

ALBERTA ENERGY AND UTILITIES BOARD

IN THE MATTER OF THE ENERGY RESOURCES
CONSERVATION ACT, Ch. E-10 OF THE REVISED
STATUTES OF ALBERTA 2000;

AND IN THE MATTER OF PROCEEDING NO. 1457147
RESPECTING A REVIEW HEARING IN CONNECTION WITH
THE ISSUANCE OF CERTAIN WELL LICENCES, AND
COMPULSORY POOLING AND SPECIAL SPACING ORDERS
IN THE CLIVE, EWING LAKE, STETTLER AND WIMBORNE
FIELDS

PART 2
SUBMISSION OF DEVON CANADA CORPORATION

August 25, 2006

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I INTRODUCTION

1. Devon Canada Corporation (Devon) applied for and obtained licences for the following wells:

02/06-08-034-26 W4 (6-8)
 02/08-08-034-26 W4 (8-8)
 02/14-08-034-26 W4 (14-8)
 02/16-08-034-26 W4 (16-8)
 02/06-17-034-26 W4 (6-17)
 00/08-17-034-26 W4 (8-17)
 00/14-17-034-26 W4 (14-17)
 00/16-17-034-26 W4 (16-17)
 03/06-09-034-26 W4 (6-9)
 02/08-09-034-26 W4 (8-9)
 00/14-09-034-26 W4 (14-9)
 00/16-09-034-26 W4 (16-9)
 03/06-15-034-26 W4 (6-15)
 00/08-15-034-26 W4 (8-15)
 00/14-15-034-26 W4 (14-15)
 00/16-15-034-26 W4 (16-15)
 02/06-35-033-26 W4 (6-35)
 02/08-35-033-26 W4 (8-35)
 02/14-35-033-26 W4 (14-35)
 00/15-35-033-26 W4 (15-35)

and for the establishment of holdings for the production of gas from the Edmonton (Coals and Sands) in Townships 33 and 34 Range 26 W4 all in the Wimborne Field. The appropriateness of the Board issuing these licenses has been raised in issue in this proceeding by Carbon Development Partnership (successor in interest to Prairie Mines and Royalty Ltd., formerly Luscar Energy Ltd.) (CDP) and by EnCana Corporation (EnCana).

2. This proceeding arises out of a Board decision, dated March 9, 2006, in which it was determined that the Board would hold a review hearing with respect to the above wells and holding approval, Part 2 of which hearing the Board indicated "... will consider the

issue of legal entitlement to coalbed methane being produced or intended to be produced from the said wells".¹

3. The issue of legal entitlement was raised initially in objections by EnCana on the basis that "uncertainty surrounds the interpretation of whether coalbed gas is included" in the language of Devon's natural gas leases.² The legal entitlement issue was also raised in objections by CDP's predecessor, Luscar, in which it was indicated that "Luscar is claiming the coalbed methane at this location".³
4. The context for the objections raised on behalf of EnCana and CDP originates with the requirement of the *Oil and Gas Conservation Act*⁴ (O&GC Act) which provides:

16(1) No person shall apply for or hold a licence for a well

- (a) for the recovery of oil, gas or crude bitumen, or
- (b) for any other authorized purpose

Unless that person is a working interest participant and is entitled to the right to produce the oil, gas or crude bitumen from the well or the right to drill or operate the well for the other authorized purpose, as the case may be.

5. In its written decision⁵ on the Devon applications the Board found that:
 - The leases Devon submitted in support of its applications demonstrates sufficiently Devon's entitlement to produce all gas from the wells and zones it applied for;
 - Luscar and EnCana do not dispute Devon's right to produce gas;

¹ EUB Decision, March 9, 2006.

² EnCana Letter of Objection, dated December 23, 2004.

³ Luscar Letter of Objection, dated January 3, 2004.

⁴ RSA 2000, c. 0-6.

⁵ Decision, dated May 26, 2005.

- There is no Canadian case law on the issue of ownership of coalbed methane or the issue of whether gas produced from coal is a substance other than natural gas; and
- Devon had, therefore, satisfied the requirement of s. 16 of the O&GC Act by demonstrating that it has the rights to produce gas that is the subject of its applications.

6. The Board, in its decision, additionally determined that:

"As the EnCana and Luscar objections rest on the issue of CBM ownership ... EnCana and Luscar have not demonstrated that they may be directly and adversely affected by the Board's decision with respect to the applications ..."⁶

7. EnCana and Luscar subsequently lodged applications for Review and Variance of the Board's decision. The Board granted those requests for a review hearing on the ground that the uncertainty surrounding the entitlement to coalbed gas was sufficient for EnCana and Luscar to satisfy the test of being potentially affected. In that circumstance s. 40(1) of the *Energy Resources Conservation Act* (ERC Act) makes a hearing mandatory.

II FACTS AND ACKNOWLEDGEMENTS

8. Devon's entitlement to recover natural gas from the areas and zones contemplated by the well licence applications and licences marked as Exhibits 05-001 to 05-024 and 05-027 to 05-042 in this proceeding is confirmed in the Petroleum and Natural Gas (P&NG) lease rights held by Devon. A summary of the well licence applications, associated lease and title rights along with copies of the relevant P&NG leases are attached as Schedules 1-5 of Appendix A hereto.
9. Each of the P&NG leases held by Devon grants the rights to natural gas and related hydrocarbons except coal.

⁶ Ibid.

10. Devon acknowledges that it has no entitlement to coal in any of the zones from which it proposes to produce gas in the areas in issue.
11. The terms coalbed gas, coalbed methane (CBM), gas in coal and natural gas from coal (NGC) are all intended to refer to and describe natural gas (within the context of the O&GC Act) stored in coal.

III ISSUES

12. The issue to be determined by the Board is whether Devon is entitled to the holding approval and to hold the licences for the wells that have been raised in issue in this proceeding. This gives rise to several subsidiary issues:
 - What is required to establish an entitlement to a gas well licence?
 - Should gas stored in coal be considered to be other than natural gas?
 - Should gas stored in coal be considered to have been reserved out of the natural gas leases held by Devon?

IV DISCUSSION

The Required Entitlement

13. Section 16 of the O&GC Act imposes an obligation on the party that applies for a licence to have the entitlement to produce for the purpose sought by the well licence.⁷
14. The Board has the authority to inquire into the entitlement issue to the extent it may consider such inquiry to be reasonably necessary and justified by the circumstances.

⁷ *Alberta Energy Co. v. Goodwell Petroleum Corp.* (2003) 22 Alta L.R. (4th) (C.A.) p. 36, at para. 92:

"The Board also relies on s. 16(1) of the *Oil and Gas Conservation Act*, which precludes a person from applying for or holding a licence for a well for the recovery of oil, gas or crude bitumen unless the person has the right to produce that hydrocarbon from that well. ... These sections will be contravened if the person who holds the well licence does not possess the right to produce the hydrocarbon authorized by the well licence."

The Energy Resources Conservation Act⁸ provides:

s. 16 Powers of Board

"The Board, in the performance of the duties and functions imposed on it by this Act and by any other Act, may do all things that are necessary for or incidental to the performance of any of those duties or functions."

15. Section 16(2) of the O&GC Act establishes the standard of proof the licensee is required to fulfill as it allows the Board to cancel or suspend a license if the licensee does not prove entitlement to the satisfaction of the Board.
16. Entitlement is an issue collateral to the Board's authority to grant a well licence and holding approval and a determination of entitlement by the Board is effective in the context of and for the limited purpose of confirming a finding by the Board that a party is or is not entitled to hold a well licence.⁹
17. The determination of entitlement made by the Board in its May 26, 2005 correspondence reflects the state of the law as established in existing legislation and jurisprudence. There is no need or reasonable purpose to be served by the Board extending its examination of the entitlement issue beyond such considerations so as to enable the Board to opine on propositions that have not yet been established in law. The determination of entitlement to be made by the Board must, in any event, be limited to a purpose that is within the Board's authority. A determination made by the Board that purports to establish the rights of the parties in other contexts or for other purposes would be without legal force of effect.
18. The evidence presented to the Board in the title documents attached as Appendix A, shows that Devon has the entitlement to produce all natural gas from the areas and zones from which Devon has applied. Unless the point can be established, which Devon

⁸ RSA 2000, c. E-10.

⁹ *Anderson v. Amoco Canada Oil and Gas* [1998] AJ No. 805 ACQB 620 at para. 147:

"The regulator's view does not determine legal ownership of solution gas. If the regulators have misconstrued the law, their practices will have to change, however, cumbersome that process might be. The court's function is not to preserve legally incorrect administrative positions. I accept evidence of the regulatory position for the limited purpose of dealing with the plaintiffs' fairness argument and considering settled expectations."

disputes, that gas stored in coal is not gas within the meaning of the O&GC Act or within the scope of Devon's leases or that gas stored in coal was reserved out of Devon's leases as coal, Devon's entitlement to hold the well licenses raised in issue should be confirmed.

Gas Stored in Coal is Natural Gas

19. Gas stored in coal, the entitlement to which is in dispute, is natural gas. It is natural gas within the legislative definitions that guide and bind the Board and it is also natural gas that is included in the granting language in the P&NG leases held by Devon.

20. In its May 26, 2006 Decision, the Board:

"... noted that Luscar and EnCana do not dispute Devon's right to produce natural gas and that there is no settled law on the issue of ownership of CBM or on the issue of whether natural gas produced from coal is a substance other than natural gas. Therefore, the Board has determined that Devon has satisfied the requirement of s. 16 of the O&GC Act by demonstrating that it has the rights to produce the natural gas that is the subject of its applications."

21. Devon submits there is no reasonable basis in fact or in law for the Board to revise or to change its decision that Devon has satisfied the requirement of s. 16 of the O&GC Act by demonstrating that it has the rights to produce the gas that is the subject of its applications. Although EnCana and CDP may wish to contest what is or is not included in the substances to which the parties were granted title under the relevant title documents, there is no doubt that under Alberta legislation gas stored in coal is natural gas and is required to be considered as natural gas.

22. The O&GC Act makes no distinction between gas that is produced from various types of reservoirs that hold gas. The Act defines gas as:

"raw gas or marketable gas or any constituent of raw gas, condensate, crude bitumen or crude oil that is recovered in processing and that is gaseous at the conditions under which its volume is measured or estimated".

Raw gas, in turn, is defined as:

“a mixture containing methane, other paraffinic hydrocarbons, nitrogen, carbon dioxide, hydrogen sulphide, helium and minor impurities, or some of them, that is recovered or is recoverable at a well from an underground reservoir and that is gaseous at the conditions under which its volume is measured or estimated”.

Marketable gas is defined as:

“a mixture mainly of methane originating from raw gas, if necessary through the processing of the raw gas for the removal or partial removal of some constituents, and that meets specifications for use as a domestic, commercial or industrial fuel or as industrial raw material.”

23. The Board and the Alberta Department of Energy have indicated that they "consider coalbed methane to be a form of natural gas"¹⁰.
24. The substance Devon has sought approval to produce and to which it has an entitlement is substantially methane, is or will be recoverable at a well from an underground reservoir and is gaseous at the conditions under which its volume is measured, and is wholly encompassed by the legislative definition of gas.
25. By comparison, the *Coal Conservation Act*¹¹ (CC Act), defines coal in the following terms:

"coal", in addition to its ordinary meaning, includes manufactured chars, cokes, and any manufactured solid coal product used or useful as a reductant or energy source or for conversion into a reductant or energy source.
26. The ordinary meaning of coal can be found in any standard English dictionary, and includes the description that coal is: "a black or brownish black solid combustible substance formed by the partial decomposition of vegetable matter ... that is widely used as a fuel."¹²

¹⁰ Alberta Energy and Utilities Board, Informational Letter IL 91-11.

¹¹ RSA 2000, c. C-17.

¹² Merriam-Websters Collegiate Dictionary, 10th Ed.

27. Because the Board must be guided by the applicable legislative definitions, it is clear that a person entitled to coal does not have a competing right to seek a gas well license application before the Board. Due to the nature and extent of the grants or reservations pursuant to which coal owners may claim title, they are unable to demonstrate that they have an entitlement to any substance that is mainly methane and gaseous at the conditions under which its volume is measured or estimated, regardless of where it is stored. This inability to establish a competing claim makes clear that the Board is compelled by the O&GC Act to issue a well license to the party that is able to demonstrate an entitlement to "gas".
28. Although CDP has in past sought to distinguish "conventional natural gas" from coalbed methane or gas from coal or gas in coal¹³ there is no reasonable basis in fact, in the common law or the legislation, including that pertaining to the interpretation of section 16 of the O&GC Act, that substantiates such a distinction being drawn between gas stored in coal and gas stored in any other type of reservoir.
29. If the Board were not constrained by the legislative definition of gas, it is clear that chemically, scientifically and from all reasonable points of analogy gas stored in coal is, in any event, a form of natural gas. In that regard Devon relies on the report and conclusions of Matthew J. Mavor, set out in his Expert Opinion, *Concerning Coalbed Methane Reservoir Behaviour*, filed concurrently in this proceeding with the Joint Submission of ConocoPhillips Canada, Devon, Fairborne Energy Ltd., Quicksilver Resources Canada Inc., Canpar Holdings Ltd. and Centrica Canada Limited, including that:
- *CBM and coal are distinct and differ from one another both on the surface, after extraction from the ground and in the subsurface, before and after disturbance by man.*

¹³ See Luscar correspondence to the Board, dated April 12, 2005, which at page 2 states "Luscar does not dispute Devon's entitlement to produce conventional natural gas by virtue of its leases from the conventional natural gas owner. However, with respect, this is irrelevant to a consideration of whether Devon is entitled to CBM."

- *CBM is a natural gas that can be produced from coal seams. It is virtually indistinguishable from natural gas produced from sandstone, shale, carbonate, or other rock types in both composition and economic value. When commercially exploited, CBM is transported on the surface usually as a vapour in pipelines.*
 - *In the subsurface, coal and CBM are distinct. Coal is a rock that serves as the container for storage of CBM both before and after the reservoir has been disturbed by man.*
 - *CBM is readily released from and flows through the coal and other rock types due to a reduction in pressure as other natural gas commercially produced from other types of rock.*
 - *From a reservoir engineering standpoint CBM shares very similar flow characteristics through coal seams as natural gas flow through other rock types.*
30. Consistent with the view that gas stored in coal is and should be considered indistinguishable from natural gas in other types of natural gas reservoirs, it should be noted that:
- Such gas attracts Provincial natural gas royalties on Crown owned production and natural gas taxes on freehold production; and
 - Provincial exploration and production of gas from coal is regulated in a manner consistent with the exploration and production of other natural gas types generally.

Gas Stored in Coal was Granted to Devon in its P&NG Leases

31. The P&NG leases, attached as Appendix A, provide unequivocal evidence that Devon is entitled to all natural gas from the areas and zones to which Devon has been granted the rights, subject only to the Board being shown a reservation which is to the contrary.

32. The granting clauses in the leases held by Devon variously describe the leased substances as:
- "all the natural gas and related hydrocarbons, all other gases, and all other substances (whether fluid or solid and whether similar or dissimilar and whether hydrocarbons or not) produced in association with any of the foregoing or found in any water contained in an oil or gas reservoir, excluding, however, coal, petroleum and valuable stone."
 - "all the petroleum and natural gas, natural gasoline and related hydrocarbons other than coal ..."
 - petroleum, Natural Gas and related hydrocarbons, other than coal, Heavy Oil and valuable stone, and all substances whether liquid or solid and whether hydrocarbons or not, produced in association with any of the foregoing"
- Natural Gas being defined as "raw gas or marketable gas whether or not the same is treated to make the same marketable other than through a processing plant."
33. While the granting clauses in each of the underlying P&NG leases held by Devon are slightly different, all leases are consistent in the fact that they grant an entitlement to all natural gas. Nothing in the leases or the reservations excludes any particular form or type of gas. No evidence or basis for construing such a reservation has yet been disclosed to the Board.
34. The reservation in all of the leases held by Devon, that are raised in issue, is for "coal", without qualification or exception. Consistent with the definitions found in the Board's governing legislation, coal does not include the gas stored in the coal.
35. Devon is not aware of any common law determination in Canada which provides any support for the proposition that gas stored in coal either is or should be considered to be separate from or distinguished from natural gas generally and as may be stored in other natural gas reservoirs.

36. The Supreme Court of the United States has concluded that the most natural interpretation of coal, in the context of a reservation of coal, was a solid rock substance and did not encompass coalbed methane gas.¹⁴
37. It is well established in Canadian jurisprudence that although decisions of U.S. Courts are not binding and must be used cautiously, that such cases may nevertheless be persuasive when not in conflict with authoritative Canadian decisions.¹⁵
38. If there is any dispute as to the meaning and intent of the grant or the reservation from the title documents, that can and should be resolved by the courts.¹⁶ The Board is not required to make that determination. The Board is only obligated to determine, to its satisfaction, that an applicant is entitled to the substance for which it seeks a license.

VI CONCLUSIONS

39. Natural gas stored in coal is gas as defined in the applicable legislation.
40. The legislative definitions of gas are supported by the technical and scientific perspective that gas stored in a coal reservoir is separate and distinct from the coal and should be considered in the same manner as natural gas stored in any other type of reservoir.
41. The PN&G leases held by Devon grant the right to all natural gas regardless of the reservoir where it is stored.
42. Based upon the applicable legislation, the supporting technical interpretation and the entitlement documentation supporting Devon's well license applications, Devon has

¹⁴ *Amoco Petroleum Company v. Southern Ute Indian Tribe et al* 526 U.S. 865 (1999)

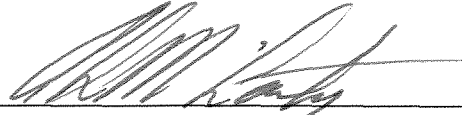
¹⁵ *Anderson v. Amoco Canada Oil and Gas* [1998] A.J. No. 805, ABQB 620 where Fruman, J. said at para. 103:
"While we cannot look to other areas of the law for a solution, we can still look to other jurisdictions. Many of our basic Canadian Oil and Gas Industry documents and concepts were developed in the United States and have been the subject of U.S. judicial scrutiny. We commonly examine American case law which, although not binding, may have persuasive force in analogous circumstances."

¹⁶ *Alberta Energy Co. v. Goodwell Petroleum Corp* (supra) at para. 98:

"Disagreements about production frequently occur and are even recognized in the energy legislation. Parties are entitled to come to court to resolve difficult disputes."

satisfied the requirement of s. 16 of the O&GC Act that it is entitled to produce the gas that is the subject of its applications.

All of which is respectfully submitted this 25th day of August, 2006.

A handwritten signature in black ink, appearing to read 'A.L. McLarty', written over a horizontal line.

A.L. McLarty, Q.C.
Counsel for Devon Canada Corporation

APPENDIX A

DEVON WELL LICENCE APPLICATION LEASE RIGHTS

Schedule 1 - Lease rights for 8-34-26 W4M

Schedule 2 - Lease rights for 17-34-26 W4M

Schedule 3 - Lease rights for 9-34-26 W4M

Schedule 4 - Lease rights for 15-34-26 W4M

Schedule 5 - Lease rights for 35-33-26 W4M