

A Supplement to

Oil and Gas Investor

THE ECONOMICS OF OUTSOURCING

A Special Report Sponsored By

Baker

Energy



COGNICASE

JUNE 2002

UNLOCK YOUR HIDDEN VALUE

INTRODUCTION

In today's demanding business world, where good time-management, people with skills and capital are growing scarce, there is no longer any room for a back-burner project or asset. That luxury is going away as managers say, "Do it or divest it."

Luckily, among the many new tools found in the corporate toolbox today, outsourcing ranks higher and higher as a means to achieving success. Consider the benefits: it allows a corporation to unlock hidden value in oil and gas assets or data, and it gives its employees breathing room to focus on their core skills, whether at the head office or in the field at the wellhead. Yet as those employees renew their focus, functions they have performed previously do not go untouched, to languish until somebody notices what is missing.

For overworked and understaffed energy-company managers who are juggling multiple priorities, outsourcing is a solution. Oil and gas properties that have potential, but that may fall outside the to-do list of

today, can now be managed rather than ignored.

It's all a matter of timing—and who has the time to devote to key functions as well as those of lesser importance that still add to the whole pie.

Outsource providers are equipped in a number of ways to help you reach your goals. For one thing, they have maintained extreme focus on a narrow niche—but they go deeper into it than any energy-company employee can. Outsource providers typically employ the latest technologies and best-trained experts, so you do not have to worry about keeping up with best practices and technical and software enhancements.

This leaves managers freer to focus on strategic matters, which in the end are what drives a company forward. This sponsored special report brings to light some trends in outsourcing and introduces some providers that can help take your company to the next level of efficiency.

—Leslie Haines, Editor

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ABOUT THE COVER: Illustration by Rob Barber.

A supplement to

**Oil and Gas
Investor**

a Hart Publication of
Chemical Week Associates

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WHY OUTSOURCE?

Managers find that outsourcing helps them better manage fluctuating personnel needs, and brings them expertise in areas not core to finding oil and gas or producing it.

ARTICLE BY GARY CLOUSER

Today's exploration and production companies, coping with volatile price swings that make personnel projections a constantly moving target, are learning they can find specialized companies willing to provide, on an outsourced basis, any function the companies don't include in their own core competencies.

The idea is not new: most E&P companies long ago recognized that specialty companies, through scale economics, could provide more expertise, more efficiently, at a lower price for a variety of functions. Included among them were drilling, well completions and logistics, such as transportation or road-building.

Now, another evolution (some say revolution) is occurring. Producers are increasingly turning to third parties—on a temporary or permanent basis—to provide or supplement numerous other functions that had previously been considered essential parts of the E&P business: back-office functions and even geological, geophysical, engineering and production operations.

The intended objective for using outsourcing is to obtain needed skills, services or technology that can be provided out-of-house better, or cheaper. By outsourcing, an E&P company can devote in-house personnel and capital to functions it believes are its main strengths, or areas that it can do better itself, and those areas the company believes differentiates itself from its peers.

Tad May, executive vice president of Brammer Engineering, says, "As the industry has consolidated, all aspects of the E&P food chain are outsourceable. The key is making sure you use people who have experience and understand your goals and objectives."

Companies can outsource partial functions of a department's operations, outsource all of those functions for a specific project, or outsource the functions of the department on a permanent basis. Tapping into these opportunities has provided producers not only with a means of reducing their in-house headcount, but also instant access to the latest technology and business practices, and the brightest minds. Access to outsourced personnel and services also has greatly improved and eased the entry access for start-up companies.

Expanding scope

"Back office," which used to simply refer to accounting and finance functions, now is much more. Now it includes a range of products and services involving information technology (IT), including a computer help desk; data gathering, processing, interpreting and disseminating; data management and storage; land administration; operations and production reporting; expense and rev-

enue accounting; payroll; royalty-check writing; gas or oil marketing; training of personnel; and even procurement. In short, back office in the independent E&P business has come to mean everything except finding and producing oil or gas.

"Many companies are turning to outsourcing simply because the technology is increasingly difficult to keep current, capital is restricted and qualified personnel are becoming more difficult to find and retain," says David Orr, senior vice president, Cognicase energy/telecom infrastructure "As a result of outsourcing, companies receive better service because the supplier has invested in both technology and people to a much greater extent than an E&P company would do internally."

Montreal-based Cognicase recently acquired Calgary-based Applied Terravision Systems. "With tight times, software procurement could be delayed, but outsourcing provides a viable technology solution that enables companies to remain competitive without bleeding their budgets," Orr says. Among benefits are scalability and flexibility, as well as the mitigation of risks in both IT and human resources. "In lieu of hiring additional staff and upgrading accounting computer systems, growing energy companies are moving to an application service provider-based business process outsourcing solution."

Most industry observers say the deal that propelled outsourcing was between PricewaterhouseCoopers and BP, which in 1996 agreed to a landmark 10-year outsourcing contract to manage the finance/accounting and related computer applications for BP's upstream operations throughout the U.S. Since that time, all the companies in the BP group have initiated outsourcing objectives in their business plans. PricewaterhouseCoopers says its business-process outsourcing is one of its fastest growing businesses.

E&P companies had been slow to adopt outsourcing back-office services but that is changing, says John Price, vice president, sales and marketing, for Novistar, the back-office and IT affiliate of Houston-based Torch Energy Advisers. "Over time, the industry will learn to be just as comfortable with back-office outsourcing as they are in allowing their bank to handle their cash account transaction information. Once the outsourcing model is embraced on a large scale, every E&P company will undergo pressure from their respective shareholders to evaluate back-office outsourcing to add bottom-line value to the company and increase the stock price."

Most of the growth in accounting and land-administration outsourcing services has come in the mid- and small-tier market space, Price says. Torch's most common

customer is the start-up that just made an acquisition and doesn't have existing infrastructure or personnel to support it.

"They can grow as fast as they want without having to deal with on-going information-system or accounting-personnel decisions," Price says. "The large-tier market space has been slow to adopt the outsourcing model mainly because they have existing systems, personnel and processes in place. Outsourcing decisions tend to be much more complex and take time to develop. It becomes a shift in business philosophy and everyone needs to buy into it."

Bill Baksi, manager of web solutions business development for Schlumberger Information Solutions (SIS), says the goal of outsourcing has evolved well beyond the stage of outsourcing noncore operations, so that the services can be defined at a lower cost that is scalable, predictable, and of a consistent quality. While retaining those attributes, the goal today is more to provide true operational flexibility, he says. For example, when SIS (GeoQuest at that time) operated the Houston Data Management Center in 1997, it was a secure-purpose-built center, connected to a high-speed network with a primary business offering built around providing data services.

That capability has now been extended to include delivery of application services and Internet-service-provider-hosting, making SIS a fully managed service provider facility. "A client from Houston can now visit a partner's office anywhere in the world and work on a project from the client's office, over a secure link having the project data and applications being served to him over the Internet. True operational flexibility," Baksi says.

Growth in outsourcing

Meta Group, which tracks outsourcing in information technology across all industries, says that, in IT alone, outsourcing is growing at an annual rate of 18% to 20% in North America and Europe, and 25% to 30% in the Asia-Pacific region. The business of outsourced IT is a \$120-billion industry, and projected to grow to \$300 billion by 2010, says Dean Davison of Meta Group.

"Outsourcing is far from homogeneous. Drivers include improving internal capabilities, reducing operating costs, financial engineering, allowing internal management to focus, and more rapid development of new skills," Davison says. "Any function can be outsourced if the remainder of the company is properly organized. But, even if the company outsources its entire IT, it would still need to determine business and unit objectives and computing requirements and need to manage the outsourcing vendor."

Outsourcing does not alleviate responsibility. IT outsourcing is frequently approached based on the belief that an outsourcing vendor will automatically be better, faster and cheaper at providing IT services. But most IT organizations realize that it is not that simple, nor that certain. Outsourcing carries with it costs and risks that must be assessed, and differ, for each company.

Terry Ray, Meta Group vice president, energy information strategies, says, "E&P firms have accepted outsourcing and tend to outsource IT, i.e. data management, application hosting, the help desk. They tend to stay away from outsourcing seismic and petrophysics. We are unclear as to the market size, however E&P firms typically spend 1% of their revenues on IT, and outsourcing could represent 25% to 50% of that."

Despite the peaks and valleys of the price and demand cycles, E&P companies must strive to have the best technology and personnel to compete. Outsourcing companies now offer technical services including geological and geophysical, seismic evaluations, reservoir engineering and management, land management, transportation logistics, production operations and gas measurement.

Jeff Myers, president of Associated Resources Inc., an outsourcing company, says, "A prototype E&P outsourcing firm is basically a fully staffed oil and gas operating company, only without the actual production or interests in the reserves." Even geological and geophysical, once thought to hold the inner-most secrets of an industry characterized by secrecy, can be outsourced. As has long been the case with the relationship between an individual E&P company and consultants, confidentiality and trust are essential.

Myers says the nature of an E&P company's growth has changed. "In the old days, companies grew by the drillbit. They grew slowly and methodically over a long period of time, which gave them a lot of lead time to adjust to increased levels of work. We have found that many companies have grown through acquisitions and sometimes double in size. They often do this several

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times during a five- or 10-year period. We have many clients who start companies, build them and then sell out entirely, only to do it all over again. It makes no sense to hire people as employees to do this since they end up laying them off."

Outsourcing for the peaks

While outsourcing in the E&P industry began with drilling, exploration was the last area to adopt outsourcing, says Daniel Tearpock, founder of Houston-based Subsurface Consultants & Associates and an ex-Tenneco Oil Co. geoscientist. In the past five years, exploration outsourcing has greatly expanded. "Many companies are now staffing for the valleys of activity in the industry's cycles. This is done in hope that the company will not have to go through the layoff-and-hiring cycles every few years."

Very small oil companies have outsourced for some time. "Out of necessity, they were the innovators. They couldn't afford the cost of a large, full-time staff, so outsourcing was the only viable option. Today, companies of every size are either taking advantage of outsourcing in one way or another, or reviewing it."

May, at Brammer Engineering, adds that now even major producers recognize that someone whose core competency is operating and project management can accomplish the job more efficiently and effectively.

Hal Miller, Conoco human resources and finding skills manager, says Conoco in the early 1990s, during a downward cycle, leveled its staff to run core business and began using consultants to handle the peaks in workload. "As we became comfortable with the quality of the outside consultants, we developed confidentiality agreements and directed the consultants' efforts on exploration teams as well, to fulfill short-term specialized skill needs."

"As companies grow over time, more of their people end up working on the legacy assets or core properties, and fewer work on developing new business or new plays," says Bob Peebler, president and CEO of Energy Virtual Partners, an E&P outsourcing firm. "What was core yesterday is non-core today if you are growing. We want to manage the core so they can come up with the future ideas [that investors are looking for]."

Baker Energy, along with a major oil company, helped create that formula when in 1998 it contracted with Baker Energy to manage the production operations of some mature legacy assets so the oil company's staff could focus on new projects, says John Young, vice president of Houston-based Baker Energy.

It was the challenge of Baker Energy to provide the "infrastructure of total capability." When Baker Energy exceeded agreed performance metrics, the word spread among other E&P companies. The number of these "total responsibility" operations has grown in number of properties from 26 in 1998 to more than 250.

Evaluating core competencies

One of the most important and difficult decisions

an E&P company has to make is honest self-determination of its strengths and weaknesses—its core competency. That cannot be based on size alone.

Arthur "Buzz" Gralla, who has been involved in financing E&P companies for more than 25 years and is presently senior vice president of Guaranty Bank, offers examples of the opposing ends of a company's core competencies and how outsourcing has been used. Houston-based Contango Oil & Gas Co.'s founders and management come from a financial background, which is its core strength. It has five in-house employees and outsources everything except financial and accounting services.

On the other hand, Spring, Texas-based Arena Energy has management that comes from a geology and engineering background, and outsources everything but those skills. From a banker's perspective, the fundamentals are still the same as they have always been: evaluate management and reserves. If the company lacks in-house expertise it had better demonstrate that it has outsourced that expertise, says Gralla.

Arena Energy was formed in 1999 to pursue development and low-risk exploration drilling opportunities on the Gulf of Mexico shelf. Its founders included two geologists and Mike Minarovic, managing director and a reservoir engineer. The company currently has nine full-time employees, six responsible for generating oil and gas opportunities and three for support. Arena has outsourced production, drilling and facility engineering operations, as well as geophysical reprocessing, accounting, regulatory permitting and approvals, gas marketing, and land due diligence and title work.

"Basically, every job function other than our core competencies of geology and reservoir engineering has been outsourced," Minarovic says. "As we have grown, we have added an in-house accountant and over time will add operations capability with an operations engineer, but outsourcing will remain a critical part of our business."

The primary benefits of outsourcing include flexibility, the ability to work with the best talent in the industry, and the capability to remain focused on core competencies, he says. "The only negatives we have seen are some scheduling and prioritization problems when consultants are busy."

Value versus cost

Denver-based Fidelity Exploration & Production Co. outsources about 20% of its general and administrative man-hours, mainly IT-related, and about an equal amount of its geology and geophysical work to supplement the company's existing departments in times of heavy workload, usually prompted by a pressing deadline to take advantage of a business opportunity.

The direct costs for outsourcing probably are higher than paying for the work with in-house personnel, says Betty Dieter, manager of administration, but outsourcing is cost-effective if one factors the opportunity that would be lost because of insufficient personnel.

BAKER ENERGY

Baker Energy, a leading operations and maintenance provider serving major and independent oil and gas companies, delivers innovative services that keep pace with the changes in the energy industry.

For both mature and emerging assets, Baker Energy has gone beyond outsourcing to pioneer the operations consolidation OPCOSM Value Network Model, which has broken through the cost floor that outsourcing alone cannot.

With the OPCO Value Network oil and gas companies have achieved operating cost savings of 10% to 20% and have sustained that savings since implementing the value network model. Health, safety, environmental and compliance (HSE&C) performance has stayed high, and production decline has been reduced in several mature fields. The success of the OPCO

model depends upon the following key elements:

Consolidation and Economies of Scale. Baker Energy acts as the network manager, consolidating production operations between the wellhead and the sales meter for multiple companies. Participating companies share costly resources and management tools such as helicopters, marine vessels, computerized management systems, and technical specialists.

Baker Energy is responsible for operations functions such as personnel recruiting and training, operations, maintenance, safety and environmental compliance, and full supply chain management, including logistics and procurement.

By sharing resources in a single, consolidated operation, those resources can be used more efficiently. Costs are distributed over a greater number of production facili-

ties and produced volumes, which reduces each company's lifting cost.

Operating efficiencies are further improved by standardizing business processes, systems, and practices throughout the consolidated network. As more companies join the network, economies of scale cut each company's lifting costs further. Total production operated by Baker Energy's OPCO network is already among the top 10 of all Gulf of Mexico producers.

Performance-Based Contracts. As the OPCO network manager, Baker Energy is responsible for production operations for participating oil companies under performance-based contracts. The oil company monitors Baker Energy's performance according to agreed-upon measures, and Baker Energy determines how to deliver the results, making daily operations decisions such as supply vessel routing and

OPCO EXAMPLE 1

Job: Oklahoma and Texas Panhandle producing properties: operating cost reduction and production uplift

Background: Operated five producing areas with 1,276 producing wells.

Value: \$15,750,000 (\$10,500,000 increase in annual operating income) from increasing production while reducing operating cost.

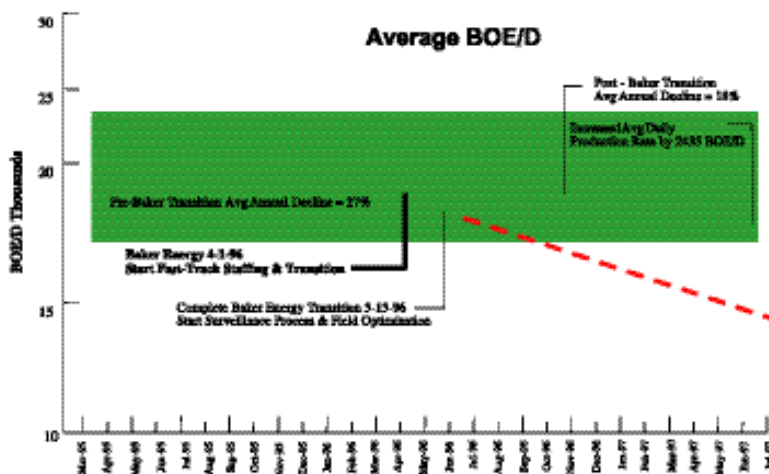
Value: Increased production by an average of 2435 BOED, increasing revenue by \$13,500,000 over 1.5 years (actual sales vs. depletion plan rate). Peak increase was 3,100 BOED.

Innovation: Increased level of engineering surveillance, identifying opportunities to increase production systems reliabilities. Reengineered and implemented well soaping program. Revised choke settings, pump speeds and strokes, and increased utilization of pump-off controllers. Increased response time to getting wells back on production after shut-downs. Increased workforce motivation and accountability to agreed to key performance indicators (KPI) for operation, and individual KPI.

Value: Achieved \$1,800,000 per year reduction in labor costs by improving work processes, then balancing work load and staff size.

Innovation: Performed workload analysis after prioritizing wells and equipment. Assessed high value work requirements, prioritized tasks on daily basis, and reduced workforce upon takeover of operations by 47%.

Oklahoma Producing Properties



OPCO EXAMPLE 2

Job: Main Pass area OPCO consolidation

Background: Six major production platforms with more than 30 unmanned structures. Equipment includes 30,000-horsepower critical equipment. Sixty producing wells: gas-lifted oil and flowing gas.

Value: Increased client's operating income by \$9,500,000 in first year (\$5,000,000 in increased production and \$4,500,000 reduction in operating cost). Production increased 8% above historical average, and fixed client's operating cost at 30% below historical average. Improved safety and environmental performance from previous operator's historical levels.

Innovation: Designed and implemented total surface operations consolidation (OPCO) model in Main Pass, in a fixed-fee, performance-based agreement. Step changes from the traditional field operating model driving this value creation include:

- Optimizing compressor loading,
- Redesigned work management, execution and training based on prioritized tasks which are driven by meeting the contractually-agreed key performance indicators (KPI),
- Increased resource (boats, helicopters, instrumentation, automation and mechanical maintenance technicians, management systems) sharing within the area with mul-

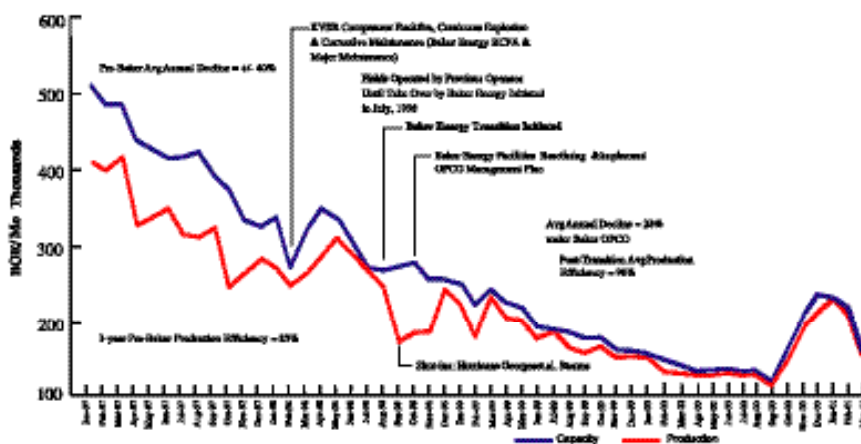
iple producers,

- Aligning all stakeholders (client-producer, Baker, Baker's employees and third-party service providers) interests, focusing each individual on achieving the same performance metrics to which Baker and the client agreed contractually,

- Applying information technology, including geographic information systems (GIS)-based Logistics Support System (LSS) and a computerized maintenance management system (Maximo) to enhance effective planning and accurate decision-making,

- Client field management monitors and measures Baker's performance per the KPI, and verifies Baker's maintaining the integrity of the facilities. This is in contrast to the traditional contract operating model where the producer's field supervision manages the "contractor." Client manages downhole operations.

Main Pass - OPCO Consolidation Model



capacity utilization, maintenance planning, and managing work execution. For assuming this additional responsibility, Baker Energy is eligible to receive a share of the cost savings it achieves for the company, as well as a performance bonus.

In addition to reducing lifting costs, HSE&C performance under OPCO is typically improved. HSE&C measures are not compromised to cut costs, and Baker Energy implements HSE&C best practices throughout the value network.

Proven Systems and Procedures. Baker Energy depends upon strong planning and management to make the OPCO model work. When

cost savings are derived from creating logistical efficiencies across operations throughout the Gulf of Mexico, expert planning and structured management systems are essential. Baker Energy's OPCO managers use leading edge computerized maintenance management systems, GIS-based logistics management tools, and web-based information exchange systems.

Outsourcing is successful when provided by a focused, experienced O&M company whose services are driven by industry trends. And by creatively building on those trends, the benefits of traditional outsourcing can be multiplied. Baker Energy

provides the knowledge and procedures, the global reach, and the ability to deliver competent staff on site that are necessary to support the outsourcing needs of majors and independents, including those with complex international operations.

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COGNICASE

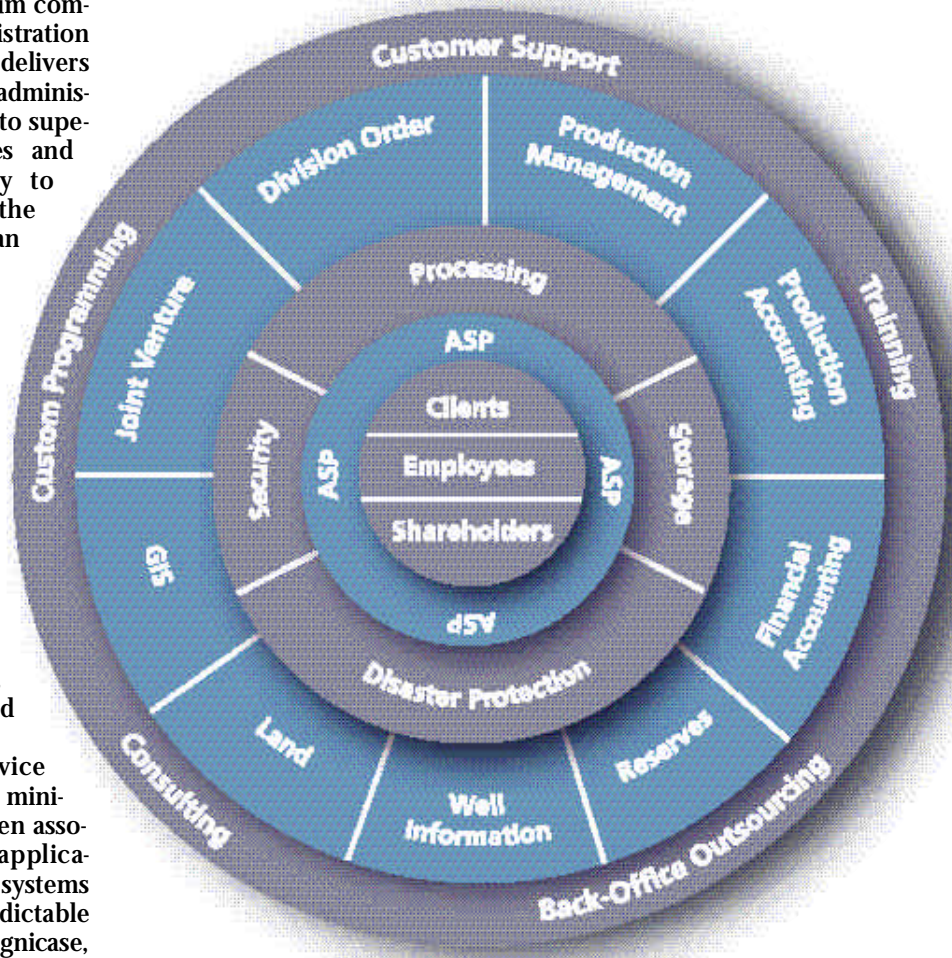
Cognicase, an information technology solutions and services provider, has shown that outsourcing a petroleum company's back-office administration and accounting functions delivers streamlined general and administrative (G&A) costs, access to superior technology, processes and personnel and the ability to focus management on the core business of running an oil and gas company.

Cognicase has established a complete offering of solutions that address the business processing needs of petroleum and trust management firms. Its products give customers the ability to manage financial, operational, ownership and asset management functions with solutions such as Cognicase Artesia, Cognicase Horizon and Cognicase Petrocomp.

Its application service provider (ASP) system can minimize the up-front costs often associated with enterprise applications, and maintain its IT systems on an affordable and predictable monthly fee. Through Cognicase, clients are able to outsource key back-office processes such as accounting, production management and lease management.

Cognicase's outsourcing team relieves customers of a host of cumbersome and administrative tasks and allows clients to focus time and energy on strategic operations. Cognicase is the only company that comprehensively covers the U.S. and Canadian petroleum and trust asset management industries, providing solutions from software and ASP to outsourcing and IT consulting. The company's goal is to help clients find innovative ways to use technology to streamline and improve business processes, so the client can focus on future growth and success.

COGNICASE ENERGY SOLUTIONS AND SERVICES



COMMON QUESTIONS, ANSWERS

The following is excerpted from "The Outsourcing Question," a white paper published by Cognicase.

What is outsourcing? Outsourcing takes place when an organization transfers the ownership and control of a business function to a supplier. In outsourcing, the buyer does not instruct the supplier on how to perform their processes but, instead, focuses on communicating what results it must obtain. It leaves the process of accomplishing those results to the supplier.

What will this cost? Financial executives need to know the true cost to process noncore back-office

functions internally. To make an apples-to-apples cost comparison, a company should compare three different scenarios—the current cost of managing the function internally, the cost to implement and execute the ideal processes and systems for managing the function internally, and the cost to outsource the function. This strategy can help objectively compare ownership costs of the in-house processing environment with not only the costs of an outsourced solution, but also with the costs of bringing the in-house solution up to top industry standards, which is what a suitable outsourcer would provide.

What is the best method of select -

ing an outsourcing partner? Smart organizations recognize that carefully selecting the right outsourcing partner is key to maximizing the effectiveness and value of these relationships. Companies must mindfully assess the offerings, experience and demonstrated capabilities of potential providers.

Customer references. The key to your due-diligence efforts must be candid interviews with a cross-section of the provider's customers. You should speak to customers with needs similar to yours and elicit detailed feedback to the following questions. How long have you been a customer? Why did you choose this provider over other vendors? How satisfied have you been with the provider? What types of problems have you encountered and how have they been resolved? How would you characterize the provider's strengths and weaknesses?

Commitment to service. Service to the customer is the single most important criteria to evaluate a potential provider. If you are going to outsource a business process, then you want to make sure the outsourcer is going to make the process as high of a priority as you would.

Key questions include: How do existing customers characterize the provider's dedication to service? Does the outsourcer have an executive manager "caring" for each customer to make sure priorities are handled quickly? What access will you have to help desk support? Does the outsourcer develop and maintain the software technology so that issues can be addressed without having to go to a third party? Perhaps most critically, does the provider "put its money where its mouth is" and offer service-level agreements (SLAs) backed by financial guarantees?

Provider's infrastructure. It is essential to check the prospective provider's infrastructure. What type of application systems does the provider utilize? Are they propri-

The financial health of your provider is critical.

Review the company's cash flow position, burn rate and other financial information so as to mitigate the risk of losing a partner to financial "death."

etary or are they dependent on other technology companies for maintenance and support? Do they manage their own data center or are they reliant on a third-party ASP company? What are the key metrics, including reliability, availability and scalability?

An on-site visit is key to establishing confidence in the provider's physical infrastructure and management expertise. Check out the provider's quality assurance processes and procedures. What recovery plans are in place in the case of a disaster or security problem? You should gain a detailed understanding of the security measures that protect a provider's facility from outside intrusion. Ask the provider about its current and planned infrastructure investments. You want to ensure that you will benefit from continual upgrades and new technologies.

Flexibility. This can be tricky to assess. You must determine whether a provider is simply trying to "sell you" by overpromising, or whether it is genuinely committed to tailoring its service to fit your unique needs. Once again, talk to existing customers. Has the provider established a pattern of working with existing customers to meet their needs? You should not expect a service provider to reinvent its business process for you. Be very worried if your prospective provider offers to do so: either they're fooling you or they won't be around long.

Provider's financial health. The financial health of your provider is critical. Review the company's cash flow position, burn rate and other financial information so as to mitigate the risk of losing a partner to financial "death."

We've selected a partner, now what do we do? Structuring an outsourcing relationship to maximize the value for both companies is not easy. When conducted thoroughly and carefully, the process for risk and reward in an outsourcing engagement emerges as a time for mutual education of business needs and culture. Trusting the outsourcer to provide what is contracted while managing each other's expectations allows each party to do what they do best and extract the best possible value from the outsourced function. (For the complete document, e-mail Kathy.Neill@cognicase.com.)

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ENERGY VIRTUAL PARTNERS

In 1999, while Bob Peebler was president and chief executive officer of Landmark Graphics Corp., he wrote a guest article, "The Virtual Oil Company" of the future, in which he bemoaned the historical misalignment of energy companies and the service sector based on "perpetual win-lose cycles."

Peebler envisioned a day when participants in the upstream industry value chain would negotiate a new business model based on trust, and operating more as a partnership. "The virtual enterprise of the future," he wrote, "will be characterized by knowledge management and collaborative decision-making by way of virtual teams, empowered by economic alignment and a willingness to do business in more productive ways."

Within three years, Peebler turned that vision into reality. In March, Energy Virtual Partners Inc. (EVP)—a cutting-edge oil and gas asset-management company headed by Peebler, president and CEO, and chairman David Work, a former senior executive of BP and Amoco—opened for business.

EVP provides an alternative to the ways oil and gas asset-owners—E&P organizations, utility companies, financial institutions and others—currently manage under-resourced properties in development and production. Built on a true virtual business model, lever-

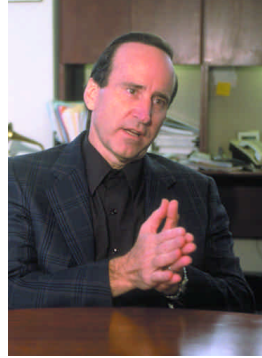
aging state-of-the-art computing and Internet technologies to link top industry talent, EVP offers a value proposition to the owners of these properties.

"We increase the value of fields that companies lack the resources to develop, but are not ready to divest," explains Work. "We do that by leveraging our virtual team of partners and consultants; by applying high-end reservoir, drilling and risk management technologies; and by reducing operating costs—all at *no additional risk or expense* to our customers.

"EVP's goal is to enable asset-owners to focus their most vital resources—capital, technical expertise and management time—on core activities, while we maximize the value of the rest of their portfolio. Not only will customers retain their current production volumes, they will also share in the upside we create. That's a win-win proposition by anyone's standard."

BUSINESS MODEL

Many E&P companies today own declining fields that hold substantial upside potential, yet fail to make



Bob Peebler

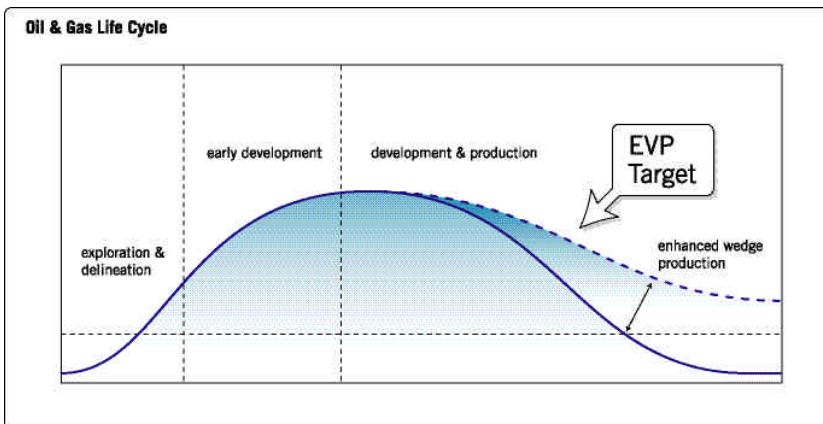
the annual budget cut for one reason or another. In some cases, mergers have generated a large backlog of properties considered noncore to new owners. Nontraditional asset-owners, such as utilities or banks, typically lack the technical and operational ability to optimize their producing properties. Without priority or attention, many assets become critically under-resourced and underfunded.

According to Peebler, in North America alone, an estimated \$20 billion worth of properties are relegated to the under-resourced dustbin every year. They may languish for years in a company's portfolio until sold—often without their true value ever being determined.

Smaller companies, however, frequently generate substantial new cash flows and shareholder returns from nonstrategic assets prematurely divested by larger organizations—much to the former owners' chagrin. How do they do it? By treating these properties as *core* to their business, by not skimping on the resources necessary to fully exploit the potential, and by maintaining lower overall cost structures. That is how Energy Virtual Partners approaches the development of its customers' under-resourced assets.

As a small, highly focused service company, EVP sets itself apart from other service providers in four main areas: people and technology, cost structure, monetization policy and risk management.

Talent and Technology. EVP deploys technical expertise and high-end computer technologies traditionally reserved for core, strategic assets. While the company controls the total solution design, it outsources the implementation to top industry professionals through economically aligning risk-sharing



Energy Virtual Partners increases the value of under-resourced oil and gas properties in the later stages of the oil-field life cycle.

agreements.

“Rather than simply paying for time and materials, we let our people share in the rewards of value creation,” says Peebler. “What’s more, they have access to the most advanced reservoir and drilling technologies through our secure web-based environment, which makes this an exciting and attractive place to work.”

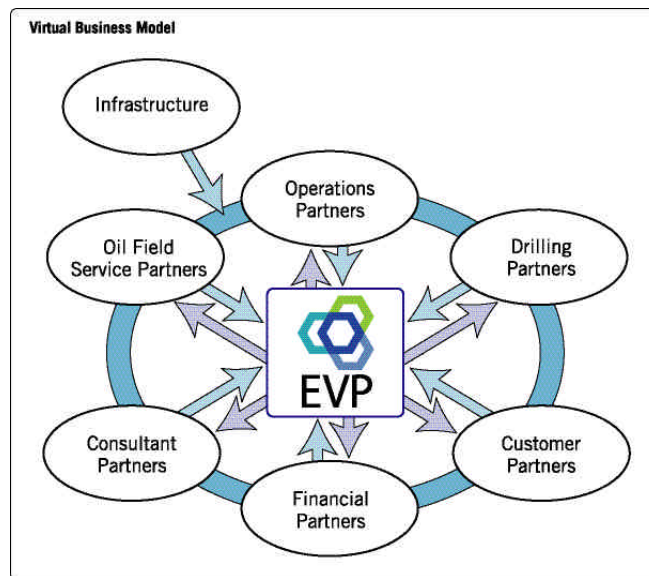
Lower Costs. EVP maintains a lower overall cost structure due to its innovative virtual business model, which treats its suppliers as partners rather than mere contractors. This approach better leverages partner resources and spreads certain operational risks. In exchange for gain sharing in reservoir upside, EVP can negotiate lower service charges. Also, through extensive outsourcing, the company avoids the normal costs of most noncore activities, such as production accounting and IT services.

Rapid Monetization. Unlike a number of small, “boutique” production companies in the oil patch, EVP ties up very little of its own capital in the ownership of proven reserves. Instead, the company pursues aggressive IRRs through a monetization process that quickly recirculates cash from previously discovered reserves into new development opportunities.

“Our goal is not to purchase existing production, but to create new value through exploitation,” says Peebler. “Also, we outsource all of our production operations. By avoiding high fixed costs tied to supporting operations, we are more effectively shielded from the impact of commodity-price swings.”

Integrated Risk Management. Uncertainties exist in all phases of

exploitation, including the location and quantity of reserves, the cost and timing of operations, and the range and duration of energy-price fluctuations. EVP, therefore, integrates the latest risk-based asset valuation, portfolio management and enterprise management techniques with every technical, operational and financial decision. The result: optimal allocation of investment capital.



EVP’s Virtual Business Model links a network of partners through its advanced web-based infrastructure.

In addition to its outsourcing model, EVP offers a financial alternative to companies that need cash, but have not sufficiently developed an asset to obtain an adequate sale price. “We can cash them out for all or part of their proven producing value,” explains Peebler, “but they retain some form of equity in the partnership. So they share in the upside that EVP creates.”

“Once we further develop the asset, we can either sell our portion of the partnership back to the original owners—or any other investors—if they wish to retain producing volumes from the property, or they can participate in the final sale.”

INVESTORS AND MANAGEMENT

Two of EVP’s major investors are Transocean Sedco Forex Inc., the world’s largest offshore drilling company, and Michael Baker Corp., a global firm that provides engineering and energy expertise, including contract production operations.

EVP’s founding management team has more than 200 years of combined energy industry experience, both in the E&P and service sectors in the domestic U.S. and international operations. In addition to Work and Peebler, the EVP leadership team includes Michael Walls, vice president of risk management and planning; David Lewis, vice president of operations; Marcia Simpson, vice president of exploitation; Chris Dale, founding vice president and director of geoscience solutions; Darrell McKenna, vice president of business development; and John D. Curtin III, vice president and chief financial officer.

“Despite our diverse backgrounds,” Work says, “we all have a shared vision of EVP’s business model and the guiding strategic principles of this unique new endeavor. We’re dedicated to building a company that will not only profit our shareholders and customers, but will have a significant impact on how the upstream industry does business in the future.”

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JUNE 2002

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