farmers' advocate office

Liability Management in the Energy Sector

What is an "orphan"?

Many landowners are familiar with the issue of orphan wells in Alberta. A wellsite, facility, or pipeline is considered an "orphan" if the licensee becomes insolvent and there are no remaining responsible parties to address the end of life obligations. The Orphan Well Association (OWA) addresses the suspension, abandonment, remediation, and reclamation of orphan infrastructure. More information is available at http://www.orphanwell.ca/.

What does the Licensee Liability Rating (LLR) Program mean to landowners?

The Licensee Liability Rating (LLR) Program is designed to ensure that companies, not Albertans, face the costs of abandoning oil and gas wells, facilities, and pipelines, and subsequently reclaiming the associated sites. This program was established in 2002 and was updated in three phases from 2013 to 2015.

How does the LLR work?

Under the LLR, each licensee with the AER receives a Liability Management Rating (LMR) based on the following formula:

Company's Liability Management Rating (LMR) = **Deemed Assets** / **Deemed Liabilities**

Deemed Assets ↓ **Volume of production** X **$ netback** X **3**

Deemed Liabilities ↓ **Company's costs for abandonment and reclamation**

When a licensee's LMR dips below 1.0, the licensee must post a security deposit with the AER. When a company's liabilities outweigh its assets, the company must provide the AER with financial security for the difference to help mitigate the risks posed by the company.

If the licensee becomes insolvent and the site is not sold, the security deposit collected by the AER will be used by the OWA to pay for suspension, abandonment, remediation, and/or reclamation.

For more information, visit the AER website at https://www.aer.ca/regulating-development/project-closure/liability-management-programs-and-processes/liability-management-rating-and-reporting.

How are deemed assets and deemed liabilities calculated?

As per the diagram above, the formula for deemed assets is:

Deemed Assets = Volume of Production x Netback x 3

The volume of production is based on the licensee's reported production of oil and gas in the last 12 calendar months. The industry netback is calculated using the three-year industry average netback. A netback is the revenue minus the cost for producing a product. Currently 2008-2010 netbacks from the Canadian Association of Petroleum Producers (CAPP) are being used.

Deemed liabilities are based on the estimated cost of abandonment and reclamation for the wells and facilities belonging to a licensee. A standard formula is used based on the licence status and type of site. Sites that have been identified as "problem sites" by the AER require a more accurate site-specific liability value, as with oilfield waste facilities and gas plants. These site specific values are provided by companies for specific sites and need to meet specific requirements in order to be accepted and used.

There are so many acronyms…. what is the difference between an LMR and an LLR?

The LMR is the overall rating of a company's liabilities and assets within the Oilfield Waste Liability (OWL) Program, Large Facility Liability Management Program (LFP), and the Licensee Liability Rating (LLR) Program. Landowners will hear about the LLR the most because it governs most conventional upstream oil and gas wells, facilities, and pipelines.

I have heard that companies will try to offload their liabilities onto smaller companies. Is this possible?

When an application for a transfer is received, the AER will assess how the transfer would affect each company's LMR. If the transfer causes either company's LMR to dip below 2.0, that company will be required to post a security deposit or demonstrate how they will improve their LMR to 2.0 by providing specific plans before the application is approved. Visit the AER's website for more information on licence transfers: Frequently Asked Questions and other resources.

The AER may refuse a licence transfer based on compliance history or if they believe it is not in the best interest of the public.

For more information on the 2016 change to the transfer process, please see the AER's Bulletin 2016-16: Bulletin 2016-16.

How do I view a company's LMR?

The AER updates the LMR ratings on the first Saturday of every month. You can view the AER's most recent monthly report on their website: https://www.aer.ca/regulating-development/project-closure/liability-management-programs-and-processes/liability-management-rating-and-reporting. When a company name is marked with an asterisk, it means that they have posted a bond with the AER. The fact that the company has posted a bond does not mean they are insolvent; it simply means that their deemed liabilities have exceeded their deemed assets. Certain companies choose to have the AER hold extra security for them.

Do companies contribute to the Orphan Well Association (OWA) before they become insolvent?

Yes, each licensee must contribute annually towards an orphan levy for the OWA regardless of their LMR. The amount of the levy is determined by the AER on an annual basis. Each licensee pays into the levy based on their share of the total liability. All companies will contribute, but some will contribute more than others.

More information on the orphan levy is available on the AER's website: https://aer.ca/regulating-development/project-closure/liability-managementprograms-and-processes/orphan-well-association.

For more information contact the Farmers' Advocate Office

Phone: 310-FARM (3276)
Email: farmers.advocate@gov.ab.ca
Web: alberta.ca/farmers-advocate-office

Mailing address:
J.G. O'Donoghue Building
7000 113 Street
Edmonton, Alberta T6H 5T6

Revised: May 2016