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The Alberta Energy Regulator Enforces New Licensee Capability Assessment and Restricts License Eligibility of AlphaBow

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AER Administrative Sanction Commented On: [202207-13, AlphaBow Energy Ltd.](#)

The Alberta Energy Regulator (AER) issued [an administrative sanction](#) to AlphaBow Energy Ltd. on July 28, 2022. Two aspects of the sanction make this an interesting case rather than a routine enforcement action: first, the history of AlphaBow, and second, that the administrative sanction is the AER implementing their new approach to liability management, so the terms and the ultimate outcome of this administrative sanction are a decent indication of things to come.

For background, the AER has been gradually implementing their new Licensee Capability Assessment (LCA) approach to liability management for oil and gas companies. See the [previous post here](#) for a general discussion of the LCA system.

The Story of AlphaBow Energy Ltd.

AlphaBow Energy Ltd. (Company Code ‘A7H2’ in the AER’s [Integrated Application Registry](#)) went by the name ‘1994450 Alberta Inc.’ until sometime in 2017, and then ‘Sequoia Operating Corp.’ until June 1, 2018, when the name was changed to AlphaBow Energy Ltd. AlphaBow is one of the companies sold as part of the complex Perpetual-Kailas Capital-Sequoia chain of transactions in 2016, another of which is ‘Sequoia Resources Corp.’, which went bankrupt in March 2018, and resulted in ongoing litigation that I have written about before: [Part 1](#), [Part 2](#), [Part 3](#).

By late 2018, [journalists had identified AlphaBow as a company with troubled finances](#) and noted that the AER was allowing AlphaBow to purchase new oil and gas assets without putting down the security deposits that the AER’s rules required to ensure abandonment and reclamation obligations (ARO) were met.

Canadian Natural Resources Limited (CNRL) also worried about AlphaBow’s ability to pay for their ARO, because if AlphaBow orphaned their assets it would cause problems for CNRL down the line (CNRL pays a substantial portion of the orphan fund levy each year). CNRL submitted a statement of concern in an attempt to block the transfer of more wells to AlphaBow in 2018. The AER [declined to give CNRL a hearing](#), and among other things, wrote:

The AER notes CNRL’s concerns relate to the ability of the proposed transferee to address the end of life obligations associated with assets that are subject to the Application.

...

The AER understands that these policy concerns have already been raised by CNRL as part of the Government of Alberta's liability management review. The AER believes that is the appropriate mechanism for CNRL to raise its concerns. (at 2)

CNRL appears to have taken the AER's advice seriously and engaged with the liability management review, because the AER's refurbished liability management system is now stepping in to do what CNRL recommended back in 2018.

The Troubles of AlphaBow

The AER's letter to AlphaBow was posted without attachments, but it lists what the two attachments are:

Attachment 1: AlphaBow Energy Ltd. Compliance History and Current Noncompliances
Attachment 2: AlphaBow LCA

The AER declined to send me the attachments without a formal request under the *Freedom of Information and Protection of Privacy Act*, [RSA 2000, c F-25](#). So, although we do not have the details of the AlphaBow compliance history or their LCA (Licensee Capability Assessment) report, we can infer both are poor. AlphaBow is not consistently meeting their regulatory obligations for safety (as you can also see from searching 'AlphaBow' on the AER's [Compliance Dashboard](#)), and the AER considers Alphabow to be at an unreasonable risk of being unable to pay for abandonment and reclamation liabilities. The AER's letter says one reason for the administrative sanction is:

Outstanding debts owed for municipal taxes, surface lease payments, or public land disposition fees. In meetings with the Director held on May 19, 2022, and July 13, 2022, AlphaBow confirmed it owes municipal property taxes, surface lease rentals, freehold mineral royalties and Crown mineral royalties. (at 2)

AlphaBow is also facing legal troubles: AlphaBow is involved in ongoing litigation against the Trustee in Bankruptcy of Sequoia Resources Corp., [as the trustee filed a statement of claim against AlphaBow and the company's 2016 directors in July 2019](#). The Trustee takes the view (similar to the Trustee's position against Perpetual in their other litigation) that the directors of Kailas improperly transferred several million dollars of abandonment and reclamation liability to Sequoia Resources Corp. in a series of non-arm's length transactions from September 2016 to January 2017, prior to Sequoia Resources Corp entering bankruptcy and leaving those abandonment and reclamation responsibilities to the Orphan Well Association (OWA). AlphaBow was also sued in a [class action lawsuit for not paying their leases to landowners](#) in late 2020.

The AER's Administrative Sanctions

The AER's order sets restrictions on AlphaBow's eligibility to hold licenses. The important restriction is that "AlphaBow is prohibited from acquiring new well or facility licences, through either transfers or applications" (at 2). This is an interesting regulatory approach, and it blocks AlphaBow from employing a strategy used by failing oil companies to prolong their fall. Failing

oil companies will sometimes accept assets nearing their end of life from other companies for payments that they use to continue to operate the business, but this strategy ultimately leaves more unpaid abandonment and reclamation liabilities behind for the OWA. If companies are allowed to limp along by buying more assets with rapidly declining reserves, they ultimately end up leaving even more ARO to the OWA.

The other condition is that “AlphaBow is prohibited from transferring licences from its current inventory without AER approval” (at 2) but this condition means nothing in particular. Pursuant to section 24 of the *Oil and Gas Conservation Act*, [RSA 2000, c O-6](#), section 18 of the *Pipeline Act*, [RSA 2000, c P-15](#), and Part 2 of the *Responsible Energy Development Act*, [SA 2012, c R-17.3](#) no company can ever transfer licenses from their inventory without AER approval. Presumably, the AER means that special attention will be paid to ensure AlphaBow does not transfer any valuable assets to other companies at undervalue.

These are rational initial approaches for the AER to take towards an oil and gas company having difficulty paying creditors. The AER has issued these kinds of administrative sanctions before, but typically after the licensee entered bankruptcy or the licensee stopped responding to AER inquiries for an extended period of time. The weakness with this regulatory approach is that it only stops oil and gas assets moving in or out of the company, so it is only effective if it is triggered early enough that the company has the assets and cashflow to pay for their ARO.

Albertans interested in what the new LCA means in practice should watch how this administrative sanction is enforced and what results it brings. The first thing to watch for is whether the new LCA approach is effective in preventing AlphaBow from leaving substantial unsecured ARO costs to the OWA.

The second thing to watch for is whether AlphaBow is granted exceptions to the license restrictions. A problem with the LCA is that it is entirely non-transparent and leaves wide discretion to the AER, just like the Licensee Liability Rating (LLR) system that preceded the LCA. One of the many reasons the LLR system failed was the AER often permitted transfers of assets to take place, even though the transfer fell below what the LLR rules supposedly required when a financially weak company threatened to enter bankruptcy unless the AER provided ‘regulatory flexibility’, usually a euphemism for ‘special favours’.

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