

Alberta Oil Sands Tenure Guidelines

Principles and Procedures

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Notice

The guidelines outlined in this document are based on the *Mines and Minerals Act*, the *Oil Sands Tenure Regulation*, and the *Mines and Minerals Administration Regulation*. The act, the regulations and the guidelines themselves are subject to regular reviews by the Department of Energy and industry. They are amended as required, in response to changing circumstances and business needs.

The current guidelines reflect the Department of Energy policies and procedures as of May 12, 2009. Industry will be notified when the guidelines are revised.

The **Alberta Oil Sands Tenure Guidelines** document is produced for the convenience of readers. It provides a general understanding of the principles and processes used to establish oil sands tenure.

Users are reminded that the guidelines have no legislative sanction.

Should the guidelines conflict with the *Mines and Minerals Act*, the *Oil Sands Tenure Regulation*, or the *Mines and Minerals Administration Regulation*, the act and regulations will prevail.

Copies of the *Act* and regulations are available through the Queen's Printer:

In Edmonton:
10611 - 98 Avenue
Edmonton, Alberta
T5K 2P7
Phone 780.427.4952 • Fax
780.452.0668
E-mail: QP@gov.ab.ca

Free, online copies may be downloaded from the Queen's Printer's website at www.qp.alberta.ca or by going to the Department of Energy website, navigating to the Oil Sands home page, and in the left menu choosing Our Business, Oil Sands, Legislation, and Guidelines & Policies.

For further information or inquiries regarding the guidelines, please contact the appropriate department representative listed in Appendix.

About this document

The Alberta Department of Energy through a consultative process, which included oil sands industry representatives, developed the *Alberta Oil Sands Tenure Guidelines*. The guidelines are designed to:

- help lessees and developers determine their oil sands tenure entitlements,
- interpret relevant energy legislation (statutes and regulations),
- communicate oil sands tenure-related policy to industry stakeholders,
- make it easier for the oil sands industry to comply with the requirements of the *Mines and Minerals Act*, the *Oil Sands Tenure Regulation*, and the *Mines and Minerals Administration Regulation*.

The Alberta Oil Sands Tenure Guidelines address a number of areas

- [Chapter 1](#) provides a brief history of Alberta's mineral rights and oil sands tenure systems.
- [Chapter 2](#) deals with acquiring oil sands rights through the public offering process by direct purchases or transfers.
- [Chapter 3](#) discusses the types of oil sands agreements (permits and leases) and explains Department of Energy policy for managing and continuing these agreements. Topics include continuations and lease selection, cancellations and surrendering oil sands agreements.
- [Chapter 4](#) deals with evaluating oil sands leases and permits. A minimum level of evaluation must be met in order for an oil sands agreement to be continued beyond its initial term.
- [Chapter 5](#) explains department policy with regard to the minimum level of production, which must be met for an oil sands lease to be considered a producing lease.
- [Chapter 6](#) deals with escalating rent, which are charged on non-producing continued leases.

The appendices include

- Forms and reporting
- Information Letters and Bulletins
- e-Subscription
- Glossary - words defined in this appendix are identified by a star (*) the first time they appear in the document
- Abbreviations
- Contact Information
- Electronic Systems

In this document

- the *Act* refers to the *Mines and Minerals Act*.
- the Minister refers to Alberta's Minister of Energy.
- the department refers to the Alberta Department of Energy.
- The ERCB refers to the Energy Resources Conservation Board.

To locate important oil sands information and links, the internet user needs to do so by going to the Department of Energy website www.energy.gov.ab.ca, navigating to the Oil Sands home page, and in the left menu choosing Our Business, Oil Sands and then choose your topic.

Chapter 1

A Brief History

Mineral Rights in Alberta

The provincial Crown owns the mineral rights to approximately 81% of Alberta's 66 million hectares. The Government of Canada through the *Natural Resources Transfer Act* of 1930 granted these rights. They encompass petroleum, natural gas, oil sands*, and other minerals.

Mineral rights to the remaining 19% of Alberta's land are held

- by the federal Crown, within national parks and Indian reserves
- or
- by freehold owners, which include
 - successors to the Hudson's Bay Company, which owned the mineral rights in what is now Alberta, Saskatchewan, Manitoba, the Northwest Territories, and Nunavut from 1670 to 1869,
 - Most of these rights were surrendered to the Dominion of Canada in 1869.
 - National railway companies, which received land concessions and mineral rights from the federal government in the 19th century, and descendants of homesteaders who settled in Alberta before 1887 were granted mineral rights by the federal government.

The Alberta Crown owns 97% of oil sands mineral rights; freehold owners hold the remaining 3%. The department, on behalf of the citizens of the province, manages mineral rights owned by the Alberta Crown.

Oil Sands: A Definition

The *Mines and Minerals Act*, defines oil sands as

- sands and other rock materials containing crude bitumen*
- the crude bitumen contained in those sands and other rock materials
- any other mineral substance (except natural gas) associated with the above-mentioned crude bitumen, sands or rock materials

Bitumen*: A Layman's Definition

Bitumen is a thick, sticky form of crude oil, which is so heavy and viscous that it will not flow unless it is heated or diluted with lighter hydrocarbons. At room temperature, bitumen behaves much like cold molasses.

Alberta's Oil Sands

Canada's resources of bitumen* occur entirely within Alberta's oil sands, which hold an estimated 1.7 trillion barrels of crude bitumen. Alberta's oil sands are one of the largest petroleum resources in the world. They are unique because the bitumen they contain is recoverable through surface mining as well as through conventional well operations. It is expected that about 20% of Alberta's oil sands bitumen will be recovered through mining.

Alberta's Oil Sands constitutes about 10–20% of bitumen, 80–85% is mineral matter such as sand and clay, and the remaining 4–6% is water.

Proven Reserves: A Definition

Those reserves recoverable under current technology and present and anticipated economic conditions specifically proved by drilling, testing, or production, plus the portion of reserves that are interpreted to exist from geological, geophysical, or similar information with reasonable certainty. NOTE: This is the same definition used by ERCB for Established reserves.

Oil Sands Areas

The ERCB has classified Alberta's oil sands resources into three areas

- **Athabasca Oil Sands Area**

Alberta's first commercial oil sands production occurred here in 1967, when the Great Canadian Oil Sands plant (now Suncor Energy Inc.) opened at Fort McMurray. The Syncrude consortium began production in 1978. Alberta's only oil sands surface mines are located in this area.

- **Cold Lake Oil Sands Area**

Alberta's major in situ* operations are located here. In situ (Latin for "in place") production methods include cold (primary) production as well as steam or solvent injection. In situ methods are used when bitumen deposits are too deep for surface mining to be feasible.

- **Peace River Oil Sands Area**

This is the least commercially developed of Alberta's oil sands areas. To date, the recovery methods used here are comparable to those used in the Cold Lake Oil Sands Area.

Oil sands tenure legislation refers to these three areas. (See [Figure 11 - Oil Sands Escalating Rent Area A and Area B](#) for details.)

Oil Sands Tenure

TENURE: a condition or form of right or title, under which...property is held.
—The Canadian Oxford Dictionary, 1998

The term tenure* describes the system through which Crown owned mineral rights—including oil sands rights—are leased and administered. By facilitating the leasing of these rights, the tenure system makes it possible for individuals and companies to explore for and develop Alberta's mineral resources for the benefit of the citizens of the province.

The viability of Alberta's economy and its non-renewable resource industries depends on the orderly development of the province's oil, gas, oil sands, and other mineral resources. It is important that both the people of Alberta and producers realize an acceptable return from the development of these resources. At the same time, non-renewable resources must be managed in a manner that considers the environment and promotes sustainable development.

Managing Alberta's Resources

The Department of Energy manages Crown-owned mineral rights on behalf of the citizens of the province. Alberta benefits from a wealth of Crown-owned natural resources, but relies on the private sector to develop these resources. In return the Department of Energy receives revenues in the form of royalties, bonus bids, offset compensation and annual rental fees. It calculates, assesses and collects these revenues and monitors and reviews the effectiveness of Alberta's royalty framework. The Department, in conjunction with other Government of Alberta ministries recommends resource development policy which support government goals.

The ERCB regulates oil, gas, oil sands, and other mineral activities and acts in the best interest of all Albertans in overseeing the efficient and effective development of Alberta's energy resources, while ensuring public safety and balancing the need for protection of the environment, conservation, orderly development, technical innovation, and service.

Other ministries such as; the Ministry of Environment and Sustainable Resource Development work with Energy and the ERCB to manage air, land and water monitoring and planning to support Government of Alberta.

A Look Back

Oil sands tenure legislation has evolved in response to the changing business needs of the oil sands industry and the government.

Alberta's earliest tenure legislation for surface-mineable oil sands was established for the Bituminous Sands Area near Fort McMurray in the 1950s. (This area is now considered part of the Athabasca Oil Sands Area.) Under this legislation, the Alberta Government issued three-year exploration agreements, which could be converted to 21-year leases.

In the early 1960s, the province issued oil sands exploration agreements which conveyed the right to bitumen present in any zone covered by an existing petroleum and natural gas lease.

In 1984, the Alberta Energy Utilities Board established the three oil sands areas and ruled that, with the exception of natural gas and coal, all hydrocarbons produced in these areas were considered to be oil sands.

For details, see the Alberta Energy Utilities Board Informational Letter IL 84-07: Declaration of Oil Sands Areas to Facilitate Orderly Leasing and Stable Regulation, which is available on the Energy Resources Conservation Board website under Industry Zone, Rules, Regulations, Requirements, Information Letters, and Interim Directives.

An external link to the Energy Resources Conservation Board website can be found on the department's website in the lower left menu under Related Links.

Legislative changes introduced in the late 1980s provided for 21-year renewals of oil sands leases*, provided that the leases were producing* a prescribed volume of bitumen.

In the fall of 1997, a joint, industry–government committee—the Industry Oil Sands Tenure Advisory Committee (IOSTAC)—was formed to review the oil sands tenure system. The committee proposed several improvements, which are now part of the *Oil Sands Tenure Regulation*.

For more information about the history of tenure legislation in Alberta, please see the publication *Alberta's Oil and Gas Tenure*, available from the Oil Sands home page, left menu, Publications & Maps.

Highlights of the Revised Tenure System

- Development plans no longer need to be filed with the department.
- Lease types and terms have been standardized. The old regulation identified nine types of oil sands leases. The current regulation uses only two:
 - primary leases*, which are issued for a standard term of 15 years, and
 - continued leases*, which are classified as producing or non-producing*.

Oil sands leases are discussed in detail in [Chapter 3](#)

Oil Sands Tenure Today

Alberta's tenure system is regarded as one of the best in the world.

Alberta's current oil sands tenure regime provides a regulatory framework which supports the major investments needed to develop the province's oil sands resources. The *Mines and Minerals Act*, the *Oil Sands Tenure Regulation*, and the *Mines and Minerals Administration Regulation* define the current regime. The regulations apply to new and existing oil sands agreements*.

The Role of the Department

Responsible tenure and stewardship of Alberta's oil sands resources are important for the long-term prosperity of the province and the people of Alberta. The department

- provides opportunities for oil sands development,
- provides an effective oil sands management framework, and
- allows for a fair economic return, both for the oil sands industry and for the people of Alberta.

Oil Sands Operations

The department

- makes it possible for companies to acquire oil sands rights,
- fosters the development of Alberta's oil sands, and ensures that oil sands agreements (permits* or leases) are in the hands of those who are committed to developing them,
- encourages the Alberta-based upgrading of bitumen,
- allows the oil sands industry to determine an appropriate pace for exploration and development activities (once required minimum levels of evaluation* have been met, and
See [Chapter 4](#) for details.
- facilitates the effective evaluation* of oil sands resources.

Oil Sands Management

The department

- establishes and maintains an open, two-way dialogue on existing management processes and proposed alternatives, and
- ensures that tenure rules are clear, fair, predictable, and consistently applied
Clear, concise, consistent rules minimize costs and reduce the administrative burden for both industry and government.

Economic Returns

The department ensures that, when oil sands resources are made available for development

- the provincial Crown receives a fair economic return in the form of bonuses*, rent, and royalty* payments, and
- industry has opportunities to receive appropriate rewards and recognition for the risks that it takes.

Chapter 2

Acquiring Oil Sands Rights

The owners of mineral rights may lease them to oil and gas companies in exchange for a royalty—a share of production or equivalent revenue. In the case of Crown rights*, the owner (the Crown) also receives a bonus and an annual rent payment when the rights are leased.

Disposition

The Mines and Minerals Act defines a disposition as a grant, a transfer, or an agreement.

The assignment of mineral rights from one party to another is referred to as disposition*. The term undisposed* refers to rights which have not been assigned.

Oil Sands Tenure Regulation, section 4

Crown-owned oil sands rights are disposed by means of agreements. Oil sands agreements convey the right to “drill for, win, work, recover and remove” oil sands that are owned by the Crown. Two types of agreements are used

- permits*
- leases*

Mines and Minerals Administration Regulation, section 7 and 12

The department is authorized to issue oil sands agreements

- by sale* through public tender, conducted in a manner determined by the Minister,
See [Public Offerings* \(Sales\)](#) for details.
- on application, if the Minister considers the issuance of the agreement warranted ,

Dispositions of this type are referred to as [direct purchases](#)*.

- by means of registered transfers, and
See [Transfers](#) for details.
- pursuant to any other procedure determined by the Minister.

Oil sands agreements are discussed in detail in [Chapter 3](#).

Public Offerings (Sales)

The public offering process for oil sands is the same as that for petroleum and natural gas.

The majority of oil sands agreements are issued through public offerings conducted by the department. Public offerings are also referred to as sales or land sales*.

Although the word “sale” or “land sale” is used by tradition, it is a misnomer: the Crown always retains title to its minerals. What is offered is the right to the minerals associated with a particular piece of land for a set term—in exchange for a bonus payment, annual rental, a fee, and royalty on recovered minerals. Oil sands rights are leased at a public offering, not sold, to the highest bidder.

There is no guarantee that a bidder who wins oil sands rights at a public offering will get a surface lease that allows access to the minerals. Surface leases for Crown land are managed by the Department of Sustainable Resource Development.

Oil sands sales are conducted at scheduled times throughout the year. Oil sands sales follow the same schedule as sales of petroleum and natural gas (P&NG) rights.

The public offerings schedule is published two years in advance, as an attachment to an Information Letter produced by the department and electronically distributed to a list of subscribers.

For more information on how to subscribe, see e-subscriptions in the Appendix. Information letters and schedules of public offerings are also available from the Oil Sands home page, using the left navigation menu.

Sales of oil sands rights are initiated by posting requests submitted by companies or individuals. If no rights have been requested, there is no need to hold a sale.

Oil Sands parcels up for public tender are advertised 8 weeks in advance of a sale.

See [Public Offerings* \(Sales\)](#) for details.

The Process

Requesting a Posting

Companies or individuals who wish to acquire undisposed oil sands rights request a posting for a specific sale date. The request must be submitted electronically through the department's Electronic Transfer System (ETS). The requestor needs an authorized ETS Account with access to the Posting Request service.

The Posting Request and ETS manuals, and the ETS Account Set Up/Change Form are available from the Oil Sands home page, left menu, ETS icon. See Electronic System and Services in the Appendix for more information.

Note:

Companies or individuals who request postings are expected to bid on the parcels when the requested rights are made available at a public offering. If you are a requestor of a parcel and fail to bid, you will be charged a penalty of \$625 plus GST for each requested parcel that is not sold.

Acceptance and Processing

Once a posting request has been received, the department processes the requested rights after which the requestor is notified by an interim posting detail regarding the availability of the rights and current surface restrictions. The available requested rights are forwarded to the Crown Mineral Disposition Review Committee (CMDRC). The members of this committee represent the Alberta Ministry of Environment, the Ministry of Sustainable Resource Development, and the Ministry of Community Development.

The committee

- reviews the lands,
- identifies potential surface-access restrictions, and (Restrictions may result from policy, legislation, or legal mandate.)
- advises the department about the nature of the restriction.

Once the department has reviewed CMDRC comments, the requestor is advised about any new restrictions and contacts.

Parcel: A Definition

The term parcel encompasses two elements:

- the lands to which these rights pertain
- oil sands rights

A parcel is the configuration of land which defines the physical location of oil sands for which rights have been requested by public offering or private sale. The land is identified by means of

- a legal description (section, township, range, and meridian), which locates the surface, and
- a description of the underlying oil sands zones.

Public Offering Notice

A public offering notice (PON) is published eight weeks prior to a sale date. The notice

- sets out the terms and conditions under which the parcels are offered,
- specifies the place, date, and time of the sale,
- provides instructions for submitting bids,
- lists and describes the parcels being offered,

The notice specifies the parcel number, the total area covered by the parcel, the legal description of the lands, and a description of the oil sands rights being offered.

- lists all relevant Zone Designations* (ZD) and Deeper Rights Reversion Zone Designations* (DRRZD), and

Further information is available in department Information Letter 98-14: Application of Zone Designations (ZD) and Deeper Rights Reversion Zone Designations (DRRZD) for Rights.

- includes relevant appendices outlining any surface restrictions which apply to individual parcels.

Electronic copies are distributed to the department's list of Oil Sands subscribers.

For more information on how to subscribe, see e-subscriptions in the Appendix. Public offering notices are also available from the Oil Sands home page, left menu, Oil Sands Public Offering icon.

The Posting Cycle

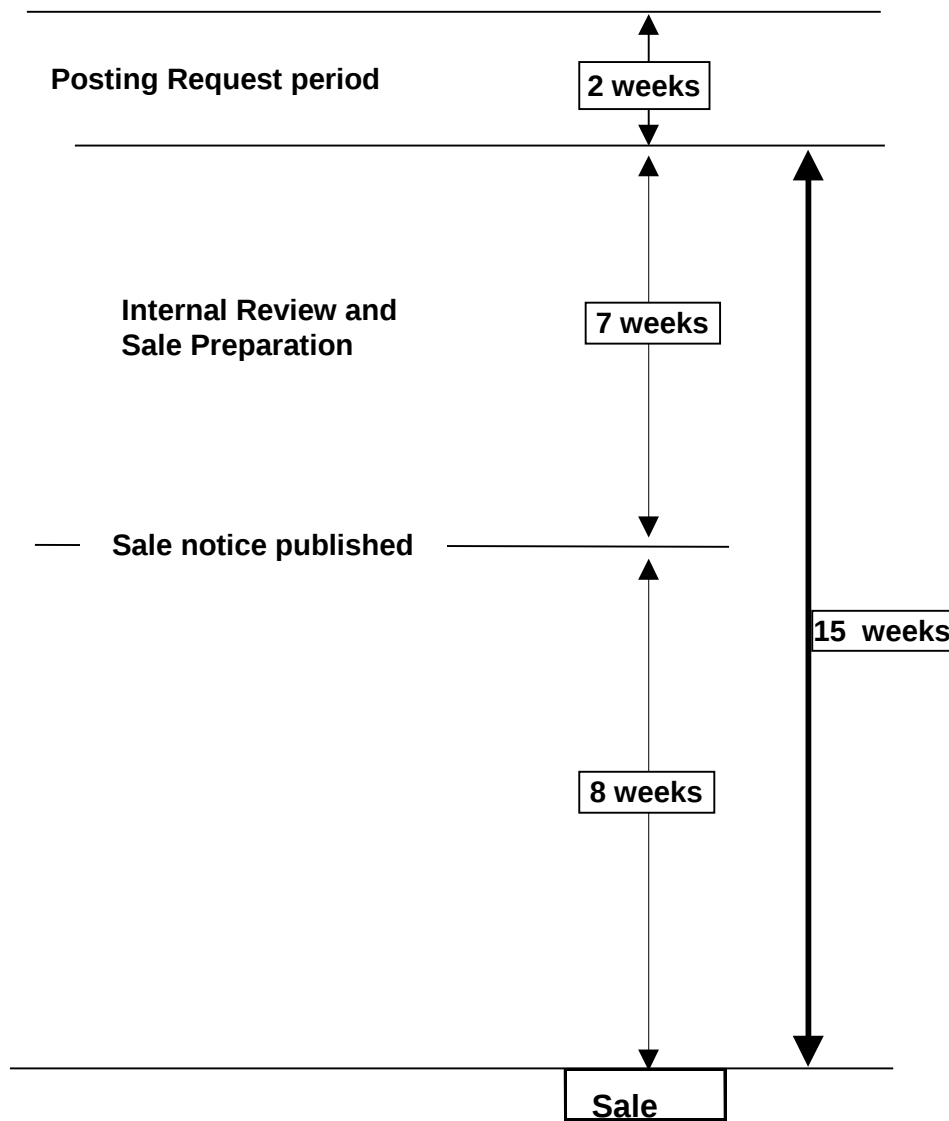


Figure 1: The posting cycle for a public offering normally takes 17 weeks.

Bidding Requirements

Companies or individuals who wish to bid on oil sands parcels posted by way of a Public Offering Notice must do so electronically through the department's Electronic Transfer System (ETS). The bidder needs an authorized ETS Account with access to the Bidding service and must be an active tenure client. All paper work to allow for an Electronic Funds Transfer (EFT) must be complete, before any bids are considered.

The Bidding and ETS manuals and the ETS Account Set Up/Change Form are available from the Oil Sands home page, left menu, ETS icon. See Electronic Services in the Appendix for more information.

Bid Request

A Bid Request consists of a bid on one or more parcels; both PNG and Oil Sands parcels may be in the same bid request. Bids on parcels from different sales dates are not allowed. The department's copy of the bid request submitted is the official record of the bid. Before submitting your bid, you are encouraged to read the terms, conditions, and sales procedures, which can be found on the second page of the PON.

Your total bid includes the bonus, rent at \$3.50 per hectare or \$50.00 whichever is greater, and a fee of \$625.00. An offer of less than \$2.50 per hectare for an oil sands lease or \$1.25 per hectare for an oil sands permit will not be considered.

Note

The department reserves the right to reject any bid.

If the same bidder submits more than one bid for the same parcel, the department reserves the right to accept the highest bid.

If there are two bids with the same highest offer, they will be processed as tie bids and the clients will be contacted by telephone and given a set time to re-bid.

Payment

The only form of payment acceptable for winning bids is electronic funds transfer (EFT). EFT authorizations are arranged through the department. The EFT Authorization Form is available from the Oil Sands home page, left menu Forms & Reporting. Debits are made on the sale day beginning as soon as the sale is completed and will be reflected in the company's account the following day. Some debits may take longer depending on which bank you conduct your business.

The bidder is responsible for having sufficient funds in the bank on sale day to cover all bids. If an EFT transaction fails due to insufficient funds, the bidder will be contacted and an interest payment of 3 percent will be charged for all parcels awarded. The parcel(s) may also be awarded to the next highest bidder or withdrawn by the department. If the situation occurs more than once, the department reserves the right to refuse future bids and/or posting requests by that company or individual.

Timelines

Bids can be created and submitted as soon as the public offering notice of available Oil Sands rights are published. At 12:00 noon on the date of the sale, the sale is closed. Any bid request not submitted before that time will not be considered for the sale. The Department of Energy time will be considered the official time. The time clock is available for viewing on the Bid Request screen.

Sales Results

Oil sands agreements are awarded to the highest bidder.

Accepted offers information will be available on the sale day in the afternoon on the department's website. The name of the successful bidder and the bonus amount paid for each parcel will be announced.

Information about unsuccessful bids is not published.

Electronic copies of the Sales results are distributed to the department's list of subscribers.

For more information on how to subscribe, see e-subscriptions in the Appendix. The Sales results are also available from the Oil Sands home page, left menu, Oil Sands Public Offering icon.

On occasion the department may require additional time to process a sale and this may delay publishing the results. Should this happen, the department will inform industry via our website and electronic mailing lists.

Agreements are issued to successful bidders electronically through the department's Electronic Transfer System (ETS) within two weeks of a sale date. Only the designated representative can pick up the agreement document. Any bidder who wishes to become an agreement holder* must have an authorized ETS account with access to the Crown PNG and Oil Sands Agreement Documents service.

The ETS bid manual and the ETS Account Set Up/Change Form are available from the Oil Sands home page, left menu, ETS icon. See Electronic System and Services in the Appendix for more information.

Additional information about the bidding process is provided in Information Letters, which are available from the Oil Sands home page, left menu, Information Letter icon. For more information about Information Letters and how to subscribe to them, see Appendix.

Direct Purchases of Crown Rights

Direct Purchase of Portions

To facilitate a company or individual in acquiring the lands in a drilling spacing unit, the Crown may lease their portion of the lands through a direct purchase if the applicant meets the requirements outlines below:

1. The Crown rights comprise less than 50 percent of the smallest applicable spacing unit in the lands applied for (i.e. less than 50 percent of an oil spacing unit or a smaller special spacing unit established by the ERCB). Where Crown rights exceed this limit, the normal process for Public Offerings should be used.
2. The application is supported by a statutory declaration stating that you or the company have ownership of or control over the oil sands in the freehold portion of the spacing unit. This control may occur by virtue of being the owner of a percentage of undivided interest in the oil sands or the holder of a percentage of undivided interest in the oil sands under a valid and subsisting freehold lease. The statutory declaration can be found on the Oil Sands home page, left menu Forms & Reporting.
3. The rights granted in the Crown lease will correspond with those included in the freehold agreement.
4. The minimum acceptable bonus is \$500 per hectare or \$2000, whichever is greater, and is non-negotiable. The department reserves the right to adjust the minimum bonus periodically to reflect market trends.
5. The first year's annual rental plus the lease issuance fee is also payable. See [Annual Rent](#) for details.
6. An applicant who does not wish to purchase the portion of rights on the above terms has the option of posting the parcel through the Public Offering process.

Spacing Units: A Definition

Spacing units are established by the ERCB.

They specify the spacing of wells drilled into individual reservoirs for producing oil, gas, or oil sands products. This regulates production rates and ensures efficient drainage of the resource.

The standard spacing unit for oil and oil sands is one well per quarter section.

Additional information about the direct purchase process is provided in Information Letters, which are available from the Oil Sands home page, left menu. For more information about Information Letters and how to subscribe to them, see Appendix.

Direct Purchase of Complementing Rights

To facilitate common ownership of Oil Sands rights and Natural Gas rights, the Crown may lease the oil sands rights to the Petroleum & Natural Gas (P&NG) agreement holder by direct purchase if the applicant meets the requirements outlined below:

1. The requested Oil Sands rights must be located in the same zone as the P&NG for which the applicant holds an agreement.
2. The department determines the term for which Oil Sands rights are granted. At the department's discretion, rights are assigned as follows:

A Primary Term P&NG agreement is complemented by a five year Oil Sands Permit,

or

A Continued P&NG agreement is complemented by a 15-year Oil Sands Primary Lease.

3. The Oil Sands rights are granted by means of a separate agreement. They are not consolidated with the applicant's P&NG agreement. Agreements granted through direct purchases are subject to the same terms, conditions, and rules that apply to agreements granted through the public offering process.
4. The bonus price per hectare for an Oil Sands parcel will be an amount that is 125 per cent of the average price per hectare of the amounts received from Oil Sands rights sales (excluding sales in the surface mineable area) occurring in the six months prior to the month in which the department received the direct purchase application.
5. The first year's rental plus the agreement issuance fee is also payable. See [Annual Rent](#) for details.
6. The direct purchase price calculated by the department is not negotiable.

The Process

Applying for a Direct Purchase

Only one parcel per request can be entered for a Direct Purchase. The request must be submitted electronically through the department's Electronic Transfer System (ETS). The requestor needs an authorized ETS account with access to the Postings Request service.

The department will review each application received and the purchase price will be added to the requestor's posting request on ETS. An email will be sent to the creator of the posting request advising them of the update. Acceptance or rejection of the purchase price is required before further processing. Should a company choose to reject a purchase price then post the lands in a public sale, the parcel will be placed into the next available sale.

The Posting Request and ETS manuals, and the ETS Account Set Up/Change Form are available from the Oil Sands home page, left menu, ETS icon. See Electronic System and Services in the Appendix for more information.

Acceptance and Processing

Once the requester has accepted the price, the applicant must pay

- a \$625 issuance fee,
- rental for the first year of the agreement, calculated at the rate of \$3.50 per hectare or a minimum amount of \$50.00, and
See [Annual Rent](#) for details.
- a bonus - the direct purchase bonus price per hectare can be found on the Oil Sands home page, left menu Sales & Administration.

This is the amount paid for Crown mineral rights. The Crown receives a bonus regardless of whether rights are sold directly or at a public offering.

Payment

The only form of payment acceptable for direct purchase is **electronic funds transfer (EFT)**. EFT authorizations are arranged through the department. Once the requestor has accepted the price, the funds will be withdrawn from the payor's EFT account within two days of acceptance of the purchase price. Should the department debit an account and find that there are insufficient funds to cover the transaction, the applicant will be contacted and interest of 3 percent will be charged, or the application may be cancelled.

The EFT Authorization Form is available from the Oil Sands home page, left menu Forms & Reporting.

Transfer of Ownership in Oil Sands Agreements

The following information applies to transfers, which are registered under the *Mines and Minerals Act* and the *Mines and Minerals Administration Regulation*.

The *Act* allows the ownership of existing oil sands agreements to be transferred between parties.

Note

Transfers are managed by the P & NG Sales & Registrations section, Tenure Branch of the department, not by the Oil Sands Operations Division.

See Appendix for contact information.

The Process

Requesting a Transfer

Companies or individuals who wish to transfer their oil sands agreements must apply to the department. The transfer must be submitted electronically through the department's Electronic Transfer System (ETS). The requestor needs an authorized ETS Account with access to the Transfers Ownership and/ or Designated Representative service.

The Transfer of Ownership on Mineral Agreements and ETS manuals, and the ETS Account Set Up/Change Form are available from the Oil Sands home page, left menu, ETS icon. See Electronic System and Services in the Appendix for more information.

Requesting a Partial Transfer

The department accepts manual submissions when only a part of the location contained in the agreement is being transferred or when special circumstances warrant it.

Transfer of ownership must be completed and submitted in duplicate on the department's Transfer Form. The transfer form must be accompanied by

- a Transfer Transmittal Letter,
- execution documents related to the transfer agreement, as applicable, and
- the appropriate registration fee is \$625.

Trespass and Compensation

Mines and Minerals Act, section 54, 55, and 63

Trespass occurs when Crown minerals are recovered without authorization under the *Act* or without an agreement. To contend with situations of trespass, the Crown has developed a series of policies and procedures.

Additional information about Trespass and Compensation is provided in Information Letters, which are available from the Oil Sands home page, left menu 'Information Letter' icon. For more information about Information Letters and how to subscribe to them, see Appendix.

Chapter 3

Oil Sands Agreements

Agreement Types

Two types of oil sands agreements are issued under the *Oil Sands Tenure Regulation*:

- permits, which can be converted to leases, and
- primary leases, which can be continued

The regulation requires that exploration or development activity begin within a specified period and according to prescribed levels of evaluation or production.

Minimum level of evaluation* (MLE) criteria are discussed in [Chapter 4](#).

Minimum level of production* (MLP) criteria are discussed in [Chapter 5](#).

At the end of the initial term, assuming that the required criteria have been met, lessees* and permittees* may apply by letter, supported by technical data, to continue their agreements or in the case of permits for the lease selection process.

- **Permit holders** apply for primary leases through the process of lease selection*. See [Applying for Lease Selection](#) for details.

Permittees must attain MLE requirement.

- **First-term lease holders** apply for primary leases. See [Applying for a Primary Lease Out of a First-Term Lease](#) for details.

No MLE requirement.

- **Primary and Deemed Primary lease holders** apply for lease continuations*. See [Applying for Lease Continuation](#) for details.

Lessees must attain MLE requirement.

Lease Types

A Primary Oil Sands Lease is one which is issued to convert an Oil Sands Permit or to extend a first-term oil sands lease. Primary Oil Sands Leases are issued for 15-year terms through public offerings, direct purchases, lease selection from permits, and extensions of first-term oil sands leases.

A First-term Oil Sands Lease is a still-active, 21-year lease which was issued before 1991, under a previous regulation. At the end of its term, the lessee may apply for a primary lease under section 11 of the current *Oil Sands Tenure Regulation*.

A Deemed Primary Lease is a second-term lease that is not subject to a development plan, a lease issued out of a permit under the now-rescinded 1991 regulation, or a lease issued under section 13 of the (now-rescinded) 1991 regulation. Deemed primary leases are granted continuation under the same criteria as primary leases.

A Continued Lease is a primary lease or deemed primary lease which has been continued past its expiry date for an indefinite term, with either a producing or a non-producing status.

Leases

Two types of leases are administered under the *Oil Sands Tenure Regulation*

- primary leases
- continued leases

Primary leases are issued for a term of 15 years. In most cases, primary leases are acquired through the public offering process. (See [Public Offering Notice](#) for details) They may also be issued as lease selections from permits and to holders of 1st term leases after continuation is granted.

Continued leases are extensions of primary leases. Two criteria are used to determine whether a primary lease will be approved for continuation:

- the extent to which the lessee has evaluated the oil sands covered by the lease
See [Chapter 4](#) for details, and
- whether or not the lease is producing
See [Chapter 5](#) for details.

When the minimum level of evaluation criteria has been attained on leases, continuations are granted for an indefinite period.

See [Meeting a Minimum Level of Evaluation \(MLE\)](#) for details.

Permits

Oil sands permits are alternatives to leases. In the 1990s, the department issued permits when relatively little evaluation had been done on an oil sands resource. Under the current tenure system, the department typically allows applicants to choose whether they wish to post a permit or a lease agreement.

Permits are issued for 5 -year term.

Permit holders who have evaluated the oils sands to the required minimum level (See [Chapter 4](#) for details) may apply in writing for lease selection at the end of their permit terms. If their applications are approved, they are assigned a primary lease (or leases).

Annual Rent

Annual rent is payable on all oil sands agreements. Rent is calculated at the rate of \$3.50 per hectare or a minimum amount of \$50 applies.

The initial annual rent payment for an oil sands agreement is due when the agreement is first acquired.

- When an agreement is acquired through the public offering process), the annual rent payment must accompany the bid.
See [Public Offering Notice](#) for details.
- When an agreement is acquired by direct purchase, the annual rent payment, the bonus, and the issuance fee must be paid at the same time—prior to the issuance of the agreement.
See [Direct Purchases of Crown Rights](#) for details.

Subsequent annual rent payments are due on or before the anniversary date of the agreement. The agreement is considered to be in default if the rent is not paid by the day following the monthly statement due date.

Mines and Minerals Administration Regulation, section 19

The Monthly Statement Process consolidates all charges (for rent on oil sands agreements and for land searches) onto one invoice every month. Clients have the option of paying by cheque or using the Electronic Funds Transfer (EFT) System to debit their account automatically. All rentals have a deemed due date of the 15th day of the month, or the first business day thereafter. Financial Services administers the collection.

Mines and Minerals Act, section 45

The department issues a rental default notice two or three working days after an annual payment is due through a Monthly Statement Process. If the rent is not paid within 30 days of the monthly statement due date, the agreement is subject to cancellation.

Mines and Minerals Administration Regulation, section 21

Interest is charged on late payments.

Designated Representatives

Mines and Minerals Act, section 29(1)

A designated representative* must be appointed for every oil sands agreement. The designated representative serves as the Crown's contact for the agreement.

Note

A designated representative must be appointed whether an agreement is held by more than one party or is held by only one lessee. A sole lessee may serve as his own designated representative. Alternatively, the lessee may appoint an agent to act on his behalf.

The designated representative for an oil sands agreement is responsible for

- picking up the agreement document electronically from the ETS system,
- ensuring the payment of the annual rent and escalating rent*, when applicable,
- addressing any administrative defaults in connection with the agreement,
- identifying expenditures to be used to offset escalating rent,
- maintaining records suitable for audit, and

Escalating rentals and audits apply to non-producing continued leases. These topics are discussed in [Chapter 6](#).

On request, the designated representative must arrange for the department to have access to all the supporting documentation it needs for an audit. (Access to this documentation will not necessarily take place at the designated representative's own office.) If access is not provided, or if the department determines that the documentation is insufficient, the designated representative is responsible for settling any resulting adjustment to the required escalating rent payment.

- pursuing payment from a party whose cost credit (regarding escalating rent) is denied by the department.

This provision extends to situations where lease interests have changed. If a former lessee received a cost credit which was subsequently denied—after the individual no longer had an interest in the lease—the designated representative and current lessees assume the obligation of settling any audit adjustments.

The designated representative plays an important role in lessees' applications to use eligible expenditures as offsets against escalating rents.

See [Who can submit expenditure information](#) for details.

Administration of Oil Sands Agreements

Applying for Lease Continuation

Leases are continued if the required minimum level of evaluation has been attained. See [Chapter 4](#) for details.

When a lease is continued, it is classified as producing or non-producing. Producing leases must meet the required minimum level of production.

See [Chapter 5](#) for details.

An agreement holder* may apply in writing to continue a primary lease or a deemed primary lease. The designated representative must make the application. If the applicant is not the designated representative, a letter of authorization must accompany the application signed by the designated representative.

Applications for continuation must be received at the Edmonton or Calgary office of the department on or before the expiry date of the original agreement.

The letter of application must

1. identify the lease number and the land or lands for which continuation is requested.

Lessees may apply for continuation of all or a portion of their lease holdings. Land identification is required only when the application deals with a portion, not all, of the lease holding.

2. indicate whether the data in support of continuation was obtained pursuant to section 3(2) or to section 3(3) of the *Oil Sands Tenure Regulation*. These sections deal with required minimum levels of evaluation.

See [Chapter 4](#) for details.

3. identify the evaluation criteria used.
See [Chapter 4](#) for a discussion of the minimum level of evaluation that is acceptable.

4. state whether the required minimum level of production has been met.
See [Chapter 5](#) for details.

5. provide technical data to support the required minimum level of evaluation and (if applicable) the required minimum level of production. The technical data report must identify the specific lands on which evaluations were conducted. It must also include:
 - a brief discussion of the data.
 - a description of the work done to achieve the MLE (and MLP, if applicable).
 - details about drilling, coring, and electromagnetic testing, as applicable.
 - The technical data report should include well information such as the drilling completion date, the well ID, and whether or not a core sample was obtained. Confidential well data, including core analyses, must be supplied.
 - production data, including monthly well production statistics.
 - details about seismic testing, as applicable.
 - Seismic data should include shot point maps which verify that the required fold, group, and coverage parameters were used.
 - Synthetic seismograms should accompany all seismic data lines.
6. include maps showing:
 - the land area covered by the agreement,
 - locations of evaluation wells,
 - locations of evaluation wells with core data,
 - locations of drill holes, and
 - locations of seismic lines.
7. be accompanied by the annual rent payment, at \$3.50 per hectare.

See [Annual Rent](#) for details.

No issuance fee is required for lease continuations.

Note

A separate application must be made for each individual lease for which continuation is requested.

The Review Process for Lease Continuations

The department reviews applications and supplemental information to assess whether the required minimum levels of evaluation and production have been met. Once a lease has been approved for continuation, the department sends a confirmation letter to the applicant. The letter identifies

- the conditions of approval for the lease, and
- the lease status—that is, whether it has been classified as a producing or a non-producing lease. Non-producing leases are subject to escalating rent. See [Minimum Levels of Production](#) for details.

Once continuation has been granted, the lease remains in effect indefinitely—as long as the conditions of approval and the requirements of the *Oil Sands Tenure Regulation* have been met.

See [Continued Leases](#) for details.

See [Non-Producing to Producing](#) for information about changing the designation of a lease from producing to non-producing, or vice versa.

Advance Rulings

Lessees may request an advance ruling at any time during the term or a primary lease. Typically, requests for advance rulings are made when a lessee wishes

- to ensure that proposed work programs will result in a minimum level of evaluation (MLE) that the department will accept,
- to confirm that evaluation work completed to date will satisfy MLE requirements, or
- to confirm that any outstanding MLE requirements can be met before the primary lease expires.

Advance rulings minimize the risk that desired leases would not be continued.

Applying for a Primary Lease Out of a First-Term Lease

A lessee who holds a first-term oil sands lease may apply in writing by letter for a primary lease on or before the expiry date of the original agreement. The application letter must:

- specify the lease number that the applicant wishes to continue to a primary lease, and
- ensure that the next year's annual rent is paid.

We encourage all payments to be by direct deposit.

Neither evaluation data nor issuance fee are required.

Note

If an application for a primary lease is not made, the original lease may be cancelled. See [Cancellation](#) for details.

Applying for Lease Selection

A permit holder may apply in writing for lease selection on or before the expiry date of the permit. The applicant may apply to select a primary oil sands lease or leases for all or part of the lands covered by the permit. A minimum level of evaluation must be attained with regard to the requested lands.

See [Chapter 4](#) for Minimum Level of Evaluation details.

See [Permit & Lease Process chart](#) .

The letter of application for lease selection must

1. identify the land or lands for which lease selection is requested.

Permittee may apply for lease selection for all or a portion of their permit holdings. Land identification is required only when the application deals with a portion, not all, of the permit holding.

2. indicate whether the data in support of lease selection was obtained pursuant to section 3(2) or to section 3(3) of the *Oil Sands Tenure Regulation*. These sections deal with required minimum levels of evaluation.

See [Chapter 4](#) for details.

3. identify the evaluation criteria used.

See [Chapter 4](#) for a discussion of the minimum level of evaluation that is acceptable.

4. provide technical data to support the required minimum level of evaluation. The technical data report must identify the specific lands on which evaluations were conducted. It must also include:

- a brief discussion of the data,
- a description of the work done to achieve the MLE, and
 - The technical data report should include well information such as the drilling completion date, the well ID, and whether or not a core sample was obtained. Confidential well data, including core analyses, must be supplied.

- details about seismic testing, as applicable.
 - Seismic data should include shot point maps which verify that the required fold, group, and coverage parameters were used.
 - Synthetic seismograms should accompany all seismic data lines.

At the applicant's request, submitted seismic data will be returned once the application has been finalized.

5. include maps showing:

- the land area covered by the agreement,
- locations of evaluation wells,
- locations of evaluation wells with core data,
- locations of drill holes, and
- locations of seismic lines.

6. be accompanied by an issuance fee of \$625 per lease.

7. be accompanied by the annual rent payment, at \$3.50 per hectare.

See [Annual Rent](#) for details.

The Review Process for Lease Selection

The department reviews applications for lease selection to determine if the required minimum level of evaluation (MLE) has been achieved.

- **If the department rules that a satisfactory MLE was obtained for all lands** for which lease selection was requested, the applicant is notified and a lease agreement is issued.
- **If not all of the requested lands have satisfied the MLE requirement**, the department notifies the applicant in writing. The notification letter specifies the lands for which the required MLE has been met—that is, the lands for which oil sands rights can be retained. The applicant has 30 days from the notification letter to appeal this decision if he does not agree with the department's assessment.

If no application is received, the permit will expire and the lands will be returned to the Crown. Producing wells will be considered for trespass.

Appeals

Applicants who are not satisfied with the department's decision regarding minimum levels of evaluation may submit an appeal within the 30-day period specified in the notification letter. Only the original applicant may submit an appeal: third-party appeals are not accepted.

An applicant can request a formal meeting to present additional data. If this additional information is deemed unsatisfactory, the department's decision is final.

Note:

Only one appeal is granted per decision, after which the department's decision is final.

Consolidation

Mines and Minerals Administration Regulation, section 12

The lessees may, with the consent of the Minister, consolidate their oil sands leases. Consolidation refers to the process of combining existing lease agreements into one agreement.

Consolidation can only be considered if the participants in the leases are the same.

The consolidation process involves amending the agreement which has the earliest applicable term commencement date. The new agreement includes the same terms and conditions as this “parent” agreement.

Taking Lease A/Lease B and merging them into a single agreement is an example of consolidation. This can only occur if the same lessees hold both of the original agreements (Lease A and Lease B).

For example

Lease A and Lease B are consolidated. Lease A has a term commencement date of October 14, 2005; Lease B has a term commencement date of January 30, 2007. Since Lease A has the earlier term commencement date, Lease B will be consolidated into Lease A and is subject to the terms and conditions of Lease A.

The department reviews all requests to consolidate leases. It ensures that the proposed consolidation will not affect the escalating rent (See [Chapter 6](#) for details) which would be payable to the Crown if the leases remained separate. Approval is granted only when consolidation would lead to further oil sands production.

Lessees who wish to consolidate their leases must provide evidence that consolidation will result in more oil sands production than if the leases remained separate.

The department does not allow consolidation for the purpose of

- avoiding escalating rent payments,
- meeting required minimum levels of evaluation, or
- meeting required minimum levels of production.

Pooling

Pooling refers to the treatment of individual leases as a single entity. An example of pooling is when Lease A and Lease B remain separate legal entities, but are treated as if they were a single lease.

Pooling oil sands leases is not allowed. However, in certain pre-approved circumstances—such as the allocation of research and development costs to offset escalating rents—costs may be allocated to a number of leases. (See [Chapter 6](#) for details.) Such cost allocations are allowable under specific conditions: this is not the same as pooling.

Surrender

Mines and Minerals Administration Regulation, section 11

The designated representatives may surrender their permit or lease rights by notifying the department. The notification must be made on the department's Surrender form.

All Oil Sands tenure forms are available from the Oil Sands home page, left menu Forms & Reporting

An oil sands agreement may be surrendered at any time.

If an agreement is surrendered prior to its anniversary date, rental payments are not refunded.

Cancellation

Mines and Minerals Act, section 45

The Minister may cancel oil sands agreements. Cancellation may occur

- if agreement conditions have been breached,

or

- if the agreement holder has not responded to notices or complied with the *Act* or related regulations.

A notice of cancellation is provided to the lessee.

Note

If an agreement is cancelled, the department advises the ERCB that the holder has no right to produce from any active wells located on lands covered by the agreement. (This also applies to surrenders of agreements.)

The department's Crown Equity group monitors wells on lands included in cancelled agreements to ensure that unauthorized production does not occur.

Reinstatement

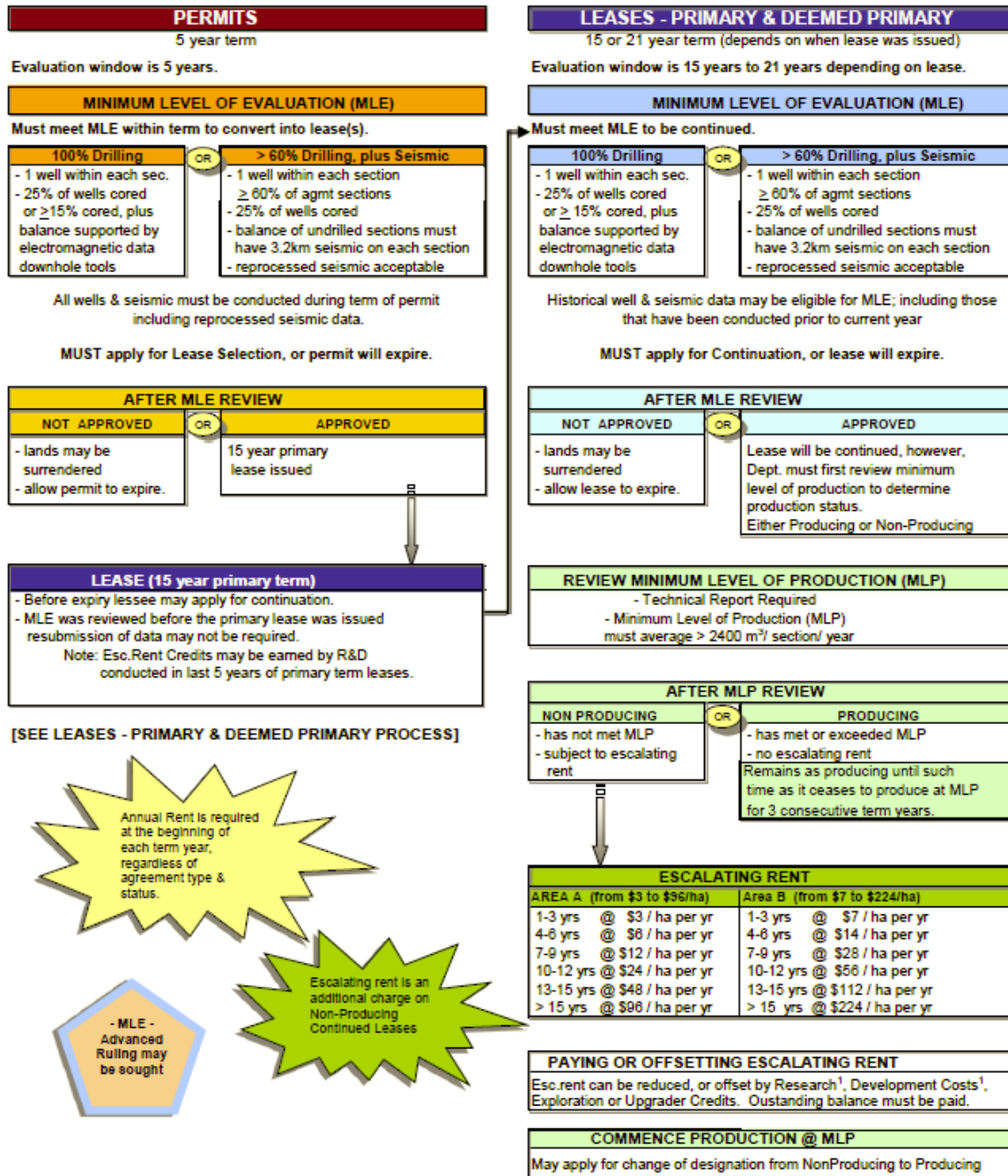
Mines and Minerals Act, section 8(1)(e)

The *Act* allows for the reinstatement of an agreement which has been surrendered or cancelled. The former agreement holder must apply to the department and satisfy the criteria set out in the act. Application must be made within 60 days of the date of the notice of cancellation.

Mines and Minerals Administration Regulation, Schedule item 8

The fee to reinstate an oil sands agreement is \$5,000.

Permit and Lease Evaluation & Continuation Process



Chapter 4

Evaluating Leases and Permits

The Rationale

The process of evaluation gathers technical data—geological, geophysical, engineering and production information—about the oil sands zone or zones included in oil sands agreements.

Evaluation data is descriptive: it provides valuable information about the nature and characteristics of the resource. Evaluation data helps to identify oil sands areas which have high potential for development. Similarly, it identifies areas in which development potential is lower, and contributes to the knowledge base about Alberta's oil sands resources.

Oil Sands Tenure Regulation, section 3

Evaluation is an important part of oil sands tenure. Applications for lease selection or lease continuation must be supported by technical data that meets a minimum level of evaluation (MLE). MLE criteria must be met before the next stage of tenure is approved.

To select leases from permits or to continue leases, holders of oil sands agreements make application to the department.

See [Applying for Lease Continuation](#) and [Applying for Lease Selection](#) for details.

MLE defines minimum level of evaluation requirements. Oil sands developers are encouraged to undertake evaluation programs which exceed these minimums.

Oil Sands Tenure Regulation, section 14

Second- and third-term leases which are subject to approved development plans, and which are meeting the milestones specified in these plans, are considered to be continued producing leases.

Meeting a Minimum Level of Evaluation (MLE)

A minimum level of evaluation must be conducted on all lands for which lease selection or lease continuation is requested.

- If an agreement holder wishes to retain all lands in an agreement, MLE criteria apply to the entire agreement.
- If an agreement holder wishes to retain only a portion of the land specified in an agreement for which continuation has been requested, MLE criteria apply only to the lands for which retention is requested.

Sections of land for which MLE requirements have not been met are excluded from lease selection or lease continuation requests.

More-than-minimum evaluation work on one section cannot be used to qualify another section which does not meet MLE criteria.

When agreement holders request continuation for a portion, not all, of their lands, they may configure the lands in a manner that best suits their ability to meet MLE criteria. However, all the lands should be contiguous. That is, on a map, the lands must lie next to one another or be in contact at their corners, with no spaces or corridors between. Non-contiguous configurations may not be approved.

MLE criteria are similar for both permits and leases. MLE data for each permit or lease must be submitted separately. Drilling or seismic work must be completed **on each section** covered by the permit or lease.

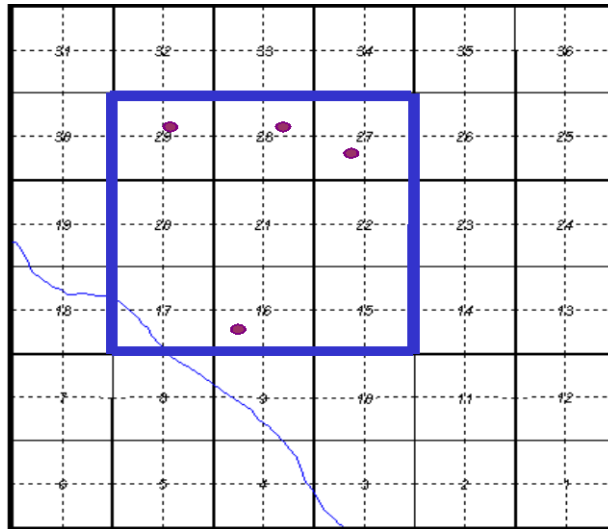


Figure 2: The agreement includes nine sections. Only the four sections which contain evaluation wells are eligible for lease selection or lease continuation. Since the eligible sections are not contiguous, the agreement holder must choose an appropriate configuration. The options are shown in the next figure. For Lease selection, two leases will have to be issued.

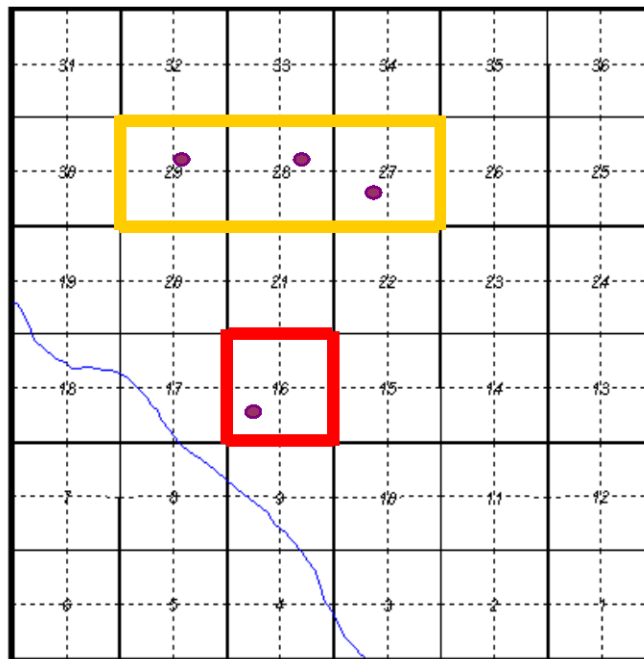


Figure 3: Two options are available to the agreement holder mentioned in the previous figure. The agreement holder may select or continue one or both of the leases shown here. The selection that stands alone may have to be surrendered.

MLE data for permits must be obtained during the term of the permit. The following conditions apply:

- Well data supporting an application for lease selection must come from wells drilled during the term of the permit.

Data obtained from wells drilled prior to the effective date of the permit will not be accepted.

- Seismic data must be acquired during the term of the permit.

Any seismic data which predates the permit must be reprocessed during the term of the permit.

MLE data for lease continuations may predate the effective date of the primary lease.

See [Types of Evaluation Data](#) for details.

The Process

Oil Sands Tenure Regulation, section 3

Evaluation to support applications for lease selection or lease continuation requires the drilling of evaluation wells for the purpose of assessing oil sands zones. A minimum level of evaluation can be achieved in two ways:

- Option 1 complies with section 3(2) of the regulation. This option requires evaluation wells on each section included in an agreement. See Option 1 for details.
- Option 2 complies with section 3(3) of the regulation. This option requires evaluation wells on at least 60% of the sections included in an agreement, and appropriate seismic data for the remaining sections. See [Option 2 - seismic](#) for details.

Wells drilled to evaluate petroleum and natural gas agreements in the location covered by an oil sands agreement may be used to satisfy MLE requirements.

For both options each section or partial section included in the agreement must be evaluated.

Option 1: Evaluation Wells on Each Section

Section 3(2) of the regulation outlines the requirements for this option.

1. An evaluation well must be drilled on each section or part of a section for which lease selection or lease continuation is requested.
2. Evaluation wells must be positioned in a sufficiently even and uniform pattern.

The department prefers a pattern which demonstrates 100% coverage, with evenly interspaced wells on every section or subsection covered by the oil sands agreement.

Patterns for less than 100% coverage should display reasonably uniform placement of wells.

Wells should be drilled throughout the area included in the agreement. Patterns which show clusters of wells in one area and no wells in other areas should be avoided.

3. **Well data** must be provided for each evaluation well used to obtain MLE.
4. **Core data** must be provided for at least 25% of the evaluation wells. This data may be obtained by

coring through the hydrocarbon-bearing portions of the relevant oil sands zones,

or

coring through the hydrocarbon-bearing portions of the oil sands zones of at least 15% of the evaluation wells and using downhole tools to obtain coring-equivalent data for the remaining evaluation wells.

For example

Assume that 12 evaluation wells have been drilled – one in each of the 12 sections. Core samples must be provided for 25% of the wells. In this case, 25% is three wells.

Core data can be provided for each of these three wells,

or

Core data can be provided for two of the evaluation wells (15% of the total drilled) and downhole data can be provided for the third well. The result is coring or coring-equivalent data for the required 25% of evaluation wells.

See [Well Data](#) and [Coring and Coring Equivalent Data](#) for details.

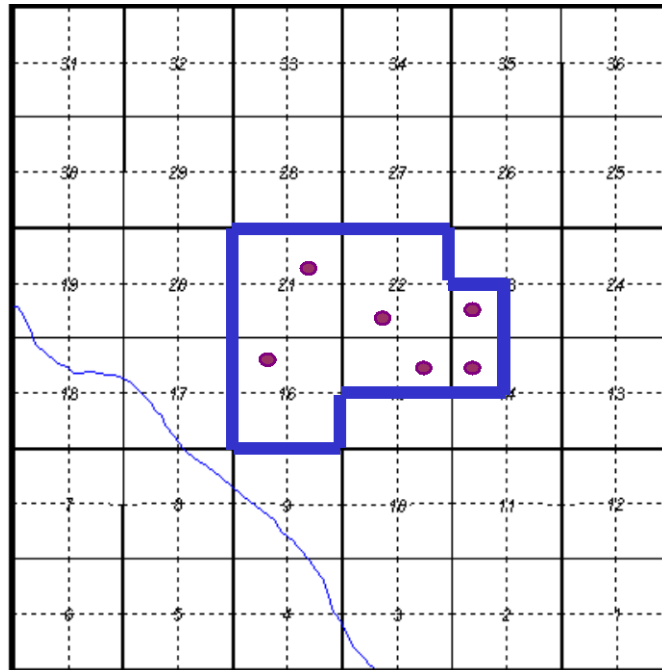


Figure 4: This agreement includes six sections or partial sections—that is, sections 14, 15, 16, 21, 22, and 23. To meet MLE criteria under Option 1, evaluation wells must be drilled on all six sections.

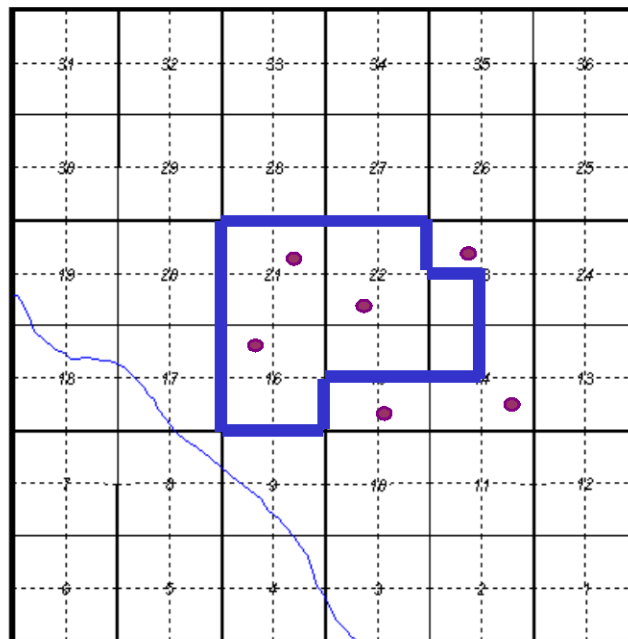


Figure 5: Six evaluation wells are required to meet MLE criteria under Option 1. The wells drilled on sections 14, 15, and 23 are not eligible because they are located outside the boundaries of the agreement area.

Option 2: Evaluation Wells on 60% of Sections

Section 3(3) of the regulation outlines the requirements for this option.

1. An evaluation well must be drilled on at least 60% of the sections or parts of sections for which lease selection or lease continuation is requested.
2. Evaluation wells must be positioned in a sufficiently even and uniform pattern.

The department prefers a pattern which demonstrates 100% coverage, with evenly interspaced wells on every section or subsection covered by the oil sands agreement.

Patterns for less than 100% coverage should display reasonably uniform placement of wells.

Wells should be drilled throughout the area included in the agreement. Patterns which show clusters of wells in one area and no wells in other areas should be avoided.

3. **Well data** must be provided for each evaluation well.
4. **Core data** must be provided for at least 25% of the evaluation wells.

This data must be obtained by coring through the hydrocarbon-bearing portions of the relevant oil sands zones.

Downhole data is not acceptable under Option 2.

5. **Seismic or electromagnetic data** from each undrilled section or part of a section must be submitted.

There must be 3.2 kilometres of seismic data line from each full section.

The length of the seismic data line from each partial section must be proportional to the length of the section.

See [Seismic Data](#) for details.

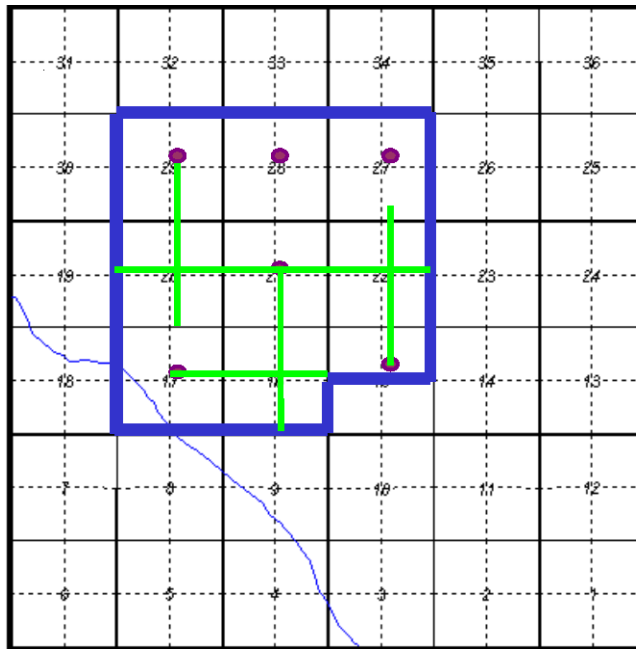


Figure 6: This agreement includes nine sections or partial sections. To meet MLE criteria under Option 2, evaluation wells must be drilled on at least 60% of the sections—that is, on six of the nine. (60% of 9 is 5.4, which is rounded up to 6.) Seismic or electromagnetic data must be provided for the remaining three sections. 3.2 km of seismic data line is required on each of these three sections.

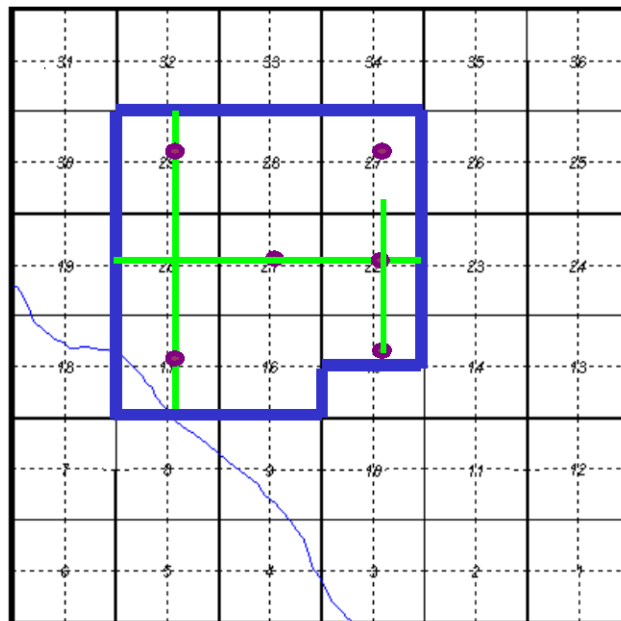


Figure 7: This agreement requires 9.6 km of seismic line (3.2 on each of the three undrilled sections) to meet MLE criteria under Option 2. Two of the three undrilled sections have no seismic data lines at all. Although there are 12 km of seismic data line over the whole agreement, the “extra” seismic (8.8 km) on the evaluation well sections cannot be used to qualify the two sections that do not have any seismic data.

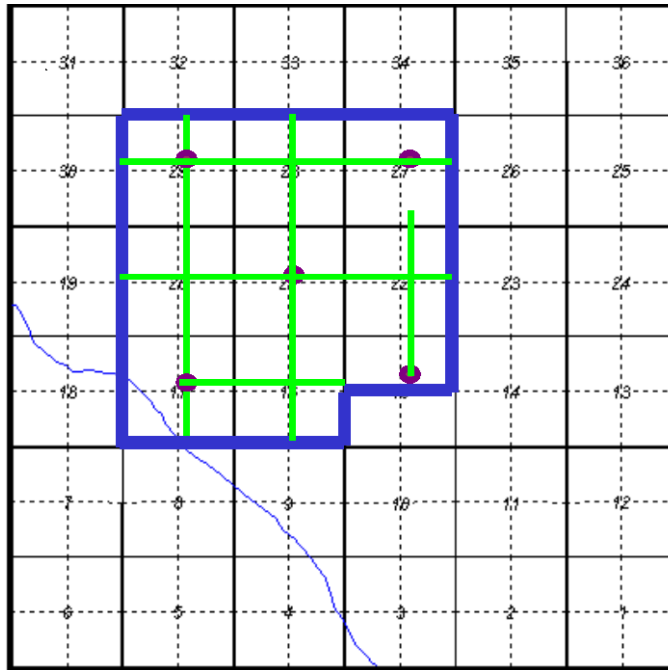


Figure 8: As there are only five evaluation wells drilled, MLE under section 3(3) is not an option: fewer than 60% of the sections include evaluation wells. Although seismic data lines have been obtained for every section, these cannot be considered under section 3(3) unless additional evaluation wells are drilled.

Special Circumstances

Oil Sands Tenure Regulation, section 3(6)

MLE requirements apply to each section for which lease selection or lease continuation has been requested. This makes it possible for the department to obtain consistent data for all disposed oil sands rights. Nonetheless, the Minister may consider and approve, on a case-by-case basis, applications in which MLE requirements have not been met.

Lessees who face unique, exceptional circumstances may request special consideration. The Minister may waive some requirements or impose different MLE requirements. In most cases, these revised requirements will provide information equivalent to what is specified in the regulation.

When the Minister grants special allowances, applicants are required to submit a comprehensive technical report. The report must provide the details specified in [Applying for Lease Continuation](#) and [Applying for Lease Selection](#).

Agreement holders who have questions about the MLE requirements for particular agreements should contact the department as early as possible. The department will provide an advance ruling on the evaluation work that has been done or proposed. See [Advance Rulings](#) for details.

The department cannot provide assurance that requests for special consideration will be approved.

Types of Evaluation Data

Well Data

For oil sands evaluation purposes, the department currently accepts well data regardless of the ownership or original intention of a drilled well. The department also accepts data from currently producing wells which have not been cored.

Note

The period during which well data is collected is an important factor for lease selection.

For Lease Selection

Well data supporting an application for lease selection must come from wells drilled during the term of the permit.

Data from wells which have been re-entered during the term of a permit *may* meet MLE criteria. The eligibility of data from such wells is at the department's discretion. In most cases, if re-entry produced additional data, the well is considered to have met the MLE requirement.

Re-evaluation of well logs which predate the issuance of a permit does not meet MLE criteria. It does not provide the required new data.

For Lease Continuation

Well data supporting an application for lease continuation may predate the effective date of the primary lease.

Although leaseholders are encouraged to obtain new data during the term of the lease, there is considerable latitude regarding the type of well data that is eligible for meeting MLE criteria. At present, the department accepts purchased well data, as well as data from

- historical wells,
- wells drilled on a shared basis,
- horizontal wells, and
- wells owned by parties other than the agreement holders (once the status of these wells is no longer confidential).

Coring and Coring Equivalent Data

Coring produces a continuous cylinder of rock cut from a wellbore. We require coring to be obtained using full diameter core barrels. Core samples provide information about the characteristics of an underground formation.

The department does not consider the downhole tool requirements specified in current ERCB regulations to be equivalent to coring.

Seismic Data

Oil Sands Tenure Regulation, section 3(4)

Seismic data can be used in place of data from evaluation wells. To ensure that the data is comparable to what would have been available from drilling; the seismic data must originate from the section where an evaluation well would otherwise have been drilled.

Note:

For Lease selection, seismic data must be acquired during the term of the permit, and any seismic data, which predates a permit, must be re-processed during the term of the permit.

Required Length of Line

3.2 kilometres of seismic data line must be obtained on each undrilled section for which lease selection or continuation is requested.

For each partial section included in a lease or permit, the length of the seismic data line must be proportional to the length of the partial section. That is, the ratio of “partial” seismic data line to 3.2 km must be the same as the ratio of partial section to full section.

For example:

A section contains 256 hectares. If an oil sands agreement comprises 128 hectares, the ratio is 256 to 128, or two to one. The same ratio applies to the required length of seismic data line. This means that 1.6 km of line are required. (3.2 km to 1.6 km is a two to one ratio.)

Seismic Requirements

The fold, station, and group interval of the seismic program must be adequate to image both the bitumen reservoir and the Devonian subcrop.

Seismic shooting parameters should be at least 15 fold, with a maximum group interval of 10 metres.

Note:

Peace River Oil Sands Area – Lessees who hold agreements in this area should contact the department regarding seismic requirements for MLE purposes. In some cases, it may not be necessary to image the Devonian subcrop.

Seismic data lines must tie to evaluation wells in a manner and to an extent that the Minister considers adequate.

Seismic data lines along a road allowance may be used for evaluation purposes. Such data will be considered for only one of the sections adjacent to the road allowance. The agreement holder may choose the applicable section.

Arithmetic averages based on the total number of sections may not be used to fulfill MLE requirements.

For example:

Consider a lease selection request for 29 sections. Evaluation wells have been drilled on 17 sections (slightly less than 60%). Twelve sections are undrilled. Seismic testing has been conducted for 29 miles (46.4 km), on both the drilled and undrilled sections of the land.

To meet MLE requirements, the lessee must drill an additional well: this will bring the well count to 18—slightly more than 60%. Each of the 11 undrilled sections must have 3.2 kilometres of seismic data lines. This means that 35.2 km (3.2 km x 11 sections) are required.

For additional examples of how seismic requirements are calculated - See [Figure 6](#), [Figure 7](#), and [Figure 8](#).

Electromagnetic Data

Oil Sands Tenure Regulation, section 3(5)

Electromagnetic data can be substituted for seismic data.

- Electromagnetic data may only be used as evaluation data for areas where the ERCB has determined that surface mining is possible.
- For evaluation purposes, electromagnetic data must be provided for the base of the deepest oil sands zone for each section or partial section.

Note

Electromagnetic data to support lease selection must be obtained during the term of the permit.

Chapter 5

Assessing Production

Continued Leases

When a lease is continued, it is classified as

- producing
- or
- non-producing

Non-producing continued leases are subject to escalating rents. The payment schedule and requirements are discussed in [Chapter 6](#).

Oil Sands Tenure Regulation, section 1(q)

A producing lease is one in which “oil sands are, in the opinion of the Minister, being produced from a zone or zones in the location of the lease.” The regulation takes an all or nothing approach: it makes no provision to designate part of a continued lease as producing and part as non-producing. This reduces the administrative burden both for industry and for the department.

Minimum Levels of Production

In order for producing status to be assigned, a lease must meet a department-defined minimum level of production (MLP). This benchmark was established after the department reviewed the production histories of a representative sample of leases from each oil sands area.

The required minimum level of production per term year* is 2,400 m³ of bitumen per section (40 barrels per section per day), on average, over the lease term.

Oil Sands Tenure Regulation, section 14

Second- and third-term leases which are subject to approved development plans, and which are meeting the milestones specified in these plans, are considered to be continued producing leases.

MLP is calculated as an average for the entire lease, not on a section-by-section basis. Nevertheless, as shown in [Figure 9](#) and [Figure 10](#), the calculation considers all of the sections included in a lease.

For a primary lease, MLP is calculated as the average production in the final 12 months of the lease term. For a continued lease, the MLP is calculated as the average production in a term year. See [MLP example](#)

The MLP requirement is the same for all leases, regardless of the type of recovery (mining or in situ) used.

Note

If the required MLP has not been attained, a lease is subject to escalating rent. See [Chapter 6](#) for details.

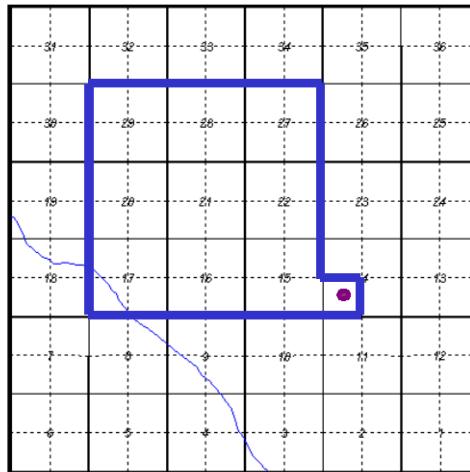


Figure 9: This lease includes 9.25 sections. The MLP requirement is 2,400 m³ per section. This means that MLP is achieved if production from the lease meets or exceeds 22,200 m³ per year (9.25 x 2,400)—even though all the production is coming from a single well producing at a rate of 1,850 m³ per month

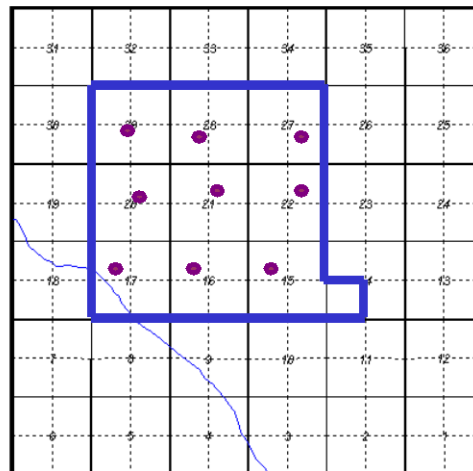


Figure 10: Although this 9.25-section lease has a producing well on nearly every section, MLP is only achieved if the total production from the lease meets or exceeds 22,200 m³ per year—that is, 9.25 x the required minimum of 2,400 m³ per section. Even though production from some wells might exceed this minimum, the MLP calculation is based on the lease as a whole. For example, if three wells each produced 2,400 m³ per year and six wells each produced at 2,000 m³ per year, total production for the lease would be 19,200 m³. This is not enough to meet the MLP requirement.

Production Criteria

MLP is the only criterion used to determine the producing status of a lease. The following measures are not accepted:

- recoverable reserves or functions of recoverable reserves,
- royalty payment,

Royalty is attributed to individual wells at any level of production. Since royalty is not necessarily related to the lease as a whole, it is not an appropriate indicator of MLP.

- assessments of sales versus operating costs, and
- ERCB-approved schemes.

Schemes may incorporate all or portions of several leases in a variety of permutations which may be amended from time to time. While leases covered under ERCB schemes are approved for production, production is not required.

Changing a Lease Designation

Producing to Non-Producing

A producing lease is redesignated as non-producing if it has produced below the required MLP in each of three successive term years.

Lessees are notified if the department has reason to question the producing status of a lease. If producing status no longer applies, the department issues a notice advising that the lease status will be changed to non-producing.

Lessees may respond to a change-of-status notice in three ways:

- They may submit information that demonstrates production.
See [Minimum Levels of Production](#) for criteria defining minimum levels of production.
- They may surrender their lease.
See [Surrender](#) for details.
- They may choose to accept the change in designation and begin to pay escalating rent according to the prescribed schedule.
See [Chapter 6](#) for details.

Oil Sands Tenure Regulation, section 22(2)

The change from producing to non-producing status takes effect on the term anniversary date of a lease. The entire lease is subject to escalating rent as of this date.

For example

A primary lease is continued as producing on October 14, 2001. For the next three years (2001–2002, 2002–2003, 2003–2004), the lease does not deliver the required minimum level of production. The department issues a notice of non-producing status on November 4, 2004. The change is effective as of October 14, 2004. Escalating rent is payable for the term year October 14, 2004 to October 14, 2005. Escalating rent is payable every subsequent year, until such time as the lease is re-designated as producing.

Section 22 is discretionary: the Minister may choose not to invoke it if a lessee can demonstrate that production is in decline prior to well abandonment.

Production Cycling

Oil Sands Tenure Regulation, section 21 and 22

The *Oil Sands Tenure Regulation* make it possible for a lease to maintain its producing designation if production meets the MLP requirement for one year, but falls short for two immediately following years. Such production cycling would most likely occur in the case of wells using primary recovery methods. The cycle could be repeated indefinitely to avoid having the lease redesignated as non-producing—and to avoid paying escalating rent.

“One-on, two-off” cycling is inconsistent with the requirement for diligent, continuous production, which is implicit in the regulation.

Oil Sands Tenure Regulation, section 23

The Minister may require a lessee to increase production, within a certain period, to a prescribed level. This provision overrides MLP criteria and can be used to prevent the use of production cycling as a means of avoiding a non-producing lease designation.

Non-Producing to Producing

Lessees may apply to have their leases reclassified from non-producing to producing status. It is the lessee's responsibility to inform the department if producing status requirements have been met.

Requests to reclassify a non-producing lease as producing must be supported by technical data which verifies production. Department staff will use the Petroleum Registry of Alberta to confirm if production levels meet the required minimum levels of production.

Requests to reclassify a lease as producing are reviewed within 30 days of receipt. If minimum levels of production were met or exceeded for the preceding term year, the department reclassifies the non-producing lease as producing. The newly assigned producing status takes effect on the next term anniversary date. Escalating rent applies until the current term year is complete.

For example

If a continued producing lease does not deliver the required minimum level of production for three consecutive years, the department classifies the lease as non-producing as of its term anniversary date October 14, 2004. In 2006, production levels exceed the required minimum and the lessee applies to have the non-producing lease changed to producing. The change is approved by the Minister and takes effect on the next term anniversary date, October 14, 2007. Escalating rent does not have to be paid for the term year October 14, 2007 to October 14, 2008—or for subsequent years, as long as minimum level of production is maintained.

Chapter 6

Escalating Rent

Oil Sands Tenure Regulation, section 15

Non-producing continued leases are subject to payment of escalating rent. Escalating rent serves to stimulate the development of oil sands resources. They provide an incentive for leaseholders to develop these resources at the appropriate time (considering market signals); using appropriate technology (refers to cost-effective alternatives).

A Fair Return

One of the goals of Alberta's oil sands tenure system is to ensure that oil sands agreements are in the hands of those who are committed to developing them. Developers who choose to keep non-producing continued leases may hold these leases indefinitely, but only if they pay escalating rent. In making this accommodation, the Crown forgoes bonus bids it might have acquired had ownership reverted to the Crown, and had the rights been re-leased to a new developer. The escalating rent structure compensates for this foregone opportunity.

Escalating rent areas, escalating rental rates, and doubling periods are designed to capture, on average, the foregone bonus bid value that a lease might have acquired over a 15-year period. Fifteen years is considered an appropriate period for lease development; this is why primary leases are issued for a 15-year term.

The department conducts periodic reviews of the escalating rent structure. These reviews examine a number of factors, including

- the effects of new and improved technology,
- changes in the bonus bid cycle, and
- the effects of the *Oil Sands Tenure Regulation*.

A number of reviews will have been completed before any continued lease is subject to the maximum escalating rent. This ensures that the cap is neither too high nor too low.

Deductions and Credits

Lessees may reduce or eliminate their escalating rent obligations by

- conducting exploration or development work on the non-producing lease,
- conducting research that directly applies to the non-producing lease, or
- earning credits for upgrading oil sands bitumen.

See [Deductible Expenditures](#) and [Upgrader Credits](#) for details.

Paying Escalating Rent

Rent is incurred for each term year in which a continued lease is designated as non-producing.

The department issues a billing statement at the end of each term year in which escalating rent is incurred. If the lessee does not pay or submit an allowable cost credit report within 30 days, cancellation procedures may commence.

See [Cancellation](#) for details.

Payment obligation resides with the designated representative for the lease.

See [Designated Representatives](#) for details.

Note

Escalating rent is payable at the end of each term year.

Annual rent for a lease is due at the beginning of each term year.

Interest is charged on any late payments.

Calculating Escalating Rent Payments

Oil Sands Tenure Regulation, section 16

The amount of an escalating rent payment depends on two factors:

- the oil sands area in which the lease is situated
- the length of time for which the lease has been designated as non-producing

Escalating Rent Areas

Escalating rents apply in two oil sands areas

- **Area A** includes leases in the Peace River Oil Sands Area and in the Athabasca Oil Sands Area, with the following exceptions:
 - leases in the surface mining areas
 - leases in the Wabasca area, defined as the land between ranges 16 to 26 (inclusive), and townships 76 to 86 (inclusive), west of the 4th Meridian
- **Area B** includes leases in the Cold Lake Oil Sands Area as well as leases in the surface mining area (as revised on June 10, 2009, pursuant to ERCB's "Alberta's Reserves 2008 and Supply/Demand Outlook 2009-2018" report) and the Wabasca area, which are defined as exceptions to Area A.

See [map of Escalating Rent Areas A and B](#).

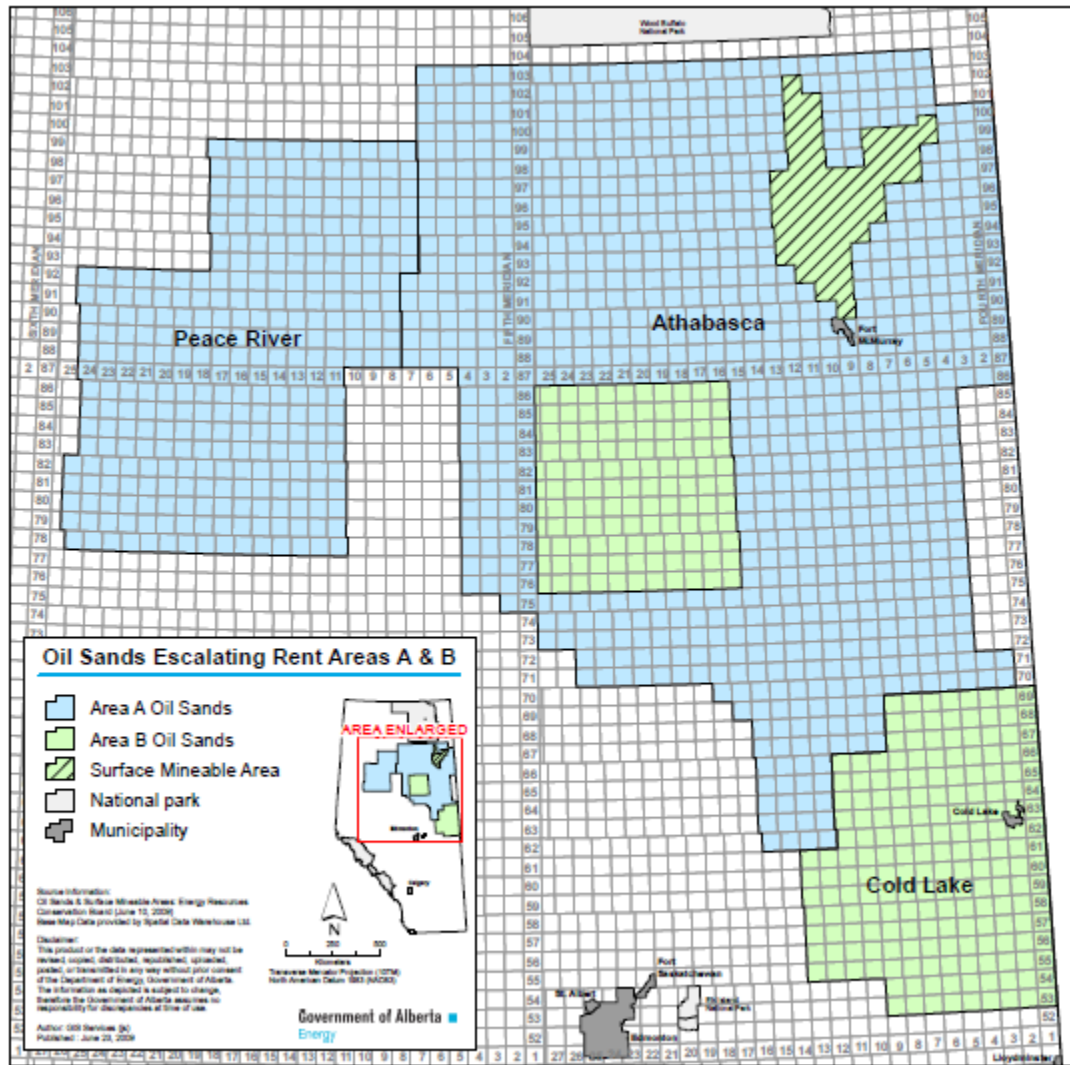
Oil Sands Escalating Rent Areas A & B

Figure 11: Oil Sands Escalating Rent Area A and Area B (Surface Mineable Area expanded June 10, 2009).

Escalating Rent Amounts

YEAR	AREA A	AREA B
1	\$3/ha	\$7/ha
2	\$3/ha	\$7/ha
3	\$3/ha	\$7/ha
4	\$6/ha	\$14/ha
5	\$6/ha	\$14/ha
6	\$6/ha	\$14/ha
7	\$12/ha	\$28/ha
8	\$12/ha	\$28/ha
9	\$12/ha	\$28/ha
10	\$24/ha	\$56/ha
11	\$24/ha	\$56/ha
12	\$24/ha	\$56/ha
13	\$48/ha	\$112/ha
14	\$48/ha	\$112/ha
15	\$48/ha	\$112/ha
16	\$96/ha	\$224/ha
17	\$96/ha	\$224/ha
18	\$96/ha	\$224/ha
19	\$96/ha	\$224/ha
20 + over	\$96/ha	\$224/ha

Table 1: The escalating rent payment schedule for Oil Sands Areas A and B.

The escalating rent for Area A begins at \$3 per hectare and doubles every three years until a cap of \$96 per hectare is reached, when the lease enters its 16th year of non-production.

For example

Over the first nine years of a non-producing continued lease, cumulative escalating rent payments for a 36-section (9,216-hectare) lease would total \$581,000. At this point, the lease would have been in effect for 24 years—for 15 years as a primary lease and for nine years as a continued lease. After 18 years of non-production, the escalating rent payments would total \$5.2 million. More than half this amount would be payable in the last three years. At this point, the lease would have been held for 33 years.

The escalating rent for Area B begins at \$7 per hectare and doubles every three years until a cap of \$224 per hectare is reached, when the lease enters its 16th year of non-production.

For example

Consider a 36-section (9,216-hectare) parcel. Over the first nine years of a non-producing continued lease, cumulative escalating rent payments would total \$1.35 million. After 18 years of non-production, the escalating rent payments would total \$12.2 million, more than half of which would be payable in the last three years.

For leases which straddle Areas A and B, escalating rent calculations are pro-rated according to the number of hectares in each area.

For example

In its first year of non-production, a lease which has 64 hectares in Area A and 128 hectares in Area B would be subject to escalating rents of \$192 (\$3/ha x 64 ha) and \$896 (\$7/ha x 128 ha) for the two respective portions, for a total of \$1,088.

When a non-producing lease is reclassified as producing, the escalating rent schedule is suspended. If the lease is subsequently deemed non-producing, the original payment schedule resumes. That is, for the purpose of rent payment, the lease is assumed to be in the same year as it was when payments were last required. Escalating rent is paid at the rate which last applied.

For example

Consider a non-producing continued lease in Area A. The lease is designated as producing at the end of its fifth year, at which time the escalating rent calculation is based on \$6/ha. Assume that, nine years later, the lease is reclassified as non-producing. At this time, rent applies as if the lease were in the sixth year of its escalating rent schedule: the payment due is based on a rate of \$6/ha. The following year, escalating rent is calculated at \$12/ha, as if the lease were in its seventh year.

Upgrader Credits

Oil Sands Tenure Regulation, section 20

Lessees can reduce their required escalating rent payments if they are eligible for upgrader credits.

A lessee who is upgrading crude bitumen derived from the oil sands within the location of the lessee's lease using either the lessee's upgrader or, under written contract, another person's upgrader may apply to the Minister for upgrader credit.

This provision of the regulation supports the development of an Alberta-based upgrading sector.

Calculating Upgrader Credits

Oil Sands Tenure Regulation, Schedule 2

The following formula is used to calculate upgrader credits:

$$UC = BI \times 0.1 \times AF$$

or

$$UC = BI \times 0.1 \times (AF \text{ for API of upgraded product} - AF \text{ for API of feedstock bitumen})$$

UC represents upgrader credits, expressed in hectares per year.

BI is the average barrels per day of feedstock bitumen derived from the company's eligible oil sands leases and supplied to its Alberta-based upgrader during the term year.

AF is an allocation factor which reflects the level of upgrading that took place during the term year. It is determined by subtracting the API gravity of the feedstock bitumen from the API gravity of the upgraded product. The **API gravities** used to calculate allocation factors represent the **annual averages** for the feedstock and the output respectively.

Upgrader credits cannot be earned for upgraded bitumen produced from a lease that is subject to a development plan, approved under section 9 of the former Oil Sands Regulation, when production is less than what is required by the plan. Only bitumen produced in excess of the production level required by the plan is eligible for upgrader credits. See example 3 in the following section.

ALBERTA OIL SANDS TENURE GUIDELINES
A u g u s t 1 4 , 2 0 0 9

API GRAVITY	ALLOCATION FACTOR
10° or less	0.00
11°	0.02
12°	0.04
13°	0.06
14°	0.08
15°	0.10
16°	0.12
17°	0.14
18°	0.16
19°	0.18
20°	0.20
21°	0.24
22°	0.28
23°	0.32
24°	0.36
25°	0.40
26°	0.52
27°	0.64
28°	0.76
29°	0.88
30° or higher	1.00

Table 2: Allocation Factors

Examples of upgrader credit calculations

Example 1:

Company A owns a 150,000 b/d-capacity upgrader in Alberta. It upgrades an annual average of 100,000 b/d of 10° API feedstock produced from its own leases. The upgraded output averages 32° API over the course of a year

Company A has a contract with **Company B**. It upgrades an annual average of 50,000 b/d of 8° API feedstock produced by Company B into a 30° API output. Both companies are eligible for upgrader credits.

Company A's upgrader credits are calculated as follows:

$$\begin{aligned} UC &= BI \times 0.1 \times (AF \text{ for API of upgraded product} - AF \text{ for API of feedstock}) \\ &= 100,000 \times 0.1 \times (1.00 - 0.00) \\ &= 10,000 \text{ ha} \end{aligned}$$

Company B's upgrader credits are calculated as follows:

$$\begin{aligned} UC &= BI \times 0.1 \times (AF \text{ for API of upgraded product} - AF \text{ for API of feedstock}) \\ &= 50,000 \times 0.1 \times (1.00 - 0.00) \\ &= 5,000 \text{ ha} \end{aligned}$$

Example 2:

Company C owns a 100,000 b/d-capacity upgrader in Minnesota. It upgrades an annual average of 80,000 b/d of 12° API feedstock into a 28° API output.

Company C does not earn upgrader credits, as the upgrader is not located in Alberta.

If the upgrader was located in Alberta,

Company C would earn upgrader credits as follows:

$$\begin{aligned} UC &= BI \times 0.1 \times (AF \text{ for API of upgraded product} - AF \text{ for API of feedstock}) \\ &= 80,000 \times 0.1 \times (0.76 - 0.04) \\ &= 5,760 \text{ ha} \end{aligned}$$

Example 3:

Company D owns a 250,000 b/d-capacity upgrader in Alberta. It upgrades an annual average of 240,000 b/d of 10° API feedstock into 30° API output. The bitumen is produced from a company-owned surface mine that is subject to a development plan under section 9 of the former Oil Sands Regulation. The production level approved by the plan is 180,000 b/d.

Company D's upgrader credits are calculated as follows:

$$\begin{aligned} UC &= BI \times 0.1 \times (AF \text{ for API of upgraded product} - AF \text{ for API of feedstock}) \\ &= (240,000 - 180,000) \times 0.1 \times (1.00 - 0.00) \\ &= 6,000 \text{ ha} \end{aligned}$$

Applying Upgrader Credits

Upgrader credits must be applied in the year they are earned. Unused credits cannot be carried forward.

Companies may apply upgrader credits against any lease for which escalating rent is payable. However, credits can be applied to several leases only if the escalating rent for one lease has been reduced to zero first. Any remaining credits can be applied to reduce a second lease payment to zero, and so on.

Examples of how upgrader credits are applied

Example 1:

Company A has earned 10,000 ha in upgrader credits. It owns three non-producing leases. Leases are in either Area A or Area B.

Lease A1— 5,000 ha located in Area B

—the escalating rent requirement is at the start rate of \$7/ha.

Lease A2 — 4,000 ha, and

Lease A3 — 4,000 ha are located in Area A.

—the escalating rent requirement for each are in the 4th year at \$6/ha.

Since 10,000 ha upgrader credits have been earned, Company A can;

- apply 5,000 ha upgrader credits against Lease A1,
- apply 4,000 ha upgrader credits against Lease A2, and
- can apply the remaining 1,000 ha upgrader credits against Lease A3.

Once the credits have been applied, the escalating rent of \$6/ha against the remaining 3,000 ha in Lease A3 is still required.

Example 2:

Company B has earned 5,000 ha in upgrader credits. It owns two non-producing leases. Leases are in Area A.

Lease B1—2,000 ha located in Area A
— the escalating rent requirement is at the start rate of \$3/ha.

Lease B2—6,000 ha in Area A
—the escalating rent requirement is in its 7th year at \$12/ha.

Company B can choose;
- not to apply any credit to Lease B1, and
- apply all 5,000 ha upgrader credits against Lease B2;

Since there is not enough credit to offset all the ha for each lease, escalating rent is still required as follows:

\$3/ha against 2,000 ha in Lease B1 and
\$12/ha against 1,000 ha in Lease B2.

Example 3:

Company C has earned 6,000 ha in upgrader credits. It owns only one non-producing lease. Lease is in Area B.

Lease C1—5,000 ha in Area B
—the escalating rent requirement is in its 13th year at \$112/ha.

Company C can apply 5,000 ha of upgrader credits against Lease C1.
This means that 1,000 ha of credits are unused: Unused upgrader credits may not be carried forward.

Deductible Expenditures

Expenditures incurred for research, exploration, and development activities may be used to offset or reduce escalating rent payments.

Oil Sands Tenure Regulation, section 17(3)(h), 18(c), and 19(d)

█ Deductible expenditures cannot be applied more than once.

Eligible Expenditures

Deductible expenditures may not reflect more than fair market value. They must be

- directly attributable to the lease,
- reasonable in relation to the circumstances under which they were incurred,
- incurred by or on behalf of the lessee,
- incurred for actual financial transactions, and
- incurred on or after the effective date of the continued lease.

See [Fair Market Value](#) for details.

Exploration

Oil Sands Tenure Regulation, Schedule 1, item 2

Exploration costs may be used to offset escalating rental if they are incurred to evaluate a lease or to bring it into production.

Evaluation involves more rigorous assessments than exploration. It identifies the quality and quantity of the resource for the purpose of determining if the resource can be economically developed.

Exploration refers to activities undertaken for the purpose of identifying the existence and areal extent of a resource. Exploration activities typically include geological and geophysical work.

- Drilling or other work which exceeds the prescribed minimum level of evaluation (MLE), and which does not qualify as a development cost, may be claimed as an exploration cost and used to offset escalating rent.

See [Chapter 4](#). for details about MLE

All oil sands wells* drilled in a section are considered exploratory until at least one oil sands well has been drilled in each quarter of the section. Subsequent oil sands wells drilled in the section are considered developmental.

An **oil sands well** is one which is drilled to penetrate an oil sands deposit for the purpose of evaluating the deposit or bringing it into production.

The definitions of exploratory and development wells apply to vertical and horizontal wells, regardless of the recovery methodology used (mining, thermal in situ, or primary-cold in situ).

Development

Oil Sands Tenure Regulation, schedule 1, item 3

Development costs may be used to offset escalating rentals if they were incurred to develop the lease, or to bring it into production. For development costs to be eligible, they must be

- physically incurred on the lease site, or
- incurred for the development of oil sands in the location of the lease.
 - In other words, off-lease costs may be allowable. This is not the case for exploration costs.

Development costs are costs incurred to bring a lease into production within the next five years. Specific examples include the cost of

- capital infrastructure such as roads, power facilities, buildings, bitumen processing facilities, well pads, disposal facilities, and tanks,
- observation, test, and disposal wells,
 - Oil sands wells are considered developmental only if a well has already been drilled on each quarter of a section. In this case, the next well drilled within the section is considered developmental. Until there is a well on each quarter section, all new wells are considered exploratory.

- Capital costs incurred to put a well in place or bring it into production are considered development costs.
- mine equipment acquisition and installation,
- surface preparation,
- regulatory approvals for production,
- business case and feasibility studies,
- landowner and stakeholder consultations, and
- environmental studies.

Lessees who use 3D or more sophisticated seismic techniques to assess reservoir production parameters may request that these be accepted as development costs.

Research

Oil Sands Tenure Regulation, schedule 1, item 1

The costs of basic, fundamental or applied research may be used to offset escalating rentals if they are incurred to address economic, environmental or technical problems associated with oil sands recovery.

Costs related to specific, directly applicable consortium research activity may be eligible.

- Funding a specific, university-based project in order to receive the research data and conclusions is an example of an eligible consortium research activity.

Expenditures Which Are Not Allowed

Oil Sands Tenure Regulation, schedule 1, items 4(2) & 4(3)

The following expenditures may not be used to offset escalating rent:

- ongoing operating expenditures associated with recovering oil sands,
- overhead or administrative expenditures, including expenditures incurred by a lessee, operator, designated representative or affiliate for internal audits, in-house legal services or other, similar services,
- borrowing or financing expenditures, or charges for late or deficient payment,
- penalties of any type,
- royalty interest (including Crown royalty), carried interest, net profit interest, or any similar interest,
- annual lease rental or escalating rental expenditures,
- expenditures incurred in acquiring an interest or estate in mineral rights,
- expenditures related to depletion or depreciation,
- expenditures related to the non-arm's-length transfer of research or technology,
- expenditures incurred as a result of acts or omissions which breach the laws, rules or regulations of a government or government agency,
- fees or expenditures related to dispute resolution, including arbitration or litigation of any dispute with any party,
- food, beverage or entertainment expenditures,
- taxes (including GST) paid to municipal, provincial or federal governments,
- credits or discounts awarded to operators, designated representatives or affiliates to offset an eligible expenditure,
- any economic assistance (other than reductions in income tax payable) that is provided to the lessee, operator, designated representative or affiliate by the

Province of Alberta or the Government of Canada (or an agency of either) for the purpose of reducing or offsetting costs, and

- expenditures which have already been used to offset escalating rent for the same or another lease.

All deductible expenditures are subject to a financial audit.
See [Financial Audits](#) for details.

Research costs are also subject to a concept audit.
See [Concept Audits](#) for details.

Exploration

Exploration expenditures incurred before a lease has been designated as continued are not eligible.

Off-lease exploration costs are not eligible.

Development

Costs arising from the actual production, handling or sale of product are not eligible. The following are examples of ineligible costs. The list is not exhaustive.

- well operating costs
- maintenance
- trucking or pipelining
- marketing

Research

- Research management costs and fees for membership in associations such as Canadian Oil Sands Network for Research and Development (CONRAD) are not allowed.
- Costs related to non-arm's-length transfers of proprietary research or proprietary technology (including research publications and licensed research or technologies) are not allowed.
See [Fair Market Value](#) for details.

Timing and Carry-Forwards

An eligible expenditure is deemed to be incurred

- in the month in which the cost is payable—that is, when the obligation to pay arises—if payment is made within three months of the time when the cost was incurred,

or
- in the month in which the cost is paid, in any other case.

For a non-arm's-length transaction where no invoice has been issued, expenditure is deemed to have been incurred in the month in which services were supplied or materials were received.

See [Non-Arm's-Length Transactions](#) for details.

Exploration

If exploration is undertaken during the term of a continued lease, eligible expenditures may be used to offset escalating rent only for the year in which they were incurred.

Development

If development is undertaken during the term of a continued lease, eligible expenditures may be used to offset escalating rent only for the year in which they were incurred.

Like research costs, eligible development costs incurred during the last five years of the primary term of a lease are eligible against escalating rent for the first 10 years of the continued term. This approach recognizes that the company is doing more than what is required for the lease to be classed as continued. The additional development work is helping to put the lease into production as quickly as possible.

Research

The *Oil Sands Tenure Regulation* recognizes that research can occur at any time. Specific timing-related rules have been developed as a result. For escalating rent offsets, the life of a research project is considered five years or less, regardless of the duration of the research project described in the application. See [Making an Application](#) for details.

- Where the life of a research project exceeds five years, the lessee must identify which consecutive five-year period should be considered for determining allowable costs.
- Once a project period has been identified, it is recorded by the department and may not be changed.

If eligible research costs have been incurred during the last five years of the primary term of a lease, the costs are eligible against escalating rent for the first 10 years of the continued term. This approach recognizes that the company is doing more than what is required for the lease to be classified as continued. The research is helping to put the lease into production as quickly as possible.

If research has been undertaken while the lease is classified as continued non-producing, eligible costs may be used in any year of the term of the research project, or carried forward for two years.

	PRE-CONTINUATION		POST-CONTINUATION		
ALLOWABLE COSTS	INCURRED	CREDITED	INCURRED	CREDITED	ALLOCATED AMONG LEASES
RESEARCH	within the last 5 years of the primary lease. must be within the lifespan of the research project	within the first 10 years of continuation	anytime within the life of a project, for a maximum of 5 years	in any term year of the lease that coincides with a project year, plus 2 years after life of project.	subject to the allocation identified in the authorization for expenditure document and DOE approval.
DEVELOPMENT	within the last 5 years of the primary lease	within the first 10 years of continuation	in the term year of the lease.	same year as incurred.	subject to the allocation identified in the authorization for expenditure document and DOE approval.
EXPLORATION	not applicable	not applicable	in the term year of the lease	same year as incurred.	not applicable

Table 3: The Timing Eligibility for Allowable Costs

Making an Application

Lessees or designated representatives who wish to apply offsetting costs to their escalating rent payments must apply to the department by submitting an Escalating Rent Offsetting Costs (EROC) form which

- clearly identifies the lease agreements to which the costs apply,
- describes the costs, and
- is signed by one of the lessee's corporate officers or by the designated representative.

When an application pertains to more than one lease, all lessees and the designated representative must complete the EROC form.

Applications to use research credits or development costs on a carry forward basis or to allocate expenditures to more than one lease must also include

- a Registration of Allocated Expenditures (RAE) form,
- the accompanying approval granted by the department, and

- an authorization of expenditure form or a comparable budgetary approval document which outlines how expenditures will be allocated.

Department pre-approvals, if these have been obtained, should also be attached. See [Pre-approval of Deductible Expenditures](#) for details.

When research and development costs are claimed to offset escalating rent, the allocations must correspond to those approved in the submitted budgetary document.

See [Allocating Costs](#) for details.

All Oil Sands related forms are available from the Oil Sands home page, left menu, Forms & Reporting

Authorization of Expenditure

An authorization of expenditure form (or comparable budgetary approval document) must be submitted when application is made to use research or development expenditures as offsets to escalating rent. This document creates a paper trail which facilitates the audit process and ensures accountability.

The budgetary approval document must accommodate various types of expenditures, including allocations to capital or operating budgets. It must provide

- a statement of intent which supports the “direct connection and application” test, and
- a description of planned expenditures.

Annual and cumulative amounts must be provided.

The corporate officer authorizing the expenditure must sign the document.

In addition to the above-stated requirements, the budgetary document for a research project must also identify

- the purpose of the research,
- the nature of the research project and its scope,
- the research participants,
- the research timeframe,
- expected deliverables and due dates,
- the leases to which the research expenditures are to be allocated,

**S U P P O R T I N G
I N F O R M A T I O N**

Supporting information may be provided by more than one document. However, all documents must be linked through a budgetary approval form which outlines the corporate decision to undertake lease activities.

Agreement numbers and lease locations must be provided.

- the location of research , and

Supporting rationale must be provided if the research project is located outside Alberta.

- any financial support which is being provided through Alberta programs or from other jurisdictions.

Note

Individual lessees may each submit their own budgetary approval documents. Although the documents do not need to be identical, each submitted form must be similar in terms of authority, wording, and content.

Supporting information may be provided by more than one document. However, all documents must be linked through a budgetary approval form, which outlines the corporate decision to undertake lease activities.

Who can submit expenditure information

Applications to offset escalating rent are sometimes made by the designated representative of a lease.

See [Designated Representatives](#) for details.

A lessee who intends to use research or development expenses to offset the escalating rent for a lease must provide the RAE reference number to the designated representative. If this number is not provided when an application is submitted to the department, the costs may be disallowed.

See [Allocating Costs](#) for details.

The RAE and its reference number are intended to protect the confidentiality of each lessee's research and development activities. When submitting an application on behalf of other lessees, the designated representative only needs to know

- the amount by which each lessee intends to reduce its share of the lease's escalating rent , and
- the RAE reference number.

Lessees are not required to share the details of their research programs with their designated representatives. To protect the confidentiality of this information, they may use EROC forms to submit the details of their research or development plans directly to the department.

See [Making an Application](#) for detail or all Oil Sands related forms are available from the Oil Sands home page, left menu, Forms & Reporting

When designated representatives submit their own EROC for the lease, they should

- specify the expenditures they are claiming,
- identify the RAE reference number, and
- note that other lessees will submit separate EROC.

Note

All lessees should be prepared to support their claims of eligibility for escalating rent offset costs. Supporting information must be available for the department's review during concept audits and financial audits.

Pre-approval of Deductible Expenditures

Lessees are strongly encouraged to apply for pre-approval before undertaking research or development activities. This minimizes the risk that expenditures will be disallowed during the department's final audits.

See [Financial Audits](#) for details.

The department typically responds to a formal application for pre-approval within 45 days.

Note

Although costs may be pre-approved, they may nevertheless be disallowed once the department's financial and concept audits are completed. Pre-approved costs may be disallowed when there have been substantial changes to originally submitted research or development plans.

If a cost is adjusted during the department's final audits, escalating rent is recalculated. The designated representative is responsible for resolving escalating rent adjustments. This responsibility is not diminished if the lessee who originally claimed the research costs no longer holds an interest in the lease.

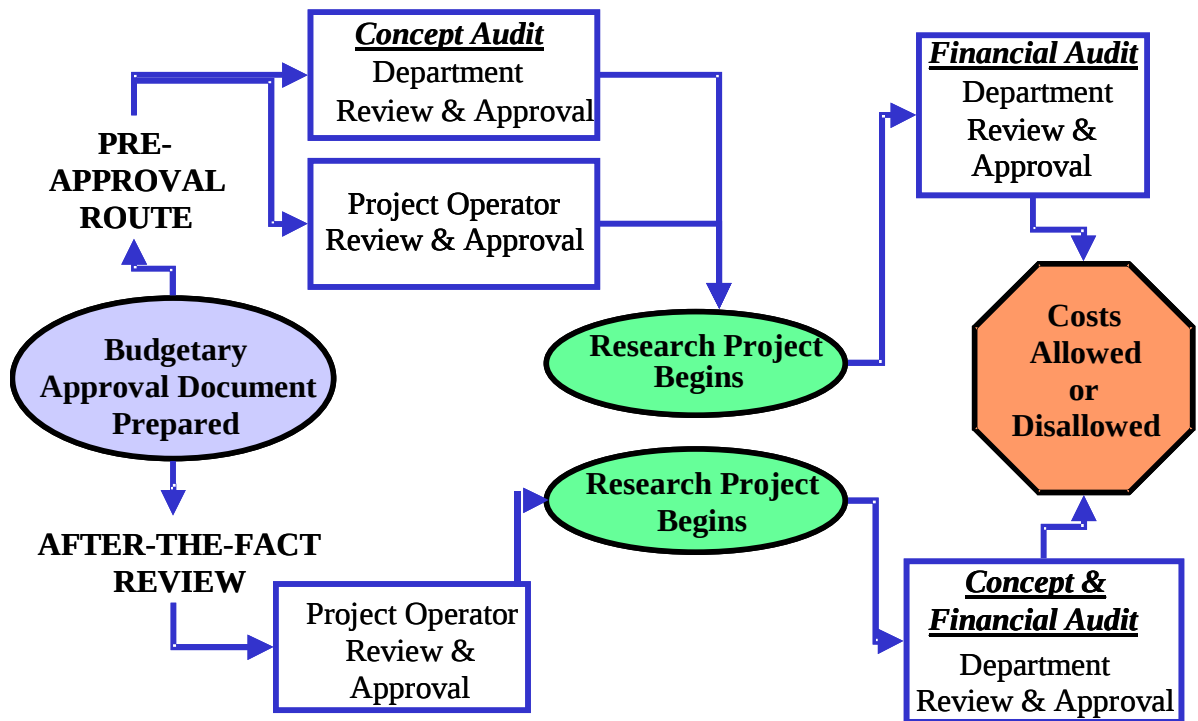


Figure 12: The Research Review Process

Allocating Costs

Lessees who wish to use research or development expenditures to offset escalating rent must submit a RAE form. The RAE must be accompanied by an authorization for expenditure form or comparable budgetary documents which

- approve the proposed expenditures
- identify what percentage of each expenditure will be allocated to each lease

Authorization of expenditure forms are company specific, they must be signed by the appropriate corporate officer.

When applications to offset escalating rents are submitted, actual costs must be allocated in accordance with the proposed plan. If the allocated amounts have not been fully expended, costs will be allocated on a pro-rated basis.

See [Authorization of Expenditure](#) for details.

All Oil Sands related forms are available from the Oil Sands home page, left menu, Forms & Reporting.

For example

Consider a research or development proposal for which \$5 million has been allocated to five different leases. This allocation is noted on the RAE form and the accompanying authorization for expenditure. If only \$2.5 million is actually expended, \$500,000 is assigned to each lease to offset escalating rent.

The department confirms acceptance of the RAE and provides the lessee with a reference number. The lessee should retain the original RAE and the department's confirmation letter and record the RAE reference number.

If a lessee cannot provide the RAE reference number when an application is made to offset escalating rent, submitted expenditures may be disallowed.

Note

Research or development expenditures may be applied against more than one lease. In the case of developmental expenditures, the leases must be within reasonable proximity. A general guide is that there must be less than 50 km between the farthest two points of any of the leases.

Transferring Costs

When partial or whole interest in a lease is transferred, costs which can be carried forward may follow the lease if they have been identified on the applicant's EROC form. If such costs are disallowed during a Crown audit, the current lessees or their designated representatives are responsible for making up any shortfall in escalating rent.

See [Timing and Carry-Forwards](#) for details.

When lands are surrendered during a period for which escalating rent is being calculated, a pro-rated portion of the claimed expenditures is deemed ineligible, regardless of why or where the costs were incurred.

Due Diligence

Current lessees or their designated representatives are responsible for acquiring or arranging access to all cost documentation used to offset previous years' escalating rents.

They are responsible for conducting due diligence and making appropriate provisions when transferring leases which are subject to escalating rent charges. This is particularly important when escalating rent charges are offset by costs which have not been audited by the Crown.

Conditions

Congruence with the Royalty Regime

Research and development costs applied against escalating rent may also be eligible as costs under the *Oil Sands Allowed Costs (Ministerial) Regulation*. If research or development costs are to be used under the *Oil Sands Allowed Costs (Ministerial) Regulation* and under the *Oil Sands Tenure Regulation*, the same authorization for expenditure must be used for cost allocation purposes.

See [Authorization of Expenditure](#) for details.

For example

A \$3 million research program is being planned. On the company's authorization for expenditure form, the cost is equally allocated to three leases. Each lease is assigned \$1 million—one third of the projected cost. Only one of the leases is associated with a royalty-paying project.

For royalty purposes, the maximum cost that can be included in the project's royalty calculation is \$1 million. None of this amount could be applied to the royalty calculation for an off lease royalty project.

Lessees may wish to consider the royalty implications associated with allocating research or development expenditures as credits against escalating rent.

Net Expenditures

The Crown recognizes net expenditures only. If a lessee recovers research or development costs from other industry participants, these revenues must be deducted from the expenditures claimed against escalating rent.

If a lessee receives credits or discounts, regardless of the source, these must be used to offset actual research or development expenditures. Any balances can then be applied against escalating rent.

All credits or discounts must be reported to the department.

- Research credits received from programs in Alberta or other jurisdictions in which the research is recognized are included in this condition.
- Economic assistance in the form of income tax reductions is excluded.

Amendments

If a lessee amends an authorization for expenditure after a research activity has begun, the department reviews the entire research activity and re-assesses its scope and applicability to the identified leases.

If the department believes that the intent of the amendment is to re-allocate costs among leases (even if the re-allocation involves the same leases as before), and if the scope of the research has not changed, it may disallow all costs related to the research activity.

Non-Arm's-Length Transfers

Costs related to non-arm's-length transfers (See [Non-Arm's-Length Transactions](#) for details) of proprietary research or proprietary technology (including research publications and licensed research or technologies) are not allowed. Allowing non-arm's-length transfers could undermine the allocation process for distributing research and development costs among different leases.

This condition is not intended to exclude research activities performed by affiliated companies. (See [Affiliates](#) for details) However, eligible expenditures incurred by affiliates are subject to the non-arm's-length rule.

Companies who are concerned that a particular research expenditure falls into a grey area are encouraged to request written clarification from the department.

Assigning Costs

The department can recognize an expenditure only once.

If proprietary research or proprietary technology (including research publications and licensed research or technologies) is sold, the purchaser may be eligible to use the purchase cost to offset escalating rent. In this situation, the purchaser and the seller must agree which of them will have the right to apply the incurred expense against escalating rent. The agreement may take one of two forms.

1. The seller may provide the original authorization for expenditure to the department. This ensures that the department recaptures the revenue resulting from any activity whose cost is used to offset escalating rent. It makes it possible for the department to determine whether the seller is using the expenditures to offset escalating rent.

If the department accepts the purchaser's costs, the revenue received by the seller must go toward reducing the research expenditures the seller is claiming. This may occur retroactively.

2. A sales agreement may include a provision that the buyer agrees not to apply the purchase cost against escalating rent. This has administrative advantages. When this option is used, neither the department nor the seller need to adjust previous years' escalating rent calculations.

Note

By default, in the absence of an agreement explicitly stating that the purchaser can claim the research expenditure, eligibility to claim the expense remains with the seller.

Audits

All audit-related information submitted to the department and its auditors is kept confidential, pursuant to the provisions of the *Freedom of Information and Protection of Privacy Act*.

Concept Audits

All research costs, claimed by a lessee or designated representative, are subject to a concept audit, in which the department verifies that the purpose of the research is directly attributable to the lease.

For example, a lessee may be conducting applied research which has marginal applicability to the lease. A concept audit might conclude that such research does not meet the “direct connection and application” criteria required by the *Oil Sands Tenure Regulation*. In this case, the costs would be ineligible for offsetting escalating rent. Alternatively, the audit might conclude that a proportion of the costs are eligible. In this case, the auditor would verify that the allocation of expenditures to leases was consistent with what was approved by the department when the applicant’s Registration of Allocated Expenditures form was filed.

See [Making an Application](#) for details.

In conducting a concept audit to determine the eligibility of research costs, the department considers

- how the research advances knowledge which has specific, practical application to the lease,
- the type and nature of deliverables, and
- the location of the research activity.

Off-lease research may be eligible if it is directly related to the development of a lease. Supporting documentation must be provided to show why an off-lease location is preferable, especially if the research is being conducted in facilities outside Alberta.

Note:

Research does not have to be successful. However, for the research expenditures to be eligible as offsets to escalating rent, the research must demonstrate the potential to provide meaningful insight or understanding of a problem that is preventing a lease from producing in commercial quantities.

Financial Audits

All exploration, development, and research expenditures claimed by a lessee or designated representative are subject to a financial audit conducted by the department. The audit ensures that claimed expenditures are

- reasonable,
- have specific, practical application for the lease, and
- reflect an actual financial transaction that is supported by appropriate documentation.

The authorized expenditure form (or comparable budgetary approval document) that is submitted when an application is made to offset escalating rent facilitates the audit process and ensures accountability. This document creates a paper trail and supports the link between a corporate decision to undertake a specific activity and the actual expenditure and results.

The department's audit group follow the trail of the authorized expenditure form, which, along with all supporting documentation, is reviewed by the auditors in the lessees' or designated representative's offices.

Definitions

The following definitions apply in the interpretation of the *Oil Sands Tenure Regulation*. They may or may not be applicable in other situations.

Affiliates

A company is considered affiliated with another company if the criteria outlined in subsection 1206(5) of the *Income Tax Regulations* apply. However, in making this determination, paragraph 1206(5)(a) shall be read as if it were replaced by the following:

The **Income Tax Regulations** are governed by the Income Tax Act (Canada).

- a) a person and another person (in this paragraph, referred to as "that other person") are connected with each other if
 - (i) the person and that other person are not dealing at arm's length,
 - (ii) the person has an equity percentage in that other person that is not less than 10%, or
 - (iii) where the person is a corporation, the corporation and that other person are linked by another person who has an equity percentage in each of them of not less than 10%.

Companies are not dealing at arm's length with each other if they would not be considered dealing at arm's length under the *Income Tax Act* (Canada).

Fair Market Value

The determination of fair market value is based on comparable, open market transactions among unaffiliated parties. The Minister makes determinations of fair market value and assesses what constitutes a “comparable open market” on a case-by-case basis.

In determining fair market value for the exchange of goods or services between affiliates, the Minister may consider

- the published price of comparable goods or services, if that price is generally adopted by buyers and sellers, and
- the average price paid for comparable goods or services during transactions by unaffiliated buyers and sellers.

The prices used to determine fair market value may be adjusted to reflect transportation or delivery costs.

Solution Gas

Mines and Minerals Act, section 87.1

Solution gas means gas that is dissolved in crude oil or crude bitumen under initial reservoir conditions, and includes any such gas that evolves as a result of changes in pressure, temperature or both, due to human disturbance.

Solution gas is disposed under agreements granting oil sands rights and not under agreements of petroleum and natural gas. However, solution gas is subject to royalty provisions under the *Natural Gas Royalty Regulation (NGRR), 2002* or *NGRR, 2009*.

Non-Arm's-Length Transactions

If eligible exploration, development or research expenditures involve an affiliate or a non-arm's-length transaction, that transaction must be evaluated in accordance with approved non-arm's length business rules.

The following considerations apply to all items provided to a lessee, operator or designated representative by an affiliate.

Goods and Services

The allowed cost of a good or service is the lesser of

- a) the amount charged to the lessee, operator or designated representative
- b) fair market value, when a reasonable determination can be made
See [Fair Market Value](#) for details.
- c) the actual expenditure incurred by a lessee, operator, designated representative or their affiliates (or by the person from whom the good or service was obtained) to produce the good or perform the service

Capital

Capital assets are valued when the asset is delivered to the lease site. The value is the lesser of

- a) the amount charged to the lessee, operator or designated representative
- b) fair market value, when a reasonable determination can be made
See [Fair Market Value](#) for details.
- c) the asset's net book value to the lessee, operator or designated representative, or to the person from whom the asset was obtained by the lessee, operator or designated representative.
See [Net Book Value](#) for details.

Amount Charged

In relation to a capital asset, good or service, the amount charged is the lesser of

- a) the price that a lessee, operator, designated representative or their affiliates charges other lessees in relation to the capital asset, good or service
- b) the amount charged to a lessee, operator, designated representative or their affiliates by the person who provided the capital asset, good or service
- c) the amount that the lessee, operator, designated representative or their affiliates report to the Crown in relation to the capital asset, good or service

Net Book Value

Net book value used to determine deductible expenditures is the remaining undepreciated amount of an asset—as recorded in the financial records of the lessee, operator, designated representative or other person who provided the asset. In other words, net book value is the original cost less accumulated depreciation.

Note

If a capital asset has been claimed under another tenure or royalty regime—such as the *Oil Sands Royalty Regulation (OSRR), 1997* or *OSRR, 2009*, *Oil Sands Allowed Costs (Ministerial) Regulation*, the *NGRR, 2002* or *NGRR, 2009*—the department's records are used to assign net book value.