Cassels

Yukon Court of Appeal Clarifies Environmental Security and Third-Party Property Rights in Receivership Proceedings

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Introduction

On March 5, 2021, the Court of Appeal of Yukon (the YKCA) released its unanimous decision in *Yukon (Government of) v Yukon Zinc Corporation* (YZC).[1] The decision dispensed with four related appeals from orders of the Supreme Court of Yukon (the YKSC) released on May 26, 2020.

The YKCA proceeding clarified a number of important issues, including the nature of regulatory secured claims for unpaid environmental remediation, the extent to which regulatory "super-priority" environmental claims attach to mineral interests, the ability of a receiver to use and obtain a priority charge over the assets of third-parties, and the ability of receivers to disclaim an agreement and unilaterally impose go-forward terms on a secured party.

While the YKCA expressed sympathy with the difficult position receivers often find themselves in when dealing with environmental remediation, it emphasized the importance of third-party rights and stated that a receivership "is not a license to ignore rules, and insolvency professionals are bound by and must comply with valid provincial laws" during receivership.

Background

In September of 2019, on application by the Government of Yukon, the YKSC appointed PricewaterhouseCoopers Inc. as receiver (the Receiver) of all assets and undertakings of YZC pursuant to the *Bankruptcy and Insolvency Act*[2] (the BIA) and the Yukon *Judicature Act*.[3] A companion proposal proceeding under the BIA was unsuccessful and, accordingly, YZC was also bankrupt.

Prior to the receivership, YZC operated the Wolverine Mine in Yukon. Since 2014, YZC struggled financially due to, among other things, the high start-up costs associated with the mine and the global downturn in metals prices. YZC put the mine into care and maintenance in 2015 and completed a restructuring under the *Companies' Creditors Arrangement Act.*[4] In 2017, the mine suffered a devasting flood. As a result, the Government of Yukon increased the reclamation security required under YZC's mining license from approximately $10 million to over $35 million. This increase was intended to address the increased

environmental risks and the anticipated future costs of environmental remediation. YZC failed to post the increased remediation security.

Welichem Research General Partnership (Welichem), the senior secured creditor of YZC had advanced multiple loans to the company. These loans were secured against all of YZC's assets, including its mineral claims. YZC used a significant portion of the funds advanced by Welichem to purchase the mining equipment at the mine. Subsequently, the company sold the equipment to Welichem and then leased the equipment from Welichem pursuant to a master lease agreement. At the time of the receivership, Welichem was the owner of the equipment.

In the course of the receivership, the Receiver determined that it required the use of some of Welichem's equipment to maintain the mine. However, after the Receiver and Welichem were unable to consensually agree on terms for the Receiver's continued use of the equipment, the Receiver issued a disclaimer of the master lease agreement. Under this disclaimer, the Receiver purported to disclaim the master lease agreement entirely but stated that it intended to continue to use certain items of the Welichem equipment on unilaterally-imposed terms.

Key Takeaways

Claims Provable in Bankruptcy

The Government of Yukon sought a declaration that it had a claim provable in bankruptcy for the amount of the reclamation security that YZC failed to pay. The YKSC found that it did not. The Government of Yukon appealed. The YKCA upheld the YKSC's finding that, for a claim to be provable in bankruptcy, it must be recoverable or enforceable by legal process. The YKCA found that, since section 139 of the Yukon *Quartz Mining Act*[5] does *not* grant the government the ability to recover any unfurnished amounts of the reclamation security by legal process, it did not have a claim provable for those amounts.

Importantly, the YKCA expressed concerns regarding YKSC's jurisdiction to determine this particular issue. The YKCA noted that the provisions of the BIA provide that proofs of claim are to be evaluated by a licenced insolvency trustee in the bankruptcy proceedings. In this case the bankruptcy proceedings were brought in British Columbia and, therefore, the YKCA noted that the Supreme Court of British Columbia likely had jurisdiction. The YKCA cautioned that its decision should not taken as a precedent for bringing an application to a court in a receivership proceeding to evaluate a bankruptcy claim within another court's jurisdiction.

Section 14.06(7) and Mineral Claims

Section 14.06(7) of the BIA grants a government a super-priority charge for the costs it incurs in remediating

the real property of the debtor. That charge is secured against the affected real property and contiguous real property of the debtor. The YKSC found that this priority charge extended to mineral claims. The YKCA overturned this finding.

In its decision, the YKCA applied the modern rule of statutory interpretation and considered, among other things, the various uses of “real property” and “interests in real property” throughout the BIA. The YKCA concluded that in section 14.06(7) the words “real property” do *not* include *interests* in real property and that the YKSC erred in finding that the section 14.06(7) super-priority charge extended to YZC’s mineral claims. This finding will be of material interest in other jurisdictions where mineral claims are interests in real property.

Third-Party Property Rights in Receivership

Welichem challenged the Receiver's disclaimer of the master lease agreement and its continued use of the select Welichem equipment.

The YKCA noted the recent British Columbia Court of Appeal decision in *Petrowest Corporation v Peace River Hydro Partners* where the Court held that a receiver cannot disclaim part of an agreement and that the doctrine of separability “does not form a basis for allowing the receiver freedom to pick and choose among the terms of a contract the receiver seeks to enforce.”[6]

However, the YKCA held that the Receiver in this case had not partially disclaimed the master lease agreement. Rather, it found that the Receiver had disclaimed the master lease agreement in full coupled with “an appropriation by the Receiver of the right to use the Essential Lease Items without complying with any of the terms of the Master Lease at a monthly rent unilaterally determined by the Receiver.” This was found to be without legal basis. The YKCA considered section 72(1) of the BIA which upholds general provincial laws regarding third-party property rights and protections. In addition, the YKCA followed the prior decisions of the Supreme Court of Canada, which found that absent explicit language to the contrary the BIA should not be interpreted to interfere with third-party property rights. Accordingly, the Court held that while section 243 of the BIA permits a court-appointed receiver to take possession and control of an insolvent person’s property, that power does *not* extend to the property of third-parties.

Welichem also appealed the extension of the Receiver’s charge over its equipment. The YKCA interpreted the charging language in section 243(6) of the BIA and found that it was, again, limited to *the property of the insolvent person* and did not grant a court the ability to charge the property of third-parties. Accordingly, the YKCA allowed the appeal on these points.

Conclusion

Mining receiverships pose a number of challenges for both courts and receivers, including balancing the interplay between commercial parties and environmental regulatory regimes and agencies. The decision of the YKCA provides clear guidance that, while there is broad remedial authority to authorise receivers to take necessary action, the general laws of property still apply. As the YKCA noted:

Despite whatever sympathy one may have for the Receiver's position, it is subject to general laws regarding property. To borrow the words of Chief Justice Wagner, for the majority, in *Orphan Well* SCC at para. 160, receivership "is not a license to ignore rules, and insolvency professionals are bound by and must comply with valid provincial laws" during receivership.[7]

This decision provides certainty to parties leasing or financing in the mining sector that their property rights will be respected in an insolvency, and how their claims will rank. In particular, the YKCA has clarified that:

1. Unless recoverable outside an insolvency, a requirement to post reclamation security is not a "claim provable" under the BIA;
2. The section 14.06(7) super-priority for environmental remediation costs is not secured against mineral claims, which is of particular importance where the ultimate property owner is the Crown;
3. The disclaimer by a receiver is a binary choice, and there is no ability for a receiver to unilaterally utilise the assets of a third-party (such as a lessor); and
4. Court-ordered receivership charges can only charge the assets of the debtor, not the assets of third-parties.

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[1] 2021 YKCA 2.

[2] RSC 1985, c B-3.

[3] RSY 2002, c 128.

[4] RSC 1985, c C-36.

[5] SY 2003, c 14.

[6] 2020 BCCA 339 at para 46.

[7] *Supra* note 1 at para 143.
