WESTERN OIL CONSULTANTS v. GREAT NORTHERN OILS LTD.*

ROSEMARY NATION**

I. INTRODUCTION

The case of *Western Oil Consultants* v. *Great Northern Oils Ltd.* raises several important issues for the oil and gas industry. Of greatest significance, it addresses the legal remedies available to and the numerous defences that may be raised against a consultant or individual who attempts to enforce his right of assignment (contained in a gross overriding royalty), on surrender of an oil and gas lease where the lease is surrendered without proper notice. The *WOC* case presents a fact situation which is typical of disputes in the oil and gas area, and the Court is forced to make decisions on how various legalities are to be interpreted in reference to this specific problem.

II. THE FACTS

The facts in this case justify being reviewed in some detail since they are typical of the way in which this type of lawsuit arises in the oil and gas industry.

Western Oil Consultants (WOC), the Plaintiff, was formed in 1965 and one of its first activities was to have Mr. Fleischman, the individual behind the company, work up a play in relation to the Vermilion area. This play was then presented by Mr. Fleischman to Penwa Oils Limited (Penwa). The lands relevant to the play were held by Union Oil Corporation of Canada Limited (Union) as a lessee of the Provincial Crown. As a result of WOC's efforts, it was agreed that Union would "farm-out" its interest in the lands to Penwa.

In consideration of the play and the role that WOC played, the WOC Royalty Agreement was executed. Under the contract, Penwa agreed, *inter alia*, to pay $7,000.00 to WOC and granted to WOC a gross overriding royalty of 2% of " . . . all production of petroleum and/or natural gas produced saved and marketed . . . ". Penwa undertook to give WOC notice of any intended surrender of lands earned in the Union farm-out, WOC having a right of assignment in that event. The terms of the notice provision in the WOC Royalty Agreement were as follows:

> It is agreed, however, in the event the Group desires to surrender the said lands, or any portion thereof or any leases selected therefrom, that, thirty (30) days prior to any rental date, the Group shall notify W.O.C. Ltd. of its intention to make such surrender, setting forth the lands to be surrendered. Within thirty (30) days of the receipt of such surrender notice W.O.C. Ltd. shall notify the Group as to whether they desire to take an assignment of any or all of the lands set forth in the said surrender notice.

On March 1, 1967, Penwa transferred to Great Northern Oils Ltd. (GNOL) a 50 per cent interest in the various lands which it received as a result of completing some of the drilling commitments under the Union

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* (1981) 121 D.L.R. (3d) 724. (Alta. Q.B.) A Notice of Appeal was filed by the plaintiff, Western Oil Consultants Ltd. However, the matter was settled by payment of damages by the defendant and costs as assessed by the trial judge and the plaintiff abandoned its appeal.

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farm-out and GNOL became the operator.

During late February or early March of 1968, Union and Penwa agreed to surrender certain lands to which the WOC Royalty Agreement applied. By letter, Penwa gave notice to WOC of these surrenders which had already taken place. WOC had been notified 'after the fact', so to speak, and in an effort to compensate WOC for its loss, a settlement was made out of Court between the parties which involved a gross overriding royalty to WOC on certain lands being increased.

It was established at trial that a number of notices of surrender in writing had been given by GNOL to WOC, to which WOC had agreed without taking an assignment. It was further established that in one situation oral notice had been given to WOC of a surrender, and WOC elected to take an assignment of the properties. A written assignment was executed by both parties.

In January of 1972, Union and GNOL agreed to surrender two sections of land. In February and again in November of 1972, a section of land was surrendered.[1] It is to the surrender of these four sections of land that this lawsuit pertained. GNOL later reaquired a 25 per cent interest in one section and held that interest at the time of the trial.

It was the evidence of Mr. Fleischman that the surrenders on the four sections were in each case made without notice to WOC. WOC first became aware of the surrenders when, in July of 1977, Mr. Fleischman noticed that two sections were being advertised in a public offering of petroleum and natural gas rights. By further investigation WOC realized that two additional sections had been surrendered. It was the further evidence of Mr. Fleischman that if these lands had in fact been offered to him in 1972 before their surrender, WOC would have retained them.

III. ISSUES AND DEFENCES

WOC commenced an action by Statement of Claim which was issued on October 12, 1978, claiming specific performance of the royalty agreement and damages. The defences raised to the action were as follows:

(1) With respect to two sections, oral notice of surrender had been given to the WOC.

(2) The claim could not be advanced because the WOC was not licenced under the Real Estate Agents Licensing Act.

(3) The action in regards to three sections was barred by the Limitation of Actions Act.

(4) The damages claimed were excessive.

The first two defences can be dealt with in a fairly summary manner although aspects of the decision are worthy of note to those practicing in the oil and gas areas. The latter two defences are two where the law is at present unclear and the case, which will not be appealed, stands as some indication of how these matters may be viewed by a Court.

A. *Must Notice Be In Writing?*

The issue arose in this lawsuit whether notice had been given orally and, if so, whether by the contract terms it should have been in writing. GNOL admitted that it had no record of written notice. However, in its records, on a letter from Union to GNOL, there was a notation made by the landman stating "by phone Stan Fleischman concurs with surrender Jan. 10/72".

1. One of the sections was incomplete. Several LSD's were missing, but for the purpose of this article, that portion of a section will be referred to as one section.

In the notice clause of the WOC Royalty Agreement there is no statement that written notice is required, and the Defendant argued the *contra proferentem* rule should be applied to mean oral notice would suffice.[2]

Mr. Justice Patterson found on the evidence presented that no oral notice had been given. However, he continued in *obiter dicta* to find that:[3]

> In view of the general practice of the industry and specifically the following words as they appear in ex. 11 "setting forth the lands to be surrendered" and "lands set forth in the surrender notice", I find that it was never contemplated by either party that anything less than written notice was acceptable and that ex. 11 required notice to be written.

This finding should not be taken lightly since it is a precedent which would indicate that there is a custom in the oil and gas industry that will be used in the interpretation of these types of documents. The finding is particularly forceful since at trial there was evidence that the plaintiff had accepted oral notice at an earlier date, although in that situation a written assignment was later executed between the parties.

The authority to take notice of a usage in the industry in interpreting a contract was found in the Supreme Court of Canada case of *Georgia Construction Company* v. *Pacific Great Eastern Railway Company.*[4] That case held, in relation to the use of trade custom in contract intepretations, that:[5]

> Usage, of course, where it is established, may annex an unexpressed incident to a written contract; but it must be reasonably certain and so notorious and so generally acquiesced in that it may be presumed to form an ingredient of the contract.

Mr. Justice Duff further went on to quote Lord Justice Banks in another case stating that a custom must be[6]

> . . . so all pervading and so reasonable and so well known that everybody doing business in railway construction "must be assumed to know" it, and to contract subject to it.

In the case of *Re Gainers Ltd.*,[7] Riley J. applied the *dicta* of Duff J. in the *Georgia* case as follows:[8]

> It would appear that the Supreme Court of Canada has clearly established the proposition that where usage is demonstrated and proved, that usage will be incorporated into any contract which does not specifically contradict that usage which is generally known and accepted.

In a more recent case, *Banks* v. *Biensch*,[9] MacDonald J. dealt with the issue of whether a code of ethics of an association of traders could be inferred into a contract. In applying the *Georgia dicta*, he held that:[10]

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2. It should be noted that the agreement was drafted by the plaintiff who by his admission had copied another agreement. The omission of the words "in writing" were deleted in error by the plaintiff or the typist.
3. *Supra* n. * at 730. As well as the evidence of the plaintiff's expert witness, a landman of some 25 years, the officer and also the former employee of the defendant admitted it was usual that such notices should be in writing. However, it is to be noted that the defendant's officer indicated he had never seen an agreement that did not specify notice in writing.
4. [1929] S.C.R. 630.
5. *Id.* at 633.
6. *Id.* at 634.
7. (1964) 47 W.W.R. 544 (Alta. S.C.).
8. *Id.* at 555.
9. (1977) 3 Alta. L.R. (2d) 41 (S.C.T.D.).
10. *Id.* at 45. It should be noted that the C.A.P.L. Operating Agreement was entered as an exhibit. It provides in Article XXII at paragraph 2201 that:
    > Whether or not so stipulated herein, all notices, communications and statements (hereinafter called 'notices') required or permitted hereunder shall be in writing.

    Although not part of this agreement, it was tendered in support of the pervasiveness of the custom.

> Unless altered by the terms of the contract of sale or by law, I find the contract of sale of a Charolais animal by a member of that association, as was the defendant, would imply, if applicable, the code of that association .... The usage of the trade in sales of Charolais animals by members of the association is so well recognized and established through the "Code of Ethics" that the guarantees established by that code can be assumed as implied terms of the sale.

The pertinent point in this respect is that there is precedent that it is a custom that notice of surrender be in writing. It is interesting to consider how far this may be extended, and whether courts in the future may find it common usage that all notices in regards to lands in dealings within the oil patch be in writing. The casualness with which some transactions are documented in the oil industry at times makes this precedent one that may be of use in future contract problems in the industry.

B. *The Applicability of the Real Estate Agents' Licensing Act.*

At first glance, it seems unusual that a lack of licensing under the Real Estate Agents' Licencing Act[11] would be pled against a geologist selling a play on various lands. However, the definitions under this Act, read widely, can be extended to this situation and indeed have been in at least one past case.[12]

In brief, the Act requires that any action for commission or remuneration for services in connection with a trade in real estate requires that the person bringing the action be registered under the Act.[13] "Agent" and "trade" and "real estate" are terms defined by the Act.[14]

The argument of GNOL was that, clearly, here one has Mr. Fleischman for WOC arranging a farm-out between Union and Penwa and receiving cash and an overriding royalty as a "commission". Clearly, here one has an agent, WOC, which for hope of a reward, brought Union and Penwa together. A "trade" in real estate was made and Penwa received an interest in the lease or an option for an interest. (Leasehold property fits within the definition of real estate under the Act.) Thus the question arises as to whether once Mr. Fleischman approached Union about the

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11. R.S.A. 1980, c. R-5.
12. *Arkansas Fuel and Minerals Ltd.* v. *Dome Petroleum Ltd.* (1966) 54 W.W.R. 494 (Alta. C.A.). In that case, a purchase of natural gas reserves was considered a "trade in real estate" as used in the definition section of the Act and the action of the plaintiff stayed as a result, due to non-registration.
13. Section 24:
    (1) No action shall be brought for commission or for remuneration for services in connection with a trade in real estate unless at the time of rendering the services the person bringing the action was licensed as an agent or exempt from the licensing provisions of this Act.
    (2) The court may stay in an action referred to in subsection (1) at any time on summary application."
14. Section 1(1)(a)(i) defines an "agent" to include:
    a person who, for another or others, for compensation, gain or reward, or hope or promise thereof, either alone or through one or more officials or salesmen, trades in real estate....
    Section 2(o)(i) defines "trade" to be:
    a disposition or acquisition of or transaction in real estate by sale, purchase, agreement for sale, exchange, option, lease, rental or otherwise....
    Section 2(l) defines "real estate" to be:
    (i) any real property,
    (ii) any leasehold property,
    (iii) any business, whether with or without premises, and the fixtures, stock-in-trade, goods or chattels in connection with the operation of the business, or
    (iv) any property user's licence.

farm-out, or set matters in motion between Penwa and Union, he had crossed over the line of professional remuneration to become a "agent" under the Act.

WOC argued that it was at no time registered pursuant to the Act, and that although a literal interpretation of the words in the statute might seem to require WOC to register, the Act was not meant to apply to the situation where a professional geologist is suing on a royalty agreement negotiated in regard to professional services. In the unreported case of *Russ Burns Petroleum Consultants Ltd.* v. *Union Oil*,[15] Mr. Justice O'Byrne looked at a case involving a geologist suing under a royalty agreement. He found as a fact that the geologist brought the parties together to make the deal and that he was remunerated for doing so by a gross overriding royalty. Further, Mr. Justice O'Byrne found that the deal in issue concerned land. The *Arkansas* and *Berkheiser*[16] cases were argued and O'Byrne J. said:[17]

> I find on the balance of probabilities that the service was more in the nature of professional geological and consulting services. In my opinion, the statute to be considered does not contemplate at all this situation. It has no application.

Mr. Justice O'Byrne further concluded that:[18]

> I find that this action is founded on specific performance or damages under an agreement and not for remuneration as contemplated by the statute. Burns was paid the cash consideration and became the owner of the gross override in U.V.'s interest in the lease dating back to 1963.

Mr. Justice Patterson in the WOC case followed the *dicta* above and held that the Act had no application and thus could not affect WOC's right of action. Mr. Justice Patterson found that WOC was using Fleischman's highly specialized geological knowledge and to such activities the Act to licence people dealing in real estate could not apply.

This decision is certainly a relief for all geologists, very few of whom, one suspects, even know about the Real Estate Agents' Licencing Act, let alone are licenced under it. Hopefully this case, together with the Alberta Court of Appeal decision in *R* v. *Clark*[19], will lay to rest the use of this defence in dealing with professional geologists suing on a royalty agreement.

C. *The Effect of the Limitation of Actions Act.*

This case raises the question of the relevant limitation period under the Alberta Limitation of Actions Act.[20] The sections were surrendered in 1972, WOC discovered their surrender in the summer of 1977 and a Statement of Claim was issued in October, 1978. In regards to three sections, the Statement of Claim was issued more than six years after the surrender or breach of contract. The delicate question arises: is this an in-

15. 20 October 1978, J.D. of Calgary, S.C. 120615 (Alta. S.C.T.D.).

16. *Arkansas, supra* n. 12; also *Berkheiser* v. *Berkheiser* [1957] S.C.R. 387, a case where a lease of petroleum and natural gas plus the right to explore and drill was found to be a profit à prendre or a licence to search for petroleum or gas but not a devise of land.

17. *Supra* n. 15 at 4.

18. *Supra* n. 15 at 5.

19. In *Regina* v. *Clark* [1973] 3 W.W.R. 666, the Alberta Court of Appeal looked at a case where a home finder agency seemed to fall under the definition sections of the Act. The Court held that it could look at the purpose of the Act, and in doing so held that the business of the accused was not within the contemplation of the Act. The Court supported the view that it was entitled to look behind the strict definition sections and determine what mischief the Act was meant to prevent.

20. R.S.A. 1980, c. L-15.

terest in land with a ten year limitation period or an action in contract with a six year limitation period? Further, if the relevant period is six years, does it run from 1972, the date of surrender, or 1977, the date the matter first came to the Plaintiff's attention?

1. *Is the action in relation to "land"?*

Section 18 of the Limitation of Actions Act sets out the ten year limitation for proceedings to "recover land".[21] "Land" is defined in s. 1(e) to include:

> (i) corporeal hereditaments, and
> (ii) a freehold or leasehold estate or an interest therein.

The argument that the action is to recover land is based on a Statement of Claim in which WOC claims specific performance, being transfer of title to leasehold interests. The action is brought to "recover" a leasehold interest and under the definition section of the Act, leases are an interest in land.

There are two obvious responses to this type of argument. First, a royalty, the major subject matter of the agreement, is not an interest in land. Second, what the Plaintiff had here was a contractual right to have notice, and it was not until notice of surrender was given that any right to an interest in land might arise.

Looking first at the question of a royalty being an interest in land,[22] this point is far from finally decided in law. There has been waffling on the issue and there is conflicting *dicta* from the Supreme Court of Canada. The Alberta Supreme Court in *Vanguard Petroleums* v. *Vermont*[23] looked at a similar royalty agreement in regards to whether a royalty agreement granted an interest which could be caveated. The Court held that the obligation was to pay the royalty once the oil had been removed from the land. The royalty holder was paid a sum of money based on the proceeds and therefore, received a contractual right, not an interest in land. Mr. Justice Moore further held that the legal nature of the royalty could not be changed by the inclusion in the agreement of a clause attempting to tie it to the land, or in that case, allowing the royalty holder to file a Caveat. (This had also been attempted in the WOC contract: " . . . the said Royalty reserved to WOC Ltd. is attached to all lands within the area indicated on said Agreement . . . ".)

In *Emerald Resources Limited* v. *Sterling Oil Properties Management Limited*,[24], the Alberta Court of Appeal looked at whether a gross over-

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21. Section 18 provides:

> No person shall take proceedings to recover land except
> (a) within 10 years next after the right to do so first accrued to such person (hereinafter called the "claimant"), or
> (b) if the right to recover first accrued to a predecessor in title, then within 10 years next after the right accrued to that predecessor.

22. The Royalty Agreement in question in the case did not give in clear language a right to an interest in minerals *in situ*, the relevant clause being:

> In addition to the cash sum payable to W.O.C. Ltd., as set forth above, there shall be reserved to W.O.C. Ltd. a gross overriding royalty of 2% of the current market value at the wellhead of all production of petroleum and/or natural gas produced, saved and marketed from any wells drilled and operated by the Group or its farmee or its assignee on the said lands.

23. [1977] 2 W.W.R. 66 (Alta. S.C.). The writer was unable to find a reported case where this case had been judicially considered.

24. (1969) 3 D.L.R. (3d) 630 (Alta. S.C.A.D.).

riding royalty on hydrocarbons produced, saved or sold from a property was an interest in land for the purposes of the Statute of Frauds. Mr. Justice Allen, speaking for the unanimous Court, held that:[25]

> I am not in a position where I can say that such leases granted a profit à prendre or any interest in land to the lessee and thus I find it impossible to say that the royalty interest claimed by Emerald is or is not an interest in land.

In the case of *Saskatchewan Minerals* v. *Keyes*,[26] the Supreme Court of Canada looked at a situation where the question whether a gross overriding royalty contract created an interest in land was considered. The majority held that they would not decide this issue.[27] However, Laskin J., dissenting, addressed the question of the status of a royalty agreement in great detail, and decided that the royalty interest in that case was an interest in land. Mr. Justice Laskin specifically directed his attention to royalties which related to a share in or return on production, as opposed to minerals *in situ*, and concluded that:[28]

> He became entitled to an overriding royalty in respect of the lessee's interest in lease A-4010, whether that interest was a leasehold in the strict sense or a profit à prendre for a term; and the royalty, unaccrued, was an interest in land, analogous to a rent-charge, and, in the circumstances, binding on the appellant as subsequent assignee of lease A-4010.

In the *Vanguard* decision, Mr. Justice Moore did not respond to the decision of Laskin J. in the *Saskatchewan Minerals* case.

Mr. Justice Patterson, in deciding the WOC case, skirted the question and dealt with the matter on the issue of whether the covenant to give notice of surrender and, upon the plaintiff's election, to provide an assignment of the surrendered lands constituted an "interest in land".

The case argued by the defendant and the case on which the trial Judge relied in deciding this issue in the WOC case is that of *Irving Industries Ltd. et al* v. *Canadian Long Island Petroleums Ltd. and Sadim Oil and Gas Co. Ltd.*[29] In that case, joint owners of an oil lease had a contract not to sell their interest without first allowing the other owner to meet the terms of the proposed sale.[30] The major issue in the trial was the effect of the rule against perpetuities, and whether there was an interest in land to which the rule would apply. The court held that there was not an interest in land and that the right was a contractual right only. The reasoning was that whereas an option (an interest in land) allows the optionee to exercise the right in the future, having control over that event, here the individual had no control over the event until another event which was out of his control (a proposed sale by the other partner) occurred. The decision was ap-

25. *Id.* at 642.
26. (1971) 23 D.L.R. (3d) 573.
27. *Id.* at 577.
28. *Id.* at 590; 585-590 for the reasoning. The decision of the Supreme Court of Canada in *St. Lawrence Petroleum Ltd. et al.* v. *Bailey Selburn Oil and Gas Ltd. et al.* (1963) 45 W.W.R. 26 should be noted also, since it would indicate an overriding royalty giving a percentage of net proceeds of production is not an interest in land.
29. (1974) 3 N.R. 430 (S.C.C.).
30. The relevant clause in that case was:

> If a party hereto receives a bona fide offer for all or any portion of its Participating Interest which it is willing to accept, it shall forthwith give to the Other Party . . . who has not received an offer, written notice of the terms of the said offer . . . and the Non-Selling Party shall have the first right for a period of Thirty (30) Days after written notice is so given to purchase such interest at the price and on the terms set forth in the said offer. . . .

This is very close to the wording in the WOC Royalty Agreement.

proved and followed by Mr. Justice Patterson who quoted at length from Mr. Justice Martland's decision in the *Irving* case.[31]

While the facts in the WOC case do seem similar to those in *Irving*, there are factors at play in the *Irving* case on which one might question its wholesale application in the WOC case. The *Irving* case was dealing mainly with the rule against perpetuities. The circumstances were such that the Court may have been leaning on the basis of fairness to find that the rule did not apply to bar the action, which would be achieved by a finding that the contract was not an "interest in land". Further, the *Irving* case fails to consider the ruling in *Ruptash*[32] which indicated that a right of first refusal is an interest capable of forming the basis of a Caveat (thus an interest in land). It would seem that the Court in the WOC case felt that an option was an interest in land, but as the WOC contract was more akin to a right of first refusal, it would not be so on the facts.

There are other authorities which would indicate that a preemptive right may be an interest in land.[33] Most worthy of a detailed discussion is the case of *McFarland* v. *Hauser*[34] which raised the question of the classification of a right of first refusal. This issue arose in the context of whether it was a disposition of an interest in land, and thus effected by the Alberta Dower Act. In the Alberta Court of Appeal, four of the five Justices hearing the appeal held that a right of first refusal was not a disposition of an interest in land under The Dower Act. The four Justices who concurred on this point based their reasoning on the *Irving* case.[35] Chief Justice McGillivray, however, expressed the opinion that the right of first refusal was converted into an option when the grantor of the right received an offer which he was prepared to accept.[36]

The Supreme Court of Canada in the *McFarland* case followed Mr. Justice Clement's reasoning. They held that the right of first refusal did not, by itself, constitute a disposition of an interest in land, thereby following the *Irving* case.[37] However, in dealing with the remedy of specific performance, it should be noted that the Supreme Court of Canada held that the right of first refusal was converted into an option to purchase upon the grantor, Hauser, receiving an offer he was prepared to accept. Thereupon, McFarland was held to have an equitable interest in land.[38]

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31. *Supra* n. 29 at 446.
32. *Ruptash and Lumsden* v. *Zawick* (1956) S.C.R. 347. In that case a contract regarding property contained a right of preemption. One party filed a caveat protecting that right. The caveat had been disallowed by the Court of Appeal; however, Cartwright J. (at 355) held that it was his opinion that the filing of the caveat was effective to protect the right of first refusal in the property.
33. In *United Fuel Supply Co. Ltd.* v. *Volcanic Oil and Gas Co.* (1911-12) 3 O.W.N. 93, Mr. Justice Sutherland held a right of preemption to a profit a prendre was an interest in land that could be caveated. G.V. LaForest, in a case comment in (1960) 38 *Can. Bar Rev.* 595, suggests that options and rights of preemption should be treated as the same types of interests. His opinion is quoted in *Thom's Canadian Torrens System* (2nd ed. Di Castra. ed. 1962) 588, where it is suggested a right of first refusal may be caveated.
34. (1977) 2 Alta. L.R. (2d) 289 (S.C.A.D.); *revd* (1978) 7 Alta. L.R. (2d) 204 (S.C.C.).
35. Mr. Justice Clement followed the *Irving* case (at 322) as did Mr. Justice Morrow, concurred with by Mr. Justice Moir (at 350). Mr. Justice Moore did likewise at 327.
36. *Supra* n. 34 at 302.
37. *Supra* n. 34 at 214.
38. *Supra* n. 34 at 218. This would seem to follow the decision of Chief Justice McGillivray in the Court of Appeal case.

This latter part of the Supreme Court of Canada's decision gives an interesting perspective to the WOC lawsuit, since it may be argued that once Union and GNOL agreed to surrender certain sections of land, WOC had an option on those lands and thereby an interest in land. Thus, it is arguable that the lawsuit involved a right of first refusal which had, in fact, been converted to an option agreement and therefore may fall under the ten year limitation period relating to land.

Further, there is case authority judicially considering various Limitation of Actions Acts that would indicate an action to recover land covers a lawsuit where the relief claimed is the transfer of or title to a parcel of land (in WOC, a leasehold interest).

In the judicial interpretation of *The Limitations of Actions Act* in Britain, an "action to recover land" is not limited to obtaining possession of the lands.[39] In the case of *Hester Vandeleur* v. *Sloan*,[40] the Court held that a case where action was brough to claim a declaration of title, even though tenants were in possession of land at the time of the action, was an action to recover land. Furthermore, in *Williams* v. *Thomas*[41] the Court of Appeal, via Buckley L.J., held that:[42]

> It has been argued, and, I think, successfully, that while on the one hand the expression "to recover any land" in s.2 of the Act of 1833 does not mean regain something which the plaintiff previously had and has lost, but means "obtain any land by judgment of the Court," yet it is not limited to the meaning "obtain *possession* of any land by judgment of the Court.

The above British cases have been approved by Mr. Justice Egbert in the case of *Turta* v. *Canadian Pacific Railway*.[43] At the trial level, Egbert J. reviewed a number of cases dealing with the meaning of the words "recover land" in a limitation of actions context, and distinguished cases which seemed to be in opposition to the *Hester* and *Williams* cases. The Alberta Court of Appeal in *Turta* found it unnecessary to deal with the limitation argument.[44] In the Supreme Court of Canada the *dicta* of Egbert J. was not interfered with.[45]

It would appear, then, that although the *Irving* case seems near on its facts, an argument can be made that the action by WOC is to recover land, land of which it has been deprived, and under this interpretation of the Limitation of Actions Act, the proper period is ten years.

2. *If the right is a contractual right, what limitation applies?*

Even if it is conceded that the right is contactual in nature, there is an interesting issue whether the six year period runs from the date of the breach, 1972, or the date on which the plaintiff became aware of the breach, in 1977. The question is whether ss. 4(1)(c) and 4(1)(g) of the Limitations of Actions Act apply or s. 4(1)(e). These sections read:

> s. (4)(1) The following actions shall be commenced within and not after the times respectively hereinafter mentioned:
>
> (c) actions
>
> i. for the recovery of money, other than a debt charged on land, whether recoverable as a debt or damages or otherwise, and whether on a recognizance, bond, covenant

39. 28 Halbury's Laws (4th) 319.
40. [1919] I.R. 116.
41. [1907] 1 Ch. 713.
42. *Id.* at 730.
43. [1952] 5 W.W.R. 529 at 551-554.
44. [1953] 8 W.W.R. 609 at 629.
45. [1954] S.C.R. 427.

> or other specialty or on a simple contract, express or implied, or
> ii. for an account or for not accounting,
> within six years after the cause of the action arose.
> (g) any other action not in this Act or any other Act specifically provided for, within six years after the cause of action therein arose.
> (e) actions grounded on accident, mistake or other equitable ground of relief not hereinbefore specifically dealt with, within six years from the discovery of the cause of action ....

The argument in favour of the six year period, running from the 1972 surrenders, would be that the action is one in contract, for monies in damages. The opposing view is that the action here is for specific performance, an equitable relief, and thus the limitation period would run from 1977.

The question becomes interesting as it is not clear that the plaintiff would have been able to discover the breach earlier than he did. This might well seem unfair since if the sale of lands had not been noticed by the plaintiff until one year later, its action under s. 4(1)c would be barred before WOC was even aware of the breach.

The trial judge held that the wording of s. 4(1)(c) clearly embraced the WOC agreement since this was an action on a simple contract. Therefore s. 4(1)(e) was not applicable since the situation had been specifically dealt with in s. 4(1)(c)(i). It is regretable that the case did not go to appeal since, with all due respect to the learned trial judge, there is a valid argument to be made that an action for specific performance of an agreement such as this does not fall under s. 4(1)(c) and the plaintiff should not be barred from recovery on the remaining sections. It would seem the Act was specifically drafted to distinguish between actions for simple breach of contract and those in equity. One can only conclude that the area raises several legal issues which have yet to be finally laid to rest by a higher court.

IV. REMEDIES AND DAMAGES

Once liability has been found in a case involving a breach of the notice on surrender provisions of a gross overriding royalty agreement, the question arises as to the assessment of damages. Can specific performance be ordered if the defendant holds title to the lands in question through a repurchase or other conveyance? If not, at what date are damages to be assessed, and dealing with the speculative nature of oil and gas properties, how is a dollar amount to be set? Is it the value of the royalty or the value of the surrendered interest that is to be evaluated?

A. *Specific Performance*

In this case, it would seem that the plaintiff has been deprived of the right to have an assignment of the defendant's interest in oil and gas leases. If the defendant could convey that title, it would seem that equity should rise to the occasion to allow a grant of specific performance, assuming none of the bars to specific performance are present.[46]

In this case, GNOL had not reacquired any interest in the one section in regards to which Mr. Justice Patterson had to deal with damages, and therefore, the judgment did not deal with this situation.

However, this very dispute was the basis of the case of *Masai Minerals*

46. For a discussion related to the rules of equity and specific performance, as opposed to damages, *see* 1 *Chitty on Contracts* (24th ed. 1977) 775.

v. *Heritage Resources Ltd.*.[47] There, the plaintiff had an option for assignment on surrender and the defendant had reacquired the lands in question subsequent to their surrender. The court in that case found that the plaintiff was limited to the value of its royalty payments. Although the plaintiff was requesting assignment of the leases, it was held by the court that damages would suffice. The court based that assessment by finding that the reassignment clause was in the contract only to protect the royalty. The court found that had the defendant not recovered the lease, the plaintiff would be limited to damages. To allow the plaintiff more than damages where the defendant had reacquired the lease to reinstate the situation as it had been, would be unjust.

One has to question the logic and reasoning behind this decision. The court tends to ignore the right on surrender clause in its own right by viewing it solely as a means to enforce the royalty. This approach seems questionable. Second, the court limits the plaintiff to receiving, at best, a royalty interest from the agreement. Clearly in that situation what the plaintiff lost was not only a royalty, but also the chance to acquire the leasehold interest itself.

In the Saskatchewan Queen's Bench, MacPherson J. in *Masai* held that if a royalty owner with a reassignment clause knows that the other party is about to surrender, the royalty owner will have an action in specific performance or damages and perhaps for injunction. However, the learned judge goes on to say that once the lease is surrendered the royalty interest is gone and the royalty owner is limited to an action in damages. No authority was given for this statement.

Mr. Justice McPherson looked at the action for specific performance and gave damages. He felt it unjust to award more than the royalty, stating equity would not intervene where a common law remedy was adequate. With respect, the writer would disagree, since the judge seems to be overlooking the point that the surrender of lease gave the plaintiff the right to have the lease itself in addition to a royalty interest.

The problems inherent in this question of reassignment are well discussed by Paul Eaton Jr. in an article appearing in The Rocky Mountain Law Institute publication,[48] and the article was considered by the trial judge in *Masai*.[49]

The Court of Appeal[50] dismissed the *Masai* appeal and found the trial judge's reasoning to be correct. Mr. Justice Hall, giving reasons for the court, indicated the trial judge exercised his discretion properly in awarding damages rather than ordering specific performance. However, the Court of Appeal in *obiter dicta* doubted that the exercise of the discretion between damages and specific performance ever came into question. Mr. Justice Hall stated that once the defendant reacquired the lease, the right of action for failure to offer disappeared, and the plaintiff was entitled only to the royalty and a right of assignment upon its disposal.

It is the writer's submission that it may have been preferable to have a decision by the Supreme Court of Canada on this matter,[51] since it would

47. [1979] 2 W.W.R. 352 (Sask. Q.B.); *affd* [1981] 2 W.W.R. 140 (Sask. C.A.).
48. Paul W. Eaton, "The Reassignment Provision — Meaningful or Not?" (1975) 20 *Rocky Mountain Law Institute* 601.
49. *Supra* n. 47 at 358.
50. *Supra* n. 47.
51. The Supreme Court of Canada refused to grant leave to hear an appeal.

seem that equity should dictate specific performance if the lands are reacquired by the defendant. The two issues to be considered are the difficulty of assessing damages in this situation, as will be dealt with below, and the fact that in oil and gas properties it is often the assembly of a number of leases or interests that gives value or the "go-ahead" on a certain drilling proposal. In this type of situation, damages may not give sufficient remedy to compensate the plaintiff.

B. *The Question of Damages*

Leaving behind the question of the possibility of specific performance, and turning to the damage question, once again one is looking at an area where the answers are not clear. It is somewhat trite to reiterate that the purpose of damages is to put the plaintiff in the position in which it would have found itself had the contract been performed. These were not lands on which the plaintiff had in the past received royalty payments. The courts would be looking to put the plaintiff in the position he would have been had he had notice of and taken an assignment of the lands in question.

First, the problem of appropriate time for the assessment of damages arises. It would seem there is a clear line of case authority on which to argue that the relevant time is the time of trial rather than the time of the breach. It was held in *Wroth* v. *Tyler* that when an action is brought in specific performance, but damages are awarded in lieu thereof, the date of the assessment of damages should be the date of the trial of the action. In that case, Megarry J., in the Chancery Division, held that where the plaintiff had a proper claim in specific performance, the Chancery Amendment Act 1858 allowed assessment of damages past the date of the breach. He further held that the date of trial would be appropriate for determining damages, since damages were intended to be a substitute for specific performance.

This case and the principles therein have been followed in Canada. In *Metropolitan Trust* v. *Pressure Concrete*,[53] Holland J. of the Ontario High Court considered a case where specific performance was not allowed, but damages in lieu thereof were assessed. The *Wroth* case was approved, and damages ordered to be assessed to the date of judgment. More recently, the Alberta District Court in *E.J.H. Holdings Ltd.* v. *Bougie*[54] allowed damages in lieu of specific performance and held that the statute relied on in the *Wroth* case was applicable in Alberta due to the provisions of section 34(11) of The Judicature Act. The Court went on to allow damages assessed on the value of the property as at the date of trial. In the case of *306793 Ontario Ltd.*,[55] the Ontario Court of Appeal followed *Wroth* and assessed damages in lieu of specific performance as the value of the property at the date of trial, in an action by a purchaser on a default by a vendor.

The argument in contradiction to the rule in *Wroth* would be that as soon as the plaintiff became aware of the breach of the contract, he was in a position to mitigate damages and that the date the plaintiff became aware is relevant. There is some authority in Alberta that the relevant

52. [1973] 1 All E.R. 897.
53. [1973] 3 O.R. 629.
54. [1977] 3 Alta. L.R. (2d) 244.
55. *306793 Ontario Ltd.* v. *Rimes* (1980) 25 O.R. (2d) 79.

date would be the date on which the breach should have come to the plaintiff's attention had he been using due diligence.[56] There is also American authorities that the appropriate date should be the date on which the lease terminates.[57] However, in the WOC case, Mr. Justice Patterson followed the *Wroth* case and held that the date of valuation was at the date of trial.

Having determined the date of assessment of damages, a myriad of questions open to which there are very few guidelines for counsel involved in these type of cases. Part of this problem involves the difficulties of obtaining the expert evidence of engineers and geologists in assessing oil and gas reserves on partially or non-tested land. The other concerns arise from non-evidentiary problems such as: is the after tax value or the pre-tax value considered? Is the defendant to receive any credit for amounts spent on drilling or developing the land? Is the defendant liable for 100 per cent of the value of the property or only proportionately to the interest the defendant or defaulting party held?

As to the first question, the problems and intricacies of evaluation are best left to textbooks and articles dealing with the presentation of expert evidence. In the WOC case, professional engineers were called who gave conflicting evaluations and bases for their assessments. The trial judge looked at a figure using a risk factor of .8 and a discount of 10.8 and assessed damages at $927,860. Further, the court held that the before tax rather than after tax figures were to be used. The judge commented that the experts' evidence which he accepted may seem "arbitrary" but that[58]

> as the whole issue is highly speculative and dependent on fluctuating costs, market price, etc., it is not a problem which can be resolved with accuracy. At best it is a value which the land would probably have to a well-informed person in the industry. Brusset refers to it as "educated guesswork' but points out that recovery procedures will improve in the future and that overall production in the field can be expected to increase.

The situation is one where perhaps the *Penvidic*[59] case applies, allowing the court to do the best it can based on expert evidence.

The WOC case, though, at least clears some ground for those faced with arriving at a damage figure in this fact-situation. Before tax values should be assessed.[60] The argument that the defendant, as a 50 per cent holder in the lease (Union holding the other 50 per cent through the farm-out), should only pay one-half the value also failed. Thus, when the breach caused the loss of all the lands, the plaintiff should be compensated on that

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56. *Russ Burns Petroleum Consultants Ltd.* v. *Union Oil Company of Canada Ltd. et al.* (1979) 10 Alta. L.R. (2d).

57. *See Tenneco Oil Company* v. *Gaffney* 369 F. 2d 306 (10th Cir. 1966); *also Gladys Belle Oil Co.* v. *Turner* 12 S.W. 2d 847 (Tex. Civ. app. 1929). Other cases are discussed by Eaton in his article, *supra* n. 45.

58. *Supra* n. * at 735. The "Brusset" referred to was Mr. Michael Brusset, the engineer called as an expert by the plaintiff.

59. The Supreme Court of Canada has given guidance on the issue of damage claims which may be difficult to ascertain, in the case of *Penvidic Contracting Co. Limited* v. *International Nickel Company of Canada*, [1976] 1 S.C.R. 267. In that case, Spence J., giving the judgment of the Court at 278 - 280, deals with the necessity for the Court to make an assessment that would place the wronged party in as good a position as if the contract had been performed. The Court held that the Judge hearing the case must do the best it can, assisted by expert witnesses.

60. This position is supported in *Faunatlantic Ltd.* v. *Province of New Brunswick* (1977) 20 N.B.R. (2d) 128 at 158-160.

basis, regardless of the interest held by the defendant.

The judgment is not clear on how one is to deal with capital expenses on the property. The plaintiff's expert, whose values were ultimately accepted, did take into consideration capital costs on some sections and not on others. It is not clear from the judgment what route is preferable to the court. A similar question was considered in the case of *306793 Ontario Ltd. in Trust* v. *Rimes*,[61] where the Ontario Court of Appeal held that it was not proper to deduct any charge which the purchaser would have had to pay from the date of breach to the date of trial where damages were allowed in lieu of specific performance. The reason given by the Court was that his remedy would put the purchaser in the position as if the contract were performed, but give the added benefit to the vendor that it could hold the land for the time period between the breach and the trial. That reasoning is attractive. However, the very large amount of dollars that often go into drilling wells on land is considerable, and it will be interesting to see how these matters are dealt with should another case of this type arise, especially if substantial sums were paid to develop the land before it was surrendered by the defendant.

The defendant, in arguing in relation to damages, encouraged the court to speculate as to what the plaintiff would have done with the lands had notice been given and the plaintiff taken an assignment. In the past, WOC had usually sold or transferred interests which it took by assignment. Also, it was likely WOC did not have the cash to finance drilling and development of the lands by itself. The trial judge steered clear of these questions and assessed damages without considering them.

The defendant argued that following the *Masai* case, merely the royalty value on the relevant sections should be considered. This was not followed by the trial judge, which may lend some question as to the effect of the *Masai* decision outside of its facts. It is interesting to note that there is an American case, *Walton* v. *Atlantic Richfield Company*,[62] which would also support an assessment of damages using the value of the overriding royalty.

Given the fact that the *Masai* case and the WOC case come to very different conclusions as to damages, although recognizing the difference as to whether the defendant reacquired the lease, it would seem that the area remains open for a higher court to examine the issue. Suffice to say that in the meantime it may be prudent for lawyers drawing up royalty agreements to consider the inclusion of a clause in regard to the assessment of damages if there is a breach of the notice provision.

V. CONCLUSION

The WOC case raised a number of issues pertinent to the oil and gas industry, and especially to geological or other consultants who take overriding royalties with reassignment clauses. Two of these issues, the necessity of written notice and the potential defence under the Real Estate Agents Licensing Act, were clarified by the court. The question of the relevant limitation period and the question of assessing damages both get into complicated realms in which law is still not clear. With neither the *Masia* nor the WOC cases under appeal to a higher court, it will take

61. *Supra* n. 55.
62. 501 P. 2d 802 (Wyo. 1972).

another case of this kind to obtain a clarification by the Supreme Court of Canada. Although the disputes reaching the court may be rare, these issues do arise with some frequency in the oil patch. The question of damages and remedies may be very relevant to the quantum of out of court settlements.