

Saskatchewan Oil and Gas Orphan Fund Annual Report 2023-24

Ministry of Energy and Resources

saskatchewan.ca



Letters of Transmittal



The Honourable Jim Reiter
Minister of Energy and
Resources

Office of the Lieutenant Governor of Saskatchewan

I respectfully submit the Saskatchewan Oil and Gas Orphan Fund Annual Report for the Ministry of Energy and Resources for the fiscal year ending March 31, 2024.

A handwritten signature in blue ink, appearing to read 'Jim Reiter', written over a faint, light blue rectangular stamp.

Jim Reiter
Minister of Energy and Resources



Blair Wagar
Deputy Minister of the
Ministry of Energy and
Resources

The Honourable Jim Reiter
Minister of Energy and Resources

Dear Minister:

I have the honour of submitting the Saskatchewan Oil and Gas Orphan Fund Annual Report for the Ministry of Energy and Resources for the fiscal year ending March 31, 2024.

A handwritten signature in blue ink, appearing to read 'Blair Wagar', written over a faint, light blue rectangular stamp.

Blair Wagar
Deputy Minister of Energy and Resources

Manager's Responsibility for Financial Statements

The Oil and Gas Orphan Fund Annual Report for the fiscal year ending on March 31, 2024, and the accompanying financial statements, are the responsibility of the management of the Ministry of Energy and Resources. Management has prepared the financial statements in accordance with Canadian public sector accounting standards. The financial information captured in this annual report is consistent with that in the financial statements.

To ensure the integrity and objectivity of the financial data, management maintains a comprehensive system of internal controls including written policies and procedures and an organizational structure that segregates duties. These measures provide reasonable assurance that transactions are recorded and executed in compliance with legislation and required authority, that assets are properly safeguarded and that reliable financial records are maintained.

The financial statements have been audited by the Office of the Provincial Auditor. The Provincial Auditor's Report to the Members of the Legislative Assembly states the scope of its examination and opinion on the financial statements, which can be found on page 8.



Blair Wagar
Deputy Minister of Energy and Resources

Introduction

The Saskatchewan Oil and Gas Orphan Fund (Orphan Fund) was established in legislation in June 2007 following extensive consultation with oil and gas industry associations and other stakeholders. The consultative process led to the development of a comprehensive and robust set of regulations and the Orphan Fund Procurement Program that is fully funded and supported by the oil and gas industry.

Funding is provided through the Orphan Fund to address the costs of abandoning and decommissioning orphan wells and facilities and reclaiming the sites, as well as the costs of containing environmental emergencies arising from oil and gas operations. The Orphan Fund receives revenue primarily through an annual Orphan Fund Levy that is paid by the oil and gas industry, thereby protecting taxpayers from exposure to these industry liabilities.

The legislative authority and specific provisions of the fund are found in *The Oil and Gas Conservation Act* and the regulations thereunder.

The Orphan Fund is administered by the Saskatchewan Ministry of Energy and Resources (the ministry).

Program Purpose

An orphan oil well is one where the licensee or owner of the well has ceased to exist due to insolvency or bankruptcy. The Orphan Fund was established as a means to pay for the costs associated with the abandonment and reclamation of orphan wells and facilities. The fund is capitalized through an annual Orphan Fund Levy paid by oil and gas companies. The Orphan Fund Procurement Program ensures that costs of abandoning and reclaiming orphan sites are not passed on to Saskatchewan taxpayers.

Program Mandate

The Saskatchewan Oil and Gas Orphan Fund mandate is to abandon and reclaim orphaned upstream oil & gas sites to its original land use in a safe and cost-efficient manner while holding public safety and the environment in the highest regard. The work allows for municipalities and landowners to utilize the lands for farming practices and recreational purposes.

Progress on Program Activities

During the 2023-24 fiscal year, the ministry invoiced the oil and gas industry \$10 million (M) in its annual orphan fund levy. The ministry also carried out approximately \$12.67M in abandonment and reclamation work tied to orphan sites. This included:

- abandonment of 83 wells;
- 248 environmental site assessments;
- 271 reclamation projects; and,
- 77 applications for Acknowledgement of Reclamation (AOR) as part of final site closure.

For the 2024-25 fiscal year, the ministry is forecasting to complete approximately 150 orphan well abandonments and approximately 500 site assessment and reclamation projects.

Risk Analysis

In order to reduce the risk and potential cost to the Orphan Fund, the ministry administers the Licensee Liability Rating (LLR) program in parallel with the Orphan Fund Procurement Program. The purpose of the LLR program is to backstop the Orphan Fund through the collection of security deposits from companies that may pose a higher risk to the fund in the event of insolvency. The security deposits are used to offset the cost to the fund of abandoning and reclaiming well and facility sites should the owner become insolvent.

Under the LLR program, each oil and gas company operating in Saskatchewan is rated numerically using the LLR system. The LLR is the ratio of a company's assets to liabilities. The asset value used in the formula is the production value from the company's operations. The liabilities are a company's total future cost to decommission all infrastructure and reclaim their sites. Companies whose rating is greater than 1.0 are considered to have assets greater than its liabilities and therefore pose a lower risk to the fund in the event of an insolvency. In contrast, those with a rating of less than 1.0 have assets less than its liabilities and are considered a higher risk to the fund in the event of an insolvency. Under the LLR program, operators with a rating of less than 1.0 are required to submit a security deposit to offset the risk posed to the fund.

As noted, the security deposits collected under the LLR program are intended to mitigate the potential risks to the fund posed by companies with an LLR less than 1.0. Figure 1, found on the following page (current to March 31, 2024), shows the number of companies in this category has decreased by almost half over the last decade. This is a good trend as it illustrates that the number of companies at a higher risk of insolvency has been reduced. The number of companies in this category collectively represent about 2.15 per cent of total provincial oil and gas liabilities and about 0.09 per cent of total provincial production value.

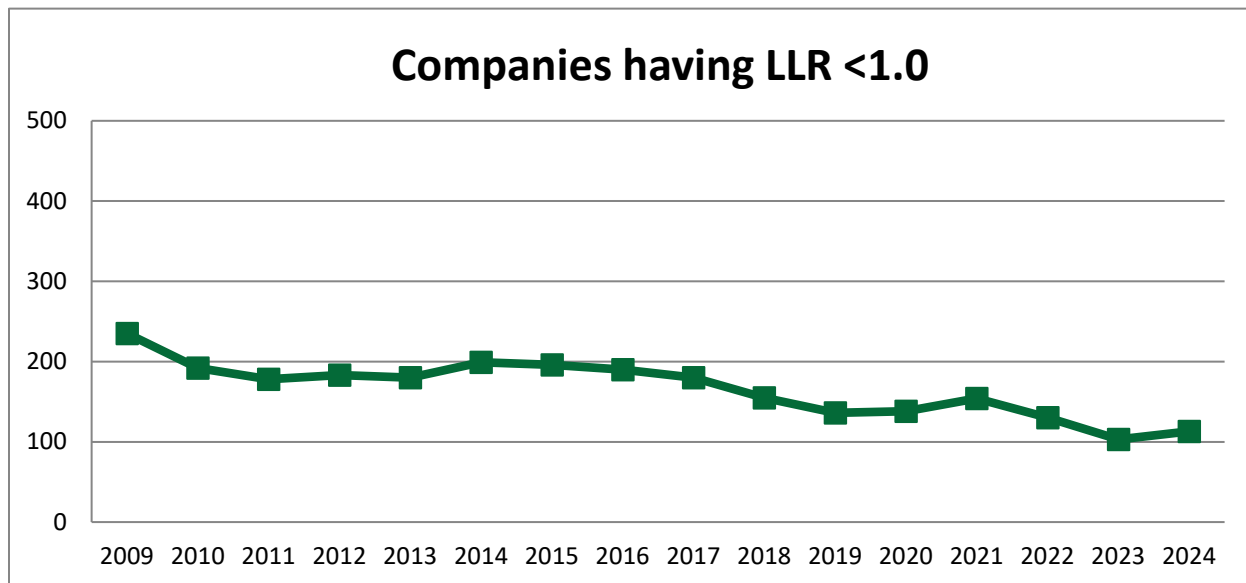


Figure 1 - Number of Companies with LLR Below 1.0

The number of companies with an LLR greater than or equal to 1.0 decreased from 141 in fiscal year 2022-23 to 137 in 2023-24 fiscal year. Companies with an LLR greater than or equal to 1.0 represent approximately 97.85 per cent of total provincial oil and gas liabilities and about 99.9 per cent of total provincial production value.

Figure 2, found on the follow page, shows that the average provincial LLR has steadily declined since the inception of the program except over the 2022-23 fiscal year where it increased from about 3.0 to about 7.5 (due to the change to the new Enhanced LLR which was introduced in February 2023). The decline can be attributed to the decline in oil prices from the high prices seen in 2022. Though the provincial LLR declined from the 2022-23 fiscal year, an industry average LLR of approximately 6.02 still shows that the oil and gas industry is generally quite healthy and should be able to meet its obligations in terms of asset retirement and closure.

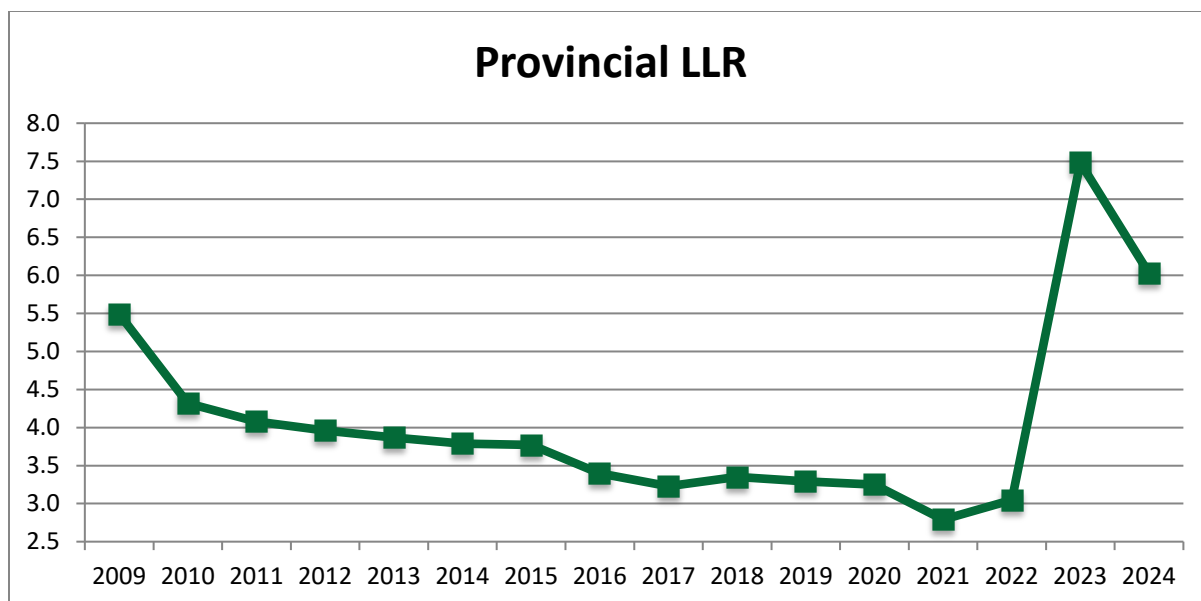


Figure 2 - Average Provincial LLR

As of March 2024, the ministry was holding \$82.73M in security under the LLR program. The total liability associated with licensees having an LLR less than 1.0 was \$90.83M. On balance, the security deposits held by the ministry, together with the assets of these companies, are expected to be sufficient at the aggregate level to address risks to the fund stemming from any future insolvencies. However, there remains a risk that for any particular insolvency, these amounts may not be enough to cover the actual cost of abandoning and reclaiming orphan sites. Any shortfall related to these costs is offset by the orphan fund capitalized through the annual levies paid by the oil and gas industry.

In addition to the LLR program, the ministry has taken several actions to mitigate risks to the orphan fund associated with increased industry liabilities. This includes:

- **Inactive Liability Reduction Program:** a new results-based program that requires all oil and gas licensees to meet annual spend targets for the decommissioning and closure of inactive wells and facilities. Licensees were given a 2023 target of five per cent of their inactive liabilities. In 2023, Industry retired 11.5 per cent of the provincial deemed inactive liabilities based on reported expenditures.
- **Corporate Financial Information:** licensees are required to submit corporate financial information annually and when requested by the ministry. This submission is used in conjunction with the LLR program to evaluate licensees' financial capacities to meet their asset retirement obligations and evaluate their risk to the orphan fund.
- **Proportional Risk Assessments for Transfers:** codification in regulations of a highly effective methodology for determining the additional security required for transfers between licensees that involve a high percentage of inactive wells and facilities.

The ministry's work in managing risks to the orphan fund has also been supported by the January 2019 decision of the Supreme Court of Canada in the *Redwater* case. This decision affirmed that industry liabilities are given priority in the sale of any assets stemming from receiverships and bankruptcies.

Oil and Gas Orphan Fund Financial Statements

OIL AND GAS ORPHAN FUND

FINANCIAL STATEMENTS

For The Year Ended March 31, 2024



INDEPENDENT AUDITOR'S REPORT

To: The Members of the Legislative Assembly of Saskatchewan

Opinion

We have audited the financial statements of the Oil and Gas Orphan Fund, which comprise the statement of financial position as at March 31, 2024, and the statement of operations and accumulated surplus, and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Oil and Gas Orphan Fund as at March 31, 2024, and the results of its operations, and its cash flows for the year then ended in accordance with Canada public sector accounting standards.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Oil and Gas Orphan Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian public sector accounting standards for Treasury Board's approval, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Oil and Gas Orphan Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Oil and Gas Orphan Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Oil and Gas Orphan Fund's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Oil and Gas Orphan Fund's internal control.



- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Oil and Gas Orphan Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Oil and Gas Orphan Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control identified during the audit.

Regina, Saskatchewan
July 18, 2024

Tara Clemett, CPA, CA, CISA
Provincial Auditor
Office of the Provincial Auditor

OIL AND GAS ORPHAN FUND
STATEMENT OF FINANCIAL POSITION
As at March 31

| | <u>2024</u> | <u>2023</u> |
|--|----------------------------|---------------------------|
| FINANCIAL ASSETS | | |
| Due from General Revenue Fund (Note 5) | \$34,812,593 | \$5,691,166 |
| Accounts Receivable | 370,952 | 308,549 |
| Interest Receivable | <u>692,942</u> | <u>883,320</u> |
| Total Financial Assets | <u>35,876,487</u> | <u>6,883,035</u> |
| LIABILITIES | | |
| Accounts Payable | <u>101,365</u> | <u>77,523</u> |
| NET FINANCIAL ASSETS AND ACCUMULATED SURPLUS (Statement 2) (Note 3) | <u><u>\$35,775,122</u></u> | <u><u>\$6,805,512</u></u> |

(See accompanying notes to the financial statements)

OIL AND GAS ORPHAN FUND
STATEMENT OF OPERATIONS AND ACCUMULATED SURPLUS
Year Ended March 31

| | <u>Budget</u> | <u>Actual</u> | |
|--|-------------------------|----------------------------|----------------------------|
| | <u>2024</u> (Note 8) | <u>2024</u> | <u>2023</u> |
| REVENUES: | | | |
| Levies (Note 6) | \$15,000,000 | \$10,000,000 | \$ 8,501,015 |
| License Application Fees (Note 6) | --- | --- | 90,000 |
| Forfeited Security Deposits (Note 6) | --- | 28,267,931 | --- |
| Abandonment and Reclamation proceeds | --- | 329,591 | 677,330 |
| Interest (Note 5 & 6) | 200,000 | 3,053,375 | 2,315,467 |
| Other Revenue | <u>---</u> | <u>100</u> | <u>---</u> |
| Total Revenues | <u>15,200,000</u> | <u>41,650,997</u> | <u>11,583,812</u> |
| EXPENSES: | | | |
| Abandonment and Reclamation | 14,670,000 | 10,558,792 | 10,816,811 |
| Other Costs (Note 7) | <u>55,000</u> | <u>2,122,595</u> | <u>71,789</u> |
| Total Expenses | <u>14,725,000</u> | <u>12,681,387</u> | <u>10,888,600</u> |
| ANNUAL SURPLUS (DEFICIT) | <u>\$ 475,000</u> | 28,969,610 | 695,212 |
| ACCUMULATED SURPLUS, BEGINNING OF YEAR | | <u>6,805,512</u> | <u>6,110,300</u> |
| ACCUMULATED SURPLUS, END OF YEAR to Statement 1 | | <u><u>\$35,775,122</u></u> | <u><u>\$ 6,805,512</u></u> |

(See accompanying notes to the financial statements)

**OIL AND GAS ORPHAN FUND
STATEMENT OF CASH FLOWS
Year Ended March 31**

| | <u>2024</u> | <u>2023</u> |
|--|---------------------|---------------------|
| OPERATING TRANSACTIONS | | |
| Cash Received From: | | |
| Levies | \$9,973,887 | \$ 8,501,239 |
| License Application Fees | --- | 90,000 |
| Forfeited Security Deposits | 28,267,931 | --- |
| Abandonment and Reclamation proceeds | 293,311 | 364,061 |
| Interest | 3,243,753 | 1,471,481 |
| Other Revenue | <u>90</u> | <u>---</u> |
| Total Cash Received | <u>41,778,972</u> | <u>10,426,781</u> |
| Cash Paid For: | | |
| Abandonment and Reclamation | 10,534,950 | 11,103,037 |
| Other Expenses | <u>2,122,595</u> | <u>152,088</u> |
| Total Cash Paid | <u>12,657,545</u> | <u>11,255,125</u> |
| INCREASE (DECREASE) IN CASH | 29,121,427 | (828,344) |
| CASH, BEGINNING OF YEAR | <u>5,691,166</u> | <u>6,519,510</u> |
| DUE FROM GENERAL REVENUE FUND | <u>\$34,812,593</u> | <u>\$ 5,691,166</u> |

OIL AND GAS ORPHAN FUND
NOTES TO THE FINANCIAL STATEMENTS
March 31, 2024

1. Authority

The Oil and Gas Environmental Fund was established on May 17, 1989, pursuant to Section 18.2 of *The Oil and Gas Conservation Regulations, 1985* (Regulations). The Oil and Gas Environmental Fund originated through a one-time assessment of \$100 per well to a maximum of \$20,000 per operator.

In June 2007, an amendment was made to the *Oil and Gas Conservation Act* (Act) that provided for the continuance of the existing Oil and Gas Environmental Fund as the Oil and Gas Orphan Fund (fund) (Order in Council #442/2007). The purpose of the fund is to address the issue of abandonment of wells, decommissioning of facilities, and clean-up of those wells and facilities where the obligations of the person responsible for carrying out those activities are not being met.

2. Significant Accounting Policies

Pursuant to Canadian Public Sector Accounting Standards, the fund is classified as a government component. These financial statements are prepared in accordance with Canadian public sector accounting standards. These financial statements do not present a statement of changes in net financial assets as the fund does not hold any non-financial assets. The fund did not have any re-measurement gains and losses; therefore, a statement of re-measurement gains and losses has not been provided.

- a) The fund recognizes orphan fund levies as revenue when the levies are assessed.
- b) The fund recognizes forfeited security deposits as revenue when the Minister declares them forfeited to the Crown in the right of Saskatchewan (see Note 6).
- c) The fund recognizes salvage proceeds from abandonment activities as revenue when the licensee fails to cover the costs of carrying out the activities on the site.
- d) The fund recognizes the costs to carry out the abandonment or decommissioning on the site from the licensee, working interest owners or any other person whom the minister considers responsible for the well, facility, flowline and their respective sites.
- e) Interest is earned monthly and received quarterly.

These standards require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates. Differences are reflected in current operations when identified.

The following new accounting standards came into effect April 1, 2023:

- PS 3400 Revenue
- PS3160 Public Private Partnerships
- PSG-8 Purchased Intangibles

The adoption of these standards does not have a material impact on these financial statements.

3. Net Financial Assets

Under section 7-1 of the *Financial Security and Site Closure Regulations* the net financial assets, together with any future recoveries of well site restoration costs, are available to provide for expenditures for the purposes of:

- a) abandonment of wells, flowlines and facilities and restoration of those sites, as a result of disappearance or insolvency of the well owner or operator.
- b) containment or clean-up of major environmental problems arising from oil and gas exploration, development, production or transportation operations.
- c) to pay for technical, administrative, legal or other costs incurred in pursuing reimbursement for the costs mentioned in a) and b) from the person responsible for paying them.
- d) to pay for a defunct working interest participant's share of abandonment and reclamations costs if those costs were incurred by a working interest participant of the defunct party.

4. Financial Instruments

The fund's financial instruments include Due from General Revenue Fund, accounts receivable, interest receivable and accounts payable. These are recorded at fair value. The carrying amount of these financial instruments is of approximate fair value due to their immediate or short-term maturity. The Fund is exposed to credit risk from the potential non-payment of accounts receivable. These instruments have no interest rate risk, liquidity risk or market

risk. The valuation allowance for doubtful accounts at the end of March 31, 2024 was \$387,305 (2023- \$387,440).

5. Related Party Transactions

Included in these financial statements are transactions with ministries and agencies related to the fund by virtue of common control by the Government of Saskatchewan. A related party exists when one party can exercise control or share control over the other. Two or more parties are related when they are subject to common control or shared control. Related parties also include key management personnel, their close family members and entities controlled by, or under shared control of, any of these individuals.

The fund's revenue and cash security deposits (Note 6) are deposited to the General Revenue Fund (GRF). These funds are included in the Consolidated Offset Balance Concentration (COBC) account held by the GRF and the fund receives interest quarterly. Participation in the COBC arrangement means that the interest on the bank account comes from the GRF rather than from a financial institution. The interest is based on the government's 30-day borrowing rate, which is calculated and paid by the Ministry of Finance. The fund earned \$3,053,375 in interest in 2023-24 (2023 - \$2,315,467). The Government's average 30- day borrowing rate for 2023-24 is 4.89%. (2023 2.89%).

The fund has not been charged with administrative costs and no provision for such costs is reflected in these statements. These costs are borne by the Ministry of Energy and Resources.

6. Levies and Security Deposits

Section 16 of *The Oil and Gas Conservation Regulations, 2012* required all first-time applicants for a well or upstream facility licensee to pay a one-time fee of \$10,000 which is deposited into the fund. Effective January 1, 2023 the new *Financial Security and Site Closure Regulations (FSSCR)* came into force eliminating the one-time fee of \$10,000. The enhanced Licensee Liability Rating (LLR) program features an updated LLR formula that better reflects a licensee's true assets and liabilities to calculate a more accurate, licensee-specific netback.

To pay the costs to abandon and reclaim orphaned liabilities, the Saskatchewan Orphan Fund Levy was established. Each licensee in the province is levied, in accordance with the Regulations, on an annual basis to pay a percentage of a budget to carry out an annual orphan abandonment and reclamation program. Section 119 of the Regulations provides the details of how the levy was calculated for each licensee.

In addition, under the Licensee Liability Rating Program, the Minister in accordance with the Act and the FSSCR Regulations may require security

deposits from holders of oil and gas licenses for the purpose of ensuring that they can meet their obligations with respect to suspension, abandonment, restoration, remediation, or reclamation of wells and upstream facilities and sites.

The cash security deposits, and irrevocable letters of credit are held on behalf of holders of oil and gas licenses and are not included in the financial statements of the fund. On March 31, 2024, the fund held irrevocable letters of credits from the holders of oil and gas licenses consisting of \$62,386,032 (2023 - \$65,039,152) and security deposits held in the Province's GRF of \$20,345,453 (2023 - \$72,167,773). As of March 31, 2024, an additional \$23,828,533 in security deposit amounts are to be provided by companies in either cash or irrevocable letters of credit.

As a licensee's liability rating improves, the cash may be refunded to the licensee. The licensees were notified in writing that interest will not be calculated or paid on security deposits.

If the criteria of the Act and FSSCR Regulations are not met, the security deposits may be forfeited fully or partially and deposited into the fund.

All 2023-24 revenues are re-occurring, however forfeited security deposits proceeds may fluctuate significantly each year.

7. Other Expenses

The fund has been charged with administrative costs in the form of legal fees relating to the receivership of Abbey Resources Corp.

8. Budget

The budget for the fund is included with the Ministry of Energy and Resources budget submission to Treasury Board. Treasury Board approves the fund's budget annually.