

SURFACE RIGHTS ACT
RSA 2000
Chapter S-24
(hereinafter "the Act")

Before:

SURFACE RIGHTS BOARD
(hereinafter "the Board").

IN THE MATTER OF certain lands subject to a surface lease (L.S. 2-13 well site and access road lease) in Plan 7822683, Block 3 (SE ¼-13-46-1-W5M), in the Province of Alberta (hereinafter referred to as "the said land").

Excepting thereout all Mines and Minerals.

B E T W E E N:

ENERMARK INC.,

Operator,

- and -

853068 ALBERTA LTD.,

Lessor.

DECISION

Upon application by the Lessor for review of the rate of compensation payable in respect of a surface lease in the said land; and upon the Board being satisfied that conditions precedent to the application had been met; the Board held a hearing on the application on September 21, 2005, at Wetaskiwin, Alberta.

PRESIDING BOARD:

- W. D. Fisher, Presiding Chair
- J. E. Logan
- H. R. Watson

APPEARANCES:

For the Operator:

- Shawn K. Brown, President/General Manager, of Landwest Resource Services Ltd., Land Agent;
- R. A. Kaminski, Manager, Surface Land, of Enerplus Resources Fund;
- Don Hoover, AACI, P.Ag., C.M.C., of Serecon Valuation & Agricultural Consulting Inc.; and
- Beth A. White, B.Sc. Ag., of Serecon Valuation & Agricultural Consulting Inc.

For the Lessor:

- Wade Stephan, Principal for the Landowner 853068 Alberta Ltd.; and
- Michael David Klause, with the law firm McDonald Street Law Office, Legal Counsel.

EXHIBITS FOR IDENTIFICATION:

Exhibit A: Copy of the surface lease as filed with the application.

Exhibit B: Application for review dated November 17, 2004.

EXHIBITS FILED:

Exhibit 1: Map showing County of Wetaskiwin — 100 metre required setback.

Exhibit 2: Summary of sales.

Exhibit 3: Cost of Phase 1 Development Beachside Estates.

Exhibit 4: By-Law Number 2002/10 adopting Area Structure Plan.

Exhibit 5: By-Law Number 2005/15 — Area Structure Plan amendment.

Exhibit 6: County of Wetaskiwin No. 10: Notice of Appeal Decision.

Exhibit 7: Operator's written presentation.

Exhibit 8: Survey Plan: Enerplus Westerosse 10-13-46-1.

Exhibit 9: Sketch Plan showing proposed subdivision.

Exhibit 10: ExxonMobil Canada Ltd.: Plan showing well site and access road 12-9-49-7.

Exhibit 11: ExxonMobil Canada Ltd.: Compiled plan showing well site 14-9-49-7.

Exhibit 12: Letter dated March 25, 2003 from McDonald Street Law Office.

Exhibit 13: Surface Rights Board Decision No. 2003/0020.

Exhibit 14: Rental Review Comparables "Town of Drayton Valley".

Exhibit 15: Serecon Appraisal Report.

Exhibit numbers 1 to 6, inclusive, were filed for the Lessor. Exhibit numbers 7 to 15, inclusive, were filed for the Operator.

AGREED FACTS:

1. The surface lease bears the effective date of April 27, 1987, and shows the area occupied by the Operator to be 3.43 acres.
2. The purpose of the surface lease is for a well site and access road.
3. The surface lease provides for a rate of annual compensation of \$3,650.00.
4. The effective date of review is April 27, 2002.
5. The Lessor purchased the said land in February 2000.
6. The said land is zoned Country Residential (CR) District within the Wetaskiwin County Land Use Bylaw #95/54.
7. The said land is current within an area structure plan pending development.

SUMMARY OF THE EVIDENCE:

Oath waived by the parties

Lessor's Evidence:

Mr. Wade Stephan appeared on behalf of the Landowner 853068 Alberta Ltd. along with his lawyer Mr. Michael David Klause.

The subject well site and access road are located in the midst of 853068 Alberta Ltd.'s 15 lot subdivision. Current annual compensation is \$3,650.00. Mr. Stephan requested the Board to increase annual compensation to \$15,000.00 due to the impacts exerted by the subject lease on the land development project.

Mr. Stephan explained that the said land has been re-zoned for country residential subdivision. The Area Structure Plan is in place and six of the fifteen lots in the subdivision have been sold.

Exhibit 1 outlines the 100 metre setback imposed by the County of Wetaskiwin. As a result of the setback, the Lessor is unable to develop eight extra lots comprising an area of 8.6 acres.

A summary of sales (Exhibit 2) shows that nine lots have been sold to date. Purchase prices follow:

- 3 lots sold for \$162,000.00
- 2 lots sold for \$115,000.00
- 4 lots sold for \$216,700.00

Exhibit 3 sets out 853068 Alberta Ltd.'s costs to develop 15 lots contained in Phase 1 of Beachside Estates. Excluding the cost of purchasing and holding the land, costs for road engineering/design, construction, services, and general conditions amounted to a total \$156,186.60.

Mr. Stephan emphasized that the Operator has agreed to screen the site from view through enhanced fencing and tree plantings. The Operator has also agreed to relocate the access road. The only outstanding issue then, is that of annual compensation.

Mr. Stephan testified that the subdivision plan was registered on February 12, 2002 and hence before the effective date of review on April 27, 2002.

Referring to Exhibit 2, Mr. Stephan emphasized that the lots sold to date are not in close proximity to the subject well site. He asserted that the lots adjacent to the lease would be harder to sell for aesthetic reasons.

Exhibit 4 indicated that on February 12, 2002, the County of Wetaskiwin adopted the Area Structure Plan for the purpose of providing a framework for further subdivision and development of portions of the NE 31, SE 31 and NW 32-46-1-W5M.

Exhibit 5 dated March 17, 2005 shows an amendment to the above mentioned Area Structure Plan. Exhibit 6, dated May 25, 2005 is a Notice of Appeal Decision upholding the amended conditions pertaining to the Lessor's subdivision.

Mr. Stephan noted that no lots were sold prior to May 25, 2005 excepting lots 1, 10 and 19 that sold in October of 2002.

The Board asked Mr. Stephan to outline the loss of use and adverse effect comprising his request for annual compensation of \$15,000.00. In response, Mr. Klause cited loss of use from the required 100 metre setback and the effect of the subject site on land sales. However, as these items have not been specifically quantified, the Lessor's request is submitted on a "global" basis and not in strict accordance with the heads determining annual compensation as set forth in the *Act*.

Operator’s Evidence:

Messrs. Brown, Kaminski, Hoover, and Ms. White appeared on behalf of the Operator.

Mr. Brown:

Mr. Brown outlined the Operator’s written presentation entered as Exhibit 7. A brief summary of this document follows:

Facts:

- surface lease dated April 27, 1987
- Lessor (853068 Alberta Ltd.) purchased the said land in 2000
- current rental since 1997 is \$3,650.00
- producing sweet gas well (with some oil) pipelined
- equipment consists of wellhead, line heater, 500 gallon and 45 gallon tanks,
- frequency of access is one truck per day (on average)
- area is 3.43 acres

History:

In December 2001, the Operator entered into discussions with the Lessor concerning the establishment of an additional well, revised rental, and issues pertaining to the proposed subdivision including the relocation of the access road.

On March 31, 2003, the Operator received a letter from the Lessor’s solicitor that offered to accept a revised annual compensation in the amount of \$7,500.00. The Operator now understands that the Lessor’s request has increased to \$15,000.00.

In April 2005 the Operator sought an external evaluation of the proposed rental. An appraisal was prepared by Mr. Hoover and issued on May 30, 2005. Based on the report’s findings, the Operator verbally offered the Lessor a revised annual compensation of \$8,617.00. Various phone conversations followed.

A meeting between the parties followed on September 14, 2005. Mr. Stephan was provided with a copy of the Serecon appraisal report (Exhibit 15). Negotiations continued to September 19, 2005 wherein both parties concluded that a hearing was necessary to resolve the rental issue.

Comparables with photographs (Exhibit 7):

- Burlington Lease: 1-13-46-1-W5M — 3.58 acres — current annual is \$4,000.00
This well site is located on the same quarter, directly east of subject location.
- Surface Rights Board Decision No. 2003/0020 (Exhibit 13) wherein two lease rentals located in Drayton Valley were brought before the Board.

1. LSD 12-9-49-7-W5M

Highest and Best Use: Urban Reserve (5.00 acres), oil well and related facilities.

Decision:

| | |
|--|--------------------|
| Loss of use: \$1,550.00 per acre x 5 acres | \$ 7,750.00 |
| Adverse effect | \$ 6,000.00 |
| Total Annual | <u>\$13,750.00</u> |

2. LSD 14-9-49-7-W5M

Highest and Best Use: Recreational (3.67 acres), oil well and related facilities located within residential/commercial area

Decision:

| | |
|---|----------------------|
| Loss of use: \$1,550.00 per acre x 3.67 acres | \$5,700.00 (rounded) |
| Adverse effect | Nil |
| Adverse effect on non - usable land..... | <u>Nil</u> |
| Total | \$5,700.00 |

- * Exxon Mobil 8-16-49-7-W5M
 Highest and Best Use: Residential/Recreation (6.46 acres)
 Oil well and related facilities located within town of Drayton Valley. Rental reviewed and settled with landowner based on Serecon appraisal.
 Loss of use: \$600.00 per acre x 6.46 acres\$3,876.00
 Adverse effect:\$6,000.00
 Total annual compensation\$9,900.00 (rounded)

- * Exxon Mobil 4-16-49-7-W5M
 Highest and Best Use: Residential/Recreation (6.99 acres)
 Oil well and related facilities located within Rotary Park in Drayton Valley. Rental reviewed and settled with landowner based on Serecon appraisal.
 Loss of use: \$600.00 per acre x 6.99 acres\$4,194.00
 Adverse effect:\$3,000.00
 Total annual compensation\$7,194.00

Note: Within Surface Rights Board Decision No. 2003/0020 it is important to note that approximately 20 settled comparable rentals provided in table format (Exhibit 14) within the Town of Drayton Valley.

Mr. Brown submitted several other exhibits including:

- Exhibit 8: Survey plan showing the subject site and its surrounding location
- Exhibit 9: Sketch plan showing proposed subdivision
- Exhibit 10: ExxonMobil Canada Ltd. compiled plan showing well site and access road in 12-9-49-7
- Exhibit 11: ExxonMobil Canada Ltd. compiled plan showing well site and access road in 14-9-49-7
- Exhibit 12: Letter dated March 25, 2003 from McDonald Street Law Office indicating that the Lessor would be willing to accept annual compensation of \$7,500.00 subject to some provisions for future changes.

Mr. Hoover and Ms. White: Serecon Appraisal Report (Exhibit 15)

The effective date of appraisal is April 27, 2002. The said land containing 50.62 acres was inspected for the purpose of appraisal on May 19, 2005. The subject well site and access road occupy 3.43 acres.

On the basis of Serecon’s investigation, annual compensation was estimated as follows:

| | |
|--|-------------------|
| Annual loss of use: 3.43 acres @ \$1,000.00 per acre | \$3,430.00 |
| Annual adverse effect: | |
| - Tangible | \$1,187.00 |
| - Intangible | <u>\$4,000.00</u> |
| Total Annual Compensation | \$8,617.00 |

The subject property is located within 1.0 km of the south side of Pigeon Lake in the Municipality of Westeros.

The Alberta Energy and Utilities Board (AEUB) requires a setback of 100 metres to residential development. Typically upon request this distance is reduced to 50 metres or to an area completely contained within the surveyed well site area. There is no assurance that a setback reduction or waiver will be granted, but precedent indicates there is a good probability it could be achieved for this well site. This potential setback is considered in the analysis of adverse effect or the impact on the remaining land.

The subject land is proposed for use as a country residential area with a rural commercial area on the east side. Land on the west side of the said land is currently zoned Country Residential District (CR). The proposed subdivision has been submitted as an Area Structure Plan within Wetaskiwin County. The current use is as a holding property awaiting development as a country residential subdivision, which is compatible with the zoning.

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The highest and best use of the subject is the completion of subdivision into country residential properties.

The intent of the appraisal is to assess the economic loss for the rights given up by the surface Lessor by addressing the *Surface Rights Act* and its provisions for determining annual compensation.

Loss of Use:

It is assumed by the appraisers that if the well site was not in place the land could have been used for country residential purposes. Therefore, loss of use and adverse effect would be based on the economic losses incurred annually based on development of the land for country residential use. Two approaches are used to determine annual economic loss:

1. Residential Rental Approach
2. Residual Value

Mr. Hoover outlined the details of his methodologies and findings as set out in pages 24 to 35 of the appraisal report.

In considering the Residential Rental Approach Mr. Hoover found that based on discussions with realtors, developers, and market participants, and based on residential and serviced lot sales described in the report, the serviced lot value of the subject land is \$37,000.00 for an average lot size of 0.6 acres.

The Residual Value Approach examined sales of unserviced lands similar to the subject land. Based on this approach, Mr. Hoover found the bareland residual value of the subject land is \$24,400.00 per acre.

Mr. Hoover compiled data on the income that could be generated from residences that could be developed on the subject land. The analysis indicated a net return per annum per lot of \$6,967.00. The final stage in the residential rental approach is to establish what percentage of the total residential property value is attributable to the land component only and provide an estimate of the loss of use based on the income from renting the residence.

The following summarizes estimated values derived by the percentage allocated to each component and in particular, the land component:

- Improved Residential Site = \$222,300.00 = 100% of total price
- Developed Lot Price = \$37,000.00 = 16.6% of total price
- Undeveloped Lot Price = \$12,200.00 = 5.5% of total price

Using net return from residential rental income and the percentage allocated to the undeveloped land in the above approach, the following loss of use is estimated on a per acre basis:

- Net return = \$6,967.00/lot
- = \$6,967.00 x 5.5% = \$383.00/lot
- = \$383.00 x 2 lots/acre = \$766.00/acre

Residential Rental Approach – Annual Loss of Use Estimate = \$766.00 rounded to \$770.00 per acre per year

Mr. Hoover then considered loss of use based on an expected rate of return. The estimated market value of the subject land is \$24,400.00 per acre. Based on current interest rates a safe, risk free investment return is 4.0 to 5.0% not accounting for any appreciation in value over time. As all the interests in the land will revert to the owner at some time in the future, this is a component of the total return to the Lessor.

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The estimated loss of use utilizing this approach is therefore:

- \$24,400.00 x 4% = \$976.00 per acre per year
 - \$24,400.00 x 5% = \$1,220.00 per acre per year
- Range = \$976.00 to \$1,220.00 per acre per year**

In the opinion of the appraisers, the approaches outlined provide a reasonable method using accepted appraisal methodology to assess loss of use based on that portion of the said land within the boundaries of the well site. The results are consistent between the two approaches.

1. Residential Rental Approach = \$770.00 per acre per year
2. Expected Rate of Return Approach = \$976.00 to \$1,220.00 per acre per year

In the appraisers' opinion the estimated loss of use for the subject well site is \$1,000.00 per acre per year.

3. Well site and Access Road = 3.43 acres
4. \$1,000.00 per acre per year x 3.43 acres = \$3,430.00 per year.

Adverse Effect:

Mr. Hoover and Ms. White considered both the tangible and intangible factors in their estimate of compensation for adverse effect.

Tangible Losses:

As shown previously, the annual loss to the land due to the well site and access road is \$1,000.00 per acre per year. The tangible adverse effect component applies to the area located within the 100 metre setback from the wellhead not contained within the well site and access road. The appraisal assumed the probability of the AEUB granting a waiver to the 50 metre setback, or within the well site area to be 75:25. The area contained outside the well site/access road is estimated to be about 4.75 acres. The annual adverse effect for this area would be \$1,000.00 per acre at 25%, or \$250.00 per acre for 4.75 acres = \$1,187.00.

Intangible Losses:

The appraisers examined recent Surface Rights Board decisions under similar circumstance. Overall compensation for adverse effect is typically arbitrary or subjective. The appraisers' opinion is that compensation for adverse effect for a residential highest and best use would fall in the range established in the market through Surface Rights Board decisions of \$2,500.00 to \$3,000.00 where there are impacts to a rural residence, to a maximum of \$6,000.00 in fully developed urban centers. The appraisers considered the subject's proximity to development, parcel size, the on-site facilities, and the subject's impact on development of the balance of the land. The appraisers found the overall impact to be significant and in referring to a similar Board decision estimate this component of adverse effect to be \$4,000.00.

Total Annual Loss of Use and Adverse Effect:

| | |
|---|-------------------|
| Loss of use: \$1,000.00 per acre x 3.43 acres | \$3,430.00 |
| Adverse effect: | |
| - Tangible | \$1,187.00 |
| - Intangible..... | \$4,000.00 |
| Total | \$8,617.00 |

DETERMINATION OF COMPENSATION:

As the Board was not privy to the initial fixing of the rate, it can only premise that what factors were considered by the parties on the execution of the lease are compatible with that now presented in evidence before the Board, subject of course to any changes in circumstances which may have occurred during the intervening period.

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Under the provisions of the *Act*, consideration of a rate of compensation is to be given in respect of loss of use of the area granted (section 25 (1)(c)), and the adverse effect, nuisance, inconvenience and noise arising or that might arise from the area granted and the operations conducted thereon (section 25(1)(d)).

The sole outstanding issue between the parties is the amount of annual compensation payable by the Operator to the Lessor. The task facing the Board is that of determining fair and reasonable compensation in this matter.

The Lessor requested compensation of \$15,000.00 per annum is based on a global or lump sum approach. No evidence pertaining specifically to the headings of loss of use and adverse effect was placed before the Board. Rather, the Lessor's request is based on losses arising from the 100 metre setback and potential losses in land sales and/or land values arising from the presence of the well site and access road.

The Board recognizes that the said lands are zoned Country Residential as of the effective date. A key issue arises however, in determining whether or not the said lands have been approved for subdivision. During the hearing, the Lessor made it clear that his request for compensation is justifiable owing to the fact that the said lands were approved for subdivision.

The Board provided the Lessor with ample opportunity to produce a Registered Certificate of Subdivision or any other instrument that would confirm the alleged subdivision approval. The Board made it clear to the Lessor and his counsel that verification of the alleged subdivision is critical to the determination of compensation. Rather than paying heed to the Board's request for verification, the Lessor and his counsel were elusive and made repeated references to the Area Structure Plan approval as sufficient proof of subdivision.

The Lessor attempted to lend further support to his request by presenting a summary of sales (Exhibit 2). However, the Board was not provided with any documentation showing title transfer or certificates of registration.

On the issue of the 100 metre setback, the Board inquired as to whether the Lessor had applied for a relaxation. After some hesitation he replied that "I believe I did" but admitted that he had made no formal or written request thereof.

The Board is frustrated by the Lessor and Counsel's elusiveness in answering questions or producing documents to verify their assertions. In turn, this behavior leads the Board to question the credibility of the Lessor's requests for annual compensation of \$15,000.00.

The lack of factual verification regarding the aforementioned matters underpins the Board's decision to attach little weight to the Lessor's claim.

In the alternative, the Board prefers to rely on the appraisal report and the Operator's written submission. The methodologies employed by the appraisers are in keeping with accepted professional practices. Upon scrutiny by the Board, it is satisfied that the appraisers were more than generous in providing the Lessor with every benefit of doubt.

The appraisal report is grounded in factual sales data involving meaningful comparables. Moreover, several approaches to valuation were taken out of an abundance of caution. The Board finds the analysis to be both credible and exhaustive. Especially when weighed against the scant facts and evidence provided by the Lessor and his Counsel in respect of comparable examples, and in respect of any attempt to calculate losses on an empirical basis.

Lastly, the Board attaches weight to the letter dated March 25, 2003 (Exhibit 12) wherein the Lessor declares his willingness to accept annual compensation of \$7,500.00. The Board would remind the Lessor that compensation in this review must be set in accordance with facts and circumstances as they existed in April of 2002. This letter provides the Board with an extra margin of assurance as to the veracity and fairness of the Operator's present offer.

Having reviewed the facts, evidence, and testimony presented by both parties, the Board finds the Operator’s offer to be abundantly fair and fixes same.

Summary of Compensation:

Loss of use: \$1,000.00 per acre x 3.43 acres\$3,430.00
 Adverse effect\$5,187.00

Total Annual Compensation\$8,617.00

On the relevant evidence heard, the Board finds a fair and adequate rate of compensation payable by the Operator under the Surface Lease, to be \$8,617.00 per annum, effective April 27, 2002.

An Order will issue varying the rate of compensation payable under the Surface Lease from \$3,650.00 to \$8,617.00 per annum, effective April 27, 2002, and payable on that date in each year thereafter unless and until varied by a further review.

INTEREST:

The Lessor initiated the proceedings for review by letter dated November 17, 2004. The Operator has not complied with Section 27(4) of the *Act* in which notice to the Lessor was to have been given within 30 days after the 4th anniversary of the date of the lease.

Under Section 27(15)(c), the Board may make an order regarding the payment of interest that it considers appropriate. The Board considers the Bank of Canada rate on the due date of the rental payment to be appropriate interest on the balance of annual compensation due. The Bank rates are as follows:

April 27, 2002 2.50%
 April 27, 2003 3.50%
 April 27, 2004 2.25%
 April 27, 2005 2.75%

COSTS:

In considering costs, it is the Board's opinion that the fundamental principle in fixing costs is that a party entitled to an award of costs is entitled to be reimbursed for any reasonable costs reasonably incurred in and incidental to the proceedings before the Board, and necessary to the determination of fair compensation payable for that which gave rise to the proceedings.

The Lessor claimed cost for legal services of \$750.00. No claim was made for personal costs.

The Operator reminded the Board that it had incurred significant costs over the course of preparing for and attending the hearing. Therefore, the Operator requested costs be assumed on a party on party basis.

Although mindful of the Operator’s concerns, the Board finds costs claimed by the Lessor to be reasonable and so fixes in the amount of \$750.00.

Dated at the City of Edmonton in the Province of Alberta this 30th day of November, 2005.

SURFACE RIGHTS BOARD

MEMBER