

RE: AER Bulletin 2016-16: A Chilling Announcement on the First Day of Summer

In a fundamental shift in the landscape for oil and gas transactions, on June 20, 2016 the AER quietly published AER Bulletin 2016-16 in response to the decision of the Alberta Queen's Bench in the *Redwater* decision (*Redwater Energy Corporation (Re)*, 2016 ABQB 278). Asserting the need for "changes to minimize the risks to Albertans" arising from the *Redwater* decision, **effective immediately** the AER has introduced the following three interim regulatory requirements for transfers of AER regulated assets:

- As a condition of transferring existing AER licences, approvals, and permits, **the AER will require all transferees to demonstrate that they have a liability management ratio (LMR) of 2.0 or higher immediately following the transfer.**
- The AER will consider and process all applications for licence eligibility under *Directive 067: Applying for Approval to Hold EUB Licences* as **nonroutine** (*affecting timing and degree of scrutiny of such applications for approval*) and may exercise its discretion to refuse an application or impose terms and conditions on a licence eligibility approval if appropriate in the circumstances.
- For holders of existing but previously unused licence eligibility approvals (*i.e. new entrants*), prior to approval of any application (including licence transfer applications), the AER may require evidence that there have been no material changes since approving the licence eligibility. This may include evidence that the holder continues to maintain adequate insurance and that the directors, officers, and/or shareholders are substantially the same as when licence eligibility was originally granted.

The impact that this sudden and dramatic regulatory change will have on the economic recovery of the oil and gas business in Alberta will play out over the next weeks and months, but it is expected to have a chilling effect on the rise in transaction activity in a province struggling to get back on its feet following a two year long rut in commodity prices. Although the requirement to maintain an LMR of 2.0 post-transfer only applies to transferees of assets, it has the potential to stop a significant number of creative good faith transactions designed to ensure that environmental liabilities do not land in the lap of the Orphan Well Association or otherwise become the responsibility of the people of Alberta. The changes are not intended to impact corporate transactions; however, parties should bear in mind the resulting LMR of any post-transaction entity and the effect on subsequent asset transactions.

The AER has indicated that it believes the proposed changes will limit the future exposure of the Orphan Well Association and minimize the risk to Albertans. Instead, we are of the view that Bulletin 2016-16 has the real potential to cause an acceleration of assets finding their way to the Orphan Well Association when good faith transactions cannot be completed due to the impact of the interim regulatory measures described above. Bulletin 2016-16 also indicates that the AER is working on

additional regulatory measures to address the impacts of the *Redwater* decision and we will be continuing to monitor new developments which are sure to be forthcoming in the coming weeks and months.

In raw numbers, and as a result of the changes: 207 licensees (additional 26%) are now below the required threshold to transact as transferees; overall, 569 of 788 licensees (72%) are now below the required threshold to be the transferee of AER regulated assets.

To read the full AER Bulletin 2016-16, visit:

<https://www.aer.ca/rules-and-regulations/bulletins/bulletin-2016-16>