The ASC's 2018 Oil and Gas Review Reflects Troubled Times in the Industry

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- On December 17, 2018, the Alberta Securities Commission ("the ASC") released its annual oil and gas review ("the 2018 Review").
- The review delineates the key areas of disclosure identified over calendar 2018 as needing improvement and highlighting future disclosure modifications necessitated by amendments made to the *Canadian Oil and Gas Evaluation Handbook* ("the COGE Handbook") in 2018.
- Tangentially, and dishearteningly, the 2018 Review also highlights the staggering decline in the number of oil and gas reporting issuers principally regulated by the ASC amidst increasing regulatory and political uncertainty and environmental and social scrutiny of oil and gas development.

Highlights of the Review

Juniors hardest hit

The total number of reporting oil and gas issuers regulated by the ASC is now just over half the amount in 2012, and the brunt of this decline has been borne by junior companies producing less than 10,000 BOE/day.[1] While in 2014 juniors constituted 80 per cent of reporting issuers, they currently make up only 65 per cent.

Consolidation and efficiencies

However, in contrast with 2017, which saw declines in the number of reporting issuers mainly due to receiverships and bankruptcies, 2018 has been a year of industry consolidation undertaken by a limited number of larger industry players.

Additionally, the industry has continued to shift in focus towards more costly and complex horizontal and multi-stage hydraulic stimulations meant to maximize existing extraction capability. 2018 observed continued sizeable improvements in well-life extension and improved recovery techniques. At the same time exploration continues to remain effectively flat, with the ASC noting negligible overall exploration with discoveries disclosed by only four seniors, two intermediates and six juniors.

Areas of concern for the ASC

Economic factors over the past year have unsurprisingly resulted in negative adjustments for all reporting issuers.

In part reflective of these changing industry dynamics, the ASC has noted a number of continuing and emerging areas of concern with the disclosure of reporting issuers. In particular, the ASC noted issues in 2018 regarding:

- Failures to disclose differentiated development plans for proved and probable undeveloped reserves, factors potentially impacting project commerciality, and adequate reasons for deferral beyond periods stipulated in the COGE Handbook[2].
- Disclosures of undifferentiated information combining both unproved and proved properties. Additionally, the ASC noted continued omissions and generic disclosures of gross and net areas owned by reporting issuers based on the proportion of their respective working interests, and of expiring exploration, development and exploitation rights;
- Inaccurate reporting of reserve reconciliations. Issues included inadequate disclosures with respect to mismatched opening and closing balances, negative volumes for some reserve change categories, erroneous technical revisions and reserves acquisitions, incorrect production volumes, omitted or inconsistent units of measurement, the use of incorrect reserve change categories and a failure to properly explain the disclosures of each reserve category; and
- Inadequate or erroneous disclosures when reporting issuers ceased oil and gas activities. Issues included failures to file the required notice at all, or on time, filing a notice when the reporting issuer did not cease engagement in oil and gas activities, and failures to update disclosure and issuer profiles on SEDAR to reflect the ceasing of oil and gas activities.

Reclamation costs

Additionally, reflecting the tumult of political and legal forces in the oil and gas industry in the past year, the ASC has once again provided explanations of the proper method to account for abandonment and reclamation costs, a topic which has gained increased importance following the Alberta Court of Appeal's decision in *Redwater*, previously discussed here. The implications of the *Redwater* decision have recently been highlighted by concerns over the size of reclamation liability estimates arising from news reports in October, and the Alberta Energy Regulator's August announcement that it intends to adopt a more stringent approach to shifting reclamation liabilities following the announcement of Sequoia Resources Corp. to cease operations in early 2018. Understandably, the disclosure of reclamation liabilities is likely to remain a top consideration for reporting issuers heading into 2019.

“Ghost barrels”

Finally, in response to recent discussions regarding “ghost barrels” resulting from unused space in transportation infrastructure, the ASC has provided a discussion of the disclosure expectations around forward transportation contracts, noting in particular that reporting issuers must disclose the size of excess and unused transportation space, the expected duration of the unused space, and the value associated with that space where reporting issuers do not maintain proved total reserves necessary to satisfy forward agreements.

Looking Ahead

In conclusion, the 2018 ASC *Oil and Gas Review* attempts to address a number of ongoing issues while also providing reporting issuers with the information they require to minimize risk and address uncertainty in response to a changing industry dynamic and the headwinds of unpredictable external forces. Such guidance is critical in the face of expected continued uncertainty in 2019.

[1] A reduction from 302 reporting issuers in 2012 to 152 in 2018.

[2] Five years absent appropriate justification with adequate explanation.