Oil Sands Royalty Project Application and Approval Process

Prepared by Alberta Energy for Oil Sands Royalty Business Training
June 11, 2019
Disclaimer:
The information contained in this presentation is provided at the sole discretion of the Department of Energy (Department). The Department makes no warranties or representations regarding the information contained in the presentation, or any statements made during the course of the presentation. All information is provided for general information purposes only. You should not use or rely on this information for any other purpose. The information in the presentation and any statements made during the course of the presentation should not be relied upon as a representation of the Department’s official position in law or policy. That material is publicly available through the Department’s website at www.energy.alberta.ca. Reproduction of the presentation in any form is prohibited.
1. What is a Oil Sands Royalty Project?
2. Royalty Project Application Process
3. Royalty Project Review and Approval Process
   - Engineering review
   - Economic review
   - PNCB audit
4. Project Approval - Ministerial Order
5. Reporting Requirements
6. References and Contacts
Oil Sands Royalty Projects
What is an Oil Sands Royalty (OSR) Project?

• OSR Projects – oil sands projects defined and approved by Alberta Energy under the provision of the Oil Sands Royalty Regulations (OSRR09)

• Pay royalty under the **Oil Sands Royalty Regime**
  - R – C Regime
  - Designed to incent capital intensive Oil Sands Projects
  - Lower royalties up front until Royalty Project pays out (first time cumulative revenues ≥ cumulative costs - PNCB and allowed costs)
Why Apply?

- Only approved OSR Projects can pay royalty under the Oil Sands Royalty Regime

- If not, conventional royalties on volumes produced from non project wells & mines will have to be paid
  - MRF royalties (wells spudded after Jan.1, 2017) and ARF royalties (wells spudded up to and including Dec. 31, 2016) for non project wells
  - NPR mine royalties for non project mines

- Oil Sands Royalty Rates (1-9% of project gross revenue, 25-40% of net revenue, based on WTI price and payout status)
Key Requirements

- Alberta Energy Regulator ("AER") scheme approval
- Oil Sands Lease(s)/Agreements
- Operational Integration & Common Management
- 50 km Limit
- Geographically and Geologically Contiguous
- Within Alberta
- Class 3 Cost Estimate
  - >$50M Processing plant & facilities additions
- Reserves data
- Economically Justified
  - Profitable (net revenue)
  - Will achieve payout within reasonable amount of time
  - Will increase royalty payable to Crown (incremental analysis)

Other Criteria
- Project development plan
- Clearly defined project
Royalty Project Application Process

Who, What, When, Types, How, Requirements
Who? What? When?

• Who can apply?
  • Primary owner of the lease(s) on behalf of the other lessee(s)

• What can be applied for?
  • Must include the whole or part of an approved AER Scheme
  • Oil sands Crown rights only

• When can an application be submitted?
  • Following the issuance of an AER approval
  • Expectation is that an operator is committed to developing the project
  • No requirement to submit application immediately, however a delay may have cost implications (impacts effective date and prior net cumulative balance)
Effective Date

• The effective date of an OSR project is the date from which royalty begins to be calculated under the terms of the OSRR’09.

• The effective date of the OSR project or OSR Project expansion must **not** be earlier than any of the following:
  
  – The first day of the month in which the application was received
  
  – The first day of the month following the month in which the AER approval relating to the proposed project or the amendment relating the expansion is approved
  
  – The first day of the month that precedes by nine months the month in which the project or the amendment relating to the expansion is approved
Types of OSR Project Applications/Amendments

- **Types of Applications**
  - New Project
  - Amendment
  - Revocation
    - Expansion
    - Amalgamation
    - Other

- **Ministerial Amendments**
  - Revocation
  - Other
Potential Triggers - Amendment

Examples

- Adding new wells (well based approvals)
- Adding new lands or facilities
- Expanding facilities
- Changing project operations/technology
- Changing maximum production capacity
- Removing Project lands, assets, or facilities
- Changing cost allocation methodology
When to Amend a Project?

- A material change to the OSR Project
- Scheme amendments may require Project Amendments
  - Will depend on significance and materiality of scheme amendment
  - A good rule of thumb is to assess any scheme amendment against the Project description in the MO
- When in doubt, contact Alberta Energy
- Risk to operators: Ineligible costs incorrectly claimed in EOPS will be removed upon audit, PNCB time limitations may impact an amendment application and costs may become stranded.
- In case of a material change resulting from a lease surrender please notify the department
How to Apply?

- Electronic Application / OASIS
  - All applications must be submitted electronically through Alberta Energy’s Electronic Transfer System (ETS)
  - Once submitted, application is processed / reviewed through OASIS system
  - Online training modules are available that provide a step by step guide for preparing an application through ETS

![Electronic Transfer System (ETS) login interface](image-url)
What Should an Application Include?

- OSR New Project Checklist

- OSR Project Amendment Application Checklist
What Should an Application Include?

• Project Ownership (all agreements and agreement owners)
• Project Identification (Project name, Operator, Contact)
• Project Overview and History
• Description of Project Operations
  – Recovery technology
  – Production profile (peak production capacity)
  – Development plans and full life cycle development schedule
  – Geographic locations of all Project components
• Scheme approval(s) and application(s)
  – Current scheme and all prior amendments not currently in Project, with associated applications
What Should an Application Include?

- Description of capital assets and engineering systems
- Description of any measured use assets and all other assets of material relevance
- A list of oil sands products
- A list of wells
- Reservoir characteristics and reserves data ([IB 2015-07](https://example.com/ib2015-07))
- Economic evaluation ([IB 2015-10](https://example.com/ib2015-10))
- Class 3 Cost Estimate for processing facilities valued at >$50,000,000 ([IB 2017-03](https://example.com/ib2017-03))
- Description of any shared assets and non-arm’s length transactions
- Proposed royalty calculation point
- Proposed effective date
- Proposed prior net cumulative balance (“PNCB”)
  - Must include all required supporting information and details
- Signature from authorized officer
Royalty Project Review & Approval Process
Primary Purposes

• Assess whether project qualifies for OSRR09
• Establish royalty ring fence
• Define the R and C in R-C royalty calculation
Review Process & Timeline

1. Receive Application
2. Pre-Screen Application
   - PNCB Review
   - Economic Review
   - Engineering Review
3. Prepare MO and Docs.
4. Review and Signoff
Pre-Screen

- Have all the essential components of the application been submitted?
- Department reviews application for completeness within 10 business days
- If application is deficient, applicant has 10 business days to submit required info
- Final Pre-screen decision: Proceed or Reject
- Rejected application can be resubmitted (new effective date)
- More information in (IB 2010-13)
- If the application passes the pre-screen, proceeds to detailed review
Detailed Review

- Consists of three main parts
  - Engineering review
  - Economic review
  - PNCB Audit
- Not all applications require all components
- All application reviews completed within 9 months
- Administrative amendments may be completed more quickly
- Final Decision and documentation
- If approved, documents sent to applicant
- Reporting requirements begin
Royalty Project Application Review

Engineering Review
Engineering Review

• Operational integration criteria met?
  – Meets criteria – can be considered one Project
  – Does not meet – consider a new stand-alone Project? (No need to reapply)

• What belongs in the Project?
  – Lands / Leases / establish geographic boundary
  – Facilities / Assets / meet Project Use Threshold
  – Establish Cost Allocation Methodologies for Shared Assets

• What terms, conditions, limits should the approval be limited to?
  – Expiry date(s)
  – Maximum Development Time, Maximum Production Capacity
Engineering Review

- Is the production forecast reasonable?
- Are there sufficient reserves in place to sustain production forecast?
  - 2P Reserves data, 3rd party 2P reserves report maybe required ([IB 2015-07](#))
- Suspended or abandoned wells or assets are generally not allowed
  - In some cases, suspended or abandoned wells can be allowed with an economic assessment made by an engineer
  - Well Inclusion Criteria ([IB 2011-09](#) for wells drilled prior to Jan 1st 2017 and [IB 2017-03](#) for post)
  - Wells will be reviewed at a license level
Engineering Review: Class 3 Cost Estimate Requirement (IB 2017-03)

- **Why?**
  - Indicates project has reached a certain level of definition and more likely proceeding as planned as per Class 3 Cost Estimate documents

- **When?**
  - The total costs of a new processing facility and modifications to an existing processing plant will cost $50 million or more

- **What?**
  - Will be determined on a case by case basis
Engineering Review: OSR Project Lands and Leases

- An OSR Project comprises the surface area and subsurface oil sands strata that will be used to produce or process bitumen.
  - Project Leases – are mineral rights in the oil sands agreements that are included in a Project.

- Project Lands – the surface areas included in a Project.

- Potentially Includable Land and Leases (PILL) – land and leases that are only included in the full lifecycle economic analysis to meet the economic requirement of an OSR project. This land must be within the “Project Area” as approved by the AER.
  - NOTE: An OSR application must be submitted for PILL to become OSR Project land and Leases.
Royalty Project Application Review

Economic Review
Economic Review

The first triage... submission of economic data?

ECONOMICS REQUIRED?

YES

- Adding new lands
- Bringing potentially includable lands to the project
- Substantial change in major cost components
- New project / new experimental project
- (...)

NO

- Administrative amendments
- Immaterial change in costs
- Immaterial change in production
- (...)

* some exceptions may apply
Economic Review

The second triage... The type of application

**TYPE OF APPLICATION**

- **NEW** project
- **AMENDMENT** to an existing project
- **AMALGAMATION** two or more existing projects into one

The type of application will impact the *economic tests performed* by the ADOE

The type of application will impact the way the *economic evaluation template* is completed

*some exceptions may apply*
Economic Review

Economic tests performed by the ADOE:

### TYPE OF APPLICATION

**NEW project**
- Positive NPV(*royalties*) to the Crown
- Positive NPV(*net revenue*)
- Project is expected to payout within a reasonable timeframe **

**AMENDMENT to an existing project**
- Positive incremental NPV(*royalties*) to the Crown
- Positive incremental NPV(*net revenue*)
- Amended project is expected to payout within a reasonable timeframe **

**AMALGAMATION two or more existing projects into one**
- Combined project’s NPV(*royalties*) to the Crown not less than the sum of the two or more separate projects
- Combined project’s NPV(*net revenue*) not less than the sum of the two or more separate projects
- Combined project is expected to payout within a reasonable timeframe **

* when applicable, i.e. exceptions are made for demonstration projects
** A case by case review. Depends on many variables such as technology used, project size, etc., i.e. 7-10 years
Economic Review

Effective November 1, 2015, these changes are implemented in the Economic Evaluation Template (IB 2015-10): 🚨

1. Bitumen production volumes will be reported under “Proved (1P) or Proved + Probable (2P) Bitumen Production Volumes” and “2C Bitumen Production Volumes” (if applicable) separately.

2. Number of Producer/Injector wells brought online or abandoned every year will be reported in separate columns.

3. Steam injection volumes for a thermal project will be reported under “Steam Injection Volumes”.

4. Sustaining and Strategic CAPEX will be reported separately for wells and facilities.

5. Abandonment Costs CAPEX will be reported separately under “Capex - Well Abandonments”, “Capex - Facility Abandonments”, and “Capex - Reclamation” separately.

Template located here:
https://www.energy.alberta.ca/OS/Documents/FORM_OSREvalNewAmendProject-January%202019.xlsx
Economic Review

The economic evaluation template has three main sheets:

Economic Evaluation template

<table>
<thead>
<tr>
<th>Notes</th>
<th>Log of changes</th>
<th>New Application OR Existing OSR</th>
<th>Project Amendment Application</th>
<th>OSR Amended Project</th>
<th>ProjRevSummary</th>
<th>ADMIN</th>
</tr>
</thead>
</table>

33
Economic Review

The type of application will determine which sheet(s) to use:

**TYPE OF APPLICATION**

- NEW project
- AMENDMENT to an existing project
- AMALGAMATION two or more existing projects into one

**Economic evaluation template**

- **#1** New Application OR Existing OSR
- **#2** Project Amendment Application
- **#3** OSR Amended Project

- New Application OR Existing OSR
- Project Amendment Application
- OSR Amended Project

- New Application OR Existing OSR
- Project Amendment Application
- OSR Amended Project

34
Economic Review

Common errors when completing the economic evaluation template

1. PNCB not entered correctly or aligned to values submitted for audit
2. For amendments, only two sheets are filled in (original #1 and amended #3)
3. Data entered in wrong units
4. First year data entries (if any) are not proportionated to the amounts for the remaining months of the year
5. SAGD has no gas consumption / gas consumption entered as positive
6. Abandonment/reclamation costs are empty
7. Real dollars are not used (prices and costs)
8. The numbers of wells drilled and abandoned do not match
9. Strategic capital is considered before a project reaches peak capacity
10. Sustaining capital is considered after a project reaches peak capacity
11. The application data do not cover the full life cycle of the project
Some features of the Excel template:

1. The worksheets are locked

2. The columns are color coded: blue for data entry; grey fields for calculated values

3. Columns pertaining to SAGD applications are blacked out for mining and primary applications

4. Notes section on top right for clients to enter additional information

5. Notes from DOE underneath the form provides further clarification to complete the form
Royalty Project Application Review
PNCB Audit
What is PNCB?

• PNCB – Prior Net Cumulative Balance
  • New Project: the balance of cumulative costs less cumulative revenues as of the effective date of the OSR Project
  • Amendment: the balance of cumulative costs less cumulative revenues pertaining to the effective date of the Amendment
• Standard 5 year PNCB period effective Jan. 1st 2017 (IB 2017-03)
  • In the past, it was a standard 3 year PNCB with possible extension up to 5 years under special circumstances
PNCB

- PNCB templates located: https://www.energy.alberta.ca/OS/Documents/FORM_OSRappl_pncb.pdf
Project Approval - Ministerial Order
What is a Ministerial Order (MO)?

• Have all regulatory criteria been met?
  • Yes → Approve Royalty Application
  • Issue Ministerial Order (MO)

• The MO is the approval and official legal document for an OSR Project

• The MO is not a public document and the information contained in the MO is confidential.
What is a MO? (cont.)

Specifies:

- Scheme approval(s)
- Project effective date
- PNCB
- Expiry date(s), if applicable
- Outlines any term and conditions to which the approval is subject to such as: Maximum Development Time/Production Capacity
- Defines the Project ring fence
  - Leases
  - Lands
  - Operations
  - Facilities
  - Assets
  - Wells
  - General criteria for future assets (i.e. wells drilled on Project lands and leases)
- Map of the Project
- Cost allocation methodologies if applicable
Reporting Requirements
Reporting Requirements

- Monthly Reporting
  - Monthly Royalty Calculation (MRC) for pre-payout Projects
  - Good Faith Estimates (GFE) for post-payout Projects
- Quarterly Reporting
  - CARE Revenue Form
- Annual Reporting
  - CARE Costs Form (In 2015 moved from quarterly to annual)
  - End of Period Statements (EOPS)
  - Operator’s Forecast (15 year Project forecast)
  - CARE Subsurface Form
  - CAMR (Cost Allocation Methodology Reports) if applicable
- Statement of Approval
  - All forms require a statement of approval (signed by an authorizing officer) except the Operators Forecast
Reporting Requirements

• Audits
  • EOPS for large Projects (>1,590m³/day) require independent third party audit opinion
  • EOPs are also audited by Alberta Energy’s Compliance and Assurance group

• Filing Penalties
  • Monthly forms are due at the end of the month following the month being reported
  • Late or incomplete forms will incur filing penalties as prescribed in the regulation

• Late Payment
  • Late payments of royalty will incur interest at rates prescribed in the regulation
References and Contacts
Reference Documents

- **Oil Sands Royalty Regulation, 2009**

- **Oil Sands Allowed Cost (Ministerial) Regulation**

- **Oil Sands Royalty Guidelines**

- **ETS Application Submission Training Modules**
  - http://training.energy.gov.ab.ca/Pages/OilSands.aspx

- **Royalty Project Application Forms**
  - https://www.alberta.ca/oil-sands-forms.aspx
Contacts

- **OSR Applications Support**
  - E-mail: OSRAApplications.Energy@gov.ab.ca

- **Manfred Pade – Director**
  - E-mail: Manfred.Pade@gov.ab.ca
  - Phone: (780) 644-1567
Questions?