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# The Mining and Lands Commissioner
# Le Commissaire aux mines et aux terres

File No. OG 009-02

L.F.G. Carter )
Deputy Mining and Lands Commissioner )

Wednesday, the 23rd day of July, 2003.

THE OIL, GAS AND SALT RESOURCES ACT

IN THE MATTER OF

An application under clause 8(2) of the **Oil, Gas and Salt Resources Act,** R.S.O. 1990, c. P. 12, as amended by S.O. 1994, C. 27, S. 131 and 1996, C. 30, ss. 56-70; 1998, C. 15; Sched. E, S. 24,1999, C. 12, Sched. N, S. 5; 2000, c.26; Sched. L, s. 6(2) and Section 15 of Ontario Regulation 245/97, amended to O. Reg. 22/00, for an Order, hereafter referred to as "The Application for Unitization of the Zone "C" Pool", that; (a) the oil or gas interests within a unit area containing a pool, part of a pool, oil or gas field or part of an oil or gas field be joined for the purpose of drilling or operating oil or gas wells, (b) management of the drilling or operation be carried out by the initial unit operator further described in this Order, and (c) the costs and benefits of such drilling or operation within the unit area be apportioned in the manner specified within this Order.

(Amended July 23, 2003)

BETWEEN:

LAGASCO INC.

Applicant

-and-

ALL LEASED LANDOWNERS AND LEASE INTEREST HOLDERS IN THE ZONE "C" POOL more particularly described in Schedule " A " attached hereto and forming a part of this Order

Respondents

(Amended July 23, 2003)

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**AND IN THE MATTER OF**

The Application by Lagasco Inc. (Applicant) for an Order joining the specific interests of the Estate of Mildred Rayleene Oliver, Kenneth Raymond Kelly, Harry Blain Lawson and William Humphreys Lawson (collectively known as the "Leased Landowners") further described in Schedule " B " attached to and forming a part of this Order.

(Amended July 23, 2003)

**AND IN THE MATTER OF**

All and singular those certain parcels, lots or tracts of land and premises, situated lying and being all of Lot 11, Concession 3, in the Geographic Township of Zone, formerly the County of Kent, now in the Municipality of Chatham-Kent, Province of Ontario, and more particularly described in Schedule " A " attached hereto and forming part of this Order hereinafter referred to as the "Unit Boundaries".

(Amended July 23, 2003)

## ORDER FOR COMPULSORY UNITIZATION

**WHEREAS** a Hearing was held in this matter commencing at two-fifteen o'clock in the afternoon on the 12th day of February, 2003 in the Wedgewood Room of the Wheels Inn, at 615 Richmond Street, Chatham, Ontario, with Mr. Christopher J. Lewis, Counsel for the Applicant, having introduced evidence and made submissions and Mr. Jed Chinneck, Counsel for some of the Respondents having introduced evidence and made submissions opposing the Application. No one from or representing the other Respondents appeared opposing the application.

**AND WHEREAS** the evidence and submissions for the adjacent Zone "B" Pool application was adopted as evidence and submissions for the Zone "C" Pool application with modifications presented through submissions and clarifying evidence upon direct and cross-examination of several sworn witnesses. Final submissions were heard in conjunction/tandem with the Zone "B" Pool application.

**AND WHEREAS** the Applicant, Lagasco Inc. has obtained Petroleum and Natural Gas Lease(s)/Grant(s) with 100%of the landowners in the proposed unit area.

**AND WHEREAS** to promote the conservation of oil, gas and unitized substances, to prevent waste, to allow the greatest ultimate recovery of unitized substances and to ensure to each of the parties to this Order obtaining his, her or their equitable share of unitized substances produced under and by virtue of the terms of the Unitization Order, it is deemed necessary and desirable to unitize the lands, oil and gas leases, formations and substances hereinafter described;

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**UPON** reading the documentation filed in support of the application and upon hearing the evidence;

1. **THIS TRIBUNAL ORDERS** that the Title of Proceedings be amended accordingly by deleting all words specifically the parties found after "Applicant" and replacing them with the words, "-and- ALL LEASED LANDOWNERS AND LEASE INTEREST HOLDERS IN THE ZONE "C" POOL - Respondents -", more particularly described in Schedule " B " attached hereto and forming part of this Order.

2. **THIS TRIBUNAL FURTHER ORDERS** that this Order for Unitization will be effective on the 1st day of January, 2003.

3. **THIS TRIBUNAL FURTHER ORDERS** that the unit to be known as the Zone "C" Pool shall be described as all and singular those certain parcels, lots or tracts of land and premises, situated, lying and being all of Lot 11, Concession 3, in the Geographic Township of Zone, formerly the County of Kent, now in the Municipality of Chatham-Kent, Province of Ontario, more particularly described in Schedule " A " attached hereto and forming part of this Order, being of the Silurian Age.

4. **THIS TRIBUNAL FURTHER ORDERS** that the unit boundaries, tracts and participating section of the Zone "C" Pool shall be in accordance with the Plan marked as Schedule " A " attached hereto and forming part of this Order, and **FURTHER ORDERS** that the allocation of each of the Leased Landowners oil and gas interests shall be as set out in the Summary of Tract Allocation, in accordance with Schedule " B " attached hereto and forming part of this Order.

5. **THIS TRIBUNAL FURTHER ORDERS** that the interests of the Applicant, Lagasco Inc., and the interests of the Respondents, described in Schedule " A " attached hereto and forming part of this Order, being all Leased Landowners in the unit known as the Zone "C" Pool, more particularly described in Schedule " B ", attached hereto and forming part of this Order, be and are hereby joined and unitized, for purposes of drilling or operating wells, being for the purposes of oil and gas production.

6. **THIS TRIBUNAL FURTHER ORDERS** that the relationship between the Applicant, Lagasco Inc., and the Respondents, being all Landowners in the Zone "C" Pool, be regulated in respect of such lands as if each of them had reached agreement on the terms and conditions, as set forth in the Unit Operation Agreement, being Schedule " C ", attached hereto and forming part of this Order and attaching to any pre-existing agreement in respect of oil and gas rights in the Zone "C" Pool accordingly.

7. **THIS TRIBUNAL FURTHER ORDERS** that where conflict occurs between the Unit Operation Agreement and this Order, the terms of the Order shall prevail.

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**8. THIS TRIBUNAL FURTHER ORDERS** that the Unit Operating Agreement may be amended by the Applicant, Lagasco Inc., with the agreement of no fewer than that number of Leased Landowners corresponding with 60 (sixty) per cent of the unit area of the Zone "C" Pool, or, if amended as may be amended from time to time, for the purposes of expanding the size of the unit area through inclusion of additional lands in the vicinity of and abutting the current unit area:

(a) by executing an agreement with the Leased Landowner(s) which conforms with the Unit Operation Agreement attached to this Order as Schedule " C ", with the necessary modifications;

(b) by serving on each Leased Landowner a copy of this Order of Compulsory Unitization, with Schedules attached; and

(c) by registering on title on the lands of each of the aforementioned Leased Landowners, or additional, a Unit Amending Agreement along with schedules attached setting out the following information:

(i) a plan of the defined unit area;
(ii) the metes and bounds of the enlarged or reduced unit area; and
(iii) a summary showing the names of the individual Landowners and tract allocation of each party's oil and gas interest within the tract and unit area

**9. THIS TRIBUNAL FURTHER ORDERS** that, in accordance with subsection 15(4)(g) of O. Reg. 245/97, amended by O. Reg. 22/00, the Applicant, Lagasco Inc., is appointed as the Initial Unit Area Operator.

**10. THIS TRIBUNAL FURTHER ORDERS** that the royalty payments to Leased Landowners shall be as set out in Clause No. 3 of the Unit Operation Agreement, Zone "C" Pool, and shall be determined on an areal basis, in accordance with Schedule " B " attached to and forming part of this Order.[1]

**11. THIS TRIBUNAL FURTHER ORDERS** that service of the Order will be affected by the tribunal by regular mail and by the Applicant, Lagasco Inc., through regular mail delivery to the residences of the Landowners as indicated on Schedule " B " attached to and forming part of this Order.

**12. THIS TRIBUNAL FURTHER ORDERS** that this Order shall be effective until such time as all of the recoverable oil and gas reserves in paying quantities have been produced from the Zone "C" Pool, and without limiting the generality of the foregoing, continuing as long as the

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[1] The royalty payments are to be in accordance with Clause No. 3 of the Unit Operation Agreement, attached as Schedule "C".

leased substances are produced from the Zone "C" Pool, as may be enlarged or reduced from time to time, or until such time as all wells located on the aforementioned pool have been abandoned or plugged.

**13. THIS TRIBUNAL FURTHER ORDERS** that the Unit Operation Agreement be modified and amended to include the wording; "The parties to this agreement recognize that the terms of this Unit Operation Agreement may be modified or affected by statute, regulation, order, or directive of any applicable government or government agency."

**14. THIS TRIBUNAL FURTHER ORDERS** that no costs shall payable by any party to this application.

**15. THIS TRIBUNAL FURTHER ORDERS** that upon payment of the required fees, Notarized Copies of the Order be filed by counsel for the applicant, in the Chatham Land Registry Office, Kent #24, 40 William Street North, Chatham, Ontario N7M 4L2, on lands corresponding to each of the Tracts listed in Schedule " B ", attached hereto and forming part of the Order.

**16. THIS TRIBUNAL FURTHER ORDERS** that this Order is binding on the Applicant and the Leased Landowners and their executors, heirs, successors or assigns.

Reasons for this Order are attached

**DATED** this 23rd day of July, 2003.

Original signed by
L.F.G. Carter

Lorne F.G. Carter
Deputy Mining and Lands Commissioner

Ontario

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24th floor, 700 Bay Street
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(Amended July 23, 2003)

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LAGASCO INC.

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Respondents

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(Amended July 23, 2003)

## REASONS

This Zone "C" Pool application was heard on Wednesday, February 12th, 2003, commencing in the afternoon at the Wedgewood Room of the Wheels Inn, 615 Richmond Street, Chatham, Ontario. In addition some evidence from the Zone "B" Pool application heard February 11th and 12th, 2003 was adopted for this application.

**Appearances** by;

| | |
|---|---|
| Christopher A. Lewis | Counsel on behalf of the Applicant, Lagasco Inc., |
| Jed M. Chinneck | Counsel for a majority of the Respondents, |

No one attending on behalf of the remainder of the Respondents

**Preliminary/Procedural Matters**

It was submitted by Mr. J. Chinneck that the Hearing matters owing to the Zone "C" Pool application hearing scheduled for February 12th, 2003 (next day) be brought forward and included in the Hearing for the Zone "B" Pool application scheduled for February 12th, 2003 (this day). He provided evidence [Exhibit #13] and submitted that the Respondents to the Zone "C" Pool application were agreeable to moving the Hearing to February 11th, 2003 and being included with the application for the Zone "B" Pool.

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Mr. C. Lewis submitted that the terms of the notices served have to be up-held. The Notices have been sent out announcing the two dates of the hearings with specific reference that the Zone "B" Pool application is to be heard on February 11th, 2003 and the Zone "C" Pool application is to be heard on February 12th, 2003. While he understands that evidence in one may well be the same for the other they are in fact separate applications/issues.

This Tribunal finds that notice is in fact specific as to each application and includes separate hearing dates. While the hearings are only one day apart and will likely produce inter-related evidence[1] the issue of service of notice must be maintained. Those Respondents for the Zone "C" Pool may well have the intentions of attending on the second day and applying to make submissions and to move the hearing to a joint application status may circumvent the rights of the respondents on either day. The Tribunal will maintain the two applications within separate hearings.

Mr. Chinneck further submitted that he was requesting the inclusion of Mr. E. Hewitt (M.N.R.) as a witness for the Respondents to be questioned on matters pertaining to Trust account conditions within the Unitization Agreement that is to be argued for inclusion in any compulsory Order of the Deputy Commissioner. Further he submitted that it is the Respondents contention that a Special Trust for the cost of plugging of wells has to be included in the Order.

Mr. Lewis submitted that while he did not object to Mr. E. Hewitt's testimony on M.N.R. policy within his station he did object to arguments on special trust conditions for good reason. He submitted that the Tribunal does not have the authority or jurisdiction to rule and consider the special trust conditions within an Order.

Upon due deliberations the tribunal provided the explanation that it is compelled to hear the arguments both for and against the issue of ordering a special trust condition. The Tribunal invited both parties to submit on the issue of trusts and the ensuing findings within the Compulsory Order will address the issue of jurisdiction in such matters.

**Service**

Mr. C. Lewis provided an affidavit of service [Ex. 11] by R. Gilders-Barrow sworn before B. L McGregor, a Commissioner, noting the service of the Application for the Unitization of the Zone "B" Pool and on the Zone "C" Pool on the Respondents listed in Schedule "A" attached to this Compulsory Order.

In addition the service of the Applicants' reply (Mr. C. Lewis) to the Respondents Reply of Mr. J. Chinneck on the Respondents as follows:

(a) Mr. J. Chinneck
(b) Mr. Christopher A. Lovell and Ms. Della Marie Lovell
(c) Mr. Roger C. Oliver
(d) Bank of Montreal, London, Ontario

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[1] Postscript - In hind-sight the evidence of the Zone "B" Pool application was adopted in its entirety into the Zone "C" Pool application at the second day hearing and no new/additional Respondents surfaced for the second day of hearing for the Zone "C" Pool application.

The Tribunal finds notice of the hearing was reasonably delivered to those directly affected by the application proceedings.

**Background**

The Zone "C" Pool has a well situated within its boundaries. The Well #5 was drilled in 1943 under a permit issued to Union Gas Company of Canada, who was developing the area. The well and area leases are currently owned by Lagasco Inc. During the period leading up to and 2003 the landowners and the predecessor operating companies tried to negotiate revised terms for the lease contracts, but to no avail or compromise, each party defending their concerns with diligence. These attempts to negotiate became of greater concern in the 90's and attempts to draw on the Ministry for resolution and the demise of the head of the producing operations stalemated the situation. In the time frame the well production has diminished and an amalgamation of efforts under unitization is considered the best course of operating the field.

In 1999 as a result of legislative and administrative changes the wells operated on issued Licence(s) Number 8832 (#5) issued to Lakeville Holdings Inc. the operator of record for the period. The Licence contained the conditions;

> 1. The production spacing unit for this well is comprised of tracts 3,4,5 and 6 of Lot 11 Concession, Zone Township, Kent County.
>
> 2. If pooling of the production spacing unit has not occurred by March 8th, 1999 all oil and gas production from the well shall be immediately discontinued by the operator and the well suspended in the manner prescribed by the Provincial Standards.

Lakeville Holdings Inc. (predecessor) appealed the licence conditions (1999) to the Ministers designate and the changes were denied.

Efforts to resolve issues and sign the landowners/lessors into a voluntarily unitization agreement (ss. 8(3) of the **Ontario Regulations 245/97, amended by O. Reg. 22/00**) and place the well back on production have been ongoing and unsuccessful since 1999.

In November 2002 a decision[2] was handed down by the Minister's designate (Mr. Hewitt) to change the Inspector's Order;

> It is my decision to replace the inspector order to plug the well in question with the following:
>
> 1. Lagasco Inc. is to make four annual deposits of $2,500 to its current well security trust established under Section 16. of the Ontario Regulations 245/97 on or before January 1st of every year starting January 1st, 2003.

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[2] Notice of Decision, Inspector Order 10-02-RWS, November 14th, 2002, Petroleum Resources Centre, London Ontario., acting under section 7.0.2 of the **Act**.

2. Lagasco Inc. is to submit proof to the Minister that the matter has been referred to the Mining and Lands Commissioner on or before January 1st, 2003. Should Lagasco Inc. fail to submit such proof, Lagasco Inc. shall plug the well in question on or before March 31, 2003.

3. Should Lagasco Inc. succeed in its attempt to refer the matter to the Mining and Lands Commissioner on time but fail to obtain a unitization agreement, Lagasco Inc. shall plug the well in question no later than 90 days from the day the Mining and Lands Commissioner issues its report.

This application, filed December 17th, 2003, for compulsory unitization is now being made to the Office of the Mining and Lands Commissioner through the hearing process.

Salient to the application for the compulsory joining of the parties is the seeming silence of some older lease terms on the subject of pooling and/or unitization and the subject of mortgage interest parties to the application.

**Issues**

1. Can the purpose of the **Oil, Gas and Salt Resources Act** be ascertained?

2. If granted, is the purpose of Unitization of a pool/field clear and understandable?

3. Should the application be granted, what is the effect of the Unit Operation Agreement proposed in relation to the terms set out in the various leases of the Leased Landowners?

4. If granted, what should the effective date and term of the ordered compulsory unitization be?

5. Is the tribunal in a position to award and assess costs related to the hearing process?

## EVIDENCE

This summary is provided from direct examination, cross examination (six witnesses) and submissions by Counsel(s) gathered during a sister hearing on a Zone "B" Pool application (refer to file number OG-008-02) in advance of this hearing and during the hearing specific to this application.

**Mr. Peter Miller,** the company field manager, provided evidence on the well operations noting that the Well #5 has been non-operational since the company take-over in 1992. He noted this application is expected to rectify the situation. Mr. Miller noted that other than the Inspection Order and Decision (see "background" herein) there is no other outstanding issues with the Ministry concerning the operation of this well.

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There are approximately thirty wells producing 140 MCF per day in the three Zone fields. Overall Lagasco has ninety-four wells under licence in the Province. Referring to the Record of Technical Data [Ex. 1, Tab 8] Mr. Miller reviewed its content and noted the Ministry concurring with the Zone "B" Pool as proposed.

The previous operator, Mr. Gout's company, had attempted to modernize the leases and have the landowners enter into a unitization agreement which proved unsuccessful. Mr. Gout was the primary negotiator in these matters which hampered negotiations due to his inflexibility and heavy-handed tactics with the landowners.

Over the approximate 10 miles of pipeline in the gathering system, Lagasco experienced fifteen to twenty leaks last year. The system is aging and rusted areas are noticeable. As a result the system has experienced blow-outs from some leaks causing some crop damage. It is the nature of the business and the frequency was not significant in his estimation. Mr. Miller added that it is the company philosophy to keep good relations with the area farmers and when crop damage occur the repairs are made and the farmer is duly compensated for the loss. A twenty-four hour a day eight hundred telephone number is posted for reporting problems observed and this is a licencing requirement. The Provincial operating standards are being met and regular daily checks are scheduled for the system.

The system production volumes are recorded by meters and based on the latest Walsh report a reasonable production picture can be expected for the field. He noted the meters are calibrated yearly (industry standard practice) and it is estimated that 140 MCF is required to maintain the system.

The company considers the liability for plugging each well is from $10,000 to $15,000 each and may be as high as $16,500. Basically the landowners have asked for an abandonment cost clause and a better royalty percentage return. The previous operating company had offered to create a separate trust fund. Mr. Miller noted that this was rejected by the landowners given their mistrust of the administration of the trust fund.

**Ms. Kathy McConnell,** a geologist and consultant in the oil and gas industry, explained that the Zone "C" Pool unit operation area is made up of three land parcel tracts. She indicated which of the lands will be participating acreage and non-participating acreage. The ownership interests were noting. The area is made up of four landowners and four parcels with participating acreage of approximately 100 acres. One hundred percent of the participating and non-participating area is currently under lease to Lagasco Inc. The well proposed for production is Well No. 5 which is situated on parcel tract #2.

She highlighted the terms of the Unit Operation Agreement [Exh.1.a, Tab 16]. She noted term differences in the proposed documents and those suggested by the Respondents. The landowners agree to the 12.5 percent royalty, but differ on the points of volume calculations and the $10 per acre rental fee offered. The Respondents have suggested restrictions on land and carbonate zone access which she considers contrary to; the lease arrangements, the **Regulations,** Standards, and the **Act.**

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Ms. McConnell concluded the application overview naming Lagasco Inc. as the Initial Unit Operator and requesting the effective date of the ordered agreements to be January 1st, 2003.

**Mr. P. Walsh**, expert witness and consultant to the Applicant, outlined his credentials as a Geologist, MBA with current studies toward a Ph.D. (geology) and his extensive field experience. He indicated previous involvement with predecessor companies (Lakeville Holdings and Lagasco Corp.). He consulted for Lagasco Inc. through his consulting firm, Energy Objectives Ltd., however, he has no ownership interest in Lagasco Inc. Two studies have been conducted on the Zone fields. The 2000 report provided a basis for landowner negotiations and the 2002 report was designed to deal with this application for compulsory unitization

Mr. Walsh reflecting on the definition of an expert and noted that an individual who has education in the field and considerable direct working knowledge may have sufficient expertise for making hearing presentations. However, a passing desire or passion for knowledge on the subject matter of this industry is not enough to be considered an expert.

He indicated support for unitization of the Zone field. Support for unitization of this pool is found in the Office of the Mining and Lands Commissioner publication[3] at page 7.;

> The benefits of unitization to the operator includes streamlined operations, centralized facilities and a lower economic production limit due to lower operating costs and additional recovery of oil and gas. The benefits of unitization to landowners include a longer production life of the pool (more royalties), less surface production equipment and a guarantee of a share in production regardless of whether a well is located on their land or spacing unit. The latter benefit occurs since all production from a unitized pool is deemed to have come from all interest owners.

There is a reasonable expectation that this location will produce gas/oil from under certain lands. Production statistics will provide the information of whether to extend or contract the area further and the unit operation agreement will provide for the flexibility of operations to do so.

Mr. Walsh agreed that the essence of unitization, according to Ballem[4], is to reduce waste and provide for efficient recoveries from which the landowners will receive benefits as a result of rendering oil/gas from under their lands. The participating lands are in a Silurian formation found under the different tracts which will share in the royalties from the production. The remaining lands are designated no-participating and will not share in the royalties unless a shift in the formation is recorded. The unit boundaries are the extreme outer limits of the estimated field. If it can be determined that gas exists under someone's lands, then they are entitled to royalties from the production.

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[3] Office of the Mining and Lands Commisioner - publication, Queen's Printer, entitled " Oil, Gas, and Salt Resources Act, Document of Explanation"

[4] Ballem, John Bishop, The Oil And Gas Lease In Canada, 2nd Ed, (Toronto: University of Toronto Press, 1985) - From an operational point of view it makes good engineering and economic sense to operate a field as an entity without regard to any artificial distinction created by the ownership subdivisions. Unitization achieves better operating procedures, enhances recovery and implements good conservation practices at a reduced cost. Unitization is encouraged by public conservation bodies."

Mr. Walsh stated that when the field was first drilled, sixty years ago, there was no unitization or organization of the lands and this, coupled with a lack of metering data, makes it difficult to determine the current reserves and the wandering directions of the field. Typically unitization of a producing field takes place within the initial period of a pool's productive life. Upon resumption of production the meter records will help to determination the remaining gas reserves. The operator today must monitor the meter data closely in order to determine the most efficient well locations and the field layout. Based on current technical information it makes sense to unitize the operations. In the alternative, when expansion of the field is required the process may be prolonged as the operator will have to step backward to unitize will be required before proceeding with production.

Mr. Walsh stated that Zone "C" Well 5 is approximately at the center of four tracts (25 acres each). Participating acreage is approximately 100 acres within the limits of the unit at 191 acres. The pool production area considered smaller than previously reported and is being determined based on old log information. In theory, this information plus downhole geophysical logs will determine the porosity and permeability of the reservoir. The area of the field is being estimated/determined from the drilling patterns of old wells and their historical production records collated (Cochrane and Bailey) for the Ministry of Natural Resources. The field layout/area for drilling is based on the current requirements of the Ministry for Well No. 5. He pointed out other plugged or dry unproductive well locations in the area, from the reference maps, and concluded that the area is "old and tired" with smaller production areas.

Mr. Walsh provided a review of the 2000 and 2002 reports filed. The first report (2000) was an economic evaluation pertaining to a specific point in time. The terms of reference for the 2000 report did not call for a new assessment of the geology as Lagasco Inc. was relying on Mr. Welychka's assessment at the time. The 2002 report takes in the increased demand and prices, raising the potential worth of the field. He reflected that longevity fits this situation. While production may be low, the dollar value of gas is high. The field is approximately one-half used and expectations for the field is possibly 10 years, based on a flat decline rate and commodity volatility.

These are old wells and generally on par with most Ontario fields. Union Gas is the marketer of the production from these fields in the Province and the volume figures they provide to the operator are sometimes two or three weeks late placing the operator at a disadvantage when producing financial information. In order to assess the viability of the reserves in Zone "C" both the physiology and economics of the pool have to be considered. The time to evaluate a field with many wells is often only after take over.

Mr. Walsh upon reviewed the production summaries 1989 to 2000[5] indicating that in 1996 Zone field volumes were 3781.61 (10-3-M3), rising to 5830.0 in 1997, leveling back to 5402.8 in 1998, dropping in 1999 to 4793.3 and falling off in 2000 at 2719.7 and then 2329.1 in 2001. Reflecting that the significant drop may have been the result of an increase in Ministry shut-in

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[5] 1989 to 2000 Drilling and Production Summary, Oil and Natural Gas Exploration, Underground Storage and Solution Mining in Ontario, Oil, Gas & Salt Resources Library (prepared by B. D. Parkes)

orders during the period, as well as, market demands. The market is dominated and at the discretion of Union Gas, and their acceptance of natural gas based on the market swings in demand. Union Gas charges a 24 cents per cubic foot marketing fee. Reflecting on the royalties and net costs, he noted a 12.5 percent royalty net of compressor fuel costs will provide a return of approximately 11 percent to the landowner. The trend in the industry toward market flexibility which, if adopted, will result in a greater share for those receiving royalties.

The operating company has different ownership and management styles than that of the previous operator. It is his understanding that the current operator has the duty to plug the wells. He also understands that as long as there is a chain of predecessor companies in existence, liability to do so, can/will transfer. Further if any operator(s) is unable or non-existent the onus falls on the Trust/Bond fund held by the MNR and then possibly the landowner. Mr. Walsh referred to the definition of an operator[6] in the **Act** and noted the term, to his understanding, deals with those who become both the landowner and the operator.

Clause 10.(1)(4) of the **Act** sets out "Plugging by previous licensee[7]" as the directive for well plugging order.

Referring to calculations in his report he noted that the $45/$50,000 forecast figure is realistic for plugging the three wells discussed for Zone "B" and "C". The production in older 2000 report has a negative $162,000, net of allocation, value. The capital costs of $1.05 million plus the average abandonment cost figures bring the total liability to $1.72 million. Based on that cost figure, the current return expectations of the pool will have no value. There is a risk in operating this pool/well as there is for any other pool/well. He concluded that the trust fund deposit requirements are being met as regulated by the Ministry. There is $40,750 currently in the trust for the Lowrie operated wells and they have been allowed 10 years by the MNR authority to raise the trust monies amount to $70,000. The Lagasco bank debt is secured and the bank is comfortable with their current accommodations and security offered. Mr. Walsh concluded that the company's philosophy is to plug wells on their own and not wait for an MNR order to do so. The Lowrie company book assets are not sufficient to cover total well plugging, however Lowrie is not the only operator in the Province who has an insufficient bond and/or asset amount based on the number of their wells in operation.

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[6] Oil, Gas and Salt Resources Act, Chapter P.12 (November 26, 2002)*,

1.(1) "operator" means, in respect of a work,

(a) a person who has the right as lessee, sub-lessee, assignee, owner or holder of a licence or permit to operate the work,

(b) a person who has the control or management of the operation of the work, or

(c) if there is no person described in clause (a) or (b), the owner of the land on which the work is situated; ("exploitant")

[7] O.G.& S.R. Act*

10.1- Plugging by previous licensee (4) If, at any time after a licence relating to a well is transferred, an order to plug the well is made under section 7.0.1 but not complied with, an inspector may require a previous licensee to plug the well at the previous licensee's expense. 1996, c.30, s.64.

Mr. Walsh noted his familiarity with the gathering systems based on his historical involvements and reflected that the reliability of the records is questionable. He provided his understanding that the information on gas production is less than adequate. The data required by the Ministry and much of what the producers have provided, and currently provide, does not meet the standards set by the Ministry. The largest producers in the Province do not provide adequate information for the public record. A producer has to manage and understand what the wells are producing based on reliable data and this unitization application addresses those concerns. If the well is not deemed to be productive then plugging and abandonment is the operator's recourse. In this case the test information indicates a commercially productive rate of gas is measurable and under sufficient pressure to produce for approximately a ten year term.

The gas deposits (A-1 and A-2 horizons) in Zone "C' are considered to be "thin and patchy". The area is known as a dolomite formation and the fluids reacting with magnesium have created fractures or crevices in the limestone, trapping the gas. As evidenced by other drilling in the area some wells produced nothing worthwhile to put on production. He concluded that there is uncertainty where to drill, without further evidence as to where to explore. Where technical data is included; well bore analysis, geological mapping (seismic), reservoir studies (pressure data), production statistics, and economic studies the participating and non-participating boundaries are easier to determine.

The 2000 report was based on the geology information provided by Mr. E. Welynchka, a geologist hired by Lagasco Inc. Mr. Walsh stated that the same historical well information he is now relying on, for his 2002 interpretations, was available to Mr. Welynchka in the year 2000. The opinions expressed in this report on the specific areas A, B and C generally agreed with the areas outlined by Mr. Welynchka, but are defined based on the latest geological interpretation. The obvious difference in the reports is the economic value from today's higher prices.

Mr. Walsh paraphrased a 1969 article[8] which summarized the issues of boundary selection processes surrounding unitization. The article recognized that it is not a perfect world when dealing with oil and gas operations and determining the extent of a reservoir. The determination is made ideally from the data mentioned above, but in the real world the industry recognizes data is sometimes in short supply so they have to use the best available information. In this case, he reported[9], the information is based on past drilling attempts and successes. The recommendations follow the Ministry designated tract boundaries laid down.

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[8] Riley, E.A. "How to Speed Selection of Participation Formulas" World Oil, May 1969 - "In circumstances where an old depleted reservoir with common well density is being unitized and little or no information is available then the suggested formula for unitization would involve the number of wells producing and the acreage developed"

[9] Energy Objectives Ltd., Zone "B" and "C" Pools, Unitization Study (prepared for Lagasco Inc., December 2002, page 5. "In determining a reasonable approach to unitizing the Zone "B" and "C" Pools, an approach is being recommended that combines the unitization formula suggested...and the current policy of the Ministry of Natural Resources respecting pooling requirements for off target locations."

The 2002 report identified the differences between pooling and unitization. A pooling agreement does not allow for expansion of the pool into non participating areas and a unit operating agreement is flexible on expansion. A pooling agreement is specific as to where the well is to be placed. The technical data derived from production will determine future compensation patterns. Mr. Walsh concluded that an expansion of participating lands within a unit will require the consent of the majority of landowners affected.

**Ms. Jane Lowrie**, Secretary/Treasurer for Lagasco Inc., indicated that the shares of Lagasco Corp. (a publicly traded company) along with the subsidiaries Lakeville Holdings Inc. and Lagasco Inc. were acquired from the estate of Mr. Gout. Subsequently all assets were transferred to Lagasco Inc. The shares of the shell company, Lagasco Corp., were sold in order to put together a profitable operating group. The current operator and Applicant is Lagasco Inc. The financing of the take-over of the faltering companies was by way of a combination of guarantees, cash injection, and renegotiating a five year term for the bank debts. The time frame of the negotiations and completion took from early 1999 until September 2000 to complete. The wells were not producing at the time of the corporate take-over. The company originally owed $2.9 million, and is now reduced to $1.8 million. In the last two years, the landowners have been paid approximately $8,000 in royalties. Today's company is solvent and meeting all obligations.

Ms. Lowrie noted that the drilling companies have to provide a well security/bond of $70,000 and based on negotiated terms the company has deposited $42,750. The Ministry's letter describing the incremental payments [Ex. 5] provides confirmation. The trust fund is an insurance policy for plugging/clean-up of a well in the event that an operator does not comply with regulations. No defaults on any bonds or trust funds have been posted by the company under her control.

Lagasco Inc., according to Ms. Lowrie, is approximately one-fifth of the total (94 wells) what her companies operate. This particular company take-over had problems to work out with the trade payables, the bank and the Ministry. The result is a more efficient and profitable operation, under new controllers, with assets greater than the liabilities.

Ms. Lowrie reported that the company has plugged thirteen wells for costs in a range from $10,000 to $15,000 each and a $17,000 figure is used in forecasting each expected plugging situation. The current well is under plugging order issued by the Ministry of Natural Resources on the previous owner/operators. It is her intention to produce from the well. Once a property with a good number of wells drilled on it, is purchased, it takes time to evaluate which wells should be in production and which ones should be plugged. There was no plans to drill fresh wells in Zone "C' in 2003. If all ninety-four wells needed plugging the costs would exceed the $70,000 trust fund amount. However, this scenario is unlikely because a good number of wells are producing and ongoing operations. Wells assets are constantly sold within the industry and there is not one operator in the Province capable of handling the plugging costs of all of their wells at once.

The well is economically viable based on today's market price for natural gas. Production is tracked daily and if there in a noticeable drop in production, the operative staff are deemed to know why. There is a flow meter planned for the well in the Zone "C" field and the compression and dehyde of the gas use will be calculated before the 12.5 percent royalty payments.

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The 1999 statements for Lakeville Holdings Inc. at the time of the purchase showed a poor financial condition with a negative net book value. However, the book value is not the only relevant issue in making the purchase decision. The decision to purchase was based on engineering reports from other Ontario pools and personal experience with other fields. Indications for the Zone fields are that they are depleted but can be run efficiently and produce a profit. Based on her knowledge of the statements, gas depletion figures may be recorded within the amortization figure or recorded separately as in the case of another company (Tribute Resources). In that case the figures were recorded on the statements as "write down of petroleum and natural gas assets". Ms. Lowrie concluded that it has been their experience, upon acquiring similar fields in Ontario, that some wells are viable producers while some are dry and have to be plugged.

**Mr. Hewitt**, manager of the Petroleum Resources Centre in Ontario (22 years) clarified the Ministry's position noting they are not intervening in these proceedings but accepted the invitation to answer questions concerning the Standards and **Regulations**. The testimony given will relate to clarifications of the **Act,** trust funds, regulations, licencing, and the issue of well plugging liability. Mr. Hewitt described his credentials, as an engineer (American University in Cairo, Egypt) and a designate of the Minister. He stated that he is not a lawyer or professing to give any legal opinions.

The **Act** and the **Regulation** underwent changes in 1997. These changes included a trust fund requirement under **O. Reg. 245/97, amended by O. Reg. 22/00** (section 16(1)(b)) for wells drilled. The trust definition underwent several changes in the ensuing period and the current requirement is that each operator in the Province place on trust a deposit of $70,000 under M.N.R. administration. Mr. Hewitt noted that the Trust currently held for Lagasco is $42,750 and will be topped up to $70,000 by 2007 based on the current agreement.

Each well drilled requires a licencing by the Ministry. In 1997 the **Act** changes requires every well to have a life time licence and all permit wells from 1959 onward became a licenced well. Permit wells prior to 1959 such as Well #5 in Zone "C" had to be issued a licence. Mr. Hewitt referred to the licence appearing in the applications and pointed out that the document contained the continuing operating licence number issued to Union Gas. It was further explained that an operator, prior to 1959, was required to have Ontario-wide credentials and file reports as each well was drilled. Based on the new licence issue minimum conditions are placed on the Licence despite the fact that the well already exists. Mr. Hewitt reflecting on his Notice of Decision (issued November 14th, 2002- Zone "C") noted that it included a $10,000 increase in the trust security for Well #5. The Ministry's policy since 1997 is to assess those wells with outstanding plugging orders and add a $10,000 increase in security. However, if the field is unitized the additional extra $10,000 levied would be part of the $70,000 Trust fund. If an affirmative Compulsory Order is issued the plugging order will be rescinded. Based on his knowledge there are no trust agreements specific to plugging wells other than the ones that are subject to the Minister's consent or release from it as a result of the 1997 **Act** and section 16 of the **Regulations**.

Mr. Hewitt responded to questions, surrounding the responsibility of landowners for abandoned well costs and noted, that the Ministry does not actively seek out wells that are not producing or suspended over one year. In theory, the Ministry goes after the wells that pose an immediate risk to the public or the environment placing a plugging order on whomever fits the definition of "operator" at the time. The plugging liability, according to Mr. Hewitt, starts with the

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Licence holder of record and in the event that the operating company does not exist, then the persons in control of the well or the previous owner (Union Gas in this case) receives the inspection order. The landowner is the last resort in the chain of liability for well plugging costs. If no previous owners can be found and legally attached to the liability the Ministry will resort to the trust fund to pay the costs of plugging. Hypothetically in this case the ordered would be placed on Lagasco Inc. in the first instance, then Lakeville Holdings, then the previous owners such as Union Gas before resorting to the trust fund. If the trust fund is depleted and insufficient to pay the costs as a last resort the landowners may be ordered to plug the well.

The 1997 **Act** includes the landowner within the definition of 'the operator". Mr. Hewitt stated that the Ministry has not had to resort to the trust fund for any Lagasco Inc. well(s). Overall since 1997, the Ministry has not had to resort to using the Trust funds of any operator in Ontario. The trust funds are for each individual operator, not a pooled trust, and it includes a clause restricting the trustee to spending from the Trust only with the consent of the Minister. If a well was being cleaned-up by a third party as a result of an Order and the fund is charged with the costs, the operator is required to top up the fund to $70,000 in order to continue to operate other licenced wells in their control or be ordered shut-down until the fund is restored.

Mr. Hewitt, prompted with a series of questions on the Mosa Township - Glencoe Field, from Mr. Lewis, noted that the Municipality in the case had inherited the lands through default on unpaid Municipal property taxes. Over 130 unplugged wells were discovered on the 150 acre land parcel. The land was then passed to the Public Trustee and put up for sale with the condition that the wells be plugged, a process which is no longer applicable after the 1997 **Act**. The trust is the MNR's ongoing security today. Mr. Hewitt expressed that to his knowledge, in the case of the Glencoe Fields, the commitment cost of plugging a well became the standard price of the land parcels. He stated that he was not an expert in market value analysis, but the abandoned wells obligation appeared to have an affect on the land values in this situation. In this reported case the owner(s) of lands that defaulted for Municipal property taxes were also the operators of the field.

Mr. Hewitt explained that each well in the Province requires a meter to record gas volumes (**O. Reg. 245/97, amended by O. Reg. 22/00,** section 6.). Co-mingling of more than one well on a meter is only allowed if the well is below a certain production threshold and unitization exists otherwise separate metering is the norm.

If a company's assets are sold to another the well licences can be transferred only with the consent of the Ministry. The transfer process is by way of application and any outstanding orders would be weighted in a decision to allow a transfer. Upon the transfer of licences to a new operator, the plugging liability/obligations for those wells will become the liability of the new operator (purchaser). Any trust build-up by the previous owner is non-transferrable and the new operator is obligated to post sufficient security. The Lagasco situation is a corporate purchase and a transfer of licences to a new owner.

Mr. Hewitt was not aware of any circumstances where, upon ordering a unitization, that a separate trust was mandated/included in the order. To his knowledge, in compulsory unitization hearings to date, there have been no additional trust obligations imposed on the Applicant

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within the Order, Unit Operation Agreement or the Petroleum and Natural Gas Lease/Grant. Mr. Hewitt concluded that the Ministry can order additional security funds be deposited however, the trust fund deposit figure of $70,000 may only be changed by the legislation review process.

**Mr. Lawson** introduced himself as a landowner (49 years) in Zone and outlined his involvement with the Zone Landowners Association (chairman), the Ontario and Kent Federation of Agriculture (director), Dawn-Euphemia Petroleum Advisory Committee (since 1999), Lambton County Storage Association Steering Committee, and the Kent County Wheat Producers (since 1996). These groups focused their efforts on oil and gas industry concerns such as; orphan wells, strengthening the safeguards for landowners, fair and modern terms, gas storage, and guidance from a landowner's perspective. He apologized for not being a geologist but noted his resume' records extensive research on oil patch issues, terminology and industry history.

Mr. Lawson noted his experience with contracts based solely on a handshake, some lasting over twenty-five years. The landowners focus here is to get a fair deal, or in the alternate get the wells plugged, sites cleaned-up, leases surrendered and the property titles cleared. It is his understanding the landowner owns the mineral rights under the property including the gas and the landowner leases the rights to the operator accepting a fair royalty payment against the oil/gas extracted.

Mr. Lawson stated that the landowners are willing to agreeable to a pooling agreement with some guarantees that the wells are going to be plugged when required. He expressed concerns with the lack of enforcement of the plugging rules and noted further that plugging decisions have to comply with the Regulations. Mr. Lawson indicated that he has no direct experience running an oil and gas operation but keeping the operation free of leaks is obviously efficient management. Responding to questions on his knowledge of Union Wells #5 he noted the production has stopped in recent years. However, previous to that he had observed leaks, crop damage and pipe breakage. It is his understanding that the Ministry has rules dealing with maintaining pipe and repairing gas leaks. Lagasco, in his estimation, is not in compliance. Mr. Lawson referring to a M.N.R. news release [Ex. 20] wherein a new home builder was ordered to plug a gas well because of the possible dangers it posed based on;

> "A. These restrictions are equally critical when dealing with the construction of new buildings near existing old abandoned gas wells as any disturbances may cause natural gas leaks and pool in the basement, which could cause an explosion if ignited."

Mr. Lawson noted that based on a conversation with Ministry staff it was revealed that in a similar operation old pipelines were ordered replaced and the production subsequently doubled. The operator should detect leaks with a gas sniffer and fix the leaks to enhance production and pay greater royalties. He is now aware, based on hearing evidence, that a call to the posted telephone number at pipeline sights transfers the caller to a Lagasco employee pager for their response.

Mr. Lawson noted that Mr. Walsh reported and rationalizes that unitization will provide for less waste, but it is his personal understanding that a unitization of a field works best when drilling a new pool/field. The well locations can be selected, eliminating the spacing units, and taking advantage of the most opportune locations. The existing wells are immovable so there is not a lot of savings or efficiency to be gained from this unitization. It is not appropriate here given

the age of this nearly dry pool. A pooled spacing unit is more appropriate. It complies with Ministry requirements for a spacing unit and the landowners are in favour of pooled spacing units rather than unitization as a method of joining the landowners together and producing gas. Mr. Walsh is a professional geologist and qualified to draw conclusions and express his opinion. However, Mr. Lawson stated that he does not necessarily agree or accept those interpretations/conclusions.

Mr. Lawson agreed that the metering of each well separately, as recommended by the consultant, will provide more realistic production information. Royalty calculations should be made at the well head meters and the operator should have to bear the cost of the leaking gas within the gathering system after that point. Also well status reports were not filed in some instances and shut-in pressure was recorded exactly the same for two years running indicating the last year's figures may have been used for reporting. He has reservations with the corporate well information, in Lagasco's control, based on the records noting no use of gas for the compressor.

Mr. Lawson referred an exhibit [Exh.2 tab 3, page 2] and noted the right bottom quadrant of Tract 2, in his estimation, is over and above what is required for the pooling. It takes in another 100 acres of land which he considers to be excessive. The 2000 Report was prepared with low figures geared to convince the landowners to take an unacceptable rent of three dollars per acre. The authors of 2000 Report have pulled assumptions out of the air from other sources which, in his estimation, are unrealistic given that gas values move up and down daily.

He noted that Ms. Lowrie is widely known throughout southwestern Ontario for her oil and gas operations. He expressed concerns about the financial position of Lakeville Holdings and Lagasco Inc. and the information provided by Ms. Lowrie at this hearing. The company debts have been reduced by one million dollars over the past two years in contrast to royalty payments to the landowners of approximately $10/$12,000 per year. The 2000 Walsh report, according to Mr. Lawson, was prepared to show the landowners the company was short of money and could not afford additional royalties. Lagasco Inc. is a private company and he is not aware of any information that will contradict statements that the company is solvent and the debt is being paid down as agreed.

The landowners want a special plugging trust within the order that is credit proof and not controlled by Lagasco Inc. Mr. Lawson noted that under the previous owners a new lease was proposed with a special trust and terms for indefinite "commercial" operations. However the administration of that trust was questionable and only a few of the landowners have accepted the new lease with a signing bonus.

The 12.5 percent royalty without deductions for transportation and compression costs is appropriate in this case given the age of the field, leases and the other factors. However, based on his research, the royalty percentage offered is lagging behind other areas in North America. Mr. Lawson referred to Ballem's book (3rd edition) "Oil and Gas Lease in Canada" and noted a royalty of 18.0 percent is a common royalty payment today and in North America the most common royalty is 3/16 (18.75 percent). Other sources in Alberta record a 40 percent royalty being paid. He agreed that the landowners will be getting reasonable royalty and shut-in payment which are better than the old arrangements of $100 per year rent.

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Mr. Lawson expressed concern that the wells will be operated based just on the legislation guarantee that a $70,000 trust fund can provide for an unlimited number of wells. Several sources that have been researched, concerning applications before the Ontario Energy Board[10], indicate plugging costs can be as high as $73,300 or $87,800. The ten dollars per acre per year presently offered is agreeable to the landowners but, another lease offered [Ex. 19, Bluewater, page 9-7, sec. 9] fifteen dollars per acre annually. The trust monies are not enough. Every drilled well should have sufficient money put aside by the operator to plug it.

Mr. Lawson pointed out that the various tracts should be under their proposed lease [Ex. 2, Tab 1]. In regard to Well #5 (Licence: Union #22, Zone 8-12-V, 8878) it should include only the area of the East half of Lot 11 and East half of Lot 12, Concession 4 comprising of the land parcel (75 acres) of Donald A. Havens, and the land parcel (100 acres) of Donald A. Bodkin. With regard to Well #87 (Licence: Union #87, Zone 8-11-V 8883) it should include only the area of the East half of Lot 11 and East half of Lot 12, Concession 4 and West half of Lot 11 and West half of Lot 12, Concession 5 comprising of the land parcel (75 acres) of Donald A. Havens and the land parcel (100 acres) of Florence J. Bodkin. The draft lease proposed by the landowners is relatively standard with an automatic pooling clause in it to govern the relationship between the operator and the landowners.

Mr. Lawson noted that the lease proposed by the landowner (Ex. 2, Tab 1) contains; a twenty dollar per acre bonus fee for signing, ten dollars per acre rental fee and suspended well payments of ten dollars per acre. The changes to paragraph 8 in their proposed lease deletes the word "practicable" and replacing it with the word "profitable" which better reflects the Ministry regulations. In paragraph 17 the clause "save as to this lease there is no valid lease of the leased substances..." is deleted, which places the onus on the leasing agent to ascertain the status of the landowner's property. At paragraph 22 the landowner's suggest a clause re-write, making all payments to the landowners by cheque directly. This will avoid the possibility of a deposit error with alike names amongst the landowners.

Mr. Lawson referred to drafted Schedule "A" [Ex. 2, Tab 1] attached to the landowner's proposed Petroleum and Natural Gas Lease and Grant. In summary, he noted the following core changes that should be made to the lease arrangements between the landowners and the operator:

- Paragraph 1.; 2 pooled and Overlapping Spacing Units - Zone #5 Well wherein he noted the words; "...will be and are hereby pooled in accordance with..." in two descriptive passages which, in his opinion, activates the pooling clause in the lease.
- Paragraph 2.; "Gross Royalty" wherein he records the royalty split amongst landowners at 12.5 percent of the current market value at the point of sale with no deductions.
- Paragraph 3.; "Metering" notes metering is required on each well separately.
- Paragraph 4.; "Access to Records" notes it is a requirement/right to see copies of the production figures.

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[10] Ontario Energy Board, Union Gas Limited Century Pools Storage Development, Phase II application - RP No. 1999 - 0047, September 27th, 1999.

- Paragraph 5.; "Plugging" wherein is the wording; "Lessee acknowledges that Provincial regulations require a well that has not produced for a year to be plugged...the Lessee undertakes to plug any well on the Said Lands, remove...pipelines and remediate [sp] the lands...as near as possible...to the satisfaction...of the...("MNR")" which, in his opinion, is set out in the Regulations.
- Paragraph 6.; "Limitation on Leased Substances" which limits the "Leased substances" to exclude anything below the A1 and A2 horizons.
- Paragraph 7.; "Limitation on Surface Rights and Drilling Rights" wherein he explained the rationale of the paragraph is for the protection of the landowners against newer wells being drilled.

The landowners are trying to be the willing participants in this gas field and, in the case of landowners Kelly and Oliver, they do not want operations to interfere with their recreational property. The landowners expectations for Zone are low and new wells drilled can be dry like previous attempts.

- Paragraph 8.; "No Storage Rights" wherein concerns are expressed about storage.

The landowners are agreeable to only production but, not storage. In support Mr. Lawson provided evidence that storage possibilities have been eliminated by an Ontario Energy Board ruling [Ex. 2, Tab 22];

> With respect to the matter of a Regulation which would have an effect of deregulating the designation of the Zone Pool, we have reconsidered the background and we do not think now that any particular action is involved either on our part or on the part of Union Gas Limited, other than to advise you that neither of us has any objection to the Lieutenant-Governor in Council issuing a Regulation to revoke the earlier Regulation under which Zone Pool was designated as a natural gas storage area. You may accept this letter as formal consent.

- Paragraph 9.; "Special Plugging Fund" whereby trust funds will be specifically tied to the wells for use in plugging and cleaning up the pipelines and such.
- Paragraph 10.; " Delete Article 15(C) of Lease" whereby the deletion disallows certain proprietary rights to the operator.
- Paragraph 11.; " Surrender of Old Leases" whereby the old leases are surrendered.
- Paragraph 12.; "Annual Well Payments" whereby well payments to the landowners of $500 are called for annually.
- Paragraph 13.; "No Depository" whereby he notes all landowners agree the payments should be paid direct to them.
- Paragraph 14.; "Minimum Annual Royalty Payments" where in the minimum annual royalty payments to landowners will be $10 per acre.
- Paragraph 15.; "Test and Repair Pipelines" which addresses the landowner's concerns for the state of the pipeline on their property in regard to safety, escaping gas and the hazards to the environment.

Mr. Lawson was frustrated with the negotiations between landowners and the previous owners Mr. Gout and Lakeville. New leases were offered and then revoked, and face to face discussions were always confrontational. The landowners turned to the Ministry to enforce their

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pooling and plugging regulations which took considerable time to be acted upon. Other lease offerings were made after the new owners took over the company. He was displeased that Lagasco/Lakeville made lease offers to individual landowners and not the Zone Landowners Association.

The landowners consider the terms of the proposed leases, for the unleased landowners, and the proposed overall unit operation agreement, to be unacceptable. The landowners suggest lease arrangements, negotiated by others [Ex. 2. Tab 16], to have greater acceptance with; initial payments of $6,000, rent at $30 per acre, delayed and suspended payments of $30 per acre, and a royalty of 12.5 percent. Mr. Lawson noted another lease [Ex. 19 - Bluewater] clause, dealing with trust funds, whereby the operator has to place $30,000 in trust before drilling a well and pay a one time fee of $10,000 per well, to be more acceptable.

Mr. Lawson agreed that a wide variety of leases are used in the industry and the landowner is expected to pay his share of transportation and compression fuel costs. Ontario leases cover a wide spectrum from the generous "Ranger lease", to the mid range "Union Gas lease", then the lower end "Romney Pool lease" and the lowest value, one page, "Norfolk County lease". He expressed his concerns that the Applicant is relying on the Romney Pool application as precedence given that it was unopposed by the Respondents.

The financial picture of Lagasco appears to have improved over the years and the management efforts are notable. The plugging efforts over the past few years have been satisfactory and meet the Regulations. Reflecting on Mr. Hewitt's testimony, he noted a slight relief knowing if the demise of Lagasco happened the Ministry will go after the licence holder, the trust fund and previous operators to pay the plugging costs before the landowners are approached for the costs. However he expressed reservations that the Ministry will probable be slow to react during an actual event.

Mr. Lawson stated that a legal should be required to determine the allowable drilling depths (horizons). The leases currently in place, are antiquated and likely invalid, but are not being challenged. He expressed uncertainty that enough provisions exist to drill an off-target well based on the old leases and the lack of a pooling clause. Mr. Lawson concluded that no other operator is being suggested for the operation of the pool and the landowners do not prefer to be a working interest operator.

**Submissions for the Application (Mr. C. Lewis)**

Mr. Lewis submitted that the applications for a compulsory unitization order are being brought forward under clause 8(2) of the **Act**. He referred to three issues provided in evidence, by the consultant, that: 1) no waste of the resource will result from an ordered unitization; 2) the unitization will ensure the ultimate recovery of the substances for over ten years and; 3) the order will ensure each of the parties their equitable share of the royalties from the unitized substances produced. Going forward with the unitization provides for a 12.5 percent royalty accruing to the landowners, pool expansion possibilities, meeting the general encouragement of unitization by regulators and providing benefits to all parties. The situation as it now exists makes achieving all these possibilities impossible.

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Mr. Lewis cited past decisions by the Mining and Lands Commissioner that dealt with the purpose for unitization and quoted from Lowrie Holdings Inc. - Romney Pool decision (2001)[11] which supports the applications for a unitization order. Further the Unit Operation Agreement presented in the application is consistent with those already ordered by the Deputy Mining and Lands Commissioner in the Romney case reference. He noted excerpts from J. B. Ballem's book[12] and a booklet by the Office of the Mining and Lands Commissioner[13] which further supports unitization.

Mr. Lewis submitted that no pooling applications and no cross-applications with the particulars called for in subsection 14. of the **O. Reg. 245/97, amended by O. Reg. 22/00** have been presented. The landowners have a lease registered on their property. The leases permit additional drilling, if required at a future date, and surface use in compliance with the Regulations as legislated. The unitization agreement will provide the necessary flexibility for the future. He stated that modifications and the adding of addendums to the lease is considered dangerous. The lease form and format has evolved through litigation and the provision changes. The modified form presented by the Respondents is unfair in many ways. He noted the up front payment requested by the Respondents is inappropriate given that such a payment is traditionally a negotiating incentive to convince unleased landowners to lease their lands.

The Respondents have not put forth technical evidence dealing with the interpretation or delineation of the unit area or participating areas. Mr. Lewis noted the Respondents testimony agrees with the consultant's interpretation of the unit area and the participating boundaries are established based on current evidence and technical information. The **Regulations** (ss. 22) permits applications, on the matter of metering, for a deviation in certain circumstances and criterion.

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The purpose of unitization quoted in Lowrie Holdings Inc. et al vs. All the Leased Landowners in the Romney 6-11-1 Pool (December 12th, 2001) at page 14, submissions by Mr. C. Lewis; "...the purpose of the unitization is three-fold in that it promotes,; the conservation of oil, gas and unitized substances so as to prevent waste, ensures the ultimate recovery of the unitized substances and ensures that each party interest to the order obtains their equitable share of the unitized substances produced. An order for unitization will make this possible."

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Ibidem, at Page 179; "From an operational point of view it makes good engineering and economic sense to operate a field as an entity without regard to any artificial distinctions created by the ownership sub-divisions.", and at Page 185; "It is impossible to say anything against the principle of unitization. It undoubtedly achieves better operating procedures, enhances recovery, and implements good conversation practices, al at reduced cost. It is not surprising, therefore, to find that unitization is encouraged by public conservation bodies."

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Office of the Mining and Lands Commissioner - publication, Queens Printer, entitled; "Oil, Gas and Salt Resources Act, Document of Explanation" at page 7.; "The benefits of unitization to the operator include streamlined operations, centralized facilities, and a lower economic production limit due to lower operating costs and additional recovery of all oil or gas. The benefits of unitization to the landowners include a longer production life of the pool (more royalties), less surface production equipment and a guarantee of a share in production regardless of whether a well is located on their land or spacing unit. The latter benefit occurs since all production from a unitized pool is deemed to have come from all interest owners."

Mr. Lewis submitted that the requirements of Subsection 15 (4) of the **O. Reg. 245/97, amended by O. Reg. 22/00** have been complied with in these submissions and noted the following under subsection 15.(4) for clarity;

(a) January 1st, 2003 is the proposed effective date of this Order,
(b) The geographical and geological description of the unit area proposed is submitted and contained in Exhibit 1.(a) and 1.(b),
(c) The unit area plan outlining the boundaries, tracts and participating sections are contained in Exhibit 1.(a) at Tab 11 for Zone "B" Pool and in Exhibit 1.(b) at Tab 15 for the Zone "C" Pool.
(d) The summary showing the tract allocation of the oil and gas interests within the unit area is contained respectively in Exhibits 1.(a) and 1.(b) at Tab 16 for each.
(e) The copy of an oil and gas lease that governs the relationship between the working interest operator and any surface rights and/or mineral rights owners.
(f) The copy of the Unit Operation Agreement governing the relationship between the working interest operators and the royalty interest owners is contained in Exhibits 1.(a) and 1.(b) at Tabs 15 & 16.
(g) The proposed Initial Unit Operator is Lagasco Inc.
(h) Recommend no costs awards to either party, however the right to submit is pending submissions by counsel.

Mr. Lewis noted the balance of the items in the regulated format are for the Commissioner's consideration or redundant for this situation.

Mr. Lewis stated that this is an unfortunate proceeding that has produced fruitless negotiations over the past seven (7) years. Attempts have been made by both sides which have failed for a myriad of reasons. It is not the job of the Tribunal to lay blame for these failed negotiations. Acceptance of the proposed unitization agreements by the landowners could have negated the need for this hearing. However, without acceptance, the hearing is necessary as mandated by legislation. All parties are being heard on the issues.

Mr. Lewis submitted that the Respondents arguments are predicated upon the Applicant's financial solvency. There has been no evidence of insolvency since Jane Lowrie purchased the company from the Gout estate in 1999. The business operates as a going concern with a well plugging program in place which complies with the **Act**. Notably seven (7) wells have been plugged since the corporate take-over. The Respondent's argument on insolvency is weak and there is no evidence of it after 1999. In a worst case scenario (insolvency), which is not suggested here, there is the potential for the successor operator of the assets or the previous /prior operators to shoulder the plugging cost liability, as well as, reliance on the trust to pay such costs. Mr. Lewis paraphrased the evidence by Mr. Hewitt of the M.N.R. noting that the trust referred to under section 16. Has not been used for any defaulted obligations in the past 6 years and the Applicant is in compliance with the **Regulations**.

In regard to health and safety issues, Mr. Lewis noted that the Applicant is in compliance with the **Act** and the Respondents did not provide any new evidence to the contrary.

Mr. Lewis submitted that the **Oil, Gas and Salt Resources Act**, the **Regulations** and the Provincial Operating Standards all have safeguards to deal with the plugging cost issues. It is inappropriate for the Commissioner to embark on a police type mission and add provisions to any lease. The system has an extensive code in place for the inspectors and the Ministry.

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Mr. Lewis noted that the existing lease land relationship between the operator and the landowners is recognized as antiquated in terms of compensation. However, the unitization terms proposed provide for a modern day 12.5 percent royalty. The Tribunal should accept and adopt the unit agreement as presented and reject the extraneous clauses and pooling as set forth by the Respondents. The royalty should be calculated in the normal fashion; after deductions for compressor changes or compressor gas not "at the well head" as suggested. The costs to market is something that should be borne by both parties as it is equitable. It is in everyone's interest to repair pipelines, get on with production and share in the revenue and benefits. The relationship is one of give and take and the operator doesn't want difficult relations with the Zone landowners.

Mr. Lewis submitted that opposing Counsel's recollection of the evidence is not completely accurate and his personal attacks on the witnesses during summations is considered petty. The evidence given by the expert witness and the company personnel is the preferred evidence on technical matters and something Mr. Lawson, for the Respondents, agrees with. The Applicant is in a position to get operations underway and produce royalty revenue resulting in compensation for the landowners.

**Submissions of Mr. J. Chinneck for the Respondents**

Mr. Chinneck submitted that the Respondents in this hearing are second generation farmers and landowners in Zone Township who have been exploited by the gas companies for over 60 years. The landowners agree with the joining of interests through a pooling agreement to protect their rights. They have tried to negotiate fair terms and the assurance that the liability to plug wells by the operating oil company will be taken care of in a timely manner.

The drafted agreements presented do not have adequate provisions for the security of the landowners interests and there is a real possibility the abandoned wells can become the farmer's liability. There is nothing in the agreements to cause the operator to operate safely and the operator if not caused or ordered to operate safely can create a risk to people in the area.

Mr. Chinneck submitted that the ultimate issue is, who will pay for a well abandonment/ plugging? The cost assumptions are calculated at $6,000 per well, but it is more likely the bill will be $17,000 for the plugging cost. Based on the financial statements Lagasco is insolvent and the $17,000 plugging/repair can eventually be the farmer's liability. The calculations for the plugging costs for the total Zone wells ($677,000) and the present value information for the whole field (negative $162,000) indicates insolvency. It is the operator's liability that is at issue here and assurances should be included in the Mining and Lands Commissioner's Order to provide comfort for the landowners.

Mr. Chinneck submitted that the expert witness, Mr. Walsh, to his estimation, impressed as a hired gun writing a report in 2000 to persuade farmers to take a $3 per acre lease based on a bleak picture he painted. The older 2000 report showed an 8.5 percent decline rate, which will deplete the field in approximately eleven years. The 2002 report, in contrast, shows a decline rate of 5 percent with a 20 year life for the field. The references are confusing and this application, to unitize, shows the field is not in its twilight years. Mr. Chinneck noted the consultant adopted a fairly significant reservoir in the first report for the Zone "C" Pool and shrunk it to 100 acres in area for the newest report.

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Mr. Miller, in Mr. Chinneck's opinion, lacked general awareness of the Zone wells in operation during questioning and appeared confused concerning well records. Mr. Chinneck noted that poorly kept company records, to his understanding, may be an offence under the Act at section 19(1)(b)[14] and subject to penalties. Based on his observations, the Ministry and the landowners have doubts concerning the production volume accuracy. The information the landowners have to accept for their royalty calculations less costs/charges..

Mr. Chinneck reflected on the company financial statements (1999) and Ms. Lowrie's testimony. She was not certain of where abandonment and capital assets cost were allocated in the statements. He provided calculations that the net equity in the statement of negative $1.35 million is possibly understated by 41.4 million or more when the potential liabilities are added in. Mr. Chinneck suggested Lagasco Inc. considers the landowners to be insignificant nuisances having paid only approximately $20,000 in fees over a two year period.

He noted that Mr. Hewitt's testimony confirmed that the landowners have the ultimate liability for plugging and the plugging liability costs can affects the value of properties. He noted the testimony shed some light on the operation of the trust funds. Mr. Chinneck added that it is his understanding the unitization of Zone "C" Pool will delete the necessity of the $10,000 extra security while the Respondents still see a need to continue the increased amount for the security reasons. He noted the dovetail fit of the requirement with the landowner's proposed pooling and trust conditions to reach a satisfactory level of security.

The landowners want a fair and modern lease similar to the "Range" lease presented into evidence. The Respondents are prepared to accept a compulsory unitization provided the lease schedule proposed by them is adopted and overrides the unit operation agreement. The Respondents require agreeable items such as; a $20 per acre initial payment, metering of each well, 12.5 percent royalty, and drilling restrictions to A-1, A-2 horizon depths only and no new wells drilled. Based on the Respondent's concerns with the accuracy of the company data, calculation of the royalties should be without deductions and fixed at 12.5 percent. Mr. Chinneck submitted that the landowners would prefer the old leases surrendered and replaced by their drafted modern version [Ex. 2, Tab 16].

Mr. Chinneck submitted that there is no new geology being relied upon, yet Mr. Walsh shrunk of the Zone "C" Pool reservoir size and changed the center point of the field in his report. He considered Mr. Walsh's attempts/recommendations to be standard pool requirements set down by the Ministry. He concluded that it is Ballem's rationale for unitization that operation efficiencies are achieved at the outset of a field development, not when the infrastructure is already in place as it is here.

The landowners have been treated poorly over the years being paid only $1 per acre by the previous operators (Union Gas and Lakeville). The current operator Lagasco has paid likewise and while reducing debts by $1 million paid the landowners only $20,000 over the same

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[14] Mr, Chinneck read from clause 19(1)(b) of the Act; "makes an offence to knowingly make a false statement or provide false information in a document or other form of communication required by the Act or by the Regulations."

two year period. Past financial information (Union Gas) showed sales of $1.2 million from this field which at a 12.5 percent royalty would be an approximate $150,000 royalty yearly however, the landowners received only $10,000. Based on the inadequacy of compensation to the landowners and the failed negotiations in the past, the Tribunal should consider a lump sum payment retroactive to 1996. He submitted that unitization of a 60 year old field is not appropriate while pooling is adequate allowing for the efficient and fair exploitation of the resources. Mr. Chinneck reviewed the lease from the previous Romney[15] decision by the Office of the Mining and Lands Commissioner noting that the lease ordered protects operator and the application for unitization was unopposed.

Mr. Chinneck submitted that Counsel for the Applicant is suggesting the health and safety enforcement issues be governed by the standards and regulations set by the Ministry of Natural Resources not the lease terms. There is a serious risk of accident and/or fatality because it is his belief the Ministry is not enforcing the Provincial Standards and Regulations due to its serious manpower shortage which precludes them from doing their jobs confirmed by Mr. Lawson's testimony that telephone calls by the landowners to Lagasco resulted in a slow reaction to problems detected throughout the gathering system.

Mr. Chinneck concluded that there is no standard lease in the oil and gas industry and no lease that protects the Lessor. The documents have been drawn by industry, for industry to protect their interests to exploit the resources. It is time for leases and the Compulsory Order to reflect some of the checks and balances the Respondents request, drafted with fairness and language that protects the landowners. Mr. Chinneck agreed that the relationship has to have give and take. The Order has to be a fair arrangement amongst the parties.

**Mr. J. Chinneck submissions on Jurisdiction (special trust)**

Mr. Chinneck submitted that the Tribunal has the authority to grant provisions under sections 8(1) and 8(2) of the **Act** that include a special plugging liability trust. It is his interpretation that 8(2) allows for a "special plugging trust" to be included in the Order according to the phrase "costs and benefits of the drilling or operation be apportioned in a manner specific in the Order". Clauses 14 and 15 of the **O. Reg. 245/97, amended by O. Reg. 22/00** stipulates at each paragraph (e); "a copy of the oil and gas lease that governs the relationship of the parties" and this gives the Tribunal the authority to include a new lease or change its terms within an Order. The Respondent's request for a special trust in the order is asking the Tribunal to act within its power under the **Act** and incorporate all the terms of the schedules proposed by the Respondents. The special trust funds are separate and identical to the trust funds already included under the **Act**.

**Mr. C. Lewis submissions on Jurisdiction (special trust)**

Mr. Lewis submitted that the power to impose additional trust is coercive. The trust obligations are covered by the **Act** and the **Regulations** and the provisions are very specific. It could change in the future, however the proper way to have any changes of this type occur is by way of

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[15] Romney 6-11-1 Pool, application for unitization; Lowrie Holdings Inc. et al v. All Leased Landowners in the Romney 6-11-1 Pool, December 12th, 2001

legislative amendment. Provisions within an order has never been done before in this type of proceedings, both before the Commissioner and the Ontario Energy Board, and Mr. Hewitt of the Ministry of Natural Resources confirmed it.

The **Regulations** (cl.16) provide for a trust that covers plugging costs therefore it is not necessary to duplicate it in the order even if the tribunal has the jurisdiction to do so.

Mr. Lewis submitted that section 8(2) of the **Act** does not provide the authority to make an order which includes a provision for trust fund monies. Sections 8(2)(a)(b) or (c) do not include the right of the Commissioner to enlarge upon trust requirements. The **O. Reg. 245/97, amended by O. Reg. 22/00** (cl. 16) sets out the requirements under the **Act**. The authority of the Mining and Lands Commissioner within the **Act** is a statutory one, with no inherent jurisdiction. Mr. Lewis submitted that support for his claim is found in **Keable vs. The Attorney-General of Canada**[16] based on the principles involving administrative issues for Boards and Tribunals (at page 27, para. 41&42);

> Section 7 of the Provincial Act purports to confer upon a Commissioner," (Police Commissioner in this case) "...all the powers of a Judge of the Superior Court in terms, but this cannot make him a Superior Court, as this is something a provincial legislature cannot do by reason of Section 96 of the B.N.A. Act: see the recent judgement of this Court in A.G. Quebec v. Farah..." and further "The Commissioner does not enjoy the status of a Superior Court; he has only a limited jurisdiction. His orders are not like those of a Superior Court, which must be obeyed without question; his Orders may be questioned on jurisdictional grounds because his authority is limited. Therefore his decisions as to the proper scope of his inquiry, the extent of the questioning permissible, and the documents that may be required to be produced, are all open to attack...", "Because a Commissioner has only limited authority he enjoys no inherent jurisdiction, unlike Superior Courts which have such jurisdiction in all matters of federal and Provincial laws unless specifically excluded. It is by virtue of this inherent jurisdiction that Superior Courts which have a general superintending power over federal as well as Provincial authorities, as held in the Three Rivers Boatman, (supra.). It is unnecessary to decide in the present case whether any possible attack against an Affidavit made under Section 41(2) of the Federal Court Act comes within the exclusive jurisdiction conferred upon the (Trial Division) of the Federal Court by Section 18 of the Act, because I find it clear that any jurisdiction for entertaining such an attack can only be found in a Superior Court."

Where jurisdiction of a Commissioner is created by Statute, there is no inherent jurisdiction.

Mr..Lewis submitted further support is found in **CBC v. Cordeau**[17], where "the Commission" is the Quebec Police Commission, at page 2;

> "...obtained its power from the Provincial legislation and has no inherent powers. To have the powers of a superior court, the members would have to be appointed pursuant to Section 96 of the British North America Act, 1867. The applicable provincial legislation only gives power to deal with contempt committed before the Commissioners."

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[16] Keable v. Attorney General of Canada Et Al, 6 C.R. (3rd) 145, [1979] 1 S.C.R. 218, 43 C.C.C. (2nd) 49, 90 D.L.R. (3rd) 161.

[17] Canadian Broadcasting Corp. v. Cordeau, 14 C.P.C. 60, [1979] 2 S.C.R. 618, 28 N.R. 541, C.C.C. (2nd) 289, 101 D.L.R. (3rd) 24.

and at page 17;

> "Unlike certain courts of law the Police Commissioner has no inherent powers: it has only those powers which are conferred on it by statute. There is no need to undertake a demonstration of this proposition, which seems neither disputed nor open to dispute. If there were any doubt on the point, it could be resolved merely by reading the observations of Pigeon J., speaking for the majority of this Court, in **A.G. Quebec vs. A.G. Canada.**"

Mr. Lewis submitted that both the **Keable** and the **CBC** cases are clear on the principle of no inherent jurisdiction. The jurisdiction of this Tribunal is confined to the statutory provisions that provide its authority.

Mr. Lewis submitted that imposing a special trust by way of clause 15(4)(e)&(f) of the **O. Reg. 245/97, amended by O. Reg. 22/00** is not appropriate given that the provision is general in nature and the actual authority to provide an order is found in the **Act** at section 8(2). Further **Keable** case support is found at page 23;

> It is therefore clear that no provincial authority may intrude into its management. While members of the force enjoy no immunity from the criminal law and the jurisdiction of proper provincial authorities to investigate and prosecute criminal acts committed by any of them as by any other person, these authorities cannot, under the guise of carrying on such investigations, pursue the inquiry into the administration and management of the force. The doctrine of colourability is just as applicable in adjudicating on the validity of a commissioner's term of reference or decisions as in deciding on the constitutional validity of legislation." "You cannot do that which you are prohibited from doing directly."[18]

The Tribunal cannot do indirectly that which it is prohibited from doing directly.

Mr. Lewis submitted support from another Supreme Court of Canada case[19] (**CP Air**) concerning a Tribunal's authority and the Canadian Labour Code (section 121);

> "... a general provision which empowers the Board to make orders requiring compliance with the provisions of Part V - does not include a power to compel the production of documents outside the context of a formal hearing. The general provisions of the Code cannot be construed so as to give to the Board powers which are broader than those expressly and specifically provided for elsewhere. Since the power to compel the production of documents has been specifically treated in section 118(a), section 121 cannot be used to circumvent the special limits imposed on the power by that provision."

and at page 11,

> " ...first, the general may not be interpreted so as to render unnecessary the other provisions setting forth the power of the Board, and second, the limitations inherent in the specific provisions, which detail with the powers of the Board, must be abided by if the intent of the legislature is to be respected. One of the issues in that case was the proper relationship between a broader, general

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[18] **Viscount Simon in; A.G. Sask. v. A. G. Canada**, [1949] A.C. 110 at 124,[ 1949] 1 W.W.R. 742, [1949] 2 D.L.R.145.

[19] Canadian Pacific Air Lines Ltd. v. Canadian Air Lines Pilot Assn., [1993] S.C.J. No. 114 (S.C.C.)

> provision, Section 121 of the Code, and the grants of powers made specifically elsewhere in the Code." " It is quite possible that Section 121 covers only the powers necessary to perform the tasks expressly conferred on the Board by the Code, as Pratt, J. indicated. Nevertheless, I considered that even if it covers autonomous or principle powers, like that of ordering a reference to an arbitration, and not merely incidental or collateral powers, it cannot cover autonomous powers to design to remedy situations which the Code has dealt with elsewhere, and for which it has not prescribed specific powers, as is the case with unlawful strikes."[20]

Mr. Lewis submitted that there is a specific provision concerning the Tribunal's powers in section 8(2) of the **Act** and the general provisions of the **O. Reg. 245/97, amended by O. Reg. 22/00** on how the order is to take shape. The legislation provides for trust obligations in clause 16 of the **Regulations** where it is set out the manner in which the Trust is to be set-up, who will hold the Trust, increments of the Trust, etc. The **CP Air** case[21] at page 14 (para. 29) reinforces the principle and in its conclusion offers;

> " The extent of the power granted by section 118(a) of the Code appears from the plain meaning of the words of the provision. The Board may exercise its power to compel the production of documents, only in the context of a formal hearing. This conclusion is supported also by the fact that the nature of the power is coercive, and that the limits on its exercise must be respected. The fact that the power is also judicial in character makes extension of its application to an administrative context, one which would require clear words to that effect. The structure of the provision makes the power to compel the production of documents a part of a complete process which is limited to a formal hearing to which witnesses may be summoned and where they may give evidence on oath. The scope of section 118(f), which is permissive in nature. Similarly, the presence of broader provisions cannot here operate to allow the special limits imposed on powers such as this to be disregarded. As there is no basis for the conclusion that such a confinement of the power would be consistent with the purposes of the Board, when its administrative and judicial functions are considered, the power which is conferred on the Board by section 118(a) is a power to require witnesses to attend a proceeding before the Board and there to give oral or written testimony and produce documents deemed requisite. In these circumstances, the powers conferred on the Board by subsections 118(a) and 121 do not include a power to compel the production of documents outside the context of a formal hearing."

Mr. Lewis concluded that the tribunal's jurisdiction to order the special trust is deemed inappropriate.

**Mr. Chinneck - cost award**

Mr. Chinneck requested an award for costs based on the rationale of the failed negotiation history to get fair rents. He suggested that both the Applicant and the Respondent legal costs be combined and apportioned 12.5 percent for the Respondent's account/payment and 87.5 percent for the Applicant's account/payment.

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[20] Beetz J. wrote in; Quebec et de L'Acadie v. Canada Labour Relations Board, [1984] 2 S.C.R. 412, at p. 432.

[21] Ibidem

**Mr. Lewis - cost award**

Mr. Lewis submitted that the Applicants hearing costs be considered based on the rambling nature of the evidence by the Respondents, as it unfolded, and the inexperience of the Respondent's counsel. It was his original approach that costs be borne by the parties for their own account(s). The usual circumstances for awarding costs is based on the criterion that; one party has acted unreasonably within the conduct of the hearing or, one party has wasted the Commissioner's time, or one party has been unreasonable and perhaps put in unnecessary evidence, or prolonged the hearing in some fashion. Counsel for the Respondent's, by his estimation, did not fall within the noted categories/definitions. He suggested the opposing Counsel's approach to costs seems to be based on wanting compensation for the landowners within awarded costs, which is, an inappropriate request of this hearing. The cost split suggested by the Counsel for the Respondents is unworkable and unrealistic. It is inappropriate to apportion fault or play catch-up in a relationship through the awarding of costs mechanism.

Mr. Lewis submitted that no expert testimony was presented by the Respondents and the applications were not dealt with on their merits. Either party can apply at any time for the combining and operation of the pools which is something Mr. Lawson intimated it in past correspondence, but did not carry through with the request. Mr. Lewis concluded by requesting the Applicant's costs be assigned to the Respondents for payment.

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## FINDINGS

**Purpose of the Act**

In Ontario, the **Oil, Gas and Salt Resources Act** has evolved since 1990 undergoing various amendments throughout the period. Within today's **Act** there is a role for the Mining and Lands Commissioner appointed under the **Ministry of Natural Resources Act**.

The **Act** does not contain a purpose statement and is therefore silent in this regard. However, upon examination of several Statute and regulatory sources, a determination of the purpose is evident.

In subsection 2 of the **Mining Act**, the legislation notably encourages exploration of mineral resources;

> 2. The purpose of the Act is to encourage prospecting, staking and exploration of the development of mineral resources and to minimize the impact of these activities on public health and safety and the environment through rehabilitation of mining lands in Ontario.

and within that **Act** is the definition of mineral which clearly supports a purpose for oil and gas exploration;

> "minerals" means all naturally occurring metallic and non-metallic minerals, including natural gas, petroleum, coal, salt,...

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Generally it can be concluded that the purpose of the **Oil, Gas and Salt Resources Act** may be derived from the **Mining Act** and the provisions of subsection 8(1)(a) and (b) of the **Act** and the **Regulation's** at clauses 14. and 15. These indicate clearly defined procedures to follow in the development of oil and gas resources.

Alternatively, rather than a clear directive stating the purpose of the **Act**, the tribunal is satisfied on the circumstances of this case that the underlying purpose of the legislation can be ascertained through a consideration of the consequences of discontinuing exploration. Specifically, if the exploration and production from under these lands were to cease altogether, the economic benefits to operators, employees, royalty interests and the economy overall would be negated. The purpose of the **Act** is evident through various definitions and their references to the procedural applications for exploration and production of oil and gas.

While the foregoing discussion is by no means absolute in these matters, it is noted by the Tribunal that effectively Lagasco Inc. cannot produce from existing wells underlying the area without having this application to unitize granted.

**Directives**

The Tribunal finds granting of a Compulsory Order under subsection 8(2) of the **Act** is directed and influenced by the **Regulation** and the Provincial Policy Statement. These references are designed to standardize operations throughout the Province, protect the correlative rights of landowners, respect the way of doing business, and continue to trust in the industry's ability to evolve equitably.

The **O. Reg. 245/97, amended by O. Reg. 22/00** outlines the remedy to a stalemated voluntary unitization situation. Clause 8(4) of these regulations, allows for an application for a Compulsory Order;

> 8.(4) if an area is unitized by a voluntary agreement among the oil and gas interest owners within an area and the Minister agrees with the unitization, or if an area is unitized by an order of the Commissioner, the Minister shall revoke or amend any pooling conditions on licences for wells located in the unitized area, and may as the circumstances of the unitized area warrant...

The background and submissions presented herein, indicate an obvious stalemate between the parties and the remedy is sought after herein.

There is clear direction provided for in the **Regulations** for consolidation efforts under unitization;

> 8.(3) No person shall,
> (a) drill a well in a spacing unit that has been pooled;
> (b) produce oil or gas from a spacing unit that has not been pooled;
> or
> (c) produce oil or gas from more than one well in a spacing unit.

The Tribunal takes further direction in providing an Order from the Provincial Policy Statement[22] at section 2.2.1;

> "Mineral resources (mineral aggregates, minerals and petroleum resources) will be protected for long term use."

and section 2.2.2.1

> "Mineral mining operations and petroleum resource operations will be protected from activities that would preclude or hinder their expansion or continued use or which would be incompatible for reasons of public health, public safety or environmental impact."

and section 2.2.2.4

> "Extraction of minerals and petroleum resources is permitted in prime agricultural areas provided that the site is rehabilitated."

The Tribunal finds the spirit of the various sections of the policy is not being compromised by the Order for unitization. Unitization addresses protection of the resource for as long as it will sustain production. The Standards and **Regulations** address the needs for public and environmental safety. Further the Standards and **Regulations** address rehabilitation of the lands after production ceases.

**Merits of the Application**

The Applicant focused their attention on submissions and testimony for a Compulsory Order for Unitization in compliance with **O. Reg. 245/97, amended by O. Reg. 22/00** at subsection 15 and put forward the argument that the field is best utilized within a Unit Operation Agreement.

The Respondents through submissions and testimony, presented their version of joining interests and new terms for their leases. They recounted considerable adversarial negotiating history for the Tribunal and argued for greater remuneration, fair terms and guarantees. In these arguments they laid out challenges to the Applicant's motives and decisions to produce from a "thin and patchy" gas field, questioned the relationship and the stability of the **Regulations** and the Standards to serve the landowners interests.

The insight and questioning provided by the Respondents is appreciated by this Tribunal in considering this Order. The Tribunal finds the Respondents arguments lead to challenges of the core elements of the industry. Questions on the ownership of the oil and gas substances underground that surfaced in the Respondent's testimony, the Tribunal finds, are best explained through the industry root terms; "Rule of Capture" and "Correlative Rights". The Respondents appeared confused on mineral and petroleum substances ownership and while their logic of land ownership is not misplaced the interpretation of carbon substance ownership requires some clarification.

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[22] **Order-In-Council 764/96** (May 8, 1996)

The ***rule of capture*** is an expression used extensively within the oil & gas industry. The tribunal relies on several sources for discussion. In Ballem[23] where he writes;

> The "rule of capture", succinctly phrased by Hardwicke[24] is, "[T]he owner of a tract of land acquired title to the oil and gas which he produces from wells thereon, though it may be proved that part of such oil and gas migrated from adjoined lands," is firmly entrenched in Canadian Law in Borys v. Canadian Pacific Railway and Imperial Oil Limited[25], the Privy Council said:
>
> The substances are fugacious and are not stable within the container although they cannot escape from it. If any of the three substances is withdrawn from his property which does not belong to the appellant, but lies within the same container and oil and gas situated in his property thereby filters from it to the surrounding lands, admittedly he has no remedy. So also, if any substances is withdrawn from his property, thereby causing any fugacious matter to enter his lands, the surrounding owners have a remedy against him. The only safeguard is to be the first to get to work, in which case those who make the recovery become owners of the materials which they withdraw from any well which is situated on their property or from which they have authority to draw.

Also found in the Kelley v. Ohio Oil Co[26] is further explanation of the *rule of capture* relevant for our purposes herein;

> The right to acquire, enjoy and own property, carries with it the right to use it as the owner pleases, so long as such use does not interfere with the legal rights of others.
>
> To drill an oil well near the line of one's land, cannot interfere with the legal rights of the owner of the adjoining lands, so long as all operations are confined to the lands upon which the well is drilled. Whatever gets into the well, no matter where it comes from. In such cases the well and contents belong to the owner or lessee of the land, and no one can tell to a certainty from whence the oil, gas or water which enters the well came.

Ontario supports the "Rule of Capture" whereby those substances found and taken into possession by the operator are within their ownership. While the surface rights are rightfully the landowners no ownership of the oil and gas laying under the lands exists until an operator has taken them into its possession. Ownership upon capture is clearly with the working operator.

The balancing rule for the landowners in this equation is the Legislative efforts to protect landowner's ***correlative rights***. The Tribunal finds that the issue of correlative rights of landowners is a core element of the petroleum industry and the protection of those rights has been argued extensively in law[27]. The Office of the Mining and Lands Commissioner has summarized the terms used in this industry in various printed pamphlets and the following explanation is quoted;

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[23] Ballem, John Bishop, The Oil And Gas Lease In Canada, 3rd. Ed., page 106, (Toronto: University of Toronto Press, 1999).

[24] Hardwicke E., The Rule Of Capture And Its Implications As Applied to Oil And Gas, 13 Texas Law Review, 391, 393 (1935)

[25] [1953] 2 D.L.R. 65, (1952-53) 7 W.W.R. (N.S.) 546, 550 (J.C.P.C.)

[26] Kelley V. Ohio Oil Co.; 57 O.S. 317, 327, 328 (1897).

[27] Ibidem, at page 32 herein - Bory's v. Canadian Pacific Railway and Imperial oil Limited

> The Correlative Rights[28] of landowners; means the inherent right of an owner of oil or gas in a pool to his share of the production and reservoir energy and his right to obtain his just and equitable share of production and to be protected from wasteful practices by others in the pool.
>
> The Protection of Correlative Rights of landowners is provided for by the Province under the **Act** in that it places requirements on the operators to drill and produce a well within the target area of a pooled spacing unit.

The statutes and **Regulations** are written with respect for the correlative rights of landowners through spacing unit designations, reasonable set-back requirements and compensation methods. This unitization application has met the pre-conditions with regard to the rights of interested parties represented by four executed lease agreements with protective, continuation and royalty clauses contained therein. The Tribunal finds the landowner's correlative rights will be addressed and accounted for in the Unit Operation Agreement.

The matter of the existing lease validity was not raised as a direct issue in this hearing. However, it was questioned extensively in the hearing testimony. The Tribunal finds such matters properly rest between the parties to the agreements who may or may not elect to challenge the terms of such leases. The lease relationship is a contract and support for the principles is found in Anson's Law of Contracts, 20th ed. (pp. 1-2);

> The parties to a contract, in a sense make a law for themselves; so long as they do not infringe on some legal prohibition, they can make what rules they like in respect of the subject matter of their agreement, and the law will give effect to their decisions.

The older lease contracts, with only basic elements recorded, relies on this theme. Further the principles of a basic contract is discussed by S.M. Waddams[29];

> ... there is nothing to prevent parties from entering into contracts on terms written out on half a sheet of notepaper...

Specific to an oil and gas lease contract support can be found in Gallagher v. Gallagher[30] where the Court resolved;

> When such a "mineral lease" (profit a' prendre) has been granted and then protected by registration of a caveat, it cannot be defeated.

The Tribunal finds the lease effectively allows the parties to the lease to determine the terms and conditions which will govern their relationship. The Tribunal is aware that the leases of a majority of landowners can serve as the cornerstone for any Order. Numerous sources and cases in law influences the description of a Petroleum Oil and Gas Lease/Grant and it is generally accepted

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[28] Oil, Gas and Salt Resources Act, document of explanation, page 4, authored by the Office of the Mining and Lands Commissioner, Queen's Printer Ontario, printed in Ontario, Canada, 2000.

[29] S. M. Waddams, The law of Contracts, 2nd Ed., Aurora; Canadian Law Book 1984, pp 29.

[30] Gallagher v. Gallagher (1962-63) 40 W.W.R. 35 (Sask.); pp 770

that it is a document "profit a'prendre" being more than a realty lease or an easement. The Tribunal dealt with the document description in Gaiswinkler[31] previously and considers the lease recognizes ownership of the hydrocarbon substances captured by the lessee, brought to the surface into their possession and inventory, provided they are a certified well licence and is the lessee of so much land held under lease for that purpose.

The Tribunal finds accepting the older leases as a basis for this Order does require some explanation. Some of these Zone "C" Pool leases were founded in the 1980's with pooling clauses allowing the Lessee to effectively join the leased lands with other adjacent landowners. There are four leases continuing in affect and registered. The salient passages within the lease(s) at each habendum form continuation. Respectively they are;

> TO HAVE AND TO ENJOY the same for a term of ten (10) years from and including the date hereof and so long thereafter as the leased substances or any of them are produced from the said lands, subject to the other provisions herein contained.

and

> The rights hereby granted shall continue for a term of twenty years from the date hereof and so long thereafter as any of the said substances is or are produced in paying quantities from the said lands or any part them and/or as long as the Lessee continues operations...

and

> ... do hereby grant and demise unto the said lessee, for the term of ten years and so long thereafter as oil or gas is produced in paying quantities, all the petroleum oil and natural gas, which may be found under the lands intended to be included in this contract, together with the exclusive right to carry on geographical research work and to drill for and remove said oil and gas...

and in one instance a pooling clause (1989 lease);

> ...The Lessee is hereby given the right and powers at any time and from time to time to pool or combine the said lands...

The passages note continuation, specific to performance criterion held within the lease agreements. The Tribunal finds the parties agree, certainly at this moment, to the continuation of the relationship and working the proposed unit for hydrocarbons.

The Tribunal's reference to the continuation clauses by no means determines their fate as a contract, that challenge is best left for the courts to decide. Further the tribunal has heard no new arguments against the lease documents that would prompt the Order to include fresh leases for all lessors. The Tribunal is convinced by the Applicant's submissions that the unitization agreement will address the modernization of terms expressed.

The Tribunal finds it is not in a position to question or rule on a lease continuation based on the ongoing features of the lease. In any event, the jurisdiction for examining the validity of the leases properly falls under the jurisdiction of the Courts, should either/any party be inclined to raise a challenge. This Tribunal will be bound by Court decisions.

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[31] Gaiswinkler

The Respondents challenged the Applicant's motive to explore and whether it is in their best interests to proceed on a minimum of geological information. The Tribunal finds that if the Lessee/operator is willing to risk its drilling investment with no onus or financial support required of the Lessor(s), then their sole determination and decision to satisfy the requirements for a licence to drill and produce hydrocarbon substances is sufficient.

This Tribunal finds the suggested term "commercially viable quantities", as well as, "found", "in producing quantities", "sufficient quantities" is or are relative to the industry root term "in paying quantities" which has been discussed extensively in law. Ballem[32] at pages 132 and 133 draws his conclusion on the matter;

> It would seem therefore that a Canadian Court forced with a reference to "producing in paying quantities" in the habendum would opt for revenue verses operating costs, and exclude the cost of drilling and equipping the well.

and further in the case **Stevenson *v.* Westgate**[33];

> *Stevenson v. Westgate* stands for the proposition that a Canadian court forced with the test of 'producing in paying quantities', would opt for revenues versus operating costs rather than some other guideline such as whether a 'reasonably prudent operator' would continue to operate the well.

The decision to continue to explore and drill for hydrocarbons is for the risk of the operator.

The Tribunal is convinced the operator is not advancing their efforts based solely on determination. The historical records submitted for past yearly gas volumes of between 2300 (10-3-M3) and 5800 (10-3-M3), submitted prior to 2000, gives them some comfort for their decisions.

The Respondents put forward text alternatives and alike modern industry terms in their attempt to negotiate better lease agreements. The Tribunal finds the Applicant's drafted unit operation agreement serves to address the expressed concerns of the Respondents in terms of; royalty percentage to be paid out, plugging liability conditions, continuation of the relationships and defining boundaries. The Tribunal notes the draft unit agreement includes fair and modern concepts and support for the modernization efforts is found in Ballem[34] ;

> (pp. 218-219)
> Effect of Unitization
> The model agreement provides that, upon the interests of each royalty and working interest owner being unitized, the unitized zone shall be treated as though it had been included in a single lease executed by the royalty owners as lessors and by the working interest owners as lessees and as if the lease had been subject to the unit agreement. This is the fundamental effect of unitization, and thereafter individual lease boundaries may be disregarded for operational purposes.

and

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[32] Ibidem, (3rd, edition)

[33] [1941] 2 D.L.R. 471 (Ont. S.C.O.), [1942] 1 D.L.R. 369 (C.A.)

[34] Ibidem; Ballem (3rd Edition).

> (pp.222)
> Amends the Lease
> The unit agreement substantially changes the terms of any lease. In Alminex Limited v. Berkley Oil and Gas Ltd.[35] It was held that unitization only amends a lease to the extent it was specifically provided for in the contractual terms. Presumably to overcome this limitation, a clause in the unit agreement provides that each lease is amended to the extent necessary to make it conform to the agreement.

and

> (pp.222)
> Lease Ratified
> By executing the unit agreement a lessor, unless a court action has been commenced or is pending, ratifies and confirms the lease and agrees that no default exists with respect thereto and that the lease is in effect. Since the lease itself requires execution under seal and the unit agreement purports to amend and ratify the lease, the agreement should also be under seal.

Further questioning of the regulations and the motives behind rules and standards was raised by the Respondents. The Tribunal finds it does not have the power of the Ontario Legislature in such matters nor is it empowered to offer suggestions as to the statutes and regulations make-up as the Respondents suggest. The scope of the Tribunal's task is to entertain applications providing a remedy for the joining of interests and protecting the various interests.

The tribunal, reflecting on testimony and submissions notes that neither party is aware nor has high expectations for the field.

The subject of the Petroleum and Natural Gas Lease(s)/Grant(s) drew considerable discussion and submissions. The relevance to this application can be identified in two distinct references. First the lease as a continuing contract and secondly maintaining the landowners correlative rights. The continuation of the current executed and registered Petroleum and Natural Gas Lease(s)/Grant(s) is upheld by the Tribunal as referenced previously above. The Tribunal finds that no replacement leases nor changes to the existing executed leases is or are needed.

The Respondents and their Counsel challenged the size of the properties on the grounds that the lands to be included in the unit will be excessive. The Tribunal accepts the spacing fabric laid down by the Ministry for the area and finds the boundaries are within those guidelines. While the lands may be non-participating at the outset of this unitization, as things progress they may well come into play as the field is assessed. The landowners directly affected will receive their due entitlement through unit management filings and notice rather than having to address a future Tribunal on the matters.

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[35] [1971] 4 W.W.R. 401 (Alta. S.C., T.D.); [1972] 6 W.W.R. 413 (Alta. S.C., App. Div.), Aff'd (1974), 1 WWR 288 (S.C.C.).

The Respondents through Mr. Lawson's testimony are attempting to re-write and supercede the original leases and have them placed within this Order. The Tribunal respects their efforts to resolve the issues as they understand them to be. The discussion of certain clauses and suggested alternatives is a healthy exercise.

**Unitization Agreement proviso**

The direction of a compulsory order is governed by the **Ontario Regulations 245/97, amended by O. Reg. 22/00** under clause 15. The Tribunal is satisfied the Applicant followed the general format in filing this application. Further the Tribunal considers the origin of the drafted unit operation agreement can be found in the CAPL[36] version of the document.

The Office of the Mining and Lands Commissioner has adopted a format for orders which takes direction from its predecessor the Ontario Energy Board in these matters. The leases with the landowners will be affixed respectively to each of their Compulsory Unitization Orders. This is considered by the Tribunal to be a precursor to the provisions set down under the Unit Operation Agreement.

Pursuant to subsection 15(4)(b) of the **Regulation** the tribunal establishes the unit boundaries within the Order. The tribunal accepts the boundary description as submitted in the application. No new evidence was presented that will alter the Unit boundaries from the description provided.

This Order effectively joins the interests of three (3) landowners with the working interests of Lagasco Inc. to allow for the continuation of the wells, exploration and production.

The Respondents opposed the unitization Order and offered an alternative pooling arrangement. The Applicant argued the unitization effort is the most efficient method for this aging pool. The Tribunal finds placing another step in the amalgamation of interests for the said lands efficient operations, given the Provincial policy and regulations, has no purpose. The alternate elements introduced by landowners are considered addressed in the Unit Operation Agreement. They expressed concerns with the wording of the unitization document. The Tribunal finds the agreement to be industry significant and considers it to be*; **Contemporonea Exposito Est Optima Et Fortissima In Lege***[37] [L.] *the current meaning is the best and most compelling influence in law.*

Regarding continuation the habendum clause of the Unit Operation Agreement will continue the spirit of the leases;

> AND WHEREAS for the purposes of protecting the Zone "C" Pool from unnecessary and wasteful drilling and depletion, and for the protection of their correlative rights therein, the parties hereto desire to amend the said Lease and to unite and combine that portion of the said lands...

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[36] Canadian Association of Petroleum Landsmen (CAPL)

[37] The Dictionary of Canadian Law, (Carswell, 1991)

The Respondents voiced their concerns with remuneration. They agreed the 12.5 percent royalty offered for the depleted field, is adequate, but less than other arrangements researched. The Tribunal finds the Unit Operation Agreement modernizes the way of doing business being both fair and modern. The royalty offered, while arguably less than the eighteen percent cited is still considered to have wide-spread acceptance in the Ontario region. Efficient operations, in the Tribunal's mind, also includes economically feasible operations and to increase royalties by approximately sixty percent, as the Respondent suggests, may prove to be burdensome and create the alternative worst result, no production. No definitive answer can be assigned the economic viability of the field. However, the Applicant has put forward a convincing argument that consolidating operations and coupling operations within a larger shell of operation makes the field viable. Alternatively, continuing with individual well production may not be commercially viable. Which would deprive the public of the use of the natural gas, as well as, the loss of income and jobs. for the operator.

The Tribunal finds that adding a general compliance clause to the Unit Operation Agreement is in order. A clause noting compliance with statues, regulations and the **Act** is usually found quite clearly in the lease agreements however, upon review of the agreements, it is clear in one lease and not so in another. The Tribunal considers it would be prudent to include the following clause in the Unit Operation Agreement;

> The parties to this agreement recognize that the terms of this Unit Operation Agreement may be modified or affected by statute, regulation, order, or directive of any applicable government or government agency.

The Respondents will find this clause particular to their plugging liability and assurance concerns. To order an absolute plugging guarantee, in all probability, is an impossibility whereas recognizing liability provides some degree of comfort. In any event the operating party (lessee) is deemed to know the regulations and standards they are licenced under by the Ministry and the **Act**. The rules are clear.

Within the alternative wording the Respondents suggested limits to surface and drilling rights. The Tribunal finds that the three paragraph reference flies in the face of Provincial regulations/standards and the process currently legislated for an oil and gas operator. Inclusion of these references is deemed not warranted.

The Mortgage Holders are named as Respondents to the Second Part. The Tribunal finds the Mortgage Holder is not bound by the Compulsory Order and no order is made upon them. Their position is immaterial to the unit operation agreement however they may elect to take up an interest position in the event of a debtors contract default. They are not deemed a party to these proceedings.

This application is made based on a unitization. The Tribunal finds where developed fields are expected to be small in volume it makes good sense to combine an area to make it economically viable for the operator. Faced with similar situations in the past the Tribunal takes the approach that small operations do contribute to the economy. Unitization of a field will eliminate the need to address the Commissioner again on this issue.

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The industry has created the unitization method which can resolve/correct past situations that are not viable in today's terms. This method does not extinguish past agreements, but addresses equality and the benefits found in a modern day document. The Tribunal is reluctant to order a lease relationship where one currently exists, whether it is on one piece of note paper in Chaucer's good English or speaks volumes in Webster's modern language. The industry views these contract documents as continuing and the Tribunal is convinced the unit operation agreement addresses the industry intentions.

The unitization of the lands, while agreed to generally, is questionable as to its appropriateness in this case and the alternative of "pooling" is suggested by the Respondents. In addition Counsel for the Respondents argued that unitization is not as effective for old field formations such as Zone with established infrastructures. He argued that Ballem, a notable reference used in this case, also agrees. The Tribunal follows Ballem's argument for unitizing new gas field exploration however, in this instance, the field as well as others in the Province of Ontario are both old and depleted. In this case the pools where founded in the early 1900's and perhaps should have been unitized then. The Tribunal finds to use Mr. Ballem statements for purposes of opposing an application for unitizing is without merit. The tribunal takes the approach that much of Ballem's written statements support the unitization of gas fields, something that is long over due the Zone fields

The Tribunal has taken its resolve in discussions favouring unitization from Ballem's book[38] at page 179;

> From an operational point of view it makes good engineering and economic sense to operate a field as an entity without regard to any artificial distinction, created by the ownership subdivisions.

and at page 185;

> ...Once a lease is included in a unit by the lessor executing the unit agreement, and all operations anywhere within the unit have the effect of continuing the lease in force.[39] Moreover, the entire lease and not just the unitized zone will continue. This is the only result that is consistent with the wording of the lease and it has also received judicial sanction in *Voyager Petroleum Ltd. v Vanguard Petroleum Ltd.*[40] It is not surprising that unitization has grown increasingly popular with each passing year. It has become almost the rule with respect to gas fields and is normally completed before production commences. The trend to unitize oil fields is steadily growing.
>
> It is impossible to say anything against the principle of unitization. It undoubtedly receives better operating procedures, enhances recovery, and implements good conservation practices, all at a reduced cost. It is not surprising, therefore, to find that unitization is encouraged by public conservation bodies. In the purely private area of contract between the lessor and lessee, different factors may come into play. Under current industry practice the lessor is expected to execute a unit agreement without any additional consideration, the benefits described above evidently being regarded as sufficient incentive.

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[38] Ibidem, (2nd Edition)

[39] Esso Resources Canada Limited v. Pacific Cassiar Ltd. (1984) 22 Alta. L.R. (2d) 175 (Alta. Q.B.).

[40] [1982]

The Tribunal finds the above statement is a specific and supporting reference to this application.

The Tribunal offers caution to those relying on that which has been ordered previously in regard to compulsory orders. Caution should be taken where; the **Act** and the **Regulations** have changed from one order date to another and new evidence is presented that may alter the scope and margins of a new Order. Also the changing practices of the Canadian Association of Petroleum Landsmen within the industry itself may call for quite another outlook in a future decision.

**Jurisdiction to Order - Trust ( plugging wells)**

The Tribunal ruled in preliminary proceedings for this hearing that arguments for and against the ordering of a special trust served a purpose for this application hearing.

The Respondents argued that the tribunal's Order should include a special trust provision to cover off well plugging liability. Their argument centered on assuring guarantees are mandated on the operator within the Order. They submitted that the tribunal has the authority to alter and include terms of a unit agreement under the **Act** [clause 8(2)] and the **Regulation** [ss.15].

The Applicant opposed the special trust and sighted various precedents in law which prohibit the tribunal from making the changes to the agreement and including them in the Order. Counsel for the Applicant noted the trust conditions of the drafted agreement address the trust as regulated (**O. Reg. 245/97, amended by O. Reg. 22/00**).

The Tribunal finds the Ministry has adopted requirements for a Trust of $70,000 per operator through due process and legislation. Comfort with the requirements of the **Regulations** can be found in Mr. Hewitt's testimony on operator trusts where, he states no trusts have been drawn upon for defaults on plugging orders. Further he stated the Applicant company has not defaulted for abandoned well plugging costs. The Tribunal finds the Ministry has legislated regulations for a trust which appears to be meeting current demands. The Respondents suggested wording changes for plugging assurances. The Tribunal finds the issue is dealt with in the **Regulations** under subsection 16.(1);

> Every operator of a well shall establish security,
>
> ...
>
> (b) in the form of a trust fund administered in accordance with the *Trustee Act* for the purpose of financial assurance that wells will be plugged and works completed in accordance with the Act and regulations and any order of the Board or the Commissioner. O. Reg. 245/97, s.16(1).

The Tribunal finds for this application that clause 16.(1) of the **Regulations** is adequate and no new evidence was presented that discounts it. The arguments for and against a special plugging trust where enlightening and most welcome. All concerns were heard. In hindsight the discussions did not weigh in the decision to Order.

## Costs

The Tribunal finds that there will be no costs payable by any party with regard to the processing of this application and the resulting Order. The Tribunal finds the arguments by Counsel for either party for the awarding of their costs were unconvincing.

Salient for this position is the reward approach by Counsel for the Respondents and the change of decision by Counsel for the Applicant. The Respondent's Counsel argued an award should be made based on the past failed negotiation efforts of the landowners. This argument the tribunal finds is not reasonable or significant enough for an award of costs. The Applicant's Counsel provided a change of mind request for payment of costs, adopting a superimposing approach. Neither party projected a genuine case for awarding costs, lacking docket and cost summary evidence to validate their claims.

## Conclusion

For the reasons herein stated, the application will be granted with the various modifications and additions to the Unit Operation Agreement as noted. Effectively the Zone "C" Pool is ordered which will include three tracts of land under Petroleum and Natural Gas Lease/Grant(s) and a Compulsory Order for those lessors to enter into a Unit Operation Agreement.

The Tribunal respects and appreciates the testimony of witnesses and the submissions of Counsel. The Tribunal notes the Compulsory Order is being made upon due consideration of all submissions, exhibits and testimony.

**Schedules:**

"A" Unit Boundaries - Legal Description

"B" Unitized Landowners and Allocation Schedule

"C" Unit Operation Agreement