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Orphan Well Association v Grant Thornton Ltd: The Supreme Court Pivots on the Enforceability of Environmental Claims in Bankruptcy

The Supreme Court of Canada today released its long-awaited decision in *Orphan Well Association v Grant Thornton Ltd*. The Court reversed a decision of the Alberta Court of Appeal that allowed the trustee of a bankrupt oil and gas company to sell its profitable wells and disclaim unprofitable ones, leaving the public to bear the end-of life liability associated with those wells. The result is a decision that clarifies the relationship between provincial environmental law and the federal regime of bankruptcy and insolvency. However, it does so in a way that may open up greater scope for the operation of provincial laws of general application in bankruptcy. In this respect, the decision could have wide implications, not simply for the fate of environmental claims in bankruptcy, but also for other claims having special protection under provincial law, such as employee, pension, and construction lien claims.

The *Orphan Well Association* case concerned the regulatory regime applicable to oil and gas properties in Alberta. Under that regime, for the purposes of assessing a company's responsibility to manage the clean-up obligations connected with the end of an asset's useful life, all the licences held by a given company are treated as a package, without any segregation or parcelling of assets. Outside of bankruptcy, a company could not monetize its profitable assets without accounting for the liabilities attached to its unprofitable ones.

Today's decision concerned whether principles of paramountcy allowed the *Bankruptcy and Insolvency Act* to permit a trustee of a bankrupt company to do what the bankrupt could not. Specifically, the issue was whether a trustee in bankruptcy could exercise its powers under subsection 14.06(4) of the *BIA* to disclaim the company's unprofitable oil and gas properties and sell the profitable ones for the benefit of the bankrupt's secured creditors, leaving unsatisfied the balance of the net

liabilities associated with the remaining assets. Under Alberta law, such a sale was not possible, since the energy regulator would not approve a transfer of licenses associated with the profitable wells without accounting for the liabilities attached to the company's entire portfolio of assets.

A majority of the Supreme Court held that the Alberta licensing regime applied notwithstanding the company's bankruptcy. The majority recognized that the oil and gas licensing regime chosen by Alberta makes the environmental costs of operating oil and gas assets an inherent part of the value of the licensed assets. This regime, the Court held, has the advantage of aligning with the polluter-pays principle, a well-recognized tenet of Canadian environmental law.

The trustee and the secured creditors, however, argued that the trustee's disclaimer right under section 14.06(4) of the *BIA* permitted the trustee to preserve the value of the company's profitable assets for the benefit of the company's secured creditors even though that value—unencumbered by the end-of-life obligations associated the company's entire portfolio—could never have been unlocked by the company outside of bankruptcy. As federal legislation, these parties argued, the BIA nevertheless displaced the operation of the provincial scheme because of the doctrine of paramountcy.

The majority rejected these arguments, holding that there was in fact no conflict between the BIA and the provincial licensing scheme. The trustee identified two alleged conflicts: the conflict between the provincial licensing scheme and the trustee's power to disclaim property under subsection 14.06(4); and the conflict said to be occasioned by the satisfaction of unsecured environmental claims ahead of the claims of the bankrupt's secured creditors, which would have first priority under the scheme of distribution under the BIA.

The majority held that neither alleged conflict existed. The Court interpreted the disclaimer right under subsection 14.06(4) as being directed primarily at protecting the trustee from personal liability, and not at relieving the bankrupt's estate of liabilities associated with its property.

No conflict existed either with the scheme of distribution under the BIA. Clarifying the test established by the Court in its earlier decision in *Newfoundland and Labrador v AbitibiBowater Inc*, the majority affirmed that the Alberta regulatory authority was

not a creditor when it enforced the regulatory regime to require the portfolio of the bankrupt's assets to bear the end-of-life liabilities associated with them. Significantly, the Court stressed that an environmental regulator is not a "creditor" for the purpose of assessing the status of an environmental liability in bankruptcy where it does not stand to benefit financially, and where it exercises its enforcement powers in the public interest. Given this, the Alberta scheme did not conflict with the federal scheme of distribution in bankruptcy because it was not designed to elevate the claim of one creditor over another in a manner inconsistent with the BIA.

The dissenting judges (Côté and Moldaver JJ) criticised the majority's approach as elevating form over substance, and specifically criticised the majority's effort to interpret the BIA harmoniously with the provincial scheme, noting that where a provision "cannot support a harmonious interpretation, it is beyond a court's power to create harmony where Parliament did not intend it."

The result in *Orphan Wells* is a significant pivot away from the Supreme Court's treatment of environmental claims in *AbitibiBowater*. Moreover, the majority's efforts to reconcile the provincial environmental regulatory scheme with federal legislation signals a greater focus on the *BIA* as being at its core a procedural statute. Under that framework, the *BIA* should work harmoniously with provincial legislation defining the substance of creditors' rights, unless there is no way to reconcile the two.