Dalhousie Journal of Legal Studies

Volume 1 Article 11

1-1-1992

Secured Creditors' Right Threatened: Oil and Gas Wells Must be Made Environmentally Safe Before Creditors Paid

Harry J. Thompson

Follow this and additional works at: https://digitalcommons.schulichlaw.dal.ca/djls

 Part of the Law Commons

This work is licensed under a Creative Commons Attribution-Noncommercial-No Derivative Works 3.0 License.

Recommended Citation

Harry J Thompson, "Secured Creditors' Right Threatened: Oil and Gas Wells Must be Made Environmentally Safe Before Creditors Paid" (1992) 1 Dal J Leg Stud 185.

This Article is brought to you for free and open access by the Journals at Schulich Law Scholars. It has been accepted for inclusion in Dalhousie Journal of Legal Studies by an authorized editor of Schulich Law Scholars. For more information, please contact hannah.steeves@dal.ca.

Secured Creditors' Rights Threatened: Oil and Gas Wells Must be Made Environmentally Safe Before Creditors Paid

Harry J. Thompson*

Panamericana de Bienes y Servicios S.A. v. ***Northern Badger Oil & Gas Ltd.***[1]

The recent decision of the Alberta Court of Appeal may have a detrimental effect on secured creditors by allowing a provincial administrative body to circumvent the ranking provisions contained in the *Bankruptcy Act*.[2]

Northern Badger Oil and Gas Limited was placed into bankruptcy on July 7, 1987 and Collins Barrow Limited was appointed Trustee in Bankruptcy. Panamericana held a floating charge debenture security over certain assets owned by Northern Badger. In May 1987, Panamericana applied for and obtained a court order appointing Vennard Johannesen Insolvency Inc.

> ...Receiver and Manager of all the undertaking, property, and assets of the Defendant, Northern Badger Oil and Gas Limited with authority to manage, operate, and carry on the business and undertaking of the Defendant....[3]

Included in the assets were licences to operate thirty-one oil and gas wells, eleven of which were producing and the balance standing in a non-producing condition. Northern Badger held about ten per cent ownership interest in each well.

The Energy Resources Conservation Board (ERCB) was concerned the wells would be improperly managed and thus left orphaned as opposed to abandoned.[4] The ERCB made its concerns known to the receiver in July 1987. The receiver reported that twenty-one of the wells had been transferred to other parties. The remaining wells were subsequently transferred to Senex Corporation by a court approved sale on January 15, 1988.

The agreement between the receiver and Senex contained a 'black out' clause whereby the purchaser could exclude any interest in wells which were valued at less than the cost of abandonment. Consequently, seven wells were passed back to the receiver and they will all require abandonment at a considerable cost. In May 1989, the ERCB learned of the black out clause and, through an Order-in-Council

obtained on June 6, 1989, enjoined the receiver to submit plans for abandonment programmes for the seven wells.

The key issue examined in this case is whether a court appointed receiver or manager of an insolvent and bankrupt oil company must comply with an order of the ERCB.

Trial Decision[5]

The trial judge found the ERCB's order tantamount to a claim and, therefore, concluded that the ERCB ranked as an unsecured creditor. Mr. Justice MacPherson's authority came from the definition of the term 'creditor'[6] and the usage of the term 'provable claim'[7] found in the *Bankruptcy Act*.[8] Having found that the ERCB ranked as a creditor, Mr. Justice MacPherson held that the Order-in-Council was *ultra vires* as it attempted to undermine the provisions of the federally enacted *Bankruptcy Act* regarding the ranking of creditors.

Appeal Decision

The Alberta Court of Appeal reversed the decision of the lower court. Mr. Justice Laycraft, speaking for the full court, held that the ERCB had the power, when authorized by the Lieutenant Governor-in-Council, to order the abandonment of wells 'by some person'. Mr. Justice Laycraft further stated that a public officer or a public authority given the duty to enforce a public law did not thereby become a creditor of the party bound to obey. By following this analysis, the court found no violation of the priority provisions under the *Bankruptcy Act*.

The Appeal Court concluded that a receiver, regardless of who appointed it and notwithstanding its lack of legal title in the property, assumed the licencee's obligations and was, therefore, bound by such orders. It made no difference that the evidence failed to establish that the orphaned wells presented any danger.

Reasons for Judgement

The process of abandonment of oil and gas wells is part of the general law of Alberta enacted to protect the environment and mankind. Therefore, it was unnecessary to establish that the wells posed a threat in the instant case.

Alberta's regulatory scheme regarding oil and gas is contained in the *Energy Resources Conservation Act*[9] and the *Oil and Gas Conservation Act*.[10] Under this regime, the ERCB, with authorization of the Lieutenant Governor-in-Council, has wide general powers to regulate the industry. The regulatory regime contemplates that all wells drilled will one day be abandoned and that the ERCB will have jurisdiction over the process.

In considering the issue of whether the assets in the estate of the insolvent well licencee should be distributed to creditors or applied to the cost of abandonment, the court applies a two step analysis. The first step

is to ascertain if Northern Badger had in fact a 'liability' and the second step determines to whom the liability is owed.

The abandonment of wells is an expense inherent in the nature of the oil and gas industry. The moment a well is drilled, a liability is created. However, a public officer or public authority given the duty of enforcing a public law does not become a creditor of the person bound by the law. Had the ERCB elected to bear the cost of abandoning the wells and then sought recovery as permitted under the *Bankruptcy Act*, it would have ranked as an unsecured creditor. As the ERCB was not owed any money, however, the case is distinguished from instances where "some actual impost had been levied against the citizen and a sum of money was due and owing to the specific public authority involved."[11]

The final issue to be determined is whether the receiver, acting as the operator of the oil wells, had a duty to abandon them in accordance with the law.

The receiver takes full responsibility for the management, operation, and care of the debtor's assets without taking legal title to them.[12] The receiver has autonomy from those who procured the appointment. A receiver is an officer of the court and as such its actions become actions of the court. Where the receiver is aware of a legal obligation, it is bound to carry this through, notwithstanding that the obligation relates to assets which are not legally owned by the receiver.

In this case, the receiver had managed the assets of the authorized licencee for more than three years. There was no other entity with whom the ERCB could deal. The receiver cannot now say that, while functioning as a licencee to produce the wells and to profit from them, it assumed none of a licencee's obligations. The court stated it would be a remarkable rule of law which would permit a receiver to walk away from a well which has blown out of control on the basis that remedial action would diminish distribution to secured creditors.[13]

Conclusions

This case addresses the issue of statutorily imposed duties on a receiver. Mr. Justice Laycraft suggests that a statutory duty may be established in situations relating to health, the prevention of fires, the clearing of ice and snow, and the demolition of unsafe structures by suggesting that each duty relates to the general law and that the enforcing authority may not become a creditor under such circumstances.

The court will first look at the powers of the authority seeking the order. If it is within the statutory scheme of the authority to make such an order, the court will consider the nature of the claim. This is a two step process; the first step is to ask if there is a liability and the second step is to determine to whom the liability is owed. If the liability does not fall into the category of "when some actual impost had been levied against the citizen [or company] and a sum of money was due and owing to the specific public authority involved", [14] it will escape the ranking provisions of the *Bankruptcy Act*.

The final determination is the extent to which the receiver is bound by the order. The Court of Appeal stated that, where the order was properly enacted under the statutory scheme, it creates a statutory duty which binds the receiver. The result is that a public authority, validly operating under its enabling statute, may enforce orders requiring a cash outlay to the detriment of secured creditors.

---

* Second year law student, Dalhousie University.

1. (1991), 81 Alta. L.R. (2d) 45 (C.A.).
2. R.S.C. 1985, c. B-3.
3. *Supra*, note 1, at 50.
4. *Supra*, note 1 at 50:

> "Abandonment" and "abandon" are terms with different meanings in the oil industry than when used in their legal sense. In the oil industry they refer to the process of sealing a hole which has been drilled for oil or gas, at the end of its useful life, to render it environmentally safe. In general terms, the process requires that the well bore be sealed at various points along its length to prevent cross-flows of liquids or gases between formations, or into aquifers or from the surface. The cost may vary from a few hundred dollars to tens of thousands of dollars depending on the circumstances.

5. *Panamericana de Bienes y Servicios S.A.* v. *Northern Badger Oil & Gas Ltd.* (1990), 75 Alta. L.R. (2d) 185 (Q.B.).
6. *Supra*, note 2 at Section 2:

> 'creditor' means a person having a claim, preferred, secured, or unsecured, provable as a claim under this Act.

7. *Ibid.*, sections 121(1) and (2) read as follows:

> (1) All debts and liabilities, present or future, to which the bankrupt is subject at the date of the bankruptcy or to which he may become subject before his discharge by reason of any obligation incurred before the date of the bankruptcy shall be deemed to be claims provable in proceedings under this Act.
> (2) The court shall, on the application of the trustee, determine whether any contingent claim or any unliquidated claim is a provable claim, and, if a provable claim, it shall value the claim, and the claim shall after that valuation be deemed a proved claim to the amount of its valuation.

8. *Ibid.*
9. R.S.A. 1980, c. E-11.
10. R.S.A. 1980, c. O-5.
11. *Supra*, note 1 at 58.
12. *Ibid.*, at 60.
13. *Ibid.*, at 65.
14. *Supra*, note 1 at 58.