

Oil and Gas Reserves and the Financial Community

Presented at the
Tennessee Oil and Gas Association
Annual Meeting
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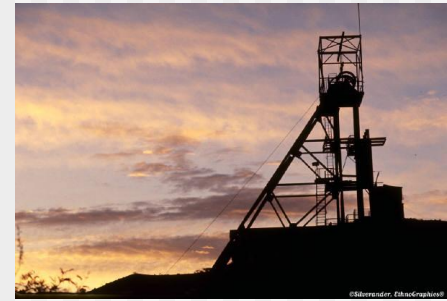


D. Randall Wright, President
randy@wrightandcompany.com
(615) 370-0755 Ext. 12



Brentwood, Tennessee

Introduction

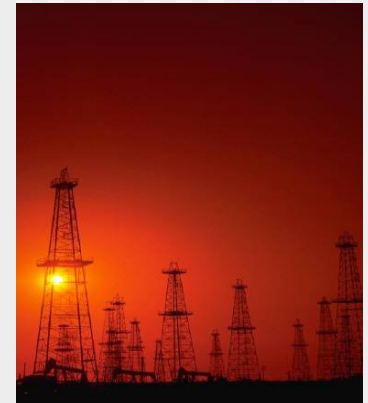


- Role of the Reserves Report
- Adequacy of Company Reserves Disclosure
- Securities and Exchange Commission (SEC) Rules
- Communication Between All Parties



Role of the Reserves Report

- Internal Information
 - *Too dynamic, detailed and complex for "outsiders"*
- Objective Estimates of Reservoir Characteristics
- Subjective Forecast of Project Feasibility
- Corporate Planning and Strategy of Investment

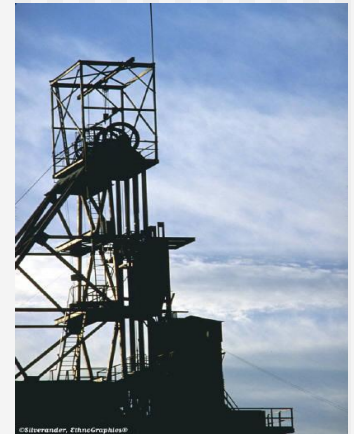


Benefits of the Reserves Report

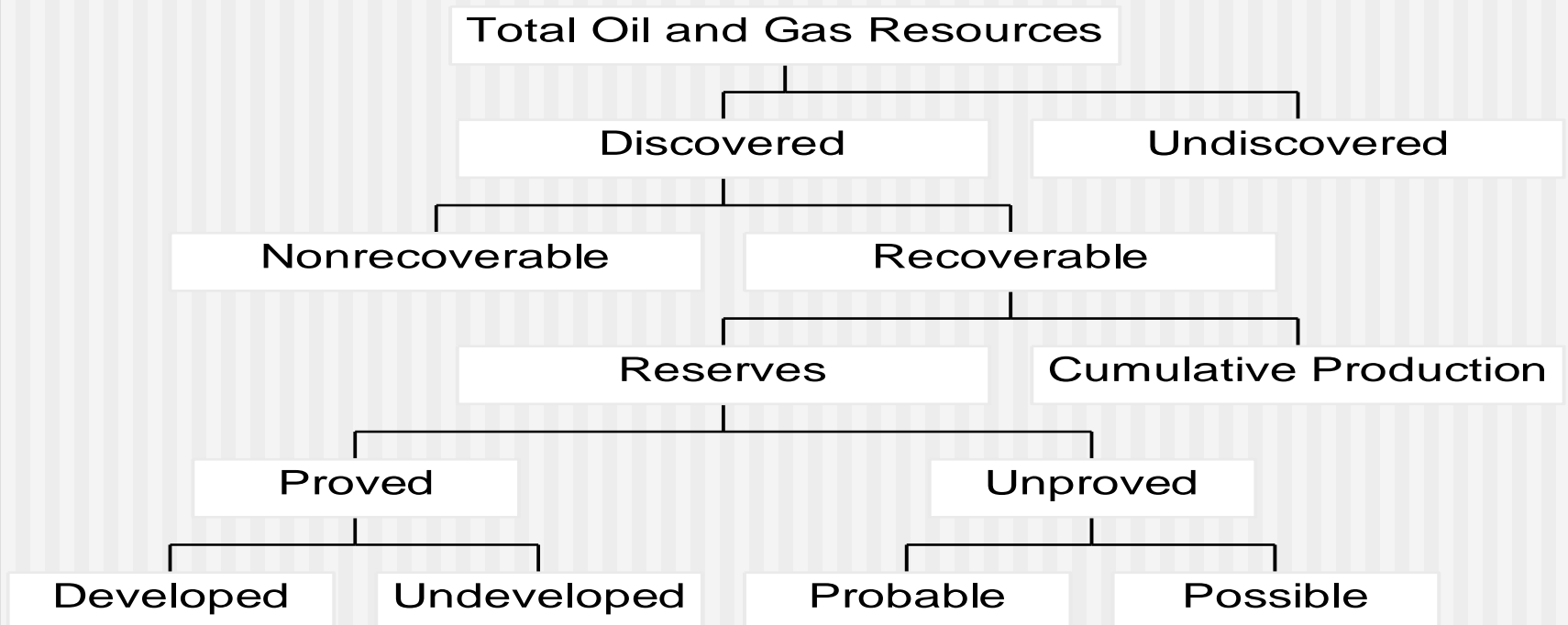
- An Independent Appraisal
- The Availability of Industry Wide Data Network
 - Technical Consultants
 - Accounting Firms
 - Banks
 - Investment and other Financial Institutions
- Technical Expertise and the Reputation of the Firm
- Cost and Time Efficient Reserves Management

Needs Satisfied by Reserves Reports

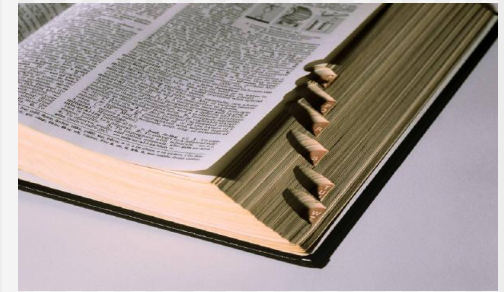
- In-House Accounting Requirements, Budgets, and Planning
- Re-organizations
- Bank Financing
- Government Filings
- Public Offerings
- Limited Partnerships and Joint Ventures
- Divestitures, Acquisitions, and Mergers
- Estates, Trusts, and Gifts



RESERVES TERMINOLOGY



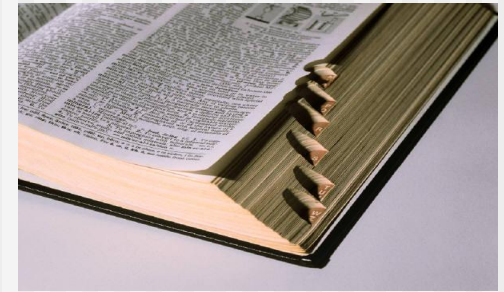
Definitions of Reserves



Proved Reserves

- Economic producibility supported by production or conclusive formation test
- Defined by oil-gas and/or oil-water contact
- Adjoining portions judged economically productive based on geological and technical data
- Successful pilot test
- Economically viable using fixed costs and prices

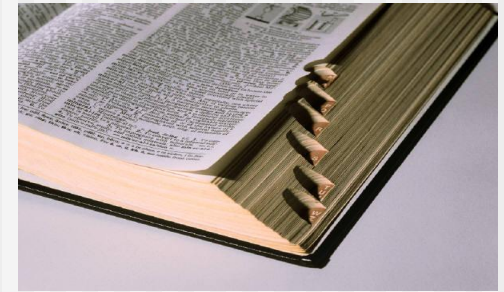
Definitions of Reserves



Proved Developed Reserves

- Expected to be recovered through existing wells
- Proved Developed Producing (PDP)
 - Actively producing wells
- Proved Developed Nonproducing (PDNP)
 - Shut-in waiting on equipment or pipeline
- Proved Developed Shut-in (PDSI)
 - Previously productive wells not currently active
- Proved Developed Behind Pipe (PDBP)
 - Recompletion to another zone

Definitions of Reserves



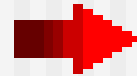
Proved Undeveloped (PUD)

- New wells on undrilled acreage
- Recompletion of existing well with major capital expenditure
- Offsetting productive units that are reasonably certain of production
- Certainty of production based on continuity of the existing productive formation
- One “legal location” offsetting commercially productive well

Reserves and Financial Statements

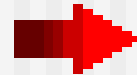


Balance Sheet



Historical Costs

Reserves Disclosure



Current Value
and
Historical
Performance

Do Reserves Reflect:



■ Underlying Value?

- Viewpoint of a **lender** –
Proved hopefully implies reassurance
that p+i will be repaid

- Viewpoint of an **equity investor** –
proved + probable + possible (3P);
more risk = bigger reward

Do Reserves Reflect:



■ **Economic Reality?**

- Proved Reserves – may be too conservative
 - “Downward Revisions” – “Upgrades”

- 3P Reserves – Future plans
 - Company’s capacity to have new development projects

Do Reserves Reflect:

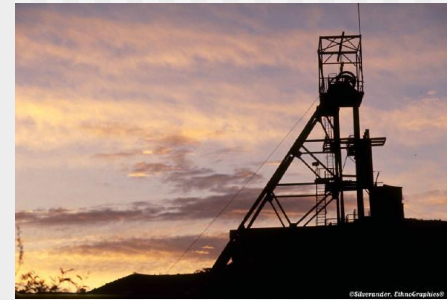


■ True Values?

➤ SEC issues

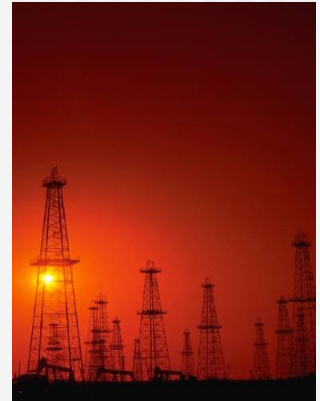
- At fiscal year-end
- Constant economics
- 10.00 percent discount

Actions by the SEC and Banks



- The SEC will use the broad reaching powers of Sarbanes-Oxley to investigate oil and gas reserves more thoroughly than ever before
- Attempt to review all E&P companies every 3 years, minimum

What Does Sarbanes-Oxley Say About Oil and Gas Reserves?



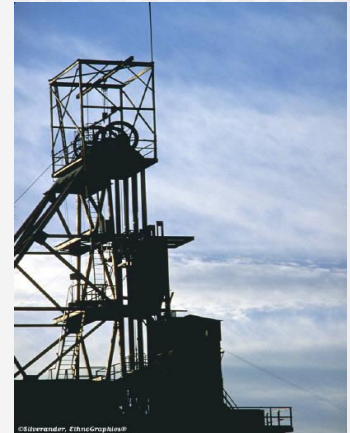
- Nothing directly, but it is clearly evident the intent is for management to ensure that **ALL** financial reporting, including future cash flow from production, provides reliable information.

Reserves and Investor Confidence

Wall Street will –

- Come to expect and demand clarity and integrity in all financial reporting from:
 - ✓ Financial Analysts
 - ✓ Investment Bankers
 - ✓ Auditors

- Become more proactive in potential litigation if issues arise in the future



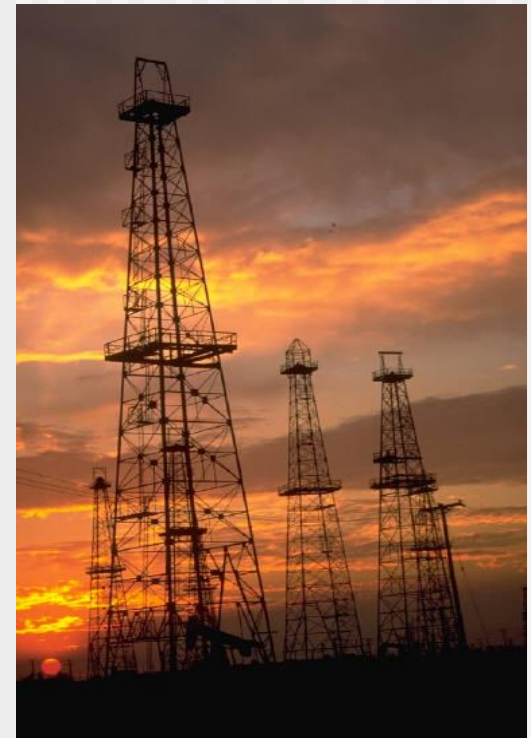
Communication of Reserves is Necessary With Financial Community



- Future production implies reward to shareholders and ability to repay debt
- Profits depend on exploration and development costs
- Proved Reserves understood by investors and creditors

Conclusions

- How Reserves Reports are Utilized
 - *Investors*
 - *Shareholders*
 - *Companies*
- Communication!
Communication!!
Communication!!!





Questions and Discussion

Thank you very much
for your attention!