# THE NEGOTIATOR

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**2012 Merit Awards**

Recognizing the Backbone of CAPL: Volunteerism

**Limitations on Lawsuits for Non-Payment of GORS:**

A Case Study

**Alberta Energy**

Tenure Branch Announcement

# The Curious Case of *Jensen*

## Limitation of Actions; and GORs on Successor Title Documents

I DON'T LIKE TO WRITE ABOUT LIMITATIONS OF ACTION ISSUES. Limitations is a goofy area of law that is full of odd twists and very fact specific issues. Tough to read too much into a particular case.

However, the recent Alberta Court of Queen's Bench decision in *Canadian Natural Resources Ltd. v. Jensen Resources Ltd.* [2012] A.J. No. 1387 bugged me enough that you now get to hear my very special rant on this topic.

*Jensen* bugs me because of the way the case deals with the application of either a 2 or 10 year limitation period in a lawsuit claiming damages for non-payment of an overriding royalty (GOR). Spoiler alert, the Court found that a sophisticated landman, working in the oil patch, was entitled to the softie 10 year limitation period and not the more strict 2 year period.

Apart from the limitations issue, *Jensen* is a fascinating case in that the core issue involves the overlap of contract law (the GOR Agreement) and tenure law (the Crown PNG Lease and "successor" oil sands lease). The Court was asked to determine if the GOR applied to an oil sands lease (OSL) which was not the PNG Lease described in the GOR Agreement. Understanding the interplay between land contracts and title documents is a fundamental landman concept that I am always happy to chat about.

### Facts

The GOR was originally granted by Kissinger Petroleum Ltd. The grantees were, I believe, a group of employees under a royalty pool program administered by Kissinger. Jensen is the successor to one such employee and is entitled to a net 0.25% GOR under the GOR Agreement. The royalty payor is Kissinger, who becomes Ranger, then Petrovera and ultimately CNRL. This is the contract part of the equation.

The title document part involves a 3 section PNG Lease subject to the GOR. All is good until the Crown "steals" (pardon my French) back petroleum in the Mannville from the PNG Lease pursuant to Oil Sand Area Order 3. Ranger (CNRL) follows the procedure under AENR Information Letter 84-15 and applies for a "substitute oil sands agreement" for the oil sands rights carved out of the old PNG Lease. For one section, the Crown offered an OSL. For the other 2 sections, the Crown offered an oil sands prospecting permit (OSPP) with specific work requirements (i.e. fresh consideration) payable by Ranger. Ranger agrees and acquires the new OSL and OSPP. The OSPP eventually becomes another OSL.

CNRL paid royalties on one section of the OSL, but not the other two. This matter came to the attention of Jensen in 2007 who "happened to be working for CNRL at the time". Surprisingly, Jensen wanted a royalty on all three sections. He sued in 2009. He was a very senior landman, had the GOR Agreement in his possession, had Accumap, and worked at CNRL since 2003.

## Limitation of Actions Generally

Here is my rant – apparently in the modern world we no longer need to wear "big boy pants", especially when dealing with the Courts. The world is, I guess, all about love and fairness, no ones feelings should ever be hurt, and God forbid we ever make someone responsible for keeping track of their own stuff. The problem with love and fairness is that it reduces certainty. No way around it. In my humble view, certainty is what makes the business world work efficiently. Love and fairness is great in church, not so great in the boardroom. Holy cow, am I starting to sound like my old man. I used to be cool, I think. Can't recall anymore due to my constant aches and pains and generally crabby mood all the time.

Now a bit of background. Years ago, provincial governments, to their credit, started to tighten up limitation rules to provide for a general two year limitation to start a lawsuit, or your claim was statute barred. The idea was to create certainty in business and commerce and provide a short but reasonable limit on the right of companies (and individuals) to sue each other for past claims. Most provinces revamped their statutes in a similar fashion. This was done because of a whack of older Court cases that constantly skirted or ignored limitations rules to increase love and fairness.

Lastly, one quick note. Actions for the non-payment of reoccurring payments are deemed at law to arise on a monthly basis. Therefore, a limitation of action defense does not bar the entire claim, simply the monthly claim that falls past the limitation period. That is to say, each month is considered a separate breach and is a separate claim. This is very important to remember in all accounting type actions for miscalculation or non-payment of monthly calculated amounts. This category includes all GOR and LOR payments and compensatory royalty payments under freehold leases.

## The Limitations Act

The Court cites the applicable section of the *Alberta Limitations Act* as follows:

> [58] Section 3(1) of the Limitations Act codified and refined the common law discoverability rule which provided that a cause of action arose for the purposes of a limitation period when the claimant discovered, or ought to have discovered by the exercise of reasonable diligence, the material facts upon which the claim is based. Section 3(1) states:
>
> 3(1) Subject to section 11, if a claimant does not seek a remedial order within
>
> (a) *2 years after the date on which the claimant first knew, or in the circumstance ought to have known,*
>
> (i) that the injury for which the claimant seeks a remedial order had occurred,
>
> (ii) that the injury was attributable to the conduct of the defendant, and
>
> (iii) that the injury, assuming liability on the part of the defendant, warrants bring a proceeding, *or*
>
> *(b) within 10 years after the claim arose.*
>
> whichever period expires first, the defendant, on pleading this Act as a defence, is entitled to immunity from liability in respect of the claim.

## Knew, Or in the Circumstances Ought to Have Known

Hence, the issue is simple:

- If Jensen "knew, or in the circumstances ought to have known" that its GOR might apply to the OSL, the limitation is two years.
- If not, he gets 10 years to sue.

Seems like a pretty simple answer for a guy like me who likes to rant about certainly. To my way of thinking, Jensen is a pretty knowledgeable dude. In the circumstances, he ought to have known that the whack of bitumen wells under the two section OSL covering the same areal lands as his GOR Agreement might be subject to his royalty. His job is to keep track of his stuff. Remember, he was being paid royalties on the other one section OSL, was a 30-year landman, working at CNRL, with Accumap, had a working knowledge of CNRL's oil sands operations, and a copy of the GOR Agreement.

But what do I know. The Court instead finds that the 10 year limitation applies:

> [69] I find that the Section 3(1)(a) of the Limitations Act does not preclude Jensen from proceeding with its claim against CNRL for failure to pay royalties on the Sections 1 and 4 OSL. Jensen's application was commenced on September 18, 2009. To the extent that any royalties are payable, they would be subject to the 10 year limitation period contemplated in section 3(1)(b) of the Limitations Act.

The Court had to do a bit of dancing to get to love and fairness. There are competing streams of logic in limitations cases. The strongest big boy language comes from the Alberta Court of Appeal in *Luscar Ltd v Pembina Resources Ltd.* (1994), 162 AR 35 (CA), where the Court states:

> ... *it is the responsibility of a party to monitor its own contract,* and put into force such mechanisms as may be required to aid it in identification of breaches, if it feels such mechanisms are necessary. If not, then it is the risk of the party whose mechanisms are not sufficient [as quoted in paragraph 65 of *Jensen*]

Love it. This is how I am trying to raise my boys. Take care of your own stuff. The world does not owe you a living. Everything is not someone else's problem.

However, the Court instead follows the Court of Appeal decision in *Meek (Trustee of) v San Juan Resources Inc.*, 2005 ABCA 448, 376 AR 202 and adopts the following rational for allowing a 10 year limitation:

> Royalty interest holders often do not have ready access to the documentation that would enable them to determine if there is production from a particular well and whether they have been paid the royalty owing on that production. A *royalty interest holder is entitled to expect the royalty payor to honour its obligations. Absent clear information to show improper payment, royalty interest holders are not obliged to take positive steps aimed at ensuring that they are being correctly paid.* Although Imperial's new reporting procedures in 2000 made it easy to know what wells were the subject of royalty payments, Carrington did not have up-to-date information from the AEUB that would indicate what wells were in production. In other words, she did not simultaneously have the information that would enable her to put together the two critical pieces of the royalty puzzle. Nor was she obliged to procure the AEUB reports. (emphasis added [in the *Jensen* decision])

I understand this view. Little old ladies who barely know why they are getting cheques from the nice oil company do not need to wear big boy pants. In fact, they might wear Depends brand underpants, but I digress. Courts can and should give the vulnerable lots of slack. A 10 year limitation for these folks is great.

However, there must be a limit to whom we consider to be the innocent that require the benevolent protection of the Court and a 10 year limitation. The 2 year limitation must have some meaning or application or why bother putting it in the Act.

For me, the problem is that the Court found that a seasoned landman dealing with an issue within his area of expertise falls within the class of vulnerable individuals that are not obligated to take positive steps to ensure they are being correctly paid. If Jensen falls in this group, I have great difficulty imagining any person, or even any corporate entity, that would be subject to a 2 year limitation. Pretty much everyone now falls within a 10 year limitation.

## A Note of Courtesy and Caution

Don't get me wrong. I don't blame Jensen for making this claim. I have been told by several landmen I know and really respect, that Jensen is a first class landman and person. FYI, "Jensen" is not his actual name, but rather the name of his holding company that owns the GOR. His actual name is not important to the case. I don't like the way the Court is treating the limitation issue, but I fully understand why someone would make this claim. Heck, that is the whole point of having fancy pants litigation lawyers.

Also, as far as I can tell, this case is on appeal, so this may not be the last word on this issue. Actually, there never is a last word for limitations issues. They just seem to go on and on and on. Too bad we couldn't just fix the statute and have a straight up time limit on all lawsuits. Oh wait, I forgot, it's not fair, and so it will never happen.

## Go Forward Application

A 10 year limitation on unpaid (or incorrectly paid) obligations under contracts, and especially freehold leases, means that many, many more claims become worth the time and effort to pursue in Court.

Of particular concern for me is the compensatory royalty payable under freehold leases for missed offset obligations. If these claims now have a 10 year limitation, we are much less likely to settle amiably and avoid the legal costs and aggravation associated with such claims. A lot more lessees are getting nasty letters demanding compensatory royalty payments for old offset wells. Generally, the parties can agree on a maximum 2 to 3 year look back for unpaid amounts. This was due to the general view that a 2 year limitation might apply and the parties should share the risk. Nice way to settle the matter and move on. Now, with a 10 year look back being more likely for non-corporate lessors (and perhaps even corporate lessors), I expect lessors will be demanding a full 10 year look back. This means the amounts will be larger and the issues likely more complex (assuming a couple of A&D deals along the way). This may result in lessees simply saying the heck with it, for that amount of money, let's have a trial. More fairness, less certainly. Really just means more lawsuits. Yuck.

## Lease Executed "In Lieu Thereof"

Now a very quick word on the fascinating tenure part of the case. The GOR applied to the PNG Lease, but should it apply to the "successor" OSLs? Without any facts, I would have said no way. However, once you are aware of the facts, the decision is pretty reasonable.

As the Court states, it really comes down to the meaning of "in lieu of" under the GOR Agreement:

> [26] The language used in each of the GOR Agreements provides that the GOR "shall attach to and encumber the Petroleum and Natural Gas Lease above described, *and any renewals or extensions thereof, or any new leases which may be executed in lieu thereof.*" As a result, oil produced by CNRL from the Oil Sands Leases that relate to Sections 1, 4 and 32 will be subject to Jensen's GOR if the Oil Sands Leases qualify as leases "executed in lieu thereof" for the PNG Leases on those sections which were subject to the GOR. (emphasis mine)

Using a dictionary, the Court and the parties agreed that "in lieu of" means "instead of" or "in place of". Due to the very unique circumstances of the OSL being issued to the same party through Information Letter 84-15, it could reasonably be said that they were issued in place of the PNG Lease. I am less sure about the two section OSPP which required a fresh work requirement by Ranger. This seems more like a new lease and not a lease issued in lieu of. But this is a minor quibble.

## Go Forward Application

Well, anyone with old terminated GOR files under OSLs, better be having a wee look at how they acquired the OSLs. If it was a private grant under IL 85-15, you might have a big problem. Especially considering a 10 year limitation period and the volume of production you can get from a section of bitumen wells.

More generally, this case joins a few others that deal with the issue of how far GOR holders' rights can extend beyond the existing title document. Sometimes the issue turns on language such as "renewals or extensions" or "successor title documents". Sometimes the cases deal with the failure to provide the GOR holder with notice of "expiry" of the title document.

GOR holders, especially geologists, tend to believe that their GOR applies to "the lands" or "the play" and expect to be paid no matter what happens to the leases at the time the GOR Agreement was entered into. This is almost never the case.

Generally, a GOR attaches to the existing title documents and a very narrow range of title documents issued in "substitution for" or in "lieu of" the existing lease. Disputes tend to arise where you have:

- Crown deep right reversion;
- Crown lease expiry; or
- Freehold Lease expiry or termination;

and then the *same company* acquires the same rights and does not recognize the GOR on the new title document.

These cases are very fact specific. If you acted in good faith and acquired the new rights above board in either a public posting (for Crown rights) or a normal course leasing program with a fresh bonus (for freehold rights), you are usually fine. You are under no obligation to drill a well or continue a lease under almost all GOR Agreements. If your rights go down, the GOR goes down.

However, as *Jensen* shows, very specific facts can lead to a Court finding the new title document was issued "in lieu of" the old document.

Special consideration must be given to cases where you are fixing or "replacing" questionable freehold leases to deal with possible termination issues. Lease termination is sometimes uncertain and it becomes fuzzy as to whether your fix of obtaining a new lease means the old GOR falls away. Likely does, but these situations are much closer to the type of facts that a Court might use to find a way for the GOR to apply to "replacement" title documents.

*Paul Negenman*
*Lawson Lundell*