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# AER Directive 088: Alberta Implements its New Liability Management Framework for Oil and Gas

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On December 1, 2021, the Alberta Energy Regulator (the AER) released *Directive 088: Licensee Life-Cycle Management*.[1] Directive 088 provides a regulated liability management system throughout the energy development lifecycle for Alberta oil and gas licence-holders. The implementation of this new liability management framework is intended to mitigate the billions of dollars of liability associated with inactive and orphaned wells in Alberta. These developments will significantly impact oil and gas industry players going forward. The more holistic approach will likely be less timely and less predictable as the AER attempts to reduce industry and public liabilities.

Directive 088 details how the AER will holistically assess each licensee to determine whether to approve license transfers or pursue specific regulatory action. It also sets forth a management program for licensees, the means for the AER to establish certain closure quotas as needed and updated requirements for the request and return of security deposits. This directive shifts the landscape from the prescribed formula of comparing deemed asset and liability values to a more holistic approach that considers a variety of financial health, asset lifespan, compliance and closure data to assess risk.

## License Capability Assessment

Fundamental to Alberta's new liability management system is the Licensee Capability Assessment (LCA), which is designed to assess the ability of licensees to meet their liability and regulatory obligations throughout the energy development life cycle. We previously analyzed the Government of Alberta's initial Liability Management Framework announced on July 30, 2020.[2]

The LCA framework utilizes multiple factors, including financial health, magnitude of liability and rate of closure activities, and a holistic approach to assess the potential need for security.[3] Any other information provided to the AER by the licensee such as applications, amendments, reporting and other submissions, including financial information submitted in accordance with Directive 067[4] may be used in the holistic licensee assessment (HLA). Notably, the HLA has no prescribed formula; it remains subjective and at the sole discretion of the AER based on the available information at the time of assessment.

The LCA will guide license eligibility under Directive 067 as well as regulatory decisions under Directive 088. Licensees and approval holders must submit a Schedule 3 to the AER, which includes audited financial statements and summaries (or to the extent audited financial statements are not available, either financial statements prepared by management or financing details for start-up companies or companies with no financial history) and a financial summary of the parent company to the extent such financial statements are consolidated. The AER may request additional information from licensees and approval holders, including reserves information, at any time.

## Licensee Management Program

Through the Licensee Management Program, the AER will continually monitor licensees throughout the energy development life cycle. The LCA will assist the AER in identifying high risk licensees and the AER will take proactive action in the form of specific engagement such as education or encouragement to follow industry best practices or if necessary, specific regulatory action such as modifying licensee eligibility under Directive 067, placing restrictions on new AER applications, requiring security deposits or issuing orders.

## Inventory Reduction Program

Through the Inventory Reduction Program, the AER will set mandatory annual closure spend targets of at least 4% of the estimated cost of the company’s wells for each licensee in an effort to reduce licensee liability on an ongoing basis.[5] As we have previously written, the AER encourages licensees to use collaborative closure planning such as area-based closure to retire inactive wells, facilities and pipelines, to reduce liability in a cost-effective manner. One government-funded incentive that licensees can take advantage of is the Site Rehabilitation Program which provides grants to oil field service contractors to conduct well, pipeline, facility and oil and gas site reclamation and closure.[6] The Site Rehabilitation Program accesses up to $1 billion for eligible abandonment and reclamation projects from the federal government’s COVID-19 Economic Response Plan.[7]

## License Transfers

A license transfer application (LTA) may be submitted by the transferor, the transferee or any consultant or agent working on behalf of either party. The parties must provide the AER with current information regarding each working interest participant including the full legal name, contact information and percentage working interest for every well and facility included in the application. Any LTA will trigger an immediate HLA of both the transferor and transferee. The AER will conduct the HLA and either approve, approve with conditions or deny the LTA. No estimated timeline is provided for the completion of this process and the AER will not provide preliminary determinations of expected security requirements or LTA approvals. If not efficiently managed by the AER, the requirement for a holistic licensee assessment for each licence transfer application could result in more uncertainty and delay for purchase and sale agreements requiring the transfer of AER licences.

The AER will consider the LTA in its entirety and may reject LTAs that do not include licenses that have received reclamation certification or are abandoned and classified as "*reclamation exempt*" but should be transferred as part of the license transfer package. This is in contrast to the prior system where reclamation exempt licenses could not be transferred; as part of Directive 088, such licenses must be transferred. AER licenses that are classified as Issued, Amended, Discontinued, Suspension, Abandoned, RecCertified or RecExempt are all eligible to be transferred. Cancelled or Re-entered licenses are not eligible for transfer.

## Security Deposits

Under Directive 088, the AER has more discretion with respect to requiring security deposits than under the previous framework where security deposits were based on a ratio of deemed assets to liabilities of the transferor and transferee.  In assessing whether a security deposit is owing as a condition to LTA approval or as part of the Inventory Reduction Program, the AER will consider the HLA, whether the licensee poses an unreasonable risk pursuant to Section 4.5 of Directive 067 or any other factor the AER considers appropriate, consistent with the broad and subjective powers of the AER to reject an LTA or require a deposit.

The maximum amount of security that can be requested is the amount of the licensee's total liabilities, including the cost of care, custody, ending operations and abandonment and reclamation of the sites. If a security deposit is not received by the specified due date, the LTA will be rejected and the file closed. The more onerous security deposit requirements will impose additional timing and transactional risk factors that parties will need to consider.

## Implications for the Oil and Gas Industry

These developments will significantly impact oil and gas industry players going forward. The primary concerns that we would note are the lack of prescription and indicative timelines. Over time, a preferred form of HLA may evolve but the lack of same may in practice be advantageous to applicants by affording flexibility to shape assessment submissions most favorably for each circumstance. Time will tell.

A lack of certainty as to timing is an issue which always vexes industry (and its financial partners). It is crucial for industry that the AER endeavours to process LTAs in a fashion that ensures discharge of its regulatory and stakeholder responsibilities but also respects the inherent timing issues associated with transfers of licensees. Strategic, timing, and other considerations necessarily associated with applications can be discussed with legal counsel to optimally position your organization to best navigate the new liability management framework.

[1] Alberta Energy Regulator, *Directive 088: Licensee Life-Cycle Management* (December 2021) online (pdf): <static.aer.ca/prd/documents/directives/Directive088.pdf>.

[2] Government of Alberta, *Liability Management Framework* (July 2020), online (pdf): <alberta.ca/assets/documents/energy-liability-management-framework.pdf>

[3] Alberta Energy Regulator, "Holistic assessment and Licensee Capability Assessment" (last visited 2 December 2021) online: <aer.ca/regulating-development/project-closure/liability-management-programs-and-processes/holistic-assessment-and-licensee-capability-assessment>.

[4] Alberta Energy Regulator, *Directive 067: Eligibility Requirements for Acquiring and Holding Energy Licences and Approvals* (December 2021) online (pdf): <https://static.aer.ca/prd/documents/directives/Directive067.pdf>.

[5] "Alberta's New Oil and Gas Liability Management Framework," Cassels Brock & Blackwell LLP (August 6, 2020), online: <https://cassels.com/insights/albertas-new-oil-and-gas-liability-management-framework/>.

[6] Government of Alberta, "Site Rehabilitation Program – Overview" (last visited 2 December 2021) online: <alberta.ca/site-rehabilitation-program-overview.aspx>.

[7] *Ibid*.