RECENT JUDICIAL DEVELOPMENTS OF INTEREST TO ENERGY LAWYERS

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This article provides an overview of recent judicial developments of interest to energy lawyers. The authors summarize and provide commentary on recent Canadian case law in the areas of: Aboriginal law, conflict of laws, contracts, environmental law, securities law, taxation, joint operators, bankruptcy law, freehold leases, administrative law, and rights of first refusal.

Cet article donne un aperçu des derniers développements judiciaires d'intérêt pour les avocats du domaine de l'énergie. Les auteurs résument la situation et commentent la récente jurisprudence canadienne dans les domaines suivants: droit autochtone, conflit de lois, droit de l'environnement, législation régissant la vente de valeurs mobilières, fiscalité, opérations conjointes, législation sur la faillite, location à bail franche, droit administratif et le droit de préférence.

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* Both of Gowling Lafleur Henderson LLP. The authors wish to acknowledge the valuable assistance of Sean Murphy, Christine Yick, Irene Chen, and Ethan Sinclair.

I. ABORIGINAL LAW

A. *BROKENHEAD OJIBWAY NATION V. CANADA (A.G.)*[1]

1. BACKGROUND

The Treaty One First Nations (TOFN) asserted treaty rights, treaty-protected inherent rights, and Indigenous cultural rights over large tracts of land in southern Manitoba. This decision addresses the Crown's duty to consult and accommodate through the project approval process of the National Energy Board (NEB). Particularly at issue here is an appeal by the TOFN of the Governor in Council's approval of the NEB's issuance of Certificates of Public Convenience and Necessity for the construction of three pipeline projects through southern Manitoba: the TransCanada Keystone Pipeline Project, Enbridge's Southern Lights Pipeline Project, and the Alberta Clipper Pipeline Expansion Project.

[1] 2009 FC 484, 345 F.T.R. 119 [*Brokenhead Ojibway*].

2. FACTS

The TOFN sought declaratory and prerogative relief with respect to the NEB approval of the Keystone Pipeline Project,[2] the Southern Lights Pipeline Project,[3] and the Alberta Clipper Pipeline Expansion Project,[4] which are proposed to pass through areas where their claim is considered by some to be relatively weak. All three pipeline projects have been approved for routes that run almost entirely over private and previously disturbed land and over existing rights-of-way. Project impacts were therefore expected to be minimal. During the respective hearings for all three projects, the NEB heard submissions from several First Nations communities and found that the respective proponent had meaningfully engaged potentially impacted groups, and had considered their concerns and made modifications to the project where appropriate.

In approving the Keystone Project, the NEB stated:

> The hearing process provided all parties with a forum in which they could receive further information, were able to question and challenge the evidence put forward by the parties, and present their own views and concerns with respect to the Keystone Project. Standing Buffalo and the Dakota Nations of Manitoba had the opportunity to present evidence, including any evidence of potential infringement the Project could have on their rights and interests. The Dakota Nations of Manitoba did not provide evidence at the hearing.[5]

The NEB went on to note the proponent's commitment to engage in continued and ongoing consultation, to develop a work plan, and to "incorporate mitigation to address specific impacts to sacred sites into its Environmental Protection Plan."[6]

These sentiments were echoed in the reasons for decision for both the Southern Lights Project and the Alberta Clipper Project; both Enbridge projects which use the same corridor. In its approval of the Alberta Clipper Project, the Board directed Enbridge to take certain measures in the event of the discovery of historical, archaeological, and sacred burial sites, and again commended Enbridge's commitment to undertake an ongoing consultation process.[7] The Board reiterated this point in its reasons approving construction of the Southern Lights Project, noting Enbridge's commitment to work with the Aboriginal communities to jointly develop a course of action to address any unidentified issues. The Board also noted that the project would involve a relatively brief period of construction and that the vast majority of the facilities would be buried, concluding that any impacts on Aboriginal interests would likely be minimal.[8]

The TOFN appealed these decisions on the grounds that the federal Crown did not fulfill its obligations of consultation and accommodation before granting the approvals. While

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2 *TransCanada Keystone Pipeline GP Ltd.*, NEB Decision OH-1-2007 (September 2007) [*Keystone*]. All NEB decisions can be found online: NEB <http://www.neb-one.gc.ca/>.

3 *Enbridge Southern Lights GP on behalf of Enbridge Southern Lights LP and Enbridge Pipelines Inc.*, NEB Decision OH-3-2007 (February 2008) [*Southern Lights*].

4 *Enbridge Pipelines Inc.: Alberta Clipper Expansion Project*, NEB Decision OH-4-2007 (February 2008) [*Clipper*].

5 *Keystone*, *supra* note 2 at 41, cited in *Brokenhead Ojibway*, *supra* note 1 at para. 5.

6 *Keystone*, *ibid.* at 42.

7 *Clipper*, *supra* note 4 at 42-43.

8 *Southern Lights*, *supra* note 3 at 34-35.

acknowledging the efforts of the NEB and the project proponents, the TOFN alleged that resolution of the outstanding land claims in the affected area was the larger issue that should have triggered the Crown's duty to consult, independent of the NEB. The Court therefore had to determine whether, and to what extent, the Crown's duty to consult can be fulfilled by the NEB process.

3. DECISION

The Court acknowledged that the NEB regulatory process is "well-suited to address mitigation, avoidance and environmental issues that are site or project specific," but that it is not intended or designed "to address the larger issue of unresolved land claims."[9] The Court then held that "the NEB process may not be a substitute for the Crown's duty to consult where a project under review directly affects an area of unallocated land which is the subject of a land claim or which is being used by Aboriginal peoples for traditional purposes."[10]

However, of particular importance in this decision was the principle that "the content of the duty to consult with First Nations is proportionate to both the potential strength of the claim or right asserted and the anticipated impact of [the] development … on those asserted interests."[11] The Court was satisfied with the NEB process of consultation and accommodation since it addressed the concerns raised by the TOFN. The Court also found that the TOFN had failed to establish on the evidence that the projects amounted to a "substantial interference with a treaty [right] or a traditional land use claim."[12] Also, the projects were on rights-of-way that the TOFN acknowledged were not available for the settlement of any land claim.[13] The process provided through the NEB therefore sufficiently addressed the specific concerns of the Aboriginal communities potentially affected by the pipeline projects. The Court then went on to find, assuming the regulatory process is meaningful, accessible, and adequate, that

> [t]o the extent that regulatory procedures are readily accessible to Aboriginal communities to address their concerns about development projects like these, there is a responsibility to use them. First Nations cannot complain about a failure by the Crown to consult where they have failed to avail themselves of reasonable avenues for seeking relief. That is so because the consultation process is reciprocal and cannot be frustrated by the refusal of either party to meet or participate.[14]

The Court did concede, in *obiter*, that had any of the projects crossed into an area that was part of an outstanding land claim, the Crown would have had an independent obligation to consult beyond the NEB process.[15]

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9 *Brokenhead Ojibway*, *supra* note 1 at paras. 26-27.
10 *Ibid.* at para. 29.
11 *Ibid.* at para. 23.
12 *Ibid.* at para. 33.
13 *Ibid.* at para. 43.
14 *Ibid.* at para. 42, citing *Ahousaht Indian Band v. Canada (Minister of Fisheries and Oceans)*, 2008 FCA 212, 297 D.L.R. (4th) 722.
15 *Brokenhead Ojibway*, *ibid.* at para. 44.

4. COMMENTARY

The broader implications of this case are with respect to the ability of any regulatory body to adequately engage in, account for, and dispense with the Crown's duty to consult in the circumstances of an alleged Aboriginal claim or right. The Crown's duty in all cases is proportionate to the potential strength of the claim or the right asserted, and to the anticipated impact of development on those asserted interests. So long as the potential impacts on those interests fall within the scope of the mandate of the regulatory body, and so long as the regulatory process by which that body operates provides an adequate avenue for Aboriginal participation, consultation, and mitigation of established adverse impacts of the development, an independent duty on the part of the Crown will not be triggered, and there is an obligation on the part of the Aboriginal communities to address their issues and concerns through that regulatory process. However, where the claim or right asserted is beyond the scope of the commission's mandate, or the adverse impact on the alleged right or claim is beyond the mitigation potential of the regulatory process, an independent duty on the part of the Crown may be triggered.

B. *ATHABASCA CHIPEWYAN FIRST NATION V. ALBERTA (MINISTER OF ENERGY)*[16]

1. BACKGROUND

A significant amount of oil sands development in Alberta takes place in traditional First Nations lands subject to the terms of Treaty 8.[17] Treaty 8 contains a hunting clause that states that First Nations people have the right to pursue their traditional hunting, trapping, and fishing activities on land surrendered to the government, "saving and excepting such tracts [of land] as may be required or taken up from time to time for settlement, mining, lumbering, trading or other purposes."[18] In 2005, the Supreme Court of Canada examined the implication of this clause in *Mikisew Cree First Nation v. Canada (Minister of Canadian Heritage)*.[19] In that case, the Supreme Court stated that an alienation of land or resources by the province for one of the purposes stated in the treaty may trigger a duty to consult. *Athabasca Chipewyan* considers whether or not such a duty was triggered by the Crown granting long-term leases to Shell Canada Inc. (Shell) for the purposes of oil sands development.

2. FACTS

The Athabasca Chipewyan First Nation (ACFN) applied for judicial review of the Crown's decision to grant the leases without consultation. The ACFN sought a declaration that the Minister had a duty to consult with the ACFN before granting the leases, and that the Minister breached this duty. The ACFN also sought a declaration that the Minister was under

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16 2009 ABQB 576, [2010] 2 W.W.R. 703 [*Athabasca Chipewyan*].

17 Canada, *Treaty No. 8 Made June 21, 1899 and Adhesions, Reports, Etc.* (Ottawa: Queen's Printer, 1966), online: Office of the Treaty Commissioner <http://www.otc.ca/siteimages/Treaty8.pdf>.

18 *Ibid.* at 13.

19 2005 SCC 69, [2005] 3 S.C.R. 388.

"a continuing duty to consult the ACFN in respect of the Leases and an order quashing … or alternatively … suspending or staying the Leases."[20]

The Minister's position was that there was no duty to consult in respect of mineral dispositions because "mineral dispositions do not result in the taking up of any land under the terms of Alberta's historical treaties, and because the leasing of … mineral rights does not result in any adverse impact on the exercise of First Nations rights and traditional uses."[21] However, any actual development of the mineral resources under the terms of the lease would trigger the duty to consult (for example, drilling, mining, exploration, etc.). The Crown and one of its lessees moved to dismiss the application on the basis that there was no merit to the claim or any genuine issue for trial since the ACFN had filed its application more than six months after the relevant decision, and therefore was out of time within the *Alberta Rules of Court*.[22]

The issue in this case is when time began to run in respect of the limitation date. Ordinarily, time begins to run in a judicial review application when the decision is made. However, a line of cases state that there is a statutory duty to provide notice of a decision and, therefore, time does not start to run until such notice has been provided.[23] The Crown admitted that no written notice was ever provided but they argued that there was no statutory duty to provide notice. The ACFN argued that they never obtained notice, and therefore the clock never started to run in terms of the limitation date.[24]

3. DECISION

The Court found that even if time did not begin to run until the ACFN obtained notice, the ACFN obtained constructive notice of the issuance of the leases by virtue of the fact that Alberta Energy posted a notice of successful bids on the Aboriginal Community Link, an electronic posting service.[25] This service, along with other electronic posting services, would have advised interested parties of lands that are open for bid and the outcomes of those bids. Constructive notice was enough to start the clock and, therefore, the ACFN was out of time.

4. COMMENTARY

By deciding that constructive notice sufficed to start the limitation clock, the Court made a crucial ruling with respect to the content of the duty to consult (that is, that constructive notice is enough to satisfy the duty). The Court effectively decided in this case that the First Nation's rights under Treaty 8 must be balanced against the Crown's duty to provide notice of conduct that might adversely affect the First Nation's rights, with due consideration given to the potential impact of the conduct. The duty to consult was satisfied by providing constructive notice on a community website with respect to the granting of leases that may

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20 *Athabasca Chipewyan*, *supra* note 16 at para. 8.
21 *Ibid.* at para. 9.
22 Alta. Reg. 390/68, r. 753.11.
23 *Athabasca Chipewyan*, *supra* note 16 at para. 51, citing *Becker v. Alberta (Director of Employment Standards)*, 2000 ABCA 329, 277 A.R. 131 at paras. 12-13; *Edmonton (City of) v. L.A. Ventures Inc.*, 1999 ABQB 649, 313 A.R. 161 at paras. 6-7.
24 *Athabasca Chipewyan*, *ibid.* at para. 52.
25 *Ibid.* at para. 74.

affect those rights because the potential adverse effects of the leases, prior to any actual operations, was minimal.

II. CONFLICT OF LAWS

A. *VAN BREDA V. VILLAGE RESORTS LTD.*[26]

1. BACKGROUND

In determining whether a province is the appropriate jurisdiction for a matter to be heard, a court must determine whether there is a "real and substantial connection" between the matter and jurisdiction,[27] and must apply the doctrine of *forum non conveniens*.[28] To determine whether to strike out the claim under the doctrine of *forum non conveniens*, the court must determine whether "there is another forum that is clearly more appropriate than the domestic forum."[29] In 2002, the Ontario Court of Appeal set out an eight-factor test in *Muscutt v. Courcelles* to determine whether Ontario should assume jurisdiction over a matter involving a foreign defendant on the basis of a "real and substantial connection."[30] This test is frequently used and cited in other Canadian jurisdictions, including Alberta,[31] and by the Supreme Court of Canada.[32] The eight factors are as follows:

- the connection between the forum and the plaintiff's claim;
- the connection between the forum and the defendant;
- unfairness to the defendant in assuming jurisdiction;
- unfairness to the plaintiff in not assuming jurisdiction;
- the involvement of other parties to the suit;
- the court's willingness to recognize and enforce an extra-provincial judgment rendered on the same jurisdictional basis;
- whether the case is interprovincial or international in nature; and
- comity and the standard of jurisdiction, recognition and enforcement prevailing elsewhere.[33]

Seven years after *Muscutt*, two decisions of the Ontario Superior Court of Justice, *Van Breda v. Village Resorts Ltd.*[34] and *Charron Estate v. Bel Air Travel Group Ltd.*,[35]

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26 2010 ONCA 84, 98 O.R. (3d) 721 [*Van Breda* (C.A.)].
27 *De Savoye v. Morguard Investments Ltd.*, [1990] 3 S.C.R. 1077 at 1108.
28 *Amchem Products Inc. v. British Columbia (Workers' Compensation Board)*, [1993] 1 S.C.R. 897.
29 *Ibid.* at 900.
30 (2002), 60 O.R. (3d) 20 (C.A.) [*Muscutt*].
31 *Robinson v. Fiesta Hotel Group Resorts*, 2008 ABQB 311, 450 A.R. 167.
32 *Castillo v. Castillo*, 2005 SCC 83, [2005] 3 S.C.R. 870.
33 *Ibid.* at para. 45, citing *Muscutt*, *supra* note 30 at 45-53.
34 (2008), 60 C.P.C. (6th) 186 (Ont. Sup. Ct. J.) [*Van Breda* (Sup. Ct. J.)].
35 92 O.R. (3d) 608 (Sup. Ct. J.) [*Charron*].

consolidated in *Van Breda*, led the Ontario Court of Appeal to reconsider the application of the eight factors.

The Uniform Law Conference of Canada has also developed a model *Uniform Court Jurisdiction and Proceedings Transfer Act*[36] intended to implement uniform statutory rules by which all Canadian jurisdictions can establish the appropriate forum. To date only four Canadian jurisdictions have adopted the *CJPTA*: Saskatchewan, the Yukon Territory, Nova Scotia, and British Columbia.

2. FACTS

In *Charron*, a Canadian couple was on an all-inclusive vacation in Cuba, which had been booked through on Ontario travel agent, when the husband died while scuba diving, an activity included in the all-inclusive package. The estate and family of the deceased brought an action for breach of contract and negligence against two Ontario defendants and several foreign defendants, including the scuba diving equipment provider, the diving instructor at the marina, and the captain of the diving boat.

In *Van Breda*, the plaintiff, a resident in Ontario, travelled to Cuba with his common-law spouse. His common-law spouse had arranged the trip through an Ottawa defendant who had also arranged for the common-law spouse to work part-time as a tennis instructor at the resort during the vacation in exchange for accommodation, meals, and transportation. The plaintiff was injured while using the resort's exercise equipment and was rendered paraplegic. This statement of claim was also for breach of contract and negligence, and named both Ontario and foreign defendants.

3. DECISION

The appellants argued that the *Muscutt* test should be replaced by the approach put forward in the *CJPTA*. The Court of Appeal found that the *CJPTA* retains the real and substantial connection test as a basic governing principle for the assertion of jurisdiction against parties who do not reside in the jurisdiction, and who have not agreed or submitted to the jurisdiction, but agreed that it should be considered in clarifying or modifying the *Muscutt* test.[37]

In finding that Ontario was the appropriate jurisdiction for both matters, the Court clarified and reformulated the *Muscutt* test by condensing the eight-step test into essentially a two-step analysis. The Court added that in the interests of order and fairness the test should not be a "mechanical counting of contacts or connections,"[38] and, as per *Muscutt*, "[n]o factor is determinative. Rather, all relevant factors should be considered and weighed together."[39]

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36 Uniform Law Conference of Canada, *Uniform Court Jurisdiction and Proceedings Transfer Act*, online: Uniform Law Conference of Canada <http://www.ulcc.ca/en/us/Uniform_Court_Jurisdiction_+_Proceedings_Transfer_Act_En.pdf> [*CJPTA*].

37 *Van Breda* (C.A.), *supra* note 26 at para. 69.

38 *Hunt v. T&N plc*, [1993] 4 S.C.R. 289 at 326, cited in *Van Breda* (C.A.), *ibid.* at para. 43.

39 *Muscutt*, *supra* note 30 at 45, cited in *Van Breda* (C.A.), *ibid.* at para. 46.

The first step under the modified test is to establish whether a real and substantial connection is presumed to exist by falling under r. 17.02 (excepting subrules (h) and (o)) of the Ontario *Rules of Civil Procedure*,[40] which provides the circumstances under which a party may be served *ex juris*. The circumstances under r. 17.02 are similar to the circumstances for presumed jurisdiction provided under s. 10 of the *CJPTA*. If a real and substantial connection may be presumed, the defendant bears the burden to show that a real and substantial connection does not exist. If one of the presumptive circumstances is not present, the onus is on the plaintiff to show that there is a real and substantial connection in the particular circumstances of the case.[41]

The second step, "the core of the analysis," looks at the connection between the forum and the plaintiff's claim, and the forum and the defendant respectively; the first two steps in the *Muscutt* analysis. The remaining six *Muscutt* factors should now serve as "analytical tools" to assist in the determination and should not be treated independently. Included in the determination should be a consideration of fairness (*Muscutt* factors 3 and 4), the relevance of involvement of other parties (*Muscutt* factor 5), the court's "willingness to recognize and enforce an extra-provincial judgment rendered on the same jurisdictional basis" (*Muscutt* factor 6), and, finally, "[w]hether the case is interprovincial or international in nature" and the comity of jurisdiction (*Muscutt* factors 7 and 8).[42] In both cases, the test was satisfied and Ontario was deemed to be the appropriate forum.

4. COMMENTARY

This rearticulation of the *Muscutt* test simplifies, to some extent, the determination of a real and substantial connection by adding two core steps to the analysis and by providing a basis for determining who bears the onus through the first step. The test retains all of the *Muscutt* factors as relevant or necessary considerations, but they are reframed as flexible tools for determining the larger issues of fairness and order, rather than prescribed steps in the determination. While all of the important factors of the test are retained, the practicality of their application has been improved by allowing more flexibility.

B. *VICTORIA OIL & GAS PLC V. ALHAMBRA RESOURCES LTD.*[43]

1. BACKGROUND

As a general rule, Canadian courts have no jurisdiction to determine title to, or an interest in, foreign land. However, a Canadian court may, in certain circumstances, exercise *in personam* jurisdiction and enforce rights that affect land in foreign jurisdictions.[44] This *in personam* exception applies where the dispute dealt with by the Canadian court is primarily concerned with a personal obligation running between the parties. The effect on a title or

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40 R.R.O. 1990, Reg. 194.
41 *Van Breda* (C.A.), *supra* note 26 at para. 109.
42 *Ibid.*
43 2009 ABCA 64, 448 A.R. 374 [*Victoria Oil*].
44 See e.g. *Catania v. Giannattasio* (1999), 174 D.L.R. (4th) 170 (Ont. C.A.); *Precious Metal Capital Corp. v. Smith*, 2008 ONCA 577, 92 O.R. (3d) 701.

interest in land must be incidental to the court's exercise of jurisdiction over that personal obligation.

2. FACTS

This case involved the appeal of an injunctive order enjoining the appellants from disposing of an oil and gas licence in Kazakhstan. The appellants were Alhambra Resources Ltd. (Alhambra), an Alberta-based public company, and Saga Creek Gold Company LLP (Saga Creek), a wholly owned subsidiary of Alhambra and the registered holder of the licence. The respondents were Victoria Oil and Gas Plc (Victoria), a British public company, and its two wholly owned subsidiaries, Feax Investments Co. Ltd. (Feax) and Victoria Energy Central Asia LLP (VECA), all carrying on oil and gas exploration in Kazakhstan.

In 2005, Saga Creek transferred the licence to VECA, then controlled by Olga Elefteriadi (Olga). Victoria acquired the licence when it bought Feax, the 100 percent owner of VECA. VECA carried out operations and expended money under the licence. Then, in 2008, Rasova Enterprises Company Limited (Rasova), another company controlled by Olga, brought an action against VECA and Saga Creek in Kazakhstan alleging that the 2005 transfer of the licence was invalid. The Kazakhstan court declared the transaction invalid. A subsequent appeal of that decision was dismissed, and the Alberta Court of Appeal accepted that Olga had "successfully created a voidable transaction under Kazakhstan law."[45] The licence was thus registered to Saga Creek at the time of this decision, and the evidence suggested that Alhambra was in the process of disposing of the licence.

In 2008, the respondents were granted injunctive relief preventing the appellants from disposing of the licence. This case was an appeal of that injunction. The respondents sought a declaration that the appellants held the licence in a constructive trust for the benefit of the respondents, and an order directing the appellants to transfer the licence back to VECA. Alhambra acknowledged that Saga Creek was the trustee of the licence and had no beneficial interest in it.[46]

3. DECISION

The Court of Appeal ultimately concluded that the statement of claim did disclose a personal obligation between the parties and that Alhambra controlled Saga Creek and was correctly subject to the Court's jurisdiction.[47] The statement of claim disclosed that the respondents had been deprived of a licence for which they had paid $14.5 million, and the appellants had been equally unjustly enriched. Injunctive relief was upheld under the *in personam* exception on the bases that there was thus a personal contractual obligation between the parties regarding the transfer of the licence, and that the respondents would have suffered irreparable harm had the appellants been able to dispose of the licence.[48]

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45 *Victoria Oil*, *supra* note 43 at para. 6.
46 *Ibid.* at para. 12.
47 *Ibid.* at para. 13.
48 *Ibid.* at paras. 13-14.

4. COMMENTARY

This case demonstrates the potential for Alberta courts to exercise jurisdiction over oil and gas interests in foreign countries. It appears that as long as the dispute between the parties is contractual in nature, or the plaintiff party can establish an equitable relationship between the parties, Canadian courts may enforce the *in personam* rights of the plaintiff party even where they directly relate to interests in foreign land.

III. CONTRACTS

A. *WALLACE V. ALLEN*[49]

1. BACKGROUND

A letter of intent regarding the purchase and sale of assets is frequently used in the oil and gas industry as a step towards a complete and final agreement between the parties. A common issue between the parties upon failure to reach a final agreement and close the transaction is the binding nature of the letter of intent. The question is whether the execution of a further agreement was a condition of the transaction, or whether it was intended to be an expression of the manner in which the contract, already agreed to, will be completed. The former is unenforceable, while the latter is enforceable.

2. FACTS

After weeks of negotiation, the parties executed a document that they referred to as a letter of intent for the purchase and sale of shares in four companies. The letter of intent between the parties in this case stated: "It is also agreed by the parties that there will be much legal work to be done upon acceptance by both sides and that the wording of this agreement may alter somewhat," and continued: "This letter of intent must be reduced into a binding agreement of purchase and sale by the parties within the next 40 days."[50] Months later, after a course of conduct by both parties representing their respective intentions to follow through with and close the transaction, the buying party did not appear at the closing and the selling party treated the transaction as at an end on the closing date.

3. DECISION

At trial it was determined that the parties did not have a binding agreement until the final share purchase agreement was signed. However, the Ontario Court of Appeal reversed the trial judge's decision, finding that the wording of the letter of intent expressed an obvious intention to be bound and that only the wording of the agreement would change when "reduced into a binding agreement," rather than the actual substance of the agreement.[51] The Court of Appeal also took into account the conduct of the parties between the time that the letter of intent was executed and the time that the deal fell through and found that both

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[49] 2009 ONCA 36, 93 O.R. (3d) 723.
[50] *Ibid.* at para. 27.
[51] *Ibid.* at para. 28.

parties had been acting throughout as though they had a binding deal, and "[t]o suggest that the parties did not consider themselves bound would be contrary to the evidence."[52]

4. COMMENTARY

This decision reinforces the importance of constructing the document to represent the parties' actual intentions at the time of execution. If the letter is merely intended to be an agreement to agree at a later date, the letter should clearly state that such further agreement is a condition of the contract. In other words, the letter should clearly express that there has not yet been a full meeting of the minds of the parties. This type of preliminary agreement is common in many industries, and the importance of clarifying the binding nature of them is often given inadequate consideration by the parties. By not fully addressing the points raised in this case the parties are creating substantial risk if the terms stated in the letter are incomplete, or the obligations of the parties are not fully understood.

B. *TERCON CONTRACTORS LTD. V. BRITISH COLUMBIA (TRANSPORTATION & HIGHWAYS)*[53]

1. BACKGROUND

The doctrine of fundamental breach has historically been applied to restrict the operation of exclusion of liability clauses, and to enable the aggrieved and innocent party to obtain redress from the party at fault despite the existence of the exclusion clause. A fundamental breach occurs when the breach in question deprives the innocent party of substantially the entire benefit of the contract.[54]

2. FACTS

The Province of British Columbia issued a request for proposals (RFP) for the construction of a highway in northwestern British Columbia. The RFP stipulated a closed list of six eligible proponents. Tercon Construction Ltd. (Tercon) and Brentwood Enterprises Ltd. (Brentwood) were the two short-listed bidders. However, Brentwood intended, with the province's knowledge and encouragement, to do the work as part of a joint venture with an ineligible bidder. The province ultimately awarded Brentwood the contract.

Tercon brought an action for damages alleging that the province "had considered and accepted an ineligible bid and that, but for that breach, [Tercon] would have been awarded the contract."[55] The case turned on the interpretation of the following clause in the RFP:

> Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim.[56]

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52 *Ibid.* at para. 37.
53 2010 SCC 4, [2010] 1 S.C.R. 69 [*Tercon*].
54 *Ibid.* at para. 106.
55 *Ibid.* at para. 12.
56 *Ibid.* at para. 60 [emphasis omitted].

3. DECISION

The trial judge concluded that the province had breached the terms of the RFP and that it had acted "egregiously" in taking active steps to hide the fact that the winning bid was noncompliant.[57] The trial judge ultimately held that the exclusion clause did not specifically exclude the province from liability for accepting a non-compliant bid. Tercon was awarded approximately $3.5 million in damages. The province appealed, and the Court of Appeal unanimously reversed the trial judge's decision. Tercon then appealed to the Supreme Court of Canada.

In its judgment, the Supreme Court unanimously eliminated the doctrine of fundamental breach as it applied to the circumstances, and in its place provided the following three-step approach:

(1) Does the exclusion clause, as interpreted in the context of the terms of the contract, apply to the circumstances of the case? This involves considerations of the parties' intentions and the context in which the contract was formed.[58]

(2) If the exclusion clause applies, was the clause unconscionable at the time the contract was entered into? This may involve a consideration of the balance of bargaining power.[59]

(3) If the exclusion clause applies and is valid, the court must then determine whether it should nevertheless refuse to enforce it because of the "the existence of an overriding public policy." This involves weighing the public policy in question against the strong public interest in enforcing executed contracts. The onus of demonstrating the existence of an overriding public policy lies on the party seeking to limit enforcement of the clause.[60]

In the circumstances of this case, the Supreme Court was split on the interpretation and application of the clause in question. The majority found that the exclusion clause did not operate to bar Tercon's claim, noting specifically the importance of upholding the integrity of the tendering process by accepting only compliant bids and, in finding the clause ambiguous, applied the *contra proferentum* principle in favour of Tercon.[61] The majority also noted the "egregious" conduct of the province mentioned in the trial judge's decision.[62] The minority found that the exclusion clause applied and was enforceable in the circumstances, focusing on the interest of enforceability of contracts[63] and the fact that there was no inequality of bargaining power.[64]

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57 *Tercon Contractors Ltd. v. British Columbia*, 2006 BCSC 499, [2006] 6 W.W.R. 275 at para. 150.
58 *Tercon*, *supra* note 53 at para. 122.
59 *Ibid.*
60 *Ibid.* at para. 123.
61 *Ibid.* at paras. 78-79.
62 *Ibid.* at para. 3.
63 *Ibid.* at para. 134.
64 *Ibid.* at para. 131.

4. COMMENTARY

This case essentially creates a new analytical framework for the interpretation of exclusion of liability clauses, abolishing the need to assess whether a contractual breach is "fundamental." However, the reach of this decision beyond the interpretation of exclusion clauses in the public procurement process remains unclear. The practicality of applying the new analytical framework also remains to be seen, and may give rise to further ambiguities in precedent as reflected in the 5-4 split in the decision.

C. *BG INTERNATIONAL LTD. V. CANADIAN SUPERIOR ENERGY*[65]

1. BACKGROUND

The Association of International Petroleum Negotiators (AIPN) *2002 Model International Operating Agreement*[66] contains default provisions substantially different than those contained in the Canadian Association of Petroleum Landmen (CAPL) form. In particular, the *2002 Model Agreement* provides that when a notice of default is delivered, and the default is not cured by the defaulting party, the non-defaulting parties are required to cover any shortfall to rectify the default. The *2002 Model Agreement* also contains provisions for the removal and replacement of operators in the event of operator default and provides that all disputes, failing a successful ADR, are to proceed through final and binding arbitration. However, the *2002 Model Agreement* also provides that parties may apply to courts for certain interim measures.

2. FACTS

This case involved an operating property off the coast of Trinidad and Tobago. Canadian Superior Energy Inc. (CSEI) was the operator of a semi-submersible rig on the site, pursuant to the *2002 Model Agreement*, and held the lease in its name. The rig was operated by Maersk Contractors Services (Maersk) on behalf of the owners. BG International Limited (BGI) alleged that it had paid its share of cash calls invoiced from CSEI for indebtedness to Maersk, but that CSEI did not make the necessary payments to Maersk. CSEI in turn alleged that the difficulties arose because a third party, Challenger Energy Corp. (Challenger), had earned a 25 percent interest and failed to pay its cash calls, causing there to be insufficient funds to pay all creditors. Maersk commenced the process under the operating agreement to terminate the contract.

BGI acknowledged its obligation under the operating agreement to rectify the default, and tendered the relevant $47 million. There was a substantial threat that Maersk would remove the rig from the property. BGI commenced arbitration proceedings in accordance with the operating agreement and applied to the Alberta Court of Queen's Bench for a partial receivership order relating solely to the Trinidad and Tobago project, as an interim measure, on the basis that continuation of the project was imminently threatened. BGI also wanted a first charge because it did not have it under contract and the sums of money involved were

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65 2009 ABCA 127, 457 A.R. 38 [*BG International*].

66 AIPN, *Model International Operating Agreement* (Houston: AIPN, 2002) [*2002 Model Agreement*].

significant. The interim order for receivership was granted and BGI was given a priority charge that was second only to CSEI's principal banker, Canadian Western Bank.

The order effected a change of operatorship and provided significant interim relief to BGI to preserve the jointly owned property and to ensure continued drilling and testing operations. CSEI appealed the decision appointing the interim receiver and granting control of the operation to BGI.

3. DECISION

The order granting the interim receivership was upheld, despite the fact that art. 4 of the *2002 Model Agreement* contains explicit remedies for such circumstances, which allows one party to replace a defaulting party as operator in the event of default. The Court of Appeal effectively curtailed the terms of the operating agreement by finding that the order should be upheld because it was too far into the proceedings and the matter was too urgent to rely merely on the remedies provided under the *2002 Model Agreement*. Under the *Judicature Act*,[67] granting a receivership order must be considered "just and convenient."[68] The Court was clear that granting an order for interim receivership is an extraordinary remedy that should not be granted lightly and must only be granted after considering and balancing the rights, interests, and position of both parties, and that "if possible a remedy short of receivership should be used."[69] However, the Court was satisfied that "[w]hile an order short of receivership might have been crafted," the receivership order was not unreasonable in the circumstances.[70]

4. COMMENTARY

This is the first Canadian decision to consider the AIPN *2002 Model Agreement*. It demonstrates the courts' willingness to step beyond the confines of the agreement when the circumstances demand an immediate and extraordinary remedy. While it establishes precedent for the availability of extraordinary remedies for a joint interest holder dealing with a joint operator that has become insolvent, it is likely that this will remain an exceptional remedy only to be considered when the stakes are high and the threat of adverse consequences is imminent.

D. *MARATHON CANADA LTD. V. ENRON CANADA*[71]

1. BACKGROUND

When dealing with local subsidiaries of larger companies, it is often of great comfort if the parent will provide a guarantee of the subsidiary's obligations. Since, in most cases, the parent will be significantly larger than the subsidiary, this guarantee gives the receiving party some degree of satisfaction that there will be value to enforce upon in the event that the

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67 R.S.A. 2000, c. J-2.
68 *BG International*, *supra* note 65 at para. 17, citing the *Judicature Act*, *ibid.*, s. 13(2).
69 *BG International*, *ibid.*
70 *Ibid.* at para. 19.
71 2009 ABCA 31, 448 A.R. 245.

guarantee is triggered. But what happens if it is the parent guarantor of a financially healthy subsidiary that falls into chaos?

2. FACTS

Marathon Canada Ltd. (Marathon) and Enron Canada Corp. (Enron Canada) were parties to a natural gas purchase contract with Marathon as seller and Enron Canada as purchaser. Enron Corp., Enron Canada's U.S. parent company, guaranteed Enron Canada's obligations up to $10 million. The natural gas purchase contract anticipated that Enron Canada and Marathon would enter into confirmation agreements from time to time specifying the details of each transaction. Under the agreement in question, each party had a right of termination on two days' notice after a "Triggering Event," which included a "Material Adverse Change" to be determined at the sole discretion and "in the reasonable opinion of the Notifying Party."[72]

Enron Corp. ran into financial difficulties in the fall of 2001 and its credit rating dropped significantly. Marathon alleged that this amounted to a material adverse change and gave the required two days notice for termination. Enron Canada was still in relatively sound financial shape at the time. The agreement provided that the material adverse change would not be considered a triggering event if Enron Canada provided a letter of credit. Enron Canada failed to do so and instead merely denied that a triggering event had occurred.

Marathon brought this action claiming $560,000 for gas deliveries for which it had not been paid in the month prior to the termination. Enron Canada counterclaimed for $126 million for improper termination of contract and argued that the triggering event provisions in the agreement should be read in light of the standard industry practice, which Enron Canada claimed required Marathon to give Enron Canada notice requesting that Enron Canada provide a form of performance assurance and to allow Enron Canada a "reasonable time" to perform, prior to the termination right arising.[73]

3. DECISION

At trial, the judge found that Marathon had reasonably concluded that a triggering event had occurred since a material adverse change had occurred to Enron Canada's parent corporation. The trial judge found that Marathon was therefore entitled to terminate on notice and was entitled to the $560,000 for unpaid gas supplied to Enron Canada, plus interest at the rate specified under the agreement.

The Court of Appeal upheld the trial decision, finding that it was reasonable to consider Enron Corp.'s financial troubles as a triggering event, despite the fact that evidence demonstrated that Enron Canada remained a solvent party and that Marathon was at all times acting within the scope of the agreement.[74] Enron Canada also failed to establish the

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72 *Ibid.* at para. 7.
73 *Ibid.* at para. 16.
74 *Ibid.* at para. 18.

existence of an industry practice requiring Marathon to provide some sort of performance assurance and a reasonable time to perform prior to the early termination right arising.[75]

Application for leave to appeal to the Supreme Court of Canada was denied.[76]

4. COMMENTARY

The Court seems to have preferred to decide the case on the basis of a straightforward enforcement of a contract, as negotiated by two sophisticated commercial parties in equal bargaining positions. Despite the fact that Enron Canada was financially sound, and despite the possibility for the termination to allow Marathon to escape a contract under which it was bound to sell natural gas at a contract price that was lower than the market price, the parties were considered to be acting within the four corners of the contract, so the Court had no reason to interfere.

E. *HUNT OIL CO. OF CANADA V. SHELL CANADA LTD.*[77]

1. BACKGROUND

This case concerns the nature of pooling arrangements and area of mutual interest (AMI) clauses. The issue is whether, under a farmout agreement, a party's right to participate in an acquisition is triggered when one party enters into a pooling agreement in relation to land within the AMI as set out in the farmout agreement.

2. FACTS

Hunt Oil Company of Canada (Hunt) and Shell Canada Limited (Shell) entered into a farmout agreement that contained an AMI clause permitting each party to participate, on a 50/50 basis, in the other's acquisition of mutual interest lands until 1 March 2005. The farmout agreement contemplated two blocks of land, Block "A" and Block "B." Hunt earned a 50 percent interest in Block A lands. However, Hunt and Shell concluded that gas production on Block B land was not economically attractive unless it could be pooled with adjacent lands owned by Talisman Energy Inc. (Talisman). An agreement to pool was never reached within the time frame given to Hunt to drill the option well on Block B lands and therefore, in April 2003, Hunt gave Shell written notice of its election not to participate in drilling the option well on Block B lands.

In July of 2004, Shell and Talisman finally negotiated a non cross-conveyed pooling arrangement with respect to Talisman lands and the Block A lands. The Talisman lands were within the geographical area of the AMI in the farmout agreement. Hunt was never given a chance to participate in the pooling agreement. At the time of the court application, Talisman and Shell were commercially producing from the pooled lands.

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75 *Ibid.* at para. 15.
76 *Enron Canada Corp. v. Marathon Canada Ltd.*, [2009] 1 S.C.R. viii.
77 2009 ABQB 627, 312 D.L.R. (4th) 543.

Hunt made an application to the Court of Queen's Bench to determine whether or not the pooling agreement triggered Shell's AMI obligations under the farmout agreement. Hunt's position was that the definition of the AMI was broad and included "any interest," even if such interest was "only a contractual interest to share in the production from the Talisman lands."[78] Shell's position was that the word "acquisition" in the farmout agreement "did not capture the rights Shell acquired in [the] Pooling Agreement."[79]

3. DECISION

The Alberta Court of Queen's Bench found that the pooling agreement between Shell and Talisman did not trigger the AMI obligations under the farmout agreement. The Court concluded that not all "acquisitions" are acquisitions "within the meaning of the AMI clause."[80] It is stated that "[a] party's ability to enter into a pooling agreement is dependent upon its pre-existing ownership of an interest eligible for pooling."[81] Shell already owned the land with which it entered into the pooling agreement. The effect of the pooling agreement was to combine Talisman and Shell's interest so that each would obtain a half interest in the pooled lands. By combining their ownership, they enhanced the efficiency of oil and gas production.[82] In the Court's mind, this indicated that "the pooling was not so much an acquisition as a prudent exercise of ownership" and production efficiency.[83] Shell obtained its interest in the pooled lands by pooling them with Talisman. It did not "acquire" its interest from Talisman. This was not the same as the "acquisition" contemplated in the farmout agreement between Shell and Hunt.[84]

4. COMMENTARY

This decision sets out the law regarding whether a non cross-conveyed pooling agreement triggers the AMI clause in a farmout agreement involving the same lands. This case in no way shuts the door on the possibility that an AMI clause could be triggered by a pooling agreement in a different scenario since the decision was heavily dependent on the facts and relied on the specific drafting of the AMI clause and on the terms of the pooling agreement. Here, the Court found that the AMI clause was not triggered because there was no conveyance of title between the parties pursuant to the pooling agreement. The door remains open for the possibility that such an AMI clause may in fact be triggered if the related pooling agreement contains a transfer of title.

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78 *Ibid.* at para. 18.
79 *Ibid.*
80 *Ibid.* at para. 35.
81 *Ibid.* at para. 42.
82 *Ibid.* at para. 44.
83 *Ibid.*
84 *Ibid.* at para. 45.

IV. ENVIRONMENTAL

A. *MININGWATCH CANADA V. CANADA (FISHERIES AND OCEANS)*[85]

1. BACKGROUND

A federal environmental assessment pursuant to the *Canadian Environmental Assessment Act* can be conducted by way of screening, comprehensive study, mediation, or panel review.[86] The vast majority of projects subject to federal environmental assessment occur by way of screening, which is the simplest of the four methods, and only requires public consultation if the assessment authority thinks it appropriate given the circumstances.[87]

A panel review, the most intensive form of review, is generally only required when the significance of public concerns and interests requires greater public involvement by way of notice and consultation, or when the proposed project may cause significantly adverse environmental effects that the proposed mitigation measures are unlikely to adequately address.[88]

Section 15(1) of the *CEAA* provides that "[t]he scope of the project in relation to which an environmental assessment is to be conducted shall be determined by … the responsible authority."[89] On its face, this provision allows the federal authority to define the scope of a project, which would potentially allow the authority to limit the assessment requirements to examining only certain elements of the project.

Oftentimes both the federal government and a provincial government are required by law to assess the environmental impacts of the same project. *MiningWatch* is a case where the federal government limited the scope of a project that had already undergone a comprehensive provincial environmental assessment such that the project would require a less intensive environmental assessment at the federal level (a screening rather than a comprehensive study). For most provinces, there now exist Federal-Provincial/Territorial Environmental Assessment Agreements that aim to limit the amount of duplication between federal and provincial assessments by mandating that projects undergo a single assessment, administered co-operatively by both governments, but with only one level of government taking the lead.

2. FACTS

The Red Chris Development Company (Red Chris) sought to develop a copper and gold mine in northwest British Columbia. The project fell under both provincial and federal jurisdiction due to the mine's impact on fish habitat and waterways, as well as the use of explosives in open pit mining. Red Chris submitted a project description to the British Columbia Environmental Assessment Office (BCEAO) and was notified that the project

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85 2010 SCC 2, [2010] 1 S.C.R. 6 [*MiningWatch*].
86 S.C. 1992, c. 37, s. 14 [*CEAA*].
87 *Ibid.*, s. 18(3).
88 *Ibid.*, s. 20(1)(c).
89 *Ibid.*

would require an environmental assessment certificate. In 2005, the BCEAO concluded its comprehensive study, which included public consultation. The BCEAO subsequently approved the project and issued an environmental assessment certificate.

Red Chris also initiated the federal environmental process when it submitted applications to the Department of Fisheries and Oceans (DFO) for dams required to create the tailings impoundment area. Both the DFO and Natural Resources Canada declared themselves a "responsible authority" for the environmental assessment under the *CEAA*.[90] Initially, both responsible authorities decided that a comprehensive environmental assessment would be required. However, prior to proceeding with the assessment, the DFO later advised that it had scoped the project description to exclude the mine and mill and only included the aspects of the project that fell under federal jurisdiction (that is, the tailings impoundment area and the explosives storage area). As such, the federal assessment process proceeded by way of screening. The responsible authorities did not seek additional public comment; instead they relied on the British Columbia environmental assessment and the public notice and responses under it. Based on the screening, they decided in 2006 that the project was "not likely to cause significant adverse environmental effects"[91] and allowed the project to proceed.

In 2006, MiningWatch Canada (MiningWatch) filed an application for judicial review in the Federal Court alleging that the responsible authorities had breached their "duty under the CEAA to conduct a comprehensive study."[92] The Federal Court allowed the application and halted the mine until the responsible authorities could conduct a comprehensive assessment and approve the project. The Federal Court of Appeal overturned the lower Court's decision and dismissed the application for judicial review. MiningWatch appealed the decision to the Supreme Court of Canada.

3. DECISION

The Supreme Court of Canada overturned the decision of the Federal Court of Appeal. In a unanimous decision written by Rothstein J., the Court decided that, based on a plain reading of the *CEAA*, the definition of the term "project" meant the "project as proposed" and not the "project as scoped" by the responsible authority under s. 15 (as had been argued by the federal government).[93] As such, because the project description fell within the *Comprehensive Study List Regulations*,[94] a comprehensive study was mandatory and the requirements of s. 21 of the *CEAA* applied, including conducting a comprehensive study and public consultation with respect to the proposed scope of the project.[95]

It was decided that the responsible authority had no discretion to limit the scope of the project in order to choose the track on which the assessment proceeds (that is, screening or comprehensive study). Once the track has been decided based upon the project description

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90 *Supra* note 86, s. 2(1).
91 *MiningWatch*, *supra* note 85 at para. 7.
92 *Ibid.* at para. 8.
93 *Ibid.* at para. 34.
94 S.O.R./94-638.
95 *Supra* note 86.

the responsible authority only has discretion to enlarge the scope of the project from the project proposal, but does not have discretion to reduce the scope.[96]

Despite this ruling, the Court did not require that a federal comprehensive study be completed and allowed the project to proceed based on the screen that had already been done.[97]

4. COMMENTARY

The Supreme Court of Canada's declaration on the meaning of "project" in s. 2 of the *CEAA* as "project as proposed by the proponent"[98] eliminates the discretion of the responsible federal authority to define the scope of the project in a way that alters the means of assessment. The Court's further finding that tracking the environmental assessment must precede project scoping is significant in clarifying that a comprehensive study track is triggered by operation of law and cannot be varied at the discretion of federal authorities.

The decision has since, on a very short time basis, effectively been reversed by the federal government in recent federal budget legislation. The budget bill includes amendments to the *CEAA* that will allow the Minister to order reviews on a limited scope of the project rather than the entire undertaking.[99] The use of budget legislation to introduce these measures has come under criticism by opposition parties and environmental groups, especially given the non-financial nature of these measures.

B. *KELLY V. ALBERTA (ENERGY RESOURCES CONSERVATION BOARD)*[100]

1. BACKGROUND

Sour gas wells contain H_2S, a gas that is life-threatening even at very low concentrations. If the gas escapes and ignites it creates SO_2, which is also an extremely hazardous substance. The *Energy Resources Conservation Act* requires the Alberta Energy Resources Conservation Board (ERCB) to grant standing to any persons who may be "directly and adversely" affected by a Board decision.[101] The ERCB's *Directive 071: Emergency Preparedness and Response Requirements for the Petroleum Industry* requires the creation of an emergency planning zone (EPZ) around the wellsite, which is defined as "a geographical area surrounding a well, pipeline, or facility containing hazardous product that requires specific emergency response planning."[102] *Directive 071* also creates a broader protective action zone (PAZ), defined as "[a]n area downwind of a hazardous release where outdoor pollutant concentrations may result in life-threatening or serious … health effects on the public."[103]

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96 *MiningWatch*, *supra* note 85 at para. 39.
97 *Ibid.* at para. 52.
98 *Ibid.* at para. 28.
99 Bill C-9, *An Act to implement certain provisions of the budget tabled in Parliament on March 4, 2010 and other measures*, 3rd Sess., 40th Parl., 2010, cl. 2155 (assented to 12 July 2010), S.C. 2010, c. 12.
100 2009 ABCA 349, 464 A.R. 315 [*Kelly*].
101 R.S.A. 2000, c. E-10, s. 26(2) [*ERCA*].
102 ERCB, *Directive 071: Emergency Preparedness and Response Requirements for the Petroleum Industry* (Calgary: ERCB, 2008) at 12 [*Directive 071*].
103 *Ibid.* at 68.

2. FACTS

In August 2007, the ERCB granted conditional approval of two sour oil wells to Grizzly Resources Ltd. (Grizzly Resources) and West Energy Ltd. (West Energy) in an area of the Pembina Field where there was a higher than normal density of rural homes and farms. The residents of the area expressed concerns during the consultation period "related to health and safety, flaring, air quality, proliferation, emergency response planning, contamination of land and animals, and compensation."[104] The ERCB denied standing to the residents to be heard in the application process because they lived outside the EPZ as prescribed by the ERCB's regulations. However, the residents did reside within the broader PAZ. The Board concluded that the mere fact of residence within the PAZ was not enough to establish that the residents had a right that may be directly and adversely affected by the approval of the application. Furthermore, the Board found that the residents had failed to put forth any evidence of a possible adverse effect.[105]

The residents appealed the Board's decision to the Alberta Court of Appeal. West Energy subsequently withdrew its application.

3. DECISION

The Court of Appeal disagreed with the ERCB decision and interpreted the PAZ as an area in which residents could be directly and adversely affected in the event of a sour gas release, finding that the residents were entitled to participation and consultation in the application process.[106] The Court concluded that residency within the PAZ was evidence itself of a possible direct and adverse effect and, therefore, the ERCB was in error when it required further evidence.[107] Once the residents established that they lived within the PAZ, the onus shifted to Grizzly Resources to show that the residents would not be adversely affected by the escape of sour gas.[108] The ERCB's decision was vacated and the ERCB was ordered to rehear the application.

4. COMMENTARY

The decision had the effect of significantly increasing the consultation obligations of applicants for sour gas facilities to include residents in the PAZ. In response to the decision, the ERCB released Bulletin 2009-41, stating that the Court of Appeal's interpretation varied significantly from the ERCB's intention in implementing the PAZ.[109]

Bulletin 2009-41 effectively removes any possible implications of the Court of Appeal decision in this case by revising the PAZ area to now fall within the EPZ.[110] The Bulletin also

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104 *West Energy Ltd.: Applications for Well Licences — Pembina Field*, EUB Decision 2007-061 (8 August 2007) at 3.

105 *Kelly*, *supra* note 100 at para. 13.

106 *Ibid.* at para. 35.

107 *Ibid.* at para. 40.

108 *Ibid.* at para. 44.

109 ERCB, Bulletin 2009-41, "Processing of Applications for Sour Oil and Gas Development in Light of the Court of Appeal Decision in the Matter of *Kelly v. Alberta (Energy Resources Conservation Board) and Grizzly Resources Ltd.*" (13 November 2009).

110 *Ibid.* at 1.

eliminated three other areas called the emergency awareness zone and two sulphur dioxide zones since the ERCB found that the EPZ was comprehensive enough to render these additional zones redundant.[111]

V. SECURITIES

A. *IRONSIDE V. ALBERTA (SECURITIES COMMISSION)*[112]

1. BACKGROUND

The Alberta Securities Commission (ASC) Panel that first issued the decision in this matter summarized the public policy objectives underlying the disclosure requirements under the securities legislation as follows:

> Adherence by reporting issuers to mandatory disclosure requirements is essential to informed decision-making by investors and other capital market participants.
>
> The disclosure required by Alberta securities laws is designed to provide investors — whether in respect of a primary distribution of securities, trading in the secondary market or a specific corporate transaction — with the information necessary to facilitate informed investment decisions. It thereby promotes investor confidence and the integrity of the capital market.[113]

2. FACTS

In December 1998, Blue Range Resource Corporation (Blue Range) was subject to a hostile takeover by Big Bear Exploration Ltd. (Big Bear), both companies being "oil and gas exploration, development, production and marketing companies."[114] Both companies were also reporting issuers on the Alberta Stock Exchange and the Toronto Stock Exchange at the time of the takeover. In March of 1999, Blue Range's new Big Bear management obtained court protection under the *Companies' Creditors Arrangement Act*.[115] Just a few days later the Executive Director of the ASC ordered an investigation pursuant to s. 41 of the Alberta *Securities Act*[116] into trading in the securities and into the disclosures of both companies. Later in 1999, the assets of Blue Range were liquidated and Big Bear sold its Blue Range shares to Avid Oil & Gas (Avid). A panel of the ASC (the Panel) found the CEO and CFO of Blue Range guilty of knowingly allowing documents to be issued in Blue Range's name containing material misrepresentations and in violation of generally accepted accounting principles (GAAP). The Panel summarily concluded as follows:

> As is evident in our summary of findings, the public information disseminated by Blue Range during the period under examination in the Hearing and, particularly during the last half of 1998, fell short, by a wide margin, of what was required. This was not the fair, accurate and timely disclosure demanded by Alberta

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111 *Ibid.* at 3.
112 2009 ABCA 134, 454 A.R. 285 [*Ironside*].
113 *Re Ironside*, 2006 ABASC 1930 at paras. 1527-28.
114 *Ironside*, *supra* note 112 at para. 1.
115 R.S.C. 1985, c. C-36 [*CCAA*].
116 R.S.A. 2000, c. S-4.

> securities laws and to which capital market participants were entitled. We saw examples of material information not being disclosed when required, or at all, and examples of disclosure presented in such a way (including omissions of material information) as to be misleading. The result, individually and cumulatively, was that the public was misled as to the true picture of Blue Range's operations and financial position during 1998.[117]

The Panel found that three of the six leases at issue were improperly treated as operating leases rather than capital leases and that this affected the financial statements in violation of GAAP.[118] The officers were found to be directly responsible for failure to meet the disclosure requirements and for withholding relevant information from the auditor.[119] The officers also violated the *Securities Act* by misrepresenting production and reserve numbers in certain materials and by not making known certain spot purchases.[120]

This appeal to the Alberta Court of Appeal was brought on procedural grounds, with respect to alleged unfairness and bias of the panel in the proceedings, alleged improper practices in investigation, and the allegation that "the fall of Blue Range was due to the actions of Big Bear's principals."[121]

3. DECISION

The Court of Appeal, applying primarily a reasonableness standard of review, dismissed the officers' appeal, finding that no unfair procedure was used at trial. The Court found that the officers clearly misrepresented information to the auditors. Investigation of the conduct of the officers was considered by the Court to be proper despite the lack of charges of malfeasance. The Court determined that the expert evidence was properly evaluated, and that the reporting methods used by the defendants were improper. The CEO was prohibited "from becoming or acting as a director or officer of an issuer for life" pursuant to s. 198 of the *Securities Act*, and was subject to a penalty of $180,000 under s. 199 and costs of $675,000 under s. 202.[122] The CFO was prohibited from "acting as a director or officer of an issuer for 10 years" under s. 198, and was subject to a penalty of $50,000 under s. 199 and costs of $175,000 under s. 202.[123]

4. COMMENTARY

This decision provides insight into the circumstances in which the ASC and Alberta courts are willing to pierce the corporate veil for the purposes of protecting the public interest. The Court found that the officers were clearly personally responsible for violations of GAAP and of requirements under the *Act*, and investors acted to their own detriment in reliance on the misrepresentations made through those violations.

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117 *Re Ironside*, *supra* note 113 at para. 1529.
118 *Ibid.* at para. 1469.
119 *Ibid.* at paras. 544-45.
120 *Ibid.* at para. 1475.
121 *Ironside*, *supra* note 112 at para. 5.
122 *Ibid.* at para. 121.
123 *Ibid.*

B. *UBS SECURITIES CANADA V. SANDS BROTHERS CANADA, LTD.*[124]

1. BACKGROUND

While this case addresses basic contract formation principles in the context of a purchase and sale of securities of a private company by sophisticated players in the securities industry, it contains important considerations for parties negotiating commercial agreements in terms of understanding when and how an agreement can actually be reached, notwithstanding the absence of an agreement in writing, as may be customary.

2. FACTS

In 2000, UBS Securities Canada, Inc. (UBS) acquired shares of the Bourse de Montréal Inc. (Bourse), a private Quebec company that administered the Montreal Stock Exchange. In 2005, UBS, wanting to increase its holdings of Bourse shares, charged its portfolio manager Asheef Lalani with the task of acquiring additional shares.

Lalani learned that Sands Brothers Canada, Ltd. (Sands Canada) owned 100,000 Bourse shares. After being advised that the shares were not for sale in October of 2005, Lalani contacted Steven Sands, director, officer, and principal of Sands Canada on 14 November 2006. During their conversation, Sands confirmed that he had the authority to sell the Bourse shares, "indicated that he might be interested in so doing," and asked Lalani to document UBS' bid in an email, which Lalani did later that day.[125]

Between 14 November and 30 November 2006, Lalani and Sands proceeded to negotiate the sale of the Bourse shares by way of emails and telephone conversations, some lasting as little as 48 seconds. The parties agreed that the sale of Bourse shares to UBS would close on 3 January 2007 at a price of $50 per share.

On 1 December 2006, Bourse announced that it expected to list its shares in March or April of 2007. Both UBS and Sands Canada were sent the press release. Counsel for UBS sent counsel for Sands Canada a follow-up email seeking comments on the draft agreement on 4 December 2006 and was advised that Sands Canada's comments would be provided on 12 December 2006.

On 7 December 2006, Sands contacted Lalani complaining that he had not heard from him following the announcement of the listing. The parties disagreed about whether they had a binding agreement for the sale of the Bourse shares. Sands asserted that "no concluded agreement had been reached"[126] because the actual written share purchase agreement had not been finalized and because Bourse's corporate bylaws required that there be written approval for the sale of its shares. On 11 December 2006, Lalani was advised that Sands Canada would not deliver the Bourse shares.

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124 2009 ONCA 328, 95 O.R. (3d) 93 [*UBS*].
125 *Ibid.* at para. 13.
126 *Ibid.* at para. 38.

UBS commenced legal proceedings against Sands Canada seeking a declaration that a valid agreement existed and specific performance of the agreement. It argued that the essential terms of the agreement had been agreed upon and that, on many occasions, UBS had received confirmation that an agreement had been reached. The trial judge found that "an oral agreement was made between the parties" and ordered specific performance.[127] Sands Canada appealed the decision.

3. DECISION

The Ontario Court of Appeal began by reviewing the two essential elements of contract formation: (1) a meeting of the minds and (2) certainty of essential terms,[128] and then upheld the trial decision on the basis that the parties were sophisticated[129] and that it is customary in the industry to execute trades by verbal agreement.[130] The Court also upheld the trial judge's finding that the parties had reached an agreement on all of the essential terms regarding the sale of the Bourse shares, notwithstanding the absence of a written share purchase agreement and that the written approval mandated by the Bourse bylaws was not a condition precedent to the sale.[131]

4. COMMENTARY

This case is interesting because much of the decision turned on industry practice. In the securities industry, it is customary for the sale of shares of publicly traded companies between sophisticated players to be concluded over the telephone, email, or other electronic communications. On the other hand, the sale of shares of a private company will typically involve a written share purchase agreement setting out the terms of the transaction.

Here, notwithstanding the fact that Bourse was a private company when the negotiation of the purchase and sale of its shares began, a binding verbal agreement was still found to exist, despite the absence of a written agreement, because all of the essential elements of the agreement were in place. The Court here provides a not-so-gentle reminder that the fundamental principles of contract formation should always be a consideration for parties negotiating a contract through the various means of communication existing today, and indicates that our reliance on electronic communications is becoming legally binding.

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127 *Ibid.* at para. 43.
128 *Ibid.* at paras. 47-49.
129 *Ibid.* at para. 73.
130 *Ibid.* at para. 78.
131 *Ibid.* at para. 94.

VI. TAXATION

A. *IMPERIAL OIL RESOURCES LTD. V. CANADA (A.G.)*[132]

1. BACKGROUND

In 1975, amendments to the *Income Tax Act*[133] required a resources producer to include any resource royalty payable to a province in its computation of taxable income. As a counterbalance, resource producers became entitled to a federal statutory resource allowance abatement. Around the same time, development of the Alberta oil sands began and oil companies entered contractual royalty agreements with the province whereby oil companies were required to enter into joint ventures with the province, and the province would receive 50 percent of the deemed net profit. In 1976, the *Syncrude Remission Order*[134] was enacted to ensure that the recent amendments to the *Income Tax Act* would not apply to royalties received by Alberta in conjunction with oil sands production. In 1997, Alberta amended its royalty agreement (Amendment No. 6) with oil companies to expand the oil sands project to include additional leases. In order to encourage investment in the development of these new leases, Alberta agreed that its share of oil sands royalties would be reduced by credits for capital costs incurred in respect of the new development. While the agreement was amended in 1997, the new leases did not come into production until 2000.

2. FACTS

Imperial Oil Resources Ltd. and Imperial Oil Resources Ventures Limited (collectively, Imperial) disagreed with the Crown on the manner in which the *Remission Order* should be taken into account in determining Imperial's tax obligations under the *Income Tax Act* for the 1997 taxation year. In computing the amount of income tax to be remitted under the *Remission Order* for 1997, the Crown reduced the royalty receivable to take into account the capital credits, and therefore the amount of remission was reduced accordingly. Imperial believed that this resulted in it "not receiving the full amount of remission and interest to which they were entitled."[135] Imperial's position was that the amount of income inclusion should have been determined as the amount of royalties that would have been receivable by Alberta if the royalty agreement had not permitted a deduction for the capital credits. At trial, Imperial was granted judgment for the underpayment of remission plus interest. The Crown appealed the judgment and Imperial cross-appealed on a question relating to interest on the remitted tax.

3. DECISION

The issue was the correct interpretation of the *Remission Order*. The Federal Court of Appeal found that the Crown had correctly determined the amount of remission for 1997. The royalty payable to Alberta was the royalty payable under the Alberta agreement as

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132 2009 FCA 325, 396 N.R. 115 [*Imperial*].
133 R.S.C. 1985, c. 1 (5th Supp.).
134 C.R.C., c. 794 [*Remission Order*].
135 *Imperial*, *supra* note 132 at para. 24.

altered by Amendment No. 6.[136] The Court also found that Imperial had not made out its entitlement to refund interest for 1997.[137] The Court found that the trial judgment was based on the flawed premise that, following amendment to Alberta's royalty agreement with the oil companies, the remission was to be determined on the basis of allocation of the resulting royalty under the new lease. Such a premise went against the "essential nature of a royalty."[138] The amendment resulted in reduced royalties payable to Alberta in respect of all production. There was no basis for differentiating between the production from old leases or new leases.[139]

4. COMMENTARY

This decision turned heavily on the basic structure of a royalty, with the Court pointing out that the principle underlying the calculation of royalties is that the royalty is fully dependant on there being production. Although it is sometimes difficult to calculate taxes owing where there are numerous credits and amendments, the calculation of a royalty is always a result based on actual, rather than hypothetical data.

VII. JOINT OPERATORS

A. *DIAZ RESOURCES LTD. V. PENN WEST PETROLEUM LTD.*[140]

1. BACKGROUND

Clause 203 of the 1990 CAPL Operating Procedure[141] sets out the way in which a joint operator may challenge the operator. Upon receiving a challenge notice, an operator must do one of two things within 60 days of the date of the notice: advise the joint operators that "it is prepared to operate on the terms and conditions set out in the challenge notice" or advise the joint operators that it will resign as operator within 90 days.[142] Failure by the operator to advise of its election within the 60-day period shall be deemed to be an election to resign. Clause 203 requires that the challenge notice contain sufficient detail to enable the receiving parties to evaluate the nature of the challenge notice and to measure the effect that the revised terms and conditions would have on joint operations.

2. FACTS

Diaz Resources Ltd. (Diaz) issued a challenge notice to Penn West Petroleum Ltd. (Penn West) under cl. 203 of the 1990 Procedure in relation to three agreements in which both parties held a 50 percent working interest in certain oil and gas interests. Under the challenge notice, Diaz indicated that it wished to replace Penn West as the operator under the agreements and that it was "ready, able, and willing to operate the interests on terms and

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136 *Ibid.* at para. 37.
137 *Ibid.* at para. 40.
138 *Ibid.* at paras. 34-35.
139 *Ibid.* at para. 36.
140 2010 ABQB 153 [*Diaz*].
141 CAPL, *1990 CAPL Operating Procedure* (Calgary: CAPL, 1990) [1990 Procedure].
142 *Ibid.*

conditions" that were more favourable to the joint account than Penn West's operations.[143] Specifically, the notice stipulated that Diaz would not charge the joint account for any costs attributable to a production office, a field office, or for first level supervisors in the field.

Penn West responded to the notice within 60 days and stated that it was deficient because it did not provide sufficient information to properly evaluate whether or not the modified terms were in fact more favourable to the joint account. Penn West also had concerns regarding whether Diaz would be able to conduct operations in a safe, good, and workmanlike manner, and Penn West was of the view that Diaz might be in default under the agreement given the quantum of current unresolved receivables owed by Diaz to Penn West.[144] Diaz commenced an application seeking a declaration that, since Penn West had failed to elect one of the options prescribed by the 1990 Procedure, it was entitled to replace Penn West as operator under the three agreements. In its affidavit filed in these proceedings and in its answers to undertakings, Diaz did ultimately provide a proper analysis of the costs savings.

3. DECISION

The Court of Queen's Bench dismissed Diaz's application. The Court was satisfied that the challenge notices did not "contain sufficient information to allow Penn West to make an informed decision on whether the proposed changes would result in more favourable terms and conditions in the operation of the properties."[145] Diaz stated that Penn West would be in the position to know how much the savings would be because they knew what they charged for the modified expenses. The Court found that it was insufficient for Diaz to tell Penn West that they could "figure out the impact themselves by reviewing the joint accounts."[146] It was not up to Penn West to figure out exactly what costs Diaz intended to eliminate. Had the challenge notice contained the information set out in the affidavit evidence and in the answer to undertakings, Penn West would have had enough information to evaluate the challenge notices.[147]

4. COMMENTARY

This case provides some guidance as to the quality of information that a joint operator must provide in order to support a challenge notice. The joint operator must provide the best and most informative information that it can to an operator so that an operator can properly evaluate whether or not it can operate under the modified conditions. If a joint operator can later adduce evidence by way of affidavit to support an application for a declaration of operatorship, then it likely could have just as easily provided this information in its challenge notice.

While the ability of Diaz to conduct operations in a safe, good, and workmanlike manner was questioned by Penn West, the Court did not address whether a challenger also has the

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143 *Diaz*, *supra* note 140 at para. 2.
144 *Ibid.* at para. 7.
145 *Ibid.* at para. 14.
146 *Ibid.*
147 *Ibid.*

burden of establishing its ability to be a competent operator who operates in a safe, good, and workmanlike manner in the challenge notice. However, it is important to note that whether or not it must be addressed in the challenge notice, it is a standard that every operator is expected to meet under cl. 304 of the 1990 Procedure, so an operator must be prepared to be held to that standard.

B. *BROOKFIELD BRIDGE LENDING FUND V. KARL OIL AND GAS LTD.*[148]

1. BACKGROUND

Clause 507 of the 1990 Procedure specifically allows for the commingling of funds by the operator. The 1990 Procedure is an improvement over its 1981 predecessor since the language with respect to joint funds is clarified to stipulate that the moneys of the joint operators — whether paid in for operations or received as proceeds from the sale of production — are specifically deemed to be trust funds.[149] The commingling of funds by the operator is a necessary and commonplace practice in the industry, and the operating procedures have been drafted with that in mind. Although the procedures do have some remedies available to the joint operators, moreso in the most recent 2007 version, it is still difficult to avoid losses when the operator becomes insolvent.

2. FACTS

The operator failed to pay production revenues out of the joint account to the joint operators in an amount agreed to be over $300,000. It was clear from the records produced that significant deposits were regularly made into this account around the twenty-fifth of every month, which would be typical in the industry of monthly revenue payments. Rather than distributing these funds to the joint operators, the operator paid other expenses and payments without distributing the trust fund revenues as required by the 1990 Procedure. When the receiver was appointed to take over the operator's affairs, there was only about $58,000 in the joint account.

The receiver then sold the assets of the operator and the contest arose between the secured lender and the non-operators, who claimed that the unpaid revenues were the subject of a trust. The trial judge imposed a constructive trust over all of the assets based on reasoning which included that the operator had breached its fiduciary duty and that the secured creditor was in a better position to ensure that the operator would not commit a breach of the operating agreement.[150] The secured creditor appealed that decision.

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148 2009 ABCA 99, 454 A.R. 162 [*Brookfield Bridge*].

149 Including the phrase "shall in no way be deemed to be funds belonging to the Operator": 1990 Procedure, *supra* note 141, cl. 507.

150 *Brookfield Bridge Lending Fund v. Vanquish Oil & Gas*, 2008 ABQB 444, 96 Alta. L.R. (4th) 329 at para. 53.

3. DECISION

The Court of Appeal agreed that there was a clear breach of fiduciary duty and breach of trust, and also agreed that had the funds been still in the bank, there would be no issue.[151] However, the Court did not agree that the test for a constructive trust was satisfied. One condition of a constructive trust is that the trust funds must be traced to specific assets. Having no evidence as to which specific assets may have been purchased with the trust funds, the Court found that the test was not met in the circumstances and that the lower court had made an error in its finding of fact.[152] More specificity in the tracking of the funds in and out of the account was necessary.

The Court also stated that the risk of misappropriation was created by the non-operator allowing the commingling of the trust funds and restated in its conclusion that the facts demonstrated the shortcomings of an industry-wide practice of commingling trust funds with non-trust funds, while purporting to limit the operator's ability to use those funds only for specific purposes.[153] It was, in the Court's opinion, the non-operators who had created the risk of these circumstances.

The dissenting justice stated that rigorous adherence to a mechanistic tracing rule does not provide an appropriate, just, or equitable remedy for the breach of fiduciary duty and breach of trust that damaged the non-operator.[154] He relied on the lower court's findings of fact and stated that those findings of fact were well-informed and reasonable and should not be impugned.[155] In his opinion, the majority ignored the constructive trust as an equitable remedy for unjust enrichment, and the true function of the constructive trust should be, as stated in *Soulos v. Korkontzilas*,[156] to "condemn wrongful acts and maintain the integrity of [important trust] relationships."[157]

4. COMMENTARY

While the trial decision had provided a powerful tool for protecting the joint operators where an operator is in financial trouble, the appellate decision has taken away that tool. Leave to appeal to the Supreme Court has been denied,[158] so it is now unlikely that joint operators will be able to rely on a constructive trust as a remedy against a non-paying operator. However, the 1990 Procedure does provide remedies for the vigilant joint operator. Here, the joint operators were distracted by their own dispute as to the ownership of the working interests, so it would seem that vigilance in the face of late payment and use of the remedies in the 1990 Procedure remain the joint operator's best defence.

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151 *Brookfield Bridge*, *supra* note 148 at para. 18.
152 *Ibid.* at para. 19.
153 *Ibid.* at para. 25.
154 *Ibid.* at paras. 36-37.
155 *Ibid.* at para. 45.
156 [1997] 2 S.C.R. 217.
157 *Brookfield Bridge*, *supra* note 148 at para. 30.
158 *Karl Oil and Gas Ltd. v. Brookfield Bridge Lending Fund*, [2009] 3 S.C.R. viii.

VIII. BANKRUPTCY, *COMPANIES' CREDITORS ARRANGEMENT ACT* PROCEEDINGS

A. *RE SEMCANADA CRUDE COMPANY*[159]

1. BACKGROUND

SemCAMS ULC (SemCAMS), CEG Energy Options Inc., and SemCanada Crude Company are all affiliated companies that are owned, directly or indirectly, by a U.S. parent, SemGroup LP. The group operated four natural gas processing plants and natural gas gathering systems and pipelines in Alberta. SemGroup LP declared bankruptcy in the U.S. after $3.2 billion U.S. in oil trading losses. In Canada, SemCAMS sought and received court protection from its creditors in July 2008 under the *CCAA* and the *Bankruptcy and Insolvency Act*.[160] The timing of the filing was such that SemCAMS had been paid for the production it marketed for the months of June and July but, by seeking court protection, it was not required to pay the producers for the product those producers supplied. SemCAMS had approximately $350 million in its possession at the time of the court ordered protection. Various producers and suppliers commenced court actions in order to recover the funds owed to them.

2. FACTS

Auriga Energy Inc. (Auriga) and Celtic Exploration Ltd. (Celtic) were producers of natural gas. As producers, both companies were able to either deliver gas to a natural gas plant for processing without an inlet sale, thereby remaining the owner of the gas through the processing and then arranging a sale of the processed products after, or to sell their gas to the owner of the plant before processing pursuant to a gas purchase agreement. The purchase option generally "gives producers the benefit of a better price for their gas and a higher priority in processing."[161] Auriga and Celtic both entered into a gas purchase agreement with SemCAMS. After SemCAMS entered into bankruptcy and *CCAA* protection, Celtic and Auriga applied to the court for a declaration that "the proceeds of sales from products derived from raw gas produced at … their wells and delivered to SemCAMS … pursuant to inlet gas purchase agreements" were "held in trust by SemCAMS for the Producers."[162] In essence, Celtic and Auriga wanted a declaration that they did not in fact sell their gas to SemCAMS. While Celtic and Auriga signed the purchase agreements, it was their position that those purchase agreements "were merely a method for SemCAMS to avoid the sharing of capital fees with other co-owners of the plant," and that the parties had entered into subsequent discussions and their conduct in these discussions indicated that they "were really in an agency relationship."[163] This agency relationship gave rise to a trust relationship and fiduciary duties between the plaintiffs and SemCAMS.

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159 2009 ABQB 398, 55 C.B.R. (5th) 284 [*SemCanada*].
160 R.S.C. 1985, c. B-3 [*BIA*].
161 *SemCanada*, *supra* note 159 at para. 4.
162 *Ibid.* at para. 1.
163 *Ibid.* at para. 5.

3. DECISION

The Court of Queen's Bench dismissed Celtic and Auriga's applications. The purchase agreements did not "contain any indication of an intention to create an agency agreement or a trust, and the evidence of conduct put forward by [Celtic and Auriga] to show such an intention [was] weak, ambiguous and often denied or contradicted by SemCAMS."[164] There was no evidence to support Auriga's statements that they negotiated directly with ultimate purchasers or that SemCAMS was selling the gas products on behalf of Auriga or Celtic.[165]

The Court found that Celtic and Auriga had "failed to establish a pattern of conduct or communication that would signal or justify the imposition of a trust or the characterization of the relationship between [Auriga, Celtic, and SemCAMS] as an agency."[166]

Auriga also submitted that they had validly terminated the purchase agreement with an effective date of 1 July 2008.[167] However, the Court found that the evidentiary burden was on Auriga to establish termination, and they failed to do so. The evidence adduced by Auriga was in large part hearsay, or conflicted with evidence adduced by SemCAMS.[168]

4. COMMENTARY

Generally speaking, it should be difficult to meet the requirements of an imposed trust or an agency relationship in the absence of clear intention, and the Court confirms those principles here. While there are some relationships that are deemed to be worthy of the protection of a trust, sophisticated parties entering into commercial agreements will continue to have a very difficult time establishing that such a relationship exists.

B. *TRILOGY ENERGY LP V. SEMCAMS ULC*[169]

1. BACKGROUND

This *CCAA* proceeding considered a claim for set-off by Trilogy Energy LP (Trilogy) against SemCAMS. The issue before the Court was whether Trilogy had a right based on contractual, legal, or equitable set-off. Contractual set-off requires that an express or implied agreement between the parties exists in the contract that purports to provide for a right of set-off. Legal set-off requires the existence of liquidated debts related to mutual cross-obligations between parties (that is, same parties involving the same right). Equitable set-off requires that parties meet the following requirements:

1. The party relying on a set-off must show some equitable ground for being protected against [its] adversary's demands.

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164 *Ibid.* at para. 7.
165 *Ibid.* at para. 8.
166 *Ibid.* at para. 9.
167 *Ibid.* at para. 10.
168 *Ibid.* at para. 12.
169 2009 ABCA 275, 460 A.R. 269 [*Trilogy Energy*].

2. The equitable ground must go to the very root of the plaintiff's claim…

3. A cross-claim must be so clearly connected with the demand of the plaintiff that it would be manifestly unjust to allow the plaintiff to enforce payment without taking into consideration the cross-claim.

4. The plaintiff's claim and the cross-claim need not arise out of the same contract.

5. Unliquidated claims are on the same footing as liquidated claims.[170]

2. FACTS

SemCAMS was the operator of four natural gas plants and gathering systems in Alberta. Trilogy is an oil and gas producer that used SemCAMS facilities to process its gas. Trilogy was indebted to SemCAMS for its services as operator in the amount of $5.3 million plus interest. However, as part of a separate inlet purchase agreement, Trilogy had sold raw natural gas to SemCAMS that SemCAMS then processed and sold on its own behalf. SemCAMS still owed Trilogy $4.1 million in respect of that sale of raw gas. Following SemCAMS' *CCAA* protection, Trilogy sought to set-off the amounts owing to SemCAMS under the gas processing agreements against the money SemCAMS owed to Trilogy under the inlet purchase agreement.

At trial, the Court of Queen's Bench found that none of the agreements Trilogy had with SemCAMS provided it with any right of set-off. Trilogy was not entitled to contractual set-off because while the inlet purchase agreement expressly provided for netting of payments between Trilogy and SemCAMS under other agreements, the Court found that the provision did not extend to other agreement where SemCAMS was contracting in its capacity as operator, as opposed to its own corporate capacity as a purchaser under the inlet purchase agreement.[171] Trilogy was also not entitled to legal set-off based on the distinction between SemCAMS as operator and SemCAMS in its own right. The Court found that this resulted in debts at issue between different parties involving different rights.[172] Finally, the Court found that Trilogy was not entitled to equitable set-off as there was no close connection between the claims. The only connection between the claims was that the agreements at issue related to gathering and processing natural gas and had a common operator.[173] Trilogy applied for leave to appeal the decision.

3. DECISION

The Court of Appeal dismissed Trilogy's appeal as they found no discernible error in the judge's reasoning that Trilogy was not entitled to set-off.[174]

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170 *Coba Industries Ltd. v. Millie's Holdings (Canada) Ltd.* (1985), 20 D.L.R. (4th) 689 at 696-97 (B.C.C.A.), cited in *Holt v. Telford*, [1987] 2 S.C.R. 193 at para. 34 [citations omitted].

171 *Re SemCanada Crude Company*, 2009 ABQB 397, [2009] A.J. No. 895 at paras. 26-27 (QL).

172 *Ibid.* at para. 30.

173 *Ibid.* at para. 44.

174 *Trilogy Energy*, *supra* note 169 at para. 26.

4. COMMENTARY

This decision sets out the important distinction that the courts make in set-off cases between the different roles that parties may play in different agreements. The fact that it is the same parties contracting to do business with each other in multiple agreements may not give rise to any right of set-off if the parties are acting in different capacities under the agreements. In this decision, SemCAMS acted as the operator in one agreement (thereby acting on its own behalf as well as on behalf of the joint owners) but in its own corporate capacity as a purchaser in others. In the eyes of the trial court, this distinction was great enough to deny Trilogy the right of set-off in this case, and the appellate court found no reason to disagree.

C. *RE SAN JUAN RESOURCES*[175]

1. BACKGROUND

The *BIA* does not specify the process for the hearing of appeals from a trustee's disallowance of proofs of claim filed pursuant to s. 135(4) the *Act*, and is silent on the issue of whether such an appeal is an appeal *de novo* or an appeal on the record.[176] As the case law on the issue is not entirely consistent, further judicial guidance would be useful in clarifying the process and providing some insight into the circumstances in which a hearing *de novo* will be warranted.

2. FACTS

San Juan Resources Inc. (San Juan), a small one-person corporation, owned a 75 percent working interest in two oil and gas wells. The remaining 25 percent was owned by a significant creditor of San Juan, Hampstead Trust Corporation (Hampstead). San Juan repeatedly failed to account to Hampstead for the revenue attributable to its 25 percent share, in spite of court orders and subsequent contempt proceedings.

Two days prior to a hearing scheduled to hear Hampstead's application to have a receiver appointed over San Juan's assets, along with an outstanding contempt application, San Juan filed a notice of intention to make a proposal under the *BIA*, resulting in an automatic stay of Hampstead's application.

Hampstead filed three proofs of claim with the trustee in the proposal, all of which were substantially disallowed on various grounds as set out in its notice of disallowance. A number of Hampstead's claims were subject to conflicting opinions of oil and gas experts and the trustee had preferred the opinion of San Juan's experts. Moreover, the trustee also rejected portions of Hampstead's claims on the basis that Hampstead had provided no documentation to support the calculation of the claim. In this regard, however, San Juan had withheld relevant information from Hampstead despite court orders to provide monthly reports.

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[175] 2009 ABQB 55, 467 A.R. 391 [*San Juan*].
[176] *Ibid.* at para. 4.

Hampstead sought to appeal the disallowance, and the issue before the Court was whether the appeal should be an appeal *de novo* or an appeal on the record.

3. DECISION

Master Prowse, acting as the Registrar in Bankruptcy, ordered a *de novo* hearing on the basis that it would be "difficult to see how a meaningful appeal could be held regarding [the trustee's] determination of [the] issues" without a *de novo* hearing, which would allow the disagreeing experts to be cross-examined before the courts and enable Hampstead to access documents in the possession of San Juan and the trustee in order to establish its claim.[177]

4. COMMENTARY

Co-ownership is a legal relationship that is typical in the oil and gas industry. The facts in this case are illustrative of the inherent risks of co-ownership and the vulnerability of a joint owner who faces a potentially dishonest operator in possession of all revenue. The Court recognized that a *de novo* hearing was necessary for Hampstead to establish its claims and make its case. We are reminded however, that, as common as a co-ownership structure may be in the industry, this decision is demonstrative of the necessity for co-owners of joint property to protect themselves to the greatest extent possible — even with the existence of an operating agreement.

IX. FREEHOLD LEASES

A. *MONTREAL TRUST CO. V. WILLISTON WILDCATTERS CORP.*[178]

1. BACKGROUND

There is a growing body of case law addressing the issues of lease validity and damages on production of a dead lease. The issue of damages, however, is typically addressed in the context of continued production that is considered to be of a tortious nature, as was the case in *Freyberg v. Fletcher Challenge Oil and Gas*.[179] In *Montreal Trust*, a series of earlier proceedings and successive judgments dealt with lease validity and the assessment of damages for production on a dead lease when the operator's activities are continued under circumstances in which the court has found that leave and licence for continued production existed. The parties appeared for a third time before the Saskatchewan Court of Appeal to clarify the issue of damages entitlements pursuant to the consent order that was granted after trial.

2. FACTS

Montreal Trust Co. (Montreal Trust) was the trustee of the mineral title to the subject well (11-8) for several beneficial owners. The mineral rights "were subject to a petroleum and

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177 *Ibid.* at para. 28.
178 2009 SKCA 85, [2009] 10 W.W.R. 458 [*Montreal Trust*].
179 2007 ABQB 353, 428 A.R. 102 [*Freyberg*].

natural gas lease which provided for the payment of a 12.5 % royalty."[180] In 1955, the lessee drilled a successful well (12-8) and continued the lease by "production" pursuant to its terms. T.D.L. Petroleums Inc. (T.D.L.) obtained a leasehold interest in the 12-8 well. However, production from the 12-8 well eventually ceased in 1990.[181]

In March of 1991, T.D.L., "believing the lease was still in effect, entered into a farmout agreement with Williston Wildcatters Corporation" (Williston), and covenanted that the lease was valid.[182] As a result, Williston undertook to drill an offset well and pay T.D.L. an overriding royalty, if successful, in exchange for an interest in the lease. Under "the mistaken belief that they had the legal right to do so," Williston drilled the 11-8 well in May of 1991.[183]

Notwithstanding that Montreal Trust questioned the validity of the lease on the basis that T.D.L. "had not worked to continue production on the 12-8 well," it continued to grant Long Riders (Williston's successor) "the right to operate the 11-8 well and to produce and sell the production as and from March 11 1992."[184] Production from 11-8 continued until June of 2003 when it was shut-in at the request of Montreal Trust. Montreal Trust then commenced proceedings seeking "a declaration that the lease was terminated by reason of non-production."[185]

The first trial addressed the validity of the lease and whether T.D.L. had breached the farmout agreement. The trial judge found that the lease had terminated according to its terms on 3 January 1990 when production had stopped and, as the lease was not valid, T.D.L. had breached the farmout agreement.[186]

Montreal Trust subsequently brought an application to preserve the proceeds of the lease. A consent order was eventually agreed to wherein Long Riders would continue production from 11-8 and pay a 12.5 percent royalty to Montreal Trust and the proceeds of production realized after 6 September 2001 into court "less any reasonable costs of production."[187]

The parties appeared before the Saskatchewan Court of Appeal on the issue of damages payable as a result of the termination of the lease. The Court found that when a lessee continued to produce upon the expiration of a lease, it is initially a tortfeasor. For the period from January 1990 to March 1992 (the trespass period), it assessed damages at an amount that was "based on the fact that Montreal Trust was leasing minerals in the general area at that time" for a royalty of 18 percent plus a signing bonus.[188] The Court explicitly rejected the lessor's proposition that damages be based on the proceeds of production minus the lessee's costs of production.

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180 *Montreal Trust*, *supra* note 178 at para. 6.
181 *Ibid.*
182 *Ibid.* at para. 7.
183 *Ibid.*
184 *Ibid.* at para. 8.
185 *Ibid.* at para. 9.
186 *Ibid.* at para. 10.
187 *Ibid.* at para. 11.
188 *Ibid.* at para. 14.

From March 1992 to November 2001, the Court found that "Montreal Trust had granted Long Riders the express leave and license to remain on the land, to continue to produce and sell oil from the 11-8 well and to pay [it] a 12.5 % royalty."[189] Damages for this period were assessed on the basis of the assumed terms of the licence. Moreover, the Court found that the licence was never revoked and had remained in effect until it was replaced by the consent order of the parties in November of 2001.[190] The consent order provided that production monies (less a 12.5 percent royalty and reasonable costs of production) should be paid into trust pending the outcome of the appeal.

Following the Court's judgment on the issue of damages, the parties ultimately ended up before it again on the issue of the monies paid into trust pursuant to the consent order granted after trial. The two issues to be determined were: (1) the gross overriding royalty (GOR) payable pursuant to the farmout agreement and (2) the respective entitlements of the lessor and the lessee/operator based on the terms of the consent order.

3. DECISION

In relation to the GOR, T.D.L. claimed a share of the proceeds paid into trust on the basis that Long Riders had initially claimed its working interest by virtue of a farmout of the lease rights in return for a GOR payable to T.D.L. The Court concluded that the GOR had died with the death of the original lease. Therefore, as there was no GOR payable under the terms of the leave and licence or while production continued pursuant to the consent order, T.D.L. was entitled to retain monies actually paid to it under mistake but not to any of the monies paid into trust.[191]

With respect to entitlements under the consent order, the trial judge had found that the lessor would be entitled to production revenues minus operating costs. The Court overturned the trial judge's decision and held that for the period during which the consent order applied, the lessor was only entitled to its 12.5 percent royalty, with the balance to be paid to Long Riders.[192]

4. COMMENTARY

This case and its earlier proceedings laid the groundwork for assessing damages where an operator continues to produce on a dead lease in Saskatchewan. Of particular interest is the ruling on the farmor's royalty. While a logical conclusion, it does raise the issue as to how much attention a party should pay to the continuing validity of a lease on which it retains only a royalty interest. There may be some comfort offered to producers in this decision by the Court's reluctance to award production to the lessor (less the costs of production) after the lease has died, ruling instead that the continuing production under the leave and licence should be according to the terms of the original lease. However, had the consent order stated that the operator was acting as a contract operator, or perhaps set out the details of the

189 *Ibid.* at para. 18.
190 *Ibid.*
191 *Ibid.* at paras. 54-55.
192 *Ibid.* at para. 58.

consent arrangement which were substantially different from the original lease terms, this comfort would certainly be diminished.

B. *CANPAR HOLDINGS LTD. V. PETROBANK ENERGY AND RESOURCES LTD.*[193]

1. BACKGROUND

There is a growing body of case law that deals with the remedies available to the owners of oil and gas rights when a lessee continues production from their land after the expiry or termination of the governing lease. This case clarifies the remedies and damages that may be awarded to owners of freehold oil and gas rights for production on a dead oil and gas lease.

2. FACTS

The plaintiff Canpar Holdings Ltd. (Canpar) and Canadian Natural Resources Ltd. (CNRL) entered into the original petroleum and natural gas lease, as lessors, with Monolith Oil Corp. (Monolith), as lessee, on 4 April 2000. CNRL subsequently assigned its interest to Petrovera Resources and Monolith subsequently assigned its interest to the defendant Petrobank Energy and Resources Ltd. (Petrobank).

The lease, prepared by an Alberta land negotiator for Canpar and the related companies, contained a royalty clause providing that

> the lessor reserves to itself and the lessee shall pay or cause to be paid to the lessor a royalty in cash of 17 1/2 percent of the greater of the actual price received, including payments received from any source whatsoever in respect thereof, or the current market value at the time and place of sale of all these substances produced from the lands, all without any deductions, provided that the lessor shall only bear its proportionate share of actual costs of transportation beyond the point of measurement to the point of delivery of crude oil.[194]

Approximately one year after Petrobank took over Monolith's interest, Canpar identified several deficiencies in relation to the two wells covered by the lease. While some of the deficiencies were resolved to Canpar's satisfaction, two issues remained outstanding between the parties and Canpar issued Petrobank a default notice for each well. Taking the position that the default remained uncured, Canpar brought an action seeking a declaration that the lease had terminated and an order for possession, as well as damages and an accounting for production from the lands.

3. DECISION

The two issues to be determined by the Alberta Court of Queen's Bench were: (1) the pricing of natural gas produced by the lessee (and thereby the amount of royalty payments under the lease) and (2) whether "fuel gas" was an appropriate deduction (and thereby

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193 (9 October 2009), Calgary 0601-05052 (Alta. Q.B.).
194 *Ibid.* at 4.

whether royalty payments were to be based on gas sold or gas produced). The Court began by stating that the issues were to "be resolved with reference to the four corners of the lease" document as a whole.[195]

On the issue of royalty price, the Court found that "a plain and unambiguous reading" of the lease indicated that the royalty price was to be "the highest of the actual price received or the current market value."[196] Petrobank's corporate practice of using an average or pooling price was held to be irrelevant. Moreover, Petrobank's claim that Canpar's position was inconsistent with industry standard was also held to be irrelevant.[197]

On the issue of the deductibility of fuel costs, Canpar claimed that it received royalty payments based on gas sales rather than production — contrary to the terms of the lease. Petrobank maintained that it was entitled to rely on a lease provision allowing it to use leased substances royalty free for its "operations." The Court found that because the definition of "operations" contained in the lease did not include the use of gas for compressors on and off the leased lands, Petrobank was not entitled to rely on the provision (and thereby not entitled to deduct for fuel gas).[198] Canpar, therefore, was entitled to royalty payments without deductions.

On the issue of damages, the Court relied on the overriding principle that damages should be awarded "in an amount that puts the injured party in the same position as they would have been had the tort not occurred."[199] It awarded damages based on the compensatory approach described in *Freyberg*; from the date of termination of the lease on 3 March 2006 to the date that the defendant vacated the premises. As it found that Petrobank's behaviour was neither high-handed nor egregious, the Court declined to award punitive damages.[200]

4. COMMENTARY

It is rare that full effect is given to "no deduction" language in royalty agreements, but the clear and unambiguous drafting of the royalty clause here resulted in the Court giving full effect to its "no deduction" language. As a result of terms such as "all without any deductions" being specifically included in the royalty clause, the defendant lessee was unable to make any deductions from the point of sale to the point of determination of value — despite industry practices to the contrary.

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195 *Ibid.* at 3.
196 *Ibid.* at 4.
197 *Ibid.*
198 *Ibid.* at 5.
199 *Ibid.* at 7.
200 *Ibid.* at 8.

C. *TRIBUTE RESOURCES V. MCKINLEY FARMS LTD.*[201]

1. BACKGROUND

This case deals with the termination of an oil and gas lease during its secondary term and the potential application of a deeming provision contained in a unit operating agreement intended to extend the term of a lease.

2. FACTS

On 12 October 1977, the predecessor of Tribute Resources Inc. (Tribute) entered into an oil and gas lease with the predecessor of McKinley Farms Inc. (McKinley). The lease was amended by a unit operation agreement dated 30 October 1984. The parties also subsequently entered into a gas storage lease agreement on 24 September 1998.

The lease provided for a ten year primary term "and so long thereafter as oil and gas are produced in paying quantities, or storage operations are being conducted."[202] Here, "gas continued to be produced in paying quantities … until some time in 2001 when it ceased completely because the pool was emptied."[203]

Tribute, as lessee, wished to have the lease, as amended by the unit operation agreement, and the gas storage lease agreement declared valid and subsisting while McKinley, as lessor, wished to have them declared void.

3. DECISION

Based on the wording of the lease, the Court held that, in 2001, the lease was automatically terminated when production in paying quantities ceased. As the lease terminated automatically, there was no default from which relief from forfeiture could be provided.[204]

Tribute, however, submitted that the lease's term was extended beyond 2001 by a clause in the unit operating agreement that allowed it to continue leased lands not included in the "participating section of the unit area" by a payment of $2.50 per acre rental.[205] The clause went on to state:

> And as long as the payments in this clause provided are made or tendered, operations for the *production of the leased substances* from the unit area shall be deemed to be conducted by the lessee on the said lands under the said lease, and the said lease as hereby amended shall remain in full force and effect as to all of the said lands retained by the lessee under the said lease and/or this agreement.[206]

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201 [2009] O.J. No. 2722 (Sup. Ct. J.) (QL).
202 *Ibid.* at para. 9 [emphasis omitted].
203 *Ibid.* at para. 11.
204 *Ibid.* at paras. 26-27.
205 *Ibid.* at para. 17.
206 *Ibid.* at para. 18 [emphasis in original].

The Court disagreed with Tribute's submission that the effect of this so-called "deemed production clause" was to deem production to continue if proper timely payments were made such that the term of the lease could extend beyond both the automatic ten-year expiration and the cessation of production in paying quantities.[207]

As Tribute had drafted both documents, the Court applied the *contra preferendum* rule against it and held that the unit operating agreement did not extend the term of the lease because: (1) the potential change in duration of the lease was camouflaged in a subclause dealing with payment and (2) the necessary wording "in paying quantities" was absent from the clause such that it dealt only with deemed production and not deemed production in paying quantities as required by the lease itself.[208]

The last issue to be addressed by the Court was the term of the gas storage lease agreement that provided for termination "on the tenth anniversary date, if any only if, the lessee or some other person has not applied to the Ontario Energy Board to have the said lands or any part thereof designated as a gas storage area on or before the tenth anniversary date hereof."[209] As Tribute had failed to make the application within the ten-year period, the Court found that the gas storage lease agreement had automatically terminated on its terms.

4. COMMENTARY

This case confirms the well-established principle that oil and gas leases terminate automatically during the secondary term for want of production or deemed production and as there is no default, there is no potential for relief from forfeiture.

Noteworthy in this case, however, are the Court's reasons for refusing to apply the lessee's deeming approach and the resulting refresher on the general principles of drafting and construction in the realm of lease agreements. Courts will generally give effect to clear language; however, where a lack of clarity exists, the rule of *contra preferendum* calls for any ambiguity in interpreting agreements to be strictly construed against the party who drafted the document. Thus, if the effect sought is a deeming approach, care should be taken to ensure that the language used is sufficiently exact such that it will achieve that effect. Moreover, clauses dealing with certain terms of the agreement should not be camouflaged within other clauses of the agreement as the Court may not give effect to the provision despite the lessee's desire.

D. *DESOTO RESOURCES LTD. V. ALBERTA (ENERGY UTILITIES BOARD)*[210]

1. BACKGROUND

The ERCB has the ability to rule on the validity of freehold oil and natural gas leases in certain circumstances and has asserted its jurisdiction to do so in a number of instances. The jurisdiction of the ERCB to rule on the validity of a lease as a stand-alone issue had

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207 *Ibid.* at paras. 19-20.
208 *Ibid.* at para. 21.
209 *Ibid.* at para. 30.
210 2008 ABCA 349, [2008] A.J. No. 1156 (QL) [*Desoto* (C.A.)].

traditionally been contested in the courts, but if the validity is closely related to an issue before the Board, the decision can be made without the courts' involvement. The ERCB's jurisdiction to rule on lease validity may have broad implications, particularly if the requirement that the validity may only be a secondary issue before the Board is relaxed.

2. FACTS

Between 1974 and 1975, EnCana granted petroleum and natural gas leases to Penn West. Desoto Resources Limited (Desoto) acquired beneficial interests under the leases by virtue of various assignments and other agreements. The leases were originally continued by a unitization agreement, but that unit terminated in 1998. The wells were shut-in and abandoned. In 2002, Desoto served notice to EnCana of its intention to drill a new well on the lands covered by the leases. EnCana's position was that it was "clear under the terms of the Leases that they had terminated, given that no well drilled during the primary term was producing or capable or production."[211] Desoto claimed that the leases continued because the wells were still capable of production.[212] Desoto made an application to the Court of Queen's Bench to review the case.[213] Desoto also concurrently applied to the ERCB for a licence and drilled a well on the leased lands.[214]

The ERCB concluded on its review that Desoto did not have an interest in the minerals because the wells were not capable of production.[215] EnCana then applied for, and was granted, summary judgment. The Court found that there had been no production from the lands since 1998 and, while there was evidence as to reserves, there was no evidence as to wells drilled that might be capable of production.[216] There was also no basis for an estoppel argument. Even though EnCana acknowledged the lease validity in 1999 or 2002, this did not mean that it was now prevented from questioning the continuation of the lease.[217]

EnCana also requested a review of the ERCB's decision to grant Desoto a well licence on the grounds that the leases on which Desoto relied were no longer valid. EnCana argued that, in the context of a private lease, whether or not a lease was capable of production within the primary term was dependent on whether the well "was capable of immediately producing oil and gas upon being turned 'on,' without the need for additional equipment, utilities, or infrastructure."[218] The Board agreed with EnCana and concluded that the leases were no longer valid and that Desoto's well licence should be suspended since the well was not capable of immediate production without additional operations being conducted. Furthermore, there was no evidence that the well could produce in paying quantities once brought on production.[219] Desoto appealed the decision of the ERCB to the Court of Appeal on the basis that the Board did not have the jurisdiction to determine lease validity.

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211 *Desoto Resources Ltd. v. Encana Corp.*, 2009 ABQB 337, 473 A.R. 94 at para. 17 [*Desoto* (Q.B.)].
212 *Ibid.* at para. 18.
213 *Ibid.*
214 *Desoto Resources Limited: Section 40 Review of Well Licence No. 0365128 — Joffre Field*, EUB Decision 2008-047 (17 June 2008) [*Desoto* (ERCB)].
215 *Ibid.* at 11.
216 *Desoto* (Q.B.), *supra* note 211 at para. 30.
217 *Ibid.* at paras. 31-33.
218 *Desoto* (ERCB), *supra* note 214 at 7.
219 *Ibid.* at 11.

3. DECISION

The Court of Appeal dismissed the application, stating that there was no merit to Desoto's argument.[220] The ERCB had jurisdiction to determine lease validity, at least in the context of issuing a well licence. The ERCB "could not have issued the well licence without having been satisfied as a result of information provided that the lease was valid."[221] When the ERCB first decided to issue the licence to Desoto, it was not aware of the outstanding litigation between Desoto and EnCana. Once that was brought to its attention, the ERCB properly conducted a hearing to determine whether the well licence should have been issued.[222] The Court made no comment as to the validity of the lease since the issue before it was jurisdiction.

4. COMMENTARY

Although the ERCB has been criticized for, and continues to dispute, its right to decide issues that are fundamentally legal issues, the efficiency of the process becomes suspect if every question of a legal nature is to be tested in court. Given the nexus of the validity issue to the granting of a licence to drill, it is essential to the process that the ERCB be able to make its determination of validity in order to rule on the well licence. The Court of Appeal simply affirmed the ERCB's jurisdiction to make such determinations.

E. *OMERS ENERGY INC. V. ALBERTA (ENERGY RESOURCES CONSERVATION BOARD)*[223]

1. BACKGROUND

Following the ERCB's decision in *Desoto* and the Court of Appeal's subsequent decision to uphold the ERCB's jurisdiction in deciding cases of lease validity, a second case was brought before the ERCB involving lease validity in the context of a well licence.

2. FACTS

In August 2004 and January 2008, the ERCB approved two applications made by OMERS Energy Inc. (OMERS) for well licences to drill gas wells on lands within the Warwick Field. On 20 June 2008, the ERCB received letters from Montane Resources Ltd. (Montane), the top lessee, requesting a review of OMERS' well licences to determine whether OMERS held "a valid and subsisting lease" for the purposes of issuing a well licence.[224] The lease was for a five-year term but would continue after the expiry of the primary term if there was a well on the lands that was "capable of producing the leased substances."[225] The parties both agreed that the lease continued past its primary term of five years. What was at issue was whether the relevant well was capable of producing the leased substances at all material

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220 *Desoto* (C.A.), *supra* note 210 at para. 2.
221 *Ibid.* at para. 3.
222 *Ibid.*
223 2009 ABCA 273, [2009] A.J. No. 873 (QL) [*OMERS*].
224 *Omers Energy Inc.: Section 39 Review of Well Licences No. 0336235 and No. 0392996 — Warwick Field*, ERCB Decision 2009-037 (12 May 2009) at 1.
225 *Ibid.* at 2.

times after the expiry of the primary term as the well was shut in for certain periods of time following the expiry of the primary term.

Prior to being shut in, the well in question had experienced a high water level in the wellbore. OMERS believed that this was due to a poor cementing job and attempted two operations to address the problem. The ERCB determined that the phrase in the lease "capable of producing the leased substances" should be interpreted to mean "the demonstrated, present ability of a well on the lands to produce the leased substances in a meaningful quantity within the timeframes contemplated in the lease."[226] In the ERCB's view, OMERS had not demonstrated that the well at issue was capable of producing the leased substances in meaningful quantities. Furthermore, the ERCB was not convinced that the well was capable of producing leased substances without some remedial operations and, therefore, held that the lease had terminated. The ERCB suspended OMERS' well licence.[227]

OMERS appealed the ERCB's decision. OMERS sought leave to appeal on three grounds: "whether the [ERCB] erred in concluding that OMERS did not have a valid and subsisting lease, whether OMERS was accorded procedural fairness and whether the [ERCB] abused its discretion."[228] OMERS was granted leave to appeal on the question of whether the ERCB erred in its interpretation of the phrase "capable of producing the leased substances" but was not granted leave for the other two grounds.

3. DECISION

The Court of Appeal found that the ERCB had erred in its interpretation of "capable of producing leased substances" and had no judicial guidance in its interpretation of that phrase.[229] Both parties agreed that this raised a question of law not fully within the ERCB's expertise, therefore warranting a standard of review of correctness on appeal.

4. COMMENTARY

While *Desoto* reaffirmed the ERCB's jurisdiction to determine lease validity, *OMERS* questioned it to some extent. This decision of the Court of Appeal will undoubtedly be watched with great interest as, traditionally, the courts have had the exclusive jurisdiction to decide on lease validity issues, and not the ERCB. This use of regulatory jurisdiction is an interesting expansion of the available options in questioning freehold leases in Alberta.

It is important to note that the ERCB does not have unlimited jurisdiction to rule on the validity of oil and gas leases. There must exist a connection between the lease validity issue and a matter falling under the ERCB's jurisdiction, such as whether the holder of a well licence has title to the relevant working interests. The ERCB must have jurisdiction to determine legal issues that arise in the course of exercising its statutory power to issue or decline to issue a well licence, but without that nexus to the matter before the ERCB it is doubtful that the ERCB can be used to determine the validity of a lease as a distinct issue.

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226 *Ibid.* at 9.
227 *Ibid.* at 13-14.
228 *OMERS*, *supra* note 223 at para. 2.
229 *Ibid.* at para. 4.

X. ADMINISTRATIVE LAW

A. *BERGER V. ALBERTA (ENERGY RESOURCES CONSERVATION BOARD)*[230]

1. BACKGROUND

This case deals with the impact of including judicial deference and the standard of review in the test for obtaining leave to appeal an ERCB decision.

2. FACTS

The applicants made an application seeking leave to appeal an ERCB decision authorizing the drilling of three sour gas wells near Tomahawk, Alberta.[231] The applicants listed over 12 grounds in their application for leave to appeal, including that the ERCB erred in its interpretation and application of its own directives and governing legislation.

3. DECISION

Under s. 41 of the *ERCA*,[232] a condition precedent to granting leave to appeal is that the proposed question be one of law or jurisdiction; leave can only be granted on particular issues of law. Here, the Alberta Court of Appeal denied the applicants' request for leave to appeal. In so doing, the Court set out several of the factors to be considered in an application for leave, including: whether the issue is of general importance; whether the issue is merely interlocutory, collateral, or tangential to the action; whether the issue has arguable merit; and the standard of review that is likely to be applied.[233]

In its discussion of the standard of review to be applied, the Court stated that "[t]here is no point in granting leave if the standard of review that the Court of Appeal will apply is highly deferential, such that the Court is unlikely to engage the issue upon which leave is sought."[234]

4. COMMENTARY

Given that the courts are typically highly deferential to the decisions of administrative boards and tribunals because they possess a specialized expertise in relation to the regulatory framework that they administer, this inclusion of judicial deference and the standard of review in the test for granting leave to appeal will likely limit an applicant's ability to meet the test for leave and may enable administrative decision-makers, such as the ERCB, to have the final say on issues of law.

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230 2009 ABCA 158, [2009] A.J. No. 417 (QL) [*Berger*].
231 *Highpine Oil & Gas Limited: Applications for Three Well Licences — Pembina Field, Tomahawk Area*, ERCB Decision 2008-135 (30 December 2008).
232 *Supra* note 101.
233 *Berger*, *supra* note 230 at para. 2.
234 *Ibid.*

B. *ATCO MIDSTREAM LTD. V. ENERGY RESOURCES CONSERVATION BOARD*[235]

1. BACKGROUND

Standing is often a discussion point for parties appearing before the ERCB and it is imperative for the efficiency of the ERCB proceedings that standing be granted fairly but judiciously. This case deals with the narrowness of the standing provisions in the *ERCA*.

2. FACTS

The respondent, Keyera Energy Ltd. (Keyera), operated a field plant that processes natural gas near Rimbey, Alberta (the Rimbey Plant). Once processed, the gas is injected into a transmission pipeline and becomes part of a "common stream."[236] Keyera applied to the ERCB "for an amendment to its licence that would allow it to extract ethane from the raw natural gas processed at the Rimbey Plant."[237]

The appellant, ATCO Midstream Ltd. (ATCO), was part owner of two straddle plants that extract ethane from the common stream. The other appellant, Nova Chemicals Corporation (Nova), purchased extracted ethane.

The ERCB sent out notices for objection to the appellants which stated, "should you have a legally recognized interest in this application and want to make a submission, please state in writing your reasons for objecting to the application."[238]

Both ATCO and Nova objected. The ERCB dismissed the appellants' objections on the basis that they were "essentially asserting a right to be economically protected from upstream ethane recovery" and that this was not a legally recognized right within the meaning of s. 26(2) of the *ERCA*.[239] Both ATCO and Nova appealed the ERCB decisions declining to grant them standing.

3. DECISION

The Alberta Court of Appeal indicated that the appellants had failed to establish any authority for the proposition that their economic interests are legally recognized rights under s. 26(2). Accordingly, the Court found that the ERCB did not err in law or jurisdiction in declining to grant the appellants standing.[240] Finally, the Court concluded that because the ERCB's finding that the appellants failed to meet the test for standing raised "at best a question of mixed fact and law the decisions [were] not subject to review on appeal."[241]

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235 2009 ABCA 41, 446 A.R. 326.
236 *Ibid.* at para. 4.
237 *Ibid.* at para. 6.
238 *Ibid.*
239 *Ibid.* at para. 9.
240 *Ibid.* at para. 11.
241 *Ibid.* The test for standing was set out in *Dene Tha' First Nation v. Alberta (Energy and Utilities Board)*, 2005 ABCA 68, 363 A.R. 234.

4. COMMENTARY

The narrowness of the standing provision in the *ERCA* has resulted in many parties, often public interest interveners and First Nations, being denied standing on the ground that they lack an adequate legal interest in the subject matter of the application. Noteworthy in this case, however, is that standing has been denied to ATCO, a leading provincial utility and gas processor, and Nova, a large petrochemical interest — two large players in the industry. The Court of Appeal has made it clear that economic interests, or economic might in the industry, will not assist a party where there is no legal right being affected.

C. *LAMB V. ALANRIDGE HOMES LTD.*[242]

1. BACKGROUND

This case illustrates the lack of clarity of s. 7 of the *Arbitration Act*,[243] which requires a court to stay a court action when asked to do so by a party to an agreement to arbitrate. As s. 7 is one of the provisions most often considered by the courts, a rare call for legislative action is made by the Alberta Court of Appeal in this decision.

2. FACTS

Brian and Melina Lamb (the Lambs) entered into a construction agreement with AlanRidge Homes Ltd. (AlanRidge), which "contained a mandatory binding arbitration agreement in standard form, in accordance with the Alberta New Home Warranty Program."[244]

After alleging various defects in the house, the Lambs invoked arbitration pursuant to the agreement but subsequently commenced court proceedings against AlanRidge and certain subcontractors.

AlanRidge applied to stay the action under the *Arbitration Act*. The chambers judge found that while all claims against AlanRidge were within the scope of the arbitration agreement, there were both arbitrable and non-arbitrable claims embedded in the lawsuit. He therefore found that "the arbitration agreement covered only some matters in dispute in the legal action."[245] The chambers judge also declined to apply s. 7(5) of the *Arbitration Act* to grant a partial stay, as he determined that the "claims were 'inextricably linked' … such that they could not be reasonably separated."[246]

AlanRidge's application to stay the action was dismissed and the arbitration was stayed in order to avoid a multiplicity of proceedings. AlanRidge appealed the decision, asking the Court of Appeal to narrowly interpret s. 7(6), which does not permit any appeal from a court's decision under s. 7.

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242 2009 ABCA 343, 464 A.R. 46 [*Lamb*].
243 R.S.A. 2000, c. A-43.
244 *Lamb*, *supra* note 242 at para. 3.
245 *Ibid.* at para. 7.
246 *Ibid.* at para. 8.

3. DECISION

The Court of Appeal concluded that the chambers judge's decision was made under s. 7 and, as such, the application of s. 7(6) precluded appeal by AlanRidge despite its claim that s. 7 was erroneously interpreted.[247] In so doing, the Court indicated that s. 7(6) reflects the policy consideration that the process of determining whether to proceed by arbitration or legal proceedings should "not become bogged down by resort to the appeal process."[248] As such, it interpreted s. 7(6) in accordance with its plain meaning and dismissed AlanRidge's appeal.

4. COMMENTARY

The Court of Appeal rarely considers s. 7 of the *Arbitration Act* because s. 7(6) precludes appeal from an order of the Court of Queen's Bench. In this rare case where s. 7 came before it, the Court emphasized that s. 7 of the *Act* is "far from a model of clarity and, in particular, the intended scope of subsection (5) is far from clear."[249]

Although it denied AlanRidge's appeal, the Court did go on to suggest that "legislative review and amendment [of the *Arbitration Act*] may be appropriate, especially in circumstances in which appellate review of decisions under section 7 is precluded."[250] The courts do not often suggest that legislation be reviewed and amended, so this decision revives the debate as to whether there should be instances where no appeal is possible from a judicial ruling, given the necessary balance between efficiency and fairness of the process.

XI. RIGHTS OF FIRST REFUSAL

A. *BEARSPAW PETROLEUM LTD. V. CONOCOPHILLIPS WESTERN CANADA PARTNERSHIP*[251]

1. BACKGROUND

Generally, the price in a right of first refusal (ROFR) notice would be the price offered by the third party purchaser. However, valuation issues for the purposes of a ROFR notice can arise where lands subject to the ROFR make up a portion of a package sale that includes other lands not jointly owned by the two parties. This is especially true where the sale price does not break out the value of the ROFR lands, or where there is concern that the vendor and purchaser have not fairly represented the price of the ROFR lands to the ROFR holder.

2. FACTS

ConocoPhillips Western Canada Partnership (ConocoPhillips) sought to sell certain oil and gas properties (the package lands) that it owned both individually and in common with

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247 *Ibid.* at para. 11.
248 *Ibid.* at para. 14.
249 *Ibid.* at para. 16.
250 *Ibid.* at para. 18.
251 2009 ABQB 202, [2009] 7 W.W.R. 125 [*Bearspaw Petroleum*].

Bearspaw Petroleum Ltd. (Bearspaw). Bearspaw held ROFRs with respect to the lands owned in common between the two parties (the ROFR lands). In 2006, Pengrowth Corporation (Pengrowth) bid successfully for the package lands for a sum of approximately $1 billion. The transaction was completed through a share purchase sale where the assets were conveyed to one of four ConocoPhillips subsidiary corporations, the shares of which were then purchased by Pengrowth. One of the subsidiaries was the vehicle through which the ROFR lands were conveyed to Pengrowth. Though ConocoPhillips issued a notice of assignment, they did not contain values for the ROFR lands and no ROFR notices were given to Bearspaw. Bearspaw subsequently requested ROFR notices from ConocoPhillips, but none were issued as ConocoPhillips "took the position that the sale of the ROFR lands was between affiliated companies."[252]

In 2008, Pengrowth (also a defendant in this action) sent a "business settlement proposal" that denied the transaction triggered the ROFR notices, but offered a ROFR notice anyway with values for the ROFR lands determined by Pengrowth in late 2007.[253] Prior to the expiration of the ROFR notices, Bearspaw issued a notice of motion requesting disclosure by the defendants of certain valuation information (allowed in part). Pengrowth cross-applied for summary dismissal (the subject of this decision).

3. DECISION

The leading case on the issue of valuation in a package sale is *Chase Manhattan Bank of Canada v. Sunoma Energy Corp.*[254] *Chase* was considered by Master Hanebury, who derived the following principles: (1) a package sale triggers ROFR rights; (2) "[w]ith a package sale, the vendor owes a duty of good faith to the ROFR holder in setting a bona fide estimate of the value" of the ROFR lands; (3) "[i]t is not obvious that a duty of good faith is owed by the purchaser in a package sale" to the ROFR holder; and (4) "the ROFR holder challenging the issuance of proper ROFR notices must establish that the purchase price allocated to the [ROFR lands] is not a bona fide estimate of their value."[255] This case, however, was distinguished from *Chase* in that, in this case, the sale was completed and then there was a direct offer by the purchaser to the ROFR holder, with such offer being made to limit its exposure to litigation by offering the equivalent rights that should have been offered by the vendor in the first instance.[256]

Master Hanebury decided that for the summary dismissal application to be successful, Pengrowth would have had to show that their remedial "settlement offer is in line with what would have been offered" under ROFR notices had such notices been provided to Bearspaw by ConocoPhillips at the actual time of sale of the assets.[257] In this case, there was evidence to indicate that Pengrowth calculated the price of the lands in the settlement offer "on the basis of what it would sell the assets [for] if it already owned them at the time the ROFR notices would have been issued" (that is, other attributes specific to Pengrowth's situation

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252 *Ibid.* at para. 14.
253 *Ibid.* at paras. 17-18.
254 2001 ABQB 142, 283 A.R. 260 [*Chase*], aff'd 2002 ABCA 286, 317 A.R. 308.
255 *Bearspaw Petroleum*, *supra* note 251 at para. 48.
256 *Ibid.* at para. 51.
257 *Ibid.* at para. 67.

were built in to the offer price to ensure that Pengrowth was left "whole" should its settlement offer be accepted by Bearspaw).[258]

Because no evidence was led to suggest that the price of the remedial settlement offer was in line with the price that would have been assigned at the time of the sale to the portion of lands subject to the ROFR notices, the application for summary dismissal was dismissed on the basis that there was a genuine issue to go to trial.

4. COMMENTARY

The ROFR holder has a significant burden to overcome in proving that the purchase price in a ROFR notice is not a bona fide estimate of the value of the ROFR lands that are part of a package sale. It will be paramount for the ROFR holder to provide evidence that shows the methodology of the valuation calculations in order to make this assessment. The evidence will be held by either or both of the vendor and purchaser, and it remains to be seen whether the vendor will be able to rely on the purchaser's particular valuation calculations, and whether the ROFR holder will be successful at obtaining evidence from the purchaser to assist its cause to show that the price attributed to the ROFR lands is not a bona fide estimate of the value of those lands.

[258] *Ibid.* at para. 67.