

Deepwater Accounting Procedure



OCS Advisory Board Workshop
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Agenda

- Project Background
- Key Concepts and Changes
- Q&A

Background



Objective

- Conform agreement to current industry practice
- Align Accounting Procedure & deepwater JOA
- Adopt 2005 AP language where appropriate
- Ensure non-operator protections
- Simplify technical labor & overhead provisions
- Rely less on overhead, more on direct charges
(leaning towards international agreements)

Drivers

- 1998 Project Team Accounting Procedure outdated
- Deepwater operations more complex, greater regulation
- Need to simplify accounting rules (tech labor & overhead)
- Need for better integration of AP & DW
JOA

Timeline

- Start – June 2009
- Draft 1 – June 2010
- Draft 2 – April 2011
- Draft 3 – July 2011
- Draft 4 – November 2011
- Approved by COPAS JI & Audit Committees – January 2012
- Council vote – April 2012

Team Members

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Key Concepts



Highlights of Major Changes

- Technical services directly chargeable
 - Eliminated overhead option
- Overhead simplified – only 2 percentage rates (Project and Operating)
- Added provisions for charging:
 - Operations Offices
 - Remote Technology Centers
 - Warehouses
 - Rig-Related Costs

JOA – Accounting Procedure

Key Interfaces

- Definitions
- Governing document – 3.1
- Affiliate equipment – 5.3
- Non-Participating Party audit rights – 5.9
- Disposal – JOA 6.2.4, 18.3
- Voting – JOA 8.2
- Project Team Costs – 12.3, Exhibit G
- Exhibit F – Payment disputes

New Definitions

- Critical Spare
- Feasibility Team
- Operations Office
- Remote Technology Center
- Rig-Related Costs

Critical Spare – I.1

- *“Material (i) owned by the Joint Account and held in inventory for emergency requirements because the lack of availability would have a major impact on operations.....”*
- Definitive list not possible
 - Varies by property
 - Equipment category (e.g., compressors) not a delineator
 - Technology, manufacturing changes
- Authority to acquire stems from JOA
- AP addresses how to account for equipment, but cannot authorize purchase

Joint Operations – I.1

- Operations necessary to explore, appraise, develop, produce....
 - Operations generally are billable
 - Many activities supporting operations are overhead
 - Accounting Procedure delineates between operations and activities – direct versus overhead

Payment Terms

- “Pay now, audit later,” with several industry-accepted exceptions:
 - Incorrect interest
 - Unauthorized project
 - Transfer of ownership interest, properly documented to operator
 - Items past the 24-month limitation
- Conflict with Exhibit F

Accounting Procedure Voting – I.6

- Any party can propose AP exception or other item needing approval
 - Examples: Affiliate rates, bill overhead item, material disposal
- Parties excluded from vote:
 - Proposing party
 - Affiliate of proposing party
 - Defaulting party

Company Labor

- Feasibility/Project Team – II.2.A.(1)
 - Assigned full- or part-time
 - Can include non-technical if assigned
 - Not assigned to team – only technical
- Other (not Feasibility/Project Team) – II.2.A.(2)
 - Field operations
 - First Level Supervision
 - Technical Services (On- & Off-site)
 - Other On-site operations not in facility rate or OH

First Level Supervision

- Definition establishes scope
 - Field operations
 - Maintenance & storage of joint material
 - RTC supervisors excluded
 - Technical supervisors excluded
- Function, not location
 - Technology allows off-site supervision

Contract Services – II.5

- Applies to 3rd party services, but not:
 - Affiliates
 - Overhead functions
- Training chargeable if operational, technical, HSE, govt.-mandated
- Awards chargeable

Equipment & Facilities – II.6

- Furnished by any Party or Affiliate
- Includes wholly or partially owned communication systems, computers *used in operations*
- Includes Rig-Related costs, Operations Offices, Remote Technology Centers
- Charge basis:
 - Rate commensurate with actual costs, *or*
 - Commercial rates for deepwater GOM

Rig-Related Costs

- Costs for a rig provided by any Party or Affiliate
- Rig modification, commissioning, mobilization
- Labor to oversee construction, modification, commissioning, mobilization
 - Excludes overhead functions
- Rig repairs
- Demobilization cost

Affiliate Services – II.7

A. Projects

- Assigned to Feasibility or Project Team
- Not assigned, but providing Technical Service to Team
- Activities/operations requiring AFE or would if not for emergency; excludes OH functions

B. Non-Projects

- Affiliate costs > \$___/yr. require approval
- No approval if below threshold

Affiliate Charges – II.7.A

- Cost Basis
 - “Actual cost” as billed by Affiliate
- Negotiated Rate Basis
 - Parties set rate, adjustment method, duration
 - Defaults to Cost basis if can't agree
 - Adjustment mechanism default – COPAS factor
- Charge basis can vary by Party/Affiliate
- Emergency – Cost basis if no negotiated rate

Affiliate Costs

- Affiliate awards & training chargeable
 - Billable Affiliate employees only
- Affiliate equipment & facilities charged under II.6
- No surcharge for Affiliate procurement

Affiliate Cost Controls

- Advance notice
- Third party attestation if Affiliate won't allow audits of its records
 - No profit
 - Consistently applied
 - Industry standards
- “JV” audit – proper application of rates, work authorized
- Commercial rate limit

Legal Costs – II.9

- Non-attorney costs billable (recording fees, fines, penalties, settlement, etc., subject to JOA indemnity, liability provisions)
- Collection costs – defaulting Party pays
- Indemnities – per the JOA
- Dispute resolution costs – per Exhibit H
- Negotiations w/ Parties – each Party pays
- No charge for in-house legal staff
- Approval of third party legal (Claims – JOA Article 22.4, Non-Claims – AP Section I.6)

Other Direct Charges

- Easements, rights of use
- Import duties, licenses, bonds, permit fees
- Pollution control, well containment equipment, and control, clean-up, subject to JOA indemnities
- Storage, preservation, maintenance of *jointly owned* materials

Overhead – III

Two Percentage Rates:

- **Project rate** – operations/activities that:
 - Require approval of parties (expend. limit)
 - Would require approval if not for operator emergency authority
- **Operating rate** – all other operations

Overhead Exclusions

- Salvage credits
- Insurance recoveries
- Costs under II.1 (Rentals & Royalties)
- Costs under II.9 (Legal)
- Value of injected substances
- Settlement of claims
- Tax assessments on property, minerals
- Production handling payments
- Deferred production payments
- Quality bank adjustments
- Insurance other than WC&EL

JOA Article 6.2 & Acctg. Procedure

- *“The Operator shall not undertake and activity or operation whose Costs are _____ dollars (\$_____) or more, unless an AFE has been approved”*
- Affect on Accounting Procedure:
 - Affiliates – Section II.7.A or B
 - OH vs. Project rate

Special Materials Situations

- Critical Spares, Contingency Purchases, Long Lead Items
 - JOA grants authority to purchase
 - Special pricing provisions not needed in the Accounting Procedure
 - Disposal rules require approval, but could overlap with JOA

Questions?

