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April 12, 2005

Alberta Energy and Utilities Board  
640 - 5 Avenue, SW  
Calgary, AB T2P 3G4

*VIA FAX: (403) 297-4117*

Attention: Ms. Carla Giesbrecht

Dear Madam:

Re: Response to Devon Canada Corporation Supplemental Submissions

**Location: 6-8-34-26 W4M  
EUB Application No. 1383132**

**Location: 6-17-34-26 W4M  
EUB Application No. 1383138**

**Location: 8-8-34-26 W4M  
EUB Application No. 1383134**

**Location: 8-17-34-26 W4M  
EUB Application No. 1383139**

**Location: 14-8-34-26 W4M  
EUB Application No. 1383136**

**Location: 14-17-34-26 W4M  
EUB Application No. 1383140**

**Location: 16-8-34-26 W4M  
EUB Application No. 1383137**

**Location: 16-17-34-26 W4M  
EUB Application No. 1383141**

**EUB Application No. 1377141  
Application to Establish Holding**

We are in receipt of your letter of March 28, 2005 enclosing a copy of a letter dated March 21, 2005 from Mr. A.L. McLarty of the Fraser Milner Casgrain LLP firm on behalf of Devon Canada Corporation ("Devon") respecting Devon's submissions in support of Devon's right to produce coal bed methane ("CBM") (also known as natural gas from coal or "NGC") from the proposed wells subject to the captioned applications ("Devon's Applications"). We are also in receipt of a letter dated March 31, 2005 from your Ms. Barbara S. Kapel Holden extending the deadline for Luscar's response to Mr. McLarty's submissions to April 12, 2005.

Luscar will address what it believes represents the fundamental fallacy of Devon's approach, then will provide specific rebuttal to certain of Devon's claims.

Mr. McLarty's entire argument is predicated upon the assumption that Devon is only required to demonstrate a *prima facie* entitlement to produce CBM from those lands in which Devon has leasehold natural gas rights and in which Luscar owns the coal (the "Lands") to enable the Energy and Utilities Board (the "Board") to process Devon's Applications. The implication embedded within this approach is that, if Devon can demonstrate a *prima facie* entitlement, the onus should shift to Luscar to demonstrate why Devon is not entitled to produce CBM. Luscar disagrees with both the underlying premise and the implicit shift of onus.

Luscar strongly submits that the test Devon must meet is not merely a *prima facie* entitlement. Rather, it is incumbent upon Devon to establish that it has the legal right to produce CBM. The reasons for Luscar's position are set out in detail in my letter of February 18, 2005 to the Board's Ms. Lori Olijnyk. Without reiterating those submissions in detail, Luscar submits that the statutory requirements contained in Section 16(1) of the *Oil and Gas Conservation Act* require Devon to establish its right to produce the CBM. Nothing in that section or elsewhere suggests that a mere *prima facie* entitlement is sufficient. Section 16(1) was judicially considered by the Alberta Court of Appeal in *Alberta Energy Company Ltd v. Goodwell Petroleum Corporation Ltd.* (2003 ABCA 277). Although *obiter dicta*, (because the Court of Appeal found a right to have been granted by the lease in the *Goodwell* case) Fruman, J. stated (in paragraphs 92 and 93):

*"[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 license 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. While this section was in force at the time of the variation decision, a predecessor section, s. 13(1) was in force at the time of the original decision<sup>40</sup>. The earlier section is not materially different.*

*[93] Neither s. 16(1) nor its predecessor section support the Board's position. These sections will be contravened if the person who holds the well license does not possess the right to produce the hydrocarbon authorized by the well license."*

(emphasis added)

Mr. McLarty spent considerable effort to demonstrate Devon's chain of leasehold title to the conventional natural gas within the Lands. 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 produce CBM, by reason of Luscar's continued dispute of Devon's entitlement to produce CBM. Mr. McLarty expressly acknowledged at page 2 of his letter that the underlying question of ownership of NGC has yet to be judicially determined in Canada.

Unlike other disputes presently before the Board, this is not a contractual dispute respecting the interpretation of an oil and gas lease. Strictly speaking, Luscar's dispute is with the owner of the conventional natural gas, who is in turn Devon's lessor. It is the conventional

natural gas owner who did not (and does not) hold clear and recognized legal title to the CBM at the time of the granting of the leases respecting the Lands to Devon. Devon can have no better title to the CBM than did its lessor(s) of the Lands, since one cannot give better title than he himself holds. The onus is on Devon, as the applicant, to demonstrate its entitlement to produce CBM. Not only has Devon failed to meet this test, given Luscar's dispute with Devon's lessor over underlying title to the CBM, and in light of the absence of judicial authority, Devon cannot meet this test. As an aside, but on a practical matter, if the Courts ultimately determine that CBM underlying the Lands is owned by Luscar, as the coal owner, then Devon will have no legal justification, whatsoever, for a well licence to produce CBM from the Lands and, consequently, will be proscribed from continuing to hold any such well licence pursuant to s. 16(1).

In his letter, Mr. McLarty set out five "bullet" points, allegedly in support of Devon's *prima facie* entitlement to the licences which are the subject of the Devon Applications. The first two bullet points are irrelevant to any determination of ownership or entitlement to the CBM. The last three are so artificially narrowed as to be rendered misleading, if not meaningless.

#### **Response to Bullet Point 1:**

The methane component within CBM may or may not be distinguishable from the methane component of conventional natural gas. However, it is Luscar's understanding that, without the coal, there would be no CBM. Therefore, unlike conventional natural gas, in which natural gas often migrates away from the source "rock", CBM remains locked in, and associated with, the "source", being the coal itself. The vast majority of CBM is sorbed within the coal itself (chemically bonded and retained by pressure) or is held in cleats in the coal. A small percentage of the CBM may also be dissolved in water in the cleats. While the chemical composition of methane is not likely relevant to ownership, its continued association with the coal as "source rock" is relevant and, in fact, supportive of Luscar's position as owner.

#### **Response to Bullet Point 2:**

Technology employed relating to the recovery of the substance is absolutely irrelevant to any consideration of entitlement to produce that substance. By way of example, open pit mining, involving draglines or excavators and trucks, is utilized with respect to any number of base or precious metals mining operations or hydrocarbons, such as coal and unprocessed bitumen. It would be impossible to ascertain, simply on the basis of commonality of technology used in recovering these substances, what substance was being pursued, let alone attempting to conclude from this fact who owned the underlying substances.

Further, no conclusion can be drawn from the fact that the Board is the regulatory agency charged with administering both conventional natural gas and CBM. The Board holds a broad mandate to administer all energy resources within the Province of Alberta.

**Response to Bullet Point 3:**

It is an oversimplification to state, as has Mr. McLarty, that the American courts have "generally" come to the conclusion that coal means the solid substance and not the associated gas in the coal. Without going into an extensive listing of cases, U.S. courts have also determined that "coal" includes the CBM (eg. *United States Steel Corp v. Hoge* (1983) 468 A.2d 1380 (Pa. S.C.); *NCNB Texas National Bank v. West* (1993) 631 So. 2d 212 (Ala. S.C.)), based on the ownership theories applicable in the states in which the cases were heard. American theories of property ownership of fugacious minerals differ from those applicable to western Canada, thereby severely limiting the applicability of any American jurisprudence to the present issue. In any event, American cases are only persuasive in Canadian courts and are not binding.

**Response to Bullet Points 4 and 5:**

Luscar acknowledges that the vernacular meaning of coal, as well as the intention of the parties to a transfer of property rights (whether or not including coal) and whether or not a reservation of rights or an exclusion of rights from a grant are relevant considerations in the determination of property rights. However, these are not the only relevant considerations and Luscar objects to Devon's implication that these matters would be determinative, in and of themselves.

In specific response to the last sentence of Bullet Point 5, Luscar agrees that there is no indication in any of the title documents before the Board to suggest any intent to reserve to the coal owner the right to the gas in the coal. However, there is no evidence before the Board as to the chain of title to either the coal or the conventional natural gas, other than Luscar's coal titles to the Lands. There is certainly no evidence supportive of either position as to the intention of the relevant parties at the time the title to the coal underlying the Lands was separated from the balance of the mines and minerals. With respect, it is therefore disingenuous to imply that the Board should conclude that the lack of any evidence whatsoever means a lack of intention to reserve CBM to the coal owner. Luscar has not placed any such evidence on the record because it does not believe that the Board is the appropriate forum to determine property rights as between Luscar and Devon's lessor (and, consequently, between Luscar and Devon).

The balance of Mr. McLarty's letter addresses issues of prejudice and the balance of interests between Devon and Luscar. These issues would be relevant in an injunction application, not in an application for well licences and for the establishment of holdings. However, for the record, Luscar would be prejudiced should the Board grant Devon the applied-for well licences and the Courts ultimately determine Luscar's ownership of the CBM underlying the Lands. The bundle of property rights affected includes, among others, the rights to determine when and by whom resources are to be developed and how many wells and other capital facilities are optimally required. In the event of a court determination in its favour, Luscar's rights of recovery against Devon may well be subject to recognition of capital expended by Devon. That capital will, in all likelihood, vary from the capital Luscar itself may have chosen to expend to recover its resource, to Luscar's detriment.

Luscar respectfully submits that the Board lacks the jurisdiction to make determinations as to the respective property rights of Devon, as lessee from the conventional natural gas owner underlying the Lands, and Luscar, as owner of the coal rights underlying the lands. As such, the Board is not the appropriate forum for the determination of underlying property rights. As has been previously stated, it has been, and remains, open to Devon to pursue its claim for a determination of ownership rights through the courts. With respect, it is specious to suggest that Luscar is somehow attempting to forestall legitimate development of CBM by simply asserting that it is incumbent upon Devon to fulfil all statutory prerequisites to demonstrate its legal right to produce CBM before applying for well licences. Contrary to Mr. McLarty's summary, Luscar has and continues to dispute Devon's entitlement to produce CBM from the Lands. Luscar respectfully requests that the Board postpone Devon's applications until such time as Devon has met its statutory obligation to establish its right to produce the hydrocarbon substance that it has applied to produce.

Should you have any questions concerning this letter, please do not hesitate to contact the writer.

Yours very truly,

Luscar Ltd.

Per:

  
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