File No. OG 004-08

Lorne F. G. Carter	)	Thursday, the 29th day
Deputy Mining and Lands Commissioner	)	of January, 2009.

THE OIL, GAS AND SALT RESOURCES ACT

IN THE MATTER OF

An application for Joining of interests, pooling order, under the **Oil, Gas and Salt Resources Act**, R.S.O.1990, c. P.12, as amended by 1994, c. 27, s. 131; 1996 c. 30, s. 56-70; 1998, c. 15, Schedule E, s. 24; 1999, c. 12, Schedule N, s. 5; 2000, c. 26, Schedule L, s. 8; 2001, c. 9,Schedule K, s. 4; 2002, c. 18, Schedule L, s. 6; 2006, c. 19, Schedule P, s. 4., c. 4, s.38, for an Order, by the Commissioner, pursuant to subsection 8(1) that, (a) the oil or gas interests within a spacing unit be joined for the purposes of drilling or operating an oil or gas well; (b) management of the drilling or operation be carried out by the persons or class of persons named or described in the order; and (c) the costs and benefits of the drilling or operation within the spacing unit be apportioned in the manner specified in order (the **"Order"**);

(Amended October 16, 2008)

AND IN THE MATTER OF

Any application pursuant to Ontario Regulation 245/97, amended to O. Reg. 75/04, at clause 9(3)(a) and (b) wherein; No person shall, drill a well in a spacing unit that has not been pooled; produce oil or gas from a spacing unit that has not been pooled and at subsections 14(3) and 14(4) whereby the application for the order to allow pooling within a spacing unit shall include specific information to the extent that it is applicable to the issues being determined (the "**Regulation**");

AND IN THE MATTER OF

All and singular those parcels, lots or tracts of land and premises, comprising of 50 acres more or less, geographically described as the North half of the South half of Lot 1, Concession 1, in the Geographic Township of Bayham, Municipality of Bayham, County of Elgin, Province of Ontario and further described on Schedule "A" attached hereto and forming part of this Order (the "Spacing Unit");

(Amended October16, 2008)

. . . 2

AND IN THE MATTER OF

All and singular those certain parcels, lots or tracts of land and premises, situate lying and being within the subject Spacing Unit, belonging to: Robert Thomas Carrel and Suzanne Lynn Carrel comprised of approximately 3.13 acres, Thomas Edward Carrel and Robert Thomas Carrel comprising of approximately 3.13 acres, and Robert Christian Pierce and Kimberley Helen Pierce comprising of approximately 43.74 acres, (Pooled Lands).

(Amended October 16, 2008)

BETWEEN:

ECHO ENERGY CANADA INC.

Applicant

- and -

NRG CORP.
[Respondent working interest party who has *not* entered into a Voluntary Pooling Agreement with the Applicant]

Respondents of the First Part

- and -

ROBERT THOMAS CARREL, and SUZANNE LYNN CARREL, THOMAS EDWARD CARREL and ROBERT THOMAS CARREL, ROBERT CHRISTIAN PIERCE and KIMBERLEY HELEN PIERCE
[such landowner(s) who have signed into Petroleum and Natural Gas Leases and Grants in favour of either the Applicant, Echo Energy Canada Inc. or NRG Corp.]

Respondents of the Second Part
(Amended October 16, 2008)

- and -

FARM CREDIT CORPORATION, SHADE OAK SWINE LTD. and ROYAL BANK OF CANADA
[Mortgagees in respect of the lands comprising of the Spacing Unit]

Respondents of the Third Part

. . . . 3

AND IN THE MATTER OF

Clause 14(3)(h) of the Ontario Regulation 245/97, amended to O. Reg. 75/04 providing that the relationship between the landowners, Respondents of the First Part, the Second Part and the Initial Unit Operator, the Applicant, be governed by a specific Pooling Agreement attached hereto and forming part of this Order under Schedule " B ";

(Amended October 16, 2008)

AND IN THE MATTER OF

Service of the Order shall include notice on all Landowners within both; the executed and ordered aforesaid Pooling Agreement in favour of the Lessee (initial unit operator) that the various habendum and pooling clauses each contained therein are being exercised by the Lessee;

(Amended October 16, 2008)

AND IN THE MATTER OF

In the alternative, an Application for an Order which joins the interests of the Respondents with the interests of the Applicant within the spacing unit pursuant to subsection 8(1)(a) (b) and (c) of the **Oil, Gas and Salt Resources Act**, R.S.O. 1990.c.P.12, as amended, on terms and conditions specified and filed with the Application and forming the Order herein.

(Amended October 16, 2008)

R E A S O N S

This matter was heard by the tribunal on Thursday, the 28th day of August, 2008, in the Duke of Connaught Room of the Hilton Hotel at 300 King Street, in London Ontario.

Appearances by:

Mr. Christopher A. Lewis, Counsel on behalf of the Applicant, Echo Energy Canada Inc. and Mr. Gary Conn for the company.

Mr. Anthony F. Steele, Counsel on behalf of the Respondent of the First Part, NRG Corp. and Mr. John Camara for the company.

No one appeared for or on behalf of the Respondents of the Second Part (landowners).

Preliminary/ Procedural Matters

Mr. Lewis, counsel for the Applicant, submitted that some agreement concerning the pooling agreement had been reached with only a few items outstanding for the tribunal's consideration. He noted that his submissions indicate that an argument regarding the jurisdiction of this tribunal under clause 8(1)(c) of the **Act** would be forthcoming upon the hearing of evidence.

. . . . 4

Mr. Steele, counsel for the Respondent, concurred that almost all matters in the Application had been resolved and only two issues for determination remained for the tribunal's order.

Mr. Lewis continued with several housekeeping matters/corrections to the content of the submissions.

Background

The Applicant and the Respondent of the First Part both have working interests in the subject (fifty acre) spacing unit by virtue of their respective Petroleum and Natural Gas Lease(s) and Grant(s) with area landowners, Respondents of the Second Part. The Applicant holds under lease approximately 87.5 percent of the said lands and the Respondent of the First Part holds the approximate balance of 12.5 percent.

The Ministry of Natural Resources issued a license to drill a well for the production of natural gas in February 2007. The Applicant positioned equipment and prepared to put Echo #59 well into production March 2008. They notified the Ministry of their intention and they were informed that the spacing unit requirements and a pooling agreement had not been completed and until they were in place, no production is allowed.

The Applicant notified the other working interest of the said land leases (NRG Corp.) in an effort to voluntarily put a pooling agreement in place and protect the correlative rights of the landowners. The Applicant submitted that they did not receive any workable responses from NRG Corp. over a three month period.

In July 2008 the Applicant filed an Application for a hearing in the matter and requested an Order supported by a pooling agreement. The Applicant made an application for an Order under the **Oil, Gas and Salt Resources Act, R.S.O. 1990, c. P.12,** as amended pursuant to sections 8(1)(a)(b) and (c) therein. The Appointment for Hearing was issued by the Office of the Mining and Lands Commissioner on July 9th, 2008.

The Respondent, through their counsel, responded to the Application in July 2008 and while they agreed to the pooling agreement drafted they felt the tribunal should rule on specific issues within the agreement surrounding transportation costs and the physical marketing of the natural gas produced.

In Addition, the counsel for the Applicant, within submissions, pointed out their displeasure that the situation had evolved and included their intent within the Application to seek a cost award.

The Applicant requested an appointment for hearing and this hearing then ensued.

Issues

1. Can the purpose of the **Oil, Gas and Salt Resources Act** be ascertained?
2. Is the Order justified under the circumstances?

. . . . 5

3. What is the purpose of the Pooling Agreement?
4. Does the Act provide for the input/changes by this tribunal in matters of the Pooling Agreement content?
5. Should the tribunal determine awards and assess costs in favour of the Applicant?

EVIDENCE

Mr. Gary Conn for the Applicant

Mr. Gary Conn representing the Applicant, Echo Energy Canada Inc. was sworn in and provided evidence through examination-in-chief by Mr. Christopher Lewis, Counsel for the Applicant.

Mr. Conn identified himself as the president of the company and noted that it has traded on the TSX since its inception in 1999. He relayed that the purpose of the company is to look for and obtain/capture natural gas for sale into the marketplace. He continued that, the business has drilled approximately sixty (60) wells, in the area within Bayham Township, Elgin County. He noted that he is also president of another resource company (Ontex Resources) which is also listed on the Toronto Stock Exchange. He noted that the Ministry of Natural Resources had issued a license to the company to drill well #59 in February 2007.

Mr. Conn conveyed that the Applicant completed the application to operate the well (Echo #59) with the Ministry of Natural Resources with the understanding that they had all the land and the spacing requirements covered. He noted that based on the area maps this specific region is primarily in 100 acre lots and they had proceeded to drill assuming there were no leased land issues. It was not until during drilling operations in March (2008) that they were informed by the Ministry that in order to drill Echo #59 and produce from it they would have to acquire leases to two small pieces of property in order to complete the required spacing unit. Mr. Conn noted that the strip of land in question is not an appreciable amount and upon physical inspection does not present itself as an extension of the developed existing lands. It is a small portion of the 50 acre unit.

Mr. Conn laid out their contact experience with NRG Corp., the other working interest holder of two small land leases. He noted that their attempts to contact NRG started immediately in March 2008. Mr. Conn noted that some seventy (70) telephone calls and letter attempts, by his firm and their land agent, Blackgold, were undertaken to no avail. Further on June 17th, 2008, through the lawyer (Mr. C. Lewis), an irrevocable letter was sent outlining pooling arrangements much the same as those in the application submitted for this hearing and demanding a response by June 30th, 2008.

Mr. Conn noted that he gave instructions to Mr. Lewis to proceed to a hearing once an inconclusive facsimile response was received on June 30th, 2008, from Mr. McCullough, former counsel for NRG Corp., [Exhibit #6] noting further delays with the pooling issue. Mr. Conn explained that the application before this tribunal commenced on July 9th, 2008.

. . . . 6

Mr. Conn indicated that an offer to pool or settle the matters was received from the new counsel for NRG, Mr. Anthony Steele, on August 26, 2008 [Exhibit #4] and within that facsimile; it was stated that the pooling of working interests was agreeable to NRG Corp. except for the issue of the transportation of the natural gas produced.

Mr. Conn referred to posted sketches pointed out that the location of the Echo #59 well and a previous well #47. He noted that NRG, after hearing of Echo's well forty-seven's (#47) success several years ago, drilled some twenty (20) wells in the vicinity. Once this was done a reduced pressure from the well was experienced. The well was totally surrounded by NRG wells and subject to production reductions. He explained that the area contains Silurian sandstone gas reserves which are usually small and subject to a decline in gas pressure as the area is drained through production. Excluding the Bayham area, Echo Energy has approximately 65, 000 acres under lease. The subject area is known as a good producer and some wells reach gas production levels of 1,000 cubic feet per day.

Mr. Conn explained that a large gathering system has been installed with a compressor and high pressure steel pipe lines costing approximately $5.8 million. The system will transport the natural gas north to Tillsonburg, Ontario where the Union Gas or Duke Energy mainline are located. Once integrated into that line, the gas will be used across Ontario and the North American markets.

Mr. Conn introduced the Jumping Pound Calculations [Exhibit #5] used by Echo Energy and noted that the internal cost of transporting 1 mcf of gas in Bayham costs approximately $3.76 per mcf. He outlined that within the costs for transportation is the compressor rental, the gathering system, the pipelines, high pressure system, maintenance, manpower, Union Gas transportation contract cost, and the total operating cost called the Jumping Pound 95 calculation. He projected that he could produce over one million cubic feet per day with the capability of 6.2 mcf per day.

Mr. Conn reflected that he had originally gone to Mr. McCullough for legal counsel in this case and was told by Mr. McCullough that he had a conflict and Mr. Lewis was suggested as a capable representation in these matters.

Mr. Conn affirmed that once Mr. Steele was counsel on the NRG side of the case that the correspondence started to flow which lead to the letter/proposal of August 26th, 2008.

Mr. Conn agreed that the transportation of gas from well #59 at $1.30 per mcf is a benefit in terms of cheaper costs and greater profit. He noted that several questions arise from the Respondents proposal such as; how the pipe line and product is to be monitored (metered), the added costs of hooking up and the compatibility of hook-ups in terms of gas pressure. Based on his knowledge NRG Corp. is primarily in the retail gas business and not in the higher pressure wholesale field such as Echo Energy. The NRG system of transportation proposed makes metering difficult as it will require another separate gas meter. Echo runs 365 days per year from their gas wells and NRG Corp. reportedly runs only in the winter months. He added that the law requires the gas to be metered and integrated and is subject to reading reports by BMP in Calgary, Alberta.

. . . . 7

Mr. Conn calculated that gas selling at $10 per mcf with a transportation cost at $2.61 per mcf calculates as a 26.1 percent cost and when compared to a transportation cost of $1.30 per mcf calculates as 13 percent and is a significant difference. However, he continued, that is just the differential in gas transportation costs and does not include the cost of manpower, the changes required weekly in calculating actual flows and the hook-up to another system with gas pressure concerns. Echo's natural gas lines are rated for 300 psi and NRG Corp. lines, it is understood are only 25 psi. This difference in pressure could cause regulator blowouts. The Echo system is engineered to produce for the wholesale market and with greater production volume the transportation price could be down to $3.00 from $3.76 per mcf.

Mr. Conn indicated that the Echo Energy will be the operator of the well and will determine how the gas is transported from the well head through Echo gas lines to connect to Union Gas lines and the wholesale market.

Mr. Conn noted that approximately 8.75 mcf (87.5 percent) of gas produced from each 10 mcf belongs to Echo Energy and the balance of 1.25 mcf (12.5 percent) per 10 mcf is NRG's share. He agreed that the current cost to transport to Dawn, Ontario is $3.78 per mcf which is greater than the costs of $2.61 per mcf that NRG will have to pay. He concluded that everyone's natural gas production (Echo & NRG) will be sold at Dawn Ont. Point of entry into the marketplace.

Mr. John Camara for the Respondent

Mr. Camara noted that he was part of the NRG. Corp. operation and because one of the main principals of NRG left the company, he was asked to help out drilling some wells. He explained that he was in charge of land positions and administration for NRG Corp. which includes land leasing. He outlined that he has been involved with high rise apartment construction for the past 38 years and currently works for the sister company to NRG Corp., known as Ayerswood. He also noted that another company in the group called NRG Limited operates as a gas utility and holds the area franchise around Aylmer including the Bayham Township. He noted that he has no actual title with NRG but, it is his responsibility to oversee the arranging for well drilling. He noted that he is familiar with this Application. He relayed that NRG, to his knowledge, is under the direct management of Mr. Mark Bristol, the controller for NRG. He noted that it is his belief that the letter of June 17th, 2008 (by Mr. Lewis) was received by Mr. Bristol.

Mr. Camara responded to queries by Mr. Lewis. He noted that he spends approximately three to four hours per day on NRG related issues such as; leases, geology and line maintenance. He expressed that the company has drilled four wells this year mostly in the spring. He noted that there has been no drilling activity in either June or August of 2008.

Mr. Camara explained that to his knowledge there had been some correspondence between NRG Corp. and Echo Energy Canada Inc. through Mr. Tim McCullough, the acting counsel for NRG, in June, 2008. He identified a letter from Mr. McCullough to Mr. Lewis,

. . . . 8

counsel for the Applicant, dated June 30th, 2008. Within that letter Mr. McCullough noted that he had a timing conflict and would not be in a position to deal with the issues/concerns until his return on July 17th, 2008.

Mr. Camara noted that Mr. Steele was retained to take over the file on behalf of NRG Corp. He noted various communications/correspondence between Mr. Steele and Mr. Lewis wherein NRG Corp. requested an analysis as to costs for production and the associate involvement with the well in order that their position could be determined.

Mr. Camara commented on the submission by Mr. Lewis [Exhibit #4] and noted that NRG indicated their willingness to participate in the well subject to their proposal regarding the transportation of the gas. He indicated that his company offered to transport the gas through their natural gas line system for $1.30 per mcf. He noted that NRG, to his knowledge, has the infrastructure in place to provide for the transportation of gas. He described the proposal's concept for a parallel gas line from their sites (wells) of approximately 1300/1800 metres which then connects to a four inch line for distribution. Mr. Camara felt that a lower cost at $1.30 per mcf for transportation compared to $2.61 per mcf would benefit both parties.

Mr. Camara reflected on his cost illustration [Exhibit #7] and noted that the transportation costs contained in the document are those currently used by NRG in conjunction with the companies noted therein. He identified that NRG uses a company called Green Tree to channel gas in the summertime. He noted that NRG is charged 50 cents per mcf by Green Tree plus 25 cents by Union Gas or 74 cents in total to move some of the gas to the Dawn Ont. market. This works out to 7 or 8 percent and at a rate of $2.00 per mcf it would work out to 23 percent for channeling the gas the way that the Applicant is proposing. The benefit of the lower costs over the higher cost of the Applicant presents cost differences.

Mr. Camara noted that the transportation of natural gas within the utility company, NRG Limited, is handled by Mr. Bristol. He expressed that it is his belief that NRG Limited sells gas directly to consumers within their franchise area. He noted that the gas is not compressed and that this could lead to input problems into the mainline at Dawn Ont.

Mr. Camara responded that he was not providing any cost breakdown of the NRG Corp.'s various components that establish their mcf charges ($1.30 per mcf). He expressed that he did not take any exception to the cost breakdown presented by the Applicant [Exhibit #5]. In addition he did not dispute the costs of Echo's pipeline reported as $6,284,000 in previous evidence. He summarized that his knowledge on natural gas transportation and its costs are limited. He indicated that he was not aware of the contact arrangements with Mr. George Chilian's company, Southern Ontario Natural Gas to transport his natural gas.

Mr. Camara noted that NRG Corp. would transport the natural gas approximately 1800 metres north of the well site and then flow natural gas into a four inch gas line owned by NRG Limited. He stated that it is his understanding that the gas does not need compression for use in this distribution system. The system distributes the gas at wellhead pressure to local con-

. . . . 9

sumers within their franchise. He confirmed that the $1.30 per mcf did not cost out as transportation to Dawn and the North American gas market. He agreed that the transportation of gas and the marketing of the gas by Echo Energy is different from the transportation and marketing proposed by NRG Corp.

Mr. Camara expressed his understanding that the larger working interest party (Echo) is the operator of the well and the marketing of the gas production captured is within their control. He restated his agreement that Echo Energy will be the operator of the well, the pooling and the spacing unit. Further he agreed that Echo's share of the production from well #59 for every 10,000 mcf is approximately 87.5 percent and NRG's share will be approximately 12.5 percent.

Mr. Camara noted that NRG Corp. has offices in Aylmer, Ontario at 39 Beech Street West along with NRG Limited the sister company and in London, Ontario at 1299 Oxford Street East where he is located. He explained that he was not aware of any of the 60 telephone calls since March of 2008 to NRG Corp. concerning this gas well matter and was not involved with this project at that time. He noted that he works for Ayerswood and NRG but was not contacted regarding the telephone calls. It is his understanding that a Mr. Paul Belfry would have filtered the telephone calls in these matters and may have sent a letter in response.

Mr. Camara indicated that prior to the July 8, 2008 Appointment for Hearing that he had seen Mr. Lewis' June 17th letter to Mr. M. Bristol. He agreed that the letter outlined the proposed pooling arrangements with a couple of options which included an overriding royalty in lieu of pooling and that the letter required a response by June 30, 2008, to negate a pooling application order. He explained that normally, such letters/correspondence are referred to others with a better understanding of the situation and this was the course of action taken. He indicated that Messrs. McCullough or Steele are usually retained by NRG Corp. in such matters and that a request for their legal counsel is made by Mr. Bristol. He explained that he was not aware of how Mr. McCullough and Mr. Bristol handled the letter of June 17th. He indicated his awareness of the July 8th application for pooling. He noted that Mr. Steele had been retained on July 24, 2008, to deal with the application.

Mr. Camara recalled that a July 28th letter was sent by Mr. Steele requesting specific information and copies of surveys. He noted that a response was received from Mr. Lewis on July 30th. Mr. Steele then sent a letter asking for a breakdown of costs which was provided by Mr. Lewis shortly thereafter. He provided that it is his belief that the August 19th letter from Mr. Steele requested further information on transportation charges and that Mr. Lewis responded the same day. He noted that he could not explain why a proposal to settle matters or proceed had been sent only two days prior to this hearing. He reflected that sometimes the situation has to be reviewed and the counsel of the superiors in the company sought out before reaching any decision. He indicated that Mr. Bristol was on vacation and was therefore unable to attend at this hearing.

Mr. Camara re-affirmed that the NRG Corp. proposal would guarantee transportation for all the natural gas that Well #59 produces at the $1.30 per mcf price.

. . . . 10

Arguments by Mr. C. Lewis, Counsel for the Applicant

Mr. Lewis submitted that it is not within the jurisdiction of the tribunal to determine the quantum of any type of expense within the pooling agreement. He noted that clause 14(4)(g)[1] specifies what is to be contained in a pooling order and the form of the agreement has to be mandated. He pointed out the similarity within clause 8(1)(c)[2] of the **Act**.

Mr. Lewis provided that under these sections of the **Act** and Regulations that the tribunal's authority and jurisdiction are limited to prescribing the form of the agreement and apportioning the costs and benefits in the pooling context as well as the percentages of production/compensation for each party entitlement. He reflected that on these issues there is no dispute. Echo Energy has a working interest of approximately 87.5 percent and NRG has a working interest of approximately 12.52 percent. He submitted that the powers of the tribunal, unlike the Superior Court, stem from the **Act** alone with no further interest or jurisdiction. He concluded that the CAPL portion of the pooling agreement put forward can not be altered by the tribunal in either content or recalculated charges. The pooling agreement allows for flexibility and the operator's right to determine what transportation costs will be.

Mr. Lewis offered that the transportation expenses could decrease from the current $3.78 per mcf charged to below $2.61 per mcf which will provide a better margin for the NRG share. He submitted that a change to $1.30 per mcf for transportation costs would not allow for the flexibility built into the pooling agreement as presented.

Mr. Lewis referred to the revised pooling agreement [Exhibit #3] and the operating procedures at clause 5 as follows;

> Clause 5: From and after the Effective date and save as may otherwise be provided herein, the Operating Procedure shall apply to all operations conducted in respect of the maintenance, exploration, operation and development of the Leases and the Spacing Unit with Echo being the Operator.

and noted that NRG Corp. has agreed to the content. He submitted further that within CAPL 1990, an industry standard, at page 14 clause 602 (a)(i)[3] and paraphrased that the operator has the authority to sell the NRG share of production and deduct processing and transportation expenses. He submitted further that within clause 221 (page 20) of the PASC accounting procedures that it states;

> Not withstanding anything to the contrary contained in this Article II, when operations in addition to the Joint Property are served, the Operator shall use an equitable allocation of the actual costs as the basis for charges to the Joint Account…

. . . . 11

[1] Section 14(4) of **Ontario Regulation 245/97**, as amended: (g) A copy of all agreements that will govern the relationship between the working interest owners with respect to operations, charges and credits;
[2] Section 8(1) of the **Oil, Gas and Salt Resources Act**, as amended: (c) the costs and benefits of the drilling or operation within the spacing unit be apportioned in the manner specified in the order. 2002, c.18,Sched. L, s.6(2).
[3] CANADIAN ASSOCIATION OF PETROLEUM LANDSMEN 1990, Operating Procedure 602 (a)(i)

the joint property does not include the transportation system beyond the well which is owned solely by Echo Energy Canada Inc. Echo, the Applicant, based on the evidence is more than equitable in allocating part of the actual costs for transportation for using the system. He concluded that the pooling agreement has language that permits the Applicant/operator to determine how and where the gas is marketed less transportation expenses.

Mr. Lewis added that the agreement is part of the order and detailing the minutiae is beyond the tribunal's jurisdiction. Further the working interest, NRG has agreed and admitted that the operator is Echo Energy who is able to market the natural gas where and how they like subject only to the joint operator's right to take the Natural Gas in-kind as noted in Article VI (CAPL 1990).

Mr. Lewis submitted that the proposal by NRG to market the gas through their NRG Limited system to area franchise consumers at a cost for transportation of $1.30 per mcf is similar to comparing apples to oranges when compared with the Applicant's marketing plan. The NRG Limited market is limited in the summer and benefits only a small area whereas Echo's distribution/marketing system will take it to the open markets through Dawn and sell the gas year round.

Mr. Lewis pointed out that Echo is incurring transportation costs of $3.78 per mcf to transport their own 87.5 percent share of the gas and giving a discounted cost to NRG of $2.61 per mcf for their 12.5 percent share is showing good faith and reasonableness. Echo's motive is clear, they intend to move the gas to Dawn and the greater marketplace rather than confine the gas production to serving a local market in the Aylmer region with its seasonal problems. Echo is agreeably the operator and the operator, according to the CAPL, decides where and how to market the natural gas. NRG's proposal is to market all the gas through their utility, a limited and seasonal market. There was no discussion on the part of NRG concerning natural gas wholesale prices because the gas under the NRG proposal can not wholesale the gas within their franchise area.

Mr. Lewis indicated that NRG's proposal would have the smaller interest party wagging the tail of the dog dictating what the wholesale price Echo will be paid for their own share of their production. NRG has the alternative option under CAPL to take their gas in-kind if the transportation cost is unacceptable. Under that option NRG will have to pay for the infrastructure to strip out the natural gas at their 12.5 percent level and pay out the royalties directly to the landowners. NRG has this flexibility option. However this alternate does not make sense in relation to the 12.5 percent share of a fairly small volume given the costs of putting the equipment in place. The August 26th, letter from Mr. Steele for NRG is somewhat disingenuous and it is obvious that they are trying to control the market and the sale of the natural gas while they are not the operator. He pointed out that the operator with their 87.5 percent interest should decide how and when to sell the natural gas. If NRG is opposed to the situation, with their 12.5 percent interest then they can pay for all necessary equipment to strip out their portion of the gas and pay royalties as the pooling agreement suggests.

. . . . 12

Mr. Lewis concluded that the tribunal does not have the jurisdiction to mandate the specific transportation costs. NRG, the Respondent, has agreed to the pooling agreement which is based on industry standards and confers upon the operator the right to sell the gas and market it how they please. He noted that NRG in their August 26th, letter tried to direct where the gas is being sold and how the gas is being sold. He explained that the agreement is not in dispute and should not be tampered with as there are other remedies available under any such contractual arrangements.

Arguments by Mr. Steele, Counsel for the Respondent

Mr. Steele briefly noted that he was presenting two issues for resolution through the Order. Firstly, of the two competing interests (Echo or NRG), who should be permitted to transport the natural gas production from Well #59. Secondly, the issue of awarding costs for the Applicant.

Mr. Steele submitted that the transportation costs proposed by NRG Corp. at $1.30 per mcf is lower than Echo's proposal and will benefit both parties.

Mr. Steele submitted that the Respondent, NRG Corp., in his August 26th letter [Exhibit #4] to Mr. Lewis specifically expressed their willingness to resolve these matters and enter into the pooling agreement provided the transportation costs could be agreed to at $1.30 per mcf with NRG providing the actual product transport.

Mr. Steele submitted that Mr. Lewis indicated in his arguments that NRG, "kind of", trapped themselves and had agreed to the Applicant being the operator and the marketer of the natural gas. However this not the case because in our letter of August 26th NRG specifically pointed out that they accepted the agreement with certain issues and indicated further that if the transportation costs component could not be resolved then they would seek a remedy through this hearing and the tribunal's order.

Mr. Steele provided that the evidence of Mr. Camara, NRG Corp., explained that NRG is in a position to transport all the gas produced and do it for a guaranteed transportation cost of $1.30 per mcf. He noted that no one has presented evidence that NRG's proposal to transport the natural gas production is not a fair process nor is the price that would be received for the gas less than that which otherwise could be received.

Mr. Steele submitted that Mr. Camara provided evidence [Exhibit #7] of costs they now pay to other operators and pointed out that it is much less than what the Applicant is proposing. In addition, he noted the evidence concerning gas pricing varies month to month. He provided the example that if the transportation costs based on $10 per mcf calculated the Echo transportation cost at $2.61 or 26.10 percent of the total sales and the total gross value of the natural gas production. In comparison NRG can effectively transport the same volume of gas for 13.0 percent ($1.30 per mcf) transportation costs. This is a significant reduction in costs which benefits both parties. Echo Energy will have the benefit of significantly less transportation costs and, when applied to their participating interest of 87.48 percent, the benefit is obvious.

. . . . 13

Mr. Steele submitted that the NRG proposal is reasonable and clearly better for both parties as the evidence states. This issue is very narrow and if an order selects NRG to transport the natural gas, they will be bound by the order.

Mr. Steele pointed out that they have shown further that under clause 8(1)(c) of the **Act** and the relevant sections of the **Regulations**[4] that this tribunal has the jurisdiction to make a determination regarding transportation costs. This tribunal is not limited, as counsel for the Applicant suggests. The tribunal can determine the operator and it makes sense for Echo to be the operator because of their 87.48 percent interest in the production. That is not in dispute. There has been no argument that NRG should be the operator. Both parties can benefit from this joint venture with NRG transporting the gas at a guaranteed price.

Mr. Steele submitted that the tribunal's mandate is to make determinations as stated in the **Act** and the Regulations and include them in the order. Mr. Steele commented on the argument of Counsel for the Applicant and his suggestion that the tribunal has no jurisdiction to determine the issue of transportation costs. He reflected that it leaves uncertainty as to whether the tribunal has anything to determine. Certainly there is nothing that says the tribunal has to impose all of the provisions of the CAPL or PASC accounting procedures. He pointed out that NRG does not have a problem with these industry standards and wants only one amendment with respect to the issue of transportation costs referenced to the CAPL and PASC portion appendices of the Pooling Agreement. NRG has a better transportation cost option for both parties and the tribunal has the jurisdiction to rule within the relevant statutes.

Mr. Lewis Argument For Costs

Mr. Lewis submitted that NRG was put on notice that Echo would be seeking the application for pooling and an award for costs. NRG should not be surprised by the request. The Applicant is dealing with a well that cost approximately $100,000 to drill and there has been a significant amount of work put into this Application and the Pooling Agreement. It meets the material requirements under the **Oil, Gas and Salt Resources Act** and the Regulations. The degree of complexity is high given the importance of the issues to Echo Energy. Echo is of the opinion that they have a well that is being potentially drained and their rights to capture the gas is being compromised.

Mr. Lewis referred to his assembled book of authorities and quoted sections 126 and 127 of the **Mining Act** for the record;

> Section 126
> The Commissioner may in his or her discretion award costs to any party, and may direct that such costs be assessed by an assessment officer or may order that a lump sum be paid in lieu of assessed costs.
>
> Section 127
> The costs and disbursements payable upon proceedings before the Commissioner shall be according to the tariff of the Superior Court of Justice.

. . . . 14

[4] **ONTARIO REGULATION 245/97, Amended to O. Reg. 75/04 – POOLING ORDERS, subsection 14.**

Mr. Lewis submitted that it is no surprise that a substantial indemnity for costs against NRG would be forthcoming if they refused to sign the Pooling Agreement. The Applicant should be entitled to substantial indemnity costs given that the Respondent has agreed to the form of Pooling Agreement except for the transportation costs issue. The tribunal's decision to award costs is within their jurisdiction similar to that of the Superior Court as the **Act** alludes to. Costs follow the event.

Mr. Lewis referred to Rules of Civil Procedure, 57.01 and 58.05.[5] He noted that these are the factors that the tribunal has to also consider in awarding costs.

Mr. Lewis argued that Echo would like to get their share of the natural gas produced except there is a legal barrier to bringing the well into production. They can not get a Pooling Agreement with NRG Corp. voluntarily. The evidence indicates that they made some sixty telephone calls and a written letter before commencing this Application and bringing it to a Hearing. Under the Rules at subsection (e)[6] the unnecessary conduct of any party to effect the duration of a proceeding is cause for a cost award.

Mr. Lewis noted that requests for information came once Mr. Steele was retained as counsel for NRG. He questioned why these queries for information by NRG Corp. were not forthcoming by someone at NRG in response to the previous sixty telephone calls starting in March 2008. These matters should have been taken seriously by NRG Corp. at that time. He submitted that perhaps NRG Corp. does not want the Echo well #59 brought on stream because they are producing in and around the same area of Bayham, Ontario.

Mr. Lewis suggested that NRG Corp. was not prepared to negotiate until the Application was brought forward. There is no evidence whatsoever of any negotiable response prior to Mr. McCullough's letter of June 30, 2008,which was in response to our letter of June 26, 2008 being the irrevocable date for a response. Then after the litigation commenced the information gathering and discussions started. This is not the way business should be done, NRG's conduct is reprehensible and it necessitated these proceedings. Issues should be resolved in good faith not forced through the bringing of a proceeding and giving an offer at the final hour, two days before the proceedings are scheduled to commence. The Respondent, NRG Corp., should have responded, requesting information and working in good faith on an agreement prior to the commencement of these proceedings. He referred to the Rules at subsection (g)[7] that deal with any party's denial or refusal to admit information which is subject to sanctions.

Mr. Lewis pointed out that the Respondent has admitted in evidence that they agreed with the Pooling Agreement and that they held back the transportation costs issue until the last minute.

Mr. Lewis provided that within the context of the **Ontario Superior Court of Justice** when the parties are sophisticated companies involved in such business, that costs follow the event. 15

[5] **Courts of Justice Act**, Tariff A – Lawyer's fees and Disbursements Allowable
[6] (e): "The conduct of any party that tended to shorten or to lengthen unnecessarily the duration of the proceeding;"
[7] (g): "A party's denial of or refusal to admit anything that should have been admitted;"

Mr. Lewis submitted that it is not the usual practice where there is a Pooling Application before this tribunal to award costs given that those past applications exclusively involved landowners. He reflected further that the landowners are not sophisticated in these matters and their bargaining powers are diminished without corporate coffers to draw on and utility companies standing behind them. The landowners rights have to be respected. In this instance there is a publically traded company with a sister company operating as a natural gas utility. These are sophisticated players. If they stonewall or do not respond to reasonable offers, costs should follow as an incentive and a message to the industry to deal in good faith to avoid going to a hearing. If the issues were different and came down to the wording of the documents or who was going to be the operator or some other issue, then those issues have to be aired. Proceeding with this hearing on the issue of transportation expenses should be cause for a cost sanction.

Mr. Lewis urged the tribunal to exercise discretion based on the evidence and the submissions and award costs to Echo Energy.

Mr. Lewis submitted his docket of accounts which included fully paid costs to July 11, 2008 ($8,081.06) and a work-in-progress report from July 15 to August 26, 2008 ($5,773.51). The total for these two accounts plus another estimated $2,968 for hearing preparation will be $16,822.57.

Mr. Lewis submitted that Echo Energy, the Applicant, is seeking payment of the reported costs from NRG Corp. on a full indemnity basis within 30 days of the date of the Order failing which there will be a charge on NRG's share of the production like the reimbursement amount referred to on Page 6 of the Pooling Agreement [Schedule "B"] bearing interest at the **Court of Justice** rate of 6 percent per annum from the date of the Order. Mr. Lewis reviewed the tariff structure and noted that the Application states at clause 24:

> Echo seeks as part of the Order, an Order requiring NRG to pay Echo's costs of the Application on a substantial indemnity basis if NRG does not execute the proposed Pooling Agreement attached hereto and marked as Exhibit "7".

Mr. Lewis submitted that while Mr. Steele, upon being retained, did in fact request information and there was an exchange of information, those requests should not have come through counsel in the face of an application. There were numerous telephone calls between March and the June 17th, letter and there is no hard evidence of any response. The Respondent alluded to a letter of sorts but it was never produced and the author of that letter was not present at the hearing. The alleged letter/response has to be disregarded. The Respondent ignored the Applicant in their attempts to negotiate in good faith. Mr. Lewis further submitted that NRG Corp. has Echo Energy over a barrel and is sucking the natural gas out from around their well #59 location. The request for information such as; cost details, a pro forma pooling agreement and transportation charges, should have been made prior to retaining counsel.

Mr. Lewis restated that his June 17, 2008 letter was very detailed and laid out chapter and verse, that NRG had until the end of June 2008 to respond/commence negotiations

underway. A response was not provided until June 26, 2008 with no instructions to proceed. The Applicant is of the opinion that he waited three and one-half months and then experienced further stall tactics.

Mr. Lewis stated that the **Mining Act** gives the tribunal the authority to make an order for costs. The Applicant and the First Respondent are working interest participants and the situation is different from past applications before this tribunal.

Mr. Lewis suggested that while past orders did not include awards for costs, surrounding issues related to landowners who often do not know or do not show up at the hearing. However, this situation is quite different as it involves two working interest parties, two companies who are players of/in the industry. The practices of the **Superior Court** in awarding costs should be followed. The party who has their application affirmed by the order should be compensated even if it takes litigation to arrive at that point. An award of costs will send a message to the oil industry. It will be good for people operating and trying to bring a well into production through good faith negotiations and working with fellow working interests, both of which in this case are sophisticated industry players. The legislation limits the Applicant's course of action for a remedy from this tribunal and there should not be another consideration for costs different from the Court.

In closing, Mr. Lewis requested that an Order be issued in a timely fashion based on the mutual agreement that Echo Energy will be the operator with the tribunal's reasons to follow in due course.

Mr. Steele Argument Concerning Costs

Mr. Steele submitted that in these pooling applications awards for costs are rare. There is no doubt that this tribunal has the discretion and authority to award costs as set out in the **Mining Act**.

Mr. Steele defended the Respondent's actions and noted that the June 17th letter was responded to by counsel. Mr. McCullough sent a letter of explanation on June 26, 2008. He noted that Mr. McCullough in his letter explained that he was retained by NRG Corp. as counsel and was prepared to deal with matters upon return from his vacation.

Mr. Steele explained that on July 8, 2008, counsel for the Applicant, even after receiving Mr. McCullough's letter, aggressively launched the application for a hearing. Mr. Lewis did not respond to Mr. McCullough's letter. NRG Corp., in good faith, immediately retained other counsel (Mr. Steele) and an exchange of correspondence with Mr. Lewis ensued. NRG Corp. needed information, it was asked for and Mr. Lewis, in due course, responded to the queries. NRG Corp. undertook a process to consider the information, costs and several alternatives before responding. The Respondent, NRG Corp., considered the situation and the options open to them and chose the best suited course of action. This hearing need not have proceeded if the Applicant had agreed to the NRG Corp. proposal for transportation costs.

. . . . 17

Mr. Steele submitted that if an award for costs is granted by this tribunal the message that it sends is; if you go to the Office of the Mining and Lands Commissioner to solve an outstanding issue after doing your best to resolve/negotiate a mutual agreement you will be dead in the water and you will be penalized, $16,822.57 as in this case.

Mr. Steele explained that whether here before the tribunal or in the **Superior Court of Justice** this is not a case for awarding costs. This was a legitimate application and not frivolous or vexatious. The Respondent has presented a proposal and provided evidence that supports the requested changes. NRG Corp.'s conduct throughout has not been reprehensible in anyway nor should they be sanctioned by the tribunal.

Mr. Steele submitted that evidence by the Applicant noted a number of telephone calls were not returned, but the real action started when Mr. Lewis was retained and sent out the June 17th, 2008 letter. The situation has proceeded normally thereafter. There is no evidence of gamesmanship, nonsense, pranksmanship nor was any bogus positions taken. NRG Corp. has dealt with the Application in good faith and has presented the issues to the tribunal for a mandated decision. The legislation put the provisions into the **Act** so that working interests that have issues and whose interests are joined by the Ministry of Natural Resources spacing unit regulations can be joined by law. Where these situations can not be resolved through voluntary negotiations the legislation has provided for a hearing mechanism to reach a resolution.

Mr. Steele respectfully submitted that the Respondent, NRG Corp., is not seeking costs and equally sees this case as one which does not call for a cost award. There has been nothing in these proceedings that is out of the ordinary. The past practice of the Office of the Mining and Lands Commissioner is normally not to award costs in these applications and this past practice should prevail. The tribunal has jurisdiction to recognize the benefits for both parties, with lower transportation costs. The NRG Corp. proposal is such a benefit and the company is prepared to offer and guarantee the transportation costs as provided for in submissions and given in evidence.

F I N D I N G S

Purpose of the Act

The **Oil, Gas and Salt Resources Act** does not contain a statement of purpose. However, upon examination of several Statute and Regulation references, a determination of its purpose can be made. Contained in the "Interpretation" section of the **Mining Act**[8] there is a definition of substance which includes oil, gas and salt resources,

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

. . . . 18

[8] **Mining Act**, R.S.O. 1990, CHAPTER M.14. Amended by: 1994, c. 27, ss. 130, 134; 1996,c. 1, Sched. O; 1996, c. 30, s. 71; 1997, c. 19, s. 36; 1997, c. 38, s. 1; 1997, c. 40; 1998, c. 18, Sched. I, s. 40; 1999, c. 12, Sched.. O, ss. 1-58; 2000, c. 26, Sched. L, s. 6; 2000, c. 26, Sched. M, ss. 1-17; 2001, c. 9, Sched. L; 2002, c. 17, Sched. F, Table; 2002, c. 18, Sched. M, ss. 1-9; 2006, c. 12, s. 63.

and further the **Mining Act** defines its purpose at section **2. ;**

> **Purpose**
> **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. 1996, c. 1, Sched. O, s. 2.

Based on these sources "*mineral resources"* are clearly defined for the our purposes herein as *"natural gas, petroleum and salt"*.

Further, it is possible to infer the purpose of the **Oil, Gas and Salt Resources Act** from Ontario Regulation 245/97, amended to O. Reg. 75/04, entitled "EXPLORATION, DRILLING AND PRODUCTION". The Regulation within its "DEFINITIONS" at clause 1. makes countless references to "oil, gas, drilling, production, well, and exploration*"* which leads the reader to a clear interpretation of the **Act's** objectives. The most compelling reference can be found under "pooling";

> "Pooling" means the joining or combining of all the various *oil and gas interests* within a spacing unit for the purpose of *drilling* and subsequently *producing from a well*;

The first part of the statement is clearly focused on "oil and gas interests" and the latter half certainly implies "drilling" and "producing from a well."

Further the provisions of 8(1) (a) and (b)[9] of the **Act** and the Regulation under subsections 14(1) and (2)[10], clearly define the development of oil and gas pooled resources.

The tribunal finds that the intent of the **Act** is focused on oil and gas exploration and production and that the Regulations focus on the conservation and management of such resources. This tribunal finds direction from the various Statute statements which form the foundation for the purpose of the **Oil, Gas and Salt Resources Act.**

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 legisla-

. . . . 19

---

[9] **Oil, Gas and Salt Resources Act. R.S.O. 1990, c. P.12,** as amended;
Joining of Interests, pooling order
8.(1) The Commissioner may order that,
(a) the oil or gas interests within a spacing unit be joined for the purpose of drilling or operating an oil or gas well;
(b) management of the drilling or operation be carried out by the person, persons or class of persons named or described in the order;

[10] **ONTARIO REGULATION 245/97, *Amended to O. Reg. 75/04***;
POOLING ORDERS
14. (1) In this section and in section 15,
"tract" means an area of land, within an existing or proposed spacing unit or unit area, of which the ownership of the oil and gas rights is distinct from any other ownership of oil and gas rights within the spacing unit or unit area.
(2) A person having an oil or gas interest in a spacing unit may apply to the Commissioner for an order to pool the oil and gas interests within the spacing unit.

tion can be ascertained through a consideration of the consequences of there being no exploration. Specifically, if the exploration and production for hydrocarbons from under these lands was to go untouched, the economic benefits to operators, employees, royalty interests and the overall economy would never be seen. While the foregoing discussion is by no means conclusive, it is noted by the tribunal that the purpose of the **Act** is in evidence and remains consistent with the **Mining Act** interpretations.

Whether the Order is justified under the circumstances?

The tribunal finds that the application for an Order is justified. The purpose of the Legislation is to protect everyone's rights and interests and to establish criterion for procedure and process. At issue in this Application is the need to complete a spacing unit in the pattern set-down by the Ministry of Natural Resources before the production of natural gas can proceed. Alternatively, the subject well can not produce and has to be shut-in.

The protection of rights includes; the ***rule of capture*** afforded the working interest parties, Echo Energy Canada Inc. (Applicant) and NRG Corp. (Respondent of the First Part), as well as, the ***correlative rights*** of the landowners (Respondents of the Second Part).

The tribunal finds that the hydrocarbon substance is owned by its captors. Oil and/or gas are wandering liquids and gases and unlike base metal minerals their movement is likely to occur and will concentrate in various places over time. This flowing tendency creates an uncertainty for establishing the limits and size of a pool based on current geological science. In this case, Echo Energy Canada Inc. has been licensed by the Ministry to drill and produce from a well they consider to be viable.

Ontario recognizes the "rule of capture" which is explained through reading Ballem[11], an authority on the subject. At page 92 he explains;

> The "rule of capture", succinctly phrased by Hardwicke[12] is, "the 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[13], 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.

. . . . 20

[11] Ballem, John Bishop, THE OIL AND GAS LEASE IN CANADA, 3 rd. Ed., (Toronto: University of Toronto Press, 1999)
[12] Hardwicke E., The Rule Of Capture And Its Implications As Applied to Oil And Gas, 13 Texas Law Review, 391, 393 (1935)
[13] [1953] 2 D.L.R. 65, (1952-53) 7 W.W.R. (N.S.) 546, 550 (J.C.P.C.)

Another explanation as to the *rule of capture* is found in the case *Kelley v. Ohio Oil Co*[14] :

> 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.

Echo Energy Canada Inc. has been identified as the Initial Unit Operator for this spacing unit and the primary captor of the natural gas produced from Well #59.

Salient to the rule of capture is the balancing effect of the correlative rights of the landowners. The benefits to landowners contracted under a Petroleum and Natural Gas Lease and Grant is paramount to any Order. The tribunal finds that the protection of correlative rights benefit two parties; those who have executed a lease agreement and those who have not. The protection is extended to all parties in the entire spacing unit area. Those in executed agreements are protected and awarded rentals and royalties for their lands under lease and share agreements according to the value of the produced hydrocarbon resources. The landowners are protected against having the resources underlying their lands siphoned-off without compensation. This protection is afforded through the spacing unit requirements found within Ontario Regulation 245/97, amended by O. Reg. 75/04. The tribunal is aware of concerns about the correlative rights of landowners (Respondents of the Second Part) in rendering a decision. The tribunal finds that in this Application, one hundred percent of the landowners (Lessors) are party to executed agreements. Further, the tribunal finds that the protection of their interests upon entering into a pooling agreement and the resulting compensation makes sense.

These landowners are party to these proceedings and did not choose to address the hearing or provide submissions of their understandings and issues and their position can only be speculated on by this tribunal. There are three landowner parties that will be subject to a compulsory order joining their interests with the operator.

The tribunal notes that the Office of the Mining and Lands Commissioner has provided several publications explaining the terminology of the oil and gas industry and that an explanation on the matter of Correlative Rights[15] is available;

. . . . 21

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

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

> The Correlative Rights 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 deal with the respect for correlative rights of landowners through spacing unit designations, reasonable set-back requirements and compensation methods. The tribunal finds that the interested parties' correlative rights have been addressed and accounted for in this pooling application.

The Petroleum and Natural Gas Lease and Grant protect the lessee's rights and powers over the said lands. It also recognizes and provides for economic compensation in the event of the production of oil and/or natural gas from under the said lands and it saves the Lessor from harm and damages related to the working operations. The agreement is considered to be greater than a real estate lease, identified as a profit a` prendre and the most commonly quoted judicial definition is that of Lord Cairns in *Gowan v. Christie*[16]*;*

> Not in reality a lease at all in the same sense in which we speak of an agricultural lease… What we call a mineral lease is really when properly considered a sale out and out of a portion of land. It is liberty given to a particular individual for a specific length of time to go into and under the land and get certain things there if he can find them and take them away just as if he had bought so much of the soil.

The oil and gas lease is heavily weighted in favour of the lessee and it is not surprising that lessors consider it to be an unconscionable transaction. Court[17] decisions in the past have struck down notions on the basis that lessors have to be established as subservient to an over-powering lessee and subject to duly onerous terms. This is most often the case in the industry where standards of royalty are established and paid to lessors with little or no effort on their part.

The tribunal relies on the submissions of the Applicant for adoption within the Order. The tribunal finds that the executed leases do not present any onerous terms or conditions that are foreign to the industry. Nonetheless a challenge to any one of the documents is certainly possible, but not within the authority of this tribunal to adjudicate. It is the tribunal's opinion that the executed lease documents are consistent with those executed leases herein and those currently used in the industry. All petroleum and gas leases have to contain core elements. Based on the writings of a learned scholar, Ballem[18], in these matters pertaining to the "Oil and Gas Lease in Canada", the following is reproduced for our reference;

. . . . 22

[16] [1873] L.R. 2 Sc. & Div. 273 at page 284.
[17] *Crommie v. California Standard Company,* [1962], 38 W.W.R. (nr) 447 (alta. S.C., T.D.)
[18] Ibidem

> There are as many definitions of contract as there are text writers. All, however, agree that a valid contract must have the following elements: (a) an intention to be bound – the parties must intend that their obligations each to the other are enforceable and that any failure to perform will involve legal consequences – there must be a binding offer, properly accepted; (b) a consideration or price to be paid for the promises or undertakings; (c) an understanding between the parties as to the subject matter of the contract[19].

The tribunal is compelled to continue to review the Petroleum and Natural Gas Lease(s) and Grant(s) submitted with each application for an Order. Differences do exist in the industry regarding the petroleum and natural gas lease and grant as do the various lease agreements involved in this spacing unit. The tribunal does not prefer one over the other. The oil industry has addressed this subject out of necessity and past legal challenges and has agreed in principle to ground rules for the preparation of various clauses and phrases for such leases. This application joins the landowners (Lessors) through the submitted versions of the Petroleum and Natural Gas Lease and Grant with the working interest operator (Lessee).

The Regulations[20] leading to the establishment of a Spacing Unit call for a ***pooling agreement*** which, in effect, is an extension of the various lease agreements with the landowners. The relationship continues based on the lease habendum and subsequent pooling/unitization clauses. Within each lease provided in submissions is a clause providing the agent or lessee with the option to pool. The lease agreement [Schedule B - A. Part II] between Robert C. Pierce and Kimberley H. Pierce (Lessors) and Echo Energy Canada Inc. (Lessee) at clause 3. states;

> 3. COMBINING PROPERTIES: The lessee may combine (pool) the said leased lands with any adjoining property or properties ("Combined Properties") to attain optimum well spacing, and the Royalty from any well or wells on properties so combined shall be apportioned to the respective land owners ("Combined Land Owners") according to the proportion of productive acreage contributed in the discretion of the Lessee.

The lease agreement, [Schedule B – A. Part I] between Robert T. Carrel and Suzanne L. Carrel (Lessors) and NRG Corp. (Lessee) at clause 11. states:

> 11. Pooling:
> The Lessee is hereby given the right and power at any time and from time to time to pool or combine the said lands, or any portion thereof, or any zone or formation underlying the said lands or any portion thereof, with any other lands or any zone or formation underlying the same, but so that the lands so pooled and combined (hereinafter referred to as a "unit") shall not exceed One (1) spacing unit as herein defined. In the event of such pooling or combining, the Lessor shall receive on production of the leased substances from the unit, in lieu of royalties herein specified, only such portion of such royalties as the surface area of that portion of the said lands placed in the unit bears to the total surface area of all the land in the unit. Drilling operations on, or production of the leased substances from, or the presence of a shut-in or suspended well on, any land

. . . . 23

[19] See Guest, ed., Chitty on Contracts, 27 ed., vol. 1 (London – Sweet & Maxwell, 1994)
[20] Ibidiem

> included in the unit shall have the same effect in continuing this Lease in full force and effect as to the whole said lands, as if such drilling operations or production of the leased substances were upon or from the said lands, or some portion thereof, or as if such shut-in or suspended well were located on the said lands, or some portion thereof.

The lease agreement, [Schedule B – A. Part I] between Thomas E. Carrel and Robert T. Carrel (Lessors) and NRG Corp. (Lessee) at clause 11. states:

> 11. Pooling:
> The Lessee is hereby given the right and power at any time and from time to time to pool or combine the said lands, or any portion thereof, or any zone or formation underlying the said lands or any portion thereof, with any other lands or any zone or formation underlying the same, but so that the lands so pooled and combined (hereinafter referred to as a "unit") shall not exceed One (1) spacing unit as herein defined. In the event of such pooling or combining, the Lessor shall receive on production of the leased substances from the unit, in lieu of royalties herein specified, only such portion of such royalties as the surface area of that portion of the said lands placed in the unit bears to the total surface area of all the land in the unit. Drilling operations on, or production of the leased substances from, or the presence of a shut-in or suspended well on, any land included in the unit shall have the same effect in continuing this Lease in full force and effect as to the whole said lands, as if such drilling operations or production of the leased substances were upon or from the said lands, or some portion thereof, or as if such shut-in or suspended well were located on the said lands, or some portion thereof.

The landowners/lessors interests will carry through to the Pooling Agreement and upon a stoppage in production, the lease will again provide the relationship of the lessor and lessee going forward. One landowner party comprises 87.48 percent or 43.74 acres of the spacing unit (50 acres) while the other two landowners account for the 12.52 percent balance or 3.13 acres each.

These leases have a working party (Lessee) or operator. In this instance there are two **working interests** each having landowners under a lease agreement. Together and separately the two working interests are the developers for the spacing unit and are compelled to pool and provide for the Lessors accordingly.

The **Act** states at clause 8(1)(a) that the tribunal shall combine the various interests for the purposes of producing from a well.

One working interest in this instance has chosen to put a well into production. Accordingly, Echo Energy with the majority of the lands under lease, applied for a license to drill and was awarded the opportunity in February, 2007, by the Ministry. This reduced the options of the second working interest party, NRG Corp., in that they either have to enter an agreement to share the development costs of the well and become a working party or, merely act as an agent for the landowner and receive a 12.52 percent net profit. The Respondent, NRG Corp., has chosen the latter with good reason.

. . . . 24

In the Order, the tribunal leaves either option open to the Respondent NRG Corp. as a working interest and appoints Echo Energy Canada Inc. as the Initial Unit Operator, as per clause 8(1)(b) of the **Act,** based on their desire or intention to create the well and their substantial interest in land leases.

At issue in this hearing is the ***Pooling Agreement*** and its content. The Regulations call for an Order which it has at its core a written Pooling Agreement[21]. Subsection 14.(4) provides the content for such a Pooling order. Clause 14.(4)(g) states that the tribunal must include a copy of all agreements in its order that will govern the relationship between the working interest owners with respect to operations, charges and credits.

Assuming the Applicant is recognized through an order as the unit operator, they are charged with the simultaneous task of providing a pooling agreement based on industry standards. In this application and in anticipation of an affirmative order, the pooling agreement was submitted. The initial unit operator, in-waiting, produced a pooling agreement with the appropriate clauses born out of industry/CAPL policy.

Mr. Steele, Counsel for the Respondent, argued that the pooling agreement was quite acceptable to NRG Corp. except for changes in the price to be charged working interests for natural gas transportation costs, as well as offering an alternate method for marketing the gas captured/produced. The change proposal placed the cost at $1.30 per mcf and flowed the gas into the control of NRG Corp. for marketing. It was Mr. Steele's position that the tribunal pursuant to clause 8(1)(c)[22], could alter/change the particulars within a submitted pooling agreement.

The language in the **Act** may have served to confuse the Respondent of the First Part and it is their understanding that the tribunal has powers beyond the scope of the **Act**. They introduced what they felt was a viable alternative for transportation costs and marketing by the Applicant. They considered that the pooling agreement changes would be in the best interests of all parties.

The tribunal will allow some latitude to the Respondent and their counsel that a "benefit", as stated in clause 8(1)(c) of the **Act,** could well be transportation costs. However they agreed to pooling which is parallel to the pooling order and the appointment of the initial unit operator. Once those two decisions have been made, the tribunal has little else to decide upon or determine other than the service of notice and registration. The transportation costs, as stated in the pooling agreement, appear to be neither excessive nor wrong in this situation.

The unit operator/captor has the exclusive right to cost and market captured natural gas which is provided for within the written pooling agreement and the appended CAPL policy. The tribunal finds that it should not undo industry contracts which can be struck between

. . . . 25

[21] Ontario Regulations 245/97, amended as O. Reg. 75/04; POOLING ORDERS 14.(3)
[22] Oil, Gas and Salt Resources Act, 1990;
Section 8(1)(c); the costs and benefits of the drilling or operation within the spacing unit be apportioned in the manner specified in the order…

working interest parties through reasonable voluntary methods. In any event, the correlative rights of the landowners are paramount in hearings before this tribunal and the October order was determined with this in mind.

Both parties are compelled to pool either voluntarily or by order. Each party holds a 100 percent interest in said lands by virtue of the pooling clauses. The percentage of holdings as working interest is immaterial for pooling purposes as each is a 100 percent party to of the requirement (spacing unit). Once the captor was awakened and the necessary steps were taken to get the well into production it became increasingly clear what must happen by way of regulation and consent for Echo Energy. NRG Corp. had the same opportunity to acquire a license. They had the same opportunity to capture the natural gas.

Clause 14(4)(g) of Ontario Regulation 75/04 calls for a pooling agreement that is to be used with respect to landowners and working interests alike. The Regulation is quite specific as to what is required and does not make reference to variations or approving the agreement. There is no request of the tribunal to alter its contents. The leases have language which agrees to pooling through the various clauses so no order has to be sought concerning landowners not yet under lease, only a follow through with a pooling order.

The Applicant and the Respondent could have cooperatively reached the same conclusion as the tribunal did in its Order. The Respondent's position regarding the application leaves the tribunal to speculate as to their possible objection or knowledge level as a working interest. Alternatively, there was no written working interest agreement in place in advance of even the first telephone call by the Applicant or at the time the drilling license was applied for by Echo Energy, which does not lay out any particular performance requirement by either party.

The legislation has been designed to protect the rights of landowners (correlative rights) while allowing the industry to cooperatively advance under strict regulations (spacing unit).

Award for Costs

The tribunal received submissions and heard arguments from Counsel for the Applicant for an award for costs given the circumstances leading up to and causing this hearing. Counsel for the Applicant argued that the work to prepare, submit and present evidence was complex and would not have been necessary if pooling had been accepted voluntarily.

Counsel for the Respondent (NRG Corp.) argued that awards of costs in similar pooling applications were rare. Further he noted that the hearing need not have commenced if the NRG Corp. proposal for transportation methods and cost amendments to the pooling agreement had been accepted by Echo Energy. He submitted that there was no evidence of gamesmanship or frivolous positions being taken by the Respondent of the First Part.

. . . . 26

The tribunal is fully aware of its jurisdiction to award costs provided for within Part VI of the **Mining Act**. The tribunal weighed the evidence and finds that an award for costs will not be made in this case.

The common law rule holds that a successful party does not have a legal right to costs, but may have a reasonable expectation of receiving costs, subject to the tribunal's discretion. The Ontario *Rules* provide the tribunal with discretion to award costs where any steps in the proceeding was improper, mistaken or unnecessary [Ontario Rule 57.0.1(1)(f)]. The *Rules of Civil Procedure* [57.01(2)] also provide for a cost award against a successful party in a proper case. Included in Rule 57.01(1) for consideration, are "(c) the complexity of the proceeding, (d) the importance of the issues and (e) the conduct of any party that tended to shorten or to lengthen unnecessarily the duration of the proceedings…and (i) any other matter relevant to the question of costs." While the tribunal is not bound by the *Rules of Civil Procedure*, nonetheless, they provide a useful framework for consideration in determining whether to award costs.

The actions leading up to the hearing of this application are broadly divided into three distinct time periods, each with sufficiently different considerations which are relevant to determining whether the tribunal should award costs or not.

The initial period was from February 2007 through to March 2008 in which the Applicant, armed with a license from the Ministry of Natural Resources to drill well #59, proceeded to ramp-up operations without, as shown from the evidence, a completed spacing unit. No award is being sought for anything expensed in this time frame except that it forms the basis for what was to come. The Applicant did not seek legal counsel, whom the tribunal believes would have possibly drawn attention to the need to complete the spacing unit and he would have avoided receiving the notice to shut-in the well. The Applicant could have benefited from legal counsel's advice on how best to proceed if for no other reason than to identify whom to serve the spacing unit matter on. The tribunal suggests that this confusion and/or miscalculation by Echo Energy Canada Inc. may well have lead to the call for a hearing. Respectfully, while legal counsel is not mandatory in these matters, counsel was not engaged until mid June 2008.

The next time frame, relevant to the question of costs is from the March 2008 "notice to pool" sent by the Ministry, through to the engagement of legal counsel by Echo Energy Canada Inc. and NRG Corp. in June 2008. There was evidence provided that Echo Energy made telephone calls and possibly wrote a letter over the next three month period to NRG Corp. Reportedly there was no response to these attempts by NRG Corp. Evidence was submitted that a total of sixty to seventy telephone calls were made. This leaves the tribunal in wonder. The tribunal further questions the negotiating practices of Echo Energy Canada Inc. It begs the question; "what would a prudent businessman have done given the same situation". The methods early on to voluntarily pool the spacing unit were less than effective given the outcome. On or before June 17, 2008 Mr. Lewis was retained as counsel for Echo Energy and the options and pooling position requirement were presented to NRG Corp. (addressed to Mr. Bristol) in a letter of that date.

. . . . 27

On the other hand, the tribunal is unaware that the other working interest, NRG Corp., even received the telephone calls or whether they chose to ignore them. It is unclear to the tribunal who the person(s) at NRG Corp. were responsible for the file. There was no conclusive evidence provided whereby the tribunal could determine whether the working interest, NRG Corp. attempted to misrepresent their position. The only concrete evidence of their awareness is the June 30, 2008 correspondence from Mr. T. McCullough counsel for NRG Corp. In the subscript of that letter a carbon copy notation to a John Camara was made which identified a contact concerning this file going forward.

At this point, the salient fact is that no binding agreement/contract was in place to determine a performance level by either party. The tribunal notes that no attempts were made to contact the Respondents of the Second Part (landowners), who had an interest in theses matters through their various leases.

The final time frame, being from June 30, 2008 until August 26, 2008, notably involves counsel for both parties and shows a definitive evidence trail. Counsel for Echo Energy issued a letter (June 17, 2008) calling for action on the part of NRG Corp. by the end of June, 2008 to deal with the spacing unit issue. This letter was met with a response from NRG's counsel of the day (Mr. T. McCullough) calling for a delay in the matter until some time in mid summer. The tribunal finds that the Applicant was forced by time constraints to get the well into production and to retain current lease terms. The Applicant took the advice of counsel (Mr. C. Lewis) and commenced the hearing process seeking a pooling order. It was the only sure action available under the circumstances. The Applicant had to work through the legal barriers to establish a spacing unit.

At this point, the tribunal finds that the request for an extension of time to deal with the pooling agreement was reasonable given that Echo Energy's position had finally been communicated and acknowledged through Counsel for the Respondent. However, the reasons given by the Counsel for the Respondent for a time extension were not in the best interests of Echo Energy or in the best interests of landowners (Respondent of the Second Part). No attempts were made to contact the Respondents of the Second Part (landowners), who had an interest through their various leases, until the decision to proceed to a hearing was made.

The Appointment for Hearing was issued by the tribunal on July 9, 2008 to all interested parties. The Respondent of the First Part retained Mr. Anthony Steele as legal counsel and correspondence and telephone contacts flowed between counsel(s) concerning the matter after that time.

Upon reviewing the submissions and the pooling arrangements, the Respondent of the First Part considered several issues to be negotiable and within the tribunal's jurisdiction to resolve. Once the Application was made and the Appointment for Hearing was issued, it appears from the evidence that the usual "to and fro" of negotiations was underway. Whether this was the time frame for requests for information or not would appear to this tribunal to be overshadowed by the Respondent's need to know.

. . . . 28

Finally the hearing itself was attended by the Applicant and the Respondent and their separate counsel. Each provided evidence and arguments for consideration.

The Applicant has failed to provide evidence that the Respondent was less than cooperative. There was no proof of the alleged efforts to contact the Respondent through over 60 telephone calls. Furthermore, there was no evidence provided/presented that contact letters were used prior to June 17, 2008 to bring the Respondent of the First Part to the negotiating table. It is not the purpose of this tribunal to determine the particulars or methods of negotiation as to how a contract should come together. Overall, a pooling of resources/leases was an agreeable conclusion with differing views surrounding the pooling agreement and its terms. There appears to be no merit to the suggestion that the Respondent of the First Part was seeking to delay resolution or adjudication. What is not known is whether the discharge of the original counsel for the Respondent of the First Part was intended to create some strategic advantage in these matters.

The submissions show that the Ministry of Natural Resources issued a license to drill a well (#59) in February, 2007 and it was not until March, 2008, upon the opening of the well, that it became evident that one piece of the puzzle surrounding the spacing unit size had been overlooked. This lead to attempts to get a working interest on-side in order for landowners leases and their correlative rights to be protected and for the Applicant to be able to proceed with both a well and natural gas production for the marketplace. There is no requirement that legal counsel has to be used in these matters, however, consulting with counsel may have improved negotiations and/or timing. The situation was not assisted by counsel until a relatively late date (June, 2008). Conclusively there was no contract for either party to perform in a certain fashion until the tribunal’s Pooling Order of October 16, 2008. The tribunal finds no fault by either party in these matters.