

February 11, 2008

SEC:

I welcome this opportunity to add my comments to the SEC's consideration of reserve reporting for oil and gas. I will begin my comments with a general overview that I will refer to in my specific answers to the questions you posed.

Overview

To begin with, I feel that the SPE/WPC/AAPG/SPEE recommendations are an excellent further step in our efforts to make reserve reporting relevant and transparent.

This is especially true in the area of probabilistic viewing of reserves. While this approach will blur the standard categorization of reserves, it paints a much more complete picture of a firm's resource assets. Indeed, probabilistic reserves are intellectually honest, maximizing information and minimizing unwarranted detail.

That being said, further work is needed especially in the area of economic and the concept of "reasonably certain". Using current prices and economic conditions to imply that future resources are economically viable reserves is not reasonable certainty and does not meet the firm's fiduciary responsibility to be "certainly reasonable" in communicating its perception of value in its reports to its shareholders, regulators and the public. This is but one of many failings that cause many in the investment analyst community to see current reserve reports as irrelevant.

This introduction summarizes my comments to the SPE/WPC work that I submitted on 1/15/07, my paper, SPE – 30042, "Virtual Reserves – And other measures designed to confuse the investing public", and my book, "Confessions of an Energy Price Forecaster – A 12 Step program to Enlightenment", Outskirts Press, Denver Colorado, 2007, ISBN 9781432717049.

Transparency and Accountability

Both in-house and 3rd party expertise in the industry are very capable in analyzing the physical characteristics of reserves in a probabilistic manner. However, the imposition of "current economic and operating conditions" are not only a "cop out", but make much of this work, while consistent, consistently wrong and misleading. Using deterministic critical components such as price in a probabilistic analysis is mixing apples and oranges.

Indeed, if one assumes that the year end price is really a probabilistic input to the analysis, the result will always be zero reserves because to probability of a single point occurring is zero. In other words, while any single point estimation for price may be any interesting scenario or snap shot of reserves, the only certainty is that there is a zero percent chance of that value actually occurring over the future life of those reserves.

We can also take the example of the firm that has taken reserves off of its books because of a price decline at the end of its fiscal year, but is still investing in those reserves, because it fully expects prices to rebound. Is such production and the remaining reserves an asset?

At the risk of belaboring this point, the following table notes just how volatile prices have been at year-end or even in the yearly averages.

Oil Price (\$/bbl)						
<u>Year</u>	<u>12/31</u>	<u>Min</u>	<u>10%</u>	<u>Avg.</u>	<u>90%</u>	<u>Max</u>
1986	17.94	10.42	11.99	15.05	17.59	26.57
1987	16.70	15.15	17.78	19.16	20.74	22.39
1988	17.25	12.60	13.90	15.97	17.55	18.60
1989	21.80	17.05	17.91	19.59	20.74	24.65
1990	28.45	15.30	17.41	24.52	34.49	40.40
1991	19.10	17.85	19.45	21.52	23.38	32.00
1992	19.50	17.85	18.80	20.57	22.20	23.15
1993	14.15	13.90	16.42	18.46	20.40	21.05
1994	17.75	13.95	14.65	17.20	19.40	20.75
1995	19.58	16.88	17.38	18.43	19.75	20.53
1996	25.93	17.45	19.09	22.16	25.06	28.10
1997	17.64	17.63	18.69	20.60	23.02	26.63
1998	12.05	10.72	11.84	14.36	16.39	17.83
1999	25.60	11.38	12.33	19.31	25.48	27.98
2000	26.80	23.85	26.18	30.36	34.23	37.20
2001	19.84	17.45	19.78	25.96	29.38	32.19
2002	31.20	17.97	20.48	26.15	29.76	32.72
2003	32.52	25.24	28.00	31.00	34.93	37.83
2004	43.45	32.48	34.47	41.47	49.76	55.17
2005	61.04	42.12	47.54	56.70	61.89	69.81
2006	61.05	55.81	59.23	66.24	73.93	77.03

Even the futures strip is only a snap shot of the market's current view of the future. Rather, price estimations for the future must also be expressed as a probability distribution to have any credibility at all. The firm should use and disclose its price assumptions for the future that it uses to justify its investments. In doing so, regulations will need to be clarified such that these disclosures will not be considered to violate anti-trust laws or seen as collusion. Those firms that do not wish to make such disclosures on the grounds of "proprietary information" will have to make their case to the public on other grounds in competition with those firms that opt for full disclosure.

An additional issue is the use of a "standard" discount rate. This eliminates the ability of the user of the reserve data to see either the firm's risk tolerance or to apply his own discount rate reflecting his own risk tolerance.

Response to Posed Questions

1. Yes. Full disclosure and add an explanation or defense of assumptions.
2. Yes. Full probabilistic spectrum of resources. No specific categories (i.e., proved) would be required.
3. Yes. However, the Commission should fund a study of the best way to handle economics and price.
4. See the probabilistic blurring of categories, above.
5. See full disclosure, above.
6. Certainly Reasonable. This should improve quality. No. No.
7. No Comment.
8. Yes. Transparency and the defense of assumptions. I.E., "We're drilling it anyhow, and here's why."
9. Yes. Need to have a look at the firm's vision of the future and the credibility of those assumptions. No. No.
10. No. Price is a range in the same sense as any other parameter in the reserve analysis. No. Yes. Too optimistic or pessimistic views will be quickly discredited in the public. Yes. Scenarios explain the points in the range. (See "Confessions of an Energy Price Forecaster.")
11. Yes. Quality = Relevance.
12. See 11.
13. Yes. Full disclosure with teeth.
14. Probability analysis
15. 3rd parties would not be needed unless that firm lacks the analytical expertise.

As noted in question 3, the Commission should fund a study of best practices and how to use one or a combination of these practices to supplant the concept of current economic and operating conditions and how to account for the time value of money, reinvestment rates and risk tolerance.

I hope that these comments will be of use.

Sincerely,

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