

EB-2015-0206
Tribute Resources Inc.
Responses to Interrogatories from
Ontario Energy Board Staff

Reference: Tribute's Evidence, page 1, Paragraph 1

Interrogatory 1:

Please explain the date of January 1, 2012.

Interrogatory 1 Response:

When Tribute purchased the former Magnum Gas assets, now Tribute assets, including the Pipelines and Wells referred to in Tribute's Pre-filed Evidence Sections 6 and 8 (hereinafter referred to as the "Purchased Assets"), certain municipal tax arrears were assumed by Tribute totalling \$375,275.36. Of these amounts, the vast majority (greater than \$345,556.00) related to the 2012 and 2013 taxation years and the appeals requested by Tribute to the Assessment Review Board were for taxation years beginning on January 1, 2012. The significance of this date is that it forms the starting date of the relevant taxation years, as outlined in Tribute's Pre-filed Evidence Paragraph 16.

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Reference: Tribute's Evidence, page 2, Paragraph 6

Interrogatory 2:

Please explain if these pipelines were characterized and taxed as transmission lines or gathering lines.

Interrogatory 2 Response:

These pipelines were, and to Tribute's knowledge have always been assessed by MPAC and taxed as transmission "pipe lines". Tribute has reviewed the files and records provided to it by Magnum Gas Corp. and has been unable to locate any documentation whereby Magnum Gas Corp. and/or Echo Energy Canada Inc. provided any notification under section 25(2) of the Act to MPAC that the pipelines or any part of them were designated as "transmission pipelines". It is Tribute's position that the pipelines have been improperly assessed by MPAC pursuant to section 25 of the *Assessment Act* and the Regulations made thereunder.

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Reference: Tribute's Evidence, page 3, Paragraph 9 and page 7, Paragraphs 23 and 24

Interrogatory 3:

Referring to the CSA Standard and the Operating Standard definitions please explain which characteristics, including type of service, qualify this pipeline as a gathering pipeline as opposed to a transmission pipeline.

What is the difference between a gathering pipeline and a gathering line?

Please provide examples of other "gathering pipelines" in the industry which are not considered transmission pipelines as defined in the *Assessment Act*.

Interrogatory 3 Response:

The definition in the *CSA Standard Z662-11 for Oil and gas pipeline systems* (published in June 2011) (the "CSA Standards") is very well worded. The Technical Committees and Subcommittees that have written and edited the CSA Standards over the years are arguably the most expert in the oil and gas industry. The names on the Committee and Subcommittee lists are recognized industry experts.

The following definitions from the CSA Standards are relevant in answering this Interrogatory (see Schedule "C" of Tribute's Pre-filed Evidence):

"Pipeline – those items through which oil or gas industry fluids are conveyed, including pipe, components, and any appurtenances attached thereto, up to and including the isolating valves used at stations and other facilities." (See Schedule "C" – page 25)

"Gathering line – see Line, gathering" (See Schedule "C" - page 23).

"Line, gathering – a pipeline that conveys gas from a wellhead assembly to a treatment plant, transmission line, distribution line, or service line." (See Schedule "C" page 24)

"Transmission line – see Line, transmission" (See Schedule "C" page - 29)

"Line, transmission – a pipeline in a gas transmission system that conveys gas from a gathering line, treatment plant, storage facility, or field collection point in a gas field to a distribution line, service line, storage facility, or another transmission line" (See Schedule "C" page - 24)

Tribute's gathering lines (including a 4 inch diameter steel main gathering line) are used to do just that – gather raw reservoir gas from each well and transport it to the central processing facility where the gas

is processed to meet the high standards of the utilities (in this case, Union Gas Limited (hereinafter “Union”)) and then deliver it to the transmission line owned and operated by Union. Tribute would like to make it clear to that the gas passing through this pipeline gathering system does not meet natural gas distribution standards of the utilities for three main reasons: Firstly, the gas contains too much water vapour to meet water dewpoint requirements, secondly, the gas contains too many heavy hydrocarbons to meet hydrocarbon dewpoint requirements and thirdly, it is not odorized to meet safety standards for detection. The gas does not meet Union’s quality requirements until it passes through the Union Gas Meter Site where the final step, odorization occurs, and it passes into the transmission system. Therefore, all of the gas in Tribute’s possession at all times is appropriately classified as produced raw gas in a gathering pipeline network.

The produced gas is gathered and ultimately delivered through Union’s Meter Site into its transmission and distribution system near the corner of Jackson Line and Mill Road west of Tillsonburg. At the delivery point, Union meters the gas, odorizes the gas and verifies the quality of the gas. Until the gas passes through the Union Meter Site, it is not suitable for sale as it is raw reservoir produced gas. The gas is not ready for sale to ultimate consumers until it reaches this Meter Site and ownership of the processed gas is transferred from Tribute to Union Gas Limited.

The *Provincial Operating Standards Version 2.0* made under the *Oil, Gas and Salt Resources Act* and its Regulations is the document used by the Ministry of Natural Resources to regulate the oil and gas production industry. Clause 5.7 states:

5.7 Piping Systems

Pipeline gathering lines shall be in accordance with CSA Z662-99 Oil and Gas Pipeline Systems. Process lines shall be in accordance with CSA B51-97 Boiler, Pressure Vessel and Pressure Piping Code.

As such, we have referred to the definition of “pipeline” as it is included in the definition of “work(s)” both as set out in the *Oil, Gas and Salt Resources Act*, R.S.O. 1990, c.P.12, as amended, which definitions are included below:

“pipeline” means a pipeline used for the collection of oil, gas or other substance produced from or injected into a well and transportation of the oil, gas or substance to a separating, processing or storage facility or to a distribution or transmission pipeline;

“work” means a well or any pipeline or other structure or equipment that is used in association with a well.

The pipelines included in the Purchased Assets are used to gather the raw reservoir gas from each well and transport it to the central processing facility where the gas is processed to meet Union’s high standards and then to deliver it to the transmission pipeline owned by Union and which is located at Union’s Meter Site at the point of sale.

There is no difference between a gathering pipeline and a gathering line; one is merely a short form with the same meaning (see the definitions in the CSA Standards quoted above).

Tribute is an oil and gas producer in Ontario. As such, it has knowledge and experience in respect of production, gas gathering and delivery to utilities, as well as transmission line designations under the *Assessment Act*.

Tribute herein provides three cases where gathering lines through which it delivers gas to Union's system have not been designated as transmission pipelines by Tribute or taxed as such. The first is the Tribute line from the well "Tribute et al #19 Stephen 3-5-XIX" to Union's pipeline system and runs along S Road in Huron County. The second line from well "Clearwood et al #12 Tuckersmith 2-30-IIISHR" and runs to Union's pipeline system at Vanastra along Front Line and Vanastra Road. The third line is from well "Tribute 26 et al Hay 2-11-XVI" and runs along Shipka Line to Dashwood Road where it connects to Union's pipeline system. These are but a few examples of many in the industry. Dundee Energy LP operates gas gathering facilities in Ontario and is in a substantially similar situation as Tribute in respect of these examples. Tribute believes that there are other producers who operate other gathering lines that are also not considered transmission lines and are not assessed by MPAC under s. 25 of the *Assessment Act*.

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Reference: Tribute's Evidence, page 3, Paragraph 11

Interrogatory 4:

What evidence does Tribute have to support its statement that the pipelines have served as a "natural gas Pipeline gathering system for Echo and Magnum since at least 2011"?

What purpose did the pipelines serve between 2004 and 2011?

Interrogatory 4 Response:

On practical basis, Tribute can determine that from the age of the wells and pipelines and the layout of the works and the production system which connects the pipelines to the wells, that they could only have been used as gathering lines for the entire system for predecessor owners Echo Energy Canada Inc. ("Echo") and Magnum Gas Corp. ("Magnum") since 2011 and before. The sole purpose of the natural gas pipeline gathering system is to gather raw reservoir gas from each well and transport it to the central processing facility where in the gas is processed to meet Union's standards and then deliver it to Union's transmission pipeline, which is located at Union's Meter Site which is also the point of sale. This was certainly the case for the natural gas pipeline gathering system when Tribute purchased the system from Magnum included in the Purchased Assets in 2014 and Tribute has no reason to believe that the system was reconfigured or used in a different manner at any time in past since the drilling of the wells and the construction of the gathering system around 2004. To support this reasoning, Union would not have purchased or accepted Echo or Magnum's raw, non-processed reservoir gas at their sales meter.

To the best of Tribute's knowledge as understood through the due diligence process completed prior to the purchase of the Purchased Assets, it appears as though these pipelines have, since on or about 2004, been used continuously as gathering pipelines to gather and move produced gas to Union's system and the point of sale.

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Reference: Tribute's Evidence, Schedule B, MPAC Property Assessment Notices for 2014-2016 Property Tax Years.

Interrogatory 5:

Please discuss all reasons why Tribute appealed this assessment.

Interrogatory 5 Response:

The two main reasons that Tribute has appealed MPAC's assessments are:

1. MPAC's assessment of Tribute's gathering pipelines on the Purchased Assets is unlawful. MPAC is assessing pipelines that have never been designated by Tribute or its predecessors for the relevant taxation years as transmission pipelines which is the sole statutory basis upon which MPAC is entitled, under section 25 of the Act, to assess pipelines.
2. On a very practical basis, the municipal tax expenses levied on the pipelines purchased as part of the Purchased Assets are uneconomic and unaffordable and will result in the premature abandonment of the natural gas reserves.

Please see the Interrogatory 6 Response below, which expands on the first point above regarding these assessments are unlawful.

To expand on the second point above, it is Tribute's position that the current assessments imposed by MPAC result in taxation against Tribute that is uneconomic, unaffordable and will ultimately lead to the premature shutting-in of the wells as they will not be economical to produce. The taxation system does not take into account asset obsolescence due to the declines inherent in both oil and natural gas reservoirs. It assumes that these reservoirs are renewable and never decline (which is definitely not the case) and as such, the pipelines increase in value over time. The taxation resulting from these assessments is disproportionate to the value of the pipelines or the revenues derived from the natural gas being produced. These assessments result in a taxation structure that is disproportionately burdensome on Tribute.

As a current example, the improper assessments that MPAC has levied on Tribute for the Purchased Assets from the period January 1, 2015 to June 30, 2015, have resulted in property taxation amounts which represent 36% of gross income from all of the production from all of the wells owned by Tribute which are connected to this gathering pipeline system. This is the single largest expense item on the income statement associated with Tribute's operation of this field.

Tribute emphasizes that the natural gas reserves are a depleting resource, once fully developed, over a number of years. Over the same number of years, MPAC would have the taxes increasing while the revenues from the produced commodities are decreasing, again rendering this pool in the industry to be increasingly uneconomic over time. If MPAC's assessments of Tribute's gathering pipelines are upheld by the Board in this proceeding, they will result in property taxes that will increase over time as revenues and reserves are decreasing and will cause premature abandonment of the gas wells and pipelines prior to the full depletion of the recoverable gas reserves in place. This is an inappropriate use of Ontario's energy and natural gas resources, which could be determined to be socially irresponsible when the required infrastructure to extract these resources is currently in place and has already been paid for by the producer.

As another practical example, MPAC has suggested in the 2014 Assessments that the pipeline assets shown in Schedule "A" of Tribute's Pre-filed Evidence are collectively valued at \$6,041,500.00, which is absurd and bears no resemblance to the commercial realities of this depleting pool. Through negotiation with Magnum, a third party in an arm's length purchase and sale transaction with Tribute, the value of the pipelines and wells was \$440,000.00 with the total price paid for the Purchased Assets being \$2,550,750.00, the majority of which was allocated to the petroleum and natural gas rights and leases (i.e. the reserves and the rights to extract them).

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Reference: *Assessment Act*, Ontario Regulation 282/98

Interrogatory 6:

Referring to Part X “Tables RE: Assessment of Pipelines”, please discuss and explain reasons for Tribute’s view on how rates and methodology set up in this regulation should be applied to tax assessment of Tribute’s pipelines?

Interrogatory 6 Response:

It is Tribute’s position that Part X “Tables RE: Assessment of Pipelines” is not applicable to Tribute’s pipelines because they are not transmission pipelines nor have they been designated as such by Tribute for the relevant taxation years. The legislature of Ontario in enacting section 25 of the *Assessment Act* only intended that natural gas transmission pipelines as so designated by their owner be the subject matter of assessments and taxation. Section 25(1) of the *Assessment Act*, R.S.O. 1990, c.A.31, as amended, (the “Act”) defines pipeline as follows:

“Pipe line

25.(1) In this section,

“pipe line” means a pipe line for the transportation or transmission of gas that is designated by the owner as a transmission pipe line ...”

This definition is paramount and is the starting basis for any assessments or regulations that govern the assessment of “pipe lines”. As a defined term and a term of art, special attention must be paid to this definition throughout in the interpretation of the Act and any regulations made thereunder.

Section 7 of the Act requires the Minister of Finance to prescribe by regulation classes of real property which classes include “the pipe line property class”. Section 7(3) of the Act gives the Minister discretion to define what is included in a class. Ontario Regulation 282/98, as amended, (the “Regulation”) is the Regulation prescribed by the Minister of Finance under Section 7 of the Act and Section 7 of the Regulation reads as follows:

“PIPE LINE PROPERTY CLASS

7. The pipe line property class consists of pipe lines within the meaning of subsection 25(1) of the Act.”

Section 7 of the Regulation incorporates the definition of “pipe line” set out in Section 25(1) of the Act as quoted above which only includes a pipe line designated by the owner as a “transmission pipe line”.

Section 41 of the Regulation and Table 2 of Part X of the Regulation together set out the method of determining the assessed values for pipe lines. Both make reference to “plastic field gathering pipe lines” and “plastic distribution pipe lines” and it is submitted that each of these terms is clearly in error and is contrary to both Section 7 of the Regulation and more importantly Section 25(1) of the Act which sets out the definition of “pipe line” for purpose of the Act and the Regulations. It is Tribute’s position that the paramount enabling legislation and the will of parliament is expressed in Section 25(1) of the Act which is paramount to the regulation making power of the Minister of Finance who has passed contradictory Regulations in Sections 7 and 41 by introducing the terms “plastic field gathering pipe lines” and “plastic distribution pipe lines”. Because Section 7 of the Regulations specifically designates the “pipe line property class” as consisting solely of pipe lines within the meaning of Section 25(1) of the Act, by introducing other types of pipe lines in Section 41 of the Regulation the Minister, in passing the Regulation, has contradicted himself both within the Regulation itself and has also contradicted the specific language in Section 25(1) of the Act which for all purposes defines “pipe line”. Clearly a transmission pipe line cannot be at the same time a gathering pipe line or a distribution pipe line. They are separate and distinct terms and it is Tribute’s position that the Act and the Regulations were only intended to apply to transmission pipe lines designated by the owner as such as set out in Section 25(1) of the Act and Section 7 of the Regulation.

The current Act does not differentiate between the use of pipelines by a utility versus the use of pipelines by oil and natural gas producers.

Utilities’ transmission pipelines transport saleable natural gas to end user markets at high non-depleting pressures.

A natural gas producer like Tribute uses pipeline gathering systems to gather raw reservoir gas from each well and transport it to a utility delivery point. The volume throughput in these gathering lines typically decrease over time as a function of gas well production declines. This gas then passes through the utility’s meter station, where the gas is odorized and where ownership is assumed by the utility, at which point it goes into the utility’s transmission pipeline and is transported to end users. The gathering pipelines owned and used by the natural gas producer are exempt from assessment and taxation under the *Assessment Act* because they are not transmission pipelines.

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