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General guidance notes for oil sands Production Allocation Unit Agreements

Production Allocation Unit Agreement (PAUA)

A PAUA is a unit-type agreement used for a single well that crosses multiple drilling spacing units of mixed ownership (Crown and freehold). The PAUA ensures that the royalty payments from one well are distributed to both Royalty Owners in a fair and equitable manner. A PAUA is a cross between a pooling agreement and a unit agreement that has been developed for use where various Royalty Owners and Working Interest Owners wish to share production from a single well.

Initial term oil sands leases can be included in an oil sands PAUA.

PAUAs – the basics

Technical data required for a PAUA

- Wellsite survey to confirm the surface hole coordinates
- Directional surveys for each drilled leg to calculate open hole lengths on each tract
- Daily drilling reports to confirm casing points and kick off points for each leg
- Plan view of the drilled legs to determine which drilling spacing units have been penetrated and should be included in the PAUA
- Geologic strip logs and electric logs
- Completion reports

In oil sands, a PAUA is the only vehicle that will achieve common royalty ownership where minerals are owned by more than one party and where there is a mix of Crown and freehold ownership. PAUAs provide for the sharing of costs, revenues and royalties on the basis of allocated production and, if possible, the tract participations are based on technical parameters rather than on surface area.

A PAUA becomes effective at 0800 on the first day of the first calendar month, which is the earliest of:

- the month in which production of production allocation substances from the well commences, or

- the month following the date of execution and delivery of the agreement by the owners of one hundred percent (100%) of the Working Interest and one hundred percent (100%) of the Royalty Interest within the production allocation area.

Typically, these agreements terminate when a second producing well is drilled within the PAUA.

The basis for determining tract participations must be equitable and technically justifiable. Generally, the tract factors are calculated using open hole wellbore lengths on each tract. Other methodologies for calculating tracts, such as acreage or mapped hydrocarbon pore volume, can be used under special circumstances. When calculating tract factors, in most cases the road allowance portion of the open hole section of wellbore may be ignored and may not be included in the calculation for either the Crown or the freehold tract.

Execution of PAUA

Unlike a standard unit agreement, a PAUA can be executed retroactively. A PAUA must become effective at 0800 on the first day of the first calendar month which is the earliest of:

- the month in which production of production allocation substances from the well commences, or
- the month following the date of execution

and delivery of the agreement by the owners of one hundred percent (100%) of the Working Interest and one hundred percent (100%) of the Royalty Interest within the production allocation area.

PAUAs can be executed retroactively; therefore, in order to determine the proposed unitized substance and zone, the well must be placed on production for three months before Alberta Energy's review can commence. In addition, ensure you have the rights to drill and produce.

Once the well has been on production for three months, the proposal can be submitted in person, by mail, or by courier. Do not e-mail your proposed document.

If the PAUA has a producing well and one or more parties refuse to execute, the following are possible consequences:

- Failure to execute a PAUA may result in the Crown taking action through the Regulator to remedy this high-risk non-compliance. No well shall be produced unless there is common ownership throughout the drilling spacing unit.

  OR

- Alberta Energy will recommend plugging back the wellbore to ensure production is isolated to one drilling spacing unit, thus eliminating the requirement for a PAUA.

<u>Exhibit "A"</u>

The Exhibit "A" template previously used by Alberta Energy for petroleum and natural gas operations was modified to add "Share of Royalty Interest (%)", a new column. Each freehold royalty interest owner can indicate its ownership percentage in respect of the overall tract participation determined for freehold. For freehold owners, there might be one or more owners listed with their respective ownership percentage indicated.

Exhibit "A"s can be revised and updates will be processed if the change occurs in an open production year. Changes will not be processed in statute-barred years. Please note that Alberta Energy does not validate or use these numbers. For the Crown, it will always indicate 100% in this column.

For any ETS request rejected, you may email the Oil Sands Tenure team at ostenure@gov.ab.ca for assistance.

GLOSSARY

Production Allocation Unit Agreement (PAUA)

Formed to allow Royalty Owners and Working Interest Owners to share in the production from a single well drilled through two spacing units of Crown and freehold interests.

Royalty Interest

An ownership interest in mineral rights.

Royalty Owner

An individual who or a corporation that owns a Royalty Interest. A Royalty Owner (lessor) who leases out their/its rights to a Working Interest Owner is usually entitled to share of the production obtained from the rights.

Working Interest

A right to produce and to dispose of minerals, associated with the responsibility for the costs of production and disposal. A Working Interest is usually acquired from the Royalty Owner of the mineral rights through a leasing arrangement.

Working Interest Owner (WIO)

An individual who or a corporation that owns a Working Interest.