

# CLEAN SLATE, CONTAMINATED LAND:

The “untidy intersection” of Insolvency  
and the Polluter Pays Principle  
and  
Recommended reforms to the  
*Bankruptcy and Insolvency Act* and  
the *Companies’ Creditors Arrangement Act*

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The Environmental Law Centre (ELC) has been seeking strong and effective environmental laws since it was founded in 1982. The ELC is dedicated to providing credible, comprehensive and objective legal information regarding natural resources, energy and environmental law, policy and regulation in the Province of Alberta. The ELC's mission is to educate and champion for strong laws and rights so all Albertans can enjoy clean water, clean air and a healthy environment. Our vision is a society where laws secure an environment that sustains current and future generations.

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Any error or omissions in this report are that of the author alone.



## EXECUTIVE SUMMARY

Canada's bankruptcy laws are aimed at two purposes: creating a clean slate for individuals who go through bankruptcy, and facilitating an equitable distribution of assets to creditors. These policy purposes are reflected in the federal *Bankruptcy and Insolvency Act* (BIA). Some insolvent firms may also restructure their debts and divest property under the *Companies' Creditor Arrangement Act* (CCAA). Prior to the 1990s these pieces of federal legislation had little to say about environmental protection and how the polluter pays principle may be reflected in insolvency proceedings. Fast forward to 2019 and the impacts of insolvency on how our environment is remediated and reclaimed was front and centre in the decision of the Supreme Court of Canada (SCC) in *Orphan Well Association v. Grant Thornton Ltd.*<sup>1</sup>

*Clean Slate, Contaminated Land* reviews the context of insolvency law and how it intersects, often untidily, with public obligations to protect and remediate the environment. The question is asked, when a polluter is no longer able to pay, who should pay to ensure that pollution is cleaned up and land is reclaimed?

A brief review of the constitutional interface of insolvency legislation and environmental protection is provided, the jurisprudence in this area is highlighted, and reforms to the BIA and CCAA are recommended.

In an effort to tidy this intersection of federal and provincial law, the ELC recommends codifying commitments in federal insolvency legislation to remedy environmental damages and restoring the environmental condition of land (and in large part codifying and evolving the approach taken by the SCC). The proposed approach adopts a "beneficiary pays" principle; reflecting an extension of the polluter pays principle. This extension of liability beyond the polluter reflects a clear policy choice that signals that investment decisions and related benefits should be accompanied by analysis, consideration and clear inclusion of known and potential environmental obligations throughout the life span of activities.

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<sup>1</sup> 2019 SCC 5, online: Supreme Court of Canada <https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/17474/index.do>.

The proposed reforms include:

1. Reform to clarify when and how a public duty should be characterized as a provable claim by way of a declaration process from provincial and territorial regulators; and
2. Clarifying when and how an insolvent estate may disclaim or abandon property.

The ELC also recommends reforms to the CCAA to ensure financial security is obtained prior to any court sanctioned compromise or agreement in relation to outstanding environmental obligations and proposes provisions that allow for the continuance of claims past the discharge of an individual bankrupt in instances where they are liable for remedying the environmental damage or condition of property.

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# Introduction

*Had Parliament intended to empower trustees to walk away entirely from assets subject to environmental liabilities, it could easily have said so.*

Justice Wagner for the majority of the  
Supreme Court of Canada in  
*Orphan Well Association v. Grant Thornton Ltd.*<sup>1</sup>

Insolvency may be driven by a variety of market and operational factors: resources run out, prices drop, stiff competition, inefficiency. When money starts running out, creditors come calling and the state of the environment left behind is often not top of mind. Our laws - pre, during, and post insolvency - all contribute to the challenges of managing impacts on the environment through the entire life of an activity. The risk of undermining environmental policy outcomes is highest when the physical and financial resources related to an activity are depleted. As firms enter federal bankruptcy or restructuring proceedings the conflicts between economic and environmental policy escalate: arguments of competitiveness and efficiency face off against the principle that a polluter should be held responsible to clean up their mess.

Repeatedly throughout history this conflict in dueling policy outcomes has resulted in the public purse picking up the tab for environmental clean-up, if the environment is cleaned up at all. Some of the starkest examples are historic mines that went bankrupt and are now part of the federal contaminated sites inventory.<sup>2</sup>

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<sup>1</sup> 2019 SCC 5, online: Supreme Court of Canada <https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/17474/index.do> at para 86 [hereinafter *Redwater*].

<sup>2</sup> See Arn Keeling and John Sandlos "Ghost Towns and Zombie Mines: the Historical Dimensions of Mine Abandonment, Reclamation, and Redevelopment in the Canadian North" in *Ice Blink: Navigating Northern Environmental History* (Stephen Bocking and Brad Martin (eds.)) (Calgary: University of Calgary 2017) pp.377-420, online: Memorial University libraries [https://research.library.mun.ca/12618/1/Ghost\\_towns\\_and\\_zombie\\_mines.pdf](https://research.library.mun.ca/12618/1/Ghost_towns_and_zombie_mines.pdf).



The Giant Mine in the Northwest Territories went bankrupt in 1999 (and operated until 2004), with remediation costs now reaching \$400 million.<sup>3</sup> Financial obligations for the site are expected to continue in perpetuity.<sup>4</sup> However, financial security collected on the Giant Mine site was reported at \$400,000 for Royal Oak Mines and \$7 million from Miramar.<sup>5</sup>

The Faro mine, in the Yukon, went bankrupt in 1998 with remediation costs over \$317 million.<sup>6</sup> The financial security taken for the mine was \$14 million.<sup>7</sup> These mines were decades old and were started when financial security took a third seat behind attracting investment and job creation, when the environment was a casualty of doing business.

Potential liabilities for oil and gas reclamation and abandonment in Alberta in 2018 were estimated at \$58.65 billion according to the Alberta Energy Regulator (AER). If one considers a worst-case scenario though, this number climbs to in excess of \$200 billion (for both conventional and unconventional resource extraction).<sup>8</sup> For

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<sup>3</sup>Treasury Board of Canada Secretariat, Federal Contaminated Sites Inventory, Site C1048001 - Giant Mine (Giant Yellowknife Mines; Royal Oak Mines; A, B & C Shafts ), online: <https://www.tbs-sct.gc.ca/fcsi-rscf/fsi-isf/C1048001-eng.aspx?qid=58749>.

<sup>4</sup>*Ibid.*

<sup>5</sup>Commissioner of the Environment and Sustainable Development, 2002 October Report of the Commissioner of the Environment and Sustainable Development (Office of the Auditor General of Canada, 2002), at Chapter 3.

<sup>6</sup>Treasury Board of Canada Secretariat, Federal Contaminated Sites Inventory, Site C2503001 – Faro Mine, online: <https://www.tbs-sct.gc.ca/fcsi-rscf/fsi-isf/C2503001-eng.aspx?qid=58750>.

<sup>7</sup>Commissioner of the Environment and Sustainable Development, 2002 October Report of the Commissioner of the Environment and Sustainable Development (Office of the Auditor General of Canada, 2002), at Chapter 3.

<sup>8</sup>Alberta Energy Regulator, <https://aer.ca/providing-information/news-and-resources/news-and-announcements/news-releases/public-statement-2018-11-01>. For other estimates and discussion of this issue see CD. Howe Institute Commentary No. 492. *All's Well that Ends Well: Addressing End-of-Life Liabilities for Oil and Gas Wells*, online: [https://www.cdhowe.org/sites/default/files/attachments/research\\_papers/mixed/Commentary\\_%20492\\_0.pdf](https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_%20492_0.pdf) where the number of wells of “insolvent or close to insolvent firms” were identified as 49,987 to be abandoned and 15,492 to be reclaimed, representing a cost of between \$4-8 billion dollars.

conventional oil and gas operations environmental cost estimates are difficult to clearly assess as each well will have its own abandonment, remediation, and reclamation challenges (with some wells reaching into the millions of dollars where contamination of soil and water must be remediated).

As of March 31, 2017 the Orphan Well Association (OWA) had spent in excess of \$248 million in Alberta on abandonment and reclamation/remediation, representing a debt owned by the defunct companies to OWA.<sup>9</sup> Of that debt, ~ \$4 million was recovered for the 2017 year.<sup>10</sup> The number of wells being transferred to the OWA in recent years has continued to escalate significantly.

In 2018 the OWA received \$149.5 million in funding, with \$100 million being part of a \$235 million loan from the Government of Alberta, with interest being covered by \$30 million from the federal government.<sup>11</sup> The expenditures in 2018 and the inventory of wells is set out in Figures 1-3 below.

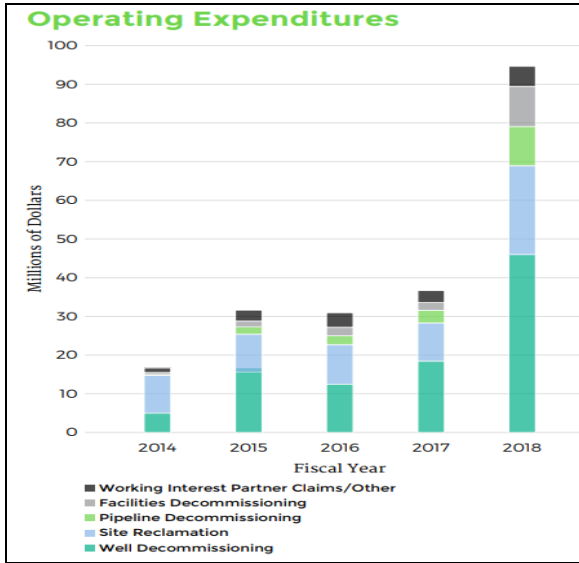
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<sup>9</sup> See Orphan Well Association, "List of Defunct Companies by company" [http://www.orphanwell.ca/?page\\_id=124](http://www.orphanwell.ca/?page_id=124).

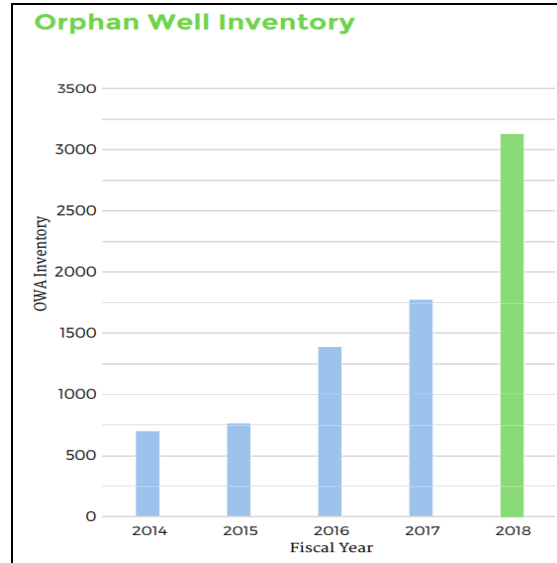
<sup>10</sup> OWA Annual Report – 2017-2018. At 24 <http://www.orphanwell.ca/wp-content/uploads/2018/10/OWA-2017-18-Ann-Rpt-Final.pdf>.

<sup>11</sup> OWA Annual Report – 2018-2019 at 6, online: <http://www.orphanwell.ca/wp-content/uploads/2019/07/OWA-2018-19-Ann-Rpt-Final.pdf>.

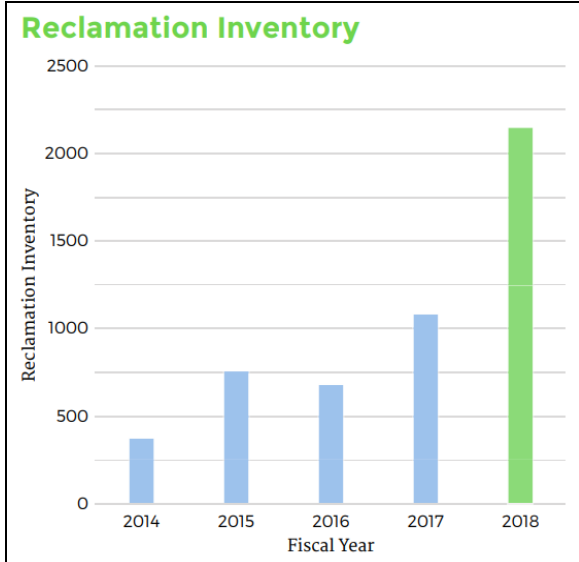
**Figure 1: OWA expenditures year over year (Source: Orphan Well Association).<sup>12</sup>**



**Figure 2: Orphan well inventory of the OWA (Source: Orphan Well Association, 2019<sup>13</sup>)**



**Figure 3: Orphan reclamation inventory of the OWA (Source: Orphan Well Association, 2019<sup>14</sup>)**



<sup>12</sup> Orphan Well Association, Annual Report 2018, online: <http://www.orphanwell.ca/wp-content/uploads/2018/10/OWA-2017-18-Ann-Rpt-Final.pdf>.

<sup>13</sup> *Ibid.* at 8.

<sup>14</sup> *Ibid.* at 8.

A clear tension exists between applying an effective and timely polluter pays principle in regulation and the financial and operational goals and objectives of firms. Operationalizing a strong version of the polluter pays principle in law requires a regulatory system that ensures the polluter bears the costs of pollution, whether through pollution avoidance and abatement technology or through cleaning up and addressing harm resulting from pollution.<sup>15</sup> (For a discussion of the principle see the ELC's publication, *The Polluter Pays Principle in Alberta Law*).<sup>16</sup>

Firms, on the other hand, will seek to generate revenue while minimizing expenses related to their operations, including those costs with complying with the polluter pays principle. Where government implements regulatory approaches that fail to safeguard against pollution or allow for the deferral of meeting environmental obligations, the potential of upsetting the polluter pays systems increases. Where firms are able to enter into insolvency or restructuring proceedings before environmental obligations are met, there is significant risk that the environmental liabilities will be under or un-funded.

For resource-based activities, where cash flows generally diminish as the activity runs its course, and liabilities typically increase due to inflation and ongoing harms resulting from activities, the application of the polluter pays principle becomes increasingly time sensitive.

Where end of life environmental obligations continues past the productive stage of the activity, the issue around securing resources for environmental purposes becomes increasingly important. The Alberta oilsands and their long-term management of tailings from open pit mines is a case in point. Currently, the proposed long-term

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<sup>15</sup> Margaret Russo Grossman, "Chapter 1: The Polluter Pays Principle and Agriculture: An Introduction" in Margaret Rossi Grossman (ed.), *Agriculture and the Polluter Pays Principle* (London, UK: 2009, British Institute of International and Comparative Law) at 1.

<sup>16</sup> Environmental Law Centre, (Edmonton: Environmental Law Centre 2019), online: Environmental Law Centre <http://elc.ab.ca/wp-content/uploads/2019/12/The-Polluter-Pays-Principle-in-Alberta-Law-December-2019.pdf>.

management of mine tailing is to use “end pit lakes”.<sup>17</sup> These lakes will require ongoing monitoring and management. Environmental costs associated with the end pit lakes will run well into the future if not into perpetuity.<sup>18</sup>

While the policy choices governments make regarding how to implement the polluter pays principle appears straight forward the decision of how to approach the application of the principle will have direct and indirect economic impacts, including impacts on the market structure of a given sector.

For example, in the energy sector, an economic analysis by Judson Boomhower (in the aptly named article *Drilling Like There's No Tomorrow: Bankruptcy, Insurance and Environmental Risk*), notes that where costs can be avoided through bankruptcy there can be an incentive to avoid environmental obligations among small to midsized firms.<sup>19</sup> In Boomhower's analysis the roll out of an “insurance requirement pushed about 6% of producers out of the market immediately.”<sup>20</sup> Boomhower further notes “The exiting firms were primarily small and were more likely to have poor environmental records.”<sup>21</sup>

“When liability is limited by bankruptcy, theory says that firms will take excessive environmental and public health risks. In the long run, this “judgment proof problem” may increase the share of small producers, even when there are economies of scale. ...These results suggest that incomplete internalization of environmental and safety costs due to bankruptcy protection is an important determinant of industry structure

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<sup>17</sup> For a discussion of the environmental impacts of end pit lakes see Louis Kabwe, J. Don Scott, Nicholas Beier and G. Ward Wilson “Environmental Implications of End Pit Lakes At Oil Sands Mine (2018) *Journal of Environmental Geotechnics* 6(2): 1-25.

<sup>18</sup> *Ibid.*

<sup>19</sup> See Judson Boomhower, *Drilling Like There's No Tomorrow: Bankruptcy, Insurance and Environmental Risk* Stanford Institute of Economic Policy Research, (February 2016), online: <https://economics.ucdavis.edu/events/papers/Boomhower1119.pdf>.

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*

and safety effort in hazardous industries, with significant welfare consequences."<sup>22</sup>

In making policy choices in this regard, the method of implementing an effective polluter pays system will have implications on both sides of the environmental and economic ledger. These policy tradeoffs will be reflected in regulatory choices both pre- and post-insolvency.

### **Pre-insolvency approaches to the polluter pays principle**

The issues that give rise to outstanding environmental liabilities are multi-faceted, and informed by firm and individual behavior, economic circumstances, and regulatory approaches. This being the case there are a variety of provincial regulatory mechanisms that can (and should) be used to ensure environmental costs are met.

Ensuring the polluter pays principle is upheld pre-insolvency is clearly a preferred approach and can be embodied in a variety of legal approaches. This includes emission standards, fees and taxes, penalties and administrative orders, extending liability to directors and officers, and requiring financial assurance (through letters of credit, bonds, insurance, or other financial instruments) to meet legal obligations for reclamation and remediation of land, water and air. For activities that cause impacts on the environment through their life, such as exploring, drilling, and producing oil and gas, there will often be legal obligations to reclaim the landscape and remediate any contamination resulting from the activity.

Under current laws in Alberta the primary approach taken is requiring financial security from the operator of an activity.<sup>23</sup> This approach can be an administratively efficient and proactive way to apply the polluter pays principle where an accurate assessment of liabilities is undertaken and full financial security (in combination with

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<sup>22</sup> *Ibid.*

<sup>23</sup> By way of example, see the Alberta Energy Regulatory, *Directive 68: ERCB Security Deposits*, (September 17, 2010) online: <https://www.aer.ca/documents/directives/Directive068.pdf>.

insurance for accidental releases) is required prior to the activity proceeding.<sup>24</sup> However, the amount of the security required by a regulator is often insufficient or it is not taken at all. Requiring full financial security for known and potential (i.e., accidental) harms resulting from operations will often give rise to arguments of inefficient use of capital, i.e., that the secured cash would be better placed in furtherance of other economic objectives.<sup>25</sup>

In Alberta, this has resulted in financial security being grossly insufficient to address environmental liabilities in the province (as noted above). Alberta's system of financial security (i.e., its liability management rating system for oil and gas operators) was put in place to require security deposits in prescribed instances, however historically these have proven deficient and were reliant on an overly optimistic view of firm health and commodity prices.<sup>26</sup>

In response to this issue, the C.D. Howe Institute has suggested a combination of approaches for the energy sector; requiring partial upfront security that escalates as the well's productive life is diminished and insurance requirements for inactive wells to provide flexibility and a price signal to abandon wells.<sup>27</sup>

While upfront security and/or insurance provides certainty and administrative efficiency, it is not without challenges. Understanding the quantum of costs of abandonment, reclamation, and remediation with precision is complicated. This is

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<sup>24</sup> See Ecosfiscal Commission, *Responsible Risk: How putting a price on environmental risk makes disasters less likely* (July 2018), online: <https://ecofiscal.ca/wp-content/uploads/2018/06/Ecofiscal-Commission-Risk-Pricing-Report-Responsible-Risk-July-11-2018.pdf>.

<sup>25</sup> See Benjamin Dachis, Blake Shaffer, and Vincent Thivierge "All's Well that Ends Well: Addressing End-of-Life Liabilities for Oil and Gas Wells" (September 2017) C.D. Howe Institute Commentary No. 492, online: [https://www.cdhowe.org/sites/default/files/attachments/research\\_papers/mixed/Commentary\\_%20492\\_0.pdf](https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_%20492_0.pdf) at 8.

<sup>26</sup> See Kelly Bourassa, Ryan Zahara and Chris Nyberg, "Restructuring Challenges in the Oil and Gas Sector: The Treatment of Regulatory orders Post-Redwater (2016) *Alberta Law Review* 54:2 online: <http://www.albertalawreview.com/index.php/ALR/article/download/471/463/>.

<sup>27</sup> See All's Well, *supra* note 8.

particularly the case where there are contamination issues that must be remediated. Costs associated with sites will also depend on the nature of the site, regulatory reclamation standards, and timing specific factors. These challenges in discerning the appropriate level of financial security can result in less security being taken than is necessary to fully cover the cost of reclamation and remediation.<sup>28</sup>

Other regulatory tools that force a polluter to pay will also challenge the status quo. This includes pursuing the recovery of costs associated with environmental harms by piercing the corporate veil and holding directors (and even possibly shareholders) responsible. While contentious, this type of approach is not so different from how secured creditors may now have to cover environmental costs and reflects a “beneficiary pays” approach to environmental liabilities. This approach has the added benefit of discouraging malfeasance and promoting environmentally proactive management by the directors.

Further any regulatory approach to environmental liabilities must be alive to the issue of how corporate structures can interplay with insolvency laws to frustrate environmental performance. For example, in the case of insolvency of Sequoia Resources Corp., the trustee in bankruptcy has filed a statement of claim and court application involving an asset sale and transfer from Perpetual Energy (and related parties) seeking to have the transaction set aside and alleging that the transaction was “under value” pursuant to s.96 of the BIA. The Alberta Energy Regulator stated the following in relation to the case:<sup>29</sup>

The AER has limited legislated authority to oversee corporate transactions. This is important to note because corporate transactions can result in AER licences

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<sup>28</sup> This can be illustrated by the northern mines described above and past surveys of deemed liabilities used by the regulator in Alberta's gas sector (as cited in Jason Unger, *Reclaiming Tomorrow Today: regulatory timing for abandonment and reclamation of well sites in Alberta* (Edmonton: Environmental Law Centre, 2013), online: [http://elc.ab.ca/media/98837/Reclaiming\\_Tomorrow\\_TodayFINAL.pdf](http://elc.ab.ca/media/98837/Reclaiming_Tomorrow_TodayFINAL.pdf) at pages 15-a6.

<sup>29</sup> Alberta Energy Regulator, Public Statement, “Facing the liability challenge in Alberta: AER president and CEO Jim Ellis, August 8, 2018), online: <https://www.aer.ca/documents/news-releases/AERPS2018-03.pdf>.



changing hands without having to go through the scrutiny of our transfer process. Unfortunately, this can be used by some companies to avoid their responsibility, potentially leaving millions of dollars of liability for the Orphan Well Association.

This is what happened after a corporate transaction between Sequoia and Perpetual Energy (Perpetual), allowing Perpetual to pass licences, and all liability, for many unprofitable and unwanted assets to Sequoia.

Similarly, in the United States it has been found that coal companies “have used the *Bankruptcy Code* to discharge or otherwise restructure substantial environmental, pension, and health care liabilities in a manner that has eviscerated the regulatory schemes that gave rise to those obligations”.<sup>30</sup> Specifically it was found that pre-bankruptcy restructuring and spinoffs of “onerous” assets to subsidiaries that then went bankrupt was used to avoid obligations.<sup>31</sup>

Insofar as these approaches are typically codified provincially and not integral to the insolvency process, we do not deal with them further. It must be recognized however that a suite of provincial regulatory tools is required to support the polluter pays principle.

It is essential to use a suite of pre-insolvency regulatory tools if the polluter pays principle is to be upheld. The rest of this report however focuses on when these regulatory tools fail.

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<sup>30</sup> Joshua Macey and Jackson Salovaara, “Bankruptcy as Bailout: Coal Company Insolvency and the Erosion of Federal Law” (2019) *Stanford Law review* 71:879, online: <https://review.law.stanford.edu/wp-content/uploads/sites/3/2019/04/Macey-Salovaara-71-Stan.-L.-Rev.-879.pdf> at 885.

<sup>31</sup> *Ibid.*

## Post insolvency approaches to the polluter pays principle: how is liability extended?

Insolvency can be simply defined as the inability to meet obligations as they come due.<sup>32</sup> This can and has included obligations arising from environmental regulations and orders against the insolvent party to clean up pollution.

In circumstances where the polluter pays principle has not been upheld pre-insolvency there are a variety of regulatory approaches that can embody the polluter pays or *beneficiary pays principle* post-insolvency. When a polluter can't pay the question becomes, who pays next?

In addressing this question the regulatory approaches could include a requirement that remaining assets of the polluter go to pay public obligations prior to payment of other creditors (i.e. the granting of a super-priority to the Crown)<sup>33</sup>, extend liability to previous operators who also caused some level of harm, extend liability to officers or directors, extending liability to creditors or shareholders, or extending liability to parent and/or affiliated companies. These types of approaches can be described as either expanding the scope of who is considered the “polluter” or applying the beneficiary pays principle.

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<sup>32</sup> The *Bankruptcy and Insolvency Act* defines an insolvent person as “a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and **(a)** who is for any reason unable to meet his obligations as they generally become due, **(b)** who has ceased paying his current obligations in the ordinary course of business as they generally become due, or **(c)** the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; (*personne insolvable*).

<sup>33</sup> Granting a “super-priority” to environmental obligations also avoids some barriers to applying the polluter pays principle during active operations. Fundamentally the question becomes for “near insolvent” firms, is it better to require suspension of operations (and related cash flows) to meet an environmental obligation or should the obligation be granted a super-priority. This again leads to debate about economic efficiency of requiring up front security versus the ability of a regulator to require abidance with the polluter pays principle in a timely fashion.

Our current laws integrate a variety of these approaches. The *BIA* and *CCAA* does provide for a super-priority to the Crown related to debts that relate to the environmental condition or damage of the insolvent party's property. As will be discussed later however, there are limitations to the scope and effectiveness of this prioritized security.

Directors and officers may also be liable to undertake environmental orders by virtue of provincial pollution laws. By way of example, the Ontario Ministry of Environment (MoE) issued an order against Northstar Aerospace (Canada) Inc. to remediate a contaminated site. The company entered bankruptcy effective August 2012.<sup>34</sup> The (MoE) had drafted an order against the directors of the company and used that order as a basis for a claim of ~\$15 million in the *CCAA* proceeding. Subsequently, in November 2012, the order against the directors to remediate the site was issued.<sup>35</sup> The Order was resolved by agreement and the payment of \$4.5 million was made to the Government of Ontario.<sup>36</sup> Using regulatory orders against directors remains contentious and various legal arguments may arise depending on the nature and scope of provincial laws.

An Alberta Court has commented on the logic in extending environmental liability to creditors, as benefactors of a polluter's operations. In the case of *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, the liquidator (PWC) was seeking advice and direction from the court regarding liability for environmental obligations and the nature of liability attributable to the Bank of Canada, as secured creditor, for the winding up of the Canadian Commercial Bank under the federal *Winding Up and Restructuring Act*.<sup>37</sup> Importantly, under that Act the liquidator does not have the similar protections from environmental liability that was codified in the *BIA* and the

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<sup>34</sup> See *Baker v. Director (MOE)* Ontario Environmental Review Tribunal, 12-158, and related decisions, online <https://www.ert.gov.on.ca/CaseDetail.aspx?n=12-158>. Specifically see a review of the facts set out in the decision regarding the staying of the proceeding, online at <https://www.ert.gov.on.ca/files/201303/00000300-CL74AB70B1O026-DCM56EFC2NO026.pdf>.

<sup>35</sup> *Ibid.*

<sup>36</sup> *Ibid.*

<sup>37</sup> *Winding-up and Restructuring Act*, RSC 1985, c W-11.

CCAA. In discerning whether a liquidator (PWC) should be indemnified by the secured creditor (Bank of Canada) in relation to environmental obligations, the Alberta Court noted:<sup>38</sup>

It is only equitable, in my view, that Bank of Canada be liable to bear any loss in relation to the properties from which it received a benefit. A loss includes an environmental claim that arises from the management of the properties during liquidation. ... However, this principle should only extend insofar as PWC acted reasonably in its management of the properties. Nor do I see why the fact that Bank of Canada benefited indirectly rather than directly should have any bearing. However, the proportion of responsibility for any loss is only equal to that of the benefit received. Where parties shared the benefit arising from a property, they should likewise share the loss.

While the circumstances of this case were unique, the court's approach is compelling insofar as it recognizes that polluting activities do not operate in isolation. The challenge in applying the beneficiary pays principle is to discern the requisite nexus between a given benefit and the environmental costs. Benefits from solvent companies flow to multiple recipients including to the public purse through taxation. Quantifying the relative benefit of a firm's operations across creditors is likely feasible but the broader calculation of public benefit is likely significantly more complex. The policy question becomes "How broadly should our laws cast the net environmental liability?", i.e. which benefactors should be liable for the environmental condition caused by polluters?

As our law currently stand, the beneficiary pays principle is applied in certain instances but may be avoided in others. Codification that clarifies the application of the beneficiary pays principle is warranted.

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<sup>38</sup> *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, 2000 ABQB 440 (CanLII), <http://canlii.ca/t/5n3x> at para 50.

## Legal Context of Insolvency and Environmental Obligations

Most activities on the landscape that are likely to have long lasting effects on the environment are accompanied with legal obligations to address those environmental harms. This may take the form of duties to abandon, decommission and reclaim land or remedy the condition of land or water from the impacts of pollution. In Alberta these obligations primarily arise pursuant to the *Environmental Protection and Enhancement Act* (EPEA), although various obligations may arise under other legislation (for more information in this regard see [The Polluter Pays Principle in Alberta Law](#)).

Where a firm becomes insolvent the meeting of environmental obligations can be undermined. From the perspective of creditors and bankruptcy practitioners the property that carries the obligation is typically viewed as a burden on the insolvent estate that is best avoided. In this report we use the term “*onerous property*” to mean the specific property that is in an environmental condition that must be addressed by way of a public law duty (either through regulations or administrative orders). These types of obligations may be avoided in a several ways, some through a formal bankruptcy proceeding and others outside of it.

An insolvent firm may enter the bankruptcy process by way of an application to the court being made by creditors. This requires that the debtor has more than \$1,000 in debt and proof that the debtor has performed an “act of bankruptcy” under section 42 of the *Bankruptcy and Insolvency Act* (BIA). An insolvent party may also seek to voluntarily assign assets to existing creditors and/or make a proposal to creditors under the BIA. For voluntary assignment to occur the official receiver must seek to appoint a licenced trustee however if there is no trustee willing to act the assignment may be cancelled.<sup>39</sup> The appointment may also be made by the court where “bankruptcy is desirable in order to protect the interest of creditors and

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<sup>39</sup> BIA at s.49. It should be noted that any proceeding to otherwise liquidate or dissolve a company is stayed if “the corporation is at any time found to be insolvent within the meaning” of the BIA (see s.207 of the *Business Corporation Act*, R.S.A. 2000, c. B-9).

shareholder.”<sup>40</sup> An insolvent firm may also seek protection against creditors and seek to restructure its debts and assets under the *Companies’ Creditors Arrangement Act* (CCAA) in certain instances.<sup>41</sup>

Some of the key aspects of the insolvency legislation and process (either under the *BIA* or *CCAA*) that impact the environmental obligations include:

- The receiver and/or trustee abandoning or disclaiming the property to which the liability is tied (the main example being contaminated land and the primary issue in the recent SCC case of *Orphan Well Association v. Grant Thornton Ltd. (hereinafter Redwater)* <sup>42</sup>;
- Characterizing the environmental obligation as a provable claim;
- The provision of a super-priority to the Crown in relation to property that is encumbered by the environmental obligation;
- Having the debtor pay part of the debts owed pursuant to a court sanctioned agreement under the *CCAA*;
- Staying of proceedings and execution of orders (section 69 of *BIA* and section 11.02 of the *CCAA*); and
- Discharging of debt claims in bankruptcy (typically of limited relevance in corporate insolvencies but otherwise of note for individuals liable for environmental clean up).

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<sup>40</sup> *Chow v. Bresea Resources Ltd.*, 1997 ABCA 386 (CanLII), <<http://canlii.ca/t/2dfhp>>. Where a trustee is not found to be willing to take on an assignment and where creditors are unwilling to pursue bankruptcy the resulting situation becomes a bit more uncertain. A corporation may simply sit as abandoned and later be dissolved by the Registrar under *Business Corporations Act* at s.213 (although the general rule is that the Registrar is prevented from dissolving insolvent companies under section 207 of the Act).

<sup>41</sup> The *CCAA* is available to a “debtor company” or affiliated debtor companies with debt claims in excess of \$5 million. See *CCAA* at s.3. A debtor company is one that is insolvent or is bankrupt (as described in section 2(1)).

<sup>42</sup> 2019 SCC 5, online: Supreme Court of Canada <https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/17474/index.do> at para 86 [hereinafter *Redwater*].

The issues of the highest concern are when an environmental order is viewed as a provable claim and when onerous property can be abandoned or disclaimed as part of the insolvency proceeding.

Until recently, the abandonment or disclaimer by the receiver of an interest in onerous property had the effect of avoiding the public duties related to that property. The *Redwater* decision appears to have changed this but significant uncertainty remains (and is discussed further below).

Where the Crown has an outstanding order related to environmental condition or damage against an insolvent party at the time of entering into the bankruptcy process, the environmental order can be viewed as a provable claim by the receiver. In this way a public duty is effectively transformed into a debt to the Crown. A “provable claim” is “any claim or liability provable in proceeding ...by a creditor” and can include contingent and unliquidated claims.<sup>43</sup> The costs of remedying the harm to the environment by the Crown, either already incurred by work being done prior to the bankruptcy or contingent on future work, are granted a super-priority by virtue of section 14.06(7) of the *BIA*. Importantly this super-priority is limited by the fact that it is “secured by security on the real property or immoveable affected by the environmental condition or environmental damage”.<sup>44</sup> This means that if the costs of environmental remediation are greater than the value of the property itself that the Crown will not be able to recover the additional funds through its super-priority.

The combined effect of these provisions is that, where property is determined to be onerous, the obligations and security of the Crown can be undermined.

Similarly, in a restructuring proceeding under *CCAA* the public obligation may be undermined by disclaiming any interest in the property, by transferring the polluted property to another party, by selling of assets that undermine the pool of assets of the company to meet its obligations post restructuring, or by way of court approved plan to address existing debts that results in less than full recovery by the Crown to meet

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<sup>43</sup> See *BIA* at s.2.

<sup>44</sup> *Ibid.* at s.14.06(7).

environmental obligations.<sup>45</sup> Under the CCAA debts may only be partially covered by virtue of a debtor's compromise or agreement with creditors (that hold 2/3 of the value of the debt owing) where a court approves such a plan.<sup>46</sup>

Finally, the meeting of environmental obligations may be further undermined where an insolvent company simply dissolves. Where the value of a firm's debts are insufficient to qualify for restructuring under the CCAA or, where the costs of entering a bankruptcy proceeding under the *BIA* are not justified, the firm's assets may simply be abandoned.<sup>47</sup>

### **Additional challenges with environmental orders being treated as provable claims**

Many provable claims relating to environmental orders will be contingent in nature, i.e., the value of the debt is based on an act, the cleaning up of the property, that has yet to occur. The cost of cleaning up the environment, whether it is remediating hazardous substances or reclaiming the land to a former state, is not easy to accurately project. For example, the effectiveness of reclamation may take years to properly evaluate. For oil and gas wells a regulatory order to remedy reclamation failings may still be issued up to 25 years after the issuance of a reclamation certificate (for those certificates issued after October 1, 2003).<sup>48</sup>

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<sup>45</sup> The CCAA does set out some restrictions on court sanctioned agreements and their impacts on Crown debts. Specifically, s.6(3) states that debts related to tax or pensions must be paid in full as a prerequisite to the court sanctioning an agreement. A similar requirement does not exist for environmental obligations. It should be noted that unless otherwise ordered by the court an initial stay order doesn't affect a regulatory body's proceeding in relation to the company. See CCAA at s.11.1. the court may stay a regulatory proceeding in accordance with ss. 11.1(3) and 11.1(4).

<sup>46</sup> CCAA at s.6 states that where creditors (holding 2/3 of the value of the creditors) agree to a compromise or agreement under the Act the court may approve the arrangement and that arrangement is binding.

<sup>47</sup> The CCAA process applies where the debtor company or affiliated debtor companies have in excess of \$5 million in debtor claims. See CCAA s.3.

<sup>48</sup> See the *Conservation and Reclamation Regulation*, AR115/1993 at s.15.



Details about the nature of the cleanup may be inaccurate resulting in an inaccurate claim and further undermining the polluter pays principle. A review of the Orphan Well Association annual reports illustrates the vast differences in remedial, reclamation and abandonment costs that might occur.<sup>49</sup> Typically even a rudimentary understanding of the potential costs only occurs once a full site assessment has been conducted, something that may or may not be available at the time of proving up a claim. This further complicates recovery of sufficient funds as the ability of a regulator to accurately assess the environmental condition and remediation costs are put to the test.

## Environmental obligations in the Alberta context

The issues of addressing environmental liabilities where the polluter is insolvent is magnified where the property interests of the polluter are minimal and the costs of remedying environmental condition are relatively high. This is the scenario that has played out in Alberta, where the interests of oil and gas operators in property (at surface) have limited value and their environmental obligations can be significant, particularly where land and water have been polluted.

The Alberta situation has been made worse by historic policy choices that saw the transfer of oil and gas properties of dwindling value to smaller firms.<sup>50</sup> These historic policy choices have failed to ensure that those companies who purchase these dwindling assets had sufficient capital or were financially healthy enough to manage liabilities in the face of lower commodity prices. The ability to defer the abandonment and reclamation of wells indefinitely allowed firms to avoid the liability.

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<sup>49</sup> See [www.orphanwell.ca](http://www.orphanwell.ca). For example, in the 2016/2017 reporting year, site remediation costs ranged from \$26,000 to \$668,000 and site reclamation ranged from \$5,900 to \$110,000. See pages 46 and 50 respectively in Orphan Well Association 2016/2017 Annual Report, online: Orphan Well Association <http://www.orphanwell.ca/wp-content/uploads/2018/01/OWA-2016-17-Ann-Rpt-Final.pdf>.

<sup>50</sup> The regulatory framework around oil and gas in the province has long taken the approach to be flexible in transfer of assets, to accommodate and facilitate mid and small firm entry into the sector. This was accompanied by, arguably, a flawed system of quantifying the financial firm fitness to meet debts on the longer term and a general failing to push for timely abandonment and reclamation of assets.

The granting of a super-priority for costs associated with remedying environmental condition or damage is of limited value where the properties are of limited value and where they can be disclaimed or abandoned. This is particularly the case where the property interest of the operator is a lease and the value is in subsurface minerals (that are substantively depleted). The linkage of a super-priority secured to the onerous property renders the priority worthless in some circumstances.<sup>51</sup>

It is this limitation, i.e., that the liability attached to a largely valueless piece of property, that was addressed in the Supreme Court of Canada decision of *Orphan Well Association v. Grant Thornton Ltd* (a.k.a., *Redwater*).<sup>52</sup>

## Abandonment of property and super-priority in other jurisdictions

The state of the law in Canada (until *Redwater*) in relation to the ability to disclaim or abandon property reflected similar approaches in other nations. In a review of US and UK law on the issue of environmental claims and insolvency, Blanca Mamutse and Valerie Fogleman concluded:<sup>53</sup>

[T]he reach of the polluter pays principle has remarkably little effect on bankruptcy/insolvency law to date. The fundamental principle of limited liability in company law has prevailed in many, if not most, cases against the fundamental principle of the polluter pays in environmental law.

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<sup>51</sup> Both the *BIA* and *CCAA* securing the environmental debt "by a charge on the real property and on any other real property of the company that is contiguous thereto" See *BIA* at s. 14.06(8) and *CCAA* at s.11.8(8).

<sup>52</sup> *Supra* note 1.

<sup>53</sup> Blanca Mamutse, Valerie Fogleman, "Environmental Claims and Insolvent Companies: The Contrasting Approaches of the United Kingdom and the United States", (2013) *Br. J. Am. Leg. Studies* 2:579. US approaches whether environmental obligations are a "claim" - to be dischargeable it must be a claim (like in Canada). U.S. s.101(5)(b) re right to an equitable remedy for breach of performance if such breach gives right to a right of payment.

In this regard, the overriding purpose of insolvency legislation to secure the highest return for creditors is not unique to Canada. The right of the trustee to disclaim contracts or abandon interests in “onerous” property finds its origins in common law but is codified in several other jurisdictions (see Table 1 below).

In the U.S. this right for a trustee to abandon onerous property has been constrained in some circumstances, including where state law required actions “where the public health or safety is threatened with imminent and identifiable harm”.<sup>54</sup> Similarly, the ability to abandon onerous property in bankruptcy exists in the United Kingdom and Australia.

While the right to abandon or disclaim onerous property in insolvency appears common, the granting a super-priority to debts related to environmental obligations appears more variable across states. Some jurisdictions, like Canada, provide a super-priority for debts incurred to meet environmental obligations in certain circumstances, whereas others have not granted any type of priority to these obligations.

Federal bankruptcy law in the United States does not provide for a super-priority but rather a higher priority can occur by virtue of state law. In relation to other federal law, liability under the *Comprehensive Environmental Response Compensation and Liability Act (CERCLA)* can be secured by a lien in favour of the federal government, the priority of which is dictated by state law.<sup>55</sup>

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<sup>54</sup> Jim Vine, “Judge Merhige’s Environmental Decisions: Expert Handling of Groundbreaking Environmental Rulings And Complex Federal Jurisdictional Questions”, (2017) *University of Richmond Law Review* Vol 52: 39, online: <https://lawreview.richmond.edu/files/2017/09/Vines-52-online.pdf>.

<sup>55</sup> US section 9607– normal priority (3). U.S. Code Title 42, Ch. 103 at § 9607(l)(3), online: <https://www.law.cornell.edu/uscode/text/42/9607>.

**Table 1: Abandonment of “onerous” property by trustees or receivers in select jurisdictions**

	Canada	UK	Australia	USA
<b>Source of Law</b>	Common law *also see BIA at s.20 re: divestiture by trustee	<i>Insolvency Act</i> 1986, c. 45 at s. s.315. <sup>56</sup>	<i>Bankruptcy Act</i> 1966 at s.133. <sup>57</sup>	U.S. Code, Title 11: <i>Bankruptcy</i> at §554
<b>Terms of abandonment</b>	By implication of s.14.06(4) and (5).  Receiver may “abandon or renounce interest in real property” and may assess value of complying with order.	Trustees (and liquidators) can disclaim “(a)any unprofitable contract, and (b)any other property of the company which is unsaleable or not readily saleable or is such that it may give rise to a liability to pay money or perform any other onerous act.”	Trustee may disclaim property or tenure with onerous covenants, or where costs and charges related of the land exceed the realizable proceeds of the land.	“The trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate” with notice and a hearing. <sup>58</sup>

Some states have codified a super-priority of liens for remediation activities.<sup>59</sup> A review of state super-priority liens was conducted by Marilyn Uzdavines in 2016.<sup>60</sup>

<sup>56</sup> *Insolvency Act* 1986, c. 45 at s. s.315, online:

<http://www.legislation.gov.uk/ukpga/1986/45/part/IV/chapter/VIII/crossheading/disclaimer-england-and-wales-only>. Also see Mackie, C and Fogleman, V (2016) Self-insuring environmental liabilities: a residual risk-bearer's perspective. *Journal of Corporate Law Studies*, 16 (2). pp. 293-332. ISSN 1473-5970, online: <https://doi.org/10.1080/14735970.2016.1181399>, <http://eprints.whiterose.ac.uk/125326/7/Self-Insuring%20Environmental%20Liabilities%20-%20Mackie%20and%20Fogleman.pdf>.

<sup>57</sup> *Bankruptcy Act* 1966 at s.133, online:

[http://classic.austlii.edu.au/au/legis/cth/consol\\_act/ba1966142/s133.html](http://classic.austlii.edu.au/au/legis/cth/consol_act/ba1966142/s133.html).

<sup>58</sup> U.S. Code, Title 11: *Bankruptcy* at §554, online: <https://www.law.cornell.edu/uscode/text/11/554>.

<sup>59</sup> Marilyn Uzdavines “Superiority of Remediation Liens: A cure to the Virus of Blight.” (2016) *University of Baltimore Law Review* Vol 45: issue 3, article 2 online:

Uzdavines notes that these state based priorities granted to remediation activities (equal or greater to tax liens) have been upheld by the courts when challenged on the basis that they constituted an illegal taking without due process (and were thereby contrary to the U.S. Constitution).<sup>61</sup>

Heightened security for environmental obligations have also been put in place in several European Union states.<sup>62</sup> The European Commission's *Study on Analysis of integrating the ELD [Environmental Liability Directive] into 11 national legal frameworks* (2013) highlighted the approach of some states:<sup>63</sup>

In France, if the operator of a site subject to the Classified Installations Law becomes insolvent and is liquidated, the liquidator must order an environmental consultant to prepare a report detailing any remediation work that should be carried out. The liquidator must ensure that adequate funds are secured from the insolvency estate's assets to pay for the remediation depending, of course, on the funds that are available.

The transposing legislation in Slovakia provides that if an operator is insolvent, the payment of costs to the competent authority for preventive

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<https://scholarworks.law.ubalt.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1998&context=ublr>.

<sup>60</sup> *Ibid.*

<sup>61</sup> *Ibid.*

<sup>62</sup> The EU Environmental Liability Directive (Article 14) which states "Member States shall take measures to encourage the development of financial security instruments and markets by the appropriate economic and financial operators, **including financial mechanisms in case of insolvency**, with the aim of enabling operators to use financial guarantees to cover their responsibilities under this Directive. Directive 2004/35/ CE of the European Parliament and of the Council of 21 April 2004 on the environmental liability with regard to the prevention and remedying of environmental damage, online <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:02004L0035-20130718&from=EN>.

<sup>63</sup> European Commission, *Study on Analysis of integrating the ELD [Environmental Liability Directive] into 11 national legal framework*, (2013), Project No. 2014.1174, online: <http://ec.europa.eu/environment/legal/liability/pdf/Final%20report%20-%20ELD.pdf>.

or remedial measures is a claim of a secured creditor and recovery under the law on bankruptcy and restructuring.

The transposing legislation in the Czech Republic contains procedures for the recovery of costs in insolvency proceedings if the operator becomes insolvent or is wound up.

The transposing legislation in Slovenia provides that a person who causes pollution under the ELD regime is also liable for its environmental effects in the event of bankruptcy or liquidation.

As can be seen, the challenges that Canada has faced is far from unique in relation to balancing environmental priorities with those of creditors in insolvency proceedings.

## The constitutional tension of insolvency and polluter pays principle

The Canadian *Constitution Act* (1867) is a source of potential conflict between regulating insolvency and effective environmental management.<sup>64</sup> Bankruptcy and insolvency are regulated federally, pursuant to s.91(21) of the *Constitution*. In contrast, most activities giving rise to environmental obligations are more squarely within provincial jurisdiction, i.e., resource extraction, resource production and manufacturing.<sup>65</sup> In this regard, the provinces are faced with securing the state of the environment, whereas Canada is focused on providing a regulated system of administering debts during insolvency: two very distinct and often incompatible objectives.

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<sup>64</sup> *Constitution Act*, 1867, 30 &31 Victoria, C. 3(U.K.) as amended, online: Justice Laws Website <https://laws-lois.justice.gc.ca/eng/const/page-1.html>.

<sup>65</sup> See *Constitution Act*, ss. 92(10), (13), (16) and 92A.

The two purposes of the federal bankruptcy legislation are:

- 1) financial rehabilitation of the debtor (where feasible), and
- 2) equitable distribution of assets to creditors.<sup>66</sup>

Financial rehabilitation of the debtor occurs by discharging outstanding debts, i.e., providing a clean slate for the debtor once the bankruptcy process has run its course.<sup>67</sup> While some debts of the bankrupt may continue through the bankruptcy process (i.e. they aren't discharged) these debts are limited in nature.<sup>68</sup> For corporations however this clean slate outcome rarely applies, as typically the bankrupt company simply dissolves once its assets are distributed. "Equitable distribution of assets is achieved by requiring creditors wishing to enforce a claim provable in bankruptcy to participate in one collective proceeding."<sup>69</sup> As this report will discuss, both of these purposes are so broad and encompassing as to be almost paralyzing in relation to certain provincial regulations that impacts an insolvent party; that was until the SCC decision in *Redwater*.<sup>70</sup>

The split in jurisdiction around bankruptcy and business generally raises the spectre of provincial regulatory regimes being rendered inoperative where the doctrine of federal paramountcy imposes itself. As noted by the Supreme Court:<sup>71</sup>

The issues in this appeal arise from what has been termed the "untidy intersection" of provincial environmental legislation and federal

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<sup>66</sup> 407 *ETR Concession Co. v. Canada* (Superintendent of Bankruptcy), [2015] 3 SCR 397, 2015 SCC 52 (CanLII), <http://canlii.ca/t/gm22n>.

<sup>67</sup> Section 178(2) of the *BIA* notes that "an order of discharge releases the bankrupt from all claims provable in bankruptcy". For corporations the creditors' claims must be satisfied in full prior to applying for a discharge from bankruptcy (see s.169(4)).

<sup>68</sup> *BIA* at s.178.

<sup>69</sup> *Alberta (Attorney General) v. Moloney*, [2015] 3 SCR 327, 2015 SCC 51 (CanLII), <http://canlii.ca/t/gm22j>, retrieved on 2018-09-07.

<sup>70</sup> *Supra* note 1.

<sup>71</sup> *Ibid* at para 64.

insolvency legislation (*Nortel Networks Corp., Re*, 2012 ONSC 1213, 88 C.B.R. (5th) 111, at para. 8). Paramountcy issues frequently arise in the insolvency context. Given the procedural nature of the *BIA*, the bankruptcy regime relies heavily on the continued operation of provincial laws. However, s. 72(1) of the *BIA* confirms that, where there is a genuine conflict between provincial laws concerning property and civil rights and federal bankruptcy legislation, the *BIA* prevails (see *Moloney*, at para. 40). In other words, bankruptcy is carved out from property and civil rights but remains conceptually part of it. Valid provincial legislation of general application continues to apply in bankruptcy until Parliament legislates pursuant to its exclusive jurisdiction in relation to bankruptcy and insolvency. At that point, the provincial law becomes inoperative to the extent of the conflict

The nature of purpose of the *BIA*, the focus on equitably distributing the bankrupt estate's assets, the treatment of regulators as debtors with "provable claims", and the ability to disclaim or abandon onerous property is at the center of the "untidy intersection" of federal and provincial law.<sup>72</sup>

Several recent court decisions resulted in the frustration of provincial regulatory action by treating regulatory orders as provable claims in bankruptcy and corporate restructuring proceedings. Regulatory actions had been found to consistently be "provable claims" or, in the case of the lower court decisions in *Redwater*, regulatory approaches were found to be unconstitutional as they directly conflicted with or frustrated the purpose of the *BIA*.

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<sup>72</sup> Justice Morowitz in *Nortel Networks Corporation (Re)*, 2012 ONSC 1213 (CanLII), <http://canlii.ca/t/fqjt7> noting at para 8 "The Nortel Motion arises from the untidy intersection of the CCAA and, in particular, the Stay provided for in the Initial Order and the powers of the MOE to make orders with respect to the remediation of real property in Ontario."



These cases emerged from the Supreme Court of Canada (SCC) case of *Newfoundland and Labrador v. AbitibiBowater Inc.*<sup>73</sup> in which the court articulated a three part test of determining whether a regulatory order should be viewed as a provable claim (in the context of the *Companies' Creditors Arrangement Act*, which has analogous language to the *BIA*). The Courts have observed that provable claims would be established as follows:<sup>74</sup>

First, there must be a debt, a liability or an obligation to a creditor. Second, the debt, liability or obligation must be incurred before the debtor becomes bankrupt. Third, it must be possible to attach a monetary value to the debt, liability or obligation.

In applying the test in *Abitibi*, Justice Deschamp observed that the first two parts of the test were readily met:<sup>75</sup>

This case does not turn on whether the Province is the creditor of an obligation or whether damage had occurred as of the relevant date. Those requirements are easily satisfied, since the Province had identified itself as a creditor by resorting to *EPA*

### Readings on Insolvency and Oil and Gas Regulations

Anna J. Lund "Lousy Dentists, Bad Drivers, and Abandoned Oil Wells: A New Approach to Reconciling Provincial Regulatory Regimes with Federal Insolvency Law" (2017) 80 *Sask. L. Rev.* 157.

Fenner Stewart, "How to Deal with a Fickle Friend? Alberta's Troubles with the Doctrine of Federal Paramountcy" (Toronto: Carswell 2018) Janis P. Sarra & Barbara Romaine, eds. *2017 Annual Review of Insolvency Law*.

Nigel Bankes "Majority of the Court of Appeal Confirms Chief Justice Wittmann's Redwater Decision", *Ablawg*, May 3, 2017.

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<sup>73</sup> *Newfoundland and Labrador v. AbitibiBowater Inc.*, [2012] 3 SCR 443, 2012 SCC 67 (CanLII), <http://canlii.ca/t/fv38t> and *Nortel Networks Corporation (Re)*, 2013 ONCA 599 (CanLII), <http://canlii.ca/t/g0sf4>.

<sup>74</sup> *Abitibi* at para 26.

<sup>75</sup> *Abitibi* at 49.

enforcement mechanisms and since the damage had occurred before the time of the CCAA proceedings.

Following *Abitibi* a trend emerged in the case law invariably treating regulators as creditors rather than as an agent of the Crown seeking to enforce a public duty. (See *Nortel Networks Corporation (Re)*, *Northstar Aerospace Inc. (Re)*, *Orphan Well Association v Grant Thornton Limited*, and *Sydco Energy Inc (Re)*.<sup>76</sup>)

In these cases, environmental orders were effectively transformed from legal obligations to remedy environmental damage into debt claims against an insolvent estate. This approach reflects a divergence from previous case law (that occurred prior to the 1997 amendments to the *BIA*) whereby energy regulation and bankruptcy law were found to be able to operate together in relation to the need for a receiver to comply with the regulatory order.<sup>77</sup>

The Supreme Court of Canada revisited the scope and application of the *Abitibi* test in the *Redwater* case.<sup>78</sup> *Redwater* recasts how environmental obligations are to be viewed in bankruptcy proceedings but has left lingering uncertainty.<sup>79</sup>

## The SCC approach in *Redwater*

The *Redwater* case involved an insolvent oil and gas company, Redwater Energy Corporation, a company with oil and gas assets of varying productivity. Some properties could be viewed as “onerous” in a bankruptcy context due to abandonment and reclamation obligations, while other oil and gas assets were profitable. The receiver determined that the onerous assets should be disclaimed (i.e.

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<sup>76</sup> See *Nortel Networks Corporation (Re)*, 2013 ONCA 599 (CanLII), *Northstar Aerospace Inc. (Re)*, 2013 ONCA 600 (CanLII), *Orphan Well Association v Grant Thornton Limited*, 2017 ABCA 124 (CanLII), and *Sydco Energy Inc (Re)*, 2018 ABQB 75 (CanLII).

<sup>77</sup> *PanAmericana de Bienes y Servicios S.A. v Northern Badger Oil & Gas Ltd.*, 1991 ABCA 181 (CanLII), 81 Alta LR (2d) 45, 117 AR 44, leave to appeal denied [1992] 1 SCR <http://canlii.ca/t/1nnwr>.

<sup>78</sup> *Supra* note 1.

<sup>79</sup> *Ibid.*

abandoned or disowned) and the profitable ones should be sold off separately to provide payment to Redwater's creditors. (For a more in-depth review of the lower court cases see the publications in the sidebar above.)

The case focused on determining the ability of a receiver to "disclaim" certain oil and gas wells and the approach taken by the Alberta Energy Regulator to manage the estates assets, including the issuance of orders to abandon and reclaim the onerous wells.

The Supreme Court of Canada concluded that Alberta's provincial regulations related to environmental obligations (or public duties):

- 1) can operate side by side with federal bankruptcy legislation, and
- 2) that environmental orders may be characterized as public duties that should not be considered "provable claims" alongside other debts of the insolvent party.

The SCC distinguished this case from its earlier *Abitibi* decision, allowing the provincial regulatory regime to stand and apply to insolvent oil and gas companies.

Other key findings of the court include:

- That receivers in bankruptcy will be protected from personal liability in relation to the environmental condition or damage and regulatory orders related thereto (such as abandoning and reclaiming a wellsite) under s.14.06 of the *BIA*;
- That the estate of a bankrupt party may still have to comply with orders even if in doing so the amount of cash left over to distribute to creditors is diminished;
- That a government or regulatory agency issuing an order to meet a public duty and seeking to enforce that order is not to be viewed as a creditor in every instance (distinguishing it from its earlier decision in *Abitibi*);
- Public duties, such as environmental obligations, will be treated as provable claims in limited circumstances; and

- Regulatory obligations may impact distribution of assets without conflicting with the *BIA* (distinguishing it from the *SCC* decision in *Moloney*).<sup>80</sup>

The end result is that the assets of the Redwater estate would have to go to the obligations as set out by the *AER* first, with remaining assets then being made available to secured creditors (and unsecured creditors if anything was left over).

Prior to the decision, disclaimed properties would make their way into the provincial orphan well program that was supported by payments from other solvent industry participants, through payments to the Orphan Well Fund (by way of an industry levy), and by periodic government contributions to the fund (\$60 million to 2019).<sup>81</sup> (With a likely tab of several billion dollars it seems that the public will be on the hook for some of the costs of these legacy sites; the question is how much.<sup>82</sup>)

As a result of the decision the estate of the insolvent party is obliged to meet the public duty, in effect the assets that would be distributed to secured creditors must address this duty first.

It should be noted that both pre- and post-decision a strict application of the polluter pays principle was not being applied. Existing provincial regulation for orphaned sites, where there was no financial security or insufficient financial security required by the regulator, did not abide by the polluter pays principle, rather other oil and gas

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<sup>80</sup> *Alberta (Attorney General) v. Moloney*, [2015] 3 SCR 327, 2015 SCC 51 (CanLII), <http://canlii.ca/t/gm22l>, retrieved on 2018-09-07.

<sup>81</sup> Under provincial law when the wells are orphaned through the insolvency process the costs of abandoning and reclaiming the sites are dealt with through levies on other companies. See Part 11 of the Oil and Gas Conservation Act, R.S.C. 2000, c. O-6, online: Alberta Queen's Printer [http://www.qp.alberta.ca/1266.cfm?page=006.cfm&leg\\_type=Acts&isbncln=9780779797325&display=html](http://www.qp.alberta.ca/1266.cfm?page=006.cfm&leg_type=Acts&isbncln=9780779797325&display=html)? These levies fund the operation of the Orphan Well Association, the association that deals with orphaned oil and gas wells (and pipelines) in Alberta. The public purse has also contributed approximately \$60 million to the OWA since 2009. This includes a \$30 million in 2009 from the Government of Alberta and an additional \$30 million from the Government of Canada to cover of interest on a \$235 million provincial. See Orphan Well Association, *Annual Report 2017/2018*, online: <http://www.orphanwell.ca/wp-content/uploads/2018/10/OWA-2017-18-Ann-Rpt-Final.pdf> at p5.

<sup>82</sup> *Supra* note 8.

operators and the public have been required to pay. In this way one could characterize the state of affairs both before and after the SCC decision as one of “beneficiary pays”. The difference being the proximity of the “beneficiary” to the polluter following the decision has become closer as creditors of the polluter have a direct benefit associated with their relationship with the polluter.

The decision resulted in a recasting of how the polluter pays principle applies when there is a bankruptcy and how environmental obligations of the bankrupt estate must be met. Specifically, the liability that used to flow through to the Orphan Well Association and its funders (both industry and the public to date), now flows, where bankruptcy or restructuring proceedings are engaged under federal law, to creditors first by virtue of their asset tied loans going to meet environmental obligations first.

One of the key conclusions of the case was that the AER’s regulatory orders and limitations on transfers of licences (in light of Redwater’s disclaiming of certain onerous assets) did not conflict with section 14.06 of the *BIA*, nor did it frustrate the purpose of s.14.06.<sup>83</sup> Further the majority found that the distribution of assets was not upset as the obligations imposed were not “provable claims” and that the government (or the Orphan Well Association) was not a creditor. The dissenting decision of the SCC concluded that the conflict did arise as the provincial regulator’s actions effectively created a “debt enforcement scheme – one that requires the environmental obligations owed to the AER to be discharged ahead of the bankrupt’s other debts”.<sup>84</sup>

One of the central issues of the case was when an order may be treated as a provable claim. When an order is viewed as a provable claim, the result is that the obligation, insofar as it can be assessed, becomes a debt like any other. The Crown may then exercise its super-priority and seek recovery of its debt. The major stumbling block, particularly so for the oil and gas industry, is that being a creditor in relation to “onerous” property is of little to no value.

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<sup>83</sup> *Redwater* at paras 72-164.

<sup>84</sup> *Redwater* at para 281.

The SCC in *Redwater* said that the *Abitibi* test should not be applied in an overly presumptive or broad fashion. Regulators are not necessarily creditors when seeking to enforce an environmental order.<sup>85</sup> The SCC adopted the position that just because a regulator issues an order that could later become a debt it is not to be considered a creditor automatically.<sup>86</sup> This is important as it recognizes that environmental obligations are not the same as simply monetary obligations to a creditor, rather, they are public duties.

The majority of the Supreme Court clearly distinguished this case from the specific circumstances of *Abitibi*. The court focused on the fact that in *Abitibi* the Newfoundland Government had expropriated assets/land of the company and was thus clearly in a position to financially gain by issuing the order. This is contrasted to the Alberta situation where the aim of the order was to meet a public regulatory duty, not for the financial gain of the government.

It should be noted that this distinction leads one to the arguable conclusion that if a regulator is only to be viewed as a creditor where an order will financially benefit the government (i.e., beyond the cost of meeting a public duty) or when actual expenditures have been incurred, then regulators will be viewed as creditors in relatively few circumstances. Yet the court does not put bounds on how a regulator will become a creditor, leaving uncertainty in where the line between a creditor and a regulator will be drawn.

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<sup>85</sup> Side note: The Alberta Energy Regulator conceded it was a creditor at the chambers and court of appeal levels. The SCC set out why they disregarded this concession in finding that the AER was not a creditor in this instance. The message: be careful what you concede.

<sup>86</sup> Citing Alberta academics Anna Lund “Lousy Dentists, Bad Drivers, and Abandoned Oil Wells: A New Approach to Reconciling Provincial Regulatory Regimes with Federal Insolvency Law” (2017) 80 Sask. L. Rev. 157, online: Heinonline <https://heinonline.org/HOL/LandingPage?handle=hein.journals/sasklr80&div=10&id=&page> and Fenner Stewart, “How to Deal with a Fickle Friend? Alberta’s Troubles with the Doctrine of Federal Paramountcy” (Toronto: Carswell 2018) Janis P. Sarra & Barbara Romaine, eds, 2017 Annual Review of Insolvency Law, online: SSRN [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3173755](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3173755).

Further the court noted that regulatory orders may not be provable claims in bankruptcy where it is not “sufficiently certain” that the government will undertake the work itself and seek to recover the debt.<sup>87</sup>

## Lingering uncertainty and “untidiness” in the *BIA* and *CCAA*

The *Redwater* decision significantly resets the approach to liability for environmental obligations particularly in relation to provincial oil and gas regulation, but areas of uncertainty persist.

Central areas for “tidying” insolvency legislation include (1) the power to disclaim or abandon property, and (2) the characterization of an environmental obligation as a provable claim versus a public duty.

### **Where lies the ability to disclaim or abandon “onerous” property?**

As highlighted above, the notion that “onerous” properties can be disclaimed or abandoned by an insolvent estate (not to be confused with abandonment of an oil and gas well) is common in other jurisdictions. Federal legislation incorporates this abandonment power in sections 14.06(5) & (6) of the *BIA* (and analogous provisions in s.11.8 of the *CCAA*). The legislation fails to adequately define or give direction to the

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<sup>87</sup> The SCC decision in this regard is of interest on a couple of points. First, there is discussion of whether the Orphan Well Association (OWA), which does abandonment and reclamation work on these sites, should be considered the same as the “regulator” or government in this case. The Court found the OWA was not sufficiently controlled by government to say that OWA actions to abandon and reclaim the oil and gas well sites can be said to be the “regulator” for the purpose of the orders that were issued. This is of likely limited relevance to other situations not involving this specific regulatory framework. The court noted that the regulator can’t “strategically avoid the “sufficiently certain” test simply by delegating environmental work to an arm’s length organization” [para147]. Second, the court noted that even if the OWA was to be viewed as a regulator and abandon the sites that there is “no certainty that a claim for reimbursement will be advanced”. The court went on to note that with the backlog of sites (i.e., the fact that the work was unlikely to be done for a decade) and that there was doubt whether the OWA would advance a claim in any event: both factors pointed to the “sufficiently certain” test not being met. [paras 149-154].

receiver or trustee in relation to the power to assess and disclaim property. Chris Nyberg has noted that:<sup>88</sup>

Parliament has arguably recognized that an act of abandonment [of assets] is inherently an economic decision. Although there is little express consideration of abandonment in the *BIA*, section 14.06(5) of the *BIA* contemplates a stay of proceedings to allow a trustee or receiver time to determine whether it is "economically viable" to comply with an order of a regulator or ministry. Where compliance would result in a benefit to the estate, a court officer would be bound to maximize value and comply with such order. Of course, the corresponding conclusion is that, where it does not make economic sense to comply, the property should be abandoned.

From the perspective of the polluter pays principle, the characterization of property by the trustee or receiver as "onerous" can undercut the obligations of the polluting owner or occupier of property. It represents a pre-insolvency policy failure to recognize the environmental cost of the activity in a timely fashion.

The decision by the majority of the court in *Redwater* brings into question the power of a trustee/receiver to disclaim or abandon property where the environmental costs exceed the asset value. The decision was focused on the narrow context of s.14.06 and was done without fully addressing the "disclaimer" power at common law or the divesting of interests in property under section 20. The majority of the SCC wrote:<sup>89</sup>

s. 14.06(4)'s scope is not narrowed to a "disclaimer" in its formal sense. Under s. 14.06(4)(a)(ii), a trustee is not personally liable for an environmental order where the trustee "abandons, disposes of or otherwise releases any interest in any real property". ***This appeal does***

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<sup>88</sup> Chris Nyberg, *Economic Triage: The Abandonment of Property in Insolvency* (August 2017) Research paper prepared for the Canadian Association of Insolvency and Restructuring Professionals in fulfillment of the Eleventh Annual Lloyd Houlden Fellowship, at 22, online <https://cairp.ca/media/144451/11th-lloyd-houlden-memorial-research-fellowship-paper-eng-final.pdf>.

<sup>89</sup> *Redwater*, *supra* note 1 at para 87.



**not, however, require us to decide what constitutes abandoning, disposing of or otherwise releasing real property for the purpose of s. 14.06(4), and I therefore leave the resolution of this question for another day. Nor does this appeal require us to decide the effects of a successful divestiture under s. 20 of the BIA.** Section 20 of the BIA was not raised or relied upon by GTL as providing it with the authority to walk away from all responsibility, obligation or liability regarding the Renounced Assets.

[Emphasis added]

The court later notes,<sup>90</sup>

Accordingly, regardless of whether GTL is properly understood as having “disclaimed”, the result is the same. Given that the environmental condition or damage arose or occurred prior to GTL’s appointment, it is fully protected from personal liability by s. 14.06(2). However, “disclaimer” does not empower a trustee to simply walk away from the “disclaimed” assets when the bankrupt estate has been ordered to remedy any environmental condition or damage. The environmental liability of the bankrupt estate remains unaffected.

The dissenting decision observed that the majority was fundamentally rejecting the right of the receiver to disclaim onerous property.<sup>91</sup> Justice Côté notes:<sup>92</sup>

Section 14.06(4) both assumes and relies on the common law power of trustees to disclaim assets, a power that the majority of the Court of Appeal described as “commonplace” (para. 47). Even my colleague appears to accept that this disclaimer power “predates” s. 14.06(4) itself (at para. 95). Indeed, the majority of the Court of Appeal recognized that “[s]ection 14.06 does not appear to create a right in a trustee to

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<sup>90</sup> *Ibid* at para 100.

<sup>91</sup> *Ibid* at paras 207-209.

<sup>92</sup> *Redwater*, *supra* note 1 paras 195 & 196.

abandon properties without value, but rather assumes that one exists upon bankruptcy” (para. 63). This is the only rational explanation for why Parliament made the effects of s. 14.06(4) available when the trustee “abandons, disposes of or otherwise releases any interest in any real property”.

...

The majority asserts that s. 14.06(4) does not allow a trustee to “walk away” from assets and the environmental liabilities associated with them (paras. 86, 100, and 102). However, disclaiming property does have precisely this effect. It permits the trustee not to realize assets that would provide no value to the estate’s creditors and whose realization would therefore undermine the trustee’s fundamental objective. A recognized purpose of the disclaimer power is to “avoid the continuance of liabilities in respect of onerous property which would be payable as expenses of the liquidation, to the detriment of unsecured creditors” (Goode, at p. 200 (footnote omitted)). These principles are no less valid in relation to valueless real property than they are in relation to unprofitable and burdensome executory contracts. Indeed, there has been no suggestion in this appeal, including from the AER and the OWA, that trustees can never disclaim onerous real property.

The right to abandon and disclaim certain onerous property (or obligations) by an insolvent estate had evolved to be an accepted aspect of the common law, but the nature and framing of the right is not clear. As environmental awareness and expectations have evolved the nature and extent of these rights warrant clarification through codification.

A review of this right in *New Skeena Forest Products Inc., Re v. Don Hull & Sons Contracting Ltd.*, illustrates the lack of determinative statement of this disclaimer right through time: relying heavily on presumed adoption of the rights of trustees under British bankruptcy legislation prior to 1869.<sup>93</sup>

Insofar as the disclaimer and abandonment rights are implied by section 14.06 and otherwise presumed to remain in the common law the *Redwater* case leaves some uncertainty; i.e. the disclaimer was deemed not to alleviate the estate of its obligations and yet the common law right was not directly repudiated. Further the rights under section 20 of a trustee to divest property and whether this divestment allows for avoidance of environmental obligations remains unaddressed.

The *Redwater* decision creates an apparent attachment of the liability to the insolvent estate. This on its face elicits a positive response as environmental liabilities are not immediately shifted to the public purse (or in the case of oil and gas in Alberta to the Orphan Well Association). Further the decision overcomes the constraints inherent in the framing of the Crown super-priority and its linkage to the environmental impaired property. From a perspective of seeking environmental redress by the polluter it makes sense that when a polluter can no longer pay, those who most closely benefited from the activity be next in line to pay, i.e., the creditors. This has the benefit of forcing creditors to evaluate risks through a different lens, particularly where activities have clear and concrete reclamation and abandonment costs and where “accidental” pollution is likely.

Yet environmental liabilities may continue to accrue to the public purse in some circumstances. Secured creditors may simply write off their debts rather than engage in any insolvency proceeding (whether bankruptcy or restructuring). Each circumstance will vary but creditors may forego any return rather than maintain the debtor creditor relationship when there is no opportunity of a return on its initial outlay of capital. Creditors will be cognizant of the net benefit of initiating the receivership process and will consider whether they simply walk away instead. In those instances, there is minimal value in the new state of the law brought about the *Redwater* case.

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<sup>93</sup> 2005 BCCA 154 (CanLII), <http://canlii.ca/t/1jzq2> at paras 25 and 26. The case also cites some articles that disputes the nature of this right (at para 30).

When other secured creditors do not seek to apply to have insolvent companies go through bankruptcy, the Crown or its agents may seek the appointment of a receiver in an effort to maximize returns. This has occurred in Alberta when the Orphan Well Association sought to have the insolvent Trident Exploration group of companies placed in receivership.<sup>94</sup> According to a filed affidavit in support of the receivership Trident had estimated their abandonment and reclamation liability at \$329 million and secured lenders were owed \$90 million and had ~1500 wells continuing to produce.<sup>95</sup>

Where property (or an interest in a lease as the case may be) is abandoned or disclaimed the property will typically end up being owned by the Crown.<sup>96</sup>

Clarity around disclaimers or property abandonment is needed to provide greater certainty, not only for environmental protection purposes, but also for creditors and insolvency practitioners.

### **When does an order to carry out a public duty become a provable claim?**

There remains uncertainty as to when a regulator, in their capacity of enforcing an environmental order, will become a creditor for the purpose of insolvency. The challenge remains that regulators may be pushed towards a position as creditor or pulled to be a regulator in a given instance, depending on the circumstances of the case. The “untidy intersection” complicates the provincial regulator’s navigation

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<sup>94</sup> In this case over 4400 sites were the subject of an AER order requiring the transfer of the wells, facilities or pipelines or the posting of over \$250 million dollars in security. See Affidavit of Lars De Pauw sworn May 2, 2019, online: PricewaterhouseCoopers [https://www.pwc.com/ca/en/car/trident/assets/trident-003\\_050319.pdf](https://www.pwc.com/ca/en/car/trident/assets/trident-003_050319.pdf).

<sup>95</sup> *Ibid.*

<sup>96</sup> The Crown can become the owner of unclaimed personal property by virtue of section 229 of the *Alberta Business Corporations Act* (R.S.A. 2000, c. B-9) (where a corporation is dissolved) and/or the *Unclaimed Personal Property and Vested Property Act* R.S.A. 2000, c. U-1.5 at section 15 and division 2 (part 3).

towards protecting the public purse and the environment. Uncertainty as to when a regulator becomes a creditor may impact the regulatory response.

The majority of the SCC in *Redwater* highlights the ongoing relevance of the past decision of *Northern Badger* case and highlighted the unique facts of *Abitibi* in addressing when a regulator should be viewed as a creditor by the receiver.<sup>97</sup> Citing professors Anna Lund and Fenner Stewart on this point, it was noted that all three parts of the test from *Abitibi* should mean something.<sup>98</sup> Therefore, it appears that a line is to be drawn as to when a regulator is really acting as a creditor and should not be a default assumption. The SCC has noted “There may very well be situations in which regulator’s action fall somewhere between those in *Abitibi* and those in the instance case”, notably where a regulator has undertaken some “environmental work itself”.<sup>99</sup>

So when does a regulator become a creditor? The *Redwater* decision indicates two instances in which regulators will be clearly viewed as creditors:

- 1) where government will realize a financial gain in the property that is subject to the order (as was the case in *Abitibi*), or
- 2) where they have incurred costs to undertake environmental work itself.

Other instances where they might be viewed as creditors remains uncertain. If it is only the two instances stated above (which is arguably implied in the decision) then the “sufficiently certain” test becomes of limited relevance: either the regulator is acting in a way to enrich itself at the expense of other creditors (i.e., it is simply trying

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<sup>97</sup> *PanAmericana de Bienes y Servicios S.A. v Northern Badger Oil & Gas Ltd.*, 1991 ABCA 181 (CanLII), 81 Alta LR (2d) 45, 117 AR 44, leave to appeal denied [1992] 1 SCR.

<sup>98</sup> *Redwater supra* note 1 at para 123. See Anna J. Lund “Lousy Dentists, Bad Drivers, and Abandoned Oil Wells: A New Approach to Reconciling Provincial Regulatory Regimes with Federal Insolvency Law” (2017) 80 Sask. L. Rev. 157 and Fenner Stewart, “How to Deal with a Fickle Friend? Alberta’s Troubles with the Doctrine of Federal Paramountcy” (Toronto: Carswell 2018) Janis P. Sarra & Barbara Romaine, eds, *2017 Annual Review of Insolvency Law*.

<sup>99</sup> *Ibid* at para 135.

to upset the purpose of the *BIA* by avoiding the creditor label), the sufficiently certain test is not engaged, or the government has already undertaken some work (i.e., it is certain that a debt then exists). This illustrates again that perhaps the test itself requires revision. Alternatively, Parliament should bring clarity to the issue through codifying the distinction between a public duty and provable claim. This approach is advocated by Professor Jassmine Girgis who notes that “courts agree on the test itself but there is little agreement on how it applies to the facts”.<sup>100</sup>

The current state of the law may cause problems for regulators. There may be instances where a regulator seeks, in the face of a firm’s inaction on a matter of environmental concern, to remedy part but not all of the environmental obligations, i.e., the regulator may choose to be a creditor in one aspect and enforce a public duty in another. For example, it is reasonable that a regulator may take measures to remedy ongoing contamination of ground or surface water in the face of a firm’s inaction but leave other obligations related to decommissioning and reclaiming the site to the owner.

The uncertainty of how the regulator is characterized in *Abitibi* and *Redwater* may (and perhaps should) cause governments pause to proactively address contaminated sites where the financial capacity of the firm is low and their secured debts come near to but not over the value of the property. It may be better for government to maintain its role as enforcer of public duties and pass on the cost to creditors. Then again, if it appears a creditor and the insolvent party are both likely to simply walk away, it may be more prudent for the government to be viewed as a creditor depending on the value of the estate.

Where a role of enforcing a public duty is maintained by government, environmental obligations will remain. This in turn elevates the need for clarity in the ability to disclaim or abandon onerous property and may increase the likelihood that the property will just be forsaken (i.e., abandoned).

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<sup>100</sup> Jassmine Girgis “Lessons from Redwater: Discard the AbitibiBowater test and Legislate Super Priority for the Regulator”, online: ABlawg <https://ablawg.ca/2019/03/01/lessons-from-redwater-discard-the-abitibibowater-test-and-legislate-super-priority-for-the-regulator/>.

## Other matters of concern

### **Frustration of environmental orders through corporate restructuring, disclaimer and staying of proceedings**

The viewing of an order as a “provable claim” has further implications for restructuring under the *Companies’ Creditors Arrangement Act*. Specifically, where regulators have previously tried to mandate remediation, a stay against any claim or proceedings and subsequent abandonment of onerous property can effectively shift the polluter pays principle to a public liability.<sup>101</sup> While the CCAA limits the staying of investigations and other regulatory orders it still may be stayed where it is viewed as a “provable claim” or where the court determines the stay should apply.<sup>102</sup>

While the primary issue remains disclaiming or abandonment of onerous property, there remains the ability to frustrate ongoing regulatory attempts to have remediation work continued during and following a restructuring. This is a concern where the net estate may have significant value but specific properties might be assessed as “onerous”.

In the Ontario CCAA related case of *Re Northstar Aerospace, Inc.*, a CCAA judge approved “the agreement for sale of substantially all of Northstar’s assets...[and] Northstar advised the [Ministry of Environment] MOE that if the sale of assets were approved, its intention was to abandon the site and terminate the remediation work”.<sup>103</sup> The MOE opposed a stay of an environmental order in relation to contaminated property.<sup>104</sup> Adopting the SCC approach in *Abitibi* the CCAA judge found:

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<sup>101</sup> See ss11.1 and 11.02.

<sup>102</sup> See s. 11.1(3).

<sup>103</sup> *Northstar Aerospace Inc. (Re)*, 2013 ONCA 600 (CanLII), <http://canlii.ca/t/g0sdk> at para 7.

<sup>104</sup> *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36. Section 11.8 of the CCAA is analogous to s.14.06 of the *BIA*. A stay of the orders related to environmental damage or condition may be granted under s.14.06(5).

“the MOE is entitled to file a claim against Northstar for any costs of remedying the environmental condition at the Cambridge Facility. However, the MOE is not entitled to attempt to use the March 15 Order to create a priority that it otherwise does not have access to under the legislation.”<sup>105</sup>

On appeal the Ontario Court of Appeal noted “as far as the MOE Orders against *Northstar* are concerned, its commencement of the work in the circumstances of this case establishes that the MOE Orders are in substance a claim provable in the insolvency.”<sup>106</sup>

Even where property is not disclaimed the transfer of the onerous property during a restructuring may pose additional challenges for enforcement by virtue of the structure of the sale and the nature of provincial or territorial law and its treatment of successors in title. This can be an issue where provincial laws focus on the “polluter” and the release of substance rather than ownership of the property and control of substances, i.e., the provincial liability system for successors or assignees of polluter or un-reclaimed property matters.

For example, if during operations company A released a substance onto a property that is then the subject of a restructuring proceeding and the land is sold to company B there is a need to ensure that regulatory powers are not solely focused on the release of the substance, as company A is now out of the picture. Successors in title, while at common law are predominantly governed by a buyer beware system, regulatory responses may be limited, complicated or curtailed.<sup>107</sup>

While provincial laws often cover scenarios of successor property owners there remains significant financial rationale for new owners of sites to fight all aspects of environmental orders.

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<sup>105</sup> *Supra* note 103 at para 66.

<sup>106</sup> *Ibid.* at para 22.

<sup>107</sup> This can become even more complicated where contamination is migrating off or on to adjacent parcels as regulators may be hesitant to hold a new owner responsible for an extensive clean up if the original source of the contamination was not of their doing.



This can be seen where regulatory and policy positions of government differ from those of the landowner and where enforcement approaches vary through time.<sup>108</sup> Enforcement challenges may include: access to documents of the polluting company, continuity in compliance approaches, further shifting of assets post transfer, and the use of corporate structures to limit current and future liability.<sup>109</sup>

### **Discharge of a bankrupt – survival of debts**

Where an individual is found to have caused contamination and the Crown has incurred costs to undertaken remedial activities the question becomes whether that individual should have that debt nullified through the discharge process under the *BIA*. An order of discharge releases the bankrupt from “all claims provable in bankruptcy” except those that survive by virtue of s.178 of the *BIA*.<sup>110</sup> The types of debts that will survive bankruptcy include family support obligations, debts arising as fines or orders imposed by a court in respect of an offence, certain debts related to fraud and misrepresentation, and certain debts related to student and apprenticeship loans.<sup>111</sup> For the latter education related debts the Act provides an opportunity to apply to the court following five years after being a student or apprentice to have those debts also removed.<sup>112</sup>

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<sup>108</sup> See, for example, *Cherokee Canada Inc. et al. v. Director Regional Compliance, Red Deer North Saskatchewan Region, Operations Division, Alberta Environment and Parks* (26 February 2019), Appeal Nos. 16-055-056, 17-073-084 and 18-005-010-R (A.E.A.B.), online: <http://www.eab.gov.ab.ca/dec/16-055-etc.-Cherokee-R.pdf>. See also *Sears Canada Inc. et al. v. Director, Regional Compliance, South Saskatchewan Region, Alberta Environment and Parks* (3 February 2020), Appeal Nos. 17-069-070 and 18-013-R (A.E.A.B.), 2020 ABEAB 6.

<sup>109</sup> See for example the case of Gas Plus which was ordered to clean up petroleum tank leak and subsequently sold the property and shifted assets, as reported in Calgary Herald, Taxpayers face \$4.3-million bill after gas station owner fails to clean up” September 9, 2015 , Matt McClure <https://calgaryherald.com/news/local-news/taxpayers-face-4-3-million-bill>.

<sup>110</sup> See s179(2).

<sup>111</sup> See s178.

<sup>112</sup> See s178(1.1)

The policy question to be addressed: should individual polluters be able to avoid liability for their actions through bankruptcy? There are clear policy reasons why this should not be allowed and as such environmental liabilities should not be discharged. To manage for undue hardship in the longer term the ability to seek relief from the debt at some future time could be included.

## Recommendations for Reform of the *BIA* and *CCAA*

The court in *Redwater* noted that Parliament may want to “re-examine s.14.06 during its next review of the *BIA*”.<sup>113</sup> The challenge with the phrasing of 14.06 lay, in part, in a conflict between the plain language about “personal liability” of the receiver and how that subsection could be interpreted when read in conjunction with related subsections that implicated broader considerations of the estate of the insolvent party.

The ELC recommends several reforms to 14.06 but also to other areas of the statute. Where the *CCAA* is analogous, similar amendments can be assumed. The fundamental purpose of the recommendations is to codify environmental protection as a public duty and to uphold the polluter or beneficiary pays principle.

## Bringing clarity in determining the scope of public duties

Fundamental to the challenges in the *Redwater* and *Abitibi* case law is the scope of the determination of when a regulator or government will be considered a creditor or a protector of the environment. This determination, barring court intervention or direction, continues to rely significantly on the decision of the receiver with the oversight of the court. The determination has direct policy implications beyond the scope of the *BIA* and it is not a role that a receiver should be forced into; it is not in their mandate nor is there regulatory guidance to make this determination. As highlighted above, the purpose of bankruptcy legislation is quite limited. The

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<sup>113</sup> *Redwater*, *supra* note 1 at para 72.

numerous other public duties with financial linkages are often at odds with an environmental protection mandate.

Sections 14.06(8), 121, and 135 are implicated in the determination of when claims or contingent claims for environmental condition or damages are provable claims under a bankruptcy proceeding. In this regard, the current focus of the legislation, setting aside the impact of the *Redwater* case for a moment, is to effectively force environmental related orders to be viewed as provable claims in insolvency proceedings (whether in bankruptcy or in restructuring under the CCAA).

The ELC recommends removing the determination of whether an order is a provable claim from the initial determination made by the trustee/receiver. The ELC also recommends providing an opportunity for the issuing agency to monetize an order, by electing to have a public obligation treated as a provable claim, if they so choose (the process for which should be detailed in the general rules). This approach removes confusion regarding the “sufficiently certain” test that the trustee/receiver must use to determine contingent claims for environmental claims.

The recommendations of reform to the BIA that follow recognize that the role of public duties and regulatory enforcement of environmental laws are best treated separate and apart from the general administration of the estate.

## Reforms to “tidy” the intersection

The potential conflicts that arise in insolvencies are, by and large, focused on when provincial regulatory action frustrates the equitable distribution of assets to creditors. Because almost any regulatory action costs money, this area of the law should be clarified.

The “tidying” of the intersection between regulator and creditor is complicated by the fact that the regulator may, in fact, validly be characterized as creditor and regulator, sometimes in the same instance. There are various circumstances in which a regulator may be forced to undertake remedial work of certain types (such as in instances to address imminent threats to property or human health) versus other types of environmental harm or damage where a regulator may choose to proceed by way of regulatory order. Assuming then that the distinction between creditor and

regulator remains relevant, the next question is what criteria or process should be used to make the distinction.

Clearly, in Alberta, the potential for the government to become a creditor is embodied in the province's environmental laws. The Alberta government has the power to enter onto lands to undertake remediation and reclamation activities. The Director under the *Environmental Protection and Enhancement Act* (EPEA) may undertake whatever "action the director considers necessary to carry out the terms of the enforcement order".<sup>114</sup> A claim related to these costs rank "above any other claim, right or charge against the land, notwithstanding any other law of Alberta."<sup>115</sup> It is worth noting that the debt so created is once again secured against specific land, and hence it faces the similar risk of being underfunded (where the costs of remediation are higher than the property value) or disclaimed. (Alternatively, parties may attempt to avoid liability by spinning off assets to another company, leaving a shell.<sup>116</sup>)

Similarly, in addition to its power under *EPEA*, the AER has the power to take action related to "escaped substances" under the *Oil and Gas Conservation Act* s.104(1). Also, where a well or facility is "suspended or abandoned" by the Regulator those costs are payable to the regulator.<sup>117</sup>

Any effective environmental legislation must enable government to undertake actions where there is polluter or firm malfeasance or negligence and seek remedial, punitive and civil remedies as it may be entitled. The public purse should be made whole where government is forced to expend funds to remediate harms of a polluter. While the *Redwater* case mitigates some of the concerns of regulators being viewed

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<sup>114</sup> See *Environmental Protection and Enhancement Act*, R.S.A. 2000, c. E-12 at s 214 (re enforcement order) and s.245 (Re environmental protection order).

<sup>115</sup> *Ibid.* at s 216.

<sup>116</sup> See for example the case of GasPlus where the regulator took over a property and other assets were allegedly sold earlier. See Calgary Herald, "Taxpayers face \$4.3- million bill after gas station owner fails to clean up", September 9, 2015.

<sup>117</sup> *Oil and Gas Conservation Act*, R.S.A., C. O-6 at ss 28-30.

inherently as creditors it remains problematic that the underlying nature of the test remains a focus of whether and if the work can create a debt under legislation.

The wording of the *BIA* related to the super-priority clearly articulates that Crown claims for remedying the environmental condition of property constitutes a claim that “ranks above any other claim”. But this is all for naught if onerous property can be disclaimed, effectively divorcing profitable or valuable properties from environmental obligations. By requiring the estate to meet the environmental obligations prior to any disclaimer the law can act to expand the scope of due diligence by creditors.<sup>118</sup>

Finally, the question of who should determine what role a government or its regulatory agent is playing is part of the policy deliberation. Should the insolvency process defer to a determination of roles driven by the provincial regulators’ perspectives or should the insolvency process maintain the role of trustees and receivers in determining the nature of a public duty versus a creditor? As it stands now (since *Grant Thornton*) there is a line, blurry, but still a line, where a regulator will become a creditor, and it appears to be, at least in part, within the control of the provincial regulatory agent.

### **Crown election or declaration of public duty or debt**

The ELC recommends a novel approach could be pursued where the *BIA* sets out a process where a provincial agency may declare or elect, as part of the insolvency proceeding, how an obligation should be treated; as a debt or a public duty.<sup>119</sup> This

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<sup>118</sup> Professor Jassmine Girgis notes in her blog “Lessons from Redwater: Discard the *AbitibiBowater* test and Legislate Super Priority for the Regulator. “Super priority internalizes the cost of environmental cleanup by the debtor by altering its behavior throughout its operations. By knowing about the Regulator’s super priority position *ex ante*, secured creditors will be more particular about lending money and if they do lend, they will ensure their lending agreements have the appropriate protections. Debtors will be required to show they are able to bear the costs of environmental remediation before the secured lenders extend credit, and, once credit is extended, creditors can ensure debtors operate responsibly and clean up as they go by monitoring the debtor’s activities. <https://ablawg.ca/2019/03/01/lessons-from-redwater-discard-the-abitibibowater-test-and-legislate-super-priority-for-the-regulator/>.

<sup>119</sup>While not directly analogous there are various instances where there is reliance on provincial regulators, including provincial support guidelines substituted impact assessments under the *Impact Assessment Act*, S.C. 2019, c. 28, s. 1.

would reflect a significant shift in bankruptcy law and a unified approach of merging insolvency proceedings and environmental protection proceedings.

For the purposes of this approach, there would be an application process set up to allow provincial and territorial governments and relevant regulators to characterize their action as a “claim” or as an enforcement obligation within a prescribed time upon the filing a proposal or the date of bankruptcy. The process may include provisions articulating rebuttable presumption of the government’s role, whereby those adversely affected by the declaration or election can bring evidence that the government’s actions are properly assessed as a provable claim (and the regulator is a creditor). This may be accomplished by including a presumption within the *BIA* that if the Crown does not elect to participate in the bankruptcy then the related order will not be treated as a provable claim. This would be analogous to how secured creditors may elect to not take part in a bankruptcy proceeding but with the added clarity that public duties will not be treated as a provable claim.

The process would require a court’s decision to affirm or amend the characterization of the obligation, directed by a list of circumstances where a provable claim may be justified, for example, where the order is lacking of merit or there is evidence of ulterior purposes. This process could also include mediation and creditor agreements with regulators.

The benefit of this latter approach is to enable the provincial government to assess the best financial and environmental outcomes of a given situation.

## **BIA amendments**

**The BIA should be amended by providing a standalone part for orders related to environmental condition or damage. This part of the BIA would include:**

- **the process for the declaration by the government agency to be a creditor,**
- **provisions outlining the nature of the rebuttable presumption, and**
- **the court approval process and related criteria to guide the court's discretion.**<sup>120</sup>

## **Bringing clarity to abandonment/disclaimer rights**

The effect of the majority decision in *Redwater* is that environmental clean-up orders (that are not provable claims) can remain as an obligation of the estate. This can occur notwithstanding s.14.06 of the BIA. Abandonment and disclaimer powers remain unclear as does the relevance of section 20 divestiture of property interests by a trustee in relation and their related impacts on environmental obligations.

The policy choice at play here is significant. Should the concept of “onerous property” exist in Canadian law? The ELC recommends that Canada lead commonwealth nations by linking bankrupt estates to environmental liabilities notwithstanding the change of ownership of property that occurs during the insolvency process. By implication this would require resolving the matters related to an environmental order prior to the discharge of the bankrupt, and more significantly, prior to any divestment of property that would impact the ability of the estate to address the environmental condition or damage. It also requires clarifying language in section 20.

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<sup>120</sup> Coinciding amendments to the General Rules would be needed to facilitate this approach. See [https://laws-lois.justice.gc.ca/eng/regulations/C.R.C.,\\_c.\\_368/index.html](https://laws-lois.justice.gc.ca/eng/regulations/C.R.C.,_c._368/index.html) and application of section 135 of contingent claims (specifically section 135(1.1)).

**BIA amendment: Divesting of property (including through abandonment or disclaimer) of an insolvent estate cannot occur until environmental obligations have been met.**

**This includes amendments to the BIA regarding:**

- 1. A new section prescribing the limitations on divestment of property of the insolvent estate (including disclaimers) while there is existing order regarding the environmental condition or damage of the insolvent estate's property; and**
- 2. Proposed approach for section 20:**
  - a. s.20(3) Where a trustee seeks to divest all or any part of the trustee's right, title or interest in any real property or immovable of the bankrupt under this section and an order related to the environmental condition or damage of the property in question remains in force, the divestiture under this section will not have any force and effect until such time as compliance with the order has been achieved.**
  - (4) Proof of compliance with the order must take the form of written confirmation from the enforcing government, regulatory agency or body, in a form provided for in the General Rules for this purpose.**

**Proposed approach to CCAA:**

**Amend section 6 (3) to include restrictions on court sanctioning of compromises and agreements under the section.**

**s.6(3.1)** Unless Her Majesty agrees otherwise, the court may sanction a compromise or arrangement only if the compromise or arrangement provides for the payment in full to Her Majesty in right of Canada or a province, within six months after court sanction of the compromise or arrangement, of all amounts that were outstanding related to costs of remedying any environmental condition or environmental damage affecting real property of the company.



## Clarifying section 14.06

The SCC decision in *Redwater* pointed to this section as requiring potential amendment for additional clarity. In light of the above amendments two provisions of s.14.06 can be removed. Inoculating trustees and receivers from personal liability remains a valid outcome and remains in s.14.06(2).

### ***BIA* amendment**

**Repeal section 14.06(4) and (5). Insofar as the role of the receiver has been fundamentally altered by other recommended amendments these provisions would serve little further purpose.**

**The analogous provision of s.11.8 of the CCAA can also be repealed.**

## Environmental debts surviving bankruptcy

The bulk of this report and the recommended reforms are focused on insolvent corporations. Environmental debts will not survive a bankruptcy where the insolvent party is a corporation as dissolution typically follows insolvency. On the other hand, where an individual has incurred a debt to the Crown for remediation of environmental damage that the bankrupt is responsible for, the debt is nullified when the bankrupt party is discharged.

Should environmental debts of individuals survive bankruptcy? The polluter pays principle would answer “yes”, whereas the purpose of bankruptcy law of providing the debtor a clean slate would answer “no”. The *BIA* does highlight areas where, for policy reasons, certain debts are not discharged. It is proposed that environmental debts should survive bankruptcy for a specified period (similar to other exceptions under the *BIA*).

**BIA amendments**

**A debt owed to the Crown for the purposes of remedying an environmental condition or damage should be included in sections 178(1) and 178(1.1). After a specified time (e.g. five years) the debtor should be able to seek a court order to not have the debt continue due to financial hardship (under section 178(1.1)).<sup>121</sup> In this regard, the amendment should recognize that the extension of environmental liability should not impair the ability of the bankrupt to pay the debts related to family obligations and criminal restitution, and thus provincial debt repayment priorities may need to be adjusted.<sup>122</sup>**

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<sup>121</sup> This would be similar process to current treatment of student loans and apprenticeship loans under s.178(1.1).

<sup>122</sup> For example, see the *Maintenance Enforcement Act* gives priority to maintenance orders over “unsecured judgment debts”. *Maintenance Enforcement Act*, R.S.A. 2000, c. M-1 at s.20.