

ENERGY AND GLOBAL TRANSACTIONS ALERT

PROPOSED REVISIONS TO THE SECURITIES AND EXCHANGE COMMISSION'S OIL AND GAS RESERVES DISCLOSURE REQUIREMENTS



For independent oil and gas companies and most integrated oil and gas companies, reserves are among their most important assets. Until fully exploited, reserve volumes are only estimates; however, the science and engineering of reserve identification, estimation and exploitation have been transformed dramatically by technology shifts in recent decades.

DECEMBER 12, 2007: SEC ISSUES A CONCEPT RELEASE

On December 12, 2007, the Securities and Exchange Commission (SEC) issued a Concept Release to gauge the public's interest in revising oil and gas reserves disclosures requirements in response to commentators and industry practice, as well as to contemplated and enacted changes by other jurisdictions that take into consideration the significant changes in technologies related to oil and gas reserve discovery and quantification.

ROBUST INDUSTRY RESPONSE LEADS TO RESPONSIVE PROPOSED RULES

More than 80 responses were received by the SEC and the responses demonstrated significant consensus regarding the issues explored by the SEC in the Concept Release. On June 26, 2008, the SEC proposed revised oil and gas company reporting requirements responsive to the many comments received. The SEC has described the overall purpose of the proposed amendment as "to provide improved disclosure about an oil and gas company's business and prospects without sacrificing clarity and comparability, which provide protection and transparency to investors."

PROPOSED CHANGES CHAMPION TRANSPARENCY

The proposed rules would permit the use of new technologies to determine proved reserves, enable companies to voluntarily disclose probable and possible reserves to investors and allow previously excluded resources such as oil sands to be classified as reserves. The proposed new rules would require that companies report the independence and qualifications of a preparer or auditor of reserve estimates based on current Society of Petroleum Engineers criteria, that

companies that rely on a third party file a report of such third party and that companies report oil and gas reserves using an average price based upon the 12-month period of the company's fiscal year.

NEXT STEPS

Public comment on the proposed rule changes will be taken by the SEC for 60 days. New rules are expected to be finalized in the fall of 2008. The SEC proposes to require compliance with these new disclosure requirements, if adopted, for registration statements filed on or after January 1, 2010, and for annual reports on Form 10-K for fiscal years ending on and after December 31, 2009, with no option to adopt earlier.

PROPOSED CHANGES AT A GLANCE

The chart below summarizes 14 key areas related to reserve reporting requirements explored in the Concept Release and what action the SEC has proposed in its June 26, 2008 announcement:

SEC CONCEPT RELEASE ISSUE	PROPOSED RULES
1. Replace our rules-based current oil and gas reserves disclosure requirements with a principles-based rule?	<ul style="list-style-type: none"> No specific changes proposed.
2. Consider allowing companies to disclose reserves other than proved reserves in filings with the SEC?	<ul style="list-style-type: none"> Proposal to make these disclosures voluntary Will require disclosure about the person primarily responsible for preparing the company's reserves estimates.
3. Adopt all or part of the Society of Petroleum Engineers – Petroleum Resources Management System (PRMS)?	<ul style="list-style-type: none"> Proposed new and revised definitions classification system based on both PRMS and the Canadian National Instrument 51-101.
4. Consider revising the current definition of proved reserves, proved developed reserves and proved undeveloped reserves (PUD)?	<ul style="list-style-type: none"> Will add a definition of the term “reserves” to describe more completely the criteria that an accumulation of oil, gas or related substances must satisfy to be considered reserves. Will expand the definition of the term “proved developed reserves” to include extraction of resources using technologies other than production through wells. Undrilled locations can be classified as PUDs generally if a development plan is adopted to drill within five years.
5. Specify the tests a company must undertake to estimate reserves?	<ul style="list-style-type: none"> Companies would now be able to select the technology used and be required to disclose that technology for investors to determine whether that technology was appropriate.
6. Reconsider the concept of reasonable certainty?	<ul style="list-style-type: none"> Propose to define the term as “much more likely to be achieved than not” under a deterministic or probabilistic method. Reasonable certainty under a probabilistic method means that there is at least a 90 percent probability that the quantities actually recovered will equal or exceed the stated volume.
7. Reconsider the concept of certainty with regard to proved undeveloped reserves?	<ul style="list-style-type: none"> Propose to define proved undeveloped reserves as reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion.
8. Reconsider the concept of economic productability?	<ul style="list-style-type: none"> Propose term to mean, “a resource which generates revenue that exceeds, or is reasonably expected to exceed, the costs of the operation.”

SEC CONCEPT RELEASE ISSUE	PROPOSED RULES
9. Reconsider the concept of existing operation conditions?	<ul style="list-style-type: none"> No change proposed.
10. Should we require or allow companies to use an average price instead of a fixed price, or a futures price instead of a spot price?	<ul style="list-style-type: none"> Propose to change the price used in calculating reserves from a single-day closing price measured on the last day of the company's fiscal year to an average price for the 12 months prior to the end of the company's fiscal year. Will add a disclosure item to permit a company, at its option, to include a sensitivity case analysis.
11. Consider eliminating any of the current exclusions from proved reserves?	<ul style="list-style-type: none"> The proposed definition would state that oil and gas-producing activities include the extraction of marketable hydrocarbons, in the solid, liquid or gaseous state, from oil sands, shale, coal beds or other nonrenewable natural resources, which can be upgraded into natural or synthetic oil or gas.
12. Consider eliminating any of the current exclusions from oil and gas activities and/or consider eliminating the current restrictions on including oil and gas reserves from sources that require further processing?	<ul style="list-style-type: none"> Consistent with the answer above in Item 11. Would continue to exclude activities relating to transporting, refining, processing; the production of natural resources other than oil, gas or natural resources from which natural or synthetic oil and gas can be extracted; and the production of geothermal steam.
13. What aspects of technology should be considered in evaluating a disclosure framework?	<ul style="list-style-type: none"> Must be consistent with definition of "reliable technology"- expressed in realistic terms, has been proved empirically to lead to correct conclusions in over 90 percent of its applications.
14. Consider requiring companies to engage an independent third party to evaluate their reserves estimates in the filings	<ul style="list-style-type: none"> Will not propose to require an independent third party. Will require disclosure regarding the qualifications of the person responsible for preparing reserves estimates.

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