Orphan Well Association

ANNUAL REPORT 2019

Contents

Our Vision and Mandate

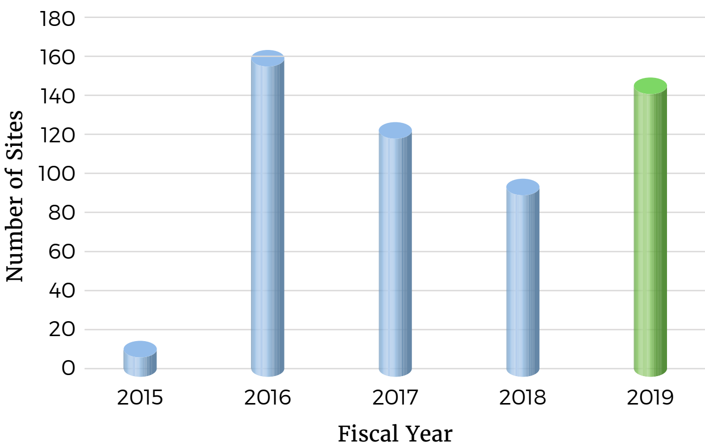
The Orphan Well Association began as an innovative collaboration among the Alberta Government, provincial regulators and the oil and gas industry to work toward a common goal: protecting public safety and managing the environmental risks of oil and gas properties that do not have a legally or financially responsible party that can be held to account. These properties are known as "orphans."

The mandate of the OWA is to safely decommission orphan oil and gas wells, pipelines and production facilities, and restore the land similar to its original state. Since its formation in 2002, the OWA has successfully decommissioned approximately 3,100 orphan wells, with 940 sites reclaimed.

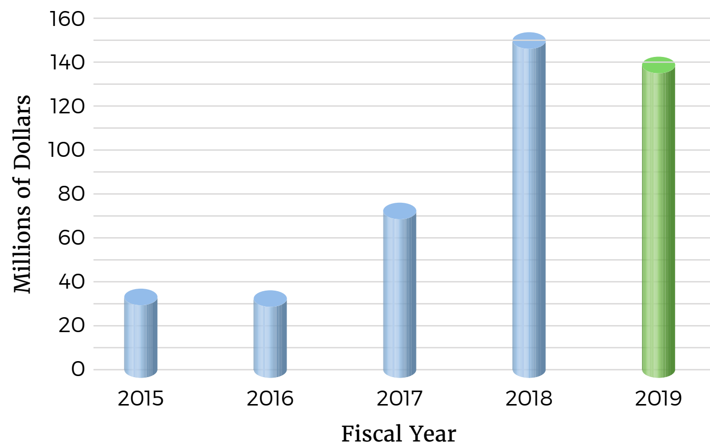
This Annual Report contains forward-looking statements based on current expectations, estimates, projections and assumptions, and certain operating and financial measures. By the nature of its mandate and work, there are potential impacts to the organization's future operations and related finances that the OWA cannot predict. Where expressed, forward-looking statements are provided in the interest of context that stakeholders may find useful. The OWA fiscal year is from April 1 to March 31. For this annual report, years are referenced as the first year; that is, 2019 refers to April 1, 2019 through March 31, 2020.

Highlights

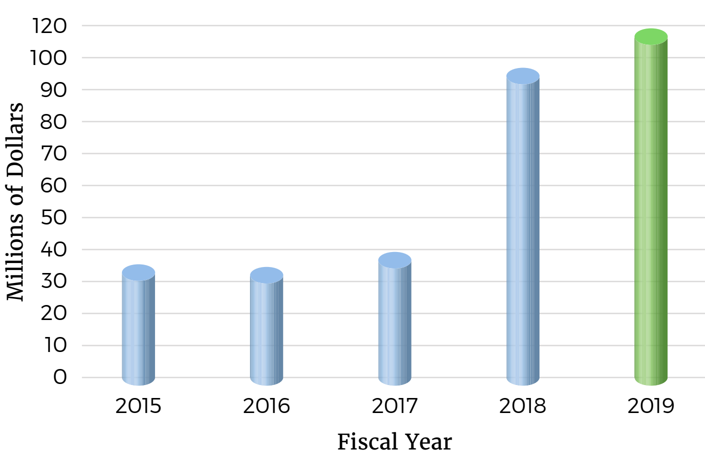
NUMBER OF SITES RECLAIMED AND CLOSED



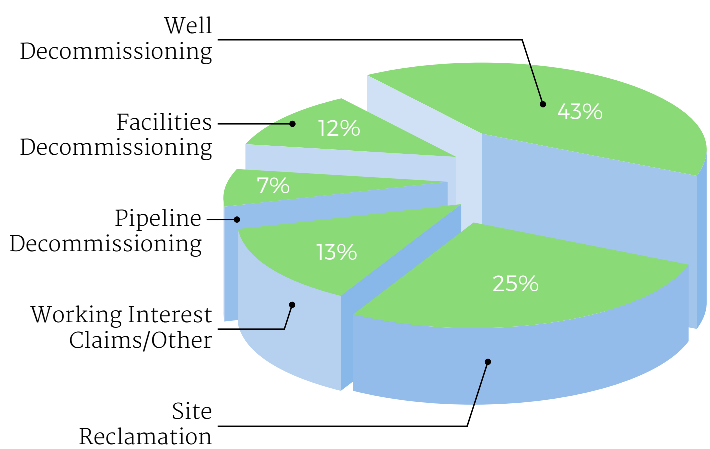
FUNDING



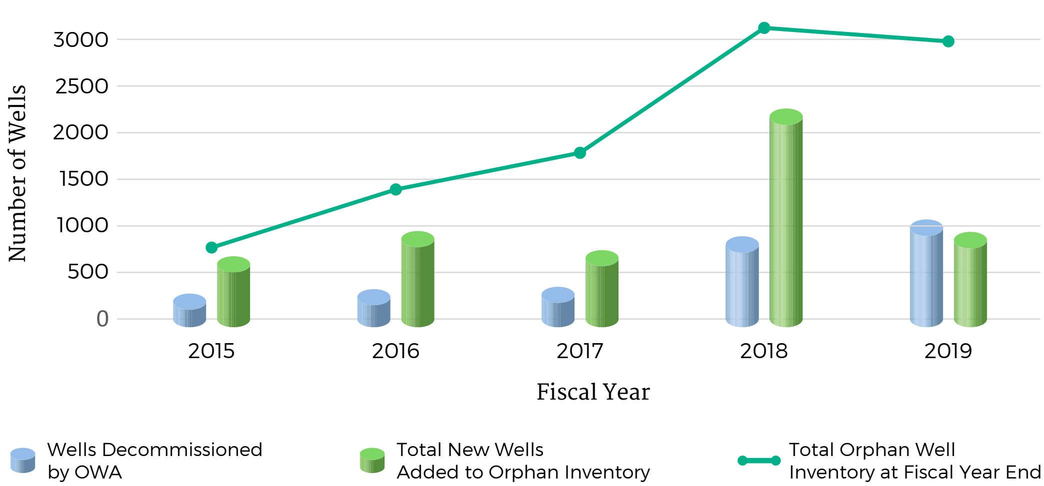
OPERATING EXPENDITURES BY FISCAL YEAR



2019 OPERATING EXPENDITURES BY CATEGORY



ORPHAN WELL INVENTORY AND WELLS DECOMMISSIONED



Overall funding for the OWA decreased in 2019 due to how the Government of Alberta loan, announced in 2017 and provided over three years, is structured. All other funding increased in 2019. The OWA increased its operational activities and, as a result, the orphan well inventory decreased. There was also an increased number of sites reclaimed and closed. The reclamation process takes several years as vegetation grows and sites become ready for the detailed site assessment required for a reclamation certificate application.

The Year in Perspective

Message from the Chair

Investment in the oil and gas industry has long been a leading indicator of prosperity for Alberta—and for all of Canada. The work of the Orphan Well Association is, frankly, more often a trailing indicator of the health of our provincial and national economies and our domestic energy industry. When our economic engine begins to slow, we see the results in our work.

We have certainly seen in the past five years some difficult times for many energy producers. It's a resilient industry, and oil and gas price cycles are nothing new, but we have experienced sustained low commodity prices over a long period, with less access to capital, and some companies have struggled to recover. This ultimately led to several insolvencies and a significant increase in our orphan well inventory in 2018. It was, however, an increase for which we were well prepared, with more funding from industry and a ramped-up mobilization plan. Critically, that accelerated work was supported by a repayable loan from the Government of Alberta to help cover near to mid-term costs, and a grant from the Government of Canada to cover interest charges on this loan.

Although 2019 was a strong year for the OWA's results on the ground, the economic context has remained difficult for the energy industry for now, and likely for the next few years which has a direct impact on our plans.

Our last fiscal quarter—January to March of 2020—saw the Saudi-Russia price war that dragged benchmark WTI prices down by half and the Western Canada Select benchmark below $5 per barrel. This price shock was compounded with the alarming spread of the COVID-19 virus. This pandemic has had the doubly deleterious effect of throwing uncertainty on our planning as we focus on safety close to home, as well as the impact of reduced energy demand in an over-supplied global market in the mid-term. Although the price war looks, at the time of this writing, to be heading toward resolution, these factors have had the collective effect of reducing capital spending plans in the energy industry. This, in turn, reduces direct and indirect jobs, and may also ultimately impact OWA budgets, as we are funded based on a levy on every oil and gas producer in Alberta.

In response to these extraordinary circumstances, we have seen extraordinary efforts from the OWA management, staff experts and contractors. And very importantly, we have seen the governments of Alberta and Canada continue to step up to support our work.

In early March of 2020, the Province committed $100 million in new, repayable loans to the OWA. This available funding is in addition to a staged loan of $235 million announced in 2017.

Along with loans, the OWA has also been supported by the Government of Alberta's passage of Bill 12, which updates and expands our mandate to better manage current challenges as our project closures have gone from single digits per year to nearly a thousand. The new legislation provides additional scope and authority as we work on the operational and financial management of sites that range from those that are economically viable to those that are truly at end of life, often within the same company. I believe the new tools and flexibility we have will help the OWA team to manage ongoing work safely, efficiently and effectively.

In addition to provincial funds and legislative support, the federal government has also stepped up to support the energy sector with a $1.7 billion commitment for decommissioning and reclamation, which includes a $200 million repayable loan to the OWA. This investment in an industry that has invested so much in Canada is timely and appreciated by working people in every corner of Alberta, not just in the energy industry, but in all the businesses, large and small, that support our work.

In our current context, we need to manage our orphan well inventory, the safety of our workers and communities, our shared environment, and the very important need to get Albertans working. The expanded work of the OWA with industry and government support is the very definition of a "win-win."

Orphan wells that range from nuisances for landowners to potential environmental risks will be decommissioned at a faster rate and the reclamation work advanced, while a significant fiscal stimulus will be pumped into communities across the province where front-line energy employees live and work.

The same skilled workforce that has driven a very professional "business-as-usual" in our industry is well prepared to take on "business-as-unusual". Over 2019, we saw steady or increased spending on decommissioning, remediation and reclamation in most regions of the province and, with additional industry and government funding now committed, that's a trend that we expect to continue over time.

On behalf of the operations, safety and environment experts who deliver results for the Orphan Well Association across Alberta, we thank you for your support. With the guidance of the OWA's Board of Directors, the Alberta Energy Regulator that oversees our efforts and the industry members that share learnings and fund us, we have been hard at work.

We have met extraordinary challenges over the past year—and we remain strong, capable and ready to meet the challenges going forward.

Brad Herald
Chair, OWA

Message from the Executive Director

Over the past year, the OWA continued to build momentum, decommissioning more wells and completing more reclamation projects than ever before. In 2019, despite receiving a substantial number of new orphan wells—more in just one year than in 2014 to 2017 combined—we actually decreased the overall inventory with a steady and strategic approach. With our existing inventory of just under 3,000 wells, we decommissioned 982 wells in 2019—that's a third of the inventory, showing that our organization is more than capable of tackling what lies ahead.

There were several drivers behind our 2019 performance. Funding from industry sources continued to increase, while the loan from the Government of Alberta allowed for additional activity in the field. With our team's growing expertise and experience, we are collaborating with other operators and fine-tuning our processes so that, simply put, we are getting the job done better, faster and at a lower cost. A substantial part of this success can be attributed to an approach that goes beyond a well-by-well basis to a regional strategy covering multiple wells and facilities known in the industry as Area Based Closure. This allows us to better leverage industry expertise, local services and economies of scale.

Better and faster can only be celebrated if it can also be done safely. One area of concern for me is injury incidents, which increased from three to five last year. Understanding the critical importance of safety, we almost doubled our safety assessments in 2019, which we expected to result in decreased injury incidents. We are disappointed that, instead, the number increased. We are steadfastly focused on investigating and reducing that number.

Taking action to protect the safety of our workers and the communities we visit took an unprecedented turn with the COVID-19 pandemic in the last quarter of our fiscal year. The pandemic began at the tail end of our winter operations as we headed into a pause in our operations when we were waiting for wet spring conditions in the field to dry up. This made it easier for us to follow the direction of health authorities for physical distancing and staying home without negatively impacting our performance in the field. The downtime was used to modify some of our procedures so that when operations can resume, they will be done safely. We believe our work is very important, but not more important than the health of our contractors and the communities where we do business.

The impact of the pandemic has, of course, also been felt economically in Alberta. The OWA will continue to support contractors during this trying time as we expect to build on a workforce impact of close to 1,600 people over the past three years to create 500 new direct and indirect jobs. Our annual spend with contractors is more than $100 million per year and growing across the province from the Peace Country and the Athabasca to the Eastern Slopes and farming and ranching communities across the province.

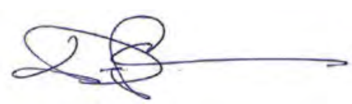
And, while we lay out plans to move quickly on decommissioning and reclamation, we are also taking all measures possible to ensure service providers are paid quickly to get money into local businesses where it means the most. Days and weeks count a lot in our current economic environment.

Looking ahead, we expect our inventories of orphan wells and reclamation sites to grow. At the same time, while we've resolved many of the easier projects in our inventory, we have some tough technical work to tackle. We continue to prepare to meet this challenge through organizational effectiveness and operational excellence. From goal setting to keep us striving forward, to end-of-project reviews so we can learn from ourselves and others, we are building our expertise and improving the "assembly line" approach to efficient decommissioning and reclamation.

We aren't alone in this work. We are also learning from our colleagues in industry, some of whom are global leaders in this type of work. We want to ensure we use the best practices to get the most bang for our buck.

We have the experience and know-how built on the foundation of a maturing organization to take care of what lies ahead. We are ready.

Underpinning all of the OWA's efforts is our relationship with our contractors—nearly 600 large and small businesses across Alberta. They are the arms and legs of the OWA and critical to how we do our job, meet our goals and perform our mandate. I would like to thank them for their hard work in 2019 and look forward to continuing our partnerships. 2020 may be the most difficult year we face as a province and an industry, but we are confident we will overcome the challenges ahead.



Lars De Pauw
Executive Director

Sometimes You Need a Plan 'Bee'

When Jeff Smitten of JSK Consulting Ltd. and his decommissioning crew arrived at the Lockwood orphan well site just outside of Wainwright the summer of 2019, they expected a typical site walk. An above-ground pipeline ran from the orphan well into a gas metering shack, where the volume of gas going into a larger pipeline was tracked. As the team approached the wooden shack to investigate the work ahead, a buzzing sound got louder and louder.

Jeff and his team had stumbled upon a colony of about 30,000 honeybees, their honeycomb filling the space between the inner and outer panels of two building walls.

"We talked to the landowner and paused the work for a few days to find a beekeeper who could safely relocate the hive," Jeff recalls. "Plus, a member of our team was allergic to bees, so we needed to be extra careful."

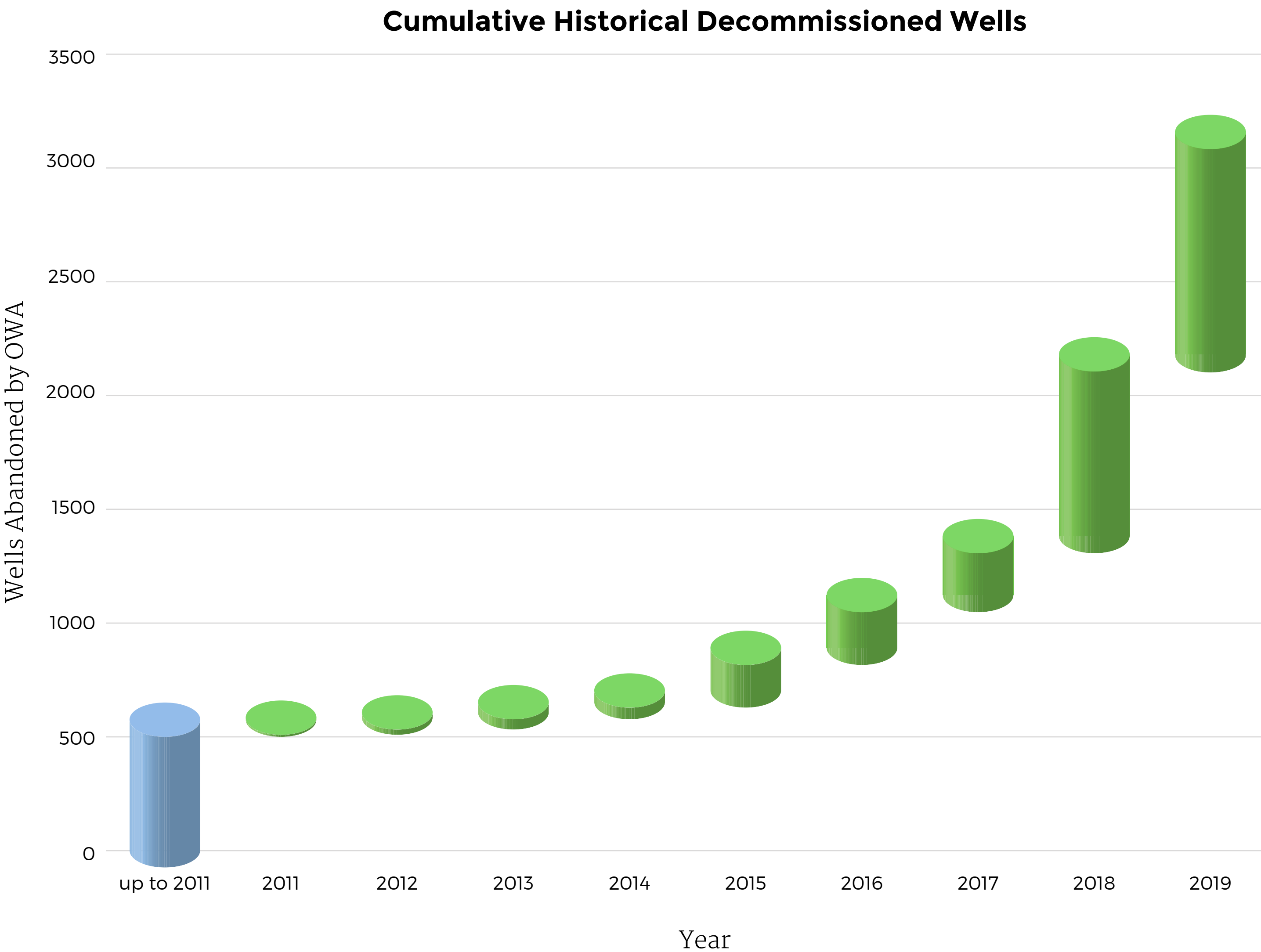
Jeff came across a couple in the area who were just starting out as honey farmers and were looking for colonies. Not only are colonies expensive, but the previous summer had been a tough one: high winds and gusts had pushed some colonies to relocate.

With Jeff in charge of site safety, the honey farmers spent two hours prying apart the building walls so they could peel and scrape the honeycombs off, using special brushes to coax the bees into their new temporary home: two bee boxes. The key was to make sure the queen bee had been transferred to one of the boxes. If she was successfully moved, then the whole hive—including the many free bees buzzing about—would join her overnight, transitioning the entire colony.

Everyone left overnight to wait and see if the bees would return to the boxes and call them home. The next day, the returning team could see the transition had been a success. The beekeepers gathered up their boxes, and the decommissioning work began.

Operational Summary

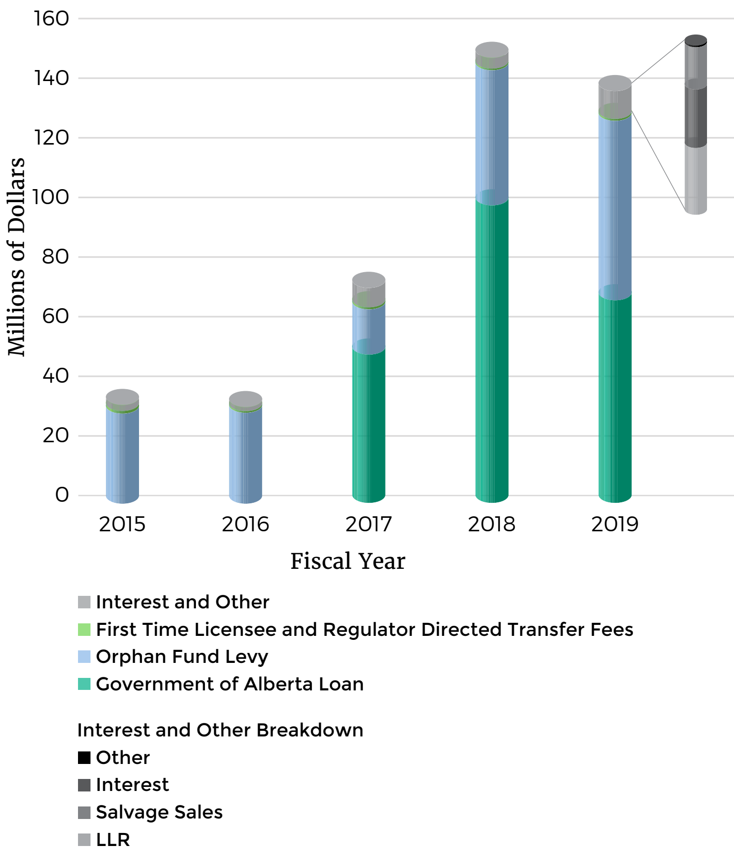
Since its inception, the OWA has been guided by our belief in a social contract, where "good neighbours" in the industry fund the clean-up for insolvent companies. Over the past several years, with the increase in our inventory, our pace of work has increased substantially, with the curve of decommissioned wells increasing with it.



The OWA is busier than ever, with a record number of projects underway. This section is a snapshot of the OWA's activities in 2019.

Overall funding for the OWA decreased in 2019 due to how the Government of Alberta loan, announced in 2017 and provided over three years, is structured. All other funding increased in 2019. The OWA increased its operational activities and, as a result, the orphan well inventory decreased. There was also an increased number of sites reclaimed and closed. The reclamation process takes several years as vegetation grows and sites become ready for the detailed site assessment required for a reclamation certificate application.

Funding the OWA



Overall funding for the OWA decreased 8% to $138.4 million in 2019, from $149.5 million the year before. This is due to the structure of a Government of Alberta loan for $235 million, provided from 2017 to 2020. Interest on this loan is covered by a $30 million grant from the Government of Canada. All other funding increased in 2019.

Typical OWA funding is provided from the Orphan Fund Levy, First Time Licensee (FTL) and Regulator Directed Transfer (RDT) fees, and interest and other sources.

The related graph shows the Orphan Fund Levy decreased in 2017; however, this is not a true representation of the trend due to the timing of when the funding was received. Historically, the financial statements showed a substantial surplus at year-end that would be used in the following fiscal year. To address this timing issue, starting in 2018, the levy was issued in April instead of March. As a result, it was accounted for in the 2018 fiscal year, causing the funding for fiscal 2017 to appear lower.

In reality, the Orphan Fund Levy provided to the OWA increased 49% to $45.4 million in fiscal 2018, from $30.4 million. The levy has continued to increase and was issued at $60 million in 2019; however, due to the insolvency of some operators, $3.4 million was not received and is written down on the OWA balance sheet as bad debt.

The Orphan Fund Levy is based on the estimated cost of decommissioning[1] and reclamation activities for the upcoming fiscal year with the goal of managing the overall inventory at an acceptable pace. The Orphan Fund Levy is set by the AER in consultation with the OWA, Canadian Association of Petroleum Producers, and Explorers and Producers Association of Canada.

First Time Licensee and Regulator Directed Transfer fees increased 9% to $634,000 in 2019, from $580,000 the year before. A First Time Licensee fee of $10,000 is required by the AER from companies applying for eligibility to hold a well, facility or

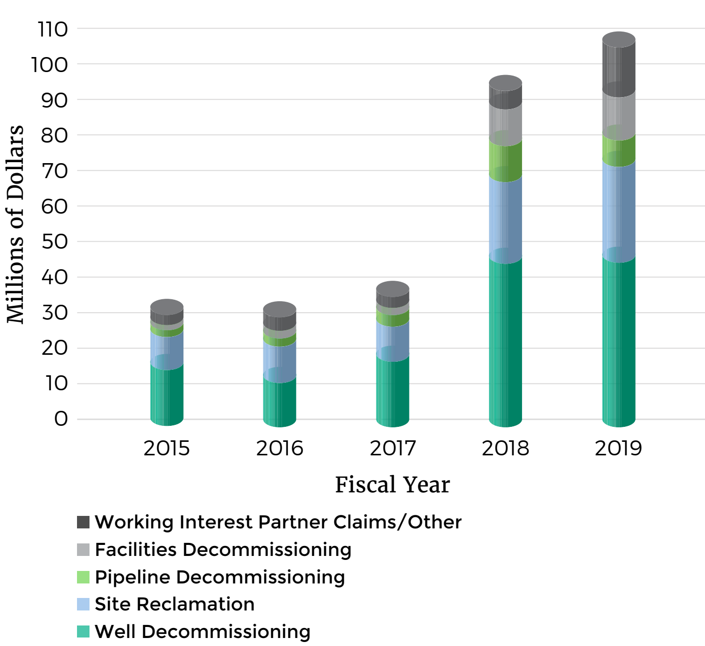
[1] *The OWA Annual Report uses the term "decommission" to refer to the responsible abandonment of energy infrastructure, in a manner that ensures it will not pose a risk to the environment or the public.*

pipeline license. The AER collects Regulator Directed Transfer fees from an active company when it acquires a property licensed to a defunct company. The AER gathers and remits these fees to the OWA.

Funding from interest and other sources increased 161% to $9.4 million from $3.6 million. This category includes salvage sales and deposits held through the Alberta Energy Regulator's (AER) Licensee Liability Rating (LLR) Program.

Salvage sales increased 191% to $2.3 million, from $780,000 the year before, due to the OWA's increased capability and focus on selling salvageable equipment. LLR funding increased dramatically to $3.7 million, from $96,000 the year before, due to work the OWA completed that was eligible for reimbursement by the AER with deposits held on behalf of various defunct companies. The LLR program assesses companies' abilities to address their decommissioning and reclamation obligations by calculating a ratio of deemed assets (oil and natural gas production) to deemed liabilities (estimated decommissioning and reclamation costs). When companies do not maintain a ratio above 1.0, the AER requires a security deposit to cover these closure costs in the event the company is not able to meet its obligations in the future. The AER remits this money to the OWA when appropriate, if the company is no longer solvent.

Operating Expenditures



The OWA's operating expenditures over the last five years are divided by well decommissioning, site reclamation, pipeline decommissioning, facility decommissioning, and reimbursement for Working Interest Partner claims and other costs, including reimbursing the AER for decommissioning work they performed in 2015.

Total OWA expenditures increased 13% to $106.6 million in 2019, from $94.4 million the year before. The increase in expenditures over the last two years is due in part to OWA receiving the loan advance from the Alberta Government, which allowed more field work to be conducted.

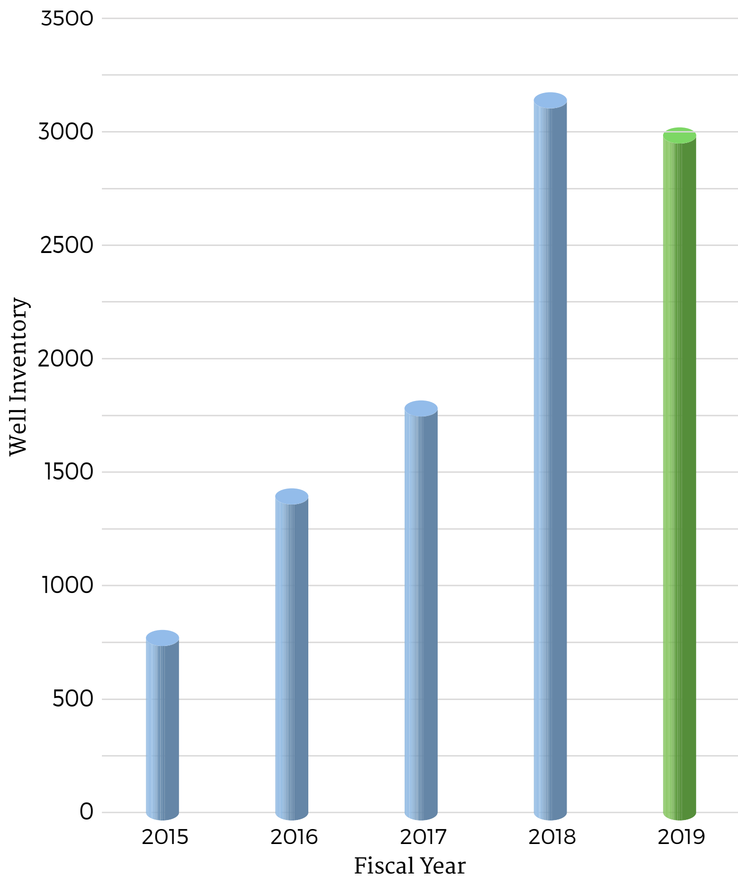
Detailed expenditures are:

- well decommissioning increased 1% to $46.2 million, from $45.9 million the year before.
- site reclamation increased 17% to $26.9 million, from $22.9 million the year before.
- pipeline decommissioning decreased 27% to $7.4 million, from $10.1 million the year before.
- facilities decommissioning increased 18% to $12.1 million, from $10.3 million the year before.
- Working Interest Partner/AER reimbursements increased 171% to $14.0 million, from $5.2 million the year before.

Working Interest Partner claims are made by active companies when they manage the decommissioning and/or reclamation of assets jointly owned with defunct partners. In these situations, the active company performs a function comparable to the OWA to properly decommission and reclaim the property. A typical project can take years for a company to complete. The OWA reimburses the active company for the defunct company's portion of the decommissioning and reclamation activities.

In fiscal 2019, working interest reimbursements were for 218 decommissioned wells, 228 reclaimed wellsites, and 9 decommissioned wells and reclaimed wellsites.

Orphan Well Inventory

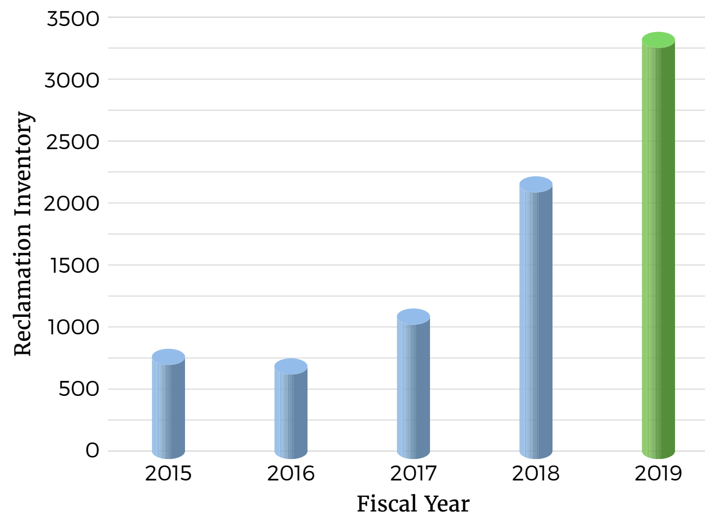


The number of orphan wells in the OWA inventory to be decommissioned decreased 5% to 2,983 at the end of fiscal 2019, from 3,128 wells at the end of fiscal 2018. The inventory number does not include orphan sites where the well has already been decommissioned and only requires remediation and reclamation.

The average cost of decommissioning a well in 2019 was $29,000, with most in the range of $8,500 to $60,000. These numbers reflect the sites that were addressed by the OWA during the fiscal year and may not be representative of all sites in the OWA inventory or those across the industry. The average cost decreased from $34,000 the year previous, demonstrating the cost benefit of bundling closure projects regionally to maximize efficiencies.

The number of new orphan wells received for decommissioning from the AER decreased 61% to 848 in 2019, from 2,170 the year before. In 2018, 1,033 Lexin Resources Ltd. wells were changed in designation from "suspension only" to "orphan," so that they then required decommissioning. There were several large insolvency processes that started during 2019, and are still underway, that prevented the orphan inventory from increasing further. The OWA expects that a large number of the assets from Trident Exploration and Houston Oil and Gas will ultimately be transferred to new responsible parties, as opposed to being designated as orphans.

Reclamation Inventory



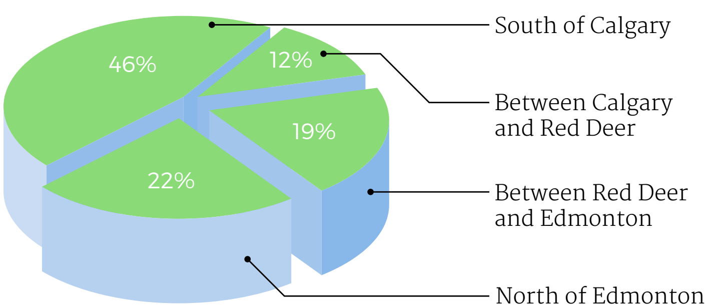
The number of sites in the OWA reclamation inventory increased 54% to 3,319 at the end of fiscal 2019, from 2,151 at the end of fiscal 2018. The reclamation inventory counts how many sites require reclamation. In many cases, there was more than one well on one site.

The average cost of reclaiming a site in 2019 was $25,000, with most in the range of $5,000 to $45,000. These numbers reflect the sites that were addressed by the OWA during the fiscal year and may not be representative of all sites in the OWA inventory or those across the industry.

The reclamation inventory increases when the OWA receives new sites—designated as orphans by the AER—that only require reclamation, and when the OWA is finished decommissioning wells, facilities and/or associated infrastructure and has transferred the sites into its reclamation inventory. The inventory decreases when the OWA receives reclamation certificates or when it is discovered that a site received by the AER requires further decommissioning operations. The inventory also decreases when a site is transferred to another oil and gas company.

Inspections

Inspections are an important activity that ensures protection of public safety and the environment. Inspection results support the OWA's risk assessment with higher risk sites being prioritized. The OWA contacts landowners or surface rights holders to notify them about the OWA and the orphan well, pipeline, facility or site to confirm land access before conducting an inspection.



In 2019, the OWA completed 1,433 site inspections throughout Alberta. 46% of these inspections were completed south of Calgary, 12% between Calgary and Red Deer, and 19% between Red Deer and Edmonton. The remaining 22% of were completed north of Edmonton.

The OWA prioritizes the inspection of new sites in its inventory to ensure they are appropriately risk-assessed and prioritized for public safety and environmental protection. Of the 1,433 sites inspected in 2019, 91% were on new orphan wells that could be assessed with a single site visit with no supplemental laboratory testing required. New site inspections requiring lab sampling, such as those with suspected surface casing vent flow or gas migration, accounted for 5% of the inspections completed. The remaining 52 site inspections were completed on long-term monitoring sites.

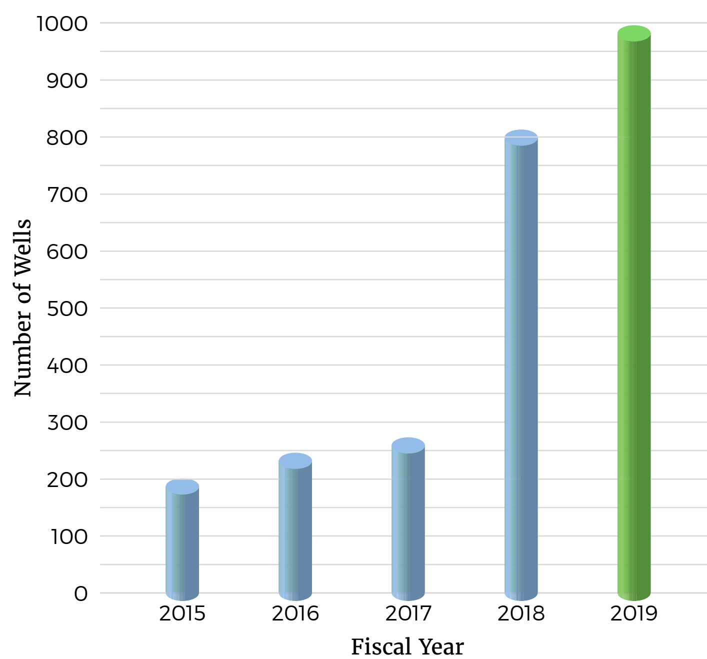
OWA SITE INSPECTIONS FOR 2019

Inspections	Count
New site inspections, routine	1,302
New site inspections, non-routine*	79
Repeat inspections/monitoring**	52
Total	**1,433**

* *New Site Inspections, Non-Routine includes sites requiring multiple visits and/or lab testing. Included are surface casing vent flow or gas migration sites.*

** *Repeat Inspections/Monitoring include return visits to confirm well repairs or inspection of long-term wells.*

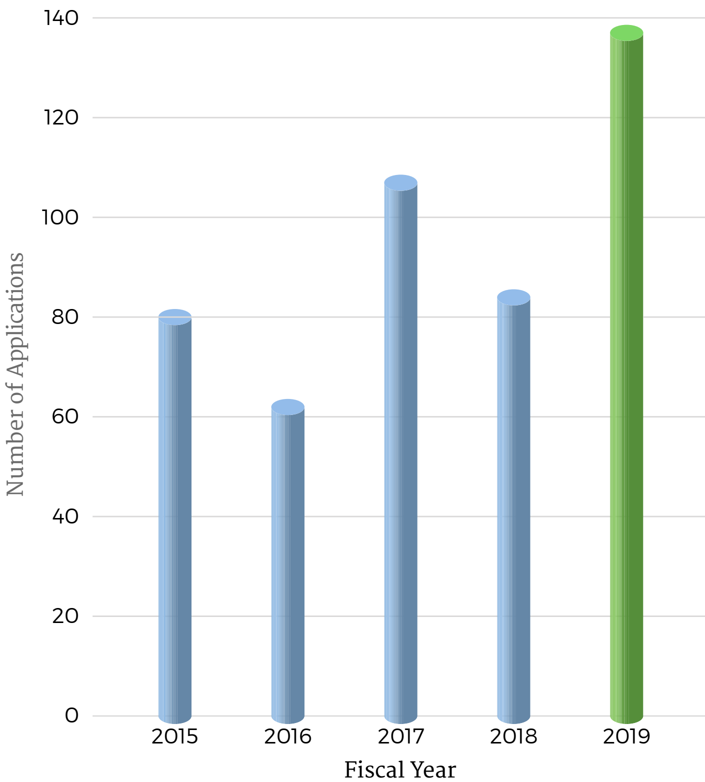
Number of Wells Decomissioned



The number of orphan wells decommissioned increased 23% to 982 in 2019, from 799 the year before. Wells include those decommissioned by the OWA and historically by the AER as an enforcement action that were subsequently designated as orphans. The AER has reduced this type of enforcement work and conducted no enforcement activities in the last four years.

A well is considered decommissioned when the AER's requirements in *Directive 020: Well Abandonment (Directive 020)* are satisfied. Once all necessary subsurface decommissioning actions are taken, the final step is to cut and cap the well. In this stage, the well casing is cut to a minimum of one metre below the surface (with some exceptions listed in *Directive 020*) and a vented cap is placed atop the well casing. At this point, remediation and/or reclamation of the site may begin.

Number of Reclamation Certificate Applications Submitted

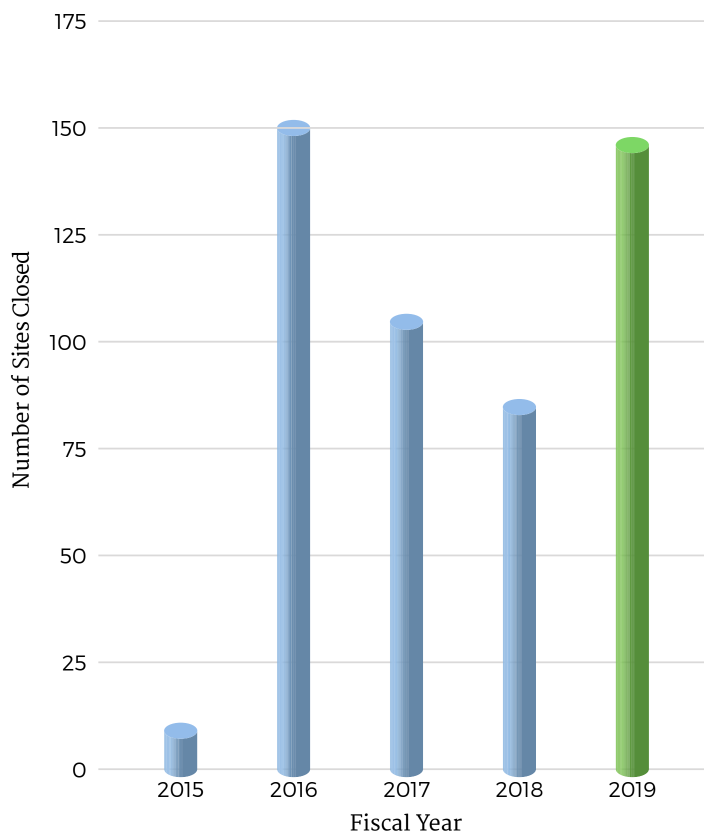


The number of orphan sites ready for a regulatory decision regarding closure is reflected in the number of applications submitted for reclamation certificates. The number of sites with applications submitted for reclamation certificates increased 63% to 137 in 2019, from 84 the year before. It takes years for a site to become suitable for a reclamation certificate application, and so this year's number reflects reclamation work performed in the last several years.

The time for a site to be ready for a reclamation certificate depends on the land use, type of vegetation and factors that affect growing conditions, such as amount of rainfall. There are several stages in the reclamation process, starting with an environmental site assessment. In 2020, the OWA had over 1,500 sites at the assessment stage. This number reflects new inventory plus sites where decommissioning has taken place.

In 2020, there were nearly 850 sites in the final stages of reclamation, including vegetation monitoring. It can take several years for sites to re-vegetate and be ready for the detailed site assessment required for a reclamation certificate application. The OWA expects to see an increase in the reclamation certificates issued next year.

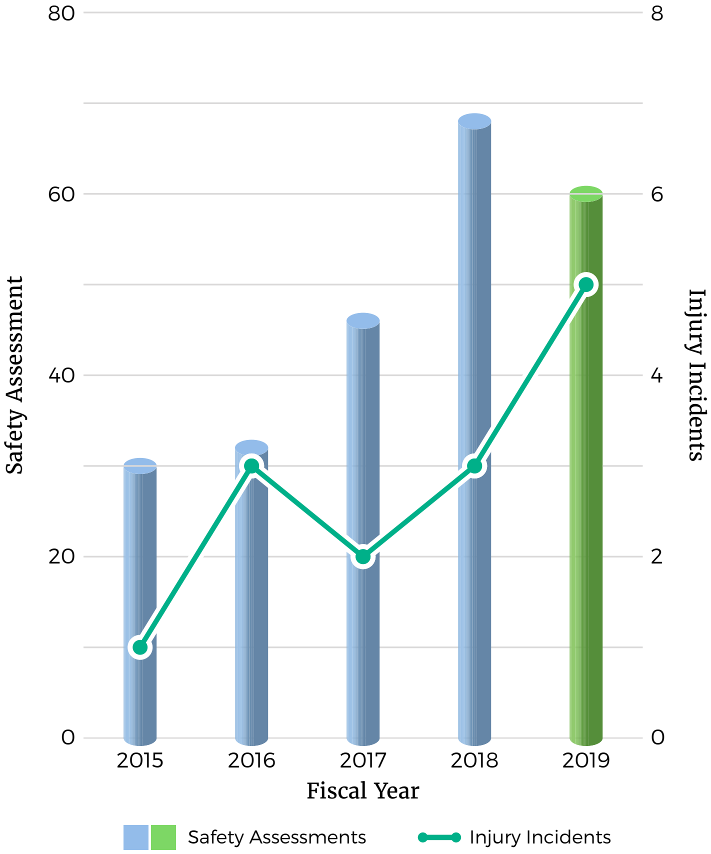
Number of Sites Closed



The number of sites the OWA closed increased 57% to 146 in 2019, from 93 the year before. Reclamation certificates peaked in 2016 when the AER introduced a new online reclamation certification system. The system, OneStop, cleared a backlog of applications, with the OWA receiving 89 reclamation certificates within a short period of time.

The increase in the number of reclamation certificates in 2019 is due, in part, to sites becoming ready for the detailed site assessment required for a reclamation certificate application.

Safety



With overall operational activity increasing in 2019, recordable injuries increased to five, from three the year before. The OWA continues to investigate these incidents and ways to reduce the number of injury incidents in the future. The OWA assesses the safety programs of its vendors and conducts site assessments to ensure safe practices are followed during operations. During 2019, there were a total of 60 safety assessments conducted on Prime Contractors. In addition to these more formal assessments, the OWA conducted 122 safety engagements, where a range of activities were undertaken to support contractors' safety performance from safety bulletins to in-person dialogue.

The OWA uses the safety benchmark of Total Recordable Injury Frequency (TRIF) to measure our field safety performance relative to the number of hours worked. In 2019 our TRIF was 1.6 based on over an estimated 614,108 contractor hours.

Jon Handforth Photography

Independent Auditor's Report

GrantThornton
An instinct for growth™

Independent Auditor's Report

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To the Members of

Alberta Oil and Gas Orphan Abandonment and Reclamation Association

Opinion

We have audited the financial statements of **Alberta Oil and Gas Orphan Abandonment and Reclamation Association** ("the Association"), which comprise the statement of financial position as at March 31, 2020, and the statements of operations, changes in net assets and 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 Alberta Oil and Gas Orphan Abandonment and Reclamation Association as at March 31, 2020, and its results of operations and its cash flows for the year then ended in accordance with Canadian accounting standards for not-for-profit organizations.

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 Association 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 accounting standards for not-for-profit organizations, 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 Association'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 or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the association'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 Association’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 Association’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 association 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 that we identify during our audit.

Grant Thornton LLP

Calgary, Canada
June 10, 2020

Chartered Professional Accountants

Financial Statements

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION
Statement of Financial Position
As at March 31, 2020
(thousands of dollars)

		2020		2019
Assets				
Current assets				
Cash	**$**	**11,820**	$	5,525
Accounts receivable from the AER		**609**		1,928
GST receivable (Note 4)		**443**		718
Prepaid expense and other receivables		**1,174**		659
Short term investments (Note 5)		**88,500**		94,000
		102,546		102,830
Tangible capital assets (Note 6)		**12**		36
	$	**102,558**	$	102,866
Liabilities and net assets				
Current liabilities				
Accounts payable and accrued liabilities		**9,167**		12,304
Current portion of long term note payable (Note 7)		**30,198**		18,056
		39,365		30,360
Long term note payable (Note 7)		**144,957**		110,770
Deferred contribution (Note 7)		**19,234**		15,619
Internally restricted assets (Note 8)		**516**		506
Unrestricted net assets		**(101,514)**		(54,389)
		(100,998)		(53,883)
	$	**102,558**	$	102,866

Commitment (Note 15)
Subsequent events (Note 16)

See accompanying notes to financial statements.

Approved by the Board:

Director

Director

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION

Statement of Operations
Year ended March 31, 2020
(thousands of dollars)

		2020		2019
Revenues				
Orphan fund levy through the AER		**60,345**		45,379
Interest income (Note 7)		**8,306**		5,869
Industry enforcement and licensee liability rating deposit recoveries through the AER		**3,715**		96
Salvage sales and rental income		**2,400**		780
First time licensee fees and regulator directed transfer fees through the AER		**694**		580
		75,460		52,704
Expenditures				
Operating				
Well abandonment		**46,247**		45,846
Site reclamation		**26,871**		22,930
Facility decommissioning		**12,112**		10,286
Pipeline abandonment		**7,351**		10,121
		92,581		89,183
Other				
Working interest claims (Note 9)		**12,168**		5,181
Fund administration (Note 10)		**4,410**		4,097
Interest on long term note payable (Note 7)		**5,066**		3,177
Bad debt expense (Note 11)		**3,353**		311
Non-recoverable GST expense (Note 4)		**2,347**		2,214
AER enforcement activities (Note 13)		**1,880**		-
Receivership expenses (Note 12)		**770**		-
		29,994		14,980
		122,575		104,163
Deficiency of revenues over expenses	**$**	**(47,115)**	$	(51,459)

See accompanying notes to financial statements.

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION
Statement of Changes in Net Assets
Year ended March 31, 2020
(thousands of dollars)

	Internally Restricted	Unrestricted	2020	2019
Balance, beginning of year	**$ 506**	**$ (54,389)**	**$ (53,883)**	$ (2,424)
Surplus (deficit)	**10**	**(47,125)**	**(47,115)**	(51,459)
	$ 516	**$ (101,514)**	**$ (100,998)**	$ (53,883)

See accompanying notes to financial statements.

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION
Statement of Cash Flows
Year ended March 31, 2020
(thousands of dollars)

		2020		2019
Cash provided by (used in)				
Operating				
Deficiency of revenues over expenses	**$**	**(47,115)**	$	(51,459)
Non-cash items				
Amortization of tangible capital assets		**24**		24
Changes in operating non-cash working capital				
Decrease (increase) in accounts receivable from the AER		**1,319**		(1,106)
Decrease (increase) in GST receivable		**275**		(507)
Increase in prepaid expense and other receivables		**(515)**		(321)
(Decrease) increase in accounts payable and accrued liabilities		**(3,138)**		9,110
		(49,150)		(44,259)
Financing				
Increase in long term note payable		**59,319**		87,233
Increase in deferred contribution		**3,616**		9,589
Repayment of long term note payable		**(12,990)**		(2,378)
Decrease (increase) in short term investments		**5,500**		(94,000)
		55,445		444
Net increase (decrease) in cash		**6,295**		(43,815)
Cash, beginning of year		**5,525**		49,340
Cash, end of year	**$**	**11,820**	$	5,525

See accompanying notes to financial statements.

Note 1 Authority and purpose

The Alberta Oil and Gas Orphan Abandonment and Reclamation Association (OWA or the Association) operates under the authority of the Oil and Gas Conservation Act, Orphan Fund Delegated Administration Regulation, and the Societies Act, Chapter S-18, 1980, as amended. The OWA was created as a Delegated Administration Organization (DAO) under the delegated authority of the Alberta Energy Regulator (AER) and was established to manage the abandonment of Alberta's upstream oil and gas orphan wells, pipelines, facilities and the reclamation of associated sites. The OWA does not assume the legal responsibility for expenditures related to suspension, abandonment and reclamation of such sites. The Members of the OWA are the Canadian Association of Petroleum Producers (CAPP), the Explorers and Producers Association of Canada (EPAC), the AER and Alberta Environment and Parks (honorary non-voting Member).

Note 2 Significant accounting policies

a) Basis of presentation

The Association's financial statements are prepared in accordance with Canadian accounting standards for not for profit organizations.

b) Cash and cash equivalents

Cash and cash equivalents consist of deposits held with financial institutions.

c) Revenue recognition

The OWA follows the deferral method of accounting for contributions. Unrestricted contributions are recognized as revenue when received or receivable if the amount to be received can be reasonably estimated and the collection is reasonably assured. Restricted contributions are recognized as revenue in the year in which the related expenses are incurred.

d) Tangible capital assets

Purchased tangible capital assets are recorded at cost . Donated tangible capital assets are recorded at their fair values at the date of donation. Amortization is provided on a straight-line basis over the assets' estimated useful lives as follows:

Computers	3 years

e) Financial assets and liabilities

Initial measurement: Upon initial measurement, the Association's financial assets and liabilities are measured at fair value, which, in the case of financial assets or financial liabilities that will be measured subsequently at amortized cost, is increased or decreased by the amount of the related financing fees and transaction costs.

Subsequent measurement: At each reporting date, the Association measures its financial assets and liabilities at amortized cost (including any impairment in the case of financial assets).

Note 2 Significant accounting policies (continued)

The Association records cash, accounts receivable from the AER, other receivables, and accounts payable and accrued liabilities at amortized cost.

Financial assets measured at amortized cost are assessed for indications of impairment. When there is an indication of impairment indicating a significant adverse change in the expected timing or amount of future cash flows from the financial asset, an impairment loss will be recognized in the statement of operations. The reversal of a previously recognized impairment loss on a financial asset measured at amortized cost is recognized in the statement of operations in the year the reversal occurs.

f) Use of estimates

The preparation of the financial statements in conformity with Canadian accounting standards for not for profit organizations, requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the year. Due to the inherent uncertainty involved with making such estimates, actual results reported in future years could differ from those estimates.

Items subject to significant management estimate include accrued liabilities, amortization of tangible capital assets and fair value of long term note payable.

g) Not for profit status

The OWA, as a not for profit organization, has no liability for income tax under the Income Tax Act (Canada).

h) Change in accounting policies

Effective April 1, 2019, the Association adopted the new standards in the Chartered Professional Accountants of Canada Handbook, Part III – Accounting for Non-for-Profit organizations Sections 4433 *Tangible Capital Assets Held by Not-for-Profit Organizations* and 4441 *Collections Held by Not-for-Profit Organizations*.

The adoption of Section 4433 – *Tangible Capital Assets Held by Not-for-Profit Organizations* had no impact on the Association's accounting policies with respect to componentization and amortization of tangible capital assets, as the cost of these assets is not comprised of significant separable component parts.

Section 4441 – *Collections Held by Not-for-Profit Organizations* has no material impact for the Association as it holds no collections.

(thousands of dollars)

Note 3 Economic dependence and contributions

The OWA receives substantially all its revenue through the AER. The AER collects the Orphan fund levy, first time licensee fees, regulatory directed transfer fees, enforcement recoveries, and liability licensee rating recoveries from industry. These funds are then contributed directly to the OWA. The annual revenue received by the OWA is subject to budget submission to the AER.

Note 4 GST receivable and non-recoverable GST expense

During fiscal 2016, the CRA pronounced a new ruling for the OWA which determined that OWA is a GST exempt entity for fiscal years ending March 31, 2014-2016. This change in ruling has resulted in a refund of GST paid during these years, as reduced by the income tax credits claimed by fifty percent as OWA is a not-for-profit entity. The net effect for this ruling has resulted in a GST receivable of $443 (2019 - $718) and non-recoverable GST expense of $2,347 (2019 – $2,214)

Note 5 Short term investments

At March 31, 2020, the Association's investments consisted of Guaranteed Investment Certificates with interest rates of 1.5% to 2.5% per annum. The investments mature at various dates from May 2020 to January 2021.

Note 6 Tangible capital assets

	Cost	Accumulated amortization	**2020 Net book value**	2019 Net book value
Computers	$ 72	$ 60	$ 12	$ 36

Note 7 Long term note payable

The OWA entered into a loan agreement with Her Majesty the Queen in Right of Alberta as represented by the President of Treasury Board, Minister of Finance and by the Minister of Energy (the Province) under which the OWA may borrow money from the Province to a maximum aggregate amount of $235,000. The date of last permitted advance is April 1, 2020, with quarterly frequencies at zero percent interest rate on the advances. The loan is fair valued at $205,000 with the difference between book value and fair value recorded as a deferred contribution and amortized into revenue over the life of the loan. As at March 31, 2020, advances of $218,000 (2019 $150,000) has been received, of which $19,234 (2019 $15,619) is recorded as a deferred contribution, and $5,066 (2019 $3,177) is recorded as interest calculated at an annual rate of 3.2% (2019 3.2%). The following is the advance and repayment schedule for the note payable.

(thousands of dollars)

		2020		2021		2022		2023		2024		2025		2026-2027
Advance schedule	**$**	**68,000**	$	17,000	$	-	$	-	$	-	$	-	$	-
Repayment Schedule	**$**	**18,056**	$	30,198	$	30,198	$	30,198	$	30,198	$	30,198	$	60,398

Note 8 Internally restricted assets

Included in cash are internally restricted assets in the balance of $516 (2019 $506). The Directors maintain sovereignty of the internally restricted fund to be used at the discretion of the Board.

Note 9 Working interest claims

The OWA accepts claims as directed from the AER made by industry for defunct working interest partners. Working interest partners are any party under a joint operating or other agreement under which the party is entitled to a proportionate share of cash flows as well as costs. If a company has a defunct working interest partner with a well, facility or associated site that is deemed orphan by the AER, the OWA will reimburse the proportionate share of costs on behalf of the defunct working interest partner of the completed abandonment and/or the completed reclamation. Reclamation is considered completed and reimbursement can be made when a reclamation certificate has been issued on the site.

Note 10 Fund administration

Fund administration includes salaries and benefits to management of $387 (2019 - $392). No remuneration and benefit payments were made to Board members for 2020 and 2019.

Note 11 Bad debt expense

Bad debt expense is directed from the AER based on the uncollected Orphan fund levy.

Note 12 Receivership expenses

The Association applies to the Courts to appoint Receivers for various oil and gas companies during the year as no other party came forward to do so when these organizations ceased operations. Appointing a Receiver will ensure that the various assets are managed and maintained safely for the benefit of the public, and where possible, placed in the hands of responsible operators through various sales processes.

Note 13 AER enforcement activities

AER enforcement activities expenditures are amounts paid to the AER for third party abandonment expenditures on wells, pipelines and facilities incurred by the AER during their enforcement actions against liable parties. In cases when the wells, pipelines or facilities are subsequently deemed orphan by the AER, the OWA will reimburse the AER for these expenditures.

(thousands of dollars)

Note 14 Financial instruments

The Association's main financial risk exposure is detailed as follows:

(i) Credit risk

The Association is exposed to credit risk, which is the risk that a counterparty will fail to perform an obligation or settle a liability, resulting in a financial loss to the Association. The Association's accounts receivable is primarily due from AER and are subject to normal credit terms. The maximum credit risk exposure associated with the Association's financial assets is the carrying amount.

(ii) Liquidity risk

The Association is exposed to liquidity risk which is the risk that the Association will be unable to generate or obtain enough cash to meet obligations as they fall due. Mitigation of this risk is achieved through the active management of cash and debt. The liquidity risk is assessed as low for the Association.

The contractual maturities of financial liabilities as of March 31, 2020 are as follows:

	Total	2021	2022	2023	2024	2025	Thereafter
Accounts payable and accrued liabilities	$ 9,167	$ 9,167	$ -	$ -	$ -	$ -	$ -
Long term note payable	$ 194,389	$ 30,198	$ 30,198	$ 30,198	$ 30,198	$ 30,198	$ 43,399

Note 15 Commitment

Office space contracted payments are as follows:

	Total	2021	2022	2023	2024	2025
Contracted payments	$ 750	$ 170	$ 170	$ 170	$ 170	$ 70

Note 16 Subsequent events

a) Since March 31, 2020, the spread of COVID-19 has severely impacted many local economies around the globe. In many countries, including Canada, businesses are being forced to cease or limit operations for long or indefinite periods of time. Measures taken to contain the spread of the virus, including travel bans, quarantines, social distancing, and closures of non-essential services have triggered significant disruptions to businesses worldwide, resulting in an economic slowdown. Global stock markets have also experienced great volatility and a significant weakening. Governments and central banks have responded with monetary and fiscal interventions to stabilize economic conditions.

The duration and impact of the COVID-19 pandemic, as well as the effectiveness of government and central bank responses, remains unclear. It is not possible to reliably estimate the duration and severity of these consequences, as well as their impact on the financial position and results of the Company for future periods.

b) On April 1, 2020, the Company executed an amended loan agreement with the Government of Alberta. The amended agreement provides access to a second loan facility with a maximum permitted advance of $100,000. Funds will be advanced in two equal payments of $50,000 on October 1, 2020 and January 1, 2021 at zero percent interest. Principal repayments will commence on January 1, 2028 and will occur every three months in equal instalments of $6,250 until October 1, 2031.

c) On April 2, 2020, Bill 12, the Liabilities and Management Statutes Amendment Act passed Third Reading and Royal Assent in the Alberta legislature. The Act will come into force on June 15, 2020. On June 3, 2020, the Orphan Fund Delegated Administration Amendment Regulation was passed by an Order in Council. The general purpose of the Bill and Amendment Regulation are to enable the Association to better manage and accelerate the clean-up of wells or sites which do not have a responsible owner. These changes will enable the Association to play a more active role in reducing the inventory of orphan wells, orphan sites and appoint receivers as may be required by specific circumstances. The impact of the Bill and Amendment Regulation on the Association's operations are under review. Based on the analysis to date, it is not expected to have a negative impact.

d) On April 17, 2020 the Government of Canada announced their intent to provide an interest free loan of $200,000 to the Association. The terms of the agreement are currently under discussion.

Note 17 Comparative figures

Certain comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year. The following financial statement line items have been reclassified:

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION
Notes to the Financial Statements
March 31, 2020
(thousands of dollars)

		2019, as reclassified		2019, as previously presented
Statement of Financial Position				
Cash	**$**	**5,525**	$	99,525
Short-term investments		**94,000**		-
		99,525		99,525
Current portion of long term note payable		**18,056**		-
Long term note payable		**110,770**		128,826
		128,826		128,826
Statement of Operations				
Fund administration		**4,097**		4,408
Bad debt expense		**311**		-
		4,408		4,408
Statement of Cash Flows				
Increase in long term note payable		**87,233**		84,856
Increase in deferred contribution		**9,589**		9,589
Repayment of long term note payable		**(2,378)**		-
Decrease (increase) in short term investments		**(94,000)**		-
		444		94,445
Net increase (decrease) in cash		**(43,815)**		50,185
Cash, beginning of year		**49,340**		49,340
Cash, end of year	**$**	**5,525**	$	99,525

Governance

The Alberta Oil and Gas Orphan Abandonment and Reclamation Association is an independent nonprofit organization, generally known as the Orphan Well Association or OWA. The OWA operates under the delegated legal authority of the AER, the provincial regulator of energy development. Funding for the association's work comes primarily from Alberta's oil and gas producers through the Orphan Well Levy.

Through its Board of Directors, industry, regulatory and government representatives oversee the OWA's operations, priorities and strategic planning to ensure the association is delivering its mandate to protect public health and safety and manage environmental risk.

Board of Directors

Brad Herald, Canadian Association of Petroleum Producers, OWA Chair

Brad Herald's work with CAPP has focused on industry operations and economics in Western Canada, including best practices related to the environment and public health and safety. He works closely with industry experts on community and regional stakeholder concerns, and with regulators and governments on policy issues and implementation.

Kendall Dilling, Cenovus Energy

Kendall Dilling has 25 years of technical and management experience in the oil and gas industry, including work in environmental protection and management of pipeline projects. He has worked with emerging Canadian and multinational energy companies in health, safety and environment portfolios. In addition to the OWA, Kendall serves on several nonprofit industry, community and research boards.

Orest Kotelko, Canadian Natural Resources Limited

Orest Kotelko has more than 45 years of experience in energy life-cycle development, operations and liability management in drilling, construction and reservoir engineering. His experience includes work with industry associations, major and emerging companies, and governments, as well as stakeholder groups in conventional and oil sands development in Western Canada.

D. Blake Reid, Paramount Resources

Blake Reid is a Professional Engineer and Executive Vice President, Operations at Paramount Resources. Prior to joining Paramount, Blake held a number of progressively senior roles over 25 years of industry experience. His work has included a broad range of technical, operational and strategic management roles, including leadership of multi-disciplinary organizations covering operations, maintenance, engineering, project management, drilling and completions, administration, and environment, health and safety portfolios.

Jim Screaton, Explorers and Producers Association of Canada

Jim Screaton is a Chartered Accountant who has held leadership roles in major, mid-size and emerging energy companies. He brings experience in organizational strategy related to financial analysis, debt and liability, securities regulation and disclosure. In addition, he has represented industry on a breadth of association and committee work, including liability management.

Rob Wadsworth, Alberta Energy Regulator

Rob Wadsworth is Vice President Compliance & Liability Management at the Alberta Energy Regulator. Since 2012, he has held several executive roles with the AER covering industry life-cycle regulation from approval processes for new projects to closure and reclamation, as well as providing organizational leadership on learning, effectiveness and efficiency initiatives. Prior to the AER, Rob worked as a departmental manager with a major nuclear power producer. He had earlier served in senior leadership roles in domestic and international operations with the Canadian Forces.

Karen Wronko, Alberta Environment and Parks

Karen Wronko is the Executive Director of Land Policy within Environment and Parks. During her career in public service she has worked in a number of areas and has provided senior level leadership to several strategic initiatives, including policy development related to water and land, the growth and diversification of the provincial economy through local economic development, entrepreneurship and small business support, and major initiatives targeted at growing the petrochemical sector in Alberta.

Management

Lars De Pauw, Executive Director

Lars De Pauw took on the leadership of the OWA in 2017. As a Professional Engineer, he has held senior positions in strategic planning, project development, environmental engineering, and client and stakeholder relationship management. His experience includes work with a major Canadian oil and gas producer, a diversified petroleum services company, and strategic and operational consulting businesses.

Wanda Sakura, Team Lead, Environment

Wanda Sakura is a Professional Geologist who brings to OWA more than 30 years of environment and safety experience, including direct work with the association's planning and operations since 2006. Her expertise includes management of environmental assessment and remediation of legacy facilities in urban and commercially developed areas. She also brings significant experience in working effectively with Indigenous communities.

Ken Willis, Team Lead, Well Decommissioning

Ken Willis has worked as a Professional Engineer in the oil and gas industry since 1980, both in the field from drilling and completions, and as an organizational leader of engineering and technology teams in Canada and internationally. His experience in life-cycle management of facilities covers a broad spectrum of expertise from downhole work to surface production operation sites.

Orphan Well Association

ALBERTA OIL AND GAS ORPHAN ABANDONMENT AND RECLAMATION ASSOCIATION

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