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Alberta Don't You Treat Me Unkind – Gonna Change My Way of Thinking

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In 2017, the Alberta Court of Appeal upheld the lower court's decision that the BIA (Bankruptcy and Insolvency Act) prevailed over a conflicting provision in the provincial regulations promulgated by the Alberta Energy Regulator (AER). In our blog posts about the appellate ruling and the lower court's decision, we announced that the decision was a boon for Canadian oil and gas lenders, but our optimism was tempered by an *asterisk* because the issue might not be settled "until the Canadian Supremes ultimately sing."

We were right to "feel a change comin' on" because, in this case, "there's only one authority and that's the authority on high" (the Supreme Court of Canada). On January 31, 2019, the Canadian Supremes sang with the conciseness of Dylan. The Court's decision in Orphan Well Association closes the curtain on the final act, placing the liability on the bankruptcy estate of Alberta's Redwater Energy Corporation ("Redwater") for the decommissioning and cleanup of abandoned drilling sites.

The core issue on consideration was whether section 14.06(4) of the Canadian Bankruptcy and Insolvency Act ("BIA"), permitting the trustee to disclaim abandoned wells to protect itself from personal liability, conflicted with AER provincial regulations imposing environmental liabilities on the estate in connection with such assets. Unlike the courts below, the Court found no conflict existed between the BIA's priority scheme and limitation of the court-appointed trustee's *personal* liability from public obligations of the bankrupt *estate* under provincial law.

AER sought to enforce provincial regulations requiring Redwater to pay remediation liabilities associated with abandoned wells to prevent the public from shouldering the costs. In so doing, AER acted in its *bona fide* regulatory capacity and "not [as] a creditor of the . . . corporation." Redwater's environmental obligations were a public "duty" and not dischargeable as claims under the BIA. Accordingly, such duties lie outside the BIA's priority scheme and have no effect on trustee protections. Although the trustee could not be held personally liable for such expenses under the BIA, such regulatory obligations must be satisfied from the estate before distributions to creditors.

"After so much oppression," AER finally prevailed. The "authority on high" "changed its way of thinking" and made "a different set of rules." Contrary to the prior decisions of the lower courts, the final Redwater decision makes clear that the liability for managing and remediating abandoned wells remains with the insolvent enterprise and, effectively, its secured lenders. The Court cautioned that

“[b]ankruptcy is not a license to ignore rules, and insolvency professionals are bound by and must comply with valid provincial laws during bankruptcy.”

Accordingly, lenders currently secured by Canadian O&G assets should take into account any provincial environmental liabilities in calculating asset value. Moreover, potential secured lenders documenting new facilities should consider regulatory obligations when drafting asset coverage ratios and other collateral- or reserve-based covenants and requirements. Finally, given the Supreme Court made it clear that the regulatory requirements did not force Redwater to satisfy obligations with assets unrelated to the “end-of-life obligations,” debtors and creditors may consider structures that would ring-fence unrelated assets from such liabilities, either retrospectively or prospectively.

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