

Ministry
of
Transportation

British
Columbia
Railway
Company



RAILWAY REGULATION OVERVIEW

Presentation to Cabinet
For Information

June 18, 2003

BACKGROUND

- BC Rail is currently provincially regulated under the *Railway Act*
- Outcome of partnership process could shift operations to federal regulation under the *Canada Transportation Act* (CTA)
 - Test of federal regulation is crossing provincial and/or international boundary
 - Test of provincial regulation is operating within British Columbia (operator can apply to be federally regulated even if provincial test is met)
- Regulatory regime has implications for railway operator, shippers and the Province

OVERVIEW

Provincial Regulatory Regime

- *Railway Act* focused on economic regulation rather than market-driven regulation
- Deregulation initiative underway to repeal antiquated, redundant and irrelevant provisions

Federal Regulatory Regime

- Regulatory framework set within context of federal transportation policy – focus is privatization, commercialization and decentralization
- CTA relies on market-driven competition, contains checks and balances when market forces cannot drive competition

RAILWAY OPERATOR

Railway Association of Canada on the CTA:

- Improved productivity, rationalized capacity, restructured labour
- Reduced costs, restored viability, increased investment
- Continental alliances and service improvements
- Specialization resulted in main line economies, short-line flexibility
- Focus now on expanding traffic, improving reliability, service and technology

SHIPPERS

Generally...

- Larger shippers support federal regulation, smaller shippers support provincial regulation

More specifically...

- Interline lumber/panel product shippers - concerned about competition, multi-modal competition does exist
- Grain shippers - concerned about competition, proposed CTA amendments will extend “maximum rate scale” provisions to British Columbia
- Pulp shippers - support Class 1 carrier because of increased access to new North American markets, potential for lower freight rates

PROVINCIAL GOVERNMENT

- Province could lose regulatory control over BC Rail's railway operations
- Creating provincially regulated subsidiary could significantly affect value and may be open to challenge
- Provincial regulation and current labour environment results in BC Rail being 15-18% uncompetitive due to union structure and collective agreement
- Move to Canada Labour Code could create significant synergies and efficiencies, would eliminate need for legislative action by the Province

SUMMARY

In considering potential shift from provincial to federal regulation:

- The Province may be unable to control future regulation
- Railway operators support federal regime
- Provincial regime offers diminishing benefits to shippers
- Many larger shippers support move to federal regime, smaller shippers concerned about competition
- Forcing continued Provincial regulation would impact value, potentially forgoing objectives sought

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RESIDUAL ENTITY AND TIMELINES

Presentation to Cabinet For Information

June 18, 2003

END STATE

British Columbia Railway Company (BCRC)

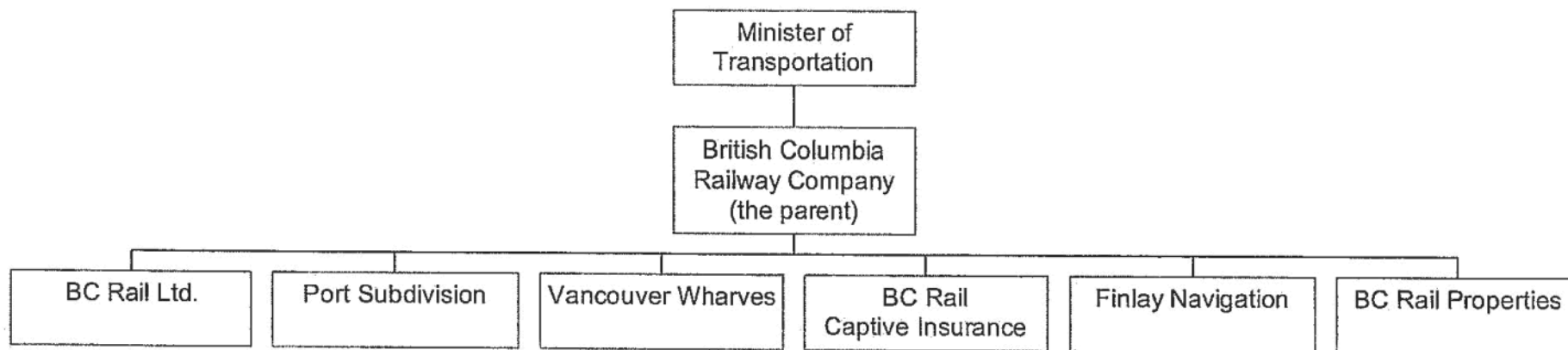
- Parent company created by the *British Columbia Railway Act*
- Province holds shares, cannot sell without legislative change
- Holds title to railway right-of-way, rail bed and track
- Holds and administers the partnership agreement (i.e., long-term lease), could be assigned

END STATE

British Columbia Railway Company (continued...)

- BCRC remains a Crown corporation
- Governance accountability continues to rest with the Minister of Transportation (BC Transportation Finance Authority, Ministry of Transportation)
- Due to complex structure of existing Crown corporation, wind down will be complicated and time consuming

CURRENT STATE



Other Components of Parent Company:

Two Numbered Companies

Three Operating Partnerships

Eleven Other Limited Companies

MEDIUM TERM

Vancouver Wharves

- Subsidiary owned by BCRC
- Offered for sale in 2002 with Casco Terminals and Canadian Stevedoring
- Sale of Wharves suspended due to environmental contamination issues
- Discussions between federal and provincial governments on-going
- Wharves to continue to operate until environmental issues resolved and sale process can resume

MEDIUM TERM

BC Rail Properties

- Real estate subsidiary owned by BCRC
- Evaluation Committee initiating review of portfolio, independent assessment to determine disposition plan focused on maximizing economic return
- Several agencies to assist private sector consultant leading the review (i.e., TNO, LWBC, BCBC, BCTFA/MoT and BCRC)
- Evaluation Committee to report back to Minister of Transportation on disposition plan, timing, roles and responsibilities of other agencies

MEDIUM TERM

BC Rail Captive Insurance Company

- BCRC's insurance for railway operations and other subsidiaries
- Entity will likely have to remain in existence for two years to deal with outstanding insurance claims
- Options are being developed by the Ministry of Finance for review by Minister of Transportation (which may shorten the wind-up time required)

SHORT TERM

Freight Railway

- Partnership process underway, transaction anticipated to close by December 31, 2003

Port Subdivision at Robert's Bank

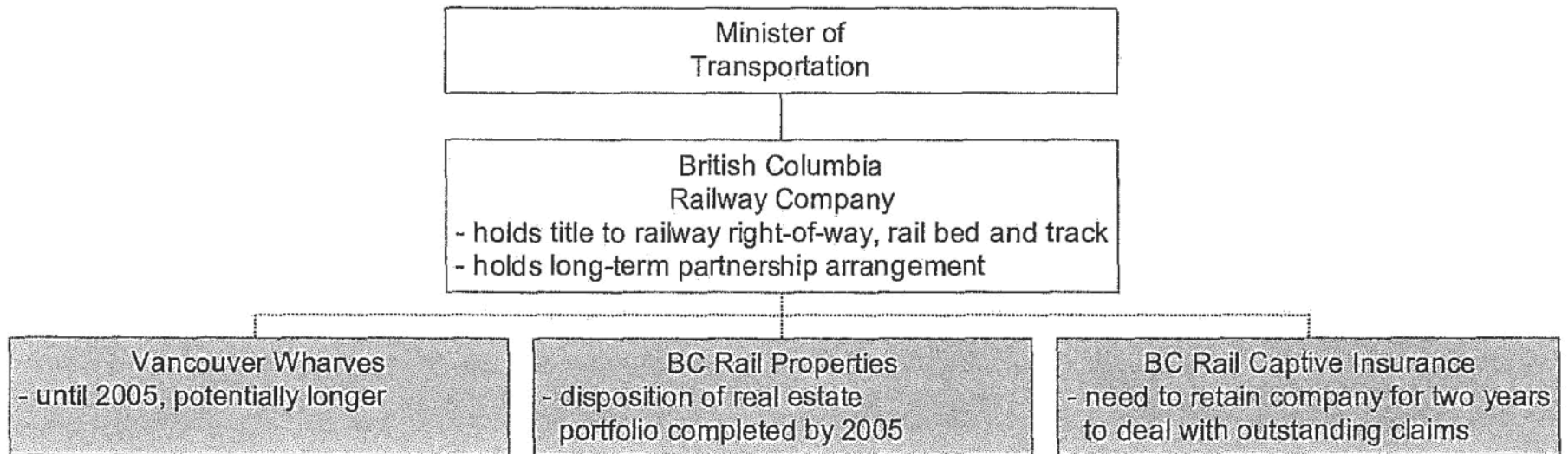
- Subsidiary of BCRC, open access railway link to two major port terminals at Delta
- Disposition process to kick off with engagement of financial advisor by the end of June
- Transaction to be completed concurrent with the freight railway process

SHORT TERM

Finlay Navigation

- Currently an agreement in principle to sell Finlay
- Consent required from Slocan is being withheld therefore, sale process stalled
- BC Rail management working to conclude this disposition as soon as possible

MEDIUM TERM TO END STATE



TIMELINE

Long Term

- Retention of BCRC, holds title to railway lands and long-term partnership arrangement

Medium Term – completed 2005

- BC Rail Properties
- BC Rail Captive Insurance Company (timing could change post-option review)
- Vancouver Wharves (may not be achievable)

Short Term – completed December 2003

- Freight Railway
- Port Subdivision
- Finlay Navigation

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RAILWAY REGULATION OVERVIEW

Presentation to Cabinet
For Information

June 18, 2003

BACKGROUND

- May 15, 2003, process initiated seeking private sector partner for BC Rail freight operations
- Private sector partner could be federally regulated
- BC Rail currently provincially regulated
- Regulatory regime has implications for railway operator, shippers and the Province

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BACKGROUND

- If new operator meets test of federal regulation (i.e., crosses provincial or international boundaries), the railway becomes federally regulated under the *Canada Transportation Act*
- If new operator meets test of provincial regulation (i.e., operates within British Columbia), the railway remains provincially regulated under the *Railway Act*

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Federal Regime

- In order to operate a federal railway company, the Agency issues a certificate of fitness when it is satisfied that a company proposing to construct or operate a railway within the legislative authority of Parliament has adequate liability insurance
- The Agency may also vary existing certificates to reflect changes in railway operations, or suspend or cancel a certificate

Provincial Regime

- Minister of Transportation issues a certificate to railways incorporated under the Act and the company is subject to the legislative authority of the Legislature

REGULATION

- Provincial regulation of railways occurs under the *Railway Act*
 - BC Rail, Southern Railway, E&N, ~45 industrial rail sites, 'amusement' railways and Skytrain
- Federal regulation of railways occurs under the *Canada Transportation Act*
 - Canadian National, Canadian Pacific, Via Rail, Rocky Mountaineer Rail Tours, Burlington-Northern Santa Fe, Amtrak, etc.

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- There are currently 35 federally regulated railways

FEDERAL REGULATION

- Transportation trend in Canada has been towards privatization, commercialization and economic deregulation
- *Canada Transportation Act* implements the federal government's transportation policy and establishes the Canadian Transportation Agency
- The Canadian Transportation Agency, a quasi-judicial tribunal, administers the Act and policies for federally-regulated modes of transportation (i.e., air, rail and marine)

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Canada Transportation Agency:

- Decisions made by the Agency are guided by the notion that transportation users, commercial shippers and individual travellers should receive the protection provided for them in the legislation, if market forces alone do not result in fair, reasonable service
- Current Chair of Agency is Marian Robson of Vancouver, once Corporate Secretary of BC Rail, more recently a Director of the Cascadia Institute
- Agency has 7 members appointed by the Governor in Council for 5 year terms, eligible for re-appointment

Rail and Marine Branch:

- Rate/service complaints
- Disputes between railway companies and third parties involved in railway infrastructure matters
- Applications for certificate of fitness
- Technical advice
- Interswitching rates advice
- Revenue caps for grain
- Costing standards and regulations
- Audit accounting and statistical information systems

FEDERAL REGULATION

- Reflects elements of modern railways:
 - Focus on efficient and effective transportation infrastructure and services
 - Ability for customers and stakeholders to provide input, seek recourse
 - Provision for users, commercial shippers and individual traveller protection
 - Demonstrates strong ties to the North American railway system

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PROVINCIAL REGULATION

- *Railway Act* one of oldest statutes in BC, reflects 19th Century objectives for economic regulation

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PROVINCIAL REGULATION

- MCAWS responsible for Railway Safety Engineering regulatory regime and rapid transit regulation (self-funding)
 - Currently moving forward on harmonization initiative with federal safety system and potentially contracting out of administration
- MoT responsible for incorporation and governance provisions contained in the *Railway Act*

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KEY ELEMENTS:

FEDERAL AND PROVINCIAL
REGULATORY REGIMES

EMPLOYEES

Federal

- Successorship applies, partner seeks to have BC Rail unions/agreements melded with partner's existing unions/agreements through application to Canada Industrial Relations Board

Provincial

- All existing terms and conditions flow with the operations to the partner

Implications

- If provincially regulated, government would need to take statutory action to address labour challenges with BC Rail's 7 private sector unions and potentially amalgamate unions
- Federal regime deals effectively with challenges

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- BC Rail has 1,573 employees, 1,167 are represented by 7 unions, all private sector

- It is estimated that BC Rail is 15-18% uncompetitive with other major railways in Canada primarily because of its inability (or previous unwillingness) to address the significant changes required in work practices, union structure and collective agreement issues

- If the operating partner is provincially regulated, absent specific provincial legislative amendment, all existing terms and conditions would flow with the assets to the partner and remain in force and effect until such time as the partner could negotiate changes or obtain a new structure through a labour board review process

- If the operating partner were federally regulated, although successorship would apply, the partner would likely immediately apply to the Canada Industrial Relations Board to have the former BC Rail unions and their agreements melded into the partner's existing unions and agreements

PASSENGER SERVICE

Federal

- No legal obligation to provide/allow service, existing service considered in route discontinuance process
- Many commercial arrangements currently in place

Provincial

- No longer any legal obligation to provide passenger services (Fall 2002 amendment to *British Columbia Railway Act*)

Implications

- No material impact on operator
- Shippers do not support provision for passenger services

INTERSWITCHING ZONES, RATES

Federal

- Prescribes interswitching regulations and rates, formula based
- Rates periodically reviewed and adjusted by the Agency

Provincial

- No provisions exist

Implications

- If moved to federal regulation, shipper's freight rates would likely increase as BC Rail's current interswitching rates higher

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Interswitching

- If a shipper only has access to one railway carrier at origin or destination, it may have its cars interswitched from the carrier to another at prescribed rates, providing its siding is within a 30-kilometre radius of the point of interchange (can apply for rates beyond 30-kilometres)
- If CN were the new operator, the interswitching rates would disappear altogether, issue would be whether would pass on savings to shippers

PRICING AND RATES

Federal

- Focus is de-regulated environment which fosters competitive, market-based rates and levels of service, grain revenue caps set by Agency

Provincial

- No specific provisions exist, market forces drive rate setting

Implications

- Federal legislation is superior to the provincial for establishing competitive freight rates and includes dispute resolution mechanism
- Cost savings could be passed onto shippers through reduced freight rates

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COMPETITIVE ACCESS REMEDIES

Federal

- Provisions for enhancing competitive access by shippers, particularly captive shippers, to nearest competing carrier

Provincial

- BC Rail has the ability to negotiate running arrangements with any other railway line in BC but other operators not obliged to accept

Implications

- Federal regime assures process for competitive access and dispute resolution for shippers
- Process can result in reduced rates for shippers

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Federal

- Competitive line rates (30+ kilometres) allows the ability for one railway to apply to the Agency for rights to operate over the lines of another railway, if no agreement, Agency sets rate

DISPUTE RESOLUTION

Federal

- Mediation services offered by Agency
- Final Offer Arbitration enshrined in Act

Provincial

- No provisions exist, some shippers have multi-modal transportation options

Implications

- Final Offer Arbitration provides shippers with certainty that disputes will be resolved in timely fashion

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Federal

- In most commercial situations, shippers and carriers negotiated freight rates and levels of service
- Decisions from the Agency are made within 120 days of receipt of all information regarding the complaint
- If negotiations break down, a number of alternatives are available:
 - Mediation
 - Final Offer Arbitration (60 day process, 30 days for freight charges <\$750K)

Provincial

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SERVICE DISCONTINUANCE

Federal

- Process for operational discontinuance of a railway line

Provincial

- No provisions exist

Implications

- With federal regime Province loses ability to oppose service discontinuance (except potentially through lease default or reversion)
- Federal regime allows railway operators to make decisions in economic interest of company
- Shippers will be concerned that service discontinuance will limit competitiveness
- Presents opportunities for short-line operators

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Federal

The process to discontinue operating a railway line is as follows:

1. The company must advertise the availability of the railway line and how it or the operating interest is to be transferred (i.e., sale, lease or otherwise) and its intention to discontinue operating the line if it is not transferred. Bill C-26 will include an additional provision for the advertisement to disclose any agreement between the company and a public passenger service provider and a provision that requires a purchaser to assume the rights and obligations of the existing public passenger service.
2. If another operator does not come forward as a result of the advertising, the company may offer the railway line operations to the federal government, the provincial government, or a municipal or district government (geographically dependent). Bill C-26 will include transit authorities in this list.
3. If an offer to a third party or a government is unsuccessful, the company may discontinue operating the line upon notice to the Canada Transportation Agency.

Re: short-line operators – in Canada 40 short-line and regional operators operate on over 13,000 kilometres of track which is 30% of the entire system

Provincial

- The *British Columbia Railway Act* never contemplated discontinuing railway lines as it was initiated to expand the railway network in BC
- Under Section 160(2) of the *Railway Act*, it states: "A company must not abandon a line of railway without first giving 30 days notice to the minister of the proposed abandonment"

ACCESS TO INFORMATION

Federal

- Federal minister has authority to require railways to provide information, provisions to protect commercially sensitive information

Provincial

- BC Rail exempt from *Freedom of Information and Protection of Privacy Act*, but subject to *Budget Transparency and Accountability Act*

Implications

- No material impact on operator to move from provincial regime to federal regime

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SAFETY REGULATION

Federal

- The *Railway Safety Act, Transportation of Dangerous Goods Act* regulate railway safety for federal carriers

Provincial

- The *Railway Act, Transportation of Dangerous Goods Act* (adopted by provincial regulation) regulate regional carriers
- MCAWS seeking to modernize safety regulation

Implications

- Federal regulation is Quality Management System, provincial performance measures not well defined, inconsistent with federal measures
- No comparable data to determine best outcome
- Regional carriers in BC charged levy for safety regulation

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LEGISLATIVE REVIEW

Federal

- Built-in statutory review of legislation every five years

Provincial

- No specific provisions exist
- s.14

Implications

- Federal regime allows for all stakeholders, including the Province, to provide input to refining the Act on a regular basis, public hearings held
- Regular reviews support changes to legislative framework that are market-driven

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CURRENT FEDERAL REVIEW

- Bill C-26: Transportation Amendment Act, at Committee Stage (started June 2000)
- Amendments fulfill commitment to railway competition, critical infrastructure needs, environmental, safety and security issues
- Significant implication for BC Rail partnership process includes federal review of railway mergers
- Anticipated passage in Fall 2003 (could be delayed by extended public review process and/or federal leadership process)

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- The federal regulatory regime has a built-in statutory review
- Province of British Columbia submitted position on railway competition to the Review Panel in February 2001
- Submission covered:
 - Safety – a railway safety benchmark be set against which any changes to rail competition will be measured
 - Running rights – limited form of negotiated/arbitrated running rights to be provided to regional carriers while ensuring that Class 1 carriers have right to appeal
 - Regional railways – continued need for provincial regulation of regional carriers
 - Mergers – support for federal review of railway mergers
 - Grain – extending the maximum rate scale provisions of the CTA to grain moving into British Columbia
 - Urban access – support for access to urban railways for commuter rail service
- Bill C-26 includes a provision for the federal government to expand the review of mergers and acquisitions to include railways (previously limited to airlines). The purpose of the review is twofold: (1) issues that relate to the public interest within the context of national transportation; and (2) issues that have the potential to prevent or lessen competition that may result from the transaction.

SUMMARY

- The Province will not be able to control how the new partner will be regulated
- Requiring a provincially regulated subsidiary to be established by the partner may not realize the operating synergies, efficiencies and economies sought
- Provincial regulation offers limited benefits to shippers
- Current Provincial regulatory regime works well for regional railways, although concerns have been expressed about safety regulation
- Many of BC Rail's larger shippers support move to federal regime

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The Railway Association of Canada (RAC)

- 56 members, represent virtually all the railways operating in all regions of Canada (large Class Ones, short-lines and regional railways, inter-city passenger, commuter rail and tourist train operators), BC Rail is not a member but does provide data to RAC
- RAC's 2000 submission to the *Canada Transportation Act* Review Panel states that the Act "is helping to drive the following trends:
 - The railways improved productivity, rationalized capacity and restructured labour, with a focus on reducing costs to restore viability and investment
 - Continental alliances and service improvements are enabling and encouraging increased north-south trade while maintaining east-west flows
 - Specialization of railway services is making the optimum use of the comparative advantage of main line economies of density together with short line flexibility and personalized service
 - The industry is now shifting the focus away from rationalization to expanding traffic, with an emphasis on reliability, faster transit times, intermodal and information technology

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RESIDUAL ENTITY AND TIMELINES

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END STATE

British Columbia Railway Company (BCRC)

- Parent company created by the *British Columbia Railway Act*
- Province holds shares, cannot sell without legislative change
- Holds title to railway right-of-way, rail bed and track
- Holds and administers the partnership agreement (i.e., long-term lease), could be assigned

2

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- All of the land ownership that supports the railway will be owned in the long-term by BCRC (land consolidation underway)
- Administration of the lease to be assigned to MoT, obligations will be minimal as lessee will lease "as if it owned"
- Governance of BCRC to include two steps, initial interim board (e.g., Minister, Deputy Minister, etc.) to manage wind-up, second step is to assign accountability of end state BCRC to BCTFA, similar to how the infrastructure for the ferry system has been dealt with

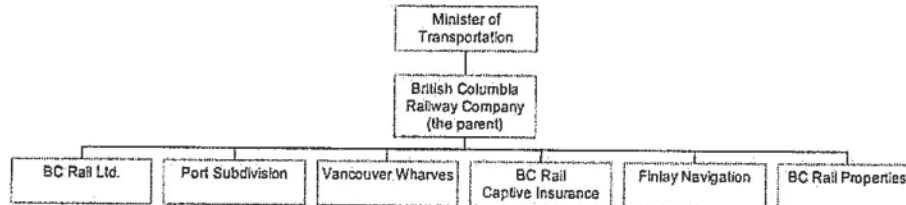
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- BCRC remains a Crown corporation
- Governance accountability continues to rest with the Minister of Transportation (BC Transportation Finance Authority, Ministry of Transportation)
- Due to complex structure of existing Crown corporation, wind down will be complicated and time consuming

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CURRENT STATE



Other Components of Parent Company:
Two Numbered Companies
Three Operating Partnerships
Eleven Other Limited Companies

MEDIUM TERM

Vancouver Wharves

- Subsidiary owned by BCRC
- Offered for sale in 2002 with Casco Terminals and Canadian Stevedoring
- Sale of Wharves suspended due to environmental contamination issues
- Discussions between federal and provincial governments on-going
- Wharves to continue to operate until environmental issues resolved and sale process can resume

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- 75% owned by BC Rail Ltd., 20% by BC Marine, and 5% by BCRC
- Vancouver Wharves is located at the entrance to the Port of Vancouver's main harbor and includes five deep-sea berths (with 900 metres of wharf frontage), 45 hectares of land, tracks for up to 400 railcars and storage facilities
- 2003 revenue estimated to be \$45.0 m with a net income of \$1.6 m

MEDIUM TERM

BC Rail Properties

- Real estate subsidiary owned by BCRC
- Evaluation Committee initiating review of portfolio, independent assessment to determine disposition plan focused on maximizing economic return
- Several agencies to assist private sector consultant leading the review (i.e., TNO, LWBC, BCBC, BCTFA/MoT and BCRC)
- Evaluation Committee to report back to Minister of Transportation on disposition plan, timing, roles and responsibilities of other agencies

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- This entity manages the real estate portfolio for BCRC
- There are 11 full time employees
- The current portfolio generates annual revenues ranging from \$16.0 – 18.0 m and net income ranging from \$8.5 – 10.0 m
- Portfolio consists of surplus buildings, raw developable land, mortgages, surplus lands, and land leases (most leased to major BCRC railway customers)

MEDIUM TERM

BC Rail Captive Insurance Company

- BCRC's insurance for railway operations and other subsidiaries
- Entity will likely have to remain in existence for two years to deal with outstanding insurance claims
- Options are being developed by the Ministry of Finance for review by Minister of Transportation (which may shorten the wind-up time required)

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- Portfolio consists of surplus buildings, raw developable land, mortgages, surplus lands, and land leases (most leased to major BCRC railway customers)

SHORT TERM

Freight Railway

- Partnership process underway, transaction anticipated to close by December 31, 2003

Port Subdivision at Robert's Bank

- Subsidiary of BCRC, open access railway link to two major port terminals at Delta
- Disposition process to kick off with engagement of financial advisor by the end of June
- Transaction to be completed concurrent with the freight railway process

8

- This 37.3 km railway line to the Robert's Bank terminals is not connected to BCRC's freight railway operations and is being treated as a separate entity for disposition
- BCRC owns and maintains the railway infrastructure but does not operate any of its own trains on the line
- The line services two major port terminals on lands leased from the Vancouver Port Authority which are both heavily reliant upon this rail line
- 2003 revenues estimated at \$4.7 m with a net income of \$2.2 m

SHORT TERM

Finlay Navigation

- Currently an agreement in principle to sell Finlay
- Consent required from Slocan is being withheld therefore, sale process stalled
- BC Rail management working to conclude this disposition as soon as possible

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Finlay Navigation

- Based in Mackenzie and provides ferry and barging services to the forest industry
- 2003 revenue estimated at \$8.1 m, net income of \$0.3 m
- Operates as a separate enterprise and runs independently of BC Rail

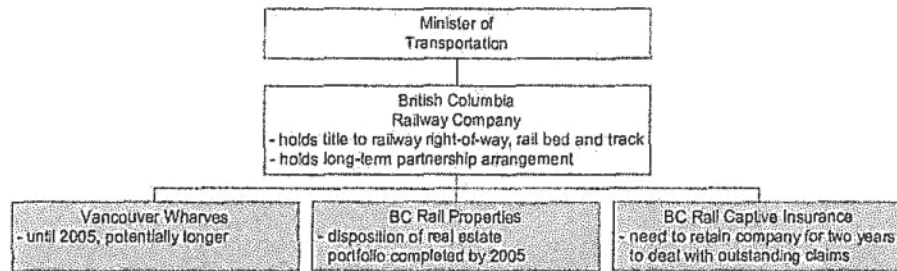
Captive Insurance

- BC Rail Captive was incorporated in 1997 as a BC domiciled Pure Captive
- The Captive provides primary property, primary general liability, primary terminal operator's liability, freight forwarder's liability, automobile physical damage and excess automobile liability coverage to BC Rail and any subsidiary in which BC Rail has a controlling interest
- The Captive is regulated by FICOMM, and co-managed by BC Rail and Aon Insurance Managers
- The Captive has assets of ~\$26.0 m, with a surplus of ~\$10.0 m

Options for Captive Insurance include:

1. Dissolve organization
2. Sold to another insurance company
3. Purchased by private sector operator of freight railway
4. Transfer shares to Province (move from pure captive to sophisticated captive)

MEDIUM TERM TO END STATE



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TIMELINE

Long Term

- Retention of BCRC, holds title to railway lands and long-term partnership arrangement

Medium Term – completed 2005

- BC Rail Properties
- BC Rail Captive Insurance Company (timing could change post-option review)
- Vancouver Wharves (may not be achievable)

Short Term – completed December 2003

- Freight Railway
- Port Subdivision
- Finlay Navigation

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To: Honourable Richard Neufeld
Minister of Energy and Mines

Date: July 31, 2003

CONFIDENTIAL

Re: Cabinet Meeting of July 23, 2003

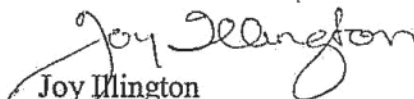
Following is an excerpt from the minutes of the Cabinet meeting of July 23, 2003, for your attention:

C. ITEMS FOR DISCUSSION/DECISION

5. For Decision: Offshore Oil and Gas

Cabinet reviewed a submission "Heartlands" Strategy: Strategy for Development of Offshore Oil and Gas that recommended a development timetable over the next eight years.

Cabinet approved the timetable of actions with one amendment: to remove reference to development in Georgia Strait.


Joy Illington
Deputy Cabinet Secretary

cc: Patrick O'Rourke

**Cabinet Decision Document
Executive Summary**

MINISTERS: Honourable Richard Neufeld, Minister of Energy and Mines
Honourable Rick Thorpe, Minister of Competition, Science
and Enterprise

TITLE: Heartlands Strategy: Strategy for Development of Offshore Oil and Gas

ISSUE: The 2003 Speech from the Throne stated:

"By 2010, your government wants to have an offshore oil and gas industry that is up and running, environmentally sound, and booming with job creation".

To achieve this vision, the Province will pursue an ambitious development timetable as follows.

RECOMMENDATION:

By September 2003

- Finalize approach to federal review of the Queen Charlotte Basin:
 - Offer advice and assistance to federal officials, to ensure provincial views and objectives are taken into account
 - Authorize Ministers Neufeld and Thorpe, and Deputy Minister Dobell to determine the Province's response if Canada asks the Province to play a formal role in the federal review

s.14

By June 2004

- Regarding development in the Georgia Basin (seabed owned by British Columbia)
 - Develop a stand alone provincial fiscal and regulatory regime based on Oil and Gas Commission and existing legislation, including statutory amendments and new regulations where required
 - Pursue private sector partnership to undertake seismic surveys in Georgia Strait
- Be prepared to respond to the federal government's review of the Queen Charlotte Basin, including provincial negotiating positions on federal/provincial fiscal and regulatory arrangements, treatment of existing tenures and First Nations issues

• s.14

- Identify potential marine protected areas in cooperation with key environmental groups and First Nations
- Develop local benefit arrangements with First Nations and communities

By September 2004

- Designate marine protected areas
- Finalize agreement-in-principle with Canada and First Nations on fiscal/regulatory regime

By April 2005

- Conclude negotiations with tenure holders and Canada
- Industry funded seismic surveys underway in Queen Charlotte Basin (seabed ownership in dispute among Canada, British Columbia and Haida) and/or Tofino Basin (seabed owned by Canada)

In longer term

By 2007

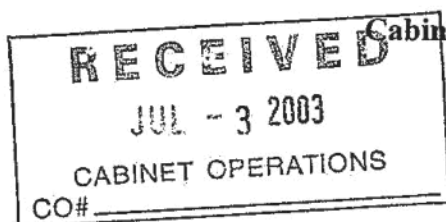
- Conclude final agreement with Canada and First Nations
- Establish fiscal/regulatory regime
- Conclude Seismic testing
- Review application for exploration license
- Begin environmental assessment for exploration activities

By 2008

- Conclude environmental assessment for exploration activities
- Approve exploration license

By 2010

- Begin exploratory drilling



Cabinet Decision Document

Confidential - Cabinet Document
Ministry Document Number 03/03

MINISTERS:

Honourable Richard Neufeld, Minister of Energy and Mines
Honourable Rick Thorpe, Minister of Competition, Science and Enterprise

TITLE:

Heartlands Strategy: Strategy for Development of Offshore Oil and Gas

ISSUE:

The 2003 Speech from the Throne stated:

"By 2010, your government wants to have an offshore oil and gas industry that is up and running, environmentally sound, and booming with job creation".

To achieve this vision, the Province will pursue an ambitious development timetable. This will involve resolution of a range of issues related to First Nations, communities, the federal government, industry and environmental concerns. This submission seeks confirmation of a strategic approach and direction on several specific issues. In particular, the submission focuses on actions designed to lead to seismic exploration of the offshore within the next two years (industry has identified seismic exploration as a key step in their decision making process).

RECOMMENDATION:

Cabinet approve the following:

1. Overall strategic approach to offshore oil and gas development:
 - Achievement of an offshore industry up and running by 2010 through focusing on reducing development timeline while ensuring environmental safeguards are met (e.g., efficient and effective regulatory and environmental assessment processes).

- Mid-term goals:
 - Provincial response to federal government's review of the Queen Charlotte Basin, with provincial negotiating positions on federal/provincial fiscal and regulatory arrangements, treatment of existing tenures and First Nation issues by Spring 2004;
 - Industry funded seismic surveys underway in one or more offshore basins by April 2005.
- Near term goals:
 - Continue working with First Nations, communities, industry and other stakeholders regarding potential development in all basins;
 - Develop local benefit arrangements to provide First Nations and communities with appropriate gains from development;
 - Develop provincial positions for negotiations with federal government (e.g., fiscal and regulatory regimes, treatment of existing tenures);
 - Develop and implement public education and communication actions to provide accurate factual information to the public.

2. Preliminary approach to federal review of Queen Charlotte Basin:

- Offshore Team to continue to offer advice and assistance to federal officials, to ensure provincial views and objectives are taken into account.
- If Canada asks the Province to play a formal role in the federal review, authorize Ministers Neufeld and Thorpe, and Deputy Minister Dobell, to determine the Province's response.
- s.14

3. Strategic Approach to First Nations:

- s.14
- Continue to work with all coastal First Nations to establish arrangements to assist First Nations to identify potential opportunities arising from offshore development.
- s.14

4. Approach to Development in the Georgia Basin:

- Authorize Offshore Team to develop a stand alone provincial fiscal and regulatory regime based on Oil and Gas Commission and existing legislation, including statutory amendments and new regulations where required.
- Authorize Offshore Team to pursue private sector partnership to undertake seismic surveys in Georgia Strait by Spring 2004, using existing Team 03/04 budget.

BACKGROUND:

The oil and gas potential off the west coast of British Columbia is estimated at approximately 9.8 billion barrels of oil and 43.4 trillion cubic feet of gas. Although these resources are unproven, the amounts compare favorably to the northeast portion of the Province from which all provincial production currently derives (estimated reserves of 0.3 billion barrels of oil and 50 trillion cubic feet of gas).

Interest in development of the offshore dates back several decades. Early exploration was not productive, and the Provincial and federal governments have prohibited exploration since 1972 (see Appendix A for a fuller history and Appendix B for a map of offshore basins).

Recently, coastal communities have expressed interest in the potential economic benefits that may arise within and through their provision of services to an offshore oil and gas industry. The oil and gas industry has quietly indicated interest in resuming exploration in the offshore, but has also stated that issues associated with regulatory and fiscal regimes, "no-go" or off limits areas, and First Nations must be resolved before they will invest significant resources.

At the same time, many environmental organizations have come to view the 30 year moratoria as major conservation and protection measures, and are adamantly opposed to any weakening of the moratoria or resumption of any type of exploratory activity. A major focus of recent opposition in other offshore areas has been alleged negative effects of seismic testing on marine mammals. Although modern seismic is generally seen as non-intrusive, and occurs around the world, some opponents allege it has negative impacts. As seismic is industry's key tool in identifying exploration drilling locations, limits on seismic may effectively preclude exploration and development.

Since the May 2001 election, government has taken several steps to further potential development of the offshore. In the July 2001 Throne Speech, Government committed to determine whether offshore oil and gas can be extracted in a way that is environmentally responsible and scientifically sound.

Three reports were subsequently prepared for the government:

- In October 2001, Jacques Whitford Environment Ltd. updated an Offshore Oil and Gas Technology Report completed by AGRA Environment in 1998, but not publicly released. Jacques Whitford extensively reviewed conditions in British Columbia compared to other areas worldwide that have an offshore oil and gas industry. The report found no "fatal flaw" issues that would rule out exploration in British Columbia, and concluded there are no specific design, geohazard or environmental issues that would preclude development of the offshore oil and gas reserves.
- An independent, three-member Scientific Review Panel, appointed in October, 2001 following receipt of the Jacques Whitford report, submitted a report to the Minister of Energy and Mines on January 15, 2002. The panel concluded, "there is no inherent or fundamental inadequacy in the science or technology, properly applied in an appropriate regulatory framework, to justify a blanket moratorium" on offshore oil and gas activities.
- The Premier asked the Northern Caucus to form an Offshore Oil and Gas Task Force to determine the views of residents in northern coastal communities (including First Nations). The task force, consisting of six MLAs, visited nine northern communities and received more than 150 oral and 130 written presentations. On January 15, 2002, they submitted a report to the Minister of Energy and Mines. The report found a high level of interest in development of the offshore oil and gas potential, provided environmental and social concerns are addressed, and coastal citizens are able to participate in the process as well as benefit directly from economic opportunities that arise.

Following receipt of the Scientific Panel and Task Force Reports, in February 2002 the Premier wrote the Honourable Herb Dhaliwal, Minister of Natural Resources, proposing that the two governments commit to a joint work plan directed at development of the offshore. Minister Dhaliwal declined, but did commit to seeking a decision by the federal Cabinet within 12 to 18 months. He publicly made this commitment in June 2002, and indicated he was seeking Cabinet approval to announce a review process.

Following Minister Dhaliwal's rejection of a joint work plan, the Province awarded a \$2 million unconditional grant to the University of Northern British Columbia (UNBC) to undertake research directed at advancing the state of knowledge on offshore matters, and in particular to respond to the Scientific Panel and Task Force Reports. UNBC placed considerable emphasis on ensuring local involvement and undertook broad consultations before developing specific research projects. While this approach produced lower than expected

expenditures in the initial year, UNBC has recently let four major contracts and has established a plan that calls for full expenditure by the end of fiscal 03/04.

In Fall 2002, Treasury Board approved funding from contingencies to the Ministry of Energy and Mines (MEM) for fiscal 02/03 and 03/04 to establish a stand alone group to pursue development of the BC offshore (MEM is to return to Treasury Board with funding options for 04/05 and beyond). The British Columbia Offshore Oil and Gas Team was announced in November 2002 in Policy Action #11 of the provincial Energy Plan. In January 2003, the Offshore Team was officially established. The February 2003 Throne Speech set out the long term goal of an offshore industry up and running by 2010.

On March 28, 2003, Minister Dhaliwal announced a federal review of the Queen Charlotte Basin. He stated the review would involve science workshops led by an independent facilitator, public hearings by a three person panel and consultations with First Nations. He gave February 2004 as the target date for a final report. Since Minister Dhaliwal's announcement, Canada has provided limited information on the intended process.

Canada's only substantive step was the May 20 appointment of Roland Priddle, former chair of the National Energy Board, to head the public hearings. The other two panel members have not been named, nor has the independent facilitator for the science workshops been identified. In light of Canada's limited substantive action, the announced timeline of a final report by February 2004 will be difficult to meet.

Canada rejected the Province's proposal that the review become a joint process. However, the Offshore Team continues to inform federal officials and Mr. Priddle of British Columbia's views and interests and to insist that the federal process not be harmful to these interests. Independent of the federal process, the Team has continued to focus on all offshore basins, and to work with First Nations, coastal communities, industry and other stakeholders.

Since its establishment, the Team has conducted extensive legal and policy research and analysis of fiscal, regulatory, environmental and other issues, and held numerous meetings with First Nations, local communities, the federal government, industry and other stakeholders. The Team has also commissioned public research and development of a communications strategy.

Based on its research and discussions with other parties, the Team has developed a strategic approach to achieving offshore development by 2010 that includes near and mid term goals. This Submission seeks approval of the overall strategy, and specific direction on three issues on which Cabinet direction is required. Future submissions on other issues, including community benefit arrangements and fiscal and regulatory matters, will be made in Fall, 2003.

FISCAL MANAGEMENT CONSIDERATIONS

In the long term, development of offshore oil and gas resources will produce substantial direct and indirect revenues to the province. However, these revenues are several years away and will not materialize unless development occurs.

In the mid term a joint federal-provincial regulatory regime will likely manage and administer all offshore oil and gas activities. Canada and the relevant province fund similar boards on the East Coast equally. The Provincial contribution could be funded from the resource revenues collected, as is the case with the Oil and Gas Commission.

In Fall 2003, the Offshore Team will be making a submission to Treasury Board regarding Team funding for fiscal 04/05 onwards. All activities proposed in this submission can be funded from the Team's 03/04 budget.

OPTIONS

Issue No. 1: Overall strategic approach to offshore oil and gas development:

The Offshore Team has developed an overall strategic approach designed to achieve the 2003 Throne Speech goal of an offshore industry in 2010 (see Appendix C for overview). It reflects an ambitious development timetable, and contemplates shorter timeframes for each step in the process (exploration, development, production) than industry currently estimates. In particular, the approach calls for initial seismic surveys at an earlier date.

Industry has based its timeline on experience on the East Coast and a linear development cycle. Although many steps in the process are sequential (e.g., 2-d seismic precedes exploratory drilling), and some time frames difficult to alter (e.g., seismic vessels must be commissioned well in advance, up to one year), the Team believes it can be compressed, without compromising environmental and other protections. Implementing the approach will require considerable interagency co-ordination and co-operation.

An ambitious approach to offshore development can be expected to generate a vigorous debate between supporters and opponents of development. As discussed above, many environmental groups are adamantly opposed to offshore development, and these groups can be expected to work against any activities. Initial opposition will probably focus on the federal process and federal moratorium, and if unsuccessful there to move to seismic testing. A key element of the strategy is to provide accurate factual information to the public to promote a balanced and well informed debate about the benefits and risks of offshore development.

In broad terms, the strategic approach entails:

- Achievement of an offshore industry up and running by 2010 through focusing on reducing development timeline while ensuring environmental safeguards are met (e.g., efficient and effective regulatory and environmental assessment processes).
- Mid-term goals:
 - Provincial response to federal government's review of Queen Charlotte Basin, with provincial negotiating positions on federal/provincial fiscal and regulatory arrangements, treatment of existing tenures and First Nation issues by Spring 2004;
 - Industry funded seismic surveys underway in one or more offshore basins by April 2005.
- Near term goals:
 - Continue working with First Nations, communities, industry and stakeholders regarding potential development in all basins;
 - Develop local benefit arrangements to provide First Nations and communities with appropriate gains from future activity;
 - Develop provincial positions for negotiations with federal government (e.g., fiscal and regulatory regimes, treatment of existing tenures);
 - Develop and implement public education and communication actions to provide accurate factual information to the public.

Option 1: Approve strategic approach as outlined above (recommended)

Advantages

- Ambitious development timeline clearly demonstrates government's commitment to establishment of offshore activity by 2010.
- Mid term goals would produce substantive activity by 2005.
- Coastal communities will support government commitment and short timeline on basis that strong action is needed to provide local economic opportunities.
- Focus on all basins, not just Queen Charlotte, signals that the province views all offshore basins as potential economic opportunities, and that the province has a broad perspective on coastal economic issues and other interests.
- First Nations will likely support emphasis on local benefits, and environmentally responsible development.

Disadvantages

- Timeline is shorter than industry's publicly stated development cycle.
- Unduly lengthy, or merely inconclusive, federal process could significantly delay industry activities and adversely impact mid term timeline.
- Opponents of development will interpret approach, particularly short timeline, as evidence government will fail to adequately protect environmental values.
- Some First Nations may criticize approach as not recognizing First Nation rights and aboriginal title.

Option 2: Establish different approach and longer timeline

Advantages

- Longer timeline would more closely correspond to industry views, and would reduce (but not eliminate) criticism about moving too fast.

Disadvantages

- Longer timeline inconsistent with Throne Speech and would be criticized by coastal communities and other supporters as failure to respond to potential economic opportunity.

Issue No. 2 Preliminary approach to federal review of Queen Charlotte Basin:

The federal government has been slow in releasing, either publicly or otherwise, details of its proposed process. Informally the Team understands federal officials are having difficulty in producing terms of reference acceptable to all federal decision makers. However, it is clear that Canada will not agree to a joint process, and views the province as having a minor role. While the federal review may advance some science issues, it has the potential to turn into a long, and ultimately inconclusive process. At the same time, the province is being asked publicly and by stakeholders to state its position the federal review, including whether the province continues to claim ownership of the Hecate Strait and Queen Charlotte Strait.

Based on all these factors, the Team proposes the following preliminary approach:

- Offshore Team to continue to offer advice and assistance to federal officials, with the objective of ensuring provincial views and objectives are taken into account.

- If Canada asks the Province to play a formal role in the federal review, authorize Ministers Neufeld and Thorpe, and Deputy Minister Dobell, to determine the Province's response.

s.14

Option 1: Approve preliminary approach as outlined above (recommended)

Advantages

- Enables province to influence process without becoming formally involved, which limits provincial exposure should federal process go astray or bog down.
- Provides opportunity to assess federal process before making any final decisions as to involvement.
- s.14

Disadvantages

- Continuing separate provincial process, rather than participating in federal process, could be criticized as duplication and waste of effort.
- s.14
- Industry would view federal provincial dispute over ownership as negative factor in considering future investments.

Option 2: Take an interventionist role in federal process

In this option, the Province would take all practical steps to present provincial interests and issues to the review, including intervening in the public review process and commissioning scientific research.

Advantages

- Provides opportunity to publicly state provincial views on matters being considered by the review.
- May be supported by those who favour slower development process.

Disadvantages

- Province would be in same position as any other intervenor, inconsistent with position that the province is a government, not a stakeholder, and consultation should occur on an intergovernmental basis.

Option 3: Wait for details of federal process before taking any position

In this option, the Province would defer taking any position on the federal review, including whether to continue an independent provincial process, until Canada provides further details of its intentions.

Advantages

- Avoids risk of province making decision on federal review based on inaccurate information.

Disadvantages

- Province could be criticized for not taking clear positions and being too passive.
- Allows federal government to establish agenda, which may impact on province's ability to advance issue.

Issue No. 3 Strategic Approach to First Nations:

Based on the Offshore Team's initial discussions, First Nations have significant interest in potential benefits, coupled with concern about environmental impacts. This is consistent with the findings of the Oil and Gas Task Force. While some First Nations have adopted a "rights and title" approach to their dealings with the Province, others have indicated a desire for further information and a willingness to consider potential benefits.

s.14

Four of five anticipated “breakthrough” First Nations are coastal, three within Georgia Basin. TNO’s timeline for achieving final agreements, and the Offshore Team’s mid term goals, share several dates, and there is obvious need to work together to achieve both outcomes.

Further, while the Offshore Team will continue to pursue development in all basins, considerable attention will likely be given to the Haida’s response to the federal review, and particularly the impact of the Haida’s rights and title litigation on any offshore development in the Queen Charlotte Basin.

To date, the Team has not made any direct contact with the Haida, although discussions have occurred with the “Turning Point” group, which includes the Haida. s.14
s.14

The Offshore Team seeks approval of the following strategic approach to First Nations:

- s.14
- Continue to work with all coastal First Nations, and where possible reach agreements to assist First Nations to identify potential opportunities arising from offshore development.
- s.14

Option 1: Approve strategic approach to First Nations as described above (recommended)

Advantages

- Ensures coordinated and integrated approach to First Nations.
- Opportunity to design new means to address First Nations interests.
- Enables First Nations to identify potential benefits from development.
- May lead to provincial-First Nations alignment that could reduce influence of environmental groups.

Disadvantages

- Difficult to establish agreement with several First Nations on broad issues.
- Raising revenue sharing and management role may raise expectations around existing issues, including treaty process and land use planning.
- No agreement from Canada to take a similar approach.

Option 2: Do not approve approach and direct Team to s.14

s.14

Advantages

- Avoids setting precedent for benefit sharing or management role that could be applied to onshore basins.
- Avoids any risk that First Nations may interpret agreement to discuss in principle as commitment to adopt benefit sharing or management role.

Disadvantages

- First Nations clearly expect benefit sharing and management role, and unlikely to reach any accommodation without these being at least considered.
- May precipitate First Nations to publicly oppose development, which would increase industry hesitancy to invest in BC offshore and delay development.

Issue No. 4: Approach to Development in the Georgia Basin

Of the four offshore basins, the Province clearly owns the oil and gas in one – the Georgia Basin. The Province has previously issued offshore tenures (these were frozen in 1972 by Order –in-Council) in the Georgia Basin. Legally, the Province could establish a stand alone royalty and regulatory regime, as is the case for onshore basins. Development of a stand alone regime would require significant changes to the existing provincial onshore regime, including amendment of statutes and regulations, and issuance of new regulations. It would also allow the Province to unilaterally authorize activity in the Georgia Basin at some future date. While Canada would retain some regulatory authority (e.g., fisheries, navigable waters), the same situation applies in onshore basins.

To date, industry has shown limited interest in the Georgia Basin, due both to the low prospectivity attributed to it, and to the anticipated public controversy that would likely come with any decision to authorize exploration. On the latter point, a previous government proposal to authorize a natural gas storage facility in the Lower Mainland produced a public outcry sufficient to lead the government to withdraw the proposal.

The Offshore Team has identified two initial steps in the development of the Georgia Basin:

- Authorize the Offshore Team to develop a stand alone provincial fiscal and regulatory regime based on Oil and Gas Commission and existing royalty legislation, including statutory amendments and new regulations where required.
- Authorize the Offshore Team to pursue private sector partnership to undertake seismic surveys in Georgia Strait by Spring 2004, using existing Team 03/04 budget.

Option 1: Approve approach to Georgia Basin as described above (recommended)

Advantages

- Although certain federal regulatory requirements would apply (e.g., *Fisheries Act*, navigable waters regulations), no need for federal consent to offshore regime.
- Would apply to offshore owned by Province (Strait of Georgia, Strait of Juan de Fuca) or claimed (Hecate Strait, Queen Charlotte Sound).
- Would provide an opportunity to establish the Province's preferred approach to any future joint federal provincial fiscal and regulatory regime, and to develop positions on that will arise in negotiations with Canada on a joint regime.
- Positions the province to pursue development of Georgia Basin if federal government continues its moratorium on other basins.

Disadvantages

- Requires development and enactment of statutory amendments and new regulations (e.g., fiscal/royalty, occupational health and safety, drilling regulations, seismic requirements).
- Development of provincial regime could be criticized on grounds the Province is ahead of industry and not respecting federal process.
- Any exploration activity, particularly seismic, in Georgia Basin would be controversial.

- Georgia Basin least prospective, and no current indication of significant industry interest.
- Offshore seismic survey requires considerable lead time, and it is not known if industry could undertake activity in 2004.

Option 2: Do not pursue development of Georgia Basin at this time

In this option the Province would not pursue development of the Georgia Basin except in the context of all four basins.

Advantages

- Avoids criticism that the Province is proceeding with undue haste is ahead of industry and is not respecting federal process.

Disadvantages

- Forgoes one method of developing provincial positions on regulatory and fiscal regime.
- Forgoes opportunity to be in position to authorize activity in Georgia Basin (subject to federal regulatory approval) should Canada refuse to allow activity in other basins.

**SIGNIFICANT IMPLICATIONS:
LEGISLATION REQUIRED? Yes**

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CONSULTATIONS? Yes

The Offshore Oil and Gas Task Force held meetings in November and December, 2001, to obtain local community and First Nation views on offshore oil and gas development. The Offshore Team has also held discussions with several First Nations.

If offshore oil and gas activities are commenced, further consultation with coastal First Nations will be required. A number of First Nations have publicly expressed their opposition to offshore oil and gas activities. Recently, however, some of their members have also said that if oil and gas exploration becomes a reality, they want to be involved.

The Oil and Gas Task Force also obtained the views of local communities, and the Offshore Team has held several follow up meetings with local government officials and other community representatives. While some local groups have expressed concerns about potential adverse impacts, many others have recognized the potential benefits and are actively seeking more information.

A number of environmental groups made presentations to the Oil and Gas Task Force opposing offshore development, and at least two groups have released reports that are highly critical of development. The Team has engaged some of the more pragmatic groups to identify potential areas of common ground (e.g., early identification of "no go" or excluded areas). In addition, the Team is also working with other agencies to co-ordinate its approach to environmental groups with other initiatives such as the Central Coast strategy, marine and oceans strategy, and land use planning.

INTER-AGENCY CO-ORDINATION

Pursuing potential development of the province's offshore oil and gas resources involves complex interplay amongst numerous provincial and federal agencies, and effective interagency management will be a prerequisite to success. The Offshore Team will co-ordinate and integrate its activities with relevant agencies, including (but not limited to):

- s.14
- The Ministry of Water, Land and Air Protection on identification of “no – go” or excluded areas based on conservation and protection values, in particular to co-ordinate with activities related to the Memorandum of Understanding with Parks Canada on marine conservation areas.
- The Ministry of Sustainable Resource Management on interactions with land use planning and coastal planning, and in particular the relationships being established by the Ministry with First Nations and with environmental groups. In addition, the Ministry would play a key role in many actions intended to assert provincial ownership of Hecate Strait.
- The Intergovernmental Relations Secretariat and the Office of Premier on the strategic approach, and on proposed specific actions, with intergovernmental implications, to ensure these are consistent with the province's overall agenda with Canada.
- The Office of the Premier to co-ordinate activities with environmental groups with the province's broader approach to conservation and environmental issues.
- s.14
- The Ministry of Finance and the Ministry of Provincial Revenue on the development of fiscal and royalty regimes.
- The Ministry of Energy and Mines and the Oil and Gas Commission on the development of an overall regulatory regime.
- The Ministry of Competition, Science and Enterprise to ensure integration with other elements of the Heartlands Strategy.

RECOMMENDED DECISION:

Cabinet approve the following:

1. Overall strategic approach to offshore oil and gas development:
 - Achievement of an offshore industry up and running by 2010 through focusing on reducing development timeline while ensuring environmental safeguards are met (e.g., efficient and effective regulatory and environmental assessment processes).
 - Mid-term goals:
 - Provincial response to federal government's review of the Queen Charlotte Basin, with provincial negotiating positions on federal/provincial fiscal and regulatory arrangements, treatment of existing tenures and First Nation issues by Spring 2004;
 - Industry funded seismic surveys underway in one or more offshore basins by April 2005.
 - Near term goals:
 - Continue working with First Nations, communities, industry and other stakeholders regarding potential development in all basins;
 - Develop local benefit arrangements to provide First Nations and communities with appropriate gains from development;
 - Develop provincial positions for negotiations with federal government (e.g., fiscal and regulatory regimes, treatment of existing tenures);
 - Develop and implement public education and communication actions to provide accurate factual information to the public.
2. Preliminary approach to federal review of Queen Charlotte Basin:
 - Offshore Team to continue to offer advice and assistance to federal officials, to ensure provincial views and objectives are taken into account.
 - If Canada asks the Province to play a formal role in the federal review, authorize Ministers Neufeld and Thorpe, and Deputy Minister Dobell, to determine the Province's response.
 - s.14

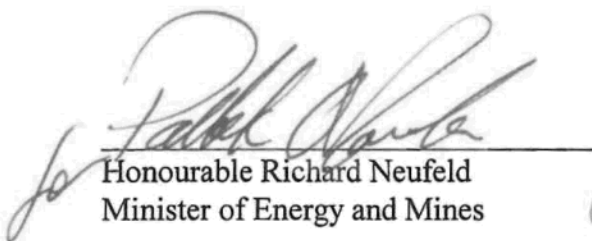
3. Strategic Approach to First Nations:

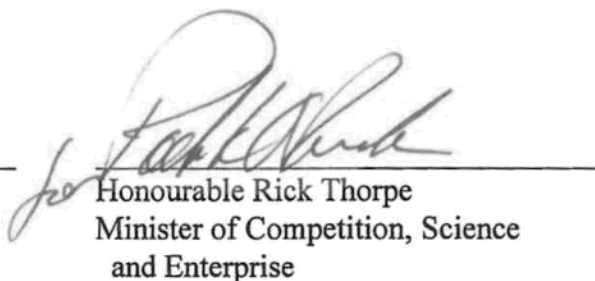
- s.14
- Continue to work with all coastal First Nations to establish arrangements to assist First Nations to identify potential opportunities arising from offshore development.
- s.14

4. Approach to Development in the Georgia Basin:

- Authorize Offshore Team to develop a stand alone provincial fiscal and regulatory regime based on Oil and Gas Commission and existing legislation, including statutory amendments and new regulations where required.
- Authorize Offshore Team to pursue private sector partnership to undertake seismic surveys in Georgia Strait by Spring 2004, using existing Team 03/04 budget.

SIGNATURES:


Honourable Richard Neufeld
Minister of Energy and Mines


Honourable Rick Thorpe
Minister of Competition, Science
and Enterprise

KEY CONTACT:

Patrick O'Rourke, Acting Deputy Minister
BC Offshore Oil and Gas Team
356-0552

Date: July 3, 2003

STRICTLY CONFIDENTIAL

18

Appendix A

History of Offshore Development

Since at least the 1950's, the ownership of and jurisdiction over oil and gas reserves in the offshore have been claimed by both the provincial and federal governments. In 1967, in a reference case to the Supreme Court of Canada (SCC), it was held that the area seaward of the baseline for the territorial sea on British Columbia's coast belonged to Canada. However, it is the Province's contention that the ownership and jurisdiction of the Hecate Strait and Queen Charlotte Sound areas has not been decided. British Columbia maintains that these two areas are landward of the baseline for the territorial sea and as such were not dealt with in the 1967 SCC decision. However, Canada has never formally drawn baselines for the territorial sea in these areas. British Columbia has reaffirmed its position that the oil and gas resources in these areas are owned by the province by declaring these areas to be provincial Crown reserves through Orders in Council in 1959, 1966 and 1981.

In the early 1970's, public concern over oil pollution in the marine environment grew in response to a number of high profile oil spills. At the same time, the west coast of British Columbia was identified as a potential route for oil tankers carrying Alaskan oil to the lower 48 states. These events led to the federal government restricting offshore oil and gas activities on the west coast in 1972. The federal policy decision, which included the Arctic, came to be known as the 'Federal Moratorium' in the British Columbia offshore. At the time, the federal government stated that the 'Federal Moratorium' would be lifted once regulations for development in the offshore were completed. s.14

s.14

exploration in the British Columbia offshore came to a halt.

As a result,

During the late 1970's and early 1980's, Canada had separate discussions with Nova Scotia, Newfoundland and British Columbia with respect to offshore oil and gas exploration and development off their coasts. Similar to British Columbia, Nova Scotia and Newfoundland claimed jurisdiction and ownership of the oil and gas resources in their respective offshore areas. Ownership and jurisdiction over Newfoundland's continental shelf was decided in 1984 by the SCC to belong to Canada. Although ownership of the territorial sea off of Newfoundland was not at issue before the Court, it referred to the decision in the 1967 British Columbia case favourably. In contrast, in 1984 the SCC also determined that the Province owned the sea floor of the Georgia Strait and the Strait of Juan de Fuca (and the resources on and under it).

Canada signed accords with Newfoundland (1985) and Nova Scotia (1986) (the "Atlantic Accords") establishing two separate federal-provincial boards responsible for the management, administration of the oil and gas development in their respective offshore areas. These agreements were political settlements reached to allow exploration and development to proceed without prejudicing any of the three governments' respective legal claims to the offshore resources.

In June 1984, Canada and British Columbia appointed an Environmental Assessment Panel (EA Panel) to conduct a public review of the environmental and related socio-economic effects of petroleum exploration off the west coast of Canada, north of Vancouver Island, and seaward to the limit of the continental shelf. The EA Panel was asked to develop recommendations on the terms and conditions under which petroleum exploration could proceed in a safe and environmentally responsible manner. In 1986, the EA Panel advised the two governments that exploration could proceed in an environmentally acceptable manner if the panel's recommendations (92) were accepted. In 1987, the two governments assessed these recommendations and instituted programs to address the information needs identified by the panel.

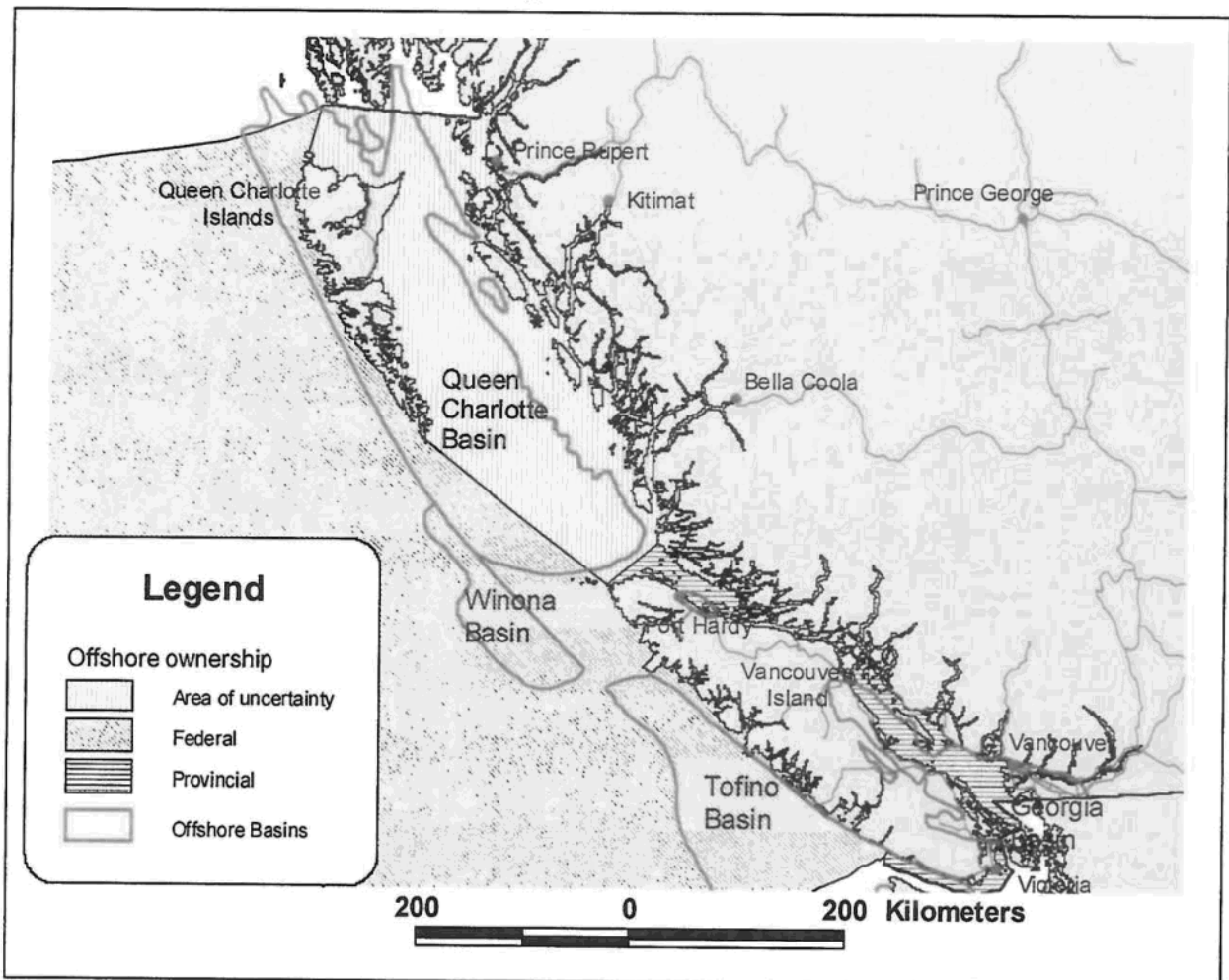
In 1987, Canada and British Columbia also began negotiations for an agreement (the "Pacific Accord") with respect to the management and administration of oil and gas off the British Columbia's offshore. Similar to the Atlantic Accords, the agreement was to be without prejudice to either party's offshore claims and would result in the development of a joint management board to manage and administer all offshore oil and gas activities. Pursuant to the discussions, all revenues from offshore oil and gas activities were to accrue to the Province as if the resources were on land. The revenues would flow through the federal Consolidated Revenue Fund and the management board would be funded by each government. However, the negotiations stalled in late 1987 when the parties could not agree on how to address First Nation land claims or the creation of a federally funded infrastructure program.

In the winter of 1988-spring of 1989, two oil spills off the west coast of North America, the Nestucca and the Exxon Valdez, heightened public concern once again over oil pollution in the marine environment. This derailed federal-provincial plans to resume their stalled negotiations. In March 1989, the provincial government announced that there would be no drilling in British Columbia's waters for at least five years. In the same year, Canada announced that it would withhold federal approval of oil and gas activity in the offshore until British Columbia advised that it supported the resumption of activity. The provincial government position, which became known as the 'Provincial Moratorium', has never been formally lifted.

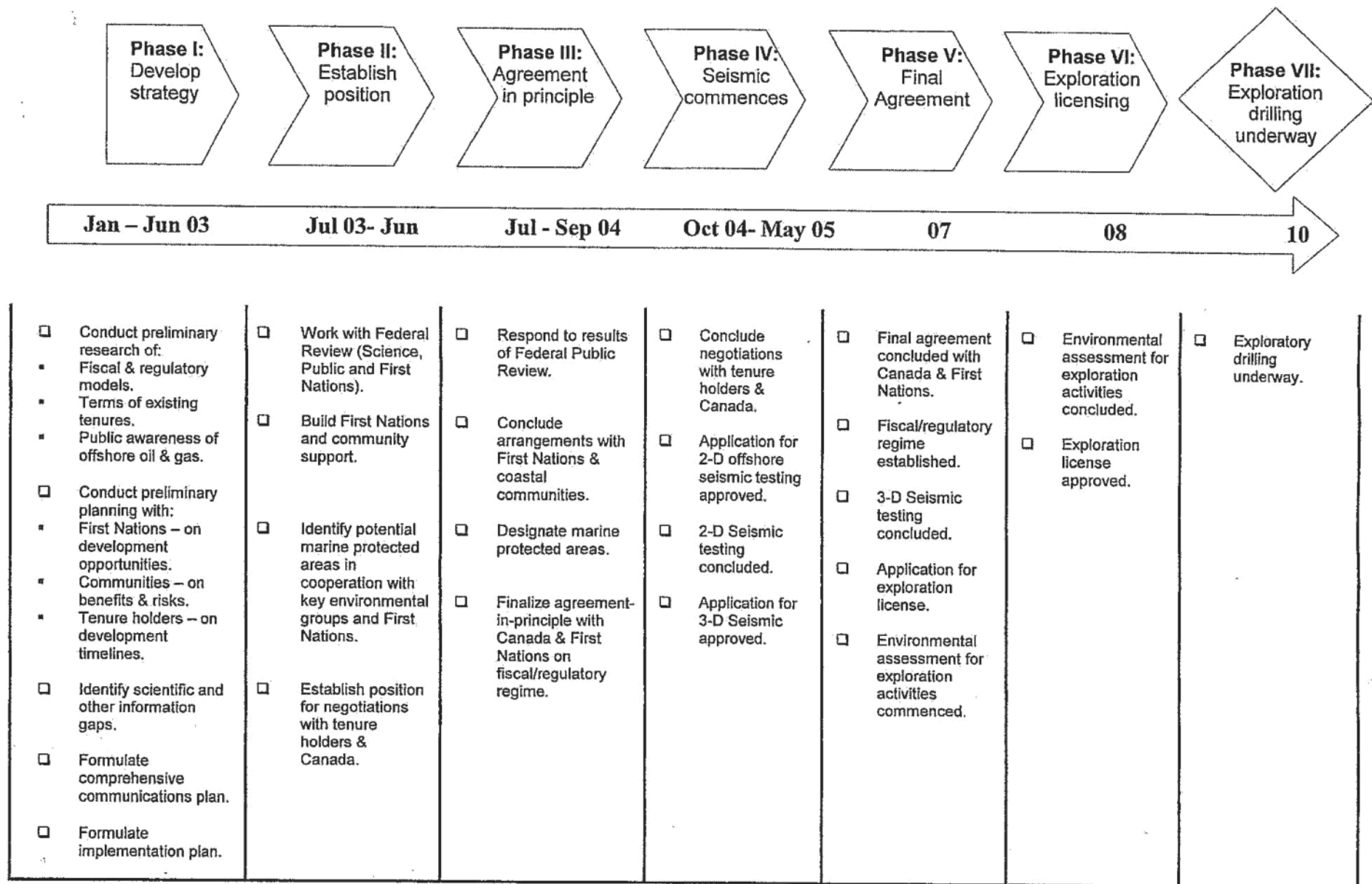
Appendix B

Map of British Columbia Offshore Resource Basins

Ownership of the Offshore

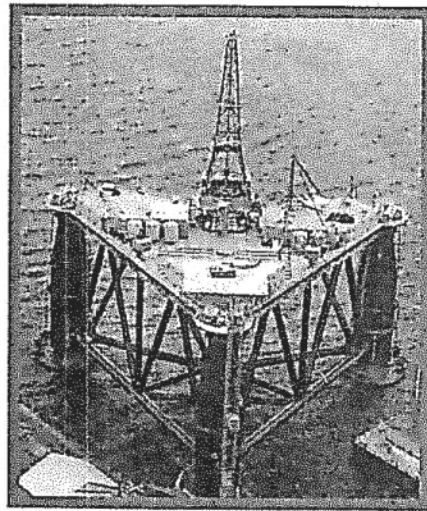


Appendix C Overview - Offshore Oil & Gas Strategy



Heartlands Economic Strategy

Developing British Columbia's Offshore Oil and Gas



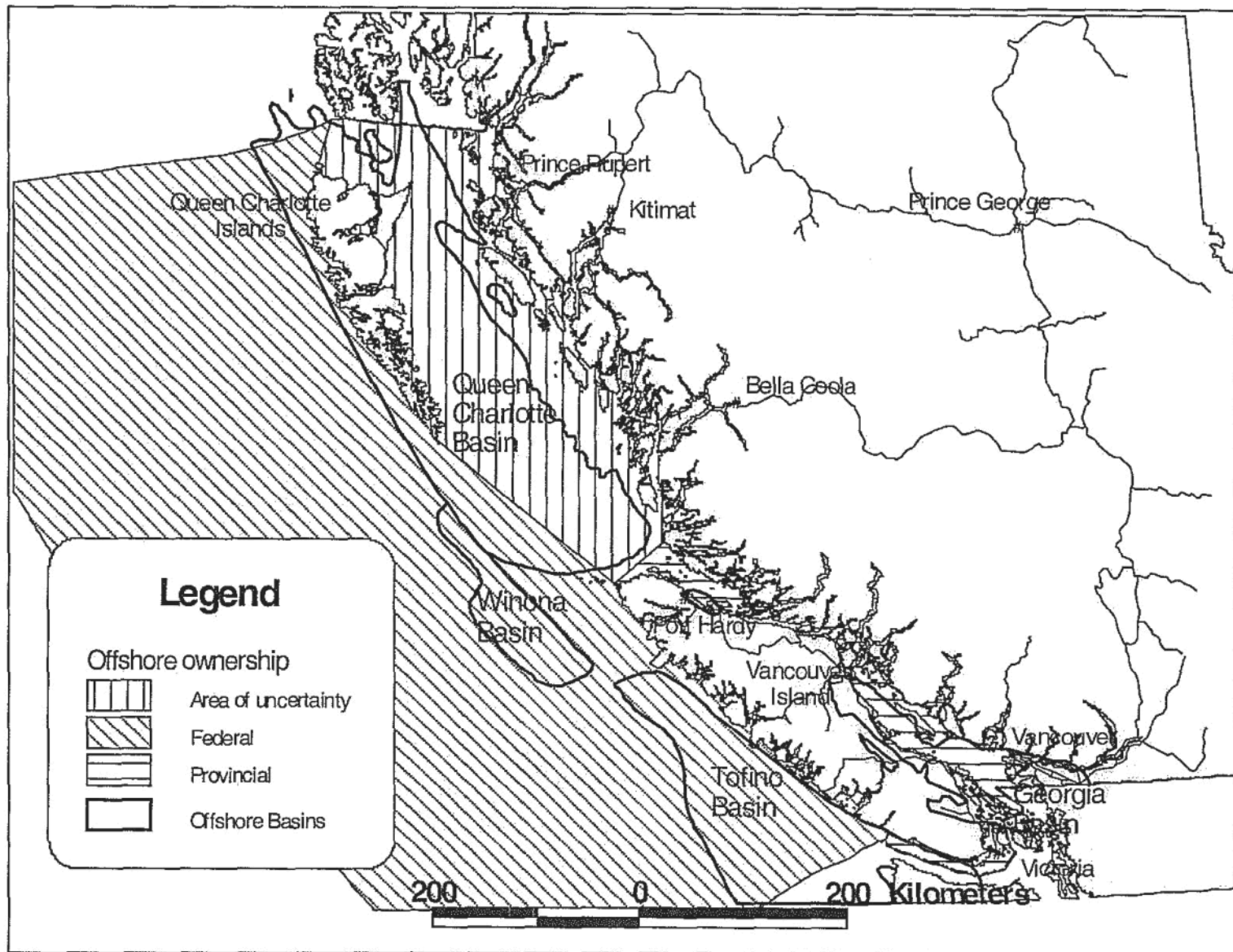
Presentation to Cabinet

Goal

“By 2010, your government wants to have an offshore oil and gas industry that is up and running, environmentally sound, and booming with job creation.”

*– The Honourable Iona Campagnolo,
Speech from the Throne, 2003*

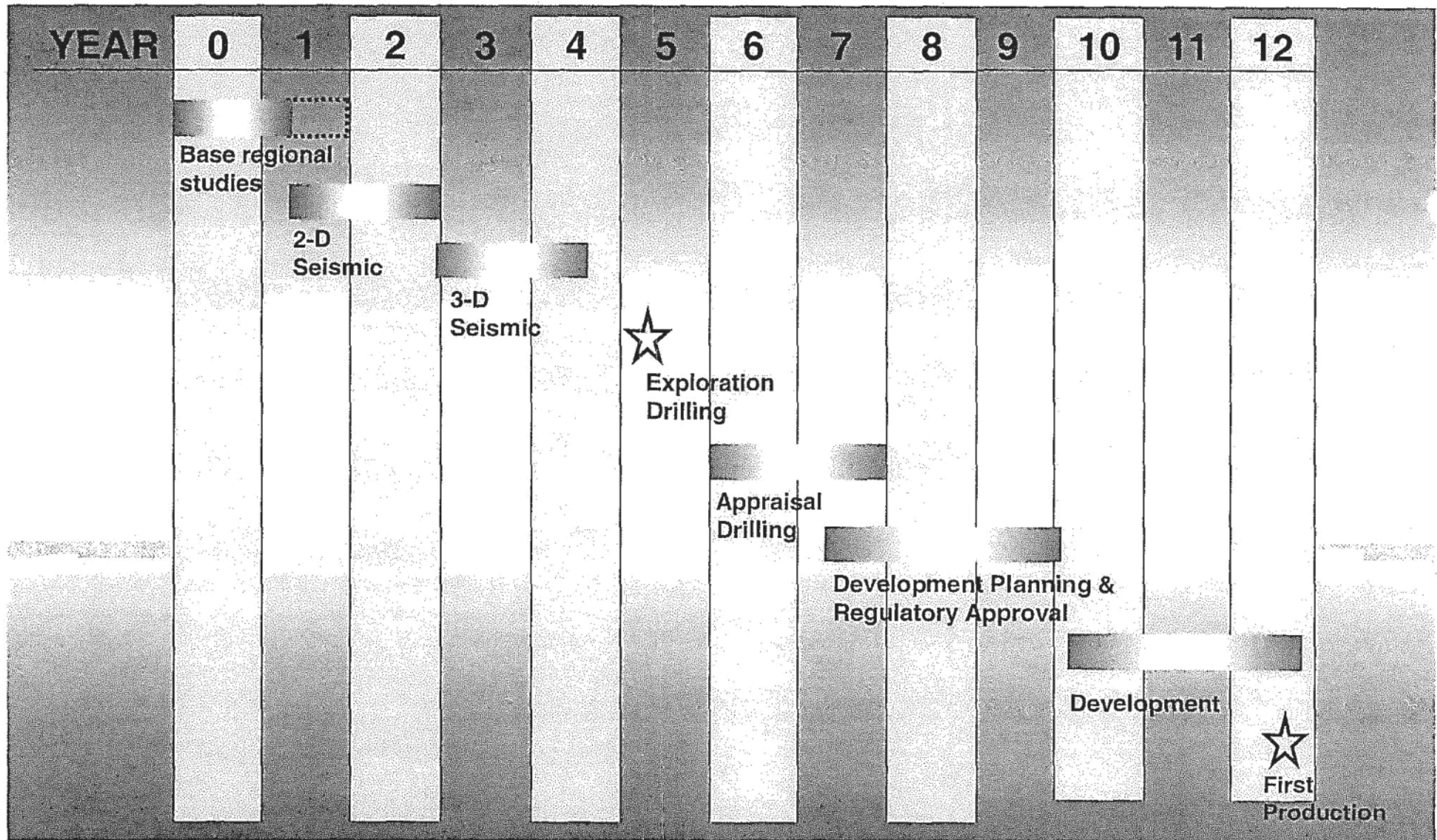
Ownership of the Offshore



Resource Potential Estimates

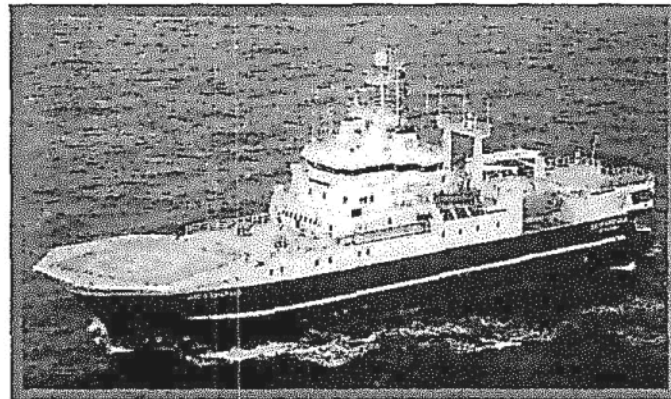
- Queen Charlotte Basin
 - Estimated 9.8 Billion Barrels Oil 25.9 Trillion Cubic Feet Gas
- Tofino and Winona Basins – off West Coast Vancouver Is.
 - Estimated total 9.4 Trillion Cubic Feet Gas
- Georgia Basin- from coastal lowlands of Van Is to Fraser delta and south to Wa State
 - Estimated total 6.5 Trillion Cubic Feet Gas (75% in BC)
 - Estimated 3 TCF offshore BC , 2 TCF Lower Mainland

Industry's Development Timeline



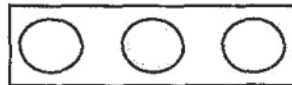
Key Development Milestone

Industry's decision to undertake seismic



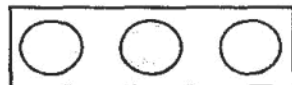
Offshore – One Company's Assessment

Technical



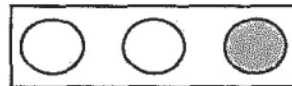
Prospectively highly uncertain, technology exists, environmental must be addressed (appears doable)

Economic



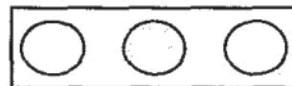
Costs and economics uncertain

Commercial



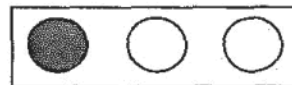
Market outlook very favourable

Organizational

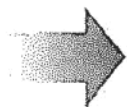


Industry capability exists, limited current capacity for West Coast Offshore

Political/societal

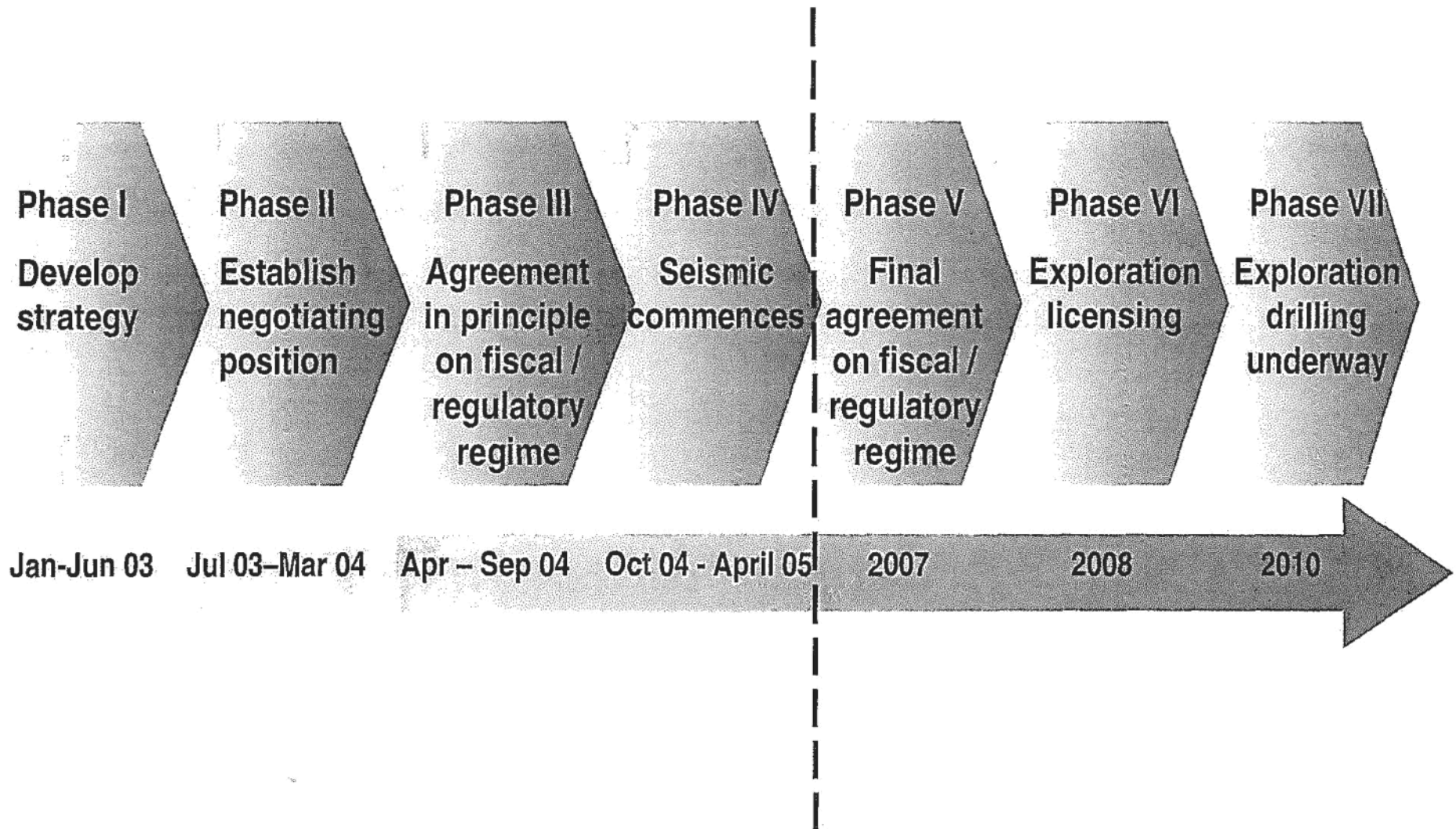


Jurisdiction, fiscal, regulatory framework are undefined, meaningful First Nations engagement required...mixed stakeholder messages



Getting to the next step (i.e., seismic) requires dealing with the red light issues

The Way Forward



Cabinet Decisions Required

1. Overall strategic approach to offshore oil and gas development:
 - Reduce development timeline / meet environmental safeguards
 - Mid-term goals:
 - Respond to Federal Review of Queen Charlotte Basin, Spring 2004
 - Industry funded seismic surveys by April 2005
 - Near term goals:
 - Work with First Nations, communities, industry and stakeholders
 - Develop local benefit arrangements
 - Develop positions for negotiations with Canada

Cabinet Decisions Required

2. Approach to federal review of Queen Charlotte Basin:
 - Offer advice and assistance to federal officials
 - Equip ministers to determine provincial response, should Canada ask BC to play a formal role

s.14

Cabinet Decisions Required

3. Strategic approach to First Nations:

- s.14
- Work with all coastal First Nations to identify potential opportunities arising from offshore

- s.14

Cabinet Decisions Required

4. Approach to development in the Georgia Basin:

- Develop a stand alone provincial fiscal and regulatory regime based on Oil and Gas Commission and existing legislation
- Pursue private sector partnership to undertake seismic surveys in Georgia Strait by Spring 2004: using existing team budget

Goal

“By 2010, your government wants to have an offshore oil and gas industry that is up and running, environmentally sound, and booming with job creation.”

Phase I:
Develop
strategy

Phase II:
Establish
position

Phase III:
Agreement
in principle

Phase IV:
Seismic
commences

Phase V:
Final
Agreement

Phase VI:
Exploration
licensing

Phase VII:
Exploration
drilling
underway

Jan – Jun 03

Jul 03- Jun 04

Jul - Sep 04

Oct 04- May 05

07

08

10

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Overview - Offshore Oil & Gas Strategy

