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Incentives for Exploiting Hard to Reach Hydrocarbons Insufficient, Industry Executives Say

By Alexander Panin

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Tax breaks for oil and gas companies are not enough to make hard-to-recover hydrocarbon reserves economically viable, executives said Thursday at a meeting organized by Rosgeologiya, a state-owned exploration company.

The comments come in the wake of government measures, including setting tax exemptions, to create favorable conditions for companies developing hard-to recover oil and gas reserves.

Hard-to-reach hydrocarbons can be found at sites with difficult geology, which require additional investment, materials and labor resources to develop, or call for unconventional equipment, technology and chemicals. Examples include traditional oil fields more than 80 percent depleted, and shale oil and gas reservoirs hidden within the Bazhenov shale formation in western Siberia.

"About 60 percent of existing oil reserves in Russia are of this category," Natural Resources and Ecology Minister Sergei Donskoi said at the meeting. Overall, Donskoi added, the country is the world leader in the potential amount of hard-to-reach hydrocarbons, which today are inaccessible for economic reasons.

One of the reasons for this is a lack of technology that could lower the cost of developing difficult to reach resources.

"We have tested many different technologies [for extracting hard-to-recover hydrocarbons] but so far have not found one that would be economically feasible," said Alexei Vashkevich, the head of geological exploration at Gazprom Neft.

To make hard-to-recover sites more attractive for development, the government adopted a new law last year that introduced a differentiated tax break system depending on the difficulty of hydrocarbon extraction.

The initial goal set by the government was to fill the state coffers with additional 60 billion rubles ($1.7 billion) per year in taxes paid from extracting oil from hard-to-reach sites, but the measure has not had the desired effect so far.

"We could ask for more benefits ... but even a zero tax rate would not make it possible to reach profitable production levels at this point," Vashkevich said.

Ilya Mandrik, LUKoil's vice president in charge of exploration, agreed.

"Our company is not ready to invest in oil production at hard-to-recover sites but we are willing to explore their potential, looking to increase the resource base of the company in the next 10 to 20 years," Mandrik said.

Efforts to start a full-scale oil and gas exploration of hard-to-recover reserves are premature, said Alexei Kontorovich, the head of the scientific council at Russian Academy of Sciences.

"According to our estimates, oil production in Russia will peak between 2020 and 2022. This output level would last for five to seven years before production is likely to decline," Kontorovich said, adding that the efforts to boost development of hard-to-recover sites would be more effective at that time.

Traditional natural gas exploration has an even more distant demise, as Russia will not run out of conventional gas reserves until the 2070s or 2080s, Kontorovich said.

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