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Ontario Court of Appeal confirms the exclusive jurisdiction of the Ontario Energy Board in relation to natural gas storage rights

By Nigel Bankes

Cases Considered:

Snopko v Union Gas Ltd, 2010 ONCA 248

Gas storage schemes offer the opportunity to take maximum advantage of existing pipeline infrastructure. Storage also helps provide security of supply and extra deliverability at times of peak demand. While some storage remains regulated as a public utility the general trend is to deregulate storage where there is adequate competition. In some provinces pore space for natural gas storage is principally publicly owned (and then acquired by private operators by way of lease) as in British Columbia and Alberta and in other provinces as in Ontario the pore space is largely privately owned as in the facts of this case.

In either case there may be a need to deal with holdout problems and there will always be the question of how to compensate the private pore space owner for the use of the storage rights. That is what was at issue in this case; and we can expect this issue to become more contentious as gas storage increases in value.

The facts

Snopko and others entered into petroleum and natural gas leases with Ram Petroleums in the 1970s and gas storage leases (GSLs) in 1987. Ram assigned the GSLs to Union in 1989 with Snopko's consent. In 1992 the area covered by these leases was included within a designated gas storage area. Compensation matters came before the Ontario Energy Board (OEB or Board) in 2000 pursuant to the Board's jurisdiction under the *Ontario Energy Board Act*, SO 1998, c.15 (the Act). At that time the Board accepted Union's argument that the Board had no jurisdiction to make a compensation order under the Act in relation to Snopko and others since compensation was addressed by the terms of the GSLs. Union did however agree to offer Snopko the same compensation terms as those fixed by the Board for other owners. Union did so and as a result Snopko and others entered into multi-year agreements with Union.

Snopko and others commenced this action against Ram and Union in 2008 alleging breach of contract, negligence, unjust enrichment, nuisance and unconscionability. Union moved for

summary judgement on the basis that the OEB had exclusive jurisdiction over all of these matters. The motions judge granted the application.

Decision on appeal

The Ontario Court of Appeal dismissed the appeal and granted summary judgement.

Snopko's action was in substance an application for compensation for use of the lands for a gas storage project (at paras 24 – 26). The Act affords the Board a broad jurisdiction to regulate natural gas storage and to require the storage operator to pay just and equitable compensation (ss.36.1 – 38). It also provides that no person shall bring an action to determine compensation (s.38(3)). The Board has jurisdiction to determine the validity of other compensation arrangements as part of assessing the appropriate compensation to be paid to a landowner (at para. 22). Given these provisions it was evident that the Board's jurisdiction over compensation matters was exclusive and could not be usurped by the courts (at paras 29 and 31). The issue was to be characterized by the substance of the issued raised by the application (compensation) and not by the form of the pleadings or the cause of action (at para. 29).

Ram took no part in the application and the claims against Ram remain outstanding.

Commentary

I have two comments on this decision. The first comment relates to the methods for compensating pore space owners for the use of their storage rights. The second comment deals with the relationship between energy regulators and the superior courts.

How should we compensate the private owners of pore space when an operator uses that pore space for natural gas storage? One easy answer is to let the market decide. But how should we deal with holdouts? Many jurisdictions (but not Alberta) allow the regulator (the OEB in the case of Ontario) to fix reasonable compensation and that was what was at issue here. It should be noted however that the OEB will decline jurisdiction (as it did here because of the terms of the GSLs) where there is an agreement between the parties fixing compensation even if such compensation rates are significantly lower than those that the Board would fix. Typically, the Board fixes a fixed rate per acre. This fee is not tied to the market value of the storage and does not vary with volumes stored in that part of the reservoir or the number of times that gas is cycled through that reservoir. A fixed per acre fee is also the standard practice in Alberta and British Columbia for granting storage rights in publicly owned pore space: for discussion of the practice in different provinces see Bankes and Gaunce, "Natural Gas Storage Regimes in Canada: a survey", (ISEEE: University of Calgary, 2009).

But perhaps it is time that we reexamined this approach as the economic value of storage space rights grows since there is an economic rent to be captured on behalf of the public owners of the resource. And on that point there is an intriguing note in this case (at para. 3) to the effect that the original GSLs between Snopko and others and Ram provided the lessor "with a 10% profit share

of all Ram's earnings from storage operations unless the leases were assigned to a third party." This is an intriguing provision and one can well imagine why Snopko and others might want to rely upon this provision in an unregulated storage market rather than the acre based fee which the parties seem to have agreed upon subsequently. Was this later agreement procured, as the plaintiffs alleged by some unconscionable behaviour which might allow the plaintiffs to rely instead on that earlier agreement? This takes me to the second comment.

As noted above my second comment deals with the relationship between energy regulators and the superior courts. Over the last number of years we have seen quite a number of matters brought before the ERCB in Alberta which have required the ERCB to determine issues of private law and issues of both property and contract. The matters include cases dealing with CBM (coalbed methane) ownership (ERCB Decision 2007-024) and the validity of leases (ERCB Decision 2008-47; see my ABlawg post The ERCB asserts its jurisdiction to determine the validity of an oil and gas lease). The statutory trigger for these cases is often the right of a party to hold and maintain a well licence. The ERCB has not shrunk from this task and in my opinion correctly so; it must decide these issues as part of exercising its statutory responsibilities. At the same time it seems to be broadly acknowledged that the parties may also be able to frame their action in private law and proceed in the ordinary courts. Indeed this is what Encana is now doing in its CBM litigation: see, for example: *EnCana Corporation v. Devon Canada Corporation*, 2009 ABQB 429.

What appears to be unusual about the present case i.e. the *Snopko* decision is that it concludes that some matters that might appear to be matters of private law are so closely connected with the core elements of an energy regulator's jurisdiction (here the jurisdiction to deal with holdouts when assembling a gas storage project and the power to set compensation accordingly) that the ordinary courts must decline jurisdiction even though the issues are presented by the plaintiff as private law matters e.g. invalidity of a lease and even unconscionability. This clearly goes beyond confirming the power of the regulator to decide points of law as a necessary element in exercising its jurisdiction; instead the decision accords to the regulator an exclusive original jurisdiction over a broad range of matters. One wonders if this is not a step too far? Is the OEB really the best place to decide whether an agreement is tainted by unconscionability? Even if it has the ability to do so as a necessary part of deciding other issues that may be put to the Board does it follow from this that a plaintiff cannot submit these issues to a s.96 Court?