for DNR a best interest finding in oil and gas lease sales under AS 38.05.035(e) does not give that duty a constitutional dimension, so too the Article VIII source of legislative authority to prescribe for DNR a public interest determination in approving unit agreements under AS 38.05.180(p) does not give that duty a constitutional dimension.

[200] Alaska Const. art. I, § 15; U.S. Const. art. I, § 10.

[201] AS 38.05.

burdens could be imposed on WIOs by DNR without respecting contractual protections, no one could be sure that the huge investments of money needed to explore for and delineate hydrocarbons in Alaska would not in effect be confiscated by the State by the simple device of terminating the unit agreement and re-leasing the acreage.

One of the important legislative limitations on DNR's authority, contained in former AS 38.05.180(m) when the PTUA was signed in 1977 and still in force as AS 38.05.180(p), is that DNR may modify the rate of prospecting, development, or production of the unitized leases only "with the consent of the holders of the leases involved."[202] As an exception to this general rule, and to provide a limited way in which DNR may unilaterally alter the rate of prospecting, development, or production, the Legislature authorized DNR to include in a unit agreement "a provision vesting [DNR] with authority to alter or modify from time to time the rate of prospecting and development and the

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[202] Current AS 38.05.180(p) provides in relevant part (emphasis added):

> The commissioner may, *with the consent of the holders of leases involved*, establish, change, or revoke drilling, producing, and royalty requirements of the leases and adopt regulations with reference to the leases, *with like consent on the part of the lessees*, in connection with the institution and operation of a cooperative or unit plan as the commissioner determines necessary or proper to secure the proper protection of the public interest.

This provision has been in effect, with small changes not relevant here, since statehood. *See* former AS 38.085.180(m); SLA 1959, ch. 169 § 3(7). *See also Exxon Corp. v. State*, 40 P.3d 786, 796 (Alaska 2001) (citing AS 38.05.180(p) in support of Exxon's contention that DNR has no statutory authority to alter a unit agreement without consent by the contracting parties).

quantity and rate of production under the [unit agreement]."[203] The inclusion of such a provision is not mandatory but optional (DNR "may" include such a provision),[204] and thus the statute contemplates that the terms of such provision would be negotiated between DNR and the WIOs, and would thereafter govern their relationship. As Judge Gleason correctly observed, Section 21 of the PTUA "corresponds to this statutory grant of authority."[205] It gives DNR the power to modify the rate of prospecting and development without lessee consent, but subject to agreed substantive and procedural requirements.

This statutory framework, which has been in place essentially without change for 50 years, is the complete answer to DNR's arguments that complying with Section 21 will somehow undermine or impair DNR's responsibility to manage state lands. Quite the contrary. Section 21 is the agreed embodiment in the PTUA of a longstanding legislative policy that expressly *restricts* DNR's ability to unilaterally impose prospecting, development, and production requirements on WIOs through its power over units. Section 21 is not contrary to legislative policy; it implements the policy of this State as pronounced by the Legislature.[206]

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[203] Former AS 38.05.180(n) (now AS 38.05.180(q)); former 11 AAC 83.315 was to the same effect.

[204] *See* former AS 38.05.180(n) (now AS 38.05.180(q)).

[205] Exc. 566 n.9.

[206] DNR's suggestion that Section 21 conflicts with AS 38.05.180(q) is precisely backward. Section 21 is the PTUA's implementation of AS 38.05.180(q). Section 21 is also consistent with 11 AAC 83.343(b), adopted in 1981, which provides that, if the Commissioner rejects a POD, he "will, in his discretion, propose modifications" to the

DNR argues strenuously that Section 21 is not a burden but a power that it can invoke. But as just explained, under the governing statutes, DNR has no power to unilaterally modify the rate of development or production under the PTUA *except* as contractually agreed by the parties under Section 21. The "burden" to which DNR refers is nothing more than the contractual limitation on the exercise of that power to which DNR consented when it agreed to Section 21. As the Superior Court held, "the provisions of Section 21 are reasonable contractual burdens that DNR knowingly assumed both in 1977 and again when the PTUA was amended in 1985."[207]

Further, there is simply no merit to DNR's argument that compliance with procedures and limitations it approved in Section 21 will somehow "subvert" its statutory authority to manage state-owned lands in the public interest. The substantive requirements of Section 21 are facially consistent with the public interest. The first requirement is that DNR's proposed rate of development and production promote the conservation objectives of the agreement. That not only serves the public interest as expressed in the agreement, but also as expressed in the constitution and Alaska Lands Act.[208]

The second substantive Section 21 requirement provides that the State's proposed rate of development and production shall not exceed what is required by "good and dili-

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unit operator. If DNR and the owners reach agreement, then the POD will be proposed and approved. Section 21 applies when DNR and the owners cannot agree on a POD and DNR instead seeks to unilaterally impose a change in the rate of prospecting, development, or production.

[207] Exc. 787.

[208] Alaska Const. art. VIII, §§ 1-2; AS 38.05.180.

gent oil and gas engineering and production practices." That too is facially consistent with the public interest. Indeed, requiring the WIOs to depart from good and diligent oil and gas engineering and production practices would plainly *disserve* the public interest.

The final substantive Section 21 requirement relevant here provides that DNR's proposed rate of development and production must not "prevent this agreement from adequately protecting all parties in interest hereunder, subject to applicable conservation laws and regulations." Applying this section to the current situation also well serves the public interest. As discussed earlier, the public's interest includes much more than just maximizing the State's revenue from natural resources located under State-owned lands. It includes promoting conservation, avoiding waste, and protecting private party investments, without which development could not occur.[209]

Nor is there any merit to DNR's complaint that requiring compliance with Section 21 would impose an undue procedural burden on the agency—especially when considered in light of the abrupt and enormous forfeiture that DNR would inflict on the WIOs. All DNR must do in a Section 21 hearing is explain the rate of development or production it seeks to require the WIOs to meet and be prepared to demonstrate that this rate promotes the conservation objectives of the agreement, does not exceed what is required by good and diligent oil and gas engineering and production practices, and does not prevent the PTUA from "serving its purpose of adequately protecting all parties in interest."

[209] See section V.A.2, *supra*.

DNR has suggested that the hearing will have to be adversarial.[210] That may be correct since DNR will presumably have to put forward evidence and witnesses, subject to cross-examination, to show that the rate it seeks to impose satisfies the requirements of Section 21. But in truth it is not yet clear what a Section 21 hearing will be like.[211] This litigation exists because DNR contends that the development of the Unit was not proceeding fast enough and that its judgment of what is "fast enough" is better than that of the WIOs. It is not unfair to require DNR to demonstrate its expertise and to prove that the rate of development it desires is consistent with conservation objectives, good and diligent oil and gas engineering and production practices, and the protection of all parties in interest.

Finally, DNR argues that it must not be required to afford the WIOs a Section 21 hearing because that would "shackle" it to recalcitrant lessees and result in years of litigation.[212] Section 21 is not a great imposition on DNR; it only requires a hearing. What has led to years of litigation in this case is that DNR has been so eager to take away the WIOs' leases that it has repeatedly violated the basics of due process, such as providing notice and a decisionmaking process that is fair in fact and appearance. If DNR had held a Section 21 hearing when it should have, this case would probably be over.

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[210] Exc. 803.

[211] The issue of what a Section 21 hearing will entail is before the superior court, which already requested and received briefs on this topic. R. 7083-92, 7058-71. The superior court has stayed making a decision pending resolution of this interlocutory appeal. R. 7056-57.

[212] DNR Brief at 32.

DNR itself correctly stated that the point of Section 21 is to protect a lessee's investment against unreasonable action by DNR.[213] If DNR had the ability to terminate a unit whenever an operator submits a POD for review, it is not DNR who would be "shackle[d]" to the lessees; it is the lessees who would be subjugated by DNR. Without the protections provided by Section 21 and the related statutory and regulatory provisions that together limit DNR's ability to mandate a change in the rate of development or production, likely no lessee would contract with the State and subject itself to the threat of forfeiting all the money it has invested in developing a unit whenever a POD expires.

B. DNR Again Violated The WIOs' State and Federal Due Process Rights.

Judge Gleason correctly applied *In re Robson* when she found that DNR violated the WIOs' due process rights by allowing the same attorneys and staff who advocated DNR's position in the initial appeal to advise the Commissioner in his decisionmaking process after remand. DNR's arguments that *Robson* does not apply are without merit. In deciding the termination issue, DNR, in its regulatory capacity, was adjudicating whether DNR, in its proprietary capacity, had a contractual right to that relief. The WIOs contested DNR's entitlement to terminate the PTU, creating direct adversity and requiring appropriate procedural protections that the agency made no attempt to provide.

Judge Gleason also correctly held that DNR's assignment of Ms. Thompson as a hearing officer violated the WIOs' due process rights under *Robson*. Ms. Thompson acted as the agency representative in the unquestionably adversarial first appeal to the Superior

[213] Exc. 800-01.

Court, and then acted in an adjudicatory capacity as the hearing officer and confidante to the decisionmaker in the remand proceeding.

1. The Superior Court Correctly Applied *In re Robson* In Analyzing Whether The Attorneys And Staff Who Represented DNR In The First Appeal Could Advise The Commissioner In The Remand Proceeding.

DNR asserts that Judge Gleason misapplied *Robson* because the attorneys and staff at issue did not serve in "dual roles" or exhibit "actual personal bias" against the lessees.[214] But the record shows conclusively DNR's attorneys and Ms. Thompson did play dual roles in violation of *Robson*, which requires no showing of actual bias. *Robson*'s *per se* bar on allowing advocates to participate in adjudicatory decisionmaking is fully applicable here.[215]

Robson arose from an Alaska Bar Association disciplinary action against a lawyer, Robson, who had been convicted of a felony.[216] The action was prosecuted by a single attorney acting as Bar Counsel. The Association's Executive Director, who was also Bar Counsel though she did not participate in prosecuting the case, attended the Disciplinary Board's deliberations to advise on procedural matters and take notes. Although the re-

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[214] DNR Brief at 10, 67-69, 71 n.242.

[215] DNR's violation of the WIOs' procedural due process rights tainted the adjudications DNR made in the remand proceedings, requiring reversal regardless of the substantive issues considered. The superior court incorrectly suggested that the *Robson* question could be reached only if the WIOs prevail on the Section 21 question. *Frost v. Spencer*, 218 P.3d 678 (Alaska 2009), cited by the superior court, does not stand for the proposition that an appellate court can avoid addressing a constitutional procedural issue by deciding an unrelated substantive issue.

[216] 575 P.2d 771 (Alaska 1978).

cord contained no suggestion that she participated in the deliberations or influenced the Board in any way, this Court ruled that her mere presence violated due process. Specifically, the Court held that both the appearance and the fact of impartiality required that neither prosecution nor defense counsel intrude into the functional equivalent of a jury deliberation.[217] The Court recognized that, while the combination of investigative, advocatory, and adjudicatory functions in one *agency* does not necessarily violate due process,

> [w]hen an administrative official has participated in the past in *any* advocacy capacity against the party in question, fundamental fairness is normally held to require that the former advocate take *no part* in rendering the decision. The purpose of this due process requirement is to prevent a person with probable partiality from influencing the other decisionmakers.[218]

The Court in 2008[219] and again just days ago[220] reaffirmed *Robson*'s principle that agency personnel who have been in an adversarial relation with a party may not later be involved with or even present during the agency's adjudicatory decisionmaking as to that party, at least in the same case. In *Amerada Hess*, the Court unequivocally reiterated that

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[217] *Id.* at 775. Although the Executive Director was not personally involved in prosecuting the case, the Court found it "reasonable to assume that assistant attorneys acting as Bar Counsel work under the general supervision and guidance of the Executive Director" and stated that "at the hearing stages, the Executive Director is aligned with the prosecution." *Id.* at 773.

[218] *Id.* at 774 (emphasis added); see also Exc. 789.

[219] *Amerada Hess Pipeline Corp. v. Regulatory, Comm'n of Alaska*, 176 P.3d 667, 677 (Alaska 2008) (per curiam).

[220] *In re Nash*, No. 6585, slip op. at 26 n.18 (Alaska, July 29, 2011) (quoting *Robson* for principle that "an impartial tribunal is basic to a guarantee of due process" and that "administrative hearings should seek not only fairness, but also the very appearance of complete fairness as well.") (internal punctuation omitted).

"all advocates, the prosecution and defense alike, are *per se* excluded from the jury room or its functional equivalent." [221]

Robson thus established that a *per se* due process violation occurs when an administrative official who acted in an advocacy role performs, assists in, or is present at the decisionmaking deliberations in the same case. This holding applies here. DNR candidly admitted that the "staff and legal personnel," including "the lawyers who defended the [first] appeal," later advised the Commissioner during the remand proceedings.[222] In the first appeal, DNR defended a unit termination decision that favored DNR in its proprietary capacity as lessor at Point Thomson. The WIOs contested DNR's entitlement to that relief, creating direct adversity between DNR and the WIOs. Under *Robson*, all DNR attorneys and staff who had a role in DNR's defense of the first termination decision were precluded from any adjudicatory role on remand.

DNR suggests that *Robson* does not apply because DNR's attorneys did not initially advocate for DNR and against the WIOs *in proceedings before DNR.*[223] According to DNR, advocating against a party on appeal is different from advocating against a party before the agency. But *Robson* makes no such distinction. Instead, it expressly prohibits an administrative official who has participated in *any* advocacy against a party from participating in a later adjudication against the party (at least in the same case).[224] This

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[221] *Amerada Hess*, 176 P.3d at 677.

[222] Exc. 1029 n.99. *See also* Exc. 798.

[223] DNR Brief at 69-70.

[224] 575 P.2d at 774.

makes perfect sense. If the problem *Robson* seeks to address is an adversarial attitude against a party tainting (or appearing to taint) a neutral administrative adjudication, it does not matter whether that attitude comes from advocating against the party before the agency or before a court on appeal.[225]

DNR also suggests that its attorneys in the first appeal did not really advocate against the WIOs because they "did not act in a prosecutorial manner" or "try to establish that Lessees had committed the acts or omissions that led the Commissioner to make his decision." The record belies this suggestion.[226] DNR's appeal brief was filled with statements attempting to establish the purported factual basis for the Commissioner's first termination decision. For example, DNR's attorneys characterized the case as being "about a calculated effort by Lessees to evade their obligations under the PTUA by warehousing the hydrocarbons in the PTU."[227] And the attorneys certainly advocated DNR's position when they sought to justify DNR's decision to reject the 22nd POD and terminate the PTUA with assertions like the following: "Lessees' record of broken development promises, refusal to invest in needed exploration wells, refusal to commit to produc-

[225] DNR likewise cites no authority for its related suggestion that attorneys who defend an agency's position on appeal should be exempt from *Robson* because they lack a "personal stake" in the outcome. DNR Brief at 71 n.242. Whether advocating in favor of an agency decision on appeal creates a "personal stake" is beside the point—nothing in *Robson* suggests that the Bar Association Executive Director's involvement violated due process because of a "personal stake" in the outcome of Robson's bar proceedings.

[226] DNR Brief at 71. DNR also argues that its attorneys on appeal "were attempting to establish that the Commissioner did not err in making his decision." *Id.* But they could not do that without arguing that the WIOs committed the acts or omissions that the Commissioner claimed to rely upon.

[227] Exc. 879.

tion of known commercial hydrocarbon deposits, and insistence on a gas blow down project, which risked the loss of millions of barrels of gas liquids and oil and indefinitely delayed PTU development, left the Director with no choice but to default the Unit."[228]

DNR has acknowledged that the first termination decision "was appealed in an adversarial setting to the superior court."[229] There is no question that DNR's attorneys and staff advocated against the WIOs in the first appeal and sought to have the court affirm DNR's right to terminate its own contract. Accordingly, their *ex parte* interactions with the Commissioner during the subsequent remand proceedings created both an appearance of partiality and a risk of improper influence. Applying *Robson* to the undisputed facts, Judge Gleason correctly found a *per se* violation because DNR's attorneys and staff defended the DNR Commissioner's decision as advocates in the superior court and then, after the decision was reversed, advised the Commissioner in his role as adjudicatory decisionmaker on remand.[230]

2. The Appointment Of Ms. Thompson As Hearing Officer Also Violated The WIOs' Due Process Rights.

DNR specifically challenges the superior court's conclusion that Nanette Thompson's participation in the first appeal in her capacity as unit manager for the PTU precluded her from "providing legal guidance or, as was the case in *Robson* simply being

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[228] Exc. 878.

[229] DNR Brief at 70.

[230] Exc. 773-74, 789-92.

present whenever the Commissioner deliberated on remand."[231] The agency argues that Ms. Thompson "was the client, not an advocate," and that her "mere presence at oral argument as a DNR employee standing in for the Commissioner does not support the conclusion that Ms. Thompson was an advocate on appeal."[232]

The record, however, shows that Ms. Thompson did much more than merely attend appellate arguments as a representative of DNR. Because Judge Gleason denied the WIOs' request for discovery in light of DNR's admission that, before the hearing on remand, staff as well as legal personnel served as advocates for DNR's position, the full extent of Ms. Thompson's internal advocacy role is not known.[233] But there is ample evidence that Ms. Thompson personally advocated for DNR prior to the remand hearing and was much more than a mere spectator at oral arguments.[234]

Ms. Thompson's position as PTU Unit Manager gave her hands-on responsibility for DNR's proprietary interest as lessor. Documents received through Public Records Act requests demonstrate that, in the months before the remand hearing, DNR and staff from other State agencies coordinated their responses to the WIOs' permit applications in an apparent effort to prevent the WIOs' from keeping the PTU leases. Ms. Thompson was

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[231] Exc. 791.

[232] DNR Brief at 73.

[233] Exc. 1029 n.99, 1096-97. *See also* Exc. 798.

[234] Should the Court determine that its disposition of this appeal turns on additional facts concerning Ms. Thompson's exact activities, then the WIOs should be permitted discovery on this issue.

central to these coordination efforts and was described as the "contact point for litigation"[235] about Point Thomson.

Before the remand hearing, Ms. Thompson personally took adversarial actions to support DNR's termination efforts. In April 2007, she discouraged another agency official from meeting with ExxonMobil to discuss permitting, asserting:

> I think EM has instructed their troops to try to create a record that the state is blocking EM's efforts to develop these leases so they can make a record in court. Posturing, rather than a sincere effort to move the project forward, is the more likely motivation. I copied the AGs working on this case in case they have a suggestion.[236]

Later, in December 2007, only a few weeks before she began acting as hearing officer in the remand hearing, DNR instructed staff to turn to Ms. Thompson for legal advice:

> [Director Kevin Banks] thinks [Exxon] [is] trying to establish a record of being a conscientious developer, trying to create and [sic] arguable case. He also asked me to contact Nan Thompson since she's the ADNR contact point for litigation. She may have advice regarding how State agencies can respond/behave rationally and consistently during this process.... In the past (~Aug), we were given direction not to spend any time with ExxonMobil's c-plan [i.e., contingency plan needed for drilling approval] until the lease situation was resolved. It appears nothing has changed.[237]

Emails sent after the Unit termination decision reinforce Ms. Thompson's ongoing role in advancing DNR's termination strategy by frustrating the WIOs in their attempts to

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[235] Exc. 1063.

[236] Exc. 1053.

[237] Exc. 1063.

engage in activity that would extend the PTU leases in the event of another reversal of the Unit termination after remand.[238]

After advocating against the WIOs in this manner and acting as DNR's representative in the first superior court appeal, Ms. Thompson played a substantial role as hearing officer in the second administrative termination proceeding. She made prehearing rulings, apparently on her own authority, allocating the burden of proof to the WIOs and limiting the hours for the evidentiary hearing.[239] She sat with Commissioner Irwin on the bench throughout the proceedings, asked numerous hostile questions of the WIOs, and helped to "frame the case" for the Commissioner.[240] Indeed, she often spoke as if she were one of the ultimate decisionmakers along with Commissioner Irwin. For example, it was Ms. Thompson—not the Commissioner—who "looked back through the record" and identified "two legal issues that we thought it would be helpful to have briefing on."[241] And it was Ms. Thompson who personally went through the Unit's POD history and asked the

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[238] In August 2008, Ms. Thompson circulated by e-mail a template (or form letter) for agencies to use to "suspend processing" of ExxonMobil's permit applications. Exc. 1065. The language was "reviewed by the attorneys defending DNR in the litigation filed by EM and others over termination of the PTU." *Id.* At Ms. Thompson's request, a DNR employee circulated the template to various agencies with instructions to show any changes to the language to Ms. Thompson before sending the letters. *Id.*

[239] T. 7-8, 56.

[240] *See* October 10, 2008 prehearing conference before G. Nanette Thompson in "Appeal By Respondents of the Notice Of The Director, Division Of Oil and Gas, Dated August 4, 2008, Entitled Lease Expiration Due To Elimination From Unit for Oil and Gas Leases ADL 28380 Et Al.," at 19:1-11 (Ms. Thompson stating that her role is to "try and frame that case" "similar to what it was in the Remand Remedy proceeding"), attached as exhibit 3 to LaPorte Affid.

[241] T. 1052.

WIOs at the end of the hearing to explain to her why certain actions by the WIOs did not constitute broken commitments: "I went back and read the plans of development, I also looked back at the expansion agreements. And I'm not going to read back all of what I found, but I have a couple of examples here that are ones that sound like commitments to me and I wanted to give you the opportunity to explain to me why they weren't. And tell me why this language...is different than what you're telling me now."[242] After reciting several examples (and providing commentary, such as "[b]ut you and I both know that that didn't happen"[243]), Ms. Thompson explained the purpose of the questioning: "The point of these questions is to give you the opportunity to appreciate why we're having a difficult time believing you really mean it this time."[244] The record thus confirms that Ms. Thompson participated extensively in the adjudicatory process on remand. The record thus confirms that Ms. Thompson participated extensively in the adjudicatory process on remand and was far more active and involved than the *Robson* Bar Association Executive Director, who merely attended deliberations and made notes.

As discussed above, both the first appeal and the remand hearing were inherently adversarial because termination of the PTUA was the ultimate issue, and DNR in its proprietary capacity was a party to that contract. Even if Ms. Thompson had acted only as PTU Manager before the remand hearing, her responsibilities and her own actions were directly adverse to the WIOs. Judge Gleason correctly concluded that under *Robson*, Ms.

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[242] T. 1028.

[243] T. 1029-30.

[244] T. 1032.

Thompson was precluded from any role in DNR's adjudicatory process, including acting as the hearing officer, advising the Commissioner in his deliberations, or even being present during the deliberative process.[245]

3. DNR's Call For A Balancing Test Is Not Appropriate In Light Of Robson's Determination That Improper Mixing Of An Agency's Advocatory And Adjudicatory Functions Is A *Per Se* Due Process Violation.

DNR attempts to circumvent this Court's decision in *Robson* by urging a separate balancing analysis. But *Robson* itself already balanced the relevant interests and determined the contours of due process in the circumstance where an agency commingles its adversarial and adjudicatory roles. The Court held that in such circumstances, there is a *per se* due process violation. The only appropriate case-by-case inquiry is whether any administrative official who has acted in an earlier advocacy role performs, assists, or is present at adjudicatory deliberations in the same case so that the *per se* rule is triggered.[246] The situation is particularly egregious here since the WIOs pointed out the due process concerns before the remand hearing commenced, and asked for the appointment

[245] Alaska's code of conduct for administrative hearing officers, applicable to Administrative Law Judges employed by the Office of Administrative hearings and "hearing officers of each other agency," *see* AS 44.64.050(b), reinforces the impropriety of appointing Ms. Thompson to act as a hearing officer in the termination proceeding here. The code expressly precludes service by "a hearing officer ...[who] previously represented or provided legal advice to a party on a specific subject before the hearing officer...." 2 AAC 64.040(a)(2).

[246] *See* 575 P.2d at 774 ("When an administrative official has participated in the past in any advocacy capacity against a party in question, fundamental fairness is normally held to require that the former advocate take no part in rendering the decision."); *P.M. v. State, Dept. of Health and Soc. Servs., Div. of Family and Youth Servs.*, 42 P.3d 1127, 1133 (Alaska 2002) ("Fundamental fairness is the main requirement of the due process clause.").

of an independent hearing officer, adversarial procedures, and a clear separation of DNR's advocates from its adjudicators.[247] DNR refused all such requests, leading to an appearance of partiality much stronger than in *Robson*.[248]

4. The Superior Court's Decision Was Necessary Under *Robson* And Is Neither Impractical Nor Unduly Burdensome to DNR.

DNR complains that its remand proceedings will become unduly burdensome if agency representatives like Ms. Thompson and attorneys who appear as counsel for DNR on appeals from agency decisions cannot participate in "non-adversarial" remand proceedings.[249] This argument simply ignores the inherently adversarial nature of the proceedings in this case once termination of DNR's own contract became an issue. As al-

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[247] Exc. 583-87, 592-93.

[248] Exc. 589-91. *Robson* is not an outlier. The federal Administrative Procedure Act expressly prohibits communications of the kind that occurred on remand between DNR attorneys and staff who had been involved in the first appeal and Commissioner Irwin. *See* 5 U.S.C. § 554(d); *Wong Yang Sung v. McGrath*, 339 U.S. 33, 41 (1950) (reversing an FTC decision refusing to disqualify the administrative law judge who had previously served as an attorney-advisor to the investigative officer in the matter), *superseded by statute on other grounds as stated in Ardestani v. INS*, 502 U.S. 129 (1991); *Grolier, Inc. v. Federal Trade Comm'n*, 615 F.2d 1215, 1220 (9th Cir. 1980) (following *McGrath* and holding that the prohibition extended to "all persons who had, in that or a factually related case, been involved with *ex parte* information, or who had developed, by prior involvement with the case, a 'will to win.'").

Other courts have found due process violations in analogous circumstances. *See Davenport Pastures, LP v. Morris Cty. Bd. of Cty. Comm'rs*, 238 P. 3d 731, 732-34 (Kan. 2010) (finding due process violation where county counselor who had advocated for the Board before the state district court and court of appeals later served as legal advisor on remand); *Botsko v. Davenport Civil Rights Comm'n*, 774 N.W.2d 841, 852-53 (Iowa 2009) (finding due process violation where executive director who had previously assisted petitioner "as a second-chair advocate" in court proceedings was present during the Commission's deliberations, even if his role was limited to answering questions).

[249] *See* DNR Brief at 74-75.

ready discussed, in the first appeal, DNR advocated for affirmance of its termination decision, placing it in a position directly adverse to the WIOs. On remand, DNR again took a position directly adverse to the WIOs when it notified them that termination was still at issue. Under *Robson*, due process required that DNR separate those responsible for advocacy from those who would be adjudicating whether termination was proper.

DNR's claim of hardship is likewise unfounded. It would have been simple enough for DNR to separate its advocatory and adjudicatory functions at the outset of an inherently adversarial proceeding like the termination proceeding here. The result would have been an initial contested hearing at the agency level. That would have allow the attorneys and staff advocating DNR's position on termination before the agency or on appeal to continue to act as advocates for DNR in all later proceedings, including any proceedings on remand.[250]

DNR also claims that complying with *Robson* will interfere with its legal mandate to manage oil and gas resources and the attorney-client relationship with its counsel. Both claims are meritless. Years ago, DNR determined that it was in the public interest to enter into the PTUA with the WIOs. Like any other contracting party, DNR has the right to

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[250] DNR claims that it "employed standard administrative hearing procedures, which this Court has previously reviewed and approved." DNR Brief at 76 n.256 (citing *White v. State, Dep't of Natural Res.*, 14 P.3d 956, 960 (Alaska 2000), and *Danco Exploration, Inc. v. State, Dep't of Natural Res.*, 924 P.2d 432, 434 (Alaska 1996)). The cited cases stand only for the proposition that institutional bias created by DNR's proprietary interest as lessor does not *automatically* preclude DNR from adjudicating a dispute over its own contract. But the fact that DNR has authority to adjudicate disputes involving its own contracts says nothing about how such administrative adjudications must be conducted consistent with due process. On the question of whether DNR may permissibly commingle advocatory and adjudicatory functions, *Robson* controls.

claim termination of the contract if warranted. But if DNR is to adjudicate whether to terminate its own contract, it cannot invoke the public interest to avoid complying with due process. Nor is there any basis for DNR's claim that complying with *Robson*'s requirement to assign different attorneys and staff to fill advocatory and adjudicatory roles will impede DNR's ability to perform its regulatory functions. And since due process precludes those performing advocatory roles from also advising DNR as the adjudicator, there is no unwarranted interference with the attorney-client relationship.

VI. CONCLUSION

The Court should affirm the superior court on the issues on which review was granted and should find that the WIOs are entitled to a Section 21 hearing and that DNR violated the WIOs' due process rights under *Robson*. The Court should remand to the superior court for further proceedings consistent with those rulings.

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PATTON BOGGS LLP

Douglas J. Serdahely
Alaska Bar No. 7210072
Barat M. LaPorte
Alaska Bar No. 9511064
601 West 5th Avenue, Suite 700
Anchorage, Alaska 99501
Phone: (907) 263-6310
Fax: (907) 263-6345

Of Counsel:

M. Randall Oppenheimer
Charles C. Lifland
O'MELVENY & MYERS LLP
400 South Hope Street
Los Angeles, California 90071
Phone: (213) 430-6000
Fax: (213) 430-6407

William B. Rozell
Alaska Bar No. 7210067
P.O. Box 20730
Juneau, Alaska 99802
Phone: (907) 586-0142
Fax: (907) 463-5647

Attorneys for Respondent Exxon Mobil Corporation

I certify that the typeface used in this document is 13 point Times New Roman.

George R. Lyle
Alaska Bar No. 8411126
GUESS & RUDD PC
510 L Street, Suite 700
Anchorage, Alaska 99501

Susan Orlansky
Alaska Bar No. 8106042
FELDMAN ORLANSKY & SANDERS
500 L Street, Suite 400
Anchorage, Alaska 99501

Bradford G. Keithley
Alaska Bar No. 1010054
PERKINS COIE LLP
1029 West 3rd Avenue, Suite 300
Anchorage, Alaska 99501

Attorneys for Respondent BP Exploration (Alaska) Inc.

Of Counsel:

P. Jefferson Ballew
G. Luke Ashley
Thompson & Knight LLP
1722 Routh Street, Suite 1500
Dallas, Texas 75201-2533

Stephen M. Ellis
Alaska Bar No. 7510065
DELANEY WILES, INC.
1007 West 3rd Avenue, Suite 400
Anchorage, Alaska 99501

Attorneys for Respondent Chevron U.S.A. Inc.

Spencer C. Sneed
Alaska Bar No. 7811140
DORSEY & WHITNEY LLP
1031 West 4th Avenue, Suite 600
Anchorage, Alaska 99501

Attorneys for Respondent ConocoPhillips Alaska, Inc.