April 9, 2020

Bill 12: A Small Step Forward in Managing Orphan Liabilities in Alberta

By: Nigel Bankes

Matter Commented On: Bill 12, Liabilities Management Statutes Amendment Act, 2020

Bill 12 addresses some issues related to the province's orphan fund and the responsibilities of the Orphan Well Association (OWA). While my overall conclusion is that the Bill is to be welcomed, the procedure under which the Bill was adopted was unfortunate. Furthermore, while the Bill does plug some gaps and extends the authority of the OWA and the orphan fund in helpful ways, the Bill is most notable for what it doesn't address. In particular, it does not address the systemic drivers of the growing orphan liability problem in the province.

Others have documented the fact that Alberta has a massive liability issue associated with orphan wells, well sites and other facilities. See, for example, Benjamin Dachis, Blake Shaffer and Vincent Thivierge, All's Well that Ends Well: Addressing End-of-Life Liabilities for Oil and Gas Wells, Green Regs and Ham, and Martin Olszynski, Alberta's Underfunded Environmental Liabilities Problem: Inactive Wells and Oil Sands Tailings Or: The Value of Alberta: The Other Side of the Ledger (extending the analysis to cover liability issues associated with oilsands tailings). "Orphan" in this context refers to a well or facility for which the licensed owner and/or other working interest participants (WIP) are insolvent. The Alberta Energy Regulator (AER) has the authority to designate a well or other facility as an orphan under s 70 of the *Oil and Gas Conservation Act*, RSA 2000, c O-6 (*OGCA*). Once designated, these wells or other facilities become the responsibility of the Orphan Well Association (OWA). The OWA is a collaborative effort of industry, government and the AER to tackle the orphan problem. It was initially developed on the premise that the industry as a whole (or the solvent part of the industry) would assume responsibility for orphans through means of the orphan well levy described in Part 11 of the *OGCA*. The orphan levy typically raised about $40 million per year. The OWA receives its authority to engage in its activities related to abandonment and reclamation by delegation under s 77 of the *OGCA* and the *Orphan Fund Delegated Administration Regulation*, Alta Reg 45/2001.

In more recent years, the OWA has received significant additional monies from the province in the form of loans to enhance the OWA's capacity but also to create oil patch jobs. The OWA also received some federal money in the last budget. As of March 2020, the OWA lists in its orphan inventory: 2789 wells requiring abandonment, 233 orphan facilities requiring decommissioning, 4113 pipeline segments requiring abandonment and 3331 orphan sites requiring reclamation. These are very large numbers and we can anticipate that current low oil prices will trigger further receivership and bankruptcies and thus an increasing orphan inventory.

In this context, the decision of the Supreme Court of Canada in the *Redwater* case (*Orphan Well Association v Grant Thornton Ltd.*, 2019 SCC 5 (CanLII), [2019] 1 SCR 150 provided some

relief to the province and the AER insofar as it decided that generally AER abandonment orders and other AER orders did not amount to claims provable in bankruptcy. The effect of this decision is that the AER need not stand in line with other unsecured creditors and that receivers and trustees in bankruptcy will be subject to AER abandonment orders. Had that decision gone the other way, receivers acting on behalf of secured creditors would have been able to push many more wells and facilities into the orphan category by stripping the producing assets out of the bankrupt's estate leaving the non-producing assets for the OWA.

Various solutions to the growing orphan problem referenced above have been identified including ensuring adequate financial security arrangements for the full cost of abandonment, reclamation and remediation of well sites and facilities (rather than just monitoring a licensee's ratio of reserves to liabilities, the so-called LMR ratio), as well as rules setting limits for how long wells can be suspended (i.e. not producing) before they must be abandoned. In both cases, the means to address these issues already exist in the *OGCA*, and in particular within the AER's rule making powers. Thus, s 10(1) of the *OGCA* allows the AER to make rules with respect to many matters including:

> (b) requiring licensees and approval holders to provide to the Regulator deposits or other forms of security to guarantee the proper and safe suspension, abandonment and reclamation of wells and facilities and the carrying out of any other activities necessary to ensure the protection of the public and the environment, including rules respecting the amount and form of those deposits and security and how they may be used, retained, forfeited and returned;
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> …
>
> (q) respecting the suspension and abandonment of wells and facilities, including the circumstances under which a well or facility must be suspended or abandoned, the timing of such suspension or abandonment and the manner in which suspension and abandonment are to be carried out…

The problem then is that the AER has failed to fully take advantage of these rule-making powers. For example, s 1.1(2) of the *Oil and Gas Conservation Rules*, Alta Reg 151/1971 (OGCR) allows the AER to require security deposits in a variety of circumstances:

> (2) The [AER] may require a licensee to provide a security deposit
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> (a) before approving a transfer of a licence,
>
> (b) at any time the licensee fails a licensee liability rating assessment conducted by the [AER],
>
> (b.1) at any time the licensee fails a liability management rating assessment conducted by the [AER],

(c) at any time where the [AER] considers it appropriate to do so to offset the estimated costs of suspending, abandoning or reclaiming a well, facility, well site or facility site,

(d) at any time where the [AER] considers it appropriate to do so to offset the estimated costs of providing care and custody for a well, facility, well site or facility site, and

(e) at any time where the [AER] considers it appropriate to do so to offset the estimated costs of carrying out any other activities necessary to ensure the protection of the public and the environment.

But given the number of orphans for which the liabilities are not offset by the security on hand one can only conclude that the AER has not been aggressive enough in requiring the security "necessary to ensure the protection of the public and the environment." Similarly, s 3.012 of the OGCR dealing with abandonment does not include any provision requiring abandonment of a well after a lengthy period of inactivity. See also AER Directive 013: Suspension Requirements for Wells (December 2018) and the AER's annual report on its Inactive Well Compliance Program (January 2020) referencing nearly 90,000 inactive wells. And see also most recently, Alberta Energy, Information Letter 2020-13, "Postponing Regulatory Reporting for Industry", April 8, 2020 advising as to the suspension of certain requirement under Directive 013 including relieving non-compliant inactive wells from the deadlines in the Directive (all pursuant to Ministerial Order 219/20, April 6, 2020).

It is against this background that the government introduced and rammed through Bill 12.

Bill 12 was introduced and given first reading in the afternoon of March 31st, passed second reading in the afternoon of April 1 and passed the Committee of the Whole on April 2. It passed third reading the same day and received Royal Assent. It will come into force on proclamation as SA 2020, c 4. All proposed amendments were voted down. Perhaps such a high-handed approach could be justified if the Bill were part of a response to the COVID-19 emergency, but it is not. Perhaps such a high-handed approach could be justified if the Bill represented a comprehensive response to the orphan problem, but it is far from being that. Instead, the Bill principally seems to be a response to concerns that the OWA lacked sufficient authority to be able to take over producing assets and manage them in the interests of public safety and resource conservation. The Bill also seems to address concerns that the OWA lacked the authority to address remediation issues as well as abandonment and reclamation issues associated with orphans. These are important issues but they are not new issues – which begs the question why we didn't see this legislation in the fall of 2019?

Bill 12 has nothing whatsoever to say about the more systemic issues driving the growing number of orphans. Thus, the Bill says nothing about actually requiring the AER to set time limits for abandoning inactive wells or to be more pro-active in exercising its discretion with respect to requiring enhanced financial security measures.

In moving second reading of Bill 12 in the legislature, Minister Sonya Savage observed that the Bill was simply "one part of a new suite of policies to be announced in the near future which will touch every stage in the life cycle of a well, from exploration to postclosure, while at the same time ensuring industry is able to meet its obligations in a manageable way." (Hansard, April 1,

2020 at 320). However, she offered no indication as to the content of that suite of new policies. Given that this government has been in office for nearly one year and given that we received the *Redwater* decision in January 2019 this is disappointing.

Not for the first time, I find myself arguing for an approach in which the government (of whatever political stripe) provides a clear statement of the problem, policy options for dealing with the problem, facilitated discussion of those policy options, and then preparation of legislation, regulations and AER Directives based on the preferred solution. Instead what we get in this case is legislation first (with no accompanying explanation other than the Minister's one-page speech) addressing only a small part of the problem and the promise of policies to be announced in the future – likely as a *fait accompli*.

The balance of this post examines how Bill 12 addresses the issues associated with the enhanced operational authority of the OWA and the uses to which the Orphan Fund can be put.
Under the current version of the *OGCA* and the *Orphan Fund Delegated Administration Regulation*, Alta Reg 45/2001, the OWA only has delegated authority in relation to "suspension and abandonment operations in respect of orphan wells, facilities, facility sites and well sites". Furthermore, the OWA can only expend funds from the Orphan Fund for these purposes. This creates some challenges when a licensee effectively abdicates its responsibilities for assets and just walks away. This can be a huge problem if the assets include wells or other facilities that are producing or processing sour gas. In such a case, public safety has to be a paramount consideration. Such seems to have been the case with Lexin Resources. See in particular Heather Lilles, Upholding the Lexin Equipment Order – The AER Wins the Battle, But Most Likely Will Lose the War, commenting on *Alberta Energy Regulator v Lexin Resources Ltd*., 2017 ABQB 219 (CanLII); see also Lilles' LLM thesis "The Statutory Liabilities of Joint Operators and Non-Participating Parties" (2017, University of Calgary), available here.

Bill 12 addresses these concerns in a number of different steps.

First, the Bill establishes an additional duty for licensees and approval holders. This is the duty (new s 26.2 of the *OGCA*) to "provide reasonable care and measures to prevent impairment or damage in respect of a well, facility, well site or facility site." "Impairment or damage" are defined (a new definition in para 1(1)(aa.001) of the *OGCA*) as "impairment or damage that results in or could reasonably be expected to result in harm to the integrity of a well or facility or harm to the environment, human health or safety or property". These duties of care, and measures to prevent impairment/damage, are carried through into various other sections of the *OGCA* including obligations with respect to associated equipment located on the site (see amended s 32) and the right of entry onto land to fulfill these duties (see amended s 101).

Second, the Bill provides that where the AER concludes that the licensee or approval holder cannot fulfil the above obligations, the duty shall be fulfilled by the WIPs. Third, if the AER concludes that the WIPs are not performing the above obligations in "a manner satisfactory" to the AER then (new *OGCA* s 26.2(3)) the AER "may order the licensee, a working interest participant or a delegated authority under Part 11 to provide reasonable care and measures to prevent impairment or damage in respect of the well, facility, well site or facility site and may

impose any terms or conditions that the [AER] determines are necessary in the order." (emphasis added)

Fourth, the reference to "delegated authority" in the new s 26.2(3) just quoted is effectively a reference to the OWA and thus allows the AER to order the OWA to assume care and custody obligations for particular facilities. Bill 12 also amends various other provisions to make this effective. For example, ss 11 and 12 of the *OGCA* are amended to ensure that the OWA can carry on operations at wells or facilities even though it is not the licensee or approval holder.

One of the amendments to s 11 clarifies that when the OWA takes over management and control of a well it must not "undertake any production without the consent of the owner or holder of the mineral rights and the person who has the right to win, work and recover the minerals." I suspect that this provision may prove to be problematic because it is just too all embracing. Consider a situation involving freehold mineral rights in which the mineral rights are owned by eight different family members and where the working interests are held by a number of different companies. Do they all have to consent before the OWA can "undertake any production"? Why do the mineral owners have to consent to production at all? Mineral owners would not normally have any role in a decision as to whether or not to produce. This provision may well prove to create an effective roadblock to production operations.

Fifth, Bill 12 amends the *OGCA* throughout by replacing the words "wells and facilities" with the more comprehensive "wells, facilities, well sites and facility sites" thus clarifying that the obligations of a licensee or facility approval holder (or the OWA when standing in for such persons) extend to this broader area.

Sixth, the Bill makes it clear through an amendment to s 70 of the *OGCA* that monies in the orphan fund can be used to cover the costs of fulfilling the broader suite of obligations outlined above as well as some additional classes of costs, including costs associated with monitoring the behavior of orphan wells and facilities and the costs of a receiver. This latter category of costs is connected to a new section (s 106.1) which allows the AER, subject to the regulations (still to be drafted) to apply to the court for the appointment of a receiver etc. of the property of a licensee. It is not clear to me why this power does not extend to the property of an approval holder. While the *Lexin* case referenced above suggests that the AER may already have the authority to make such an application (presumably under s 13 of the *Judicature Act*, RSA 2000, c J-2) this combination of amendments serves to regularize that position but also to provide some assurance to the receiver that it can be paid, if necessary, out of the monies in the orphan fund thereby addressing the post-*Redwater* concern that receivers would be hard to find.

Seventh, the Bill includes an additional regulation-making authority with respect to the orphan fund that is framed in unusually broad terms. The current regulation-making power in Part XI of the *OGCA* (the Orphan Fund part) is drafted in conventional terms and provides (s 77(1)), that "The Lieutenant Governor in Council may make regulations" with respect to a number of prescribed matters. This section (with some amendments) will continue in the amended *OGCA*. But Bill 12 adds to this another regulation-making power (s 77(1.1)) framed as follows:

> The Lieutenant Governor in Council may make regulations necessary to carry out the provisions of this Part according to their intent or to meet cases that arise and for which no provision is made by this Part, including regulations …
>
> ….
>
> (b) limiting, regulating and controlling the exercise of the Regulator's discretion with respect to the orphan fund… (emphasis added)

This is an extraordinarily broad regulation-making power. It is not clear why the government considered it necessary to have two regulation-making powers in the same part of the *Act*; the one drafted in conventional terms, the other in such a sweeping manner.

Eighth, the *OGCA* is amended throughout to ensure that the OWA can undertake remediation activities associated with orphan sites in addition to suspension, abandonment and reclamation activities and that the costs of these activities can be recovered from the Fund. Bill 12 defines "remediation" and "remediation costs" as follows:

> "remediation" means remediation within the meaning of the *Environmental Protection and Enhancement Act*;
>
> "remediation costs" means the reasonable costs actually incurred in the remediation in respect of a well, facility, well site or facility site, and, whether or not an application for a remediation certificate is made, includes such costs associated with assessment for the purpose of applying for a remediation certificate under the *Environmental Protection and Enhancement Act*…

The "definition" of remediation uses the "within the meaning of" formulation because the *Environmental Protection and Enhancement Act*, RSA 2000, c E-12 does not actually define the term. "Remediation" is principally used in Part 5 of *EPEA* in the context of releases and the duty to remediate the effects of any such release.

Conclusions

These amendments to the *OGCA* (and parallel amendments to the *Pipeline Act*, RSA 2000, c P-15) by and large should be welcomed: they fill gaps and extend the coverage of the Orphan Fund in useful and important ways. Indeed, one wonders why they have been so long in coming. The real issue is not what is in Bill 12 but what is missing from Bill 12 – and what is missing is a comprehensive plan for dealing with the systemic problems underlying the increasing number of orphan well and facility problems as well as other unfunded liability problems in the oil and gas sector (including tailing pond liability issues). The UCP and previous governments have been booting this problem down the road for decades. It is ironic that the government chose to introduce Bill 12 at the very time when oil prices hit historic lows and when the industry is very poorly positioned to deal with this suite of issues – but the stark risk posed by $20/barrel WTI oil is exactly the stark risk that has been staring at us in the face for so long. Now we need to see the balance of the plan – for the sake of future generations of Albertans. And the plan better not

depend on $100/barrel WTI oil. In reviewing the plan it will be important to examine how it apportions responsibilities (and direction) as between the Department and the AER. The AER now has a new board of directors and, as of April 15, 2020, a new CEO – an appointment that has attracted some adverse media attention.

Thanks to Drew Yewchuk, Shaun Fluker, David Wright and Martin Olszynski for comments on an earlier draft of this post.

This post may be cited as: Nigel Bankes, "Bill 12: A Small Step Forward in Managing Orphan Liabilities in Alberta" (April 9, 2020), online: ABlawg, http://ablawg.ca/wp-content/uploads/2020/04/Blog_NB_Bill12_April2020.pdf