EB-2019-0166
Lagasco Inc.
Responses to Interrogatories from
Ontario Energy Board Staff

Reference: Pre-filed evidence of Jane E. Lowrie, Tab A

Interrogatory 1a:

Please provide a map(s) that clearly shows the location of the Pipelines relative to readily identifiable landmarks such as towns, roads, shorelines, rivers, railway lines, municipal boundaries, etc., and a north arrow. Please clearly label the beginning and end points of the Main Pipeline.

Interrogatory 1a Response:

All of the Pipelines in the maps provided in Exhibit A of the Affidavit of Jane E. Lowrie sworn May 25, 2020 (the "Lowrie Affidavit") are located in Lake Erie (they are offshore pipelines). Please see attached map titled "Lagasco_IR_OEB_Q1(A)_Maps_20200810". The red square on this map depicts the area in question.

Interrogatory 1b:

Either on the same map(s) as in part a) or on a separate map(s), please clearly identify all portions of the Pipelines that occupy municipal road allowance / right of way.

Interrogatory 1b Response:

The Pipelines in Exhibit A to the Lowrie Affidavit are all offshore Pipelines. As such, they do not occupy any municipal road allowances/rights of way.

Interrogatory 1c:

Please explain the difference between the pipelines represented by solid lines and those represented by dashed lines.

Interrogatory 1c Response:

Solid lines represent active pipelines. The dashed lines represent abandoned pipelines. The abandoned pipelines are still in place but have been abandoned according to the abandonment protocol approved by the Department of Fisheries and Oceans.

Interrogatory:	July 29, 2020
Response:	August 10, 2020
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Reference: Assessment Act
OEB's Decision and Order, Tribute Resources, EB-2015-0206
Pre-filed evidence of Jane E. Lowrie, page 6

Interrogatory 2a:

Given that one option for pipeline type explicitly includes "gathering pipe lines", please explain why Lagasco believes that the general term "pipe line" does not include gathering pipelines?

Interrogatory 2a Response:

The paramount definition of "pipe line" is the definition in Section 25(1) of the *Assessment Act* (the "Act"). Only if a "pipe line" meets this definition is it eligible for taxation under Part VIII of Ontario Regulation 292/98 (the "Regulation").

Section 25(1) defines "pipe line" without any reference to "gathering":

"pipe line" means a pipe line for the transportation or transmission of gas that is designated by the owner as a transmission pipe line and a pipe line for the transportation or transmission of oil, and includes,"…

The Regulation cannot expand the scope of its enabling statute. Based on the definition above, a gas "pipe line" must satisfy both of the following conditions:

1) it is "for the *transportation or transmission* of gas" and
2) it "is designated by the owner as a *transmission* pipe line"

A "transportation" line is not one whose purpose is gathering oil or gas. Moreover, the second condition makes clear that the tax classification is intended only apply to gas **transmission** pipelines.

Interrogatory 2b:

Does Lagasco share Tribute Resource's view that gathering pipelines owned and used by a natural gas producer should be exempt from assessment and taxation under the Assessment Act? If so, and given that other types of pipelines are municipally taxed, please explain why Lagasco believes that gathering pipelines should be exempt from municipal taxation.

Interrogatory 2b Response:

Yes, Lagasco agrees that *gas* gathering pipelines should be exempt from assessment and taxation under the Act.

There is a fundamental difference between gas gathering pipelines and gas transmission pipelines, which makes it irrational for them to be taxed in the same manner. Natural gas resources are harvested through small gas gathering lines that are life-limited, carry declining volumes as the natural resource is exhausted and become redundant when the underlying resource has been depleted. This is distinct from permanent ongoing higher pressure gas transmission/transportation pipelines (such as those owned by Enbridge), which are used indefinitely and carry consistent volumes. The fixed-rate per foot taxation scheme under the Regulations rationally fits the transmission type of pipeline, but not the life-limited gathering pipeline. The concept of "depletion", the natural decline in oil and gas reserves that occurs when these reserves are extracted or harvested, is completely ignored in the taxation system, leading to increasing taxation burdens as production declines at a fairly steady rate, year over year.

The CSA standards organization has responsibility for microscopic assessment and interpretation of all pipelines. As such, the CSA, which has standards applicable across Canada, is clear that a gas gathering line must be differentiated from a transmission line, a distribution line or a service line.

Under the current Act and Tables, it is Lagasco's view that these *gas* gathering lines should be exempt from municipal taxation.

Interrogatory 2c:

In Lagasco's view, what new facts or new information has become available since the Tribute Resources case that could cause the OEB to change its view that gathering pipelines used in natural gas production are gas "pipe lines" within the meaning of section 25(1) of the Assessment Act? Please explain.

Interrogatory 2c Response:

Lagasco believes that the OEB erred in finding, essentially that all pipelines are used for the transportation of gas in the ordinary meaning of that word because "pipelines are used to move or transport gas from one location to another.[1]" The OEB also found that MPAC had provided "sufficient evidence for the OEB to determine that the Tribute Pipelines were designated by the owner as transmission pipelines" when in fact, MPAC had provided *no* evidence of the election for designation

[1] OEB Decision and Order dated May 5, 2016 to Tribute Resources Inc. EB-2015-0206 page 6, paragraph 2

had been made by Tribute's predecessor. Furthermore, the designation is to be provided *annually* as outlined in Section 25(2) of the Act which reads:

(2) On or before March I of every year or such other date as the Minister may prescribe, the pipe line company shall notify the assessment corporation of the age, length and diameter of all of its transmission pipe lines located on January I of that year in each municipality and in non-municipal territory. 2004, c. 31, Sched. 3, s. 8; 2006, c. 33, Sched A, s. 16 (1).

In this proceeding the Board has the opportunity to re-evaluate its position on the basis of fresh evidence (including an expert opinion, not available in the prior proceeding) and with the additional context of recent market turmoil. The evidence in this proceeding more clearly demonstrates the importance of distinguishing between transmission and gathering pipelines, and the absurd consequences that flow from failing to make this distinction.

The nature and characteristics of these different types of pipelines can not be blurred to make a finding that they all "transport or transmit" gas.

In the years since the Tribute proceeding, there have been significant industry challenges and commodity market fluctuations, which illustrate the dangerous consequences of taxing gathering pipelines in the same manner as transmission pipelines, including:

- Alberta's immediate interim tax reduction across the Board (July 30, 2020 - CBC article titled "'It's going to hurt': Tax break for oil and gas firms would drain rural budgets, communities warn[2]"). This article is attached titled "Lagasco_IR_OEB_Q2(C)_EX1_CBC_News_It's_Going_To_Hurt_20200810". In Alberta, in 2019, the province openly recognized the need to focus on the sustainability of the provincial gas industry, and has in particular, zeroed in on the deleterious effects of the municipal tax system as it currently applies to the industry. A 35% immediate decrease in municipal taxes was imposed to save the industry from a multitude of bankruptcies due to dramatically lower natural gas prices around the world and especially in Alberta and North America (July 3, 2019 – Global News articled titled "Alberta natural gas producers getting tax relief[3]"). This article is attached titled "Lagasco_IR_OEB_Q2(C)_EX2_Global_News_Alberta_Natural_Gas_Producers_Getting_Tax_Relief_20200810".

- Ontario's current municipal taxation system is unsustainable for the oil and gas industry. Lower prices in Ontario have benefited consumers but have had the effect of making certain gas production fields, which are all taxed at annually escalating MPAC rates, unsustainable. The most recent example in the Municipality of Bayham, which resulted, in part, in the ongoing reorganization of Clearbeach Resources Inc. under the *Bankruptcy and Insolvency Act*. This is one of many pending examples of an unsustainable taxation system that fails to recognize (a) a depleting resource with lower revenues as the wells age, and (b) fluctuations in the global commodity prices, which when lower as they are in the current climate, make it impossible to

[2] https://www.cbc.ca/news/canada/edmonton/oil-and-gas-taxes-municipalities-tax-relief-industry-1.5667230
[3] https://globalnews.ca/news/5456362/alberta-natural-gas-producers-tax-relief/

operate the oil and gas fields profitably if municipal taxes are not flexible to recognize the exigencies of this resource sector.

Lagasco believes that the Board is the only expert economic tribunal suited to assess these industry realities; the Board bears responsibility to the industry is to ensure fairness and responsibility in exercising its regulatory jurisdiction.

Reference: Pre-filed evidence of Jane E. Lowrie, pages 1-5

Interrogatory 3a:

It is clear that some of the assets acquired by Lagasco from Dundee include both onshore and offshore pipelines, and that the Pipelines are a subset of the assets acquired from Dundee. However, it is unclear whether the Pipelines that are the subject of the current application are all onshore pipelines or whether they include some offshore pipelines. Please clarify.

Interrogatory 3a Response:

The Pipelines in Haldimand County that are specifically subject to the current application are all offshore pipelines, located on the bed of Lake Erie. However, Lagasco's position is that the onshore/offshore distinction is not material to whether a pipeline is a "transmission" pipeline (as opposed to a gathering pipeline), and that any determination made with respect to the offshore pipelines in Haldimand County should also apply to onshore gathering pipelines.

Interrogatory 3b

Please confirm that the Pipelines do not include any plastic pipelines. If not, please explain.

Interrogatory 3b Response:

Confirmed. All of the offshore Pipelines on the bed of Lake Erie are made of steel.

Interrogatory 3c

Notwithstanding the answers to parts a) and b) above, please confirm whether the Pipelines are currently being assessed as offshore, plastic gathering/distribution, other, or a combination. If they are being assessed as a combination of pipeline types, please provide the approximate lengths of the pipelines that are being assessed as offshore, plastic gathering/distribution, and other.

Interrogatory 3c Response:

They are being assessed as “offshore”. Please refer to Exhibit A of the Affidavit of Ryan Ford of Municipal Property Assessment Corporation sworn on July 29, 2020.

Interrogatory 3d

As a result of its purchase of the Pipelines in the context of an application commenced by Dundee under the Companies' Creditors Arrangement Act, was Lagasco able to purchase the Pipelines for less than their book value? If so, please provide the estimated book value of the Pipelines at the time they were purchased.

Interrogatory 3d Response:

At December 31, 2017 the Pipeline Infrastructure value recorded in Note 8 – Oil and Gas Properties in the Dundee Energy Limited financial statements was recorded at nil as they were transferred to discontinued operations and impaired.

Interrogatory 3e:

Please confirm that the collective values stated by Lagasco are in fact for all of the assets acquired from Dundee and not just the Pipelines. If not, please explain.

Interrogatory 3e Response:

The collective values stated by Lagasco are the current values ascribed by MPAC to the three Haldimand county pipeline roll numbers *only*. To be clear, these values related to the sum of the values for rolls: 2810021003242000000, 2810157002260000000 and 2810332001503000000.

Roll Number	Municipality	Description	2016 Value	2017 value	2018 value	2019 value	2020 Value
2810021003242000000	Haldimand	Pipeline	$4,945,000	$5,074,500	$5,204,000	$5,333,500	$5,463,000
2810157002260000000	Haldimand	Pipeline	$4,512,000	$4,645,250	$4,778,500	$4,911,750	$5,045,000
2810332001503000000	Haldimand	Pipeline	$3,568,000	$3,677,000	$3,786,000	$3,895,000	$4,004,000
TOTAL			**$13,025,000**	**$13,396,750**	**$13,768,500**	**$14,140,250**	**$14,512,000**

The MPAC valuations for the 26 total pipeline rolls owned by Lagasco (former Dundee) were $43,111,000 in 2016 increasing to $46,829,000 in 2020. The table below summarizes these valuations.

Roll Number	Municipality	Description	2016 Value	2017 value	2018 value	2019 value	2020 Value
2810021003242000000	Haldimand	Pipeline	$4,945,000	$5,074,500	$5,204,000	$5,333,500	$5,463,000
2810157002260000000	Haldimand	Pipeline	$4,512,000	$4,645,250	$4,778,500	$4,911,750	$5,045,000
2810332001503000000	Haldimand	Pipeline	$3,568,000	$3,677,000	$3,786,000	$3,895,000	$4,004,000
3408000070007010000	Malahide	Pipeline	$5,656,000	$5,763,000	$5,870,000	$5,977,000	$6,084,000
3310543040151000000	Norfolk	Pipeline	$5,271,000	$5,327,500	$5,384,000	$5,440,500	$5,497,000
3650210004402170000	Chatham	Pipeline	$2,819,000	$2,907,000	$2,995,000	$3,083,000	$3,171,000
3401000009009010000	Bayham	Pipeline	$2,616,000	$2,649,000	$2,682,000	$2,715,000	$2,748,000
3706920000051000000	Leamington	Pipeline	$2,216,000	$2,269,750	$2,323,500	$2,377,250	$2,431,000
3650010003233020000	Chatham	Pipeline	$1,783,000	$1,835,250	$1,887,500	$1,939,750	$1,992,000
3650010001902020000	Chatham	Pipeline	$1,624,000	$1,667,500	$1,711,000	$1,754,500	$1,798,000
3751630000086000000	Lakeshore	Pipeline	$1,584,000	$1,605,750	$1,627,500	$1,649,250	$1,671,000
3650260003208000000	Chatham	Pipeline	$902,000	$920,500	$939,000	$957,500	$976,000
3418000011009010000	Central Elgin	Pipeline	$881,000	$893,000	$905,000	$917,000	$929,000
3434000050500000000	West Elgin	Pipeline	$850,000	$869,250	$888,500	$907,750	$927,000
3650110012361000000	Chatham	Pipeline	$648,000	$660,000	$672,000	$684,000	$696,000
3650140010955000000	Chatham	Pipeline	$456,000	$463,750	$471,500	$479,250	$487,000
2711040006198000000	Port Colborne	Pipeline	$341,000	$361,000	$381,000	$401,000	$421,000
3650210004402160000	Chatham	Pipeline	$547,000	$381,000	$381,000	$381,000	$381,000
3650210004402990000	Chatham	Pipeline	$346,000	$352,000	$358,000	$364,000	$370,000
3650060003792000000	Chatham	Pipeline	$334,000	$342,000	$350,000	$358,000	366,000
3429000002500000000	Dutton	Pipeline	$260,000	$266,000	$272,000	$278,000	$284,000
3424000010007010000	Southwold	Pipeline	$131,000	$136,500	$142,000	$147,500	$153,000
3310493110538000000	Norfolk	Pipeline	$85,000	$89,000	$94,000	$98,500	$103,000
2714000006245000000	Weinfleet	Pipeline	$71,000	$75,000	$79,000	$83,000	$87,000
3650010003233000000	Chatham	Pipeline	$618,000	$618,000	$618,000	$618,000	$618,000
3711670000051000000	Kingsville	Pipeline	$47,000	$118,000	$127,000	$127,000	$127,000
TOTAL			**$43,111,000**	**$43,966,500**	**$44,927,000**	**$45,878,000**	**$46,829,000**

When Lagasco Inc. acquired the Dundee assets in November 2018, the total purchase price paid for all of the assets was approximately $30 million. The vast majority of the value purchased by Lagasco was ascribed to the oil and natural gas reserves (in the ground to be extracted over time) as well as the equipment purchased.

Only $900,000 of the purchase price was allocated to the pipelines, which allocation was also agreed to by Dundee, FTI Consulting Inc. (the court appointed Monitor) and the Court. The Dundee to Lagasco purchase price allocation is as follows:

DUNDEE
PURCHASE PRICE ALLOCATION

Land	$	400,000
Vehicles	$	200,000
Equipment - rigs on shore and off shore	$	2,000,000
Equipment on wells	$	7,800,000
Seismic	$	8,000,000
PNG rights	$	10,700,010
Pipelines	$	900,000
	$	30,000,010

*This third party agreed pipeline value allocation is **less than 2%** of what MPAC has in terms of a valuation for these same pipelines.*

Interrogatory: July 29, 2020
Response: August 10, 2020
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Interrogatory 3f:

If the collective values stated by Lagasco are in fact for all of the assets acquired from Dundee and not just the Pipelines, please comment on whether it is possible that the increase in the collective values is driven by assets other than the Pipelines.

Interrogatory 3f Response:

It is not for the collective assets, please see 3(e).

Interrogatory 3g:

Please explain how the alleged misclassification of the Pipelines leads to their assessed value increasing over time. In the response, please identify and explain any applicable assumptions, accounting practices, calculations, figures or tables

Interrogatory 3g Response:

Please see table in 3(e). The maximum depreciation factor from the Tables is 80%. Depletion on many of these wells is 95% + since they were drilled. The depreciation applied does not and is not able to keep up with the valuation increases from the Tables year over year, as is evident by the chart above.

Interrogatory 3h

Please explain in detail what happened in respect of the stays by the ARB after the OEB issued its decision in Tribute Resources case.

Interrogatory 3h Response:

The Tribute Resources taxes owing were stayed waiting for the OEB hearing (EB-2015-0206) and then became due and payable as soon as this hearing was lost and the OEB considered these gas gathering lines “pipe lines”. They remain due and payable and Tribute’s successor, Clearbeach Resources Inc. has not had the ability to pay these taxes, which has resulted in the Municipality of Bayham disallowing the use of their municipal road allowances and will ultimately mean that the production that flows through these road allowances to the sales point will be shut in. This is one of the major contributing factors that led to Clearbeach filing a Notice of Intention in July 2020 under the *Bankruptcy and Insolvency Act.*

Reference: Pre-filed evidence of Robert Koller, pages 5-6

Interrogatory 4a:

Please confirm that the Deloitte Report was included in the pre-filed evidence in order to support Lagasco's assertion that the Pipelines are gathering lines and not transmission lines. If there were any other reasons for including the report, please identify and explain them.

Interrogatory 4a Response:

The Deloitte Report was included in the pre-filed evidence to more clearly explain and evidence the differences between transmission pipelines and gathering pipelines (and in particular, the economic differences). These differences are relevant because they motivate and justify different tax treatment for gathering and transmission pipelines, and support Lagasco's position that the Pipelines at issue are gathering pipelines. The Deloitte Report also provides valuable context for interpreting the Act and the Regulations rationally and purposively, with an appreciation of the practical consequences that the Board's decision will have on the industry.

Interrogatory 4b:

Please explain what relevance the various asset valuation methodologies have in respect of pipeline classification for the purposes of taxation, if any.

Interrogatory 4b Response:

As set forth in paragraph 3 of the Deloitte Report, "… we have been asked to prepare an Expert Report regarding the classification of Lagasco's natural gas pipelines, which includes differences between natural gas gathering pipelines and transmission pipelines from an economic perspective." The Deloitte Report then explains the purpose and, to some degree, the physical characteristics of the various types of pipelines, which include gathering and transmission pipelines. This is meant to help the reader understand that each of these two classifications of pipelines have different purposes.

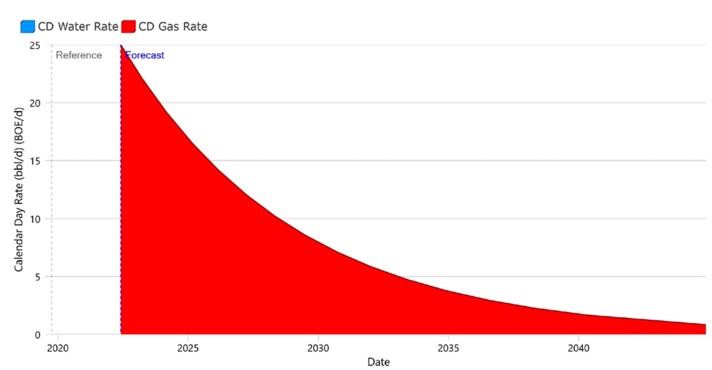
What is more important, though, is that the Deloitte Report then discusses the economics of these two classifications of pipelines and how their values are determined differently. The economics relate to the purposes of these different pipelines. Taxation regimes are meant to be fair and equitable. In short, the amount of property taxes to be levied should be commensurate with the value of the underlying assets. The greater the value, the greater the amount of taxes that should be levied and vice versa. In short, the economics and, hence, the value of gathering pipelines decreases over the life of the underlying natural gas reserves. The economics and, hence, the value of transmission pipelines do not decrease over their useful lives.

It is important to understand physically how oil and gas reserves work. When a natural gas well is drilled, there is only a certain amount of physical natural gas in that reservoir that is recoverable. The same is true with oil. Using a natural gas example, say that amount is 100 thousand cubic feet ("mcf"). Generally, the initial production out of a well is high, but then decreases each year until the reservoir is fully depleted. This is the decline curve. So, for the example, maybe production in the first year is 20 mcf, the year after 18 mcf, the year after 15 mcf, and so forth until the reservoir is depleted and annual production is nil. Due to this, the value of gathering pipelines is directly correlated to the underlying natural gas reserves that feed these pipelines. Simply due to depletion of the reservoir, the value of gathering pipelines and the associated natural gas reserves declines each year, all else held equal, until the value is nil when the reservoir is fully depleted. Hence, for valuation purposes, the discounted cash flow method is used and the projection period is limited to the life of the reservoir. There is no terminal value. Cash flows associated with the reservoir and gathering pipelines decrease each year until they are nil.

Like gathering pipelines, the economics, and resulting value, of transmission pipelines relates to their purpose. Transmission pipelines are fed by both existing reservoirs and future reservoirs to be developed. Therefore, these pipelines are not subject to depleting volumes unlike gathering pipelines that are confined to a single reservoir. Consequently, in general, transmission pipelines are expected to generate consistent cash flows (i.e., not declining) for many years in the future. Hence, the value of transmission pipelines does not deplete. As such, for valuation purposes, the discounted cash flow method is used and the projection period is not limited to the life of a certain reservoir.

A typical gas well decline curve is below. Generally, the decline is sharp in the first few years and then levels out. From the Interrogatories for the Municipalities, Interrogatory 10 it can be seen that Lagasco's actual oil declines over the last five years have been 8% on average per year and gas has been 5% on average per year, making total average production declines 6% per year currently.

A typical decline curve for both oil and gas wells is as follows:



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Reference: Ontario Petroleum Institute (OPI) intervention request letter

Interrogatory 5:

Please briefly describe the 2020 Ontario Upstream Oil and Natural Gas Sustainability Plan. In the response, please note if Lagasco is involved in this initiative, who else is involved, and the initiative's key activities and associated timelines.

Interrogatory 5 Response:

Lagasco is a member of OPI. The 2020 Ontario Upstream Oil and Natural Gas Sustainability Plan (the "Plan") is an initiative undertaken and written by the (former) Executive Director and supported by the Board of Directors of OPI. One person from Lagasco was involved in reviewing the plan prior to its submission to the Minister of Natural Resources and Forestry.

The Plan's aim was to inform government as to the status, challenges and future vision of the industry as well as stimulate drilling starts and increases to current production. It included historical information to set a background as well as requested the collaboration of different government agencies to meet the industry goals.

The OPI also submitted a Crisis and Action Memorandum (the "Memo") to both the Ministry of Natural Resources and Forestry and the Ministry of Finance in May 2020. This Memo, which Lagasco reviewed and supported, outlined five main areas that require regulatory adjustment to allow for the Ontario oil and gas industry to remain sustainable and to enable them to responsibly continue to meet their environmental obligations with respect to well abandonment. The first and most important of these five areas was Municipal Tax Assessments. A copy of the OPI's submission to government is attached as "Lagasco_IR_OEB_Q5_EX1_Ontario_Oil_and_Gas_Industry_Survival_20200810" and "Lagasco_IR_OEB_Q5_EX2_Ontario_Oil_and_Gas_Industry_Survival_Appendix_20200810".