

E.B.O. 184

THE ONTARIO ENERGY BOARD
 IN THE MATTER OF the Ontario Energy Board Act, R.S.O.
 1990, c. O.13;
 AND IN THE MATTER OF an Application by certain
 landowners in the Sombra Pool Designated Storage Area
 for the Ontario Energy Board to determine the purchase
 price for the residual gas in the Sombra Pool
 Designated Storage Area as of July 17, 1990, and other
 related matters

 Peter Glasgow et al
 VOLUME 2

Hearing held at 2300 Yonge Street,
 25th Floor, Hearing Room No. 1,
 Toronto, Ontario on Wednesday,
 March 19, 1997, commencing at
 9:10 a.m.

B E F O R E :

P. VLAHOS The Presiding Member
 E.J. ROBERTSON Member
 F.A. DROZD Member

2

158

A P P E A R A N C E S

STEVE McCANN	Board Staff
FRED CASS) The Consumers' Gas
ROBERT CRAIG) Company Ltd.
GABRIELLE KRAMER) The Applicants
STEPHEN WAQUE)
WALLACE LANG)
PETER GLASGOW)
JAMES LEO JOHNSTON)
D.A. SULMAN, Q.C.	Union Gas Limited

3

[Page: 159]

---On commencing at 9:10 a.m.
 ~ THE PRESIDING MEMBER: Please be seated.
 ~ Good morning everyone.
 ~ Any preliminary matters Mr. McCann?
 ~ MR. McCANN: I don't have any, Mr. Chairman.
 I believe Mr. Sulman had a transcript correction
 he wished
 to address.

~ MR. SULMAN: Yes, Mr. Chairman. Good morning.

~ It is a very minor transcript correction, but it is found at 139 of the transcript, line 2. It currently -- it was a discussion with Mr. Johnston and I was asking him -- it starts at line 28 on the previous page. And the question is:

~ "And if you could take a quick look at it

~ and tell me if this is the document by which

~ you conveyed those 13 acres to Consumers Gas

~ Limited in 1992?"

I think I certainly didn't ask whether they conveyed it to Consumers Gas. It might have been subconscious dealing with the company that may heat this building and those in Toronto.

~ I just ask that that reflect Union Gas Limited, not Consumers Gas Ltd.

~ THE PRESIDING MEMBER: Thank you, Mr. Sulman.

~ MR. SULMAN: There are no other substantive corrections.

4

[Preliminary Matters Page: 160]

~ THE PRESIDING MEMBER: Mr. Waque?

~ MR. WAQUE: Thank you, Mr. Chairman.

~ THE PRESIDING MEMBER: No preliminary matters?

~ MR. WAQUE: No, thank you.

~ THE PRESIDING MEMBER: Mr. McCann, we should proceed then with Mr. Cochrane?

~ MR. McCANN: Yes, I believe Mr. Waque should continue his case at this point, Mr. Chairman.

~ MR. WAQUE: Mr. Chairman, I am going to be referring first to Mr. Cochrane's curriculum vitae which is found at Exhibit 1, tab 2.

~ THE PRESIDING MEMBER: Perhaps Mr. Cochrane can come up and be sworn.

~ ROBERT COCHRANE; Sworn

~ MR. WAQUE: Mr. Chairman, Members of the Board, remembering my friend's admission with respect to the capacity of Mr. Cochrane to give opinion evidence, I just want to refer briefly to his curriculum vitae which is found under tab 2 of Exhibit 1. It is the last couple

of pages under tab 2. Tab 2 was the original prefiled evidence of Mr. Cochrane and after page 6 there are exhibits to that, including his curriculum vitae.

DIRECT EXAMINATION BY MR. WAQUE:

~ Q. We see that you are qualified as -- with a Bachelor of Science degree in Engineering, and I take

it you have been employed in undertaking geological work in the oil and gas industry for approximately the last 28

[Cochrane dr ex (Waque) Page: 161]

years?

~ A. That's correct. Actually, 27. I took one year off for the grand tour.

~ Q. And since 1992 you have been employed as an independent consultant in the oil and gas industry?

~ A. Yes.

~ Q. And as we see in this resume, you have published in your field on a number of occasions?

~ A. That's correct.

~ Q. And you've appeared to give expert testimony before the Ontario Energy Board on I believe two

prior occasions and were qualified at that time to give opinion evidence?

~ A. Well, nobody said that I couldn't.

~ Q. Here we are again.

~ Now, we have your original report in Exhibit 7.1 under tab 4(b) and that report was prepared on February 22nd, 1996.

~ Subsequent to that, the parties entered into an agreement following the ADR session that was held before the Board and I understand that as a consequence you have issued a revision to your report dated March 11th, 1997 which is now filed as Exhibit 7.3?

~ A. That is correct. I essentially revised the report to reflect the agreed volume of residual gas,

and in the revised Exhibit No. 7.3 I underlined every instance where there was a change made in the original report.

[Cochrane dr ex (Waque) Page: 162]

~ Q. All right, then. For expedition, I will be referring and asking you to refer to Exhibit 7.3 and if

I take you to page 4 of Exhibit 7.3, can I ask you to briefly describe the model or approach you used to calculate the value of gas, the residual gas?

~ A. Well, essentially there is a certain volume of residual gas left in the reservoir in 1968 and was still in the reservoir in 1990.

~ This volume of gas had a value and the approach that I used was to calculate the value of this

gas reserve if it was produced into the open market from the landowner's point of view.

~ Q. All right. Now, do you normally undertake evaluation of oil and gas properties for clients as part of your consulting practice?

~ A. Generally. It is a function of what the clients wish and what the industry is doing.

In the year 1990, I did eight reserve evaluations for seven different clients.

~ Q. All right. Is the method you followed in this report the same as the method that you followed in your everyday practice in 1990 to value reserves?

~ A. Yes. This is a fairly standard method of analysis. It has been adopted by the industry for the evaluation of reserves.

~ Q. All right. Now, in giving his evidence yesterday, Mr. Inwood described the value from his perspective at one moment in time when the ownership of

[Cochrane dr ex (Waque) Page: 163]

the gas in situ or in place in the ground changed.

~ In your work, did you assume a transaction based on a one-time transfer of the gas?

~ A. No. Essentially the gas was going to be produced on the open market over a period of time.

~ Q. Now, what principal components did you include in your model to estimate the value of the gas if

produced by the owner?

~ A. Well, in any analysis, essentially what
you start off with is, first of all, to determine if there
are recoverable reserves that are economic.

So you do a

 certain number of tests in order to find
this out because
 there is no point wasting the client's time if the
 reserves start off to be uneconomic.

~ And then you create -- you assemble all the
technical information that's available from the prior
history of the pool and from the geology

and whatever

 other things to determine a number of parameters
which you

 can use in the study. Because when you're projecting
income and operating costs into the future for a
commodity

 like natural gas, which is very sensitive to market
forces, there are limits to the accuracy
of any report

 that you can make. So there really is no
unique solution
 to the value.

~ So what you attempt to do in the first
 instance is that you try to
create models which will limit
 the value. According to Mr. Waque, the current
technology

 here is to bracket the problem.

[Cochrane dr ex (Waque) Page: 164]

~ Essentially you try and find out what an
 optimistic value of the reserves would
be and then a
 pessimistic value and then when that analysis is
done and

 you get a range of the numbers, then you have an
 opportunity to come back and refine some
of the parameters

 that you used, if it's possible, and to bring
the number

 within finer limits. And this is essentially the approach
 that I took in this study.

~ What you do is create a number of models
 which reflect both ends of the spectrum. And

then you sit down and determine what parameters are going to most affect the economics of the production. In this case, there were two primary parameters which were going to affect the production.

~ First of all, it was the capital cost that you had to spend in order to put the pool back into production. And the second thing that was quite critical was how fast you could put the gas into the open market.

~ Q. All right. Can I take you then to page 6.

~ The top of page 6, you have a capital cost summary, and does this indicate the two capital cost cases that you inputted into your model?

~ A. Yes, it does.

~ Essentially, it's -- the two cases are, first of all, you assume that when the pool was on production in 1968, there were facilities in place. The most valuable of those facilities was the pipeline which

[Cochrane dr ex (Waque) Page: 165]

would take the gas from the field to the sales market line. If that line was still in place and could be used by the producer of the gas, then that would be a cost that would not have to be entailed. If you had to build the pipeline, then there would be a certain capital cost for that.

~ And what I did was I took the nearest pipeline, which I felt had enough capacity to handle this production at the time, and estimated the cost of building a line from the field to that pipeline.

~ So that, in case one, the capital cost, let's assume that there was no pipeline needed, construction necessary, so the number was \$98,000, if you had to construct a pipeline plus the other facilities, you would come to a number like \$330,000.

~ Q. In terms of the pipeline, was there a

pipeline there - I think it's
a self-evident question but
for the record - was there a pipeline there
to produce the
gas?

~ A. There must have been a pipeline present
in 1968 because the gas was sold at that
particular time.

Since that time, though, Union was
very -- very helpful in
constructing a six-inch line right to the site.

~ Q. So there was one there in the past and
there is one today?

~ A. That is correct.

~ Q. But notwithstanding that, you developed
a second case which imposed the cost of building a

[Cochrane dr ex (Waque) Page: 166]

10

pipeline on the owner?
~ A. That was right because that is a cost
that a producer would have to accept if he wanted to
produce the gas in normal circumstances.

~ Q. All right.

~ And then you address the other parameters of
value on page 6, which includes the
issue of how quickly
the gas is produced over time?

~ A. That is correct.

~ That's the second biggest factor in this
analysis. If you're looking at producing gas and you're
dealing with present value, which we'll get into in a few
minutes here, the faster you produce the
gas, the more

value it has. In general, it's a function of the price
escalations.

~ And so, in this case, I put the model
together where you could produce
the gas quite quickly.

And you would get a high value for doing that.

~ The other factor that affects the rate of
which you can produce gas is the reservoir
itself. And so

you may want to, as a matter of economics,
produce the gas
as fast as possible, but the reservoir may

not allow you

to do that. And so the second case was
assuming that the
reservoir had some limitations and would not be able to
produce gas at the rate you like it over
a period of time.

~ Q. All right.

~ And then, with respect to future gas prices,
how did you deal with that?

[Cochrane dr ex (Waque) Page: 167]

11

~ A. Future gas prices, I prepared an
escalation -- a forecast of the prices.

~ One of the things that's happening these
days that becomes a relatively easy thing to do because,
in Calgary, the consultants and everybody gets together
and generally decide what the forecast is going to be.

~ So, in this particular instance, I adopted a
forecast very similar to one that was

in common use in

Calgary at that particular time. And I was quite
interested to see that when the report -- when I saw the
report by Sproule and Associates, that we were in quite
good agreement as far as the forecast of
gas prices. And

that's not because we're that much smarter; it's just
because the consultants in Calgary have got together and
come up with a number that is the best that they can.

~ Q. All right. Now, putting all those
factors together, you came up with four cases.

~ And can I take you then to page 8 of your
report, and can you summarize the four cases for

us, and

the results?

~ A. Perhaps, the easier place to do -- okay.
This is also summarized in Exhibit 15--

~ Q. Right?

~ A. --which actually gives the numbers.

~ Just to be continuous here, for the benefit
of the Board who may not be into

this kind of performance,

once you determine what the models are that
you can live

with, then you can -- you can go to computers, and it's

[Cochrane dr ex (Waque) Page: 168]

the one good thing that computers do for you
 is that they
 can spin out all kinds of models for it.
 ~ So once you've decided on what the
 parameters that you want to use in a study are, then you
 can put the numbers into the computer and they will
 generate the numbers for you.
 ~ So that is, after I -- I just want to list
 the parameters that go into the calculations, but I'm not
 going to belabour them. You can do
 that at your leisure
 if you want to read the report.
 ~ The factors that have to go into the
 computer are essentially the initial
 gas production, so
 you have to assume what kind of gas production you're
 going to get right off at the start.
 ~ You've got to put a decline rate in there as
 how fast you expect the gas to be produced.
 ~ You have to determine what interests that
 you're actually evaluating.
 ~ And then you have to forecast the price.
 And price, you have to start off with an
 initial price,
 and that's usually the price that's available at
 the start
 of whenever your effective date is, and then
 you put the
 forecast of the gas prices.
 ~ The other element that has to be addressed
 is the operating costs. Now, the
 operating costs have to
 be calculated from various sources, and then they have to
 be escalated in various cases, as well.
 ~ And then the final thing is the initial

[Cochrane dr ex (Waque) Page: 169]

capital cost, what cost you have to put into
 it before you
 can get it into production.
 ~ Now, you put all these numbers into the
 computer, the computer will present you with numbers in
 various formats, but it will tell you how long the

production will be economic for, what your recoverable
reserves will be down to the
abandonment pressure, and the
economic limit, whichever comes first, and
then what the

revenue will be to the working interest or net revenue
interest, as the case may be.

~ In this particular case, there are four
models. The model has four components which
I have listed

as case C1, C2, D1 and D2. And case C in general is where
you have a uniform decline; in other words, the decline
rate for the pool is uniform over a long
period of time.

In this case, I assumed an exponential rate. And case C1
in this case would be the case where your capital costs
are \$98,000.

~ Q. That's using the existing pipeline?

~ A. Case C1 is -- yes, \$98,000 where you use
an existing pipeline and case C2 would
be -- excuse me a

minute while I check that out. That's right, C1 is the
case where we use the existing pipeline. C2 is the case
where we construct a pipeline.

~ And similarly, case D is the case where you
get the gas out as fast as you can, and D1 would be using
the existing pipeline, and D2 would be the case where
you're using -- where you're constructing a new line.

[Cochrane dr ex (Waque) Page: 170]

14

~ Q. All right. Then can we turn to your
conclusions on page 8?

~ A. The conclusions are better demonstrated
in Exhibit 15 actually if you'd like to turn to that. If
you look at Part 2 of Exhibit 15
on the revised figures,

you can see that the range of values are
starting on the
left and moving to the right. If you assume
that there's

no pipeline construction so your capital
costs are

\$98,000, then the pool will be on commercial production
according to this model for nine years and the value of
those reserves is \$965,000 to the hundred per cent working

interest.

~ If there's no pipeline construction but it takes 17 years to produce the pool, then the number falls to \$845,000.

~ If you have to build a pipeline, of course the capital cost has to be paid out of the production, so that the numbers fall. And if, in the first case, which is D2, the numbers are \$733,000 and on the low side they move to \$613,000.

~ So that is the value of the reserves according to the parameters that we used in the model and it assumes that you just take the money as it comes. You can look at it as if it was an income property that you were happy to take the income over a number of years. Those would be the numbers that you would get.

~ The next component that comes into the analysis, though, is the time value of money because if

[Cochrane dr ex (Waque) Page: 171]

15

you make an investment in the bank, you assume an interest rate. There is money. There is a value for -- let me regroup on that. If you invest -- if you put money into the bank at a certain interest rate, you expect a certain rate of return and your capital will increase over time. If you do the exact opposite, then you're expecting a rate of income and you want to find out what that income is now -- what that present value of that income is, then you do the reverse thing and we call it a discount factor. And, of course, the discount factor is a variable and in most analyses of reserves in economics, we ask the client what a discount -- range of discount factors that he's interested in and print those out. That's one of the

wonderful things that computers can do for you.
~ In this particular case, we selected a
discount rate of 11 per cent per
year. Essentially the
rationale for that was explored in one of the
interrogatories, but we figured that 11 per
cent per year
in 1990 was the rate of interest that you could get in a
long-term bond and it was my opinion at this time because
if we're dealing with a reserve that's pretty well been
established - the pool was on production for
quite a few
years - that there was a small, a relatively
low risk in
the oil and gas business that you could produce that
487,000 cubic metres of gas.
~ And so part 3 of Exhibit 3 is essentially
the range of present values for the models that were
presented in this study at a discount factor of 11 per

[Cochrane dr ex (Waque) Page: 172]

16

cent per year. Now you can see that they range from a
high of \$717,000 to a low of \$321,600.
~ Q. What is your conclusion then or your
opinion as to the fair and equitable sum to be assessed
for the reserve in question, residual gas in question?
~ A. Well, that is essentially what the Board
is here to decide. Essentially what this study does is to
show you the range of values that is possible for the
present value of the gas if it was
produced into the
economic market over a period of time.
~ MR. WAQUE: Thank you, those are my
questions in-chief.
~ THE PRESIDING MEMBER: Thank you, Mr. Waque.
~ Mr. Sulman?
~ MR. SULMAN: Mr. Cochrane, good morning.
CROSS-EXAMINATION BY MR. SULMAN:
~ Q. In addition to the extensive resume that
you filed, Mr. Cochrane, I understand that you've got a
reputation as somewhat of an historian in the Ontario
Petroleum Institute.
~ A. Well, I guess if you say so.
~ Q. Well, I do.
~ A. Thank you.

~ Q. Do you disagree with me on that?
~ A. Well, I do what I can.
~ Q. Thank you. The reason I ask you that,
Mr. Cochrane, is that you have knowledge
and experience of
drilling in Lambton County over the years and
so I just
[Cochrane cr ex (Sulman) Page: 173]

17

wanted to ask you a couple of quick questions in the
beginning about that.
~ Do you have an idea of how many exploratory
wells have been drilled in Lambton County?
~ A. Not for a precise number. In geological
terms, we call it a very mature exploration area.
~ Q. Well, can you give me a range of -- I
know you can't tell me to the last decimal of how many
exploratory wells, but can you give me an idea?
~ A. Oh, probably in the order of -- I just
couldn't bring my mind to that right at the present time,
I'm sorry.
~ Q. Okay. So you wouldn't know whether it's
over 2,000 or under 2,000?
~ A. It is probably -- well, I suspect it's
over 2,000.
~ Q. Do you know how many production pools,
actual production pools there are in Lambton County?
~ A. I should, I did quite an extensive study
on it. Unfortunately the study was done over
such a short
period of time that the numbers are a blur, but I would
believe that there could be at least 300 or 400.
~ Q. Thank you, sir. Do you know how many
storage pools there are? That should be
available.
~ A. There's 22 I believe at the present
time.
~ You mean designated storage pools?
~ Q. That's correct.

18

[Cochrane cr ex (Sulman) Page: 174]

~ A. There's 22.
~ Q. Yes. Thank you, sir.
~ Now, as I understand your evidence, sir, you
indicated that the amount of gas between

the shut-in

pressure and the 50 pounds per square
inch by definition

is the residual gas. Have I understood that correctly?

~ A. That's correct.

~ Q. Do you know of any physical or
geological impediment to Imperial Oil producing
the gas,

this residual gas, by definition, prior to 1990?

~ A. No, I don't think there is any reason
why that couldn't have been put into the open market.

~ Q. Okay. Produced and put into the open
market?

~ A. Yes.

~ Q. Now prior to injecting the
non-indigenous gas, or I think that's how you
refer to it,

as non-indigenous
sir, but it is variously referred to

gas, non-native gas. Am I correct with my terminology?

~ A. No, my term would be storage gas, but --

~ Q. I thought you used non-indigenous, but
maybe that was Mr. Inwood. You would agree with me that
non-indigenous is not a common industry term?

~ A. Yes.

~ Q. Prior to injecting the non-indigenous
gas into this pool, was there any physical
or geological

impediment to prevent Union as the operator and joint
venture partner with Imperial from producing the gas?

[Cochrane cr ex (Sulman) Page: 175]

19

~ A. I am not aware of any particular problem
in that respect.

~ Q. So in your study there is no, and in
your opinion as an expert there is no physical or
geological impediment to producing the gas?

~ A. Correct.

~ Q. Okay. Now, if the joint venture then
were to produce -- had produced the gas; that
is, what we

are defining as the residual gas in 1990,
what value would

the joint venture have received for this gas in the
marketplace?

~ Is that the \$2.84 figure that you have been using?

~ A. If you could have sold it all at one particular time it would have been \$2.84 per thousand, but

if you are into the production business, even with a fairly significant compressor you could not produce the gas in one year.

~ Q. Okay. So it would be a figure that would be starting at \$2.84 and varying over the production period?

~ A. That would be right. If you could produce -- start in July of 1990, the first price you would get would be \$2.80 and then you would be getting whatever the market was paying at that particular time for the rest of the production.

~ Q. Okay. I take it then if the joint venture in turn were to replace that gas over that same

[Cochrane cr ex (Sulman) Page: 176]

20

period of time, it would have to pay the same amount in the marketplace that it received on producing and selling into the marketplace? I take it that's intuitive?

~ A. Yes, I suspect that's the case.

~ Q. So if the joint venture had decided in 1990 - and I say the joint venture because, as you are well aware, it was not Union but Union and Imperial - if the joint venture had decided in 1990 to produce the residual gas, are you aware of any reason that would have prevented them from doing so?

~ A. No.

~ Q. What was the shut-in pressure of this pool?

~ A. According to the analysis by Mr. Sproule, it was 266 psia as of the last measurement.

~ Q. When you say Mr. Sproule, you mean...?

~ A. Sproule and Associates report.
~ Q. Thank you. So I understand, it is
technically possible to be produce the gas below that
shut-in pressure? Technically possible?
~ A. Yes.
~ Q. With the addition of compressors, as
you've suggested, it's the ability to produce gas below
that shut-in pressure would be --
~ A. Yes. The shut-in pressure just is the
starting point for the production.
~ If you are going -- if your sales market
line, for instance, has a 60-pound maximum operating

21

[Cochrane cr ex (Sulman) Page: 177]

pressure, then you can free-flow gas from the existing
wells right into your sales gas line with a
certain amount
of processing.

~ Once the flowing -- but the field will not
maintain that 266 pounds once it
goes on to production
because if you produce gas, the pressure is
going to fall.

~ At some point in time you are going to --
the flowing pressure of the gas is going to
fall below the
sales volume pressure in which case compression is then
necessary to move the remaining gas from the
wells up to
the level of your sales volume pressure.

~ Q. Okay. So there is nothing that would
technically prevent gas being produced below the
reservoir

pressure? We are in agreement on that?

~ A. Yes.

~ Q. Now, I was asking you about production
in 1990 prior to injection, prior to the
first injection
of the gas storage cycle.

~ If Imperial had produced what we are calling
the residual gas at that time, what
would the landowners
have received by way of payment?

~ A. The landowners would receive a royalty
as specified in a petroleum and natural gas lease

primarily, but this royalty was amended by a unit operation agreement and that unit operation agreement, if I'm correct, specified a landowner royalty of 2 cents per thousand cubic feet of gas.

~ Q. Now, I would ask you to turn up your
[Cochrane cr ex (Sulman) Page: 178]

22

the evidence and that would be not the update of
evidence,
but your evidence that's dated November 1994.

That would

be tab 2. I would like you to just briefly look at
paragraph 21.

~ A. Which document?

~ Q. It is your prefiled evidence entitled
"Prefiled Evidence of Robert Osborn Cochrane" and it is
dated 30th of November. It is in the application at tab
2. Just immediately before your curriculum

-- the list of

exhibits and curriculum vitae that you referred to.

~ MR. WAQUE: I am providing the witness with
my copy.

~ MR. COCHRANE: Thank you very much, Stephen.
Carry on.

~ MR. SULMAN: Q. Do you have that in front
of you now, sir?

~ A. I do, sir.

~ Q. Can you look at paragraph 21, please.

~ A. Yes.

~ Q. I will read it to you:

~ "During the storage operation, the
~ remaining gas in place will become
~ commingled indistinguishably with the
~ injected gas. As a consequence it is not
~ possible to differentiate between the
~ indigenous and the injected gas during the
~ withdrawal cycle."
~ If I can end there.

23

[Cochrane cr ex (Sulman) Page: 179]

~ I take it that the statement that you made
there you still believe to be accurate?

~ A. Yes, I do.

~ Q. The only reason I ask that, sir, is it
was almost three years ago.

~ A. I had no reason to change my opinion in that time.

~ Q. Thank you, sir. The opinion that you've indicated, that the gas, remaining gas would become commingled indistinguishably with the injected gas or what I have referred to as the non-native gas or non-indigenous

gas, that's a general view that the industry takes?

~ A. Yes.

~ Q. Okay. Thank you.

~ Now, once it is -- that is, once the residual gas or the remaining gas is indistinguishably commingled with the interjected gas, I take it what that means is that as gas is then withdrawn it is impossible to

differentiate between the native gas and the non-native

gas or the non-indigenous gas?

~ A. Yes.

~ Q. And that as the withdrawal cycle goes on, both native gas and non-indigenous gas are produced from the wells and from the formation?

~ A. Yes.

~ Q. I take it then that it is intuitive that

over a period of withdrawal cycling, I guess it has now been six years since the date of first injection, have I

[Cochrane cr ex (Sulman) Page: 180]

24

got that right first?

~ I realize we are in 1997 and the first injection was 1990, but from your knowledge of the industry would that be a six-year injection/withdrawal cycle?

~ A. I think you have to talk to Union Gas about that.

~ Q. They are the experts in that area?

~ A. Sorry.

~ Q. Take it, if you would, for purposes of this question, assume that it is a six-year injection/withdrawal cycle, the first injection being in 1990 and we have not got to July 1997 yet for the next injection; is that a fair assumption?

~ A. Yes.

~ Q. So over that six-year injection/
withdrawal cycle -- by the way, do you know how much in
this pool how much gas is injected in a regular cycle?

~ A. Sorry, I don't follow the procedures for
injecting and withdrawal of gas in storage pools.

~ Q. Okay. Do you know the volume in this
pool then from your studies?

~ A. Do you mean the storage volume?

~ Q. Yes, sir.

~ A. I saw the number somewhere, but I
certainly wouldn't want to introduce it as evidence from
my memory.

~ Q. Okay. So you don't know whether it is 1

[Cochrane cr ex (Sulman) Page: 181]

25

bcf or 10 bcf?

~ A. Oh, it's not one of the best storage
pools in Ontario, so I suspect it would be less than 1
bcf.

~ Q. But substantially higher than 487 mcf?

~ A. Yes, I would hope so.

~ Q. So over that six-year period of time
there has been injection and withdrawals
of natural gas,
and I take it in what you've said in your evidence at
paragraph 21, the so-called residual gas has
now in effect
been withdrawn from this pool?

~ A. Not necessarily. If you are into
statistics, it could still all be there, two
per cent of
it could have been produced, a hundred per cent of it
could have been produced. You know, gas being gas, it
doesn't really allow for figuring out which gas comes out
and which gas goes in.

~ Q. Exactly. I think that's your point in
paragraph 21, isn't it, sir?

~ A. Exactly.

~ Q. That it is indistinguishable --

~ A. But your point you seem to be driving at
is that it is quite possible that all of the gas, the
residual gas has been produced or
withdrawn from the
reservoir as part of the storage recycling

process and I

couldn't even make a comment on that because, as I say, it
could be one -- it could be zero
of actual residual gas

that's produced or it could be a hundred per cent. It's
[Cochrane cr ex (Sulman) Page: 182]

26

not something that can be ever determined.
~ Q. That's right, sir. I'm not driving at
any point, I'm just trying to understand your evidence.
~ It is appears from what you've said that it
is impossible to determine whether all of the
indigenous
gas has been withdrawn now or only part of it or
some part
of it?

~ A. Exactly.
~ Q. That's all I'm trying to understand.
Molecules don't -- there is not red molecules of gas and
blue molecules of gas--

~ A. Nicely put.
~ Q. --they are all indistinguishably
commingled? You are nodding, sir.

~ A. That's right, there are no red molecules
and no blue molecules.

~ Q. That's right. That's what I am trying
to understand, sir.

~ I want to look at the most recent evidence
that you filed and that would be the
evidence that Mr.

Waque walked you through in direct and
that is what is now
entitled Exhibit No. 3 -- 7.3.

~ A. 7.3.

~ Q. Do you have that in front of you, sir?

~ A. Yes, I do.

~ Q. I just very briefly want to look at page
3 of the evidence.

~ You were asked a question by Mr. Waque, I

27

[Cochrane cr ex (Sulman) Page: 183]

take it, as your instructions to
-- direction in
preparation of this report, in fact that's what you have
said, the report is written in answer to

the question:

What was the value in 1990 of the remaining recoverable reserves of natural gas in the Sombra pool if the sale of gas had been resumed at the time and continued until the economic limit or abandonment reservoir pressure of 50 psa was reached?

~ A. That's correct.

~ Q. Now, in your response to the question, have you assumed that in July 1990 Imperial Oil or Union

Gas could no longer produce gas from the pool?

~ A. No. That was not part of the question essentially. It was if someone could have produced the gas at that particular time, what was the value?

And the

someone that I assumed because of the nature of this thing, that the landowners would be able to, for some reason, to produce the remaining residual gas reserves at that particular time.

~ Q. I see. Did you make the assumption that the landowners had the right to produce and sell natural gas?

~ A. No, I didn't assume that they had the right, but I assumed that someone had the right and because I was representing the landowners I took their part because they could -- essentially the landowners themselves could produce the gas with a minimum payment of royalty to third parties.

[Cochrane cr ex (Sulman) Page: 184]

28

~ As you see, when I do the analysis that my working interest and net revenue interest in that analysis

are still both a hundred per cent.

~ Q. I see. So the study that you have done, aside from the fact that you are doing it as a result of

questions from the landowner applicants, the

study that

 you have done has determined the value
that the person who
 had the right to produce the natural
gas would obtain in
 the marketplace in 1990?

~ A. That is correct, but, in this particular
case, I must say that I assume that there would be no
royalty paid.

~ In other words, the working interest -- the
owner of the gas would also be -- would
own 100 per cent
 of the gas and have 100 per cent revenue
coming from that

gas. You would not be paying a royalty to a third party,
any third party.

~ Q. Only because you're working for the
landowners did you assume that they had the right to
produce?

~ A. That's right.

~ Q. Okay. So you make no determination--

~ A. That's a legal --

~ Q. --in your study who has the right to
produce?

~ A. That's a legal issue, and that's not my
concern.

~ Q. That would be dependent upon, in your

[Cochrane cr ex (Sulman) Page: 185]

29

experience in the oil and gas field in Lambton County,
dependent upon who had oil and gas leases and who had unit
operating agreements like you've referred to earlier?

~ A. Exactly, the operator of the pool.

~ Q. Right, exactly. Thank you.

~ There was one other interesting - and I
don't want to dwell on this, but I was trying to
understand it - you spoke about your analogy to the bonds,
to investment in a bond.

~ You were telling Mr. Wague, in direct, that
if you put money in the bank - let me just make sure I
wrote this down correctly - if you put money in the bank,
you would expect, in 1990, or put it in bond, you would
expect to get an 11 per cent return--

~ A. That is correct.

~ Q. --is my understanding on that?

~ And I think you said that if you were to put
 money in the bank, you would see your
capital grow at that
 rate?

~ A. Exactly.

~ Q. Okay. When I put money in the bank,
 unfortunately, I get 11 per cent return
some -- I did in
 1990, but I also had to pay tax at a 54 per
cent rate.

~ A. That's -- but that is a problem that's
 endemic to every Canadian citizen. I don't
think you have
 to look upon yourself as being special in that, so --
 [laughter]...

~ Q. I was trying find common ground between
[Cochrane cr ex (Sulman) Page: 186]

30

 you and I, not all other Canadians, Mr. Cochrane.
~ No, what I'm asking, Mr. Cochrane, is if I
 were to put the money in at 11 per cent in
1990, I would
 also take into account my 11 per cent return
would be then
 discounted by whatever tax I have to pay to
come to my
 ultimate return?

~ A. From your point of view, you know, it's
money -- you're looking at money in your pocket at the
 end. That's -- that's what everybody does who is
 investing, but, no, you don't need to -- it's not
 necessarily that you're going to -- you are
going to pay a
 certain percentage to Revenue Canada, but there are other
 factors that come into effect.

~ You know, one of the ways you can reduce
your paying off revenue to Internal Revenue on that amount
is not to earn any other income in 19 -- in the
 appropriate years, in which case, you would entitled to
 the full 11 per cent.

~ Q. I understand that. I'm just trying to
 understand then, in your analysis when
you come up with 11
 per cent, is it a before or after tax amount?

~ A. It's always before tax, unless my

clients asks for an after-tax analysis.
~ Q. Okay, thank you. So the analysis --
that's all I really want to know, Mr. Cochrane--
~ A. Yes.
~ Q. --so the analysis done here --
~ A. And I can make it quite clear that all

31

[Cochrane cr ex (Sulman) Page: 187]

of the numbers that are in my testimony are before income
tax values because, essentially, for the
majority of my
clients they have accountants and various legal advisors
who worry about their income tax implications
of their
investments.

~ MR. SULMAN: Okay, thank you, Mr. Cochrane.
Those are all the questions I have.

~ THE PRESIDING MEMBER: Thank, you Mr. Sulman
~ Mr. McCann?

~ MR. McCANN: Yes. Thank you, Mr. Chairman.
CROSS-EXAMINATION BY MR. McCANN:

~ Q. Now, Mr. Cochrane, in your
examination-in-chief, you've made reference to the
remarkable ability of computers to generate a range of
results or outputs from various mathematical models,
but I
take it you would agree with me that in determining this
claim for compensation, the only mathematical
models, the

only results that the Board should be interested in are
those which have valid and well-founded assumptions at
their basis?

~ A. I would hope so.

~ Q. And, that leads me to want to ask you
some questions about the assumptions in your evidence.

~ Now, first of all, in your revised
evidence

which is dated March 11, 1997, you've
very helpfully

underlined the changes that are made from your previous
evidence; is that true?

~ A. That's true.

32

[Cochrane cr ex (McCann) Page: 188]

~ Q. But I take it that the -- all of those

underlined passages reflect the ADR agreement that the remaining recoverable reserves are 487-million cubic feet?

~ A. 487-thousand cubic feet.

~ Q. I'm sorry.

~ A. That, in fact, is correct.

~ The only change in the document was those changes necessitated by the reduction of the residual gas

to the agreed number.

~ Q. Great, thank you.

~ THE PRESIDING MEMBER: Mr. Cochrane, I believe -- would you repeat the number again because, I believe--

~ MR. McCANN: Yes.

~ THE PRESIDING MEMBER: --Mr. McCann was correct.

~ MR. McCANN: Can I refer you to the first page of text of your evidence and the first underlined passage there, and it reads:

~ This report was revised in March 11th, 1997 to reduce the remaining recoverable reserves from 598-million cubic feet to the 487-million cubic feet.

Revisions have been underlined.

~ MR. COCHRANE: A. That's right.

~ Q. And that 487-million cubic feet was the amount agreed to in the ADR agreement to

which reference

has been made in the --

[Cochrane cr ex (McCann) Page: 189]

33

~ A. That's right. I'm just getting confused because we're changing our --

~ Q. Yes?

~ A. Our references here, but --

~ Q. We're going to try to discuss this in MCF, if we possibly can.

~ A. Okay.

~ Q. Now, you've described in some detail the assumptions that were made -- well, let me,

first of all,

say that what I'm looking at is the first page, particularly point five of your evidence, but also Exhibit 15 which is the very last page of your evidence to which reference has been made.

~ I'd like to ask you, for example, if we go
to point five on the first page,
certain assumptions have
been made here.

~ The first case, and I take it now that's
case C1, I see:

~ The constant exponential decline of sales
~ at 13.38 per cent per year for a period of
~ 17 years.

Can I ask you how those, how "13.38 per cent" and "17
years" were chosen?

~ A. It's quite a specific number.
What you do, you can -- it's a
mathematical calculation.

If you know how much your initial gas production
is going
to be, in this case, from the various numbers I estimated
it to be 250,000 cubic -- let's get
it right, the mcfs,

[Cochrane cr ex (McCann) Page: 190]

34

250 mcf per day, and you know that
you're going to have
487,000 mcf of gas in the reservoir, and you
assume that
it will decline at an exponential rate which is an
assumption which we have empirically
found from decline
rates of oil and gas pools in general,
then you just need
to plug that number into your computer and it comes up
with the rate of decline at
which the gas will produce,
and it can -- and because it is a calculated number, it
can go from -- to be quite -- quite specific, and so, in
this case, it's 13.38 per cent.

~ Q. So would it be fair to say that what you
wanted to do in carrying out your study was
there were any
number of possible scenarios on how gas might be
produced.

You wanted to show one which was a fairly
modest decline
each year over time and another which started out with a
fairly modest decline but then fell precipitously?

~ A. Exactly, and that case is illustrated graphically on Exhibit No. 7 in the figure that we're talking about.

~ The part here is essentially if your annual gas sales on the "Y" axis, and your year on the "X" axis, and the value, with heavy squares on it, is producing the gas at a constant decline over a long period of time.

~ And the second case there where the crosses are is the model that produces the gas at a very much more rapid period of time.

~ Q. Could you just identify which of those would correspond to C1 and which would correspond to D1?

[Cochrane cr ex (McCann) Page: 191]

35

~ A. C1 would be the slow decline rate is the 13.3 point -- the one with the black squares which says "constant decline" is the one that would be your moderate decline over a very long period of time.

~ Q. With your indulgence, Mister -- I'm sorry, Mr. Cochrane. Go ahead and finish your thought.

~ A. I'm finished, unless you want more.

~ Q. With your indulgence.

~ And I believe that in your assumptions you assumed a production rate of 250 mcf per day. You've

already made mention of that--

~ A. Initially.

~ Q. --initially, at least, and this would decline.

~ A. That's right.

~ Q. Can I ask what was the basis of your assumption of 250 mcf per day as a production rate?

~ A. If you look at Exhibit No. 5 in that same document, Exhibit No. 5 is another graph that the numbers are actually in the report, but the graph is meant to show you how it's good -- does.

~ On the "Y" axis here, we have the daily gas production on an mcf per day basis and on the "X" axis, we

have the year. And this is a graph of the average daily gas production from the date that the pool went on in 1954 to the time it was shut in, in 1968. And you can see half way through the graph where I have my arrows a range from 1956 to 1966, the range of flows varied from 230 mcf a day

36

[Cochrane cr ex (McCann) Page: 192]

to 430 mcf a day.
~ One of the things that I be don't know from the information that's available is whether those flow rates were dictated by the ability to sell gas into the open market or whether those were dictated by the amount of gas that could be produced from the wells.

~ And so, for this particular analyses, I could have chosen any particular number from 230 to 428 mcf a day. To be on the conservative side, I took the 250 mcf a day.

~ The work that Sproule Associates did in their report where they did a whole bunch of sand face calculations and that suggests that the reservoir could produce at larger rates than the 250 mcf a day, I did not

have that information available at that time.
~ Q. In looking at this, at Exhibit 5 to your evidence, if one looks at the shape of the graph after the period that you've marked with arrows "range of flows" which is roughly -- and that ends roughly in 1965, there seems to be a quite steep decline after that.

~ A. Yes. That was one of the things that made me select the 250 mcf a day rather than the 400. I didn't know whether that is a function of -- once again of the operator's choice to start reducing the production or whether it was a function of the market or a function of the well capacities themselves.

~ Q. So just to return once more to the underlying assumptions, would I understand it correctly

[Cochrane cr ex (McCann) Page: 193]

this way, that assuming the 250 mcf per day of production which is a conservative assumption, and assuming a scenario of constant but gentle decline and assuming another scenario of small decline at the beginning and

then sharp decline, the figures that you've used in terms of the decline rate and the number of years represent the production of all the producible gas in that pool?

~ A. Exactly.

~ Q. Okay, thank you. Now perhaps we could turn to your Exhibit 15 to which you made reference before. And part 1, if I understand it correctly, is just

a simple calculation showing the posted gas price in July 1990, of \$2.84 per mscf. The remaining gas reserves which

we've already discussed, you multiply one by the other and you get the value of the reserves?

~ A. Exactly.

~ Q. And that's a kind of a raw number to start out with, a benchmark against which the assumptions below which we'll get to in a minute can be - I don't want to use the word compared - but measured against to some degree or seen in common --

~ A. In context.

~ Q. -- context. Context is a good word, thank you.

~ And I take it that it would now be your view that it's reasonable that valuing a hypothetical cost of production, a deemed cost of production, is a reasonable way of valuing the gas, the residual gas in the Sombra

[Cochrane cr ex (McCann) Page: 194]

pool?

~ A. This is -- yes, this is a standard practice in industry.

~ Q. Now, you've described in some detail the assumptions that underlie part 2 and part 3. I'd just like to direct your attention for a moment to --

and we'll

have to go back here to page 6 of your evidence and the capital cost summary.

~ May I ask you, for example in case 2 which assumes new pipeline, the quoted price is \$8 per foot.

Can I ask the basis for assuming \$8 a foot as the cost of that pipeline?

~ A. I hadn't constructed the pipeline for a few days, but I called some of the contractors, my favorite contractors, and asked them to give me a rough price for the installation of \$29,000 feet of three-inch line and that was the number that I received.

~ Q. Are we talking about steel pipe or plastic pipe or...?

~ A. Yes. Well, there are a range of options, but the contractor I talked to would be putting in three-inch yellow-jacketed steel pipe.

~ Q. And I take it then from what you're saying, that that \$8 a foot would include construction costs and labour costs?

~ A. Right-of-way constructions, you know, everything to get that pipeline in the ground and serviceable.

39

[Cochrane cr ex (McCann) Page: 195]

~ Q. Okay. Can I ask you the same question with regard to the purchase and installation of a compressor which is a number that occurs in both scenarios?

~ A. Yes. What I did there was I pulled out my petroleum engineering book there and calculated what

kind of horsepower that I would need to move the gas at the rates that I was going to look at. The compressor that's required requires about -- I think it's 35 -- sorry, 30 horsepower of -- be able to -- will have a size

of 30 horsepower and then I called up a contractor and had him quote on a price for a compressor installed at -- for

it to do that job.

~ Q. Would that be a portable compressor or a

permanent installation?

~ A. The size of the compressor, 30 horsepower, would be portable just because of its nature of its size. So if you're going to put it in there for 17

years, you would put it in there as a permanent installation. If you could get the gas out of there in five years, you'd put it in such a fashion that you could salvage the compressor at the end and recover some capital costs.

~ Q. Can I ask you a similar question with regard to the purchase and installation of the desiccant dryer?

~ A. A similar process went through. Fortunately, recently I've purchased a desiccant dryer for

[Cochrane cr ex (McCann) Page: 196]

40

one of my clients so that I didn't even need to call a contractor.

~ Q. And I'm going to ask you the same question about the meter site.

~ A. The meter site is a number that's specified by Union Gas. So at the present time if you want to sell gas in Lambton County to Union Gas, they will charge you \$25,000 for the privilege of having a meter site.

~ Q. And can I just go back up to item A which is the pipeline again? And I'm sorry, I meant to ask you, what underlay the assumption of 29,000 feet of three-inch pipeline?

~ A. If you look at -- there's an exhibit in this report. It's Exhibit No. 8. There is a pipeline of which I am aware of because some of my clients sell gas into it that runs north/south just between the 'R' and the 'A' in Sombra. If you just look at the label Sombra there--

~ Q. Yes.

~ A. --it runs between the 'R' and the 'A' and you can see the arrows.

~ Q. Yes.

~ A. That pipeline has an operating pressure of approximately 185. It varies from

150 to 200 pounds
per square inch and that was the line
I targeted because I
knew it had some capacity without having
to harass Union
Gas and ask them if there was one that was closer.

41

[Cochrane cr ex (McCann) Page: 197]

~ Q. And that's a Union Gas pipeline, the one
that runs between the 'R' and the 'A'?

~ A. It is a Union Gas pipeline, yes, it is.

~ Q. And then on Exhibit 8 is marked proposed
pipeline route from the Sombra pool to that pipeline?

~ A. And that's 29,000 feet of line.

~ Q. Good. Thank you. Now, in making
assumptions about the production of gas from
the pool,
were any assumptions made about the delivery
of the gas;

for example, was it assumed that it
would be delivered to
Union?

~ A. Yeah. As of 19 -- the gas marketing
business has just exploded in the last few
years, but in
1990, Union Gas was the best company to sell gas
to. That

wouldn't necessarily be the case in 1997.

~ Q. But, therefore, you did assume in your
research in your study that delivery
of the gas would be
to Union Gas?

~ A. No, I didn't really assume that. I
assumed -- nowhere did I specify that
it would go to Union
Gas, but the price that was being posted
at the time was

Union's price.

~ Q. And did you make any allowance in
determining production cost, for example, for
acquiring

easements from private landowners?

~ A. I assumed that would be in -- well, the
anticipated line would be on present road

allowance, and

so that most of the pipeline would be on public

42

[Cochrane cr ex (McCann) Page: 198]

right-of-ways, so there was a limited necessity to use private lands for the use. A meter site would have necessitated the rental of a small piece of property for

the meter site near the connection with the Union Gas sales line. Usually they're about -- well, 100-feet-by-100-feet square, so it's not a great expense.

~ Q. And I take it that if the pipeline were to be laid on road allowance, there would have to be agreements with the municipality which might be a township

or I'm not quite sure -- Sombra Township, I believe?

~ A. That is correct.

~ Q. And in your experience, are there negotiations that take place as to a cost of making use of the road allowance?

~ A. It varies from township to township. Sombra Township is fairly used to having gas pipelines on

their property. And the last time I built a pipeline in

Sombra Township, which was many years ago, there was no

cost. There were some requirements for restoration of properties and damages, but there was no extra cost other

than -- restoration costs, I guess, is what -- is the only thing that was used.

~ Q. Thank you. One moment, panel.

~ But to your knowledge, Borden & Elliot's clients don't have any legal agreements as of this time with Sombra Township to lay pipe along the road allowance?

~ A. No. I think that would be quite presumption on our clients.

43

[Cochrane cr ex (McCann) Page: 199]

~ Q. Okay, thanks very much.

~ Now I would like to take you back to Exhibit 15. I don't really want to belabour this too much because we've been over this quite a bit. Just before I

specifically refer to Exhibit 15, with regard to the
assumed price per mcf to be paid by
Union for Ontario
production, can you provide us with any information on the
price that's paid in 1996?

~ A. Unfortunately my client who kept me up
to date in the gas business sold their assets
last year,

so I'm a little bit behind. The market price has been
quite high at least on the spot market. It's been quite
high at the end of the year. So that I would anticipate
that the projection that we made
would be fairly accurate
and it will be here somewhere if you want the actual
number.

~ Q. Can I ask the basis of the -- one
moment, panel.

~ Can we talk about your forecast of prices
for a moment and I think it is page 7
of your evidence.

Well, can you just describe how these prices were
forecasted? Are they forecasted on
the basis specifically
of what Western Canadian producers might
be asking for
their gas or on the basis of what Union might be paying
Ontario producers?

~ A. Well, for the first -- because this is
a -- for the first part of the price, because this is an
after effect kind of thing, the actual price that was --

[Cochrane cr ex (McCann) Page: 200]

average posted price by Union was used for those years
which I knew what prices they were.
~ The second component was now you are moving
out into 'no man's land' when you are projecting
it into
the future.

~ What I made allusion to earlier, is that the
Calgary consultants got together and came up with a
forecast of the prices. Their forecast
of prices is
usually relative to the wellhead or
some delivery point
that's common as the gas leaves Alberta; for instance,

Empress or something like that.

~ What I did essentially is to take that out and add a component to it for the transportation and delivery to spot in Ontario.

~ I don't exactly remember the methodology, but it would be using a Toronto city gate price or some relative price where I could get some idea of what the totals were for moving the gas.

~ Q. You have not considered the fact that Union may have been paying less since 1995 to its Ontario producers that had been paying for Western produced gas?

~ A. Not directly, but intangibly that's a fact of life. So that it was probably subconsciously built into my calculations.

~ Q. Can you expand on that a little bit, "subconsciously"? We are having difficulty with the word subconsciously over here.

~ A. Oh, well. There are certain --

[Cochrane cr ex (McCann) Page: 201]

45

petroleum engineering in its nature is not an exact science. So that you use a lot of judgment when you are doing this in order to try and get a number which you can live with.

~ Unfortunately, not all of the numbers that you come up with are demonstratable by evidence.

~ Q. Okay. It would be fair to say that you have applied your expertise and looked at a range of prices and--

~ A. Exactly.

~ Q. --made an expert judgment as to what forecast --

~ A. I was quite happy to see that the report from Sproule and Associates Limited, who did it independently from another province, had numbers that were very similar to mine.

~ Q. Can I just ask you, still in relation to natural gas price forecast, the last sentence in that paragraph:

~ "For price escalation, the industry is

~ projecting a 10 per cent per year increase

~ for '97 and '98 and then a 3 per cent per
~ year increase thereafter."
What was the basis for that?
~ A. That was the numbers that I had received
from Calgary's projection forecasts.
~ Q. Now, I would like to take you back to
Exhibit 15. I think this has been explained in some
[Cochrane cr ex (McCann) Page: 202]

46

shows a detail, but just to remind ourselves, it
range of values for the remaining gas reserves that goes from
\$321,600 at the lowest to \$965,200 at the highest --
sorry, \$965,200 at the highest. Thanks.
~ Now, you referred I believe in your
examination-in-chief to optimistic and pessimistic
scenarios.
~ Could you identify which of these scenarios
you would characterize as optimistic and which is
pessimistic?
~ A. I thought that would be immediately
obvious. When you are in the oil and gas business --
~ Q. Well, lawyers are thick-headed and we
like to bring these things out.
~ A. In the oil and gas business, the higher
value of the dollar is the one that is most optimistic.
So the \$965,000 is the optimistic one, and the \$321,000
would be the pessimistic one.
~ Perhaps optimistic and pessimistic are not
really the terms that you could use. The upper range of
values based on my analysis would be \$965,200 and the
lower range would be three hundred and twenty-one six.
~ Q. Now, you have explained in --
~ THE PRESIDING MEMBER: I'm sorry Mr.
Cochrane, you may want to revisit those numbers.
~ You use 965 which is part two of your
evidence and you use the \$321,000
which is part three of
your evidence. One is undiscounted, the other is
[Cochrane cr ex (McCann) Page: 203]

47

discounted.
~ MR. COCHRANE: That's right. But it was the
Board Staff lawyer here that reviews that range of values.
We're not talking apples and apples when we are talking

about that.

~ THE PRESIDING MEMBER: I thought the questions related only to part two of that Exhibit 15, but in any case...

~ MR. McCANN: No, I'm sorry, Mr. Chair. I think the witness interpreted my question correctly, but you are raising a good point.

~ Part 2 and part 3 are based on rather different assumptions. Part 3 is the discounted value and part 2 is the undiscounted value.

~ THE WITNESS: Exactly.

~ MR. McCANN: Q. We have discussed the basis of why would one would discount or one would not discount.

~ So just to be absolutely clear then, the lower range of values in part 2 would be \$613,700, the upper range of values would be \$965,200. That's the undiscounted value of the remaining gas reserves.

~ Looking at the discounted value of the remaining gas reserves, the lower range would be \$321,600 and the upper range would be \$716,700?

~ A. Exactly.

~ Q. Now, you have explained the assumptions that underlie these values at some length.

~ Can I ask you which of these scenarios in

[Cochrane cr ex (McCann) Page: 204]

48

your view and in your experience seems the most reasonable basis to value these reserves in relation to this claim for compensation?

~ A. I don't -- you know, my job is essentially to provide a range of values. It's up to the Board to make the decision as to which one they pick.

~ This is no different from any other client that I work for. I provide them with a range of values and then they take it from there.

~ Q. One moment, please.
~ Would you agree with me that in projecting
the value of the remaining gas reserve it
would be more in
accordance with a reasonable valuation to look at the
discounted values in part 3 rather than the undiscounted?
~ A. That's a particularly interesting point
because it depends from where you are coming.
~ If you are going to be selling the property
now or relatively close to this time, then the present
value of that property is important.
~ If you were, say, a landowner and looking at
the production from the property as an income property,
then the undiscounted value is the number that you hope
that your estate will use.
~ So it depends on your perception, but
present value is for sales. Undiscounted value is for
income.
~ Q. The assumptions underlying this all seem
to assume that it will take time to produce the gas in
[Cochrane cr ex (McCann) Page: 205]

49

these reserves. It is production over time.
~ A. (nodding)
~ Q. Would that not suggest that the
discounted value is a more realistic model to value the
gas given that its value has to be assessed
over the
deemed period of production?
~ A. Yes.
~ Q. One moment, panel.
~ Thanks very much, Mr. Cochrane. Those are
all my questions.
~ THE PRESIDING MEMBER: Thank you, Mr.
McCann.
~ The Board has some questions.
~ Ms. Drozd?
~ MS. DROZD: Thank you, Mr. Chair.
EXAMINATION BY MS DROZD:
~ Q. Mr. Cochrane, you've mentioned on a
couple of occasions that this is standard
valuation
practice in the industry.
~ My experience with valuations, which I
assure you is not in valuations of natural gas reserves,

has been that different valuations, different methods of

valuations are used for different purposes.

~ Would you say that this is standard practice for purposes of transfer of ownership, for calculating a

lease, for what purpose?

~ A. At this particular stage in Sombra pool, there is -- virtually all the types of analysis would lead

[Cochrane ex (Drozd) Page: 206]

50

down the same road.

~ So that from this analysis you should be able to determine interests of just about everybody who would have an interest in the production or the pool.

~ Q. Thank you. I wasn't particularly limiting my question to Sombra pool. You said -- I think

I believe you said that sort of 1990 you had done nine evaluations for seven clients. What was the purpose?

What was the reason for doing those evaluations?

~ A. There are a number of reasons why these evaluations are undertaken. The primary reason is for

providing technical information to buyers and sellers during the transfer of interests.

~ Many companies do this kind of analysis for their annual reports, public companies do this kind of analysis on a regular basis. It also is used in the same context for their ceiling tests for accounting purposes to make sure that the depreciation and calculations are correct.

~ The third use of this kind of analysis is for financing of oil and gas projects.

~ Q. This would be standard practice in all four of those types --

~ A. The methodology that is used is fairly common. There are all sorts of twists depending

on the

nature of the project, but the mechanism is fairly standard.

~ Q. Thank you, Mr. Cochrane.

[Cochrane ex (Drozd) Page: 207]

~ MS. DROZD: Thank you, Mr. Chair.
 ~ THE PRESIDING MEMBER: Thank you, Ms. Drozd.
 ~ Just a couple of questions, Mr. Cochrane.
 EXAMINATION BY THE PRESIDING MEMBER:
 ~ Q. On page 7 when you referred to the
 forecast on average price, you mentioned
 a forecast that
 comes from Alberta. Is it is a particular publication you
 had in mind?
 ~ I don't think I heard a name of a
 publication or the organization.
 ~ A. There is a forecast that has recently
 been put together by a consulting company in Calgary
 that's available to certain subscribers. The company is
 Chenery Dobson Resource Management.
 ~ What they do or have undertaken over the
 past few years is they go to selected clients and banks
 and ask them to publish anonymously what projections of
 gas forecasts that they are using at the present
 time, and
 they combine them and do a statistical analysis and
 present those subscribers with kind of a composite
 of what
 the industry is thinking.
 ~ Q. How much history does that forecast
 have?
 ~ A. How do you mean? How long has it been
 done?
 ~ Q. How long has it been around, yes.
 ~ A. It is relatively recent. I think it is
 three or four years since it has come into place.

[Cochrane ex (Presiding Member) Page: 208]

~ Q. You have no sense about the
 predictability or the accuracy?
 ~ A. How accurate they have been.
 ~ Q. Yes.
 ~ A. Well, the report that comes from the
 consultants does not say this is
 going to be the price.
 ~ They give the statistical analysis of what
 the consultants in Calgary are all thinking about, but I
 don't think -- I'm sure, I haven't read the fine print,

but I am sure there is a disclaimer saying that they have no recourse if the price doesn't turn out to be what they expected.

~ Q. Just a small point, Mr. Cochrane. When you referred to \$2.84 per mscf, what's the 's'?

~ A. We get a little bit sloppy in our terminology here. The mscf stands for thousand standard cubic feet and the standard means that it is at a standard pressure in temperature because with different temperatures and pressures the volume of gas changes.

~ Q. All right. Thank you. Now, there was some questions with respect to the discount rate that you have used. I think Mr. Sulman established that that was an after-tax rate?

~ A. No.

~ Q. I'm sorry, I apologize.

~ A. For all my calculations they are before-tax calculations.

~ Q. It was pre-tax calculations?

[Cochrane ex (Presiding Member) Page: 209]

53

~ A. Exactly.

~ Q. So if I have to assume, say, a tax rate of 50 per cent, that would then double the discount rate?

~ A. I would have to think about that. You know, from an experience point of view, I would anticipate

that to be correct, but I just can't turn my mind to that. I can't answer that in short notice.

~ Q. Okay. Direction is going to go up?

~ A. Yes.

~ Q. The question is --

~ A. There's no question that the direction of the discount factor is going up. I just can't tell you whether it would be double or not.

~ Q. But if it were not double, it would be substantially more; it would be close to doubling?

~ A. Yes, significantly different.

~ Q. And do you have any sense as to if you were to double, for purpose of my question, if you were to double the discount rate to 22 per cent,

what would be the
sensitivity on your scenario part 3, of a pool life of 17
years which, right now, based on your scenario,
gives you

\$321,600.

~ A. There would be a significant reduction
of the highest discount factor I've used in the analysis
is 15 per cent and to which part, certainly which -- if
you tell me which one it was, I can
tell you what it is at

15 per cent. Was it part 3?

~ Q. Part 3, yes?

[Cochrane ex (Presiding Member) Page: 210]

54

~ A. It would be D2, case D2 is that..?

~ Q. That would be case C2?

~ A. Case C2? Case C2 at 15 per cent would
be 410,000.

~ Q. What exhibit are you looking at, sir?

~ A. I'm looking at the previous exhibit --
sorry, the previous exhibit is Exhibit No. 14.

~ Q. Okay. And I see that --

~ A. And, at the bottom of the page, you can
see the accumulative net income for various

-- for various

values of the discount factor, and the largest one that
I've used is 15 per cent. And the number is 259 -- sorry,
it's 259,000.

~ Q. So it does go down by sixty-thousand-or
so-dollars by using --

~ A. Exactly.

~ Q. All right. So everything else being
equal, if I were to use 20 or 22 per
cent, then I would be

looking at \$120 to \$150,000 and change?

~ A. I think that would be correct.

~ Q. And that would bring us down to well,
321 plus or minus \$120,000?

~ A. You're about half way there.

~ Q. I'm half way. Okay.

~ MR. McCANN: Would any purpose be served,
Mr. Chair, by an undertaking from the witness
to provide

this data?

~ THE PRESIDING MEMBER: Well, does the

[Cochrane ex (Presiding Member) Page: 211]

witness feel comfortable with the numbers that he just gave, or would you rather make another run?

~ MR. COCHRANE: Well, I would feel -- being a technician, I would feel more happy to get in front of my computer and generate through the numbers, but I think what you're say is approximately correct.

~ MR. WAQUE: Mr. Chairman, excuse me, I have some re-examination on that point. Maybe, we could leave the undertaking until after the re-examination.

~ THE PRESIDING MEMBER: I'll be happy without an undertaking there.

~ MR. COCHRANE: Thank you.

~ THE PRESIDING MEMBER: Thank you, Mr. Cochrane. Those are the Board's questions.

~ Mr. Waque, you do have some re-direct?

RE-EXAMINATION BY MR. WAQUE:

~ Q. Let's start with the last point first, Mr. Cochrane.

~ If you use a discount rate of 22 per cent and assume the tax rate of 50 per cent, do I take it that what you're assuming is an after-tax return of 11 per cent, approximately?

~ MR. COCHRANE: A. Could you rephrase that one, so I can think about it for a minute.

~ Q. If you use -- if you use the consideration of tax to double the discount rate from 11 per cent to 22 per cent, the consequence of that thinking is that you want to ensure in your analysis an after-tax

[Cochrane re ex (Waque) Page: 212]

return of 11 per cent?

~ A. Yes.

~ Q. All right. And if I went into the marketplace in 1990 to buy a long-term bond, and I got a return at 11 per cent, what would be my after-tax return in my pocket, assuming a 50 per cent tax rate?

~ A. It would be half.

~ Q. It would be half.

~ So if you were doing a after-tax analysis, you would take half of the discount rate; you would not double it?

~ A. I'm sorry, you're starting to boggle my mind here, Stephen.

~ Q. All right. Maybe, we can leave that for argument.

~ Let me return to the thick-headed lawyer approach Mr. McCann suggested.

~ You mention in response to questions he put to you with respect to the flow rate, that Sproule used, in their calculations, a higher rate of flow then you did?

~ A. That is correct.

~ Q. Now, just so we understand the impact of that on the analysis. If you hold all other factors constant, and you employed a higher rate of flow, such that like that that Sproule employed, in your analysis, would your values go up or down?

~ A. It would be -- the value of the property would go up considerably.

57

[Cochrane re ex (Waque) Page: 213]

~ Q. All right.

~ Now, Mr. McCann also asked you about the pipeline and where it was going. And you directed our attention to Exhibit 8. And in fact if we look at Exhibit 8, we see that there are closer pipelines in place that could be reached?

~ A. That's correct.

~ Q. All right. And, in fact, in their analysis, did Sproule assume a longer or shorter pipeline?

~ A. Sproule Associates report, in one of their cases, assumed a shorter pipeline, one of 5500 feet.

~ Q. All right. Now, if you hold everything else constant, and you adopt Sproule's shorter pipeline, and you employ that in your analysis, does the value go up or down?

~ A. The value of the -- because you have less capital cost invested in the project, the value is

going to go up.
~ Q. All right?
~ A. One additional thing there though, is if
you get into a pipeline with a higher pressure, you may
need a bigger compressor to get into there
and so you may
have an offset in capital cost.
~ Q. Just so that we have the direction. If
you assume all other things constant, and a shorter
pipeline, the value has what direction?
~ A. Up.
~ Q. Now, you were also asked questions about

58

[Cochrane re ex (Waque) Page: 214]

your price predictions. And, as I understand your
analysis, you have employed a price for gas, a market
price for gas of \$2,25 for 1996; is
that correct?

~ A. That is correct.
~ Q. Now, if we learn later that, in fact,
the market price for gas for 1996 is
a higher amount,

this --
~ A. That would increase the value of the
property, as well.

~ MR. WAQUE: Thank you. Those are my
questions in re-examination.

~ THE PRESIDING MEMBER: Thank you, Mr. Waque
~ Mr. McCann, there are no other matters, so
we can excuse the witness.

~ MR. McCANN: I think we can, Mr. Chair.

~ THE PRESIDING MEMBER: Thank you, Mr.

Cochrane. You are excused now.
---Witness withdraws.

~ This would be a good time to take a break
then and, according to the clock on the wall,
it says
eight minutes to eleven. We'll return
at ten minutes

after.
~ MR. McCANN: Could I just say one thing,
before we break, Mr. Chair.

~ We may wish to ask the parties to begin
thinking about argument and the best way
in which argument

could be made in this case, and the
most efficient way,
and the panel will wish to be considering that, as well.

59

[Page: 215]

~ I don't know exactly when we want to
address it, but we may start turning our minds to it.
~ THE PRESIDING MEMBER: That's fine. When
you do get your minds on it, perhaps you
can advise us

after lunch. Thank you.

~ MR. McCANN: That's fine, thanks, Mr. Chair.

---Recessed at 10:52 a.m.

---On resuming at 11:19 a.m.

~ THE PRESIDING MEMBER: Please be seated.

~ Mr. Sulman, we're in your hands.

~ MR. SULMAN: I'm pleased to have that
awesome responsibility, but has the evidence in-chief been
completed, just for the record? I've got my people up
here assuming that it has, but I didn't hear anything.

~ THE PRESIDING MEMBER: I believe it has.

~ MR. SULMAN: Okay then, I was -- now that
things are in my hands, I would ask that
the witnesses

come forward and be sworn, then I'll briefly introduce
them and ask questions of them.

~ JOHN CARLSON,

~ NORA STUART,

~ DAVID ROBERT LOWE,

~ ALISTAIR LUCAS,

~ BEVERLY HOWARD WILTON; Sworn.

~ MR. SULMAN: Mr. Chairman, Members of the
Board, if I can introduce everyone as we go
along and then

I think what I'll briefly do is ask them to tell you what
their role is in today's evidence so you will
know who's

who on a rather large panel and then I've got
some direct

questions I'd like to ask them.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 216]

60

DIRECT EXAMINATION BY MR. SULMAN:

~ Q. First, immediately is Mr. John Carlson.
Beside him is Nora Stuart. Both Mr. Carlson

and Ms. Stuart are employed by Sproule Associates Ltd. I hope I got that all correct.

~ And beside Ms. Stuart is David Lowe of Union Gas Limited. Beside David Lowe is Professor Alistair Lucas of the University of Calgary, Faculty of Law. And beside Professor Lucas is Bev Wilton, who you've heard about previously in his role at Imperial Oil, and is now a lands agent at Union Gas.

~ So if I could start with you, Mr. Carlson. If you could explain to the Board what your role in today's evidence is?

~ MR. CARLSON: A. I'm here to speak to the report prepared in part myself entitled "Technical and Economic Assessment of the Sombra Gas Pool" as it relates to the issues in front of this Board at this hearing.

~ Q. Mr. Carlson, do you adopt the prefiled evidence that has been filed in the name of Sproule Associates Ltd.?

~ A. Yes, I do.

~ Q. Ms. Stuart, what is your role in today's evidence?

~ MS. STUART: A. Very simply --

~ Q. Now, you may have to, because we've got more bodies on the panel than we have microphones -- I'm not sure whether you're accustomed to these microphones,

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 217]

61

but they are all voice activated. They're live all the time and you may have to get the microphone directed at you so that the Board can hear and the court reporter can hear. I say that to everyone. And when you're not speaking, you may want to turn it away so there's not a reverberation or mumbling. Please proceed.

~ MS. STUART: A. My purpose in this proceeding is to speak to the Sproule report, the technical and economic assessment of the Sombra gas pool

as well as to comment on evidence of the Applicant.
~ Q. Thank you. Mr. Lowe -- before I leave
you, Ms. Stuart, do you adopt the
evidence that's been
prefiled in this proceeding?

~ A. Yes, I do.
~ Q. Okay. Mr. Lowe, your role, please.
~ MR. LOWE: A. Yes, I'm here to speak to the
issues of ownership, price and practice as follows: I'll
be presenting a short case summary statement. I'll be
speaking to Union's prefiled evidence, the
report entitled

"Development of Unitization in Oil and Gas Pools Operated
by Imperial Oil in Ontario", the gas storage report to the
Lieutenant Governor-in-Council by the Ontario Energy Board
dated May 4th, 1964, the Reasons for
Decision in EBO 64-01
and -02, the Bentpath compensation hearing,
the various
interrogatory responses, as well as
responses to the
prefiled evidence of the Applicant.

~ Q. Thank you, Mr. Lowe. And do you adopt
the evidence of Union Gas Limited prefiled in this
[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 218]

62

hearing?
~ A. Yes, I do.
~ Q. Professor Lucas, can you tell us what
your role is in today's evidence?
~ PROF. LUCAS: A. I'll be speaking to the
agreements including the lease, the unit operation
agreement and the storage lease agreement. I'll also be
speaking to the question of ownership
of the natural gas
that's in issue here and as well to the practice in other
jurisdictions for resolving disputes of this kind.
~ Q. Thank you, sir. And do you adopt the
evidence that is prefiled as Union Gas
Limited evidence?

~ A. Yes, I do.
~ Q. Thank you, sir.
~ Mr. Wilton, what is your role in today's
evidence, sir?
~ MR. WILTON: A. I'm here to assist the

Board with respect to practices in the resolution of
residual gas payments for pools which are
being converted

from production to gas storage operations.

~ Q. Sir, will you also be able to speak
about what happened in 19 -- your role in 1990 briefly for
us as an agent of Imperial Oil?

~ A. Yes, I would.

~ Q. Okay, thank you, sir. And do you adopt
the evidence as filed under the title of Union
Gas Limited

insofar as it relates to the role that you
play in today's
evidence?

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 219]

63

~ A. Yes, I do.

~ Q. Thank you.

~ Okay, if I could go back again and start
over. Mr. Lowe, you indicated when you told
me what role

you're going to play in today's evidence, you said that,
in part, that you would be dealing with policy
issues and,

more or less as the chairman of the panel if you will.

~ Can you summarize the role of the members of
the panel from your point of view and Union's position in
the proceeding?

~ A. Yes, I can.

~ Q. Can you pull that microphone a little
closer to you, please?

~ A. It doesn't have an extension cord on it.

~ THE PRESIDING MEMBER: Actually, Mr. Lowe,
you can pull the other one as well. You
can have two. We

find that it works better that way.

~ MR. LOWE: Yes. Ms. Stuart and Mr. Carlson
from Sproule & Associates will be speaking to the issues
of ownership price in other tribunals from the perspective
of experienced evaluators of natural gas properties.

~ Mr. Lucas will speak to the same issues from
the legal perspective.

~ Mr. Wilton will be able to provide
information on the directions he received
from Imperial

Oil in the negotiations in 1990 as well as speaking to other matters from a historical perspective in the compensation of residual gas in Ontario.

64

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 220]

~ I will be speaking to matters generally related to leasing practices and policies of Union Gas and other historical perspectives.

~ The basis of our case in these proceedings are as follows: The witnesses will explain that this is not an involuntary taking of gas case as presented by the

Applicants. Union's panel of witnesses will indicate that the petroleum and natural gas leases, unit operations agreements and the gas storage lease agreements are there in place as valid agreements in these proceedings.

~ As you heard from the landowners yesterday, Union has maintained all of the lease payments in good standing. The witnesses will further explain in greater

detail than I'll present in a summary that Union has retained the right to produce the residual gas and to develop any remaining exploration potential within deeper formations within these properties in question in the future. The witnesses will explain that

the right to

produce the residual gas -- and that this right has not been frustrated or forfeited by the actions of going to the storage service.

~ The witnesses will further explain that the language in clause 16 of the gas storage lease agreement

anticipates the commingling of the residual gas with the injection gas such that they are indistinguishable, and

that language is right in that clause.

~ The payment for residual gas is provided to reimburse the landowner for the royalty interests that

65

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 221]

would have otherwise been received had production continued under the unit operations agreements and which

is anticipated by the lease to take place during the withdrawal of storage gas.

~ The witnesses will indicate that the appropriate rate of payment for the lessor's interest in

the residual gas is two cents per mcf as set out by contract in the storage lease agreement and the unit operations agreement.

~ The witnesses will indicate that just because the landowners would like to negotiate a better deal, there's no obligation by the lease agreements to do so.

~ It is Union's assertion that the terms of payment as agreed to by the parties in the leases are clear.

~ The witnesses will further show that Union's position is supported not only by the lease agreements themselves but also past practices in the industry, historical precedents and previous decisions of this Board. That basically concludes my summary account of Union's position in these proceedings.

~ Q. Okay. Mr. Lowe, in your prefiled evidence, you filed a document entitled "The Imperial Oil Report". Can you explain why you filed that and what the significance of it is to this case?

~ A. Yes. The Imperial report outlines the process by which Imperial Oil management had selected the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 222]

66

royalty rate for use in their unit operations agreements

for gas and oil production in Ontario. The report shows the various royalty rate options that were considered by

Imperial which included percentage royalties, sliding scale royalties, square root royalties, fixed well payments and fixed rate royalties.

~ The report also shows that the alteration of the existing rates that were in place at that time were being considered to be altered to values

as high as 12-1/2

per cent because of the discovery of the Payne pool. The

Payne pool had been discovered to be able to be capable of
proceeding 40-million cubic feet per day
and it was far in
excess of anything that had been experienced
to that point
in prior discoveries.

~ MR. McCANN: Could I just interject for a
moment? Board Staff doesn't seem to have a copy of the
report that Mr. Lowe is referring to.

~ MR. SULMAN: It was filed in the prefiled
evidence. If you don't have one, we can get you another
one.

~ MR. McCANN: It doesn't appear to be on the
List of Exhibits.

~ MR. SULMAN: It probably wouldn't be. It's
not part of Sproule's evidence.

~ MR. McCANN: It's not part of Sproule's
evidence. It's not part of the evidence of Union Gas
Limited.

~ MR. LOWE: It can be found in a spiral-ring

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 223]

67

binder that was filed.

~ MR. SULMAN: I can see my friend has his
with him.

~ MR. McCANN: Okay. Well, we must have a
copy and we'll make sure we get it. Thanks very much.

~ MR. SULMAN: But if it's easier, Mr. McCann,
we'll make another copy, what ever is easiest for you.

~ MR. McCANN: Does the Panel...?

~ THE PRESIDING MEMBER: Yes, we do have
copies of this.

~ MR. McCANN: You do have this. Okay, that's
fine.

~ THE PRESIDING MEMBER: In fact, that is
referenced in the Union Gas exhibit. I guess it's 9.1, is
it? In Exhibit 9.1 there is a reference made
to that

report.

~ MR. LOWE: I have an extra copy here that
I'd be happy to lend to Board Staff in the interim.

~ MR. McCANN: That's very kind of you.

~ Sorry, I have no wish to interrupt the flow
of proceedings. Thanks very much.

~ MR. SULMAN: Q. Mr. Lowe, would you

conclude your comments on the significance
of the Imperial
Oil report.

~ MR. LOWE: A. Yes. As Mr. Cochrane spoke
to this morning, the evidence before this Board is that
the Sombra pool is capable in its remaining production
life to be capable of producing in the neighbourhood of
[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 224]

68

250,000 to 300,000 cubic feet per day which, under the
considerations at the time in the Imperial Oil report,
would not allow it to receive any further than 3
per cent

royalty. The 12-1/2 per cent royalty
in the Imperial Oil
report was reserved for pools that were capable of
significantly better production than that value.

~ Q. What you're talking about right now, Mr.
Lowe, is that the scale that -- or akin to
the scale that

Mr. Inwood told us about yesterday?
~ A. Yes, it would be exactly the same scale
that is currently found in many leases in Ontario and
still being leased today. The report shows that
the final

selection of the royalty rate of
two cents took into
consideration the economics of production in Ontario as
well as consideration to what would be fair, just and
equitable compensation for the landowners.

~ Q. Okay. Now, I'm not sure whether Board
Staff has this report that I'm about to refer to next, but
in your evidence, Mr. Lowe, you also filed a document
entitled "The Gas Report to the Lieutenant
Governor-in-Council". Do you have a copy of that? My
friend does.

~ The gas storage report that I'm referring
to, can you explain that significance to
this proceeding?

~ A. Yes. The gas storage report outlined
nine principles or requirements that the Ontario
Energy
Board recognized for the determination
of compensation of
residual gas.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 225]

~ Principle 1 of that evidence states that the
 compensation for residual gas should be based
 on the compensation for the lost royalty payments.
 The royalty payments in this case as outlined
 in the unit operations agreement is two cents per mcf.

~ Q. So, the principle that you just spoke
 about, the primary principle in this Board's report to the
 Lieutenant Governor-in-Council, can you tell me what the
 significance of that principle is to this case, in your
 opinion?

~ A. Yes. It's my opinion that the principle
 supports Union's evidence that the residual
 gas payment is in lieu of the lost royalty.

~ It implies that where there is a rate
 specified in the agreements that that
 is the rate that should be used in evaluation of compensation of residual
 gas.

~ This principle has been supported in a
 number of arbitration cases, including the Payne
 pool and

the Bentpath pool, and it has been the basis of all the
 residual gas payments for all gas storage pool
 developments in Ontario over the last 30 years.

~ Q. You mentioned the Bentpath compensation
 case. What, in your opinion, is the significance
 of that case to the matters at hand?

~ A. Yes. The significance of the Bentpath
 compensation hearing, EBO 64, in that decision
 it explains how the Board decided an application for
 the determination

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 226]

of compensation for residual gas.
 ~ In that case, the same issues of residual
 gas ownership, price compensation and practices of other
 jurisdictions were reviewed quite extensively.

~ At the time of the decision, which was only ten years ago relative to this case, in 1982, the marketplace at that time had leases of 12-1/2 per cent royalties.

~ There were even higher gas prices in place to be considered by that Board, and in summary I guess all of the outside influences were very similar to what exists in this case.

~ In that case, the Board determined that the language in the agreements, which were exactly the same storage agreements as are being dealt with in this case, meant that the gas storage agreements... Excuse me for a

second.
~ So we have established that the leases were exactly the same. There were ten landowners in that case who sought standing before the Board. The five landowners with exactly the same gas storage agreements as are here

were not giving standing in front of the Board.

~ They concluded in that case that the language was clear and the compensation for them was not dealt with in the hearing. The only landowners that were given standing were those landowners who did not have gas storage agreements.

~ In the final conclusions that they drew in [Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 227]

71

that case, in the absence of the gas storage agreements,

the Board looked to the unit operations agreement, royalty rate of two cents per mcf and that was the award in that case to the landowners.

~ Q. Okay. So that case occurred and the decision was rendered in 1992 (sic.). How has that decision influenced Union's compensation policies?

~ MR. WAQUE: I think my friend must mean '82.

~ MR. SULMAN: Did I not say 1982? Well, the

record will show. I think I said 1982.

~ THE PRESIDING MEMBER: I thought it was '92
you said.

~ MR. SULMAN: Well...

~ MR. ROBERTSON: What is it, '82 I think.

~ MR. LOWE: '82 case.

~ MR. SULMAN: It was a 1982 case, decided in
'82. Compensation in this case relates to 1990.

~ Q. Mr. Lowe, would you tell us how the
Bentpath pool decision from 1982 influenced
Union's
compensation policies?

~ MR. LOWE: A. Yes, I can. Union has
considered this decision by the Board to
be a landmark
document which has set precedents in many areas of
landowner negotiations.

~ The decisions in that case not only dealt
with the compensation for residual gas, but also
additional acreage, rentals and a number of -- and

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 228]

~ petroleum and natural gas lease payments.
In that regard, Union has relied heavily on
that Board's decision to successfully reach a settlement
with the landowner compensation committee in the
settlement of its landowner compensation packages
in 1985,
1990 and 1994.

~ Union has felt bound by this decision in its
negotiation strategies and has the contracts in place to
show that. The decision to continue to offer
the two cent
agreement to the landowners in the Inniskillen 28 pool
which was a subject before this Board in 1988,
we stood by
our ground in that case as well and continued to
offer the
two cents per mcf.

~ All of the landowners in that pool have
accepted payment at that rate.

~ Q. Okay. Now, Mr. Lowe, those are some of
the policy issues I wanted to discuss with you. If we
could turn up your evidence, there is a schedule
A at the

back of Union's evidence. I will give you a moment to turn that up.

~ A. Yes, I have that in front of me.

~ Q. I'll just give everyone else an opportunity to turn that up.

~ That schedule A is entitled "Reported Royalty Payments on Residual Gas (Union pools)". Okay?

~ A. Yes. There is also a page 2 of that schedule which deals with the pools of the other storage companies in Ontario, as well.

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 229]

73

~ Q. Okay. Can you explain to me what the significance of that table is to the matter at hand?

~ A. Prior to dealing with that, perhaps I could just explain how to read this.

~ Across the top we have the case numbers and pool names of each of the pools; the date of first injection; the abandonment pressure that was stated in the

lease for which we had to pay the residual gas down to; the royalty rate that's set out in the storage lease; the

abandonment pressure that the lease specified that the pool was to be paid to -- sorry, the pool pressure that

the owners paid the leases down to; the royalty rate that was paid for the settlements in each case; and, on what

basis the values were determined which signifies the areas

where the decision was made by arbitration; the last column indicates the party that was making the payments in

each case.

~ The table clearly shows that all the pools except for the Oil Springs East pool were paid out at the rates set out in the gas storage lease agreements.

~ The predominant compensation rate for residual gas in lieu of royalty prior to 1990 has always

been two cents mcf in accordance with

the gas storage
lease and the unit operations agreement. That
applies to
both Union leases and the Tecumseh Imperial leases.
~ In almost all cases, the rate in the gas
storage lease agreement was consistent with the royalty
rate in the unit operations agreement which
is exactly the

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 230]

74

case we have before us here.
~ With the exception of the Dow Moore pool,
where there were only corporate interests
involved, the
residual gas payments to the landowners
did not increase
to more modern rates of 12-1/2 per cent until 1993 and
then only in a few exceptional cases.
~ That's basically the importance of that
summary.
~ Q. You were here in the hearing room
yesterday, were you, Mr. Lowe?
~ A. Yes, I was.
~ Q. You listened to Mr. Inwood's evidence?
~ A. I did.
~ Q. I may not have Mr. Inwood's evidence --
I have a transcript and I will try to find
it exactly, but
I believe Mr. Inwood indicated that he sat -- that he was
satisfied that the majority of the leases he reviewed
contained a 12-1/2 per cent residual gas payment
in the

gas storage lease. Did you --
~ A. Yes, I heard him say that.
~ Q. Can you comment on that, please.
~ MR. WAQUE: Well, just before we do, let's
make sure we have the evidence right.
~ His evidence was the majority of the gas
storage leases executed since the late 1980s contain
12-1/2 per cent.
~ MR. SULMAN: No, that's what his written
evidence was. Mr. Lowe just referred to
his oral evidence

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 231]

75

given yesterday and I have the transcript of that now.

~ MR. LOWE: Yes. I reviewed Mr. Inwood's evidence both yesterday and the prefilled evidence. In one of the interrogatory responses he gave us a little bit better insight as to the various -- where he got his leases from and what pools, for example, were included in his '90 lease summary.

~ It is my determination from the evidence, as far as I can tell, that the survey is not a representative sample as it failed to adequately represent the holdings of two of the largest leaseholders in the region where residual gas clauses are likely to be paid in the future or have already been paid.

~ Union, Imperial and Consumers Gas are by far the largest leaseholder in Lambton County. Union alone represents over 40 per cent of the lease holdings in this area.

~ As far as I can tell, his '90 lease survey was the entire lease package that he reviewed for all the 30-year period that he reviewed.

~ So his restriction of leases to 1980 and forward is even a much smaller sample.

~ MR. SULMAN: Q. Were you here this morning, Mr. Lowe, in the hearing room?

~ MR. LOWE: A. Yes, I was.

~ Q. Did you hear Mr. Cochrane indicate, in fairness, give a rough estimate that there were about 2000 wells drilled in Lambton County?

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 232]

~ A. Yes. I have looked at it in the past and my number and my recollection is 1800. So I think we are fairly consistent on that.

~ Q. All right.

~ And of that, whatever that number maybe, 2000, 1800, he indicated that about 300 of them actually

resulted in production?

~ A. Yes, I heard that estimate as well.

~ Q. And he indicated that of that only 22 have resulted in and become storage pools?

~ A. Yes, there are 22 currently and I'm aware of three other -- four other pools that would be classified as storage candidates. So we might be looking at a sample as large as 26.

~ Q. What I'm interested in, Mr. Lowe, is that -- just to know of the 2000 wells that are out there, 22 storage -- there is 22 storage pools. Of those, I don't know whether you can, but can you tell me how many have a pay residual or paid a residual gas payment of above two cents per mcf?

~ A. Yes. The only ones were Oil Springs East pool which was voluntarily increased by Centra Gas, the Edys Mills pool where the landowners by contract were paid 12-1/2 per cent. The two other pools that were paid above that -- sorry, not paid above that, but in the representative sample were the Dow A pool where there were no landowners involved in the participating area; and the Dow Chemical, Dow Moore pool where, again, there was only

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 233]

a small commercial holding in that pool and their leases specified a 12-1/2 per cent payment.

~ Other than that, all the other pools were paid at two cents.

~ Getting back to the sample, though, there are just a few more points that I wanted to make on that.

~ Union currently holds over 400 leases which hold some 24,000 acres in Lambton County. Taking Mr. Inwood's sample of 90-some-odd leases out of a potential 1200 leases that might be held at any one time in the county, that represents a rough sample of about seven per cent.

~ Now, although statistically that may be a representative sample, I'm summarizing from the

interrogatory response that I reviewed that there is a significant lack of content of both Union Gas and Consumers' leases in his sampling.

~ Both the -- as a result of that, the Union leases and the Consumers leases are all at two cents. There is a significant lack of sampling of two cent leases in his sample.

~ In addition, I have been made aware recently through my involvement on the unitization committee development with the Ministry of Natural Resources that there have been -- a number of the major companies in Ontario having recently re-evaluated their position in a mature market, as Mr. Cochrane pointed out, are in the process or have been in the process of relaxing their

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 234]

78

12-1/2 per cent lease rentals in their production leases

down to a sliding scale royalty.

~ I've had further discussions in the past as part of the Edys Mills storage pool purchase with Mr. Bob

Opekar of RAM Petroleum who has redirected all of his funds out of Ontario into the Columbian gas discovery market for purposes of getting a better return on his investment in a mature market.

~ Those two things combined indicate that the marketplace is now moving back to a sliding scale royalty even though the evidence may be on the record

that there is a significant amount of 12-1/2 per cent leases out there.

~ Within Mr. Inwood's sampling, he only represented, as near as I can tell, three of Tecumseh's pools and only one of Union's pools. So that's only four pools out of the 22 pools available, and the only one from

Union that seems to have gotten into the sample is the Edys Mills pool which is the only pool that we hold that have 12-1/2 per cent leases.

~ So my conclusion of all that is that is not a representative sample.

~ In addition, I have conducted a specific search for the first three months in 1990 and very easily uncovered at least 40 leases where the sliding scale royalty is contained in the production lease agreements. That's further confirmation.

~ That's a fairly active market for a mature

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 235]
market and I think it represents a more representative sample of the leasing that's going on out there at the moment.

~ THE PRESIDING MEMBER: Mr. Sulman, so we can have it all in one place on the record, there was a reference by Mr. Lowe about an IR, an interrogatory. Could you give us a number for that so it can be in the same place in the transcript.

~ Also, Mr. Sulman, you referred to a transcript reference for Mr. Inwood and we may want to get the number for that.

~ MR. SULMAN: Page 57.

~ THE PRESIDING MEMBER: Thank you.

~ MR. LOWE: I apologize. I should have identified that in advance. I just can't seem to put my finger on it at the moment.

~ MR. SULMAN: Q. Could you look at Interrogatory Response No. 12, Mr. Lowe?

~ MR. LOWE: A. Which interrogatories, Mr. Sulman?

~ Q. The Union Gas response to the interrogatories from the applicant, I believe.

Union to

the applicants.

~ A. Oh, yes, sorry. I overlooked that in my scan here. It's Interrogatory 12(B), on page 25 of the interrogatory responses for Phase 2.

~ Q. Okay.

~ A. That identifies the four gas storage

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 236]

pools that were included in the sample.

~ THE PRESIDING MEMBER: Thank you.

~ MR. SULMAN: Q. Mr. Lowe, I'm going to try to direct you to the conclusion.

~ I'd like you to turn, Mister -- there's a table in Mr. Inwood's evidence. I wonder if you could

turn that up. That would be found at tab - make
sure I've
got it here - tab 4(a), and it's page 6 of Mr. Inwood's
prefiled evidence. It's table 2.
~ MR. LOWE: A. Yes, I have that in front of
me.
~ Q. And you can see in one column -- it's
got several columns in table 2 being the year,
the pool,
the seller, the purchaser, bip, or (bcf), and the value
for land rights. And I don't want to
misquote Mr. Inwood,
but I seem to recall him yesterday saying
that he had the
view that, although he couldn't tell us the exact amount,
that there may be an inclusion in the value for land
rights column of a payment for residual gas.
~ Did you hear Mr. Inwood in that regard?
~ A. Yes, I did.
~ Q. Okay. Now, were you involved in any of
the negotiations in the sale of any of these pools?
~ A. Yes, I was involved in the Dow Moore
pool and the Edys Mill pool, and I attended the Oil
Spring's East hearing, and I reviewed all the documents on
it, as well, I have reviewed all the documents
for the two
pools, Terminus and Wilkesport.

81

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 237]

~ Q. And what is your review with regard to
the inclusion of any residual gas payments
in the column
"value for rights"?
~ A. It's my conclusion, from review of the
evidence and the purchase and sales
documents where I had
them available, that the column listed as
"land rights" is
strictly the storage rights payments to the
producers or
owners of the gas storage rights, because there's no
inclusion of residual gas payments to the landowners or
residual gas payments to the producer.
~ Those two payments were included in those
cases as base pressure gas.

~ Q. Okay.
~ Lastly, Mr. Lowe, I want to talk to you just
yesterday very briefly about some evidence that occurred
from Mr. Johnston. Were you present
in the hearing room
yesterday--
~ A. Yes, I was.
~ Q. --when Mr. Johnston was?
~ Thank you. And you heard Mr. Johnston's
evidence?
~ A. Yes, I did.
~ Q. Did you also review the transcript of
Mr. Johnston's evidence?
~ A. Yes, I have, this morning.
~ Q. Okay. Now, did you hear Mr. Johnston's
evidence regarding his belief that he's still
entitled to
compensation payments for the residual gas attributed to
[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 238]

82

the 13-acre parcel he sold to Union Gas in 1992?
~ A. Yes, I heard him say that.
~ Q. And I believe he indicated that -- Mr.
Johnston indicated, in his evidence yesterday,
that his
negotiations for the 13-acre parcel were
with a Mr. Brad
French?
~ A. That's correct.
~ Q. In these negotiations, from whom did Mr.
French take his instructions?
~ A. Because the purchase included both land,
residual gas, storage, lease payments, and
well payments,
it was a combination of Mr. Stonika (phoen) and myself.
~ Q. And how would you divide the
responsibility between Mr. Stonika -- who is Mr.
Stonika,
rather than throw names out on the record?
~ A. Gerry Stonika is the manager of lands
department for Union Gas.
~ Q. Does anyone on this panel report to him?
~ A. I believe Bev Wilton reports to him,
yes.

~ Q. What did you instruct Mr. French with
regard to the paying of Mr. Johnston for residual gas?
~ A. I instructed --
~ MR. WAQUE: Mr. Chairman, I wonder the
relevance of this evidence. How is it to
assist the Board
to understand how one party in the negotiation was
instructed.
~ We have direct evidence from one participant
[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 239]

83

in the negotiation. I mean, in a large corporation, I'm
sure there are very many types of instructions and
directions that are given, but whether or not that has any
impact or is relevant to the discussion between the
parties is unknown to me, and I presume is unknown to Mr.
Lowe because he wasn't there at the time.
~ MR. LOWE: I think the purpose will become
relevant. I have a letter --
~ THE PRESIDING MEMBER: Mr. Lowe, will you
let your counsel respond to that, please.
~ MR. SULMAN: Mr. Lowe just did. On the
record, he has a letter that indicates from
Mr. French to
Mr. Johnston, which is the offer. Mr. Johnston -- this
all came as news to us yesterday
that -- it isn't in the
prefiled evidence.
~ Mr. Johnston's prefiled says he's claiming
for 50 acres; suddenly, it's 61-point-whatever, 29.
~ The 13 acres was never, in our view, from
the evidence that's here, the residual gas payment was
never an issue.
~ We thought the deed was pretty clear, but,
as I said at the end of the evidence yesterday, we could
call another witness. I can ask for
an adjournment and
get Mr. French to come here, but the person who's given
him instructions on the residual gas
is on the panel and
sworn, and he has a letter that is the offer that then
culminates in the deed which, of course,
doesn't have any
reservation in it for residual gas.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 240]

~ Now, I can do it one way or the other, but I
was trying to save the Board time, and I think
it's quite

proper that the individual who has given instructions
introduce the letter that Mr. Lowe, under his
instructions, that made the offer to Mr. Johnston which
Mr. Johnston obviously subsequently accepted, and that
deed is already on the record to which Mr. Johnston
identified yesterday.

~ THE PRESIDING MEMBER: Mr. McCann, can you
help us?

~ MR. McCANN: Well, sorry, I got a bit
distracted. I didn't hear the last part of what Mr.
Sulman said.

~ MR. SULMAN: I'll do that just briefly
again. Mr. Lowe is not going-- while hearsay is
permissible here, Mr. Lowe is not going to tell us what
his conversations with Mr. Lowe -- or with Mr. French
were. He's simply going to tell us he instructed Mr.
French - well, I think he's already said that - to
purchase the residual gas, and he's simply going to
introduce the document that indicates--

~ MR. WAQUE: He didn't say that.

~ MR. SULMAN: --that.

~ MR. WAQUE: He hasn't said that yet because
I was objecting to that evidence going in.

~ MR. SULMAN: Actually, he said that before
you objected, but, in any event, I'll call
Mr. French if

it's necessary.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 241]

~ MR. McCANN: Can I ask if Mr. Waque is still
objecting to this question being put to the witness?

~ MR. WAQUE: First of all, the issue didn't
just arise yesterday. My colleague, Ms. Kramer,
described

the issue to Mr. Sulman in previous discussions
we've had,

including at the ADR session.

~ And if there is a letter that's relevant to
this matter, I would like to have an opportunity
to look

at it, and understand the implications of it, and consider the appropriateness of the alternatives that Mr.

Sulman is

putting forward.

~ MR. SULMAN: I, by the way, do not agree that there was a discussion of the 13 acres in the residual gas. I have no recollection of that.

If someone wants to get up and give evidence on it, that's

one thing.

~ THE PRESIDING MEMBER: Perhaps, then this letter can be submitted and, Mr. Waque, you'll have the opportunity to study the letter, and then come back to it and ask the witnesses.

~ MR. McCANN: There seems to be some competing theories about the nature of Mr. Johnston's entitlement to compensation in relation to the natural gas which -- related to residual gas to which he feels he had some rights, I believe, in July of 1990, rights which he

did not surrender later on in his conveyance.

~ I think this is going to be a subject matter for argument. Obviously, one would like all the relevant

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 242]

86

evidence possible to be on the record and, maybe, if we could simply -- I note that Mr. Waque seems to be reading that letter now. If we could simply get it in somehow,

and its significance remains to be determined, I think, is

perhaps the issue.

~ I'm just not sure -- I don't want to interrupt the flow of the proceedings here. Maybe, Mr. Sulman, is it possible to move on to another subject and come back to this, if necessary?

~ MR. SULMAN: It's the last question I have for Mr. Lowe. There is a deed that speaks for itself, but this is the offer that then culminates in a deed. Actually, it's the exercise of an option.

~ MR. McCANN: Mr. Waque, do you have any --

can I ask you, do you have any response? I see that
you're reading the letter. Can I ask the Panel that we
give a moment's indulgence to Mr. Wague to have a look at
this document and respond.

~ MR. SULMAN: I should say that had I had the
document yesterday and known it was an issue,
I would have
put it to Mr. Johnston, but I didn't have the document
because I didn't realize -- I didn't fully understand his
evidence, as you could recall from yesterday,
about the 13
acres.

~ MR. WAQUE: Mr. Chairman, unfortunately Mr.
Johnston had to go back to the farm today and feed his
cattle. He has 70 cow -- a cattle and calf operation and
the animals have to be fed and he's the only
one to do it,

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 243]

so he couldn't be here today. So I don't have an
opportunity to consult him about this, but I
would like a
moment to look at the letter in the context of the deed
that was submitted yesterday as an exhibit.
We can come

back to it after lunch, I would think.
~ MR. SULMAN: That's certainly fair. I have
no problem with that and I'm willing to have Mr. French
drive up here if it's necessary, but
I -- he took his
instructions from Mr. Lowe. I don't think it's necessary.

~ THE PRESIDING MEMBER: You'll defer any
further questions then, Mr. Sulman?

~ MR. SULMAN: I will. I'll defer any further
questions on this issue until after my friend has had an
opportunity to look through it.

~ MR. McCANN: Board Staff has a copy.
Perhaps you could move on, Mr. Sulman, to your next
questions.

~ MR. SULMAN: Okay.

~ Q. If I could then turn to Ms. Stuart.
You've fully filed all your CVs and I won't go through all
of that. But I understand from Mr. Cochrane's -- first
from Mr. Cochrane's evidence this morning -

- were you in

the room, by the way?
~ MS. STUART: A. Yes, I was.
~ Q. Okay. And he indicated that he does
evaluations of reserves, natural gas
reserves. You heard
him say that?
~ A. Yes.

88

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 244]

~ Q. And he indicated that he does -- I
believe he did eight in 19 -- let me make sure I've got
that right. He did a certain number in 1990, I believe
was his evidence. Not having the transcript...
~ A. Yes, I don't have the transcript of it,
but it was in that order of magnitude.
~ Q. Okay. And do you likewise do
evaluations?
~ A. Yes, I do evaluations. John does
evaluations. That's Sproule's main business activity.
I'd say that 80 per cent of our business is the evaluation
of oil and gas assets.
~ Q. And in the order of magnitude, how many
evaluations of that type as described by

Mr. Cochrane

would your firm do in a year?
~ A. I've never counted them, but John did an
assessment of his individual ones and then we spread it
around the rest of the company, so I would say that it has
to be 10,000 a year.
~ THE PRESIDING MEMBER: Ms. Stuart, John is
Mr. Carlson?
~ MS. STUART: Yes, sorry, John Carlson.
~ THE PRESIDING MEMBER: All right. Just so
it can be clear on the record.
~ MS. STUART: Right.
~ MR. SULMAN: Q. And you individually would
do how many in a year, approximately?
~ MS. STUART: A. I don't do a great deal of

89

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 245]

individual evaluations. I'm more involved in
the teaching
of the evaluation of oil and gas properties
which includes
the same process.

~ Q. Okay. So you teach the evaluation. Is there a course that you teach in that regard?

~ A. Yes.

~ Q. And where do you teach it?

~ A. The course is taught, oh, probably 15 to 20 times a year. We teach it in-house.

We teach it for

CIM, which is the Canadian Institute of Mining and Metallurgy. We teach it at the University of Calgary.

And a number of large producing companies have us come in-house and teach it to their engineers.

~ Q. You say "us", you're once again referring also to Mr. Carlson?

~ A. Well, they hire Sproule. John and I are both involved in the teaching.

~ Q. In your evidence, Ms. Stuart, at page 19, you've directed your mind to the issue of ownership and I believe you've indicated that ownership rests with the lessee.

~ Have I got that correct, first?

~ A. Yes.

~ Q. Now, on what do you base that opinion?

~ A. When Sproule is examining oil and gas assets, it is our opinion and experience that ownership rests with the party that has the right to sell that asset. Now, the sale can take place in basically one of

90

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 246]

two ways: When you come to oil and gas assets, you can actually produce the asset and sell it into the marketplace, incurring incremental costs as you proceed

and receive revenue that way; or you can actually sell the asset in the ground to another party who might be interested in producing the asset themselves.

~ So, one has to look at who is allowed to benefit from the sale of the property.

~ When I look at this particular case, it is Union that actually owns the residual gas in this case subject to the payment of a royalty. So in that case,

Union benefits from the sale of the proceeds. They can produce the asset now if they so choose.

They still

retain that right. And if they wanted to, they could sell
the asset on the open market.
~ The landowner has a royalty interest and
they are free to sell that royalty
interest on the open
market as well and to benefit. Should Union decide that
they want to produce the natural gas,
the residual natural
gas, at any time, they would receive the royalty.
~ Now, going on from that, you know, a little
bit, if you go into the agreements as I have read the
agreements, that royalty interest is
two cents.
~ So it would be my interpretation that
ownership of the residual gas rests with
Union, okay?
This is based on years of experience of
evaluating oil and
gas assets in the provinces of Alberta, Saskatchewan,
Western Canada, actually around the world,
and it's also

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 247]

91

consistent, I think, with the position put forward by the
Ontario Energy Board in their gas storage report
and it is
also consistent with the Alberta Department
of Energy as
they have reported in their storage task force report.
~ So, a royalty interest is due to the
landowner and that royalty interest as expressed in the
agreements is two cents, and I would suggest
that that is
to be paid.
~ Q. Ms. Stuart, have you reviewed Mr.
Cochrane's evidence in this case?
~ A. Yes, we have.
~ Q. And you were present and heard Mr.
Cochrane's evidence today?
~ A. That's correct.
~ Q. And his evaluation is not the same as
yours, I take it?
~ A. There are a number of differences
between the way that Sproule would assess value. There
are a number of things that Mr. Cochrane and myself and

Mr. Carlson would agree with and there are a few, in
listening to his testimony today, that I
think if he and I
were sitting down across the table that we
could come to
terms on fairly quickly. But I would
like to address a
few ones that I think we would have some major
difficulties with.

~ We do evaluations. Those evaluations are
often used to assess value, value to a producer which is
what we call a going-concern value; a value to the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 248]

marketplace which might be considered market value.
~ In assessing that, the discount rate that is
typically used on producing properties is, in my
opinion,

not comparable to a bond rate. If I had a choice of
investing \$500 in a bond or \$500 in a
producing oil or gas
asset, there's no question if the return was going to be
the same for both them, I would put the money
into a bond.

The risk inherent in the production
of an oil and gas
asset is not the same as the
risk inherent in a bond.

~ Also, when Sproule takes on the assessment
of an oil or gas asset, you know one
of the questions that

is important to ask right off the top is: For whom is
this being done? And it is important
to understand what
their tax position would be. It is critical to the
evaluation process.

~ We ascertain that. In doing so, we have
also determined that most parties that have producing oil
or gas assets are in a taxable position and the assessment
is typically done on an after-tax basis in determining the
market value or making an estimate of what the transaction
value will be if you are exchanging a
gas asset for money.

~ Another area I'd like to address as well is
the issue of energy price forecasts and I do not want to

take issue with price forecasts or the comments that Mr.
Cochrane made on price forecast.
I'm one of the parties
that actually develops the price forecast for
Sproule and
I've been contributing a price forecast to the Chennery
Dobson survey since 1989, though I think
they've been
[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 249]

93

around for a few years before that.
~ But, I also then understand the development
process of a price forecast and there are usually two
components in that. You will look at the
price forecast
on a real basis and then you will include an inflation
component. That same inflationary component
is then used
in the escalation of operating costs.
~ If an evaluation is done on escalating
dollars, we always use escalating costs and
this is also
consistent with other evaluators in Alberta.
It's part of
the process of determining going-concern value.
It's part
of the process of determining market value. If you were
using real dollars, then you don't escalate the costs
~ I think those would be sort of the three
major issues - you know, the rate of return,
the tax issue
and escalated dollars in -- escalated price
in combination
with escalated costs.
~ I would also like to comment that when you
are coming up with the value of an oil and gas asset,
there are, indeed, a range of numbers that people can
generate. But when Sproule develops an evaluation, we
come up with one assessment and we will give
guidance if
someone is interested in the interpretation of that
assessment. Eventually a dollar offer has
to be made and
it is the negotiated settlement between two parties. But
we have, you know, a great deal of experience

in coming to terms with what is considered a reasonable -- for assessing the value of the assets.

94

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 250]

~ Q. Sorry, I don't know whether that got on the microphone.

~ THE PRESIDING MEMBER: Mr. Sulman, can I interrupt for a second? I just wanted to make sure that -- I did not understand the very last

point about the constant versus nominal or whatever that was.

~ MS. STUART: Sure, okay.

~ THE PRESIDING MEMBER: Would you repeat that and the point of contention with Mr. Cochrane's evidence.

~ MS. STUART: Okay. There are general guidelines that are used by evaluators in evaluating oil

and gas assets. It's not just Sproule and Sproule's guidelines. The other major companies which Gilbert, Lausten and Jung McDaniel are two, use the same guidelines

in evaluating and doing the evaluation process and coming up with the discounted cash flow.

~ One of those - I would call it a guideline - it's a process that is consistent among the three, is, if you were using a price forecast that has included

inflation, i.e., the 2 per cent, 3 per cent inflation,

then your operating costs also include inflation of the 2

to 3 per cent, so the same inflation.

~ If you were doing a constant dollar assessment which is necessary for other purposes, you would use constant dollars and constant prices. But I have never seen an evaluation where someone has used a price forecast that has included the three per cent escalation in price and not included any escalation in

95

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 251]

operating costs, which is the process which Mr. Cochrane used.

~ THE PRESIDING MEMBER: Thank you.

~ MR. SULMAN: Q. Thank you, Ms. Stuart.

~ Mr. Carlson, you were present in the hearing room yesterday, were you, sir?

~ MR. CARLSON: A. Yes, that's correct.

~ Q. And do you recall Mr. Inwood's evidence, my cross-examination of him with regard to production from a pool that's in the storage phase?

~ A. Yes, I do.

~ Q. Now, in your opinion, once a pool goes to storage, does production cease?

~ A. I would say not necessarily. I think somebody used the terminology "abandonment" yesterday and that may be checked in the transcript, but just because the pool is now in a storage situation, we would not consider that it has abandoned the residual gas that was there. Production can occur from that residual gas in a number of processes.

~ I think we're all in agreement, from what I've heard, that commingling is a fact, and I don't dispute that. I totally agree with it. The gas doesn't move in the reservoir by displacement much like an oil reservoir. There is commingling. It's just the nature of the way gas flows. So as the withdrawal process happens over time, that commingled stream will be produced.

~ Certainly the operator of the pool has the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 252]

96

opportunity to deem a sale at any point in time. He can do that either by actual withdrawals and deem a certain portion to be the residual gas stream and some be the storage gas. Or he can do it by an exchange arrangement, take gas somewhere else, out of a different pool, and deem that as a production from the existing pool.

~ I know of cases where reservoir integrity is an issue. And in Alberta, there has been a

case where
production has come out of a well that was drilled into a
storage reservoir. Obviously somebody didn't do their
homework and there was production out of
that storage
reservoir.

~ I understand that there's down-dip well
production in some of the pools in Ontario that are
associated with storage reservoirs. It's conceivable that
gas migration happens into the oil leg over time

and that
gas can be produced in solution with the oil
production.

~ That is not an unreasonable assumption
either. So those are just four types of
examples I can

think where production could be occurring, whether
it is a
deemed or actual molecules coming back to the surface.

~ Q. From what you just said, I take it that
there is also the possibility of gas
being at different

horizons, geological horizons in a formation?
~ Not being a geologist or an engineer, maybe
I haven't described that accurately, but maybe you can
comment on that?

~ A. Well, I guess -- I don't want people to

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 253]

97

think you can differentiate between the gas that is
residual gas and the gas that
is storage gas. That's a
book number. But really in the reservoir there is
homogeneity, within the reservoir, and that gas mixes and
you don't have a little compartment where you just keep
the residual gas forever until you
decide to produce it at

the end of the life of the storage reservoir.
~ That gas is mobile and it mixes and it just
makes up the whole part of the reservoir.

~ Q. Thank you, sir.

~ Maybe if I can go to the other end of the
table, to Mr. Wilton for just a minute.

~ For the record, sir, you were employed by
Imperial Gas in 1990? Imperial Oil, although

I guess they

~ had some gas production, too.
MR. WILTON: A. I was an independent
consultant at that time, but had a
contract to provide
services for Imperial Oil Limited.

~ Q. Okay. What were the services that you
were to provide for Imperial Oil?

~ A. I administered all of their remaining
Ontario oil and gas producing and storage properties and
also their free hold leases.

~ Q. Okay. I take it one of those properties
was the Sombra pool and the subject matter of this
hearing?

~ A. Yes, it was.

~ Q. You are, just for purposes of the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 254]
record, you are the same Bev Wilton who made
the offer to

Mr. Glasgow and Mr. Johnston?

~ A. Yes, I am.

~ Q. So you said that you were an independent
contractor, under contract with Imperial Oil. What
directions were you given by Imperial Oil with regard to
residual gas payments on these properties?

~ MR. WAQUE: Again, Mr. Chairman, I object to
that question. I don't understand the relevance of
directions that were given by another company with respect
to negotiations.

~ The relevant fact for the purpose of this
arbitration is that an offer was made, we

know that, and
not accepted and to explore this further
is, in my

respectful submission, not relevant.

~ THE PRESIDING MEMBER: Does anything turn on
this, Mr. Sulman?

~ MR. SULMAN: I think it is important for
you -- this is an arbitration, it's not a question.

~ The only issues that are outstanding really
are the ownership and the price, and we will hear about
other tribunals.

~ I mean, the leases aren't in question. The
only thing that's in question is getting before you all
the information necessary and it's a wide band of

information on the practices in the field in 1990, what
numbers you should look to, what the royalty
prices are.

~ You have heard the market price evidence and
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 255]

99

you have heard other contrary evidence to
that now, but I
think you should have all the evidence before
you of what

was going on in the Lambton County oil patch in 1990.
~ The only evidence - and remember, this an
Imperial Oil offer that was given - the only
evidence you

are going to get about what Imperial was
doing at the time
is from the Imperial witness, the witness who is
here now

who was the contract employee at Imperial at
the time.

~ I don't know what the objection is about.

I'm simply asking: What direction were you given with
regard to offering, making an offer for residual gas?

~ I would like to know whether it's -- I guess
the point of the question is, is it -
- did you only make

the offer -- I can phrase it in a different manner. Maybe
that's the better way that might help my friend. Maybe
that is instead what I will do.

~ MR. SULMAN: Q. Did you make other offers?

We know you made the offer in this pool,
sir. Did you

make offers to other landowners for residual gas in
Imperial Oil properties in Lambton County?

~ MR. WILTON: A. At the time those offers
were made they were no longer owned by Imperial Oil.

~ Q. They were no longer owned by Imperial
after they were made. I see. Okay.

~ MR. WAQUE: I mean, for the record, Mr.
Chairman, a two cent offer was made I assume with
instructions from Imperial. I just don't see the reason
to explore it.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 256]

100

~ MR. SULMAN: Okay. I will move on from

there.

~ Q. Did you make offers to other landowners
within the same pool on behalf of Imperial Oil?

~ MR. WILTON: A. Yes, I did.

~ Q. What were the results of those other
offers that you made at two cents per mcf?

~ A. They were accepted.

~ Q. What was the number of offers that were
accepted in this particular pool?

~ A. To individual parties?

~ Q. How many individual landowners accepted
the two cent offer in this particular pool?

~ A. I believe that number would be in the
order of five or six other individual owners.

~ I'd have to check that against the division
of the properties at the time that the offers
were made.

It involved all of the owners of land within
the pool.

~ THE PRESIDING MEMBER: Are we talking about
the same time now, Mr. Wilton?

~ MR. WILTON: At exactly the same time.

~ MR. SULMAN: Q. "Exactly the same time" for
the purposes of the record was when?

~ MR. WILTON: A. Effective the 19th of July,
1990.

~ Q. Thank you, sir.

~ I understand that Sombra, the Sombra pool
was part of a joint venture with Union
and Imperial; am I

101

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 257]

correct there?

~ A. That's correct.

~ Q. I understand that the Bickford pool was
also part of that joint venture?

~ A. Yes.

~ Q. Is that correct?

~ A. Those were the assets that Imperial Oil
brought into the joint venture with Union Gas.

~ Q. Okay. What was the offer that was made
to the Bickford pool landowners for purposes of payment of
residual gas?

~ A. The offer to the Bickford landowners was
based on two cents per mcf.

~ Q. Do you know how many landowners were
involved in the Bickford pool?
~ A. Again, I would need to, for accuracy
purposes, check the record, but in Bickford there are
many, many more owners since the pool is
much larger. I
would estimate in the order of 24 to 25 individual farms.
~ Q. Can you tell me how many did not accept
the two cent per mcf offer?
~ A. There were no parties that did not
accept the offer. Would you like me to
rephrase that?
All of the offers were accepted.
~ MR. SULMAN: Thank you, sir.
~ THE PRESIDING MEMBER: What was the timing,
again, of that, Mr. Wilton, the Bickford offer and
acceptance?

102

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 258]

~ MR. WILTON: A. Much earlier in time. I'd
have to, again, check the records, but it
would be, in all
likelihood, in the early '70s.
~ MR. McCANN: Mr. Chairman, if I could, Board
Staff is having some difficulty seeing the relevance of
these questions, too. There is a Phase 1 decision, in
this matter. The Board has decided that in relation to
the compensation in issue here, there is
not agreement.
And I don't think anyone's disputing that there are other
agreements in place, and other agreements
were negotiated,
but there is not an agreement in this
compensation matter.
~ We're just not clear on what the relevance
of this line of questioning is.
~ MR. SULMAN: It has absolutely nothing to do
with -- we're not proposing that there's any
agreement. I
don't understand your confusion, quite frankly. Maybe,
you can clarify that for me.
~ My understanding is that the Board --
~ MR. McCANN: It's very difficult to clarify
confusion.
~ MR. SULMAN: My understanding is the Board

wants to hear all the evidence on all the comparatives that they might consider, and so they want to know what other pool matter -- what other amounts were accepted because their obligation is to determine a fair and

equitable compensation in this matter. And so, in determining fair and equitable, they'll want to look to what has been paid throughout Lambton County, and what [Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 259]

103

have the majority of landowners in Lambton County generally accepted, and what had the landowners within this particular pool accepted, and what have they accepted in the joint venture that's attached to this pool accepted.

~ MR. WAQUE: Mr. Chairman --

~ MR. SULMAN: But that's all argument.

~ You're asking me to clarify. All I'm doing is getting on the record what other acceptances there are

in Lambton County. And I don't -- I, obviously, wasn't putting it forward as argument. I'm simply explaining to

Mr. McCann what the relevance is.

~ I would think you'd want to know -- and, besides, that's what Mr. Inwood has put forward; that's what Mr. Lowe has put forward generally in his table and

Mr. Wilton, employee of Imperial, is telling us what was accepted in Bickford which was an Imperial pool.

~ MR. WAQUE: If it assists, Mr. Chairman, I would have thought it would have been here by now, but the

position of the applicants is not that the price they maintain on either of the goal posts was an appropriate

price in 1970, or even in 1980. We're addressing ourselves to July 19th, 1990. And even Mr. Inwood didn't maintain that two cents wasn't the appropriate rate or wasn't the rate negotiated in the marketplace in the 1970s.

~ So to lead evidence about what was negotiated when the dates of injection are in the 40s or

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 260]

50s or 60s or 70s, in our respectful view, has no relevance at all. It's no part in our case. There's no dispute between the parties at all on that point. It's just that after 50 years, maybe it's time to revisit the rate, but it's not that there wasn't a different

rate 50

years ago. We accept that.

~ MR. SULMAN: And I'm sure my friend accepts
the fact that Mr. Lowe has given evidence
that these

two -- acceptances are not just 50 years ago; they were also accepted 1989 and more recently than that, in fact.

~ So all we're doing, and it's already
completed, it's on the record, what was accepted in
Bickford, which is the adjacent pool. That's the whole
point of the evidence. You can weigh all that at some
point in time.

~ Q. Mr. Wilton, I want to turn to another
matter. You were present in the hearing
room yesterday?

~ MR. WILTON: A. Yes, I was.

~ Q. Before I go to that, you've been a
land's agent for how many years?

~ A. 22 years.

~ Q. And where have you spent the majority of
that period of time?

~ A. Primarily in Lambton County.

~ Q. And do you regularly -- I take it, as a
land's agent, you regularly deal with transfer of
land/deeds?

~ A. Yes, I do.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 261]

~ Q. Now that they're known as that.
Formerly, in your earlier years, it was just
simply known
as deeds?

~ A. Yes.

~ Q. Okay.

~ And have you, in your experience, seen deeds
that have a reservation of mineral rights or reservation
of other rights in them?

~ A. Yes, I've seen examples of those.

~ Q. Okay. Have you ever seen a deed that
purports to retain a mineral right that does
not have a reservation in it?

~ A. No, I don't think I've ever seen a deed
that had that effect.

~ Any deed that I have seen that, from my
reading of it, I could conclude that there -- a
reservation of minerals is present, there's language
specific to that reservation. It's
something that the
selling party reserves onto themselves. It's
clearly set
out in the document.

~ MR. SULMAN: Okay, thank you.

~ Those are all the questions I have for you,
Mr. Wilton, thank you.

~ I have one more witness that I want to ask
some direct questions. It's now 12:35. I can continue.
It will take a little while, or we can break for lunch.

~ THE PRESIDING MEMBER: Why don't we
continue, Mr. Sulman, we can finish your
direct, and then

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 262]

106

Mr. Waque will have an opportunity to digest what the
direct is. How long would you be?

~ MR. SULMAN: I'm only asking the questions.
I can't tell how long the responses will be. We'll
certainly be finished before one.

~ THE PRESIDING MEMBER: Go ahead then.

~ MR. SULMAN: Q. Professor Lucas, if I can
turn to you now for a second.

~ There are several lease documents, and I
will call them that, although for purposes of the record,
there's an oil and gas lease, there is a unit operation
agreement, and a natural gas storage
agreement which were
filed by the applicants in this proceedings.

Have you had
an opportunity to review all those documents?

~ PROF. LUCAS: A. Yes, I have.

~ Q. And can you describe for this Board the
purpose of each document and the inter-
relationship of

each of those documents?

~ A. The purpose of the oil and gas lease --

~ MR. WAQUE: Mr. Chairman, again, I wonder if

we're not revisiting a matter which has already been

determined by the Board.

~ The Board heard argument in Phase 1 about

the three documents and about the inter-relationship

between each other. And a major part

of Union's argument

was that you had to read all

three documents together, and

that was determined of the issue.

~ And the Board made a specific finding, in

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 263]

107

the Phase 1 decision, which is found in paragraph 1.2.1,

and the finding is:

~ The Board agrees with the applicants that

~ each of the agreements, the oil and gas

~ leases, the unit operation agreements and

~ the gas storage lease agreements serve

~ separate purposes.

~ And that while the provisions of each set

~ of agreements may amend or reference the

~ provisions of the preexisting agreements,

~ for the purpose of this decision they need

~ not be read together.

~ Now, I'm concerned that this evidence is

directed toward an attempt to retry that

issue, and I'm

also concerned that --

~ THE PRESIDING MEMBER: Mr. Waque, I don't

know how you got that impression

because I didn't. Let's

wait and see where Mr. Sulman is going with it.

~ I, for one, would like to know -- at least

get some definitions for this record.

There are two

panelists here that were not part of that hearing. All

I'm saying, let's get a definition of things on the table

that would be of assistance to us. And it goes to

argument as to what Mr. Sulman will do with that

information.

~ MR. WAQUE: Let me deal with my second

objection then, with respect to this type of evidence.
~ The witness, as I understand it, is a
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 264]

108

professor of law. He's not bringing to the Board any kind
of market experience or industry experience. As I
understand it, he is interpreting the documents as a
lawyer.
~ We have an opportunity in argument to
submit, make submissions, about what the arguments
mean as
lawyers.

~ And, in my respectful view, it's not
appropriate to try to disguise legal argument as
evidence.

To have a level playing field, we should have legal
arguments made at the argument portion of the case, and
not have a witness purport to interpret the
documents when

the lawyers can do that in argument and set out the
parties' position perfectly properly.
~ And it's the Board's role in final analysis
to determine what the agreements mean insofar
as that is
relevant to the determination it has to make.

~ So, in my respectful view, that's not
proper -- it's not proper evidence to have a witness
provide a legal interpretation.

~ THE PRESIDING MEMBER: Well, I have not seen
an answer yet from Mr. Lucas. You see, my problem, Mr.
Waque, is I don't know how far Mr. Sulman is going with
it, yet.

~ Can you reserve your objection until he asks
some more questions?

~ MR. WAQUE: All right, thank you.

~ MR. SULMAN: I can be right up front with

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 265]

109

you, Mr. Chairman. We're not retrying the previous
decision. The decision was restricted. Well, you know,
you were one of the authors of the decision. And, in my
view, the decision dealt with that very narrow issue of
whether there was an agreement, so that we wouldn't need
to go to arbitration. The Board clearly
ruled there is

not an agreement within the section of the statute, and so, therefore, there shall be a determination by this Board of just and equitable compensation.

~ We're not disagreeing with any of that. And while we argued at that time that the agreements were determinative, we're not doing that now.

~ We think it's important, as Mr. McCann clearly said yesterday, to get the information before this Board and not wait until it's argument, in effect, by the applicants.

~ So all I want, I've got an expert here who wrote the text on oil and gas law in Canada. I've got a unique opportunity, and I simply want to ask him about the -- he's reviewed these documents and explain to us the operation.

~ You can hear it from me, I'm an advocate; you can hear from him, he's an advocate. We're going to be taking our clients' position. This is an independent witness who's come forward. So I'll proceed to ask the questions, and if we get into trouble as we go, I'm sure Mr. Waque who may not want to hear this will object.

~ MR. WAQUE: Mr. Chairman, now my friend has indicated that he intends to do exactly what I object to.

~ The witness is not the author of the oil and gas text in Canada. He's the author of a text which specializes in dealing with not freehold lease interest but crown interest it's in Alberta centered text which deals with the legal -- particular legal circumstances in Alberta which have no application at all to Ontario. Don't accept that he's qualified to give the evidence, in the first place. But what my friend intends to do, and he's just said it, is that rather than have it as a matter of argument, he wants this witness to pronounce to the Board what the law is, what the proper legal interpretation of these documents is.

~ That's the very matter that the Board has to

decide, and it's not appropriate or fair to disguise that argument in the form of evidence.

~ THE PRESIDING MEMBER: Mr. McCann, can you help us with that?

~ MR. McCANN: Well, it's a difficult one. I think there are precedents for lawyers and law professors being sworn-in before tribunals as experts in the law.

~ I guess it's often the case when one is dealing with foreign law or the law of another jurisdiction - which is not the case here - we're dealing with Ontario law; therefore, what I would say, I

think, is

this: we should hear from Professor Lucas. He's here and

he obviously has some background information and general

views of the interrelationship of these documents and the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 267]

111

effect of these documents which may be helpful to the Board. But I think we need to be clear that this Board as we know has jurisdiction to decide all the questions of fact and law that are necessary to make its decision.

~ In determining the law of Ontario, it will pay particular attention to the advice and the argument it

receives from members of the Bar of Ontario who are

representing various clients here today and that Professor

Lucas' contribution needs to be understood as evidence; that is, as information which may help the Board to understand the issues, but not as necessarily determinative of any of those legal issues.

~ I don't know if that's a fair statement that my friends could accept or not.

~ MR. WAQUE: Well, I can't accept it and I think Mr. McCann has raised another interesting point. Mr. Lucas, as I understand, is not a member of the Bar of Ontario; is that correct?

~ PROF. LUCAS: That's correct.

~ MR. WAQUE: And for him to practise law in Ontario, he would need a call from the Law Society of

Upper Canada. He would be practising law in Ontario if he purported give opinion evidence interpreting agreements in accordance with their application and effect in Ontario. And so the Board would be, in effect, receiving evidence that he's not legally permitted to give. It's a matter of some seriousness.

~ When I go to argue a case, for example, in [Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 268]

112

BC, I have to go to the BC Bar and get a special call to be able to act in British Columbia and the appropriate inquiries are made at that time.

~ THE PRESIDING MEMBER: Mr. Waque, this is a tribunal and we are interested in the best information possible and tribunals of this kind do have some flexibility in terms of what should be submitted and who is going to testify to evidence. So we entertain information. And now I'm not sure whether that gets us into any hot water, Mr. McCann, in terms of the legalities of it, but ...

~ MR. McCANN: Well, I think as long as we're clear that Professor Lucas is giving evidence and that it is the job of the tribunal to weigh the relevance and the significance of that evidence at the end of the day, and that the legal effect of the evidence and of the information that's before the Board will be addressed by counsel and that the Board will accept that those views of the law and how it relates to the evidence, as the panel reflects on it, will -- their reflection will be primarily on what counsel representing the parties have said. I think, on that basis, hearing evidence from Professor Lucas is not illegal or unlawful in a way that will expose us to unfortunate consequences.

~ MR. SULMAN: I'm not putting Professor Lucas up as a -- he's not practising law. He's put up as a

witness, an expert witness. And the irony of this is that my friend in his evidence has put forward, without any [Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 269]

113

person's name on it, and didn't call any evidence at all on direct on the issue of ownership, yet in his evidence liberally quotes from John Ballem who happens to be an Albertan practitioner of law who wrote another textbook on oil and gas law. And what I've done has gone -- because I knew this Board needed that information and someone had to speak to it rather than just hear two advocates give you their positions, which we'll ably do at the end I'm sure, but I went to the source and said, look, there's quotes from a textbook here. I've brought an individual who's recognized as an expert. I can't understand how that can be objectionable to my friend when in his application which we've only responded to, he quoted liberally from John Ballem's textbook and I've got an author of the text here.

~ In addition to that, there hasn't been any evidence on ownership. I suppose if I stopped and simply say in argument later, which will give you no information to deal with this issue, that we're not going to call any evidence on ownership -- and my friend didn't -- no one came forward and gave any evidence and there's no one -- there's a file here, but it's not under anybody's name. So I don't want to do that.

~ I think the whole process is to get the greatest amount of information that the Board can have on

this issue and get it resolved. These things only come
before this Board about every, it seems, 15
years - this
one, Bentpath and you heard from Mr. Lowe about Payne
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 270]

114

arbitrations - and it's an opportunity for the Board to
try and resolve these things so they don't come all the
time. We're just trying to get the best evidence we can
and that's -- I don't think there's any doubt about the
ability to give this evidence. He's not practising in
Ontario.

---Off the record discussion.

~ THE PRESIDING MEMBER: Mr. Waque, I guess as
I pointed out earlier, we are still interested in
information and will probably want to give Mr. Sulman a
chance to see how far he can go with this and
I would also

ask Mr. Lucas to keep in mind that
we're not lawyers, as
he responds to the questions.

~ MR. WAQUE: Mr. Chairman, I just wanted to
make one other point which hadn't been made
earlier rather

than go over common ground. In determining how much of
this evidence you will receive, I'd submit to you that
there has to be a balancing of the opportunities
to make a
fair and proper case before you. And
obviously Union Gas
has significantly more resources than the
applicants do.

And it may be that all the applicants can afford
to do is
to photocopy pages from case books and Union Gas can
afford to fly in the author from Alberta.

That's an
economic difference between the power and the
capacity of

the parties to make a case before the Board.
~ When the Board then is consisted of lay
people who admit that they are disadvantaged, with
respect, because of their experience
to listen to legal

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 271]

argument, there's an unfortunate risk that having a professor of law and hearing directly from him will give

Union an unfair advantage in terms of making the appropriate legal arguments. In my respectful submission,

this question of ownership is not one for factual evidence. It's a question of law.

~ The Board is not now about to engage in an exercise of getting more information because there's no

factual information to come from this witness. The information to come from this witness is on legal interpretations on the legal impact of documents, as I understand the next series of questions. And

that puts,

from the applicants' perspective, them at a very significant disadvantage in these proceedings

and I ask

you to keep that in mind, please.

~ MR. SULMAN: I don't know that I want to make any comment on the issue of economic ability to

retain witnesses. We're simply the respondent here and this Board has a record of being very generous in its cost

awards and experts are usually -- well, I've rarely seen them not be paid and not paid in full. So I don't think

that that's a legitimate argument.

~ Over a year ago we provided, in response to an interrogatory from Board Staff, asking who our witnesses would be, and over a year ago -- I misspoke myself because it's actually March 22nd, 1996, that we gave the names of the panel. So this

is no surprise. It could have been another -- a contrary oil and gas law

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 272]

professor, but I don't think -- there aren't any in Ontario and that's why you have an Albertan before you and that's where the basis of the law of oil and gas is now in Canada.

~ Anyway, I want him to explain simply so you
have evidence before you. Okay? If I might proceed.
Well, we're now at -- it's going to be
disjointed now, Mr.

Chairman, that we're almost at one o'clock.
~ Would you like me to still proceed to ask
him the questions?

~ THE PRESIDING MEMBER: Yes, could you,
please?

~ MR. SULMAN: I will.

~ Q. I think I left with you that -- asking
you to describe the purpose of each lease and the
interrelationship of those leases. And please bear in
mind the statement of the Chairman, that

-- let's not be
too legalese on these. We want to understand how they
operate and how the clauses operate.

~ PROF. LUCAS: A. What I'll try to do, Mr.
Chairman, is to look at the leases in terms of what they
provide for but particularly with a view to
what they say

about the interests of the parties here; what interests
the landowner has in the natural gas,
what interest the
lessee has. So I guess, in a sense, I'm
anticipating some
further questions, but I won't go into a
detailed exercise

in interpreting the leases because my understanding is
that that's really not what's required or what would be

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 273]
helpful to the Board here.

~ I'm going to refer to the agreement of
lease. It's at tab 10 of the -- I think it's the
applicants' prefiled evidence. And under tab 10, there is
the agreement of lease and it's followed by the unit
operation agreement and then the gas storage
agreement.

~ MR. McCANN: Just for clarification, I think
the agreement of lease is tab 9 in the applicants'
prefiled evidence; am I right about that?

And then tab 10
is the unit operation agreements and tab
11 are the gas
storage lease agreements? I'm not right about that.

~ PROF. LUCAS: Perhaps in the version that I
 have -- they are all together under --
 ~ MR. McCANN: Well, is anybody having any
 difficulty finding them, I guess, is the question?
 Apparently not.
 ~ THE PRESIDING MEMBER: In my copy, it starts
 at 9, tab 9.
 ~ PROF. LUCAS: Okay.
 ~ So with respect to the agreement of lease,
 that's the oil and gas lease, and this is a common form
 lease that was used by Imperial Oil in the 40s and 50s and
 it's virtually identical to leases that were used in
 Alberta at the time the leases in the Leduc No. 1
 discovery, which was the original
 discovery that set
 Alberta on the road to wealth and fame, that Imperial Oil
 lease would have been, virtually word
 for word, similar to
 this one.

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 274]

118

~ These leases are aimed at affecting a sale
 of rights to the oil and gas that is
 in the landowner
 initially, the oil and gas rights, a sale in transfer of
 rights in relation to that oil and gas to the lessee. And
 the lessee is particularly interested in exploring
 - that
 is drilling a well - producing and selling the oil or gas,
 and that is the purpose of the lease. It's not an
 outright sale of the oil and
 gas that the landowner has
 and that's why I characterized the lessee's interest as
 rights in relation to the natural gas. And those rights,
 the critical rights, are the rights to go on
 the land, to
 drill, to produce and to sell the substance,
 assuming that
 the exploration is successful.
 ~ So the way the lease does that is in the --
 if you look at the lease and start with the
 first clause,
 the witness said, that is the granting clause and that has
 the effect of granting the rights that I've mentioned to
 the lessee.

~ In this lease, the rights that are granted
are actually spelled out in the clause below,
the one that

begins "to have and to hold..."
~ The clause that I have just mentioned, "to
have and to hold" is referred to as the
habendum clause,

the holding clause, and what the habendum
clause does is
establish the term of the oil and gas lease and, in
effect, it establishes the conditions on which
the oil and
gas lease will be continued, and it normally
establishes a
primary term. Here it's ten years, you can see, and so

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 275]

119

long thereafter as oil or gas are produced from the leased
lands.

~ You can see, if you look at that clause in
the third line, the second and third line:

~ So long thereafter as the substance or
~ any of them are produced from the said lands
~ or the lessee conducts operations... et
~ cetera. The key is production to
continue the lease.

~ If you drop down a couple of lines, you will
see the reference to the precise rights
that are granted
under the lease. So it would be the
sixth line, "to
prospect and explore and to drill for,
recover, remove
and/or sell the said substances."

~ Okay, the right to explore, produce and sell
and that's the essence of the interest that the lessee
acquires.

~ This lease goes on and says:

~ ...which substances the lessor hereby
~ grants to the lessee absolutely as and when
~ the said substances are recovered.

~ So it grants the gas in this case absolutely
and the "as and when the said substances are recovered" is
in there to ensure that the lessee actually
obtains title

to the oil and gas when recovered, and there is no argument about that because the term "lease" is used here.

~ In the early days of the use of these oil and gas leases, there was some doubt about whether "lease" simply meant use for a period of time as in a surface

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 276]

120

lease of land. And so the drafters have made it perfectly clear that it is the substances when produced that are vested in the lessee. Not merely the right to do something as a lessee with those substances, but the

absolute title to the substances.

~ So that's the essence of the lease.

~ If you turn to the next page, Mr. Chairman, Members of the Board, and look at clause 4, that's the clause that provides for the right that the lessor retains

under the lease when the rights that I've mentioned are transferred to the lessee. What the lessor retains is a

royalty interest and that is spelled out in clause 4.

~ The only other clause that I wanted to draw to your attention was clause six. In this lease it's kind

of a catch-all. It begins with a covenant of title, the lessor warrants that the lessor actually has title to the oil and gas.

~ But the second sentence that begins with

"notwithstanding" on the third line:

~ Notwithstanding the use of the word

~ 'lease', the lessor acknowledges and agrees

~ that subject to the lessor's royalty rights

~ the ownership in all and any of the said

~ substances as and when produced shall be in

~ the lessee.

~ It is the same concern that I have just mentioned. The parties want to make absolutely sure that the substances, the natural gas or petroleum, when

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 277]

produced, vests in the lessee notwithstanding that they have used the term "lease" and they put that in quotes here. Okay?

~ So the lease then transfers or sells certain rights in the oil and gas that the lessor has initially to the lessee and the essence of what the lessee gets is the right to go on the land, drill, produce and market.

~ So the production rights, the producing rights are the key as far as the lessee is concerned.

~ What the lessor gets and retains out of the transaction is the royalty interest. The lessor retains

something else as well, and that's usually referred to as the reversion, because we've looked at the habendum clause, ten years and so long thereafter as the substances

are produced, at some point production may cease and at that point the lease would lapse, and the entire interest

in the oil and gas would then revert to the lessor. ~ So the lessor also has a right, that may be a valuable right, to the reversion if and when the lease comes to an end.

~ So the lessor has two things; the royalty that's expressed in clause 4 and the reversionary interest.

~ Okay. So that's the oil and gas lease in this particular situation.

~ That lease here was then amended, was modified, was amended by the unit operation agreement. And, again, this is a common event in Alberta and in the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 278]

western -- the other western provinces where oil and natural gas is produced. And the unit agreement provides for the more efficient production of oil and gas from the pool in which the lease, the individual lease is as a unit.

~ So it may be then in those circumstances that production from the unit will not be from the well that is on the particular lease, and you will recall the habendum clause specifically provided ten years and so long thereafter as production continues.

~ So when the unit is established, if production does not continue from the lease, the lease would lapse even though production would continue somewhere else on the unit.

~ So the parties are trying to ensure that the lease doesn't lapse for that reason. So they amend the lease to provide that the lease will continue if there is production from the lease or if there is what is usually referred to as deemed production. And deemed production would be production anywhere else in the unit that is the subject of the unit operation agreement.

~ That's what the unit operation agreement does. And if you look at it, you can see that it specifically refers to and amends the oil and gas lease.

~ So on the first page of the unit operation agreement, if you go down about three-quarters of the way down, the second "whereas". If you look at the lease, there is a description of the property in the middle and

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 279]

then one "whereas", two "whereases", and the second "whereas", the parties indicate that they desire to amend the said lease and to unite and combine that portion of the said lands into a single unit. Okay. So they make it clear that they are amending the lease.

~ How are they amending the lease? If you then go to clause 4 of the unit operation agreement on the next page, this clause makes provision for payments.

~ These would be royalty payments, but you will notice that it specifically says:

~ It is understood and agreed that in each
~ calendar year the lessee shall pay or tender
~ to the lessor in lieu of all payments under
~ the said lease...

~ In lieu of, okay. So if these payments that
are specified here - and what is specified here is
payments of two cents per mcf, with a minimum payment -
then you go down to the bottom of that
clause, "and so

long as the payments in this clause are made or tendered
the leased substances shall be deemed to be
produced from
and operations for the recovery shall be deemed to be
conducted on the said lands." That is, the
leased lands.

~ Okay. This means that the parties have
amended the lease to make it clear that so long as there
is either production from the lease or deemed production;
namely, the making of these payments, the two cents per
mcf with a minimum 250 per acre, so
long as those payments
are made, production is deemed to have occurred and that

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 280]

124

continues the lease.

~ If you turn to the next page, I will just
refer to one more clause, clause 15.

The parties want to
be very clear as to what they are doing
in relation to the
lease. So, once again, for greater certainty,
they spell

it out again:

~ Accepting as herein and hereby expressly
~ modified or amended, the said lease shall
~ continue in all respects in full force and
~ effect for as long as therein provided and
~ the same as so amended, et cetera.

~ Okay. So they have made it very clear that
they intend to amend the lease and provided the deem
production is maintained; that is, the payments as
provided under the unit operation agreement are
maintained, the lease will continue in force and
effect.

~ Now, that lease as amended by the unit

operation agreement is the lease that is referred to in

the gas storage lease agreement.

~ So if you turn to the gas storage lease agreement and look at the first page. Again, down at the bottom of the page, "the lessor doth hereby demise and lease..." Archaic law language, okay. Storage rights are being granted by that clause, but notice that the parties

are very specific, "subject to the oil and gas lease."

~ So the storage rights are being granted under the storage lease agreement. The parties make it very clear "subject to the oil and gas lease."

125

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 281]

~ They then provide for what the lessor gets under the storage agreement; namely, several species of rental.

~ The only other clause I want to refer you to is over the page, clause 16. Under the lessees and lessors covenants, clause 16 and, again, subject to its rights if any under the oil and gas lease.

~ Okay. So, again, there is a reference to the oil and gas lease. The parties make it clear that they are entering into this storage agreement on the basis

that there is an oil and gas lease in existence. Okay?

~ So subject to its rights, if any, under the oil and gas lease, the lessee shall not inject, shall not begin to you use the land for storage until it is paid or

tendered the rentals provided for storage under the storage agreement and until it has offered to purchase the lessor's interest in search of the oil and gas. Okay?

~ What is the lessor's interest? The lessor's interest is the interest that the lessor has under the oil

and gas lease as amended by the unit operation agreement.

~ As I've indicated, in my opinion that interest would be the royalty interest and the reversionary interest that I mentioned. Okay?

~ Q. Can you explain, sir, how the oil and gas lease, the unit operation agreement and the gas

storage agreement fit together?
~ In your opinion, did Imperial Oil, first,
through these documents retain the right to
production in

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 282]

126

this particular field?
~ A. What Imperial obtained under the
original lease was, as I've indicated, the right to
produce and sell the natural gas under the lease.
~ Q. Has that right now been extinguished?
~ MR. WAQUE: Mr. Chairman, again, we're
now -- my friend is now asking the witness specific
questions, legal questions, not questions of fact, but
legal questions on the application of these documents to
the particular subject matter before this Board.
~ In my respectful submission, that's not
appropriate, and I object to the question
for that reason.

~ MR. SULMAN: I won't repeat the arguments I
made before.
~ MR. McCANN: May I just make a comment, Mr.
Chair--
~ THE PRESIDING MEMBER: Sure, Mr. McCann.
~ MR. McCANN: --before we continue?
~ I tend to agree that it would not be
appropriate at this point for Professor Lucas to

comment

on the specific application of these documents to the
compensation matter in question here.
~ I think the background information we've
been provided is very interesting and very helpful, but
I'm concerned, too, that we should not be tending towards
conclusions of law about this specific dispute through
evidence rather than through legal argument.
~ THE PRESIDING MEMBER: Thank you, Mr.

127

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 283]

McCann. The Board has, in fact, come
to the same
conclusion.

~ MR. SULMAN: I didn't make any argument on
that yet, but I'd like to make it, for the record, in the
event I have to use the record for an appeal. But I
don't -- quite frankly, Mr. Chairman, there's -- the

issue -- there's are only very few issues, the issue of
ownership. I want to get to the question of profit a
prendre. I don't know who's going to tell you -- if we
don't get to the question of profit a prendre through this
witness, then all you get is opinion from me,
or argument
from me, and that's not opinion and it's
not something
that can be tested in argument from my friend.
~ You don't get a chance to test any of that,
and you know we're both advocates and you're not
getting
an objective opinion.
~ I want my witness to speak to the issue of
profit a prendre which my friend
put in issue in his
prefiled evidence and yet no one has spoken to it.
~ So, I mean, I can take the strict legal view
later that it was filed as prefiled evidence with no one's
name on it, and no one speaking to it, you can't consider
it later.
~ But I'm trying to get this material before
the Board. The burden of proof isn't on me, by the way.
It's on my friend, and he's closed his case
~ So all I want -- I think to get to the
question of profit a prendre, you have got
to know whether

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 284]

128

the company that has these leases still has
the right to
produce. In fact, Mr. Inwood raised that and
so did Mr.
Cochrane.
~ MR. McCANN: I have no objection to
Professor Lucas explaining the concept profit a prendre
and how it may relate to these documents
in the same
general sense that he's been doing so far. I think that's
helpful. I'm just concerned about applying it to the
Sombra pool as such.
~ I mean, he started off his evidence by
saying that the documents were very similar, if not
identical, to documents that were in common use in Alberta
in the early days of oil exploration. And that's a very

useful way to go about this. If we
can continue on in
that manner to explore the issue of profit a prendre,
that's certainly useful from the Board Staff's point of
view.

~ MR. SULMAN: I've made my argument. You've
heard the other arguments. The decision has been made.
I'll move on.

~ THE PRESIDING MEMBER: Well, could you
respond to Mr. McCann's suggestion, Mr. Sulman?

~ MR. SULMAN: Which is that the expert
witness shouldn't comment on the particular leases that
he's just reviewed in relation to the Sombra Pool?

~ MR. McCANN: Well, all I'll say is that the
witness, I think very helpfully,
started off by saying
that these documents were very similar to documents, if

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 285]

129

not identical, to documents that are in common use in
Alberta. What I took from that,
perhaps incorrectly, that
he was try to explain the common understanding,
in law, of

this type of document. He said at some point that it's a
common form document, and I don't recollect him having
mentioned the Sombra Pool in his commentary.

~ And all I'm trying to do is keep it at that
general level which I think is helpful to the Board.

~ MR. SULMAN: I'm prepared to move on then.

~ THE PRESIDING MEMBER: Thank you.

~ MR. SULMAN: Q. Professor Lucas, could you
turn to the Applicant's prefiled evidence, phase 2, issue
3, which is found at tab 3 of the
Applicant's prefiled
evidence.

~ This is the evidence that's related to the
ownership of the remaining gas in place at
the date of the
injection.

~ PROF. LUCAS: Excuse me, Mr. Chairman,
I'll --

~ THE PRESIDING MEMBER: Mr. Sulman, we'll
probably have to take a break in
five minutes or so.

So...

~ MR. McCANN: Are you missing the document,
Professor?
~ PROF. LUCAS: I'm just missing my own copy.
~ MR. McCANN: We'll be happy to supply you
with a copy for the purpose of getting on with this
question. Perhaps, we can...

130

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 286]

~ PROF. LUCAS: I have a copy here. That's
fine.
~ MR. SULMAN: Q. Do you have it before you,
Professor Lucas.
~ PROF. LUCAS: A. Yes, I do.
~ Q. I would particular like you to look at
~ paragraph 3, which I'll read into the record:
~ "By contrast, the lessee under an oil and
~ gas lease has interest limited to a profit a
~ prendre and has no other interest in the oil
~ and gas other as so long as they remain in
~ the ground and uncaptured: Canadian Oil and
~ Gas, supra, at 2.10 and 2.41; Berkheiser v.
~ Berkheiser (1957) S.C.R. 387. The owner of
~ the profit a prendre does not own the
~ minerals in situ; R. v. Tener (1985), 1
~ S.C.R. 533 at 541.
~ That's the entire paragraph; you see that, do you sir?
~ A. Yes.
~ Q. Now, what I'd like to understand is,
first, for purposes of the Board understanding
the concept

of profit a prendre. We have got some legal
terms in here
that I think you can help us with. And I'm going to ask
you particularly to explain what profit
a prendre is and
what relationship it has to the case at hand. Knowing
what it means floating in mid-air, I don't think helps
this Board much.

~ So if you could just start off with that,

131

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 287]

the explanation of the "profit a prendre", and you can see
it's quoted from the Canadian Oil and Gas text, and
Berkheiser v. Berkheiser case?

~ A. Yes, the concept of profit a prendre --
sorry--

~ Q. Yes.

~ A. --is fundamental to an understanding of
the relationship between the lessor
and the lessee under
an oil and gas lease.

~ The Supreme Court of Canada in the
Berkheiser case made it clear that when an oil and gas
lease is entered into, it does not
amount to a complete
sale, an outright sale of the mineral rights to the
lessee, because that was the question in
the Berkheiser
case, whether it amounted to an outright
sale or whether
it was some interest in the lessee that was less than an
outright interest in the minerals.

~ And the court there, interestingly enough,
took the same view that the Ontario Court of
Appeal, in a
case called "Dawson and Bell," had taken a few years
previously, and said it's in interest in the nature of a
profit a prendre.

~ And what a profit a prendre is, apart from
being bad French, is a classification that was given in
English property law to a certain category of property
interests. The holder of a profit a prendre has
the right
to go on to the property of another
and remove something
from the soil of that property. So
it's more than merely

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 288]

132

a lease of land to go on and use the land.

~ It involved actually taking something out of
the property permanently, whether it's trees, hard
minerals, or, in this case, natural gas. Okay?

~ The way to think about the difference
between what the lessor and the lessee have,
and we --
maybe, I'm going down a slippery slope here, Mr. Chairman,
but the analogy that we use with our students
is that of a

bundle of rights.
~ If you think about the full interest, the full freehold interest, that includes the surface and the minerals as the starting point, that represents a bundle of rights, and those rights would include particularly, the critical rights, would be the rights to exclude other people. Right? You can sue for trespass. And secondly, you can sell the rights that you have. You can sell the surface. You can sell the minerals. Okay? So those are

sticks in the bundle of rights.
~ And the next step is to think about dividing those rights because it's perfectly possible to lease the surface and create another interest and that would then represent a little bundle of sticks taken out of the larger bundle.

~ Similarly, you can sell an interest in the minerals and that, too, represents another little bundle of sticks taken out of the larger bundle. And that's what the oil and gas lease does in the kind of situation that we're looking at. So, the net result is that the lessor

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 289]

133

and the lessee have little bundles of sticks that represent legal property interests in relation to the oil

and gas. Okay?
~ So, in law, it's, in a sense, more appropriate to think about it in the abstract than to think about the oil and gas themselves sitting there in the ground, and that's the reason for the little bundles of sticks.

~ So, what then does the lessee have? The lessee's bundle would include the right to explore for, to drill, produce and transport gas from the land and to sell it. Those would be the sticks in the bundle.

~ The lessor's bundle in relation to the minerals would particularly include the right to the

royalty, the reversionary interests that
I mentioned previously, and under the lease, there would
be some other things: delay rentals in the primary term of
the lease and so on.
~ If you look at it that way, if certain
sticks are in the lessee's bundle, they are removed from
the lessor's bundle. So the lessee has the right to
produce and sell the gas. The lessor does not, okay?
~ So once the lease is entered into, the
lessor does not have the right to produce and sell the
gas, nor does the lessor have the right
to exclusively lease those rights to anyone else because the lessor has
already leased those rights, given those sticks to the
lessee.

134

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 290]

~ So the lessor, in a sense, has a legal right
to the natural gas, but that legal right is
represented by the royalty and the reversionary interest and
the rentals and so on. Those are the sticks in the bundle.
~ And I wanted to refer the Board to a very
short quote from a recent judicial decision
in Alberta on this question that speaks directly to what the lessor's
interest under an oil and gas lease of a
similar nature, in fact, is. This is a decision of
the Alberta Court of Appeal called Scurry Rainbow Oil Limited
versus Galloway Estate.
~ And my understanding, Mr. Sulman, is that
this has been filed?
~ MR. SULMAN: That's correct. It was sent
Monday -- in fact, it was delivered Monday. I've got
other copies available.
~ PROF. LUCAS: This is a decision that
involved a question of whether or not the royalty --
~ MR. SULMAN: If you could stop for a minute,

Professor--
~ PROF. LUCAS: Sorry.
~ MR. SULMAN: I'm not sure whether anybody
has this in front of them. I know they've
apparently got
it, but I'm just not sure that you -- I can see my friend
has got it.
~ MR. McCANN: We have a number of copies that
you provided to Board staff.
~ MR. SULMAN: It's been provided to the

135

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 291]

panel, the Board panel.
~ THE PRESIDING MEMBER: We don't have those.
~ MR. McCANN: Okay, we've got copies, I
think, of Scurry Rainbow Oil Limited
versus Galloway
Estate.
~ MR. SULMAN: What you have is the Scurry
Rainbow v. Galloway Estate at the Alberta Queen's Bench
and you have it at the Court of Appeal where it's
affirmed, so...
~ PROF. LUCAS: And it's the Court of Appeal
decision, the short one that I'm referring to, Mr.
Chairman.
~ MR. SULMAN: Before you do that, and we're
not going to have much more time before we break, but I
just wanted to know -- it says Alberta Queen's Bench on
the first page and it says Hunt J.
~ Is that the co-author with you of your oil
and gas law in Canada?
~ PROF. LUCAS: Yes, it is.
~ MR. McCANN: Could we just pause for a
second to get this material to the panel?
~ Do you have it?
~ THE PRESIDING MEMBER: We do have those, but
I'm just mindful of the time, Mr. Sulman. I wonder if
this is a good time to break. I know that the witnesses
have been there some time--
~ MR. SULMAN: I would suggest that.
~ THE PRESIDING MEMBER: --and the rest of us

136

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 292]
as well.

~ You did have some more questions of
Professor Lucas?

~ MR. SULMAN: Yes, I do.

~ THE PRESIDING MEMBER: Okay. Mr. McCann,
any suggestions in terms of the duration of lunch?

~ MR. McCANN: It is 1:30. Could I suggest
2:30 as a time to return? I think everybody needs some
time to seek refreshment and ideas and
instructions. I'm
suggesting 2:30.

~ THE PRESIDING MEMBER: Two-thirty. And I
suspect that the parties will try to
find some minutes to
discuss argument?

~ MR. McCANN: Yes.

~ THE PRESIDING MEMBER: You haven't allowed
for that?

~ MR. McCANN: I haven't -- we've had some
preliminary discussions. I believe the applicants are
agreeable to oral argument. I believe that the
respondents may favour written argument. Perhaps
we could
have some discussions in here at, say, twenty after two
and then make some submissions to the Board when we
resume, if that's agreeable to my friends. Perhaps they'd
rather just --

~ MR. WAQUE: I might suggest we do it at the
end of the day because I don't know how much longer my
friend will be, but I'll certainly have a very good
understanding of where my cross is going
by ten to four

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 293]

137

and then we'll have a more relevant discussion
rather than
discussing it hypothetically.

~ MR. McCANN: Okay, that's agreeable.

~ THE PRESIDING MEMBER: That's fine. That
sounds good. Okay, we'll be back at 2:30 then.
---Luncheon recess at 1:34 p.m.
---On resuming at 2:42 p.m.

~ THE PRESIDING MEMBER: Please be seated.

~ Mr. Sulman?

~ MR. SULMAN: Thank you, Mr. Chairman. When
we last left off, Professor Lucas just had us turn up the
Ontario (sic.) Court of Appeal case in Scurry Rainbow, so
if I can turn back to Professor Lucas.

~ MR. WAQUE: I believe my friend misstated
that. It's an Alberta Court of Appeal case. You said
Ontario.
~ MR. SULMAN: Oh, did I? I thought I said
Court of Appeal case, but whatever.
~ PROF. LUCAS: Yes, the Alberta Court of
Appeal decision in Scurry Rainbow and Galloway Estate.
~ This was a case that required the court to
decide whether the lessor's interest was an interest in
land or merely a contractual interest, so the
court had to
focus on the lessor's interest in particular.
~ And the particular page that I'm looking at
in the Court of Appeal's decision is 320. This decision
is based on a trial decision in the Alberta Court of
Queen's Bench by Madam Justice Constance Hunt. And
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 294]

138

Justice Hunt is now on the Court of Appeal
of Alberta, but
previously she was a colleague of mine at the University
of Calgary Law School and, in fact, was dean of the law
school prior to her appointment to the bench and
she's an
expert in oil and gas law. And consequently, she was
saddled with most of the oil and gas
cases that came
before the Alberta Court of Queen's Bench while she was
there.
~ And in this particular case, she wrote a
lengthy decision that analyzed the legal
character of the
lessor's royalty interest and concluded that it was an
interest in land. And in a very short
decision, which is
the one we're looking at, the Court of Appeal basically
said the trial judge was right.
They say three quarters
of the way down:
~ We find no reversible error in the trial
~ judge's analysis. We find her answers fully
~ supportable.
~ And then it's the next paragraph that I
wanted to direct the Board's attention to, the one that
begins "it is our conclusion":

~ It is our conclusion that following each
~ of the so-called initial P&NG leases - and
~ those would be free hold leases, Mr.
~ Chairman, in relatively similar terms to the
~ leases that you're looking at in this
~ application - the lessor retained not only a
~ reversionary right to the lessee's profit a
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 295]

139

~ prendre on the lease substances.
~ So that's the reversionary interest in the
lessor that I referred to. And the court is also noting
the lessee's profit a prendre. And you'll notice they
specifically say "on the lease substances". So it's in
relation to the oil and gas. So the
lessor retained the
reversionary interest but also a fee simple interest in
those substances in situ. So this court says quite
clearly, the lessor does have a fee
simple interest in the
oil and gas in situ in the ground.

~ But they go on:
~ As constituted by the royalty reserve to
~ the lessor in the lease.
~ So they are saying, that interest in the oil
and gas in the ground is represented by the
royalty that

was reserved to the lessor in the lease.
~ That interest, the court concludes, is,
~ of course, subject to the grant under the
~ lease of a profit a prendre to the lessee.
~ And that's the lessee's profit a prendre
interest, you'll recall, that gives the lessee the right
to go on the land, drill, produce, market, sell the oil
and gas. And the court quotes the Berkeizer
case which is

the same case that the applicants have referred to and
included in their prefiled evidence.
~ So, the statement is a very concise judicial
summary of the, I suppose, more general review that I've
given trying to look at the nature of the lessor's
[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 296]

140

~ interest and the lessee's interest.
~ And I wanted to just conclude by emphasizing

that this statement that I've just quoted refers to the lessor's interest and it emphasizes that that interest is the royalty and the reversionary right.

~ The lessee's interest is also referred to.

That's the profit a prendre. And that interest is the bundle of rights that I've mentioned. The right to produce essentially is the key stick in that bundle and the profit a prendre is not just a right to the produced substances. It is a right that relates to those substances in the ground and it includes

- and this is critical for the lessee - it includes the right to go and get those substances and produce them and sell them.

~ THE PRESIDING MEMBER: Mr. McCann, do we need an exhibit number for this?

~ MR. McCANN: We don't usually, I believe, give exhibit numbers to legal cases and material of that nature and I think we can just accept these as cases that are in the Law Reports and treat them that way. We've got the citations of them.

~ MR. SULMAN: Q. Professor Lucas, I had, before the break, referred you to paragraph 3 of the applicants' prefiled evidence, Phase 2, issue 3, and you've just been responding to the issue of profit a prendre.

~ The second part of that paragraph reads:

~ The owner of the profit a prendre does

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 297]

~ not own the minerals in situ.

~ And it quotes R v. Tenor, Regina v. Tenor.

~ I take it from that the applicants say the gas in situ is the property of the owner of the fee simple of the land, but that's, once again, a mouthful of legal terminology, some of which is Latin.

~ I wonder if you can explain what that means, what "in situ" means, and what it means when it said that the gas in situ is the property of the owner of the fee

simple of the land. What's that mean and do you agree?
And once again, I caution you, and I think
you're aware of this in the answers that you've given, I'm
not asking that

you refer to the Sombra lands.
~ PROF. LUCAS: A. The term "in situ" simply
refers to the substances in the ground as they are
situated in the ground, in the formation, if
you like.

~ The last statement in paragraph 3 - the
owner of the profit a prendre does not own
the minerals in
situ - is correct as a bald statement. But what
the owner

of the profit a prendre has is an interest - remember a
bundle of rights - in relation to the minerals in situ.
~ And similarly, the lessor has a bundle of
rights in relation to the minerals in situ and the
lessor's bundle of rights, the lessor's interest, is
represented by the royalty and the reversionary interest.
So this statement is too general to be meaningful.

~ Q. I ask you to turn to the -- I'm not sure
whether you have them before you, but the
interrogatories

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 298]

142

from Board Staff which would be found at
-- in a moment I
will have it.

~ It is the interrogatories of Board Staff,
the Applicant's answers to their interrogatories, phase 2,
which would -- I don't have a tab number for that.

~ It is the Applicant's answers to the Board
Staff interrogatories. Tab A, I am not told by Mr.
McCann. Do you have that in front of you?

~ A. Yes, I do.

~ Q. In particular I want to refer you to
paragraph 2.

~ THE PRESIDING MEMBER: Which number
interrogatory, Mr. Sulman?

~ MR. SULMAN: It would be Interrogatory No.
2.

~ THE PRESIDING MEMBER: No. 2.

~ MR. SULMAN: Q. In Interrogatory No. 2

there is a reference to the second edition,
page 91 of --
it says Ballem, it is John Bishop Ballem's text on oil
and gas law. Do you see that in
the interrogatory?

~ PROF. LUCAS: A. Yes.

~ Q. Do you know John Bishop Ballem?

~ A. Yes, I do. Mr. Ballem is a leading oil
and gas lawyer in the City of Calgary, and actually he has
been associated with the University of Calgary
law school,

has given lectures there and I do talk to him
on occasion.

~ He received an honorary degree from the
university a couple of years ago.

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 299]

143

~ Q. Okay. I wonder if you could explain Mr.
Ballem's analysis at page 91 of what an oil and gas lease
grants?

~ MR. WAQUE: Mr. Chairman, I object to that.
What is the utility of having Professor Lucas explain
somebody else's explanation?

~ THE PRESIDING MEMBER: Mr. Sulman?

~ MR. SULMAN: We don't have Mr. Ballem here,
this is the evidence of the Applicant, and we have an
opportunity to have the Professor of the University of
Calgary law school explain the analysis.

~ I mean, certainly he has read Ballem's text,
he has talked to Ballem, he knows him
well. All you've

got is a boldface statement here; we don't have any
explanation of what it is.

~ It's an easy way to put in evidence, but no
one comes to give anything that I can cross-examine.

~ MR. WAQUE: Mr. Chairman, it's not evidence.

We were asked to comment on whether
this text was an
authoritative text and we are dealing with it in

terms of

legal argument.

~ THE PRESIDING MEMBER: Mr. McCann?

~ MR. McCANN: I am concerned that we are kind
of reaching the limits of useful information
for the Panel

on this question of ownership.
~ It is getting very abstract and there are a
number of textbook extracts which have been brought to the
attention of the Board by one or another
of the parties.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 300]

144

~ I don't think anybody is disputing the
authority of these texts, and I think some reliance can be
placed on them in making argument.
~ But I'm concerned we're engaged in legal
argument here which is getting us further and
further away
rather than bringing us closer to what the Panel
needs to

decide this case. I would suggest that we try to limit
this type of evidence and get on with things.
~ I guess I would specifically suggest that we
let the interrogatory stand as it is. I'm not sure any
useful purpose is going to be served by further
explanation of it.
---Off the record discussion.

~ THE PRESIDING MEMBER: Mr. Sulman, could you
please move on to your next question.

~ MR. SULMAN: Certainly. By the way, I think
my friend should -- it should be clear that the
interrogatories do form part of the evidence in the case.
If they don't -- a decade of practice indicated to me that
these are all part of the evidence.

~ Q. Now, lastly, Professor Lucas, and I want
to be clear, you heard the ruling of the
Chairman earlier
that he didn't want you to draw conclusions in law with
regard to Sombra in particular.

~ But I would ask you from your position of
expertise as a professor of law specializing in oil and
gas law, there has been presented by the
Applicant in this
case certain case law.

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 301]

145

~ I just want if you can explain in layman's
terms the significance of the case law to the
interpretation of oil and gas leases.

~ MR. WAQUE: Mr. Chairman, isn't that

inviting the witness to engage in legal
 argument on behalf
 of the respondent?
 ~ THE PRESIDING MEMBER: Mr. Sulman?
 ~ MR. SULMAN: I take the view that when we
 get to legal argument there will be two
 advocates arguing
 and they will be applying the law to
 the particular facts
 at hand, I trust.
 ~ But what you will then have is no
 opportunity to ask anyone any questions whatsoever about
 their interpretation. I have got someone
 before you who
 you will have an opportunity to ask
 questions, Mr. McCann
 will and so will Mr. Waque.
 ~ Mr. McCann, of course, his duty is to make
 sure all the evidence gets before this Board.
 ~ I think it is an excellent opportunity. It
 is not argument. He's not going to apply it
 to this case
 at all. He is going to tell you what
 those cases mean.
 That's what a professor of law, that is what their
 expertise is and he is up here giving opinion
 evidence in
 his area of expertise.
 ~ Mr. McCann particularly, in the first day,
 gave us an admonition, that if you are going to rely on
 the law, try to put these matters in language
 that's going
 to benefit the tribunal members. Now, you are going to
 hear argument from two people who are hired to take a
 particular view. Now you've got a law professor
 and you
 can weigh what he says, but he is not going to apply it to
 Sombra. He is going to talk about these
 cases in regard
 to leases and lessees.
 ~ It is an opportunity that should not be
 missed by this Board. If they miss it by not hearing from
 Professor Lucas, I think that's very

unfortunate and the

missing of a very unfortunate opportunity, but you can weigh what he says after having heard it.

~ It is a rare opportunity to have a professor who specializes in oil and gas to come and give us this information.

~ THE PRESIDING MEMBER: Mr. McCann?

~ MR. McCANN: I agree with a good deal of what Mr. Sulman says, but I do feel that

we have had a background explanation of the interrelationship of certain common form documents.

~ To extend this to an explanation of case law and how it affects those common form documents,

it seems

to me we are almost working towards a law school seminar

or something here and I just -- the practical usefulness of this to the Panel begins to be difficult for me and I would urge us to try to deal with this with great conciseness.

~ I would submit that we have a pretty sufficient set of background information on the record now

from Professor Lucas who has been very helpful in

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 303]

147

providing this information and would urge that we move on to other matters.

~ THE PRESIDING MEMBER: Mr. Sulman, invariably in every rates case there is always legal arguments or case law that applies or being cited in legal arguments and we don't have a law professor every time to

tell us how case law would apply to specific situations.

So I suggest we move on.

~ MR. SULMAN: Fine. Those are all the questions I have for Professor Lucas.

~ There is one outstanding issue and that is back to the letter to Leo James Johnston from Bradley French.

~ Now, I guess what we are waiting to find out is if there is still objection to it and whether

I should

call Mr. French?

~ MR. WAQUE: Mr. Chairman, my position is pretty much what I expressed before lunch.

I don't have Mr. Johnston here. I have no indication that he got the letter. There is no indication that he agrees with the statements in the letter. So, from my perspective, it must remain as a self-serving letter.

~ Now, the Board has the power, I don't have to tell it, it knows, under the Statutory Powers Procedure Act, to accept evidence even if it isn't properly proven, even if Mr. French doesn't come and say I wrote the letter, but I don't think in that circumstance the letter can be accepted for the truth of the assertions in the

[Carlson, Stuart, Lowe, Lucas, Wilton dr ex (Sulman) Page: 304]

letter.

~ The fact the letter exists and apparently was written by Mr. French, I suppose we can accept that pursuant -- the Board can accept that pursuant to the Statutory Powers Procedure Act, but I don't have any capacity to go beyond that.

~ So in an effort to be of assistance, I would suggest the letter be marked an as exhibit, if that's what my friend wants to do, but I ask the Board to understand that I cannot accept the truth of the assertions in the letter as evidence for the reasons I suggested.

~ MR. McCANN: Well, on that basis I would be satisfied to give this an exhibit number. I think it is always clear that the relevance and weight of any piece of evidence is for the Board to determine.

~ It would, therefore, be Exhibit 9.8 unless Mr. Sulman objects to that. So Exhibit 9.8.

~ MR. SULMAN: No. This evidence has been given Exhibit 9.8 and it will be given the weight that it deserves by the Board in light of the deed and the evidence that's been giving orally. That's all I have ever asked, but it's not given conditionally, on the conditions that Mr. Waque puts forward. He can make his eloquent submissions on that.

~ You can give the weight to this evidence
 that you intend to give to it.
---EXHIBIT NO. 9.8: Letter to Leo James Johnston from
 Bradley French.

149

[Carlson,Stuart,Lowe, Lucas,Wilton dr ex (Sulman) Page: 305]

~ MR. SULMAN: With those final questions to
 Professor Lucas and with the letter from
Mr. French to Mr.
 Johnston that predated the deed from Mr.
Johnston to Union
Gas, that concludes the Union evidence-in-chief from this
panel and they are open for cross-examination.

~ THE PRESIDING MEMBER: Thank you, Mr.
 Sulman.

~ Mr. Waque?

~ MR. WAQUE: Thank you, Mr. Chairman.
 CROSS-EXAMINATION BY MR. WAQUE:

~ Q. Mr. Lowe, let me start with you. I take
 you back to Interrogatory 19 which is Union
Gas' response
 to the interrogatories from the Ontario Energy Board
 Staff.

~ There is reference to what was earlier
 described as the more modern royalty rates
and I think you
 have also referred in your evidence to the more modern
royalty rates, and the statement is made
that since 1991

 Union has included a purchase price of 12-1/2 per cent of
 the current market value for the remaining
recoverable gas
 in its gas storage agreements.

~ That answer is still true today, sir?

~ MR. LOWE: A. I'm sorry, I'm having
 difficulty finding that reference. Is it in the green
 binder?

~ MR. McCANN: No, it's in Union's responses
 to, in this case, Board Staff interrogatories. It is not
 in the green binder. It is not in this.

150

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 306]

~ MR. WAQUE: Q. Well, it is a simple
 statement, Mr. Lowe. I'm happy if you want to have it in
 front of you, but the simple statement in the

interrogatories was that since 1991 Union has included a

purchase price of 12-1/2 per cent of the current market value for the remaining recoverable gas in its gas storage lease agreements. That's true, is it not?

~ MR. LOWE: A. We have 12-1/2 per cent in some of the leases that were taken out after that period. We also had some leases that were still at 2 cents.

~ Q. Well, I'm not asking you about the agreements that are outstanding. I'm asking you since 1991 when you signed new agreements, has the purchase

price been 12-1/2 per cent? ~ A. In the majority of cases, that would be true, yes.

~ Q. All right.

~ A. But it's not a purchase price. It's an offer to purchase that's in the lease, and the impact of

that purchase may not be for some time.

As we've seen in the Sombra case, it can be upwards of 30 years before

those prices can be realized.

~ Q. Did you participate in preparing the answers to these interrogatories?

~ A. Yes, I did.

~ Q. So you were aware of this answer being made to the Board Staff when it was made last year?

~ A. Yes. I'm just trying to be responsive

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 307]

151

to the question and explain that a little further than what was asked in the question.

~ Q. I understand. Now, when Union decided in 1991 to put in a more modern royalty rate of 12-1/2 per

cent, presumably it did that with the same understanding

of ownership that we've heard from this panel today?

~ A. Could you rephrase the question?

~ Q. I understand there's a difference of opinion between Union and the Applicant about ownership of the gas--

~ A. Mm-hmm.

~ Q. --residual gas?

~ A. Yes.

~ Q. That has no impact on the royalty rate
 issue as to whether THE royalty rate should
 be 2 per cent -- 2 cents or 12-1/2 per cent?

~ A. Not in the signing of new contracts, no.

~ Q. No. So if from Union's point of view,
 if this agreement was being negotiated in 1991, it would
 have had a 12-1/2 per cent royalty rate and
 had nothing to do with the issue of ownership?

~ A. Hypothetically, that's correct.

~ Q. All right. You also gave evidence with
 respect to the Bentpath decision.

~ I wonder if we can have some common ground
 about that.

~ The Bentpath decision, you indicated, was
 rendered in 1982. Will you agree with me,
 however, that

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 308]

152

the date of first injection in Bentpath Pool
 was February, 1995 -- sorry, 1975?

~ A. I had thought it was 1974, but I stand
 corrected on that.

~ Q. All right.

~ Let's go forward using '75. I don't think
 it matters much if it's '74 or '75. If we apply the same
 approach that the Board is applying here
 which is to say that the relevant date for analysis is the
 date of first injection, then the Bentpath speaks as of 15 years before
 the relevant date before this Panel, is that
 not correct?

~ A. I would agree with that, yes.

~ Q. All right. And when union was
 negotiating new deals in 1991 it didn't
 think that the Bentpath decision still governed; it was
 prepared to move to a more moderate royalty rate, was it not?

~ A. No, I would disagree with that. The --
I would say the Bentpath decision, in our mind, still
ruled the payment of contracts that were set
at 2 cents.

~ Q. But if you take the point of view that
what we're involved in today is revisiting the issue of
price, taking a fresh look at it as of July 19th, 1990 -
and I'll get you back to there in a minute - but Union is
in 1991. In 1991, if Union was revisiting
that afresh, it
would be applying 12-1/2 per cent notwithstanding
Bentpath?

~ A. No, that's not correct. We would be
applying 12-1/2 per cent in new
agreements that were being

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 309]

153

executed at that time which may not
take effect for
another 30 years.

~ Q. If the Board thought that the relevant
information to determine a rate as of July
19th, 1990 was
the new agreement rate, then 12-1/2 per cent would be the
appropriate rate notwithstanding that?

~ A. I think the Board would have to take
into account other contracts that were being entered into
by other companies in addition to Union Gas.

~ Q. All right. That may be. But just
looking at Union's position, Union is saying the modern
rate, Ontario Energy Board, is 12-1/2 per cent?

~ A. No, I disagree with that. The modern
rate for a new contract which is on a
yet undiscovered
property whose effect may not be for
30 years as has been
the case in Sombra, the payment of the residual
gas added

12-1/2 per cent rate would be deferred for some time into
the future.

~ Q. Let me go at it at another way.

~ You -- in the interrogatories, Union filed
oil and gas leases and entered into two, I
think we're

told, selected at random. In answer to interrogatory --

Board Interrogatory 4(i), produce examples of gas storage agreements negotiated as of July, 1990, union produced two

agreements; is that not correct?

~ A. Again, I'm having difficulty finding that reference. Is it...?

~ Q. Now, I think you're going to need the

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 310]

154

document, so perhaps your counsel could provide you with a

copy of the answers.

~ THE PRESIDING MEMBER: Did you say Board Staff interrogatories, Mr. Waque?

~ MR. WAQUE: Yes. I'm sorry. No, I'm corrected. It's from the Applicants and it's 4(i). It's my mistake.

~ Q. Now, just stay with me for a minute on the general. We'll go to the documents in a minute?

~ MR. LOWE: A. Okay.

~ Q. Union's position is when we're negotiating new agreements in 1990, we stuck to 2 cents per mcf, and here is two examples of it. Is that not the

import of this answer?

~ A. That's correct.

~ Q. All right. And if this agreement had been in 1991, more likely than not, this would have been

at 12-1/2 per cent, would it not; that's the import of Interrogatory No. 19?

~ A. My instructions to the land agents are to attempt to get 2 cents per mcf, but if asked to move to 12-1/2 per cent by the landowner--

~ Q. Right.

~ A. --that is what we would negotiate.

~ Q. I see. So you drive the best bargain you can. You try to get 2 cents

if you can get it. You

tell the landowners, 'Gee, that's what the Board said in

Bentpath.' And if you can't get it, then you adjust your

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 311]

155

rate?

~ A. No, that's not true at all.

~ As you know, these agreements are a matter of negotiation. They're -- as I pointed out this morning, there's still also lot of companies using sliding scale royalties. The issues between 2 cents, 12-1/2 per cent, or sliding scale is a subject of that negotiation. And we do not specifically point to Bentpath in any way in those negotiations.

~ Q. I thought you said here in-chief that you were governed by Bentpath or felt governed by Bentpath?

~ A. Yes, that's true.

~ But leasing practices are a very dynamic process. And you have to start -- you have to be competitive in the marketplace. We do a lot of 3D seismic programs for example. And when we want to go outside the boundary of our designated storage areas to get what they call tail-spread coverage for 3D seismic, we often take out new leases.

~ When we're doing an extensive 3D seismic program, we have to assure ourselves that we can get those leases.

~ Q. But when you were in the marketplace in 1991, Interrogatory No. 19 tells us you were happy to pay 12-1/2 per cent; that was your experience, generally speaking?

~ A. Generally speaking, yes, I would agree

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 312]

with that.

~ Q. Now, just by way of interest because you've mentioned the sliding scale, and my friend put the sliding scale to Mr. Inwood, I presume at the time these

gas storage agreements were negotiated, of the two that you've extracted here they were also production leases that were negotiated?

~ A. Yes, that's correct.

~ Q. All right. And do you know what rate was prescribed in those production leases?

~ A. The majority of our leases were at 12-1/2 per cent.

~ Q. Maybe I can help you understand it a bit better. I asked for and obtained copies of the companion production leases to these gas storage leases.

~ MR. SULMAN: Is this the reverse of what you objected to yesterday, me doing yesterday?

I haven't seen

any of these I don't think and I didn't know you were going to introduce them.

~ MR. WAQUE: These are Union Gas documents. They are the companion documents to the one produced in the interrogatories.

~ MR. SULMAN: I'm sure there are thousands of Union Gas leases.

~ MR. WAQUE: Well, Union Gas was asked to produce examples of gas storage agreements.

It produced

two and I just think it is interesting to look at the companion documents, particularly in light of my friend's

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 313]

157

position on the sliding scale and how the sliding scale was still in the marketplace.

~ MR. LOWE: Am I allowed to make a statement?

~ MR. SULMAN: Well, just before we go any further, I just want to have a look at the documents, that's all, before they're submitted to the Board panel. Before they are submitted to the Board panel,

Mr. Mackie,

the same treatment I got earlier, if you would. Just let me -- if I might, Mr. Chairman, I'd like to have a look at them.

~ THE PRESIDING MEMBER: Certainly.

~ MR. SULMAN: I'm having a little trouble
reading the bottom page.

~ MR. WAQUE: If it helps my friend, the
portion of the documents that I want to refer
the witness
to are the production rates and the crossing over of those
rates as Mr. Inwood referred to in his evidence.

~ MR. SULMAN: Well, I'm not objecting to --
unlike what happened to me yesterday, I'm not objecting to
my friend using these for cross-examination purposes even
though this is the first time I've seen them. The only
concern I have, Mr. Chairman, is that there's
some areas
that -- I can't tell whether these are the original
documents. There's some areas that are crossed out and
they are not initialed by the Union Gas signatories.

~ So I can accept them for purposes that Mr.
Waque may want to put them for cross-examination, but I
can't say that these are the original documents and I

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 314]

can't say that the areas that are blacked out -- and
there's an addition in handwriting here that only has the
initials of the landowner but isn't initialed
by the Union
Gas representatives. The initials simply aren't there. I
don't have a problem with him using them for
cross-examination, but --

~ THE PRESIDING MEMBER: Mr. Sulman, I take it
that if you're not satisfied those were copies of the
originals, then you would let the Board know in due
course?

~ MR. WAQUE: I can go further --

~ MR. SULMAN: Yes, that's a fine way to do
it.

~ MR. WAQUE: Mr. Chairman, I will have
certified copies of these documents in my
office today and
I will file them with the Board.

~ THE PRESIDING MEMBER: Would that be
necessary, Mr. Sulman?

~ MR. SULMAN: It will only be necessary if on
seeing them I'm not satisfied that the changes were made
at the time. And I'm not suggesting they are. I just
can't tell from the documents I've been given.

~ THE PRESIDING MEMBER: All right. We'll
assume that they are unless you notify us otherwise.
~ MR. SULMAN: That's a fair way to do that.
Thank you, Mr. Chairman.
~ MR. LOWE: Am I free to look at the
documents, Mr. Sulman?

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 315]

159

~ MR. SULMAN: Certainly. Mr. Waque is going
to ask you questions on them.
~ MR. McCANN: We should get some exhibit
numbers for these. Exhibit 7.4 would be -- I see the
surname Kinnegan (phoen) and 7.5, I
see the surname
Sexton.

---EXHIBIT NO. 7.4: Companion document, Kinnegan,
to the
gas storage agreements.

---EXHIBIT NO. 7.5: Companion document, Sexton,
to the
gas storage agreements.

~ MR. WAQUE: Q. Mr. Lowe, first of all,
you'll agree with me that these are the companion
documents to the two gas storage
lease agreements produced

by Union in its interrogatories?

~ MR. LOWE: A. If you'll just give me a
moment while I check the property descriptions,
please.

~ Q. You can do that. You can also check the
instrument number which is cross-referenced in the gas
storage agreement.

~ A. Thank you, that's helpful.

~ Q. That's how I found them.

~ MR. McCANN: For the assistance of the
Board, perhaps Mr. Waque could explain what he means by
the 'companion leases'; I mean what he means by that term
in asking the question.

~ MR. WAQUE: What I mean is that, at the same
time or about the same time as the gas storage leases were
negotiated, production leases were also negotiated. These
are the production leases that were negotiated and are

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 316]

160

referred to as being in existence in the

gas storage lease

agreements.

~ MR. McCANN: I think someone's having a bit
of difficulty just collecting the documents.

~ MR. WAQUE: If you turn to Interrogatory No.
4(i)--

~ MR. McCANN: Okay, that's where --

~ MR. WAQUE: --Union was asked to produce
examples of gas storage agreements negotiated
as of July,

1990. It chose to produce two. One --

~ MR. McCANN: Sorry, whose interrogatory to
Union Gas?

~ MR. WAQUE: These are the Applicants'
interrogatories.

~ MR. McCANN: Okay. I think we're catching
up with you now. And the question in that -- no, just a
minute. The question 4(i) was, as you said: Produce
examples of gas storage agreement negotiated

as of July,

1990. Okay. I think -- sorry to be laborious, but just
to get everybody on the same page.

~ MR. WAQUE: And Union said here, look, here
are two leases we got at two cents and I'm simply now
drawing to the witness' attention that associated with
these leases were production agreements. And now I'm
going to draw the witness' attention to the

rates in the

production agreements.

~ Q. And will you agree with me, if we look
on page 3 of each production agreement, the question,

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 317]

161

Exhibits 7.4 and 7.5, that apparently
this was a form
which presented a sliding scale type agreement?

~ MR. LOWE: A. That's correct.

~ Q. And that was crossed out and substituted
with a flat 12-1/2 per cent arrangement?

~ A. That appears to be correct, subject to
Mr. Sulman's clarification on the certified copy.

~ Q. So in the marketplace in July of 1990,
here's at least two examples of Union being required at
least on the production side to pay a 12-1/
2 per cent

royalty?

~ A. That's correct.

~ Q. And the sliding scale which Mr. Sulman suggested to Mr. Inwood was the market experience in about 1990. That certainly wasn't accepted by these two owners.

~ A. That's correct.

~ Q. All right.

~ Now, let me understand how this works from your point of view, Mr. Lowe. Let's say that - to give you a hypothetical, so I understand your evidence - let's say that we carry on the resources produced for a time and then Union decides to convert to gas storage. Do I take it that it was Union's intention that at any point in time they could say to these landowners, although we've been paying you 12-1/2 per cent, we now decide we're going to use the well for gas storage and we will pay you two cents per mcf for the residual gas?

~ A. That's correct, that's the impact of [Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 318]

these leases. But as Mr. Inwood spoke yesterday in his cross or cross-examination, storage leases often lag the production leases.

~ Q. It doesn't seem fair or just or equitable to me, Mr. Lowe, that you would put Union in the position where it could elect to convert them at 12-1/2 per cent royalty to two cents per mcf. Does it seem fair, equitable or just to you?

~ A. It would depend on the level to which the gas had been produced. There's less value in the last production than there is in the initial production.

~ Q. In any event, by 1991, Union had moved off this position and decided to go to 12-1/2 royalty on the gas storage residual gas?

162

~ A. In general, that's correct. There were changes in our leasing practices, but again, I reiterate that the impact of that change in our leasing practice may

not be realized for 30 years.

~ Q. Yes, you said that a number of times, sir.

~ A. And in addition to that, I spoke this morning about the fact that, having worked on the unitization committee, I only recently, as

December and

January, became aware that the leasing practices in and

around 1990 may not have changed to 12-1/2 per cent as I

had expected it had. And that was the reason for doing my search for the first three months in 1990 and easily uncovering 40 leases that were, in fact, still at the

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 319]

163

sliding scale approach.

~ Q. But they weren't leases negotiated in 1990. They were leases negotiated from 1950 to 1970.

~ A. No, that is not correct. They are leases negotiated in the first three months in 1990 and Mr. Sulman tried to get them submitted yesterday.

~ Q. You said in your evidence that each of Union and Consumers did all of their leases at two cents.

~ Do you recall that evidence?

~ A. We had been doing all of our leasing at two cents up to that point in time, yes.

~ Q. And I believe you also, in the written interrogatories, you suggested that it was the smaller producers that were paying more than two cents in 1990, although by '91, Union was paying 12-1/2 per cent.

~ A. Our leasing practice did lag the market in that respect.

~ Q. All right.

~ A. Small producers often have to provide an additional incentive for landowners to lease with them because they don't provide the same level of security in the payment.

~ Q. Well, I gather that it would surprise you then if you learned that there were Consumers Gas leases executed in 1990 or in 1989 at 12-1/2 per cent?

~ A. No, it wouldn't surprise me. I don't know exactly when their leasing practices would have changed.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 320]

164

~ Q. That's important because -- if I can just have a moment, I'll get the prefiled evidence.
~ So when you said in paragraph 33 of your prefiled evidence, you made reference to the Edys Mills

and Oil Springs situations and noted they were not transacted by either Union or Imperial but by smaller operators, you didn't mean to suggest that a larger operator like Consumers was not in the marketplace in 1990

paying 12-1/2 per cent?

~ A. Okay. I think I'm running into a bit of confusion between Telesis and Consumers and Tecumseh.

~ Q. Well, let me show you a gas storage lease agreement.

~ A. It's very common practice for the Board's point of view for Consumers Gas to hold the leases for Tecumseh and Telesis, so I'm a little uncertain as to

who was intended to be the holder of this lease.

~ MR. SULMAN: Before you answer, if I could have a chance to look at this. I'm sure Mr. McCann would

like a copy, too.

~ MR. McCANN: I would suggest Exhibit 7.6.

~ MR. SULMAN: Well, I may have objections.

~ MR. McCANN: Sorry, okay, we'll reserve on that.

~ MR. SULMAN: I have no objection. There's no objection to using this document in cross-examination.

~ MR. LOWE: Having reviewed the signatures on this document --

165

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 321]

~ THE PRESIDING MEMBER: Can we get some copies?

~ MR. McCANN: Oh, yes. First of all, the panel needs copies. Also, it would be helpful to know which pool we're talking about in relation to this gas storage lease.

~ MR. SULMAN: Can you put that on the record?
You asked the question. I think the
response that I just
heard should be on the record.

~ MR. McCANN: Yes. I don't think the
microphone quite picked up your response.

~ MR. WAQUE: This is not a designated pool.
This is an exploratory situation.

~ MR. LOWE: With that understanding and
reviewing the signatures on this document,
it would be my

conclusion that that lease was taken out for the
exploration division as opposed to the storage division of
Consumers Gas and my --

~ MR. WAQUE: Q. Well--

~ MR. LOWE: A. Sorry.

~ Q. Consumers Gas company is a large
company, Mr. Lowe?

~ A. Yes, it is.

~ Q. And this document happens to be signed
by Mr. Craig. He was the gentleman who was here
yesterday

but did not have an opportunity to give evidence?

~ MR. McCANN: Could I just suggest that
this should be Exhibit No. 7.6.

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 322]

166

~ THE PRESIDING MEMBER: So marked.

---EXHIBIT NO. 7.6: Gas Storage Lease Agreement.

~ MR. WAQUE: Q. That's the same Mr. Craig as
far as you know, the Robert Craig that we
were discussing
yesterday?

~ MR. LOWE: A. Yes, I recognize his
initials.

~ Q. All right. He was with Consumers Gas,
and Mr. Cass here was from Consumers Gas saying
we should

not have Mr. Craig in evidence, it will be a
prejudice to

Consumers Gas?

~ Did you hear that, Mr. Lowe?

~ A. Yes, I did. But I understand Mr. Craig
has changed roles and gone back for his M.B.A. and
returned to Consumers Gas since this signature.

~ So I can't say that he is speaking from the
 same position today as he was at this time.
 ~ Q. Let me take you to paragraph 17 which is
 on page 3 of this document.
 ~ A. Yes, I have that.
 ~ Q. This is a 12-1/2 per cent rate--
 ~ A. Yes, it is.
 ~ Q. --for gas? This is a document
 apparently signed in June of '89 and registered in August
 of 1990; is that correct?
 ~ A. Yes, I see that.
 ~ Q. All right. Now, go with me to paragraph
 18.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 323]

167

~ A. Yes.
 ~ Q. Is this provision not a similar
 arbitration provision to the one we
 have in issue in this
 case before the Board?
 ~ A. It appears to be similar, yes.
 ~ Q. So if it happened that the gas storage
 designation and the value of the residual gas
 didn't come
 to be settled for many years, as you suggested in your
 earlier questions, and the owner was dissatisfied
 with the
 old rate of 12-1/2 per cent, what would then be the old
 rate of 12-1/2 per cent, he would have a right to
 arbitrate and get a new rate, wouldn't he?
 ~ A. That's not been our interpretation of
 this clause, no.
 ~ Q. No, I know it hasn't. But wasn't that
 the interpretation of the clause that the Board gave in
 its Phase 1 decision?
 ~ A. That would be a legal opinion that I
 would defer to counsel.
 ~ Q. I see.
 ~ THE PRESIDING MEMBER: Mr. Lowe, it is an
 easy question. What did the Board say?
 ~ MR. LOWE: The Board said that there was not
 agreement.
 ~ MR. SULMAN: In Sombra. We are trying to
 keep these things very specifically. These are apparently

not precedent setting.
~ MR. LOWE: But it has been my evidence as
[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 324]

168

well that in the Bentpath case the landowners with
standing or without -- the landowners that applied that
had disagreement were not given standing. So I cannot
anticipate what the next Board may do with a
similar lease

in a similar situation.
~ MR. WAQUE: Q. I think we are understanding
you, sir.

~ If the Board acts consistently, however, the
situation is that the landowner who signed this lease in
1989 will have a chance to revisit the royalty rate at a
later date if he finds what will then
be the old royalty
rate of 12-1/2 per cent isn't satisfactory or appropriate?

~ MR. LOWE: A. If everything was the same,
yes, that would be correct.

~ Q. Now, I would like to turn to Mr. Wilton
for a second. Sir, you gave evidence about five or six
owners, you weren't sure how many, who settled -- I think
your evidence was they accepted two cents in the Sombra
pool.

~ MR. WILTON: A. If that's my evidence, I
advanced offers to all owners within the
pool. I thought

I had said that.

~ Q. And let me just understand what the five
or six represent. You were asked in terms of numbers of
owners. I want to direct you to the
percentage of the
pool.

~ The five or six who from your perspective,
and I will question you on it in a moment, accepted the

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 325]
two cents, would I be fair in understanding
that they

represented less than 10 per cent of the pool?

~ A. My understanding is that this matter
deals with about 85 per cent of the interests
in residual

gas and that the offers that were accepted
represent about

169

15 per cent of the outstanding interest or the interests in residual gas.

~ THE PRESIDING MEMBER: I'm sorry, 15 per cent of the total area or is it numbers of landowners?

~ MR. WILTON: I thought what I was being asked was, if I could consider the amount of residual gas to be compensated for.

~ My knowledge is that 15 per cent of that number, 15 per cent of 100 per cent have accepted the offers as they were tendered.

~ THE PRESIDING MEMBER: Thank you.

~ MR. WAQUE: Q. Of those five or six owners who represented that 15 per cent, now that we understand that percentage, when you say they accepted, am I correct

that it's not the case that they gave you any formal acceptance; they just chose not to issue notice of their intention to arbitrate?

~ MR. WILTON: A. There was no notice provided to Imperial Oil of their intention to arbitrate, that's true. But as the contracts are constructed and as Imperial Oil understood, and as I administered those leases, our understanding was that if we had not received a notice of objection within the time period that is

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 326]

170

allowed within the provisions of the gas storage lease, that the payments are to be issued in accordance with the offer.

~ Q. I am not disputing the status of those five or six situations. I just want the Board to understand that these owners didn't take any positive step of accepting. They simply did not take the action of issuing a notice of arbitration?

~ A. I would agree they didn't take action by issuing a notice of arbitration, but I don't know whether or not I would categorize what they did as positive or

negative.

~ Q. All right. And you don't know whether they were pleased or happy or satisfied or content; they just didn't take any action?

~ A. I don't know their mental state at that point.

~ Q. All right. Would you agree with me that -- I mean, you are out there negotiating with farm families on a regular basis?

~ A. Yes.

~ Q. And by nature and generally speaking we are talking about a fairly conservative group of people?

~ A. I don't know that I'd go that far.

~ Q. All right.

~ A. If I could say, I consider them to be down-to-earth on the whole. Perhaps I can say that.

~ Q. Generally having limited financial

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 327]

171

resources these days?

~ A. Oh, no, I wouldn't say generally having limited financial resources these days, no. I wouldn't agree with that.

~ Q. Would you agree with me that to issue a notice of arbitration and to get involved in a two-year legal process and to pay for legal counsel and experts as the two owners have had to do in this proceeding, that's a

very significant commitment on their part?

~ A. That would seem like a reasonable observation.

~ Q. You wouldn't expect that people who had a modest interest, maybe a one or two per cent interest in

a pool, would be inclined to do that, would you?

~ A. I don't know that it would be something they would leap into.

~ Q. Thank you.

~ Now, maybe we can get started a little bit and lay some background on the question of ownership with Professor Lucas.

~ First of all, I want to see if we can have some common ground about the difference between

Ontario

and Alberta, Professor Lucas.

~ Have you a copy of the Applicant's book of
authorities?

~ PROF. LUCAS: A. Sorry, no, I don't.

~ MR. SULMAN: What's the date of this?

~ PROF. LUCAS: I'm sorry, this is what was

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 328]

172

filed just recently?

~ MR. WAQUE: It was delivered to Mr. Sulman
on Monday.

~ PROF. LUCAS: Yes. I'm sorry, I do have a
copy, though of course it's not nicely tabbed.

~ MR. WAQUE: If it suits you to use that one,
you are welcome to do that.

~ Q. Just starting at tab 2, pursuant to the
Constitution Act, 1867, mineral rights, generally
speaking, reside with the Crown; is

that not correct?

And, in particular, with the Crown of the particular
province?

~ PROF. LUCAS: A. Well, unless those mineral
rights have been granted by the Crown
to private parties.

~ Q. All right. And if we go to tab 3, there
is an act of the legislative assembly, the Province of
Ontario, and in particular clause 2.3 of
that act which

fundamentally revokes Crown ownership of mineral
rights in

Ontario where lands have been deeded and
deems that

mineral rights pass with those lands with the
passing of
the fee simple interest.

~ A. Yes, I see that.

~ Q. All right. And there is no such
companion act in Alberta?

~ A. No, there is not.

~ Q. So, generally speaking, in Alberta,
there is public ownership of natural resources
including

oil and gas?

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 329]

~ A. My understanding is that approximately 15 per cent of mineral rights in Alberta are freehold mineral rights; that is, they were obtained under an earlier regime in the history of the province when the rule was similar to that under section 3 of the act to which I have been referred. That would have been in the latter part of the 19th century.

~ And after that, the government, and at that time it would have been the Government of Canada of course and not the Government of Alberta, enacted legislation that had the effect of automatically reserving the mineral rights to the Crown.

~ Q. So in answer to my question, it was fairly put for me to say that generally speaking in Alberta mineral rights including oil and gas are owned by the Crown?

~ A. That's correct.

~ Q. Generally speaking in Ontario they are freehold?

~ A. That's correct.

~ Q. All right. So we have those two different regimes, generally speaking?

~ A. The other thing that is important to understand about Alberta is that the freehold minerals

represent the older developed fields in the parts of the province that were settled earlier; namely, the southern and eastern parts of the province. So they were the pools that were first developed.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 330]

~ Q. Let me take you now to your text that we have heard reference to. Do you have a copy of it there?

~ A. Mr. Sulman has a copy.

~ Q. I have prepared extracts from the text,

but it may not be necessary for them to go into evidence if we can agree.

~ MR. McCANN: I just remind you, I don't think the Panel has this text in front of them.

~ MR. WAQUE: I understand. It may not be necessary for it to go in if we quickly can come to some understanding about what I'm addressing.

~ Q. I'm at the bottom page 3 and the top of page 4. We have had reference here to John Ballem's text, the Oil and Gas Lease in Canada, which my friend correctly notes we have quoted from, and you make reference to it here.

~ I put it to you, sir, that the reference you make here is that the freehold lease is not explicitly treated here, meaning in your text, as it has been the subject of much commentary, particularly John Ballem's, The Oil and Gas Lease in Canada, now in its second edition. Have I got that right?

~ PROF. LUCAS: A. That's correct.

~ Q. So what you are saying is, to the reader, look, if you want to know about freehold lease situations, like, for example, the ones we deal with in Ontario, read Ballem's book because I'm not focusing on that? Is that a fair paraphrasing of that?

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 331]

~ A. We decided not to cover in detail the ground that had already been covered by Ballem in his book. But we did, if you look at chapter 1, beginning on page 5, we did treat the subject of the legal nature of oil and gas interests, including the question of ownership of oil and gas in situ, and if you flip over to page 7 we also look at the oil and gas lease and the nature of -- the legal nature of interests under the oil and gas lease which I thought was what we were discussing here.

~ Q. I gather you would have no difficulty in

deferring to John Ballem's text with respect to freehold interests given your characterization here on pages 3 and 4 of your text?

~ A. It's an authoritative text but like any other text it's subject to interpretation itself, and sometimes the subject of disagreement.

~ Q. I guess that would apply to your text, as well?

~ A. Indeed it would, yes.

~ Q. And some people would agree with your interpretation on the question of ownership; some people would disagree; some people would agree with Mr.

Ballem,

and some people would disagree with him; am I not correct?

~ A. Some of these issues are certainly subject to disagreement, particularly the subject of the ownership of oil and gas in situ and the nature of the interest under the leases. And that's the reason that we decided to treat those issues in our book even though

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 332]

176

Ballem also deals with the same issues in his book.
~ Q. I'm on page 144. And we have reference to the American experience and hence the prefiled evidence, and I'm sure we'll hear about it in argument.

~ The paragraph begins:

~ However, while the American experience in literature can be helpful in understanding was certain contracts are written the way they are and why certain contractual practices exist almost unquestioned, there are limits to this usefulness...

~ And then there's reference to tax issues.

~ ...and finally the fact of extensive crown ownership of minerals in Canada has required the utilization of many clauses which would be viewed with puzzlement by an American attorney.

~ Now, I gather that what you're saying there

is that a Crown ownership regime is a different
frame of reference from a freehold regime; is that correct?
~ A. That's partly what is being said here.
~ The other part, and perhaps the more
important part, concerns the relevance of the American
case law and the American literature.
~ Q. All right. But you'll agree with me
that the American experience is with freehold leases?
~ A. Uh --

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 333]

177

~ Q. Generally speaking?
~ A. Generally speaking it is although at
this point in time a great deal of American oil and gas
law is concerned with government leases
as well because the Americans have developed the easily
reachable reserves for the most part, and they are more concerned these days
with oil and gas rights in Alaska and
offshore, and those are -- those rights, in fact, are owned by the federal or
sometimes by the state government.
~ So there is a comparability if you look at
the current situation.
~ Q. But if we were addressing,
for example, the continental United States and the experience
there, because that is a freehold lease experience,
that would be more relevant than dealing with the cases, for example, in
Alberta that dealt with Crown ownership situations?
~ A. If you've spent any time in northern
Alberta, you might conclude that Alaska
was in fact more comparable.
~ Q. I'm not talking about the geography or
the climate. And for your information I have
spent some time there. I was addressing the question of whether
leases were freehold or crown owned?
~ A. It's correct that in the lower 48 the
U.S. oil and gas leases tend to be

freehold. I've pointed
out that you really have to look
at the whole picture in
the United States covering Alaska and the offshore as
well.

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 334]

178

~ Q. Right.
~ Now, just for the record, because I want to
be careful about the questions I ask
of you here, I don't
want to be responsible for drawing you into any
difficulty. Can we just confirm, for
the record, I think
we got it that you weren't qualified to practice in
Ontario, and that you didn't request a special
call from
the Law Society of Upper Canada in connection with this
retainer?

~ A. That's correct.

~ Q. All right.

~ A. And the reason is that I'm participating
in this regulatory hearing, I understand, purely as a
witness and not as counsel. I'm not retained by any party
as counsel.

~ Q. I understand your interpretation, but I
want to be clear about your position and
ask you the right
question. I'm not asking -- I'm going to ask
you to refer
to the Robbins and Woolf decision, a decision
of Mr.
Justice Day of the Ontario Court of Justice, which is
found under tab C; that would be 3C of Exhibit

7.1 of the
prefiled evidence of the Applicant.

~ A. Yes, I have that.

~ Q. All right. Now, I just ask you, you've
read that decision before today?

~ A. Yes, sir, I have.

~ Q. And I'm not going to ask you to opine on
Ontario Law, but I'd like you to turn to page 5.

[Carlson,Stuart,Lowe, Lucas,Wilton cr ex (Waque) Page: 335]

179

~ I think we can agree that Mr. Justice Day

has reviewed the history of the leasehold interests.

~ THE PRESIDING MEMBER: Mr. Waque, we're a bit lost here. Can you give us the reference again?

~ MR. WAQUE: Mr. Chairman, it's --

~ THE PRESIDING MEMBER: The Phase 2 binder, Phase 2.

~ MR. WAQUE: Exhibit 7.1, tab 3C.

~ THE PRESIDING MEMBER: Thank you.

~ MR. WAQUE: Mr. Justice Day of the Ontario Court of Justice has been reviewing the leases in question

which are oil and gas leases. And he concludes:

~ The Woolf and Robbins leases provide the
~ lessee the right to produce while retaining
~ with Robbins and Woolf the ownership in the
~ oil and gas resources.

~ Now, I'm not asking you to opine on Ontario Law. I'm just asking you is it not the case, sir, that you disagree with that statement?

~ PROF. LUCAS: A. No, sir, I do not disagree with that statement. The judge says the "leases"

which as

I understand are freehold leases at least comparable to

the ones in issue in this application.

~ The leases provide to the lessee the
~ right to produce...

~ That's the profit a prendre interest that I outlined earlier while retaining

with Robbins and Woolf the ownership in the oil and gas resources. That's the

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 336]

180

ownership in relation to the oil and gas resources in situ

as represented by the royalty as I'd indicated earlier. The judge simply doesn't spell it out here.

~ Q. So you have, if I can put it on a gloss or a further explanation of what you think the judge

means, but insofar as the simple statement that Robbins and Woolf retained the ownership in the oil and gas interest -- or the oil and gas resources, you

agree with

the statement?

~ A. If you, sir, are interpreting this statement as meaning that Robbins and Woolf retain the full fee simple interest in the oil and gas resources,

then I would disagree with that statement.

~ Q. What happened in this case, Professor Lucas, is that Robbins and Woolf were found to be entitled to the full ownership in those oil and gas resources; is

it not the case?

~ A. I'm sorry, could you repeat, please.

~ Q. What happened in this case is that Robbins and Woolf were found by Mr. Justice Day to be entitled to the complete ownership of the oil and gas resources in question?

~ A. What happened in this case is that the court decided that the oil and gas lease terminated because production had failed. Because there was no further production according to the habendum clause - you will recall the habendum clause that we looked at 10 years

and so long thereafter as production continued - when

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 337]

181

production failed, the condition that provided for the continuation of the lease failed, and the lease went click. The entire interest then vested, okay, the reversion then vested in Woolf and Robbins.

~ Q. Isn't what Mr. Justice Day is saying, that it didn't have to revest or come back because it never left? They never gave it away. They always had the oil and gas resource ownership in their possession.

~ A. No, he's not saying that. He's saying that the lease failed and, therefore, the lessee's profit

a prendre terminated when production terminated.

Therefore, the lessee -- the lessor ends

up with the full fee simple interest in the minerals.

~ Q. There's no language in this decision about revesting. The language in this decision,

Professor, is that the ownership was with these gentlemen

from the beginning.

~ MR. McCANN: The Board has this case, and I think its significance can be developed in argument. I'm not sure --

~ MR. WAQUE: I accept that.

~ MR. McCANN: I don't believe it would serve any purpose to go on answering -- asking the professor to

answer questions about it.

~ MR. WAQUE: I think I understand his position.

~ PROF. LUCAS: The answer to your last question is no.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 338]

182

~ MR. WAQUE: Q. When you mentioned the rights that remained with the owners, I take it that it's your perspective -- I'll go to your bundle of rights example.

~ In your bundle of rights approach to these interests, we have the question of title to the oil and gas. That's one of the sticks in the bundle of rights in your example; have I got that right?

~ PROF. LUCAS: A. The term "title" can be used, in fact, in relation to any particular interest; that is, one can have title to a profit a prendre interest - that is the lessee's interest.

One can equally have title to the minerals as lessor. One can also have title to the entire fee simple in minerals.

~ Q. Well, I'm just using your language, sir. You said in your evidence that you conceived of it by way of one law school example as a bundle of rights and one of

the sticks is title to the oil and gas.

~ A. One of the sticks would be a right in relation to the oil and gas in the lessor's case under an

oil and gas lease. That, as I said, would be represented by the royalty and the reversion. That's what the -- it's that little bundle of rights to which the lessor has

title.

~ Q. I'm going to be very simple about it.
When I use your sticks example and I want to understand
when we're passing the stick back and forth between lessor
and lessee.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 339]

183

~ When you read these documents to the Board,
you repeatedly made reference to the language
as and when
the substances are recovered. And I put it to you that
the ownership of the gas, the legal title to
the gas, that
stick passes from me, as lessor, to
you, as lessee, when
you produce the gas.

~ A. When the lessee obtains the lease - the
lessee, as I mentioned repeatedly - the lessee has certain
rights - the right to go on the land,
to drill, to
produce, to market and sell. At the
time the lease is
executed, the lessee has all those rights,
okay? The
lease makes it clear that when the substances are
produced, the lessee has title to those
substances so that

they can be sold with no question.

~ Q. I understand, Professor. I'm not
questioning their other rights.

~ But are you agreeing with me that the title
to the gas passes from me, as lessor, to you,
as lessee,
when you produce it?

~ A. The title to the gas as personal
property, okay? The substances that are
the subject of

the lessee's profit a prendre is normally considered to
pass at the wellhead.

~ Q. Thank you. Now, let's go to the gas
storage situation. In the gas storage situation, we're
not producing it so we can't pass the stick.

I can't pass

the stick as lessor to you as lessee at the wellhead, so
we have to have another moment in time to pass the stick.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 340]

~ Is that moment in time in accordance with the Board's phase 1 decision the moment of first injection?

~ A. Under the oil and gas lease, the moment of first injection would really not be relevant. The rights would be determined, as I understand it, under the lease and the unit operation agreement.

~ Q. Under the gas storage agreement, the requirement to purchase from the lessor the lessor's interest in the gas in situ, that requirement is triggered at the moment of first injection?

~ A. Yes, for the purpose of the storage rights--

~ Q. All right.

~ A. --granted under the storage lease.

~ Q. Okay.

~ A. Those rights are triggered at that point.

~ Q. That's when I'm passing the stick of title or ownership or whatever nomenclature you want to do

as lessor to you as lessee?

~ A. No. The lessee is merely realizing upon the lessee's rights. The sticks are not being passed at that point. The lessee retains the right to produce which

is the subject of the profit a prendre interest under the lease.

~ Q. Prior to the moment of injection, the lessee has a distinct - not in the sense that the gas is

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 341]

in situ in the ground - interest in that gas. You and I

may debate for the next week about what the nature of that interest is, but the lessor has at that moment in time before injection and intermingling a distinct interest in

that gas; is that not correct?

~ A. What the lessor has at that moment is an expectation that the lessor may be paid royalty when that gas is extracted.

~ Q. I understand that --

~ A. That's what the royalty represents.

~ Q. I understand that's your perspective.

But what happened in Robbins & Woolf is that they got a lot more than that, didn't they? They got to have it all back.

~ MR. McCANN: Again, we're engaging in legal argument. I'm not sure this is appropriate, panel.

~ MR. WAQUE: Q. Professor Lucas, be patient with me. Let's not debate what the nature of that interest is. Let's just try to establish some common ground if we can when the interest ends or it's passed or

is terminated so that the Board understands your perspective, all right?

~ PROF. LUCAS: A. Okay.

~ Q. Okay. There is an interest. You and I disagree about the extent of the interest or the nature of the interest that the lessor has.

~ At the moment that this agreement requires an offer to be made, will you agree with me that that

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 342]

186

interest ends and what the lessor has is a right to make a claim for compensation?

~ A. The lessor's rights, as I understand it, under the lease and the unit operation agreement continue.

The lease has not failed at that point as the lease failed in the Woolf case. The problem, as I understand it, in

the Woolf case is that there was no production. If there

had been, if there had been a unit operation agreement similar to the one in this situation that established deemed production, namely payment under the unit

operation

agreement as something that could continue the lease, and
if that payment had been made on a
continuous and regular
basis, the lease would not have failed in the
WoOLF case.

~ THE PRESIDING MEMBER: Are we going in
circles?

~ MR. McCANN: I think we've established that
there is a serious difference of opinion
about the nature

of the rights in certain molecules in
the ground and what

happens when they're taken out the ground. I just don't
know how much further we're going to get by continuing
this line of questioning. That there's agreement is clear
and that there will be an opportunity for
counsel for both

the applicants and the respondents to state their views is
equally clear.

~ MR. SULMAN: By the way, Mr. Chairman, as
respondent, a different role than Board Staff who appear
to get evidence on the record, a clear record,
I have no
objection to Mr. Waque cross-examining this witness as

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 343]

187

he's doing. That's why the witness is here, because he's
the expert in that area, so you haven't heard
me object.

In fact, I would have liked to have
asked these questions,
but of course someone else objected.

~ MR. WAQUE: Q. Ms. Stuart, I want to
understand your evidence about ownership.

~ THE PRESIDING MEMBER: Mr. Waque, I'm just
looking at the time.

~ Can you help us as to what would be an
opportune time for you to break?

~ MR. WAQUE: Well, this would be as good a
time as any I suppose. I'm moving to another witness.

~ THE PRESIDING MEMBER: To another witness,
sorry?

~ MR. WAQUE: I'm moving to another member of
the panel, I'm sorry.

~ THE PRESIDING MEMBER: You are, okay. Let's
break then for today.

~ MR. McCANN: Could we get some estimate of
how much more time? I realize that's difficult
to do, but

how much more time your cross-examination is likely to
take? I'm wondering whether we're going to
reach argument
tomorrow, for example.

~ MR. WAQUE: We'll definitely reach argument
tomorrow.

~ MR. McCANN: We were going to have some
discussion of --

~ THE PRESIDING MEMBER: I'm sorry, which

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 344]

188

argument? To discuss argument, or...?

~ MR. WAQUE: To argue the case.

~ MR. McCANN: Argument of the case.

~ MR. SULMAN: Well, there's a difference of
opinion on that.

~ MR. McCANN: There's a difference of opinion
on that. I thought we were going to have
some -- after we

had concluded the evidentiary portion today, I thought we
were going to have some brief discussion of argument.

Maybe it's not opportune at this moment since we're still
in the thick of things, but

~ MR. SULMAN: I would suggest that we do that
first thing in the morning as we open up
and get that out

of the way and that way there's a good flow for Mr. Waque
in his cross-examination.

~ MR. McCANN: Perhaps counsel could remain
for a few minutes and we can have at least a brief
discussion of it among ourselves so we can present
something to the Board or at least some options to the
Board tomorrow morning if that's possible.

~ THE PRESIDING MEMBER: Sorry, Mr. McCann, I
missed your last comment.

~ MR. McCANN: Well, I'm really just
addressing myself to counsel. Perhaps after the
session

is completed today, counsel could meet and we could
briefly discuss what we're going to talk about tomorrow

morning to try and save time when we come before you
tomorrow morning.

[Carlson, Stuart, Lowe, Lucas, Wilton cr ex (Waque) Page: 345]

189

~ THE PRESIDING MEMBER: That would be
advisable because to the extent that there
is a conclusion
that some people may want to argue tomorrow
orally, then

at least they can use the evening to that effect.

~ MR. McCANN: Exactly.

~ THE PRESIDING MEMBER: Any other matters?

~ MR. McCANN: I don't have any further
matters, Mr. Chairman.

~ THE PRESIDING MEMBER: Well, then, we'll
adjourn for today and we'll be here tomorrow morning at
nine o'clock.

---Whereupon, the proceedings were adjourned at 4:16 p.m.,
to be reconvened on Thursday, the 20th day
of March,
1997 at 9:00 a.m.

190

[Page: 346]

I N D E X o f P R O C E E D I N G S

Page No.

Preliminary matters 159-160

ROBERT COCHRANE; Sworn. 160

Direct Examination by Mr. Waque 160

Cross-Examination by Mr. Sulman 172

Cross-Examination by Mr. McCann 187

Examination by Ms. Drozd 205

Examination by the Presiding Member 207

Re-examination by Mr. Waque 211

JOHN CARLSON,

NORA STUART,

DAVID ROBERT LOWE,

ALISTAIR LUCAS,

BEVERLY HOWARD WILTON; Sworn. 215

Direct Examination by Mr. Sulman 216

LUNCHEON [1:34/2:42 p.m.] 293

Cross-Examination by Mr. Waque 305

191

[Page: 347]

L I S T o f E X H I B I T S

No. Description Page No.

9.8	Letter to Leo James Johnston from Bradley French.	304
7.4	Companion document, Kinnegan, to the gas storage agreements.	315
7.5	Companion document, Sexton, to the gas storage agreements.	315
7.6	Gas Storage Lease Agreement.	322
JB/MC/PG	[(c) Copyright 1985].	

192

[Page: 348]

E R R A T A

and

C H A N G E S

~ to Tuesday, March 18, Volume 1

Page No. Line No. Discrepancy [s/r

= should read]

139 2 Consumers Gas Limited

~ s/r Union Gas Limited