

Joint API/SPE Houston Chapter General Meeting, 12/18/03



“Recent and Current Activities affecting Oil and Gas Reserves Definitions”

presented by

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Background of 1997 SPE/WPC Petroleum Reserves Definitions



- Joint effort of WPC and SPE in establishing Proved, Probable and Possible reserves definitions
- 9-person committee, worldwide representation, observers from EIA, AAPG, WPC, SPEE, SEC (invited but declined)
- WPC represents 59 oil-producing countries
- Introduced definitions for probabilistic methodology

Current SPE Reserves Committee Activities



- Working toward publication of glossary relevant to reserves/resource definitions
- Cooperating with United Nations and Russian Federation in efforts to “harmonize” reserves definitions
- Recommendation made to SPE board in October to initiate communications with US SEC
- Recommendation generated through 4-person subcommittee consisting of 3 major oil companies and 1 consulting firm

SPE - SEC Dialogue



- Letter sent from SPE President, Kate Baker, on November 7, 2003 to Roger Schwall, Assistant Director, Office of Corporate Finance, SEC
- Offer extended to establish broad-based committee or group of SPE members to assist SEC in a better understanding of
 - (1) industry reliance upon technology in estimating and classifying reserves and
 - (2) other matters that may be of interest to the SEC
- Not “Advisory Panel” – Simply a resource or focus group to serve at request of SEC

Increased Surveillance and Enforcement by SEC



- “Comment Letters” from SEC engineers
- Inquiries about certain reserves issues
- Example: Oct 2002 letters to 55 producers regarding flow testing
- Letters may lead to “debooking” of reserves
- 14% of producer attendees at October 28, 2003 SPEE Forum have been asked by SEC to “debook” certain reserves

SPEE Forum Series



- Begun in 2000 by SPEE as effort to create better understanding (and dialogue) between industry and SEC
- 80 attendees in 2000, 120 in 2001, 120 in 2002 and 209 in 2003
- Both SEC engineers attend and render opinions on matters that are not well understood
- Hypothetical “case studies” presented to determine SEC position and interpretation
- Cases include all “Hot-Button” issues described in following slide plus others

More on Comment Letters



Questions from an October 2003 letter to a reporting company:

- Identify all independent engineering firms used during the past 5 years.
- What properties were reviewed?
- How much the firms were paid for work on projects other than year–end type work?
- If the firms were discharged, reason(s) why?

Even More About Comment Letters



Review and inquiry may be prompted by:

1. Routine inquiry of all IPOs and securities offerings
2. Interest triggered by press releases
3. Rotating three-year reviews
4. Third-party requests
5. Whistle-blowers

Excerpts from 10/28/03 Forum



Ron Winfrey “... we think unproved reserves, the probable reserves, deserve some light of day. The push will necessarily come from the industry, not from the internal folks of the SEC.”

Ron Harrell (Moderator) “If such a movement were to be instituted or instigated, would that come from an individual company, an organization like the SPEE, would that come from SPE, API ?”

Ron Winfrey “Yes”

Jim Murphy “Any or all of the above”

More Excerpts from the 10/28/03 Forum



Jim Murphy “If you are an independent engineer, you should realize that, although you are hired by management and report to them, the check you receive for your services comes from the Company, who are really the Shareholders. You have an obligation to the Shareholders to provide a fair, honest and unbiased reserves report.”

Even More Excerpts from the 10/28/03 Forum



Jim Murphy “If the SEC feels that reserves that have been booked as proved do not meet the requirements of being classified as proved reserves and they have a material effect on the company’s financial statement, we will request that the company not only take the write-down if necessary, but also restate their reserves and financials for the past periods the reserves were on the books.”

(Continued next slide)

Even More Excerpts from the 10/28/03 Forum



“This may have serious consequences under the new Sarbanes-Oxley Act of 2002 because the officers of the company will have had previously certified the financial statements as being correct. Engineers appear to have additional liability under the act, as well; but this is yet to have been tested in court.”

Effect of the Sarbanes-Oxley Act of 2002 (SOX)



Most significant securities law since
1933 and 1934 Securities Acts

Increased level of concern by:

- (1) Regulators (SEC)
- (2) Boards of Directors
- (3) Corporate management
- (4) Accounting firms
- (5) Financial Rating Agencies
- (6) Internal Reserves Audit
Policies and Procedures
- (7) Increased involvement by
third-party firms

Continuing SEC “Hot Button” Issues



- (1) Year-end pricing (spot)
- (2) Recovery factors (relatively new concern)
- (3) Requirement for flow-testing (under study)
- (4) Undeveloped reserves (PUDs)
- (5) Lowest-known hydrocarbons –
well bore data only (reversal of earlier position)
- (6) Interpretation of PSCs
- (7) Sales of non-hydrocarbons
- (8) OPEX to include appropriate overhead costs
- (9) Reliance on 3-D seismic
- (10) Industry confidence in MDT data
- (11) Assurance of adequate markets
- (12) GTL reserves
- (13) Attribution of reserves to NPIs

SEC 10-K Disclosures



- Revenues from non-hydrocarbon sales
- Significant (material) events post December 31
- Alternate pricing (reasonable) cases
 1. Higher prices - same reserves
 2. Lower prices - reduced reserves
- Financial effect of price hedging

“Regulation without Representation ?”



- Argument has been made that a combination of technology and SOX is driving SEC Staff to create and impose new rules or regulations “on the fly” without industry input
- Typical federal regulations result from “Notice of Proposed Rulemaking” (NPR) inviting input from the industry to be regulated

Canadian Update



- National Instrument 51-101 supercedes prior reserves reporting requirement (old regulation 2-B)
- Revised definitions of all reserves categories – NI 51-101 proved reserves similar to US SEC
- Requires annual reporting of proved AND probable reserves
- Allows reporting of proved and probable and possible reserves
- Requires third-party verification of reserves (large producers exempted)
- Glenn Robinson (engineer) and David Elliott (geologist) as employees of Alberta Securities Commission are functional equivalent of SEC engineers
- Requires reporting of aggregate proved reserves at corporate level of P-90; not clear about how this is to be done



Questions / Comments ?

<http://www.spegcs.org/en/studygroups/display.asp?sgid=6>



MERRY CHRISTMAS

AND

HAPPY NEW YEAR

TO YOU ALL !!!