

Chapter I

Introduction

Section 1

Principles and Procedures Manual Overview

1. Principles and Procedures Manual Overview

1.1 Authority and Scope

The *Alberta Natural Gas Royalty Principles and Procedures 2003* (referred to as the Guidelines) described in this manual are the result of extensive discussion and effort between representatives of both the Alberta Department of Energy (the **Department***) and of the petroleum and **natural gas*** industry (**Industry***). The **Regulation*** relating to this manual is the “*Alberta Regulation 220/2002.*”

The *Alberta Natural Gas Royalty Principles and Procedures, September 2001 edition*, describes the principles involved in assessing, levying and collecting Alberta’s Crown royalty share of gas and gas products produced from lands subject to a Crown lease agreement, and the procedures that were used to carry out the assessment, levy and collection for production periods between January 1994 and October 2002.

These Guidelines are provided for the convenience of the reader in order to give an understanding of the general application and principles for determining royalty. Application of the Regulation in specific situations may vary, and implementation and practice of the Regulation may change without amending the Guidelines. This manual interprets the relevant energy legislation (statutes and regulations), and communicates policy decisions made, based on the legislation.

Should any conflict arise among the Mines and Minerals Act (the Act), the Regulation and the Guidelines, the Act and the Regulation will prevail. Where there is a conflict between the Principles and the Procedures, the Principles prevail; and where there is a conflict between the Principles and the Regulation, the Regulation prevails.

The Department’s **advance ruling*** process (refer to *Ch. II, Sec. 9.1*) interprets the manner in which the relevant legislation, policies and guidelines will apply to proposed business arrangements.

This manual, effective October 2002, describes the **principles** involved in assessing, levying and collecting Alberta’s Crown royalty share of **gas*** and **gas products*** produced from lands subject to a **Crown lease*** agreement. It also describes the **procedures** that will be used to carry out the assessment, levy and collection.

1.2 Purpose and Use

Use this manual as:

- A business reference, to assist Alberta's petroleum and natural gas industry in their evaluation and decision-making processes;
- A practical guide to reporting and compliance with business rules and procedures associated with the assessment, levy and collection of Crown natural gas royalty.

Chapters I-IV and the *Appendices* are written sequentially and are cross-referenced for ease of use. The contents of these are as follows:

- *Chapter I, Sections 1-3* deal with the overview of the Guidelines.
- *Chapter II, Sections 1-10* deals with the principles and policies involved in assessing, levying and collecting Alberta's Crown royalty share of gas and gas products produced from lands subject to Crown's lease agreement.
- *Chapter III, Sections 1-8* deals with the procedures that will be used in assessing, levying and collecting the Crown royalties.
- *Chapter IV, Section 1-6* is a Reporting Guide.
- The *Appendices* deal with sundry items for the information of the royalty clients. It includes various calculations, rules, definitions, and other administrative information to assist the royalty clients.
- ***Refer to Appendix P for the forms referred to throughout the Guidelines.***

The Table of Contents should permit easy reference to specific business principles and policies. The relevant legislation is referenced and will direct the user to the pertinent section of legislation. This manual contains words that are defined in Appendix N. Words defined in the appendix are identified by **bold** letters and a star (*) the first time they appear in the document.

If the Guidelines do not provide an answer, questions should be directed to the Client Services Help Desk or the agencies listed in *Appendix L*.

1.3 Maintenance and Distribution

The Department will update the Guidelines when there is a major change in relevant policy or legislation, and routinely, to incorporate information published in Information Letters and Information Bulletins.

Information Letters are sent to **Royalty Clients*** each month to provide notification of:

- **Reference Prices***, Par Prices and other Crown natural gas royalty factors;
- Changes in legislation and policy; and
- Interpretations and other information relevant to Crown royalty programs.

Information Bulletins are sent to Royalty Clients each month to provide notification of:

- Changes in procedures;
- Filing dates, reminders, interest rates; and
- General information relating to the ongoing administration of Crown natural gas royalty.

Royalty clients, or other persons directly affected by the administration of Alberta Crown natural gas royalty, who wish to receive copies of Information Letters, Information Bulletins or additional copies of this manual should check the Department's Internet site at <http://www.energy.gov.ab.ca> or contact Gas Royalty Calculation at (780) 427-2962, or by fax at either: (780) 427-3334 or 422-8732, or by mail at the address provided in *Appendix L*.

The Information Letters, Information Bulletins and other related Gas Royalty information is available on the internet at the following website address:

<http://www.energy.gov.ab.ca>

Section 2

Executive Overview

2. Executive Overview

2.1 Background

In 1991, the Department organized a Joint Project Team with recognized petroleum and natural gas industry associations to address the simplification of Crown natural gas royalty administration. The Joint Project Team worked extensively with representatives of many sectors of the petroleum and natural gas industry, chiefly through the following industry associations:

- Canadian Association of Petroleum Producers (CAPP), formerly Canadian Petroleum Association (CPA);
- Independent Petroleum Association of Canada (IPAC);
- Small Explorers and Producers Association of Canada (SEPAC);
- Canadian Association of Petroleum Production Accountants (CAPPA).

The Joint Project Team worked with employees from more than 30 royalty clients to research and develop the Crown Natural Gas Royalty Guidelines that are described in this manual.

In 1998, the Royalty and Related Information Review (RRIR) task force, consisting of industry and Ministry members, recommended changes to the administration of Crown royalties and the reporting of upstream production information. The RRIR committee recommendations included developing a central registry that would contain key gas and oil information. This central registry, called the Petroleum Registry of Alberta (**Registry***), is a joint strategic initiative of the oil and gas industry (coordinated through CAPP and the SEPAC) and the Ministry of Energy [Alberta Energy and Utilities Board (EUB) and Department of Energy (DOE)]. Implementation of the Registry involves numerous changes in DOE and the EUB reporting that are described in this manual.

The Ethane and NGL Task Force reviewed all aspects of the policy framework pertaining to ethane. The Task Force consulted with representatives of the upstream oil and gas and the petrochemical industries, as well as senior officials from the DOE. The Task Force recommended changes to treat recovered Ethane as a distinct product, recognize the **in-stream components*** (ISC) of residue gas streams recovered downstream from a field plant, and charge royalty based on them. Implementation of the Ethane and NGL changes and changes to DOE and the EUB reporting are described in this manual.

2.2 Synopsis of Business Change

Much of the complexity of the pre-1994 Crown natural gas royalty administration was created by the requirement to relate individual sales contracts and **facility*** costs to the **Crown interest share*** of **well event*** production. Retroactive changes

to valuation, cost and production data resulted in extensive industry re-filing and, as a consequence, closing the Crown natural gas royalty accounts for a given production year could take up to four years.

To address the complexity in administration, the Joint Project Team developed the following major changes, which were implemented effective 1994:

- Crown royalty liability is triggered when the product leaves the **royalty network*** (except where gas is sold within the royalty network). Crown royalty credits are established to defer the liability arising from qualified gas and gas product injection. Existing Crown **royalty paid banks*** are reverted to native status (for Crown royalty purposes only).
- Monthly Reference Prices are used to value the Crown's royalty share of gas (**raw gas***, **residue gas*** and **ethane***), **propane***, **butane*** and **pentanes-plus***; however, royalty clients may elect to value their Crown royalty gas at an annual **Corporate Average Price***.
- **Monthly and Annual Sulphur Corporate Average Price (S-CAP)*** is used to value **sulphur***; however, in certain circumstances, sulphur is valued monthly and annually at the Sulphur Default Price.
- Crown's share of the operating costs of compressing, **gathering*** and processing natural gas is recognized through a Standard Operating Cost as a rate per **unit***. The **unit operating cost rates*** (UOCR) are determined annually.
- Crown's share of Capital Costs (CCA) and **Crown Share of Custom Processing Fees*** (CP) are determined based on the **Corporate Effective Royalty Rate*** (CERR) of the royalty client.
- The Department issues monthly **invoices** to royalty clients in respect to Crown natural gas and natural gas product royalties.

Implementation of the Registry in October 2002 (October 2002 production month), involved numerous changes to DOE and EUB reporting. The Registry is a shared, interactive, secure, web-based database targeted to improve the quality and management of key volumetric, royalty and infrastructure information.

The major reporting changes are as follows:

- Most industry volumetric reporting to and from the DOE and EUB will take place through the Registry (Registry has replaced S- and OAS-reporting);
- Royalty invoicing occurs through the Internet;
- Some business rule and process changes have occurred;
- Implementation of the Natural Gas Liquids (NGL) policy, which was announced in December 1999;
- Late Filing Penalty changes.

Section 3

Alberta Natural Gas Royalty - Process Summary

3. Alberta Natural Gas Royalty Process In Summary

3.1 Overview

The Crown gas royalty process can be separated into four distinct groups of submissions:

- **Once Only**—those through which a royalty client may elect a valuation method;
- **As Required**—typically those that establish production and cost allocation or accountability for Crown royalty;
- **Monthly**—those from which the monthly Reference Prices are calculated and the Crown's royalty share of gas and gas product volumes/quantities is determined. Monthly submissions are also used to determine monthly Sulphur Corporate Average Price and monthly Sulphur Default Price;
- **Annual**—those that relate to establishing costs, corporate average prices for gas (CAP) and for sulphur (S-CAP), or special conditions under the Gas Reference Price.

A summary description of the reports in each group is provided in *Ch. I, Sec. 3.2* (following) and a graphic overview of the relationship of these reports to the Crown royalty invoice is provided in *Ch. I, Sec. 3.3*.

3.2 Industry Reporting to the Department (refer to the chart on *Ch. I, Sec. 3.3*)

Group 1. Once Only Submissions

There is one submission in this reporting group, filed by a royalty client.

- The "Election for Gas Valuation" (VA1 submission), is a royalty client's election to value the Crown royalty share of gas at either the Reference Price or the Corporate Average Price. The due date of the VA1 submission is on or before the 15th day of the second month following the **production month***in which new royalty clients were first allocated **volumes***either through the **OAF***or RMF2 submissions. Only clients that have elected **CAP***may subsequently use the VA1 submission to change their election to the Reference Price.

Group 2..... As Required Submissions

Of the seven submissions in this group only the:

- Raw Gas Allocation Factor (RGA submission),
- "Reassignment of Volumes Set-up/Change" (RMF2 submission);

- “Reassignment of Volumes Termination” (RMF2-T submission) are filed by royalty clients.
- The RMF2 and RMF2-T submissions advise the Department of re-allocations of Crown royalty responsibility and the termination of re-allocations of Crown royalty responsibility.

The other four submissions are filed by **Facility Operators*** to set-up/change:

- Single Well/**Injection Schemes*** (RMF3 submission);
- **Facility Cost Centres*** (AC1 submission);
- Static **Stream Allocation Factor*** (SAF submission)
- Static **Owner Allocation Factor*** (OAF submission) which report stream and owner allocations that do not change monthly.

Exhibit A*, which is part of the Unit Agreement, is sent by the Unit Operators to the Units & Well Administration area of the Tenure Division. This is sent either with the new Unit Agreement or when changes in the Unit Ownership take place.

Group 3. Monthly Submissions

This group consists of seven submissions that are filed with the Department. They are as follows:

- The gas pricing (APMC series 600) submissions filed monthly by companies that fall under various categories for which reporting is required under the Natural Gas Marketing Act;
- The **NGL*pricing/transportation cost** filed monthly by **Designated Purchasers***, (NGL100 submission);
- The Sulphur Corporate Average Price (VA4 submission) filed monthly by specified royalty clients;
- The dynamic SAF submission filed monthly by Facility Operators;
- The dynamic OAF submission filed monthly by Facility Operators; and
- The Statement of **Proprietary Gas***- Royalty Waived (PW1 submission) filed monthly by some royalty clients;
- Volumetric submissions.

Group 4..... Annual Submissions

There are eight submissions in this group. Royalty clients file the following five submissions:

- Two to report the calculation of the Corporate Average Prices (gas on the VA2 submission, sulphur on the VA3 submission);
- One to report sales under co-generation and other long-term contracts (GR2 submission);
- One to report re-allocations of capital cost (AC3 submission); and
- One to report custom processing fees paid (AC5 submission).

Facility Operators file three submissions:

- Two to report **allowable costs***(capital on AC2 submission, operating on AC4 submission); and
- One to claim Sulphur Emission Control Assistance Program (SECAP) annual operating costs (SECAP 595 submission).

The SAF and OAF are standard formats for industry to report gas facility allocations as developed for the Registry. The SAF/OAF are industry-generated submissions that provide the pivotal volume/ ownership information upon which the Crown natural gas royalty administration depends. These submissions report volumetric and ownership information at the stream level for batteries, **gathering systems***, processing plants, and injection facilities for Crown royalty related allocations. Submissions of the SAF/OAF must be made on the Registry. Volumetric reporting on S and OAS documents is replaced by Volumetric, SAF and OAF submissions in the Registry. The Volumetric submission identifies the volumetric activities at a facility. The SAF submissions allocate the volumetric activity quantity to producing streams. The OAF submission allocates the stream quantities to owners.

3.3 Crown Royalty Monthly Invoice

The following figure depicts the once only, as required, monthly and annual reporting of the petroleum and natural gas industry (Royalty Clients, Facility Operators, Pipelines/Common Stream Operators, and Designated Purchasers), and the flow of information as it relates to the monthly Gas Royalty Invoice Package.

3.4 Release of Royalty and Related Information

To maintain the confidentiality of royalty information client specific information will be released, to a third party, only with the written consent of the royalty client. If a royalty client has a third party preparing royalty submissions on their behalf, they must ensure the department receives written notice, from the royalty client, authorizing the release of royalty information.

