

August 9, 2017

Shoal Point Energy  
Suite 203, 700 West Pender Street  
Vancouver, BC  
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Attention: Mr. Mark Jarvis, Chief Executive Officer

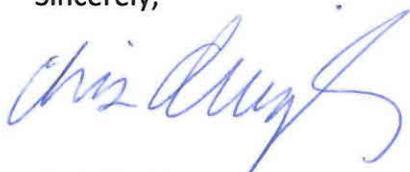
Dear Mr. Jarvis:

**Re: Application to Pursue Alternative Completion Strategy**  
**Respecting Diligent Pursuit - Exploration Licence 1070**

Further to Susan Gover's email of July 25, 2017, attached please find the Board's Reasons for Decision in the above-noted matter.

If you have any questions or require further information, please do not hesitate to contact the undersigned at 709-778-1458

Sincerely,



Chris Quigley  
Legal Counsel

Enclosure

## **Reasons for Decision**

### **In the Matter of**

### **Shoal Point Energy Ltd.**

**Application to Pursue Alternate Completion Strategy  
Respecting Diligent Pursuit - Exploration Licence 1070**

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## 1.0 Introduction

The Canada-Newfoundland and Labrador Offshore Petroleum Board (the “C-NLOPB” or “the Board”) was created by the *Canada-Newfoundland and Labrador Atlantic Accord Implementation Act* and the *Canada Newfoundland and Labrador Atlantic Accord Implementation Newfoundland and Labrador Act*. For the purpose of this decision report, reference will be made to the federal version of the legislation (the “*Accord Act*”).

As part of its mandate, the C-NLOPB is responsible for petroleum resource management in the Canada-Newfoundland and Labrador Offshore Area (the “offshore area”). This includes the administration of statutory requirements with respect to exploration, development and production in the offshore area.

Pursuant to the *Accord Act*, the Board administers the land rights granted in the offshore area. In that regard, when the Board issues a call for bids to grant licences in the offshore area, the call for bids contains the terms and conditions to be applied to exploration licences. The sole criterion for selection of the winning bid is the monetary value of the work commitment to be expended during the first five years of the licence term.

A successful bidder becomes an interest owner and is issued an exploration licence that has a nine-year term consisting of two Periods, I and II. Period I requires the drilling of a well to validate the exploration licence as a pre-requisite for continuing to Period II which is the remaining years of the nine-year exploration licence term. Failure to validate an exploration licence during Period I results in the lands reverting to the Crown. An exploration licence may be extended beyond the nine-year term only in accordance with the provisions of the *Accord Act*.

Exploration Licence 1070 (“EL 1070”) was issued effective January 15, 2002 with a nine-year term, Period I being five years and Period II the remaining four years. During the last 15 years, the Board has granted amendments to the terms and conditions (Fundamental Decisions 2006.03, 2007.15, 2008.01) to afford the interest owner the opportunity to commence Period II of the licence. Period I of EL 1070 was validated with the 2K-39Z well and the licence term proceeded to Period II.

Shoal Point Energy Ltd. (SPE), the Applicant, is the current interest owner and representative of EL 1070.

In 2012, the Board permitted diligent pursuit to drill well 3K-39Y, for a non-conventional play, to be conducted using hydraulic fracturing operations pursuant to section 70 of *the Accord Act*. As with all wells that have been drilled on this licence, this well is spud on an onshore licence and drilled into the offshore area (an onshore to offshore well).

In November 2014, the Government of Newfoundland and Labrador appointed a panel to review the implications of hydraulic fracturing operations in Western Newfoundland. A so called “pause” (in practical effect, a discontinuance) was put in place on such activity in Western Newfoundland, which also meant a pause on the Applicant’s hydraulic fracturing plans. Although the panel

presented its report and recommendations on May 31, 2016, the “pause” remains in place preventing the hydraulic fracturing operations in relation to this well.

## **2.0 The Application – Overview**

SPE has made application to the Board to pursue work on their other well on EL 1070, 2K-39, including the drilling of a side track. They request that the Board confirm that this work on well 2K-39 would meet the criteria of subsection 70(3) of the *Accord Act* respecting diligent pursuit of EL 1070.

## **3.0 Analysis of the Merits of the Application**

### **3.1 Further History of EL 1070**

On January 15, 2011, the Board agreed that the 3K-39 well was being diligently pursued and permitted the extension of the term of this licence beyond the nine-year term pursuant to subsection 70(1). That well was spud on February 18, 2011 by Dragon Lance Management Corporation (DLMC), the operator on behalf of SPE.

DLMC conducted several formation flow tests. The initial flow test was conducted on the main well bore, 3K-39, consisting of a closed chamber test carried out over several open-hole intervals with no indication of oil influx. Due to poor hole conditions, DLMC was granted approval to sidetrack and test 3K-39Z. Again, due to operational issues (Measurement While Drilling Tool that was stuck in hole), the sidetrack was abandoned resulting in a cased-hole Drill Stem Test (DST) being conducted over the main well bore. The subsequent DST was performed over one of the three approved intervals and even with the aid of artificial lift there was no visible sign of oil influx into the well bore. DLMC suspended the well in the summer of 2012 with the potential to re-enter the well to test the remaining two intervals of 3K-39Z at a later date.

In December 2012, SPE again approached the Board respecting diligent pursuit of the 3K-39Y well on this licence. SPE asserted that it needed to hydraulically fracture the formation in order to complete its assessment of the formation since the well tests proved unsuccessful. The rationale for that request was that hydraulic fracturing would afford additional data collection.

On December 18, 2012 the Board wrote SPE to confirm diligent pursuit, given SPE’s intention to:

*“...re-enter 3K-39Z, drill a sidetrack (3K-39Y) and then test the well including a limited program of near well bore stimulation that would itself include a limited hydraulic fracturing operation.”*

SPE has acknowledged in this Application that this prospect “still is an unconventional play” requiring hydraulic fracturing. In the Application, SPE has also confirmed that “it is technically able to safely complete the testing of 3K-39 by means of hydraulic fracturing.”

### **3.2 Authority**

Accord Act, Section 70:

Continuation of exploration licence where drilling commenced

*70 (1) Where, prior to the expiration of the term of an exploration licence, the drilling of any well has been commenced on any portion of the offshore area to which the exploration licence applies, the exploration licence continues in force while the drilling of that well is being pursued diligently and for so long thereafter as may be necessary to determine the existence of a significant discovery based on the results of that well.*

Deemed pursued diligently

*(2) Where the drilling of a well referred to in subsection (1) is suspended by reason of dangerous or extreme weather conditions or mechanical or other technical problems encountered in the drilling of the well, the drilling of that well shall, for the purposes of subsection (1), be deemed to be being pursued diligently during the period of suspension.*

Drilling of second well deemed commenced

*(3) Where the drilling of a well referred to in subsection (1) cannot be completed for mechanical or other technical problems and if, within ninety days after the cessation of drilling operations with respect to that well, or such longer period as the Board determines, the drilling of another well is commenced on any portion of the offshore area that was subject to the exploration licence, the drilling of that other well shall, for the purposes of subsection (1), be deemed to have commenced prior to the expiration of the term of the exploration licence.*

### **3.3 Technical Assessment**

SPE has recognized and agrees that the 3K-39Y well was the well upon which the Board determined diligent pursuit to afford a hydraulic fracturing of a non-conventional play. This was also made clear by the Board in its December 18, 2012 correspondence. That is not contested.

The Board has permitted a substituted well under subsection 70(3) when there was a valid technically sound basis for such determination as a mechanical or technical problem was encountered which prevented the achievement of the well objectives. That was the case for EL 1090R for the Glenwood H-69 well held and operated by Husky Oil Operations Limited.

Given the condition of the wellbore prior to the suspension, SPE now advocates it would be better suited to take advantage of subsection 70(3) of the *Accord Act* and drill another well, without prejudice, allowing them the proper basis of design to meet the data acquisition and testing requirements. SPE asserts that the premise for the Application is the casing design in 3K-39 and issues related to tools stuck in 3K-39 which SPE claims are mechanical issues.

The C-NLOPB disagrees with SPE's assessment of what constitutes a "mechanical and technical issue" as required by subsection 70(3). DLMC did not identify any technical or mechanical problems at the time the well was suspended that would have precluded testing the remaining two intervals. All objectives of the Approval to Drill a Well up to that point in time had been achieved. DLMC sought a suspension of well operations to afford time to address the environmental assessment scope related to hydraulic fracturing and to plan a hydraulic fracture test program. Therefore, subsection 70(3) does not apply. While hydraulic fracturing would afford a further opportunity to ascertain whether data can support a significant discovery application, such operations are stalled, not because of a mechanical or technical problem, but because of the "pause" with respect to hydraulic fracturing.

#### **4.0 Final Determination**

The Board must exercise its jurisdiction in rights matters with the goal of maintaining the integrity of the land tenure system and also apply the *Accord Act* in a fair, consistent and reasonable manner. This regulatory approach fosters exploration by creating a clear understanding that those who acquire lands must explore within the nine-year term and the granting of extensions on the basis of diligent pursuit must be in compliance with the legislative framework. This provides certainty for all participants in the offshore area and the public.

Given diligent pursuit is premised on a sound technical rationale, the governments have delegated section 70 decisions solely to the Board, recognizing the Board's technical expertise. Notably, Board decisions under section 70 are not fundamental decisions requiring subsequent approval of the federal and provincial natural resource ministers.

In this matter, the Applicant, SPE, has not established a mechanical or other technical problem to justify the drilling of an alternative well in accordance with subsection 70(3). As stated in the Application, the request is "because of delays in the environmental assessment of Western Newfoundland and Labrador onshore and offshore fracking".

The Board has determined that the "pause" on hydraulic fracturing is not a technical or mechanical issue that would warrant a substitute conventional well required under subsection 70(3). Had the governments contemplated dispensation for such reasons, the language of section 70 would have been broadened to include language similar to that contained in section 56 of the *Accord Act*, to include matters respecting an environmental or social problem of a serious nature for example.

To permit the re-entry of 2K-39 as a substitute well without a valid mechanical or technical issue would have serious consequences for offshore exploration and regulatory certainty. The Board

must exercise its discretion in a fair, reasonable and consistent manner, not only for the Applicant, but for all interest owners regulated by the Board.

In considering the merits of this Application, the Board has reviewed the evidence and arguments presented by the Applicant and the technical advice of staff. The Board does not see the merit in permitting the drilling of the substitute well as requested in the Application where there is no technical or mechanical basis, and given the Applicant acknowledges they will eventually require hydraulic fracturing, which continues to be subject of a pause, to assess flow potential of this non-conventional play.

Based upon the foregoing, the Board denies this Application.



Scott Tessier  
Chair  
On behalf of the Board

St. John's, Newfoundland and Labrador  
August 9, 2017