**File No. 1742**
**Board Order No. 1742-1**

---

**November 21, 2012**

# SURFACE RIGHTS BOARD

IN THE MATTER OF THE PETROLEUM AND NATURAL GAS ACT, R.S.B.C., C. 361 AS AMENDED

AND IN THE MATTER OF

THE NORTH EAST ¼ OF SECTION 32 TOWNSHIP 83 RANGE 17 WEST OF THE 6TH MERIDIAN PEACE RIVER DISTRICT, EXCEPT PLAN 8630

(The "Lands")

BETWEEN:

Laurie William McDonald

(APPLICANT)

AND:

Penn West Petroleum Ltd.

(RESPONDENT)

---

## BOARD ORDER

---

Heard: July 31, 2012
Panel: Valli Chettiar
Appearances: Laurie William McDonald (the Applicant)
Daron K. Naffin (for the Respondent)

---

## INTRODUCTION

[1] The Applicant, Laurie McDonald, owns the Lands, which are located near Fort St. John, in the Peace River District. He granted a surface lease (the "Subject Lease") of a portion of the Lands (the "Leased Area") to Titan Exploration Ltd., a predecessor in interest to the Respondent, Penn West Petroleum Ltd. ("Penn West"), effective August 4, 2005. Under the Subject Lease, Penn West is entitled to use the Leased Area comprising approximately 4.0 acres for the drilling and operation of a single well, and all roadways on the Leased Area only for the rights granted under the Subject Lease. The Subject Lease provides for a one-time payment of $10,500 for the entry, and an annual compensation of $3,800 that Penn West has been paying Mr. McDonald to date.

[2] In addition to Penn West, another company, Twin Butte Energy Ltd. ("Twin Butte"), operates a wellsite and access road on the Lands. Twin Butte holds the rights to enter, occupy and use its wellsite and access road through a right of entry order dated February 21, 1978, as amended (the "Twin Butte Order"). By a Road Use Agreement made February 5, 2008 (with effect from July 13, 2005) between Twin Butte and Penn West, Penn West uses the Twin Butte access road to get to its own access road, for which it compensates Twin Butte.

[3] The following are Mr. McDonald's claims, and Penn West's response to them.

[4] Mr. McDonald says the annual compensation of $3,800 is inadequate compared to annual compensation being paid under comparable leases in the area. He claims $5,200 is more appropriate. Penn West disagrees with Mr. McDonald's figure, and maintains that $3,800 is the proper annual compensation.

[5] Mr. McDonald says Penn West is using the Twin Butte access road without any agreement with him or compensation to him, and he seeks compensation for Penn West's use of such access road. Penn West says the Surface Rights Board does not have jurisdiction to determine this issue in this proceeding, and even if it did, it is Twin Butte as operator of the Twin Butte access road, and not Penn West, that should be liable for any compensation to Mr. McDonald.

## PRELIMINARY ISSUE

[6] Since Penn West questions the Board's jurisdiction to determine Mr. McDonald's second claim, I will deal with it first.

[7] On May 21, 2010, Mr. McDonald filed with the Board a "Form 2 – Notice to Lessee/Lessor for Rent Renegotiation" under section 11 [now subsection 165(2)] of the *Petroleum and Natural Gas Act,* RSBC 1996, c. 361 (the "Act"). The subject of this Notice is the Subject Lease between the parties to this proceeding, which deals only with the Leased Area and not with any area that Twin Butte operates.

[8] Since Mr. McDonald was not successful in negotiating an amendment of the rental provisions in the Subject Lease, he applied to the Board, under section 166 of the Act, to resolve the disagreement. In his application for rent review, dated December 12, 2011, he refers to the Subject Lease and summarizes the nature of his dispute as follows:

> "1) Penn West offer of $4,100 for surface lease rent appears to be somewhat low.
> 2) The use of road by Penn West without an agreement or remuneration with the landowner has to be addressed."

[9] The Board conducted mediation between the parties. On the first issue, the parties did not agree on an acceptable rent, and on the second issue, Penn West objected to the Board's jurisdiction. Therefore, the Board mediator referred both issues to the Board for arbitration.

[10] Penn West has continually maintained that the issue of compensation for the Twin Butte access road should be dealt with as part of the rent review between Mr. McDonald and Twin Butte when the Twin Butte Order comes up for renegotiation, and the proper forum is not this proceeding. Penn West says any compensation that may be payable is properly payable by Twin Butte, and not Penn West.

[11] The Subject Lease is the subject of Mr. McDonald's application under subsection 166(1). Subsection 166(3) provides that "[o]n an application under subsection (1) of this section, the board may make an order varying the rental provisions in the surface lease or order." The Twin Butte access road does not form part of the Subject Lease and, therefore, the Board has no authority to deal with any issue relating to the Twin Butte access road within the scope of this proceeding.

[12] I agree with Penn West that if Mr. McDonald chooses, he can certainly bring a separate application under section 163 (which deals with loss or damage caused by right of entry) or section 164 (which deals with disagreements or non-compliance with surface leases) to deal with the Twin Butte access road issue.

[13] It is, of course, critical that Twin Butte be properly served if either of these applications is brought to the Board, as Twin Butte will be directly affected by an order of the Board.

## ISSUE

[14] The issue to be determined is the amount of annual compensation payable by Penn West to Mr. McDonald under the Subject Lease, effective August 4, 2009, for the continued use and occupation of the Leased Area.

## FACTS

[15] Penn West presents the following information regarding the Lands and the Leased Area, which Mr. McDonald does not dispute. Therefore, I accept them as undisputed facts:

- The Lands are located approximately 2.5 miles east of Fort St. John.
- The Lands are designated Large Agricultural Holding Zone (A2).
- The current land use is agricultural – hay.
- The Canadian Land Inventory (CLI) soil classification is Class 3c.
- The Leased Area comprises a single well (at NE (9) 32-83-17-W6M) and an access road that are tied-in to a pipeline system. There is a small production building and some equipment including a pump jack, propane tank and methanol tank on site. Traffic on site consists of an operator visiting on a regular basis as part of the inspection of other wells in the area. The site is mowed and weeds are sprayed in the summer months, and snow is plowed in the winter months as required.

[16] Section 18 of the Subject Lease provides that notwithstanding anything contained in the Subject Lease to the contrary, upon the request of either party, the amount of annual compensation payable shall be subject to periodic review as provided for in applicable legislation. The applicable legislative provision is subsection 166(4) of the Act, which provides that "[a]n order . . . varying the rental provisions in the surface lease . . . is effective from the anniversary of the effective date of the surface lease . . . immediately preceding the date of the notice under section 165(2) and is retroactive to the extent necessary to give effect to this subsection."

[17] The Subject Lease is dated August 4, 2005 and its anniversary date is August 4. Mr. McDonald filed the subsection 165(2) notice on May 10, 2010. Therefore, the effective date of the rental review is August 4, 2009 (the "Effective Date"). The parties do not dispute this date.

[18] Mr. McDonald attempted to negotiate a higher annual compensation with Penn West, through its agents, without success. Penn West made an offer of $4,100, which Mr. McDonald declined. In the end, Mr. McDonald filed a section 166 application with the Board in December, 2011 for mediation and arbitration assistance.

## EVIDENCE AND ANALYSIS

[19] In determining the annual compensation payable by Penn West to Mr. McDonald, I must look to section 154 of the Act, any binding authorities of our Courts, and any guidance from Board decisions respecting annual compensation under the Act.

[20] Section 154 of the Act provides as follows:

> **154** (1) In determining an amount to be paid periodically or otherwise on an application under this Part, the board may consider, without limitation, the following:
>
> (a) the compulsory aspect of the right of entry;
> (b) the value of the applicable land;
> (c) a person's loss of a right or profit with respect to the land;
> (d) temporary and permanent damage from the right of entry;
> (e) compensation for severance;
> (f) compensation for nuisance and disturbance from the right of entry;
> (g) the effect, if any, of one or more other rights of entry with respect to the land;
> (h) money previously paid for entry, occupation or use;
> (i) the terms of any surface lease or agreement submitted to the board or to which the board has access;
> (j) previous orders of the board;
> (k) other factors the board considers applicable;
> (l) other factors or criteria established by regulation.
>
> (2) In determining an amount to be paid on an application under section 166, the board must consider any change in the value of money and of land since the date the surface lease or order was originally or last granted.

[21] Since this is an application under section 166, I must consider any change in value of money and of land referred to in subsection 154(2). However, I do not have to consider all the factors listed in subsection 154(1); I will only discuss those factors relevant to the issue at hand, relating the applicable evidence before me. I will also discuss the applicable case authorities as I discuss the various factors. In my final analysis, I will consider whether the total award, comprising compensation for various components, does not exceed or fall below, but represents, proper compensation in all the circumstances of this case (*Scurry Rainbow Oil v. Lamoureux* [1985] B.C.J. No. 1430 (BCSC)).

[22] Both parties filed documentary evidence marked as Exhibits 1 through 9. Mr. McDonald gave evidence at the hearing. Mr. Robert J. Telford, Land Consultant & Appraiser, on behalf of Penn West, gave expert evidence through oral testimony and written expert report respecting estimate of annual compensation, going through the various factors listed in section 154.

[23] At the hearing I pointed out to Mr. Telford and the parties, and I emphasize here again, that the amount of annual compensation is for the Board to determine applying the criteria prescribed by section 154 of the Act. The amount of compensation is not a matter for another person (a land consultant, appraiser or anyone else) to conclude and present to the Board. Compensation determination is unlike an appraisal exercise where an appraiser, who is the expert, after analysis of the market, renders an opinion of value. In the compensation context under the Act, the Board is charged with determining the amount of compensation based on the evidence before it. Therefore, it is up to the parties to present relevant evidence with respect to the section 154 factors to assist the Board in determining the amount of compensation.

[24] Mr. McDonald, in his negotiations with Penn West, managed to obtain details of some leases (the "PW Leases"), which he says Penn West led him to believe are comparable to the Subject Lease, although Penn West now disagrees that they are comparable to the Subject Lease. He presents these details, including his proposed rent for the Leased Area, in a grid form as follows:

| PROPERTY | 1<br>14-4-83-17<br><br>5.0 acres | 2<br>4-9-83-17<br><br>4.9 acres | 3<br>6-31-83-17<br><br>6.0 acres | 4<br>8-36-83-18<br><br>3.8 acres | 5<br>10-23-83-18<br><br>6.4 acres | 6<br>9-23-83-18<br><br>5.8 acres | SUBJECT<br>A-9-32-83-17<br><br>4.0 acres | PROPOSED RENT FOR SUBJECT A-9-32-83-17<br><br>4.0 acres |
|---|---|---|---|---|---|---|---|---|
| LOSS OF USE | $1,250 | $1,225 | $2,700 | $1,710 | $960 | $870 | $1,000 | $1,600 |
| SEVERANCE | $1,200 | $1,000 | $800 | $500 | $500 | $500 | $500 | $1,000 |
| NUISANCE & DISTURBANCE | $1,500 | $1,500 | $1,500 | $1,500 | $2,500 | $2,000 | $1,500 | $1,500 |
| ADVERSE EFFECT | $850 | $975 | $400 | $490 | $940 | $1,130 | $1,100 | $1,100 |
| TOTAL | $4,800 | $4,700 | $5,400 | $4,200 | $4,900 | $4,500 | $4,100 | $5,200 |

[25] Not all compensation factors noted in the first column directly coincide with the factors under section 154. Mr. McDonald says this is the breakdown that Penn West gave him.

**Section 154 Analysis**

[26] I now turn to the section 154 analysis.

[27] Mr. McDonald's general contention is that Penn West is paying him considerably less annual compensation than what it is paying other lessors in the area and also that it has not taken into consideration the rising land values in the area.

[28] As a general proposition, when determining annual compensation, the Board should consider only the actual and ongoing losses to the landowner; an amount that exceeds the loss sustained will no longer be compensation and the Board will have exceeded its jurisdiction (*Western Industrial Clay Products Ltd. v. British Columbia (Mediation & Arbitration Board)*, 2001 BCSC 1458).

Section 154(1)(a) – Compulsory aspect of right of entry

[29] Not applicable in this case.

Section 154(1)(b) – Value of land

[30] Typically, the value of the land is accounted for in determining the one-time payment for the initial entry. However, as the Board in *Helm v. Progress Energy Ltd.*, SRB Order 1634-1, December 2, 2010, at para. 24 noted, the value of the land may be a relevant consideration in determining annual compensation in the sense that land that is more valuable may command a higher rent than land that is less valuable.

[31] Mr. McDonald argues that the highest and best use of the Lands, including the Leased Area, is not agricultural or farming, but rather a home site. He says all of the quarter sections in the area, including the Lands, are home sites, and are worth more, and that he could develop the Lands at any time.

[32] Penn West submits that the concept of highest and best use is associated with market value; it is a prospective and future-looking phenomenon; and it does not relate to the actual loss or impacts arising from Penn West's use of the Leased Area, which are the focus of this proceeding.

[33] Under cross-examination, Mr. McDonald admitted that as at the Effective Date, no development of the Lands had taken place, and also, as at the hearing date, he had no plans for any future development.

[34] Regardless of the parties' submissions, I find that any amount of compensation under this heading may lead to overcompensation as the value of land will generally be accounted for under paragraph 154(1)(c) in determining ongoing annual loss of profit.

Section 154(1)(c) – Loss of a right or profit

[35] This factor is intended to compensate the landowner for loss of a right or profit (or use) relating to the subject site. An award for annual compensation would necessarily have to be based on evidence of probable and reasonably

foreseeable ongoing and recurring loss or damage that can be reasonably quantified (*Arc Petroleum Inc. v. Piper,* MAB Order 1598-2, December 5, 2008, at para. 51). Further, there is no right to remuneration beyond the loss or damage incurred (*Western Industrial, supra,* and *Arc Petroleum Inc. v. Miller,* SRB Order 1633-3, May 24, 2011, at para. 26).

[36] Penn West says, in the agricultural context, as is the case with the Leased Area, this compensation factor relates to loss of crop production caused by an operator's occupation of the wellsite area. It says compensation for such crop loss is payable annually and is set at the value per acre of the farmed crop times the number of acres lost as a result of the entry (*Terra Energy, Corp. v. Rhyason Ranch Ltd.,* MAB Order No. 403A, March 4, 2007, at pp. 31-32).

[37] Penn West also refers to *Piper, supra,* at para. 40, where the Board reasoned that an estimation of crop loss ought to be based on average yield and, in the absence of evidence of average crop prices in average yield years, the Board estimated crop loss based on the most recent prices.

[38] Penn West submits that in the absence of a statutorily mandated reference period for calculating compensation for loss of production, the Board should estimate crop loss based on crop prices as at the Effective Date.

[39] Mr. Telford testified that based on a review of air photos taken in 2010 and an inspection of the Lands on June 14, 2012, the Lands are primarily used for hay production. He says the CLI soil class of the Lands is Class 3c as there are some limitations that adversely affect the productive capability of the Lands, particularly for crop production.

[40] Mr. Telford says according to the British Columbia Forage Council 2009 data, hay yields range from 1.5 to 3.0 tonnes per acre, and the prices range from $65 to $100 per tonne. Based on this data, he suggests that a rate of 2.5 tonnes per acre at $100 per tonne, or $250 per acre, is reasonable compensation for any potential losses associated with hay production. Applying this rate, he concludes that loss of profits associated with the 4.0 acres of the Leased Area is $1,000 as at the Effective Date. He says the actual loss would be less because portions of the Leased Area are cropped. Mr. Naffin points out that this is supported by compensation for hay land in comparable lease agreements submitted by Penn West.

[41] Mr. McDonald disagrees with Mr. Telford's data and says they are highly speculative. He says he should receive $1,600 for loss of profits.

[42] Firstly, Mr. McDonald says even though the Leased Area is currently used for hay production, it could, at any time, be put into grain or seed production, and that good farming practice involves crop rotation. Mr. Telford testified that the rates for crop land is $450 per acre, for hay land in $250 per acre, and for mixed pasture and hay land is $200 per acre (midpoint between $150 for pasture and $250 for hay).

[43] Secondly, at the hearing, when asked on what basis Mr. McDonald arrived at the $1,600 figure, he said he averaged the loss of use amounts for the six PW Leases shown in the table above (which came to $1,452), and rounded it up to $1,600. He admitted that he had a hard time coming up with an appropriate figure, so he averaged the amounts for the six PW Leases, thinking that those were the leases Penn West considered comparable to the Subject Lease.

[44] Thirdly, Mr. McDonald points to the *Helm* decision, at para. 29, and says even though the Helm lands are inferior to the Lands, the Board awarded a higher amount ($2,000 for 4.79 acres) for loss of profits.

[45] With respect to Mr. McDonald's first point, Penn West says the Board should dismiss Mr. McDonald's claim for compensation respecting alleged losses that may result from prospective and speculative future land use. It says any such proposed change in land use, including the planting of seed crops had not arisen as at the Effective Date or even as at the hearing date. It says should Mr. McDonald ultimately plant seed crops leading to actual losses, he can seek compensation for such losses at the next rent review or potentially through an application under paragraph 163(1)(a) of the Act. I agree.

[46] With respect to Mr. McDonald's second point about averaging the loss of use amounts for the PW Leases, Penn West says those leases are not true comparables to the Subject Lease and it is inappropriate to consider those amounts. I will discuss the PW Leases in more detail below.

[47] With respect to Mr. McDonald's third point, Penn West submits that other Board decisions are for guidance only and specific awards in one case cannot be equally applied to another because of the unique circumstances of each case. It says the glaring difference between the *Helm* case and this case is the effective date: in Helm it was 2007 and here it is 2009; also, there are other factual differences between the two cases. I agree. It is highly unlikely that the factual circumstances of any two cases will be identical or even highly similar, lending to similar results.

[48] Having no information from Mr. McDonald to assist me in quantifying the probable and reasonably foreseeable ongoing loss or damage from Penn West's use of the Leased Area, I accept Mr. Telford's data and confirm the compensation for loss of profits payable by Penn West to Mr. McDonald at $1,000.

Section 154(1)(d) – Temporary and permanent damage from right of entry

[49] The parties did not identify any damage requiring compensation under this heading.

Section 154(1)(e) – Severance

[50] This factor is intended to compensate the landowner where land is severed as a result of an entry such that the landowner not only loses the use of the occupied land but also the use of other land; where there is loss of use of, and profit from, the severed land on an ongoing basis, compensation should be included in an annual payment (*Helm, supra,* at para. 34).

[51] Penn West submits that the Board in *Terra Energy, supra,* at pp. 34 – 35, accepted severance to mean "land that cannot be accessed by farm equipment."

[52] Mr. McDonald claims $1,000 for severance. He says the presence of the subject wellsite makes it difficult for him to farm the Leased Area and the adjacent 5.0 acre parcel to the south (the "Adjacent Parcel"), which he also owns. Furthermore, he says, it affects the development of the Adjacent Parcel into a home site, if he so chooses, as there used to be a residence on it before.

[53] Under cross-examination, Mr. McDonald agreed with the Board's definition of severance in *Terra Energy, supra.* He also agreed that no part of the Leased Area or the Adjacent Parcel is inaccessible by farm equipment, although it may take a bit longer to manouevre around the areas. He confirmed that: wellsite 9-32-83-17 on the Adjacent Parcel which Penn West's predecessor, Titan, used to operate has been abandoned; now there is no activity on that wellsite; and he signed a General Release of Claim, dated August 4, 2005, releasing Titan from any claims arising out of that wellsite.

[54] Mr. Telford concludes that there is no severance.

[55] Mr. Naffin says Penn West's current offer includes $500 for severance even though based on Mr. Telford's and Mr. McDonald's evidence, Mr. McDonald is not entitled to any compensation for severance. Mr. Naffin says the $500 Penn West offers is supported by the comparable leases Penn West submitted.

[56] I do not accept that there is no severance. The evidence appears to indicate minimal severance. So, the question is what is the appropriate compensation? The Board noted in *Helm, supra,* at para. 54, that the Act specifically allows the Board to consider other leases, implying there should be some sense of fairness or equity between landowners in compensation paid. Considering the minimal severance in this case and the fact that Penn West is offering to pay $500 (perhaps to maintain equity amongst all its leases), I accept that $500 is reasonable compensation for severance in this case.

Section 154(1)(f) – Nuisance and disturbance from right of entry

[57] This factor is intended to compensate the landowner for nuisance and disturbance arising from the operator's entry and use of the lands. Ongoing nuisance and disturbance is also compensable in an annual payment.

[58] Mr. McDonald says because of the wellsite, there is: a lot of trespass; a lot of kids and other people, including operators, drive up and down with their four-wheelers which cause a lot of noise and extra dust on the road, which in turn causes lower crop yields; and gas smell. He says also because of the presence of the wellsites, both on the Leased Area and on the Adjacent Parcel (even though the wellsite on this Parcel has been abandoned), there is additional nuisance as it is difficult to farm around these areas and it takes longer and more effort.

[59] Mr. Telford estimates that $1,475 should be attributed to nuisance and disturbance based on certain tangible and intangible factors.

[60] Penn West says tangible factors include increased time, costs and inconvenience associated with farming around the Subject Lease and intangible factors relate to Mr. McDonald's time spent dealing with Penn West on its visits to the Leased Area.

[61] Mr. Telford says the intangible factors may involve noise from the facilities, and dealing with surveyors, contractors and operators. Mr. Telford says there are fewer facilities on the Leased Area compared to some of the other leases Mr. McDonald referred to, and as a result, the level of noise, traffic and other impacts is lower.

[62] Mr. Telford calculates the *tangible* portion as follows:

> <u>Premises:</u> based on the cropping program and the typical farming patterns relating to the Leased Area, operations would involve six to eight passes over the Leased Area each crop season; for interior and midfield locations, the estimated additional operating time is 23 to 32 minutes depending on the size of equipment and rate of speed, taking into consideration the location of the wellsite, and the extra corners, inputs, and manoeuvres around the wellhead facilities; and from 2006 to 2010, custom equipment rates ranged from $150 to $375 per hour depending on the type and size of the equipment.
>
> <u>Calculation:</u>
> 23 min. x 6 passes = 2.3 hrs. @ an average rate of $250/hr. = $575
> 32 min. x 8 passes = 4.3 hrs. @ an average rate of $250/hr. = $1,075

[63] Mr. Telford calculates the *intangible* portion as follows:

> <u>Premises:</u> The Leased Area is considered to be low impact due to the limited visitation and activity; therefore, very little time and inconvenience would be associated with this site.
>
> <u>Calculation:</u>
> 1 day (8 hrs.)/year @ $50/hr. = $400

[64] Based on the above, he suggests a total of $1,475 for any nuisance and disturbance. Penn West's offer included $1,500 for nuisance and disturbance, and it also included $1,100 for "adverse effect."

[65] The term "adverse effect" is not one of the factors referenced in section 154. Interestingly, in cross-examination, Mr. Naffin questioned Mr. McDonald as to where he would find the term "adverse effect" in the Act, to which Mr. McDonald replied he does not know and that he was simply accepting the factors Penn West was using.

[66] Then in Mr. McDonald's cross-examination of Mr. Telford, he asked Mr. Telford why Penn West would use the factors shown in the table above, including "adverse effect" to allocate compensation. Mr. Telford says he does not know why Penn West uses these factors, but in his mind, "adverse effect" relates to nuisance and disturbance.

[67] Mr. McDonald also says that to him "adverse effect" fits in the same category as nuisance and disturbance.

[68] In his closing submissions, Mr. Naffin explained that the term "adverse effect" is used in the compensation context in Alberta, where tangible and intangible effects are considered, as Mr. Telford does in his report in quantifying compensation for "nuisance and disturbance" in the BC context.

[69] What is not clear is why Penn West offered $1,100 for "adverse effect" separate from "nuisance and disturbance" when both Mr. Telford and Mr. McDonald testified that they understood "adverse effect" to mean "nuisance and disturbance." While Mr. McDonald is agreeable to Penn West's offer of the $1,500 and $1,100, he did say that he does not know what "intangible" is in this context.

[70] While I have insufficient evidence to challenge Mr. Telford's $1,045 estimate for the tangible portion, I do have plenty of evidence to challenge the $400 estimate for the intangible portion.

[71] Even if the $1,100 can be said to be attributable to the extra noise, dust and traffic and other factors Mr. McDonald is referring to, no consideration has been given to Mr. McDonald's time, effort and frustration he has had to endure in dealing with Penn West with respect to this rent renewal.

[72] Mr. McDonald tried, without success, to negotiate with Penn West for more than a year and a half – from May 21, 2010 when he filed the Notice to Negotiate to December 12, 2011 when he filed his section 166 application to the Board.

[73] The email communication between Penn West's agents and Mr. McDonald shows that it took a lot of time, effort and persistence on the part of Mr. McDonald to extract lease information from Penn West. Mr. McDonald insisted that he wanted to compare "apples to apples" and yet he was given information

about the six PW Leases, which Penn West now says are not true comparables to the Subject Lease. Mr. McDonald relied on this information to his detriment. (Parenthetically, I add that this does not excuse Mr. McDonald from critically analyzing the evidence he intends to rely on.) At no point during this year and a half did Mr. Darren Rosie or Mr. Nolan Treble, with whom Mr. McDonald was dealing, say that the PW Leases were not proper comparables. This begs the question as to whether Penn West's representatives intentionally misled Mr. McDonald or they were not fully knowledgeable about the requirements of the Act. I rather suspect it is the latter, as they seem to allocate compensation to factors not referenced in the Act – such as "adverse effect."

[74] The renewal letters Mr. Rosie sends out to landowners still say "adverse effect." All of this can cause unnecessary confusion and frustration to landowners, and also waste their time, which could lead to additional compensation.

[75] Although Mr. McDonald, being a realtor and an appraiser, should have done his own independent research and questioned the information Penn West provided, I find Penn West's dealings in this respect less than forthcoming.

[76] Operators, such as Penn West, should ensure that their practices are transparent, forthright, and above all compliant with the Act (as opposed to legislation or practices of other jurisdictions).

[77] In light of all of the evidence before me, I find that $3,400 [$1,500+$1,100+$800 (16 hrs./yr. @ $50/hr.)] should be awarded as compensation under this factor, which works out to 2.0 hours per month at $50 per hour for the intangible portion.

[78] Since Penn West has not provided me with the breakdown of the compensation for the leases it says are comparable to the Subject Lease, I cannot make any comparison; however, I find that, in all the circumstances of this case, this award is reasonable.

Section 154(1)(g) – Effect of other rights of entry

[79] Not applicable in this case.

Section 154(1)(h) – Money previously paid for entry, occupation or use

[80] Not applicable in this case.

Section 154(1)(i) – Other leases

[81] Mr. McDonald says his rent increase represents only 8%, whereas the increases for some of the neighbouring leases (seven concluded renewals which include the six PW Leases and one 2012 offer) range between 10% and 45%.

[82] Penn West says simply comparing rent increases, without knowing the circumstances of the negotiations, is not helpful. It says perhaps the starting rental was low.

[83] In addition to the six PW Leases, Mr. McDonald references a few other leases showing the following information: total rental range: $2,220 to $6,000; size range: 2.5 acres to 5.4 acres; effective date range: Oct. 2001 to Oct. 2010 (none in 2009); and lease numbers. He does not provide the land use or the proximity of these properties to the Leased Area. Nor does he provide the breakdown of the compensation paid or any analysis of how all of this information relates to the issue at hand.

[84] Mr. Telford says he would not rely on any of the six PW Leases because the effective dates for four of them are in 2011 (two years after the Effective Date), and for two of them are in 2010; other than lease 4 which is 3.8 acres, they are all larger than the Subject Lease; only leases 1 and 2 are for hay, whereas leases 3 and 4 are for cultivated use, and leases 5 and 6 are a mixture of bush pasture.

[85] Mr. Telford completely dismisses the other leases Mr. McDonald references as there is insufficient information to determine whether they are comparable to the Subject Lease, and besides many of them are dated. I too find the limited information Mr. McDonald provides with respect to these other leases completely unhelpful.

[86] Penn West provides 22 other leases (the "PW Comparables") detailing the surface location, well site acreage, access road acreage, total acreage, total current rental , land use, original lease date, rental effective date (all in 2009), and well status. The lease sites range from 3.65 acres to 7.5 acres; annual rental ranges from $3,000 to $7,360; and the land use is described as one of hay/pasture, pasture, cultivation or hay.

[87] Mr. Telford says the largest driver of compensation is size and land use. Of the PW Comparables, he says leases D, I, K and O are all very close to the Subject Lease in terms of their size – around 4.0 acres; D is cultivated whereas the Subject Lease is not; and I, K and O are close in land use - being hay. He says lease I is the best indicator as it is 4.19 acres, with a rental of $4,000 for hay.

[88] Penn West complains that Mr. McDonald does not provide the breakdown or the circumstances of the other leases he refers to, but neither does Penn West provide any breakdown of the total rental in terms of the section 154 factors for any of the 22 PW Comparables. The breakdown it provided on the six PW Leases does not fully coincide with the section 154 factors. So, for any analysis of these leases, the only available point of comparison is the total rental.

[89] In analyzing the PW Comparables, the 14 leases with hay as their only land use indicate an average rental of $857 per acre. Two of the six PW Leases (with

effective dates in 2010, which are closer to the Effective Date) that have hay as their only land use indicate an average rental of $960 per acre. Applying these rates to the Subject Lease of 4.0 acres, which is currently used only for hay, produces $3,428 and $3,840 respectively. The current rental of $3,800 is higher than the 14 2009 leases and slightly lower than the two 2010 leases.

[90] This, of course, is a very rough estimation and does not reflect the individual circumstances of these leases. With respect to the Subject Lease, Penn West's offer of $4,100 is close, except that it does not take into account the intangible aspect of the additional nuisance Mr. McDonald experiences in dealing with the Subject Lease.

Section 154(1)(j) - Previous orders of the board

[91] The parties did not refer to any previous orders of the Board with respect to the Subject Lease.

[92] Mr. McDonald referred to the Board's order in *Helm*, *supra*, with respect to the quantum of the loss of profits. As I said earlier, the facts in that case are distinguishable, and, therefore, the Board's award in that case is not directly applicable in this case.

Section 154(1)(k) – Other factors the Board considers applicable

[93] The parties did not particularly point out any factors that I should consider under this heading.

[94] However, I consider the relationship between landowners and operators as an important factor in this context. This factor may not lead to direct compensation, but it may have an indirect influence on compensation under some of the other factors in subsection 154(1) – for example, if the parties' behavior exacerbates nuisance or disturbance.

[95] In this case, Mr. McDonald exclaimed that Penn West (through its agents) misled him on a number of occasions – for example, they gave him inapplicable leases for comparison, when he specifically informed them that he wanted to compare "apples to apples"; the heads of compensation they use to negotiate with landowners are not in line with the Act; they gave incorrect information on the process to deal with the Twin Butte road access issue; and they were very slow and unresponsive to Mr. McDonald's requests.

[96] I do not have sufficient evidence before me to determine whether Penn West intentionally led Mr. McDonald astray, and neither is that the focus of this proceeding.

[97] However, I do want to emphasize that it is incumbent upon every party to a transaction or process to act in good faith with the other parties, particularly when there may be, or may appear to be, power imbalance amongst the parties. Even

where there may be no legal duty to do so, parties should treat each other with respect and care, particularly where long-term relationships, such as those between landowners and operators, are at stake.

[98] On another note, it is also incumbent upon each party to seek their own independent advice to serve their best interest.

Section 154(1)(l) – Other factors or criteria established by regulation

[99] There are none.

Section 154(2) – Change in value of money and of land

Change in value of land:

[100] One of Mr. McDonald's main concerns is that Penn West has not taken into account the change in value of his Lands. Mr. McDonald argues that market value of farmland has continued to rise since the Subject Lease was signed in 2005. He provides some rudimentary data on resales (paired sales), between 2004 and 2011, of seven properties (which he characterizes as farmland/agricultural land) in the wider Fort St. John area indicating price increases in the range of 35% to 169%, without any source, analysis or conclusion as to how this information should be applied in this case – should it be in support of a change in value under paragraph 154(1)(b) or under subsection 154(2)? Mr. Naffin says it may be considered in support of one, but not both. There were also inaccuracies in Mr. McDonald's calculations that Mr. Naffin corrected.

[101] Mr. Telford testified that the properties Mr. McDonald refers to are not the same type of property as the Lands – they are recreational and not agricultural; many of them are much further away from the Lands – some 40 or 50 miles away and others near the Alberta border; and all of the resale dates are after the Effective Date.

[102] Mr. Telford says Farm Credit or MLS statistics would have been better.

[103] Mr. McDonald says there are no sales in the immediate vicinity of the Lands because "people hold onto their lands." Mr. Naffin argues that is the most compelling evidence that there has been no change in land value.

[104] As I indicated above, the value of the land is generally accounted for in the initial one-time payment. Mr. McDonald received $10,500 in this respect. I found that, for purposes of paragraph 154(1)(b), any compensation for change in land value may lead to overcompensation in determining annual compensation. For purposes of subsection 154(2), I do not find Mr. McDonald's evidence compelling or reliable.

Change in value of money:

[105] In determining the change in value of money, Mr. Telford applies the Consumer Price Index as the best indicator. He says the value of money has increased by 5.64% from 2005 (Subject Lease acquisition date) to 2009 (Effective Date). Therefore, he says the annual rental of $3,800 in 2005 would cost $4,014 in 2009. However, he concludes that because subsection 154(1) indicates an annual compensation of $2,475 and subsection 154(2) indicates $4,014 and the current annual compensation of $3,800 falls between these two amounts, it should not be adjusted upwards.

[106] I agree with Mr. Telford that the Consumer Price Index may be used to determine the change in value of money, but I do not agree with his conclusion because that is not what subsection 154(2) says.

[107] First of all, if subsection 154(1) only indicates an annual compensation of $2,475, as Mr. Telford opines, I question why Penn West has been paying $3,800 since the commencement of the Subject Lease in 2005. I have no evidence to suggest that this was an improper amount. The existing compensation is an important consideration, as the Board in *Miller, supra,* found.

[108] Secondly, subsection 154(2) mandates the Board to consider the change in value of money. The starting point for this in this case is the $3,800 that is being paid to Mr. McDonald. Therefore, as of the Effective Date, at least $4,014 should be paid to Mr. McDonald as annual compensation. Perhaps, that is why Penn West offered $4,100 to Mr. McDonald, which he refused to accept.

**Determination of a global sum**

[109] Based on the evidence in support of the various section 154 factors, the following breakdown results:

| Section 154 Factor | Annual Compensation |
|---|---|
| Loss of profit | $1,000 |
| Severance | $ 500 |
| Nuisance and disturbance | $3,400 |
| **Total** | **$4,900** |

[110] As the Court pointed out in *Western Clay, supra,* and the Board reiterated in *Helm, supra,* the Board should not order an amount to be paid in excess of the actual, or probable, loss sustained by the landowner. However, the practical reality is that quantifying compensation for intangible loss, such as nuisance and disturbance, is unscientific and is incapable of formulaic determination as it depends on the unique circumstances of each case. In this respect, the Board, in *Helm, supra,* at para. 55, aptly said "calculating damages for intangible loss,

such as for nuisance and disturbance, is not a precise exercise but involves the exercise of judgment and discretion to determine what is appropriate and just in the circumstances of any particular case. . . .All in all, determining annual rent involves consideration of the evidence and all of the circumstances, coupled with the exercise of judgment."

[111] Based on the evidence before me, I find the annual compensation should be increased from $3,800 to $4,900 effective August 4, 2009. I am satisfied that, in the circumstances of this case, this total award, comprising compensation for the three factors listed above, does not exceed or fall below, but represents, proper compensation.

**ORDER**

[112] The Surface Rights Board orders that the rental provisions under the Subject Lease are amended to provide that effective August 4, 2009, the annual rent payable to Mr. McDonald is $4,900.00. Penn West Petroleum Ltd. shall forthwith pay to Mr. McDonald any difference in annual rent paid since August 4, 2009 and the revised annual rent effective August 4, 2009.

DATED: November 21, 2012.

FOR THE BOARD

Valli Chettiar, Arbitrator