MERCURY OILS LIMITED (DEFENDANT) ..... APPELLANT;

AND

VULCAN - BROWN PETROLEUMS LIMITED (PLAINTIFF) ..... RESPONDENT.

1942

*May 13, 14, 15.

*Dec. 24.

ON APPEAL FROM THE APPELLATE DIVISION OF THE SUPREME COURT OF ALBERTA

Gas and oil leases—Effect upon lease of subsequent legislation preventing performance of a condition—Whether lease frustrated—Constitutional law—Validity of Oil and Gas Wells Act, Alberta, 1931, c. 46.

The appellant held under a lease from the owner "the right and interest of the lessor in all the petroleum" in a certain parcel of land. The respondent held under a prior sublease the petroleum and natural gas

*PRESENT:—Rinfret, Kerwin, Hudson and Taschereau JJ. and Gillanders J. *ad hoc*.

(1) [1923] A.C. 695.

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rights in the same parcel of land. Under the last agreement, it was agreed that the respondent should drill an oil well within a certain time, and within twelve months after completion of the first well it would drill a second well and that, in default of so doing, it should be deemed to have abandoned the property, except the first well and the five acres surrounding it, and the appellant was to be entitled to re-enter. The respondent drilled the first well, but did not drill the second well owing to the fact that certain regulations under *The Oil and Gas Wells Act*, Alberta, 1931, c. 46, enacted after the execution of the lease, prohibited the drilling of a well within 440 yards of any producing well. The effect of these regulations was to make it impossible for the respondent to drill a second well on a forty-acre plot such as was covered by the lease. The respondent brought an action for a declaratory judgment that there was no default or abandonment and that its rights in the premises still continued. The trial judge held that the respondent was entitled to the declaration as claimed and a majority of the appellate court affirmed his decision.

Held that the judgment appealed from ([1942] 1 W.W.R. 138) should be affirmed. When all the provisions of the sublease agreement are read together, it cannot be said that the respondent was in default within the contemplation of the particular clause providing for the drilling of the second well.

The Oil and Gas Wells Act, Alberta, 1931, c. 46, is not *ultra vires* of the provincial legislature.

APPEAL from the judgment of the Appellate Division of the Supreme Court of Alberta (1), affirming the judgment of the trial judge, Shepherd J. (2), and maintaining the respondent's action for a declaratory judgment.

The material facts of the case and the questions at issue are stated in the above head-note and in the judgment now reported.

S. J. Helman K.C. for the appellant.

George Steer K.C. for the respondent.

W. S. Gray K.C. for the Attorney-General for Alberta, intervenant.

The judgment of Rinfret, Kerwin, Hudson and Taschereau JJ. was delivered by

HUDSON J.—This is an appeal from the judgment of the Appellate Division of the Supreme Court of Alberta which, by a majority of four to one, dismissed an appeal from a judgment of Mr. Justice Shepherd awarding the plaintiff a declaration as claimed in its statement of claim.

(1) [1942] 1 W.W.R. 138; [1942] 1 D.L.R. 209.

(2) [1941] 3 W.W.R. 384; [1942] 1 D.L.R. 210.

The material facts in the case are not in dispute. They are fully set forth in the judgments below.

Briefly, the defendant appellant holds under a lease from the owner

> the right and interest of the lessor in all the petroleum which may be found within or upon a parcel of land consisting of forty acres in the provinve of Alberta.

The plaintiff holds under a prior sublease the petroleum and natural gas rights in the said parcel of land. The lease to the plaintiff provides that the plaintiff as lessee shall pay as a rental or royalty for the premises: (1) twenty per cent of all merchantable products received from the demised premises; (2) a rental of forty dollars per annum payable half yearly; (3) that the lessee should drill a well of a defined character and capacity upon the land; and (4) that within twelve months after completion of the first well it would drill a second well and that, in default of so doing, it should be deemed to have abandoned the property, except the first well and the five acres surrounding it.

The plaintiff has fulfilled the first three obligations as above mentioned but did not drill the second well because meanwhile new regulations under *The Oil and Gas Wells Act*, 1931, chapter 46, Alberta, were passed. These regulations made by order in council dated January 11th, 1939, provided that the Board constituted under the Act may prescribe the points at which wells may be drilled, and provided that no person shall commence to drill a well without a licence and that no licence shall be issued for any well at any point which was within 440 yards of any producing well. These regulations ordinarily made it impossible to drill a second well on a forty-acre plot such as was covered by the lease here. The plaintiff respondent applied to the Board for a licence under the regulations to drill a second well on the leased premises but such application was refused.

The defendant appellant (to whom the plaintiff had attorned) took the position that the agreement to drill the second well was absolute, that the plaintiff's failure to drill amounted to a default under the terms of the lease and that it must thereby be deemed to have abandoned its interest in all, except the first well and the five acres surrounding same. The plaintiff respondent thereupon com-

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menced this action claiming a declaration that there was no default or abandonment and that its rights in the premises still continued.

The trial judge held that the plaintiff was entitled to the declaration as claimed and the court of appeal by a majority affirmed his decision.

The clause in the sublease providing for the second well is as follows:

> 28. It is understood and agreed by and between the parties hereto that upon the completion of the first well agreed to be drilled under the terms of this lease, to commercial production or upon the abandonment of the said well, that the lessee shall within a period of four months thereafter commence the actual drilling of another well on the premises hereby demised, *and that in case of default of the lessee in so doing, he shall be deemed to have abandoned the property* hereby demised excepting only that in case the first well hereby agreed to be drilled shall recover commercial production then and in such case the lessee shall be entitled to retain the five acres immediately surrounding the said well and of which the said well shall be the centre; and in case the lessee shall abandon the said well or any part thereof under the provisions of this clause, the lessor shall be entitled to re-enter upon the said premises or such part thereof as shall have been abandoned and the same to have again to repossess and enjoy, anything herein contained to the contrary notwithstanding.

There are several other clauses in the sublease which have a bearing on this question. Clause 9 provides:

> 9. The lessee shall in respect to the premises hereby demised, faithfully and punctually do and perform all covenants and conditions, acts, matters and things as are required in the original lease from The Calgary and Edmonton Corporation Limited, or which may be contained in any regulations from time to time in force or promulgated by any proper authority.

The original lease referred to in this clause 9 contained a provision as follows:

> The lessee shall and will carry on all drilling operations in strict compliance with the statute and regulations and all other provisions of law applicable thereto.

This provision, therefore, must be taken to be incorporated in the sublease. Then, it should be stated that the original lease referred to above was surrendered and a new lease to the defendant appellant substituted therefor. This new lease contained a provision as follows:

> That the lessee shall and will carry on all drilling operations in strict compliance with the statute and regulations and all other provisions of law applicable thereto, also in accordance with the regulations of the Government of the province of Alberta applicable to Crown leases.

Subsequently, by agreement between the lessor, the plaintiff respondent and the defendant appellant, the respondent attorned to and became tenant of the appellant and acknowledged itself to be bound by the covenants and conditions of the said sublease and all amendments thereto and of such assignment.

The position then is that the defendant claims that the plaintiff has made default in not doing something which if done would be contrary to another covenant in the lease and at the same time contrary to a covenant made by the plaintiff appellant in its own lease, and which act if done might jeopardize the defendant's own title.

In view of this paradoxical situation let us next look at two other provisions of the sublease:

8. The lessee covenants and agrees that he will from and after the commencement of drilling operations as herein agreed, carry on such drilling operations continuously thereafter in a skillful and workmanlike manner with competent workmen and efficient machinery and equipment until the said well shall be drilled to commercial production or shall be abandoned, subject only to such interruptions and delays as may occur from causes beyond the control of the lessee, provided that lack of funds shall not be considered a cause beyond the control of the lessee.

16. It is distinctly understood and agreed between the parties hereto that drilling, pumping or other operations for procuring or producing petroleum and natural gas in, upon or from the said premises shall be suspended only in the event that said operations are prevented by causes beyond the control of the lessee and such operations shall be carried on for so long a time as petroleum and natural gas or other products can be produced and marketed at a price that shall be remunerative to the parties hereto.

Reading all of these provisions together as we must, can it be said that the plaintiff is in default within the contemplation of clause 28? I do not think so.

The present is not a case of frustration or of unjust enrichment. There is no total failure of consideration. The plaintiff has paid the money rental in the past and is under an obligation to pay it in the future. The plaintiff is, so far as we know, operating the first well and paying the defendant the royalty on production provided for by the sublease. Nor is it shown that there is any special hardship imposed upon the defendant. It does not appear that the defendant could get a licence to drill where the plaintiff has failed. If the regulations are altered to permit the drilling of another well, then both parties will profit. The defendant will get the royalty and the plaintiff the remaining share of the products.

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Apart from the construction of the contract itself, it was argued that the *Oil and Gas Wells Act* was *ultra vires* of the provincial legislature, and that the order in council establishing the regulations was beyond the power of the Lieutenant-Governor in Council. All of the judges in the courts below have held this argument to be unfounded. With this conclusion I agree.

The title in fee simple passed from the Crown in the right of the Dominion in 1906 and thereafter the provincial legislature had power to legislate in respect of same. The statement of the Chief Justice in the *Spooner* case (1) is quite in accord with this conclusion.

I would, therefore, dismiss the appeal with costs to the respondent, but there shall be no costs in respect of the intervention of the Attorney-General.

GILLANDERS J. (*ad hoc*)—I am of the opinion that the appeal should be dismissed with costs.

Appeal dismissed with costs; no costs as to intervention.

Solicitors for the appellant: *Helman & Mahaffy.*

Solicitor for the respondent: *John W. Moyer.*

Solicitor for the Attorney-General for Alberta: *W. S. Gray.*