

September 25, 2018

By e-mail only

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MLT AIKINS
Attention: John Gruber

Torys LLP
Attention: David Wood

Re: Reasons for Adjournment
Proceeding ID 360
Bearspaw Petroleum Ltd. (Bearspaw)
Common Carrier Order and Rateable Take Order

Introduction

On September 17, 2018 Harvest Operations Corp. (Harvest) filed a motion under section 44 of the *Alberta Energy Regulator Rules of Practice* for an order to immediately suspend or adjourn this proceeding (Harvest motion).

The AER hearing panel (the panel) established a process for Bearspaw Petroleum Ltd. (Bearspaw) to respond to the motion and for Harvest to file a reply. By noon on September 20, 2018 the panel had received the last of the parties' submissions on the motion. After considering all of the submissions the panel decided to grant the motion and adjourned the hearing of Bearspaw's applications for a common carrier order and rateable take order to no fixed date.

The parties were notified of the panel's decision and were advised that the panel's reasons would follow. The panel has asked that I convey its reasons to the parties. The following are the panel's reasons.

Procedural Background

In 2016 Bearspaw applied for a delineation of the Crossfield Basal Quartz C Pool (BQC pool). Harvest contested the application and filed a statement of concern. The AER held a hearing the same year and issued a revised pooling order to incorporate the 102/11-24-24W4M well (102/11-24 well) in the BQC Pool.

In January 2017 Bearspaw applied for orders pursuant to sections 48 and 36(2) (b) of the *Oil and Gas Conservation Act* (OGCA) for:

- i) an order declaring Harvest, Exxon Mobil Canada Energy, Nexen Energy Partnership ULC and Breeze Resources Ltd. to be common carriers of natural gas and associated liquids produced from the BQC Pool through a series of pipelines operated by Harvest. The pipelines extend from 5-36-24-28W4M to 14-16-24-28W4M and include the compressor at 13-6-27-27W4M;

- ii) an order declaring the delivery point for natural gas produced from the 102/11-24 well and directing the proportion of the production to be taken by the common carrier from the producer or owner;
- iii) a direction under section 56 of the OGCA that the common carrier order be effective January 1, 2017;
- iv) an order allocating the production of raw gas from the BQC pool among the BQC pool wells including the 102/11-24 well with a minimum of 20,000 m³/day allocated to the 102/11-24 well;
- v) an order declaring that a minimum of 29% of the BQC pool be allocated to Bears paw subject to certain balancing provisions; and
- vi) a direction that the orders be effective January 1, 2017.

In early 2018 Bears paw's applications for the common carrier and rateable take orders were referred to hearing commissioners for a hearing. A prehearing meeting with the parties was held on April 27, 2018. At the prehearing the parties were asked to provide their views on hearing process steps and timelines. There is nothing on the transcript for that proceeding about a need to have the matter resolved before June 22, 2018 or any specific date.

After considering the parties' submissions the panel issued its prehearing decision which established a timeline for the hearing of Bears paw's applications. The hearing was scheduled to begin on September 24, 2018.

Legal Framework

Section 4 of the OGCA states that the purposes of the OGCA include the conservation of oil and gas resources, affording each owner the opportunity of obtaining its share of the production of oil or gas from any pool and providing for the economic, orderly and efficient development in the public interest of the oil and gas resources of Alberta.

Under section 36 of the OGCA, the AER may limit the amount of gas that may be produced and/or distribute the amount of gas that may be produced from a pool or part of a pool. Historically, this legislation has been used to authorize the distribution of gas production among wells in a gas pool:

36(1) The Regulator may, by order, restrict

(a) the amount of gas... that may be produced during a period defined in the order from a pool in Alberta.

(2) The restriction referred to in subsection (1) may be imposed by either or both of the following means:

...

(b) by distributing the amount of gas that may be produced from the pool or part of the pool in an equitable manner among the wells or groups of wells in the pool for the purpose of giving each well owner the opportunity of receiving the well owner's share of gas in the pool.

Section 48 (a) of the OGCA allows the AER to declare a proprietor or a pipeline to be a common carrier:

48(1) On application the Regulator may from time to time declare each proprietor of a pipeline in any designated part of Alberta or the proprietor of any designated pipeline to be a common carrier as and from a date fixed by the order for that purpose, and on the making of the approved declaration the proprietor is a common carrier of oil, gas or synthetic crude oil or any 2 or all of them in accordance with the declaration.

(4) On application the Regulator, in order to give effect to a declaration under subsection (1), may direct

(a) the point at which the common carrier shall take delivery of any production to be gathered, transported, handled or delivered by means of the pipeline, or

(b) the proportion of production to be taken by the common carrier from each producer or owner offering production to be gathered, transported, handled or delivered by means of the pipeline.

Section 1.3.4 of *Directive 065: Resources Applications for Oil and Gas Reservoirs* sets out what an applicant for a common carrier order must demonstrate for the AER to consider granting the order. For the purposes of panel's decision on the Harvest motion, the key requirement is that an applicant must demonstrate that: "producibile reserves are available for transportation through an existing pipeline."

Under section 56 of the OGCA, the AER may specify the date on which the common carrier declaration is effective. That section says "...that all or any part of the declaration or order be effective as of a date specified in the declaration or order, and a date so specified may be previous to the date the declaration or order is made but may not be previous to the date on which the application for the declaration or order was made to the Regulator."

Key Considerations

Bearspaw currently holds the mineral rights to $\frac{3}{4}$ of the relevant drilling spacing unit for the 102/11-24 well (DSU), leased by Bearspaw from the Crown. Bearspaw originally leased the rights to produce natural gas from the Basal Quartz in the remaining $\frac{1}{4}$ section of the DSU from Encana (the natural gas lease). Encana subsequently assigned the natural gas lease to PrairieSky Royalty Ltd. (PrairieSky). PrairieSky has taken the position that the natural gas lease terminated on June 22, 2018. On July 6, 2018 Bearspaw commenced an action in the Alberta Court of Queen's Bench against PrairieSky (CQB action) seeking, among other things, a declaration that the natural gas lease remains in full force and effect.

PrairieSky has filed a statement of defence in the CQB action in which it asserts that the natural gas lease has been surrendered or terminated. It asks to have Bearspaw's statement of claim dismissed. PrairieSky has also filed a counter claim relating to a caveat registered by Bearspaw. Among other things PrairieSky seeks to have the lease declared to be no longer valid and subsisting.

Parties' Arguments

The core of Harvest's argument is that a prerequisite to or fundamental requirement for seeking a common carrier order is the party seeking the order must have the legal right to produce the commodity to be transported. Harvest argues that the commodity must be available for transport through the pipeline that is to be the object of the common carrier order. Harvest said that as a result of the CQB action, Bearspaw does not have the undisputed legal right to produce gas through the 102/11-24 well and so cannot seek a common carrier order.

Harvest also argued that the legal right to produce must be maintained throughout the common carrier proceeding. Implicit in this argument is that it is not sufficient that Bearspaw had the right to produce and offer for transportation gas produced through the 102/11-24 well at the time it filed its common carrier application. Harvest said "The AER cannot grant rateable take orders and common carrier declarations on the basis of ownership and production rights that may or may not exist".

Harvest's motion asked the AER to suspend or adjourn the proceeding till the issue of Bearspaw's legal right to produce gas through the 102/11-24 well is resolved. Harvest filed copies of the pleadings from the CQB action in support of its motion.

Bearspaw's argument did not respond directly to the arguments made by Harvest. Bearspaw said that in order to decide Harvest's motion the panel would have to adjudicate the contractual issues raised in the CQB action. Bearspaw said that there was nothing on the record to suggest that the 102/11-24 well is not

capable of production. Bearspaw pointed to the fact that in Harvest's submission in this proceeding it conceded that Bearspaw had producible reserves available for transportation.

Bearspaw also argued that because it holds the mineral rights for $\frac{3}{4}$ of the DSU, pursuant to a valid and subsisting Crown mineral lease, it would not be precluded from producing gas from the 102/11-24 well even if PrairieSky ultimately prevails in the CQB action.

Bearspaw asserted that section 16 of the OGCA requires that the holder of a well license be entitled to the right to produce the oil or gas. It said that its license has not been challenged in this proceeding or in the CQB action. It added that PrairieSky has not taken steps to prohibit Bearspaw from producing the 102/11-24 well. Bearspaw states that it has the contractual right to produce the 102/11-24 well unless and until the courts determine otherwise.

Finally, Bearspaw submitted that the relevant provisions of the OGCA, specifically including sections 36 and 48, do not oust or suspend the mandate and jurisdiction of the AER in circumstances where there are unproven contractual claims. Bearspaw suggests that if the panel grants the adjournment on the basis that there is a dispute over the validity of Bearspaw's lease with PrairieSky it will open the floodgates to challenges to the validity of leases to oust or suspend the AER's jurisdiction.

In its reply submissions Harvest pointed out that section 4.021(2) of the *Oil and Gas Conservation Rules* (OGCR) requires common ownership in the DSU. Harvest also explicitly stated, in case it was not clear from its motion, that it no longer concedes that Bearspaw has producible reserves available for transportation. Harvest went on to note that as of July 5, the date it filed its submissions in this proceeding, Harvest was unaware that PrairieSky had purported to terminate the lease.

Reasons

A common carrier order is an extraordinary remedy. In making such an order the Regulator is forcibly interfering with existing contractual rights and, in effect, making what was private property into public property. Common carrier orders are available only as a last resort where there is petroleum (in this case natural gas) that is stranded because the person with the right and ability to produce and offer that gas for transportation and sale is prevented from doing so because it has no other or better means of getting that gas to market.

The evidence filed with Harvest's motion and Bearspaw's submissions lead the panel to conclude that Bearspaw's right and ability to produce and offer gas for transportation on the Harvest system is currently the subject of a dispute. The AER, and more specifically the panel, cannot resolve that dispute. Unless and until the question of whether Bearspaw has the rights to produce gas from the 102/11-24 well is resolved in its favor, Bearspaw does not satisfy the requirement of section 1.3.4 in Directive 065.

Section 1.3.4 requires the applicant to demonstrate that producible reserves are available for transportation through an existing pipeline. A common carrier order gives access to transportation service to a person with the right and ability to offer gas for transportation. If the ability of the person seeking the order to produce gas is in dispute, as is the case here, there is no way to give effect to a common carrier order.

Bearspaw's reliance on section 16 of the OGCA to argue that it has a well licence to produce gas from the Basal Quartz from the 102/11-24 well regardless of whether its lease from PrairieSky is valid cannot be sustained. The Court of Appeal in *Alberta Energy Company Ltd. v. Goodwell Petroleum Corporation Ltd.* said the following about section 16:

Neither s.16(1) or its predecessor section support the Board's position. These sections will be contravened if the person who holds the well licence does not possess the right to produce the hydrocarbons authorized by the well licence. The right to produce could be acquired by agreement, reservation, grant or, as in this case, crown lease. Again, the application of the sections depends on the interpretation of the instrument that grants the rights...

The proper interpretation of section 16 in the context of the OGCA as a whole is that legal entitlement to the right to produce petroleum from a well is a prerequisite and ongoing requirement to be able to secure and rely on a well licence.

Finally, Bearspaw argued that it would not be precluded from producing gas from the 102/11-24 well even if PrairieSky convinces the Court that its lease terminated on June 22, 2018. This argument neglects that, as Harvest says in its reply submissions, Bearspaw would not be able to meet the requirement set out in section 4.021(2) of the OGCR for common ownership throughout the drilling spacing unit before a well can produce.

Conclusion

Harvest's motion for adjournment is granted. AER Proceeding ID 360 is adjourned; however, Bearspaw or Harvest may request that the proceeding be resumed if there is a change in circumstances.

Bears paw is to provide a written update to the panel on the status of its applications on or before January 4, 2019.

Yours truly,

<original signed by>

Barbara S. Kapel Holden
Legal Counsel

cc: Brent Prenevost, AER Counsel
Elaine Arruda, AER Hearing Coordinator