RECENT JUDICIAL DECISIONS OF INTEREST TO OIL AND GAS LAWYERS

DON MACDIARMID,* JO'ANNE STREKAF AND J.P. PHAM**

The purpose of this article is to provide a brief review of recent Canadian judicial decisions of interest to oil and gas lawyers. The authors have surveyed Canadian case law in various areas including contract, creditors' rights, employment, royalties, split title, surface rights, environmental and taxation.

Le but de cet article consiste à donner un bref aperçu des récentes décisions judiciaires canadiennes pouvant intéresser les avocats travaillant dans le secteur pétrolier et gazier. Les auteurs ont passé en revue la jurisprudence canadienne dans divers domaines dont les contrats, les droits des créanciers, l'emploi, les redevances, les titres divisés, les droits de surface, l'environnement et l'impôt.

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* Don MacDiarmid, Partner, Osler, Hoskin & Harcourt LLP, Calgary, Alberta.
** Jo'Anne Strekaf, Partner and J.P. Pham, Associate, Bennett Jones LLP, Calgary, Alberta. The authors would like to thank Jason Roth and Kelly Caruk for their dedicated assistance in the preparation of this article.

I. ADMINISTRATIVE LAW

A. *BP CANADA ENERGY COMPANY V. ALBERTA (ENERGY AND UTILITIES BOARD)*[1]

1. BACKGROUND

In matters before tribunals there is often an issue regarding the adequacy of the reasons given by the tribunal to justify its decision. The following case addresses this issue, as well as the issue of tribunals relying on evidence provided by the tribunal's staff.

2. FACTS

This case involved an application by BP Canada Energy Company (BP), Paramount Resources Ltd. (Paramount) and Devon Canada Corporation (Devon) for leave to appeal a decision by the respondent Alberta Energy and Utilities Board (the Board).

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1 (2003), 27 Alta. L.R. (4th) 108 (C.A.).

The applicants hold certain lease rights to natural gas in a particular geographical area. The Board held hearings to consider applications from various parties related to natural gas production from 145 gas wells in the subject area that were also prone to bitumen production. The matter at issue was whether natural gas production was harmful to future bitumen production in the vicinity of the gas wells.

The Board decided that natural gas production presented a high risk in some areas and a lesser risk in others. The Board ordered the shut-in of 39 wells and denied production applications for 21 wells. The applicants were owners of the wells that were ordered shut-in.

The three applicants sought leave to appeal on various overlapping grounds of appeal. All of the applicants argued that the Board failed to provide proper reasons for its decision.

Devon and Paramount argued that the Board erred in law: (i) in its use of staff experts; and (ii) by receiving evidence in the absence of the applicants, both during and after the hearing. They submitted that these actions breached the *audi alteram partem* rule. While BP did not directly argue the improper use of Board staff, it joined Devon and Paramount in seeking leave on the basis of inadequate reasons. That argument was based, in part, on the fact that the Board's conclusions, as reflected in its written reasons, went beyond the mapping and opinion evidence entered at the hearing. All applicants argued that the Board failed to give any explanation for the discrepancies between the expert opinion and interpretive evidence adduced at the hearing on the one hand and the conclusions the Board ultimately reached on the other.

BP also raised its own unique ground of appeal. At the hearing, PanCanadian Energy Corporation (PanCanadian) withdrew its application seeking the shut-in of two of BP's wells. This occurred after all the evidence was submitted but before final arguments. BP alleged that the Board breached the rules of natural justice by shutting-in those wells without providing specific notice of its intention to deal with the wells, notwithstanding the withdrawal of PanCanadian's application. As a result of this lack of notice, BP argued that it did not present argument with respect to those wells.

3. DECISION

The Alberta Court of Appeal allowed the application. The Court found that the applicants had demonstrated a serious arguable issue as to the Board's failure to provide an adequate explanation as to why it reached the conclusions it did. The Court cited *Lor-al Springs Ltd. v. Ponoka (County of) Subdivision and Development Appeal Board*,[2] where Picard J.A. agreed with the statement that "the test for determining whether the reasons given by a delegate are adequate in law is whether they show why or how or on what evidence the delegate reached the conclusion."[3] The Court found that it was at least a serious, arguable issue that the Board's decision failed to meet this standard.

2 (2000), 271 A.R. 149 (C.A.).

3 *Ibid.* at para. 15, citing David P. Jones & Anne S. de Villars, *Principles of Administrative Law*, 2d ed. (Toronto: Carswell, 1994) at 307.

The Court found that there was also a serious arguable issue as to the relationship between the staff and the Board panel hearing an application. The Court concluded that, among other things, the examination by the Board or its staff of core, logs and other data not in evidence at the hearing raised a serious question going to loss of jurisdiction, and the fact that the applicants were not present for those examinations contributed to the issue's seriousness.

Finally, the Court found that it was not clear that the Board had complied with the statutory notice requirements merely by relying on the fact that BP was aware that its two wells were previously the subject of a shut-in application that was withdrawn before the conclusion of the hearing. Moreover, the fact that the Board did not give notice when BP failed to address the two wells in final arguments, and yet commenced to order the shut-in of the wells, resulted in the Court's decision that the applicants had demonstrated a serious, arguable issue as to whether the Board complied with the statutory notice requirements.

The Court granted leave to appeal the Board's decision on the following terms:

(i) BP, Devon and Paramount were granted leave to appeal on the question of whether the Board failed to furnish adequate reasons for its decision;
(ii) Devon and Paramount were granted leave to appeal on the question of whether the Board erred in law or jurisdiction in any aspect of its use, or disclosure of use, of Board staff;
(iii) Devon and Paramount were also granted leave to appeal on the issue of whether the Board erred in law or jurisdiction by taking into account any collateral considerations or evidence; and
(iv) BP was granted leave on the question of whether the Board committed an error of law or jurisdiction in failing to provide BP with adequate notice that its wells remained subject to a potential shut-in order after the Board granted the withdrawal of PanCanadian's application in respect of the shut-in of those wells.

4. COMMENTARY

The Court has given the applicants a broad range of grounds upon which they may appeal the Board's orders relating to their respective natural gas wells. The Court granted leave to challenge whether the Board: (i) provided adequate reasons for its decisions; (ii) acted appropriately in considering evidence collateral to that presented in the presence of the applicants (whether from the Board's own staff experts or otherwise); or (iii) erred in continuing to consider for a shut-in order the two BP wells for which PanCanadian had withdrawn its application for shut-in, without giving BP specific notice that such wells remained under consideration for shut-in.

This case is interesting not only for the administrative law issues it addresses but also because of the wide attention that has been gained by the Board's efforts to balance the diverging interests of natural gas rights holders and bitumen rights holders. Since the decisions of the Board to order the shut-in of gas wells can have extremely serious economic consequences for the natural gas rights holder, it seems appropriate that the Court hold the Board to a very high standard both as to the manner in which it formulates its decisions and as to how it communicates them to affected persons. If the applicants are ultimately to be denied the right to produce the natural gas for which they have expended considerable funds and efforts to secure, it seems only just that any such denial must only occur after the applicants have: (i) had an opportunity to hear and respond to all evidence being considered by the Board; and (ii) received a cogent explanation as to why the rights they have paid for are now being postponed by an instrumentality of the government that originally sold them.

There have been a number of ongoing developments in this case and related cases involving both Alberta Energy and Utility Board re-hearings and pending appeals at the Court of Appeal that are beyond the scope of this article due to timing issues.

II. CONFLICT OF LAWS

A. *BEALS V. SALDANHA*[4]

1. BACKGROUND

The diminishing size of Canadian oil and gas discoveries, coupled with the aging of existing reservoirs, has prompted oil and gas companies to focus their exploration and development efforts on opportunities abroad. The increasing internationalization of oil and gas operations gives rise to multi-jurisdictional activities that can lead to disputes involving a conflict of laws.

2. FACTS

The appellants, residents of Ontario, sold a vacant lot in Florida to the respondents for US$8,000. A dispute arose as a result of that transaction and in 1986 the respondent sued the appellants in Florida. The appellants failed to defend the action and the respondents were awarded US$260,000 in damages. On the advice of Ontario legal counsel, the appellants took no steps to have the judgment set aside or to appeal the judgment in Florida. The damages were not paid and an action was commenced in Ontario to enforce the Florida judgment, which had grown to approximately CDN$800,000.

3. DECISION

Justices Gonthier, Major, Bastarache, Arbour and Deschamps and McLachlin C.J.C. for the majority enforced the Floridian judgment. The Court held that the "real and substantial connection" test set out in *Morguard Investments Ltd. v. De Savoye*,[5] which until now has only been applied to interprovincial judgments, should apply equally to the recognition and enforcements of foreign judgments. The test requires that a significant connection exist between the cause of action and the foreign court. The majority determined that international comity and the prevalence of international cross-border transactions and movement call for a modernization of private international law, which would include the application of generally accepted principles of conflicts of laws.

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4 [2003] 3 S.C.R. 416 [*Beals*].

5 [1990] 3 S.C.R. 1077.

The majority also concluded that the common law defences available during interprovincial enforcement actions of fraud, public policy and lack of natural justice should apply equally to actions involving the enforcement of foreign awards.

The defence of fraud provides that neither foreign nor domestic judgments will be enforced if obtained by fraud. However, the desire to avoid the relitigation of issues has led the courts to treat the defence of fraud narrowly and to limit the type of evidence for fraud that can be pleaded in response to a judgment.

The denial of natural justice can also form the basis of a challenge to a foreign judgment and, if proven, will allow the Canadian courts to refuse enforcement. The Court held that the burden of alleging unfairness in the foreign legal system rests with the defendant in the foreign action. A condition precedent to the defence is that the party seeking to impugn the judgment must prove, to the civil standard, that the foreign proceedings were contrary to Canadian notions of fundamental justice and must satisfy the domestic court that the foreign courts have applied minimum standards of fairness. The minimum standards of fairness include ensuring that the defendant was granted a fair process in which there was judicial independence, adequate notice and the opportunity to defend.

Finally, the defence of public policy prevents the enforcement of a foreign judgment that is contrary to the Canadian concept of justice. The public policy defence turns on whether the foreign law is contrary to the Canadian view of basic morality. However, the Court held that the public policy defence is not meant to bar enforcement of a judgment entered by a foreign court with a real and substantial connection to the cause of action for the sole reason that the claim in that foreign jurisdiction would not yield comparable damages in Canada. Thus, the Court held that the sums involved in a foreign award, even if grossly excessive by Canadian standards, are not by themselves a basis for refusing to enforce a foreign judgment in Canada.

4. COMMENTARY

This recent decision of the Supreme Court of Canada expands upon the principles that Canadian courts should apply when faced with the enforcement of court awards issued in foreign jurisdictions. Since the Canadian courts will enforce foreign awards in accordance with the principles established in *Beals*, Canadian lawyers, and the corporations that they represent, should ensure that they approach and defend court actions commenced in foreign jurisdictions with the same seriousness that they would approach domestic court actions. A foreign action should not be disregarded or dismissed on the presumption that any award made in the foreign jurisdiction will not be enforceable in Canada without a careful analysis as to these expanded principles of recognition.

III. CONTRACTS

A. *HUSKY OIL OPERATIONS LTD. V. LEDCOR INDUSTRIES LTD.*[6]

1. BACKGROUND

This case illustrates the importance of reducing oral amendments to agreements into writing.

2. FACTS

Husky Oil Operations Ltd. (Husky) entered into a contract with Ledcor Industries Ltd. (Ledcor) for the construction of a 62 km pipeline. The pipeline was intended to carry sour gas. Under the terms of the contract, Ledcor was to be paid a fixed cost of $14 million for construction of the entire pipeline and that construction was to be completed by 31 March 1998.

The project experienced complications from the onset. Husky was delayed in acquiring the necessary regulatory approvals for the pipeline. This resulted in a delay of two to three weeks before Ledcor could begin work on the project. Furthermore, Husky could not acquire the necessary temporary bridging permits required for crossing three major rivers along the pipeline right-of-way. This inability to bridge the rivers temporarily meant that equipment had to be moved large distances to get from one side of the water to the other. Additionally, both parties experienced difficulties crossing minor streams that resulted in significant changes to the contract. The parties began discussing alterations to the compensation clause of the contract early on in the project.

Ledcor and Husky agreed that Ledcor could utilize a mechanical welding process aimed at improving the pipeline's rate of progress compared to the manual welding process contemplated in the contract. As the pipeline was a sour gas pipeline, Husky had insisted on stringent welding requirements. Variations in the type of welding methods Ledcor utilized and alterations imposed by Husky to the welding requirements resulted in a dramatic increase in the failure rate of inspected welds. Welds that failed inspection had to be repaired, adding cost and delay to the completion of the project. Both parties agreed that these welding failures were due to the project itself as opposed to negligence on behalf of Ledcor.

Further complicating matters, due to Ledcor's labour agreements, Ledcor could not keep employees on the project past 31 March 1998. Both parties made it clear at the beginning of contractual negotiations that they did not anticipate that the project would continue past this date. However, by late February both parties realized the project would not be completed on time due to the above mentioned difficulties. Both Ledcor and Husky worked cooperatively to bring a subcontractor, Midwest Management Ltd. (Midwest), onto the project to continue the work Ledcor was unable to finish. By 31 March 1998, Husky had paid approximately $11.5 million to Ledcor under the contract. Ledcor's total invoice for the project was just over $18 million. Additionally, Husky paid Midwest approximately $12.6 million to finish

[6] [2003] A.J. No. 1111 (Q.B.) (QL).

work on the pipeline and $1.2 million to other contractors to perform the required cleanup work. Both parties agreed that the high number of welding repairs required, the inability to build temporary bridges across waterways and Husky's failure to get regulatory approval at the specified time resulted in delays to Ledcor's performance under the contract.

Husky brought a claim against Ledcor for damages and Ledcor counterclaimed for the unpaid portion of its account.

3. DISCUSSION

In reaching its decision, the Court of Queen's Bench considered many aspects of the project and their effects on the ongoing negotiations between Ledcor and Husky regarding amendments to their initial contract. The Court ultimately concluded that the decision to utilize mechanized welding as opposed to manual welding was made and agreed to by both parties. The changes to the scope of the project were significant and caused ongoing negotiation between the two parties. In its final accounting, the Court found that Husky was focused on getting the project completed while Ledcor wanted to make sure it would be fairly compensated for its work on the project. Ledcor was determined not to bear the risk of a lump sum contract when the project scope was changing on a nearly daily basis. The Court further found evidence that Husky failed to track properly the cost figures for the project until the project had been completed and an audit was performed.

When considering the changing welding specifications, the Court noted that Husky relaxed the welding criteria three times throughout the project but additionally increased the welding specifications regarding certain types of welds at various points in the contract. The Court found that these changes to the welding specifications were important when determining the context of the contractual amendments. The introduction of these increased requirements equated to an amendment to the original written contract.

In addressing Ledcor's labour issues, the Court noted that Ledcor's labour difficulties merely added evidence to the fact that Ledcor could not work past the final completion date noted in the written contract, but did not materially affect the parties' original intentions to have the project completed before spring breakup.

Once it became clear to both parties that Ledcor would not be able to complete the contract by March 31, the services of Midwest were employed. The evidence presented made it clear that the parties did not discuss who would be responsible for Midwest's completion costs of the project. Midwest signed onto the project on a cost plus and fee arrangement basis with an initial estimate of $5 to $6 million. Midwest's final billing at the end of the project equated to $12 million. As with Ledcor, Husky experienced litigation with Midwest regarding who would cover the cost of repairing welding to Husky's specifications.

The Court found that there was ample evidence that both Husky and Ledcor intended to alter the written contract from a fixed fee of $14 million to a cost plus basis. Unfortunately, the Court found that the parties did not come to a consensus on what exactly would constitute a "cost." After discussion of what terms in the contract would continue to apply post-amendment by the parties, the Court found that while the compensation was changed to cost plus, the requirement in the written contract that Ledcor be responsible for welding repairs necessary to complete the project would remain in force.

The Court concluded that the parties had not vacated the original contract but merely negotiated amendments to the written form. The changes to remuneration methods did not override the written requirements in the original contract regarding the repairing of welds, worker safety issues, *etc.* The Court noted that Husky could not be entirely successful in its claim that the delay of the project was purely due to Ledcor's inability to maintain welding specifications. Husky itself had contributed to the delays in a number of manners and the project encountered delays not anticipated by either party.

The Court then went on to consider the actual damages payable from Ledcor to Husky. The Court considered a number of reports, comments and calculations relating to the repair of the defective welds, bringing a third-party contractor on-site, disrupting work at various times throughout the project, cleanup costs and consequential costs due to the late completion of the project. Ultimately, the Court awarded damages to both Husky and Ledcor arising from under the contract with a net result of Husky owing Ledcor a sum of $1.5 million.

4. COMMENTARY

This case illustrates in graphic detail the consequences of oral amendments to contracts that are not later followed up by written documentation. When project scopes, complications and compensation schemes are altered through the course of a project, it is imperative for both parties that these amendments be reduced to writing. Failure to do so will result in high litigation costs for both parties.

When the contract was initially negotiated, the magnitude of the project (62 km pipeline), the complexity of the undertaking (sour gas service, winter construction, river crossings) and the timing imperative (Ledcor's need to release its employees from the project by 31 March 1998) should have made it obvious to both parties that the lump sum $14 million contract would almost certainly be under pressure from a myriad of changed circumstances. Even as this in fact occurred as the performance of the contract unfolded, the parties either did not discuss or did not reduce to writing how many very material changes would be reflected in the pricing, timing and scope of services that Ledcor was obligated to provide. As a result, the parties went to great expense and waited five years to have the Court write a contract that almost certainly satisfied neither of them.

It is not unusual for parties to a construction contract to disagree on the implications of a particular change in the scope of the services that are to be provided under that contract. It is unusual, as occurred here, for them to carry forward with the contract to its conclusion in the face of so many significant changes, without either discussing the impact of or reducing to writing their agreement on any change. No matter how unpalatable scope change negotiations may be, they do not taste any better when served cold. We understand from counsel that this case is under appeal.

B. *TRANSCANADA PIPELINES LTD. V. POTTER STATION POWER LIMITED PARTNERSHIP*[7]

1. BACKGROUND

Indemnities provide an important reassurance under many contracts. This case illustrates why it is necessary for parties to make these clauses as clear as possible if they wish to avoid costly litigation.

2. FACTS

Potter Station Power Limited Partnership (Potter) entered into an agreement with TransCanada Pipelines Limited (TransCanada) whereby Potter would purchase waste heat produced by one of TransCanada's compressor stations. In addition to this purchase agreement, the parties entered into an indemnification agreement, which required the parties to indemnify each other in certain situations.

Following construction of the Potter generating facility, the land on which the TransCanada compressor station was situated began to subside. TransCanada argued that Potter drawing too much water from an underground aquifer caused the subsidence and TransCanada sued Potter under the indemnity agreement. The indemnity provided that Potter would indemnify TransCanada from all liability suffered by TransCanada arising out of the construction of the plant, negligent or wilful misconduct of Potter and a breach by Potter of any of the terms of the agreement, except to the extent that such losses or damages result from negligence or wilful misconduct of TransCanada.

The motions judge determined that the wording of the indemnity, in the context of the construction of the plant being so close to TransCanada's compressor station, took on a broader meaning in that Potter would indemnify TransCanada for any losses arising from the operation of its facility and not just against third-party claims.

Potter's insurer appealed the decision on the basis of the *contra proferentum* principle (TransCanada had drafted the agreement) and claimed that the motions judge failed to find, at a minimum, that the indemnity was ambiguous.

3. DECISION

The Court of Appeal disagreed with Potter's insurer's position as previously stated. The Court held that because the motions judge did not find the indemnity to be ambiguous, it did not need to consider the *contra proferentum* rule.

The Court of Appeal found that the motions judge was correct, in the context surrounding the indemnity, that the indemnity was fully capable of being interpreted as extending to damages suffered by TransCanada directly and not just those for which TransCanada had to indemnify third parties.

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7 (2003), 172 O.A.C. 379.

4. COMMENTARY

The fact that TransCanada had to pursue this matter to court further illustrates the necessity for parties to pay careful attention to the drafting of indemnity clauses. Parties should always clearly express the circumstances under which the indemnity is to apply.

IV. CREDITORS' RIGHTS

A. *MSI ENERGY SERVICES V. D&K HORIZONTAL DRILLING (1998) LTD. (TRUSTEE OF)*[8]

1. BACKGROUND

In bankruptcy cases, the parties will often dispute the ownership of interest earned on money paid into court prior to judgment. The following case illustrates that such interest will belong to the parties legally entitled to any remaining principal left from the money originally paid into court.

2. FACTS

The Saskatchewan Court of Appeal had held in the previous decision of *D&K Horizontal Drilling (1998) Limited (Trustee of) v. Alliance Pipeline Limited*[9] that money paid into court in relation to a court order regarding builder's liens filed by subcontractors, but originally owed to the general contractor, could not be claimed by the trustee of the general contractor, D&K Horizontal Drilling Limited (D&K), as the money was no longer the property of D&K.

Alliance Pipeline Limited (Alliance) engaged D&K as a contractor to build sections of a pipeline. D&K eventually went into bankruptcy and a number of their subcontractors placed liens on the Alliance pipeline. Alliance paid $1.2 million into court to satisfy a number of competing lien claim actions. Following the payout of the sum, there was a total of $83,000 in interest remaining in the account. The lien claimants asserted that they were entitled to the sum of interest as the money that generated the interest did not belong to D&K, whereas D&K's trustee felt entitled to the $83,000 in interest in the account as it was derived from money related to an account owing to it.

3. DECISION

The Saskatchewan Court of Queen's Bench held that both D&K and Alliance were entitled to share in the interest amounts based on a previous court decision that held that D&K and Alliance were entitled to any remaining principal in the account. The trustee for D&K was entitled to the interest earned on the amount of money Alliance had originally paid into court until such time as the liens had been paid out of court, as the contractual claims to interest of the lien claimants would constitute an unsecured creditor claim in terms of the bankruptcy.

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8 [2004] 3 W.W.R. 566 (Sask. Q.B.).

9 [2003] 4 W.W.R. 29 (Sask. C.A.).

4. COMMENTARY

This case clarifies that in the situation where money has been paid into court to satisfy builders' liens against property, the interest generated from such funds belongs to the parties originally paying the money into court and not the lien claimants.

B. *RE GAUNTLET ENERGY CORP.*[10]

1. BACKGROUND

Courts have often been called upon to determine what forms of property are caught by the Alberta *Personal Property Security Act.*[11] In this case, the collector of seismic data tried to argue that seismic data was not in fact personal property, but rather constituted a *sui generis* form of property to which the *PPSA* does not apply.

2. FACTS

Gauntlet Energy Corporation (Gauntlet) entered into three proprietary agreements for the collection of seismic data with Pulse Data Inc. (Pulse) on 20 December 2002, 25 February 2003 and 20 December 2003. All three contracts provided that "[u]pon final payment as set out in Schedule 'B', Ownership of the data shall pass to the Purchaser."[12] At no time did Pulse register a security interest in the Alberta Personal Property Registry (PPR).

On 17 December 2001, Gauntlet had granted a security interest on all the debtor's present and after-acquired property and a debenture to the Alberta Treasury Branch (ATB) in exchange for a revolving production loan facility. The ATB had received both the General Security Agreement and debenture from a predecessor company, Scorpion Energy Corporation. The ATB had properly registered its security interest on the Alberta PPR on 10 July 1998. At the time of trial there was $42,672,803.07 outstanding on the loan.

Gauntlet entered into *Companies' Creditor Arrangement Act*[13] proceedings on 17 June 2003. The monitor appointed under the *CCAA* sought to sell the data Gauntlet received from Pulse to pay off Gauntlet's creditors in priority under the *PPSA*. Pulse took the position that the seismic data was not personal property and that therefore Pulse's claim to any benefit derived from the sale of the data was not subject to the *PPSA*.

At trial Gauntlet argued that the seismic data collected by Pulse was in fact intangible personal property and as such was subject to the creditor priority scheme in the *PPSA*. Gauntlet further contended that Pulse's failure to register its security interest invalidated any purchased money security interest priority that Pulse may have enjoyed.

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10 (2003), 336 A.R. 302 (Q.B.).
11 R.S.A. 2000, c. P-7 [*PPSA*].
12 *Supra* note 10 at para. 7.
13 R.S.C. 1985, c. C-36 [*CCAA*].

Pulse argued that the seismic data it collected for Gauntlet was not in fact personal property, but rather was confidential information and as such was *sui generis* and therefore beyond the scope of the *PPSA*. Pulse further argued that as Gauntlet had not completely paid Pulse for the data, the data rightly belonged to Pulse.

The ATB sided with Gauntlet in its arguments before the Court that the seismic data sales agreement were conditional sales agreements as defined under the *PPSA* and that the ATB registered security interest took priority over Pulse's unperfected security interest.

3. DECISION

The Alberta Court of Queen's Bench concluded that the information contained in the Pulse's seismic data files could, in fact, be considered intangible personal property. As support for this conclusion, the Court noted that since the oil and gas industry considers seismic data something capable of being bought and sold, it has propriety rights attached to such data and refers to such agreements as "Proprietary Agreements." The Court concluded that the agreement between Gauntlet and Pulse was in fact a conditional sales agreement. As such, the agreement would qualify as a purchase money security interest had Pulse not failed to perfect such interest. Given that Pulse had failed to perfect its interest, the ATB's perfected interest was in fact superior to that of Pulse.

4. COMMENTARY

This case serves as yet another reminder to counsel that in circumstances where a client is entering into an agreement that in any way could be considered a conditional sales agreement under the *PPSA*, it is imperative for that interest to be registered in the PPR.

V. BUILDERS' LIENS

A. *CAMBRIAN BLASTING CO. LTD. V. TRICAN WELL SERVICES LTD.*[14]

1. BACKGROUND

Questions of priorities between builders' lien claimants and other security holders often arise in the event of a receivership.

2. FACTS

Cambrian Blasting Co. (Cambrian) provided drilling and blasting services to Hanson Lake Sand Corp. (Hanson) for five quarry dispositions leased by Hanson from the Crown. By 31 August 2001, Hanson owed Cambrian $103,131.95. On 16 October 2001, Cambrian registered a builder's lien with Saskatchewan Energy and Mines.

In July 2000, Hanson obtained loans in the amount of $1,350,000 from Trican Well Services (Trican) and $1,000,000 from the Saskatchewan Opportunities Corporation

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[14] (2003), 237 Sask. R. 289 (Q.B.).

(SOCO). In return, Hanson granted security agreements over all present and after-acquired property, including the five quarry leases noted above.

Hanson defaulted on its loan to Trican. As a result, Trican initiated an action against Hanson in April 2002 and applied to the Court of Queen's Bench of Alberta for the appointment of a receiver-manager of Hanson's assets. By 1 May 2002, when Ernst & Young Ltd. (the Receiver) was appointed as receiver-manager, Hanson had accumulated debts owing to Trican and SOCO totaling \$1,695,616 and \$1,156,311, respectively.

The Receiver took possession of Hanson's property, including its equipment, tools, inventory and the five quarry leases and offered them for sale. Since no suitable offers were received on the assets, Trican and SOCO offered to purchase the assets for \$2,517,838, as well as accepting certain liabilities owing to Saskatchewan Environment and Nexen Canada Ltd. In accordance with the receivership order, it was necessary to obtain court approval for the sale, which was eventually received on 27 September 2002. The order, granted by Moshansky J., included the following provisions:

> 2. Title to the Assets be vested in Trican Well Services Ltd. and Saskatchewan Opportunities Corporation ("the Purchasers"), free from all rights and equity of redemption on the part of the Defendants or any person claiming through or under the Defendants, except the claim of a builders lien registered against the Assets by Cambrian Blasting Co. Ltd. as Document No. 3360 (the "Lien").
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> ...
>
> 6. This Order is granted without prejudice to the right of the Receiver or the Purchasers to contest the validity, enforceability or amount of the Lien.[15]

This case involved an application to the Court to determine Cambrian's position with respect to the priority position between it and the secured party/purchasers.

Citing *Canada Trust v. Cenex Ltd.*,[16] Cambrian argued that that s. 22(2) of the *Builders' Lien Act*[17] provided it with a priority position over the two secured parties extending to the severed ore and the minerals *in situ* under the five quarry leases.

3. DECISION

After reviewing the applicable statutory provisions, Rothery J. noted that the appeal in *Cenex* involved assets consisting of extracted ore, mining leases and equipment. In that case, the Court determined that the lien holder had a priority claim over the severed ore. Accordingly, Cambrian, as lien holder in this case, was entitled to a priority claim over the interests of the secured party in the ore extracted from the mine and eventually taken, and later sold, by the Receiver. Justice Rothery stated that such a priority position "does not extend to ore to be extracted in the future by a purchaser of the quarry lease. It is only the debtor's assets that become the pool of assets available for distribution amongst the

15 *Ibid.* at para. 8.
16 (1982), 131 D.L.R. (3d) 479 (Sask. C.A.) [*Cenex*].
17 S.S. 1984-85-86, c. B-7.1.

competing parties."[18] Since the Receiver's listing of Hanson's seized assets did not list severed or extracted ore, the Court determined that Cambrian was not entitled to any of Hanson's assets in priority to Trican or SOCO.

4. COMMENTARY

The distinction made by the Saskatchewan courts between a lien attaching only to severed minerals and not to minerals *in situ* was not adopted in Alberta, under parallel but not identical legislation: see *Alberta Gold Well Servicing v. Snow Hawk Energy*[19] and *Re Smoky River Coal Ltd.*[20]

B. *BADGER DAYLIGHTING V. SUNOMA ENERGY CORP.*[21]

1. BACKGROUND

The following case provides guidance as to when a project is "completed" and limitation periods for when contractors may place a lien on a bankrupt's property.

2. FACTS

Sunoma Energy Corp. (Sunoma) contracted with Delta Pipeline Limited (Delta) to install a pipeline between two of Sunoma's wells near Zama City in northwestern Alberta. Badger Daylighting Inc. (Badger) was Delta's sole shareholder to whom Delta assigned the Sunoma debt. Delta dug a trench for the pipeline in January, February and March of 2000. By the end of March, the pipeline was finished and all that remained was for Delta to remediate the trench and surrounding area by replacing the soil in the trench. Due to frozen soil conditions, Delta submitted to the Court that it was not possible to remediate the surrounding area until sometime after spring breakup. The contract between Delta and Sunoma provided for "final cleanup at time of construction." Additionally, the contract specified that Delta would perform erosion control and environmentally friendly tie-ins.

In April 2000, Sunoma entered into Court-ordered bankruptcy. The bank refused two cheques provided to Delta in partial consideration of its account on 3 May 2000. It was unclear at what point Delta became aware of Sunoma's bankruptcy. On 13 May 2000, Delta sent a crew to the site to remediate the surrounding area and perform the final site cleanup. The crew could still not remediate the area due to excessive amounts of surface water on the site. They did, however, clean up the construction waste surrounding the area and provide a limited amount of site improvement using hand tools around the pipeline risers. Under the applicable legislation, Delta had until 45 days after the final construction to file a builder's lien on the property. Delta filed a builder's lien against Sunoma's property on 13 June 2000.

18 *Supra* note 14 at para. 21.
19 (1987), 53 Alta. L.R. (2d) 333 (Q.B.).
20 (1999), 238 A.R. 158 (Q.B.).
21 [2003] 10 W.W.R. 480 (Alta. Q.B.).

The Court was faced with two issues: (i) whether the builder's lien was valid; and (ii) what was the proper interpretation of the "final cleanup at time of construction" clause of the contract? The receiver in charge of Sunoma's assets argued that Delta's lien was invalid, as it had not been filed within 45 days of the final construction. The receiver argued that the date of final construction was the date the pipeline itself was completed, not the date of the final remediation. Delta contended that the contract included remediating the surrounding area and, as such, the date of final construction was the date of the final site remediation.

3. DECISION

The Court held that the construction referred to in the contract included the final site remediation. To hold that construction was completed upon completion of the pipeline itself but prior to any site remediation activity would not be a reasonable interpretation of the contract, as the contract specifically contemplated site remediation and did not impose a time limit to complete the project. The contract specifically contemplated Delta completing the ground remediation.

The Court further held that the remediation and cleanup work Delta performed on May 13 was not an attempt by Delta simply to extend the time to file its builder's liens, but a *bona fide* attempt to complete the site remediation. Delta had submitted evidence that it had moved and stored equipment close to the site in preparation for the final remediation work.

4. COMMENTARY

By addressing site remediation issues in a construction contract, the parties to the contract will extend the final completion date beyond when the physical asset constructed is completed until such time as the site remediation work can be finished. Such an extension can act to prolong limitations periods.

VI. EMPLOYMENT

A. *HILTON V. NORAMPAC INC.*[22]

1. BACKGROUND

The alteration of employee work hours has long been a contentious issue between both employees and employers. Often the demands of drilling programs, equipment maintenance and alteration of production will require employers to alter unilaterally an employee's regular working hours. The following case gives employers reason to give careful consideration to any increase or decrease of employee hours, regardless of compensation.

2. FACTS

Michael Hilton was an employee of Norampac Inc. (Norampac) from 1985 until his termination in June 2000. Hilton had a work history of being a responsible employee and of

22 (2003), 176 O.A.C. 309, leave to appeal to S.C.C. refused, [2003] S.C.C.A. No. 459 (QL).

being promoted within the company. In April 2000, Norampac unilaterally imposed upon the four employees in the same position as Hilton a requirement to be on-call from 5:00 p.m. Friday night to 6:00 a.m. Monday morning every sixth weekend. These employees were not offered compensation for the increased of amount of on-call time. However, they were offered days off in lieu.

Hilton refused the imposition of these additional on-call responsibilities and cited family matters as the reason for his refusal. Hilton had four young children at home and his wife worked on weekends. The company insisted that Hilton accept these additional hours of work as part of his job position. Hilton proposed not only alternative structures, where he would work on-call hours during certain hours during the week, but also formally requested a demotion to a union position that would allow him to attend to his family responsibilities. Hilton had met a number of times with Norampac's management team to discuss his on-call refusal and had written letters to the president of the corporation expressing his concerns. Despite his efforts, the company insisted he accept the additional on-call hours by June 7 or it would terminate his employment. Upon his refusal to accept the weekend on-call hours, Hilton was terminated, without severance pay, in June 2000.

Hilton sued Norampac for wrongful dismissal.

3. DECISION

In their Agreed Statement of Facts, both Hilton and Norampac agreed that the on-call requirement of Hilton's job had not been a term of his employment contract. As such, the issue before the trial court was to decide whether the introduction of an on-call requirement amounted to a material change in Hilton's employment contract. In upholding the lower court's decision, the Ontario Court of Appeal held that "[i]t seems to me that a trier of fact could reasonably find that the unilateral imposition of additional hours of weekend work without pay materially changed the terms of Hilton's employment."[23] The Court of Appeal further addressed the issue of whether or not Hilton breached his duties to mitigate by refusing the new on-call requirements of his employment. The Ontario Court of Appeal found that Hilton did not have an obligation to accept the on-call requirement; it would be patently unreasonable for Hilton to have to continue on in his current employment, given the circumstances.

4. COMMENTARY

An important consideration in this case is that the company was unilaterally increasing Hilton's employment hours without monetary compensation. A further consideration is the rather sympathetic situation the Court found Hilton to be in with four young children at home and the demands that such a family situation places on an employee. This case helps to illustrate that employers wishing to alter an employee's working hours unilaterally should give careful consideration to the effect such a change may have on an employee's commitments outside the employment relationship.

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23 *Ibid.* at para. 17.

B. *PIPED Act* Case Summary #114 from the Office of the Privacy Commissioner of Canada — Employee Objects to the Use of Digital Video Surveillance Cameras[24]

1. Background

In an era where oil and gas corporations are facing problems with increased vandalism and acts of sabotage, many operators may find it tempting to install video surveillance cameras on vulnerable assets such as plant facilities, compressor stations, *etc.* As of 1 January 2004, all jurisdictions in Canada will be subject to new privacy legislation requirements. The following case helps illustrate situations where employers may be restricted under this new legislation when installing video surveillance equipment.

2. Facts

A federally regulated railway company installed a number of digital surveillance cameras in one of the company's switching yards. The railway company's employees complained to the Privacy Commissioner of Canada that the company was in fact collecting their personal information by monitoring their activities. The railway explained that the cameras were stationed in various locations throughout the switching yard and operated from a central location. The cameras, which did not have a zoom capacity, were fixed on one field of view and provided surveillance tapes for 48-hour periods. Upon installation, the company informed the employees of the cameras' existence and the stated purposes for placing the cameras throughout the yard. The company further reiterated to the employees that these cameras were not being used by the company for monitoring their productivity and, in fact, did not provide views of typical employee work areas; the intention of the company was to have the cameras installed to reduce instances of vandalism and theft and to improve staff safety.

The cameras provided extremely poor picture quality and it was only on rare occasions that an individual could actually be identified from the footage provided from the cameras. The company had gone so far as to install shields on the cameras that would prevent the cameras from viewing any employee productivity areas. Furthermore, the railway company already had an existing camera system in place that had zoom and directional abilities. These cameras did not record information, but were used to monitor train movements throughout the yard.

3. Decision

The Privacy Commissioner acknowledged that the railway's stated purposes of reducing vandalism and theft, limiting potential liabilities for damages and improved security for employees would seem to be appropriate reasons to install video cameras. However, the Commissioner stated that the decision to use video surveillance cameras must pass four questions scrutinizing the necessity of them:

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24 (23 January 2003), Privacy Commissioner of Canada's Findings, online: Privacy Commissioner of Canada <www.privcom.gc.ca/cf-dc/2003/cf-dc_030123_e.asp>.

(i) whether the measure is demonstrably necessary to meet a specific need;
(ii) whether it is likely to be effective in meeting that need;
(iii) whether the loss of privacy is proportional to the benefit gained; and
(iv) whether there is a less privacy-invasive way of achieving the same end.

The Commissioner found that in this instance the railway company was not justified in its use of video surveillance equipment. The Commissioner cited evidence that acts of vandalism within the train yard were relatively minor and further noted that the digital system appeared, at least to him, to be ineffective. The Commissioner noted that at certain points during the day, the new camera system that recorded images could possibly identify an individual. The Commissioner further noted that "the mere presence of these cameras may have given rise to the perception among employees that their comings and goings were being watched, even if that was not objectively the case, and that the adverse psychological effects of a perceived privacy invasion may have been occurring."[25] The Commissioner further noted that increased amounts of lighting could perhaps be as or more effective than the camera system without invading the employees' privacy.

4. COMMENTARY

This case highlights some of the many impacts the privacy legislation will have on corporate activities. Corporations that wish to monitor plant sites or vulnerable areas for incidents of vandalism, theft or sabotage will want to document heavily considerations given to various other methods that may not involve the collection of personal information when assessing whether or not the use of video surveillance equipment is necessary.

C. *R.J.V. GAS FIELD SERVICES LTD. V. BAXANDALL*[26]

1. BACKGROUND

Courts have long been loath to uphold non-competition agreements or impose restrictions on an employee's ability to enter into employment relationships with a former employer's competitors. This case is another example of the difficulties faced by employers when trying to curtail former employees from becoming competitors.

2. FACTS

R.J.V. Gas Field Services Limited (R.J.V.) manufactured polyurethane panels through one of its business divisions. Baxandall had been an employee of that division from December 1996 through September 2001. R.J.V. considered Baxandall to be a key employee. R.J.V.'s largest polyurethane panel customer convinced Baxandall to set up a competing manufacturing facility for polyurethane panels. In June 2001, Baxandall left his employment with R.J.V. and started a competing operation with R.J.V.'s former customer. R.J.V. sought an injunction to prevent Baxandall from going into a competing business based on his use of confidential information obtained while employed by R.J.V.

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25 *Ibid.*

26 (2003), 330 A.R. 115 (C.A.).

The chambers judge granted an interim injunction based upon the test found in *American Cyanamid v. Ethicon Ltd.*,[27] the considerations of which are:

(i) whether there is a serious question to be tried;
(ii) whether the applicant will suffer irreparable harm unless the injunction is granted; and
(iii) whether the balance of convenience favours the granting of the injunction.

The chambers judge found that R.J.V. had satisfied all three conditions and granted an interlocutory injunction preventing Baxandall from selling polyurethane panels to any of R.J.V.'s customers. The trial court judge did not enjoin Baxandall from utilizing the confidential information obtained while an employee at R.J.V. on the basis that there was insufficient evidence illustrating that the information was confidential. Additionally, the trial court judge did not enjoin Baxandall from producing polyurethane panels.

Baxandall appealed the grant of this injunction.

3. DECISION

Based on the four-part test found in *Physique Health Club Ltd. v. Carlsen*,[28] the Alberta Court of Appeal held that the trial judge had found that Baxandall showed clear signs of being a fiduciary or, at the very least, a key employee of R.J.V. For that reason, it assumed, without deciding that there was a strong *prima facie* case, that Baxandall was in fact in a fiduciary-like relationship with R.J.V.

Stating two principles for fiduciaries relevant to the case at bar, the Court held that an employee entering into an employment agreement with a competitor of his former employer is not, in itself, a breach of the fiduciary duty owed by employees to employers and that the former employee may compete with their former employer, but may not actively solicit the business of a customer of the former employer. The Court further noted that this restriction continues for a reasonable period of time post termination.

The Court of Appeal held that in this case the injunction could be quashed on the basis that whatever constituted a reasonable period of time, that time had surely passed by the time the Court of Appeal heard the case.

4. COMMENTARY

This case once again stresses the very limited situations in which employers can restrain former employees from entering into employment contracts with competitors. Employers must think very carefully about the actual confidentiality of information an employee possesses prior to attempting to restrain the employee from utilizing that information in a new employment situation.

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27 [1975] A.C. 396 (H.L.).
28 (1996), 193 A.R. 196 (C.A.).

VII. ROYALTIES

A. *COMPUTERSHARE TRUST CO. OF CANADA V. JONAS*[29]

1. BACKGROUND

This case serves as a cautionary note that a lapsed caveat may not in fact be lapsed in circumstances where there is no *bona fide* purchaser for value.

2. FACTS

This action was brought by Computershare Trust Company of Canada, the successor to Montreal Trust Company of Canada, as successor of The Prudential Trust Company Ltd. (Prudential), as trustee of the Frank James Crandall Gross Royalty Trust (GRTA) against Jonas, the registered owner of the lands in question and successors in title to the Estate of Frank James Crandall.

On 27 April 1956, Frank James Crandall (Crandall), as owner in fee simple, granted a lease to Imperial Oil Limited (Imperial) for a primary term of ten years in return for a gross royalty of 12½ percent of all production from any well drilled on those lands.

On 28 November 1956, Crandall created the GRTA by granting to Prudential certain rights as described in the trust agreement, including assignment of the above mentioned royalty. Subsequently, on 4 December 1956, Prudential filed a caveat against the title to the lands as notification of its interests under the trust agreement. The Imperial lease expired without production but further leases were granted over the years. However, no wells were ever drilled or produced commercially from the lands between 1956 and 6 June 2001.

On 5 May 1976, the mineral title to the lands was transmitted to Katherine Crandall as beneficiary of the Estate of Frank James Crandall. On 18 July 1983, the mineral title was transmitted to Deborah Lynn Healing, as Executrix of the Estate of Katherine Crandall, who in turn transferred it to the present owners as beneficiaries.

On 24 May 1984, the defendants obtained a discharge of the Prudential caveat following a notice to take proceedings being served upon Prudential.

A petroleum and natural gas lease was entered into with Lomalta Petroleums Ltd. (Lomalta) and protected by a registered caveat on 17 April 2000. At the time the caveat was registered, there were no caveats or other instruments registered on the title to notify Lomalta of the interest claimed by the plaintiff, as a new caveat was not filed to protect the GRTA until 2002. As a result, the plaintiff brought this action to seek a declaration that the trust was still in force and an order sanctioning the 2002 caveat with retroactive effect pursuant to s. 145 of the *Land Titles Act*,[30] which reads:

[29] (2003), 347 A.R. 25 (Q.B.).
[30] R.S.A. 2000, c. L-4.

> Except as mentioned in this Act, no one shall file more than one caveat in respect of the same matter, but nothing contained in this Act prejudices the right of the Registrar to enter any caveat under the powers vested in the Registrar by this Act, and a judge may, if the judge thinks proper on application made to the judge for that purpose, and on any terms as to costs or otherwise that the judge considers just, order that a new caveat may be filed, and the order shall fix a time within which the caveator must proceed on the caveat.

3. DECISION

The Court found that the particular wording of the royalty assignment set forth in cl. 2 of the GRTA included a royalty on production from the original Indenture of Lease, as well as any subsequent leases granted by the owner (Frank James Crandall) or his "heirs, executors, administrators or assigns." Furthermore, cl. 27 of the GRTA bound those heirs, executors, administrators and assigns to the owner's covenants. The defendants are the successors in title as beneficiaries under the will of their mother who, in turn, had inherited the same from their father, Frank James Crandall. Therefore, the defendants were deemed bound by the personal covenants of the GRTA as would Crandall be, if he were alive. As a result, Mason J. determined that, since there was no *bona fide* purchaser for value of the property in question, the 2002 registration was deemed properly filed and with retroactive effect, and the plaintiff was therefore entitled to 12½ percent of the production from the lands as royalty.

4. COMMENTARY

This case provides another example of a gross royalty trust agreement being interpreted by the courts. The key provision of the GRTA at issue was once again the royalty assignment clause. As with some of the other agreements that have been the subject of the gross royalty trust test case litigation, the Crandall GRTA had particular additional wording within its royalty assignment provision, as indicated in italics in the full text of cl. 2 of that GRTA reproduced below:

> The Owner herein doth hereby grant, bargain, sell, assign, transfer and set over unto the Trustee, its successors and assigns forever, all the estate, right, title, interest, claim and demand whatsoever, both at law and in equity of the Owners in and to the above mentioned Twelve and One Half (12½%) percentum gross royalty or share of production from any well or wells that may be drilled upon the said lands or any part thereof, *pursuant to the terms and provisions of the Indenture of Lease hereinbefore recited and pursuant to the terms and provisions of any other lease or agreement for developing the said lands which may be entered into by the Owner or his heirs, executors, administrators or assigns* (hereinafter referred to as "the Gross Royalty") TO HAVE AND TO HOLD the same with all and every benefit that may or can be derived from the same unto the the [sic] Trustee, its successors and assigns forever, subject only to the terms of this Trust Agreement.[31]

Once the caveat in respect of the GRTA was discharged from the fee simple title to the minerals, the interest in land that the Court found the GRTA had created could have been thwarted by a *bona fide* purchaser for value. The succession for the mineral fee simple by the defendants through both of their parents' estates left them subject to the covenant originally made by their father to the predecessor of the plaintiff.

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31 *Supra* note 29 at para. 7 [emphasis in original].

B. *BANK OF MONTREAL V. DYNEX PETROLEUM LTD.*;[32] *LORNE H. REED & ASSOCIATES LTD. V. PROMAX ENERGY*;[33] *RE: PROMAX ENERGY*;[34] AND *JAMES H. MEEK TRUST (TRUSTEE OF) V. SAN JUAN RESOURCES*[35]

1. BACKGROUND

It was hoped that the Supreme Court of Canada's decision in *Bank of Montreal v. Dynex Petroleum Ltd.*[36] would provide some clarity to the question of whether or not a grant of an overriding royalty created an interest in land. Since that time, four Alberta Queen's Bench decisions, including the re-trial of the *Dynex* matter, have attempted to apply the principles of the Supreme Court of Canada's decision. While these cases are consistent to the extent that they employ the same test, the application of the test to the particular facts of each case illustrates that the judiciary is still grappling with: a) the sufficiency of the test; and b) what evidence best represents the parties' intentions at the time of the grant.

2. DECISIONS

In the re-trial of *Dynex*, Hawco J. stated that, based on Major J.'s approval of *Vandergrift v. Coseka Resources Ltd.*,[37] the following summary was the appropriate test to employ:

> [I]t appears reasonably clear, that under Canadian law, a "royalty interest", or an "overriding royalty interest", can be an interest in land if:
>
> 1) the language used in describing the interest is sufficiently precise to show that the parties intended the royalty to be a grant of interest in land, rather than a contractual right to a portion of the oil and gas substances recovered from the land; and
> 2) the interest out of which the royalty is carved, is itself, an interest in land.[38]

In *Dynex*, the royalties were granted to an engineer's private corporation as consideration for his geological assistance to the oil and gas companies that owned the working interests. Justice Hawco went over the wording of the relevant agreements in detail. The language used was much the same: the grantor agreed to pay an overriding royalty of a certain percentage of the proceeds received by the grantor on the sale of petroleum substances produced, saved and marketed from the lands. Justice Hawco noted that this wording contrasted with two earlier agreements that had been superceded in which the grant contained a right to take a share of the petroleum substances in kind.

Justice Hawco reiterated that he had to look to the language used in describing the interest to determine what the parties intended. However, Hawco J. agreed with scholarly

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32 (2003), 1 C.B.R. (5th) 188 (Alta. Q.B.) [*Dynex*].
33 [2003] A.J. No. 774 (Q.B.) (QL) [*Reed*].
34 [2003] A.J. No. 1718 (Q.B.) (QL) [*Re: ProMax Energy*].
35 (2003), 356 A.R. 72 (Q.B.) [*Meek*].
36 [2002] 1 S.C.R. 146.
37 (1989), 95 A.R. 372 (Q.B.).
38 *Ibid.* at para. 29.

commentary that no one in the oil and gas industry would intentionally create a royalty that was merely a contract. He also quoted an article by J.F. Newman[39] that stated evidence of the common intention to create an interest in land is found in the common practice of registering caveats in the Land Titles Office. Lastly, the Court stated that the plaintiff had advised that at the time the royalties were granted, the only text authority published in Canada was *The Oil and Gas Lease in Canada* by John Ballem,[40] which states that royalty clauses where there is an agreement to pay a percentage of the value of the substances produced, saved and sold from the reference lands "would appear not to create an interest in land, but only a contractual right."[41]

In the end, the Court held that there was no other evidence to show any intention that would vary the effect and intention of the agreements other than the documents themselves. But the Court also took note of the fact that no caveats "except one" were filed protecting the royalty interests. It appears from this that, although Hawco J. followed the direction of the Supreme Court of Canada in looking to the language of the agreement, he also considered one extraneous factor respecting the commercial context, namely the failure to file caveats (except one).

Justice Hawco's decision was largely, although not entirely, based on the language of the agreement granting the royalty. More specifically, the fact that the agreements did not grant any right to take in kind but only a right to a share of the proceeds of the substances produced, saved and sold was persuasive, as was the fact that two of the agreements superceded previous agreements where such a right to take in kind had been granted. Lack of caveats aside, it does not appear that extraneous factors played a role in the decision.

This is similar to the method employed by McIntyre J. in *Reed*. In *Reed*, the royalty was granted pursuant to arm's-length inter-corporate conveyances of certain petroleum and natural gas interests. In holding that the royalty was clearly intended to be an interest in land, the Court appears to have been solely concerned with the wording of the royalty agreement. It included the following terms:

- a requirement that the purchaser sell the vendor's share of production at the same price and terms as it sold its own substances;
- a set of deductions allowable in the same manner and to the same extent as deductions under Crown royalties (which are interests in land);
- permission to secure the royalty by a lien on the purchaser's interest in the royalty lands;
- an acknowledgment that the royalty would be an interest in land and run with the land; and
- a reiteration that the terms of the agreement would run with and be binding on the title documents and the royalty lands for the duration of the agreement.[42]

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39 "Can a Gross Overriding Royalty Be an Interest in Land?" in *Insight Educational Services, Oil & Gas Agreements Update* (Mississauga, Ont.: Insight Press, 1989).

40 (Toronto: University of Toronto Press, 1973).

41 *Ibid.* at 119.

42 *Reed*, *supra* note 33 at para. 32.

A third recent decision on this subject was the oral decision of Romaine J. in *Re: ProMax Energy*. There, the royalty holders were private corporations owned by consultants who provided geophysical and geological services to ProMax. The compensation for these services was originally to include a casing point election to acquire a 5 percent working interest, but this aspect was later replaced with an overriding royalty interest. The Court, after quoting the test from *Dynex*, stated that the question was whether the language of the agreements was sufficiently precise to show that the parties intended the creation of an interest in land rather than merely a contractual right. Little weight appears to have been given to the fact that the granted interest was changed from an option to acquire a working interest to a royalty interest.

The Court also quoted Hunt J. in *Scurry-Rainbow Oil Ltd. v. Galloway Estate*[42] in saying that a literal approach to the interpretation of such an agreement "should not be followed if it would bring about an unrealistic result not contemplated in the commercial context"[43] of the agreement and that regard should be given to what can be gleaned from the agreement as a whole, as opposed to "searching for some magic words."[44] *Scurry-Rainbow* was referred to in *Reed* and in the re-hearing of *Dynex*, although these principles were not explicitly included in the test approved by the Supreme Court of Canada.

Justice Romaine, as contrasted with Hawco J. in *Dynex* and McIntyre J. in *Reed*, considered the commercial context in arriving at her decision. For example, she stated that there is a difference between the commercial context in which freehold (that is, lessor) and overriding royalties are granted and that this difference should be taken into account when interpreting a royalty, although she stated this should not go so far as to become the application of a presumption.

The Court also stated that the words used in the granting clause, namely "grants" and "assigns," are more consistent with the granting of a contractual right than a conveyance.

Little weight was given to the fact that the royalty owners had the right to take their share of production in kind and that the royalty was expressly stated to exist for the life of the lease.

Other factors were stated by the Court to support its conclusion that an interest in land was not intended, including:

(i) The agreement did not authorize the filing of a caveat; and
(ii) The royalty owners had no development rights and bore no investment risk or liability for drilling costs.

According to the Court, the finding that no interest in land was intended was supported by portions of the royalty agreements, including that fact that the royalty was calculated on "petroleum substances produced, saved and marketed," as in *Dynex*,[45] and that a lien was

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[42] (1993), 138 A.R. 321 (Q.B.) [*Scurry-Rainbow*].
[43] *Ibid.* at para. 86.
[44] *Meek*, *supra* note 35 at para. 35.
[45] *Dynex*, *supra* note 32 at para. 29.

only permitted on the substances removed from the ground (in contrast with *Reed*, where a lien was allowed against the actual lands). Nonetheless, the fact that commercial context, as well as the precise wording of the agreement, was taken into account shows that the courts are not prepared at this time to follow solely the precise wording of a particular agreement in arriving at a decision.

This conclusion is supported by LoVecchio J.'s decision in *Meek*. After referring to *Dynex*, he states:

> I must interpret the precise words used in the agreement having regard for the whole of the agreement as well as the circumstances surrounding it. In so doing, a balance must be struck between two competing forces. I must be wary of simply searching for some magic words while at the same time considering whether the precise words used had been carefully chosen so as to convey a particular meaning.[46]

The particular agreement in *Meek* stated that the royalty was equal to a percent of the hydrocarbons produced, saved and marketed from the relevant lands. Justice LoVecchio noted that other cases have found that a royalty payable out of production is indicative of a mere contractual obligation to pay money and not an interest in land. He went on to consider the other portions of the agreement and found that they supported the conclusion that only a contractual right was granted.

Justice LoVecchio pointed to the fact that the royalty owner did not have the right to drill, produce, market or operate the lands. This is different from granting the right to take in kind (which this agreement was also lacking).

Additionally, the Court stated that the phrase in the granting clause, "sells, assigns, conveys, transfers and sets over," was not, in the circumstances, sufficiently precise to create an interest in land. The Court noted the lack of the phrases "to have and to hold" and "all the estate, right, title, interest, claim and demand whatsoever, both at law and in equity."[47] Lastly, it also made note of the fact that the royalties were granted as compensation for services.

3. COMMENTARY

From the foregoing analysis of these recent cases, one can infer the following principles:

- While the precise wording of the agreement is paramount, courts may construe the wording in their commercial context;
- The presence or absence of registered caveats protecting the royalty interest may, however controversially, be a factor;
- A lack of a right to take production in kind may be strong evidence that no interest in land was intended, however the presence of a right to take in kind will not necessary lead to the finding of an interest in land;

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46 *Supra* note 35 at para. 35.
47 *Ibid.* at para. 41.

- Words granting a royalty based on a percentage of the proceeds from substances produced, saved and sold (or variations thereof) may be strong evidence that no interest in land was intended;
- A royalty granted as compensation for services rather than part of a farmout or other property transfer transaction might require stronger evidence if an interest in land is to be found; and
- In general, the more explicit the parties make their intention to convey an interest in land, the better, to the point of stating more than once in the agreement that the royalty is intended to be an interest in land and run with the land.

VIII. RIGHTS OF FIRST REFUSAL

A. *CALCRUDE OILS LTD. V. LANGEVIN RESOURCES*[49]

1. BACKGROUND

In this case the Court had to determine the impact of a right of first refusal provision in a Farmout Agreement (Clause 2401, CAPL 1974 Operating Procedure) upon a series of disposition transactions for which no right of first refusal notices were sent to the respective rights holders.

2. FACTS

Pursuant to a Farmout Agreement governed by the Canadian Association of Petroleum Landmen 1974 Operating Procedure (CAPL), the plaintiffs collectively owned a 32.5 percent working interest in certain lands, which also involved the defendants. The plaintiffs alleged that they did not receive proper right of first refusal (ROFR) notice as a result of the alleged actions and omissions of the defendants, resulting in an inability to exercise an option to acquire a further 5 percent and 0.5 percent interest in the lands.

In August 1993, Langevin Resources (Langevin) entered into an agreement with Enerplus Resource Corporation (Enerplus) to sell various assets including its working interest in the lands. Later that month, a ROFR notice was provided to the other working interest owners, but the other parties elected not to exercise their rights. On 1 May 1995, the defendant Enerplus entered into an agreement with the defendant Canadian Outlook Resources Ltd. (Canadian Outlook) to acquire its interest in the lands (totaling 5 percent). On 12 June 1995, Enerplus wrote to all of the working interest owners indicating that since this purchase represented "substantially all of Canadian Outlook's petroleum and natural gas rights, Clause 2402 [of the 1974 CAPL] applies and no notice of Right of First Refusal will be issued."[50]

On 30 June 1995 the defendant Lochwest Resources Ltd. (Lochwest) acquired a 0.5 percent interest in the Canadian Outlook lands, but sent no ROFR notices to the working interest owners with respect to the acquisition.

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49 (2003), 349 A.R. 353 (Q.B.).

50 *Ibid.* at para. 29.

On 21 October 1996 Enervest Energy Inc. (Enervest) and Enerplus Management Limited entered into a Management Advisory and Administration Agency Agreement whereby Enerplus agreed to manage the assets of Enervest.

On 20 December 1996, Lochwest sold all of its assets to Enervest for $3.5 million. No ROFR notices were sent by Lochwest or Enervest to the working interest owners following the transaction. On 20 December 1996, Enerplus, Lochwest and Enervest entered into a trust agreement whereby Enerplus would agree to hold Enervest's interests in the lands in trust. However, on 6 November 1997, Enerplus terminated its management of the Enervest assets effective 180 days from that date. On 1 April 1998, Millenium Energy Inc. (Millenium) purchased the assets of Enervest, including the lands. As a result, on 9 July 1998, Enerplus wrote to Enervest and indicated that Enervest was not recognized as a working interest owner, as Enerplus held its assets in trust.

On 14 August 1998, Enerplus wrote to Millenium to describe how the ROFRs were treated by Enerplus following its purchase of the lands from Langevin. In response, on 5 January 1999, Enervest advised the working interest holders that there was no obligation to send a ROFR notice following the transaction with Millenium, as there was the sale of substantially all of the assets of Enervest. In that same month, two of the plaintiffs wrote to Enerplus inquiring into Enervest's acquisition of a 5.5 percent interest in the lands. Enerplus responded on 25 January 1999 by stating:

> Enerplus is of the opinion that as long as a party is silent and not recognized in an agreement their interest can be held without attracting a right of first refusal. The nature of these two parties' relationship has no impact on the ability of one to hold the other in trust. In our opinion, if at any time this party requests to be recognized by the other joint interest owners, a right of first refusal would necessarily be served.[50]

In the same letter, Enerplus did not inform the plaintiffs of the existence of the previous ownership of the lands by Lochwest. Following further enquiries by the plaintiffs, Millenium wrote to the working interest owners on 24 March 1999 stating its position that the transfer from Enervest did not trigger the ROFR clause, as it involved a disposition of all or substantially all of their interest.

3. DECISION

In analyzing the law on rights of first refusal, Power J. notes:

> The general purpose of this Right of First Refusal, it seems to me, is evident. It is to protect the parties' respective interests by ensuring that if one party decides to dispose of all or a portion of its shares to a third party the other party has the pre-emptive right to acquire those shares first, on the same terms and conditions, including price, as that being offered by the third party. In this way, a party is protected against having an unwanted co-shareholder foisted upon it.[51]

And further:

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50 *Ibid.* at para. 45.
51 *Ibid.* at para. 55.

In *Chase Manhattan Bank of Canada v. Sunoma Energy Corp.* [2002] A.J. No. 1550, the Alberta Court of Appeal stated at p. 5, para. 25:

> It is clear that the grantor of a ROFR has a duty to exercise its rights in such a manner to ensure that the other party's rights are not rendered meaningless.[53]

Since the transaction involving Canadian Outlook and Enerplus involved the acquisition of all, or substantially all of, Canadian Outlook's petroleum and natural gas interests in Alberta, it qualified under Clause 2401 of CAPL as an exception to the requirement of serving ROFR notices, since Canadian Outlook was a party to that agreement. As a result, the plaintiffs abandoned their claim against Canadian Outlook.

The transaction involving Lochwest and Enerplus involved a measure of secrecy, as neither the unit holders of Enerplus nor the plaintiffs were advised of Lochwest's existence, option to participate or interest in the lands. The Court determined that the reason for that secrecy was the desire on the part of the parties to avoid the issue of ROFR notice when Enerplus sold to Lochwest. Further, the Court stated that the five attempts by Enerplus to purchase the plaintiffs' interest in the lands was an effort to avoid the potential for a legal dispute over the lack of ROFR notices.

With respect to the sale involving Enerplus' transfer of its 0.5 percent Canadian Outlook interests to Lochwest, the Court determined that since the sale involved a "disposition" as defined under the Farmout Agreement, a ROFR notice should have been provided to the plaintiffs. Enerplus took the position that there was no obligation to provide a ROFR notice pursuant to the Farmout Agreement "as long as some other party (not necessarily the vendor) holds the interest in trust following the disposition."[54] CAPL Clause 2401 clearly states that a ROFR notice must be provided upon any intention to sell an interest. As noted by the Court:

> In *GATX Corp. v. Hawker Siddeley Canada Inc.*, [1996] O.J. No. 1462 (supra) at p.17, para. 71 it states as follows:
>
> > It is well established that the grantor of a right of first refusal must act reasonably and in good faith in relation to that right, and must not act in a fashion designed to eviscerate the very right which had been given. This is an illustration of the application of the good faith doctrine of contractual performance, which in my view is part of the law of Ontario. The law in this respect is nicely summarized in the following passage from the judgment of Saunders J. in *Landymore v. Hardy* (1991), 21 R.P.R. (2d) 174 (N.S.S.C.T.D.) at pp. 193-194:
> >
> > ... the grantor of a Right of First Refusal is not entitled to frustrate by conveying the property in such a way as to avoid having to give the right in the first place.[55]

Thus the Court determined that the defendants, by design, bought and sold the 5.5 percent interest in the lands in violation of the Farmout Agreement. Moreover, there was no authority to support the claim that they were relieved from their contractual obligations by arranging for Enerplus to hold the interest in trust.

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53 *Ibid.* at para. 56.
54 *Ibid.* at para. 71.
55 *Ibid.*

Lastly, with respect to the Enervest sale of the 5.5 percent interest to Millenium, the Court determined it was also a "disposition" pursuant to the Farmout Agreement and thus a ROFR notice should have been provided to the plaintiffs. However, in April 1999 Millenium provided what it regarded as ROFR notice to the working interest owners thereby informing them of the opportunity to purchase the interest. The plaintiffs' failure to accept the offer was determined by Power J. to bar any claim asserted against Millenium.

Justice Power noted that the plaintiffs could have protected their interest in the lands by registering a caveat under the *Land Titles Act*.[55] The failure to do so meant that Millenium acquired its interest free from the plaintiffs' unregistered ROFR interests.

Since the plaintiffs were seeking specific performance for the exact same interest to which they were afforded an opportunity to pursue in 1999, the Court dismissed the action.

4. COMMENTARY

The Court made a number of interesting findings in its consideration of the series of transactions. First, it concluded that if a party that is subject to an agreement containing a ROFR holds its interest in the subject agreement in trust for one or more other parties who are not privy to the contract, disposition by such parties may trigger the ROFR. Second, after the Court made a finding that there had been a technical breach by one of the defendants in respect of its ROFR obligations, it went on to bar the plaintiffs from all but nominal recovery of damages. The defendants had challenged a ROFR notice that was provided to them in 1999 on the basis that the price specified therein was unreasonably high in the circumstances. Having determined not to proceed at the price offered in 1999, the Court was not willing to allow the plaintiffs to have the benefit of five years' hindsight on production and pricing information in order to have a second chance to exercise their ROFR rights in the face of the technical breach by the defendants. Finally, the Court noted that the ROFR interests claimed by the plaintiffs could have been protected by them through the registration of a caveat against the fee simple title to the mineral interests.

IX. SPLIT TITLE

A. *XEREX EXPLORATION LTD. V. PETRO-CANADA*[56]

1. BACKGROUND

This is a somewhat unusual split title case in that it does not relate to competing interests of parties entitled to different substances (such as gas versus oil or gas versus bitumen) in the subject lands, but rather to a competition between lessees with petroleum and natural gas rights in different geological horizons layered on top of one another in such lands.

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55 *Supra* note 30.

56 (2003), 343 A.R. 347 (Q.B.).

2. FACTS

Petro-Canada owned shallow rights to oil and gas under a Crown lease in the zone above that of the plaintiff's license. Xerex Explorations Ltd. (Xerex) held deep rights under the terms of a Crown licence due to expire on 3 December 1996.

In November 1996, Petro-Canada began drilling a well on its lands to test for natural gas. Petro-Canada's Alberta Energy and Utilities Board drilling licence indicated that the well was not to exceed 15 m below the Bluesky-Bullhead zone. On 20 November 1996, Petro-Canada drilled to a depth beyond the 15 m allowance, discovering the presence of oil shows or stains. Without disclosing that it had already drilled into the deep rights and encountered oil showings, Petro-Canada contacted the sole shareholder of Xerex, Mr. Apt, in an effort to acquire the Xerex interests. Xerex declined the offer to sell its interest outright, but by 22 November agreed to transfer its interest to the defendants in return for a 3 percent gross overriding royalty. The well was subsequently completed and sold to Progress Energy Ltd. free of the royalty interest. Xerex sought to set aside the transfer or, in the alternative, to obtain damages on the basis of trespass, actual misrepresentation or misrepresentation on the basis of a failure to disclose information in circumstances where there was a duty to disclose.

3. DECISION

Justice LoVecchio concluded that by the time the agreement had been entered into, Petro-Canada had already drilled beyond its authorized (15 m) zone, and as such, acquired additional insight into the deep rights held by Xerex. Since the agreement had not yet been completed, the extended drilling was without legal justification and amounted to a trespass. Moreover, given the removal of material from the plaintiff's licence (revealing the presence of oil), the activities were further regarded as conversion.

With respect to misrepresentation, LoVecchio J. determined that while there was no actual misrepresentation by false statement, Petro-Canada was guilty of misrepresentation by non-disclosure in the negotiations with Xerex, since it had an obligation to disclose the full extent of the drilling activity to that date and the information obtained.

Since Petro-Canada had sold its property interest, rescission was not regarded as an appropriate remedy; however, damages were deemed appropriate. The Court determined that damages should be calculated on the basis of the type of deal that Xerex would have been able to negotiate had it been aware of the oil showings. Given the plaintiff's history in the industry and the fact that the licence was nearing its expiry, the Court determined that the likely result would have been a farmout to the plaintiff on a 50-50 participation basis. Therefore, damages were awarded in the amount of $8,133,000 (50 percent of the total net revenues from the well plus 50 percent of the present value of the future net cash flow from the lands).

On appeal, the Alberta Court of Appeal[58] upheld LoVecchio J.'s finding of misrepresentation by silence or incomplete disclosure but also found that he had erred by

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[58] [2005] A.J. No. 774 (C.A.) (QL).

failing to find an actual misrepresentation by Petro-Canada. Although not addressed by the trial judge, the Court of Appeal concluded that a special relationship arose between Petro-Canada and Xerex once Petro-Canada entered the Deep Rights Zone which imposed fiduciary duties and disclosure obligations on Petro-Canada when negotiating with Xerex. The balance of the appeal and cross-appeal were dismissed.

4. COMMENTARY

The Court found that the defendant Petro-Canada committed trespass, conversion and misrepresentation. As a result of Petro-Canada's conduct, it held information to which it was not entitled. Furthermore, the Court found that once it had the illegally obtained information it had an obligation to disclose the same to the plaintiff and failing to do so amounted to misrepresentation. The plaintiff, Xerex, held an Alberta Crown Deep Rights Licence that was due to expire 13 days after Xerex was first contacted by Petro-Canada regarding a sale of its interests to Petro-Canada or, failing that, the exchange of its interest for an overriding royalty. Because of what the Court found to be egregious conduct by Petro-Canada, it determined what it felt Xerex would have negotiated had all of the relevant information been provided to Xerex. Ultimately, Xerex received damages based on the value of an undivided 50 percent interest in the well with a total value of $8,133,000. Given the short amount of time left before the expiry of the Xerex licence, one can question whether or not Xerex would have in fact been able to negotiate such a rich deal in respect of the subject well. By virtue of its tortious conduct, however, Petro-Canada denied Xerex the opportunity to negotiate the best deal it could and instead left the negotiation to the unilateral musings of a Court that was clearly sympathetic to the victimized plaintiff.

B. *ALBERTA ENERGY V. GOODWELL PETROLEUM CORP. LTD.*[59]

1. BACKGROUND

This split title dispute between a natural gas lessee and a bitumen lessee reached the Alberta Court of Appeal after the matter had been addressed by the Alberta Energy and Utilities Board (AEUB).

2. FACTS

Goodwell Petroleum Corporation Ltd. (Goodwell) held the petroleum and natural gas rights on five contiguous sections in the Athabasca oil sands area. Amber Energy Incorporated (Amber) originally held the bitumen rights to the lands, drilling and operation of 16 horizontal bitumen wells until October 1998, when Alberta Energy Co. (AEC) acquired Amber's bitumen interests and operating wells.

Goodwell claimed that production from the sixteen wells was producing an "exceptionally high" gas-to-oil ratio, suggesting that a significant portion of its initial gas-cap was produced with bitumen. As a result, Goodwell participated in discussions with the plaintiffs to negotiate compensation for past natural gas production and a sharing agreement for future production.

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59 (2003), 339 A.R. 201 (C.A.).

When talks broke down, Goodwell took legal action against the plaintiffs and also applied to the AEUB to shut-in the 16 horizontal bitumen wells.

The AEUB shut-in four wells whose performance and geological position suggested they were producing significant gas volumes, which it regarded as gas-cap gas. The four wells were shut-in for two reasons:

(i) The AEUB was concerned that the high gas-to-oil ratios seen in the wells would have a negative impact upon the overall recovery of bitumen in the region by dropping the pressure in the bitumen site; and
(ii) The AEUB determined that AEC did not have any right under its oil sands leases to produce initial gas-cap from the four wells, stating that AEC's only interests in this pool included bitumen and solution gas. Therefore, AEC was required to obtain all of the rights to produce overlying gas through some form of agreement or revenue sharing formula in order to extend the scope of its production.

AEC took the position that the AEUB's decision was patently unreasonable since it imposed a condition that AEC could not fulfill on reasonable commercial terms; the shut-in of the wells effectively weighed the stakes in favour of the gas-cap holder, thereby placing AEC in an untenable negotiating position. Moreover, AEC further contended that the AEUB erred in law by citing *Borys v. Canadian Pacific Railway*,[59] which held that incidental production of natural gas was allowed, provided that modern operating methods were followed and the relevant statutes and regulations were observed.

In response, the AEUB acknowledged this case law but argued that *Borys* was based on the wording of a specific CPR grant. In addition, the AEUB argued that the same considerations may not apply in a competition between a bitumen holder and a gas-cap holder. Moreover, the AEUB took the position that for both conservation and legal entitlement reasons, Alberta's regulatory scheme qualifies the unfettered ability of an oil producer to deplete the gas volumes belonging to another.

Leave was granted by the Alberta Court of Appeal to determine: (1) whether the AEUB erred in law or jurisdiction in determining that AEC's right to produce did not include any production of initial gas-cap gas; and (2) whether the AEUB erred in law or jurisdiction in shutting the wells until such time as AEC had the "full rights to produce" the initial gas-cap gas and by encouraging it to enter into a production and cost sharing agreement.

3. DECISION

Justice Fruman noted that the AEUB's position that a bitumen lessee does not have a right to produce gas-cap gas in connection with bitumen recovery was at odds with long-standing authority in Alberta. In response, the AEUB took the position that the *Borys* principles did not apply to Crown oil sands leases and attempted to distinguish from that case on the basis of:

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[59] [1953] 2 D.L.R. 65 (P.C.) [*Borys*].

(i) science: the geological principles and extraction methods for bitumen are not sufficiently similar to petroleum to justify application of the *Borys* principles; (ii) contract: the terms of the specific oil sands leases and related instruments override *Borys*; and (iii) statute: the Alberta oil sands statutory regime abrogates the *Borys* principles, and the settled expectations of industry participants confirms that interpretation.[61]

In addressing the scientific argument, Fruman J.A. stated:

Oil and gas law is a specialized area that has developed because of the unique and fleeting nature of the subject matter. Hydrocarbon molecules change phases and migrate to other tracts of land as no other substances do. In the past, courts have struggled with difficult analogies to come to terms with oil and gas law. These extrapolations of legal principles have sometimes created awkward and inconsistent rulings. Now that we have a better understanding of hydrocarbon behaviour, we should not extend oil and gas principles to other substances, even those with a similar molecular structure, unless they exhibit similar scientific characteristics. Therefore, the *Borys* principles should not apply to oil sands unless the role of initial gas-cap gas in bitumen recovery is similar to its role in conventional oil recovery.[62]

And further:

[T]he Board confirmed to this Court that the scientific principles for bitumen recovery in the four shut-in wells are similar to those for conventional oil: because a gas-cap is present, initial gas-cap gas pressure assists in moving the bitumen and is therefore critical to recovery, and some initial gas-cap gas is inevitably is inevitably produced with bitumen. *Borys* is not distinguishable because of scientific differences.[63]

Justice Fruman summarizes the Court's reasoning on the AEUB's contractual arguments by stating:

[O]il sands and natural gas leases create overlapping, but not inconsistent, rights with respect to initial gas-cap produced incidental to bitumen recovery. AEC's right to recover bitumen gives it the corollary right to produce initial gas-cap gas. Although Goodwell loses some control over the actual production of initial gas-cap gas, its leased natural gas rights entitle it to compensation for initial gas-cap gas produced in the bitumen recovery operation.... This interpretation protects the economic interests of both lessees. It is also consistent with conservation principles, which at this time dictate that bitumen production should precede natural gas production.[64]

Finally, the Court addressed the AEUB's arguments based on statute as follows:

First, the Board relies on s. 54 of the *Mines and Minerals Act*, R.S.A. 2000, c. M-17, which prohibits the production of resources belonging to the crown unless the person recovering the resources is authorized to do so "under this Act or by an agreement." ... A similar statutory provision was in place at the time of *Borys*; ... however, the section would have had no application to that dispute because neither the C.P.R. nor Borys derived their rights from the crown.

61 *Supra* note 59 at para. 37.
62 *Ibid.* at para. 38.
63 *Ibid.* at para. 43.
64 *Ibid.* at para. 84.

At first glance, it appears that s. 54, by requiring an "agreement", overrules Lord Porter's statement in *Borys* that when two parties have the right to recover hydrocarbons, no agreement between them is needed: *Borys* (P.C.) at 77. However, s. 54 references a specific type of "agreement", a term defined in s. 1(1)(a) of the *Mines and Minerals Act, supra*.... An oil sands lease ... is required to recover bitumen, and a crown natural gas lease is required to recover initial gas-cap gas.

In a split title situation, when the recovery of one leased substance results in the incidental production of another leased substance, s. 54 will be contravened if the oil sands lease does not permit initial gas-cap gas production incidental to bitumen recovery. The section does not further restrict the oil sand's lessee's rights; its application depends entirely on an interpretation of the leases.

According to the reasoning in the "Contract" section of this judgment, under its oil sands leases, AEC is entitled to win, work, recover and remove its bitumen even though some initial gas-cap gas is produced incidental to bitumen recovery. As AEC is authorized by an "agreement" to recover bitumen, including initial gas-cap gas, it follows that it has not contravened s. 54.

The Board also relies on s. 16(1) of the *Oil and Gas Conservation Act*, which precludes a person from applying for or holding a license for a well for the recovery of oil, gas or crude bitumen unless the person has the right to produce that hydrocarbon from that well.

...

Neither s. 16(1) nor its predecessor section support the Board's position. These sections will be contravened if the person who holds the well license does not possess the right to produce the hydrocarbon authorized by the well license. The right to produce could be acquired by agreement, reservation, grant or, as in this case, crown lease. Again, the application of the sections depends on the interpretation of the instrument that grants the rights. The sections themselves do not further restrict the oil sands lessee's rights.

Because, on a proper interpretation, AEC's oil sands leases grant it the right to recover bitumen and initial gas-cap gas incidental to bitumen recovery, AEC is not violating s. 16(1) or its predecessor, s. 13(1). In any event, a similar statutory provision was in place at the time of *Borys* and the court nevertheless concluded that the petroleum rights holder was entitled to produce initial gas-cap gas incidental to petroleum recovery.[65]

In summary, the Court determined that, upon examination of principles of science and contract, as well as the relevant statutory regime, AEC was entitled to produce gas-cap gas incidental to its bitumen recovery subject to the rights Goodwell might have for compensation for the gas-cap gas produced. In allowing the appeal, the shut-in order was ordered rescinded and AEC was permitted to resume production of bitumen, associated solution gas and gas-cap gas incidental to its bitumen recovery operation, provided such efforts follow modern operating practices and comply with relevant legislation.

4. COMMENTARY

Of significance with respect to oil sands and bitumen recovery projects, this case establishes that the production of gas-cap gas incidental to bitumen recovery will be permissible, provided that compensation is provided to those holding title to the gas resource.

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65 *Ibid.* at paras. 88-94.

Following this decision, it would appear that the right to recover bitumen under Alberta Crown oil sands leases also entitles the lessee to produce initial gas-cap gas incidental to that bitumen recovery, despite the fact that the right to recover that gas-cap gas is held by a competing leasehold interest. While this decision appears to confirm long-standing law and industry practice, it also highlights the risks associated with such production in split title situations. Until an ownership contest is resolved with respect to the gas-cap production incidental to bitumen recovery, parties may be well advised to obtain either the consent of the owner of those gas rights or negotiate a production sharing agreement. Otherwise, exposure to potential claims in tort for trespass, conversion or a claim for an injunction restraining any recovery activity may result. Therefore, it is advisable that such risks be minimized by the parties with competing interests agreeing to settle their ownership disputes through contracts that protect their respective interests, through agreements affording each party certain rights to exploit their respectively distinct interests, or alternatively, through jointly seeking a judicial declaration of ownership.

X. TAXATION

A. *BJ SERVICES CO. CANADA V. CANADA*[66]

1. BACKGROUND

These two companion cases dealt with the treatment of professional fees incurred by a target company in a hostile takeover situation under the *Excise Tax Act*[67] and the *Income Tax Act*.[68]

2. FACTS

Nowsco Well Service Ltd. (Nowsco) was a publicly traded corporation that provided well stimulation and pipeline services in the oil and gas industry. On 1 April 1996, Nowsco received an unsolicited offer from BJ Services Company (BJ) to purchase its shares for $27 per share. The Board of Directors of Nowsco was advised that it had a fiduciary obligation to obtain the highest price for Nowsco's shares. Nowsco proceeded to retain the financial services of RBC Dominion Securities Inc. (RBC) and Simmons & Company International of Houston, Texas (Simmons) to evaluate the BJ proposal and any subsequent proposals. Nowsco also retained the law firm of Blake Cassels & Graydon (Blakes) to advise it on a number of legal issues arising from the proposal. Upon receiving advice from RBC, a Director's Circular was circulated to shareholders recommending that the BJ proposal be rejected.

On 4 May 1996, Great Lakes Chemical Corporation (GLCC) entered into an agreement with Nowsco whereby GLCC offered $30.90 per share. Nowsco agreed to pay a non-contingent "Hello" fee plus a contingent "Break" fee to GLCC if a higher offer was made by

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66. [2002] G.S.T.C. 124 (T.C.C.) [the GST Case]; [2004] 2 C.T.C. 2169 [the Income Tax Case] [*BJ Services*].
67. R.S.C. 1985, c. E-15.
68. R.S.C. 1985, c. 1 (5th Supp.).

another party and accepted by Nowsco. BJ made a second offer of $35.00 per share and was successful in acquiring all of the issued and outstanding common shares of Nowsco.

Nowsco claimed Input Tax Credits (ITCs) under the *Excise Tax Act* with respect to the fees paid to RBC (the RBC Fees) and Blakes (the Blakes Fees). The Canada Customs and Revenue Agency (CCRA) denied the ITCs on the RBC Fees, except to the extent that they related to the initial fairness opinion, and the Blakes Fees.

Nowsco deducted the RBC Fees, the Blakes Fees, the fees paid to Simmons (the Simmons Fees) and the Hello and Break fees in computing its income tax payable for the year. The CCRA denied these deductions, but prior to trial, agreed that the Blakes Fees were deductible under the *Income Tax Act*.

3. DECISIONS

a. The GST Case

The decision in the GST Case focused on whether the fees had been incurred in the course of Nowsco's commercial activities. Under the *Excise Tax Act*, "commercial activities" included all activities except those relating to the making of exempt supplies or those relating to non-business activities. Since Nowsco did not make exempt supplies, the issue was whether the fees related to non-business activities. The Court concluded that the fees were tied to the overall operation of the company and, therefore, the ITCs should be allowed because they had been incurred in the course of Nowsco's commercial activities. The Court also noted that, from a policy perspective, it made sense that the fees would be a business cost passed on to the customer.

b. The Income Tax Case

In order to be deductible as a current expenditure under the *Income Tax Act*, an expense must be made for the purpose of gaining or producing income from the taxpayer's income or property and must not be on account of capital. In the Income Tax Case, the Tax Court concluded that the fees at issue were incurred for the purpose of gaining or producing income because the expenses were of a business nature and satisfied a need of the company. Maximizing share price is inextricably interwoven with the business of any company, and the Board had an obligation to seek a better alternative than the original BJ offer. The Court also noted that, in order to satisfy this test, there was no need for a direct link between revenues and expenditures.

The Court then considered whether the fees were on account of capital. The Court decided that capitalizing the expenses would not result in a more accurate portrayal of income. The Court also relied on an earlier case of *International Colin Energy Corp. v. Canada*[69] and concluded that the fees were not on account of capital.

69 [2003] 1 C.T.C. 2406 (T.C.C.) [*International Colin*].

The Court also briefly considered the alternative argument that the fees could be deducted as a financing expense under s. 20(1)(bb) of the *Income Tax Act*. In the Court's opinion, since the paragraph used the phrase "in the course of," it should be interpreted broadly and therefore the fees could be deducted as a financing expense.

The Court also entertained the alternative of deducting the fees as expenses relating to the sale of shares of the company under s. 20(1)(e) of the *Income Tax Act*. The Court suggested that the provision may apply to a situation where someone other than the corporation sold the shares, but (just as in the GST Case and *International Colin*, discussed below) the Court declined to decide the issue at that point in time.

4. COMMENTARY

Although the GST Case and the Income Tax Case involved statutory provisions with quite different wording, many of the same factors were considered in both cases. Both cases stressed that creating shareholder value is important to the business, not just to the shareholders.

B. *INTERNATIONAL COLIN ENERGY CORP. V. CANADA*[69]

1. BACKGROUND

International Colin is another case dealing with the deductibility of professional fees, though in a slightly different context than *BJ Services*. This case was decided after the *BJ Services* GST decision, but prior to the Income Tax decision.

2. FACTS

International Colin Energy Corp. (ICEC) was in the business of drilling and exploring for oil and gas. ICEC began to experience financial problems due to declining income and cash flow. ICEC retained PowerWest Financial Ltd. (PowerWest) to prepare a corporate valuation report, and possibly to assist with evaluating strategic alternatives and negotiating an acquisition or merger transaction. The fees to be paid to PowerWest (the Fees) included a success fee component in the event of a sale, merger or refinancing.

ICEC received proposals from several companies and PowerWest entered into negotiations with two of the companies. ICEC performed due diligence with respect to the two companies in order to determine which association would be the most beneficial for ICEC's business. The Court noted that it was important that the well-being of the business, and not just the sale of the shares, was carefully considered. At PowerWest's recommendation, ICEC's Board of Directors accepted the merger proposal from Morgan Hydrocarbons Inc. (Morgan). The Alberta Court of Queen's Bench and the ICEC shareholders both approved the Plan of Arrangement, and the shareholders of ICEC became the shareholders of Morgan.

69 *Ibid.*

3. DECISION

ICEC's position was that the Fees were deductible under the *Income Tax Act*. The Crown's position was that the Fees were not incurred in order that ICEC would earn income and, accordingly, were not deductible.

The Tax Court of Canada held that the Fees were intended to improve the ability of ICEC to earn income by combining its resources with that of another entity, and therefore the Fees were laid out to earn income from the appellant's business. The Fees were not capital, as no capital asset was acquired, nothing of an enduring benefit came into existence and no capital asset was preserved. The Court heard testimony from an accountant who stated that the Fees would not all be treated as expenses under generally accepted accounting principles. The Court did not agree with the facts assumed by the accountant and stated that, in any event, generally accepted accounting principles were of limited assistance in determining what was income for the purposes of the *Income Tax Act*. The Court concluded that the Fees were deductible as a current expenditure.

The Court proceeded to discuss the alternative argument that the Fees were deductible under s. 20(1)(e) of the *Income Tax Act* as an expense in the course of a sale of shares of capital stock of the taxpayer. The Court identified the question as whether or not the provision was limited to a sale by the corporation of its own shares, or whether, as in this case, it also applied to a sale of the corporation's shares by the shareholders. The Court favoured the more expansive view of the provision, but chose not to make a decision on the point.

4. COMMENTARY

This case and *BJ Services* are groundbreaking decisions concerning the taxation of professional fees incurred by corporations. It will be interesting to see whether the decisions will be applied to other situations.

C. *BP CANADA ENERGY RESOURCES COMPANY V. CANADA*[70]

1. BACKGROUND

The issue of whether a payment is income or capital in nature continues to be disputed. This case considered the nature of a payment made following the major restructuring of contracts for the supply of natural gas.

2. FACTS

BP Canada Energy Resources Company (BP) was involved in the exploration and production of oil and gas in Canada. In order to access the U.S. market, Canadian producers sold natural gas to Alberta Southern Gas Co. Ltd. (A&S), a Canadian subsidiary of the U.S. company Pacific Gas Transmission Company (PG&E). A&S would then sell the gas to a U.S.

[70] [2003] 1 C.T.C. 2497 (T.C.C.).

subsidiary of PG&E, which would in turn sell the gas to PG&E. BP had a number of long-term contracts to sell natural gas to A&S, and the contracts related to specific fields owned by BP. The U.S. regulatory authorities forced A&S to terminate its existing contracts with BP and to restructure its arrangements. As a result, BP continued to sell natural gas to A&S, but under short-term contracts. The fields dedicated to the old contracts were not a part of the new arrangement and were sold by BP. The transportation arrangements were also altered under the new contracts.

As a part of the restructuring, BP received two large payments from A&S and PG&E. The Crown's position was that the amounts received were on income account, but were not resource income because they did not result from production but from refraining from production. BP argued that the amounts were a disposition of a capital asset, and, alternatively, if the amounts were found to be income, that they qualified for the resource allowance.

3. DECISION

The Tax Court of Canada couched the issue as "whether the payment is made for the termination, disposition or sterilization of a capital asset or is one of the ordinary incidents of an ongoing business so that the receipt properly forms part of the normal receipts of the trade."[71] The Court's conclusions can be summarized as follows:

- The long-term gas supply contracts that Amoco (later BP) had with the other parties were capital assets. They formed a significant part of the structure of its business and lands were dedicated to the contracts.
- The payments made to Amoco were not for a loss of a stream of income; they were not based on the income that the appellant expected to receive from the contracts. Rather, they were an aspect of the entire decontracting arrangement, which involved a major restructuring of a significant part of Amoco's business.
- Even if the payments were measured by the present value of the profits that Amoco might reasonably be expected to earn, this would not deprive the payments of their quality of capital because they were compensation for the sterilization of a capital asset.

The Court did not accept that the payments were for a loss of a "stream of income," as they were not calculated by determining BP's lost profits. The payments were to be treated as proceeds of disposition of the contracts and, since the contracts had an adjusted cost base of nil, they represented a capital gain.

4. COMMENTARY

This is an important case regarding the tax treatment of "decontracting" or settlement payments in the termination of petroleum agreements. Although this case involved long-term gas purchase agreements, the principle may extend to other oil and gas agreements, including transportation and processing agreements, if they are also found to be capital assets forming a significant structure of a party's business. We understand the Crown appeal has been

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[71] *Ibid.* at para. 54.

abandoned, so the principles of the case will stand until further clarified and developed by subsequent cases.

XI. OCCUPATIONAL HEALTH AND SAFETY

A. *R. v. GENERAL SCRAP IRON AND METALS LTD.*[73]

1. BACKGROUND

This case was an appeal of a 2002 decision that considered the role of industry standards in determining whether an employer has taken all reasonable steps to ensure the health and safety of its employees.

2. FACTS

A worker was killed by a bale of scrap wire that crushed him. General Scrap Iron and Metals Ltd. (GSIM) was fined $100,000 and a 15 percent victim surcharge. GSIM argued that, in the absence of government safety regulations, it was sufficient for an employer to adhere to safe industry standards. The Alberta Court of Queen's Bench rejected the argument and concluded that industry standards are simply one factor to consider in determining whether an employer took all reasonable steps to ensure the health and safety of their employees. GSIM claimed on leave to appeal that the judge erred because he ignored evidence of the industry standard and erroneously applied his own standard of care.

3. DECISION

The Alberta Court of Appeal denied GSIM's leave to appeal the sentence. The Court held that GSIM had failed to prove that the appeal raised issues dealing solely with questions of law and that were of sufficient public importance to justify an appeal. Since the appeal related solely to the industry standard, the basis of the conviction appeal was factual and did not involve a question of law alone. The Court concluded that although industry standards may be a relevant starting point, it is only one fact or inference that will be considered in determining whether a corporation has met the appropriate legal standard. As such, the Court concluded that GSIM had not raised a question of law alone and that the appeal must be rejected.

4. COMMENTARY

The Court of Appeal upheld the Queen's Bench decision that industry standard is simply one factor that the courts will consider in determining whether an employer has taken all reasonable steps to ensure the health and safety of its employees. As a result, complying with industry standards does not provide a full defence.

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[73] (2003), 327 A.R. 84 (C.A.).

Future incidents involving matters of occupational health and safety may be subject to prosecution under the *Criminal Code of Canada*.[73] The passage of Bill C-45[74] (the Westray Bill) on 7 November 2003 amended the *Criminal Code* to establish a legal duty for all persons directing work to take reasonable steps to ensure the safety of workers and the public and to hold corporations, directors and their representatives accountable for their failure to do so.

B. *R. v. Canadian National Railway Company*[75]

1. Background

This case discussed the burden of proof for the Crown and the defence when arguing whether an employer has failed to provide employees with adequate supervision to protect their health and safety. The Court considered the issue of what constitutes the *actus reus* of the offence of failing to provide adequate supervision and a safe work environment.

2. Facts

Canadian National Railway (CNR) was charged with failing to provide employees with adequate supervision in failing to ensure that the movement of a rail car was planned and supervised so as to protect employee health and safety. The charge arose out of the death of an experienced employee who fell from a flat car and was run over during a switching operation. At the time, the employee was in breach of at least five safety rules, codes, operation guidelines and railway policy. As well, there was evidence that the employee might have been under the influence of drugs at the time of his death.

3. Decision

The Manitoba Provincial Court acquitted the CNR. The Court concluded that the employee was experienced, qualified and knowledgeable. As a result, it was unnecessary for his supervisor to oversee his work at all times. The Court held that adequate and reasonable supervision does not in all cases require that a supervisor be physically present on site. The nature of the supervision required will depend upon the particular situation and the training, experience and knowledge of the employees. The Court concluded that the CNR acted with due diligence in providing training, safety courses and manuals and in giving competent employees supervisory responsibility.

The Crown argued that the death of the employee was the *actus reus* of the offence. The Crown contended that this prohibited act was proven by the mere fact that the employee was employed by the CNR and was killed at the workplace. The defence argued that the *actus reus* of the offence was a breach of the duty of care, which was to take all reasonable care to ensure the health and safety of employees. The defence submitted that the fact that the

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73 R.S.C. 1985, c. C-46 [*Criminal Code*].

74 *An Act to Amend the Criminal Code*, 2d Sess., 37th Parl., (2001) (assented to 7 November 2003), S.C. 2003, c. 21.

75 [2003] 8 W.W.R. 503 (Man. Prov. Ct.).

employee died while at work does not satisfy the burden of proof on the Crown to prove the prohibited act beyond a reasonable doubt. The fact that an employee has suffered a severe injury or death at work is simply "evidence" that the employer did not ensure the safety and health as required.

The Court rejected the Crown's argument on the basis that it would mean that any time there is a death or injury of an employee at work, however caused, the employer could be charged with an offence under the *Canada Labour Code*.[76] The Crown would then need only prove: (1) that the accused was a employer within the meaning of the statute; (2) that the deceased or injured person was an employee of the accused; and (3) that at the time of death or injury the employee was at work in order to prove its case beyond a reasonable doubt. The Court did not accept that such evidence alone is sufficient in all cases to prove the prohibited act beyond a reasonable doubt.

In the Court's view, when the death or injury of an employee is the direct result of the employee's own negligence and a deliberate breach of safety rules and procedures that the employer has put in place, something more should be required in order to prove the *actus reus* of the offense. The Court held that the Crown's view was illogical because an employer would not meet the standard of care set out in s. 124 of the *Canada Labour Code* by doing all that is reasonable, yet could successfully raise a defence of due diligence by showing that all that was reasonable in the circumstances was done. As a result of the safety rules, safety courses, manuals and training policies in place by the CNR, the Court concluded that the Crown had not proven the *actus reus* of the offence. The Court determined that the CNR could not have foreseen that an employee with training and experience would deliberately ignore a number of safety procedures.

4. COMMENTARY

This case indicates that, under the *Canada Labour Code*, the death of an employee in the workplace does not immediately place the burden of proof on the corporation to prove due diligence and reasonable care. The *actus reus* of the offence of failing to provide adequate supervision and a safe work environment is the breach of a duty of care. The burden of proof therefore rests on the Crown to prove a breach of the duty before the corporation is required to provide evidence of due diligence and reasonable care.

XII. GUARANTEES

A. *BANK OF MONTREAL V. TSESHAHT INDIAN BAND*[77]

1. BACKGROUND

It is not uncommon to have a debt secured by a number of guarantors. One issue that arises in this context is what duties, if any, the secured party owes to the individual guarantors.

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76 R.S.C. 1985, c. L-2.

77 [2003] B.C.J. No. 1649 (S.C.) (QL).

2. FACTS

This was an application by the plaintiff, the Bank of Montreal (the Bank), for judgment by way of summary trial against the defendant Tseshaht Indian Band (the Band), on a guarantee of the debts and liabilities of Nation Seafood Company (the Company).

The Company was a joint venture between Allen Nikiforuk, Frank Kendall, the Band and their respective companies, Clayoquot Sound Products Ltd., Skidegate Sales & Service Ltd. and Tsisha Investments. The Company was created to operate a fish plant, which it did.

By a written application, the Company had applied to the Bank for a credit facility, subject to the terms and conditions therein set out. The Bank confirmed its approval of the written credit application subject to terms and conditions detailed in an attachment to the credit offering letter. The letter was signed by all the parties to the joint venture, expressly accepting and acknowledging the terms and conditions of the letter of offer.

The terms and conditions in the letter required the Company to provide a General Security Agreement and a General Assignment of Book Debts, required all of the parties to the joint venture to provide joint and several guarantees in the amount of $100,000 for the borrowings of the Company and required the Band and the corporate guarantors to provide enabling resolutions.

The Band passed a resolution providing that it was affiliated and had business relations with the Company and authorizing the execution of the guarantee in favour of the Bank. It signed the guarantee on the same day. The defendant Tsisha Investments (Tsisha), in which the Band was a 51 percent shareholder, and the individual defendants also executed a guarantee of the Company's debt.

The Band was a long-term customer of the Bank. The Bank did not advise the Band to seek independent legal advice before signing the guarantee. The Band claimed that it was not advised that it would be potentially liable for the entire amount of the guarantee. There was no evidence that the Band had asked about the effect of the guarantee.

The Company became insolvent. The Bank sought judgment only against the Band on its guarantee in the amount of $92,445.09 together with interest.

In their defence, the Band and Tsisha raised three defences:

(1) Misrepresentation of guarantees;
(2) Abuse of special relationship; and
(3) Estoppel.

The Band alleged that, prior to entering into the guarantees, the Bank was aware that the guarantors, except the Band and Tsisha, likely would not be able to pay "their proportionate share" of the guarantees. The Band argued that because the Bank did not make these defendants aware of this information prior to these defendants entering into the guarantees, the Bank's silence was a misrepresentation of the guarantees. The Band argued further that it relied on the Bank's misrepresentation when it entered into the guarantees and that it would not have entered into the guarantees had it been aware of the information.

The Band stated that the Bank was the financial institution that provided most financial services to the Band and Tsisha, and that the Bank had a special relationship with them as their banker. The Band stated that the Bank did not make the Band and Tsisha aware that independent legal advice should be sought prior to them entering into the guarantees and that the Bank's silence was an abuse of its special relationship with these defendants. They argued further that they would not have entered into the guarantees had they received independent legal advice and that the guarantees should be rescinded due to the Bank's misrepresentation of the guarantees and the Bank's abuse of its special relationship with these defendants.

The Band argued alternatively that the Bank was estopped from demanding payment from it in accordance with the guarantees due to its misrepresentation of the guarantees and its abuse of its special relationship with the defendants.

3. DECISION

In allowing the application, Hood J. found that, while a bank may gather in guarantees from all of the participants in a project on the basis that by the time there is a default some of the security may have value, it is not obligated to look to all or any particular guarantor. The bank will always look to the guarantor who has assets at the time of default. Justice Hood stated that the fact that the Band was the "best bet" at the time that the guarantees were signed did not impose a positive duty on the Bank to tell the Band this or to discuss the credibility of the co-guarantors or their assets. There were simply no special or unusual circumstances in the case giving rise to such a duty.

Justice Hood found that there was no basis for a finding of innocent misrepresentation by silence and that the Bank, by remaining silent, did not breach any duty to the Band. The Band was a sufficiently active participant in the joint venture that the absence of independent legal advice was not a defence. Justice Hood found that there was no special relationship between the Band and the Bank, nor was there a duty on the Bank to warn the Band that the Company's business might be risky or that its co-guarantors would likely not be able to contribute to any loss in the event of default.

4. COMMENTARY

This case illustrates that secured parties owe no special duties to the individual guarantors. Canadian lawyers whose clients are about to execute guarantees should be particularly diligent not only with regards to the extent of the guarantee to be entered into, but also the financial situation of the other guarantors involved.

XIII. SURFACE RIGHTS

A. *BALISKY V. CANADA (MINISTER OF NATURAL RESOURCES)*[79]

1. BACKGROUND

This was an appeal by Balisky from the dismissal of its application for judicial review. Under s. 112(1) of the *National Energy Board Act*,[80] landowners are not permitted to excavate using power operated equipment or explosives in the controlled area without first obtaining approval from the National Energy Board (the Board). The appellants submitted that they were entitled to refer to an arbitration committee compensation claims for damages arising from the limits imposed by s. 112(1).

2. FACTS

Alliance Pipeline (Alliance) and its U.S. affiliate owned and operated a natural gas pipeline extending from British Columbia to Chicago. Most of the land required for the right-of-way of the pipeline was acquired by agreement. Where an agreement could not be reached, Alliance applied for and was granted right of entry orders by the Board. The appellants sought to refer to an arbitration committee claims for compensation arising from the restrictions imposed by s. 112(1). The Minister refused to refer the matter to arbitration on the basis that the *NEB Act* restricted the scope of the arbitration committee to determining damages directly related to the acquisition of land or to the construction or repair of the pipeline and that the landowner's damages were not related in any direct manner to the company's acquisition of the right-of-way. The appellant's application for judicial review to the Federal Court was also dismissed. This was an appeal from that dismissal.

3. DECISION

The Federal Court of Appeal allowed the appeal. In its decision, the Court evaluated the effects of ss. 84(a) and 112(1) of the *NEB Act*. The Court determined that s. 84(a) is directed at negligent or even innocent acts of employees, subcontractors or others acting on behalf of the pipeline company that cause damage to a landowner. However, claims for compensation arising from s. 112(1) arise by virtue of the presence or existence of the pipeline. The Court concluded that, just as s. 84(a) cannot be read to exclude from arbitration claims for damages arising from the ordinary operation of the pipeline, it cannot be read to exclude from arbitration claims for compensation arising from the effects of s. 112(1). The Court was therefore of the opinion that s. 84(a) does not preclude claims for compensation arising from the effect of s. 112(1) from being referred to an arbitration committee.

The Court concluded that the purpose of the arbitration scheme in Part 5 of the *NEB Act* is to provide a summary and expeditious procedure for the determination of damages suffered by landowners effected by a pipeline, with the object of keeping them whole. The Court could see no valid reason for why losses arising from limitations placed on a controlled area

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[79] [2003] 4 F.C. 30 (C.A.), leave to appeal to S.C.C. refused, [2003] S.C.C.A. No. 193 (QL).

[80] R.S.C. 1985, c. N-7 [*NEB Act*].

should not be compensated, or why the arbitration procedure should not be available for determining such compensation. As a consequence, the Court held that the Minister was in error when he found that the statutory scheme precluded the use of arbitration to determine compensation for losses arising from the controlled area. The Court allowed the appeal, quashed the decision of the Minister and directed the Minister to refer to an arbitration committee the matter of compensation relating to the controlled area.

An application for leave to appeal to the Supreme Court of Canada was dismissed without reasons.[81]

4. COMMENTARY

Arbitration is becoming an increasingly important means by which disputes between oil and gas companies and local landowners are resolved. Since arbitration provides an expeditious procedure for determining damages suffered by landowners, this case demonstrates the broad interpretation that the Courts may give to dispute resolution provisions in legislation that provide alternatives to litigation.

B. *ELK POINT RESOURCES V. BINGEMAN*[82]

1. BACKGROUND

For years oil and gas activities have been the driving force of the Alberta economy. However, exploration and development in the province usually means that a company must build a road and a drill site on a farmer's field. Mechanisms are needed to provide for entry onto private lands, to provide for compensation for use of the lands and to ensure that reclamation takes place upon abandonment. In Alberta, these responsibilities have been given to the Surface Rights Board (the Board) by the *Surface Rights Act*.[83] The following case was an application by Elk Point Resources Inc. (Elk Point) for *certiorari* quashing a decision by the Board and for an order prohibiting the Board from proceeding with an inquiry.

2. FACTS

In 1990, Bingeman signed a consent for the surrender and release of a surface lease so that a reclamation certificate could be issued. Notice of the surrender and termination of the lease was not served on Bingeman. In 1996, the application for a reclamation certificate was cancelled. In February 2002, Conestoga Farms, a Bingeman family company and successor in title to the lands, applied to the Board for rentals owing from February 1991 to 2002. After the Board had conducted standard searches on Elk Point, it notified the company that it was required to provide proof of payment, failing which the Board could suspend its right to enter and order payment by the Minister of Finance. Elk Point said that it ceased to pay rent because of the release and consent signed by Bingeman in 1990. The Board advised that the remediation process had not been completed and that the obligation to pay continued. A

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81 [2003] S.C.C.A. No. 193 (QL).

82 [2003] A.J. No. 205 (Q.B.) (QL).

83 R.S.A 2000 c. S-24 [*Surface Rights Act*].

suspension order was issued. Elk Point requested a hearing. It argued that the application submitted by Conestoga was deficient, that the lease had been surrendered and that any claim was barred by the passage of time.

3. DECISION

The Alberta Court of Queen's Bench dismissed the application. The Court concluded that there were outstanding issues regarding: (1) whether the lease was valid or whether it was surrendered; (2) the effect of the issuance of a reclamation certificate; (3) the effect of the executed release signed in 1990; and (4) whether limitations legislation was applicable. In light of these unresolved issues, the Court concluded that the Board's actions were entirely appropriate because they had to be decided in order to resolve the matter with finality.

Prior to contacting Elk Point, the Board had obtained three documents: a corporate search, the status of the reclamation certificate and a document entitled "List of Mineral Holders for Recovery of Rental Applications." Elk Point argued that the Board violated the rules of natural justice by conducting its own investigation. The Court noted that the rule against administrative tribunals conducting their own inquiries is to ensure that one or both sides have seen all the evidence that the Board considers and to avoid the appearance that the Board is entering into the arena of adducing evidence. However, the documents obtained in this case were all documents of public record, which simply confirmed the status of Elk Point and its relationship to the land in question. In the Court's view, obtaining those documents did not violate the rules of natural justice. When it became clear that Elk Point disputed the obligation to pay, the Board set a hearing date. The Court concluded that in doing so, the Board did not violate the rules of natural justice and did not err in law.

4. COMMENTARY

The *Surface Rights Act* provides an important means by which to ensure that a landowner will be compensated where it cooperates with the oil and gas industry and provide access to its lands. The scheme for addressing claims for unpaid rent is set out in s. 36, which provides that where money payable by an operator under a surface lease has not been paid, the person entitled to receive the money may submit written evidence of non-payment to the Board. Upon receipt of the evidence, if the Board considers that the evidence satisfactorily proves non-payment, the Board shall send written notice to the operator demanding full payment. If payment is not made pursuant to that notice, the Board may by written order suspend the operator's right to enter the site and, further, may terminate the operator's right to enter upon giving written notice. If the operator's rights have been terminated and full payment is still not made, the Board may direct the Provincial Treasurer to pay the claim. That then becomes a debt against the operator. The *Surface Rights Act Rules of Procedure and Policy*[83] provide that where a party requests that the Board review, rescind or amend a decision, the Board may hold an inquiry if the matters raised by the request justify an inquiry.

[83] Alta. Reg. 190/2001.

XIV. INJUNCTIONS

A. *ALTAGAS SERVICES V. BELAIR ENERGY CORP.*[84]

1. BACKGROUND

This was an application by AltaGas Services Inc. (AltaGas) for injunctive and declaratory relief requiring BelAir Energy Corporation (BelAir) to direct its gas to a shared gas plant and gathering facility. When determining whether an injunction is appropriate under the circumstances, the courts will apply the tripartite test established by the Supreme Court of Canada in *RJR MacDonald v. Canada (A.G.).*[85] The test involves an assessment of whether:

(i) there is a serious issue to be tried;
(ii) irreparable harm would result that cannot be compensated by damages; and
(iii) the balance of convenience favors a granting of the injunction.

2. FACTS

The plaintiff, AltaGas, was a midstream energy company with a majority interest in a natural gas plant and gathering facility. The defendant, BelAir, was an oil and gas exploration company with a minority interest in the plant and facility. A gathering and processing agreement existed between the parties under which BelAir was required to send dedicated gas to the existing facility but was allowed to arrange for alternative processing for new gas. AltaGas accused BelAir of breaching the gathering and processing agreement by directing dedicated gas to another facility and applied for an interlocutory injunction to restrain BelAir from diverting the gas.

3. DECISION

The Alberta Court of Queen's Bench allowed the application. The Court held that BelAir was under a contractual obligation not to process dedicated gas at facilities other than the one contemplated in the agreement. In determining whether to issue an injunction, the Court considered that if the injunction was not granted, AltaGas would be forced to decommission the facility and reclaim the land. The Court noted that although an award of damages could compensate AltaGas for the decommissioning and reclamation, it would be difficult to quantify the damages associated with the permanent market loss caused by the premature closure and decommissioning of the facility. Thus, the Court concluded that the premature shutdown of the facility and subsequent loss of business constituted irreparable harm.

AltaGas submitted that BelAir had committed a clear breach of a negative covenant. The Court confirmed that if such a breach is established, the tripartite test for an interlocutory injunction is applied less rigorously and an applicant is not required to prove that it will suffer irreparable harm. The Court held that the relaxation of the tripartite test should only be used where the applicant provides compelling evidence of the breach of a negative

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84 [2003] A.J. No. 1127 (Q.B.) (QL).

85 [1995] 3 S.C.R. 199.

covenant; otherwise, a full examination of the tripartite factors must be carried out. The Court concluded that by processing the gas through an alternate facility, BelAir breached a negative covenant, such that the tripatite test for an interlocutory injunction did not have to be strictly applied. The Court ultimately allowed the application and concluded that there was a serious issue to be tried, that AltaGas had shown irreparable harm and that the balance of convenience favoured AltaGas.

4. COMMENTARY

This case demonstrates the need for corporations to comply with contracts for the gathering and processing of oil and gas. Where a corporation deviates from the terms of a contract, a court may find the breach of a negative covenant and thereby relax the tripartite test required to obtain an injunction. Although courts typically demonstrate a reluctance to grant injunctions except in the most serious cases, the relaxation of the tripartite test facilitates the ability of a plaintiff to obtain injunctive relief pending the resolution of a dispute.

XV. ENVIRONMENTAL LAW

A. *MCCOLL-FRONTENAC V. ALBERTA (MINISTER OF THE ENVIRONMENT)*[86]

1. BACKGROUND

The legislative scheme for appealing an Environmental Protection Order is somewhat unusual. The appeal is commenced through the Environmental Appeal Board (the Board). The Board conducts the appeal through an oral hearing or by written submissions. Under s. 95(2) of the *Environmental Protection and Enhancement Act*,[87] the Board determines what matters will be included in the hearing of the appeal. Section 99(1) requires that following the hearing the Board must submit a report to the Minister with its recommendations and a summary of the representations that were made to it.

Under s. 92(1), it is the Minister and not the Board who decides the matter and he can confirm, reverse or vary the decision appealed. The Minister is empowered to make any decision he considers appropriate. Once the Minister makes a decision, he is required under s. 100(2) to give notice to the Board immediately and the Board is then required to give notice of the decision to all interested parties. Thus, while it is the Board that holds the hearing, it is the Minister who makes the ultimate decision.

2. FACTS

This was an application by McColl-Frontenac Inc. (McColl) for the judicial review of a decision of the Minister of the Environment to confirm an Environmental Protection Order granted by the Director of Enforcement and Monitoring. McColl stored gasoline in underground tanks on their lands. The tanks were removed before McColl sold the site to

86 (2003), 336 A.R. 234 (Q.B.).
87 R.S.A. 2000, c. E-12 [*EPEA*].

another company. Following the sale, it was discovered that the land was contaminated by hydrocarbons. The *EPEA* came into force after the sale. An Environmental Protection Order (the Order) was issued in respect of the contaminated lands. McColl appealed the decision to the Environmental Appeal Board, which recommended upholding the Order. The Minister accepted the recommendations of the Environmental Appeal Board without reasons. McColl then applied for a judicial review of the Minister's decision on the basis that his failure to give reasons was a breach of natural justice.

3. DECISION

The Alberta Court of Queen's Bench dismissed the application. The Court determined that where the Minister does not issue reasons of his own and signs the Order proposed by the Board, it can be presumed that the Minister has adopted the reasoning of the Board and that the Board's reasons are essentially the Minister's. The Court noted that if the Minister was aware of a possible breach of natural justice by the Board, he could act to cure the breach by providing reasons that demonstrated that he was aware of the breach and his decision was able to cure the taint. However, where the Minister does not provide reasons and has adopted the Order prepared by the Board without changes, any breach of natural justice or duty of fairness by the Board must render the Minister's decision *ultra vires*. The Court concluded that, in this case, there was no requirement for the Minister to provide reasons because there were no material misrepresentations that would render the Board's reasons inaccurate and thereby require the Minister to give reasons of his own.

McColl argued that the Environmental Appeal Board erred in finding that there was a public protection exception to the presumption against retrospectivity. The presumption against the retrospective operation of legislation holds that statutes are not to be construed retrospectively unless such a construction is expressly or by necessary implication required by the language of the statute. One exception to this presumption, however, is where the purpose of the statute is for public protection. The Court concluded that the purpose of the *EPEA* was public protection. The Court noted that the principal aim recognizes the value of protecting the environment, which is essential to the integrity of human health and the well-being of society, as well as ensuring that there is economic growth and prosperity. As a consequence, the Court concluded that there was an absence of the presumption in this case. In addition, one of the objectives of the *EPEA* is that the polluter should pay. The Court held that this is consistent with imposing an obligation not on the present occupier, but upon those who caused the pollution in the first place.

4. COMMENTARY

The Court held that there is no requirement for the Minister to provide reasons where there are no material misrepresentations that render the Board's reasons inaccurate, thereby requiring the Minister to give reasons of his own. The decision makes it clear that the appeal of an Environmental Protection Order is a two-step process in which the Board holds a hearing, accepts submissions and renders an advisory opinion to the Minister, who can then either accept or reject the recommendation. Where the Minister decides to accept the Board's recommendations in their entirety, the Minister's reasons are those of the Board.

B. *IMPERIAL OIL LTD. V. ALBERTA (MINISTER OF THE ENVIRONMENT)*[88]

1. BACKGROUND

This was an application by Imperial Oil Ltd. (Imperial) for the judicial review of a decision of the Minister ordering Imperial to remediate lands that it previously owned. The issue under consideration was whether the Director could delegate to the property owner his authority to determine whether a contaminated site was adequately remediated.

2. FACTS

Over 30 years ago, Imperial owned lands that were used in conjunction with a hydrocarbon refinery. The lands were reclaimed and redeveloped into a residential community. However, the levels of hydrocarbon vapors and lead in the soil exceeded acceptable levels. An Environmental Protection Order was issued that required Imperial to remediate the site "to the satisfaction of the property owner." Imperial appealed the Order to the Environmental Appeal Board. The Board provided a report to the Minister recommending that the Order be confirmed, but varied it to read that the remediation must take place to the satisfaction of the Director. The Minister issued his decision without the modifications recommended by the Board. Imperial applied for the judicial review of the decision on the basis that the Minister breached the rules of procedural fairness and natural justice by delegating his decision-making authority to a party adverse in interest.

3. DECISION

The Alberta Court of Queen's Bench allowed the application. The Court concluded that the Director could not delegate the determination of the level of remediation to the property owner. The Court noted that when the Board provided its report to the Minister, the report recommended that the Order be varied to indicate that all work under the Order should be performed to the satisfaction of the Director. However, when the Minister issued his decision, he ordered the Director to require compliance with the Order without mentioning the modifications recommended by the Board. The Minister, in rejecting part of the recommendations but not providing reasons, left unanswered questions that were significant to all parties. The Court held that if the effect of the Minister's decision was to confirm the direction that Imperial was required to restore all private residential property to its predisturbed condition to the satisfaction of the property owner, then the decision was patently unreasonable and a reviewable error. As a result, the Court directed the Minister of the Environment to provide reasons for his Order and specifically address his decision.

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88 (2003), 338 A.R. 1 (Q.B.).

4. COMMENTARY

Since the statutory scheme provides that the remediation must be done to the Director's satisfaction, the Court concluded that this responsibility cannot be delegated to the satisfaction of a third party. A third party has no objective standard, especially where the decision-making authority has been delegated to parties who are adverse in interest. The Court concluded that the statutory scheme puts the decision-making power in the Director and gives legislative sanction for the work to be done to the Director's satisfaction. As a consequence, the Director cannot delegate the level of remediation and must clearly retain ultimate control over "satisfaction" with the remediation. We understand from counsel that some issues are under appeal.

C. *SIERRA CLUB OF CANADA V. CANADA (MINISTER OF FISHERIES AND OCEANS)*[89]

1. BACKGROUND

The development of infrastructure for oil and gas operations may trigger environmental impact assessments under the *Canadian Environmental Protection Act, 1999*.[90] Environmental Impact Assessments under *CEPA* require public participation and stakeholder involvement. The public is entitled to review both the Environmental Impact Statement (EIS) and the Screening Report and to provide their comments so that the potential impacts of the project can be properly assessed. The issue under consideration in the following application was what constitutes providing adequate and meaningful public review of an EIS and the screening report.

2. FACTS

This was an application by the Sierra Club of Canada (Sierra Club) for judicial review of a decision of the Minister of Fisheries and Oceans approving a request by Bounty Bay Shellfish (Bounty) and 5M Aqua Farms (5M) to operate aquaculture facilities. During the statutory procedure for public consultation, Bounty and 5M advised the Minister that information in the EIS disclosed commercially sensitive information to competitors. To help alleviate the problem, the Minister allowed the corporation to make five copies of the statement available at public areas, with the stipulation that none of the copies were to be reproduced or removed. The Sierra Club asked for a copy of the statement so that their marine experts could review it. The Minister advised them that the material was copyrighted and could be viewed only at the five locations. Since the locations were inaccessible to the Sierra Club, they were eventually sent a copy of the report.

The Sierra Club objected to the delay and asked for an extension of five weeks to the review period to allow it to make an appropriate study of the statement. The Minister replied that an environmental screening was ongoing and that comments on the EIS were welcomed. However, the review period was not extended. The screening report supplied to the Minister

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89 (2003), 229 F.T.R. 31 (T.D.).

90 S.C. 1999, c. 33 [*CEPA*].

determined that the proposed project was not likely to cause significant adverse environmental effects. Relying on the screening report, the Minister approved the project. The Sierra Club objected on the basis that the Minister breached its right of procedural fairness and committed a reviewable error in granting the approval.

3. DECISION

The Federal Court of Canada allowed the application and quashed the Minister's decision. The Court concluded that the Minister breached the Sierra Club's right to review the impact document effectively. The limited access to the statement did not provide the Sierra Club with enough time to undertake its review properly. The Minister therefore unreasonably relied on the screening report without adequately soliciting public review and comment. As a result, the decision could not stand.

The Court noted that *CEPA* requires that the responsible authority give the public notice and an opportunity to examine and comment on the screening report and on any record that has been filed in the public registry before taking a course of action. *CEPA* also provides that a public registry must be established and operated in a manner to ensure convenient public access in respect of every project for which an environmental assessment is conducted. The Court was of the opinion that, because the EIS was only available in five locations and that the applicant was unable to secure a copy until less than three weeks before comments were due, the Sierra Club was not provided with enough time to properly undertake its review. In addition, the Court concluded that by unjustifiably declaring the EIS copyrighted and protected property in light of the supposedly sensitive commercial nature of some of its parts, the Minister failed to meet his obligations pursuant to *CEPA*. The Court required that a reasonable period be given so that the public could review and comment on the EIS and the screening report before the final decision is made. The Court therefore concluded that the Minister unreasonably relied on the screening report without adequately soliciting public review and comment and, as a result, the decision could not stand. The Court granted the application for judicial review and the decision of the Minister of Fisheries and Oceans approving the project was quashed.

4. COMMENTARY

The Court concluded that once a responsible authority has exercised its discretion and determined that public participation is appropriate, it has an obligation to give the public an adequate opportunity to examine and comment not only on the EIS but also the screening report. However, in this case, the public was not given the opportunity to examine and comment on the screening report due to the brief period of time that was provided in between issuing the screening report and making the final decision. The Court therefore concluded that the Minister's failure to fully comply with *CEPA* was an error that justified setting aside the decision under review.

XVI. FIRST NATIONS

A. *SAULTEAU FIRST NATIONS V. BRITISH COLUMBIA (OIL AND GAS COMMISSION)*[91]

1. BACKGROUND

Although s. 35 of the *Constitution Act, 1982*[92] gives significant constitutional status to Aboriginal and treaty rights, there are other provisions that give the federal and provincial governments the power and the responsibility to make laws with respect to various matters, to make decisions and ultimately to govern. These include the power to restrict the way certain activities are carried out and the power to authorize activities that may affect third parties, including First Nations.

In order to give effect and meaning to the various provisions of the *Constitution Act, 1982*, the courts have had to reconcile these provisions and have done so by holding that, notwithstanding that s. 35 rights are constitutionally recognized, such rights are not absolute and may be infringed by the federal and provincial governments when the circumstances justify such an infringement.

2. FACTS

In this case, the Saulteau First Nations (SFN) applied to have the Court quash a decision made by the British Columbia Oil and Gas Commission (the Commission), which allowed Vintage Energy Canada Ltd. (Vintage) to construct an exploratory well site with associated roads and infrastructure in the SFN's traditional territory. Additionally, the SFN applied for various declarations that would restrict the Commission's powers and require the Commission to engage in good faith consultation with the SFN in the future.

Vintage is a corporation that explores for and develops oil and natural gas resources in British Columbia and other places. Vintage held rights to explore for and produce oil and gas in an area to the northwest of the SFN reserve, and it sought to exercise these rights by constructing a well, winter access road, decking site, remote sump and temporary camp site. This development proposal, however, required the approval of the individual who is the Wells Program Manager of the Commission (the Decision-Maker). This proceeding therefore arose out of an earlier application by Vintage to have the Commission approve a well authorization permit pursuant to s. 85 of the *Petroleum and Natural Gas Act*.[93]

Prior to the application for well authorization, the SFN had identified several geographical areas of interest for the purpose of alerting the province to its concern that its treaty rights were being negatively impacted by oil and gas development. As well, there is a smaller area in closer proximity that the SFN identified as the Area of Critical Community Interest

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91 (2004), 11 Admin. L.R. (4th) 210 (B.C.S.C.), aff'd (2004), 201 B.C.A.C. 78, leave to appeal to S.C.C. refused, [2004] S.C.C.A. No. 341 (QL).

92 Being Schedule B to the *Canada Act 1982* (U.K.), 1982, c. 11.

93 R.S.B.C. 1996, c. 361.

(ACCI) and a relatively undeveloped portion of land known as the "Peace-Moberly Tract." The Commission consulted with the SFN about all oil and gas development in these areas and did so with respect to the Vintage application as well. The consultation between the SFN, the Commission and Vintage consisted of face-to-face meetings and the exchange of written documents. At one such meeting, held 22 January 2003, the SFN asked that Vintage hold off its activities until a cumulative effects assessment, a First Nations land use plan and an Integrated Resource Management Study could be completed and that the Commission not approve the application until the assessment and studies had been completed.

Despite SFN's request, the Decision-Maker issued his reasons for approving Vintage's application on 14 March 2003. All elements of the application were approved on the condition that Vintage construct the well in frozen ground conditions so as to minimize the impact to the environment and fish and wildlife habitat, in addition to First Nation treaty rights and trapping activities. The SFN applied for a review of the well authorization by the Advisory Committee, and the Advisory Committee recommended the parties engage in alternative dispute resolution. The Commission refused to heed this recommendation, forcing the SFN to apply for this review by the British Columbia Supreme Court.

The SFN's primary argument was that the Commission's constitutional and statutory duties regarding Aboriginal and treaty rights require consideration of how the Crown's approval of activities affects those rights. The SFN submitted that this obligation is not limited to local or direct effects, but includes the obligation to consider all relevant effects. The SFN also says that the evidence clearly shows that the Commission did not accommodate, and had no intention of accommodating, its Treaty 8 rights.

3. DECISION

The Court in this case had to resolve the conflict between the s. 35 treaty rights of the SFN and the provincial government's exercise of powers under the *Petroleum and Natural Gas Act*. To do so, Cohen J. employed the test initially set out *R. v. Sparrow*[94] and summarized in *R. v. Gladstone*:[95]

a. Is there an existing Aboriginal right?
b. Has the right been extinguished?
c. Has there been a *prima facie* infringement of that right?
d. Can the infringement be justified?

In applying this test, the Court found that the SFN established that there is an existing Aboriginal right. Vintage accepted that these rights exist and noted that these rights were the basis for their consultation efforts with the SFN. Vintage argued, however, that it was not sufficient for the SFN, having established its treaty rights, simply to show that the activities associated with the well application will take place in areas important to the exercise of those rights. The SFN bears the further onus of establishing a *prima facie* interference with their treaty rights.

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94 [1990] 1 S.C.R. 1075 [*Sparrow*].
95 [1996] 2 S.C.R. 723 at para. 20.

Vintage's position was that there was no evidence or indication during the consulting process that the approval of a well authorization permit would have any direct or indirect effects on the exercise of the SFN's treaty rights to hunt, fish and trap. Further, there was certainly no indication that it would constitute an erosion of an important aspect of the SFN's treaty rights. Lastly, Vintage submitted that there was never any suggestion made by the SFN on how Vintage's proposed activities could be changed or modified to avoid or minimize any direct or indirect effects on the SFN's rights.

If the SFN could demonstrate a *prima facie* infringement, the onus shifts to the Commission to show that the infringement is justifiable. The justification test involves a further two-part analysis set out in *Sparrow* as follows:

a. Is there a valid legislative objective?
b. Has the Crown met its "fiduciary" obligation to the First Nation?[97]

On the first part, Vintage submitted that the general development of the province's petroleum and natural gas resources under the *Petroleum and Natural Gas Act* and its related legislative enactments represent a compelling and substantial legislative objective. Therefore, if there has been a *prima facie* infringement of a First Nation's treaty rights, the underlying objectives of the legislative scheme can provide justification for such an infringement.

On the second part, there was not only argument as to whether the Commission satisfied its fiduciary obligation to the SFN, but the Commission also questioned whether such duty was owed at all. The Commission submitted that the existence of a duty of procedural fairness, which the Commission owes to Vintage, is fundamentally inconsistent with the existence of a fiduciary duty of the kind alleged by the petitioner. The Commission based its argument on *Quebec (A.G.) v. Canada (National Energy Board)*,[98] where it was suggested that the courts must be careful not to compromise the independence of quasi-judicial tribunals and decision-making agencies by imposing upon them fiduciary obligations that require that their decisions be made in accordance with a fiduciary duty.

Justice Cohen distinguished the present case from that of *Quebec (A.G.)* by finding that the Commission, unlike the National Energy Board, is simply an administrative decision-maker and does not perform a quasi-judicial role. For this reason, the Commission (including the Decision-Maker) has fiduciary and constitutional obligations to engage in good faith consultation with the SFN. Consultation must be in good faith and with the intention to substantially address the concerns of the First Nation whose lands are in issue. Furthermore, the Crown's duty to consult imposes on it a positive obligation to ensure reasonably that the First Nation has the opportunity to express their concerns to ensure that their representations are seriously considered and, wherever possible, to ensure that their representations are demonstrably integrated into the proposed plan of action. A reciprocal duty exists on the part of the First Nation to participate and consult in good faith and not to frustrate the process by refusing to meet or participate or by imposing unreasonable conditions.

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97 *Sparrow*, *supra* note 95 at paras. 71-75.
98 [1994] 1 S.C.R. 159 [*Quebec (A.G.)*].

Based on the criteria above and a standard of correctness, the Court assessed whether the Commission had satisfied its fiduciary obligations. Justice Cohen came to the conclusion that the Commission was correct in law by granting the well authorization. He noted that the SFN did not categorically object to the application and that at no time leading up to it did the SFN identify to the Commission any adverse direct or indirect impacts the well may have if granted. In the absence of any contradictory evidence from the SFN, the Decision-Maker took into account all of the relevant factors and imposed the necessary conditions. He also found that the Commission listened to the SFN's concerns and made serious efforts to accommodate them. In doing so, Cohen J. found that the Commission met its constitutional and fiduciary obligations and he therefore dismissed the application on this issue.

Justice Cohen also found the legislation as a whole to be constitutionally valid as well, in spite of the SFN's contention that it allowed the Decision-Maker unstructured discretion to infringe Aboriginal or treaty rights. He stated that the *Petroleum and Natural Gas Act* provides a set of unifying principles to guide the Commission's exercise of discretion in a diverse array of factual and statutory settings. The nature of regulation of oil and gas natural resources requires that the Commission be granted broad authority with these guiding principles to ensure a balance between economic, social and environmental considerations. As a result, the constitutional challenge to the Commission's governing legislation was also dismissed.

4. COMMENTARY

The important principle to take from this case is that there is a firm constitutional requirement for oil and gas companies and regulators to undergo consultation with First Nations when treaty lands are the subject of a development proposal. The British Columbia Oil and Gas Commission in particular was found not to be a quasi-judicial body and thus owes certain fiduciary duties toward First Nations. In this case, however, the First Nation had failed to provide evidence to the Commission how the well authorization would create adverse impacts and infringe on its treaty rights. Judging from this case, decisions made by regulatory authorities in relation to conventional oil and gas development on treaty lands will be subject to less judicial scrutiny than the granting of tree farm licences, for example. This case was affirmed by the British Columbia Court of Appeal shortly before the finalization of this article.