I. INTRODUCTION

1. Quicksilver Resources Canada Inc. ("QRCI") is a major developer and producer of coalbed methane ("CBM") in Alberta. As of December 31, 2005, QRCI held interests in 1,685 (778.2 net) productive wells in Alberta. QRCI's total Canadian approved reserves as of the same date were estimated to be 305 Bcfe with an average daily production for 2006 of 49 MMcfd. The vast majority of this development and production is CBM.

2. QRCI drills and produces its CBM wells under and by virtue of petroleum and natural gas ("PNG") leases. The PNG leases held by QRCI are a combination of Crown and freehold leases. Many of these freehold PNG leases are on "split-title" lands, where the coal rights are owned by a third party.

3. QRCI's ongoing business depends on the existence in Alberta of a stable regulatory regime under which QRCI can reliably apply for and be granted well licences by the Alberta Energy and Utilities Board ("EUB") provided QRCI meets all regulatory requirements, including demonstrating that it is entitled to produce natural gas from the wells for which it seeks approval to drill and operate.

4. On May 30, 2006, the EUB issued *Bulletin 2006-19: Applications Involving Objections Relating to Entitlement of Coalbed Methane*. *Bulletin 2006-19* states in part:

> In light of Proceeding No. 1457147, the Board has decided that all applications regarding which legal entitlement to CBM is at issue will be held in abeyance pending issuance of the Board's decision in Part 2 of Proceeding No 1457147. The decision to hold applications in abeyance applies to all facilities applications, resources applications, and review and variance applications regarding which legal entitlement to CBM on split-title lands is at issue.
>
> Applicants have the option of withdrawing their applications and refiling at a later date, amending their applications to remove the freehold mineral lands at issue, or waiting for a decision respecting Proceeding No. 1457147.

5. Since the Board issued *Bulletin 2006-19*, Quicksilver has had three (3) applications held in abeyance by the EUB (Applications No. 1440865, 1465743 and 1421686). In addition, knowing that they will not be processed, Quicksilver is currently withholding more than sixty (60) additional applications, a number that will increase almost daily as QRCI completes surface acquisitions in furtherance of its 2006 drilling program. Thus, the uncertainty surrounding the issue of entitlement to produce CBM on split-title lands is having a significant direct and adverse effect on QRCI.

6. As a result, by letter dated July 4, 2006, QRCI requested that it be granted intervener status in this Proceeding. By letter dated July 19, 2006, the EUB granted QRCI the right to fully participate in the proceeding, including filing written submissions and evidence, participating at the scheduled public hearing and making argument. These submissions are filed with the EUB pursuant to the Board's letter of July 19, 2006.

7. In addition, QRCI has participated in the preparation of and adopts the Joint Submission filed concurrently by the Natural Gas Rights Holders, ConocoPhillips Canada Resources Corp. ("ConocoPhillips"), Devon Canada Corporation ("Devon"), Fairborne Energy Ltd. ("Fairborne"), QRCI, Canpar Holdings Ltd. ("Canpar") and Centrica Canada Limited ("Centrica").

II. EVIDENCE OF QUICKSILVER RESOURCES CANADA INC. ("QRCI")

A. NATURE OF QRCI'S OPERATIONS IN ALBERTA

8. QRCI is the corporate successor to MGV Energy Inc. ("MGV"). In 2000, MGV entered into a joint venture with PanCanadian Petroleum Corp. ("PanCanadian") to explore for CBM reserves in an area of over 3 million acres of land in the Western Canadian Sedimentary Basin. In 2003, after PanCanadian amalgamated with AEC to form EnCana Corporation ("EnCana"), MGV entered into an "Asset Rationalization Agreement" with EnCana (the "2003 Agreement") that divided the assets and the rights subject to the joint venture and allowed MGV to pursue independent operations.

9. As a result of the 2003 Agreement and other agreements under which QRCI has been able to acquire additional working interests, QRCI held approximately 430,000 net acres in Alberta with the opportunity to earn in approximately 63,000 additional net acres as of December 31, 2005.

10. During 2005, QRCI drilled 483 (249.1 net) productive CBM wells and installed eight CBM facilities for processing its natural gas production. As indicated above, as of December 31, 2005, QRCI held interests in 1,685 (778.2 net) productive wells and had 305 Bcf of reserves attributable to its CBM projects in Alberta.

11. As of the beginning of this year, it was QRCI's expectation that it would drill 451 (267 net) wells and install three new CBM processing facilities during 2006. Each new facility will be capable of processing 5-10 MMcfd of natural gas production.

B. QRCI'S LEASES

12. QRCI has directly entered into over 770 individual freehold leases with lessors on lands having a split title. These leases cover lands in approximately 148 sections. In addition, through its various joint ventures, QRCI has the potential to earn in on over 66 sections of land involving split title interests. The total number of sections that QRCI has an

interest in that are impacted by the split title issue is therefore approximately 214 sections.

13. The majority of QRCI's freehold leases with individual lessors follow the basic form of the 1991 CAPL Petroleum and Natural Gas Lease with some amendments to address exploration and production practices unique to CBM. All of QRCI's PNG leases on split title lands contain language the same or virtually the same as the language contained in the Devon, Fairborne and Bearspaw leases in issue in this Proceeding. Under these leases QRCI has obtained natural gas rights by virtue of the fact that QRCI has leased "all mines and minerals except coal within, upon or under" the lands. Some of the leases also except "petroleum and valuable stone". Examples of QRCI's typical leases are attached to these submissions as Appendix "1".

14. As a result of the Board's Bulletin 2006-19, QRCI was forced to issue Notices of Force Majeure to each of its lessors having an interest in split-title lands as it is unable to drill on these lands due to its inability to obtain well licences from the EUB.

C. SIGNIFICANCE OF SPLIT-TITLE ISSUE TO QRCI

15. Resolution of the issue before the EUB in this proceeding is very important to QRCI. While the legal uncertainty surrounding the entitlement to produce CBM on freehold, split-title land has been known for some time, the objections filed by the owners of coal rights to well licence and holding applications, and the Board granting the Review and Variance Requests that have given rise to this Proceeding, have created regulatory uncertainty which is seriously impacting QRCI's ability to carry on business in Alberta.

16. As already indicated, more than 60 of QRCI's applications are being held in abeyance by the EUB or have been withheld from filing by QRCI. This number will continue to grow throughout the balance of 2006. Given that the public hearing in this proceeding is not scheduled to commence until October, it seems unlikely that there will be a decision before the end of the year. Accordingly, this regulatory uncertainty will have a

substantial adverse impact on QRCI's 2006 drilling program. Effectively, *Bulletin 2006-019* has brought the drilling program to a near stand-still.

17. QRCI has already drilled a large percentage of its Crown lands and would normally be now proceeding with development on adjacent or proximal freehold lands. Given the current regulatory uncertainty, many of these freehold lands stand in significant danger of being stranded. QRCI estimates that it has approximately 214 gross freehold sections of land on which CBM development has been delayed as a result of the current uncertain regulatory environment. QRCI's working interest across these lands varies from approximately 25% to 100%, with an estimated weighted average of 50%.

18. In addition, QRCI has developed substantial infrastructure (gathering and processing) in connection with its CBM development in Alberta. Specifically, QRCI and its partners have built gathering systems serving 12-14 townships of checkerboard Crown and freehold lands. When this system was built, additional capacity was provided for freehold development. If the freehold lands continue to be sterilized from development, QRCI will find itself in a situation of having substantially over-built its infrastructure.

III. SUBMISSIONS OF QRCI WITH RESPECT TO THE ISSUE OF LEGAL ENTITLEMENT TO PRODUCE CBM

A. JURISDICTION OF THE EUB

19. The EUB has stated (for example in its Notice of Hearing) that in Part 2 of Proceeding No. 1457147, the Board will consider "the issue of legal entitlement of coalbed methane being produced or intended to be produced" from the wells licenced to Bearspaw Petroleum Ltd. ("Bearspaw"), Devon and Fairborne.

20. It is a matter of record that the issue in this proceeding, namely the legal entitlement to produce CBM on freehold, split-title lands where the coal and natural gas rights are owned by different parties, flows from s.16 of the *Oil and Gas Conservation Act*, R.S.A. 2000, c. O-16 ("OGCA"). That is, both EnCana and Carbon Development Partnership ("CDP") have based their Review and Variance requests of the well licences in question on the assertion that Bearspaw, Devon and Fairborne have not satisfied the requirement of s.16 of the OGCA that they have the right to produce CBM on the lands in question.

21. QRCI acknowledges and takes no issues with the fact that the EUB has jurisdiction to interpret the statutes it administers, including the OGCA. More specifically, therefore, the Board has jurisdiction to interpret s.16 of the OGCA.

22. In doing so, however, the Board must not lose sight of the fact that its jurisdiction is regulatory. The Board does <u>not</u> have jurisdiction to adjudicate the property rights of two competing parties under a legal instrument such as a lease or a transfer of land. Therefore, the Board's interpretation of s.16 of the OGCA must be consistent with its role as the regulator of the oil and gas industry in Alberta and in furtherance of the purposes of the OGCA. Its role is not to settle disputes between commercial parties, nor is that one of the purposes of the OGCA.

B. QUESTION BEFORE THE EUB IN THIS PROCEEDING

23. Section 16 of the OGCA states:

> 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 to the right to drill or operate the well for the other authorized purpose, as the case may be.
>
> (2) If, after 30 days from the mailing of a notice by the Board to a licensee at the licensee's last known address, the licensee fails to prove entitlement under subsection (1) to the satisfaction of the Board, the Board may cancel the licence or suspend the licence on any terms and conditions that it may specify.

24. Clearly, the plain meaning of s.16 of the OGCA is that an applicant for a well licence is under an onus to "prove entitlement" to the right to produce oil, gas or bitumen from the applied-for well. QRCI submits, therefore, that the question before the Board in this proceeding may be framed as follows:

> *For the EUB's regulatory purposes, what must an applicant for a well licence demonstrate to satisfy the onus that it is entitled to the right to produce oil, gas or bitumen from the applied-for well?*

Or, to put it more simply:

> *What is the standard of proof under s.16 of the Act?*

25. QRCI submits that the answer to that question is that the applicant must satisfy the EUB that it has a subsisting natural gas lease. Applying any other, more stringent standard of proof would involve the Board engaging in an exercise beyond its jurisdiction.

26. Moreover, such an exercise would simply not be practical. If every time a coal owner on freehold, split-title lands objected to a well licence application submitted by the natural gas owner, the Board were to assess the competing arguments of the coal owner and the natural gas owner as to the proper interpretation of the instrument granting or reserving mineral rights with respect to CBM, the regulatory system would cease to function effectively.

27. In other words, an applicant for a well licence (or a holding or spacing order) must satisfy the EUB, on a *prima facie* basis, that it holds the rights to produce natural gas from the well and lands in question. This will be accomplished in most, if not all, cases by satisfying the Board that it holds a subsisting natural gas lease. Since CBM is natural gas (as will be discussed below), the Board will then be in a position to issue the licence or approval in question. Making further inquiries or investigations into whether the parties to the lease intended that CBM should belong to the coal owner or the owner of the natural gas would embroil the Board in issues beyond its regulatory jurisdiction such as adjudicating the respective property rights of the parties in question.

28. Thus, QRCI submits that the procedure followed by the Board in issuing the well licences under review to Devon, Fairborne and Bearspaw was proper and correct. The licences should therefore be confirmed as valid. More importantly to QRCI as an interested party, the procedure followed by the Board should be expressly validated as being the procedure the Board will follow in dealing with all pending and future CBM applications on freehold, split-title lands.

29. QRCI submits this interpretation of s.16 of the OGCA not only accords with common sense but is also consistent with relevant policy and legislation.

30. First, in the Board's Information Letter IL91-11 (which has been in force for the past 15 years), it is expressly stated that both the EUB and the provincial Department of Energy "consider CBM to be a form of natural gas".

31. Second, this statement of policy was codified in s.67(1) of the *Mines and Minerals Act*, R.S.A. 2000, c. M-17 in 2003. Section 67(1) states:

> A coal lease grants the right to the coal that is the property of the Crown in the location in accordance with the terms and conditions of the lease but subject to subsection (2), does not grant any rights to natural gas, including coalbed methane.

32. While s.67(1) of the *Mines and Minerals Act* applies only to Crown minerals, for regulatory purposes logic dictates that freehold minerals be treated in the same manner. In the context of this Proceeding, the Board's primary role is to receive, process and issue (or refuse) well licence and associated holding and spacing applications. If the holder of a Crown coal lease objected to a CBM well licence application filed by the holder of a valid natural gas lease, the position would be clear: the rights to CBM would belong to the well-licence applicant. For regulatory purposes, the situation should be no different if the coal rights are freehold.

33. Third, well licence applications must of course be submitted in accordance with the EUB's Directive 56. Section 7.9.11 of Directive 56 repeats the statutory requirement of s.16 of the OGCA that prior to submitting a well licence application an applicant must be entitled to the right to produce the oil, gas or bitumen from the well in question. It goes on to say:

> The issuance of a well licence or conducting of an EUB audit is not to be relied upon by the licencee or third parties as a legal determination of confirmation of mineral entitlement or of the right to produce hydrocarbons or to conduct activities on lands covered by the licence.

34. This confirms, it is submitted, that upon receiving well licence applications the EUB should not, for the regulatory purposes of s.16 of the OGCA, engage in the exercise of interpreting leases to determine legal entitlement to produce. Rather, the Board should simply satisfy itself that the applicant has a lease for the rights in question. If it does, and all other regulatory requirements are met, the licence should be issued.

35. The position being advocated by QRCI does not in any way constrain or prohibit coal owners such as EnCana or CDP from making arguments in the appropriate forum, namely the Courts, that in any given instance the legal instrument transferring or reserving the coal or natural gas rights was intended by the parties to convey or reserve the right to produce CBM to the coal owner. However, for regulatory purposes, the holder of a subsisting natural gas lease must be considered by the Board to be entitled to produce CBM. The only way this could not be so is if the Board were to accept that CBM is something other than natural gas.

36. QRCI submits that clearly CBM is natural gas. As stated above, this position is the same position taken by the EUB and the Department of Energy under IL91-1, now codified in s.67(1) of the *Mines and Minerals Act*. In support of this position QRCI also relies on the Joint Submission filed on behalf of the Natural Gas Rights Holders. In particular, QRCI relies on the report of Mr. Matthew J. Mavor of Tesseract Corporation filed as Attachment "A" to the Joint Submission (the "Mavor Report").

37. As stated in the Mavor Report:

- CBM is generally indistinguishable from natural gas produced from sandstone, siltstone, shale, carbonate or other rock types in both composition and economic value.

- 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.

- 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 their reservoir has been disturbed by man. CBM is a vapor that is compressed or adsorbed in porosity (void space) within the solid rock.

- From a reservoir engineering standpoint, CBM shares very similar flow characteristics through coal seams as natural gas flows through other rock types.

- The economic value of coal and CBM are distinct.

38. QRCI submits that science, policy and regulatory efficiency all lead overwhelmingly to the conclusion that CBM is natural gas. Therefore, the holder of a subsisting natural gas lease should *prima facie* be entitled to issuance by the EUB of a well licence.

IV. CONCLUSION

39. QRCI respectfully requests that the EUB deny the Review and Variance requests of EnCana and CDP. Further, QRCI requests that, in doing so, the EUB expressly confirm that henceforth CBM well licences will be issued to applicants (assuming all other regulatory requirements are met) upon them furnishing to the Board evidence that they hold subsisting natural gas leases. Finally, based on the foregoing, QRCI requests that the EUB rescind *Bulletin 2006-019* and resume processing all facilities and resources applications (and QRCI's in particular) filed in respect of freehold, split-title lands.

ALL OF WHICH IS RESPECTFULLY SUBMITTED at the City of Calgary, in the Province of Alberta, this ____ day of August, 2007.

McLENNAN ROSS LLP

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Per: Gavin S. Fitch
Solicitor for Quicksilver Resources Canada Inc.

TABLE OF CONTENTS

I. INTRODUCTION 1

II. EVIDENCE OF QUICKSILVER RESOURCES CANADA INC. ("QRCI")....................3

III. SUBMISSIONS OF QRCI WITH RESPECT TO THE ISSUE OF LEGAL ENTITLEMENT TO PRODUCE CBM..6

IV. CONCLUSION..12

ALBERTA ENERGY AND UTILITIES BOARD

IN THE MATTER OF THE *ENERGY RESOURCES CONSERVATION ACT*, R.S.A. 2000, C. E-10; AND THE *OIL AND GAS CONSERVATION ACT*, R.S.A. 2000, C. 0-6.

AND IN THE MATTER OF PART II OF PROCEEDING NO. 1457147, COALBED METHANE (CBM) REVIEW HEARING

WRITTEN SUBMISSIONS OF QUICKSILVER RESOURCES CANADA INC.

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