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Offshore Presents Unique Challenges

By T. Paul Bulmahn

Editor's Note: ATP Oil & Gas Corp. is one of the fastest growing U.S.-based independents active offshore. With operations in the Gulf of Mexico Shelf and deep water, as well as the U.K. sector of the North Sea, the company's revenues have practically doubled every year since 1994, achieving a compounded annual growth rate of 142 percent. ATP was first in *Inc. 500's* fastest-growing energy company rankings in 2000, and was a finalist in the 2000 *Financial Times'* Best Oil & Gas Company Award (with Shell, BG Group, and Tyumen Oil Co.). ATP has also stayed ahead of the technology curve, pioneering offshore horizontal drilling at South Timbalier 30 in 1995, receiving the *Inc./Cisco* 2000 Growing with Technology Award for innovative utilization of internal operation techniques, and ranking among the most active operators for subsea completions in the last 10 years. With these credentials in mind, we asked ATP's founder and chief executive, T. Paul Bulmahn, to share his insights on challenges and opportunities for independents offshore.

HOUSTON—The small boy was given a chance to catch his dinner. The large glass tank was filled with fish and the restaurant host handed the boy a net. The youngster was immediately aware of a high activity level everywhere inside the tank when he swung his net, and frequently looked up to find he was the center of attention of bystanders around the tank. With swipes this way and that, he netted only frustration. He lacked the discipline to focus on one fish to the exclusion of other possibilities and distractions.

To those able to overcome challenges, the offshore oil and gas industry has a high activity level these days, with an abundance of possibilities and opportunities for rewards. Challenges do abound, however. They include the magnitude of capital required to construct the offshore "net," finding the people with sufficient talent to comprehend how to swing that net, understanding the regulatory arena of operations, and remaining focused to avoid

distractions in order to, hopefully, secure "dinner."

Magnitude Of Capital

One of the more significant hurdles in offshore oil and gas operations is the sheer magnitude of capital required for any operation. Beyond representing a most effective barrier to entry for becoming an offshore entity, the aggregation of capital to perform even a small task in an offshore development represents a sizeable initial step. Formed in August 1991 with the objective of acquiring, developing and operating proved offshore reserves, ATP Oil & Gas Corp. turns 10 years old this year, and I do not remember ever seeing a single offshore project go from A to Z without at least one expensive, unanticipated hitch during these years.

A great stumbling block inherent in every project is the enormity of the dollars required to address a hitch or flaw—a failure of some kind—whether it is in scheduling, equipment or facilities, underperformance, or the like. It seems that the costs of simple necessities, such as well control insurance, are ever-increasing, along with all of the customarily anticipated expenditures of rig day rates and service industry spread costs.

Although the industry is capital intensive—particularly the offshore segment—and there are a number of companies led by sound management that enjoy successful track records, the investment community continues to prefer what it calls "high tech" over energy. The preference continues despite the implosion of dozens of Internet dot-coms (which held Wall Street's attention this time a year ago) and the fact that many oil and gas companies have posted strong gains over the last several months, while stock prices in the high-tech sector have generally suffered from slowing economic growth.

The truth is, there has never been a better time to be an offshore operator. Coming off a record-setting year in 2000, ATP achieved new performance thresholds for reserves, production, revenues and cash flows in the first quarter of this year from its Gulf of Mexico and

North Sea asset bases. Many other offshore companies are also posting record results, and are aggressively moving forward in an attempt to maintain the strong showings. But capital is the lifeblood of the upstream business, and companies cannot grow without access to the prerequisite financing. This can be a particular challenge for smaller private companies. ATP accomplished a major step in its evolution in February when it conducted an initial public stock offering, generating net proceeds of \$78.3 million. The stock offering positions ATP for continued growth in the future.

Technology Incubator

What's more, the investment community's prevailing attitude toward energy and its stubborn devotion to high-tech not only fails to acknowledge the upstream sector's performance in the last couple years, but ignores the fact that the oil and gas industry is a great technology incubator. The technologies by which we identify and add reserves—from three-dimensional to multicomponent (4-C) seismic, and from horizontal to multilateral drilling—have been refined, and the technologies enabling operators to attach and produce reservoirs more efficiently—like subsea development techniques—have proliferated.

Recognizing the enabling capabilities of subsea technology, ATP has quickly become an industry leader in utilizing subsea solutions, with 13 subsea wells now producing or under development in the Gulf of Mexico and Southern Gas Basin of the U.K. sector of the North Sea. The company, serving as the operator, completed its first subsea development in 1997 in a joint venture with Shell at Ship Shoal 321. Only two years later, ATP accomplished the technological achievement of utilizing a direct hydraulic umbilical for an 11.75-mile flow line for a Garden Banks project. With the game-changing aspects of subsea completions on small and marginal field economics, and with ATP now entering the deepwater Gulf of Mexico, subsea technology will continue to be an important enabler for the company.

Some of the emerging technologies that I believe have been underutilized to date include coiled tubing drilling and steerable drilling assemblies that result in more precise directional control for difficult wells. There are also a number of new logging technologies, such as "deep look" applications that can see farther away from the well bore, new logging-while-drilling tools, and nuclear magnetic resonance (NMR) logging tools. Other important advancements are sand control technologies used with solid expandables to achieve zonal isolation, and intelligent fiber optic well surveillance devices. Technology, as the most effective offshore companies utilize it, continues to swiftly move forward to bring forth greater productivity.

Intangible Assets

A specter looming before the offshore industry is the potential disappearance of intangible assets—a shortage of qualified offshore personnel. As the industry has lurched from booms to busts, price spikes and peaks to valleys and bankruptcies, we have almost been our own worst enemies in every season. We have gone through periods where companies have been forced to lay off

some of their most experienced hands because of their high salaries (a result of their longevity and well-honed skill sets developed through years on the job), then suffered the expensive mistakes of new employee learning curves.

The industry has also allowed some universities to dismantle their petroleum engineering programs, then it laments the dearth of educated talent exiting the classroom to enter the industry. For its part, ATP is an active supporter of the Offshore Energy Center at Galveston, Tx., and the educational opportunities represented by the Ocean Star, an offshore drilling rig turned into a hands-on learning tool. The company has also become involved in advisory and mentoring relationships at various universities, and encourages every offshore company to help educate, in whatever fashion it can, the next generation of offshore talent to help "net" its goals.

The governmental regulatory arena is also an emerging stumbling block to offshore development. As the time periods for securing permits and necessary approvals has lengthened, the most immediate impact is lowered rates of return on invested capital. The bureaucracy has also experienced its manpower shortages, and the industry must

encourage governmental agencies to maintain proper staff levels.

Traditionally, the U.S. Minerals Management Service has been one of the governmental agencies most understanding of the industry's needs and concerns. I trust that, under a new administration in which the two top executives have had exposure to the problems and complexities of the industry, we will not see the rigid application of impractical regulations. During the previous administration, and particularly as its politicians left office, millions of acres of land were removed from potential exploration in the Pacific Coast off California, the Atlantic Coast, the Arctic National Wildlife Refuge, and offshore Florida.

Yet, the industry has been a responsible and a responsible one. Research shows that most oil spills have occurred not from offshore exploration and development, but from maritime tankers running aground and spilling their cargoes. The oil and gas industry has become increasingly prudent, safe and environmentally responsible. During this window of potential administration understanding, the industry needs to be particularly mindful of ways to environmentally and safely speed and minimize the implementation of bureaucracy on offshore projects.

Price volatility is yet another potential stumbling block. First, the industry was told the financial community deserted upstream energy because oil and gas commodity prices could not generate sufficient returns. Now the industry is hearing that the financial community is tentative about energy because the prices operators are receiving for their production are not sustainable at today's strong levels, so investors are awaiting price declines. Until the exploration and production sector can convince investors that it can generate a solid return on invested dollars at varying price decks, price volatility will remain a stumbling block.

Core Competency Focus

There are many other hurdles, dilemmas and stumbling blocks for the offshore industry, but there is one significant challenge I feel compelled to discuss: corporate focus. An American Indian proverb says, "If you chase two rabbits, both will escape." Many upstream



Focusing on core corporate competencies is one key to success offshore. By dedicating itself to the proven, undeveloped niche in the Gulf of Mexico and North Sea, and honing expertise in such areas as using subsea technology to develop marginal fields, ATP Oil & Gas Corp. has emerged as one of the fastest-growing independents active offshore.

companies try to chase too many rabbits. The most successful companies, not surprisingly, are typically those that maintain a strict adherence to their fundamental business competencies.

ATP, for example, focuses on the proven, undeveloped niche in its development and production operations in the Gulf of Mexico and North Sea. We understand that the company exists to provide a solution. ATP does not engage in exploration activities, but simply addresses developmental projects with proven reserves that fall off the table of the budgets of more exploration-minded companies. We are delighted to offer to E&P companies a way to monetize and develop such assets, enabling them to remain focused on what they do best: exploration.

Obviously, I believe a core competency focus is compelling, because as a focused "D&P" company, ATP could not even exist if it did not afford a method for exploration companies to monetize non-strategic proven, undeveloped properties that failed to meet the thresholds of those companies' developmental budgets.

An accounting firm recently described the oil and gas industry as one

characterized by a "continuing cascade of assets transferring from one company to another." The obvious truth of that statement underscores the success that could come to the entity that could capture a component of that cascade with core competency focus. ATP is living proof of an ability to focus narrowly on a cascade component, and it has become astute in developing properties, just as exploration-focused companies are similarly astute in their core competency area of finding elusive reservoirs.

Success will come to the offshore entities that position their companies to overcome the obstacles the industry will continue to encounter, and that:

- Utilize technology most effectively;
- Recruit and retain the most talented individuals;
- Proactively address the tenants of the regulatory arena; and
- Focus on what makes them unique.

The results of that success will assure available funding to meet the capital needs of the offshore company. Consequently, successful companies will not only "catch their dinner," but be rewarded in the process as well. □



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