



Ministry of
Natural Gas
Development

Petroleum and Natural Gas Permits

Consultation Paper

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1. INTRODUCTION

This paper is intended for the purpose of consultation only. The power to make a regulation rests entirely with the Lieutenant Governor in Council. No assurance is provided in this document with respect to whether a regulation will be made or as to its content.

The British Columbia Ministry of Natural Gas Development (Ministry) recently completed a review of the *Petroleum and Natural Gas Act (PNG Act)*. The review resulted in amendments to the *PNG Act* being passed as part of Bill 12, *Natural Gas Development Statutes Amendment Act, 2014*.

One goal of the amendments was to modernize the *PNG Act*, which was achieved in part by replacing some petroleum and natural gas permit provisions with power for the Lieutenant Governor in Council to make regulations respecting permits. Once the amendments are brought into force, the new power to create regulations will allow government to modernize the permit rules to better align with current exploration and development techniques. Having the detailed rules in a regulation rather than in the *PNG Act* will better enable future adjustments to the framework as circumstances change.

The purpose of this consultation paper is to:

- provide relevant background information,
- outline the Ministry's objectives for potential changes to the rules for permits, and
- solicit comments for consideration as part of the Ministry's analysis and to inform development of potential new regulations.

Discussion questions are posed throughout this paper and are also listed at the end of the paper. The discussion questions included in the paper serve to highlight areas where the Ministry believes that stakeholders may have important feedback; they are not intended to limit the scope for input during the consultation process.

The regulatory development process consists of six stages:

1. Scoping – identifying potential regulatory changes;
2. Ministry consultation paper – this paper outlines the Ministry's regulatory objectives;
3. Consultation – hearing from interested parties and the general public via responses to this consultation paper and other means as required;
4. Drafting – preparing legal language for consideration by the Minister and the Lieutenant Governor in Council (Cabinet);
5. Decision – by the Lieutenant Governor in Council on whether to make the regulatory changes; and
6. Implementation – informing all parties affected by the changes (government staff, companies, organizations and individuals) of the new regulatory requirements, enabling effective implementation if the Lieutenant Governor in Council decides to make the regulatory changes.

This paper makes reference to sections of the *PNG Act* as they existed at the time of writing. There are specific references to sections that are to be changed or repealed as part of Bill 12, *Natural Gas Development Statutes Amendment Act*, 2014. The sections are referenced as they are now – prior to the amendments in Bill 12 coming into force – for the purpose of explaining how permits have worked to date in the province. If there is a discrepancy between this paper and a statute or regulation being referenced, the statute or regulation should be taken as correct.

2. BACKGROUND INFORMATION

2.1 CONTEXT

Crown-owned petroleum and natural gas rights are granted through three forms of tenure under the *PNG Act*: permits, drilling licences and leases. Permits and drilling licences provide the exclusive right to do exploratory drilling for petroleum and natural gas; they are acquired by a successful bidder at a Crown sale. Leases are the only form of tenure that grant the right to produce petroleum and natural gas; they are acquired by a successful bidder at a Crown sale or issued from permits and drilling licences upon completion of the required exploratory work. Each form of tenure under the *PNG Act* grants rights to the subsurface resource only – any activity taking place must be permitted by the BC Oil and Gas Commission.

- For more information on petroleum and natural gas tenure in British Columbia, please see our website at www2.gov.bc.ca/gov/content/industry/natural-gas-oil/petroleum-natural-gas-tenure.
- The PNG Act and its regulations can be accessed on the BC Laws website at www.bclaws.ca.

In recent years, permits have rarely been requested for disposition at the monthly Crown petroleum and natural gas dispositions. The last permit issued through a Crown disposition was in 2006. One permit was requested in 2007 and received no bids. Four permits were requested in 2009 but were withdrawn from the disposition when the Ministry was informed by the requester that they were not going to bid on the permits. There are currently no active permits in the province.

In 2011 the Ministry issued a Discussion Paper on the Tenure Provisions of the *Petroleum and Natural Gas Act* and Regulations. Feedback from industry indicated that some of the restrictions on leases issued from permits conflict with development of unconventional resources. The framework for permits was developed many years ago before unconventional resource plays became the predominant source of natural gas production in British Columbia. The Ministry believes some of the permit provisions require amendments given the substantial changes in industry practices in recent years.

2.2 OBJECTIVES OF THE REVIEW

The Ministry's objective is to identify changes to the permit rules to better align with industry practices and the natural gas plays in British Columbia with the following principles in mind:

- viewing tenure as an element in a continuum of the exploration and development process, rather than as a discrete component;
- recognizing the close integration of tenure with the broader regulatory and royalty regimes;
- creating and maintaining a fair, efficient, effective and transparent process for management of tenure across the province;
- maintaining flexibility to address custom solutions for specific emerging play-types and developing technologies;
- ensuring the Crown, as the resource owner, receives a fair return for the value of the rights;
- ensuring industry receives an economically commensurate reward and recognition for risks taken;
- recognizing close linkages to environmental footprint and stakeholder considerations;
- recognizing the importance of First Nations considerations; and
- recognizing the relationship and responsibility industry and the Ministry have to the people of British Columbia.

2.3 PERMITS – EXISTING RULES

The purpose of permits is to enable exploration in relatively unknown areas. Permits are acquired through Crown disposition. They confer the exclusive right to apply under the *Oil and Gas Activities Act* to do exploratory drilling for natural gas, petroleum or both within a defined location (*PNG Act*, sec. 38 (1)). They carry annual exploration spending requirements (which can be met without drilling wells) and are, in part, convertible to lease.

2.3.1 Classes of Permits

Permits are issued as one of four classes: A, B, C, or D. The class of a permit is not determined by an administrative boundary, as with drilling licences and leases. Rather, the Ministry's Director of Petroleum Lands (a statutory position currently held by the Executive Director, Tenure and Geoscience Branch) classifies permits with regard for the comparative accessibility of the location and the terrain within the permit area. Permits classified as A are those with the highest level of accessibility and most traversable terrain, and permits classified as D must have at least three quarters of their area covered by water (*PNG Act*, sec. 42). For example, permits that were previously issued within the vicinity of the Rocky Mountains were issued as Class B permits.

2.3.2 Permit Terms and Rent

All permits have a term of one year. Beyond the initial one-year term, a permit may be renewed annually contingent on the completion of work requirements. Class A & B permits may be renewed annually up to four times (five-year term in total) and after this may be renewed for one year or less up to three times on approval by the Minister (possibility for an eight-year term in total). Class C & D permits may be renewed annually up to seven times (eight-year term in total) and, beyond this, may receive any number of ministerial approvals for a further renewal of one year or less (*PNG Act*, sec. 47). Permits have annual renewal, rather than a single multi-year term, to ensure that tenure holders are conducting exploration work and not just holding the lands.

The annual rental for a permit is \$1.05 a hectare for years one through five, and \$1.75 a hectare for the sixth and subsequent years (*PNG Act*, Fee, Rental and Work Requirement Regulation, sec. 3.1).

2.3.3 Permit Work Requirements

Permit holders earn the right to convert a portion of a permit to lease (which provides the right to produce natural gas and oil) by completing exploration work equal to a set monetary value. The class of a permit determines its annual work requirements. Work is defined in the *PNG Act* Fee, Rental and Work Requirement Regulation as geological work, geophysical exploration or exploratory drilling to the satisfaction of the Director of Petroleum Lands. Work requirements for each class of permit are listed in Table 1 below. In order to conduct work on a permit, the permit holder must apply for and receive the necessary authorizations from the BC Oil and Gas Commission.

TABLE 1 – ANNUAL WORK REQUIREMENTS FOR PERMITS (\$ PER HECTARE)¹

YEAR	CLASS A	CLASS B	CLASS C	CLASS D
1	\$1	\$1	\$1	\$0.50
2	\$2	\$1.50	\$1	\$0.50
3	\$4	\$3	\$2	\$1
4	\$5	\$4	\$2.50	\$2.50
5	\$5	\$4	\$3	\$3
6	\$7.50	\$6	\$5	\$5
7	\$15	\$10	\$7.50	\$7.50
8	\$20	\$15	\$7.50	\$7.50

¹ *PNG Act* Fee, Rental and Work Requirement Regulation, sec. 4

If a permit holder is unable to complete the work requirement for the year, they may pay an amount equal to the value of the work not done in order to have their permit renewed. Alternatively, they may undertake in writing to do the work required in the following year as long as they submit a deposit of money or securities with the application (*PNG Act*, sec. 44 (1)).

If a permit holder has conducted work in excess of what is required under the regulation, the excess work is applied to the work requirements for one or more of the three years immediately following the year in which the work was done (*PNG Act*, sec. 48). Alternatively, if a permit holder knows that they will be conducting excess work, they may apply to the Ministry to group the permit with other permits as long as the grouped permits are contiguous and the grouping does not exceed 30 blocks in area (750 gas spacing areas), or the other permits are within a radius of 80 km of the permit (*PNG Act*, sec. 46 (1)).

2.3.4 Leases Issued from Permits

Upon completion of a permit's associated work requirements, a portion of a permit may be converted to lease, which allows production of natural gas and oil. A lease issued from a permit has several location restrictions. These are:

- The lease cannot cover more than half the area of the permit and must be within the boundaries of the permit location (*PNG Act*, sec. 52 (1)).
- The shape of a lease issued from a permit must have four boundaries and the dimensions must be 2x2, 2x4, 4x4, 4x6, 4x8 or 6x6 units. If it is not possible for a tenure holder to select a lease under these dimension restrictions, a lease of a different shape may be granted but must not exceed fifty percent of the size of the permit it is selected from (*PNG Act*, sec. 55 (1)).
- The lease must coincide with the boundaries of natural gas well spacing areas (*PNG Act*, sec. 55 (2)).
- Two or more leases issued from the same permit can be located corner to corner only or must be separated from each other by at least two units (*PNG Act*, sec. 55 (3)).

2.3.5 Comparison to Drilling Licences

The other form of exploratory tenure under the *PNG Act* is a drilling licence. While drilling licences are also intended for exploration, they are better suited to areas where more geological characteristics are known. Drilling licences reward the drilling of wells, which can be more costly than other exploration techniques; however, drilling licences offer more flexibility in terms of conversion to lease, which is the only form of tenure that allows production.

Table 2 compares the restrictions on leases issued from permits to the restrictions on leases issued from drilling licences.

TABLE 2 – LEASES ISSUED FROM PERMITS VS. DRILLING LICENCES

	Leases issued from Permits ²	Leases issued from Drilling Licences ³
The lease must coincide with the boundaries of the natural gas spacing areas	Yes	Yes
The lease must fall within the boundaries of the existing tenure location	Yes	Yes
The lease cannot cover more than 50% of the area of the existing tenure	Yes	Entire licence convertible if licensee has enough earnings
The shape of the lease must meet specific restrictions	Yes	No
Two or more leases issued from the same tenure must be located corner to corner or separated by at least two units	Yes	No – leases can be contiguous

3. MINISTRY INTENTIONS

3.1 SCOPE

The Ministry intends to limit the review of the rules for permits to the aspects of permits that can be addressed through regulations under the *PNG Act* or through Ministry policy. As such, the review will focus on the following aspects of permits:

- monetary value of work requirements,
- rental rates,
- penalty for late application to renew or convert to lease, and
- rules for leases issued from permits.

The Ministry intends for permits to remain a form of tenure that is most useful in frontier or exploratory areas with relatively unknown geology.

Discussion Question: With some modifications to the rules for permits, do you see the potential for permits to be a useful form of tenure in relatively unknown areas of the province? Why or why not?

² See section 2.3.4 Leases Issued from Permits (above)

³ Petroleum and Natural Gas Drilling Licence Regulation, sec. 4

3.2 CONFIGURATION OF LEASES

Based on previous feedback from industry and internal analysis, the Ministry understands that the most significant issues with permits are the restrictions on leases issued from permits. Specifically, the restrictions on dimensions and the requirement that multiple leases meet only corner to corner conflict with normal development practices for unconventional resources. Development of unconventional resources requires contiguous areas of land to allow for drilling of long, horizontal wells – allowing larger volumes of resource to be accessed with a smaller surface footprint. The current lease configuration restrictions can make such development on leases selected from permits impractical or impossible. The Ministry intends to propose more flexibility for the configuration of leases issued from permits; however, the Ministry has not yet determined what form that flexibility should take.

Discussion Question: Should the restrictions on lease dimensions be modified? Why or why not?

Discussion Question: Should the restrictions on the configuration of multiple leases be modified? Why or why not?

Discussion Question: In your opinion, would modifying or removing the restrictions on lease configuration be sufficient to address the conflicts between permits and development of unconventional resources? Why or why not?

3.3 REQUIREMENT TO SURRENDER A PORTION OF LOCATION

The Ministry also understands there are some industry concerns regarding the requirement to surrender half of the location of a permit when converting to lease. Any requirements to surrender a portion of a permit should be considered in conjunction with several factors, including:

- the cost of acquiring and maintaining a permit,
- the value and difficulty of the work requirements,
- industry's need to receive an economically commensurate reward and recognition for risks taken ("risk/reward"), and
- the Province's need to earn a fair return for the value of rights, which may be unknown at the time of tenure issuance when tenure is issued in a relatively unknown area.

Discussion question: Do you think it is reasonable to require tenure holders to surrender fifty percent of the location of a permit upon conversion to lease? Why or why not?

Discussion Question: In your opinion, would it be reasonable to require tenure holders to surrender a different amount of the location of a permit? Why or why not?

3.4 RENTAL RATES AND OTHER AMOUNTS

The Ministry will also be considering whether any amounts under the regulations should be changed, such as rental rates, penalty amounts and the monetary value of work requirements; however, the Ministry does not have any particular intentions to change these amounts at this time. These amounts will be reviewed in conjunction with any other potential changes to the regulations.

Discussion Question: Do you think the monetary values of the work requirements are reasonable? Why or why not?

Discussion Question: If the restrictions on leases issued from permits were relaxed, would it be reasonable to increase the monetary value of work requirements? Why or why not?

Discussion Question: Do you think the rental rates for permits are reasonable? Why or why not?

Discussion Question: If the restrictions on leases issued from permits were relaxed, would it be reasonable to increase rental rates? Why or why not?

4. DISCUSSION QUESTIONS

1. With some modifications to the rules for permits, do you see the potential for permits to be a useful form of tenure in relatively unknown areas of the province? Why or why not?
2. Should the restrictions on lease dimensions be modified? Why or why not?
3. Should the restrictions on the configuration of multiple leases be modified? Why or why not?
4. In your opinion, would modifying or removing the restrictions on lease configuration be sufficient to address the conflicts between permits and development of unconventional resources? Why or why not?
5. Do you think it is reasonable to require tenure holders to surrender fifty percent of the location of a permit upon conversion to lease? Why or why not?
6. In your opinion, would it be reasonable to require tenure holders to surrender a different amount of the location of a permit? Why or why not?
7. Do you think the monetary values of the work requirements are reasonable? Why or why not?
8. If the restrictions on leases issued from permits were relaxed, would it be reasonable to increase the monetary value of work requirements? Why or why not?

9. Do you think the rental rates for permits are reasonable? Why or why not?
10. If the restrictions on leases issued from permits were relaxed, would it be reasonable to increase rental rates? Why or why not?

5. PROVIDING COMMENTS

Responses to this Consultation Paper are being solicited until May 31, 2016.

The discussion questions included in this paper are designed to gather input on key points that will guide the Ministry's analysis of the rules for permits. The discussion questions are not intended to limit the scope of consultation and comments on all aspects of petroleum and natural gas permits are welcome.

Comments received will be treated confidentially by Ministry staff; however, please note that comments you provide and information that identifies you as the source of these comments may be publicly available if a Freedom of Information (FOI) request is made under the *Freedom of Information and Privacy Protection Act*. Each FOI request will be evaluated, and consultations with the providers of comments would occur before any information is released.

This consultation paper can be accessed at www2.gov.bc.ca/gov/content/industry/natural-gas-oil/petroleum-natural-gas-tenure/publications.

Interested parties are invited to submit comments to the Director, Pricing, Tenure and Royalty Policy.

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Thank you for your time and consideration.