

ExxonMobil, Rosneft Pair up for Fracking

By [The Moscow Times](#)

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Putin wants ExxonMobil to help drill oil fields in the Bazhenov shale formation in west Siberia. Above, an Exxon drill rig that is part of the Sakhalin-1 project off the coast of Sakhalin Island. **Sergei Porter**

President Vladimir Putin is counting on ExxonMobil to help drill oil fields that may hold almost half the proven reserves of the United States.

Having slipped behind Saudi Arabia last year as the biggest crude producer, Russia is looking to use Exxon's technology in a venture with Rosneft to wring "tight oil" from the Bazhenov shale formation in west Siberia.

They plan pilot wells to locate deposits that Rosneft said may hold 13.2 billion barrels of oil, a prospect needed for Russia to keep supplying 16 percent of global exports for another decade.

Putin's hopes for Bazhenov to someday match the explosive growth of North Dakota's Bakken shale discovery hinge on his timely delivery of promised tax breaks that drillers say are needed to make projects profitable.

Tax cuts, however, can reduce the state's petroleum revenue, which last year accounted for about half its \$350 billion in income.

"If the government is serious about promoting tight oil production, it is within their grasp," said Ronald Paul Smith, a Moscow-based oil and gas analyst at Citigroup.

Smith said extraction taxes, which were around \$24 a barrel last quarter, may need to be almost eliminated to spur output of what's called unconventional oil.

Because the Bazhenov geology is proving more difficult than that of much of the similar areas in the United States, Rosneft is pursuing deals with Irving, Texas-based Exxon to use hydraulic fracturing, or fracking.

The companies will target existing Siberian wells, some of which are 50 years old, that no longer produce much conventional oil.

Fracking typically uses horizontal drilling while injecting millions of gallons of water laced with chemicals and sand to smash underground shale rock to unlock petroleum. It has driven the U.S. oil boom in the last decade, leapfrogging the nation ahead of Russia as the world's largest natural-gas producer.

Bazhenov's geology is similar to the Bakken shale's. Crude oil production at the North Dakota site has more than doubled in two years.

As part of the alliance with Exxon, Rosneft said in April that it had acquired a 30 percent stake in a Texas tight-oil project to gain experience with the technology.

"The in-place potential [for Bazhenov] is enormous, billions of barrels," Exxon chief executive Rex Tillerson said. "The real issue is can we develop it in a cost-effective way, same as the issue we have with tight oil and unconventional resources in North America."

Exxon will be able to book reserves in a mature oil province without taking on the exploratory or environmental risks it faces in its offshore projects with Rosneft, which will require an initial \$3.2 billion investment to explore in the Arctic Kara Sea and the Black Sea.

While Exxon and European rivals such as Statoil have generated more media interest in their projects to develop virgin deposits in the Arctic by the 2020s, fracking Soviet-era Siberian wells may yield crude sooner.

Putin has pledged that Russian output, which in May was 10.34 million barrels a day, will remain stable until at least 2020. But he conceded that tax revenue will fall as Russia gives incentives to stimulate production.

The state has approached tax changes with caution. Oil and gas provided half of Russia's income in 2011, and the Finance Ministry projects that Urals crude needs to average \$117 a barrel to balance the budget this year.

Rosneft and Exxon will have competition. Nonstate Russian oil companies, including LUKoil and Surgutneftegas, also have resources in the billions of barrels in the Bazhenov formation.

“LUKoil is already using horizontal wells and multistage fracking to support its west Siberian production and therefore may be the earliest, clearest beneficiary” of the tax breaks, Smith said.

LUKoil subsidiary Ritek produces about 2,000 barrels a day from the Bazhenov formation in “experimental” projects, spokesman Vladimir Semakov said.

Another competitor, Gazprom Neft, along with Royal Dutch Shell, plans to drill an extended-reach horizontal well with multistage hydrofractures next year to tap tight oil at the Siberian Salym Petroleum Development venture, Gazprom Neft deputy chief executive Vadim Yakovlev said.

Unconventional resources will eventually contribute as much as 40 percent of Russia’s total oil output, according to comments in April by Igor Sechin, who left the deputy prime minister job in May to become Rosneft CEO.

“This will be a giant leap forward of a scale comparable to development of oil production in western Siberia in the 1960s and 1970s,” Sechin said.

Russia accounts for almost 16 percent of the world’s oil exports, shipping 5.14 million barrels a day in December, according to the Joint Oil Data Initiative’s website.

Putin in early May called for discounts on the extraction tax for unconventional oil to increase Russian output of hard-to-reach crude. The incentives center on a reduced crude-extraction tax of 50 to 100 percent, depending on the project’s difficulty.

He ordered the government to draft a proposal by Oct. 1.

The extraction tax for oil is based on the price of Urals crude, Russia’s benchmark export blend. It averaged 5,284 rubles a ton, or \$23.77 a barrel, in the first quarter, according to Rosneft.

Rosneft also plans an unconventional oil project with Norway’s Statoil, which expanded into the Bakken last year through the \$4.5 billion acquisition of Brigham Exploration.

Statoil and Rosneft are studying tight-oil prospects and high-viscosity projects, which will also qualify for tax breaks.

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