

Supreme Court Redwater Decision: Implications for the North

Charles J. Birchall

Partner, Certified Specialist in Environmental Law by the Law Society of Ontario

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Orphan Well Association v. Grant Thornton Limited – Redwater Facts

- **Redwater Energy Corporation was a publicly listed oil & gas production company in Alberta**
- **Held 127 licences for oil & gas wells, pipelines & waste disposal facilities**
- **Alberta Energy Regulator administers the *Oil & Gas Conservation Act* (“OGCA”) & *Pipelines Act* (“PA ”)– a complete framework for oil and gas extraction & pipeline operations**

Redwater Facts Continued (2)

- **AER can issue orders requiring a licensee to remediate & decommission a Licenced Asset (“Abandonment Order”)**
- **Under Directive 006 the AER will only approve the sale of Licenced Assets if it does not worsen the Licensee’s Management Rating (“LMR”) below a certain threshold**
- **Purpose of LMR is to protect the public from bearing costs of End of Life Obligations**

Redwater Facts Continued (3)

- **Orphan Well Association (“OWA”) is another means of protecting the public from bearing these costs**
- **OWA’s primary purpose is to perform End of Life Obligations that are designated by AER as “orphans”**
- **The orphan fund is funded almost entirely by industry contributions collected by the AER**

Redwater Facts Continued (4)

- In 2015, Redwater's principal creditor, Alberta Treasury Branches ("ATB"), applied for a bankruptcy order against Redwater
- Grant Thornton ("GT") was appointed as Receiver under the *Bankruptcy and Insolvency Act* ("BIA")
- AER advised GT that it was responsible for Redwater's End of Life Obligations

Redwater Facts Continued (5)

- **GT advised AER that it would only take 20 of the 127 Licensed Assets and disclaim the rest**
- **GT's reason was that the End of Life Obligations for the Disclaimed Assets exceeded their value**
- **AER issued Abandonment Orders for the Disclaimed Assets**

Redwater Issues

- **Do AER's statutory Abandonment Orders to remediate environmental harm have priority over secured claims in bankruptcy?**
- **Can trustees and receivers renounce these environmental obligations?**

Alberta Court of Queen's Bench

- **ACQB issued a bankruptcy order vesting all of Redwater's property with GT as Trustee of the estate**
- **AER & OWA brought an application directing GT to comply with Abandonment Orders**
- **GT & ATB brought a cross-application for an declaration that the OGCA & PA were inoperative**

ACQB Decisions

- **Abandonment Orders are provable claims & interfere with the priority of distribution under the BIA**
- **Abandonment Orders are “intrinsically financial” since GT required to post security deposits**
- **Section 14.06(4) of the BIA creates a positive entitlement for GT to renounce the Disclaimed Assets**

Section 14.06(4) of the BIA

“... where an order is made which has the effect of requiring a trustee to remedy any environmental condition or environmental damage affecting property involved in a bankruptcy, proposal or receivership, the trustee is not personally liable for failure to comply with the order, and is not personally liable for any costs that are or would be incurred by any person in carrying out the terms of the order,

(a) if... the trustee

(i) complies with the order, or

(ii) on notice to the person who issued the order, abandons, disposes of or otherwise releases any interest in any real property, or any right in any immovable, affected by the condition or damage;

Alberta Court of Appeal - Decision

- **AER & OWA appeal dismissed (2-1 decision)**
- **Abandonment Orders are provable claims in bankruptcy and subject to the BIA**
- **AER & OWA concede they are creditors & Court finds that Abandonment Orders are “intrinsically financial”**
- **The BIA does not give Abandonment Orders super priority status**

ACO – Decision (2)

- **OGCA & PA in conflict with the BIA**
- **Section 14.06(4) provides insolvency officials with an unqualified right to renounce assets**
- **Abandonment Orders would frustrate the purpose of the BIA because they would interfere with the priority of distribution**
- **Abandonment Orders would reduce amounts recoverable by the ATB thus frustrating the BIA's purpose**

Alberta Court of Appeal - Dissent

- **Abandonment Orders are not provable claims but are continuing regulatory obligations**
- **AER's requirement to post security is not the enforcement of a debt but a condition inherent in the granting of an operating licence**
- **Section 14.06 of the BIA does not apply to Licenced Assets but does protect the trustee from personal liability**

Supreme Court of Canada - Decision

- **AER & OWA appeal granted (5-2 decision)**
- **Definition of “licencee” in OGCA & PA does not create a conflict with s. 14.06 nor frustrate the purpose of the BIA**
- **End of Life Obligations are not claims provable in bankruptcy that are subject to the BIA - based on the *AbitibiBowater* test**

SCC – Decision (2)

***AbitibiBowater* Test re Provable Claim**

- **Does the bankrupt owe a debt, liability or an obligation to a creditor?**
- **Did the bankrupt incur a debt, liability or an obligation before becoming bankrupt?**
- **Is it possible to attach a monetary value to the debt, liability or obligation?**
- **If the answer is “yes” to all three questions, the claim is provable & subject to distribution scheme under the BIA**

SCC – Decision (3)

- **Majority answered “no” to two of the three questions**
- **AER is not a creditor & is enforcing a law of general application for the benefit of all Albertans**
- **But Redwater did incur the liability before becoming bankrupt**
- **Not certain that AER/OWA would fulfill End of Life Obligations hence no monetary value attaches to the Obligations**

SCC – Decision (4)

- **Is there a conflict between the Alberta Regulatory Scheme & the BIA, s. 14.06?**
- **Applying the principle of co-operative federalism, the Majority rejected GT’s argument that the definition of “licencee” created the potential for a conflict with the BIA**
- **“The mere theoretical possibility of a conflict” should not render the regulatory provision inoperative**

SCC – Decision (5)

- **Section 14.06(4) of the BIA is not in conflict with “licensee” provisions under OGCA & PA**
- **Section 14.06(4) only shields trustees from personal liability**
- **Section 14.06(4) does not relieve the bankrupt’s estate from liability arising from the trustee’s failure to comply with a regulatory order**

SCC – Dissent

- **Applying the first part of the *AbitibiBowater* test, the AER conceded that it was creditor before the lower courts. Not appropriate to revisit the issue**
- **Applying the third part of the *AbitibiBowater* test, the AER would eventually be responsible for Redwater's End of Life Obligations**
- **Alternatively, the AER would deem the renounced assets as orphan wells and thus become the responsibility of the OWA. No real distinction between the AER & OWA**

SCC – Dissent (2)

- **AER & OWA created a monetary debt in a favour of the AER by imposing conditions on the sale of Redwater’s assets**
- **End of Life Obligations would frustrate the purpose of the BIA, replacing the “polluter-pays principle” with a “lender-pays regime”**
- **Definition of “licencee” creates an operational conflict with s. 14.06 of the BIA**



Implications of SCC Decision

- **Could be amendments to the BIA to better reflect the Dissent: environmental liabilities will not have super-priority status**
- **Notwithstanding the AER “win”, regulators could be more rigorous in demanding up front (before issuing licences) hard financial assurance to meet closure and reclamation obligations. Will also continue to issue orders against current and former directors and officers of the company**
- **Regulators may seek to upgrade their skills and knowledge to better assess corporate financial capacity throughout the life of a project**

Implications of SCC Decision (2)

- **Regulators may copy/emulate AER-type licensing regime to improve chances of achieving super-priority status for orders**
- **Processes may be put in place for better communication between regulators to co-ordinate security requirements**
- **Lenders/creditors could conduct more thorough investigations into potential borrower environmental liabilities throughout the lender-borrower relationship**

Implications of SCC Decision (3)

- **“We expect lenders or creditors to now require more of their borrowers to buy [environmental liability insurance] coverage before they are willing to provide loans or cash to borrowers” – Miles Foxworth, Underwriter, Lloyd’s insurer Beazley Canada**
- **Lenders more likely to require security “readily convertible to cash” and in a form beyond the reach of regulators and other creditors**
- **Courts may revisit *AbitibiBowater* test**

Implications of SCC Decision (4)

- ***Redwater* adds to law on the priority of environmental regulatory orders in cases of insolvency**
- ***Redwater* confirms that the BIA protects trustees and receivers from personal liability but that they cannot easily renounce environmental obligations**
- ***Redwater* is unlikely to be the final word**

Contact Information

Charles J. Birchall

(613) 761-2424

cbirchall@willmsshier.com

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Called to the Bars of Ontario, Nunavut and
the Northwest Territories



Willms & Shier Environmental Lawyers LLP

www.willmsshier.com

