

Honourable Ed Stelmach
Premier of Alberta
Office of the Premier
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Edmonton, AB T5K 2B6

Dear Mr. Premier

After 14 years as CEO of Talisman Energy, in which time we have invested heavily in Alberta, I feel I have a duty to write to you about the Report of the Alberta Royalty Review Panel. The debate following the publication of the recommendations of the panel seems to overlook a number of important points.

World oil prices may be at \$80 per barrel (as Frank Atkins, Hugh MacDonald and others point out) but we need to distinguish between oil and natural gas. The vast majority of conventional drilling in Alberta is for natural gas and the price of domestic gas is around \$5 per gigajoule, or \$30 dollars per barrel of oil equivalent (boe). The government takes its share from revenues, not from profits, which effectively lowers Alberta natural gas prices by an additional 20%.

In this mature basin, new gas is being found in smaller quantities or in deep, technically difficult plays. Industry finding and development costs are running around \$20/boe and operating costs are near \$10/boe. Producing natural gas at a cost of \$30 in a \$30 price environment doesn't leave much pie to share. This may seem tough to fathom in a world where the industry is reporting record profits, however, these profits come largely from the oil side or from natural gas discoveries made when costs were much lower. The decisions being made now affect the investments required to make future natural gas discoveries. You can't get royalties from wells that are not drilled.

Marginal economics is the primary reason why rig utilization rates are as low as they are and recent estimates suggest that 12,000 jobs have been lost so far in the service industry. Talisman decided to cut \$500 million in spending next year, even before the panel report, because as much as a third of our drilling program is marginal at current gas prices.

This leads to the next point, which is that government take can only be seen in the light of costs and prospectivity. In many parts of the world, government take is a higher percentage than the old Alberta terms, or the new terms, if it comes to that. It all depends on how big the available pie is.

Industry needs to make a reasonable return on capital employed, to reward investment for the risks incurred, regardless of the relative share. In many areas of the world, the size of the potential pie is big and government take is high. But in Alberta, the discoveries are getting smaller, while prices (low) and many of the costs (high) are set elsewhere. Typically, as basins mature, governments reduce the royalty burden to encourage activity and maintain revenue.

Most, if not all, of the money the industry generates in Alberta finds its way back to the people of Alberta by way of capital expenditures, lease payments, taxes, salaries or operating costs. Talisman expects to pay the Alberta Crown approximately \$400 million in royalties this year, while investing approximately \$1.8 billion in the province and paying an additional \$500 million in operating, general and administrative costs. If these proposals are implemented, the Company would likely cut around \$500 million from our capital program in Alberta, beyond the \$500 million decrease as a result of low natural gas prices. To deter investment in the name of increasing government take hurts Albertans, primarily in small towns and rural areas across the province.

The report provides its version of economics for high productivity wells, assuming costs of \$4.6 million per well to produce 6 1/2 million cubic feet per day. These numbers do not reflect reality. As the leading deep gas driller in Alberta, we see costs of \$10-14 million for a successful well of this magnitude. On average seven of 10 wells are successful (which is an astounding feat, due largely to the technical teams we have established) and given that successes have to pay for failures, the cost jumps to \$17 million per well. Economics for these wells are vastly different from those presented. I sincerely hope bad data won't lead to poor policy decisions.

At current gas prices, I believe it will be difficult for anyone to grow their natural gas production in Alberta and if you implement these proposals we will see a significant loss of investment, jobs, taxes and the loss of world class technical expertise. If the natural gas price were to be \$10 to 12 per gigajoule, there would be something to talk about. At current prices, there are only degrees of pain.

Mr. Premier, I urge you to be cautious about implementing the major changes that are contemplated by the Royalty Review paper.

Yours sincerely,

Jim Buckee
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Calgary, Alberta