The Accord Acts Twenty Years Later

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The authors examine key provisions of the Accord Acts and the experience with them to date, and make comparisons with other jurisdictions. They address regulatory issues, such as the resource conservation powers of the Boards, the relationship between the Boards and other agencies, and the relative success of regulation streamlining efforts. Finally, they consider exploration and development matters and commercial issues such as flow-testing of exploration wells, benefits, royalty agreements, Board guidelines, disclosure of information, and conditions or requirements attached by the Boards to authorizations.

Les auteurs examinent les principales dispositions des lois de mise en œuvre de l’Accord ainsi que leurs incidences jusqu’à maintenant, et ils établissent des comparaisons avec ce qui se produit dans d’autres ressorts. Ils étudient des questions réglementaires, par exemple les pouvoirs des Offices en matière de conservation de la ressource, la relation entre les Offices et d’autres organisations ainsi que le succès relatif des travaux de simplification des règlements. Enfin, ils examinent des questions relatives à l’exploration et à l’exploitation et se penchent sur des enjeux comme les essais de détermination de l’écoulement des puits d’exploration, les retombées économiques, les accords de redevance, les lignes directrices des Offices, la divulgation de renseignements et les conditions ou les exigences dont les Offices assortissent les autorisations.

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Introduction

The Canada-Newfoundland Atlantic Accord Implementation Act (Newfoundland Accord Act),¹ and the Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act (Nova Scotia Accord Act)² (collectively, the Accord Acts) represent joint management schemes based on political compromises following years of disputes and negotiations. The most important developments include: the introduction of the Canada Oil and Gas Land Regulations³ in 1961; jurisdictional disputes between the Atlantic provinces and Canada (coupled at times with threatened references

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³ C.R.C., c.1518.
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to the Supreme Court of Canada; the beginning of deep water drilling in 1966; various federal proposals for revenue sharing; the Supreme Court of Canada decision in 1967 on the British Columbia Offshore Reference (confirming the federal position that Canada was entitled to the rights of exploration and exploitation of resources in offshore areas); statements of principles on proposed offshore administration and management regimes with the Atlantic Provinces; the Clark government’s short-lived proposal to transfer ownership and jurisdiction of offshore mineral rights to the coastal provinces; the National Energy Program and the infamous Crown Share; the Hibernia reference to the Supreme Court of Canada in 1984; the 1982 Canada-Nova Scotia Accord (Nova Scotia Accord), subsequently revised in 1986, and the 1985 Canada-Newfoundland Accord (Newfoundland Accord) (collectively Atlantic Accords).

Although the Hibernia reference to the Supreme Court of Canada definitively established that the rights to explore for and exploit the offshore natural resources located on the continental shelf belonged to the Canadian government, the practical reality of the constitutional division of legislative power between provinces and the federal government on other matters and the reluctance on the part of the federal government to enact its own laws for the offshore areas subject to the Accord Acts has meant that the legal framework for the commercial exploitation of these offshore natural resources requires the involvement of, and coordination with, onshore provincial jurisdictions. This requirement, coupled with the


historical, socio-economic and political circumstances of Atlantic Canada, has resulted in the joint management regimes under the *Accord Acts*.

During the third and final reading of the Bill for the federal *Canada-Newfoundland Offshore Petroleum Resources Accord Implementation Act*, the Hon. Jack Shields, Parliamentary Secretary to the Minister of Energy, Mines and Resources, described the Act as "stimulat[ing] economic development and foster[ing] social justice" with the federal and provincial governments as "equal partners." During the second reading of the Bill, the previous Parliamentary Secretary for the Minister stated: "The Accord will provide a stable and permanent management regime that recognizes the equality of the federal and provincial Governments in the development of offshore resources. It will provide a clear regulatory regime for industry."

Similarly, during the third and final reading of the federal *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act* the Hon. Jack Shields described the Act as having "at [its] heart...a new shared management regime under which the province has an equal share in decisions" which would "assure the Government of Nova Scotia of its rightful place as an equal partner...in the management of petroleum resources," and "set aside the question of which level of government has jurisdiction" to "create a stable investment climate." The Act was also lauded as bringing the benefits of training and employment and security of energy supply.

Exploration and development activity offshore Nova Scotia, Newfoundland and Labrador has brought a new focus on the regulatory procedures and commercial arrangements governing those activities. Although the *Accord Acts* were implemented in the late 1980s, it was not until the commencement of offshore commercial production in 1992 that many of the provisions and processes under the *Accord Acts* were tested in practice. As commercial activity has increased and some of the anticipated economic benefits have begun to materialize, political developments in Atlantic Canada have tested the scope available for provincial initiatives under what are still joint management regimes. This, coupled with what could be generously described as a "hands-off" attitude of the federal government towards East Coast energy development during the same period, has created the legal and political environment in which the *Accord Acts* currently operate. Recent disputes over revenue sharing, and

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the effects on equalization arrangements, in relation to offshore resource revenues have been the latest chapter in this continuing saga.

Nearly twenty years after their implementation, the Accord Acts remain the framework for east coast offshore development. In the intervening period a number of issues have demonstrated both the strengths and weaknesses of the Accord Acts approach. This paper reviews some of these issues, specifically: the use of the Atlantic Accords in interpreting the Accord Acts; the powers of the Boards and limitations on their roles as regulators and their enforcement powers; the roles of the Boards, governments and proponents in relation to benefits agreements and the standing of other parties to challenge their actions; developments in relation to petroleum practices such as: pooling, unitization, third party access to facilities, and production flow testing; developments in private royalty agreements; and the ongoing process of regulatory streamlining.

I. The Atlantic Accords
The Atlantic Accords themselves continue to play a role in the interpretation of the Accord Acts. Each of the Atlantic Accords contains an important statement of principles that provides context for interpreting the provisions in the Accord Acts.

One of the stated purposes of the Newfoundland Accord is “to recognize the right of Newfoundland and Labrador to be the principal beneficiary of the oil and gas resources off its shores, consistent with the requirement for a strong and united Canada.” This, and the equivalent provision in the Nova Scotia Accord, are the focus of the current debate between the federal government and these two Atlantic provinces over equalization in the context of resource revenue.

A further purpose of the Newfoundland Accord is “to provide for a stable and fair offshore management regime for industry.” This is expressly stated as a core purpose of the Newfoundland Accord Act, and of equal weight to the purpose with respect to the relationship between the interests of the respective governments.

The Supreme Court of Canada has recognized this “stable and fair management regime for industry” purpose and intention, and the

9. Supra note 4.
10. Newfoundland Accord, supra note 4., at s. 2(c); Nova Scotia Accord, supra note 4., s.1.02(c).
12. Newfoundland Accord, supra note 4 at s. 2.(f); Nova Scotia Accord, supra note 4 at s. 1.02(f). Note: The complete text of the Nova Scotia section states: “to ensure the continuance of a stable offshore administrative regime for the industry consistent, insofar as is appropriate, with regimes established for other offshore areas in Canada.”
contextual importance of the *Newfoundland Accord*, in interpreting and applying the *Newfoundland Accord Act*. In 1982, Mobil Oil Canada, Ltd., Gulf Canada Resources Limited, Petro-Canada Inc., and Chevron Canada Resources Limited drilled the Nautilus C-92 discovery well. In 1984, the companies requested a significant discovery declaration (SDD) from the federal government in respect of the Nautilus well and forty-one surrounding sections. In 1986, the Canada Oil and Gas Lands Administration informed the companies that it would recommend an SDD with respect to eleven sections only. The Minister of Energy, acting upon this recommendation, made a SDD for eleven sections. Following an unsuccessful appeal to the Minister in 1990, after the *Canada Oil and Gas Act* was repealed, the companies applied to the Administrative Board established under the new statutory regime for an SDD of twenty-five sections. The chairman of the Board responded by letter to the 1990 proposal and stated that it would not be put before the Board “because any application for an additional significant discovery would have to be based upon the results of a well other than Nautilus C-92 and because no additional well has been drilled, your letter, which is based upon the Nautilus C-92 well, cannot be considered a bona fide application pursuant to [s.] 71” of the federal *Newfoundland Accord Act*.

The companies took their case to court, claiming that they had been unjustly denied an opportunity to be heard by the Board. Although the Supreme Court of Canada’s determination was that the applicants did not succeed on the merits, the Court found that the Board had failed to observe its obligations under the *Newfoundland Accord Act*. As Justice Iacobucci stated, on behalf of the Court:

> Finally, attention must be given to the object and scheme of the legislation at issue. The federal and provincial Implementation Acts gave effect to the provisions of the Atlantic Accord, and the Board must conduct itself with the Accord in mind: s. 17(1). Two purposes of the Accord were “to provide for a stable and fair offshore management regime for industry” and “to provide for a stable and permanent arrangement for the management of the offshore”: see clauses 2(f) and (g).

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14. Prior to the implementation of the *Newfoundland Accord Act*, these matters were governed by the *Canada Oil and Gas Act*, S.C. 1980-81-82-83, c. 81, and the Canada Oil and Gas Lands Administration was charged with the statute's administration.
16. For the complete facts, see *Mobil, supra* note 13 at paras. 3-5.
In terms of legislative history and intent, Justice Iacobucci compared the legislative scheme under the *Newfoundland Accord Act* to that which existed under the *Canada Oil and Gas Act*. He noted that under the *Canada Oil and Gas Act*, the Minister was invested with significant discretionary authority in respect of SDDs. Under the *Accord Act*, however, he noted that this discretion had given way to “an objective test which favours industry participants.”

Justice Iacobucci further noted that a purpose of the *Newfoundland Accord* was “to provide for a stable and fair offshore management regime for industry” (see cl. 2(f) of the *Accord*), that the applicant had a right of procedural fairness, because of the significant effect on the applicant’s investment if a declaration of significant discovery is not made, and that “industry fairness was an important goal of the Atlantic Accord.”

The most significant recognition of this purpose has already been described, in that “the ministerial discretion which governed SDDs under s. 44(1) of the *Canada Oil and Gas Act* was replaced by s. 71(1) of the *Newfoundland Accord Act* and a procedure that requires the objective reasonableness of declarations.”

The broader point made by the Court is that “the Board must conduct itself with the [*Newfoundland Accord*] in mind.”

Iacobucci J.’s recognition of an objective test and the requirement of fairness to industry has been subsequently applied by Justice Barry of the Newfoundland Supreme Court, Trial Division. Citing Justice Reed from *Mobil Oil Canada Ltd. v. Canada (Minister of Energy, Mines and Resources)*, Justice Barry stated that the legislative purpose of the significant discovery provisions under the *Newfoundland Accord Acts* is “to accord someone who spends time and money exploring for oil and gas the rewards which arise out of a discovery which is made.”

It is clear from these decisions that the *Accord Acts* are to be interpreted in light of the legislative objective and purpose of achieving a stable (and, in the case of Newfoundland, fair) offshore management regime for industry. These principles are fundamental to the *Atlantic Accords*. It will be interesting to see the extent of their influence in the future.

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18. Ibid. at para. 9.
19. Ibid. at paras. 15-16.
20. Ibid. at para. 13.
II. **Powers of the Boards**

The Canada-Nova Scotia Offshore Petroleum Board (C-NSOPB) and Canada-Newfoundland and Labrador Offshore Petroleum Board (C-NLOPB) (collectively, the Boards) have responsibility for offshore oil and gas activities including issuing and administering interests, monitoring operations, and the approval of development and benefits plans. In addition, the Boards are the lead regulator when regulatory responsibilities of other provincial and federal agencies overlap with those of the Boards.23

1. **Appropriate use of guidelines**

Each of the Accord Acts authorizes the relevant Board to issue and publish, in such manner as the Board deems appropriate, guidelines and interpretation notes with respect to certain provisions under the Accord Acts including those dealing with benefits plans, licences and development plan approvals.24 The Accord Acts are clear that these guidelines are not statutory instruments.25 This reflects the principle that "a non-statutory instrument cannot impose mandatory requirements enforceable by sanction; that is, the regulator cannot issue de facto laws disguised as guidelines."26 Nevertheless, the Boards have linked the content of their guidelines to the conditions of the authorizations they issue. For example, condition 34 of the C-NLOPB decision on Terra Nova requires the proponents to provide in their Environmental Protection Plan "that the treatment and disposal of wastes are consistent with the September 1996 Offshore Waste Treatment Guidelines and with revisions to these Guidelines following their approval by the Board."27

Because offshore operations and projects are so large and complex, it is not surprising that legislative and regulatory gaps exist. Due to the inaction of the federal and provincial governments in amending and updating the Accord Act regimes, various sets of guidelines have been used by the Boards to provide guidance in the absence of definitive legislation and regulations. There is a concern that the Boards are using guidelines

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24. Nova Scotia Accord Act, supra note 2, s.156(1); Newfoundland Accord Act, supra note 1, s. 151.1(1).
25. Nova Scotia Accord Act, supra note 2, s. 156(2); Newfoundland Accord Act, supra note 1, s. 151.1(2).
to create just such a *de facto* legislative scheme to the extent that the guidelines create (or are part of) hard conditions and create operational parameters.

Two examples of the guidelines that the Boards administer are the *Offshore Waste Treatment Guidelines* referred to above (issued in 2002 by the National Energy Board (NEB), C-NSOPB, and C-NLOPB), and the *Compensation Guidelines Respecting Damages Relating to Offshore Petroleum Activity* (issued jointly by the Boards in 2002).

The *Offshore Waste Treatment Guidelines* are intended to establish a minimum standard applied by the Boards in making authorizations concerning the treatment and disposal of wastes from petroleum drilling and production operations. Failure to adhere to the contents of the guidelines exposes an offender to enforcement measures, as discussed below. These guidelines largely deal with specific practices, volume and concentration restrictions for various discharged substances (e.g., greenhouse gas emissions and drilling mud). They also deal with the mixing of waste discharge streams, the location of waste streams on offshore installations, and the creation of environmental monitoring programs.

The *Compensation Guidelines Respecting Damages Relating to Offshore Petroleum Activity* are designed to provide information about compensation sources for persons claiming offshore petroleum-related losses and the regulatory/administrative role of the Boards in that respect. These guidelines establish a framework that encourages potential claimants in respect of damage attributable to petroleum spills or debris, where the cause of the damage is unambiguous, to contact operators with the goal of a voluntary settlement. If unsuccessful, an application can be made to a Board relating to an operator’s security deposit. Where the identity of the operator is unknown, applications may be made to either the Canadian Association of Petroleum Producers Unattributable Damage program or the Ship-Source Oil Pollution Fund (in place since 1973).

The ability of the C-NLOPB to impose conditions as part of its authorizations was examined by the Newfoundland Supreme Court in *Petro-Canada v. Canada-Newfoundland Offshore Petroleum Board.*\(^{28}\) Petro-Canada, as the operator in respect of the King’s Cove A-26 well, had applied to the C-NLOPB for a declaration of significant discovery in relation to an offshore test well. The C-NLOPB denied the request. Petro-Canada successfully applied to quash the Board’s decision by way of an order in the nature of *certiorari.*

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The drilling program authorization from the Board required the operator to comply with the *Draft Newfoundland Offshore Petroleum Drilling Regulations* “and all modifications and amendments thereto as may be promulgated from time to time” (*Draft Drilling Regulations*). The *Draft Drilling Regulations* defined “formation flow test” as “an operation to induce the flow of formation fluids to the surface of a well for the purpose of procuring reservoir fluid samples and determining reservoir flow characteristics.”

Subsection 177(2) of the *Draft Drilling Regulations* required every operator to conduct a formation flow test if fluid samples and productivity data were required to assist in the evaluation of a formation, and wireline formation samples did not provide sufficient information.

Petro-Canada had run two drill stem tests on the well. The first suffered from a mechanical error and the second produced 1.6 m$^3$ of oil over a six hour period. The fluid composition averaged six percent oil before declining to zero at the end of the test. Petro-Canada had explained to the Board that the reservoir and pressure data indicated a “washout” during the course of the test and therefore it had extrapolated an estimated production rate based on the maximum oil production rate during the course of the drill stem test. The C-NLOPB initially denied the application and, following receipt of a report from its Oil and Gas Committee (requested by Petro-Canada under the *Accord Act*), rejected it a second time. The Board’s reasons were essentially that Petro-Canada’s test results were insufficiently compelling.

In the course of its application, Petro-Canada argued that the Board exceeded its jurisdiction by requiring production to the surface in formation flow testing in accordance with the *Draft Drilling Regulations*. Justice Barry rejected that argument and held that the Board’s power under section 133(1)(b) of the *Newfoundland Accord Act* to authorize, in its discretion “such requirements ... as the Board determines or as may be prescribed” entitled the Board to require compliance with the draft regulations. He also held that this did not conflict with a provision authorizing the Lieutenant Governor-in-Council to make regulations requiring and prescribing the making of tests and the taking of samples, where no such regulations had been enacted.

This ruling upholds the Board’s power to prescribe operational conditions, including the incorporation by reference of the standards or

30. *Supra* note 22 at 487.
specifications of other organizations, similar to that of a legislator. Justice Barry noted in passing that a subsequent amendment to s. 144 of the Newfoundland Accord Act, which allowed the Lieutenant Governor to incorporate other standards or specifications by reference in the regulations it was authorized to make, might require a different interpretation of the Board’s authority but that he need not decide this. What remains an issue, however, is the scope and latitude enjoyed by the Board in its role as rule-maker as well as regulator. The case does not provide clarity with respect to the extent of the Board’s powers, but signals that they may be more substantial than one might have thought. In this case the Court expressly recognized the Board’s power to fix standards in the absence of regulations contemplated by the Accord Act.

In the recent case of Hibernia Management and Development Company Ltd. and Petro-Canada v. C-NLOPB, the Trial Division of the Supreme Court of Newfoundland considered a situation where the Board, following consultation with industry, had issued a set of Guidelines for Research and Development Expenditures (R&D Guidelines). Other aspects of this case are discussed in Section III below, but what is relevant for the present purpose is that the applicants in that case submitted that the Accord Acts did not give the Board the power to impose expenditure obligations on the applicants by means of the R&D Guidelines, as the guidelines permitted under the Accord Acts are intended to be administrative only and they did not have the force of regulations under the Statutory Instruments Act. Adams J. dealt with this argument as follows:

However, in this case, Section 151.1 of the Act has given the Board the express power to issue guidelines and interpretation notes in respect of, among other things, the application and administration of Sections 45, 138 and 139. As stated by Orsborn, J., in Saint John’s v. C-NLOPB, supra, at paragraph 95:

Clearly, it was the intent of both governments that issues relating to economic benefits would be left to the Board, subject only to joint direction from the governments.

As there had been no joint directive from the governments respecting research and development, the Court was satisfied that the Board’s decision to establish the R&D Guidelines was a reasonable interpretation of the

32. Ibid.
33. 2007 NLTD 14, 263 Nfld. & P.E.I.R. 40 [HMDC and Petro-Canada].
34. Infra note 60.
36. Supra note 33 at para. 55.
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Canada-Newfoundland Accord and the Newfoundland Accord Act and expressed the legislative intent of the governments regarding the power of the Board to issue the R&D Guidelines and to make them binding upon the applicants.

Both of these cases acknowledge the powers of the Board to make guidelines binding upon parties carrying on operations offshore and thereby fill perceived gaps in the legislative/regulatory schemes under the Accord Acts.

2. Constraints on board powers

With respect to constraints upon the powers of a Board, the decision in Saint John's (City) v. Canada-Newfoundland Offshore Petroleum Board is instructive. An application to the C-NLOPB for Development Plan approval must include a development plan application (DPA), an environmental impact statement (EIS) and a benefits plan. In approving an application, the Board will generally accept these foundation documents subject to specific conditions.

As part of the Terra Nova Benefits Plan, Petro-Canada, as operator, had committed to a “best-efforts” plan to relocate engineering and procurement activities to Newfoundland and Labrador. The C-NLOPB approved the benefits plan subject to certain conditions, including that “as soon as practicable after Project Sanction, the Proponent relocate engineering and procurement activities for the Project to Newfoundland.” Petro-Canada subsequently asserted that, because of cost and scheduling concerns, it was not practical to move engineering and procurement activities to Newfoundland and Labrador. On 30 June 1998, the Board, based on its interpretation of the “best efforts” condition, “reluctantly accepted” that Petro-Canada had complied with the condition.

The City of Saint John’s asserted that the Board had failed in its statutorily imposed duty to enforce this condition of the Board’s approval. Since the City and its citizens would have been the major beneficiaries of any relocation of such activities to the province, the City brought an application before the Trial Division of the Supreme Court of

38. Ibid. at para. 1 (citing Decision 97.02).
39. Ibid. at para. 2.
40. Ibid. at para. 3. This action by the City involved the Mayor, Andy Wells, who was later in another dispute relating to the Board, this time including the Province, who wanted Mr. Wells to be appointed as the Chair of the Board, and the federal government, who, after a failure to reach agreement with the Province and an arbitral procedure as required under the Accord Act, preferred the candidate recommended by the arbitration panel. See Ruelokke v. Newfoundland and Labrador, 2006 NLTD 127, (2006), 258 Nfld. & P.E.I.R. 308.
Newfoundland to require the Board to enforce the condition imposed upon Petro-Canada.

One of the remedies the City sought in the application was an order of *mandamus* to compel the Board to perform what the City asserted was the Board’s statutory duty — to force Petro-Canada to operate its engineering and procurement operations out of Newfoundland and Labrador. Despite the fact that the Court determined that the “Proponent did not in fact comply with the Condition,” Justice Orsborn noted the following:

> Inherent in the City’s request for relief is the assumption that the Board actually has the authority to force the Proponent to move its engineering activities to Newfoundland. This assumption may not be well-founded. The Board does possess certain powers of enforcement — notably the power to revoke a licence or authorization. But whether its statutory authority extends to a direct order to carry on work in a certain location is an unanswered question. The ability to revoke a licence may provide opportunities to achieve a particular outcome through influence and persuasion, but the actual order of the Board sought by the City may not be within the authority of the Board.

This limitation on the Board’s remedial authority is important. In *HMDC and Petro-Canada*, Justice Adams noted that the C-NLOPB’s ability to revoke a production operations authorization was “the ultimate mechanism by which the Board may control activity in the offshore area.”

There is a view that Boards ought not to dictate specific operational methods and modes, nor should they have the power to dictate what shall be done and when. That does not mean the Boards do not have a direct impact upon the day-to-day operations of industry participants working in the offshore. Quite the opposite is true. However, as these decisions have noted, the Boards’ powers of enforcement may be limited to their ability to revoke licences or authorizations where the conditions of such licences or authorizations have been breached. This is a blunt instrument and, in many circumstances, it may not be an appropriate remedy for failure to comply with guidelines or conditions issued by the Boards.

Another avenue a Board might take is to treat the breach of a condition or requirement of an authorization or approval as “an environmental or social

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44. *Supra* note 33.
45. *Newfoundland Accord Act*, *supra* note 1, s. 134(5).
problem of a serious nature," which gives rise to the Board’s statutory power to prohibit the commencing or continuing of any offshore work or activity. This provision may have a very limited scope, however a plain interpretation of a “social problem of a serious nature” would probably not include the absence of a transfer of engineering and procurement, and even if it were concluded that it did, prohibiting work on a project such as Terra Nova would have made little sense in the circumstances. While a stop work order may be seen as less onerous than a suspension of the authorization or licence, it is still a very reactionary response. Monetary penalties, for example, might be a more effective means of achieving compliance in the future.47

The Petro-Canada and Saint John’s cases demonstrate the uncertainties about the rule-making role the Boards should play in a multi-jurisdictional, expert context, given the limited enforcement remedies they have. The notion of a “one-window” gateway of regulatory expertise is inconsistent with the absence of technical rule-making authority. By contrast, the Alberta Energy and Utilities Board (AEUB), the equivalent oil and gas practices regulator in Alberta, although subject to statutes and regulations passed by the legislator, also has the ability to pass regulations in its own right in discrete areas.48 In considering potential improvements in the operation and effectiveness of the Accord Acts, it would be worthwhile to spend some time on clarification of the powers of the Boards and, if they are going to have an expanded rule-making authority, on their ability to effectively monitor and enforce the rules they make. The present situation under the Accord Acts invites problems and disputes, with the lacunae in the legislative/regulatory regime due to government inaction being filled by guidelines made by agencies lacking practical and effective powers of enforcement.

On the other hand, if “smart” (in the sense of performance-based) regulation is more fully embraced for the Accord Acts, the setting of principled standards by the legislators may provide the Boards a more legitimate way to specify or influence operating practices subsequent to the issuance of authorizations. Smart regulation has been an initiative in

46. Newfoundland Accord Act, supra note 1, s. 56(1)(a); Nova Scotia Accord Act, supra note 2, s. 62(1)(a).
the offshore context since 2002. It consists of making regulations that are outcome-based rather than prescribing the methods an operator must employ to meet a legislative requirement. Blunt enforcement powers may be less problematic when they target the breach of clear standards rather than the enforcement of detailed guidelines. The guidelines would, in other words, have a different role and not be enforced in a strict way, i.e., enforcement would only occur if the performance goal is not met. This regulatory initiative is discussed in more detail in Section IX.

III. Benefits requirements

It has been observed that one of the key elements of the Accord Acts is the desire to use a finite and exhaustible resource to create a lasting economic legacy for the people of the respective provinces. The Accord Acts establish that one of the requirements that proponents of offshore developments must fulfill in order to obtain approval for a development application is a benefits plan approval.

The Accord Acts spell out the requirements that a Board must consider prior to approving a benefits plan:

1. consistent with the Canadian Charter of Rights and Freedoms, employment of Canadians and residents of the Province, giving first consideration to residents of the Province for employment and training during the project;
2. participation of Canadian manufacturers, consultants, contractors and service companies and, in particular, giving first consideration to services provided from within the Province and to goods manufactured in the Province, where those services and goods are competitive in terms of fair market price, quality and delivery;
3. expenditures for research and development to be carried out in the Province and for education and training to be provided in the Province;
4. provisions to ensure that disadvantaged individuals or groups have access to employment and business opportunities generated by the project; and,
5. provisions to ensure manufacturers, consultants, contractors and

49. E.g., the Atlantic Energy Roundtable conference of 2002 highlighted “smart regulation” as a goal to pursue in the offshore context, as did the federal 2002 Speech from the Throne, see Canada “Speech from the Throne” 37th Parliament of Canada, 2nd Session (2002) House of Commons Debates (30 September 2002) at 1.
service companies in the Province and other parts of Canada are given a full and fair opportunity to participate on a competitive basis in the supply of goods and services used in any proposed work or activity.\textsuperscript{51}

Considering that much of the Accord Acts are based upon the Canada Oil and Gas Operations Act (COGOA), it is not surprising that this language closely reflects that found within the COGOA which states:

\section*{5.2 (1)} In this section, “benefits plan” means a plan for the employment of Canadians and for providing Canadian manufacturers, consultants, contractors and service companies with a full and fair opportunity to participate on a competitive basis in the supply of goods and services used in any proposed work or activity referred to in the benefits plan.

(2) No approval of a development plan shall be granted under subsection 5.1(1) and no authorization of any work or activity shall be issued under paragraph 5(1)(b), until the Minister has approved, or waived the requirement of approval of, a benefits plan in respect of the work or activity.

(3) The Minister may require that any benefits plan submitted pursuant to subsection (2) include provisions to ensure that disadvantaged individuals or groups have access to training and employment opportunities and to enable such individuals or groups or corporations owned or cooperatives operated by them to participate in the supply of goods and services used in any proposed work or activity referred to in the benefits plan.\textsuperscript{52}

The Accord Acts provide for an additional layer of preferential treatment to that mandated under the COGOA, giving priority to manufacturers, consultants, contractors and service companies resident within the applicable province above those resident in other parts of Canada, who, in turn, receive preferential treatment to those not resident in Canada.

In practice, developing an acceptable benefits plans requires involvement from project proponents, provincial authorities, federal authorities and the applicable Board. Because of the highly political nature of a benefits plan, the typical experience involves an initial negotiation between the provincial government and the project proponents. Once an agreement or understanding on appropriate benefits has been reached, this

\textsuperscript{51} \textit{Newfoundland Accord Act, supra} note 1, s. 45(3); \textit{Nova Scotia Accord Act, supra} note 2, s. 45(3).

\textsuperscript{52} \textit{R.S.C. 1985, c. O-7, s. 5.2.}
will form the basis of the benefits plan submitted by the proponents for approval to the relevant Board.\textsuperscript{53}

Unlike the approval of a Development Plan, by nature a highly technical document, the approval of a benefits plan, an inherently political document, is not a "fundamental decision" under the \textit{Accords Act} and therefore not subject to approval by the Provincial Minister. In other words, the approval of the benefits plan is strictly a matter for the Board, unless the Board is issued a joint directive from both levels of government.\textsuperscript{54}

In November 2006, EnCana filed a Development Application for Deep Panuke with the C-NSOPB consisting of a Development Plan, Canada-Nova Scotia Benefits Plan, a Socio-Economic Impact Statement and an Environmental Impact Statement. Prior to filing its application, EnCana had entered into an Offshore Strategic Energy Agreement (OSEA) with the Province of Nova Scotia on 22 June 2006. The Nova Scotia Department of Energy (NSDOE) represented the Province in negotiating the OSEA. The C-NSOPB was not involved in the negotiation of the OSEA. In Section 3 of the Benefits Plan volume of its application, EnCana incorporated Section 3 of the OSEA outlining EnCana's commitments to Nova Scotia benefits, including its commitment to the statutory obligations of Section 45 of the \textit{Nova Scotia Accord Act}. EnCana further stated that the OSEA describes additional commitments by EnCana to provide specific industrial and employment opportunities for Nova Scotians, with minimum commitments for person hours of work in Nova Scotia.\textsuperscript{55}

The C-NSOPB appointed a commissioner to oversee the public review of the proposed Deep Panuke Offshore Gas Development Project. The C-NSOPB and the NEB jointly drafted and circulated a draft list of issues for the Deep Panuke Coordinated Public Review. Among the issues to be considered was the following:

The Canada-Nova Scotia benefits plan having regard to, among other things:

- The extent to which the plan meets the requirements of the \textit{Accord Acts} by providing a process that gives residents of Nova Scotia,\textsuperscript{53} The Letter of Intent entered into between the Province and the project proponents with respect to the Terra Nova Project, for example, contained the benefits agreed between the Province and the proponents. In the case of Hibernia, the Hibernia Framework Agreement contained a Section on Benefits. See the discussion in \textit{HMDC and Petro-Canada v. C-NLOPB}, supra note 33 at 20-21. \textsuperscript{54} \textit{Newfoundland Accord Act}, supra note 1, s. 45(6); \textit{Nova Scotia Accord Act}, supra note 2, s. 45(6). \textsuperscript{55} EnCana Corporation, "Deep Panuke Offshore Gas Development Canada – Nova Scotia Benefits Plan" (November 2006), online: C-NSOPB <www.cnso.pb.ns.ca/whatsnew/pdf/Volume_3_Benefits_Plan.pdf>.
and other Canadians, a full and fair opportunity to participate on a competitive basis in the supply of goods and services;

- The extent to which the plan provides an acceptable process for the employment of Canadians and, in particular, members of the labour force in Nova Scotia in any proposed work or activity;

- The extent to which the plan provides an acceptable process and commitment towards education and training in Nova Scotia including provisions to ensure that disadvantaged individuals or groups have access to training and employment opportunities and to enable them to participate in the supply of goods and services; and

- The extent to which the plan provides an acceptable program and appropriate financial commitment for research and development in Nova Scotia.\(^{56}\)

In her report, the Commissioner identified areas in which she felt the proposed benefits plan to be deficient and concluded:

The Commissioner cannot recommend approval of the Canada-Nova Scotia Benefits Plan. There are no provisions, other than making monies available, with respect to education and training, and research and development. There are no provisions to ensure that disadvantaged individuals or groups have access to education, training and employment opportunities to enable them to participate in the supply of goods and services for the proposed Project. There is also a question about the impact the definition of “Nova Scotia Person Hour” in the OSEA will have on employment opportunities for current “residents of Nova Scotia.\(^{57}\)

The Deep Panuke application is the first instance in which an agreement of a provincial government on the sufficiency of a proposed benefits plan has been rejected. Prior to this occurrence, industry participants expected that the negotiations surrounding a benefits plan would be a bilateral process between project participants and the relevant provincial authorities. Once an agreement was reached, it would form the basis of an acceptable benefits plan which would then be brought forward for approval by the Board.

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\(^{57}\) Ibid. at 48.
Because of the political nature of a benefits plan, there are some who feel that the affected province should have the ultimate authority as to the sufficiency of a particular benefits plan. This, however, is not the scheme under the Accord Acts, where the relevant Board clearly has the exclusive authority to approve benefits plans. It will be interesting to see whether that authority survives in the future.

1. Post-acceptance conformity of approved benefits plans to section 45

The life of some offshore projects is measured in decades, not years. Over time, the political climate in a given jurisdiction will change. Even relatively short-term projects, such as Deep Panuke, are subject to changing political circumstances. As offshore projects represent significant sources of income to the affected province, the participants in an offshore project can expect to be directly impacted by these political changes. Changing political winds may mean that the benefits plans, approved years earlier, may again come under scrutiny.

Such a question was recently examined by the Supreme Court of Newfoundland and Labrador (Trial Division) in *Hibernia Management and Development Company Ltd and Petro-Canada v. C-NLOPB*. As already noted, Section 151.1 of the Newfoundland Accord Act authorizes the C-NLOPB to issue guidelines and interpretation notes with respect to the application and administration of the benefits plans provisions of that Act. Following consultation with the industry, on 5 November 2004, the Board established the Guidelines for Research and Development Expenditures. These R&D Guidelines outlined the amounts operators were required to spend on research and development over the life of their respective projects. They apply to all existing and future offshore petroleum projects in the area subject to the Accord Acts and came into effect on 1 April 2004. The R&D Guidelines establish expenditure obligations for project operators during the three recognized phases of an offshore petroleum project: the exploration phase, the development phase and the production phase. Hibernia, Terra Nova and White Rose are all currently in the production phase.

Based on Statistics Canada data, the Board undertook research to determine the “upstream” research and development expenditures norms
by oil and gas extracting companies in Canada. Using a five-year moving average, the Board established a percentage of total annual revenue to be spent on research and development in the Province. The actual amount of expenditure in a year depends on the five-year benchmark and the price of oil.

The Board estimated that the annual costs for these research and development expenditures would be approximately $3.7 million for each project. The total cost over the life of each project was estimated by the Board to be $85 million for Hibernia out of a total of approximately $19 billion in revenue, or .45%; and approximately $62 million for Terra Nova out of a total revenue of $13 billion, or .48%. Petro-Canada and the Hibernia Management and Development Company (HMDC) estimated the cost of these Guidelines to be significantly higher than this in the case of the Hibernia (approximately $159 million) and slightly higher for Terra Nova (approximately $68 million). Regardless of whose figures were used, the cost of the R&D Guidelines will be significant in total dollar figures over the lives of these projects.

Petro-Canada, as the operator of Terra Nova, and HMDC, as the operator of Hibernia, submitted that these actions of the Board amounted to a unilateral amendment of the applicants’ benefits plans. The benefit plans had been previously agreed to by the federal and provincial governments as part of the project approval process. Petro-Canada and HMDC believed the Board did not have the authority to amend these plans. They also submitted that since the Board had already approved the applicants’ benefits plans and development plans it was therefore functus officio. Further, Petro-Canada and HMDC asserted that they had acquired vested rights pursuant to the approval process which dated back to the mid-1980’s in the case of Hibernia, and the mid-1990’s in the case of Terra Nova. The R&D Guidelines would deprive them of some of these rights. They further submitted that the Board had overstepped its authority by establishing an R&D Fund into which would be placed any unexpended portion of the R&D expenditure requirements under the Guidelines. The Fund was to be spent by the Board in consultation with the industry. Petro-Canada and HMDC submitted that the Fund amounted to a tax that the Board had no statutory authority to levy.61

Petro-Canada and HMDC asserted that once the Board approved their respective benefits plans, that fixed their obligations regarding benefits for the entire duration of their respective projects. If the Board wished to establish targets for expenditures on research and development these

61. *Supra* note 33 at paras. 3-9.
should have been fixed at the time of the approvals of the respective benefits plans and could not now be imposed after the fact. They asserted that they undertook these expensive, long-term projects with the firm understanding that the benefits they would be obliged to provide would be as set out in those plans as approved. They asserted that the Board no longer had any authority to impose any additional or different obligations on them.

The Court rejected this assertion stating:

With respect, I find that this is not a reasonable or purposive interpretation of the Accord and the Acts and the Board’s previous decisions approving these developments. These offshore developments have a life spanning decades. The benefits plans themselves proposed the establishment of general principles and commitments and eschewed any specific expenditure commitments for research and development and education and training. They proposed regular reporting by the operators and ongoing monitoring by the Board to ensure compliance with the commitments undertaken and that maximum benefits would flow to the Province in particular and Canada generally.

To adopt the applicants’ submissions would be to allow them to unilaterally determine what amount to spend on research and development and education and training. They could choose to spend nothing and simply report that they were spending nothing. This, in their interpretation, would be the fulfilment of their obligation. As I have already stated, this is not a reasonable and purposive interpretation of the legislation and the Board’s authority and obligations under the Accord and the Acts.62

The Court noted that the applicants’ ability to proceed with their developments were dependent on Board approval and that by accepting the Board’s approval of their respective benefits plans, the applicants had accepted that the Board had an ongoing obligation and authority to assess and monitor the appropriateness of the levels of expenditure on research, development, and education and training. Having accepted these approvals on that basis, the Court found it was not open to the applicants to deny the Board’s ability to fulfill its duties under the Newfoundland Accord, and the Newfoundland Accord Act.

The Court also rejected the functus officio argument. Adams J. noted that the Board is granted the continuing power to monitor and assess the appropriateness of the level of expenditures of the applicants on research and development from time to time throughout the duration of these

62. Ibid. at paras. 45, 46.
decades-long projects. He concluded that the principle of *functus officio* has no application to continuing powers.\(^6\)

In rejecting the applicants' assertion that their vested rights had been interfered with, Adams J. stated that:

> the benefits plans provided for nothing more than general principles and commitments respecting research and development. It was left to the Board to determine from time to time what would amount to an appropriate and adequate level of expenditure. This could not be and was not determined at the beginning of the project and this was acknowledged by the applicants.\(^6\)

It is interesting to note that the decision does not articulate how the result in the case fits with the observations of the Supreme Court of Canada in the *Mobil* case on one of the purposes of the *Accord Acts* being to create a stable and fair offshore management regime for industry. The decision is currently under appeal.

Industry may well be concerned about the possibility that project participants may be required to contribute unbudgeted monies in the years following substantial capital expenditures. If the trial decision stands, each participant in a producing project could be subject, throughout the life of the project, to the ability of the Board to retroactively determine the appropriateness of the expenditures being made by the project proponents in compliance with their obligations for the duration of the project, with the result that the proponents cannot predict with certainty what the expenditures will be. The fact that this is in part the result of the very general "principles" language used in some of the benefits plans approved to date (Justice Adams expressly noted that he was not dealing with specific expenditure commitments in the areas that were the subjects of the plans before him) suggests new caution in the language used for benefits plans commitments. No doubt consideration will also be given to possible means of restricting the Board's ability to require such additional expenditures in relation to benefits plan commitments. Since the Boards have the ultimate power to set the benefit plans and administer their compliance as envisioned by Justice Adams, absent a joint directive from the relevant province and the federal government, it is difficult to see how an agreement with the province will have much effect on the Board's actions. The limitation will have to come in the form of the commitments themselves.

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64. *Ibid.* at para. 52.
2. Standing to enforce benefits plans

A further issue that has arisen with respect to benefits plans under the Accord Acts is who has standing to enforce the obligations arising pursuant to the provisions of a benefits plan. As noted above, in City of Saint John's v. Canada-Newfoundland Offshore Petroleum Board the City of St. John's tried to enforce a benefit commitment made by Petro-Canada in the Terra Nova Development Plan even though the city was not a party to the benefits plan.\(^{65}\)

The Court rejected the City's application because, in part, the City did not have the capacity to bring an action to enforce the Benefits Plan. Noting that a "municipal corporation such as the City of St. John's has no greater capacity than that given by its incorporating legislation,"\(^{66}\) the Court observed that there was nothing in the City of St. John's Act\(^ {67}\) which gave the City the legal capacity to bring an action for the general benefit of its citizens. The Court concluded that the City did not have the capacity under its incorporating legislation to maintain the proceeding.

In another case, a local manufacturer of containers, A.M.O. Containers Limited, was not invited to tender on a contract to supply offshore containers to Hibernia. The company launched a suit naming the Government of Canada, the Government of Newfoundland, the C-NLOPB, HMDC and two agent-corporations as defendants.\(^ {68}\) A.M.O. brought an action in which it alleged that the Province had breached a legislative scheme that imposed certain duties on the Province to act in accordance with A.M.O.'s economic interests. A.M.O. also alleged that the Province was negligent. The Province responded that the legislation placed no obligation or duty on the Province to act in order to protect A.M.O.'s interests.\(^ {69}\) The Province successfully applied to have A.M.O.'s claim struck for disclosing no reasonable cause of action. The Court found that the Province "owed no duty to A.M.O. Containers, breached no duty to A.M.O. Containers, and caused A.M.O. containers no loss."\(^ {70}\)

Other commentators have suggested that the Boards be given alternatives in enforcing specific commitments in the benefits plans.\(^ {71}\) Currently, the only remedy the Boards possess is the suspension or

\(^{65}\) Supra note 37.
\(^{66}\) Ibid. at para. 40.
\(^{67}\) R.S.N.L. 1990, c. C-17.
\(^{69}\) Ibid. at paras. 1-10.
\(^{70}\) Ibid. at para. 48.
\(^{71}\) Supra note 58 at 133.
revocation of licences or authorizations. As already noted, this ‘heavy remedy’ is clearly insufficient when dealing with matters of this nature.

Finally, there is some debate about the most effective methods by which to monitor the effectiveness of and adherence to benefits plans. In the 2005 Report of the Implementation Committee, the Atlantic Energy Roundtable noted concerns that benefits reporting requirements were adding to administrative overhead and costs without providing commensurate advantages to the industry or governments. The challenge was to identify improvements that would reduce costs while ensuring that required information remained available to the industry and governments for planning and monitoring purposes and that the importance of local benefits remained undiminished. Consensus among all stakeholders on the specific recommendations was not reached.

IV. Pooling and unitization

1. Pooling

Whether located in the Western Canadian sedimentary basin or beneath the seabed, the oil and gas in a reservoir is migratory by nature. There is a possibility that a well drilled by one party into a reservoir shared with adjacent lands held by another party may drain the resource from those adjacent lands. Drainage issues are as problematic offshore as they are on land.

The common law deals with drainage through the rule of capture. In Borys v. Canadian Pacific Railway and Imperial Oil Limited the Alberta Court of Queen’s Bench held that the mineral owner acquires title to the oil and gas produced from wells on his land even though the oil or gas has migrated from adjoining properties. This doctrine was recently affirmed by the Supreme Court of Canada.

The only protection against drainage at common law was to drill an offset well. The early results of the application of this rule were “development and production practices that failed to maximize ultimate recovery from reservoirs and that produced massive economic waste in the form of unnecessary wells.”

To avoid the adverse consequences of drilling more wells than required to effectively drain a reservoir, most jurisdictions have enacted conservation legislation and regulations that limit, through well spacing

72. AER, infra note 119 at 12.
75. Alastair Lucas & Constance Hunt, Oil and Gas Law in Canada, (Toronto: Carswell, 1990) at 199.
The Accord Acts Twenty Years Later

requirements, drilling density for both drilling and production purposes. Traditionally, the purposes of such well spacing has been four-fold:

1. to promote conservation of the resource;
2. to protect the correlative rights of well owners;
3. to reduce the economic waste of drilling more wells than necessary; and
4. to eliminate the safety hazard of closely spaced wells.\(^76\)

Leases of smaller tracts than required by such well spacing requirements may be the subject of pooling arrangements under which interest holders may aggregate their interests to the extent sufficient to justify a well. Such pooling agreements allow interest holders to combine their lands for the purpose of drilling or producing under existing conservation laws.

In most jurisdictions, a spacing unit is well defined and easily discernible. In Alberta, for example, the normal spacing unit for an oil well is 160 acres and the normal spacing unit for a gas well is 640 acres.\(^77\) When spacing requirements are imposed upon a system previously governed by the rule of capture, some mechanism will generally be created to deal with correlative rights – in this context, the rights of an owner to obtain an equitable share of production and to be protected from the wasteful practices of others with rights in a common pool. In Alberta, procedures exist for the recognition of voluntary pooling arrangements and for forced pooling where parties cannot agree. The owner of a tract within a drilling spacing unit may apply to the Energy Resources Conservation Board for an order that all tracts within the drilling spacing unit be operated as a unit to permit the drilling for or the production of oil or gas from the spacing unit.\(^78\)

Similarly, under the Accord Acts, all working and royalty interest holders in a spacing unit may voluntarily pool their interests for the purpose of drilling for and producing petroleum.\(^79\) The Accord Acts also allow a working interest holder in a spacing unit to apply to the Board for a mandatory pooling order directing the working interest and royalty owners

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\(^76\) See Rowland Harrison, "Regulation of Well Spacing in Oil and Gas Production" (1970) 8 Alta. L. Rev. 357.
\(^77\) Oil and Gas Conservation Act, Oil and Gas Conservation Regulations, Alta. Reg. 151/71, s. 4.020.
\(^78\) Oil and Gas Conservation Act, R.S.A. 2000, c. O-6, s. 80(1).
\(^79\) Nova Scotia Accord Act, supra note 2, s. 172; Newfoundland Accord Act, supra note 1, s. 167. Note: the pooling agreement and any amendments must be filed with the Chief Conservation officer.
within the spacing unit to pool their interests. The Accord Acts prohibit oil and gas production if there are two or more leases or separately owned working interests within a single spacing unit.

One difficulty under the Accord Acts is determining one of the basic parameters for a pooling agreement. The definition of “spacing unit” under the Accord Acts lacks the specificity of the Alberta definition. Under the Accord Acts, a “spacing unit” is defined as “the area allocated to a well for the purpose of drilling for or producing petroleum.” Thus, the Accord Acts’ definition of a “spacing unit” neither describes precisely the area of a spacing unit nor indicates how such area is to be ascertained.

There may be an historical reason for the lack of specificity in this regard. The pooling sections of the Accord Acts are based on the COGOA, which appears to be the source of the “spacing unit” definition. The recently circulated draft Drilling and Production Regulations under the COGOA state:

The Board is authorized to make orders respecting the allocation of areas, including the determination of the size of spacing units, and the well production rates for the purposes of drilling for or producing oil or gas and to exercise such powers and perform such duties as may be necessary for the management and control of oil or gas production.

The same clause is currently out for comment with respect to the Draft Newfoundland Offshore Petroleum Drilling and Production Regulations. The draft regulations would create in the offshore a regime similar to that which currently obtains in Alberta. They state that they are similarly intended to “promote conservation, prevent the waste of oil and gas resources and to protect correlative rights.” The draft regulations impose

80. Nova Scotia Accord Act, supra note 2, s. 173(1); Newfoundland Accord Act, supra note 1, s. 168(1).
81. Nova Scotia Accord Act, supra note 2, s. 176(1); Newfoundland Accord Act, supra note 1, s. 171(1).
82. Nova Scotia Accord Act, supra note 2, s. 176(1); Newfoundland Accord Act, supra note 1, s. 166.
84. Supra note 52, s. 29.
a standard grid, indicating well spacing units, target areas and penalty formulas to be applied if a well is drilled off target.

The incorporation of such regulations would allow the Boards to develop a consistent and easily identifiable spacing unit, allowing for predictability and better protection of correlative rights.

2. **Unitization**

Related to the concept of pooling is unitization. While pooling involves the bringing together of small tracts sufficient for the granting of a well permit under applicable spacing rules, unitization involves the joint operation of a producing reservoir where there is separate ownership of rights in relation to it. Unitization is a useful conservation tool. Through unitization, producers can make efficient use of reservoir pressures and secondary recovery operations can be used at the appropriate early stage in the development of the resource. Only with unitization of fairly sizeable tracts is it economically feasible to use advanced methods of cycling for maximum extraction of liquid constituents from gas. Under a unitization program, input and production wells may be located in accordance with the best engineering practices and without regard to lease, interest or spacing unit boundaries.

The Accord Acts permit unitization where there are several working interest holders in all or part of a pool that exceeds the area of a spacing unit. Unitization may occur under the Accord Acts in three ways. First, one or more working interest owners in a pool or part of a pool exceeding in area a spacing unit, together with the royalty owners in respect of that pool, may voluntarily enter into a unit agreement and operate their interests under the terms of the unit agreement or an amendment to it where a copy of the agreement and an amendment have been filed with the Chief Conservation Officer.

In the case of Terra Nova, the field was comprised of five significant discovery licences with varying ownerships. In C-NLQPB Decision 97.02 in which the Board approved the development plan for the Terra Nova Development Project, the Board required a unitization agreement which, although it was being negotiated, was necessary for "conservation purposes":

The Board acknowledges the unitization efforts by the Proponent.

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88. See Lucas & Hunt, supra note 75 for a more fulsome discussion of the principles of unitization.
90. Nova Scotia Accord Act, supra note 2, s. 177(1); Newfoundland Accord Act, supra note 1, s. 172(1).
and believes that unitization of the field is important for conservation purposes and for effective administration of the regulations governing production of the resource. Therefore, it is a condition of the Board's approval that:

Condition 15:
The Proponent file with the Board a unit agreement and a unit operating agreement prior to initiating oil production.91

In this case, the Board made a voluntary agreement a condition of the Board’s approval.

Second, where, in the opinion of the Chief Conservation Officer of the relevant Board, the unit operation of a pool or part thereof would prevent waste, the Chief Conservation Officer may apply to the Oil and Gas Committee for an order requiring the working interest owners in the pool or part thereof to enter into a unit agreement and a unit operating agreement in respect of the pool or part thereof.92

The *Accord Acts* define “waste” as follows:

(2) In this Part, “waste”, in addition to its ordinary meaning, means waste as understood in the petroleum industry and in particular, but without limiting the generality of the foregoing, includes

(a) the inefficient or excessive use or dissipation of reservoir energy;

(b) the locating, spacing or drilling of a well within a field or pool or within part of a field or pool or the operating of any well that, having regard to sound;

(c) engineering and economic principles, results or tends to result in a reduction in the quantity of petroleum ultimately recoverable from a pool;

(d) the drilling, equipping, completing, operating or producing of any well in a manner that causes or is likely to cause the unnecessary or excessive loss or destruction of petroleum after removal from the reservoir;

(e) the inefficient storage of petroleum above ground or underground;

(f) the production of petroleum in excess of available storage, transportation or marketing facilities;

(g) the escape or flaring of gas that could be economically recovered and processed or economically injected into an underground reservoir;

92. *Nova Scotia Accord Act*, *supra* note 2, s. 178(1); *Newfoundland Accord Act*, *supra* note 1, s. 173(1).
or

(h) the failure to use suitable artificial, secondary or supplementary recovery methods in a pool when it appears that such methods would result in increasing the quantity of petroleum ultimately recoverable under sound engineering and economic principles. 93

In the third category of unitization under the Accord Acts, the relevant Board may refer to the Committee an application for a unitization order by one or more working interest owners who are parties to a unit agreement and a unit operating agreement and own in the aggregate sixty-five per cent or more of the working interests in a unit area. 94 The Committee is required to hold a hearing at which all interested persons have an opportunity to be heard and, if the unitization order would accomplish the more efficient or more economical production of petroleum from the unitized zone (and the other requirements of the Accord Act are met), the Committee may order that the unit agreement be binding on all working interest and royalty owners in the unit area and that the unit operating agreement be binding on all working interest holders in the unit area. Under the COGOA, the NEB has no such jurisdiction. 95 If there is no waste, the NEB and the Chief Conservation Officer appointed by the NEB cannot compel unitization.

Despite the ability of the Boards to require unitization agreements on this additional ground, the Accord Acts do not indicate that the Board should consider questions of equity and fairness between the parties when determining whether or not to issue a mandatory unitization order.

3. Special spacing units
Since normal drilling spacing units (DSUs) are not always appropriate to all reservoirs, most jurisdictions provide regulators with the ability to vary the size and configuration of DSUs. 96 As previously noted, a spacing unit under the Accord Acts is a malleable concept, essentially delimited by what the relevant Board determines it to be. This too may change if draft regulations are implemented.

93. Newfoundland Accord Act, supra note 1, s. 154(2); Nova Scotia Accord Act, supra note 2, s. 159(2).
94. Nova Scotia Accord Act, supra note 2, s. 179(1); Newfoundland Accord Act, supra note 1, s. 174(1).
95. Sections 39 through 47 of the COGOA, supra note 52, would allow the NEB to issue a unitization order if one or more working interest owners who are parties to a unit agreement and a unit operating agreement and own in the aggregate sixty-five per cent or more of the working interests in a unit area may applied for a unitization order with respect to the agreements. These sections remain unproclaimed.
96. See e.g., Oil and Gas Conservation Regulations, Alta. Reg. 151/1971, s. 4.040(3).
The draft *COGOA D&P Regulations* also contain a provision allowing the NEB to vary the area assigned to a spacing unit or target area:

9. The Board may vary the area assigned to a spacing unit or the size or shape of the target area if the Board is satisfied that:

(a) improved recovery will be obtained,

(b) additional wells are necessary to provide capacity to drain the pool at a rate that will not adversely affect the recovery from the pool,

(c) increased deliverability from a gas field is desirable,

(d) there is common ownership,

(e) recovery will be improved while not affecting the recovery of adjacent rights holders, or

(f) it is deemed necessary by the Board for the management or control of oil or gas production.\(^9\)

Importing a substantially similar clause into the *Accord Acts* would allow the Boards to maintain flexibility in offshore development, while dealing with issues of waste and correlative rights.

Because of the undefined nature of a spacing unit under the *Accord Acts*, it is not surprising that there are no applications to date for a special spacing unit. If the draft regulations are enacted, however, we may see special spacing unit applications in the future.

V. Third party access to facilities

A common concern in some parts of the oil and gas industry is that restricted, or unreasonable terms of, access of third parties to facilities may hamper development of offshore resources.

In Alberta, regulatory aspects of gas processing facilities, including the negotiation of processing terms between plant owners and third party producers and the construction of new facilities, are administered by the AEUB. The regulations reflect a policy of the Alberta government to avoid unnecessary duplication of facilities having regard to environmental and resource conservation concerns while at the same time providing for competitive development of the oil and gas industry. To ensure access to a facility for producers who do not have an interest in it, the AEUB may declare it to be a common facility. This means that facility owners or

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operators cannot discriminate in favour of one producer or owner of gas as against another in a particular gas pool, discriminate in favour of the owner’s own gas, or charge unreasonable prices for third party access.

The AEUB may, as part of the common processor procedure:

- regulate the total amount of gas to be processed from a particular pool;
- regulate the proportion of production capacity to be allocated to each owner or producer in a pool; and
- where the common processor and a person seeking to have its gas processed at the common processor’s facility cannot agree on price, the AEUB may fix a fair and reasonable price to be paid.

The availability of the common processor procedure and the potential for the AEUB to establish rates acts as a deterrent to the raising of rates or other exercises of market power by processors. Added to this is the fact that most producers must, at some point, seek access to other producers’ facilities, and so are inclined to be reasonable in the terms they set.

Under the Accord Acts, the terms of an operating licence or authorization for a facility used in the production, conservation, processing or transportation of petroleum in the offshore area, or the development plan approval for the overall development project itself, may include terms requiring that third party access to the relevant facilities, where excess capacity exists, be on reasonable terms and conditions. The Accord Acts themselves do not contain anything equivalent to the Alberta common processor provisions and again the Board would be faced with adding provisions for dealing with such matters in the form of conditions of authorizations or approvals the Board is empowered to give under the Accord Acts with respect to the project or facility in question.

A condition of the C-NSOPB approval for the Sable Offshore Energy Project (SOEP), for example, required third party access on “reasonable terms and conditions” which would allow the C-NSOPB, in the event of a dispute, to:

- determine if third party access is to be provided,

98. *Newfoundland Accord Act*, ss. 138 (operating licences and authorizations for work) and 139 (development plan approval); *Nova Scotia Accord Act*, ss. 142 (operating licences and authorizations for work) and 143 (development plan approval).
99. Ibid.
specify the proportion of production to be taken by the proponents, and
set pipeline tariffs and processing fees, and fix the delivery location.

In the case of the Hibernia Project, the proponents recognized from the outset the importance of facilities and logistics sharing. As stated on the project’s website:\textsuperscript{100}

\begin{itemize}
\item When Hibernia began construction in 1991, Newfoundland was a ‘greenfield’ site in petroleum industry terms, with very little supporting infrastructure in place. Hibernia has changed all that, through the development of:
\begin{itemize}
\item shorebase facilities
\item warehousing complex
\item heliport
\item transshipment terminal
\item training simulator
\end{itemize}
\end{itemize}

Much of this infrastructure can be utilized by future oil developments and will form the foundation for an east coast offshore oil and gas industry. By utilizing the “shared services” approach to industry support, there is the potential for considerable cost savings for all petroleum industry participants - Hibernia included. In fact, the Terra Nova development is already utilizing the heliport, warehouse and shorebase facilities developed for Hibernia, resulting in significant cost reductions for all parties.

One method of obtaining access to third party facilities is by contractual arrangements with the operator of the facilities. In the Gulf of Mexico, for example, much of the recent field development activity has to do with facilities and platform use and construction and there has been a trend of operators specifically designing development structures with sufficient excess capacity to handle future third party production.\textsuperscript{101}

In offshore Atlantic Canada, certain participants in the Hibernia and Terra Nova projects have entered into contractual arrangements with

\textsuperscript{100} Hibernia, online: <www.hibernia.ca/index2.html>.
respect to the use of marine tankers and storage facilities by both projects and of course the services of the Newfoundland Transshipment Limited (NTL) terminal and facilities at Whiffenhead are available to persons who enter into a reserved capacity service agreement with NTL. It is no doubt helpful that these projects and facilities have a number of common participants.

The Sable Offshore Energy Project began production in late 1999 and today is producing from five gas fields. A number of undeveloped discoveries in the Nova Scotia offshore are close enough to the SOEP infrastructure to be technically capable of being tied back to this infrastructure. They remain undeveloped because the parties holding interests that are the subject of these discoveries have yet to consider them economically viable.

While the C-NSOPB has expressed the view that the prospects for further gas developments in the Sable Island area are good, interest in exploring this area has been low in recent years with most explorers focussed on deepwater or carbonate plank opportunities. Like certain areas of the North Sea, Sable Island is now a mature area and its remaining potential may involve smaller discoveries. Interest owners discovering resources in the area must access third party infrastructure in order to make their projects viable. One view is that any new discovery in the Sable Island area, other than a major discovery, would have to use the SOEP infrastructure, including the onshore gas plant and fractionation facility, in order to be commercially viable.

In the case of Deep Panuke, the proponent sought regulatory approval for each of two configurations, one being a parallel pipeline to shore and the second a “hot tap” tie-in to the SOEP infrastructure. The justification advanced to the C-NSOPB/NEB review panel as to the need to evaluate both options was that the most economic of the two alternatives was not yet apparent (chiefly, but not exclusively, comparing construction to tariffs, rather than capacity constraints, in light of SOEP production declines).

Similar considerations apply to other areas offshore Atlanta Canada where interests relate to or overlap common reservoirs.

This is not a problem unique to the Canadian offshore. Throughout the North Sea there is potential for commercial tension between the owners of infrastructure and the owners of third party fields seeking access to that infrastructure. The U.K. has addressed this issue through both voluntary and compulsory legal frameworks for commercial arrangements for third

party access. If requested by a would-be user, the Secretary of State has powers, having considered the interests of all parties, to impose a solution to problems of pipeline sizing, connections or tariffs. However, these powers have not to date been exercised.\textsuperscript{103}

Similarly, the Australian \textit{National Third Party Access Code for Natural Gas Pipeline Systems}\textsuperscript{104} establishes a transparent regulatory process to set access terms and conditions for both transmission and distribution pipelines. The \textit{Code} also contains rules which establish which of these pipelines ought to be made subject to the \textit{Code}'s third party access provisions. Proposed reforms include a move to a "light-handed" regulatory approach consisting of price monitoring and the prospect of binding arbitration should a commercial arrangement appear unlikely.\textsuperscript{105}

Norway's \textit{Petroleum Act}\textsuperscript{106} and the \textit{Petroleum Regulation}\textsuperscript{107} also establish a third-party access regime upon demonstration of "reasonable need" (i.e., producing or trading in natural gas), subject to non-discriminatory conditions. Gassco, the statutory "independent system operator" oversees the access regime, which consists of rounds of spare capacity booking and a distribution formula.\textsuperscript{108}

As the industry continues to expand in the east coast offshore and fields mature and decline, access of third parties to facilities will become increasingly important. The experience to date has been generally positive, driven by economic exigencies, co-operative arrangements among producers and best development considerations rather than a desire to control or dominate aspects of facilities' usage. The "sharing" approach evidenced from the beginning of the Hibernia Project may be tested in the future with respect to different operator and project configurations and it will be interesting to see how the Boards are able to influence the resolution of disputes among commercial parties given the differences between the powers available to regulators such as the AEUB and what the Boards possess under the \textit{Accord Acts}.

\textsuperscript{104} National Third Party Access Code for Natural Gas Pipeline Systems 1998 (W.A.) Similar to the \textit{Accord Acts}, the "Code" is implemented in each Australian State and Territory by local legislation.
\textsuperscript{105} 2007 Offshore Acreage Release, Overview for Applicants, Gas Access Regulation in Australia, online: <http://www.mce.gov.au>.
\textsuperscript{106} Act 1996-11-29 no. 72 (Nor).
\textsuperscript{107} Regulations to Act Relating to Petroleum Activities (Royal Decree, 27 June 1997, last amended 22 December 2006) (Nor).
\textsuperscript{108} See Gassco Capacity Management, online: Gassco <www.gassco.no/SW3092.asp>.  
VI. Production flow testing

At the time the Accord Acts were initially enacted, the subsurface geology of the Scotian shelf and the Grand Banks was largely unknown. The Hebron, Ben Nevis, West Ben Nevis, Terra Nova and White Rose fields were relatively recent discoveries. The offshore petroleum drilling regulations that had been enacted were, in part, to assist in identifying the nature and scope of the offshore resources claimed by both the provinces and the federal government. They reflected the technology of the times. For example, when they were enacted, the Offshore Petroleum Drilling Newfoundland and Labrador Regulations under the Newfoundland Accord Act stated:

170. (1) Subject to subsection 170(2), every operator shall ensure that every formation in a well is sampled or tested to obtain fluid flow and reservoir pressure data from the formation where there is an indication that the result of such a sample or test will contribute substantially to the evaluation of the formation.

(2) For the purposes of subsection (1), every operator shall ensure that a formation flow test is conducted if fluid samples and productivity data are required and wireline formation samples do not provide sufficient information for the evaluation of the formation.

The flow testing regulations enacted under the Accord Acts mirrored the language found in s. 196(1) and (2) of the Canada Oil and Gas Drilling Regulations under the COGOA. The COGOA has been described as a largely prescriptive regime that specifies “what was to be done...how it was to be done, what would be inspected, and when it would be inspected, and who would conduct the inspection.” As the COGOA is the basis for this aspect of the Accord Acts, it is not surprising that the initial

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109. Hebron was discovered in 1981; Ben Nevis was discovered in 1980; White Rose was discovered in 1984; West Ben Nevis was discovered in 1985; Terra Nova was discovered in 1984. For a timeline of offshore development in Newfoundland and Labrador, see Key Events Chronology 1999 – 2012 online: Government of Newfoundland and Labrador <http://www.nr.gov.nl.ca/mines&en/industry/milestones.pdf>.

110. Offshore Petroleum Drilling Newfoundland and Labrador Regulations, Nfld. Reg. 748/96, s. 170; Nova Scotia Offshore Area Petroleum Drilling Regulations, N.S. Reg. 137/92, s. 171. It is understood that the practice of the Board under the Newfoundland and Labrador regulations has been to waive the requirement for a production flow test on exploration wells.

111. S.O.R./79-82.

provisions of the *Accord Acts* in this area are largely prescriptive by nature (despite the inconsistency of this approach with the purpose and intent of the *Accord Acts*, as articulated by the Supreme Court of Canada in *Mobil*). The difficulty with a prescriptive regime is that where the provisions are out of date, regulatory requirements can present barriers to the use of new and innovative technologies, and can create unnecessary costs for industry and regulators.

These regulations had the effect of removing much of an operator’s discretion as to the necessity and economics of flow testing each exploratory well encountering hydrocarbons. For example, the Joint Guidelines Respecting Data Acquisition and Reporting For Well, Pool and Field Evaluations in the Newfoundland and Nova Scotia Offshore Areas stated that the “Board requires that the operator conduct a formation flow test where hydrocarbons are encountered within a sufficient thickness of porous and permeable reservoir rock for the purpose of acquiring representative fluid samples and pressure data to determine the in situ flow characteristics of the reservoir.”\[^{113}\] It is understood that these guidelines have been treated by the Board as equivalent to regulations, rather than just one way to achieve the test objective, and some view this as having made the testing requirements even more rigid than what would seem to be required under the *Accord Act*. Wherever operators encountered a hydrocarbon formation with sufficient pressure and size to complete a flow test, they were expected to complete such flow test based on these guidelines.

A flow test allows the hydrocarbons in a specific section of the rock to flow into the well bore and up the drill pipe towards the surface.\[^{114}\] Fluctuations of the pressure in the reservoir as it depletes permit the reservoir engineer to determine the type of fluid in the reservoir, reservoir parameters such as permeability, connectivity, communication, compartmentalization, etc., and, in many cases, the areal extent of the hydrocarbon accumulation. This information is critical in determining the size of the oil or gas accumulation and the rate at which it can be produced. At the time the *Accord Acts* were enacted, a flow test was the only method by which such information could be reliably gathered.

The flow test itself requires the use of specialized equipment that must be attached to the bottom of the drill pipe and lowered into the well to the

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\[^{114}\] For a more in-depth discussion of the technical aspects of flow testing, see *Regulations Amending the Nova Scotia Offshore Petroleum Drilling Regulations*, C. Gaz. 2006.1.832.
desired depth. The particulars of a flow test are dependent upon many things, including the type of rock to be tested, the depth, and potential reservoir pressures and temperatures. Depending on the complexity of the well bore and the reservoir, designing a test represents a significant investment of time and capital. It is not unusual for an operator to plan for three to four months prior to undertaking a flow test on a standard offshore well. A deepwater or high-pressure well can require more than a year of planning.

A flow test may take more than thirty days to conduct. Workers must remove the drill pipe from the well bore, install and perforate a production liner, attach and calibrate testing tools, and put the drill pipe back down the hole. The zone to be tested is allowed to flow for a minimum of 8 hours and then closed in to allow reservoir pressure to re-build. This process may be repeated several times. During the period, the operator will be responsible for the cost of the floating platforms and any other vessels required to store and transport hydrocarbons the test may produce, as well as the consequence of any inadvertent spills during flaring operations.

As operations move into more complex and technically challenging areas, costs associated with flow tests become so high that mandatory flow test requirements may actually reduce or inhibit exploration activity. The estimated cost of conducting an offshore formation flow test ranges from $10 million to $30 million, depending on the type of rig, water depth, and reservoir depth. This is a significant expense and often simply serves to increase costs when the test fails to demonstrate hydrocarbons in commercially viable amounts. Exploring for oil and gas in a subsea environment is an expensive and ‘high risk’ (in the commercial sense) business. The chance of finding hydrocarbons, even after seismic work has been completed, is in the range of one in ten. Finding resources in commercial quantities is even less likely. Accordingly, offshore industry participants have long believed that the decision to conduct a flow test should be at the discretion of the operator, based on its assessment of the overall risks and benefits.

115. As the offshore industry matures, exploration activities are moving from the Laurentian Shelf and Scotian Shelf into much deeper water. The Terra Nova field lies in roughly 100 metres of water. Current exploration is taking place at depths of greater than 1,000 metres.
117. Supra note 114.
The twenty years since the enactment of the Accord Acts have brought substantial technological advances in well testing. Basic well information may be obtained through mud logging, logging while drilling and wireline testing. In a wireline test, equipment is lowered into a well on a wire, allowing for a small fluid sample to be taken. The test also provides a reading of the reservoir pressure. It is a much quicker and less costly procedure than flow testing but still provides useful basic reservoir information. Although the test is not at all novel, advances in technology have enabled wireline testing to gather more complete and accurate data than at the time the Accord Acts were enacted.

The most definitive way to test the production potential of a well is still to conduct a flow test. Accordingly, legislation requires that an operator undertake a comprehensive flow test in order to obtain a declaration of significant discovery, without which further development is prohibited.¹¹⁸

Production flow tests are an example of the challenges of adapting legislation to reflect changes in technology. In 2005, the Atlantic Energy Roundtable (AER) recognized that “Canada’s regulations for the offshore industry would benefit from updating and modernizing.”¹¹⁹

Performance-based regulation (smart, or goal-oriented regulation, as discussed previously in Section II and later in Section IX), establishes “standards which specify measurable outcomes or performance goals, leaving the means of achieving those outcomes or goals largely to the discretion of the regulated firm or entity.”¹²⁰ Underlying this theory is the idea that operators are in a better position to understand and employ economically-sound new technologies than are government agencies.

¹¹⁸ Section 47(n) of the Newfoundland Accord Act states: “‘significant discovery’ means a discovery indicated by the 1st well on a geological feature that demonstrates by flow testing the existence of hydrocarbons in that feature and, having regard to geological and engineering factors, suggests the existence of an accumulation of hydrocarbons that has potential for sustained production.” [emphasis added]


There has been some movement, particularly in the Canadian offshore, towards performance-based regulation. In 2005, after research to identify international and national practice, including the NEB’s experience with goal-oriented regulation, AER participants encouraged governments to establish a plan to renew the offshore regulations.

In the past two years, draft offshore drilling regulations in both Nova Scotia and Newfoundland and Labrador have been circulated, apparently with a view to granting greater discretion to operators on formation testing. The draft regulations state:

56. The operator shall ensure that every formation in a well is tested and sampled in a manner to obtain reservoir pressure data and fluid samples from the formation, if there is an indication that such data or samples would contribute substantially to the geological and reservoir evaluation.

The broader wording in the draft regulations has removed the prescriptive instruction in its predecessor as to when an operator must conduct a formation flow test. The new provisions would appear to give an operator more discretion to decide what testing is required; however, past experience has shown that the regulations are further supplemented by guidelines and guidance notes that may increase the prescriptiveness of the regulations. The revised guidelines associated with the drilling regulations have not yet been circulated and are needed to determine if greater discretion will in fact be achieved under the new regulations.

This seeming change in the flow testing requirements would be consistent with the intention of updating the regulations and moving towards a performance based regulation. Whereas industry participants have previously been instructed to flow test every exploration well as a method of reservoir evaluation, such participants will likely be granted

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121. The Report of the Implementation Committee, supra note 119, indicates the following schedules for implementation of the updated regulatory framework: Diving, September 2005; Submerged Pipelines, end 2006; Drilling regulation amendment (well costs), 2005; Drilling and Production, end 2006; Geophysical, 2006 (start 2005); Installations/Certificate of Fitness, 2008 (start 2006); Occupational Health and Safety, 2009 (start 2006). To date, none of these regulations have been fully implemented. See also supra note 49.

122. The flow test portion of the draft regulation reflects the current state of the flow test regulations under the Accord Acts following amendments in 2006. The flow test portion of the existing regulations was amended in 2006 by N.L.R. 102/06 in Newfoundland and Labrador and by N.S. Reg. 165/2006 in Nova Scotia.

more discretion in their work, only requiring the expensive and time consuming flow tests prior to being issued a significant discovery license. Hopefully the wording of the requirements, in conjunction with relevant guidelines, will be consistent with this approach.

VII. Private royalty agreements

A private royalty agreement is a project specific royalty arrangement between a provincial government and the project proponents that is entered into by the parties to it as a binding contractual commitment. Prior to 1997, private royalty agreements were entered into between the Alberta government and parties holding oil sands interests, but that practice was replaced in 1997 with a generic oil sands royalty. Both Accord Act regimes provide for private royalty agreements in the provincial oil and gas legislation that is used to authorize the regulations that impose the royalty under the respective Accord Act. There are currently four sets of private royalty agreements in relation to offshore Atlantic Canada: Hibernia in Newfoundland and Labrador, Sable Island (where there are actually five separate royalty agreements regarding the Sable Offshore Energy Project), Deep Panuke and Cohasset in Nova Scotia. There were extensive negotiations on a private royalty agreement for Terra Nova but this was superseded by a royalty imposed by regulations enacted by Newfoundland and Labrador.

At least one commentator has suggested that provincial royalty agreements will continue to be required, given the risks, conservative approach, pro-government nature and limited scope of a generic royalty regime, and the need for proponents of major developments to have particular issues and risks dealt with in a binding way outside the generic regime. Confirmation of this view is evidenced by the fact that Nova Scotia has implemented, as part of its public policy, an Energy Strategy, one of the features of which is Offshore Strategic Agreements to be entered into by the Province with proponents of offshore project developments to reflect the Province’s expectations in developing the offshore in light of

124. Supra note 58. For a thoughtful and provocative discussion of the subject of royalty agreements for East Coast offshore oil and gas, see Alan T. Pettie, "Are Royalty Agreements Required for Canada East Coast Offshore Oil and Gas?" (2001) 24 Dal. L.J. 151.

125. There are still some private royalty agreements extant in the Alberta oil sands but it is very difficult to obtain information about these.


127. See Pettie, supra note 124 at note 130.

128. See Thrasher, supra note 126 at 367-71.

129. See Pettie, supra note 124 at 196-97 and at 212-13.
market conditions facing proposed developments. The Deep Panuke Offshore Strategic Energy Agreement between EnCana and the Province is a recent example of such an agreement. The OSEA sets forth, among other things, EnCana's royalty and benefit commitments in respect of the project and includes the following provision in respect of the royalty commitments of the Province:

4.2 Amendments made to the Regulations after the date of this Agreement will not affect the provisions described herein or the royalties payable by EnCana, or the calculation thereof, or any amounts provided for in this Agreement, subject to the ability of the Minister to enact technical amendments to the Regulations (not relating to market conditions or prices) to close loopholes that are contrary to the combined intent of the provisions of this Agreement and the Regulations and result in the royalty payable by EnCana being materially reduced.

The advantage of a provision such as this in a royalty agreement with a province is that, unlike the situation with benefit plans, the provinces do in fact have the authority under the Accord Acts to set the terms of the royalties applicable to projects in the relevant offshore areas.

One of the peculiar characteristics of a contract with a provincial government (or indeed the federal government) in Canada arises from the doctrine that the power of Parliament and of the provincial legislatures to legislate cannot be fettered by contract. This doctrine was confirmed by the Supreme Court of Canada in Reference re: Canada Assistance Plan (B.C.). In that case, it was argued that because of a prior agreement with the Province of British Columbia, the Government of Canada was precluded from introducing into Parliament certain amendments to the Canada Assistance Plan, unless they were consented to by the B.C. provincial government. The prior agreement with the Province, it was alleged, gave rise to a legitimate expectation that changes to the federal Act which operated to the disadvantage of British Columbia would not be introduced without prior consent by the Government of that Province.

In rejecting this argument, Sopinka J., writing for the Court, adopted the following statement from an Australian Court:

Ministers of State cannot, however, by means of contractual obligations entered into on behalf of the State fetter their own freedom, or the freedom

132. Ibid.
of their successors or the freedom of other members of Parliament, to propose, consider and, if they think fit, vote for laws, even laws which are inconsistent with the contractual obligations.

Sopinka J. went on to add that a restraint on the power of the executive to introduce legislation into Parliament would be a fetter on the sovereignty of Parliament itself. The doctrine stated in Reference re: Canada Assistance Plan appears to apply to the provincial legislatures as well as to Parliament.

The ability of a Canadian federal or provincial government to unilaterally alter the terms of a contract with another party, however, does not mean the party is without remedy. There remains an issue as to whether the government that is party to the contract may be liable for damages for breach of contract in such circumstances. Holding the government liable for such damages arguably does not fetter legislative sovereignty, as it does not constrain the power of the government to legislate.

A recent decision of the Supreme Court of Canada suggests that a federal or provincial government may be held liable for damages if it breached a private contract. In Wells v. Newfoundland the plaintiff had been appointed by the Government of Newfoundland as a member of the Public Utilities Board to hold office to the age of seventy during good behaviour. These terms were in accordance with the legislation then in force. Four years later, the Government enacted new legislation, restructuring the Board and abolishing the plaintiff’s position. The plaintiff brought an action for damages for breach of a contract of employment with the Crown. The plaintiff’s claim was upheld by the Supreme Court of Canada. The Court concluded that the plaintiff’s terms of appointment constituted a contract of employment with the Crown, and that this contract had been breached by the Government’s abolition of the plaintiff’s position. The fact that the breach of contract had been brought about by legislation did not excuse the Government from liability for damages in the absence of an express provision in the legislation insulating the Crown from such liability. In reaching this conclusion, the Court stated:

there is no question that the Government of Newfoundland had the authority to restructure or eliminate the Board. There is a crucial distinction, however, between the Crown legislatively avoiding a

135. Supra note 133 at para. 65, citing West Lakes Ltd. v. South Australia (1980), 25 S.A.S.R. 389 at 390 (Supreme Court of South Australia).


contract and altogether escaping the legal consequences of doing so. While the legislature may have the extraordinary power of passing a law to specifically deny compensation to an aggrieved individual with whom it has broken an agreement, clear and explicit statutory language would be required to extinguish rights previously conferred on that party.

...In a nation governed by the rule of law, we assume that the government will honour its obligations unless it explicitly exercises its power not to. In the absence of a clear express intent to abrogate rights and obligations – rights of the highest importance to the individual – those rights remain in force. To argue the opposite is to say that the government is bound only by its whim, not its word. In Canada this is unacceptable, and does not accord with the nation’s understanding of the relationship between the state and its citizens.

Reilly should be taken as turning on the interpretation given to the specific statute of abolition. To the extent it is relied upon for the proposition that the Crown can implicitly avoid its contractual obligations by indirectly legislating a breach, it is no longer the law in Canada.\(^{138}\)

The Hibernia experience has demonstrated how the parties to a private royalty agreement under one of the Accord Acts have handled issues arising under the agreement. Taking more than two years to negotiate, the Hibernia royalty agreement represented a significant commitment of resources on the part of both the proponents and the province.

On 17 February 2000, the C-NLOPB approved a request from Hibernia Management and Development Corporation (HMDC), the operator of Hibernia, to increase the facility maximum daily production rate from the previous limit of 150,000 barrels a day to 180,000 barrels a day immediately, and to further increase it to 200,000 barrels a day following the completion and testing of equipment modifications in March of that year. The HMDC proposal also sought an increase in the annual production limit from the then-current level of 50 million barrels to 66 million barrels.\(^{139}\) As the decision to increase the rate of depletion of the Hibernia field was a fundamental decision and as such required the approval of the Provincial Minister and the Federal Minister, the C-NLOPB provided notice of its decision to the federal and provincial energy ministers. The government of Newfoundland and Labrador did not approve the decision. Minister of Mines and Energy, Paul Dicks, released a statement saying that had the government approved the application, “more oil would have been taken

\(^{138}\) Ibid. at paras. 41, 46-47, citing Reilly v. The King, [1934] A.C. 176 (P.C.).

from the field at a lower royalty rate. Over the life of the project, this would have negatively impacted royalties to the province.” 

While the government of Newfoundland and Labrador expressly stated that its goal was not to reopen the Hibernia royalty agreement, its subsequent actions clearly effected a different result than would have obtained under the royalty agreement. The Hibernia royalty agreement provided for a gross royalty of one percent to be increased by increments of one percent every eighteen months to a maximum of five percent. The increase in gross royalties under the royalty agreement was tied only to the passage of time. The Province's position was that the ability to produce more oil earlier represented a real saving to the consortium, as it would be able to produce greater amounts of petroleum at a lower royalty rate.

Following negotiations between the parties, the Newfoundland Department of Mines and Energy announced an add-on to the existing royalty regime whereby the consortium would pay the province higher royalty rates earlier in the term and the gross royalty rates would reflect production levels, rather than just the passage of time. In the circumstances described in Hibernia, the opportunity for the provincial involvement and action arose because of the requirement, under the Newfoundland Accord Act, for approvals from the federal and provincial ministers in relation to a fundamental change.

Private royalty agreements will continue to be a feature of the Accord Acts, even with the advent of generic royalty regimes, given the size of offshore projects and the need for more certainty and specifics on key issues than can be obtained from a generic regime. It will be interesting to see how they develop in future.

VIII. Regulatory streamlining

The application and approval process for offshore developments has changed since the early days of Hibernia environmental and regulatory approval. The Boards have an important environmental mandate with respect to offshore oil and gas, in that they must (i) monitor environmental effects from operations, and (ii) ensure that an environmental assessment (EA) has taken place before authorizing a project.

Three broad changes have occurred to streamline the development application process. First, the Canadian Environmental Assessment Act[141] (CEEA) was amended in 2003 to designate a federal agency to enhance

coordination among regulators and reduce project delays.\textsuperscript{142} Second, in response to concerns that EAs were being coordinated in a less than optimal fashion, the federal cabinet issued a directive to regulators to better coordinate the \textit{CEAA} process.\textsuperscript{143} Finally, a number of local and more discrete efforts have been undertaken by the Boards to encourage offshore development. The effect of these efforts is perhaps reflected by the Deep Panuke application by EnCana, initially begun in 2001 following the 1998 discovery of the pool, ultimately withdrawn and its subsequent more efficient revival in 2006/2007.

1. \textit{Environmental monitoring}

Environmental effects generally consist of noise, air and liquid emissions to the marine and terrestrial environments. Operational discharges take the form of produced water, drilling mud and cuttings, deck drainage and bilge water, all of which must conform to the Boards’ Waste Treatment Guidelines and Chemical Selections Guidelines, as applicable. Of note, s. 36(3) of the \textit{Fisheries Act}\textsuperscript{144} (regarding deleterious substances) also requires a discharge authorization from Fisheries and Oceans Canada, an authorization which Board conditions or guidelines cannot satisfy owing to their non-statutory status. An authorization in respect of the potential “alteration, disruption or destruction of fish habitat,” under section 35 of the \textit{Fisheries Act}, could create the same issue.

2. \textit{CEAA and the Accord Acts}

With respect to the environmental assessment of proposed developments, regulatory scrutiny of offshore projects is evolving towards more efficient regulation. Streamlining efforts have responded to criticism that overly onerous requirements discourage exploration.\textsuperscript{145} Despite the fact that the Boards were established to be the lead regulator of offshore project facility approvals, other federal and provincial regulators have impacted the “one window approach.” As one commentator succinctly points out, “the question arises, who is in charge?”\textsuperscript{146} Indeed, the difficulty of coordinating suites of regulators from three different jurisdictions (federal, provincial and joint) is reflected in a directive from the federal Cabinet to regulators

\textsuperscript{144} R.S.C. 1985, c. F-14.
\textsuperscript{146} Ibid. at 320.
with respect to the implementation of the CEAA and need for increased coordination and cooperation.

The basic model for assessing offshore development applications is a joint federal/provincial panel considering environmental, technical and socio-economic issues at a public hearing. Despite what may seem to be generic and comparable structures, the regulatory challenges a proponent faces will be significantly affected by the ultimate regulatory structure. The major contemporary approvals are SOEP, Terra Nova, White Rose, and both Deep Panuke processes. In between the two Deep Panuke processes were two events which subtly altered the functioning of the CEAA and thereby the hearing process.

First, the mandatory five-year review of the CEAA resulted in a number of amendments in 2003. Notable in these was a new requirement for a federal environmental assessment coordinator (FEAC). The CEA Agency assumes this role in the case of a Comprehensive Study Report (CSR) or joint review process. The FEAC role is to coordinate and enhance cooperation among review participants, including federal and provincial regulators as well as proponents and the public. It is to assist proponents with the EA process and ensure that regulators respect timelines and process commitments. It has been observed that, prior to establishing the FEAC role, regulations establishing environmental assessment timelines for federal regulators were poorly respected and that the FEAC role was a response.

Second, in 2005 the federal Cabinet issued the “Cabinet Directive on Implementing the Canadian Environmental Assessment Act” (the Directive), alluded to above. The Directive is to ensure “high quality environmental assessments in a predictable, certain and timely manner.” It establishes common principles for the content of a federal EA and clarifies the responsibility of ensuring the implementation of mitigation measures to prevent significant adverse effects. The Directive also ensures that senior officials become involved to ensure a coordinated federal process and identifies a leadership role for the CEA Agency in the EA process.

147. Supra note 141, s. 12.5.
148. Regulations Respecting the Coordination by Federal Authorities of Environmental Assessment Procedures and Requirements, SOR/97-181.
150. Supra note 143.
3. Past environmental assessments

It is instructive to consider the evolution of the various development project assessments to date. Five “Responsible Authorities” (RAs) were represented on the joint review panel which reviewed the SOEP project. The panel was appointed pursuant to an agreement between the Canadian Environmental Assessment Agency (CEA Agency), the NEB, Natural Resources Canada (NRCan), the Nova Scotia Ministries of Natural Resources and Environment (MNR), and the CNSOPB. The Terra Nova Memorandum of Understanding (MOU) between various regulators involved in the Project review similarly sought CEAA approval via a joint panel in conjunction with the RAs of Environment Canada, NRCan, Newfoundland Mines and Energy, and Newfoundland Environment and Labour.

The White Rose project is similar to the Terra Nova project, both in roughly equivalent depths of water and each employing a floating production storage and offloading (FPSO) vessel. The Minister of the Environment approved the White Rose comprehensive study report (CSR) (the initial drafting of which was delegated to the proponent) without referring it to a panel, as had been the case in Terra Nova.\(^5\) The public hearing under a Commissioner of the C-NLOPB began upon the release of the complete CSR and, while present in less detail, environmental issues still formed part of the public review process. The C-NLOPB approved White Rose, although unlike the Terra Nova decision, the C-NLOPB was unable to accept many of the Commissioner’s recommendations, often ruling that they were outside the Board’s jurisdiction.

Larger projects with the potential for significant adverse environmental effects may have to be assessed through a comprehensive study\(^5\) instead of a less-intensive screening.\(^5\) Pursuant to section 21 of the CEAA, a CSR results if a project, such as a production facility, is on the Comprehensive Study List Regulation (CSL).\(^5\) If so, the Responsible Authority must undertake public consultation with respect to the scope of the EA. Following public consultation, the RA must report to the Minister with respect to potential project effects, public concerns and the ability of a CSR to address project issues, culminating with a recommendation to refer the project to a mediator or review panel hearing, or continue the EA as a CSR.

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151. Referring a CSR to a review panel is a matter of Ministerial Discretion per s. 29 of the CEEA, supra note 134.
152. Supra note 141, s. 21.
153. Ibid. s. 18.
4. The Deep Panuke applications

The Deep Panuke EA also proceeded by way of a CSR instead of a full CEAA panel review. The regulatory process for the first Deep Panuke application commenced on 23 July 2001 with the filing of the Project Description with the CEA Agency. A “Memorandum of Understanding on Environmental Assessment Process For the Deep Panuke Project” was signed by a number of RAs on 17 December 2001 to coordinate the environmental reviews required by the C-NSOPB, NEB and CEAA processes (the RAs were the C-NSOPB, NEB, DFO, Environment Canada, Industry Canada, NRCan and the Nova Scotia Department of Environment and Labour). The MOU delegated to EnCana the preparation of a draft CSR with a written comment process. The MOU also established the C-NSOPB as the lead RA and provided that the final CSR would form part of the DPA filed by the Proponent to the C-NSOPB under the DPA approval process.

EnCana subsequently altered the Project Description for Deep Panuke and the CSR scoping document was amended accordingly in February, 2002. EnCana filed a draft CSR in conjunction with its DPA with the C-NSOPB and NEB on 1 March 2002. Following the filing of the draft CSR over 1,300 Information Requests (IRs) were submitted to EnCana in May 2002 on the part of six community groups and nine government departments and agencies, including the five RAs.155 In addition to the CSR environmental review, with respect to the project the C-NSOPB made several Project Clarification Requests between March and December 2002, requiring formal responses on the part of EnCana.

EnCana provided its response to the CSR IRs in September 2002, as well as an additional volume to the CSR to take into account the results of public consultation. The NEB and C-NSOPB requested further information from EnCana on 17 October 2002. EnCana filed the final CSR on 1 November 2002. The NEB and C-NSOPB issued a Draft Joint Direction on Procedures on 7 November 2002. An MOU was signed between the NEB and C-NSOPB in December 2002 to establish a coordinated public review of the project, whereby the two public hearing processes operated simultaneously before an appointee of each regulator. In recognition of the length of the process to that point, the Draft Joint Direction on Procedures initially only afforded EnCana one week in which to respond to IRs and deprived it of the right of reply in written evidence. This restriction was later removed.

In addition, finalizing the list of issues for the hearing generated confusion and concern among all parties with respect to the extent that environmental issues would be considered. While the scope of the review by the NEB and C-NSOPB was for those environmental matters not considered by the CSR,156 intervenor comments concerning the draft list of issues and IRs continued to raise the environment as an issue.157

On 14 February 2003 EnCana announced that it was seeking an adjournment to the process to change its project design and better understand the resource. While the uncertainty in respect of reserves was presaged by the Maritimes & Northeast Pipeline hearing,158 commentators have noted that EnCana had stopped the process “558 days into a process that contained no finish line”159 and that the “excessive regulatory burden... contributed mightily to Encana’s decision to shelve Deep Panuke.”160 The C-NSOPB recognized this itself, noting that “to date, the environmental assessments have placed an undue burden on the industry in preparing the assessments”161 and it would develop a “more efficient and cooperative review [process] pending a new application.”162

An MOU between Environment Canada, DFO, Transport Canada, NRCan, the NEB, the C-NSOPB and the Nova Scotia Department of Energy and Labour was signed on 19 February 2005, with the purpose of, inter alia, fostering regulatory cooperation and avoiding duplication.

EnCana drilled two new wells during the next three years and enhanced its reservoir simulations. In the summer of 2006 the Province of Nova Scotia announced that it and EnCana had negotiated the OSEA. On 28 August 2006, the CEA Agency announced that the previous regulators were responsible for recommending how a new project should proceed.

157. For example, the Ecology Action Coalition, Heartland Resources and the Province of New Brunswick were all concerned with environmental issues. Heartland Resources was concerned with compensation following environmental effects and the Province of New Brunswick also demanded that EnCana update the gas supply evidence from the M&NP pipeline hearing.
158. Gordon M. Nettleton, “Recent Regulatory and Legislative Developments of Interest to Oil and Gas Lawyers”(2004) 42 Alta. L. Rev. 247, noting the “step-down” shipping option available to EnCana in its gas shipper contract was a particular concern of the Board, and rather than justifying the need for the pipeline based on demonstrated basin supply, the Board looked at basin “prospectivity.”
EnCana reapplied to the NEB and C-NSOPB on 9 November 2006, with an updated DPA and EIS and having negotiated the OSEA with the Province. On the same day, the Minister of the Environment determined that the project should continue as a CSR, without a public hearing.

The updated CSR was released for public comment on 11 June 2007 and was unique in that it:

1. was informed by the joint report previously issued by the C-NSOPB and NEB members;
2. reflected only the differences resulting from project design changes; and
3. was authored by the C-NSOPB, the NEB, DFO, Transport Canada and Industry Canada with input from Environment Canada and NRCan.

The second hearing lasted only one week and on the whole was remarkably efficient as compared to the initial attempt. This is attributed, in part, to the role of the CEA Agency as the FEAC, ensuring that regulators respected timelines and remained in communication. There was also a smooth coordination of issues and proceedings between the NEB, C-NSOPB and Deep Panuke Secretariat. Additionally, at the hearing stage EnCana only sat a single skilled expert panel, rather than a series of topical panels, which streamlined the physical hearing process. It did, however, provoke complaints from some intervenors who expected the opportunity to cross-examine subsequent panels.

To provide a sense of the changed timelines, EnCana responded to government regulators' IRs on 12 January 2007, and to other parties' IRs on 19 January 2007, having had approximately two weeks to respond in each case (although the NEB also posed IRs in advance of the main suite of requests). Following the filing of reply evidence on 26 February 2007 the hearing began on 5 March 2007 and concluded on 9 March 2007. The second process contrasted strongly with the first attempt.

The joint environmental report was released on 11 April 2007 with both appointees concluding that, following mitigation, the project was unlikely to cause significant adverse environmental effects. The C-NSOPB commissioner issued her individual report on 8 May 2007, the most notable aspect of which being the rejection of the Benefits Plan portion of the application (as previously discussed). An additional concern was the end use of Deep Panuke’s volumes, which the C-NSOPB was recommended to investigate, relating to both climate change and local gas market concerns.
Finally, the NEB member issued his final report, also recommending the project, on 18 July 2007.

The second hearing benefited from well-understood issues, not only as a result of the first process and a previously-approved CSR, but from the precedent set by SOEP and other offshore projects. The panel and intervenors were familiar with both the hearing process and the considerations at play. The hearing process succeeded, in other words, in part because of its lack of novelty. In addition, cooperation and coordination between regulators allowed for reasonable timelines and an organized IR process. It is to be hoped that this spirit of cooperation, possibly resulting from the effects of the Cabinet Directive and FEAC role, will continue into any subsequent offshore development application hearings. Furthermore, early and active management of the process should ensure that delays in the schedule and appeal risks are minimized.

5. Other streamlining efforts

A number of other streamlining efforts have also been made recently. On 19 April 2007, the C-NSOPB announced a lower cost second tier exploration licence will come into effect in October 2007 with a term of between two and three years, aimed at encouraging offshore Nova Scotia exploration by no longer requiring up-front long-term commitments. A corollary to new exploration is a state-of-the-art data management system and revamped, regulatory competitive bids featuring packaged data to, in conjunction with lowered drilling costs and obligations, better circulate offshore geoscience information.

In addition, as of November 2005, following a change to the CSL, offshore oil and gas exploratory drilling projects are no longer subject to CSRs. Similarly, as mentioned above, the C-NSOPB, C-NLOPB, NEB and other federal and provincial authorities also entered into a MOU for coordinated environmental offshore regulations in early 2005. While this includes parallel processing of regulatory documents, including any EIS or DPAs, it is not yet a “one-window” approach.

Conclusion

Numerous issues have tested the arrangements under the Accord Acts over the past twenty years.

The Courts called upon to interpret these arrangements to date appear comfortable doing so in the spirit of the joint management regime and in dealing with the questions of legislative interpretation, scope and standards of judicial review, burdens of proof and evidentiary and decision-making requirements that have come before them. They have recognized, at the
highest levels, that a core purpose of the *Accord Acts* is to ensure a stable and fair management regime for industry.

The Boards have made efforts, where permitted by the *Accord Acts*, to clarify and supplement perceived gaps in the legislation and regulations through the use of guidelines and to give these force, in some cases, by making compliance with these guidelines conditions of their various approvals. Courts have recognized and generally been supportive of the Board's powers to do in a way that makes these efforts effective and of real consequence to the parties subject to them. The opportunity for such efforts of the Boards arises in part from the inability or unwillingness of the federal and provincial governments to properly address, through legislation and regulation (notwithstanding the long experience of other Canadian jurisdictions, such as Alberta, in dealing with similar issues) the gaps and inefficiencies in the applicable legislative and regulatory scheme. Unfortunately, the *Accord Acts* do not recognize a regulation-making authority on the part of the Boards, and do not give the Boards a proper suite of remedies to deal with failure of a party to observe the guidelines the Board has established.

The Board's powers with respect to benefits plans have been confirmed and earlier practices with respect to benefits plans are likely to be reconsidered in light of recent affirmations of the Boards' powers to monitor and modify the obligations arising under general statements of principle.

Changes in production testing methodologies and technological improvements in other areas of petroleum operations that have made the original approaches to some issues under the *Accord Acts* outdated or at least questionable have been addressed in some instances, such as production flow testing, although only after long delays and not in as effective a manner as one would prefer.

Third party access to facilities, an issue that has been addressed by project proponents and used as a basis for their planning from the beginning of major developments under the *Accord Acts*, may become more important as fields and basins mature and facilities costs and requirements increase and have been dealt with to date by a combination of private contractual arrangements, stand-alone facilities available to their owners and others on a service agreement basis, and through conditions of Board approvals. Again, the role of the Boards under the *Accord Acts* needs to be reviewed and considered in the light of regulatory practices and experiences in other jurisdictions dealing with similar issues.

Private royalty agreements, also a feature of major developments under the *Accord Acts* from the beginning, have continued to be utilized (and
respected by the parties to them) as a means of particularizing that aspect of the fiscal regime applicable to a particular project and in an attempt to improve the certainty of treatment in that area for proponents investing in major projects.

The approach to the regulatory regime shows some signs of changing in favour of a “smart” system and the process of streamlining review and hearing procedures continues and appears to be making good progress in some areas, as evidenced by the recent Deep Panuke hearings.

There remain, however, numerous instances where the Boards, proponents and governments have resorted to ad hoc solutions to what are really recurring or industry-wide issues. The system cries out for a coordinated, informed response from the ultimate rule-making authorities under the joint management regimes – the federal and provincial governments. Canadians have a world-class resource opportunity in the east coast offshore and have to date enjoyed world class projects to develop them. It is unfortunate that they suffer from an inadequate and incomplete system to regulate the complex activities necessary to develop these resources. It is even more unfortunate (and inexcusable) when other jurisdictions in Canada, though far from perfect, have already done, and have extensive experience under systems including many of the things necessary from a legal and regulatory standpoint to deal with the areas that go begging under the Accord Acts. The inaction of successive federal governments in the area is an embarrassment to all Canadians, not just to those who live in Atlantic Canada. Yet in the current political climate in Ottawa it is difficult to imagine an enthusiastic federal involvement in any effort to put things right. And in case of the joint management regime under the Accord Acts, it takes two to fix it.