



May 2, 2013

## OIL SANDS INFORMATION BULLETIN 2013-10

### Subject: GUIDELINES ON SUPPORT SERVICES COSTS

Pursuant to [Ministerial Order 97/2012](#), Alberta Energy was directed to “issue guidelines on support services provided through a central business model for which the costs may or may not be considered an allowed cost under the Oil Sands Royalty Regulation, 1997”. Ministerial Order 97/2012, issued on October 31, 2012, is the Minister’s decision on the recommendations made by the Imperial Oil Sands Dispute Review Committee (Imperial Committee) on the Imperial Oil Resources’ Cold Lake Project.

This Information Bulletin provides guidelines for determining the eligibility of support services costs submitted under the [Oil Sands Royalty Regulation, 1997](#) (OSRR 1997). It applies to all oil sands royalty Projects for the production year 2008, provided that section 38(5) of the [Mines and Minerals Act](#) applies, and any production year, including 2008, in which an objection has been filed with the Director of Dispute Resolution regarding a support services cost and the dispute resolution process has not been concluded. It is not applicable to cost determinations pursuant to the [Oil Sands Royalty Regulation, 2009](#) and the [Oil Sands Allowed Costs \(Ministerial\) Regulation](#).

### OIL SANDS ROYALTY REGULATION, 1997 (OSRR 1997)

For oil sands royalty purposes, the allowed costs of a royalty Project for a non-qualifying joint venture are defined under Schedule 1 of OSRR 1997. More specifically, section 2 of Schedule 1 states:

- 2** *Subject to the other sections of this Schedule, a cost is an allowed cost of a Project only to the extent that:*
- (a) it is directly attributable to the Project,*
  - (b) it is reasonable in relation to the circumstances under which it is incurred,*
  - (c) it is incurred by or on behalf of the Project owners of the Project,*
  - (d) it is incurred on or after the effective date of the Project and on or before December 31, 2008, and*
  - (e) it is incurred to*
    - (i) recover oil sands from the development area of the Project,*
    - (ii) purchase oil sands products for processing or reprocessing in one or more processing plants that are part of the Project,*

- (iii) *process or reprocess oil sands or oil sands products in one or more processing plants that are part of the Project,*
- (iv) *process*
  - A. *oil sands or oil sands products recovered from the development area of the Project, or*
  - B. *oil sands products purchased and previously processed in one or more processing plants that are part of the Project, in one or more processing plants that are not part of the Project, before the oil sands products obtained as a result of such processing are delivered at a royalty calculation point,*
- (v) *transport oil sands and oil sands products from one part of the Project to another,*
- (vi) *transport oil sands and oil sands products described in sub-clause (iv)(A) or (B) from the Project to the processing plant or plants referred to in sub-clause (iv) that are not part of the Project,*
- (vii) *market an oil sands product obtained pursuant to the Project,*
- (viii) *conduct planning, designing and engineering in relation to expansions of the Project,*
- (ix) *conduct research that is directly attributable to the Project, other than basic research referred to in section 3(g) of this Schedule, or*
- (x) *provide field, office, administrative or other services in relation to the activities described in subclauses (i) to (vi) and (ix). (emphasis added)*

Section 3 of Schedule 1 also sets out the types of costs that are not allowed costs. Section 3(a) states:

- 3** *A cost is not an allowed cost of a Project*
  - (a) *if it is in respect of overhead or an administrative expense, including internal audit, “in-house” legal and other like expenses, of the operator, a Project owner or an affiliate of either, and is not allowed under section 2(e)(x) of this Schedule*

Costs identified in section 3(a) will normally be disallowed unless a case can be made that they are allowed under section 2(e)(x) of Schedule 1.

## **IMPERIAL COMMITTEE RECOMMENDATIONS**

The meaning of “field, office, administrative or other services” and of “overhead or an administrative expense” (collectively referred in this guideline as “support services”) and the circumstances in which support services costs may be allowed costs of an oil sands royalty Project was addressed by the Imperial Committee.

The Imperial Committee recommended that (as varied by Ministerial Order 97/2012):

**134(d)** *“... subject to the regulation, the cost of providing support services to persons who have been accepted by Alberta Energy as providing services to the Project and whose salaries, wages and benefits have been determined to be allowed costs be treated as allowed costs for the purpose of the royalty regime.”*

Furthermore, the Imperial Committee made the following recommendations relative to support service costs:

**72.** *“... Overhead is a cost that can be directly attributable to the Project if it is a cost described in section 2(e)(x).”*

**79.** *“... determinations as to whether costs are excluded or included overhead for the purpose of determining whether they are allowed costs of necessity are very much fact driven.”*

**81.** *“... the fact that some support services are provided through a central business model does not exclude them from the category of allowed costs... But not all of the head office costs could be conveniently identified with or directly related to the operation of the Project ... The question to be asked is: when the functions of the central cost centre being allocated are analyzed, do they primarily relate to support services to various different operational activities including the Project, which, for the purpose of cost and efficiency, are delivered through a central office, or are they cost centres which are primarily serving corporate interests, but whose level of activity may be driven in part by the facility operations. In the former case, the costs would in general terms be costs contemplated by section 2(e), while in the latter case they may be excluded by section 3(a).”*

To summarize the analysis, at paragraph **85**, the Imperial Committee stated that the examination of head office costs requires two steps:

1. an analysis on whether the support service is one that is in relation to the (allowed) activities in section 2(e); and
2. a determination if the costs are properly allocated so that only costs that are directly attributable to the Project are claimed.

## **ANALYZING SUPPORT SERVICES COSTS**

Considering the recommendations made by the Imperial Committee, Alberta Energy provides the following guidelines in determining the eligibility of support services costs submitted under OSRR 1997:

1. When claiming such support services costs, a Project operator must be able to distinguish between:
  - costs that are incurred to carry out the activities under section 2(e)(i) to (ix); and
  - support services costs, which are costs claimed under section 2(e)(x) to support the activities under section 2(e)(i) to (vi) and (ix), including any section 3(a) costs that are allowed by section 2(e)(x).
2. The Project operator must likewise be able to show costs that are clearly excluded from claimed allowed costs, such as:

- those related to internal audit
  - those related to “in house” legal, and other like expenses
  - those incurred to support the marketing of an oil sands product obtained pursuant to the Project
  - those incurred to support the conduct of planning, designing and engineering in relation to Project expansions
  - those related to function or activities not in any way related to oil sands, such as natural gas marketing and refining.
3. Support services costs that cannot be assigned to an oil sands Project in its entirety must be allocated between Project and non-Project use. As Alberta Energy’s determination of a cost’s eligibility will depend on documented facts, the Project operator must provide sufficient evidence, to the satisfaction of Alberta Energy, of how those support services are shared between or among business units, including the Project. The Project operator is also responsible for choosing a reasonable and appropriate allocation methodology that is properly documented and auditable by Alberta Energy.
4. For support services costs, Alberta Energy will ensure the following:

- The cost claimed must be for a function necessary to support section 2(e) activities except section 2(e)(vii) and 2(e)(viii).

[Table 1 \(Overhead/Support Services Activities\)](#) provides a list of support services activities that will be allowed, subject to audit by Alberta Energy.

- Costs that are primarily corporate in nature are excluded.

To be an allowed cost, the support services function must not primarily serve general corporate interests. If the direct connection to the Project is not clear or it is not readily apparent that it relates to the activities listed in section 2(e)(i) to (vi) and (ix), then the cost is not allowed.

In addition to internal audit and “in-house” legal identified in section 3(a), [Table 1](#) of this guideline provides examples of support services activities that are primarily corporate in nature and therefore not allowed.

- Costs are allocated between Project and non-Project components using a reasonable and appropriate allocation methodology.

The method of allocating costs provided through cost centers, for example, must be one that fairly determines the portion of the costs which can be directly attributable to the Project.

## COST ALLOCATION METHODOLOGIES

The costs of support services, which are provided on a shared basis, may be allocated based on a method that is reasonable and appropriate to the situation. The preferred methodology is reasonable if it is able to allocate costs that are directly attributable to the Project and the allocated costs are in direct proportion to the service received by the Project. The methodology is appropriate if it matches the support service activity, the cost of which is being allocated between Project and non-Project use. The preferred allocation method should be the same from year to year unless significant business changes are later adopted by the company.

The allocation methodology used must be documented and auditable. Documentation should include specific costs being allocated and indicate how the allocation methodology is logically related to the cost being allocated. This documentation must be made available to Alberta Energy for audit purposes.

The following are examples of allocation methodologies which may be used to allocate a portion of overhead or support services cost to an oil sands Project. The portion of cost allocated to the Project is determined by the ratio.

### 1. Headcount

Headcount is a common way of allocating head office costs and the easiest to implement. The main assumption with headcount is that the support service provided to the different departments or business units is the same across all cost centers, i.e., there is no distinction between “heavy” users and “light” users. The cost to the department or business unit is in direct proportion to the number of its users.

Headcount is best used in allocating “people” support services costs, such as payroll and employee benefit administration, among others.

**Headcount ratio (HCr)** is used to determine the proportion of support services costs that are allocated to an oil sands Project. It is obtained by dividing the total number of Project employees by the total number of employees serviced. “Project employees” include all staff working on the Project whether they are full-time, part-time or contractual employees.

$$\text{HCr} = \frac{\text{Project employees}}{\text{Project employees} + \text{non-Project employees}}$$

### 2. Square Footage/Floor Space

Square footage or floor space method allocates costs in the same proportion as amount of floor space occupied by each department. It is most appropriate when the costs being allocated are building-related (e.g., lease costs, rent, building

maintenance) and individual departments occupy specific floor space. When using this method, the Project operator must clarify which floor space is to be treated as occupied by the support services department.

Consider, for example, a HR Department of the company providing HR support services to the Project and non-Project units. If this HR Department occupies two out of the ten floors of the building being rented by the company, then that HR Department's share of the total rent cost will be equivalent to 20%. The rent cost allocated to the Project will be further determined by multiplying the HR Department's share of the rent by the headcount ratio (i.e., total Project employees divided by the total number of employees serviced by the HR Department). In this example, the cost allocated to the Project is determined by a two-step process involving two allocation methodologies, i.e., floor space and headcount.

### 3. Activity-Based Allocation

Activity-based allocation is used to allocate head office costs to a function or activity (e.g., purchasing, accounts payable) on the basis of identified cost drivers (e.g., purchase orders, invoices). The cost of activity allocated to an oil sands Project is in direct proportion to the number of transactions completed for the Project.

$$\text{Activity-Based ratio (ABr)} = \frac{\text{number of Project transactions completed}}{\text{total number of transactions completed}}$$

If the amount of time necessary to complete the work varies significantly from transaction to transaction, the cost allocation process must likewise take into account the differences in time required to complete the work.

### 4. Workstation Allocation

Information technology expenses may be allocated using workstations. Workstations are distinct areas where work of a particular nature is performed or carried out. Each workstation is typically outfitted with equipment and furnishings for one person and usually including a computer. The computer is dedicated to a professional or business use and is usually attached to a local area network to allow for the access and sharing of network resources.

The IT cost allocated to an oil sands Project is in direct proportion to the number of workstations assigned to the Project.

$$\text{Workstation ratio (Wr)} = \frac{\text{number of workstations in the Project}}{\text{total number of workstations sharing in the IT cost}}$$

## STANDARD OF EVIDENCE

In order for Alberta Energy to properly determine whether costs being claimed may be allowed or not, Project operators must submit sufficient and appropriate documentary evidence. Again as indicated by the Imperial Committee, the determination of whether overhead costs are excluded or included is very much fact driven. Evidence must be valid, relevant, and impartial to be considered appropriate. Acceptable standards of evidence might include:

- auditors' direct, personal knowledge, obtained through physical observation, or mathematical computation
- documentary evidence obtained directly from independent external sources (external evidence)
- documentary evidence that has originated outside the Project operator's system, but which has been received and processed by the Project operator (external-internal evidence)
- internal evidence consisting of documents that are produced, circulated, and stored within the Project operator's system (internal evidence)
- verbal and written representations by the Project's officers, directors, owners, and employees

Examples of acceptable documentary evidence include, but not limited to, the following:

- verified timesheets or time records
- contracts
- invoices
- insurance policies
- lease agreements
- organizational charts

The sufficiency or quantity of evidence needed for audit purposes will be determined by Alberta Energy.

Questions regarding this Information Bulletin may be directed to:

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**Authorized by:** Anne Denman  
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**Attachment – Table 1 Overhead/Support Services Activities**

**Table 1  
OVERHEAD/SUPPORT SERVICES ACTIVITIES**

The following support services activities may be allowed provided sufficient detailed information satisfactory to Alberta Energy are submitted for audit purposes.

Support Services Categories	Allowed Activities	Proposed Allocation Methodology for Allowed Activities	Not Allowed Activities
Human Resources	<ul style="list-style-type: none"> <li>• Recruitment services, including campus and non-campus recruitment, job postings and job interviews</li> <li>• HR advisory services</li> <li>• Payroll administration</li> <li>• Employee pension and benefit administration</li> <li>• Development and administration of workplace policies, guidelines and programs for employees</li> </ul>	Activity-based	
Controller, Financial, and Treasury	<ul style="list-style-type: none"> <li>• Project planning, budgeting, operations analysis, government reporting, and related business controls</li> <li>• Accounting for the physical assets and controllable equipment of the Project, including verification of their continued existence and use</li> <li>• Processing of equipment and asset transfers</li> <li>• Accounting support for the ongoing operations of the Project</li> <li>• <i>Pension services</i>, which include:               <ul style="list-style-type: none"> <li>○ overseeing pension plan assets,</li> <li>○ administration of employee financial plan, including retirement funds</li> </ul> </li> <li>• <i>Insurance services</i>, which include:               <ul style="list-style-type: none"> <li>○ overseeing insurance programs</li> <li>○ contract reviews</li> <li>○ claims management</li> </ul> </li> </ul>	Activity-based, Headcount	<ul style="list-style-type: none"> <li>• <i>Corporate finance</i>, including providing business advice on Project economics</li> <li>• <i>Cash operations</i>, such as:               <ul style="list-style-type: none"> <li>○ cash forecasting</li> <li>○ foreign exchange trading</li> <li>○ issuance of commercial paper</li> <li>○ money market investing</li> <li>○ inter-company financing</li> <li>○ letters of credit</li> <li>○ management of bank accounts</li> </ul> </li> <li>• <i>Credit management services</i>, such as:               <ul style="list-style-type: none"> <li>○ providing adjudication of credit limits</li> <li>○ financial stability reviews for suppliers</li> <li>○ management of account receivables</li> </ul> </li> <li>• Financing/Debt negotiations</li> </ul>



Support Services Categories	Allowed Activities	Proposed Allocation Methodology for Allowed Activities	Not Allowed Activities
Purchasing / Procurement	<ul style="list-style-type: none"> <li>• <i>Contracting services</i> for the Project, including contract preparation and administration, price negotiations, and day-to-day management of material and service agreements</li> <li>• Management of warehousing activities, logistics, inventory control, disposal of surplus equipment, material catalogue activities</li> <li>• Management of procurement services, including staffing, development of annual business plans, and setting procurement strategies and direction</li> <li>• Accounts payable, i.e., payment of invoices for third party goods and services, taxes, and government assessments.</li> </ul>	Activity-based	
Health and Safety	<p>Health and Safety provided to meet Alberta's requirements for workers' compensation and occupational health and safety, such as:</p> <ul style="list-style-type: none"> <li>• <i>Industrial hygiene services</i> for identifying and evaluating workplace environmental exposures which may present health risks, including: <ul style="list-style-type: none"> <li>○ identification of health hazards</li> <li>○ assistance with ergonomic concerns</li> <li>○ advice on occupational exposure limits</li> <li>○ advice on health hazards control and protective equipment</li> <li>○ training and education, and advice on health issues related to spills, air emissions, or waste disposal</li> </ul> </li> <li>• <i>Medical services</i>, such as <ul style="list-style-type: none"> <li>○ periodic employee health assessments based on regulations</li> <li>○ job requirement and exposure potential</li> <li>○ pre-placement health assessments</li> <li>○ advice and assistance for first aid</li> </ul> </li> </ul>	Headcount, Activity-based	

Support Services Categories	Allowed Activities	Proposed Allocation Methodology for Allowed Activities	Not Allowed Activities
	<p>procedures at Project sites</p> <ul style="list-style-type: none"> <li>○ advice on health-related matters</li> <li>○ health promotion and education programs</li> <li>● <i>Security management</i>, such as: <ul style="list-style-type: none"> <li>○ in-site security management</li> <li>○ investigation of security breaches including interfacing with local law enforcement authorities</li> <li>○ performing periodic site penetration tests to guard against loss from unauthorized access to Project facilities</li> </ul> </li> </ul>		
Stakeholder	<ul style="list-style-type: none"> <li>● Stakeholder consultation necessary for Project operation or as a prerequisite for Project application or Project amendment</li> <li>● Commitments made to stakeholders pursuant to <a href="#">Information Letter 2010-44</a></li> </ul>	N/A	
Corporate			<ul style="list-style-type: none"> <li>● Quarterly and annual financial reporting</li> <li>● External regulatory filing requirements <u>unless</u> required for Project activities</li> <li>● Senior executive management</li> <li>● Business process re-engineering</li> <li>● Other corporate activities or functions that would be undertaken without the existence of the oil sands Project</li> </ul>

Support Services Categories	Allowed Activities	Proposed Allocation Methodology for Allowed Activities	Not Allowed Activities
Telecommunication and Information Technology (IT)	<ul style="list-style-type: none"> <li>• IT hardware (and their maintenance), IT software (including licenses), and IT client support services for employees or personnel providing support services to the Project</li> <li>• Telecommunication equipment, including their operation and maintenance, used for the Project</li> <li>• Local area network</li> <li>• Electronic data specific to the Project and required for Project operations and reporting, including servers, storage and maintenance</li> </ul>	Workstation	
Building/Facilities	<ul style="list-style-type: none"> <li>• Lease costs and maintenance</li> <li>• Custodial services</li> <li>• Utilities</li> <li>• Facilities administration</li> <li>• Building security</li> </ul>	Floor Space, Headcount	<ul style="list-style-type: none"> <li>• Building renovations and improvements</li> <li>• Unrelated workplace amenities, such as fitness center, gaming room or play station, yoga studio, food café, etc.</li> </ul>