Alberta Releases Curtailment Rules for Crude Oil and Crude Bitumen Production

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Summary of the Rules

The Rules are made pursuant to the *Oil and Gas Conservation Act* ("OGCA"),3 *Oil Sands Conservation Act* ("OSCA"),4and *Responsible Energy Development Act* ("REDA").5 "Operator" is defined in section 1 to include only crude bitumen operators pursuant to the OSCA and crude oil licensee and approval holders pursuant to the OGCA.

The purpose of the Rules are set out in section 2 as follows: (a) effect conservation and prevent wasteful operations; (b) prevent improvident disposition, and (c) ensure the economical development in the public interest of the crude bitumen and crude oil resources of Alberta.

Pursuant to section 3, the Rules prevail over any approvals, directives or orders issued by the Alberta Energy Regulator ("AER"), or any agreements or approvals under the *Mines and Minerals Act*6 that require or permit production at a rate greater than is permitted under a curtailment order.

Sections 4 and 5 of the Rules give the energy minister ("Minister") authority to issue curtailment orders on a calendar monthly basis, commencing January 2019. The orders will provide the monthly combined provincial crude oil and crude bitumen production volume, and pro-rate that combined volume among operators by fixing the combined amount of crude oil and crude bitumen that may be produced by each operator.

Subsection 3(2) of the Rules exempts operators that only began initial production after August 31, 2018 for a three-month grace period from when the operator began to produce crude oil or crude bitumen, to allow new operations to stabilize. Further, the schedule to the Rules sets out defined formulas which have the effect of exempting operators from the Rules if their average production during a specified baseline period is less than 10,000 barrels per day. Nevertheless, all operators' first 10,000 barrels per day are exempt from curtailment under section 8.

Although the curtailment orders will be issued on an individual operator basis, section 6 of the Rules provides for joint ventures or partnerships operations. For those operators, the Rules allow the joint venture participants or partners to enter into agreements about how their total allowable production is allocated as between themselves.

Subsections 7(1) to (3) of the Rules allow separate operators to apply to the Minister for permission to consolidate their allocated maximum production amounts, so that each of their production counts toward a single consolidated pool.

Finally, subsections 7(4) to (6) create a mechanism for operators to trade production allocations among themselves, with approval of the Minister. Pursuant to these subsections, two or more operators can apply for an order amending their individual curtailment orders by redistributing one another's allocations.

Implications of the Rules

The Rules appear to capture some of the fears and concerns of some industry members. They incorporate certain protections for new and small-volume operators. There likely are, however, small producers that may not benefit from the 10,000 barrels per day exemption.

The Rules also incorporate commercial principles. The allocation-sharing features of the Rules are clearly designed to encourage cooperation between large Alberta operators in a way that makes the most commercial sense to them. The recognition of joint ventures and partnerships under section 6 is an important feature that provides some flexibility allowing commercial arrangements to adapt to the curtailment orders. The ability of separate operators to apply to the Minister for transfer or consolidation of their allocations under section 7 may be useful to operators in various ways, including pursuing diversification initiatives and investments. The Rules, however, do not provide any criteria or guidance for the Minister's determination of such applications. This appears to be entirely discretionary.

Other concerns highlighted in our previous update remain outstanding. Neither the curtailment plan nor its enabling Rules considers whether the curtailment may put some wells into inactive status, or how many. It should be carefully considered whether the curtailment may have the effect of increasing Alberta's number of inactive wells or creating more orphan wells and facilities. Further questions are whether wells and facilities that become inactive due to the curtailment may be exempt from calculating an operator's liability management rating for a defined period of time, or whether the AER's liability management programs may be suspended during the period the curtailment is in force. These unintended consequences should be given adequate attention.

Trade and competitiveness issues have also been highlighted by some operators, although opinions are divided on this point. The Province of Saskatchewan, however, has declared that it will not curtail production, due in part to the fact that the majority of Saskatchewan oil production is light and medium oil that does not suffer from the same price discount as Alberta's crude oil and crude bitumen. Still, Saskatchewan officials have indicated that they will work with industry to ensure that Alberta's efforts are not undermined.

We will continue to monitor and provide updates and practical advice for dealing with these issues.

1 OC 375/2018.

2 Alta Reg 214/2018.

3 RSA 2000, c O-6.

4 RSA 2000, c O-7.

5 SA 2012, c R-17.3.

6 RSA 2000, c M-17.

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