

Royalty Program for Coalbed Methane Projects

Petroleum and Natural Gas Act

Do you own an interest in gas produced from a coalbed methane (CBM) project?

Do you operate a well event that is part of a CBM project or a well event connected to a battery that is part of a CBM project?

This bulletin provides specific information to help producers understand the royalty program for CBM projects, including the additional producer cost of service (PCOS) allowance and PCOS bank that are unique to CBM projects. This bulletin also provides information to help producers and operators understand what information they need to submit to the ministry for CBM projects.

For general royalty information that applies to all well events, please see the [Oil and Gas Royalty Handbook](#).

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Overview

The royalty program for CBM projects was introduced in 2001 and was designed for the title leases, operating conditions and costs that are unique to CBM production. Each month, when the ministry calculates your royalty due on production from a well event that is part of a CBM project, the ministry applies the program to your royalty payable in three ways.

First, the ministry adjusts your royalty rate based on the applicable type of lease and a production-based reduction factor. Second, the ministry reduces your royalty payable with a PCOS allowance that is based on the actual costs of producing the gas and transporting it to a plant or sales line. Third, the ministry establishes a project PCOS bank for you and adds amounts to it for each well event that you own an interest in as part of the project. The ministry deducts amounts from your PCOS bank as needed to reduce your royalties on production from any well events that are part of the project.

Please note: Although this bulletin refers to royalties, the program for CBM projects applies to tax on production from freehold land in the same manner.

Definitions

A **BPO lease** is a lease for the right to produce petroleum or natural gas that meets the following three criteria.

1. The right to produce petroleum or natural gas is a result of a Crown Petroleum and Natural Gas Tenure Disposition Agreement dated May 19, 2004.
2. The lessee has chosen to make a 50% bonus payment as indicated in section 1.1 of the agreement.
3. The right to produce petroleum or natural gas relates to lands that are, or form part of, the Coal Lands (as that term is defined in the agreement).

An **NBPO lease** is a lease for the right to produce petroleum or natural gas that meets the following three criteria.

1. The right to produce petroleum or natural gas is a result of a Crown Petroleum and Natural Gas Tenure Disposition Agreement dated May 19, 2004.
2. The lessee has chosen **not** to make a bonus payment as indicated in section 1.1 of the agreement.
3. The right to produce petroleum or natural gas relates to lands that are, or form part of, the Coal Lands (as that term is defined in the agreement).

Royalty Rates for CBM Well Events

The ministry calculates the base royalty rate for a CBM well event in the same way as the ministry calculates the base royalty rate for a conventional gas well event. For more information on base royalty rates, please see section 5.2 of the *Oil and Gas Royalty Handbook*.

If the average daily raw gas production for a CBM well event is less than 17,000 m³, the ministry adjusts the base rate and calculates the royalty rate as follows:

$$\text{Royalty Rate} = \text{Base Royalty Rate} \times (1 - [(17,000 - \text{ADV}) / 17,000]^2)$$

where

ADV = average daily production volume of raw gas during the month. ADV is equal to 24 times the volume of raw gas produced in the month divided by the hours during which the well event produced in the month, as reported on the *Monthly Production Statement (S1)*.

If CBM is produced from a well event under a **BPO lease**, the ministry multiplies your royalty rate by 0.75 after applying the production-based adjustment.

If CBM is produced from a well event under an **NBPO lease**, the royalty rate must be at least 6%, even after applying the production-based adjustment.

Producer Cost of Service (PCOS) Allowance

All producers are eligible for a monthly PCOS allowance to help cover the costs of transporting the province's share of raw gas to processing plants. The ministry deducts this allowance from producers' gross royalties.

As a producer of a CBM well event, you are eligible for a monthly PCOS allowance that is based on the actual costs of producing and transporting the gas, including water handling and disposal costs.

The ministry uses information provided by the CBM project operator on the *Application for a Coalbed Methane Producer Cost of Service Allowance (BC26)* to calculate your production-based PCOS allowance rate for each well event.

The PCOS allowance formula is provided in the guidelines to completing the BC26. The guidelines are available on our website at www.sbr.gov.bc.ca/business/Natural_Resources/Oil_and_gas_royalties/forms.htm

If CBM is produced from a well event under a **BPO lease**, the ministry multiplies your PCOS allowance by 0.75.

CBM PCOS Bank

While the ministry calculates royalties and PCOS allowances at the well event level, you have one PCOS bank for all of the well events that you own an interest in as part of a CBM project. There are five steps that the ministry takes to calculate the monthly closing balance in your PCOS bank.

1. If your PCOS allowance for a CBM well event in a month is greater than your gross royalty on production from that well event in the month, the ministry:
 - adds the difference to your PCOS bank, and
 - deducts it as needed in **future** months to reduce your royalties on production from any well events that are part of the project.
2. The ministry adds a credit to your PCOS bank when a CBM well event is completed. The credit amount depends on your interest in the completed well event and the type of lease for the land on which the well event is located. The ministry multiplies one of the following amounts by your interest in the well event:
 - BPO lease on crown land, \$37,500
 - NBPO lease on crown land, \$30,000
 - other lease on crown land, \$50,000
 - any well event on freehold land, \$30,000
3. The ministry adds an amount to your PCOS bank when you acquire an interest in a CBM well event from another producer. This amount is the portion of the balance in the other producer's PCOS bank that is proportionate to the interest you acquire.
4. The ministry deducts an amount from your PCOS bank when you sell an interest in a CBM well event to another producer. This amount is the portion of the balance in your PCOS bank that is proportionate to the interest you sell.

- The ministry deducts amounts from your PCOS bank as needed to reduce your royalties on production from any well events that are part of the project.

Amounts added to your PCOS bank in a given month (e.g. excess PCOS allowance or credit for completed well events) cannot be used to reduce royalties due in the same month. The maximum amount that the ministry can deduct from your PCOS bank in a given month is your closing balance from the previous month.

CBM PCOS Bank - Example

For January 2008, Producer A has an excess PCOS allowance of \$12,730.89 for five well events and owes \$67.50 in royalties for one well event.

During the month, two well events that Producer A owns an interest in were completed. Also, Producer A acquired an interest in a well event from Producer B and sold an interest in a well event to Producer C. The following table shows how the ministry calculates Producer A's closing PCOS bank balance for January.

January 2008 Producer A PCOS Bank for CBM Project 1		
Opening balance = December 2007 closing balance		\$42,000.00
Excess PCOS allowance over royalties	+	\$12,730.89
Credit for completed well events	+	\$20,000.00
Transfer from Producer B's PCOS bank for an interest acquired in a well event	+	\$15,000.00
Transfer to Producer C's PCOS bank for the sale of an interest in a well event	-	\$1,300.00
Royalties due	-	\$67.50
January 2008 closing balance		\$88,363.39

The tables below follow the example of Producer A's PCOS bank over the next two months.

February 2008		
Producer A PCOS Bank for CBM Project 1		
Opening balance = January 2008 closing balance		\$88,363.39
Excess PCOS allowance over royalties	+	\$3,179.76
Credit for completed well events	+	\$0.00
Transfer from the PCOS bank of another producer for an interest acquired in a well event	+	\$0.00
Transfer to the PCOS bank of another producer for the sale of an interest in a well event	-	\$0.00
Royalties due	-	\$573.41
February 2008 closing balance		\$90,969.74

March 2008		
Producer A PCOS Bank for CBM Project 1		
Opening balance = February 2008 closing balance		\$90,969.74
Excess PCOS allowance over royalties	+	\$0.00
Credit for completed well events	+	\$0.00
Transfer from the PCOS bank of another producer for an interest acquired in a well event	+	\$0.00
Transfer to the PCOS bank of another producer for the sale of an interest in a well event	-	\$0.00
Royalties due	-	\$40,418.76
March 2008 closing balance		\$50,550.98

Forms

For the ministry to calculate the royalty rates and PCOS allowances, producers and operators need to provide the ministry with certain information.

For guidelines to filling out the forms mentioned below, please see our website at www.sbr.gov.bc.ca/business/Natural_Resources/Oil_and_gas_royalties/forms.htm

Well Operators

Each time production from a CBM well event begins or is suspended, the well operator needs to submit a *Notice of Commencement or Suspension of Operations* (**BC11**) and specify CBM as the product type. The ministry has added a checkbox for CBM under the heading, Commencement/Resumption of Well Activity.

Battery Operators

Each time there is a change in ownership of a CBM well event, the battery operator must submit an *Ownership Interest Statement* (**BC12**).

Once production from a CBM well event begins, the battery operator must submit a *Monthly Production Statement* (**S1**) and *Monthly Disposition Statement* (**S2**) each month.

Project Operators

For each year of the CBM project, the project operator must submit an *Application for a Coalbed Methane Producer Cost of Service Allowance* (**BC26**) to the ministry.

Producers

Once production from a CBM project begins, each producer must report their shares of marketable gas produced from each well event on a *Marketable Gas and By-Product Producer Allocations Report* (**BC08**).

For each month of the CBM project, producers must submit copies of sales invoices to the Ministry of Energy, Mines and Petroleum Resources.



Need more info?

Oil and Gas Royalties and Freehold Production Tax website: www.sbr.gov.bc.ca/business/Natural_Resources/Oil_and_gas_royalties/oil_and_gas_royalties.htm

Telephone (Victoria): 250 952-0192

Toll free in Canada: 1 800 667-1182

Fax: 250 952-0191

E-mail: Oil&GasRoyaltyQuestions@gov.bc.ca

The information in this bulletin is for your convenience and guidance and is not a replacement for the legislation. The *Petroleum and Natural Gas Act* and Regulations are on our website at www.sbr.gov.bc.ca/business/Natural_Resources/Oil_and_gas_royalties/legislation.htm