



New SEC S-X 4-10, S-K 1200: Update

January 2010

John Lee

Texas A&M University



Disclaimer

Opinions expressed in this presentation are mine alone; they represent the opinions of neither the Securities and Exchange Commission nor of its staff members.



Where Are We in Rules Updating?

- SEC adopted new rules in late December 2008
- Rules effective for filings on or after January 1 2010
- Rules include new and revised definitions (S-X 210.4-10(a)), disclosure requirements (S-K 229.1200), and limited guidance (rules release document dated December 30 2008)



Significant Uncertainties Remained in Rules

- Five-year rule for Proved Undeveloped Reserves (PUDs) – how implemented?
- Prices and costs for proved and unproved reserves – how determined?
- Unproved reserves below lowest known hydrocarbons – possible reserves only, or also probable reserves?
- Reliable technology – what qualifies?

Guidance for S-X and S-K issued by SEC staff on 26 October 2009



Five-Year Rule and Added Word [4-10(a)(31)]

- Undrilled locations classified as having **proved** undeveloped reserves only if development plan has been adopted indicating they are to be **scheduled to be drilled within five years** unless specific circumstances justify longer time
- Implication: Unproved reserves not subject to five-year with added word – **but without it, unproved reserves are subject to rule**

Five-Year Rule and Development Project

(Question 108.01)



- **Question:** For an issuer that intends to develop a large field involving the drilling of numerous wells in multiple stages, what constitutes a development project?
- **Answer:** A development project is typically a single engineering activity with a distinct beginning and end, which, when completed, results in the production, processing or transportation of crude oil or natural gas. A project ... will be fully operational after the completion of the initial construction or development.



Five-Year Rule and Exceptions – (Question 131.03)

Question: In the definition of "undeveloped oil and gas reserves," what "specific circumstances" would justify a time period longer than five years to begin development of those reserves?

Answer: Although several types of projects — such as constructing offshore platforms and development in urban areas, remote locations or environmentally sensitive locations ... any extension beyond five years should be the exception, and not the rule.



Five-Year Rule and Adoption of Development Plan

- **Question 131.04:** The definition of "undeveloped oil and gas reserves" requires that the company have adopted a development plan with respect to the reserves. **What constitutes adoption of a development plan?**
- **Answer:** The mere intent to develop, without more, does not constitute "adoption" of a development plan and therefore would not, in and of itself, justify recognition of reserves. Rather, **adoption requires a final investment decision.**



Five-Year Rule and Extension of Field Economic Life

- **Question 131.05:** Would a company's decision to **slowly develop a field in order to extend its economic life** justify recognizing proved undeveloped reserves in the field beyond five years?
- **Answer: No.**



Implications of Questions 131.03 – 131.05?

Exceptions to five-year rule will be rare,
and case for exceptions must be
persuasive



Existing Economic Conditions [4-10(a)(22)(v)]

- Prices and costs at which economic producibility is to be determined
- Price is average price during 12-month period immediately prior to ending date of period covered by report
 - Unweighted arithmetic average of first-day-of-month price for each month during period unless prices are defined by contractual arrangements, excluding escalations based upon future conditions (same calculation procedures as year-end but done for each first day of the month)
- Computational procedure for costs not specified

Prices and Costs for Unproved Reserves

(Question 122.01)



- **Question:** What oil and gas prices should be used to estimate probable and possible reserves?
- **Answer:** Unproved reserves should be evaluated using the same price as used for the evaluation of proved reserves.



Determining Costs: Guidance (Question 122.02)

- **Question:** Does the new definition of "proved oil and gas reserves" require issuers to change their existing procedures for determining costs?
- **Answer:** No.

Unproved Reserves Below Lowest Known

Hydrocarbons: Question 117.03

- **Question:** The definition of the term "probable reserves" does not include instructions regarding reserves below LKH. Does this mean that probable reserves cannot be assigned below proved areas, such as below LKH limit, and can be no higher classification than possible reserves?
- **Answer:** No. Probable reserves may be assigned if reliable technology and data exist that ... support characterizing those reserves as probable reserves.

Probable or Possible Reserves without Proved?

[Question 117.02]



- **Question:** Can an issuer assign probable or possible reserves in an area in which it does not, or cannot, assign proved reserves?
- **Answer:** Yes. However, disclosure of unproved reserves without associated proved reserves should be done only in exceptional cases, such as for (1) development projects where engineering, geological, marketing, financing and technical tasks have been completed, but final regulatory approval is lacking or (2) improved recovery projects, at or near primary depletion, that await production response. ... Volumes that are not economically producible are not reserves of any classification and should not be disclosed.



And, Finally, Reliable Technology [4-10(a)(25)]

- Grouping of one or more technologies (including computational methods) that has been field tested and demonstrated to provide **reasonably certain results** with consistency and repeatability in formation being evaluated or **analogous formation**



Reliable Technology Guidance: Question 125.01

- **Question:** Does the staff intend to publish a list of reliable technologies that the SEC will accept for the determination of proved reserves?

- **Answer:** No.



Summary of Major Updates

- Five-year rule for Proved Undeveloped Reserves (PUDs) – almost always required
- Prices and costs for proved and unproved reserves – basically estimated using existing procedures (prices estimated more frequently)
- Unproved reserves below lowest known hydrocarbons – can be either probable or possible, depending on evidence supporting certainty level claimed
- Reliable technology – up to filer to demonstrate that technology has worked in past; no approved list to be issued



New SEC S-X 4-10, S-K 1200: Update

January 2010

John Lee

Texas A&M University