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Whoever heard of such a thing? A Crown oil and gas lease an intangible form of personal property?

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Case considered:

Kasten Energy Inc v Shamrock Oil and Gas Ltd, 2013 ABQB 63

In this case Justice Lee granted Kasten's application to appoint a receiver\manager over all of the assets of Shamrock, including Shamrock's Crown oil and gas lease. Kasten was a secured creditor of Shamrock claiming under a general security agreement (GSA) over Shamrock's present and after acquired *personal* property. In the course of making his decision to appoint a receiver Justice Lee concluded that Shamrock's lease was an intangible form of personal property. Kasten brought its application for the appointment of a receiver\manager Kasten under section 13(2) of the *Judicature Act*, RSA 2000, c J-2 rather than under section 65(7) of the *Personal Property Security Act*, RSA 2000, c P-7 (*PPSA*).

The Facts

Shamrock held a Crown oil and gas lease on which there was a producing oil well. Shamrock had granted security to Kasten's predecessor in interest in the form of a GSA in relation to all its present and after acquired personal property, in order to secure an existing indebtedness. A meeting of Shamrock creditors in response to a Notice of Intention to Make a Proposal pursuant to the *Bankruptcy and Insolvency Act*, (*BIA*) RSC 1985, c B-3 resulted in Court approval (over Kasten's objections) of a proposal to allow Shamrock's parent company (Stout) to recover its capital investment after which net revenues would be paid 80% to secured creditors and 20% to unsecured creditors. Several months later Kasten issued a demand for payment along with a Notice of Intention to Enforce Security under section 244 of the *BIA*. Following that, Kasten brought this application for an Order appointing a Receiver and Manager of Shamrock's assets and undertaking under section 13(2) of the *Judicature Act* which provides as follows:

> An order in the nature of a mandamus or injunction may be granted or a receiver appointed by an interlocutory order of the Court in all cases in which it appears to the Court to be just or convenient that the order should be made, and the order may be made either unconditionally or on any terms and conditions the Court thinks just.

The Decision

Justice Donald Lee granted Kasten's application and appointed a receiver and manager of all of the current and future assets, undertakings and properties of Shamrock until Kasten and other creditors (secured and unsecured) are paid in full. The GSA under which Kasten claimed

authorized the appointment of a Receiver and thus it was not necessary for Kasten to show irreparable harm if a receiver were not appointed. The Order was restricted to preclude the Receiver\Manager from selling the property without further approval from the Court and the effect of the Order was postponed until April 1, 2013 to afford Shamrock the opportunity to succeed in its efforts to sell the property.

Commentary

This is the second case in recent years in which there are published reasons supporting the appointment of a receiver\manager of oil and gas assets, although the context of the two cases is very different: see *BG International Limited v Canadian Superior Energy Inc*, 2009 ABCA 127 and my post on that decision here. Both cases acknowledge that the decision to order the appointment of a receiver should not be lightly undertaken and any case dealing with the application of a statutory power as broad as section 13(2) of the *Judicature Act* is always going to be fact driven. What makes this case remarkable are Justice Lee's comments on the nature of a Crown oil and gas lease.

The balance of this comment reviews that part of Justice Lee's reasons and then offers some thoughts on what might have led Justice Lee down this particular garden path.

Justice Lee on Crown oil and gas leases

Drawing upon the reasoning in the Supreme Court of Canada's decision in *Saulnier v Royal Bank of Canada*, 2008 SCC 58 (a case dealing with a commercial fishing licence) Justice Lee held that Shamrock's Crown oil and gas lease "is a proprietary interest within the purposive contemplation of Alberta's *Personal Property Security Act*." And further "Shamrock's oil and gas lease is covered by the GSA and Alberta's PPSA in the category of 'intangibles' [defined as personal property other than goods, chattel paper, investment property, a document of title, an instrument and money." The reason for this seems to be that "during the term of the oil and gas lease/licence, Shamrock, the leaseholder has a beneficial interest to the earnings from its oil and gas lease ….".

With respect this must be wrong. A freehold oil and gas lease is a lease is a profit à prendre for an uncertain term (*Berkheiser v Berkheiser*, [1957] SCR 387) as is a Crown oil and gas lease in Alberta (*R v Industrial Coal and Minerals*, [1977] 4 WWR 35, rev'd on other grounds, [1979] 5 WWR 103 (Alta. App. Div)). And there is a good reason for this. The words of grant in the province's standard form petroleum and natural licences and leases grant a set of rights which perfectly match the elements of a profit: i.e. the right to go on to somebody else's property and win, work and remove a valuable resource. The Crown owns the corporeal estate (i.e. the oil and gas in place) and the lessee has an incorporeal right in relation to the oil and gas in place. Once severed from the ground, title to the oil and gas in place passes to the lessee as personal property. The lessee doesn't have a beneficial interest in the Crown's oil and gas in place because it doesn't need a beneficial interest – it has a legal profit à prendre.

Why this garden path?

One possible answer might well be that counsel led Justice Lee down this particular garden path. I infer this from the summary of Kasten's submissions reported at paragraph 17 to the effect that:

> The Applicant notes that Shamrock's argument on the issue of whether the GSA covers the oil and gas in the ground along with the right to extract the minerals distracts from the main issue of whether this Court should appoint a Receiver in the circumstances of this matter. Kasten argues that there is no doubt that a Crown oil-and-gas lease is a contract that contains a profit à prendre, which is an interest in land: *Amoco Canada Resources Ltd v Amax Petroleum of Canada Inc*, 1992 ABCA 93 at para 10, [1992] 4 WWR 499. Nevertheless, leases have a dual nature as both a conveyance and a commercial contract; and as such, are subject to normal commercial principles: *Highway Properties Ltd v Kelly, Douglas and Co Ltd*, [1971] SCR 562 at 576, [1972] 2 WWR 28. The contract is assignable and subject to seizure.

Thus, while counsel for Kasten acknowledges that a Crown lease is a profit he also wants to characterize it as a contract, relying, interestingly enough on a commercial lease case, the *Highway Properties* decision, which is not a case dealing with a profit. *Highway Properties* stands for the proposition that a lessor in a commercial lease can take the benefit of the contractual remedy of repudiation for an anticipatory breach where a tenant abandons the premises before the end of the term. It is no authority for the proposition that a lease is a form of personal property. Commercial leases still have to registered\caveated in the Land Titles Office and Crown petroleum and natural gas leases are registered with the Department of Energy.

But was it necessary for Justice Lee to shoehorn an oil and gas lease into the category of personal property in order to reach the conclusion that he had the authority to appoint a receiver\manager? Now I am not much of an insolvency lawyer but there is nothing in the language of the *Judicature Act* which suggests that this was necessary; and after all the Court appointed receiver will have to act in the interests of all the parties and will presumably be bound by the terms of the Court approved proposal. The fact that Kasten's security was confined to personal property might affect the willingness of the Court to approve a sale by the receiver\manager of property that was not subject to the security interest, but it is less clear that Justice Lee needs to conclude that Shamrock's principal asset is covered by the terms of the security instrument before acting on the terms of the *Judicature Act*. There was some discussion in the case that any decision to appoint a receiver\manager should take into account the "nature of the property," but the discussion of that point revolved (at para 22) around whether or not the receiver\manager would have the necessary expertise to operate the property. In sum, I don't think that Justice Lee needed to go down this particular garden path at all but I would certainly be interested in hearing from readers with more expertise in insolvency law and practice than I can claim.