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What Happens When an Insolvent Energy Company Fails to Pay its Surface Rent to a Landowner? Part 2

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Cases Commented On: *PetroGlobe Inc v Lemke*, 2015 ABSRB 740; *Portas v PetroGlobe Inc*, 2015 ABSRB 708; *Rodin v PetroGlobe Inc*, 2015 ABSRB 737

This comment is an update to my July 2014 post What happens when an insolvent energy company fails to pay its surface rent to a landowner?. Readers are directed to this earlier comment for more background to this case and for this comment. In short, the matter involves the failure by PetroGlobe to pay its 2013 rent under a surface lease to the lessors Doug and Marg Lemke. The Lemkes filed an application with the Alberta Surface Rights Board ("Board") under section 36 of the *Surface Rights Act*, RSA 2000 c S-24 to recover the unpaid rent. PetroGlobe was assigned into bankruptcy in 2013 under the federal *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, and in its 2014 *Lemke* decision 2014 ABSRB 401 the Board ruled this federal legislation precludes the Board from proceeding with the Lemkes' section 36 application under the *Surface Rights Act*. In April 2015, then Premier Jim Prentice announced he was asking the Board to reconsider its 2014 *Lemke* decision. The Board subsequently struck a new panel to hear additional submissions, and earlier this month the Board rescinded 2014 ABSRB 401 and replaced it with 2015 ABSRB 740. This new ruling from the Board upholds its earlier decision not to proceed with the Lemkes' section 36 application, but does so with more reasons. This comment examines this new reasoning.

Where a landowner provides the Board with satisfactory evidence of non-payment of surface rent by a lessee, section 36 obligates the Board to demand payment from the energy company. Where the company fails to comply with this demand for payment, subsections (5) and (6) in section 36 provide the Board with the power to extinguish the company's surface access rights and direct the Minister to pay the landowner. As I explained in my July 2014 post, we might then summarize section 36 simply as holding that Albertans collectively guarantee that a landowner will receive their rent as compensation for having to endure the disruptions to their quiet enjoyment brought by the oil and gas industry (although the Board has stated in this new ruling that these subsections do not amount to a true guarantee). The following table sets out the number of section 36 applications received by the Board over the past decade and the amount of monies it has directed the Minister to pay over that time:

Year	Number of New section 36 applications received by the Surface Rights Board	Amount Directed to Pay pursuant to section 36(6) of the *Surface Rights Act*
2004	427	$776,979.95
2005	446	$837,446.06
2006	350	$553,942.47
2007	340	$580,209.76

2008	329	$489,806.50
2009	360	$729,945.36
2010	364	$656,558.31
2011	278	$592,533.23
2012	288	$579,753.85
2013	346	$683,736.27
2014	505	$722,063.49
2015 (9 months)	460	$1,081,067.82

*Source: Alberta Surface Rights Board

These numbers certainly suggest section 36 is an overworked provision, and that the failure by energy companies to pay their rent is not uncommon. Alberta taxpayers have paid out nearly $10 million to cover rent owed by the oil & gas industry to landowners over the past 10 years.

The Board's position remains that it is precluded from proceeding with the Lemkes' section 36 application (more later on why I've underlined this application specifically) because it runs afoul of provisions of the *Bankruptcy and Insolvency Act* which, generally speaking, state no proceeding outside of the federal bankruptcy and insolvency process may be commenced against a bankrupt, and that the doctrine of federal paramountcy means section 36 is inoperable for non-payment of rent by a bankrupt energy company. The Board rejected each of the following arguments put forward by the Lemkes in the review hearing:

- The Lemkes argued the *Surface Rights Act* is intended to provide landowners with a guarantee that the compensation payable for the surface rights given to an energy company will be paid. This assurance is in return for what is tantamount to the expropriation of the landowner's land.

The Board's response is that the literal terms of section 36 only empower the Board to direct the Minister to pay a landowner, and even then, only after the Board has directed the company to pay its debt and on its failure to do so the Board has terminated the company's rights under the lease. Thus section 36 does not provide a true guarantee for the landowner. A literal reading of section 36 certainly supports the Board's position here, although judicial interpretation – as noted in my July 2014 ABlawg – has suggested section 36 operates like a guarantee in an insolvency scenario even if the section itself doesn't expressly put it that way.

- The Lemkes argued a section 36 application is a claim by the landowner against the Alberta government, rather than an action or proceeding against the energy company. The section provides the landowner with a right to pursue payment from the Minister, and this right is independent of the bankruptcy of the company. The effect of a successful section 36 application is to place the Minister into the shoes of the landowner for the recovery of the unpaid rent under the lease. Moreover, the Board is not a creditor of the bankrupt company, and thus any action taken by the Board against the company is not an action or a proceeding outside of the federal regime for a claim provable in bankruptcy.

The Board's response is that the landowner's application under section 36 and subsequent demand by the Board for payment of rent under section 36(4) and/or the termination under section 36(5) of the company's surface rights does amount to a "proceeding" and that for rent owing prior to the petition into bankruptcy this proceeding is for "a claim provable in bankruptcy". The Board relies – unsatisfactorily in my view – on Black's Law Dictionary to give meaning to what is a 'proceeding' under the *Bankruptcy and Insolvency Act* and its finding that a section 36 application is thus a proceeding because it is a means for seeking redress from a tribunal or agency. In my view, the Board's reasoning seems to overlook the simple fact that the landowner is a creditor of the bankrupt and the landowner never commences any action against the bankrupt. This fact is lost in the Board's attempt to reason thru its position with statutory interpretation and references to case law interpreting the *Bankruptcy and Insolvency Act.* Indeed the Board itself acknowledges some of those cases are distinguishable from this case on the facts.

The foregoing is essentially the justification provided by the Board for denying the Lemkes' claim here for a second time.

What is already a convoluted set of reasons is arguably made worse by the Board's finding that it is not precluded from proceeding with a section 36 application for unpaid rent that accrues after an energy company goes bankrupt. In its September 2015 *Portas v PetroGlobe Inc*, 2015 ABSRB 708 decision the Board ruled that unpaid rent that accrued after PetroGlobe was assigned into bankruptcy was not a claim provable in bankruptcy under the *Bankruptcy and Insolvency Act* (at paras 11 – 17).

And then to take this matter even a step further toward the absurd, the Board has recently ruled in *Rodin v PetroGlobe Inc*, 2015 ABSRB 737 that while the Board is precluded from proceeding with a section 36 application for unpaid rent that accrued before an energy company goes bankrupt the Board is not precluded from directing the Minister to pay that prior amount where the landowner subsequently files a new section 36 application for unpaid rent owing by the bankrupt company that accrued after the assignment (as per *Portas*). The Board's position here being that the direction to the Minister for the prior unpaid rent is not against the bankrupt debtor – the difference from *Lemke* being that the demand for payment and termination of surface rights is attached to the unpaid rent that accrued after bankruptcy.

If you find the Board's reasoning across these cases hard to follow, I'm sure you are not alone. It seems the Lemkes may apply under section 36 to recover unpaid rent from PetroGlobe that accrued before it was assigned into bankruptcy, but that request will only be processed by the Board if it is attached to a further request for the recovery of unpaid rent that accrued after the company was assigned into bankruptcy. This is legal formalism at its worst.