

The Pad Site Sharing Agreement (Draft 2)

Accounting Implications & Overview of PASC AG-19 Accounting for Shared Pad Site Costs (Draft 2)

Petroleum Accountants Society
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Producing Well Pad



Topics

- Accounting under the PSSA – the good news and not-so-good news
- Illustrations - accounting for pad site operations
 - Single JOA, common ownership scenario
 - Single JOA, common ownership with penalty scenario
 - Multiple JOAs, blended ownerships scenario
- Overview of PASC AG-19 “Accounting for Shared Pad Sites” (Draft 2)
- Summary of industry feedback

Accounting Implications of the PSSA

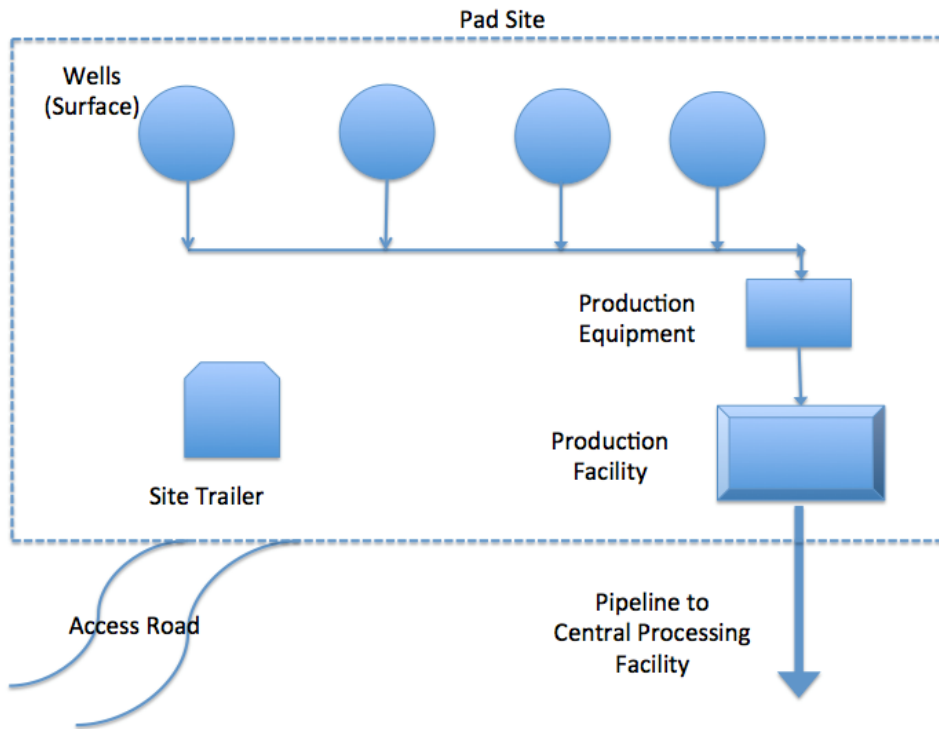
- The good news for Accountants and Auditors:
 - The PSSA provides a lot of guidance on how to manage the life cycle of a shared pad site
 - The PSSA works really well if everything is held in common ownership
 - Same parties with the same interests or a blending of interests where appropriate
 - It recommends keeping it simple and straightforward

Accounting Implications of the PSSA

- The not-so-good news for Accountants and Auditors:
 - The PSSA facilitates customization adding cost/administration
 - Asset definition
 - Structure of the Joint Account
 - Potential variations in cost sharing methodologies from simple well count approach
 - Potential variations in ownership structures (well ownership linked, throughput, invested capital)
 - Possibility of a separate facility CO&O agreement that is subordinate to the PSSA in some cases
 - Changes in ownership from elections under the Mineral Land contract
 - Addition, replacement or removal of shared equipment
 - Possibilities of costs and fees for non-Pad or non-Pad Owner usage
 - Abandonment/reclamation cost sharing options

Keep it simple
Stay with the base model
It works !

Single Pad Site
 Common Ownership
 JOA & Operating Procedure
 Accounting Procedure



AFE & Cost Centre Set-Up

- Site (Surface)
- Access Road
- Individual Wells
- Production Equipment
- Site Trailer
- Production Facility
- Pipeline to Central Processing Facility

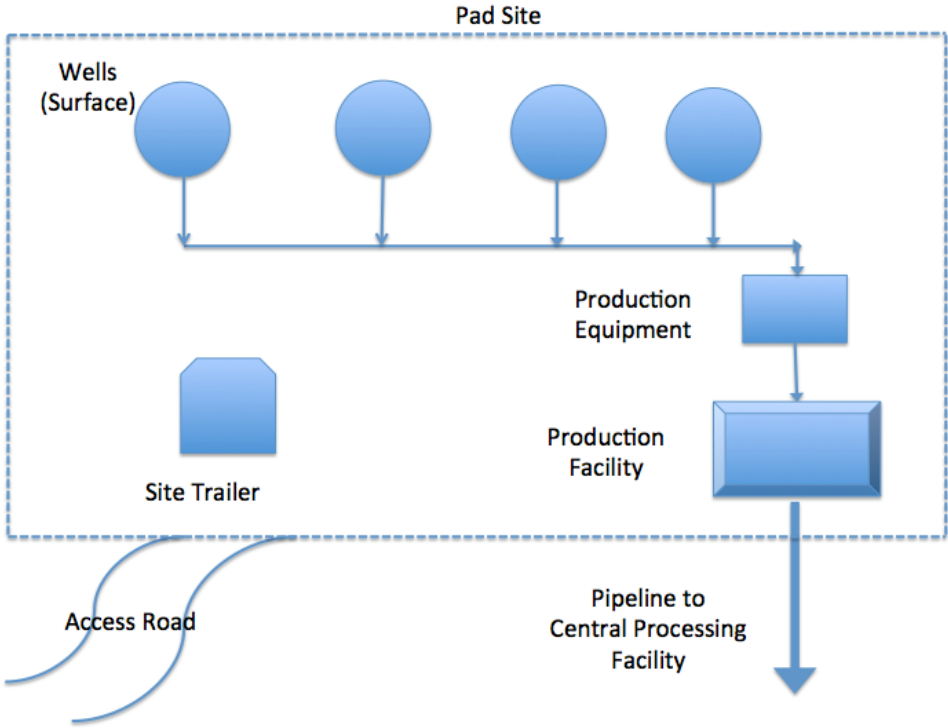
Ownership (DOI)

- Common Ownership under the JOA

Accounting

- JOA Accounting Procedure
- Capital & Operating
- Direct Charges & Overhead
- Well specific costs for drilling, completion, equipping and ongoing operations
- Equitable allocation of common costs
 - If drilled, completed & tied in as a program
 - Mud costs
 - Rig Mobilization/Demobilization Costs
 - Operating Costs
 - Labour
 - Electricity
 - Chemicals
 - Others

Single Pad Site
Common Parties
Penalty Well
JOA & Operating Procedure
Accounting Procedure



AFE & Cost Centre Set-Up

- Site (Surface)
- Access Road
- Individual Wells
- Production Equipment
- Site Trailer
- Production Facility
- Pipeline to Central Processing Facility

Ownership (DOI)

- Wells at actual DOI
- **Others at blended ownership until payout depending on capital sharing**

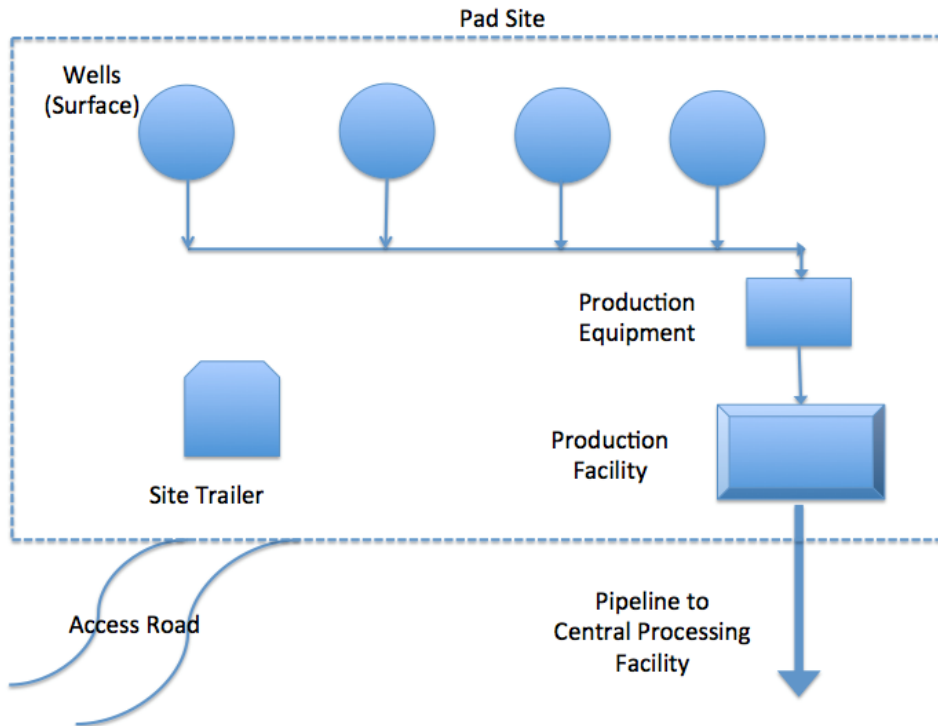
Accounting

- JOA Accounting Procedure
 - Capital & Operating
 - Direct Charges & Overhead
- Well specific costs for drilling, completion, equipping and ongoing operations
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 - Operating Costs
 - Labour
 - Electricity
 - Chemicals
 - Others

Adjustments

- Those necessary due to the party in penalty
- Depends on what the party has paid capital for
- Possible re-equalization and adjustment upon payout

Single Pad Site
Multiple Parties
Multiple Ownerships
Multiple JOAs, Operating Procedures
& Accounting Procedures



AFE & Cost Centre Set-Up

- Site (Surface)
- Access Road
- Individual Wells
- Production Equipment
- Site Trailer
- Production Facility
- Pipeline to Central Processing Facility

Ownership (DOI)

- Wells & Well Equipment at actual DOI
- All others at blended ownership based on well count

Accounting

- JOA Accounting Procedure
- Capital & Operating
- Direct Charges & Overhead
- Well specific costs for drilling, completion, equipping
- **PSSA Accounting Procedure**
 - **Common construction costs**
 - **Ongoing well operations**
 - **Equitable allocation of common costs**

Adjustments

- Arising from parties in penalty / conversion of interests
- **Equalizations as wells are added**
- **Enlargements (pad site or facilities)**

Scenario Summary

Similarities

- Asset Definition
 - Associated AFEs
 - Associated Cost Centres
- DOI set up and managing changes
- Payout accounting
- Allowable direct costs
- Allowable allocated costs
- Some adjustments

Differences with Multiple JOAs

- Cost sharing managed by blended DOIs for select assets
- Accounting adjustments vary with drilling activity and then stabilizes
 - Initial area development
 - Equalization / Re-equalization of capital
 - Re-distribution of operating costs as well count changes
- Addresses enlargements and changes over the life of the operations

The Accounting Set-Up is Key

Hierarchy – An Alberta Pad Site – 1P0/01-01-001-01W5/00

Asset	DOI	Maintained by	Capital Costs (AFEs)	Operating Costs (Cost Centres)
Surface/Site Costs	Blended	Site Operator	Segregated Construction Costs	PSSA - Allocated Costs, Direct Charges, Overhead
Access Road (if part of the Pad Site)	Blended	Site Operator	Segregated Construction Costs	PSSA - Allocated Costs, Direct Charges, Overhead
Well A & Associated Wellsite Equipment	JOA #1 DOI	Site Operator	Traditional Drilling, Completion & Equipping for Each Well	JOA –Well Specific Direct Charges & Overhead; Allocated Well Costs
Well B & Associated Wellsite Equipment	JOA #2 DOI			
Shared Common Equipment	Blended	Site Operator	Segregated Installation Costs	PSSA - Allocated Costs, Direct Charges, Overhead
Site Production Facility	Blended	Site Operator	Segregated Construction Costs	PSSA - Allocated Costs, Direct Charges, Overhead

PASC Pad Site Sharing Accounting Guideline AG-19

- Background
 - Companion document to the PSSA
 - Draft #1 issued prior to PSSA Draft #1
 - Draft #2 issued prior to PSSA Draft #2
 - Identified issues for the PSSA Task Force to consider during the initial development of the PSSA
 - PASC & the PSSA Task Force solicited industry feedback on both documents
 - Draft #3 should see closer alignment with PSSA Draft #3

AG-19: Three Key Principles

- “equitable sharing”
- “consistency”
- “align costs with benefits” within reason

AG-19: Content

- Structure and Sharing of the “Pad (*Joint*) Account”
 - Discusses capital and operating cost sharing
 - Construction, drilling, completion, equipping costs
 - Handling of multi-well programs and cost allocations (*rig costs*)
 - Ongoing operating costs (*power demand and consumption costs*)
 - Recommends segregating and recording costs at different levels
 - Individual well costs
 - Individual pad site components (*the site, access road, common equipment*)
 - Pad facility & other shared infrastructure (*compressor, discharge line*)
- Addresses cost allocations for multiple pads within an operating area
- Proposes how to share abandonment and reclamation costs

AG-19: Content

- Quick reference guide
 - Capital Costs
 - Charged to individual well or all wells based on well count
 - Operating Costs
 - Charged to individual well or all wells based on well count
 - Excludes D&A wells from certain costs
 - Abandonment & Reclamation Costs
 - Charged to individual well or all wells based on well count
 - Includes D&A wells
- Provides some qualifiers and considerations
- Proposes how often to perform adjustments
- Presents an option to allocate costs to a subset of wells in some situations, a scenario not currently contemplated in the PSSA

AG-19: Quick Reference Guide

CAPITAL COSTS

	Individual Wells	All Wells	Comment	Recommended Basis	Adjustment Frequency
Pad Construction and Installation Costs		X		Well Count	Upon completion of installation and equalized as new wells are drilled
Pad Expansion Costs		X		Well Count	Upon completion of expansion and equalized as new wells are drilled
Well Drilling Costs	X				
Well Completion Costs	X				
Well Equipping Costs (e.g. wellhead)	X				
Installation of Common Equipment (e.g. group meter, satellite dishes, lease trailer, buildings, etc; excludes roads)		X	Unless equipment is used by a subset of all wells	Well Count or as otherwise agreed by Owners	Upon completion of installation and equalized as new wells are drilled
Pad Site Compressor or Other Production Equipment Installation Costs (Optional)		X	Unless equipment is used by a subset of all wells	Well Count or as otherwise agreed by Owners	Upon completion of installation and equalized as new wells are drilled
Flowline Installation Costs		X	Unless equipment is used by a subset of all wells	Well Count or as otherwise agreed by Owners	Upon completion of installation and equalized as new wells are drilled
Road Construction Costs (Includes Road Upgrade Costs)		X		Well Count	Upon completion of installation and/or upgrade and equalized as new wells are drilled

AG-19: Quick Reference Guide

OPERATING EXPENSES (OPERATIONS & MAINTENANCE)

	Individual Wells	All Wells	Comment	Recommended Basis	Adjustment Frequency
Well Operations & Maintenance	X				
Pad Site Operations & Maintenance (Routine repair and maintenance)		X	Exclude D&A Wells		
Lease Maintenance (Routine repair and maintenance)		X	Exclude D&A Wells		
Common Equipment Operating		X	Exclude D&A Wells		
Pad Site Compressor or Other Production Equipment Operating Costs		X	Exclude D&A Wells		
Flowline Operating Costs		X	Exclude D&A Wells		
Road Operating Costs (Routine repair and maintenance)		X	Exclude D&A Wells		

ABANDONMENT & RECLAMATION COSTS

	Individual Wells	All Wells	Comment	Recommended Basis	Adjustment Frequency
Wells	X				
Pad		X	Include D&A Wells	Well Count	
Lease		X	Include D&A Wells	Well Count	
Common Equipment		X	All Previously Producing Wells	Well Count	
Pad Site Compressor or Other Production Equipment		X	All Previously Producing Wells	Well Count	
Flowline		X	All Previously Producing Wells	Well Count	
Road		X	Include D&A Wells	Well Count	

Industry Feedback

- Expand the scope / Provide more guidance
 - The document speaks to what to do but not how to do it
 - How do I manage DOI changes?
 - If wells are drilled at different times how and when do I re-equalize the costs?
 - How often do I have to re-equalize costs; will they ever stop?
 - Which capital costs do I re-equalize and when?
 - What are valid costs and how should I allocate them?
 - When and how do I adjust operating costs for new wells?
- Use the PSSA definitions for added clarity
- Clarify how the Pad Account and payout accounts work together

Industry Feedback

- Clarify which Accounting Procedure is the basis for
 - Direct charges and overheads
 - Approvals and other joint account matters
- Provide general guidance on audit rights and the audit scope
 - Which audit clause prevails
 - What documentation is needed
 - Limit auditability of re-equalized costs
 - Consider revising the standard audit clause
- Even though the PSSA doesn't recommend a 13th month adjustment, shouldn't there be a true-up of costs in active years?

Industry Feedback

- What do I do if the pad site or production facility is enlarged or altered, or if there's an upgrade to the road?
- Expand on how rig costs are to be shared
- How do we treat spills and other environmental remediation costs (both ongoing and at end of life)?
 - Charge to a single well?
 - Charge to a subset of wells?
 - Charge to all wells?
- Is it realistic that costs would be shared by a sub-set of wells?

PASC Pad Site Sharing

Accounting Guideline AG-19

- General observations from the feedback
 - The guideline was intended to provide general guidance
 - The PSSA provides a lot of guidance on the issues raised
 - A closer linkage with the PSSA may be helpful
 - Familiarity with the PSSA helps understand the AG and vice versa
 - Balance is needed between a guideline specific to the PSSA and a general guideline
- The PASC Sub-Committee in consultation with the PSSA Task Force will consider how to strike the necessary balance

A Final Word

- Accounting for shared pad site operations can be
 - Very straightforward
 - Very complex
- Accounting for share pad site operations “feels” complicated
 - There are precedents
 - Unit Operations with payout wells
 - Cost allocations over a large operating area with a mix of operations
 - Facility expansions and/or ongoing re-equalizations
 - Leverage “blended interests” to make the accounting easier
 - Ongoing costs are not expected to be significant*
 - Ensure any added complexity is worth the cost and effort*
 - No need to add complexity to something that is straightforward*

What You Can Do

- Become familiar with the PSSA and the AG
 - From an accounting perspective
 - From an audit perspective
- Design your company's accounting practice
 - Provide it to the negotiators as a guide to manage complexity
- Have your say while the agreement and the accounting guideline are being developed
 - Deadline for comments is **February 10th, 2017**

Thank You !

- PSSA Task Force
- PASC Pad Site Sharing Sub-Committee
 - Wayne Fuller
 - Lynda MacNeill
 - Dave Sandeman
 - Earl Robbins
- PASC Joint Interest Research Committee
- PASC Joint Venture Audit Committee
- Industry reviewers