

## BACKGROUND – HORIZONTAL GAS WELL DRILLING INCENTIVE

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*The Incentive: The new gas well incentive is volume-based and establishes a maximum Crown royalty rate of 2.5 per cent and a freehold production tax rate of 0 per cent on the first 25 million cubic metres of natural gas produced from all horizontal gas wells drilled between June 1, 2010 and March 31, 2013.*

The oil and gas industry is a major part of Saskatchewan's economy accounting for about 18 per cent of provincial GDP. The industry invests over \$2 billion annually in exploration and development activities and maintains 27,350 direct and indirect jobs. In 2009-10 it generated an estimated \$1.4 billion in revenues for the province.

Saskatchewan's natural gas industry is at a mature stage of development with many pools discovered in the early 1950s. Nearly 70 per cent of Saskatchewan's established natural gas reserves have already been produced. The majority of remaining reserves are contained in low permeability formations. As such, recoveries are much less than in more conventional reservoirs.

Saskatchewan's gas reservoirs have been developed almost exclusively with vertically drilled wells -- only one horizontal gas production well has been drilled to date. Industry has already drilled a number of horizontal gas wells in Alberta reservoirs. Initial production rates in some instances are about four to five times that of vertical wells drilled in the same pool.

The new horizontal gas well drilling incentive builds on a similar and long-established policy of volume drilling incentives for horizontal oil wells. These incentives have been in place since April 1991 and have resulted in a positive response from industry. Over 10,000 horizontal oil wells have been drilled to date in Saskatchewan and oil production from horizontal wells now makes up almost one-half of provincial oil production. The results are a significant increase in both the established reserves and annual production volumes of oil. It is expected that techniques developed for the drilling and completion of horizontal oil wells can be successfully applied to the development of natural gas resources.

This new incentive comes about as a result of a recent review the government undertook of the opportunities for horizontal gas well development and ways to make our natural gas resource more competitive with those of other jurisdictions. The government had discussions on this initiative with oil industry associations and other stakeholders, in particular the Canadian Association of Petroleum Producers, the Small Explorers and Producers Association of Saskatchewan and Enterprise Saskatchewan. Through those discussions the government concluded there is a lack of information at this time to definitively determine the appropriate incentive and royalty/tax structure for horizontal gas well drilling. The government has therefore implemented an interim three-year incentive and royalty/tax structure similar to the strategy that had initially been established for horizontal oil wells. The incentive will be evaluated at the end of the three-year period and revised as required.

The standard horizontal well approval process established under *The Oil and Gas Conservation Act* and regulations will apply to horizontal gas wells, including the submission and approval of a horizontal well plan and the submission and issuance of a well licence.