ALBERTA ENERGY AND UTILITIES BOARD

PART 2 OF PROCEEDING NO. 1457147

**IN THE MATTER OF
BEARSPAW PETROLEUM LTD., CARBON DEVELOPMENT PARTNERSHIP (SUCCESSOR IN INTEREST TO PRAIRIE MINES AND ROYALTY LTD., FORMERLY LUSCAR LTD.), DEVON CANADA CORPORATION, ENCANA CORPORATION AND FAIRBORNE ENERGY LTD.
CLIVE, EWING LAKE, STETTLER AND WIMBORNE FIELDS**

REPLY OF THE INTERVENER FREEHOLD PETROLEUM AND NATURAL GAS OWNERS ASSOCIATION TO THE FINAL ARGUMENTS OF ENCANA CORPORATION AND CARBON DEVELOPMENT PARTNERSHIP

December 13, 2006

I. INTRODUCTION

1. In reply to the arguments that have been advanced by Carbon Development Partnership ("CDP") and EnCana Corporation ("EnCana"), the Freehold Petroleum & Natural Gas Owners Association ("FHOA") provides the following brief submissions:

II. ARGUMENT OF CARBON DEVELOPMENT PARTNERSHIP

A. Scope of Proceedings

2. In paragraph 38 of its submission, CDP correctly states that the scope of this Proceeding is narrow and should be restricted to the validity of the Devon, Fairborne and Bearspaw well licences, holding orders and pooling orders.

3. FHOA agrees that any rescission or variance of the licences and orders at issue should not have a direct impact upon the interests of other freehold owners who hold title to the natural gas interest, or lease the natural gas interest, with respect to Split Title Lands. However, the remedy and ultimate disposition sought by CDP, and EnCana, is extremely broad. Both CDP and EnCana have asked that this Board maintain and continue Bulletin 2006-19, the effect of which is to place a moratorium on all CBM development on Split Title Lands. That is, if CDP is successful in arguing that the licences and orders at issue should be rescinded, then CDP would have this Board apply this result to all Split Title Lands without the Board hearing the facts, evidence and arguments of other freehold owners.

B. Intent of the Parties

4. At paragraph 55 of its submission, CDP poses a hypothetical question which implies that settlers would not have accepted title to the CBM due to the worthless and noxious nature of the CBM. Put another way, CDP suggests that the CPR intended to reserve for its own account dangerous and worthless substances, such as CBM, while transferring to the settler only the valuable and safe substances.

This is inconsistent with the findings of the Alberta Court of Appeal in *Goodwell*[1] where it was held that the CPR did not reserve unto itself natural gas rights due to **the CPR's** mistaken belief that natural gas was a "worthless and noxious substance".

5. It is also important to note that while the Court of Appeal has ruled on CPR's position with respect to its reservation of worthless "dangerous and noxious substances" the Court of Appeal did not comment on what the settlers' intent would have been with respect to these same substances. It is important to bear in mind that it was the CPR that chose to reserve "coal", "coal and petroleum" and "coal, petroleum and all valuable stone" as the case may be. On the other hand, the settlers were granted and accepted title to everything that was not reserved to the CPR, whether or not such land or minerals were worthless, noxious or dangerous. Theirs was the remainder of whatever the CPR did not want.

C. The Relevance of Phase Change

6. In paragraphs 73 and 74 of its submission, CDP suggests that the phase of CBM while *in situ* is irrelevant to the determination of CBM ownership. FHOA submits that in light of the relevant authorities, CDP is incorrect and the phase in which CBM exists while *in situ* is very significant when determining ownership of the CBM.

7. The Privy Council in *Borys*[2] was quite clear in stating that in Split Title Lands, the CPR did not reserve to itself those substances that exist as gas while *in situ*:

> "The substance which is found in the form of gas *in situ* is therefore not the subject of reservation and remains the property of the appellant."

8. FHOA submits that the location of the gaseous substance, whether it is in the coal *strata* or not is irrelevant. On the other hand, natural gas that exists as a liquid *in*

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[1] *Alberta Energy Company Ltd. v. Goodwell Petroleum Corporation Ltd.,* 2003 CarswellAlta 1394 [2004] 8 W.W.R. 116 at paragraph 34 **(See TAB D of Exhibit 13-002)**

[2] *Borys v. CPR and Imperial Oil Limited,* 1953 CarswellALta 25, [1951] 4 D.L.R. 427, Reversed [1952] 3 D.L.R. 218, Affirmed [1953] 2 D.L.R. 65 at paragraph **18 (See TAB G of Exhibit 13-002)**

situ would be subject to a reservation of petroleum and presumably natural gas that exists as a solid while *in situ* may very well be subject to a reservation of the coal.

D. The *Little* Case

9. In paragraphs 76 to 79 of its submission, CDP suggests that property concepts that apply to corporeal coal may be applicable as opposed to oil and gas theories of ownership. However, as discussed at paragraphs 5 to 9 of FHOA's submissions at Exhibit 13-006, the Supreme Court in *Anderson*[3] suggests that where title to minerals has been split, traditional ownership theories are not applicable.

10. Simply stated, when the CPR reserved certain substances to itself what becomes paramount is CPR's intent to split title on certain terms. This intent cannot and should not be defeated or altered based on the application of a theory of ownership that is incompatible with the original intent. If CPR did not reserve the gas for its own benefit then CDP cannot defeat this intent by claiming that it now owns all gas located within a specific *strata*.

11. As Justice major held in *Anderson:*[4]

> "The appellants submitted that Canada is not an ownership *in situ* jurisdiction and therefore no rights vest in hydrocarbons until they are reduced to possession. They relied on this ownership theory as support for their position that it is not until the time of possession that the phase of the hydrocarbon becomes important for determining ownership, because no one has any rights before that. This is the type of broad ownership theory that is not required to be determined in this appeal. **Irrespective of any other rights the parties may have in relation to the hydrocarbons in the ground, they chose to divide their interest by contract. It is not open to later argue that division was meaningless on the basis that no rights can attach until the substance is reduced to possession. When the substance, which was not in their possession at the time of the contract, is reduced to possession, the date and terms of the contract govern their relative entitlement."** (Emphasis added.)

and

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[3] *Anderson v. Amoco*, [2004] S.C.R. 3 **(See TAB C of Exhibit 13-002)**

[4] *ibid* at paragraphs 36 and 39

> "The rule of capture does not apply to the division of ownership by phase as it does to divisions of ownership based on surface land ownership. **Applying the rule of capture to parties who have agreed to divide their interest under the same tract of land would defeat the purpose of the contract.** This is because if it applied, the party who reduced the substance to possession by drilling the well and producing the hydrocarbons would be entitled to all of them and the other party would have no claim. **At the time the CPR sold the land to the settler they agreed to divide the property on certain terms. To hold that either party could later take the other party's property with impunity would defeat the purpose of the reservation."** (Emphasis added.)

E. Are Devon and Fairborne Entitled to Produce CBM

12. While CDP cites no authority for its proposition at paragraph 133 of its submission, CDP suggests that in order for this Board to be satisfied that an applicant is entitled to a well licence, an applicant should prove its entitlement to a standard that is close to virtual certainty.

13. Then at paragraph 141 of its submission, CDP suggests that "in the face of a *bona fide*, seriously arguable issue as to ownership of CBM, the Applicants are unable to satisfy the Board that they are entitled to produce CBM…" whether the standard of proof is on the balance of probabilities or at the level of virtual certainty. That is, it appears that CDP may be suggesting that the standard of proof is different upon receipt of an objection to a well licence application.

14. FHOA submits that an applicant for a well licence should not and cannot be held to a higher or stricter standard of proof on the mere basis that there is an objection to the applicant's entitlement to the well licence.

15. Furthermore, the Board should bear in mind that it is CDP and EnCana that assert that their predecessor in title, the CPR, reserved or intended to reserve the CBM when it reserved unto itself "all coal" or "all coal and petroleum".

16. In light of the assertions of both CDP and EnCana, FHOA would argue that the more appropriate question before this Board is: **Has CDP and EnCana met their burden of proof with respect to their respective allegations that the CPR reserved CBM on Split Title Lands?**

17. At paragraphs 10 to 19 of FHOA's submissions at Exhibit 13-006, FHOA reviewed the principles enunciated in *Freyberg v. Fletcher Challenge Oil and Gas Inc.*[5]

18. Devon and Fariborne have shown that they are entitled to their well licences on the basis that the applicants hold leases that entitle them to produce natural gas from the subject lands. To rebut the validity of these leases, with respect to CBM, EnCana and CDP assert that the CPR reserved the CBM when it reserved the coal in the subject lands. As a result, EnCana and CDP now bear the onus to prove, on the balance of probabilities, this assertion.

19. This is especially critical in light of the fact that the assertion of EnCana and CDP is that their predecessor in title reserved the CBM. It should not fall upon Devon and Fairborne to produce evidence with respect to the CPR's business decisions or to explain what the CPR intended when it reserved "all coal" or "all coal and petroleum". It is submitted that such an obligation falls squarely upon the shoulders of EnCana and CDP.

20. As stated by Ritter J. in *Freyberg*:

> …The burden should not fall on Lady Freyberg to produce evidence about Voyager's business decision and to explain why Voyager made the decision that it did. This evidence lies particularly within the knowledge of Voyager.[6]

F. Quiet Title

21. At paragraph 143 of its submissions CDP suggests that it is unaware of any situation where the Board issued well licences in circumstances where ownership to a substance was at issue. FHOA submits that in the case of the lands at issue in *Borys*, the owner of the natural gas did in fact object to the issuance of the well

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[5] *Freyberg v. Fletcher Challenge Oil and Gas Inc., 2005 A.B.C.A 46* **(See TAB 5 of EnCana Authorities 07-026)**

[6] *ibid*, at paragraph 80

licence on the basis that the applicant did not own title to the natural gas[7]. Imperial Oil argued that it did own title to the natural gas and that in any event the question of ownership of the gas rights was not relevant to any application for a drilling licence with Mr. Borys' proper remedy being an action through the courts and not by way of opposing the application.[8] Imperial Oil Applied for a well licence on December 19, 1949[9] with the Board issuing the Licence to Drill a Well on January 19, 1950.[10]

22. Therefore, FHOA submits that in so far as Split Title Lands are concerned, the Board has in fact issued well licences even in the face of title disputes, with the ultimate remedy of the objecting party being the commencement of legal action through the courts.

23. With respect to paragraphs 145 and 146 of is submissions, CDP suggests that Fruman J. in *Anderson* suggests that the Board has a policy of requiring quiet title prior to issuing a well licence. However, FHOA submits that the agreements between the petroleum and non-petroleum owners referred to by Fruman J. at paragraph 144 of *Anderson*[11] are in respect to conservation of the natural resources and the orderly development of the various substances and not in respect to any adverse claims to the various substances as between the petroleum and non-petroleum owners.

G. Bulletin 2006-19

24. With respect to CDP's characterization of Bulletin 2006-19 as a "non-proliferation of hearings" policy, at paragraph 149 of its submissions, FHOA would suggest that while such a policy may assist the Board in dealing with **hearings** in an orderly and efficient manner, this is not the mandate of the Board.

[7] **TAB A** Letter to the Petroleum and Natural Gas Conservation Board from Fisher, McDonald & Fisher dated November 12, 1949.
[8] **TAB B** Letters from Imperial Oil Limited to the Petroleum & Natural Gas Conservation Board dated November 22, 1949 and January 9, 1950
[9] **TAB C** Application for Licence to Drill a New Well, dated December 19, 1949
[10] **TAB D** Licence to Drill a Well, dated January 19, 1950
[11] *Anderson v. Amoco Canada Oil & Gas* (1998) AB QB 620

One of the defined purposes and mandates under section 4(c) the *Oil and Gas Conservation Act*[12] is to provide for the economic, orderly and efficient development of the oil and gas resources. As FHOA has argued, the continuation of Bulletin 2006-19 would serve to frustrate that mandate.

25. At paragraph 150 of its submissions, CDP states that continuing Bulletin 2006-19 does not have the same effect as an injunction since the Bulletin would require that the owners of natural gas rights and coal rights negotiate a commercial settlement or resolve their dispute through the courts. Regardless of what CDP may claim, this is no different than what would happen if CDP sought an injunction through court proceedings. If CDP obtained an injunction through court proceedings such an injunction would remain in place until such time that the parties concluded the court proceedings or settled the matter outside the court.

26. The difference is, and FHOA's concern remains unanswered, that CDP seeks what is effectively the extraordinary remedy of injunctive relief without satisfying the strict requirements that a court would impose prior to granting such relief.

27. Furthermore, while CDP claims that these Proceedings are narrow and only impact the licences and orders that were issued to Devon and Fairborne, CDP clearly desires that the Board impose a remedy that is far broader and will impact Freehold owners and lessees who are neither parties to nor interveners in the within Proceedings.

28. To argue, as CDP does at paragraph 151 that the continuation of Bulletin 2006-19 somehow promotes the Board's mandate of conservation of the resource, is illogical. The evidence of the parties to this Proceeding suggests the opposite. If Bulletin 2006-19 is continued this will result in checkerboard development of CBM, which may result in offset obligations being triggered by production from Crown lands, the expiry of leases and the drainage of CBM underlying adjoining Split Title Lands.

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[12] RSA 2000, c. O-6 **(See TAB A of FHOA Written Argument)**

H. Drainage

29. At paragraph 157 CDP states that there is "no technical evidence that drainage is occurring on the lands which are the subject of the Devon Applications and the Fairborne Applications."

30. If the effect of Bulletin 2006-19 was restricted to only the lands that are the subject matter of these Proceedings then FHOA may take some comfort in CDP's position. However, the Bulletin is clearly intended to apply to all Split Title Lands that may potentially produce CBM and even CDP does not go so far as to suggest that there is no risk of drainage on any of the lands that may be impacted by Bulletin 2006-19.

31. Furthermore, the witness for EnCana would only go so far as to suggest, "drainage might not be an issue" [13] and stopped well short of stating that there will be no risk of drainage.

32. While there may be no technical evidence that drainage is occurring, there is no technical evidence that drainage will not occur, either on the specific lands that are the subject of the well licences at issue or on any other lands that may be subject to the potential continuation of Bulletin 2006-19.

I. Economic, Orderly and Efficient Development

33. At paragraph 159 of its submissions, while CDP concedes that Bulletin 2006-19 will impact a "large number of parcels of land" (contrary to its submission that this Proceeding is narrow and is restricted to the Devon and Fairborne well licences), CDP also suggests that this is only a small portion of potential CBM production and that CBM production will not grind to a halt.

34. Once again, this highlights one of FHOA's concerns with respect to CDP's proposed disposition of this matter. CBM underlying Split Title Lands will not be operating on the same playing field as all other CBM production within Alberta.

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[13] Transcripts at Page 850, line 15 to Page 851, line 19; Page 1055, line 22 to Page 1056, line 16

The result will be that CBM will be developed in a checkerboard manner with the potential for drainage, the possible expiry of leases and the triggering of offset obligations under leases that adjoin those lands where CBM can be drilled for and produced.

35. With respect to paragraph 160 of CDP's submission, the concerns raised therein are largely irrelevant. All decisions of the Board may be subject to judicial review and appeal. This should not make the Board wary of fulfilling its mandate under its governing legislation. Regardless of the decision of this Board, the parties will eventually have to resolve the underlying dispute, either through the courts or by agreement. However, until such resolutions occur, the Board can make decisions with respect to the issuance of well licences and allow for the orderly and efficient production of CBM on Split Title Lands.

36. Similarly, with respect to paragraph 161 of its submissions, the issues raised therein are not a bar to this Board making a decision with respect to the issuance of well licences on Split Title Lands. While CDP suggests that freehold lessors are somehow placed in jeopardy if the natural gas lessees are allowed to produce CBM, the reality is that the dispute over the right to CBM is between CDP and EnCana, as the owners of the coal reservations, on the one hand and the freehold title owners of the natural gas rights on the other hand. Whether this matter is resolved through the courts, or by way of commercial agreements, CDP must include the freehold owners of natural gas rights as a party to any resolution since the rights and title to the freehold owner's CBM is at issue.

III. ARGUMENT OF ENCANA CORPORATION

A. Drainage

37. With respect to paragraphs 56 to 60 of EnCana's submission and EnCana's comments in relation to drainage or 'competitive drainage', EnCana fails to appreciate FHOA's concerns.

38. FHOA does not suggest that the Board must compel a party to drill and exploit its resources. Neither does FHOA argue that the Board should withhold a well licence on the basis that drainage may occur from adjacent lands.

39. What is at issue is that EnCana and CDP seek a disposition that would continue the application of Bulletin 2006-19; effectively placing a moratorium on CBM production from Split Title Lands while CBM production may continue from all other lands. That is, EnCana urges the Board to create an environment where certain lands have an unfair competitive advantage over Split Title Lands as a consequence of Bulletin 2006-19.

40. The effect and consequence of EnCana's preferred disposition is not in keeping with the mandate of the Board under the *Oil and Gas Conservation Act.*

41. Further, EnCana is simply incorrect when it states at paragraph 59 that "there is no drainage". EnCana and CDP have led no technical evidence to prove that there is no risk of drainage. Further, EnCana's witness acknowledged that there might be a risk of drainage.[14]

B. Procedural Fairness

42. With respect to EnCana's submissions at paragraphs 61 to 70, EnCana argues that the Board should not make a determination as to ownership of CBM for want of procedural fairness.

43. If correct, then this argument supports FHOA's position that Bulletin 2006-19 should not be continued. As stated by EnCana at paragraph 63, the common law duty to proceed fairly requires that the parties affected by the possible outcome of an administrative dispute receive adequate notice of proceedings.

44. The Notice of Hearing in these Proceedings does not suggest that the continuation of Bulletin 2006-19 would be at issue. Therefore, if EnCana wants such a disposition then all affected parties (being all freehold owners of Split Title Lands

[14] Transcripts at Page 850, line 15 to Page 851, line 19; Page 1055, line 22 to Page 1056, line 16

and their respective lessees) should have been provided with adequate notice. If EnCana is correct that the Board cannot determine ownership due to administrative shortcomings, then the disposition sought by EnCana, specifically the continuation of Bulletin 2006-19, must also fail as a consequence of these very same administrative shortcomings.

C. The Requirement for "Quiet Title"

45. With respect to paragraphs 114 to 118 of its submissions, EnCana argues that not only should the Board have a general policy of quiet title prior to an application to drill a well, but that it is a legal requirement. Furthermore, at the hearing of this Proceeding EnCana took the position that this should apply not only to CBM, but also in other situations where the dispute would impact the property rights of EnCana.

46. However, certain of EnCana's titles to minerals are themselves the subject of dispute and litigation.

47. For example, Her Majesty the Queen in Right of Canada ("Canada") is elsewhere arguing that in certain instances Canada may have a reversionary interest with respect to some of EnCana's mineral interests that were derived from CPR lands.

48. A recent example may be found in the B.C. Court of Appeal decision in *Canada (Attorney General) v. Canadian Pacific Ltd.*[15] Lands taken and appropriated by the CPR under s. 7(3) of the *Consolidated Railway Act, 1879* did not allow the CPR to subsequently alienate such lands.[16] Presumably this includes transfers of coal rights to successor companies such as EnCana.

49. Upon determining that the lands in dispute were no longer being used for railway purposes, the Court of Appeal held that the lands reverted to Canada for the use and benefit of three Indian Bands by way of a resulting trust.

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[15] **TAB E** *Canada (Attorney General) v. Canadian Pacific Ltd*. 2002 CarswellBC 1983, 217 D.L.R. (4th) 83
[16] *ibid*, at paragraph 19

50. With respect to EnCana's lands in Alberta, FHOA is aware of at least one instance where EnCana's title to its mineral interests are in dispute. The Stoney Tribal Council has commenced proceedings as against Canada, the CPR and EnCana in QB Action No. 9901-03798.[17]

51. While FHOA does not support, take a position or make submissions respecting the merits of that action, FHOA does note that in Canada's Statement of Defence[18] Canada claims a reversionary interest in the mines and minerals underlying the rights of way as a consequence of CPR transferring the mineral interest to PanCanadian Petroleum Limited, a predecessor corporation to EnCana.

52. Given Canada's position regarding railway lands granted under the *Railway Acts*, it may also be that the coal certainty agreements that EnCana suggests would serve to quiet title must also include the Government of Canada as a party in certain instances.

53. Furthermore, aboriginal claimants are asserting claims of aboriginal title within Alberta, including rights to CBM, in a number of legal proceedings. [19]

54. While FHOA does not support, take a position or make submissions respecting the merits of any of the cited actions, it is clear that by virtue of the filing of these three statements of claim there is evidence of *bona fide* disputes as to the ownership of not only CBM but also **all** other mineral rights within southern and central Alberta.

55. If the Board accepts EnCana's position that quiet title is required prior to well licences being issued, then the result of these title claim assertions would be not only the sterilization of CBM on Split Title Lands, but the sterilization of all oil

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[17] **TAB F** Statement of Claim in QB Action No. 9901-03798
[18] **TAB G** Statement of Defence of Her Majesty the Queen in Right of Canada in QB Action No. 9901-03798 See specifically paragraphs 24(a), (f), (g), (i) and (k)
[19] **TAB H** *Kainaiwa Nation (Blood Tribe), et al. v. Her Majesty the Queen in Right of Canada* Action No. T-340-99 (See paragraphs 41, 42, 43 and 44)
TAB I *Chief Florence Buffalo, et al. v. Her Majesty the Queen in Right of Canada, et al.* Action No. 9903-03868 (See paragraphs 5, 11, 21 and 26)
[19] **TAB J** *Chief Ernest Wesley, et al. v. Her Majesty the Queen in Right of the Province of Alberta, et al.* Action No. 0301-19586 (See paragraphs 10(a), 34, 36 and 41)

and gas development on many EnCana lands and throughout wide areas of Alberta.

III. CONCLUSION

56. FHOA requests that the Board uphold the licences and orders that form the subject matter of these proceedings and rescind Bulletin 2006-19.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 13th day of December, 2006.

RAE AND COMPANY

Per: ________________________________
L. Douglas Rae

Per: ________________________________
W. Tibor Osvath

Solicitors for the Intervener
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