RECENT JUDICIAL DEVELOPMENTS OF INTEREST TO OIL AND GAS LAWYERS

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This article serves to provide an overview of recent judicial decisions of interest to oil and gas lawyers. The areas discussed include wide ranging topics such as confidentiality, employment, taxation, solicitor-client privilege, duty to consult, and other fundamental issues relating to petroleum law.

Cet article vise à donner un aperçu des récentes décisions judiciaires intéressant les avocats travaillant dans le secteur pétrolier et gazier. Les domaines discutés incluent des sujets vastes dont la confidentialité, l'emploi, la fiscalité, la relation procureur-client, l'obligation de consulter et autres questions fondamentales liées à la législation pétrolière.

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I. BUILDERS' LIENS

A. *RAHCO INTERNATIONAL INC. V. LAIRD ELECTRIC LTD.*[1]

1. BACKGROUND

Oil sands development in Alberta has and will continue to generate new and different scenarios for consideration by our courts due to the uniqueness of the operations and their governing contracts. This case deals with the application of builders' lien legislation to oil sands mining operations.

2. FACTS

The defendant Laird Electric Ltd. (Laird) had contracted with the plaintiff Rahco International Inc. (Rahco) to assemble and complete the electrical connections for several large pieces of mining equipment near Fort McMurray. The equipment was custom-built and had to be brought to the site in pieces and assembled on site. It could only leave the site by being dismantled; however, it was built to move around the site and was only affixed by way of the electrical connection. A dispute arose between Laird and Rahco as to the amount of

[1] 2006 ABQB 592, 398 A.R. 332.

Laird's invoices and Laird filed a builders' lien against the title to Suncor Energy Inc.'s freehold and leasehold mineral interests in the lands where the equipment had been assembled. Rahco brought an application on a summary basis to discharge the lien, claiming that the equipment was not an "improvement to the land" as required by the *Builders' Lien Act*.[2]

3. DECISION

The Court started with the fundamental principle that builders' lien legislation must be strictly interpreted because builders' liens interfere with common law property rights. A two-step analysis had to be undertaken. The first question to be addressed was whether the structure or equipment at issue was attached or affixed to the land. Mere attachment is not sufficient. Second, the Court has to consider the degree of permanence of the attachment, both physically and from a time perspective. The Court found that the inclusion of a clause in the contract indicating that the *Builders' Lien Act* was to apply was not sufficient to change what was mining equipment into an improvement to the land. As a result, Rahco had established that the lien should be removed.

4. COMMENTARY

The expenses incurred on oil sands equipment are significant. Parties supplying goods and services in these circumstances need to keep in mind that, notwithstanding that the goods or services may result in an improvement to the lands, that is only part of the test; the second part, namely the requirement that it form an attachment to the land, may be more difficult to establish in order to provide for the remedies available under builders' lien legislation.

B. *CONSUN CONTRACTING LTD. V. SURMOUNT SAND AND GRAVEL LTD.*[3]

1. BACKGROUND

The application of the concept of a continuing or prevenient arrangement between contracting parties giving rise to an extension of time to file a builder's lien is relevant to many arrangements relating to services in the oil industry based on the ongoing relationships that frequently develop between contractors and developers.

2. FACTS

Two brothers owned two corporations that had worked together for many years. The defendant Surmont Sand and Gravel Ltd. (Surmont) supplied sand, gravel, and equipment to the plaintiff Consun Contracting Ltd. (Consun), who in turn had contracts with various oil companies. Difficulties arose between the two companies as Surmont had not been paid. Surmont filed a builders' lien for the outstanding amounts, some of which related to goods and services supplied outside of the statutory time limit. Consun brought this application to

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[2] R.S.A. 2000, c. B-7, ss. 1(d), 6(1)(2).

[3] 2006 ABQB 164, 392 A.R. 376 [*Consun Contracting*].

either discharge the liens due to late registration, or reduce the amount payable based on the fact that Surmont was out of time for all but a small portion of its claims.

3. DECISION

The onus was on Surmont to establish that a prevenient arrangement existed. Whether that arrangement exists is a question of fact. Relying on the prior decision of *Tage Davidsen Drywall Supplies Ltd. v. Alberta Natural Gas Co.,*[4] and *Re Blue Range Resource Corp.*,[5] the Court found that an arrangement that had a general right to furnish ongoing goods or services for a particular project was sufficient to lead to a finding of a prevenient arrangement. There was a sufficient "thread" linking all of the supply of goods and services to allow for filing of the builders' lien for the full amount of the goods and services supplied regardless of the lapse of time since Surmont had supplied the goods under each of Consun's contracts with third parties.[6]

4. COMMENTARY

The Canadian Association of Oilwell Drilling Contractors model form drilling services contract has the potential to create prevenient arrangements as it provides for ongoing services under one contract. Section 12.5 was specifically included in the model form agreement to find a balance between allowing a contractor who is providing ongoing services with some flexibility before it has to file a builders' lien, and allowing the owners certainty as to when their properties would be free from any lien claims by limiting the prevenient arrangements to defined projects, the scope of which would be set out on the schedules. Similar care needs to be taken in drafting other master form agreements for services.

II. CONTRACTS

A. *HUSKY OIL OPERATIONS LTD. V. LEDCOR INDUSTRIES LTD.*[7]

1. BACKGROUND

Oil and gas pipeline construction projects have many challenges including the high cost of labour and materials, short construction windows (due to weather), and increasingly stringent environmental regulations.

This case illustrates the problems that can arise when a contract is renegotiated under a tight timeline once a project is under way.

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4 (1991), 117 A.R. 143 (C.A.).

5 1999 ABQB 873, 254 A.R. 103 [*Blue Range*].

6 *Consun Contracting*, *supra* note 3 at para. 26.

7 2006 ABCA 122, rev'g 2003 ABQB 751.

2. FACTS

In January 1998, Ledcor Industries Ltd. (Ledcor) entered into a fixed price construction agreement with Husky Oil Operations Ltd. (Husky) to construct a sour gas pipeline by 31 March 1998. With Husky's permission, Ledcor used a mechanized welding process which was new to sour gas pipelines. This process, it was discovered during the course of construction, frequently produced welds which did not meet contract specifications, requiring significant re-welding and causing considerable delay. The welding-related delays combined with other causes (including stringent river crossing requirements imposed by Alberta Environment) made the 31 March 1998 deadline for the original scope of work unreachable. Husky did not want to pay force account rates, and accordingly the parties changed the work schedules and implemented a cost-plus arrangement in place of the earlier fixed price compensation. Although neither party addressed these issues specifically in their negotiations, Ledcor was under the impression that the completion deadline no longer applied and that welding repairs would be done on a cost-plus basis. In contrast, Husky believed that the deadline applied and that Ledcor remained responsible for the welding repairs. Welding difficulties continued after the revisions to the construction contract and Ledcor became concerned that its unionized workers would be raided by other unions if Ledcor worked past the 31 March 1998 deadline. As a result, Ledcor ended up leaving the project with Husky's permission prior to 31 March 1998, with the pipeline incomplete. Husky completed the project, using a different contractor, and sued Ledcor for damages arising from the faulty welding and Ledcor's failure to meet the 31 March 1998 completion date. Ledcor counterclaimed, demanding payment of its unpaid invoices relating to work done prior to 31 March 1998.

At trial, the Court found that: (1) the welding difficulties had arisen because of the use of the new welding procedure, but were not due to Ledcor's negligence and there was no evidence that another contractor would not have had similar problems; (2) the changes to the contract as a result of the delays were amendments to, not a rescission and replacement of, the old contract; (3) the amendments eliminated the 31 March 1998 completion deadline and substituted "cost plus" compensation for "fixed price" compensation; and (4) Husky had agreed to relieve Ledcor of its obligation to complete the contract and thereby: (a) "assumed general liability for the costs associated with having to hire someone else to finish the pipeline,"[8] and (b) relieved Ledcor of the obligation to supply a finished pipeline built to contractual specifications. The trial Court held Ledcor liable for the costs of repairing welds that were not made to specification and for a portion of additional costs resulting from the delay caused by the defective welds. Husky was found liable for payment of Ledcor's outstanding invoices.

Both parties appealed. Ledcor appealed the trial Court's: (1) award to Husky of damages for extra costs occasioned by delay resulting from the faulty welds; (2) use of a subjective test to determine the parties' intent regarding compensation; and (3) estimation of the cost to Ledcor of complying with Husky's increased welding specifications. Husky appealed on the grounds that the trial Court: (1) incorrectly determined the costs resulting from the delay caused by the faulty welds; (2) did not award damages in relation to the ultrasonic testing of

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[8] *Ibid.* at para. 42.

the welds; and (3) overestimated the cost to Ledcor of complying with Husky's increased welding specifications.

3. DECISION

The Court of Appeal found that Ledcor was not liable for the damages arising from the delay caused by the faulty welds and that Husky was entitled to the costs of ultrasonic testing, but dismissed the other grounds for appeal and cross-appeal.

a. Ledcor's Appeal

The first ground of Ledcor's appeal was that the trial Court incorrectly awarded damages to Husky for costs arising from the delay caused by the faulty welds. The Court of Appeal agreed that these damages should not have been awarded by the trial Court because that Court had determined that there was no completion deadline. With the completion deadline gone, the Court of Appeal found there was no obligation on Ledcor to get the welds right the first time, or within a specified period of time; Ledcor merely had the obligation to correct the faulty welds. The Court noted that it was the acknowledged expectation of the parties that 5 to 10 percent of the welds would be defective. The amendments to the contract meant, in the Court's view, that Husky had simply said to Ledcor, "Help us build a pipeline. We will pay you for work done. Work as long as you think that you are able."[9] Accordingly, and contrary to the trial Court's finding, Ledcor was not liable to Husky for: equipment costs for working in break-up, premium costs for clean-up, or consequential costs for late completion.

The Court of Appeal found however that Husky's costs arising from the inspection of Ledcor's deficient welds was not a consequential cost of late completion (despite the trial Court's characterization) and accordingly, Ledcor remained accountable to Husky for those costs.

With respect to Ledcor's second ground of appeal, the Court of Appeal found that the trial Court had in fact used an objective test and did not err in determining the parties' intent with respect to compensation. With respect to Ledcor's third ground of appeal (and Husky's third ground of cross-appeal) the Court of Appeal characterized the trial Court's assessment of the cost to Ledcor of complying with Husky's increased welding specifications as a determination of fact, and found that the evidence did not suggest that the trial Court's determination was a palpable and overriding error (the threshold for review of errors of fact). Accordingly, there were no grounds to appeal that determination.

b. Husky's Cross-Appeal

Husky's first ground for appeal was dismissed. The Court of Appeal found that Ledcor was not liable for damages related to delay and accordingly, the assessment of delay costs was unnecessary.

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9 *Ibid.* at para. 43.

The Court of Appeal however did find that the trial Court's determination of fact that ultrasonic testing had not been done (and the trial Court's consequent failure to make Ledcor liable to Husky for those costs) was a palpable and overriding error since "[t]he evidence was clear that all of the repairs done to welds that Ledcor welded automatically were tested using radiography *and* by using a manual ultrasonic testing device."[10] Accordingly, the Court of Appeal found that Husky had grounds for appeal on this point and was entitled to damages for the ultrasonic test costs.

4. COMMENTARY

As a result of the Court of Appeal's decision, Ledcor was able to recover close to CDN$1.3 million more than it had been awarded at trial.

The Court of Appeal's comment that as a result of the amendments "the parties were left with a contract without a set cost, an expected date of completion, or even a requirement that the contractor complete the project,"[11] coupled with its further comment that "[w]hile it is somewhat troubling that the trial judge found the parties did not have a meeting of the minds about the exact meaning of cost-plus, or how such an arrangement would affect the issue of meeting welding specifications, neither party argued that there was no meeting of the minds and, therefore, no agreement"[12] raises the following question: What would the result have been had the parties argued that no agreement was reached?

B. *ANADARKO CANADA CORP. V. CANADIAN NATURAL RESOURCES LTD.*[13]

1. BACKGROUND

For decades it has been common to include in petroleum and natural gas purchase and sale agreements a clause whereby the purchaser indemnifies the vendor for all environmental liability associated with the assets whether the liability arose before or after the sale. This case demonstrates that such indemnities may not be interpreted as broadly as vendors may have anticipated.

2. FACTS

Anadarko Canada Corp.'s (Anadarko) predecessor obtained a crown mineral lease and a freehold surface lease, and in 1952 constructed an oil battery on the leased lands. The battery was abandoned in 1963, Anadarko reclaimed the battery, and in 1968 received a Reclamation Certificate. The surface lease was surrendered in 1968, but the crown mineral lease continued to be in force. In 1995, Anadarko sold the crown mineral lease to Canadian Natural Resources Ltd. (CNRL) pursuant to the terms of a purchase and sale agreement (the Sale Agreement). However, in 1998 Anadarko received a notice from Alberta Environmental Protection indicating the former battery site showed evidence of salt water and hydrocarbon

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[10] *Ibid.* at para. 31 [emphasis in original].
[11] *Ibid.* at para. 43.
[12] *Ibid.* at para. 51 [references omitted].
[13] 2006 ABQB 590 [*Anadarko*].

contamination, and demanding that Anadarko, as licence holder for the battery, undertake further remediation of the site. Anadarko started remediating the battery site, but also commenced an action claiming indemnification by CNRL for the costs of the additional remediation pursuant to the terms of the Sale Agreement.

3. DECISION

Anadarko's action was dismissed.

The Court, citing *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*,[14] indicated that the Sale Agreement should be interpreted using its plain meaning derived from reading the Sale Agreement as a whole and that the Sale Agreement should not necessarily be interpreted based on the intent of the parties at the time they signed the document.

The Sale Agreement contained: (1) a general indemnity relating to matters which occurred or accrued after the effective date; (2) an abandonment and reclamation clause making the purchaser responsible for abandonment and reclamation obligations related to the Assets (as defined in the Sale Agreement), and pursuant to which the purchaser indemnified the vendor in relation to the performance or non-performance of those abandonment and reclamation obligations; and (3) an environmental matters clause pursuant to which the purchaser indemnified the vendor for "any matter or thing arising out of, resulting from, attributable to or connected with any environmental damage or contamination or other environmental problems pertaining to the Assets or to any well located on the Lands, or any of them, whether occurring or accruing before, on or after the Effective Date."[15] The Sale Agreement indicated that the parties had taken into account the purchaser's responsibility for the future abandonment, reclamation, and environmental responsibilities associated with the Assets in determining the purchase price of CDN$71,151,000.

Anadarko alleged that pursuant to the Sale Agreement, CNRL had indemnified Anadarko for the additional remediation costs under all three indemnities because the indemnities related to matters and obligations pertaining to the Assets and the abandoned battery was either an Asset or pertained to an Asset.

In contrast, CNRL argued that the three indemnities did not apply. In CNRL's view, the general indemnity did not apply because the salt water and hydrocarbon contamination occurred prior to the effective date, and the second and third indemnities did not apply because the abandoned battery was not an Asset purchased by CNRL. In support of this argument, CNRL suggested that if the parties had intended to include abandoned batteries, they would have included a description of the abandoned batteries in the Sale Agreement in the same way that they had listed the abandoned wells for which CNRL did assume liability.

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[14] *Ibid.* at para. 16, citing *Canada Deposit Insurance Corp. v. Canadian Commercial Bank* (1991), 113 A.R. 371 at 421-22, aff'd [1992] 2 S.C.R. 3.

[15] *Anadarko*, *ibid.* at para. 9.

The Court found that the abandoned batteries did not fit within any one of the three categories comprising the Assets (namely Petroleum and Natural Gas Rights, Tangibles, or Miscellaneous Interests) as defined in the Sale Agreement.

The Court did not explicitly state its reason for concluding that the abandoned batteries did not fit within the definition of Petroleum and Natural Gas Rights, but the Court appears to have accepted CNRL's position that "the Petroleum and Natural Gas Rights contemplated by the agreements … are the *operational* rights to explore for, drill for, take, use or market oil, natural gas and related hydrocarbons or to share in the production thereof."[16]

Although the definition of Tangibles included oil batteries, the Court interpreted the definition as applying to existing batteries only. The Court appears to have been particularly influenced by the fact that an abandoned well and an abandoned pipeline still exist (and are therefore tangible) while an abandoned battery no longer exists.

The definition of Miscellaneous Interests in the Sale Agreement specifically included surface rights and Anadarko argued that the abandoned battery should be considered a surface right. The Court did not accept this argument indicating that it "fail[ed] to see how this [could] be the case when it [was] no longer there,"[17] and again stressed the view that the Asset definition and its component categories had an operational purpose (except where specifically mentioned as in the case of abandoned wells). A battery which was not there could not be used operationally, and hence was not an asset. The Court also indicated that the definition of Miscellaneous Interests clearly included licences and accepted CNRL's submission that Anadarko's failure to transfer the licence relating to the abandoned battery was evidence that the abandoned battery was not a Miscellaneous Interest and was never intended to be transferred to CNRL.

With respect to Anadarko's argument that the abandoned battery pertained to the Assets, the Court, after reviewing the case law cited by CNRL and Anadarko, found that: (1) the first indemnity only applied to matters that occurred or accrued after the effective date, and the salt water and hydrocarbon contamination had occurred before the effective date set out in the Sale Agreement; and (2) the abandonment and reclamation indemnity and the environmental indemnity (the second and third indemnities) did not apply to the abandoned battery even though those indemnities applied to liabilities "pertaining to the Assets."[18] The Court emphasized that the Asset definitions were to be interpreted as operational assets, and "pertaining to" should therefore be interpreted as pertaining to operational assets. The abandoned battery was not an operational asset; therefore, the second and third indemnities did not apply.

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16 *Ibid.* at para. 32 [emphasis added].

17 *Ibid.* at para. 36.

18 *Ibid.* at paras. 37-40.

4. COMMENTARY

This is not a case where an asset of low value was sold with a debilitating abandonment liability. The CDN$71million sale price dwarfs the roughly CDN$3.5 million abandonment liability.

For vendors who do not want to retain reclamation obligations related to old facilities, the solution is fairly straightforward — we can expect to see lists of abandoned facilities on future Sale Agreements. With the purchaser having operations in the area, and presumably more easily able to do the remediation, there are grounds to consider the purchaser the logical holder of such remediation responsibilities.

The narrow interpretation given to the term "pertaining to" by the Alberta Court of Queen's Bench in this case is interesting in light of the broad interpretation given to the term "related to" by the British Columbia Supreme Court in *Minera Aquiline Argentina SA v. IMA Exploration Inc.*[19]

Will this decision lead to higher demands on the orphan facility fund when past vendors who do not have corporate successors have entered into similar agreements, but are no longer around to conduct the remediation?

C. *MUNTEAN V. ADVANTAGE OIL & GAS LTD.*[20]

1. BACKGROUND

Prior to drilling a well, a well site and an access road must be constructed. This requires a surface lease from the owner of the surface rights. Where an existing road can be used to gain access to the well site, a road use agreement is often negotiated instead of leasing additional land to construct an access road. This case pertains to implied terms in a road use agreement.

2. FACTS

Larry Muntean gave Advantage Oil & Gas Ltd. (Advantage) permission to survey lands he owned for a proposed well site and access road. After surveying had been completed, a landman acting for Advantage commenced negotiations with Muntean for a lease of the well site and access road, and was then told the access road Advantage wanted to use was a private road on his land. As a result, instead of negotiating a surface lease covering both the well site and access road, the landman proposed entering into a surface lease for the well site and a road use agreement which together would provide the same total consideration as the surface lease initially proposed for the well site and access road. Muntean executed both agreements, but Advantage retained the consideration (CDN$6,800 for the Surface Lease Agreement and $6,350 for the Road Use Agreement) pending commencement of construction of the lease. The Surface Lease Agreement clearly indicated that: (1) the lease consideration

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19 2006 BCSC 1102, [2007] 1 W.W.R. 43 at para. 76 [*Minera*].

20 2006 ABPC 318 [*Muntean*].

was not payable until the lessee entered upon the lands for other than survey purposes; and (2) if the leased lands were not accessed (other than for survey purposes) within a year of the date of the lease, that the lease would terminate and Advantage would only be required to pay Muntean $1,500. The Road Use Agreement provided that "[t]he road may be used by Advantage, its servants, agents, contractors, or invitees for any transportation purposes including drilling rig movements and servicing the captioned well,"[21] but did not specifically set out when consideration was to be paid. Muntean did not demand payment at the time he executed the agreements.

Due to poor results of neighbouring wells, Advantage decided not to proceed with the well on Muntean's lands. Advantage indicated to Muntean that they would not be drilling a well on his lands and sent him a cheque for the $1,500 provided for in the Surface Lease Agreement. Muntean cashed the cheque and demanded payment of the full consideration stipulated in the Road Use Agreement, alleging that Advantage had used the road one to three times after the surveying was complete. Advantage argued that there was an implied term in the road use agreement that no consideration was payable until well site construction commenced.

3. DECISION

The Court was not convinced that the access road was used by the defendants in any manner contemplated by the parties in the Road Use Agreement, and found that there "was no well site preparation or construction commenced by the defendant on the plaintiff's land following the date of the Agreement."[22] The Court also noted: (1) the evidence of the landman acting as agent for Advantage "that it is standard oilfield practice that the landowner is paid at the time of construction being the commencement of the preparation of the well site for the purpose of drilling a well,"[23] and (2) that Muntean had not requested payment at the time the road use agreement was executed. Citing *Catre Industries Ltd. v. Alberta*[24] as precedent, the Court found an implied term in the Road Use Agreement that "no consideration would be paid to the plaintiff pursuant to the *Road Use Agreement* unless and until a well site was constructed on the plaintiff's land"[25] on the basis that it was either (a) a term which the parties had in mind but did not express, or (b) a term which the parties would likely have added if the issue had been brought to their attention.

4. COMMENTARY

This is a useful reminder of the importance of clearly indicating when consideration is to be paid.

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21 *Ibid.* at para. 10.
22 *Ibid.* at para. 26.
23 *Ibid.* at para. 24.
24 *Ibid.* at 21, citing *Catre Industries Ltd. v. Alberta* (1989), 99 A.R. 321 (C.A.) at paras. 52-55.
25 *Muntean*, *ibid.* at para. 27 [emphasis in original].

D. *ANTORISA INVESTMENTS LTD. V. 172965 CANADA LTD.*[26]

1. BACKGROUND

The issue of vendor and purchaser liability for environmental conditions present prior to the sale is highly contested in the oil and gas industry. Typically, the majority of sale agreements hold the purchaser liable for environmental conditions whether they occurred on, before, or after the closing date of the transaction. The vendor only retains liability for contractual matters that accrued prior to the transfer of ownership.

2. FACTS

In 1989, Imperial Oil Limited (Imperial) acquired the shares of Texaco Canada Inc. (Texaco). The acquisition was subject to approval by the federal Competition Bureau (Bureau). The Bureau ordered Imperial to divest itself of several hundred service stations across Canada, in a relatively short time frame. Imperial adopted a process to determine which of the properties posed a high risk of contamination, and slated the high risk properties for remediation prior to divestment. In addition, Imperial adopted detailed provisions into the sale agreements in order to transfer liability for environmental matters to the new owner. Antorisa Investments Ltd. (Antorisa) purchased one of the properties that was not deemed to be in the high risk category, but ultimately required remediation. The property in question had been the site of a gas station for many years; Texaco acquired it and constructed a service station and gas bar on the property. In 1981, Texaco demolished the existing station and replaced it with a two-bay self service facility, which it held until the acquisition by Imperial. Antorisa had received advice from its counsel that indicated the environmental provisions in the Imperial sale agreement were too onerous on purchasers. However, in order to avoid making its bid less attractive, Antorisa did not make any amendments to the sale agreement. In addition, the purchaser had been friends with two Imperial representatives, and claimed that they had made assurances that the property was clean.

3. DECISION

The Court held that it was clear from the terms of the contract that the parties intended that Imperial would have no liability for the environmental condition of the property or for any representations made, whether or not they induced the contract. In addition, prior to closing, Antorisa's due diligence indicated that the property had some degree of contamination and Antorisa proceeded with the transaction notwithstanding. As such, it was not reasonable for the purchaser to rely on the assurances of the Imperial representatives that the property was clean. Imperial had no knowledge that the property was contaminated at the time of sale and the purchaser was not an unsophisticated party. In the result, the case was dismissed.

4. COMMENTARY

This case demonstrates that it is possible to transfer environmental risks to a buyer through contract. However, it is important to bear in mind that the terms of the contract must be clear

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[26] (2006), 82 O.R. (3d) 437.

and straightforward, that the land is being sold "as is," and that the buyer is accepting all environmental risks. In addition, the buyer should be sophisticated enough to undertake the risk it is accepting. In this case, it is also relevant to note that the cost award amounted to only 60 percent of the actual fees billed to Imperial.[27] This was the case notwithstanding that there was an agreement between the plaintiff and Imperial which gave Imperial a contractual right to be fully indemnified for legal fees if such fees are reasonable. In this regard, the Court relied on the "reasonable expectations" principle,[28] in finding that there needed to be objective limits placed on the costs burden.

E. *KLEMKE MINING CORP. V. SHELL CANADA LTD.*[29]

1. BACKGROUND

Prior to the trial, a series of applications were made to the Court of Queen's Bench. The Court ruled on the degree to which: (1) individuals were to be available for examination; and (2) documents were producible. The applications are reviewed in the "Confidentiality" segments of this article, found in Part III, below. The trial decision reviewed in this segment concerns the main dispute: whether or not a contract for certain mining and consulting work at the Albian oil sands mine had been granted to Klemke Mining Corp. (Klemke).

2. FACTS

Klemke commenced an action against Shell Canada Limited (Shell), Chevron Canada Resources Limited (Chevron), Western Oil Sands Inc. (Western), and Albian Sands Energy Inc. (ASEI) alleging that they had agreed to give Klemke work at what became the Albian oil sands mine.

Klemke first approached Shell about the development of Shell's Bituminous Sands Lease 13 around 1994 and participated in two subsequent feasibility studies. Shell wanted joint venture participants in the project and was interested in Klemke's oil sands expertise, so Shell suggested Klemke join with two other companies to purchase a 25 percent interest in the project. At a meeting on 25 June 1999, Neil Camarta, then Vice President of Oil Sands for Shell, offered Klemke mining work on the conditions that (1) the project went ahead, and (2) Klemke "put skin in the game."[30] Klemke accepted these two conditions. On 29 June 1999, Klemke sent an agenda to Camarta that outlined Klemke's intent to "put skin in the game," and set out a scope of work and a mechanism for determining price. In a telephone conversation on 30 June 1999, Camarta acknowledged that the agenda "hits nail on head at first read."[31]

Klemke offered to invest in Western (one of the proposed Albian joint venture participants) to meet Shell's "skin in the game" requirement. Western indicated they were satisfied with the terms pursuant to which Klemke proposed to invest in Western, except for

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[27] See *Antorisa Investments Ltd. v. 172965 Canada Ltd.* (2007), 27 B.L.R. (4th) 77.
[28] *Ibid.* at paras. 31-32.
[29] 2007 ABQB 176 [*Klemke*].
[30] *Ibid.* at para. 36.
[31] *Ibid.* at para. 63.

a link between the investment and Klemke being provided with contract mining work. On 13 October 1999, Camarta told Klemke that a Mr. Barber would be responsible for "papering" the 29 June 1999 letter.[32] At a 30 November 1999 meeting, Klemke agreed to remove the term linking the award of the mining work to Klemke with Klemke's investment in Western, and Camarta "told his management team to do what was necessary to implement the deal."[33] In Klemke's view the deal included: labour at cost, equipment benchmarked, and a term of three to five years. The Court rejected evidence from several of the defendants that Camarta indicated at this meeting that there was no contract with Klemke to do the mining work.

On 6 December 1999, the Albian joint venture project officially came into being, and on 10 December 1999, Western sent an unsigned Term Sheet to Klemke setting out the type of work and the pricing for the work to be provided by Klemke (the Memorialization). Klemke signed the document on 14 December 1999 and returned it to Western. The document was given to Camarta to sign. On 17 December 1999, Klemke met with ASEI (the entity that operated the mine on behalf of the joint venture participants) to discuss the benchmarking mechanism. Further discussions about the work to be conducted by Klemke took place in December 1999 and January 2000. Camarta did not sign the 10 December 1999 document, indicating he did not agree to an arbitration clause inserted in the agreement and that the agreement should have been sent out by ASEI not Western. Klemke was informed of Camarta's concerns and replied that he had never requested the arbitration clause, that the arbitration clause had been inserted by Western, and that he was fine with the arbitration clause being removed. Klemke was then told that Camarta would be taking the agreement to the Executive Committee for approval on 24 January 2000. On 22 January 2000, Klemke followed up with Camarta to confirm the agreement would be brought before the Executive Committee on 24 January 2000. Camarta indicated that due to a heavy agenda, the item had been deferred to the Executive Committee meeting at the end of February 2000. On 28 January 2000, Klemke and several other companies were sent an Invitation to Express Interest in the Albian mining work. Klemke expressed concern about this, indicating his belief that they had already been given the work, but was told it was just a formality. Klemke submitted an expression of interest. On 24 March 2000, Klemke was informed that the mining work had been awarded to a competitor.

3. DECISION

Having reviewed the case law relating to credibility and having made an assessment of the credibility of the various witnesses, the Court held that an oral agreement had been reached which was subsequently memorialized in writing and awarded Klemke CDN$21,805,122 for loss of the mining work and a further $200,000 for the consulting work.

Using the criteria set out *Ron Ghitter Property Consultants Ltd. v. Beaver Lumber Co.*,[34] the Court found that the parties had come to a meeting of the minds (*consensus ad idem*)

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[32] *Ibid.* at para. 86.

[33] *Ibid.* at para. 96.

[34] *Ibid.* at para. 159, citing *Ron Ghitter Property Consultants Ltd. v. Beaver Lumber Co.*, 2003 ABCA 221, 330 A.R. 353 at paras. 8-9.

because: (1) on an objective basis the parties intended to contract, and (2) the terms of the agreement were sufficiently clear. The Court found that both parties wanted a contract: Camarta wanted Klemke's oil sands expertise; and Klemke wanted the contract mining work. The meetings and documentation circulated between the parties reflected an agreement rather than ongoing negotiations or agreements to agree. The Court found that a meeting of minds occurred at the 25 June 1999 meeting:

> [T]he oral meeting of the minds on June 25 as evidenced by the June 29 documents and June 30 phone call and December 10 Memorialization amount to a binding contract notwithstanding the absence of a formal agreement.
>
> The events on both dates captured the essential terms agreed to, although I concede the Memorialization provides stronger evidence for this finding. This is in part because the parties were as at December 10 on firmer footing, having satisfied the two conditions precedent of skin in the game and the existence of a project.[35]

The Court considered and rejected several of the defendants' arguments that no contract had been formed including: (1) the parties never reached anything beyond an agreement to agree; (2) Camarta never signed the Memorialization; (3) no final price was ever agreed to; (4) conditions precedent had not been met; (5) the memorialization was sent out without authorization; and (6) the requirements of the *Statute of Frauds*[36] had not been met.

In answer to the defendants' argument that the discussions and documents were an agreement to agree the Court stated:

> An agreement is not incomplete simply because it calls for some further agreement between the parties or provides for the execution of a further formal document. The question is whether the further agreement or documentation is a condition of the bargain or whether it is simply an indication or expression of desire as to the manner in which the contract already made will be implemented.[37]

The Court went on to find that both parties had acted as if a deal had been made and the essential terms of the deal were not changed over a period of months. As the essential terms had been agreed upon, it did not matter that details continued to be negotiated.

Even though Western's letter was never signed by Camarta, the Court found that the "signature on the cover letter to the Memorialization was sufficient to show the defendants' endorsement of and agreement with the package."[38] It was not necessary that Camarta sign the Memorialization as well given that "the signature and representations on the cover sheet and the words and conduct of Mr. Camarta … manifest an intent to be legally bound."[39]

The defendants argued that the terms of the contract were not sufficiently clear to evidence a meeting of the minds, stressing in particular that the final price had not been determined.

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35 *Ibid.* at paras. 176-77.
36 1677 (29 Cha. 2), c. 3.
37 *Supra* note 29 at para. 183.
38 *Ibid.* at para. 198.
39 *Ibid.* at para. 202.

The Court found that the nature of the work to be performed did not permit a final price to be determined, and the best that could be achieved was to agree on a method of determining the ultimate price (the benchmarking mechanism). Although some changes were made to the benchmarking mechanism during the course of negotiations, those changes were refinements of, and not changes to, the essential terms of the agreement. The Court applied the same reasoning to the scope of work — it had not been determined, but the mechanism for determining it had been put in place.

The Court rejected the defendants' arguments that executive approval of the agreement was necessary, as this condition was not raised with Klemke until the Memorialization had been signed by Klemke and returned to Camarta. The Court also rejected the argument that the agreement was conditional on Klemke's satisfactory performance of a separate contract.

In response to the defendants' argument that the individual who sent out the Memorialization did not have the authority to do so, the Court indicated:

> Mr. Barber was the individual who signed the cover letter to the December 10 Memorialization. At the time he was an employee of Western with a contract of employment to Shell. Mr. Klemke, along with several of the defendants' employees, thought that Mr. Barber was an employee of Albian with authority to manage and enter into contracts. There is no issue about the authority of Western to bind the other joint venture participants. Western, as a joint venturer with Shell and Chevron, shared a community of interest in which each was both principal and agent of the others. Albian is their shared operating entity over which the agency right extends. Therefore, Western had the right and authority to bind the others to the Agreement as it was Memorialized. The question is whether Mr. Barber had the authority delegated to him to enter into contracts on behalf of Western or any other joint venture participants, or, if he did not, then if KMC was entitled to presume he did.[40]

With respect to the authority to bind, the Court went on to find that Barber had the ostensible authority to bind Western and the other joint venture participants because: (1) Camarta had the actual authority to do so; (2) Camarta had represented on several occasions that Barber had such authority to do so; and (3) Klemke relied on those representations.

The Court found that the Memorialization was sufficient to meet the requirements of s. 4 of the *Statute of Frauds*,[41] which requires that all agreements not performed within the space of a year be in writing and signed by the party who has the obligation to perform the contract.

4. COMMENTARY

If an agreement is intended to be non-binding or conditional, then this case illustrates the necessity of clearly documenting and communicating that intent. In the absence of such documentation and communication, a contract may be found to exist even though a price has not been agreed to and the scope of the work has not been finalized.

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40 *Ibid.* at para. 250.

41 *Supra* note 36.

III. CONFIDENTIALITY

A. *MINERA AQUILINE ARGENTINA SA v. IMA EXPLORATION INC.*[42]

1. BACKGROUND

Vendors of resource properties typically require potential purchasers to enter into confidentiality agreements prior to granting access to confidential information. This case highlights the importance of understanding the scope of a confidentiality agreement and the severe consequences which can flow from using confidential data in contravention of a confidentiality agreement.

2. FACTS

Newmont Mining Corporation (Newmont) and several other mining companies owned a mining property called Calcatreu. Calcatreu was found to be an uneconomic gold mine, but the owners continued to explore for other economic mining sites in the area both inside and outside of the boundaries of the Calcatreu property. Some of the data from these activities (the A Data) pertained to approximately one thousand samples and was primarily generated outside the Calcatreu area. It cost several hundred thousand dollars to obtain and none of it was in the public domain.

In 2002, the Calcatreu owners decided to sell and they prepared a bid package which did not contain any raw technical data. All prospective purchasers were required to sign a confidentiality agreement (CA).

IMA Exploration Inc. (IMA) had a pre-existing interest in the general region of Calcatreu and in part of the area covered by some of the A Data, but did not have an active sampling program nor any claims in the vicinity. IMA executed the CA, received the bid package, and sent representatives to conduct due diligence. These representatives visited the project office data room and toured the Calcatreu property. During the first visit to the field office, IMA's representative observed a satellite map showing the early progress of A Data generation and IMA, alone among the potential purchasers, requested copies of the A Data. At the time that the A Data was given to IMA's representative, there was no discussion of confidentiality by either party. In addition, the CA did not expressly mention the A Data.

After declining to bid on Calcatreu, IMA reviewed the A Data, discovered promising signs of silver-lead deposits, and staked claims on lands outside of Calcatreu but in the general area (the Navidad Claims).

Minera Aquiline Argentina S.A (Minera), a prior part owner, was the successful purchaser of the Calcatreu property and brought an action against IMA and its subsidiary[43] alleging that IMA had misused information obtained in IMA's due diligence process to the detriment of Minera and contrary to the provisions of the CA.

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[42] *Supra* note 19.

[43] This summary, in the interest of brevity, treats references to IMA's subsidiary as references to IMA.

3. DECISION

The Court declared that IMA held the Navidad Claims pursuant to a constructive trust in favour of Minera and granted a mandatory injunction requiring IMA to transfer the Navidad Claims and any assets related thereto to Minera, subject to payment to IMA of all reasonable amounts expended by IMA for the acquisition and development of the Navidad Claims.

The Court focused on two main issues: (1) the scope of information covered by the CA, and (2) the appropriate remedy for the breach of the CA.

a. Scope of the CA

IMA argued that the A Data was not covered by the CA because the A Data was not specifically listed in the CA, nor did it relate to the Calcatreu property which was for sale. Minera countered that the A Data was implicitly covered by the CA because it was made available during the site visit and because it related to the evaluation of a possible Calcatreu transaction.

The Court viewed the CA through a business purpose lens:

> It is important to bear in mind that the purpose of the [CA] is to protect proprietary information and to maintain its confidentiality in respect of all bidders who may be interested in considering the evaluation of Calcatreu, whether or not they ever make a bid or are successful in acquiring it. This is not a Purchase Agreement that will define the assets to be sold and the terms and conditions of such sale.[44]

The Court found that the CA's definition of confidential information should be interpreted broadly as it included information "in respect of" the project and the Supreme Court of Canada had determined that the term "in respect of" should be interpreted broadly.[45] As well, the Court indicated that: (1) several experts stated that data like the A Data could be relevant or desirable when evaluating a resource such as Calcatreu; (2) the Calcatreu owners created the A Data for the express purpose of potentially adding to the Calcatreu gold property; and (3) the Calcatreu owners who provided the data believed that it was requested as part of IMA's evaluation of Calcatreu.

Accordingly, the Court ruled that A Data was covered by the CA.

Despite the claims of IMA's senior management to the contrary, the Court also found that IMA used the data to stake the Navidad Claims. This finding was based in large part on IMA's lack of activity in the Navidad area prior to reviewing the A Data, and the Court's conclusion that if IMA had plans for the Navidad area prior to reviewing the A Data, then IMA would have been too concerned with being precluded by the terms of the CA from further exploration to request data that did not relate to Calcatreu.

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[44] *Minera*, *supra* note 19 at para. 98.

[45] *Ibid.* at para. 75, citing *R. v. Nowegijick*, [1983] 1 S.C.R. 29 at 39.

b. Remedies for Breach of the CA

In determining which remedy to apply to the contractual breach, the Court considered constructive trusts, damages, and mandatory injunctions.

(i) Constructive Trusts

The CA specifically contemplated Minera's right to equitable remedies and Minera requested the imposition of a constructive trust.

IMA argued that a constructive trust was inappropriate because constructive trusts were: (1) not recognized in Argentina; (2) reserved for "vicious and deliberate" conduct;[46] (3) only available where there was a link between the wrong, the information, and the acquisition of the property; and (4) only awarded when damages would be inadequate. The Court found that: (1) it did not matter that the constructive trusts were not recognized in Argentina because they were enforceable in British Columbia; (2) IMA did not supply case law supporting their position that constructive trusts were reserved for "vicious and deliberate" conduct; (3) "the use of the BLEG A data led directly to the 'discovery' of Navidad and that without its use, it is very unlikely in the circumstances that IMA would have found and staked Navidad"[47] and that was a sufficient link; and (4) damages were not an adequate remedy.

The Court indicated that the purpose of compensatory damages, whether assessed in equity or at common law, was to put the plaintiff in the position it would have been in "but for" the defendants' breach and that this required the Court to consider, on the balance of probabilities, what would have happened had the defendant lived up to its legal obligations.[48] After reviewing the steps taken by IMA in staking Navidad, and Minera's actions in connection with data similar to the A Data, the Court concluded that Minera would have taken the same steps as IMA, and thus, but for IMA's actions, Minera would be owner of the Navidad Claims. In the absence of any evidence from IMA's witnesses to the contrary, the Court also found that the confidential data was used not only to stake the areas covered by the A Data, but also to stake other properties which "had similar characteristics to the Navidad Project and IMA hoped to find a similar style of Navidad mineralization on those properties."[49] The Court found that these "similar characteristic" properties were also subject to the constructive trust.

(ii) Damages

The Court found that damages would be an inadequate remedy because "[a]ny amount of damages that this court might award would amount to speculation as to the value of the claims and would quite conceivably cause an injustice to one of the parties through over- or under-compensation."[50] The Court cited *Lac Minerals Ltd. v. International Corona*

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[46] *Minera*, *supra* note 19 at para. 280.
[47] *Ibid.* at para. 282.
[48] *Ibid.* at para. 285.
[49] *Ibid.* at para. 296.
[50] *Ibid.* at para. 301.

Resources Ltd. in support, because in that case the Supreme Court of Canada held that a constructive trust remedy should be granted based on the difficulties of valuing (with any degree of certainty) mine reserves, mineral prices, exchange rates, and inflation rates.[51]

(iii) Mandatory Injunctions

Moreover, the Court indicated that: "Even if I were not satisfied that a constructive trust was the appropriate remedy in this case, I would find that a mandatory injunction requiring the defendants to transfer the Navidad Area Claims to the plaintiff would, standing alone, be appropriate as a remedy for the defendant's breach of confidence and breach of contract."[52]

The Court further indicated that IMA's total forfeiture of its interest did not unjustly compensate Minera because if IMA had wanted a shared interest in the A Data, "IMA could have negotiated with the plaintiff (or its predecessor) to buy the BLEG A data outright or come to some other arrangement to enable it to use the data for its own purposes. Alternatively, IMA could have pursued property in the area covered by the data through publicly available information."[53]

The Court did find, however, that Minera "would be unjustly overcompensated if it was not required to reimburse the defendants for the development that they have funded on the site since the claims were staked,"[54] and therefore the Court ordered an accounting for the development expenses.

4. COMMENTARY

Although this case relates to mining claims, it has obvious analogies to the petroleum industry where data rooms, confidentiality agreements, and development of prospects with similar characteristics are also commonplace.

The ease with which the Court found that IMA had used the confidential information to stake its Navidad Claims and that Minera would, on the balance of probabilities, have successfully staked the Navidad Claims in the absence of IMA's behaviour, highlight that the plaintiff's burden of proof regarding damages is not insurmountable. In addition, the Court's imposition of a constructive trust on all "similar characteristics" properties which IMA staked highlight that the misuse of confidential data can have far-reaching consequences.

The Court's decision was subsequently affirmed by the British Columbia Court of Appeal and leave to appeal dismissed with costs by the Supreme Court of Canada on 20 December 2007.[55]

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51 *Ibid.* at para. 299, citing *Lac Minerals Ltd. v. International Corona Resources Ltd.*, [1989] 2 S.C.R. 574 at 674 [*Lac Minerals Ltd.*].

52 *Minera*, *ibid.* at para. 308.

53 *Ibid.* at para. 315.

54 *Ibid.* at para. 318.

55 2007 BCCA 319, [2007] 10 W.W.R. 648, leave to appeal to S.C.C. refused, 32211 (20 December 2007).

B. *MURPHY OIL CO. V. PREDATOR CORP.*[56]

1. BACKGROUND

In the petroleum and natural gas industry, drilling deep exploratory wells is an expensive and risky proposition. There is a low success rate for exploratory wells. The first company in an area to drill a successful exploratory well obtains a competitive advantage because it has established the presence of petroleum and natural gas in paying quantities. Based on this and the information it has obtained from drilling the well (cores, logs, etc.), it is better able to determine the value of un-leased mineral rights in an area. The information relating to an exploratory well is not required to be publicly released for some time after drilling, and the company which generated it will usually attempt to keep it confidential. Accordingly, it is common practice in the industry to hire individuals (scouts) who attempt to determine how successful an exploratory well is by various means, including observing drilling rigs from a distance.

Because the common law imposes penalties on the improper use or disclosure of confidential information where there has been a breach of a fiduciary duty or a breach of a general duty of confidence, the methods used to obtain confidential well information can have serious consequences even in the absence of express or implied contractual protection for that confidential information, as this case demonstrates.

2. FACTS

The plaintiffs Murphy Oil Company Ltd. (Murphy), Apache Canada Ltd. (Apache), and Beau Canada Exploration Ltd. (Beau) (the Ladyfern Partners) put together an exploratory drilling program for lands in the Ladyfern area. They had plans to drill four wells including the "a-97-h"[57] well. If the wells proved successful, the Ladyfern Partners intended to bid on adjacent un-leased lands.

Initial gas flow rates for the a-97-h well suggested it might be a highly productive well and the Ladyfern Partners hired Bonnett Wireline Services Limited (Bonnett) to conduct downhole pressure testing in February 2000. Downhole pressure is the pressure at which gas enters the wellbore from the reservoir. Downhole pressure data in conjunction with flow rates will give an idea of the size of a reservoir; if the size of the reservoir exceeds the spacing unit of the well, the reservoir likely extends to neighbouring lands.

Various public announcements were made by Apache and Beau about the discovery at Ladyfern in February and at several times during the spring and summer of 2000, but the pressure data was not publicly released.

Predator Corporation Ltd. (Predator) became interested in the Ladyfern area as a result of the announcements by Apache. Mr. O'Reilly, a geologist with Predator, realized after checking the location of the a-97-h well, that there was un-leased Crown land adjoining the

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[56] 2006 ABQB 680, 408 A.R. 98 [*Predator*].

[57] *Ibid.* at para. 5.

well. He suspected that if the land was bid for and won in a land sale, it would allow the successful party to drill into the same pool. As a result, Predator took a number of steps to obtain information about the Ladyfern area. In addition to hiring a scouting company to collect data about the drilling of the four wells, Mr. Longdo, Predator's engineer, contacted his friend Mr. Toews, a part owner and general manager of Bonnett, and requested the a-97-h well pressure data. Toews gave this information to Longdo.

Predator had an agreement with Ricks Nova Scotia Co. (Ricks), to show prospects to Ricks, which then decided which prospects would be funded by the Predator Partnership (between Predator and Ricks). Ownership of the funded prospects would be split with Predator retaining a 25 percent interest and Ricks obtaining the remaining 75 percent. After presentations which included the pressure data, the Predator Partnership agreed to fund bidding for prospects in the Ladyfern area. During 2000, the Predator Partnership competed many times, with mixed success, against Murphy and its partners at Crown sales in the Ladyfern area. The Predator Partnership beat the Ladyfern Partners in a 29 March 2000 bid for lands in the area and were also partially successful in their bids for area lands at a later land sale on 19 July 2000 (the Disputed Lands).

After the Ladyfern Partners became aware that Bonnett's had given the pressure data to Predator, they commenced legal proceedings alleging that Predator obtained the plaintiffs' confidential information (pressure data) in circumstances that Predator knew constituted a breach of confidence by one of the plaintiffs' contractors, and that Predator wrongfully used that information to evaluate the play and to bid on adjacent un-leased lands.

In response to the litigation, Ricks dissolved the Predator Partnership and entered into an agreement whereby it transferred its 75 percent interest in the Disputed Lands to Murphy and Apache, and Murphy and Apache refunded the total cost spent by Ricks. As a result, the plaintiffs ended up with a majority interest in the Disputed Lands with Predator holding the remaining 25 percent interest. By Court order, that 25 percent interest was held by PriceWaterhouse Coopers Inc. pending the outcome of the action.

Predator counterclaimed, alleging that the Ladyfern Partners operated the joint wells in such a way to incur higher costs, lower production, and in a manner that favoured production of wells owned by the Ladyfern Partners alone.

3. DECISION

The Court held that the pressure data was confidential information that was subject to an obligation of confidence and found that Predator had misused the pressure data to the detriment of Murphy, Apache, and Beau. The Court imposed a constructive trust on Predator with respect to the Disputed Lands and related production, but did not award damages to compensate the plaintiffs for having to increase their bids at subsequent land sales. While the Court found that the defendants had trespassed on the Plaintiffs' lands (by virtue of unauthorized site visit), no damages were awarded for the trespass. The Court did not award punitive or exemplary damages and did not find the individual defendants personally liable to the plaintiffs. The defendants' counterclaim was dismissed.

4. COMMENTARY

Although the case had many interesting facts and involved one of the largest new gas discoveries in the last decade, not much legal ground was broken. The Court simply applied the breach of confidence principles set out by the Supreme Court of Canada in *Lac Minerals Ltd.*[58]

This case has however, generated interest because of the concern that it created new restrictions on scouting. Although this decision does discuss scouting, it should be noted that, as Nation J. indicates, "obtaining the complete faxed report, and the complete computer file of pressure data from a contractor of the owner of a well still designated as a tight hole, is not 'scouting.' It was a direct interaction between an engineer at Predator and the contractor."[59]

Accordingly, the portion of the judgment that analyzes what is and what is not acceptable scouting is *obiter dicta*, and one should be careful not to read too much into the Court's comments on scouting.

To the extent that the Court did comment on scouting, the comments were not a departure from, or expansion of, existing legal principles. The Court indicated that the expert opinion on industry custom regarding scouting is that "anything goes, as long as it is not illegal"[60] and noted intercepting cell phone calls and trespassing on lands leased by others are both illegal. The Court also noted that "scouts are used to observe activity from the edge of leases, and talk to people to get second hand information,"[61] but the Court neither explicitly endorsed those activities nor suggested that they are illegal, although in context it would appear that the Court regarded those activities as being, in general, acceptable forms of scouting.

C. *KLEMKE MINING CORP. V. SHELL CANADA LTD.*[62]

1. BACKGROUND

In past cases such as *Husky Oil Operations Ltd. v. Anadarko Canada Corp.*,[63] courts have shown a willingness to compel the disclosure of confidential information. The *Klemke* applications discussed below are reminders that the courts have the power to compel disclosure of documents which the receiving and disclosing party had agreed to keep confidential.

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58 *Supra* note 51.
59 *Predator*, *supra* note 56 at para 82.
60 *Ibid.* at para. 78.
61 *Ibid.* at para. 77.
62 2006 ABQB 486 [*Klemke2*]
63 2004 ABCA 154, 354 A.R. 16. For a review of the case, see Mark Houston *et al.*, "Recent Judicial Developments of Interest to Oil and Gas Lawyers" (2006) 44 Alta. L. Rev. 233 at 253.

2. FACTS

As more thoroughly indicated in the discussion of the trial decision in the *Klemke* case above,[64] Klemke Mining Corp. (Klemke) commenced an action alleging that in June 1999 a Shell Canada Ltd. (Shell) vice-president had orally promised Klemke earth moving work at Shell's prospective (at the time) Albian oil sands mine if the project went ahead. The project did go ahead, but the earth moving work was given to North America Mining Inc. (NAM), one of Klemke's competitors.

Preparation for trial resulted in a series of Queen's Bench applications requesting that the Court rule on the degree to which: (1) individuals were to be available for examination, and (2) documents were producible. In 2002, the Court had determined that Shell's in-house counsel was subject to examination to the extent that she participated in negotiations for a contract as opposed to giving legal advice.[65]

In March 2006, Klemke applied to the Court to determine whether a number of documents indicated on the Affidavit of Records but for which privilege had been claimed (including many from in-house counsel's files), were required to be produced.

In June 2006, Klemke made another application requesting the production of the Schedule A to the Mining Services Contract between Shell and NAM. This schedule A set out commercially sensitive and highly confidential information regarding NAM's prices for a wide range of services including those which Klemke alleges it had been promised.

3. DECISION

In the June application, Klemke argued that the Schedule A to the Mining Services Contract should be produced because the basis of the alleged oral agreement between Klemke and Shell was that the price for the work would be determined by benchmarking Klemke's proposed charges against Shell's alternatives. NAM, which was granted intervener status for the purpose of the application, objected to the disclosure on the basis that the information was commercially sensitive, highly confidential, and its full disclosure was not necessary given that only part of the Schedule A related to work that Klemke claimed it had been promised. The Court accepted the plaintiff's argument that proper benchmarking could only be done if the plaintiffs had access to the entire Schedule A and decided to compel disclosure of the Schedule A on the conditions that: (1) the Schedule was only to be provided to plaintiff's counsel and a benchmarking expert selected by Klemke who was not employed by or related to Klemke; (2) the contents of the schedule were not to be disclosed to anyone else; (3) the Schedule was only to be used for the purposes of the litigation; and (4) all copies were to be returned to NAM at the end of the litigation.

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[64] See Part II.E, above.

[65] *Klemke Mining Corp. v. Shell Canada Ltd.*, 2002 ABQB 1131, 332 A.R. 154.

4. COMMENTARY

While the Court's decision in the June application appears to offer scant comfort to NAM regarding its commercially sensitive price list, one wonders whether the Court's willingness to compel disclosure of the Schedule was affected by the fact that Shell had already given Klemke access to the Schedule A:

> In March 2003, at the Plaintiff's request the Defendants produced the Mining Services Agreement which include [Schedule A]. One year later [Defendants'] counsel asked [Plaintiff's] counsel to return [Schedule A] on the basis [Schedule A was] irrelevant and highly confidential. Prior to the request for return of [Schedule A], Plaintiff counsel had provided copies of [Schedule A] to their client, to their expert and had examined one of the Defendants' employees generally on [Schedule A].[66]

Given the cost increases related to oil sands services in the last couple of years, release of price lists from several years ago may not have as much impact as it would have in the past.

D. *AURIZON MINES LTD. V. NORTHGATE MINERALS CORP.*[67]

1. BACKGROUND

This case deals with the application of standstill agreements in relation to the need to allow for the sharing of confidential information in the context of potential mergers and corporate transactions without the risk of the use of that information for other purposes.

2. FACTS

The plaintiff Aurizon Mines Ltd. (Aurizon) and defendant Northgate Minerals Corp. (Northgate) entered into discussions regarding a possible transaction between the two companies. As is customary, a confidentiality agreement was signed. This confidentiality agreement included a standstill provision that prohibited the other party from acquiring securities of or communicating with the shareholders of the other party for a period of time. Each party signed a separate agreement as provider and recipient of confidential information. Aurizon provided some information to Northgate, although it was not clear that the information was confidential, and then advised that it no longer wished to pursue a possible transaction. Northgate then provided a letter to Aurizon accepting Aurizon's position and advising that it regarded all parties' obligations under the confidentiality agreements to be at an end.

Prior to the expiry of the standstill period, Northgate purchased voting securities of Aurizon and on 1 June 2006 issued an offer for all outstanding securities of Aurizon. Aurizon brought an action seeking declaratory injunctive relief and damages. The applications were heard in June 2006 and the appeal was heard a week later.

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[66] *Klemke2*, *supra* note 62 at para. 6.
[67] 2006 BCSC 1022, 19 B.L.R. (4th) 318, aff'd 2006 BCCA 340, 19 B.L.R. (4th) 171.

3. DECISION

Both levels of court were prepared to grant final judgment in favour of Aurizon for the relief that it sought, finding that the standstill agreement was binding on Northgate. Finding that it was not an express term of the standstill agreement that Aurizon provide confidential information, it was not necessary to review whether Aurizon had misrepresented its intention to proceed with a transaction. The Courts could find neither rescission nor repudiation of the standstill agreement by Aurizon's refusal to provide further information. The permanent injunction was granted based upon the finding that the balance of convenience favoured Aurizon. The Courts held that it is in the public interest to permit market participants to enter into meaningful discussions without incurring the risk of a hostile take-over bid.

4. COMMENTARY

Non-competition and standstill agreements are commonplace additions to confidentiality agreements, frequently inserted without sufficient consideration given to their application. This case reinforces the need to review such contracts carefully to ensure that the non-competition or standstill provision will not hamper or prevent prudent business development without the accompanying benefit received in the form of confidential information. The drafters may not have considered the possibility that no confidential information would be provided and therefore the need to provide for the termination of the standstill provisions where no benefit had been received had likely not been addressed. It is not clear whether the result would have been different if Northgate's letter confirming that the agreements had been terminated had specifically mentioned the standstill provisions.

IV. CREDITORS' RIGHTS

A. *RE CALPINE CANADA ENERGY LTD.*[68]

1. BACKGROUND

In this case, the issue was whether or not a Call on Production Agreement (COP) entered into between Pengrowth Corporation (Pengrowth) and Calpine Canada Natural Gas Partnership (Calpine) was an eligible financial contract (EFC) as defined in the *Companies' Creditors Arrangement Act*,[69] such that a court could not stay the termination of an agreement pursuant to its terms. A COP is a right to purchase petroleum and/or natural gas from specific properties.

2. FACTS

Effective 14 September 2002, Calpine and Pengrowth entered into a Purchase and Sale Agreement, pursuant to which Calpine sold certain petroleum and natural gas rights and assets to Pengrowth and the parties agreed to enter into a COP at Closing. The COP provided Calpine with a recurring preferential right to purchase gas or petroleum produced from the

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[68] 2006 ABQB 153, 19 C.B.R. (5th) 187.

[69] R.S.C 1985, c. C-36 [*CCAA*].

lands. The agreement contained a fixed delivery point and a price calculated by reference to current market prices. On 20 December 2005, the Calpine applicants were granted an initial order under the *CCAA* restraining persons from terminating or suspending their obligations under agreements, which order, pursuant to the *CCAA*, would not apply to EFCs. On 21 December 2005, Pengrowth provided notice to Calpine that it was suspending the delivery of gas under the COP. According to Pengrowth, Calpine's filing for protection under the *CCAA* constituted a "triggering event"[70] under the COP, allowing for suspension or termination of the agreement. Pengrowth alleged that the COP was an EFC, and as such was exempt from application of the stay.

3. DECISION

The Court indicated that the key issue was whether or not such long-term purchase and sale contracts can be characterized as forward commodity contracts and derivatives. The Court listed elements often present in derivatives which included that: derivatives can be "marked to market,"[71] meaning the net present value of the contract may be determined by the market price of the underlying interest and derivatives have a determinate price, which would allow hedging. Following the decision in *Blue Range*,[72] the Court applied the "fairness of result"[73] test to find that it was unfair to permit the termination of the COP. This was due to the fact that it would deprive Calpine of a valuable asset. In contrast, Pengrowth, which was not hedged in relation to the COP, would be in no worse off position than any other supplier required to purchase production at market prices. As the COP agreement in this case did not contain provisions such that it could be marked to market or provide for a determinate price, and was entered into in consideration of the sale of oil and gas producing land, the Court held that the COP did not have a financial purpose and as such, did not fall within the definition of an EFC. In the result, the Court exercised its jurisdiction to stay the termination of the Agreement.

4. COMMENTARY

Some Canadian courts have applied a subjective fairness test in deciding what will or will not qualify as an EFC under the *CCAA*.[74] This approach allows the courts to be flexible in order to ensure that the definition does not interfere with the dominant purpose of the *CCAA*, which is to facilitate the restructuring of insolvent companies for the benefit of stakeholders. However, this approach does not provide certainty, and it is likely that the resulting risk will be built into the cost of such financial instruments.

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70 *Supra* note 68 at para. 7.
71 *Ibid.* at para. 10.
72 *Supra* note 5.
73 *Ibid.* at para. 28.
74 See e.g. *Blue Range*, *ibid.*

B. *GMAC COMMERCIAL CREDIT CORP. – CANADA v. T.C.T. LOGISTICS INC.*[75]

1. BACKGROUND

Bankruptcy suspends business activity and turns over the operations of a business to a court appointed receiver. It is the role of the receiver to liquidate the assets of the business and maximize the return to creditors. This case deals with what happens when the rights of unionized employees are in conflict with the goal of maximizing return to creditors. The main issue in this case was the test applied under s. 215 of the federal *Bankruptcy and Insolvency Act*,[76] the provision which prevents lawsuits against receivers without prior judicial approval. The order appointing the interim receiver purported to protect the receiver from being designated as a successor employer and from being subject to any employment obligations arising under either provincial or federal legislation. The unionized employees sought to challenge this aspect of the order.

2. FACTS

The bankrupt, T.C.T. Logistics Inc. (T.C.T.), was a national trucking outfit with more than a dozen operating companies and 1300 employees. Forty-two employees at a Toronto warehouse were represented by the Industrial Wood and Allied Workers of Canada, Local 700 Union (the Union). GMAC Commercial Credit Corporation – Canada, T.C.T.'s largest secured creditor, applied for an order appointing KPMG Inc. (KPMG) interim receiver following the discovery of serious misrepresentations with respect to T.C.T.'s financials. The order provided that KPMG would not be considered a successor employer in its role as interim receiver. Pursuant to an agreement of sale in respect of T.C.T.'s warehousing division, KPMG dismissed all employees except for those required to manage the divestment. The Union applied to the Ontario Labour Relations Board (OLRB) seeking a declaration that the purchaser was a successor employer to T.C.T. and/or KPMG. The OLRB stayed the application pending the necessary court approval pursuant to s. 215 of the *BIA*. The Bankruptcy Court denied the Union leave to pursue its "successor employer" application. On appeal, the majority of the Court of Appeal held that the Bankruptcy Court had not applied the proper test for leave under s. 215 of the *BIA* and that only the OLRB had jurisdiction to determine who was a successor employer.

3. DECISION

The approach to granting leave under s. 215 of the *BIA* is derived from the 1993 decision in *Mancini (Trustee of) v. Falconi*.[77] The test provides for leave to be refused if a claim is frivolous, vexatious, or manifestly unmeritorious. In this case, the Court indicated that "[t]o impose a higher s. 215 threshold when it is a labour board issue is to read into the [*BIA*] a lower tolerance for the rights of employees represented by unions than for other creditors."[78] In this case, the Union argued that the interim receiver became the employer of employees

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[75] 2006 SCC 35, [2006] 2 S.C.R. 123.
[76] R.S.C 1985, c. B-3 [*BIA*].
[77] [1993] 61 O.A.C. 332 [*Mancini*].
[78] *Supra* note 75 at para. 71.

after its appointment, due to the fact that it continued to use the employees to operate the warehouse after its appointment. The Union further argued that KPMG, as an employer, was required to comply with the collective agreement in place, as well as applicable labour and employment statutes. The Union claimed that KMPG had failed to do so by entering into an agreement of sale that did not deal with the fact that there was a union in place in respect of the warehouse workforce. The Court, in this case, held that the threshold set forth in *Mancini* had not been met, as the Union's claim could not be considered frivolous, vexatious, or manifestly unmeritorious on the evidence. Accordingly, the Court granted leave to the Union to bring its successor employer application before the OLRB.

4. COMMENTARY

The Court noted that it is common practice to provide no notice to a Union of a Motion appointing an interim receiver. As such, unions are excluded from the process of formulating a plan to divest of the company's assets. While the Court indicated that it is not clear how the Board would deal with the Union's claim, this case suggests that allowing unions to participate in formulating a plan to divest of a company's assets may be necessary in order to be confident that the insolvency process will proceed in a timely manner.

V. EMPLOYMENT

A. *KEAYS V. HONDA CANADA INC.*[79]

1. BACKGROUND

On 29 September 2006, the Ontario Court of Appeal released its much anticipated decision dealing with the pitfalls of terminating the services of a disabled employee.

2. FACTS

After fourteen years, the defendant Honda of Canada Inc. (Honda) terminated the employment of the plaintiff Kevin Keays (Keays), allegedly for cause. Keays had been diagnosed with Chronic Fatigue Syndrome (CFS) and had been on long-term disability for a period of time. Those benefits were cancelled and he returned to work, but required frequent absences due to illness, absences which he was required to validate by doctor's notes. Eventually Keays was ordered to see Honda's occupational health physician, which he refused to do without an explanation as to the purpose of the assessment. He was dismissed and sued Honda for wrongful dismissal.

3. DECISION

The trial judge had found that Keays's employment had been terminated without cause and awarded him fifteen months' pay in lieu of reasonable notice, a nine month extension of the notice period for "bad faith" discharge and ordered Honda to pay a further CDN$500,000

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[79] (2006), 82 O.R. (3d) 161 (C.A.), leave to appeal to S.C.C. granted, appeal heard on 20 February 2008.

in punitive damages.[80] The punitive damages were for the discrimination and harassment Keays had endured.

The Court of Appeal upheld most of the trial Court's findings but did reconsider the punitive damages claim. In a 2-1 decision, the Court of Appeal reduced the punitive damages claim to $100,000, stating that the objective of punitive damages is to punish the defendant rather than to compensate the plaintiff. In reviewing the punitive damages amount the Court of Appeal found that the misconduct had only been for the last seven months of employment, being the period of time when Keays was required to provide a doctor's note for every absence, rather than the five years the trial judge had found. In addition, Honda had acted on wrong and incomplete information that had caused it to question Keays's disability and had, for almost a year, accommodated his absences. While a court may take into account the size of the employer, it should only be relevant in determining punitive damages if the employer misuses that power, or the court finds that a lesser award will not be a sufficient deterrent. In addition, the award failed to accord with the fundamental principles of proportionality, and the award was therefore reduced to $100,000.

4. COMMENTARY

The decision reinforces the sensitivities of dealing with disabled employees. The Court found that an employer has a duty to accommodate a disabled employee until such accommodation results in hardship to the employer and in doing so, must do so reasonably and in good faith. The duty to act in good faith and proceed with caution in any such termination is a must.

B. *HIBBERD V. HURRICANE HYDROCARBONS LTD.*[81]

1. BACKGROUND

This case reads like a primer in basic contract law, dealing with parol evidence, collateral contracts, misrepresentation, mistake and rectification, while simultaneously dealing with stock option and employment issues.

2. FACTS

The individual plaintiff Michael Hibberd, through his consulting company, the co-plaintiff, MJH Services Inc. (MJH), provided consulting services to the corporate defendant Hurricane Hydrocarbons Ltd. (Hurricane) over a period of approximately four years. Hibberd initially entered into oral agreements with Hurricane's president to provide financial consulting services that were subsequently formalized into written agreements. Hibberd's agreement was a stock option agreement that provided that the stock options would expire 60 days after the termination of the contract for services. The contract between MJH and Hurricane provided for termination by MJH on seven days notice, and by Hurricane only for cause. Hibberd was not happy with the termination clause in his stock

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[80] See *Keays v. Honda Canada Inc.*, [2005] O.T.C. 222.

[81] 2006 ABQB 707, 407 A.R. 1.

option agreement and claimed that he had received assurances from the president of Hurricane at the time the contract was signed that the clause would not be enforced. Following *CCAA*[82] proceedings and a plan of arrangement by Hurricane, termination notices were provided, first to MJH and subsequently to Hibberd. Hibberd did not exercise his options within the sixty day notice period and tried unsuccessfully to do so after the time period had elapsed. The value of the Hurricane shares went up significantly in the interim.

Hibberd and MJH brought an action for unlawful termination of the consulting contract without notice and for the resulting termination or expiry of the stock options which had been issued as compensation for services rendered.

3. DECISION

In dismissing all of the plaintiffs' claims, the Court reviewed once again the law in Alberta regarding parol evidence, including inconsistent terms, collateral contracts, and provisions in the contract which stated that the contract was the entire agreement between the parties. In this case, the alleged verbal agreement directly conflicted with the terms of the written agreement and was found to be inadmissible.

The claim for misrepresentation was similarly dismissed on the basis that in order to be actionable the misstatement must be one of fact, not of intention.

No damages were payable under the consulting contract, notwithstanding that the contract had no provision allowing for termination by Hurricane without cause. As Hibberd and MJH had taken pains to ensure that they remained as independent consultants and not as an employee, Phillips J. found that this was an inappropriate case for implying a reasonable period of notice.

4. COMMENTARY

This case, besides summarizing once again the law on many basic legal principles, reinforces the need to ensure that the contract reflects the agreement reached. "Don't worry, I'll look after you," just does not provide protection of a party's legal rights.

VI. ENVIRONMENTAL LAW

A. *KA'A'GEE TU FIRST NATION V. PARAMOUNT RESOURCES LTD.*[83]

1. BACKGROUND

The *Mackenzie Valley Resource Management Act*[84] creates an integrated co-management for public and private lands and waters throughout the Mackenzie Valley in the Northwest Territories. The *Act* establishes public boards to regulate the use of land and water, to prepare

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82 *Supra* note 69.
83 2006 NWTSC 30, 22 C.E.L.R. (3d) 112.
84 S.C. 1998, c. 25.

regional land use plans to guide development, and to carry out environmental assessments and reviews of proposed projects.

2. FACTS

In November 2005, Paramount Resources Ltd. (Paramount) applied to the Mackenzie Valley Land and Water Board (MVLWB) for a land use permit and water licence to build six well sites in the Cameron Hills area, traditional territory of the Ka'a'Gee Tu First Nation (the First Nation). Paramount asked that its application be exempt from the preliminary screening process under the *Act*, based on a wide area environmental assessment done in June 2004. The wide area assessment focused on the cumulative effects of drilling, testing, and tie-in of up to 50 wells over a period of 10 years, production of oil and gas over 15 to 20 years, and abandonment and reclamation of the entire development. The MVLWB granted the application, indicating that the wide area assessment satisfied the preliminary screening requirements under Part V of the *Act*. The First Nation sought judicial review of the decision.

3. DECISION

The Court held that the preliminary screening requirement cannot be considered to have been met if the MVLWB has not complied with the steps set out in Part V. The requirement for preliminary screening cannot be avoided at the time that licences or permits are being sought for specific types of development. Since the *Act* requires the Board to comply with the steps set out in Part V, and the Board failed to do so, the Board had no jurisdiction to decide that the wide area assessment was sufficient. The Court also reviewed the notice that had been sent to the First Nation and held that it was inadequate, as it did not properly inform them of the decision that the MVLWB intended to make. The First Nation had been denied natural justice, and as such the Court overturned the Board's decision.

4. COMMENTARY

While the Court in this case emphasized the importance of the preliminary screening requirement, it went on to state that it was not necessary for a preliminary screening to deal with every aspect of a prior broad environmental assessment. The Court noted that the process could be more streamlined, but failed to go into detail as to what a more streamlined process would entail. However, what is clear is that the existence of a prior environmental assessment will not replace the requirement for preliminary screening.

B. *GEHRING V. CHEVRON CANADA LTD.*[85]

1. BACKGROUND

This case is what is often referred to as a "remediation cost recovery" or "remediation cost allocation" lawsuit.[86] The plaintiffs sought relief under s. 47 (5) of the *Environmental*

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[85] 2006 BCSC 1639, 25 C.E.L.R. (3d) 167.

[86] *Ibid.* at para. 2.

Management Act.[87] The plaintiffs being the current owners of the property claimed that the seven defendants were "responsible persons"[88] for the costs of remediation as set out in s. 45 of the *Act*. The plaintiffs had spent approximately CDN$120,000 to clean up the property, and asked that the remediation costs be allocated appropriately.

2. FACTS

The defendants included: a director of Shiskin Motors Ltd. (Shiskin), a company that sold gasoline from the property to retail customers from early 1949 to October 1963; representatives of L. & L. Motors Ltd. (L. & L.) including Mr. Filiatrault, a director of the company since 1964 and Ms. Filiatrault, a director of the company since 1977, which company sold gasoline to retail customers from the property from October 1963 to June 1978; Chevron Canada Limited (Chevron), successor to Standard Oil Company of British Columbia, which supplied gasoline to the retailers on the property from 1940 to 1976; and Fireside Electric Ltd. (Fireside), which was the registered owner of the property from 10 July 1978 until February 1992. In March 2004, an assistant regional waste manager determined that the property was a contaminated site. The Court found that 50 percent of the contamination occurred from leaking valves and piping from 1940 to 1978. Another 7 percent of the overall contamination was the result of a sudden underground storage tank (UST) leak during the L. & L. period of ownership. About 4 percent of the contamination occurred from a slow UST leak during the Shiskin period of ownership and 39 percent of the contamination occurred during the L. & L. period of ownership.

3. DECISION

The Court found that all but one of the defendants were "responsible persons" under the *Act*. L. & L. and Mr. Filiatrault were found jointly responsible for 50 percent of the total remediation costs. Ms. Filiatrault was found responsible for 5 percent of the total remediation costs. Fireside was found responsible for 25 percent of the remediation costs, and the plaintiffs, as current owners were found responsible for 25 percent of the total remediation costs. However, according to the Court, Chevron, the supplier of gasoline to the property, did not cause the gasoline to be used in a way that resulted in the contamination, and therefore, was not liable for the costs of remediation. The decision stands for several points of interest: directors who authorize or permit the activities of their companies that result in contamination are responsible persons under the *Act*; the language of the legislation is such that it does not include directors of dissolved companies as responsible persons; and the liability for the clean up will be allocated amongst the responsible persons that remain in existence.

4. COMMENTARY

The decision to allocate a significant portion of the clean up costs to the current owner of the property, being the first party to conduct remediation, may deter parties from voluntarily cleaning up their own properties. This is particularly the case, given that it appears that once

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[87] S.B.C. 2003, c. 53.

[88] *Supra* note 85 at para. 2.

a company has been dissolved, neither it nor its former directors will be responsible persons under the *Act*, a result which is inconsistent with the underlying rationale of environmental legislation.

C. *WINDSOR V. CANADIAN PACIFIC RAILWAY LTD.*[89]

1. BACKGROUND

This is a case involving the first certification of an environmental class action in Alberta. Under the *Class Proceedings Act*[90] there are five criteria that must be satisfied in a certification motion. The litigants must establish that: (1) the statement of claim discloses a cause of action; (2) there is an identifiable class of two or more persons; (3) the claims of the potential class members raise a common issue; (4) a class proceeding is preferable in order to have a fair and efficient resolution of the common issues; and (5) there is a person that can be appointed to fairly and adequately represent the interests of the class.[91] If these criteria are met, the application for certification must be granted.

2. FACTS

In this action, the plaintiffs alleged that the properties of the potential class of persons had groundwater beneath them that was contaminated with trichloroethylene (TCE). The defendant owned a railway maintenance facility near the properties and had used TCE for many years to clean engines and rolling stock. The plaintiffs claimed damages as a result of TCE contamination, including a reduction in property values. The plaintiff's case was founded in negligence, nuisance, trespass, and strict liability.

3. DECISION

The Court held that the "evidentiary basis" for the establishment of the common issue required for a class action is a "low bar,"[92] and that there need only be evidence sufficient to support certification. The Court emphasized that the role of a court is not to make a factual determination regarding the outcome of the action. Rather, the role of the court is to rely on the evidence only insofar as it pertains to the certification requirements. In this case, the Court held that the proposed common issue, that is whether there were certain common polluting substances affecting the properties, would be advanced in a meaningful way by the proposed common action. This was the case notwithstanding the need for individual assessments on the issues of causation and damage. The Court went on to suggest that certification was also justified in this case on the principles of judicial economy, access to justice, and deterrence.

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89 2006 ABQB 348, 402 A.R. 162, var'd 2007 ABCA 294, [2007] 12 W.W.R. 5 only with respect to removing the word "affected" from the class definition.

90 S.A. 2003, c. C-16.5.

91 *Ibid.*, s. 5(1).

92 *Supra* note 89 at para. 50.

4. COMMENTARY

Generally speaking, the biggest obstacle to certification of environmental class actions is the establishment of a common issue. This is due to the fact that environmental actions generally involve individuals whose lives had been affected in different manners and to different degrees. In addition, complaints typically relate to different dates and different locations, and are spread out over a number of years. As such, there was no economy to proceeding by class action; rather the merging of claims creates a single action that may be overly complex and unmanageable. It is, however, important to note that since this decision, the same Court has denied the certification of another proposed environmental class action.[93] In that case, the Court focused on the fact that the success of one member of the class in the action would result in the failure of the action of another, and on that basis dismissed, the application for certification.

VII. FREEHOLD LEASES

A. *AMETHYST PETROLEUMS LTD. V. PRIMROSE DRILLING VENTURES LTD.*[94]

1. BACKGROUND

Pursuant to cl. 1010 of the 1990 Canadian Association of Petroleum Landmen (CAPL) *Operating Procedure*, a "title preserving well" is "a well which is drilled, completed or recompleted … where the failure to conduct such operation would result in the forfeiture of all or a portion of the joint lands contained in a title document."[95] According to the Court in *APL Oil & Gas Ltd. v. Amoco Canada Resources Ltd.*,[96] whether a well was drilled as a title preserving well is not so much a question of law as it is a question of fact, depending upon the evidence as to the intention of the parties at the time the well was drilled. Further, where the controlling parties intended to drill a well for business reasons unrelated to the question of preserving the lease, the well may not be considered a title preserving well.

2. FACTS

On 18 September 1997, the lessor, Bearspaw Petroleum Ltd. (Bearspaw), issued a notice of default pursuant to the offset well provisions of the lease, to Amethyst Petroleums Ltd. (Amethyst), one of the lessees. That provision required the lessee to drill an offset well, in order to prevent drainage, in the event of commercial production being obtained from any well drilled on any laterally adjoining spacing unit. The lessees disputed the validity of the notice and soon after the notice of default was withdrawn. Notwithstanding that the first notice of default was invalid, Primrose Drilling Ventures Ltd. (Primrose), a lessee, reviewed the prospect of drilling an offset well and determined it to be a viable option. Bearspaw later

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93 *Paron v. Alberta (Environmental Protection)*, 2006 ABQB 375, 402 A.R. 85.

94 2006 ABQB 595, var'd 2007 ABCA 355 (ss. 4, 5 and 7 of para. 5 the trial judge's supplementary reasons were set aside as the reasons exceeded the remedy previously agreed to by the parties under the direction of the case management judge).

95 CAPL, *Operating Procedure* (1990), online: CAPL <http://www.landman.ca/store/capl_publication_list.php>.

96 (1993), 147 A.R. 345 (Q.B.).

served a second notice of default, which contained substantially the same terms as the first, but added to it an offer to allow the lessees certain of its rights under the lease, notwithstanding the failure to drill an offset well. Shortly thereafter, Primrose issued a notice of independent operations in respect of the offset well; indicating that the well was title preserving and failure to participate in the operation would result in the non-participant's forfeiture of its rights under the lease. That notice forms the basis of this dispute.

3. DECISION

The primary issue in this case was whether Primrose was entitled to terminate the plaintiff's interest in the section and the producing well thereon, for failure to participate in a purported title preserving operation. The Court held that Primrose should not be entitled to claim that the operation was title preserving, since the default notice that Primrose relied upon in making the claim was invalid. Although this case was decided based on the fact that the default notice was invalid, the Court went on to discuss the factual context in which the well may be seen as title preserving. In this regard, the Court noted that the only thing that had changed between the first and second notice of default was that Primrose had determined that the well was economically viable. To this the Court suggested that the intention of the party proposing to drill the well may be considered in making the determination as to whether a well is or is not title preserving. In addition, the second notice of default included an offer to surrender only a portion of the rights held under the lease, rather than the termination of the entire lease. This fact, according to the Court, was inconsistent with the claim that the well was title preserving. In the result, the offset well was held not to be a title preserving well and failure on the part of the other parties to participate would not result in forfeiture, but rather a penalty on production.

4. COMMENTARY

Although the Court was able to determine that the well in these circumstances was not title preserving based on the fact that the notice of default in question was invalid, the Court's discussion of the facts that may be considered in general, in order to determine whether a well is title preserving is of interest. In this regard, industry participants should be aware that the intention of the proposing party may be a consideration of the Court in determining whether or not a well is title preserving, as well as the context in which the need to drill the well in order to preserve title arises.

B. *MISSILINDA OF CANADA LTD. V. HUSKY OIL OPERATIONS LTD.*[97]

1. BACKGROUND

The CAPL 1991 lease introduced a negotiable cap on the expenses which may be deducted from royalties by providing that the royalty "shall not be less than ___ percent (___ %) of the royalty that would have been payable to the lessor if no such expenses had been

97 2007 MBCA 24, [2007] 3 W.W.R. 613.

incurred by the lessee."[98] The introduction of this cap was clearly intended to benefit the freehold lessor owner.

2. FACTS

Missilinda of Canada Ltd. (Missilinda) was the lessor of an undivided 50 percent interest in a parcel of land in Saskatchewan known as the Red Jacket field. The defendant, Husky Oil Operations Limited (Husky) was one of the lessees and the operator of the oil well to which the lease applied. Pursuant to cl. 2 of the lease, "[t]he Lessee shall remit to the Lessor, on or before the 25th day of each month, (a) an amount equal to the current market value at *the wellhead* on the date of delivery of Seventeen & One Half (17 ½%) per cent of the crude oil and crude naphtha produced, saved and marketed from the said lands during the preceding month."[99] It is of note that there was a period of time when trucks were used to move the product from the well to the battery and from the battery to the point of sale and no deduction for the cost of trucking was made.

3. DECISION

The issue in this case was whether Husky was entitled to make certain deductions under the terms of the lease, including deductions for facility operating expenses, capital cost allowances, and a sum calculated to represent return on investment. Pursuant to the terms of the lease, the royalty was payable in respect of the current market value at the wellhead. However, oil is not saleable at the wellhead. As such, according to the Court, this clause of the lease contained a latent ambiguity. Based upon the rule of contractual interpretation, the latent ambiguity allowed the Court to look at the extrinsic evidence to determine the meaning of the provision of the lease. The Court held that such evidence indicated that deductions in this case were to be made in accordance with a standard approach to calculating deductions, and included such components as capital expenses, operating expenses, and return on investment. The Court also relied on the decision in *Resman Holding Ltd. v. Huntex Ltd.*[100] which dealt with a similar provision in a lease, and in which it was held that the industry practice is that the royalty is computed at the wellhead and deductions for such costs as compression, gathering, transportation, and processing were permissible. In the result, the appeal was dismissed.

4. COMMENTARY

This decision is in line with the prior case law in which the Courts have construed "at the wellhead"[101] as allowing the lessee to deduct all costs beyond the wellhead, which would include the costs of treating, separating, dehydrating, and storing leased substances. This is due to the fact that these costs are legitimate expenses incurred by the lessee in order to make

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[98] CAPL, *Petroleum and Natural Gas Lease* (1991), online: CAPL <http://www.landman.ca/store/capl_publication_list.php>.

[99] *Supra* note 97 at para. 3 [emphasis added].

[100] (1983), 54 A.R. 281 (Q.B.).

[101] *Supra* note 97 at para. 4.

the leased substances marketable. This is so, notwithstanding the fact that this is not an express term of some of the older lease forms that are still in use.

C. *FREYBERG V. FLETCHER CHALLENGE OIL AND GAS INC.*[102]

1. BACKGROUND

On 10 February 2005, the Alberta Court of Appeal decided that a petroleum and natural gas lease between Lady Ivry Freyberg and Apache Canada Ltd. (Apache) was no longer valid.[103] This decision deals with the measure of damages to which Freyberg is entitled.

2. FACTS

In 1975, Freyberg's cousin as to a 2/3 interest, and NV Resources Ltd. (NV) as to a 1/3 interest, entered into a lease with Voyageur Petroleum Ltd. (Voyageur). Freyberg inherited her cousin's interest. In 1978 the 6-3 well was drilled and shut-in until 1999. The defendant, Tudor Corporation Ltd. (Tudor), became the operator of the 6-3 well. In 1999, Tudor entered into an agreement with Kalta Energy Corp. (Kalta) whereby Kalta could earn 50 percent of Tudor's interest and Kalta became the operator. Kalta had entered into a prepaid gas purchase contract with Direct Energy Marketing Limited (Direct Energy), with payments on that advance to be made from the supply of gas, including the 6-3 well. In 2000, Kalta was placed into receivership and Tudor resumed operatorship. Apache was successor in interest to Voyageur, retaining an interest in the 6-3 well and was contract operator. Apache took its production in kind.

The 6-3 well produced from 1999 until it was shut-in as a result of a demand by counsel for Freyberg to cease production of Freyberg's gas in 2006.

NV never disputed the validity of its interest in the lease and entered into a new lease with Apache in 2006 after the Court of Appeal had ruled on the invalidity.

3. DISCUSSION

The Court found that there were three categories of defendants, with issues and liability differing in each instance. The first category of defendants were the working interest owners, (Oil Company Defendants) which included, among others, Tudor, Kalta, and Apache. The second category was Direct Energy who had received gas from the 6-3 well under the contract with Kalta. The last category was AltaCanada Energy Corporation (AltaCanada) and Alberta Selecta Corporation (Alberta Selecta), who, while they were working interest owners, had only received revenue from production from the well for one month because they had elected to not participate in the certain operations on the 6-3 well and were in a penalty position.

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[102] 2007 ABQB 353, [2007] 10 W.W.R. 133.

[103] 2005 ABCA 46, 363 A.R. 35 [*Freyberg*]. For a discussion of this decision, see David J. Stanford & Sean S. Smyth, "Recent Judicial Developments" (2007) 44 Alta. L. Rev. 661 at 713.

Dealing first with the Oil Company Defendants, the issues were: (i) tort of conversion; (ii) level of damages; and (iii) joint and several liability.

(i) Tort of Conversion

Freyberg claimed that in unlawfully taking leased substances, the Oil Company Defendants had committed trespass and conversion. The Court held that the defendants "had the right to take the NV third of the gas and it is not possible to extract some of the gas."[104] Since the Oil Company Defendants had an undisputed right to 1/3 of the production, the Court held that there was no trespass. As a result, there was nothing unlawful about bringing Freyberg's gas to the surface. The tort occurred when they dealt with the gas by taking it from the wellhead.

(ii) Level of Damages

There are two approaches to the measure of damages in cases of conversion: on a restitutionary basis, where the remedy is to remove any benefit or gain from the defendant wrongdoer; or, on a compensatory basis, where the focus is on placing the plaintiff back into the position he or she would have been in but for the commission of the tort, rather than in stripping the benefit from a wrongdoer. After reviewing the case law considering the applicable remedy for conversion of natural resources, including a detailed discussion of the Saskatchewan Court of Appeal decision in *Montreal Trust Co. v. Williston Wildcatters Corp.,*[105] Kent J. found that the appropriate approach to damages in this case was the compensatory approach. If Freyberg could establish that she could have removed the minerals on her own, she would be entitled to receive the value of the minerals removed minus the costs of removing the minerals. If it was shown that she could not have removed the minerals on her own, the amount will be calculated in a different manner, such as a bonus payment and an increased royalty.

The Court then reviewed whether at any time the conduct of Freyberg was such that the Oil Company Defendants had been granted leave and licence to continue to produce. Acceptance of royalty payments, even after Freyberg had knowledge that the lease may not be valid, was not sufficient to grant leave and licence. As a result, the only period of time where Freyberg knew of her rights and did not demand that production cease was from the date that the Supreme Court of Canada refused leave to appeal[106] until the date when she demanded that production cease.

It was then determined that Freyberg could not have produced the 6-3 well on her own. NV, as owner of the other 1/3 interest, would not have allowed her produce it on her own and she needed access to the well-bore and the surface lease that belonged to the Oil Company Defendants, or she would have needed to obtain an order from the Alberta Energy and

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[104] *Supra* note 102 at para. 101.

[105] 2003 SKQB 360, [2004] 3 W.W.R. 574.

[106] *Freyberg*, *supra* note 103, leave to appeal to S.C.C. refused, 30874 (10 November 2005).

Utilities Board (AEUB),[107] the results of which were felt to be uncertain. As a result, the Court found that Freyberg would have had no option but to enter into a lease arrangement with the Oil Company Defendants. In doing so however, she would have a very strong bargaining position. In addition, since there was no risk to the Oil Company Defendants, the Court found that the typical royalty of 15 percent was too low, but did not have sufficient evidence to establish what that royalty might have been. The parties were sent away to try to negotiate the terms of a lease, failing which there will be a further hearing.

(iii) Joint and Several Liability

Because Kalta had been placed in receivership, the issue of several versus joint and several liability among the Oil Company Defendants took on additional significance. In order to find joint and several liability there must be a wrongful act mutually performed by the defendants in the furtherance of a common purpose. The wrongful act was producing the gas without a valid lease, and the common purpose was the development and production of the 6-3 well, with the result that the Oil Company Defendants were found to be jointly and severally liable for the conversion. As among themselves they would only be liable for their percentage interest; however, jointly they would need to pay the amount otherwise allocated to Kalta.

Direct Energy argued that they should not be liable as purchaser of the gas. The Court found that since the claim against Direct Energy in the initial statement of claim was only for filing a wrongful registration of a caveat, the subsequent claim for conversion was barred under the *Limitations Act*.[108] As a result the Court did not have to rule on whether Freyberg had acted in a manner inconsistent with her ownership such that she was not now entitled to claim ownership against Direct Energy as purchaser of the gas.

Lastly, AltaCanada and Alberta Selecta had done nothing to participate in the conversion and as a result, were only responsible to repay the money they had received in 2004 after the trial decision had been released finding that the lease was valid, and before the Court of Appeal reversed that decision.

4. COMMENTARY

This decision may in many instances be distinguished on its facts. For example, it does not fully answer the question of what the remedy may be if the lease covers the entire interest in the lands, or what the remedy may be if the lessor had the level of sophistication to own and operate the well.

As noted, trespass was pleaded but found not be applicable. This assumes that the Oil Company Defendants had the right to NV's gas by virtue of "leave and licence"[109] as NV's interest was governed by the same lease that had been determined to have lapsed. What the

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107 Please note that as of 1 January 2008 the AEUB has been divided into two regulatory bodies, the Energy Resources Conservation Board (ERCB) and the Alberta Utilities Commission (AUC).

108 R.S.A. 2000 c. L-12.

109 *Supra* note 101 at para. 121.

Court does not address in the decision is whether the rights of an "overholding tenant" have any application in an oil and gas lease situation,[110] nor does it address the rights of a tenant in common to deal with its interest in the joint property.

There is limited authority on what rights a co-tenant (or his lessee) has to develop minerals in a tract without the consent of concurrent owners. The *Statute of Westminster II*[111] and the *Statute of Anne*[112] provide the basis from which the current law on the liability of mineral estate co-tenants to account to each other for benefits derived from shared real property. American authorities vary depending upon the interpretation of these two English statutes and their contemporary counterparts.[113]

The *Statute of Westminster II* subjects a co-tenant to the law of waste, essentially restricting a co-tenant from removing minerals from the land concurrently owned without the consent of his concurrent owners.[114] The *Statute of Anne* provides for an accounting by one joint tenant or tenant in common for receiving more than a just share or proportion of rents, revenues, monies, or similar profits derived from the lands.[115] As a result of these two statutes, a mineral co-tenant may be restrained from extracting oil or gas and be required to respond in damages for wrongful extraction, or, on the other hand, the mineral co-tenant may be permitted to extract minerals but be required to account to the other co-tenants for taking an undue proportion of the profits, depending upon the law applied in the particular jurisdiction. Although the Court did not address the rights of co-tenants, it appears that the end result may not have differed significantly, provided that the Court is able to determine that the production of gas was not "waste" under the *Statute of Westminster II*.

Unlike the decision in *Kensington Energy Ltd. v. B & G Energy Ltd.*[116] where the Court limited the accounting for revenue from a well on an invalid lease to the date that pleadings were filed, it appears Freyberg is entitled to an accounting from the date that the well was placed on production.

Practice tips arising from this decision include careful monitoring by companies producing from wells on freehold lands of the financial status of their joint venture partners where there is any question of the validity of the underlying leases, based on the finding of joint and several liability. When advising a lessor, careful consideration should be given to the timing of a directive to cease production to ensure that there is no room for arguing that there has

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[110] For a discussion of this and other issues relating to rights and remedies after a lease has terminated, including a discussion on the rights of a tenant who holds over at the end of a term without the landlord's dissent or assent, see Nigel Bankes, "Termination of an Oil and Gas Lease, Covenants as to Title, and Assessment of Damages for Wrongful Severance of Natural Resources: A Comment on *Williston Wildcatters*" (2005) 68 Sask. L. Rev. 23.

[111] 13 Edw. I; 1 Statutes at Large, 196.

[112] 4 Anne, C. 16, Sec. XXVII, 11 Statutes at Large, 161.

[113] Eugene Kuntz, *A Treatise on the Law of Oil and Gas: Including Forms, Statutes, Regulations*, vol. 1 (Cincinnati: Anderson Publishing Co., 1987) §5.2 at 138.

[114] Patrick H. Martin & Bruce M. Kramer, *Williams & Meyers Oil and Gas Law*, Abr. 2d ed. (Newark, N.J.: Matthew & Bender, 2004) §502 at 5-2.

[115] Kuntz, *supra* note 113 at 139.

[116] 2005 ABQB 734, currently under appeal.

been leave and licence to produce. This consideration has to be balanced with the potential for liability for demanding that a well on a valid lease be shut in.

VIII. SURFACE RIGHTS

A. *MACARTHUR V. BLUE MOUNTAIN ENERGY LTD.*[117]

1. BACKGROUND

Section 25(1) of the *Surface Rights Act*[118] sets forth the following considerations that the Surface Rights Board (the Board) may take into account in determining the amount of compensation payable to a surface land owner:

> (a) the amount the land granted to the operator might be expected to realize if sold in the open market by a willing seller to a willing buyer on the date the right of entry order was made,
> (b) the per acre value, on the date the right of entry order was made … based on the highest approved use of the land,
> (c) the loss of use by the owner or occupant of the area granted to the operator,
> (d) the adverse effect of the area granted to the operator on the remaining land of the owner or occupant and the nuisance, inconvenience and noise that might be caused by or arise from or in connection with the operations of the operator,
> (e) the damage to the land in the area granted to the operator that might be caused by the operations of the operator, and
> (f) any other factors that the Board considers proper under the circumstances.[119]

The common law also permits the Board to take into account the pattern of dealings in the area.

2. FACTS

In this case, the appellants challenged certain compensation orders issued by the Board. The operator had applied for and was granted a right of entry by the Board, pursuant to statutory authority, to occupy and use certain lands for its operations. The highest approved use for the lands as of the date of the right of entry order was for agricultural purposes. The area of the lands that were occupied by the operator was determined to be bush land; however, the Court made a finding of fact that the operations would also have an adverse effect to the normal use of the remainder of the land owner's property.

3. DECISION

The main issue in this appeal was the Board's application of the factors listed in s. 25(1) of the *Act*. According to the Court, the amount of compensation must be determined at the time of the taking, looking forward, in respect of such matters as nuisance, disturbance, or

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117 2006 ABQB 507.
118 R.S.A. 2000, c. S-24.
119 *Ibid.*, s. 25(1).

tangibles lost. The Court rejected the position that the Board erred in failure to consider all of the factors set forth in that section of the *Act*, by holding that s. 25(1)(a) did not apply. The Board had held that s. 25(1)(a), pertaining to the amount the landowner would realize if the lands were sold in the open market, did not apply, as there was no evidence that the lands were a saleable parcel and, as such, there were no appropriate means of valuing the land. In this regard, the Court held that the Board had in fact put its mind to value of the land by its determination that there was no evidence that the parcel was saleable and no definitive pattern of dealings in the area. On the pattern of dealings requirement, the Court indicated that individual settlements or deals are admissible; however, in order to be relevant, the pattern of dealings must be comparable with the situation before the Board. Since this was not the case in these circumstances, the Board was justified in consideration of the other heads of compensation in making its determination and the appeal was dismissed.

4. COMMENTARY

While the Court's decision was based primarily on the finding that the Board had considered all of the factors set out in s. 25 of the *Surface Rights Act*, and as such had not erred in making its determination as to compensation, the Court's discussion on the pattern of dealings criteria further highlights the pitfalls of relying on this factor in setting compensation. In this regard, this decision is in line with the cases in which courts have instructed the Board to focus more on the loss of use and adverse effect criteria, as opposed to the pattern of dealings in the area in making the determination as to appropriate compensation.

B. *IMPERIAL OIL RESOURCES LTD. V. 826167 ALBERTA INC.*[120]

1. UPDATE

This is an appeal of the Alberta Court of Queen's Bench decision, set forth in last year's article.[121] In that case, the Court had reduced an award by the Surface Rights Board of annual rentals under a surface lease from CDN$179,750 to $120,340, on the basis that the evidentiary burden to demonstrate the uniqueness of the landowner's use of the land, in relation to other ranchers in the area, had not been met. In this case, the appeal was dismissed. While the Court of Appeal noted that the judge appeared not to follow a pragmatic and functional analysis of the Board's decision, the judge had applied the correct standard of review, that of reasonableness.

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[120] 2007 ABCA 131, 404 A.R. 212.

[121] *Imperial Oil Resources Ltd. v. 826167 Alberta Inc.*, 2005 ABQB 309. See Stanford & Smyth, *supra* note 103 at 724.

IX. RIGHTS OF FIRST REFUSAL

A. *DE BEERS CANADA INC. V. SHORE GOLD INC.*[122]

1. BACKGROUND

The question of what is a disposition of an interest under a preferential right to purchase when the entire interest or an undivided percentage of the whole has not been assigned is not one of the typical questions that our courts have been asked to address, but it raises some interesting issues. Unfortunately, much of this decision turns on the exact wording of the contract, which is not the wording found in most oil and gas contracts.

2. FACTS

The plaintiff De Beers Canada Inc. (De Beers) and the defendants — Shore Gold Inc. (Shore Gold), Cameco Corporation (Cameco), UEM Inc. (UEM), and Kensington Resources Ltd. (Kensington) — with the exception of Shore Gold, had entered into a joint venture agreement (JVA) for the exploration, development, and production of diamonds. The JVA provided that a management committee would make decisions based on the approval of the majority votes cast based on the percentage ownership in the properties. No one party had a majority interest. The JVA also included a right of first refusal on transfers as follows:

> 14.01 If a Party (denoted in this Article XIV as the "Vendor") shall wish to sell, assign, transfer, convey or otherwise dispose of all or part of its Participating Interest in the Program Lands or a Project Area (herein called the "Offered Interest") (the Parties being absolutely prohibited from selling, assigning, transferring, conveying or otherwise disposing of any interest other than all or part of its Participating Interest) at any time during the currency of this Agreement, the other Parties hereto then having a Participating Interest in the Program Lands or Project Area affected (hereafter in this Section 14.01 called the "Purchasers") shall be entitled to a right of refusal in respect thereof.[123]

A disagreement arose over the timing of the exploration and development program with Shore Gold (who was the parent company of one of the joint venture participants, Kensington leading the initiative for a faster pace of development). Shore Gold entered into an agreement with Cameco and UEM whereby Cameco and UEM agreed that for a period of seven years they would vote their percentage interest in accordance with the written instructions of Shore Gold as to matters relating to the exploration plan. The votes of UEM and Cameco together with Kensington's votes were sufficient to support a majority decision in favour of Shore Golds's proposals. De Beers took the position that by entering into the voting agreement, UEM and Cameco had effectively sold their vote, which De Beers claimed was the sale of an "interest" contrary to the provisions of s. 14.04 of the JVA.[124]

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[122] 2006 SKQB 154, 18 B.L.R. (4th) 50 [*De Beers* (Q.B.)], aff'd 2006 SKCA 58 [*De Beers* (C.A.)].

[123] *De Beers* (Q.B.), *ibid.* at para. 17.

[124] *Ibid.*

3. DECISION

The Saskatchewan Court of Queen's Bench found that s. 14.01 of the JVA created a right of first refusal that applied to a sale of a portion of a party's participating interest, but only to the interest in the joint venture property. The right to vote was not joint venture property. The words in parentheses did not create additional rights.

The matter was appealed and heard by the Court of Appeal in May 2006. In a unanimous decision, the Court of Queen's Bench decision was upheld. The Court of Appeal held first that the words in parentheses did not add any additional right and obligations, but rather were there to "recall to the parties their dedication of assets to the joint venture, and their inability to dispose of them qua separate assets."[125] The Court went on to find that if the parenthetical phrase was a substantive provision creating new obligations and prohibitions, they would find that the voting agreement did not create a disposition of the voting rights.

4. COMMENTARY

Unfortunately, while the question of what is a disposition sufficient to trigger preferential rights arises from time to time, this decision, as is so often the case, is very fact specific, in that the case turns on the use of the word "interest" within the parentheses, implying clarification rather than adding new obligations.

X. TAXATION

A. *MCLARTY V. CANADA*[126]

1. BACKGROUND

The purchasing and licensing of seismic data gives rise to unique issues relating to intellectual property rights and, in this case, rights to claim Canada Exploration Expense (CEE) under s. 66.1(6) of the *Income Tax Act*.[127] While the facts in this case are somewhat unique, as the rights arose under a joint venture financing, the discussion of when the acquisition of seismic data fulfills the purpose test for CEE has a broader application. The Court also had to consider what was required to establish that the vendor and purchaser were operating at arms length, and if they were not at arms length, how was fair market value to be determined.

2. FACTS

Ernie Sapieha, at that time the sole owner, officer, and director of Compton Resources Corporation (Compton), created a joint venture to purchase an interest in a seismic data library owned by Compton. Allan McLarty subscribed to purchase an interest in the seismic

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125 *De Beers* (C.A.), *supra* note 122 at para. 4.

126 2005 TCC 55, [2005] 1 C.T.C. 2875, [*McLarty* (T.C.C.)], rev'd 2006 FCA 152, [2006] 4 C.T.C. 16 [*McLarty* (F.C.A.)], leave to appeal to S.C.C. granted, 31516 (22 February 2007).

127 R.S.C. 1985, c. 1 (5th Supp.) [*ITA*].

data (the Data) by paying CDN$15,000 cash and delivering a promissory note for CDN$85,000 (the Note). The principle objectives of the offering were stated to be:

> (a) [t]he principle objectives of this offering are to provide subscribers with an opportunity to participate in the acquisition of, exploration for and development of Petroleum Rights while at the same time enabling investors to avail themselves of the income tax deductions and federal incentive programs which have been proposed to encourage petroleum and natural gas exploration developments; and
>
> (b) [t]he primary purpose of the purchase of the Technical Data Base will be to analyze the data with a view to determining development and exploration prospects of the Joint Venture and to assist with the identification of producing PNG Properties for the Joint Venture to purchase. However, after a review and analysis of the Technical Data Base, some portion of the data may be licensed or sold to the industry in a manner and under circumstances consistent with industry practice.[128]

The Note granted limited recourse security to Compton, with payment to be from the proceeds of the sale or licensing of the Data and allowed Compton to sell the seismic data or the interests in the joint venture properties if payment was not made. Compton set up an office and hired a geophysicist who reviewed the Data to determine whether an opportunity existed to develop oil and gas plays.

McLarty claimed Cumulative Canadian Exploration Expense (CCEE) for the two tax years following the acquisition for the full $100,000 and the Minister of National Revenue (MNR) disallowed these additions to McLarty's CCEE account. The Tax Court allowed McLarty's appeals in their entirety and the MNR appealed to the Federal Court of Appeal.

3. DECISION

The Court of Appeal had to address a number of issues as follows:

> 1. Did the respondent purchase the Data for the purpose of exploration for petroleum or natural gas as required in paragraph 66.1(6)(a) of the Act?
>
> 2. Did the Note constitute an expense as required by paragraph 66.1(6)(a) of the Act?
>
> 3. Was the respondent's purchase of an interest in the Data a non-arm's length transaction? If so, was the [Fair Market Value] of the Data in excess of the amount assumed by the Minister?[129]

In order to qualify as CEE under s. 66.1(6) of the *ITA*, an outlay must be an expense incurred and the expense must be for the purpose of determining the existence, location, extent, or quality of an accumulation of petroleum or natural gas in Canada. If seismic data is acquired simply for the purpose of licensing, it is inventory, and does not qualify for CEE. The Tax Court of Canada departed from the prior jurisprudence and found that since the respondent was an individual who had entered an agreement that stipulated that exploration for oil and gas would occur, it was unnecessary to look beyond his purpose in obtaining the

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[128] *McLarty* (T.C.C.), *supra* note 126 at para. 9.

[129] *McLarty* (F.C.A.), *supra* note 126 at para. 26.

Data. The Federal Court of Appeal found that this was not the correct approach, and that the Court must always examine either what was actually done or what was planned to be done with the seismic data.[130] However, since there had been actual use of the Data the test had been met.

The Court of Appeal went on to find that the Note was not a contingent liability on the basis that even if both the seismic data and the drilling program failed to generate revenues, the respondent was obliged to surrender property for the benefit of the noteholder.

As Compton had been agent for the purchasers and was the vendor and Sapieha was a "common mind … dictat[ing] the terms of the bargain on both sides of the transaction,"[131] the sale was not at arm's-length and therefore the burden fell on the respondent to refute the MNR's assumed fair market value of the respondent's interest in the Data. The Tax Court had not reached a conclusion on whether the transaction was at fair market value, which is a question of fact and therefore the matter was sent back to the Court to be heard by a different judge so the respondent could "discharge his burden to establish on a balance of probabilities that the FMV of his interest in the Data exceeded the Minister's appraisal of its value."[132]

4. COMMENTARY

By overturning the Tax Court's findings that the intention to use the seismic data for exploration was insufficient to establish the purchase to be eligible for inclusion in CCEE, the Federal Court of Appeal has reaffirmed the prior test requiring that the Court must always examine either what was actually done or what was planned to be done with the seismic data. Therefore, transactions where unrelated seismic data is included in a sale transaction should be reviewed with caution if there is no real connection between the seismic and the purchaser's land base. Leave to appeal and cross-appeal to the Supreme Court of Canada was granted on 22 February 2007.

XI. SOLICITOR-CLIENT PRIVILEGE AND CONFLICTS

A. *BLANK V. CANADA (MINISTER OF JUSTICE)*[133]

1. BACKGROUND

In this decision the Supreme Court of Canada addressed for the first time the distinction between "litigation privilege" and "solicitor-client privilege," providing guidelines to both distinguish between the two types of privilege and to define the duration of the litigation privilege.

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130 See *Global Communications Ltd. v. Canada*, [1999] 3 C.T.C. 537 (F.C.A.); *Gulf Canada Ltd. v. Canada*, [1992] 1 C.T.C. 183 (F.C.A.).

131 *McLarty* (F.C.A.), *supra* note 126 at para. 57.

132 *Ibid.* at para. 66.

133 2006 SCC 39, [2006] 2 S.C.R. 319.

2. FACTS

In 1995, the Crown laid 13 charges against the plaintiff, Blank, and a company, for regulatory offences. The charges were quashed and Blank, an unrepresented plaintiff, sued the government for fraud, conspiracy, perjury, and abuse of prosecutorial powers. Blank sought disclosure of documents, but his requests for information in the penal proceedings and under the *Access to Information Act*[134] were denied on various grounds, including solicitor-client privilege under s. 23 of the *ATIA*. The Court had to address whether there was a distinction between solicitor-client privilege and the litigation privilege, as only solicitor-client privilege was excluded under the *ATIA*.

3. DECISION

The Supreme Court found that while litigation privilege and solicitor-client privilege were related, and both were covered by the *ATIA*, there is a major distinction between them resulting in the litigation privilege being of a temporary duration while the solicitor-client privilege is not.

In making this distinction, the Court looked to the underlying basis for each type of privilege. Solicitor-client privilege is necessary to ensure that there is full, free, and frank disclosure between those who seek legal advice and those who provide that advice, without fear of that information being disclosed. A lawyer can only properly advocate for his or her client with all the facts which the client may only be prepared to provide on the basis that they will not be disclosed.

Litigation privilege on the other hand is based on the objective of ensuring the lawyer and client can prepare their case without the fear of premature disclosure. It is not premised only on the solicitor-client relationship, covering communications not necessarily directly to the lawyer. The Supreme Court found that there were three distinguishing features:

(1) Solicitor-client privilege only applies to communications between lawyer and client while the litigation privilege applies to a wider range of information and communications;

(2) Solicitor-client privilege applies to all communications between the solicitor and client regardless of whether litigation is involved; and

(3) Finally and most importantly, solicitor-client privilege is there to protect the interest of citizens to have full and ready access to legal advice so as to facilitate a relationship, while the litigation privilege is there to facilitate a process.[135]

As the purpose of litigation privilege is to create a "zone of privacy"[136] for the litigation process, once the litigation is resolved, the purpose of that privilege has ended.

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134 R.S.C. 1985, c. A-1 [*ATIA*].

135 *Supra* note 133 at para. 28.

136 *Ibid.* at para. 34.

The Court found that the litigation privilege may continue if it involves the same or related parties and the same or related sources or if it remains exempt by virtue of the legal advice privilege.

In addition, the Court found that the privilege applied to documents created for the "dominant" purpose of litigation, rather than the lesser test of "substantial purpose" or the more stringent test of "sole purpose."[137] Here the Court found that because the documents were prepared for the purpose of a criminal prosecution and as the current claim was a civil action, there was not a sufficient relationship to extend the privilege.

4. COMMENTARY

While the decision provides some very useful guidelines as to the application of litigation privilege and its expiry, it does leave open for further challenge the question of when there will be a sufficient connection between the two actions to have the privilege continue. It is somewhat difficult to see how much closer the matters can be without *res judicata* being at issue. Subsequent cases will be needed to provide the necessary clarification.

Of importance to lawyers and clients alike is the reinforcement that it is essential to have lawyers involved in the early stages of information gathering that may lead to litigation in order to ensure the continued privilege of documents and communications. It also reinforces the necessity for in-house counsel to make sure that their role is clearly that of solicitor and not a business role, a distinction sometimes open to challenge.[138]

B. *CELANESE CANADA INC. V. MURRAY DEMOLITION CORP.*[139]

1. BACKGROUND

The matter of solicitor-client privilege was once again before the Supreme Court of Canada, however this time documents potentially subject to solicitor-client privilege ended up in the hands of opposing counsel following a seizure of documents under an *Anton Piller* order (the Order).[140] The Court had to resolve the conflicting values between solicitor-client privilege and the right to select counsel of one's choice.

2. FACTS

The respondent, Celanese Canada Inc. (Celanese) sued Canadian Bearings Ltd. (Canadian Bearings) for alleged industrial espionage. In order to ensure documents were not destroyed prior to disclosure, Celanese sought and obtained an *Anton Piller* order (Order). The search was undertaken by an accounting firm and overseen by an independent lawyer. While Borden Ladner Gervais LLP (BLG), lawyers for Canadian Bearings were present for much of the search, time and volume did not permit a complete review and documents were copied

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137 *Ibid.* at para. 59.
138 See generally *ibid.*
139 2006 SCC 36, [2006] 2 S.C.R. 189.
140 See *Anton Piller KG v. Manufacturing Processes Ltd.*, [1976] 1 Ch. D. 55.

electronically without any review. No list of the documents was compiled, contrary to the Order. One disc containing documents identified as potentially being subject to privilege was sealed and initialled by BLG and the supervising lawyer. A lawyer from Cassels Brock and Blackwell LLP (CBB), without notice to BLG, downloaded the documents onto his computer and reviewed some, if not all the documents. A copy was also given to Kasowitz, Benson, Torres and Friedman LLP (Kasowitz), Celanese's U.S. counsel. After the disclosure was discovered, CBB and Kasowitz, rather than returning potentially privileged matters as requested, chose to delete such documents from their respective systems. Canadian Bearings then brought an application to disqualify CBB and Kasowitz from representing Celanese in the espionage action. Celanese claimed that they had a right to counsel of their choice.

3. DECISION

The Supreme Court of Canada found that:

> The conflict must be resolved, it seems to me, on the basis that no one has the right to be represented by counsel who has had access to relevant solicitor-client confidences in circumstances where such access ought to have been anticipated and, without great difficulty, avoided and where such counsel has failed to rebut the presumption of a resulting risk of prejudice to the party against whom the *Anton Piller* order was made.[141]

The Court then went on to set out guidelines for drafting and executing an *Anton Piller* order, finding that had the Order been correctly drafted, the search carefully supervised, and the lawyers requesting the search keeping the purpose of the Order in mind, namely to preserve the documents rather than rushing to exploit the opportunity, Celanese's rights would have been adequately protected and Canadian Bearing would have been entitled to retain counsel of their choice.

4. COMMENTARY

A review of this decision is a must for lawyers drafting *Anton Piller* orders, or for lawyers whose clients have been made subject to a search under such an order. However, it also serves as another reminder of the importance of solicitor-client privilege, and the need to preserve that privilege wherever possible.

C. *DE BEERS CANADA INC. V. SHORE GOLD INC.*[142]

1. BACKGROUND

This case was a preliminary application to the subsequent *De Beers Canada Inc. v. Shore Gold Inc.*[143] discussed in Part IX. Rights of First Refusal, above, and is another review of the duty of loyalty lawyers owe to their clients. Generally speaking, a lawyer may not represent one client whose interests are directly adverse to the immediate interests of another current

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141 *Supra* note 139 at para. 2.
142 2006 SKQB 101, [2006] 8 W.W.R. 124.
143 *Supra* note 122.

client. This is so, even if the two matters are unrelated. The exception to this rule is where both clients have consented to the lawyer acting in both capacities, after full disclosure, and preferably after both clients have obtained independent legal advice in this regard.

2. FACTS

In 1997, Mr. Scherman with Balfour Moss (Balfour) had been retained by an insurance company to represent Cameco Corporation (Cameco) on a wrongful death suit in respect of a mining incident. In February 2006, Scherman was retained by De Beers Canada Inc. (De Beers) in respect of the present matter. In the interim, De Beers had entered into a Joint Venture Agreement with Cameco for the exploration and development of certain diamond bearing mineral properties. In the present case, De Beers claims that Cameco breached the terms of the Joint Venture Agreement when it purported to sell to Shore Gold Inc., Cameco's voting rights under the Agreement. At no time did Scherman seek the consent of Cameco to act for De Beers in the present matter. Cameco only became aware that Scherman had been retained by De Beers when it was served a statement of claim for this action on 23 February 2006.

3. DECISION

Relying on the principles stated in *R. v. Neil*,[144] the Saskatchewan court found that Balfour must be removed as counsel for De Beers. The duty of loyalty to current clients includes a broad principle of avoidance of conflicts of interest. As noted by the Court in *Neil*:

> [I]t is the firm not just the individual lawyer, that owes a fiduciary duty to its clients, and a bright line is required. The bright line is provided by the general rule that a lawyer may not represent one client whose interests are directly adverse to the immediate interest of another current client — *even if the two mandates are unrelated* — unless both clients consent after receiving full disclosure (and preferably independent legal advice), and the lawyer reasonably believes that he or she is able to represent each client without adversely affecting the other.[145]

De Beers and Balfour argued that De Beers should be entitled to its choice of counsel, however, the court found that it was impossible to say that Cameco's entitlement to loyalty from Balfour did not outweigh De Beer's right to choice of counsel, having regard to the nature of the claim being made by De Beers.

4. COMMENTARY

The emphasis on the duty of loyalty in this decision, rather than the "avoidance of conflicts of interest,"[146] suggests that there may be an ongoing obligation on firms to take the necessary steps to ensure that they are acting in the best interests of their clients. It should be noted, however, that recent lower court decisions appear to shift the emphasis away from

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144 2002 SCC 70, [2002] 3 S.C.R. 631 [*Neil*].
145 *Ibid.* at para. 29 [emphasis in original].
146 *Ibid.* at para. 17.

the duty of loyalty. This may be due to the fact that placing such a positive obligation on firms is inconsistent with the business model of a law firm.

XII. DUTY TO CONSULT

A. *PLATINEX INC. V. KITCHENUHMAYKOOSIB INNINUWUG FIRST NATION*[147]

1. BACKGROUND

The source of the duty to consult is the Crown's obligations not to infringe on the rights of Aboriginal people in Canada. Those rights are derived from s. 35 of the *Constitution Act, 1982*.[148] In the context of resource development, the infringement does not arise from the project itself, but from the government's approval required in order to undertake the project. The scope of the duty will depend upon the strength of the right that is asserted and will be particular to the situation in question. In this regard, the primary question that needs to be addressed is as follows: "[W]hat is required to maintain the honour of the Crown and to effect reconciliation between the Crown and the Aboriginal peoples with respect to the interests at stake?"[149]

2. FACTS

In this case, Platinex Inc. (Platinex), a small exploration company sought an injunction preventing the Kitchenuhmaykoosib Inninuwug (the KI), an Aboriginal community, from obstructing or interfering with its access to certain mining claims and leases in the Big Trout Area, Ontario. The KI confronted Platinex in order to prevent the company from drilling on a property. Platinex contended that the confrontation was hostile and threatening, and included the blockade of a public road and damage to an airstrip. The KI claimed that their protest was peaceful. Platinex ultimately vacated the property and the KI dismantled the Platinex camp. Platinex sought injunctive relief as well as CDN$10 billion in damages (including loss of profits), the largest claim ever against a First Nation.

3. DECISION

The Court held, on the basis of the principle of the balance of convenience, that Platinex's motion for injunctive relief should be dismissed and issued an interim order preventing Platinex from conducting any further exploratory work on the property for a period of five months. With respect to the consultation process, the Court stated that the Crown is required to: (1) provide notice to the First Nation with full information about the proposed activity; (2) fully inform itself of the practices and views of the First Nation; and (3) undertake meaningful consultation with the First Nation.[150] In addition, the Crown must make good faith efforts to negotiate towards reconciliation. However, the Court noted that the duty to consult is not one-sided; First Nations must also make *bona fide* efforts to reach an

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147 (2006), 272 D.L.R. (4th) 727.
148 Being Schedule B to the *Canada Act 1982* (U.K.), 1982, c. 11.
149 *Haida Nation v. British Columbia (Minister of Forests)*, 2004 SCC 73, [2004] 3 S.C.R. 511 at para. 45.
150 *Supra* note 147 at para. 90.

agreement. In this case, the Court found that the Crown had not satisfied its duty to consult, and the Court exercised its discretion to relieve the KI from providing an undertaking for damages.

4. COMMENTARY

This case elaborates on what is required in order for consultation with Aboriginal peoples to be considered to be meaningful. While the duty to consult is that of the Crown, resource companies need to consider not only whether affected First Nations have been consulted, but whether the Crown has conducted such consultation in a meaningful fashion. Companies also need to take into account that the duty to consult can arise at various stages of a project. Project planning should factor in the Crown's duty to consult whenever federal, provincial, and municipal permits or approvals are required.

B. *DENE THA' FIRST NATION V. CANADA (MINISTER OF ENVIRONMENT)*[151]

1. BACKGROUND

Nine "core regulatory bodies"[152] commenced development of a "Cooperation Plan"[153] to coordinate regulatory and environmental efforts to construct the Mackenzie Gas Pipeline (MGP) in 2000. The pipeline would originate in Inuvik in the far north of the Northwest Territories and terminate 15 metres south of the Northwest Territories/Alberta border, where a proposed connecting pipeline would link it up with existing provincial pipelines for southern distribution. The focus of this judicial review is the alleged failure of the Government of Canada to meet its obligations towards affected First Nations, and specifically the Dene Tha' First Nation (Dene Tha'). The Dene Tha' is an Aboriginal group with approximately 2500 members and seven reserves. The Dene Tha' define their traditional territory as lying primarily in Alberta, but also extending into northeastern British Columbia and the southern Northwest Territories. While the pipeline does not run through a Dene Tha' reserve, it is a well-established principle that a reserve does not have to be affected in order to engage a Treaty 8 right.[154]

2. FACTS

The MGP project consists of seven major regulatory and environmental layers, one of which is the Cooperation Plan. The objective of the Cooperation Plan is to reduce duplication. To this end, the Cooperation Plan sets up a framework for the environmental and regulatory processes. This includes how these processes would be integrated, how joint hearings would be conducted, and the terms of reference for any future environmental assessment process. The Government of Canada did not consult the Dene Tha' in respect of the formulation of the Cooperation Plan. Rather, the Dene Tha' was engaged only by virtue of a single media release dated 3 June 2004 inviting public consultation on a draft

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151 2006 FC 1354, 25 C.E.L.R. (3d) 247.

152 *Ibid.* at para. 21.

153 *Ibid.* at para. 20.

154 *Mikisew Cree First Nation v. Canada (Minister of Heritage)*, 2005 SCC 69, [2005] 3 S.C.R. 388.

Environment Impact Terms of Reference and the Joint Review Panel Agreement, as well as a 24 hour deadline for the public to respond to those documents.

3. DECISION

The Court concluded that: (1) there was a duty to consult with the Dene Tha' even at this early stage of the MGP project; (2) that the duty arose at the design stage of the review process some time between 2000 and 2002; (3) that the duty was not met at this time because there was no consultation whatsoever concerning the review process; and (4) that the media release in 2004 regarding the draft Environment Impact Terms of Reference and Joint Review Panel Agreement could not be considered meaningful consultation.[155] According to the Court, the Cooperation Plan functioned as a blueprint for the entire project. While the Cooperation Plan by itself confers no rights, it sets up the means by which a whole process will be managed, a process in which the rights of the Dene Tha' will be affected. To preserve the current situation until the final remedy has been determined, the Court stayed the Joint Review Panel from considering any aspect of the MGP project which affects either treaty lands of the Dene Tha' or the aboriginal rights claimed by the Dene Tha'. The Court also decided to hold remedies hearings on a number of issues, including, (a) the role of the Court in supervising the consultation process, and (b) the role of various entitles, such as the Joint Review Panel and the National Energy Board, in the consultation process.

4. COMMENTARY

This case addresses the question of when the Crown's duty of consultation commences with Aboriginal peoples. The duty to consult may arise very early on, as early as the initial planning stages of a project. Accordingly, project proponents must consider the implications of the Crown's duty to consult at the first instance that the Crown is engaged.

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[155] *Supra* note 151 at paras. 98-110.