

The Reasons for JP-90/95 – Lest We Forget

It would seem that many of the people making decisions on processing non-owner gas or fluids in existing facilities do not remember why the Joint Industry Task Force on Processing Fees (JP-90) was established. In the late 80's many plant owners were charging fees for processing that were, to say the least, outrageous. Fees calculated using rates of return of 40% and based on the replacement capital cost of the facilities, were not uncommon. When processing fees approached \$0.80/mcf, and gas prices averaged \$1.20/mcf, the parties hurt by the high fees, small producers and royalty holders, started to lobby the Alberta government to regulate the processing industry. The government, in its capacity as the provinces largest mineral owner, was also a big loser, as processing fees were deducted from royalties. The Minister of Energy asked the industry to resolve the problem; before the government was forced to regulate it. In response, the industry producer associations formed a Joint Industry Task Force, which developed the JP-90 Guidelines for Gas Processing Fees. The JP-90 guidelines were generally accepted and industry gradually changed the way processing fees were calculated. JP-90 fees called for the use of a capital rate base that reflected the actual cost of older facilities, a rate of return based on actual tax rates and long term bond rates, and the capacity of the facility, rather than throughput. In 1990, bond rates were 9.9%; the effective tax rate for resource companies was 35%, so a JP-90 rate of return was 23%.

Since many industry plant owners were still calculating fees based on replacement cost, another industry task force was formed in 1995. The JP-95 Task Force reinforced the principles developed in JP-90 and clarified the use of an appropriate capital base and the proper calculation for a rate of return. In 1995, bond rate were 8.0%, the corporate effective tax rate for resource companies was 37%, so the calculation yielded a JP-95 rate of return of 20%. Still some industry processors did not change their fees.

The JP-90/95 Guidelines were put to the test in 1996, when Rider Resources filed an application with the EUB to have the Canadian Occidental Keystone Gas Plant declared a common processor. The essence of the dispute was that Rider was not allowed to take their NGL products in kind, as these were retained by the processor as compensation for processing. At the time, the NGL's were worth an estimated \$1.97/mcf. Rider asked the EUB to set reasonable fees at the Canadian Oxy plant. Cdn. Oxy argued that the common processor application should not set the stage for an order regulating gas processing fees. The Board believed that "all the factors that may prevent the parties from obtaining fair value for their resources" should be considered; and, under the Oil and Gas Conservation Act, processing fees is one of the factors to be considered in a common processor application. During the hearing, both parties were compelled to present evidence that could be used to calculate processing fees, and much of the argument centered around the fees calculated in accordance with JP-90/95. The Board concluded that the effective processing fees that were being charged by Cdn. Oxy were "excessive", and declared the Plant a common processor. They then gave the

parties 90 days to negotiate a processing fee, and stated that, if they were asked to set the fees, “the Board would rely on the JP-90/95 Guidelines for determining the appropriate fees”. This precedent means that any facility charging excessive fees could be declared a common processor, or a common carrier.

Today, we are again finding a lot of people who seem to believe that calculation of processing fees is completely at the processors discretion, and they are not accountable to anyone. When asked for the bases of their fees, they are not willing to disclose the capital base, capacity or rate of return used in their calculations. Some are even using a 25% rate of return in their calculations. Currently, long term bond rates are 5.5%, or less, the effective tax rate for a resource company is 34%, and going down, so the JP-95 rate of return should be 16%. Processors that continue along the path of non-disclosure and quoting unreasonable fees, do so at their own peril. The EUB can still intervene, and will use JP-90/95 as the test of whether processing and transportation fees are considered “reasonable”.

Stay tuned for new developments in the guidelines – The birth of JP-04.

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