



CANADIAN ASSOCIATION
OF PETROLEUM PRODUCERS

July 8, 2008

Hon. Thomas A. Hockin
Panel Chair
Expert Panel on Securities Regulation
Ottawa, ON K1A 0G5

Dear Mr. Hockin:

Re: Securities Regulation and the Canadian Upstream Petroleum Industry

Thank you for the invitation to appear and discuss securities regulation with the Expert Panel on Securities Regulation when it was in Calgary on Wednesday, May 7th. We enjoyed the opportunity to meet with you and your colleagues on the panel and discuss different regulation issues and structures as they do and could impact on Canada's upstream oil and gas industry. It was also good that the panel heard from individual companies, members of CAPP, both at our meeting and on their own. As was made clear, each company's comments represented those of their individual company and not necessarily those of our association as a whole.

The Canadian Association of Petroleum Producers (CAPP) represents 140 companies that explore for, develop and produce natural gas, natural gas liquids, crude oil, oil sands, and elemental sulphur throughout Canada. CAPP member companies produce more than 95 per cent of Canada's natural gas and crude oil. CAPP also has 135 associate members that provide a wide range of services that support the upstream crude oil and natural gas industry. Together, these members and associate members are an important part of a \$100-billion-a-year national industry that affects the livelihoods of more than half a million Canadians.

Of the areas under discussion in the panel's consultation paper, CAPP is most interested in securities regulatory structure (Consultation Item 5). *What is the most effective and efficient regulatory structure?* This is not a new issue and we realize there are significant policy and political components to answering this question. The key principles for producers in the Canadian upstream oil and gas industry include:

- Effectiveness – meets the objectives outlined in the consultation paper for ensuring shareholder protection while adhering to the underlying principles behind securities regulation
- Efficiency – regulations should be applied consistently across jurisdictions at minimal cost of compliance
- Simplicity – regulations should be simple to understand with easy compliance
- Clarity – principles and rules are transparent to both issuers and shareholders

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These principles can be met with a range of regulatory models, each of which has both merits and drawbacks.

In 2004, CAPP lent its support to the development of uniform securities legislation (USL), which was an initiative of the federal Wise Persons' Committee and the Interprovincial Securities Initiatives Committee. We liked the establishment of a common language, the streamlining of regulations, and the potential to reduce filing and reporting expenses. A copy of our letter is attached.

Uniform securities legislation was a key element in developing an effective regulatory passport system. However, it can also be seen as an important initial step to establishing a single securities regulator since nearly identical regulatory wording across jurisdictions makes it easier from a regulatory perspective to collapse several regulators into one.

Whether a passport system or a single regulator, each system needs to assure the oil and gas industry that it will be effective regarding oil-and-gas specific issues. One current example of particular importance to producers is oil and gas reserves definition and reporting. Reserves are the foundation of the oil and gas business. As such, how reserves are defined and reported has an enormous impact on the value of company shares.

This was the key element for our comments to the Alberta Securities Commission (ASC) in 2006 during its review of the Standards of Disclosure for Oil and Gas Activities under National Instrument 51-101 (NI-51-101). The discussion involved a wide range of opinions, encompassing the views of both non-exempt and exempt filers. NI-51-101 had different impacts and raised different concerns for different companies. Much discussion and debate, both across different groups of companies within the industry and with the ASC, led to a great depth of understanding for all parties involved. There was recognition that a single standard would not address all parts of the industry.

The implemented policy was not praised by all. But it gained acceptance and respect in large part because of the thorough discussion of all facets of the issue and a perception that the regulator had thoroughly understood and appreciated the issue. Because of this acknowledged understanding by the regulator, NI-51-101 has since been amended to adjust specific areas where it had not been working well.

This highlights the importance of a regulatory system that is knowledgeable and engaged with our industry in order to develop regulations that benefit both filers and shareholders alike.

In contrast, the industry's experience with the US Securities and Exchange Commission (SEC) to modify its rules for recognizing oil sands reserves has been quite different. The petroleum industry is only one of numerous industries that fall under the SEC's view, and Canadian oil and gas is merely a subset of that. As only a small part of what the SEC regulates, oil sands reserves definition and recognition had been designated a low priority even though billions of barrels were written off the books at year end 2004 (with a commensurate reduction in book value) because of their "*last day of the year pricing policy*" for reserves valuation.

It is interesting and instructive that this write-down was largely ignored by the investment community as they recognized that this was a rules-driven change rather than a material change in company value. This questions the helpfulness to investors in this instance of a securities reporting regulation that is ultimately ignored by investors.

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After much effort by CAPP, the US oil and gas industry and many US consultants, the SEC undertook a systematic review. Just last month they announced their new reserves rules, which includes many of the recommendations made by industry.

The point of this example is that to serve the investment community well, a regulatory system needs sufficient insight and sensitivity to a particular industry. Responsiveness to issues that affect material investor information, relevant reporting and filing requirements and effective and efficient adherence to significant principles-based regulation all have the potential to be impeded unless sector and industry-specific responsiveness is built into the system.

The attractiveness of a passport system for the oil and gas industry is that it promises to retain this sector-specific sensitivity while still promoting effectiveness and efficiency. While a single-regulator system may achieve this efficiency, for our industry, the effectiveness of industry-specific responsiveness is vital.

One possible suggestion to address sector or geographic balance in a single regulator could be to structure the regulator based on the size of market capitalization. This could ensure both shareholder interest and responsiveness to filers based on their proportion of the value of equity either held or traded. For petroleum, since twenty-five percent of the market capitalization on the Toronto Stock Exchange is in oil and gas shares, a quarter of a single regulator's structure could be developed around the understanding and responsiveness to oil and gas. In any event, given the position of the Canadian oil and gas industry in the Canadian financial market, any change may have a significant impact on us.

As stated in our consultation meeting, we appreciate the opportunity to be involved to this point and would be ready and willing to provide input on any options that the panel may find to meet the wide range of principles. Please do not hesitate to call me at (403) 267-1159 should you wish to discuss any of these views further.

Yours truly,



Greg L. Stringham
Vice President, Markets & Fiscal Policy

Attachment