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INTRODUCTION

This is Lawson Lundell LLP's quarterly Energy Law Newsletter. Written and edited by Lawson Lundell lawyers who practice in the energy sector, it aims to keep readers informed of significant regulatory developments in the energy sectors in Alberta, British Columbia and the North. For information about Lawson Lundell or its energy law practice, please contact Chris Sanderson at 604.631.9183. For information regarding this newsletter call Jeff Christian at 604.631.9115. You can also visit our website at www.lawsonlundell.com.

NATIONAL

The Kyoto Protocol Comes Into Force

The Kyoto Protocol to the United Nations Framework Convention on Climate Change (the "Protocol") comes into force on February 16, 2005. With the entry into force of the Protocol, Canada is required to report, by January 1, 2006, on progress and to demonstrate progress in achieving its commitments under the Protocol.

The Protocol requires that Canada reduce its emissions on greenhouse gases (GHGs) to 6% below its 1990 emissions, as averaged over the five years of 2008 to 2012 inclusive. However, Canada's GHG emissions are estimated to have increased by 20% to 30% over 1990 levels. The federal government's 2002 Climate Change Plan for Canada

included reduction targets, flexibility mechanisms, and complimentary measures. Legislation has already come into force requiring large final emitters to report their GHG emissions (see our April 2004 Environmental Law Newsletter). Large industrial emitters include emitters over specified levels of GHGs in the following sectors: upstream and downstream oil and gas; electricity generation; mining; and manufacturing, such as cement plants and iron and steel mills. Covenants are planned, and have been agreed to in some cases, to modify or replace regulation. Emissions trading would to some extent be available as credit against emissions over permitted levels.

The federal government has initiated a review of its Climate Change Plan for Canada. The review includes a study by the House Standing Committee on Environment and Sustainable Development (the "Committee"). An outline for the study was published in November 2004. The outline suggests reviewing the current situation, achieving a lower carbon energy supply, reducing demand, and developing the appropriate policy regime, particularly through fiscal mechanisms. As part of the latter, the Minister of Finance recently appeared before the Committee and stated the February 23rd budget would include new money for Kyoto implementation and tax changes, as well as investment in GHG emission reduction projects in other countries.

NEB Cost Recovery Regulations (Electricity)

The National Energy Board (NEB) is currently reviewing its cost recovery regulations as they relate to the electricity industry. An all day workshop was held on December 9, 2004 in Calgary to exchange views and ideas. A focus of participant interest was the historic practice of recovering the NEB's electricity related costs from exporters, on a volume basis. In light of the separation in most jurisdictions between the market participants and the transmission owners and operators, and the ongoing benefit the latter get from the existing international tie lines, a key concern for some participants was the fairness of the historical allocation. A particular irritant for electricity exporters has been the cost of the Sumas Energy 2 international transmission line hearing, which ran into the millions of dollars and was largely borne by electricity exporters even though the line would have been used for imports only (see our Spring 2004 Energy Law Newsletter for further information about Sumas Energy 2). The proposed solution to this problem, presented by the Canadian Electricity Association and Manitoba Hydro, is that the owners of international power lines ought to bear the non application costs of the NEB relating to electricity matters. Such a solution would, it was said, be stable, simple to administer, and more fairly allocate costs. Since the December workshop, the NEB has issued a request for further suggestions on cost recovery models

(to be submitted by March 14, 2005), and has announced a further industry meeting.

ALBERTA

Gas Over Bitumen Royalty Relief Announced

Effective December 2004, Alberta Crown royalty invoices are being adjusted for Athabasca oilsands natural gas producers whose gas has been shut-in to protect underlying bitumen. As previously reported in our newsletters, the Alberta Energy and Utilities Board (AEUB) shut-in 1021 Wabiskaw-McMurray natural gas wells on an interim basis effective July 1, 2004 to address the risk posed to the ultimate recovery of bitumen in the area. The Alberta Government has announced a 10-year royalty program that will result in reduced royalties for operators of completed gas wells which have been denied the right to produce. Retroactive to the date of shut-in, royalty adjustments are scheduled to end 10 years after continuous shut-in, or when the well is allowed to come back on production, whichever occurs first. If the wells ever come back on production, producers will be required to repay the deferred royalty amount. Such repayment will take the form of an increase in royalty over and above the normally applicable royalty rate, established at 1% of production for each year of shut-in, to a maximum of 10%. Such incremental royalties owed to the Crown upon the return to production would be limited to amounts recovered by a gas well

operator through the reduced royalty. The final hearing to confirm the production status of the impacted wells is expected to proceed in Spring 2005.

AEUB Hears Application for Six-Well Critical Sour Gas Project

Compton Petroleum Corporation ("Compton") has applied to the AEUB for licences to drill six horizontal level-2 critical sour gas wells from a single well pad located 1.1 km east of the Calgary city limits. Each well would have a hydrogen sulphide content of approximately 35.6%. In addition to the well licence and associated facility applications, Compton has also applied for a reduction in the Emergency Planning Zone (EPZ) for both the drilling and completion operations for the wells. Based on the calculated hydrogen sulphide release rates, the calculated EPZ for drilling operations is 11.94 km, and 14.97 km for completion and servicing operations. Compton has applied for a reduced EPZ with a radius of 4 km. Without a reduction in the EPZ, Compton would be responsible for evacuating some 250,000 city residents in the case of an emergency. There is existing sour gas development in and near the lease where Compton's proposed wells would be drilled. At the current rate of recovery, the existing wells could continue to produce for over 50 years. Through this project, Compton is seeking to accelerate depletion of the reserves to 15 years. The Board hearing into the matter started January 11, 2004 and is expected to



run 5 weeks. It is anticipated that a decision in the matter will be issued later this Spring.

Alberta Court of Appeal Denies Solex Appeal Request

The Alberta Court of Appeal has denied Solex Gas Processing Corp.'s (Solex) application for leave to appeal AEUB Decision 2004-006 in which the Board denied Solex's application to reprocess natural gas from Nova Gas Transmission Ltd.'s (NGTL) Western Alberta system. Solex had applied to construct and operate two 9 km natural gas pipelines between NGTL's Western Alberta System and Solex's Harmattan-Elkton gas plant, seeking to sidestream sweet natural gas from the NGTL system by removing natural gas liquids (NGL) at the plant and returning the processed gas back to the NGTL system. As previously reported in our newsletter, the Board held that although straddle plant owners do not have a pre-emptive right to the NGL in the common stream, maintaining the viability of the straddle plant industry as a whole continues to be in the public interest, and should not be changed without proper stakeholder consultation. In denying Solex's application for leave to appeal the Board's decision, the Alberta Court of Appeal confirmed that the matters considered by the Board in determining that the sidestreaming scheme was not in the public interest were within the scope of the Board's public interest mandate, and that the Board acted properly in making its decision.

BRITISH COLUMBIA

PNG Re-Applies for BCUC Approval to Re-Capitalize as an Income Trust

After having its application to re-capitalize as an income trust rejected by the BCUC in July 2004 (see our Fall 2004 Newsletter) Pacific Northern Gas Ltd (PNG) has applied again for the same relief. By application dated December 17, 2004 PNG seeks BCUC approval of a series of steps involved in the proposed conversion, including share transfers, share redemptions, and a share issuance. The proposed final structure would see PNG amalgamated with its affiliate Pacific Northern Gas (North East), and the shares of the amalgamated entity to be held by the trustees on behalf of the unitholders. The amalgamated entity would continue to be a regulated public utility under the jurisdiction of the BCUC. Distinguishing the current application from the previous failed application, PNG says the current application is not dependent on the BCUC's acceptance of a deemed capital structure, nor a deemed corporate income tax, two of the sticking points in the BCUC's previous reasons. In the application PNG argues that the benefits of the proposed conversion include lower cost of service (and rates lower than they would otherwise be), and a less-leveraged, more efficient capital structure, arising primarily from the ability under the model to retire some of PNG's existing debt. PNG also has its 2005 revenue requirement application before the BCUC, and proposes that the resolution of

that application wait pending the conclusion of the income trust conversion application.

Duke Point Power and BC Hydro Contract for Vancouver Island Supply

On November 16, 2004, BC Hydro and Duke Point Power Limited Partnership (Duke Point) entered into a 25-year electricity purchase agreement (EPA). The agreement was the culmination of the year-long Call for Tender process embarked upon by BC Hydro after the BCUC rejected BC Hydro's 2003 application for a CPCN for a gas-fired generation plant on Vancouver Island. Duke Point was the successful bidder out of an initial field of 23 registered bidders as of November 2003. On February 17, 2005 the BCUC ordered the EPA accepted as filed, rejecting intervenor submissions to render it unenforceable and not in the public interest. The order is conditional on BC Hydro successfully negotiating a gas transportation contract with Terasen Gas Vancouver Island (TGVI). Intervenors have already announced their intentions to seek leave from the BC Court of Appeal to appeal the order.

Under the agreement, BC Hydro will sell to Duke Point for \$50 million the assets it had developed in connection with its CPCN application, including the necessary environmental permits, the Vancouver Island site near Nanaimo, British Columbia, and a steam turbine. Duke Point plans to complete the development of these assets and have the 252 MW CCGT plant in operation by May 1,



2007 to be available to provide capacity on Vancouver Island to meet needs anticipated in the winter of 2007/08.

The hearing into the EPA was the first major review by the BCUC of an energy supply contract under section 71 of the *Utilities Commission Act* (although dozens of other agreements have been filed for approval without a review by the BCUC under the same provision).

BCTC Granted CPCN for New System Control Modernization Project

On February 15, 2005 the BCUC granted the British Columbia Transmission Corporation (BCTC) a Certificate of Public Convenience and Necessity (CPCN) for a new proposed system control centre in the Vancouver area, and a new fully functional back up control centre in the Southern Interior. Total project costs are estimated at \$133 million, including \$73 million for 2 new buildings. The project is required, says BCTC, to replace obsolete technology, resolve seismic criteria issues at existing facilities, provide a geographically remote back up facility, and to address future siting limitations at the current facility.

TGVI Application for LNG Facility Approved

TGVI's application for a CPCN to build a liquid natural gas (LNG) storage facility near Ladysmith on Vancouver Island, was approved by the BCUC on February 16, 2005, conditional on BC Hydro entering into the EPA with Duke Point (noted above). The proposed 1.0 Bcf (billion cubic feet)

facility may be up to 60 m in diameter and 55 m to the top of its domed roof. LNG storage allows for the purchase and liquefaction of gas to a fraction of its original volume. This can take place during the summer when consumer use and market gas prices are lower, with vaporization and release of the gas during the winter when consumer use and gas market prices are higher.

NORTHWEST TERRITORIES

NWT Public Utilities Board Approves Diesel Fuel Rider

On January 13, 2005, the Northwest Territories Public Utilities Board (the Board) approved the Northwest Territories Power Corporation's (NWTPC) application to impose a fuel rider of 3.37 cents/kWh applicable to all customers in the 19 diesel fuel powered communities. The fuel rider is intended to clear the balance of the fuel stabilization fund, which was set-up to capture variances between forecast and actual fuel costs. The fuel rider was the first proposed by the NWTPC since the fuel stabilization fund was approved in the last General Rate Application in 2001. Intervenor concerns focused on the different impacts on different communities arising from the fixed 3.7 cents/kWh order being additive upon varying community based rates. The Board noted that while a rate rider based on a percentage would result in uniform impacts on communities, the NWTPC's billing system does not currently permit such a rider. The 3.7 cents/kWh rider came into effect on February 1, 2005.

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BARRISTERS & SOLICITORS

VANCOUVER ▼ CALGARY ▼ YELLOWKNIFE

Lawson Lundell LLP – Limited Liability Partnership

Effective February 14, 2005, Lawson Lundell has become a limited liability partnership as permitted by recent amendments to the British Columbia Partnership Act. The new amendments introduce to the practice of law a degree of limited liability and are consistent with other jurisdictions where limited liability partnerships are recognized. The firm is now known as **Lawson Lundell LLP** and our firm logo has now been updated to reflect this change.

Lawson Lundell LLP continues to be liable for the professional negligence of its personnel, and the firm's assets and insurance still stand behind the firm's obligations and liabilities. Registration as an LLP means that the firm's partners are not personally liable for negligent acts or omissions of another partner or employee of the firm unless he or she was aware of the negligent act or omission and did not take reasonable steps to prevent it. Each partner of the firm continues to be personally liable for his or her own actions.

The registration of the firm as an LLP does not affect our business practices or approach to the practice of law. Lawson Lundell LLP and its partners, associates and staff will continue to provide our clients with the highest quality legal services in an efficient, timely and cost effective manner. If you have any questions regarding our registration as a limited liability partnership, please feel free to call me at 604.631.9185.

Yours very truly,

LAWSON LUNDELL LLP



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Managing Partner