

## Note #3: Technically, you may be good, but are you Competent?

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I don't know if it is surprise or envy that my colleagues feel when I introduce myself as the Competent Person (CP) at Rockflow. When I graduated 30 years ago, I had greater aspirations than merely to refer to myself as "Competent"!

But as such, I sign off the Competent Persons Reports (CPR) for my company, which are important, if not essential, documents for any company seeking to raise finance for oil and gas projects on the AIM or LSE. Investors rely upon CPRs, together with the Prospectus as a starting point for assessing whether or not to invest in a company. An investor should also do their own research in order to better understand the company and the inherent risks of a business opportunity, but is unlikely to have access to the types of information (e.g. seismic, computer models, licence documents, etc) that are reviewed as part of a CPR. So even though a CPR is paid for by the company seeking to raise finance, I feel that as a CP, I'm writing the document on behalf of the investor, rather than the company.

### What does it take to be "Competent"?

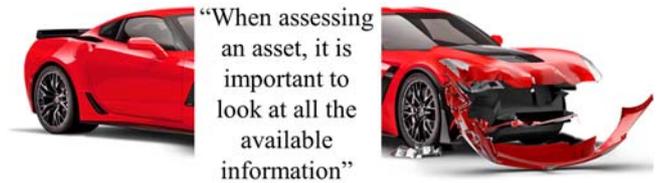
AIM summarises the minimum requirements that a CP should:

- be professionally qualified and a member of an appropriate professional organisation;
- have at least five years relevant experience;
- be independent to the Company in question;
- not be remunerated by way of a fee that is linked to the admission or value of the applicant; and
- not be a sole practitioner.

These requirements are a minimum. Personally, I find the requirements for independence in the Canadian COGEH regulations to be more detailed (for instance, excluding the ownership of shares in the Company by the CP – something I insist on with my colleagues as well).

There are some topics not covered by the AIM guidance, for instance:

- Which Reserves Standards are approved in AIM?
- What are the key criteria which determine Reserves from Contingent Resources?
- How to assess upside?
- How to perform an commercial evaluation and risk a project?



### Reserves or Resources?

AIM doesn't specify which reserves standard should be used, but (for the time being) as part of the European Securities and Market Authority (ESMA), acceptable standards are: 1) Society of Petroleum Engineers – Petroleum Resource Management System (SPE-PRMS), 2) Canadian Oil and Gas Exploration Handbook (COGEH) and 3) the Norwegian Petroleum Directorate (NPD) resource classification.

We always have to look carefully at projects which are near the Reserves/Contingent Resources or the Contingent/Prospective Resource boundaries. When a project has been approved by the Company, its partners and the relevant Authority, the project may well have Reserves which are "Approved for Development".

When a project has Reserves which are "Justified for Development", it is worth asking what does that mean? There is a phrase in PRMS that explains this as "a firm intent to proceed with development" - but what do we mean by intent? This can result in some discussion between the CP and the Company - the CP may see the evidence in a different light to that described by the Client.

There are similar issues for projects that may have crossed the Prospective/Contingent Resource boundary. It is not a requirement that a field has to be tested in order to be "discovered" – there could be reasonable grounds from nearby analogues which demonstrate "the potential for commercial recovery".

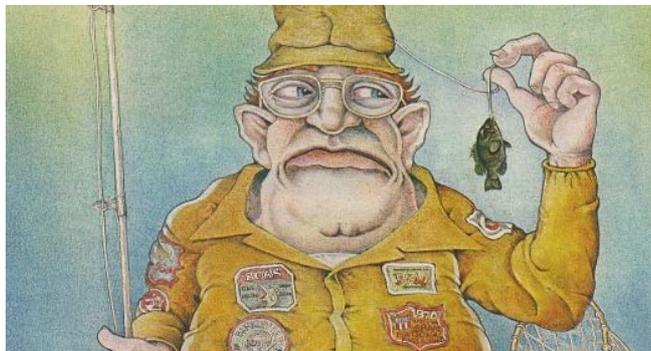
I could use an angling analogy (not taken from PRMS!):

**Prospective Resources:** I'm going for a drive into the mountains and hopefully find a lake with some fish in it.

**Contingent Resources:** I intend to go fishing in the mountains, there's a lake there with a lot of fish in it; all I need is a fishing rod, bait, a rowing boat and some cash.

**Reserves:** I'm in the boat in the lake in the mountains, I've got fish in my net, and I can see more in the water.

When assessing an asset, it is important to look at all the available information, and I would expect that the CP would do so. But, it is also important that the investor understands why a project has been classed as Reserves or Resources. This may highlight some of the key issues that would need to be overcome in order to deliver the project and value that has been indicated.



“The CP may see the evidence in a different light to that described by the Client.”

### Upside or Additional Projects?

When PRMS came out in 2007, it set out that resources (or reserves) are worked out for each project, and each project would have a low, mid and high case outcome. In 2018, PRMS went on to state that a single project could not have a mixture of both reserves and resources (this would be a case of “split-categorisation”). A field or asset, on the other hand, could have more than one project, and so could have a mixture of reserves and resources. Most, if not all producing fields do, such as those with existing production would be considered as one (already developed) project, and then a potential future infill well in the same field should be considered as another project. Some people may like to add the reserves together with the resource estimates to create a single, larger figure, but this isn't recommended, and I wouldn't expect to see this done in a CPR. It would be misleading to combine the volumes of something that is happening (i.e. reserves) with those of another project which may not happen. You could ask yourself, “What is it about the contingency that makes the ‘Contingent Resources’, contingent?”

### How much is it all worth?

AIM does not give any guidance on which Oil (or gas) Price Scenario to use: all oil price forecasts are wrong – if I knew what the oil price would be, I wouldn't need to earn a living as a CP! The best we can do is use a scenario which is realistic at the time of issue. Within the

CPR there should be a price sensitivity analysis, although this doesn't always appear in the cover letter.

In order to qualify volumes as reserves, they have to be economic. The CP has to do an economic analysis, using production profiles, costs and assumed oil/gas price scenarios, and can estimate the economic cut off, and the NPV for the project. The same analysis can be done for a project with Contingent Resources. Whether the project has Reserves or Resources, the investor should not assume that the NPV value is a statement of the “fair market value”, for instance:

- A value of NPV can be calculated separately for the low, mid and high cases – there is no right way to combine these three valuations into an estimate of fair market value.
- Projects with Contingent Resources carry a chance that the projects may not proceed. The NPV is normally an unrisks valuation.

### Do CPRs just reflect the Company's view?

No. A CPR should be based on an independent evaluation. In a recent project, we were asked to prepare a CPR for a Client, who had adopted an extreme upside as their business case. We reviewed the data and identified a range of outcomes, with both the low and mid cases being considerably below their business case, with correspondingly low (or even negative) NPVs.

When something like this happens, it is usual to discuss this result with the Client, in order to give them a chance to respond, and highlight any key pieces of information which might have been overlooked. In this case, there was no silver bullet, and we were unable to change our evaluation whilst still being reasonable, realistic and honouring the available data.

So unfortunately for the Client, the work on the CPR was stopped, and it was never finalised or published. A few months later there were some resignations from the board of the company.

### The Bottom Line

When preparing a CPR, the CP has access to a considerable amount of information, and with his/her colleagues, has the opportunity to present a fair and reasonable view of the likely range of outcomes, based on the available data. The work is paid for by the Client/Company, but the ultimate end user is the potential investor.

In the world of a Competent Person, Client Service is important; but Integrity Matters.