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## The Land Tenure System in the Newfoundland and Labrador Offshore Regulatory Regime: Review, Analysis and Current Issues

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Nicholas Crosbie\*\*

The Land Tenure System in the  
Newfoundland and Labrador  
Offshore Regulatory Regime:  
Review, Analysis and Current  
Issues

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*The development of an offshore oil and gas industry in the Gulf of St. Lawrence has created, for the first time, the potential for interactions between the Newfoundland and Labrador offshore regulatory regime and other regimes (either the new regime in Quebec or the National Energy Board). As industry participants evaluate where they will spend their exploration dollars, they will need to understand the various regulatory regimes in place. Land tenure in Newfoundland and Labrador is similar to the regime in places subject to the jurisdiction of the National Energy Board. Over the past 25 years, however, the decisions of the courts and the guidelines and policies of the Canada–Newfoundland and Labrador Offshore Petroleum Board have given rise to a unique regulatory regime. This paper describes the Newfoundland and Labrador offshore regulatory regime. The types of interests that are available are identified and described. Finally, two current issues in respect to land tenure are identified and discussed.*

*Le développement d'une industrie des hydrocarbures extracôtière dans le golfe du Saint-Laurent a apporté, pour la première fois, la possibilité d'interactions entre le régime réglementaire de la région extracôtière de Terre-Neuve-et-Labrador et d'autres régimes (le nouveau régime en vigueur au Québec ou l'Office national de l'énergie). À mesure que les joueurs de l'industrie déterminent où ils dépenseront les fonds consacrés à l'exploration, ils devront apprendre à connaître les divers régimes réglementaires en place. Le régime de tenure foncière à Terre-Neuve-et-Labrador est similaire au régime en vigueur dans les provinces qui relèvent de l'Office national de l'énergie. Au cours des 25 dernières années, cependant, les décisions des tribunaux ainsi que les lignes directrices et les politiques de l'Office Canada–Terre-Neuve-et-Labrador des hydrocarbures extracôtiers ont donné naissance à un régime réglementaire unique. Cet article décrit le régime réglementaire extracôtier de Terre-Neuve-et-Labrador. Les types d'intérêts qui sont offerts sont définis et décrits. Enfin, les auteurs cernent deux questions actuelles concernant la tenure foncière et en discute.*

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### *Introduction*

This paper provides a survey of the oil and gas interest regime in the offshore industry off the coast of Newfoundland and Labrador, concentrating on describing the process and legal tests surrounding the issuance of Exploration Licences, Significant Discovery Licences, Commercial Discovery Licences, and Production Licences. The various approvals and authorizations that are necessary in order to carry on activities in the offshore area are not canvassed in this paper.

The examination which follows is divided into four sections. The introduction provides a background and history of the offshore regulatory environment. Part I describes in detail the application process, legal requirements, and rights that are applicable to each form of land tenure—Exploration Licence, Significant Discovery Licence, Commercial Discovery Declarations, and Production Licence. Part II discusses two current issues with respect to land tenure in the offshore area: stratigraphic ownership and protection of data. Finally, a brief conclusion is offered.

#### 1. *Background and history*

##### a. *Oil and gas industry in offshore Newfoundland and Labrador*

The history of the oil and gas industry in offshore Newfoundland and Labrador dates back over fifty years, when the first wells were drilled in the 1960s. Most of the offshore activity, however, has been concentrated in the past fifteen years, with the first oil being produced in 1997. Interest in Newfoundland and Labrador offshore oil increased dramatically in the 1970s along with increases in oil prices, which led to an increase in exploratory drilling. As the exploration continued and large oil field discoveries were made (such as the Hibernia oil field in 1979), it became apparent that there were opposing views on who controlled the oil off the coast of Newfoundland and Labrador; the federal or provincial government.

The 1980s were marked by conflict and legal battles between the federal and provincial governments, beginning with the Government of Canada introducing its National Energy Program (NEP) in 1980, which outlined a desire to have the Supreme Court of Canada determine the question of offshore oil ownership.<sup>1</sup> After a number of years of negotiations between the federal and provincial governments, the *Canada–Newfoundland Atlantic Accord (Atlantic Accord)* was signed in 1985, establishing a joint

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1. John C Crosbie, "Overview Paper on the 1985 Canada–Newfoundland Atlantic Accord," (2003), online: Government of Newfoundland and Labrador <<http://www.gov.nl.ca/publicat/royalcomm/research/Crosbie.pdf>> at 261 [J. Crosbie Paper].

management system to be regulated by the Canada–Newfoundland and Labrador Offshore Petroleum Board (the Board).

After the battle between the provincial and federal governments was over, the second half of the 1980s involved deliberations between the provincial government and oil companies. At this time, the price of oil had declined significantly, meaning less profit for oil companies interested in offshore production. An agreement was reached between the provincial and federal governments and the oil companies in 1990, with “the government agree[ing] to give developers \$1 billion in grants and \$1.7 billion in loan guarantees...” as well as the oil companies agreeing to implement a gravity based system (GBS) for the Hibernia development, which would create more jobs in the province as compared to other less expensive modes of development.<sup>2</sup>

Since then, the offshore oil industry in Newfoundland and Labrador has been progressing at a quick pace. Production of oil began from the Hibernia oil field in 1997, the Terra Nova oil field in 2002, and White Rose field in 2005. Both Terra Nova and White Rose are being produced with a Floating, Production, Storage and Off-Loading vessel. Since production began, in 1997, these three oil fields have produced a total of 194.4 million cubic meters of oil (as of 30 April 2011).<sup>3</sup> Currently, the Hebron oil field project is in the development phase with a projected production date of 2017 using a GBS production platform, as well there are potential expansion projects from both White Rose and Hibernia.

b. *Regulatory background*

Canada Oil and Gas Operations Act

The *Canada Oil and Gas Operations Act*<sup>4</sup> applies to exploration, drilling and production of oil and gas in any submarine areas that are not within a province.<sup>5</sup> The stated purpose of the *Oil and Gas Act* is to promote safety, protection of the environment, conservation of resources, joint production arrangements, and economically efficient infrastructures.<sup>6</sup> The *Oil and Gas Act* gives powers to the National Energy Board (NEB) to issue operating licenses, prescribe requirements for operating licenses and

2. Leah Fusco, “Offshore Oil: An Overview of Development in Newfoundland and Labrador” online: Memorial University of Newfoundland <<http://www.ucs.mun.ca/~oilpower/documents/NL%20oil%207-25-1.pdf>> at 4.

3. Canada–Newfoundland and Labrador Offshore Petroleum Board, “Cumulative Production-Offshore Newfoundland,” online: Canada–Newfoundland Offshore Petroleum Board <[http://www.cnlopb.nl.ca/pdfs/off\\_prod.pdf](http://www.cnlopb.nl.ca/pdfs/off_prod.pdf)>.

4. *Canada Oil and Gas Operations Act*, RSC, 1985, c O-7 [*Oil and Gas Act*].

5. *Ibid*, s 3(b).

6. *Ibid*, s 2.1(a)–(e).

suspension and revocation privileges. The *Oil and Gas Act* also governs the Oil and Gas Administration Advisory Council, the Offshore Oil and Gas Training Standards Advisory Board, and the Oil and Gas Committee. There are several regulations made pursuant to the *Oil and Gas Act* that regulate drilling, production, diving, installations, conservation, and other administrative matters.

#### Accord Act

The *Canada–Newfoundland Atlantic Accord* is an agreement for offshore petroleum resource management and revenue sharing between the Government of Canada and the Government of Newfoundland and Labrador. Discussions surrounding sharing of offshore revenues between Canada and the provinces began in the 1960s, encouraged by the British Columbia Offshore Reference from the Supreme Court of Canada in 1967 that found “Canada was entitled to the proprietary...rights in areas offshore from the historic...” limits of the province.<sup>7</sup> In 1982, Canada made a proposal to Newfoundland that was similar to an agreement on offshore oil and gas resource management and revenue sharing made in 1982 with Nova Scotia.<sup>8</sup> An agreement was finally reached in 1985, which is implemented through the *Canada–Newfoundland Atlantic Accord Implementation Act* and the mirror legislation in the province<sup>9</sup> (the *Accord Act*).

The *Accord Act* consists of seven parts, including joint management, petroleum resources, petroleum operations, revenue sharing, fiscal equalization offset payments, offshore development fund, corporate income tax and transitional, consequential and commencement provisions. Most notably, the *Accord Act* contains provisions for the creation, operation, and regulatory activities of the Board, the payment of royalties (as would be payable under the *Petroleum and Natural Gas Act*<sup>10</sup> if produced within the Province), as well as a method by which to calculate equalization offset payments to be paid to the Province. These equalization provisions were structured to allow Newfoundland to catch up to the rest of Canada, economically and socially.

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7. J. Crosbie Paper, *supra* note 1 at 259, referring to *Reference Re: Offshore Mineral Rights*, [1967] SCR 792.

8. J. Crosbie Paper, *supra* note 1 at 261.

9. *Canada–Newfoundland Atlantic Accord Implementation Act*, SC 1987, c 3 [*Accord Act*]; see also *Canada–Newfoundland and Labrador Atlantic Accord Implementation Newfoundland and Labrador Act*, RSNL 1990, c C-2 [*NL Act*]; for convenience, the federal legislation is used here.

10. *Petroleum and Natural Gas Act*, RSNL, 1990, c P-10.

## 2. Regulatory regime

### a. Accord Act

The *Accord Act* regulates oil and gas discoveries in the offshore area. This includes outlining the operation of the land tenure process, generally. The *Accord Act* empowers the Board to issue interests, exploration licenses, significant discovery licenses, drilling orders, development orders, and production licenses.

There are several sets of regulations pursuant to the *Accord Act* relating to land tenure or interests in the offshore industry, including the *Newfoundland Offshore Area Registration Regulations*.<sup>11</sup> The *Registration Regulations* delegate the responsibility of registering and maintaining records of interests and instruments with respect to the offshore area to the registrar, who maintains these records at the office of the registrar. The *Accord Act* also sets out regulations under the *Newfoundland and Labrador Offshore Area Line Regulations*,<sup>12</sup> which establish the boundaries of the offshore area that are subject to the *Accord Act*.

### b. Federal legislation

The *Oil and Gas Act* regulates the issuance and content of operating licenses for offshore producers. These operating licenses are subject to requirements set by the NEB and are valid until the thirty-first day of March proceeding the day the license was issued, and may be renewed successively for periods of one year each.<sup>13</sup> The *Oil and Gas Act* also gives power to the Governor in Council to make broad regulations including “[e]xploration and drilling for, and the production, processing and transportation of, oil or gas in any area to which this Act applies and works and activities related to such exploration, drilling, production, processing and transportation.”<sup>14</sup> Specific requirements for operating licenses are outlined in the *Canada Oil and Gas Operations Regulations*,<sup>15</sup> and include that the applicant be an individual who is over the age of 18 or a corporation entitled to carry on business in any province.<sup>16</sup>

The *Canada Oil and Gas Land Regulations*<sup>17</sup> are regulations under the *Federal Real Property and Federal Immovables Act*,<sup>18</sup> as well as the

11. SOR/88-263 [*Registration Regulations*].

12. SOR/2003-192 [*Line Regulations*].

13. *Oil and Gas Act*, *supra* note 4, ss 5(2), 5(3).

14. *Ibid*, s 14(b).

15. SOR/83-149.

16. *Ibid*, s 3(1)(a), (c).

17. *Canada Oil and Gas Land Regulations*, CRC, c 1518 [*Land Regulations*].

18. *Federal Real Property and Federal Immovables Act*, SC 1991, c 50.

*Territorial Lands Act*<sup>19</sup> that apply to Canadian lands under the control, management or administration of the Minister of Energy, Mines and Resources. The *Land Regulations* outline a process for licensing, exploration agreements and permits, as well as oil and gas leases.

c. *Provincial legislation*

Generally, federal legislation applies to the offshore area, except when explicitly stated in the *Accord Act*. Newfoundland social legislation (as defined in section 152(1) of the *Accord Act*) applies pursuant to section 152(2) of the *Accord Act*, which states that “Newfoundland social legislation and regulations...apply on any marine installation or structure that is within the offshore area in connection with the exploration or drilling for or the production, conservation or processing of petroleum within the offshore area.”<sup>20</sup> Provincial social legislation includes health and safety legislation, workers’ compensation legislation, and labour standards legislation, as discussed below.

3. *Regulators*

The Canada–Newfoundland and Labrador Offshore Petroleum Board is a joint regulatory body created by the 1986 *Atlantic Accord* that is responsible for petroleum resource management in the Newfoundland and Labrador offshore area. The mandate of the Board is to apply the provisions of the *Atlantic Accord* to operators in the offshore area, as well as ensuring operator compliance with these provisions. The Board is comprised of seven members; three members each are appointed by each of the provincial and federal governments, and the seventh member, the Chief Executive Officer and chair of the board are jointly appointed by the two governments.

The Board regulates exploration licenses, significant discovery licenses and production licenses for an area of over 185 million hectares, which is the “offshore area” as defined in the *Accord Act* (the Offshore Area). The Offshore Area is divided into two sections, the northeast Grand Banks region, and the remainder of the offshore area (frequently subdivided for convenience as the Labrador region and West Coast region). Terms of the interest available are different in the two areas.

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19. *Territorial Lands Act*, RSC 1985, c T-7 [TSL].

20. *Accord Act*, *supra* note 9, s 152(2).



I. *Review of land tenure regime*

1. *A note on terms*

The Board has the authority under the *Accord Act* to issue “interests,” which are defined to mean exploration licences, significant discovery licences, Production licences, and predecessor licences issued under earlier legislation.<sup>21</sup> The *Accord Act* further permits that interests may be subdivided into shares, which shares are: (i) an undivided share in the entire interest; or (ii) a divided share of an exploration licence, “[h]eld with respect to a portion...of...the exploration licence” (i.e. one or more sections of land which form part of a licence).<sup>22</sup> A reference to an interest owner refers to the person(s) who owns all of the interest (or all of the shares of the interest) whereas an interest holder refers to a person who holds either an “interest or a share of an interest” (and therefore does not necessarily own an entire interest).<sup>23</sup>

2. *Exploration licence*

a. *Application process*

The *Accord Act* stipulates at section 58 that prior to the issuance of an Exploration Licence (EL), the Board must first issue a call for bids (a Call for Bids).<sup>24</sup> The Board has adopted a practice whereby it establishes which lands it will offer by way of a Call for Bids by issuing a call for nominations<sup>25</sup> (a Call for Nominations) in which interested parties are invited to nominate lands for inclusion in a future Call for Bids. The Call for Nominations procedure is an internal procedure of the Board and has no statutory basis. The Board is not bound to issue any lands contained in a Call for Nominations, and may also issue lands in a Call for Bids that were not suggested in a Call for Nominations. Essentially, a Call for Nominations is an opportunity for industry participants to identify areas where they would be interested in engaging in exploration.

In its standard form Call for Nominations, the Board encourages industry participants to submit technical information and data for consideration with respect to the prospectivity of the nominated lands. Once it has received and reviewed any Calls for Nomination that it has received, the Board then determines which portions of the offshore area

21. *Ibid*, s 47(1)(j).

22. *Ibid*, ss 47(1)(m), 66.

23. *Ibid*, s 47.

24. *Ibid*, s 58(1).

25. See Board website: <[www.cnlopb.nl.ca](http://www.cnlopb.nl.ca)>. The 2010 call for nominations is available online: <<http://www.cnlopb.nl.ca/new/pdfs/cfn2010.pdf>>.

it will offer to industry participants pursuant to a series of Calls for Bids. There are two types of bids: cash bids, and work expenditure bids. The Call for Bids will specify which type of bid is acceptable for the particular lands.<sup>26</sup> Typically, a cash bid is used where a Significant Discovery Licence (see below) will be issued rather than an EL (which occurs when the lands subject to the Call for Bids is already subject to a Significant Discovery Declaration). A work expenditure bid is an agreement to spend a certain amount of money over the course of a specified period of time engaged in a series of pre-determined exploration activities. A work expenditure bid of \$10 million is a commitment to spend at least \$10 million over the next seven years engaged in exploration activities with respect to the land subject to the Call for Bids.

The lands that the Board identifies for inclusion in a Call for Bids is subject to approval by both provincial and federal governments under the fundamental decision framework found in sections 31–40 of the *Accord Act*.<sup>27</sup> Once both levels of government have agreed upon the lands, the Board issues the Call for Bids.

The Call for Bids procedure is a regimented process set out in the *Accord Act*. Pursuant to section 58(4) of the *Accord Act*, a Call for Bids must specify:

- (a) the interest to be issued and the portions of the offshore area to which the interest is to apply;
- (b) where applicable, the geological formations and substances to which the interest is to apply;
- (c) the other terms and conditions subject to which the interest is to be issued;
- (d) terms and conditions that a bid shall satisfy to be considered by the board;
- (e) the form and manner in which a bid is to be submitted;
- (f) subject to subsection (5), the closing date for the submission of bids; and
- (g) the sole criterion that the board will apply in assessing bids submitted in response to the call.<sup>28</sup>

26. For an example of a work expenditure bid, see the 2011 Call for Bids CFB 11-01, Section 3.3, online: <[www.cnlopb.nl.ca/news/pdfs/cfb11\\_01.pdf](http://www.cnlopb.nl.ca/news/pdfs/cfb11_01.pdf)> [CFB 11-01]. For an example of a cash bid, see Call for Bids 10-03 Section 3.3, available online: <[www.cnlopb.nl.ca/news/pdfs/cfb10\\_03.pdf](http://www.cnlopb.nl.ca/news/pdfs/cfb10_03.pdf)> [CFB 10-03]. CFB 10-03 was a call for bids to issue an SDL as the lands were already subject to an SDD (Mizzen O-16).

27. *Accord Act*, *supra* note 9, s 56(2).

28. *Accord Act*, *ibid*, s 58(4).

The Board has adopted a standard form of Call for Bids.<sup>29</sup> The Call for Bids will identify the sections of land to which the call will apply. A Call for Bids will apply to all of the geological formations on the lands and equally apply to all hydrocarbons found on those lands. It is the Board's standard practice to attach to the Call for Bids a sample form of EL and Significant Discovery Licence to the Call for Bids.<sup>30</sup> The sole criterion that the Board uses in awarding compliant bids is price.

Furthermore, once it has issued a Call for Bids containing the information set out in the *Accord Act*, the Board must then only issue an EL to a party that: (a) satisfies the terms and conditions of the call and who has submitted in the specified form and manner in the call; and (b) is selected on the basis of the criterion set out in the call.<sup>31</sup> Once a successful bidder has emerged, the "terms and conditions of the interest shall be substantially consistent with [the] terms and conditions in respect of the interest..."<sup>32</sup> defined in the Call for Bids. As a result of the inclusion of a form of EL, the Board is statutorily bound to issue the EL "substantially consistent" with the draft form of EL found in the Call for Bids.<sup>33</sup>

b. *Terms of exploration licence*

Section 68 of the *Accord Act* allows the Board (with approval of the provincial and federal governments, and the consent of the interest owners) to establish the terms and conditions of exploration licences, provided that the EL must contain any terms and conditions proscribed by regulation.<sup>34</sup> The Board's current practice is to issue ELs on the terms and conditions set out in the Call for Bids. By making a bid pursuant to the Call for Bids, the interest owners are agreeing before they submit a bid to consent to the terms and conditions set out in the draft form of EL.

ELs are currently for a period of nine years, consisting of two periods, Period I and Period II. Period I commences on the effective date of the EL and runs for five or six years, extendable for an additional year upon the payment of a Drilling Deposit (typically \$1 million). Recently, the Board has provided interest owners an option with respect to the Drilling Deposit: make a \$1 million deposit and forfeit one half of the lands subject

29. For an example of the standard form call for bids, see Call for Bids 11-01, *supra* note 26.

30. See CFB 11-01, *ibid* for an example of a Call for Bids with a sample EL and SDL.

31. See *Accord Act*, *supra* note 9, s 59(1).

32. *Ibid*, s 59(3).

33. *Ibid*, s 59(3). As the draft terms and conditions of the interest are contained in the Call for Bids, and the Board is obliged to issue an interest that arises from a Call for Bids upon terms and conditions "substantially consistent" with those contained in the Call for Bids, the Board becomes bound by the terms it sets out in the Call for Bids.

34. *Ibid*, s 66(1).

to the EL, or make a \$5 million Drilling Deposit without forfeiting any lands.<sup>35</sup> The Drilling Deposit will be returned if the EL is eventually validated. Period II begins once the EL has been validated and runs until the end of the ninth year. In order to validate an EL, “the drilling of a well must be commenced within Period I and diligently pursued to termination in accordance with good oilfield practice.”<sup>36</sup> Furthermore, the validation well must “adequately test a valid geological target to be declared to the Board by the interest owner prior to the commencement of the well.”<sup>37</sup> As a best practice, interest holders are advised to declare as many valid geological targets as possible to avoid the situation where well control issues prevent the validation well from reaching the main target. With the dearth of drilling rigs available off the Canada’s Atlantic Coast, the five or six year drilling commitment is a significant constraint on interest holders. Any interest that is not validated by the end of the nine year period reverts to the Crown and is potentially subject to inclusion in a new Exploration Licence in the future.

The Board also requires that the interest holders supply the Board with a security deposit in the amount of 25% of the work expenditure commitment. During Period I, the security deposit is credited back to the interest holders at a rate equal to 25% of the allowable expenses (which are the expenses that count towards the work expenditure commitment) incurred during the period. Beginning in Period II, the interest holders are required to pay rentals on the lands subject to the Exploration Licence. Rental rates begin at \$5.00 per hectare for the first year, and rise to \$7.50 for the second year and \$10.00 for the third year and every year thereafter. Exploration Licence EL-1124, for instance, covers 125,421 hectares of land; as such, a rental payment would range from \$600,000 to \$1.2 million per year.

ELs are subject to a number of other standard terms. Interest holders agree, pursuant to the EL, to be liable “under the provisions of this Licence, the Act and the Regulations for all claims, demands, losses, costs, damages, actions, suits or other proceedings, in respect of any work or activity conducted, or caused to be conducted, by, through, or under, or with the consent of the interest holder.”<sup>38</sup> Furthermore, the interest

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35. See Exploration Licence Abstract EL-1124, Section 7, issued 15 January 2011 to Statoil Canada Ltd. and Husky Oil Operations Limited, online: Canada-Newfoundland and Labrador Offshore Petroleum Board <<http://www.cnlopb.nl.ca/abstract/el1124.shtml>> [EL-1124].

36. *Ibid.*, s 5(4).

37. *Ibid.*, s 5(5).

38. *Ibid.*, s 13(1).

holders agree to indemnify the Board, and both the provincial and federal governments for any claims.<sup>39</sup>

c. *Substantive rights*

Section 65 of the *Accord Act* provides that an EL provides the licence holder with:

- (a) the right to explore for, and the exclusive right to drill and test for, petroleum;
- (b) the exclusive right to develop those portions of the offshore area in order to produce petroleum; and
- (c) the exclusive right, subject to compliance with the other provisions of this Part, to obtain a production licence.

Typically, the short time periods for which ELs are valid (7–9 years) means that in the event that an interest holder makes a discovery that may prove to be commercial, the interest holder is not in a position to avail itself of the option to acquire a Production Licence during the term of the EL. The scarcity of drilling rigs, along with the long lead time necessary to explore in the offshore area means that even nine years is often insufficient time to plan and execute an exploration program and then plan and execute a development program. Instead, the interest holder will apply to the Board to have a Significant Discovery Declaration and eventually a Significant Discovery Licence issued for all or part of the area subject to the Exploration Licence.

3. *Significant discovery licence*

a. *Introduction*

Once an operator has carried out drilling under an exploration licence, the results of the drilling and other work undertaken pursuant to the exploration licence may warrant an application to the Board by the interest holders of the EL for a declaration of significant discovery. This process is set out in sections 71–75 of the *Accord Act*. The process involves two steps: first, an interest holder makes an application to the Board for a Significant Discovery Declaration (SDD), and second, once the SDD has been issued, the interest holder makes an application to the Board for the issuance of a Significant Discovery Licence (SDL). The first step involves a detailed analysis by the Board of the technical information submitted by the interest holder, while the second step is an administrative step that occurs once the SDD is issued and the interest holders have made the

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39. *Ibid*, s 13(1).

application in the required form. The SDD, which is based on the technical information provided by the interest holder, may easily extend beyond the boundaries of the land held by the interest holder into Crown Reserve areas or lands held by other interest holders. The SDL application covers only those portions of the SDD that are held by the interest holder(s) making the application.

The threshold issue for the issuance of a SDL is that the interest holders must demonstrate the existence of hydrocarbons by the drilling of a well and flow testing the well to the surface. The advantage for an interest holder of a SDL rather than an EL (or even commercial discovery licence or Production Licence) is that the SDL is for an unlimited duration. While SDLs are now being issued subject to conditions (as further discussed below), traditionally interest holders of SDLs were subject to minimal fees or further financial commitments.

b. *Application process*

As noted above, the application process for the issuance of an SDL is a two-step process: first an application is made to the Board for an SDD, and secondly, an application is made to the Board for an SDL. Guidance from the Board indicates that the process for the application of both an SDD and an SDL typically takes six months.<sup>40</sup> The threshold testing stage takes place at the application for a SDD. In addition to a thorough technical review, the SDD application can also include a hearing held by the Board and a second hearing held by the Oil & Gas Committee. In contrast, the process by which an interest holder is issued an SDL is relatively straightforward.

The Board is authorized pursuant to section 71(1) and section 47(1)(l) of the *Accord Act* to develop its own guidelines setting out the “form and manner” of the application for a SDD. The Board’s guidelines with respect to the process of making an application for a SDD can be found in the Joint Guidelines Regarding Applications for Significant or Commercial Discovery Declarations and Amendments.

*Application process—SDD*

Once an applicant informs the Board of its intention to apply for an SDD, the Chief Executive Officer of the Board (who is also the Chair appointed jointly by the provincial and federal governments) appoints Board

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40. Canada–Newfoundland and Labrador Offshore Petroleum Board and Canada–Nova Scotia Offshore Petroleum Board, *Joint Guidelines Regarding Applications for Significant or Commercial Discovery Declarations and Amendments* (2003), online: Canada–Newfoundland Offshore Petroleum Board <[http://www.cnlopb.nl.ca/pdfs/guidelines/sda\\_0503.pdf](http://www.cnlopb.nl.ca/pdfs/guidelines/sda_0503.pdf)> at 8 [SDA Guidelines].

employees to act as Board representatives with respect to the application. The Board representatives include legal and technical advisors.

The Board's representatives will commence a preliminary technical review upon receipt of a completed application. The preliminary technical review consists of a series of meetings between the Board's technical and legal representatives and the interest owner's corresponding employees. Once the Board's representatives have completed the preliminary technical review, they provide the Board's Chair/CEO with a report and recommendation. On the basis of this report and recommendation, the Board's Chair/CEO will either: (i) determine that there are no substantive issues and recommend that an SDD be issued; or (ii) determine that one or more substantive issues have arisen and a hearing is necessary.

In the event that no substantive issues are identified and the Board's Chair/CEO recommends the issuance of an SDD, a notice of proposed decision<sup>41</sup> is sent to all parties that "the board considers to be directly affected by the proposed [SDD]."<sup>42</sup> While the definition of "directly affected" does not appear to have been judicially considered in Newfoundland and Labrador or Nova Scotia (where a similar term applies<sup>43</sup>), in practice, the parties that the Board considers to be directly affected are all interest holders in lands subject to the SDD and all interest holders in lands adjacent to the SDD.

In the event that the Board has identified what it considers to be substantive issues, the Board's Chair/CEO will recommend that the application be the subject of a Board hearing before a Board Review Panel. The Board Review Panel typically consists of all of the Board members, but may be comprised of less than all of the Board members.<sup>44</sup> The Review Panel process is somewhat problematic from an administrative law process as the organization tasked with making the decision (the Board) is the same organization tasked with advocating for one side of the decision. The applicant presents its evidence via its experts to make the case why it is entitled to an SDD in accordance with its application. Rebuttal of the applicant's case is made by the Board representatives (i.e. the technical and legal advisors appointed by the Board to conduct the preliminary technical review). Chairing the process is the Chair/CEO of the Board,

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41. *Ibid* at 9.

42. *Accord Act*, *supra* note 9, s 124(2). As section 71(1) is expressed to be subject to section 124, the Oil & Gas Committee review process is applicable to the decision to issue an SDD.

43. *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation (Nova Scotia) Act*, SNS 1987, c 3, s 126(2).

44. SDA Guidelines, *supra* note 40 at 4.

who has previously determined that the application gives rise to sufficient substantial issues to warrant a Review Panel.

*Oil & gas committee*

Once the Board's Review Panel has made its determination, the Board issues a notice of proposed decision to all parties it considers to be "directly affected." Either the applicant or any party that is "directly affected" may seek to have the proposed decision reviewed by the "Oil and Gas Committee." The Oil and Gas Committee is established pursuant to section 141 of the *Accord Act* and is comprised of "[five] members, not more than [three] of whom may be [Crown] employees."<sup>45</sup> Members and employees of the Board are prohibited from serving on the Oil & Gas Committee,<sup>46</sup> and individuals with significant interests in the Canadian oil and gas industry do have a right to vote.<sup>47</sup> Finally, at least two members of the Oil & Gas Committee shall "appear to the board to have specialized, expert or technical knowledge of petroleum."<sup>48</sup>

The purpose and role of the Oil & Gas Committee were considered at length by the Supreme Court of Canada (SCC) in *Mobil Oil Canada Ltd. v. Canada–Newfoundland Offshore Petroleum Board*.<sup>49</sup> In that case, the SCC considered whether the Board is required to refer an SDD application to the Oil & Gas Committee at the request of the applicant. The SCC found that as a general principle, matters of a technical nature must be referred to the Oil & Gas Committee when so requested by the applicant. The Board has the residual authority to decide non-technical matters without reference to the Oil & Gas Committee.<sup>50</sup> As an independent organization consisting of subject matter experts, the Oil & Gas Committee is also afforded a significant amount of deference. Findings of the Oil & Gas Committee with respect to matters of fact within its jurisdiction are "binding and conclusive."<sup>51</sup> Furthermore, in considering the role of the Oil & Gas Committee in the Mobil Nautilus Case, the SCC stated:

35. The involvement of the Committee in respect of technical decisions is clearly intended by the offshore scheme. As already noted, one purpose of the Atlantic Accord was "to provide for a stable and fair offshore management regime for industry"

45. *Accord Act*, *supra* note 9, s 141.

46. *Ibid*, s 142(2).

47. *Ibid*, s 143.

48. *Ibid*, s 142(1).

49. *Mobil Oil Canada Ltd v Canada–Newfoundland Offshore Petroleum Board*, [1994] 1 SCR 202 [*Mobil Nautilus Case*].

50. *Ibid* at para 39.

51. *Accord Act*, *supra* note 9, s 145(3).



(clause 2(f), emphasis added). The most significant recognition of this purpose has also already been described, inasmuch as the ministerial discretion which governed SDDs under s. 44(1) of the Canada Oil and Gas Act was replaced by s. 71(1) and a procedure which compels the objective reasonableness of declarations.

37. Without reviewing s. 124 of the Implementation Act in great detail, it is clear that it permits a significant inquiry into whether "reasonable grounds" for an SDD exist for the purposes of s. 71(1). The procedural protections found in that provision go some distance toward ensuring that interest holders have ample opportunity to prove an entitlement objectively before the Committee. The Board must consider the recommendations of the Committee (s. 124(7)), and this must have a significant impact on the Board's ability to determine whether "reasonable grounds" exist to support an SDD under s. 71(1).
38. The language of s. 71 is clear with respect to Committee involvement. In ss. 71(1), (2) and (4), the phrase "subject to section 124" indicates that SDD decisions by the Board which involve technical considerations presuppose the potential involvement of the Committee. To the extent that the SDD process is initiated by the interest holder, e.g., in a s. 71(1) application, automatic reference to the Committee will be qualified to the extent that a Committee hearing must be requested by the applicant whose interests are at stake. It is interesting to note that when Mr. Jack Shields (then Parliamentary Secretary to the Minister of Energy, Mines and Resources) reintroduced Bill C-6 to Parliament following the Legislative Committee reference, he stated that the Committee's main function was a review function initiated "at the request of an interest holder" (House of Commons Debates, 2nd Sess., 33rd Parl., 2 March 1987, at p. 3707).<sup>52</sup>

Upon referral to the Oil and Gas Committee, it will conduct a formal hearing that will include representations made by the applicant, the Board's representatives, and any parties that are both directly affected and have indicated to the Board their intention to participate. Generally, the Oil & Gas Committee will only consider evidence presented to the Review Panel, and in the event that new evidence is presented or arises, the Board has a policy of suspending the Oil & Gas Committee's proceedings and revisiting the matter at the Review Panel level.<sup>53</sup> Once the Oil & Gas Committee has completed its hearing, it will draft its recommendation, a copy of which is presented to the Board, the applicant, and any participants in its hearings.

52. *Mobil Nautilus Case*, *supra* note 49 at paras 35, 37-38.

53. SDA Guidelines, *supra* note 40 at 7.

Once in receipt of the Oil & Gas Committee's report, the Board has several options. In the event that the Oil & Gas Committee recommends acceptance of the application and the Board agrees with the recommendation, it will issue a notice of proposed decision to accept the application (i.e. to issue the SDD as set out in the application). In the event that the Oil & Gas Committee has recommended that the application either be approved over a different (frequently smaller) area than in the application, or it has recommended that the application be denied in its entirety, the Board will issue a Decision Report, which shall include its findings and the reasons upon which it has based those findings. The final option is that the Oil & Gas Committee could recommend that an application be approved, but the Board could choose to either reject the application, or to approve an application over a different area than what is contained in the application.

The Supreme Court of Newfoundland and Labrador, Trial Division, in *Petro-Canada et al v. Canada–Newfoundland Offshore Petroleum Board*<sup>54</sup> held that the *Accord Act* imposes a statutory obligation on the Board to provide reasons for its decision.<sup>55</sup> The Court found that “[the Board’s] ‘conclusions,’ merely recites the matters the board was required to consider and states conclusions. This does not constitute ‘reasons’ as contemplated by the legislation.”<sup>56</sup> Given the threshold of reasons required, it is highly unlikely that the Board would reject the technical determinations made by the Oil & Gas Committee unless the Board was certain the Oil & Gas Committee was fundamentally wrong on the issue, as the decision would certainly be subject to challenge and the Board would be required to provide reasons to the applicant to support its decision.

#### *Application process—SDL*

Once an SDD has been declared in respect to a particular area, interest owners holding interests in lands subject to the SDD may make an application at any time for the issuance of an SDL. Section 73 of the *Accord Act* sets out the (modest) test for the issuance of an SDL: (1) an SDD must be in force over the land; (2) an EL must be in force over the land; (3) the application must be made by the interest holders of the EL; and (4) the application must be in the prescribed form and contain the prescribed information.<sup>57</sup> With respect to the last criteria, the Board does not appear to have issued a form or prescribed information (beyond demonstrating compliance with issues (1)–(3) above.

54. 1995 CanLII 10613 (NL SCTD), 133 Nfld & PEIR 91 [*East Rankin Case*].

55. *Ibid* at para 38.

56. *Ibid* at para 38.

57. *Accord Act*, *supra* note 9, s 73.

While it is typical for interest holders to make application for an SDL immediately upon the issuance of the SDD, there is no time limit for making application for an SDL. Nor is there a requirement that the EL be in force at the time the SDL application is granted. The Board has recognized this right, and on occasion, will issue a call for bids for the issuance of an SDL rather than an EL. The Call for Bids NL10-03<sup>58</sup> resulted in the issuance of SDL 1048 to Statoil Canada Ltd. (*Statoil*) and Husky Oil Operations Ltd. (*Husky*), as the lands subject to Call for Bids NL10-03 were already subject to the Mizzen O-16 SDD.<sup>59</sup>

c. *Legal test for issuance of SDD*

The test for the issuance of an SDD is set out in the *Accord Act*. Section 71(1) of the *Accord Act* states that:

Subject to section 124, where a significant discovery has been made on any portion of the offshore area that is subject to an interest or a share therein held in accordance with section 66, the Board shall, on the application of the interest holder of the interest or the share thereof made in the form and manner and containing such information as may be prescribed, make a written declaration of significant discovery in relation to those portions of the offshore area in respect of which there are reasonable grounds to believe that the significant discovery may extend.<sup>60</sup>

The *Accord Act* also defines what constitutes a “significant discovery.” Section 47 defines a “significant discovery” as

[A] discovery indicated by the first well on a geological feature that demonstrates by flow testing the existence of hydrocarbons in that feature and, having regard to geological and engineering factors, suggests the existence of an accumulation of hydrocarbons that has potential for sustained production.<sup>61</sup>

58. Canada–Newfoundland and Labrador Offshore Petroleum Board, Call for Bids No NL10-03 (Area “C”—Central Ridge / Plemish Pass) Significant Discovery Licence in the Newfoundland and Labrador Offshore Area, online: Canada–Newfoundland Offshore Petroleum Board <[http://www.cnlopb.nl.ca/news/pdfs/cfb10\\_03.pdf](http://www.cnlopb.nl.ca/news/pdfs/cfb10_03.pdf)>.

59. SDL 1048, online: Canada–Newfoundland Offshore Petroleum Board <<http://www.cnlopb.nl.ca/abstract/instrum/11002.pdf>>.

60. *Accord Act*, *supra* note 9, s 71(1).

61. *Ibid*, s 47.

The SCC,<sup>62</sup> the Board,<sup>63</sup> and the Oil & Gas Committee<sup>64</sup> have found that the term is to be broken down into a test with three component parts:

1. The first well on a geological feature;
2. That demonstrates by flow testing the existence of hydrocarbons in that feature; and
3. Having regards to geological and engineering factors, suggests the existence of an accumulation of hydrocarbons that has potential for sustained production.

Each of these component parts or prongs must be met in order for an operator to be entitled to a declaration of SDD over a particular well.

While the first prong of the test for a SDD is fairly straightforward, the remaining two are less so. The Board,<sup>65</sup> the Oil and Gas Committee,<sup>66</sup> the Supreme Court of Canada,<sup>67</sup> and the Supreme Court of Newfoundland and Labrador Trial Division,<sup>68</sup> have all considered various definitions for the term “flow testing,” the quantity and quality of geological and engineering factors necessary for an operator to be entitled to an SDD, and the sufficiency of the potential for sustained production necessary for an operator to be entitled to an SDD.

In discussing the nature of the test, the SCC has written that “[u]nder the current regime, however, this discretion has given way to an objective test which favours industry participants [as] the Board ‘shall’ make declarations once ‘reasonable grounds’ have been proved.”<sup>69</sup>

Each of the following documents further refines and clarifies the meaning of the terms found in the test for a significant discovery set out in the *Accord Act*:

- The *Newfoundland Offshore Petroleum Drilling and Production Regulations*<sup>70</sup>;

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62. *Mobil Nautilus Case*, *supra* note 49 at para 32.

63. SDA Guidelines, *supra* note 40 at 15.

64. Report and Recommendation to the Canada–Newfoundland Offshore Petroleum Board by the Oil and Gas Committee Respecting Application by Petro-Canada RE: East Rankin H-21 SDA Application, April 1992 [*East Rankin Oil & Gas Committee Report*].

65. SDA Guidelines, *supra* note 40; and Canada–Newfoundland and Labrador Petroleum Board and Canada–Nova Scotia Offshore Petroleum Board, *Data Acquisition and Reporting Guidelines*, Draft December 31, 2009 [*Data Acquisition Guidelines*].

66. *East Rankin Oil & Gas Committee Report*, *supra* note 64.

67. *Mobil Nautilus Case*, *supra* note 49.

68. *East Rankin Case*, *supra* note 54.

69. *Mobil Nautilus Case*, *supra* note 49 at para 22.

70. SOR/2009-316 [*Drilling Regulations*].

- Board's *Guidelines Regarding Applications for Significant Discovery or Commercial Discovery Declarations*<sup>71</sup> (the *SDA Guidelines*);
- Board's *Data Acquisition and Reporting Guidelines*<sup>72</sup> (the *Data Acquisition Guidelines*); and
- Board's *Drilling and Production Guidelines*<sup>73</sup> (the *Drilling Guidelines*).

*First Well on a geological feature*

The SCC considered this requirement and found that “there is nothing ambiguous about ss. 47 and 71(1) and that a well requirement exists.”<sup>74</sup>

*Demonstrates by flow testing the existence of hydrocarbons*

While the term “flow test” is not defined anywhere in the *Accord Act* or in the regulations or guidelines, a similar term is defined in the regulations and the guidelines. Neither the Supreme Court of Newfoundland and Labrador Trial Division nor the Oil and Gas Committee have found any meaningful distinction between the term “flow test” and the similar term applied in the regulations and guidelines, “formation flow test.”<sup>75</sup> The Drilling Regulations section 1(1) define a “formation flow test” as an operation:

- (a) To induce the flow of formation fluids to the surface of a well to procure reservoir fluid samples and determine reservoir flow characteristics or
- (b) To inject fluids into a formation to evaluate injectivity.

The effect of the definition of “formation flow test” found in these Drilling Regulations is to greatly restrict the term “flow test” from what the ordinary plain meaning of the words may otherwise indicate. An operator is required to demonstrate that fluid is brought to the surface, and such fluid is capable of being used to procure reservoir fluid samples and determine reservoir flow characteristics in order to qualify as a “formation flow test.”

71. SDA Guidelines, *supra* note 40.

72. Canada–Newfoundland Offshore Petroleum Board, *Data Acquisition Guidelines*, online: Canada–Newfoundland Offshore Petroleum Board <[http://www.cnlopb.nl.ca/pdfs/guidelines/data\\_aq\\_guide.pdf](http://www.cnlopb.nl.ca/pdfs/guidelines/data_aq_guide.pdf)>.

73. Canada–Newfoundland Offshore Petroleum Board, *Drilling Guidelines*, online: Canada–Newfoundland Offshore Petroleum Board <[http://www.cnlopb.nl.ca/pdfs/guidelines/drill\\_prod\\_guide.pdf](http://www.cnlopb.nl.ca/pdfs/guidelines/drill_prod_guide.pdf)>.

74. *Mobil Nautilus Case*, *supra* note 49 at para 21.

75. *East Rankin Case*, *supra* note 54; *Drilling Regulations*, *supra* note 70 at s 1(1).

The SDA Guidelines further set out the evidence the Board has adopted as being necessary in order to meet this prong of the SDD test. The Board states that:

For the purpose of determining a significant discovery, the Board will require a formation flow test as defined in the *Newfoundland Offshore Petroleum Drilling Regulations* [Prior version—now repealed] and detailed in sections 171–174 [now no longer applicable]. This testing is intended to provide the substantive foundation upon which reliable data can be obtained to support an application for a significant discovery. The test should provide the applicant with the information to satisfy the Board that the possibility of sustained production is more than unsupported speculation.<sup>76</sup>

The first portion of the guidance provided by the Board about the threshold that an operator must meet to support a SDD (the flow test must be a formation flow test as defined in the regulations) is in line with existing legislation, regulations, and case law. The second aspect (that the formation flow test provide the information necessary to satisfy the Board that the possibility of sustained production is more than unsupported speculation) is troubling as it contradicts the decision of the Oil and Gas Committee in Petro-Canada's East Rankin decision.<sup>77</sup> In the East Rankin decision, the Oil and Gas Committee found that:

[T]he legislation requires that the final assessment of whether or not a discovery is significant requires the following:

mobile hydrocarbons must be demonstrated to exist in the reservoir by flow testing....; and

geological and engineering evidence must suggest firstly, a feature of sufficient size and quality, and secondly, hydrocarbon contents and indicated production behavior, which together suggest the potential for sustained production<sup>78</sup>

In the decision, the Oil and Gas Committee considered and expressly rejected the concept that the formation flow test would be the basis upon which an applicant would demonstrate the possibility of sustained production. Instead, the Oil and Gas Committee interpreted the *Accord Act* to require all of the geological and engineering data to be the basics upon which sustained production is proven. While it is worth noting that the decisions of the Oil and Gas Committee are not binding on subsequent

76. SDA Guidelines, *supra* note 40 at 11.

77. *East Rankin Oil & Gas Committee Report*, *supra* note 64 at 12-14.

78. *Ibid* at 16.

decisions of the Oil and Gas Committee, the committee enjoys considerable deference from courts. Furthermore, it is submitted that the committee's reasoning is sound and there is no reason why a subsequent decision of the Oil and Gas Committee would resolve this matter differently.

With respect to the first portion of the Board's discussion of the SDA Guidelines, the SDA Guidelines can reasonably be read by changing references to a prior version of the *Drilling Regulations* to the new *Drilling Regulations*, and references to specific sections (171–174) to those sections in the new *Drilling Regulations* that most closely approximate the repealed sections (52–55). As such, the SDA Guidelines confirm that the formation flow test that is acceptable for a SDD is one that constitutes formation flow testing as set out in the *Drilling Regulations*.

*Formation flow testing under drilling regulations*

The *Drilling Regulations* require, before an operator may drill a well, that the operator must obtain a well approval pursuant to Section 13 of the *Drilling Regulations*. Section 13 states that:

The Board shall grant the well approval if the operator demonstrates that the work or activity will be conducted *safely, without waste and without pollution, in compliance with these Regulations*.<sup>79</sup>

This section provides a mandatory right for an operator to receive a well approval, provided the operator is able to demonstrate that it meets the requirements with respect to safety, lack of waste, lack of pollution and compliance with the regulations. In addition, section 11 lists the evidence necessary to demonstrate that an application for a well approval meets these requirements. One of the most significant requirements is that the application must be accompanied by

[A] well data acquisition program that: allows for the collection of sufficient cutting and fluid samples, logs, conventional cores, sidewall cores, pressure measurements and formation flow tests, analyses and surveys to enable a comprehensive geological and reservoir evaluation to be made.<sup>80</sup>

Once an approval to drill a well has been issued, the operator is under an obligation pursuant to section 49 of the *Drilling Regulations* to ensure that “the well data acquisition program and the field data acquisition program are implemented in accordance with good oilfield practices.”<sup>81</sup> This clause

79. *Drilling Regulations*, *supra* note 70, s 13.

80. *Ibid*, s 11.

81. *Ibid*, s 49.

means that, pursuant to the *Drilling Regulations*, an operator's obligations with respect to a data acquisition program (including formation flow testing), is subject to good oilfield practice and safety considerations. Section 38 of the *Drilling Regulations* also states that:

If the well control is lost or if safety, environmental protection or resource conservation is at risk, the operator shall ensure that any action necessary to rectify the situation is taken without delay, despite any condition to the contrary in the well approval.<sup>82</sup>

Furthermore, in the event of a conflict between good oilfield practice/safety and a well data acquisition program (including formation flow testing), section 50(2) states that:

If the operator can demonstrate that those procedures can achieve the goals of the well or field data acquisition program or are all that can be reasonably expected in the circumstances, the Board shall approve them.<sup>83</sup>

This general language applies to all of the provisions relating to the "evaluation of wells, pools and fields" found in Part 5 of the *Drilling Regulations* (sections 49–55). Part 5 includes sections pertaining to the testing and sampling of formations, the submission of samples and data, and formation flow testing. The Board must accept a formation flow test that is "all that can be reasonably expected in the circumstances," notwithstanding non-compliance with the requirements set out in Section 52 (i.e. that the formation flow test be approved by the Board (Subsection 52(2)(b)) or even that the operator has "submit[ted] a detailed testing program" (Subsection 52(2)(a))).

*Having regard to geological and engineering factors, suggests the existence of an accumulation of hydrocarbons that has potential for sustained production*

In the *East Rankin Case* the Newfoundland Supreme Court, Trial Division found that section 47 "only requires the applicants to establish that information on their well 'suggests' the 'potential' for sustained production of hydrocarbons."<sup>84</sup> The Court went on to state:

- 42 [S]o the statutory language supports the conclusion that the proper burden to impose upon the applicants is that suggested by Reed J. in *Mobil Oil*, namely, require them to prove "reasonable grounds

82. *Ibid*, s 38.

83. *Ibid*, s 50(2).

84. *East Rankin Case*, *supra* note 54 at para 42.



to believe there is a possibility” of sustained production, that is, reasonable grounds to believe sustained production may be practicable.

[...]

- 44 The legislation makes it clear, for example, by reference to geological and engineering factors in s. 47, that the board is to act in a scientific fashion on the basis of scientific knowledge. It is useful, therefore, in discussing the appropriate standard of proof, to consider the nature of scientific inquiry and the extent of its dependence upon the formulation of hypotheses, the construction of theories, and the observation of data.

[...]

- 54 Now, how is this related to the real world and the present case? Here Petro-Canada had the evidential burden to present data, hypotheses, and theories relating to the possibility of sustained production of hydrocarbons which met the board’s threshold test of evidentiary reliability or trustworthiness. See *Mohan* and *Daubert*. Evidentiary reliability, in a case such as this involving scientific evidence, will be based upon scientific validity. See *Daubert*. The board was entitled to evaluate the hypotheses, theories, and models put forward by Petro-Canada in terms of whether they were a systematic body of propositions falsifiable (or verifiable if the board preferred this philosophical approach) by observation. See Lasswell and McDougal; Shapere; and Popper. The board was entitled to ask whether the intellectual or logical constructs of Petro-Canada were grounded in the methods and procedures of science and not just subjective belief or unsupported speculation. See *Daubert*. The board was entitled to consider whether Petro-Canada’s propositions were generally accepted by the scientific community. See *Mohan* and *Daubert*.
- 55 Petro-Canada also had the legal burden of satisfying the board by the data, hypotheses, and theories presented that Petro-Canada had met the standard of proof required by the legislation. The civil standard applies, that is, proof on a preponderance of probabilities. See Sopinka; Lederman, and Bryant; and *Vout*. The unusual situation, here, however, is that what must be so proved is merely data which ‘suggests’ a ‘potential,’ that is, a *possibility*. The result is that Petro-Canada had to prove the suggestion of a possibility on a balance of probabilities, a ‘fairly generous test,’ in the words of Reed J. in *Mobil Oil*, to say the least.
- 56 I do not believe it necessary to decide whether proof of a possibility on a preponderance of probabilities constitutes, in effect, a third standard of proof, legislated for significant discoveries of petroleum. The result in this case is the same, in any event.

- 57 One may argue that proof of a possibility requires no proof at all, since a possibility, in the sense of something ‘that may be or happen,’ see *Websters*, by definition, may exist or happen, whatever the data, hypotheses, or theories submitted. The legislation in the present case, however, by its reference to ‘geological and engineering factors’ in s. 47 and to ‘reasonable grounds’ in s. 70(1), convinces me that Parliament and the Newfoundland legislature contemplated an applicant having to produce sufficient unrefuted data, hypotheses, and theories to satisfy the board that the possibility was more than a random one or based just on chance or unsupported speculation. See Lasswell and McDougal; and *Daubert*.
- 58 The Board, therefore, is entitled to require of applicants that they supply reliable data and acceptable scientific hypotheses and theories to explain these. The data, hypotheses, and theories are not to be rejected, however, merely because doubts are raised regarding them by other data, hypotheses, or theories available to the board. These other data, hypotheses, and theories must be weighed against the applicant’s, using the expert knowledge available to the board. And the board must expressly explain why it is left with no ‘suggestion’ of a ‘potential’ for sustained production after this process has been completed. If the board is left with reasonable grounds to believe there is a possibility of sustained production, that is, grounds based upon unrefuted data, hypotheses, and theories, the applicant should obtain a declaration of significant discovery. If the data, hypotheses, and theories supplied by the applicant are refuted, then the board need not issue a declaration.<sup>85</sup>

The third prong of the test for an SDD is, then, that an applicant must demonstrate, on a balance of probabilities, that having regard to geological and engineering factors, the flow testing suggests the existence of an accumulation of hydrocarbons that has potential for sustained production. The test is generous, and the applicant is permitted to rely on geological and engineering factors. The applicant is not required to prove beyond a reasonable doubt the existence of an accumulation of hydrocarbons that is capable of sustained production; nor is the applicant required to prove beyond a reasonable doubt that such an accumulation may exist. Instead, the applicant is required to prove on a balance of probabilities that such an accumulation may exist. To use the language of Barry, J., an applicant must “produce sufficient unrefuted data, hypotheses, and theories to satisfy

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85. *East Rankin Case*, *ibid* at paras 42-58.

the board that the possibility was more than a random one or based just on chance or unsupported speculation.”<sup>86</sup>

d. *Substantive rights*

Section 72 of the *Accord Act* provides a SDL holder with the same rights as an Exploration Licence:

- (a) the right to explore for, and the exclusive right to drill and test for, petroleum;
- (b) the exclusive right to develop those portions of the offshore area in order to produce petroleum; and
- (c) the exclusive right, subject to compliance with the other provisions of this Part, to obtain a production licence.

The principal advantage of a SDL compared to an EL is that there is no expiry term for a SDL. Recently, the Board has adopted a practice of requiring licence holders to pay rentals on the licenses. At time of writing, license holders, after the fifth year, are required to pay a rental rate of \$40 per hectare, which rises to \$200 per hectare after ten years, and \$800 per hectare after fifteen years. Similar to ELs, there are a number of other boilerplate terms of SDDs, including an agreement to indemnify the Board and the Crown from any third party claims.

4. *Commercial discovery declaration*

a. *Application process*

The *Accord Act* provides that the Board has authority to prescribe the “form and manner” and setting out the information that is required in order to make an application for a Commercial Discovery Declaration (CDD).<sup>87</sup> The application process for a CDD is identical to the application process for a SDD. While the legal thresholds are different, as set out below, the steps are the same. First, a preliminary technical review is completed, followed by a recommendation to the Chair. The Chair then decides whether to hold a Review Panel of the Board to consider the application. Once a review panel has made a recommendation, a notice of proposed decision is sent to all directly affected parties. In the event that the interest holders or the directly affected parties object, the Oil & Gas Committee hears the dispute and makes a recommendation to the Board. As with the SDD application process, the Board suggests the entire process can take up to six months

86. *East Rankin Case*, *ibid* at para 57.

87. *Accord Act*, *supra* note 9, s 47(1)(l) defines the term prescribed and s 78(1) allows the Board to prescribe the form, manner and information.

and, as such, recommends applications be made at least six months prior to the planned production.

b. *Legal test for issuance*

While all levels of courts in Newfoundland along with the Board and the Oil & Gas Committee have all been required to consider a legal definition of a “significant discovery,” there has been remarkably little debate as the interpretation of the term “commercial discovery.” Section 47(1)(b) defines a commercial discovery as:

[A] discovery of petroleum that has been demonstrated to contain petroleum reserves that justify the investment of capital and effort to bring the discovery to production[.]<sup>88</sup>

The SDA Guidelines describe the Board’s approach to its review of applications for commercial discoveries. The Board has broken the definition found in the *Accord Act* into three components: (i) the discovery “has been demonstrated to contain”; (ii) “petroleum reserves”; and (iii) that “justify the investment of capital and effort.” The Board has interpreted “has been demonstrated” to mean that the application must show conclusively that the petroleum reserves exist (and not that they are probable or possible). Petroleum reserves must be “considered to be recoverable using current technology and under present and anticipated economic conditions.”<sup>89</sup> The final portion, “justify the investment of capital and effort,” is not generally considered a difficult threshold. As the only reason why an interest holder would apply for a declaration of commercial discovery is in order to obtain a Production Licence, there is generally little doubt given the interest holder’s expenditures with respect to the lands that the discovery is believed to justify the expense.

The only judicial consideration of the term “commercial discovery” took place in the *East Rankin Case*. In that case, Petro-Canada argued that the Board erred when it considered the size of the hydrocarbon accumulation and the economics of production in determining whether there was a ‘potential for sustained production’ (the test for a significant discovery licence). Petro Canada argued that by “considering the size of the accumulation and the economics of production,” the Board had erred and applied the test for a commercial discovery.<sup>90</sup> The Court disagreed and found that the Board had “clearly distinguished between the tests in the definition of commercial discovery and those for a significant

88. *Ibid*, s 47(1)(b).

89. *SDA Guidelines*, *supra* note 40 at 13.

90. *East Rankin Case*, *supra* note 54 at para 74.

discovery.”<sup>91</sup> By accepting a (limited) role for the size and economics factors in the issuance of a significant discovery licence, the Court seems to be indicating that the threshold for a commercial discovery is higher, without providing much in the way of guidance to describe what might be the appropriate threshold.

c. *Substantive rights*

The only right of interest holders whose lands are subject to a CDD is the right to apply for a Production Licence.

5. *Production licence*

a. *Application process*

The application process for a Production Licence (PL) is very informal. Once a CDD has been made in respect to a particular piece of land, an application for a PL consists of a letter from the interest owner, defined as the individual “who holds an interest” or those who collectively “hold all of the shares in an interest” in a particular piece of land.<sup>92</sup>

b. *Legal test for issuance*

The legal test for the issuance of a PL is prescriptive—the Board must issue the licence when presented with an application meeting all of the requirements. The requirements are also very straightforward: an interest owner who holds lands that are subject to a CDD and either a SDL or an EL is entitled to a PL.<sup>93</sup>

c. *Substantive rights*

PL holders have the exclusive rights to: (i) drill and test for petroleum; (ii) develop the lands; (iii) produce petroleum from the lands; and (iv) title to any petroleum produced from the lands.<sup>94</sup>

II. *Review of current issues*

1. *Stratigraphic ownership issues*

The development of the Hebron project will likely require that the Board address an issue that it has previously been able to avoid: stratigraphic ownership. Specifically, which interests can be divided on a geographic or stratigraphic basis?

91. *Ibid* at para 76.

92. *Accord Act*, *supra* note 9, s 47(1)(k).

93. *Ibid*, s 80(1)(a).

94. *Ibid*, s 80(1).

Section 66 of the *Accord Act* permits interests in an EL to be held “with respect to a portion only of the offshore area subject to the [EL].”<sup>95</sup> An interest holder of an EL can therefore hold a share in an interest over only a portion of the interest—either divided on a geographical or stratigraphical basis (a “divided interest”). There are two ways that an interest in an EL could be divided: geographically (i.e. some but not all sections) or stratigraphically (i.e. some but not all formations). Traditionally the Board has been prepared to recognize geographical but not stratigraphical ownership of ELs. At time of writing, we are not aware of any divided interests outstanding that are registered with the Board.

The ability to hold interests in SDLs and PLs over less than all of the lands subject to the interest is less satisfactory. Section 47 defines “shares” as either “an undivided share in the interest or a share in the interest....”<sup>96</sup> (for all types of interests—ELs, SDLs and PLs) or divided interests (for ELs only). While the legislation appears to be clear that it does not contemplate the issuance of divided interests in SDLs and PLs, this gives rise to certain problems of practical application. In the event that the interest owners of divided interests seek to convert the interest into a SDL, the interest owners are required to address the issue.

The issue is an issue of timing—when do the interest holders of an interest that has been divided based on a geological or stratigraphical basis have to agree upon shares of the entire interest? As previously discussed, the threshold test for the issuance of a SDD (and subsequently a SDL) is fairly low. By prohibiting interest holders in a divided interest EL from obtaining a divided interest SDL, the *Accord Act* and the Board is essentially forcing the interest holders to either create trust arrangements in respect to the divided interest, or to negotiate amongst the interest holders to agree on shares based on an undivided basis for the whole SDL. Trust arrangements would presumably create unnecessary complicated legal arrangements, whereas negotiation amongst the interest holders is likely premature to agreement on the final shares. Realistically, when the interest holders have resolved to apply for a SDL they may not have all of the information necessary to settle on a final allocation of shares in the interest and could therefore give rise to a renegotiation at some point prior even to production. Given the level of this complication arising from this issue, it may appear to be a situation where a legislative change—to permit the Board to recognize divided interest SDLs and PLs—may be appropriate.

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95. *Ibid*, s 66.

96. *Ibid*, ss 47(1)(m), 66.

A second stratigraphic issue is exemplified by the Hebron project's proximity to the existing Terra Nova project. While the primary lands to be included as a portion of the Hebron project are not within the boundaries of the Terra Nova project, the Hebron project has identified additional lands that may be included into the project that are already subject to the Terra Nova PLs PL-1003 and PL-1004.<sup>97</sup> In the event that the Hebron project's reserves do ultimately include hydrocarbons on PL-1003 and PL-1004, the Board will have to address the stratigraphic dimension to the problem. Section 58(3) of the *Accord Act* permits the Board to issue interests (including ELs, SDLs, and PLs) "restricted to [one or more] geological formations."<sup>98</sup> The Board could conceivably issue a PL for the Hebron project over some but not all of the geological formations (and, with the cooperation of the Terra Nova interest owners, amend the Terra Nova Production Licences accordingly). Otherwise, the Terra Nova interest owners could conceivably seek a unitization or pooling order from the Board with respect to the Hebron project, which is clearly an untenable situation.

It appears that the Board will soon be required to adopt a procedure for the issuance of interests, including interests in PLs and SDLs. The procedure will require that the Board put in place a recordkeeping procedure to recognize geological and stratigraphic restrictions on interests. As the offshore regime matures, and in particular with the developments in the western Newfoundland offshore area, the Board will need to develop a policy for dealing with situations where two or more fields may overlap stratigraphically.

## 2. *Protection of data*

Information provided to the Board is subject to the confidentiality provisions of the *Accord Act* found in sections 119(2) and 119(5). Any information not covered by the sections is subject to disclosure under access to information requests and may otherwise be disclosed by the Board. Section 119(5) provides for expiry periods for the protection of certain classes of information (i.e. exploration wells, delineation wells, development wells) and the outright exclusion of certain other types (environmental studies, diving work, accidents and spill statistics).<sup>99</sup>

97. "Hebron Fiscal Agreement" (20 August 2008), online: Department of Natural Resources <[http://www.nr.gov.nl.ca/nr/energy/petroleum/offshore/projects/hebron\\_fiscal\\_aggre.pdf](http://www.nr.gov.nl.ca/nr/energy/petroleum/offshore/projects/hebron_fiscal_aggre.pdf)>, at Exhibit A-2, Exhibit A-5.

98. *Accord Act*, *supra* note 9, s 58(3).

99. *Ibid*, s 119(5).

One issue of note, however, is that while the Board has adopted a position that it treats information contained in Calls for Nomination as confidential, there is a legitimate concern that the information is not protected under section 119(2) of the *Accord Act*. Section 119(2) provides that:

Subject to section 18, ...information or documentation provided for the purposes of this Part or Part III or a regulation made under either Part, whether or not that information or documentation is required to be provided under either Part or a regulation made under either Part, is privileged and shall not knowingly be disclosed without the written consent of the person who provided it except for the purposes of the administration or enforcement of either Part or for the purposes of legal proceedings relating to the administration or enforcement.<sup>100</sup>

A Call for Nominations procedure is not either required by the *Accord Act* or a regulation made under the *Accord Act*, and it appears at least arguable that it is not “provided for the purposes” of the *Accord Act* or a regulation made thereunder.<sup>101</sup> As such, the statutory protection of information found in the *Accord Act* may not be applicable to information submitted pursuant to a Call for Nominations, and it may be subject to disclosure under an access to information request. Companies considering nominating lands must be careful about the nature and quantity of information that they share with the Board under the Call for Nominations procedure. In some circumstances, even disclosing which lands the participant is interested in exploring can negatively affect the company.

### *Conclusion*

While there have been relatively few court decisions considering the provisions of the *Accord Act*, these decisions, considered in conjunction with the regulations and guidelines promulgated by the Board, and the decision reports of the Oil & Gas Committee, have created a reasonably complicated series of application processes. In particular, the process by which the Board considers applications for the issuance of SDDs and SDLs appears to have been the most contentious issue.

When the Board determines its course of action with respect to stratigraphic ownership, it would be appropriate to consider implementing

100. *Ibid*, s 119(2).

101. Section 58(3) of the *Accord Act*, *ibid*, states that “[a] request received by the board to make a call for bids in relation to particular portions of the offshore area shall be considered by the board....” It can be argued that information submitted to the Board under the Call for Nomination procedure is then caught in the purposes of the *Accord Act*, but this appears somewhat weak in respect to the voluntary submission of information to the Board.



a process of recognizing stratigraphic and other divided interests in SDLs and PLs as well as ELs.