**The 2017 CAPL Property Transfer Procedure: Why it matters**
**CAPL Negotiator, September, 2016**
**John Wallace**

On July 6 of this year, CAPL released the first draft of the 2017 CAPL Property Transfer Procedure (2017 PTP) for industry comment. The overseeing committee intends to finalise it in the second quarter of 2017. The 2017 PTP is to succeed the 2000 CAPL Property Transfer Procedure. The 2000 PTP was an ambitious attempt to standardise the procedural aspects of purchase and sale agreements, enhance efficiencies, and mitigate bias in the same way that the CAPL Operating Procedures have standardised operating agreements and the CAPL Farmout & Royalty Procedures have simplified earning agreements.

For a variety of reasons, the 2000 PTP did not achieve the kind of wide acceptance achieved by other CAPL precedent forms, and its benefits remain largely unknown to many land professionals. Nonetheless, it has found a niche among small producers who lack the personnel and budgets to engage in protracted drafting for their routine transactions. By using the 2000 PTP, these producers have been able to reduce the effort required to complete their typical straightforward transactions.

The 2017 PTP has been drafted to build and expand on this niche, with a focus on low to medium value transactions. As demonstrated by the sample head agreements included in its addendums, the updated document simplifies the process of generating swaps and sale agreements for small asset packages and undeveloped lands without compromising either breadth or depth of coverage.

But given the lack of traction achieved by the 2000 PTP, why does the 2017 PTP matter now?

Put simply, it matters now because the needs of industry and the profession have changed so much over the intervening years. As resource plays have grown in importance, the nature of our deal activity has also changed. An emphasis has been placed on asset rationalisation as a means of establishing the large contiguous blocks of land that characterise maturing resource plays. For many producers, this means that small-scale swaps and sales have largely replaced farmins and joint operating agreements.

Landmen, as a profession, must adapt to these changes to stay relevant. During the era of conventional production, Landmen developed the operating and farmout procedures and became the custodians of these documents. As these types of agreements are increasingly replaced in the resource play era by simple small-scale sales and swaps, Landmen should respond by developing a standard form property transfer procedure designed for these transactions. To do otherwise would cede this ground to other professions and to allow the role of Landman to diminish in importance in an already contracting industry.

The 2017 PTP would benefit industry too. A good, widely accepted precedent form sale agreement would reduce two things: risk and cost. Anyone buying a house knows that their sale agreement does not go through thirteen iterations prior to closing. The legal cost of such an approach would be prohibitive and the resulting document would be unique. And unique is not a good thing. Unique leads to uncertain outcomes and knowledge asymmetries. But this is the approach we take in industry.

While oil and gas transactions do have greater complexity than residential real estate transactions, there are nonetheless many relatively simple transactions we conduct every day in which both parties would be better served by a good and well-understood standard form sale agreement administered by capable professionals.

The 2017 PTP would help to level the playing field between companies. When it comes to garden-variety transactions, the 2017 PTP's extensive annotations and an expanding body of courses, articles, and sample head agreements will make it more accessible to land professionals than nearly anyone's dusty precedent. So, rather than spending our days trying to tease out the impact of subtle variations in wording, we can get on with the business of closing the deal.

Whether your company is likely to use the 2017 PTP for all or any of its transactions, there is a benefit to participation in the drafting process. It is a good occasion to judge your own internal precedents by an external yardstick. And it is a chance to have your say on how the thorny points of sale agreements are handled in the 2017 PTP—before a standard is set.

In the abstract, a precedent form sale agreement is not a revolutionary concept. They are used in other industries all the time for one simple reason: they are vastly more efficient. The only question is whether this particular document will be good enough to meet industry's needs. And that's where you come in: by participating and commenting on the first draft, you have the opportunity to ensure that industry gets the document it needs, that the land profession has ownership of this document, and that both you and your company have the type of mastery of the document that can only come from participating in its drafting.

**Undeveloped Property Transactions And The CAPL Property Transfer Procedure**
**CAPL Negotiator, November, 2016 (Updated December, 2017)**
**Jim MacLean**

The initial draft of the CAPL Property Transfer Procedure ("PTP") was made available to industry in early July through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed matrix that outlines all material changes and their rationale; and (iii) the text and annotations.

The Addendum to the document includes five case studies that show the potential use of the PTP for: (i) a simple sale of a producing property; (ii) a simple swap involving producing properties; (iii) a simple sale of an undeveloped property; (iv) a more complex sale of an undeveloped property involving reserved rights and the reservation of an ORR; and (v) a simple swap of undeveloped properties. The common theme was that use of the schedule of elections from the draft 2017 PTP allowed the Head Agreement for each of those case studies to be not greater than two pages.

The Committee is currently in the process of reviewing the industry comments received on that draft, with the vision of issuing an updated draft in December.

There are four common themes in any industry project for the creation of a new or updated industry agreement form, such as the PTP. The first is the attempt to position users to negotiate, document and administer their applicable Agreements more efficiently and effectively than would otherwise be the case. The second is the desire to mitigate the potential for unnecessary disputes to disrupt or damage ongoing business relationships. The third is to enable users of all experience levels to enhance their expertise and ability to contribute to the value creation process. And, last, but certainly not least, the fourth is to create a document that will be widely used in due course.

The obvious question that arises with respect to the current project to update the 2000 CAPL Property Transfer Procedure is a very simple one – why bother when the 2000 document was not used by industry?

That's a fair question and a conclusion I had admittedly shared for a long time in the context of my larger company experiences and the small number of calls I had ever received about the document.

Rather, that was my conclusion until the fall of 2015 when I was discussing the 2015 updates to the Operating Procedure and the Farmout & Royalty Procedure with representatives of the EPAC Land Committee. I became aware around that time that the 2000 PTP was being used by smaller companies more frequently than I had thought, so asked in passing if it was being used often by smaller companies and if an update to the PTP would be a worthwhile project. They answered both questions in the affirmative, and commented very positively about their personal experiences in using the document for their own low to modest value transactions.

That was the genesis for the project to create the 2017 CAPL Property Transfer Procedure, the decision to design the document around the typical relatively simple low to modest value transaction and the more extensive and visible participation of EPAC representatives on the Committee.

This article is about one particular type of low to modest value transaction – the sale or swap of undeveloped lands without wells.

## Undeveloped Lands Transactions

Most landmen are spending much more time negotiating the acquisition or swap of undeveloped land interests that complement their existing land blocks than traditional farmouts.

Given the changing characterization of our work, it was important to design the PTP to facilitate this type of straightforward transaction and to be able to demonstrate convincingly to landmen how the PTP could simplify significantly the negotiation and finalization of those transactions.

It seems like overkill, for example, to use a Vendor's precedent 30 page Purchase & Sale Agreement for a simple $200,000 acquisition of all rights in a two section undeveloped lease. Similarly, use of a Vendor's streamlined 5-8 page simplified conveyance document would still require a Purchaser to review that document very carefully because each Vendor would address similar content with its own preferred language.

Notwithstanding the efficiency uplifts associated with a simplified conveyance style document, significant inefficiencies remain. Vendors would continue to address the same type of content in a multitude of different ways, often with significant bias in their favour. Negotiations would also frequently continue to get bogged down in discussions about the choice of language, with resultant delays in the completion of transactions.

The potential benefits of the PTP can be illustrated by considering the simple example noted above in which a Vendor is selling its entire interest in a two section undeveloped lease for $200,000. While an initial investment of time with the Property Transfer Procedure would admittedly be required, use of the PTP would allow the Head Agreement to be prepared very easily. As shown in the sample Head Agreement below, the transaction dependent variables in the resultant agreement are ultimately just the dates and the sale price.

**UNDEVELOPED ACREAGE SALE AGREEMENT**
**ABC AREA, ALBERTA**

THIS AGREEMENT made this 1st day of ____, 201X.

BETWEEN:

YYY, a body corporate, registered to carry on business in the Province of Alberta and having an office in the City of Calgary, in the Province of Alberta (hereinafter called the "Vendor")

- and -

ZZZ, a body corporate, registered to carry on business in the Province of Alberta and having an office in the City of Calgary, in the Province of Alberta (hereinafter called the "Purchaser")

Whereas the Vendor wishes to sell the Assets to the Purchaser and the Purchaser wishes to purchase them, the Parties agree as follows in consideration of the premises hereto and the covenants and agreements hereinafter set forth, the receipt and sufficiency of which are hereby acknowledged:

**1. Definitions**

Each capitalized term used in this Head Agreement will have the meaning given to it in the Property Transfer Procedure. In addition:

(a) **"Effective Date"** means ___1, 201X.

(b) **"Scheduled Closing Date"** means _____, 201X.

## 2. Schedules

The following Schedules are attached hereto and made part of this Agreement:

(a) Schedule "A", which is a list of elections and amendments to the Property Transfer Procedure;

(b) Schedule "B", which identifies the Lands and the Leases; and

(c) Schedule "C", which is a copy of the General Conveyance.

Subject to the elections and amendments identified in Schedule "A", the Property Transfer Procedure is incorporated by reference into this Agreement.

## 3. Purchase And Sale

This Clause replaces Clause 2.02 of the Property Transfer Procedure. The Purchaser agrees to purchase the Assets from the Vendor and the Vendor agrees to sell them to the Purchaser on the terms and conditions set forth in this Agreement. The Base Purchase Price is $200,000. Except for $1.00, which is allocated to the Miscellaneous Interests, the entire value of the Assets is allocated to the Petroleum and Natural Gas Rights because there are no Tangibles or Wells associated with the Lands.

In witness whereof the Parties have duly executed this Agreement.

| YYY | ZZZ |
| --- | --- |
| Per: ___________________________ | Per: ____________________________ |

**Hey! Look What Zog Do…**

This is the title of a Gary Larson cartoon in the Far Side series. The cartoon shows three cavemen who are cooking their meat by holding it over an open fire with their bare hands. One of the cavemen points at another caveman a few feet away who is cooking his meat by holding it over his fire using a stick, saying, "Hey! Look what Zog do."

I like to use this cartoon to show in a fun way the potential benefits of looking at a problem in a very different way, particularly when the current approach is, well, fairly painful.

The combination of the inefficiency inherent in addressing similar content in a multitude of different ways, delays in completion of A&D transactions, prolonged debates about the choice of language, biased documents and overkill for simple transactions require us to reconsider the manner in which we approach at least our simple, low to modest value transactions.

We believe that a review of the sample case studies in the Addendums to the draft 2017 update to the CAPL Property Transfer Procedure will demonstrate that it offers a very different way to manage simple, low to modest value transactions, and that it will allow users to negotiate, document and administer those transactions much more easily than would otherwise be the case. This offers major benefits to our employers, our profession and each of us personally at a time when we are all challenged to become increasingly efficient by doing more with even less.

We hope that you choose to participate in the review of the upcoming draft to optimize the quality of this important industry document.

**“Making Simple Transactions Simple Again”: The 2017 CAPL Property Transfer Procedure**
**CAPL Negotiator, March, 2017**
**Jim MacLean**

The second draft of the 2017 CAPL Property Transfer Procedure (“PTP”) was made available to industry in late January through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 34 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the second draft relative to the initial July draft; and (vi) a redline of the second draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 document will be reviewed in any detail, we believe that even a cursory glance at that document will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last 11 months by our 15 member committee.

As noted in my earlier November, 2016 article in The Negotiator, the Addendum to the draft includes five case studies that were prepared to provide a compelling case for use of the 2017 PTP for the low to modest value transactions for which it has been designed. To a large degree, those case studies will determine the willingness of companies to allocate resources to the review of the document and the pace at which the PTP will ultimately be accepted by industry. They show the potential use of the PTP for: (i) a simple sale of a producing property; (ii) a simple swap involving producing properties; (iii) a simple sale of an undeveloped property; (iv) a more complex sale of an undeveloped property involving reserved rights and the reservation of an ORR; and (v) a simple swap of undeveloped properties. The common theme was that use of the schedule of elections from the draft 2017 PTP allowed the head agreement for each of those case studies to be not greater than two pages, as shown for item (iii) in the November article.

This month’s article offers additional context and an updated perspective on the path forward for the project in the context of the informal and formal feedback we received on the initial draft.

**“Making Simple Transactions Simple Again”**

Our committee is a diverse one, with representation from smaller companies, intermediate sized companies and larger companies. Our members represent not only CAPL, but also our partners in CAPLA, EPAC, PADA, PASC and the Legal Community. Despite our differences in background and functional expertise, we are united by a common belief-that our industry does not efficiently process our low to modest value, straightforward A&D transactions.

One of the major contributing factors to this is the lack of standardization in our agreements. We currently have hundreds of different companies saying basically the same thing in many different ways. This lack of consistency is apparent when we see the deficiencies in agreements presented to us and when we recall the bias in the documents we often see proposed. It is most apparent, though, when we consider the additional effort and associated delays respecting many of our low to modest value, straightforward transactions because of labour intensive reviews of different presentations of similar concepts and a tendency to debate how best to say basically the same thing as what had been originally proposed.

Put simply, we, as industry, have done a remarkable job of making simple transactions much more complex than they should be, than they must be in a business environment that requires us to do more with even less.

We believe that our work demonstrates that there is, in fact, a better path available to us for low to modest value, straightforward transactions. We believe that current industry conditions create an appetite for efficiency, effectiveness and change. Most importantly, however, we believe that a critical mass of the smaller and intermediate sized companies will quickly embrace the 2017 CAPL Property Transfer Procedure as “first followers” for the transactions for which it is designed.

This strong existing undercurrent of support for “making simple transactions simple again” is why we have dedicated so much of our effort on this project to target the smaller and intermediate sized companies and why we believe that use of the 2017 PTP will cascade quickly within at least that segment of potential users. (For a fun context on “first follower” theory, do a search and watch the three minute You Tube video “First Follower: Leadership Lessons from Dancing Guy.”)

**But Don’t Confuse Simpler Transactions With A Lack Of Quality**

The PTP is analogous to the CAPL Operating Procedure and the CAPL Farmout & Royalty Procedure. Each document is basically a “car manual” that offers a breadth and depth of coverage that addresses reasonably foreseeable issues in a way that is logical and reasonably complete. The resultant simplicity in the ability to complete transactions is not because those documents are simple- they are inherently complex. The efficiency gain they offer is a common platform of process and language that allows us to complete transactions much more simply than would be the case if those documents did not exist.

While we have tried to use “plainer language” in the PTP to simplify the presentation of the content, we did so without ever sacrificing the quality or depth of coverage for the transactions for which the PTP has been primarily designed. In fact, a cursory review of the materials comparing the 2017 draft to the 2000 PTP will show that the breadth and depth of coverage in the 2017 PTP are vastly superior to the corresponding content in the 2000 PTP.

**The 2000 PTP Is Already Obsolete**

As shown in the case studies in the Addendums, much of the former head agreement content contemplated for the 2000 PTP has been shifted to the 2017 PTP, and the number of elections has been significantly reduced, even though there are five new elections included in the 2017 document. More importantly, the handling of the concepts is much stronger than in the 2000 PTP because of a combination of feedback on the 2000 document, the intervening evolution in the way industry addresses issues in A&D agreements and our aggressive editing of the document.

Some companies that have been using the 2000 PTP have already begun to use the 2017 draft for new transactions, as modified for any changes they require for their particular transaction. They include both a schedule of elections and modifications and a copy of the draft document to provide context for that schedule. The significant mutual benefits to be obtained from use of the current draft are such that parties that would otherwise use the 2000 PTP for a particular transaction should consider possibly using this approach for their current transactions.

Parties considering this approach must be aware of a key qualification, though. The PTP needs to be supplemented with custom provisions if there are any issues associated with the transfer of regulatory licences for the reasons explained in the next article of this series. (For the moment, see the annotations on Paragraph 6.02(q) of the draft for an explanation about why this key business issue was not addressed within the PTP.)

**A Completed 2017 CAPL Property Transfer Procedure In Early Fall**

Fewer companies provided comments on the initial draft than we had hoped. However, the informal feedback was uniformly very supportive of the project, and the specific comments were both positive and very thorough. The combination of those comments and our own aggressive editing efforts resulted in the second draft being a greatly improved document.

We have requested industry comments by April 12. This positions us to issue the third industry draft in the spring, have any required iterations with commenting parties by early September and move to closure on the document in the late September to mid-October window.

**A Riddle That Offers Perspective**

As noted by the American inventor Charles Kettering, “The world hates change, yet it is the only thing that has brought progress.”

In speaking to a skeptical industry audience in late 1996 about an early draft of the 1997 CAPL Farmout & Royalty Procedure, I asked the audience the following riddle, “What do landing a man on the moon and the standardization of the procedural aspects of industry earning agreements have in common?” Not surprisingly, the audience thought that it was a very odd question. They were right, of course, since it was a trick question. I reinforced my point about our ability to implement major change in the way we conducted our business by reminding the audience that only one of them had been done.

That question puts the project to create the 2017 CAPL Property Transfer Procedure into perspective.

We cannot continue to manage low to modest value, straightforward A&D transactions in the traditional way when we are expected to optimize organizational efficiencies. How can we justify using a 35-65 page head agreement on a straightforward swap of non-operated properties when we can handle that transaction just as well with a two page head agreement and the 2017 PTP? How can we rationalize using a 10-25 page head agreement on a straightforward purchase of a five section, 100% interest lease for $200K that can be handled just as well with a one page head agreement and the 2017 PTP?

We are confident that the final product we submit to the CAPL Board for endorsement in due course will be a very good document that will enhance significantly industry’s ability to process the typical low to modest value, straightforward transactions for which the PTP has been designed. It will be a better document, though, if you choose to participate in the comment process and offer your insights.

Together, we are going to “make simple transactions simple again” with the 2017 CAPL Property Transfer Procedure.

**2017 CAPL Property Transfer Procedure: The Elections**
**CAPL Negotiator, April, 2017 (Updated December, 2017)**
**Jim MacLean**

The second draft of the 2017 CAPL Property Transfer Procedure ("PTP") was made available to industry in late January through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 34 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the second draft relative to the initial July draft; (vi) Word versions of the election sheet and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the draft in a new transaction; and (vii) a redline of the second draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that document will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last year by our 15 member committee.

This month's article offers additional context about the PTP by reviewing the elections that are included in the 2017 draft.

**Reduction In Number Of Elections**

One of our objectives when preparing the 2017 PTP was to minimize the number of elections and optional elements, so that the 2017 PTP would be more user friendly. One of the things we did, for example, was to choose a value that we thought reflected the prevalent practice or a logical outcome without presenting it as an option, while recognizing that there are a number of these for which Parties might modify the PTP to use a different value in any particular transaction.

Ignoring the need to select applicable Vendor representations under Clause 6.02, the identification of GST/HST registration numbers and the addresses for service, the number of data fields required to be completed has been reduced from 21 to 14. Even then, two of the 2017 data elements pertain to provisions that were expected to be handled in the Head Agreement when using the 2000 PTP.

The reduction in the number of elections has allowed for a single page Schedule of Elections and Modifications in Addendums I (annotated) and II (unannotated). As noted near the end of this article, it also includes a bolded instruction for users to assess if they wish to override certain listed time periods or thresholds, including several 2000 elections that are no longer elections in the 2017 PTP. Those potential modifications are also identified in the general annotations at the beginning of the PTP and in the applicable provisions.

**Overview Of The PTP Elections**

An overview of each election included in the PTP follows.

<u>Definition of Title Defect</u>: The PTP includes two Alternate elections. The first, Alternate 1, is similar to the definition in the 2000 PTP, and is a simple objective test. It does not include the prescriptive elements included in Alternate 2 that are examples of deficiencies that are and are not Title Defects. Alternate 1 would most likely be used with the simple "walk or close" approach in Alternate 1 of Subclause 8.02B. That approach is most likely to be used on low value transactions.

Alternate 2 is a much more elaborate definition, designed primarily for the threshold based approach to Title Defects in Alternate 2 of Subclause 8.02B. Those Alternates are more likely to be used for transactions on the higher end of the range for which the PTP is likely to be used. In summary, the threshold approach included in the latter requires the Purchaser to close on all applicable Assets if the Title Defects have an attributed value not greater than 10% of the Base Purchase Price. The Purchaser may exclude the affected Assets if the attributed value is greater than 10% of the Base Purchase Price, and either Party may terminate the transaction if the attributed value is greater than 25% of the Base Purchase Price.

<u>Definition of Wells</u>: The identification of an accurate list of wells is becoming increasingly important because of the restrictions on the transfers of well licences under the Regulations and the sensitivity about the handling of Abandonment and Reclamation Obligations and the assumption of other Environmental Liabilities. Given the importance of the issue and the nature of the typical transaction for which the PTP will be used, this definition has been structured with three Alternates, recognizing that Alternate 1 might be used singularly or in combination with Alternates 2 or 3. While Alternate 2 can be used without Alternate 1 being selected (albeit unlikely), it is inherent that Alternate 3 can only be used with Alternate 1.

Alternate 1 captures all Wells the Parties have chosen to list in a Schedule. This is the preferred approach because of the certainty and the context it offers for the acquired interests. It unlikely to be an onerous obligation for the typical transaction for which it is likely that the PTP will be used in practice. This is subject to the important qualification that the list of Wells on the Schedule is not necessarily limited to Wells located on the Lands or other lands pooled or unitized therewith. This recognizes that there may be circumstances in which the Parties have agreed to transfer residual responsibility to the Purchaser for certain other Wells not located on the live mineral rights (e.g., a well drilled into deeper rights that have since reverted to the Crown, a well drilled under one of the Title and Operating Documents at a location for which the mineral rights have expired). Alternate 1 can be used by itself or in combination with Alternate 2 or 3. Alternates 2 and 3 are mutually exclusive, and are only relevant if the Schedule of wells is incomplete (e.g., the Schedule did not list unit wells).

The PTP is not structured to include a requirement to list all Wells to be included in the Assets, though. Although it is a preferred practice to be as precise as possible in this area, it can often be difficult (e.g., a disposition of a large area, units with a large number of wells, units for which the operator does not maintain a current well list exhibit in the unit agreement). Alternates 2 and 3 include the more typical generic reference to Wells located on the Lands and other lands pooled or unitized with them insofar as they have not already been set forth on the Schedule.

Alternate 3 offers a major exception to the handling in Alternate 2. Insofar as abandoned, injection, water source or disposal wells not included in a unit are intended to comprise part of the Assets, they must be listed on a Schedule if Alternate 3 is selected to apply. This requires the Parties to address the handling of these wells specifically, and is designed to minimize the possibility of subsequent disputes. This treatment reflects the degree to which the handling of abandoned wells is actually a matter of negotiation and the need to confirm if service wells are intended to be retained by the Vendor because they serve other assets. (See the last paragraph of the definition of Tangibles for a similar treatment of abandoned non-unit pipelines.) The corollary of this if Alternate 2 applies is that a simple test of if the Wells are located on the Lands and other lands pooled or unitized therewith applies to all Wells not set forth on a Schedule (including reclaimed).

<u>Base Purchase Price and Tax Allocations (Clause 2.02)</u>: The 2000 PTP required the Parties to address the Base Purchase Price and the tax allocations among the Petroleum and Natural Gas Rights, the Tangibles and the Miscellaneous Interests in their Head Agreement. To simplify preparation of the Head Agreement, this content was moved to Clause 2.02 of the 2017 PTP. This sees the Base Purchase Price being a blank that the Parties would need to complete and the tax allocations specified as the typical 80-20 split between the Petroleum and Natural Gas Rights and Tangibles, respectively, after an allocation of $10 to the Miscellaneous Interests.

The onus is on the Parties to modify Clause 2.02 for an Asset Exchange and for circumstances in which a different tax allocation is required, as identified in the annotations on the Clause and on the Addendum I election sheet.

Deposit (Clause 2.03): This Clause has been modified significantly to simplify the Head Agreement. It is an optional Clause that addresses the requirement to submit a Deposit, if any. It includes some content from Subclause 2.02B of the 2000 PTP. If selected, the Deposit threshold has been specified at 10%, when the amount of the Deposit was expected to be addressed in the Head Agreement used with the 2000 PTP. The 10% Deposit was chosen to reflect the typical handling in industry agreements under which a Deposit is required. The Parties would need to modify the provision if they wished to use a different Deposit threshold after selecting that this Clause will apply.

GST/HST Election (Clause 2.05): As was the case in the 2000 PTP, the Parties have the ability to have the Vendor collect and remit the applicable GST/HST (Alternate 1) or to make a joint election under Section 167 of the *Excise Tax Act* (Canada) in Alternate 2. This Clause also requires the Parties to include their respective GST/HST Registration Numbers.

Interest Accrual (Clause 2.06): Although it is a common practice for Vendors to require the accrual of interest prior to Closing, the Parties will often choose not to use an interest mechanism for the low to modest value transactions for which the 2017 PTP will be used. As was the case with the 2000 Clause, the Parties will choose if their Agreement includes an interest accrual for the period up to Closing. If so, the Parties will select whether the interest accrual is from the Effective Date (Alternate 1) or only from the original Scheduled Closing Date (Alternate 2). The latter is designed to recognize the logistics of effecting a transaction and to link the interest accrual to delays in Closing.

Distribution of Specific Conveyances (Clause 3.05): The structure is consistent with the 2000 PTP.

Alternate 1 provides that the Vendor is to handle the distribution and registration of the Specific Conveyances described in Paragraph 3.03A(b) on behalf of the Purchaser. This reflects the practical fact that the Purchaser's immediate focus after Closing is on getting the property into its system. Both Parties benefit through earlier recognition by the operator, as less accounting rework will be required. The Vendor particularly benefits by reducing the recognition period and in knowing that the registration of documents is complete.

The Purchaser controls the distribution and registration of the documents under Alternate 2. This Alternate may be attractive if there are concerns about the diligence with which the Vendor would distribute the ancillary documents. While this structure had typically been used for industry's dispositions in the 1980s and much of the 1990s, it is now used infrequently.

Pipeline Records and Associated Transfers (Subclause 3.07B): Clause 3.07 is new in the 2017 PTP.

The references to Pipeline Records reflect AER Bulletin 2015-34. It contemplates that the AER could conduct compliance monitoring (for existence and transfer of required records) on a random basis or during routine field inspections, typically after the transfers have been processed. The new licencee (transferee) is responsible for producing the applicable records on request of the AER, which places an onus on the Purchaser to protect itself through its due diligence process. A licencee that fails to do so will be in a non-compliance position. Non-compliance could, among other things, force it to conduct an engineering assessment to demonstrate that the applicable pipeline is fit for its intended use and service. Pending such an assessment, the AER could order the pipeline out of service, which may require wells to be shut-in. Compounding the challenge of compliance is that the Parties might not agree about whether the Pipeline Records are complete for the purposes of the review by the Regulatory Authority and that the Regulatory Authority's expectation for completeness might not be known until any site inspection.

The references to Pipeline Records require the selected Party (Vendor or Purchaser) to bear accountability to address any deficiencies associated with Pipeline Records. The optional representation included in Paragraph 6.02(r) is fairly onerous, and Vendors will typically be extremely reluctant to assume a trailing liability. One would typically expect Vendors would have a strong preference not to accept that representation and to select Alternate 1 (Purchaser accountability) in this Clause as a consequence. Conversely, one would expect that Alternate 2 (Vendor accountability) would be selected only (but not necessarily) if a Vendor has agreed to provide that representation.

Alternate 3 of Clause 3.07 has been included to add flexibility. It allows the parties to choose to share financial responsibility for any engineering assessments required to rectify identified deficiencies on a different negotiated basis under the Head Agreement. A negotiated cost sharing creates reinforcement for each party to address any deficiencies in a timely and cost effective manner.

*Per Diem* Rental Adjustment (Paragraph 4.01(d)): Paragraph (d) is an optional Paragraph as of the 2017 document. Parties will often choose to ignore a *per diem* rental adjustment for many small to modest sized transactions for which the PTP will be used, particularly for any transactions involving only undeveloped lands. This is consistent with the approach in the CAPL Farmout & Royalty Procedure, which has significantly reduced the frequency with which *per diem* rental calculations are used in farmouts. If selected, rentals are apportioned on a *per diem* basis under Paragraph (d).

Adjustment for Income Tax-Interim Period Income (Clause 4.03): This Clause has been modified significantly relative to the 2000 PTP because the CRA is no longer willing to offer the latitude in enforcement from its general practice contemplated in optional Subclause 1B of the 2000 PTP. That Subclause reflected some latitude in enforcement with respect to transactions for which: (a) the Effective Date and Closing were in the same calendar month; (b) the amounts in question were minor (or there was no significant tax benefit accruing to a Party); and (c) all of the income realized during the Interim Period was fully recorded as between the Parties.

The CRA's view is that beneficial ownership of the Assets is retained by the Vendor until Closing, notwithstanding that beneficial ownership might be acquired at Closing by the Purchaser under the Agreement retrospectively to an earlier Effective Date. The net effect is that this Clause reflects the CRA's requirement that income realized during the Interim Period be reported by the Party that has beneficial ownership of the Assets on a real-time basis during the Interim Period. This necessarily requires an equitable adjustment mechanism to the Base Purchase Price.

The CRA's needs are satisfied if Interim Period income is recognized by the Vendor for tax purposes. The CRA is not normally concerned by the percentage negotiated by the Parties under this Clause.

The negotiation of this percentage can often be contentious, though. Vendors will often request an adjustment percentage that reflects that they are currently fully taxable (even if in a tax deferred position). On the other hand, Purchasers will often request a very small percentage to be used if their belief is that their Vendor is in a tax deferred position in the near to medium term, even though this outcome would not consider the resultant impact on the Vendor's tax position in the outer years.

The Parties should be cautious about deviating from the CRA's requirements for recognition of Interim Period income. Audit risk for the transaction potentially increases significantly if the Parties purport to handle Interim Period income in a different manner, particularly if the amounts involved are significant.

Vendor's Representations and Warranties (Clause 6.02): The representations and warranties of the Vendor in Clause 6.02 will be a matter of negotiation between the Parties. This reflects the wide variance in transaction circumstances (i.e., operated property, non-operated property to another owner or operator, non-operated property to a third party, high or low value, ORR holder and corporate philosophies). Many of these issues pertain more to whether a specific representation should be included at all, rather than its wording. As was the case with the 2000 PTP, each representation in this Clause has been presented as an option, so that it only applies if selected, even though some of them will be used in the vast majority of transactions.

The menu of potential representations and warranties is designed to provide Parties with greater flexibility for their transaction. An election not to include an optional representation is not intended to place the Purchaser in any different position with respect to the subject matter of the representation than is the case for any item that is not included in the menu of representations in this Clause.

The Clause 6.02 representations will be addressed specifically in the next article in this series.

Right of First Refusal Values (Subclause 7.01B): Agreements are often structured so that the Vendor issues required ROFR notices using the values supplied by the Purchaser, with an indemnification of the Vendor by the Purchaser if the Purchaser's ROFR values are challenged by any of the applicable third parties. That approach was not used in the base Subclause because of the Vendor's pre-existing responsibilities to the other working interest owners, but it was accommodated through the inclusion of the optional sentence at the end of the Subclause.

Rights of First Refusal-Termination Right (Subclause 7.01E): Subclause E and Paragraph (d) of Alternate 8.02B(2) were updated significantly in the 2017 document. The 2000 document included a negotiated threshold for the combination of Title Defects and ROFR exercises. As of the 2017 document, the two processes are independent.

If selected, optional Subclause E allows the Purchaser to terminate the transaction if the value of the exercised Assets is 50% or more of the Base Purchase Price, a threshold that the Parties could easily modify for any particular transaction. The Subclause has been included as an option because Vendors will often resist providing a Purchaser with an option to terminate a transaction because of ROFR exercises. This is particularly the case for a transaction structured as an Asset Exchange. The outcome in which the Vendor receives only cash instead of properties is a negative one to the Vendor if it originally had no interest in selling the ROFR Assets. The Party that ultimately assumes the risk of a ROFR exercise in a transaction structured as an Asset Exchange is one of the important issues to consider when negotiating it.

That being said, a Purchaser would often struggle with a construction that would require it to close on the remaining Assets if the majority of the original value of the Assets were with respect to a property it would not acquire because of the exercise of a ROFR by a third party.

Purchaser's Review (Article 8.00): This Article was modified to be an optional Article in the 2017 PTP. This reflects the increasing trend to require the due diligence process to be completed prior to execution of the Agreement, particularly for the low to modest value transactions for which the 2017 PTP has been designed. This provides each Party with greater control over any negotiations required to resolve any negative matters encountered in the due diligence review, and ultimately increases deal certainty if the Parties are able to resolve those matters. This allows each Party to know if there are material problems before execution, rather than finding themselves in a potential lingering dispute after the Agreement is executed. This approach may be particularly attractive for the more straightforward Assets for which the 2017 PTP will typically be used, and it also offers a significant potential simplification if the Assets comprise only undeveloped lands.

Even if this Article was not selected to apply, the duties in Clause 8.01 should apply to the Vendor with respect to access provided to the Purchaser for its due diligence review prior to execution of the Agreement (something that should be reinforced in the letter of intent), and the obligations in the last paragraph of that Clause should apply to the Purchaser with respect to its due diligence review. (See also the Vendor's representation about the provision of documents in Paragraph 6.02(p).) Similarly, Subclause 8.02D should apply to that due diligence review to ensure that the Purchaser is in the same position after Closing if the Article is not selected as it would have been if it had acquired the Assets in an Agreement in which Article 8.00 was selected to apply.

Election Respecting Title Defects (Subclause 8.02B): This Subclause is only relevant in the 2017 PTP if Article 8.00 has been selected to apply. As noted in the review of the definition of Title Defect earlier in this Article, there are two Alternates for this Subclause.

Alternate 1 provides the Purchaser with three options. It may: (a) provide the Vendor with additional time to remedy the Title Defects by delaying the Closing Time to such date as the Parties may agree; (b) waive the uncured Title Defects and proceed with Closing; or (c) terminate the transaction. Alternate 1 of the definition of Title Defects should be used if Alternate 8.02B(1) is selected.

The construction of this Alternate is ultimately binary. Unless otherwise agreed by the Parties, the ultimate choice of the Purchaser is to proceed to Closing or to terminate the transaction. The major advantages of this approach are its relative simplicity and the prohibition against "cherry picking", such that it can be particularly attractive for minor value transactions. In addition to avoiding the potential for cherry picking, this mechanism also avoids the valuation problems inherent with the potential exclusion of portions of the Assets.

Alternate 2 includes greater flexibility in the handling of the Title Defects. Closing will proceed without any adjustment for Title Defects if the value of the outstanding Title Defects is below a threshold of 10% of the Base Purchase Price, a threshold that might not be appropriate for a minor value transaction.

If the value of uncured Title Defects is above the 10% threshold, the Purchaser has four options. It may: (a) provide the Vendor with additional time to remedy the Title Defects by delaying the Closing Time to an agreed date; (b) waive the uncured Title Defects and proceed with Closing; (c) proceed with Closing for the Assets not affected by the Title Defects, with the consideration being reduced accordingly, insofar as that value is greater than the 10% threshold; or (d) terminate the Agreement if at least 25% of the consideration is applicable to the Assets affected by the uncured Title Defects. However, the Vendor may also terminate the transaction if the Purchaser is proposing to exclude Assets with a value of at least 25% of the Purchase Price under Paragraph B(c). There are protections included to address the situation in which the Vendor does not agree with the values the Purchaser attributed to the Assets affected by the Title Defects.

The thresholds in Paragraphs (c) and (d) of this Alternate were modified from a blank to be negotiated for each transaction to 25% as of the 2017 document. This was done to reflect the most typical negotiated outcome and to reduce the number of elections associated with use of the PTP. The Parties always remain free to negotiate a different handling in any particular transaction.

Addresses For Service (Clause 15.02): The Parties are expected to add their respective addresses for service in this Clause, as was the case for the 2000 PTP.

**Users Need to Validate Time Periods And Financial Values**

One of the areas of emphasis in the update to the 2000 PTP was to eliminate unnecessary elections by structuring the applicable provisions to reflect what appeared to be the prevalent practice or a logical outcome without presenting it as an option. This was to facilitate acceptance of the 2017 PTP by reducing significantly the number of required elections in order to allow a more user friendly platform for the typical low to modest value transaction.

It will not be uncommon, though, for Parties to choose a different value in any particular transaction. The more common anticipated changes of this type are identified in the applicable annotations and in the bolded reference in the Schedules of Elections and Modifications included in the Addendums at the end of the document. Those references remind users to confirm that the defaults in the document are appropriate for their particular transaction.

Modifications to the defaults included in the PTP might be considered, for example, if: (a) the transaction is an Asset Exchange (e.g., GST/HST Registration Numbers; Clause 3.01 place of Closing; and possible differences in the Clause 6.02 Vendor representations); or (b) the Parties want to override prescribed time periods or thresholds that had been elections or Head Agreement content in the 2000 PTP. Examples of these are: (i) Clause 2.02 tax allocations; (ii) Clause 2.03 optional 10% Deposit; (iii) Subclause 3.04B access to files period; (iv) Paragraph 4.02A(b) final statement of adjustments within six months; (v) Clause 6.05 and 13.01 survival period on representations and warranties; (vi) optional Subclause 7.01E 50% or more ROFR exercise threshold; (vii) Subclause 8.02A seven Business Day period for notice of Title Defects; (viii) Subclause 8.02B Alternate 2 Title Defects thresholds of 10% and 25%; (ix) including a different value in Subclause 13.03A; and (x) the $25,000 minimum claim threshold in Subclause 13.03B.

Other provisions that specify timing or a financial threshold that might be modified include: (i) the 31 day thresholds for marketing and J.V. agreements used in Paragraphs (c) and (g) of the definition of Title and Operating Documents and the corresponding representations in Paragraphs 6.02(i) and (j); (ii) the contemplated handling of freehold mineral tax in Clause 4.01; (iii) the $10,000 threshold in Subclause 4.02B; (iv) the $50,000 authorized expenditure threshold in Clause 5.01, Subclause 5.03A and Paragraph 6.02(h); (v) the $100,000 threshold for addressing regulatory requirements under Paragraph 6.02(l); (vi) the 60-day period prescribed for replacing signs under Clause 11.02; and (vii) any modifications to the handling of surplus equipment contemplated in Clause 11.03.

**Balancing Simplification With Flexibility**

As part of “making simple transactions simple again,” the 2017 PTP has been designed to balance simplification with the retention of required content and optionality.

We chose to reduce significantly the number of elections in the 2017 PTP relative to the 2000 document by retaining necessary options and eliminating options for items for which we believed there was a prevalent industry practice. That being said, we structured the annotations and the Schedule of Elections and Modifications included as Addendum I to the PTP to remind users of the timing and financial thresholds that Parties might choose to modify for any given transaction.

In essence, the overarching philosophy in the 2017 PTP is one of options where necessary, but not necessarily options.

Next month’s article reviews the Vendor’s representations and warranties, as outlined in Article 6.00 of the PTP.

**2017 CAPL Property Transfer Procedure: Reps And Warranties-Part I**
**CAPL Negotiator, May, 2017 (Updated December, 2017)**
**Jim MacLean**

The second draft of the 2017 CAPL Property Transfer Procedure ("PTP") was made available to industry in late January through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 34 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the second draft relative to the initial July, 2016 draft; (vi) Word versions of the election sheet and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the draft in a new transaction; and (vii) a redline of the second draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that document will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last year by our 15 member committee.

This month's article offers additional context about the PTP by reviewing Clause 6.01 and Paragraphs 6.02(a)-(t). Next month's article will address the remainder of Article 6.00.

**Context For Representations And Warranties Article**

The representations and warranties provision has historically been one of the most heavily negotiated provisions of a Purchase and Sale Agreement with respect to both the types of representations that are to be included and their wording.

The Vendor generally wishes to provide the most limited representations and warranties as are acceptable to a Purchaser. It wishes to sell the Assets on an "as is" basis, and wants the future risks associated with the property to be assumed by the Purchaser. The inclusion of broad representations and warranties is inconsistent with the Vendor's objective of reducing G&A costs by exiting an area. The potential liability resulting from their breach means that the Vendor is not entirely free of responsibility for the property.

The Purchaser, on the other hand, generally wishes to include the broadest representations and warranties that it is able to negotiate. Many of these will pertain to factual matters about either the Vendor or the Assets that the Purchaser is otherwise unable to confirm conveniently. That being the case, it may be reluctant to proceed with an acquisition if it believes its requests for broader representations and warranties are being unreasonably refused by a Vendor.

One must place a Party's optimization of its legal position in a larger context, though. The objective is to sell/purchase a property in the manner that will maximize the degree to which the benefits associated with the transaction exceed the applicable costs and risks. If differences on this issue are such that the transaction is not completed, the pursuit of one goal has frustrated the objective.

The Agreement is ultimately one part of the product that a Vendor may be attempting to sell in a very competitive marketplace. Personnel must always remember that the form of the document could have a material impact on the assessment of the attractiveness of the product to potential Purchasers. Reps and warranties that indicate that the Vendor has reasonable confidence in its product should help it in its attempt to obtain the greatest value for its properties. This is particularly so if it has done an internal review of the property and its continued financial viability is not in doubt. However, a Vendor must weigh the associated potential risks and benefits for each broader rep and warranty.

The menu of representations and warranties in Clauses 6.01, 6.02 and 6.04 is designed to focus negotiations on the appropriateness of the inclusion of a particular representation in the Agreement, while significantly reducing the degree to which the choice of wording is debated.

It is also important for users to remember that the remedy available for a breach of a representation or warranty after Closing is in damages. The representations and warranties are analogous to an indemnification obligation, as their enforceability ultimately depends upon the financial viability of the Party making the representation. If there is a concern about a Vendor's financial viability, for example, a Purchaser should not rely unduly upon the representations.

**Clause 6.01 – Mutual Representations And Warranties**

These are reciprocal representations and warranties that pertain to the personality of the Parties. Including them in a single Clause avoids duplication. There may be instances in which some customization is required for one (but not both) of the Parties.

These representations relate to: (a) the standing of the Party as a subsisting entity; (b) the authority of the Party to execute the applicable documents; (c) the execution and delivery of the Agreement and completion of the transaction not being in conflict with the governing documents of the Party, the Regulations, court orders, etc.; (d) the enforceability of the Agreement, subject to certain qualifications respecting bankruptcy, insolvency, etc.; (e) the other Party not being subject to any finder's fees; and (f) there being no plan to cease to remain in existence.

**Clause 6.02 – Vendor's Representations And Warranties**

General: The representations and warranties of the Vendor in Clause 6.02 will be a matter of negotiation between the Parties. This reflects the wide variance in transaction circumstances (i.e., operated property, non-operated property to another owner or operator, non-operated property to a third party, high or low value, ORR holder and corporate philosophies). Many of these issues pertain more to whether a specific representation should be included at all, rather than its wording. As was the case with the 2000 PTP, each representation in this Clause has been presented as an option, so that it only applies if selected, even though some of them will be used in the vast majority of transactions.

The menu of potential representations and warranties is designed to provide Parties with greater flexibility for their Transaction, as shown on the Schedule of Elections and Modifications included as Addendums I (annotated) and II (unannotated) to the PTP. An election not to include an optional representation is not intended to place either Party in any different position with respect to the subject matter of the representation than is the case for any item that is not included in the menu of representations in this Clause.

Residency for Tax Purposes (6.02(a)): This representation is admittedly structured awkwardly. Unfortunately, it cannot be rewritten to state simply that the Party is a resident of Canada. As a Party can be a resident of more than one country, the Vendor represents that it is not a non-resident. It is included primarily to provide the Purchaser with a justification for not applying a withholding tax with respect to the amount paid to the Vendor.

Lawsuits and Claims (6.02(b)): The Purchaser has an expectation that there are no judgments or claims respecting the Vendor's interest in the Assets, with a requirement to identify any exceptions in a Schedule. The Parties should clearly address their expectations about any existing lawsuit or claim in the Head Agreement to minimize the possibility of subsequent dispute.

This rep is somewhat broader than the rep that Vendors often prefer to use because of the reference to circumstances that the Vendor reasonably believes would give rise to a claim. The first portion of the rep that is typically used assumes that a third party is aware of the problem and is pursuing the exercise of legal rights. The latter reference would apply if the Vendor is aware of the problem, but is not aware of any intention of a third party to pursue a legal remedy.

No Default Notices (6.02(c)): This rep pertains not only to defaults, but notices alleging defaults, and any exceptions are to be identified on a Schedule. The disclosure requirement alerts a Vendor to the need to review the issue.

Compliance with Title and Operating Documents (6.02(d)): Provisions such as this Paragraph are often drafted so that the reference to "default" is modified by adding a reference to "material". Although a default that has a material and adverse impact on the Assets would logically be a "material default", some Purchasers object to the "material default" reference. The last phrase addresses the concerns of both Parties by referring to a default that “would reasonably be expected to have a material adverse effect on the total value of the Assets.”

Payment of Royalties and Taxes (6.02(e)): The Purchaser expects that the Vendor will remain responsible for royalties and taxes associated with the period of the Vendor’s ownership.

Encumbrances and Rights of First Refusal (6.02(f)): The Vendor’s interest in the Assets is subject to the Permitted Encumbrances. Vendors will not give an absolute title warranty. They also avoid any implied warranties of title that otherwise may exist by including an express statement that the Vendor does not warrant title. This rep reinforces to the Vendor why it should be very careful in modifying the definition of Permitted Encumbrances.

No Reduction (6.02(g)): The Vendor's interest in a Well may be reduced at payout or upon the recovery of a production penalty, and the Lands might be subject to a farmout agreement. These potential reductions must be identified in the Land Schedule to qualify as Permitted Encumbrances, and should be noted in any sale brochure.

Authorized Expenditures (6.02(h)): Procedures must be implemented by the Vendor to ensure that the Purchaser is aware of all new AFEs, operation notices, mail ballots, etc. respecting the Assets. This should be coordinated through the relevant A&D personnel, who in turn would advise the Land A&D contact. The better practice is to list all such AFEs or commitments in a Schedule. If any such obligation accrues under the maintenance of business provisions in Article 5.00 following execution of the Agreement, it is a good practice to capture that information on a reference table for the benefit of Accounting and Joint Ventures personnel.

The financial threshold for the Purchaser’s share of a particular discretionary expenditure was increased from $25,000 to an estimated $50,000 in the 2017, as the $25,000 threshold had typically been used since the early 1990s. This threshold is also included in Clause 5.01 and Paragraph 5.03A(a), and is one that Parties may prefer to modify for particular Transactions or as a corporate preference change. Users are reminded of this item in the general annotation at the beginning of the PTP and on the sample annotated Schedule of Elections and Modifications included as Addendum I.

It is important to remember that this threshold is linked to the amount that was reasonably estimated to be applicable to the Vendor’s share of the cost. The Vendor’s authority to have made an expenditure is not compromised if the ultimate share of costs exceeds that amount.

Sale Agreements (6.02(i)): A production sales contract that is not terminable on notice of 31 days or less only falls within the definition of Title and Operating Documents (and the resultant treatment as a Permitted Encumbrance) if it is identified in a Schedule. Otherwise, the Vendor is representing that there are no such contracts.

A 31 day threshold is used in this Paragraph and Paragraph 6.02(j), as well as Paragraphs (c) and (g) of the definition of Title and Operating Documents. Parties may prefer to modify it for particular Transactions or as a corporate preference change to the PTP. Users are reminded of this item in the general annotation at the beginning of the PTP and on the sample annotated Schedule of Elections and Modifications included as Addendum I.

<u>Production Handling Agreements (6.02(j))</u>: This rep was introduced in the 2017 PTP. It is similar to the preceding representation about sales agreements. Other than for J.V. service type agreements that can be terminated on short notice (i.e., the typical 31 days or less termination mechanism), the Vendor represents that there are no service agreements of this this type that have not been identified on a Schedule. Again, any such agreement that satisfies those requirements is a Permitted Encumbrance. The inclusion of this representation reflects the importance of J.V. Agreements to the value of a Transaction.

<u>Various Operational Matters (6.02(k)-(o))</u>: These reps relate, respectively, to “Environmental Matters”, “Operations And Compliance With Regulations”, “Condition Of Wells” and “Abandonment Of Wells”.

In light of the focus on environmental issues, these representations can be quite contentious in the negotiation of A&D Agreements. There are several major issues associated with these representations. The first is the linkage to the Vendor’s knowledge, which is addressed in Clause 1.08. The second reflects the practical consideration that parties other than the operator generally have very limited direct operational knowledge about a property for the purposes of Paragraphs 6.02(l)-(o), such that non-operators generally will not be willing to include them.

That being said, Paragraph 6.02(k) is not qualified by limiting the representation to Assets operated by the Vendor. While a non-operator Vendor’s knowledge would not be as complete as the operator’s, it is quite possible that such a Vendor would be aware of environmental problems for non-operated Assets that should be disclosed to the Purchaser.

Another potential issue is the reference to the “the material requirements of the Regulations as they existed at the relevant time” that is included in Paragraphs 6.02(m), (n) and (o). While Purchasers may object to the materiality qualification, its deletion would require the Vendor to provide an absolute warranty that it is not aware of any violation of the Regulations. The remedy for a minor violation discovered after Closing would be in damages, and would almost certainly be minimal. However, the consequences could be quite serious if a minor violation were discovered before Closing. Such a violation could literally enable a Purchaser with “cold feet” to terminate the Transaction, a particular risk if market conditions were volatile. The materiality qualification attempts to balance the interests of the Parties. Any violation which has a material and adverse impact on any of the Assets is logically a material violation.

The other difficulty with the unqualified representation is that regulatory approvals or licences often include performance objectives, rather than standards. If Regulatory Authorities do not require strict compliance, is it appropriate to provide a Purchaser a remedy for minor violations?

The inclusion of the phrase “as they existed at the relevant time” also reflects the degree to which the regulatory environment has evolved over time. The test for compliance at any particular time should be linked to the regulatory regime then in existence, not current regulatory standards, except insofar as current regulatory standards then apply to an outstanding specific problem. Paragraph 6.02(k) would potentially apply to any such situation, and Subparagraph (iii) is not contingent on there being an order or directive issued under the Regulations regarding such a problem.

Paragraph 6.02(k) specifically addresses the Vendor's environmental representations. Except as identified in a Schedule, the Vendor represents that, to its knowledge, it is not aware of: (a) any environmental orders or directives requiring expenditures that have not been complied with in all material respects or otherwise satisfied; (b) any outstanding regulatory demands or notices pertaining to the breach of any environmental health or safety law applicable to the Assets; and (c) any circumstance it reasonably believes to be a reportable event under the Regulations.

Paragraph 6.02(l) was introduced in the 2017 document, and addresses operations in a wider sense than environmental matters. To its knowledge, the Vendor has not received any notices respecting the occurrence of a material violation of the Regulations and is not aware of any such material violation that remains outstanding at the Closing Time in circumstances in which the Vendor's share of costs to remedy the problem is estimated to exceed $100,000. That amount is one that Parties may prefer to modify for particular Transactions or as a corporate preference change to the PTP. Users are reminded of this item in the general annotation at the beginning of the PTP and on the sample Schedule of Elections and Modifications included as Addendum I.

The Vendor will usually have much greater knowledge under Paragraphs 6.02 (m), (n) and (o) for Assets operated by it at the relevant time than it will about non-operated properties. These reps were modified in the 2017 PTP to limit them to Wells and Tangibles operated by it.

There are some subtleties associated with Paragraph 6.02(n) respecting the abandonment of Wells. Notwithstanding that a Vendor may not transfer a well licence for a Well that has been abandoned and that has been reclamation certified, the Parties are free to agree in contract that the Purchaser will assume the Vendor's potential ongoing financial obligations for that Well through the liability and indemnification provisions, as noted in the annotations on the definition of Well in Clause 1.01.

Whether an abandoned well is a Well for purposes of the Agreement will depend on the selection of the Alternates in the definition of Wells and if the particular well has been identified on a Schedule. The net effect is that an abandoned well on the Lands may or may not be a Well, depending on how the Parties have negotiated their Agreement.

<u>Provision of Documents (6.02(p))</u>: The reps and warranties and title review effort are premised on the Vendor making the relevant documents and files available for the Purchaser's review: (i) on the basis contemplated in Clause 8.01 if Article 8.00 was selected to apply; or (ii) in conjunction with any due diligence process conducted by the Purchaser prior to execution of the Agreement in circumstances in which optional Article 8.00 has not been selected to apply in accordance with Paragraph (a) in the introduction to Article 8.00.

The obligation does not extend to all files and documents included in the Miscellaneous Interests because any delivery less than full compliance could provide the Purchaser with an option to terminate the Transaction prior to Closing if it could satisfy the materiality requirement in Paragraph 10.01(c). However, the Purchaser will also often include additional conditions under Article 10.00 (i.e., Paragraph 10.02(d)) under which it is to be provided with access to other types of documents. The Purchaser will often require similar conditions respecting access to applicable materials if it is being asked to agree to conduct its due diligence review prior to execution of the Agreement, as would be the case if optional Article 8.00 were not being selected.

As a consequence, the files to which this obligation pertains are not limited to those relating to title and environmental. In addition to the land and environmental files, the Purchaser will sometimes also wish to expand the specific list of files made available for review to include such files as J.V. and marketing agreements and production and accounting records. This Paragraph is consistent with the expectations in Paragraph 8.01(a).

<u>Well and Tangibles Transfers (6.02(q))</u>: This representation is included because of the possibility that the transfer of Wells to the Purchaser would result in the Vendor having a ratio of inactive to active wells that would not satisfy the requirements of applicable Regulatory Authorities, such as the Alberta AER.

The definition of Licencee Rating, this representation, the corresponding rep in Paragraph 6.04(d) and the condition in Paragraph 10.01(e) are structured so that they can apply across multiple jurisdictions.

If the ability to effect a transfer of any licence for any of the Assets is in question, the onus is on the Parties to add custom content in their Head Agreement to address their particular needs. This might be done, for example, by including additional definitions, a Clause that relates to the specific handling required for their circumstances and the inclusion of additional conditions to Closing. Reviewing the Regulations for a Transaction is particularly important if they include a requirement for a review of a proposed transfer of a regulatory licence, permit or approval through a process in which that approval might not be granted, since this could require the inclusion of a Closing in escrow process in the Agreement.

There were two reasons for this approach. The first was the belief that the PTP should not attempt to predict or prescribe the handling of an important emerging issue that should be assessed and handled by the Parties and their applicable business and legal advisors on a case by case basis. The second was that the fluidity of the Regulations on this area over time and across jurisdictions was such that any more specific handling of the issue in the PTP would potentially create unintended consequences for the Parties over time.

Simplifying the review of the other procedural aspects of the overall Transaction through use of the PTP facilitates a more focused examination of this important issue by the Parties' representatives relative to what would be the case without the PTP.

<u>Records Relating to Operated Tangibles (6.02(r)</u>: As noted in last month's article, this representation is inserted as a potential response to AER Bulletin 2015-34. Vendors should consider very carefully if they will select it (or any modified version thereof) in conjunction with their review of Clause 3.07. There is uncertainty at this time as to what the AER considers as 'records required by CSA Z662 and the Pipeline Rules', such that the most prudent approach for pipelines of any age may be for Parties to agree (with the AER if possible) on a list of required records for pipelines to be transferred until there is greater certainty on this issue.

<u>Regulatory Production Penalties and Regulatory Production Allowable (6.02(s)&(t)</u>: A Vendor should be required to disclose any regulatory production penalties and any overproduction above regulatory allowables if it is aware of those problems. As not all off-target wells will result in a production penalty under the Regulations, the representation pertains to only a subset of off-target wells.

**"You Say Tomato, I Say Tomato"**

The negotiation of the reps and warranties provisions of the typical Purchase & Sale Agreement for a low to modest value, straightforward sale reinforces why the 2017 CAPL Property Transfer Procedure is an important industry initiative.

It is inherently inefficient and expensive to engage in labour intensive reviews of different presentations of similar concepts and debates about how best to say basically the same thing as what had been originally proposed for the typical straightforward low to modest value asset deal.

Far too often, such a debate is, in the words of Lady Macbeth, "a tale…full of sound and fury signifying nothing."

The PTP will mitigate the potential for this to occur for the Transactions for which it is used by providing a common framework that shifts the focus from the words of the particular representation to the more fundamental question of whether the rep should be included in a particular Agreement at all.

Next month's article addresses the remaining provisions of Article 6.00 of the draft 2017 PTP, including the Parties' ability to include additional reps and warranties of the Vendor and Purchaser as required for the particular circumstances.

**2017 CAPL Property Transfer Procedure: Reps And Warranties-Part II**
**CAPL Negotiator, June, 2017 (Updated December, 2017)**
**Jim MacLean**

The second draft of the 2017 CAPL Property Transfer Procedure ("PTP") was made available to industry in late January through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 34 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the second draft relative to the initial July, 2016 draft; (vi) Word versions of the election sheet and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the draft in a new transaction; and (vii) a redline of the second draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that redline will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last 13 months by our 15 member committee.

Last month's article addressed the common reps in Clause 6.01 and the Vendor's reps and warranties in Paragraphs 6.02(a)-(t). This month's article offers additional context about Article 6.00 of the PTP by reviewing the remaining reps and warranties of the Vendor in Paragraphs 602(u)-(bb), the Purchaser's reps in Clause 6.04 and the remainder of the Article.

**Clause 6.02 – Vendor's Representations And Warranties**

<u>Area of Mutual Interest or Area of Exclusion (Paragraph 6.02(u))</u>: Except as identified in a Schedule, no Title and Operating Document includes an area of mutual interest or area of exclusion that is in effect as of the Effective Date.

Few P&S Agreements include this representation. It is an important item, though, particularly if the Purchaser intends to expand its position in the region. There is limited scope for application under new agreements, as the AMI term under those agreements tends to be relatively short. However, care must be taken for old agreements, as they occasionally include large, perpetual AMI obligations. This representation is particularly relevant if the transaction primarily involves undeveloped acreage.

This rep was modified in the 2017 PTP to extend to any area of exclusion obligation. While it is likely that any such obligation assumed by the Vendor would be personal to it, the Vendor should review any such document to ensure that it does not adversely affect the transaction. This reinforces to users why it is important to track these types of obligations carefully in internal records systems.

<u>No Notice of Offset Obligations (Paragraph 6.02(v))</u>: Except as identified in a Schedule, the Vendor has not received a notice from the applicable lessor that any Lease is subject to an offset obligation.

The representation is linked to the receipt of a lessor notice for two reasons, even though an offset notice as such is not required under a freehold lease. The first is that a potential Purchaser has the ability to conduct an initial due diligence review from public data sources. The second is that Crown offset notices are often discretionary, such that a notice from the Crown is required to trigger the obligation. Some agreements include an additional component in the provision, such as "and is not aware of any particular circumstance that has created such an offset obligation." However, a Vendor should be cautious about extending the scope of the application of this representation.

It is a good practice for a Vendor to review offsetting lands to determine if there is recent drilling activity that might cause an offset obligation, to make a note of any such well on the applicable lease file and to conduct such further investigations as may be appropriate in the circumstances.

No Commitment to Deliver (Paragraph 6.02(w)): J.V. Agreements sometimes include a requirement that an owner deliver all of its production from a designated area to a particular facility. This is typically not addressed in A&D Agreements, even though there could be a large negative impact on a Purchaser's regional strategy. Purchasers should review this issue very early in their due diligence process, even if this representation is not included.

This Paragraph was expanded in the 2017 PTP to address take or pay obligations for use of Tangibles or other facilities in addition to the commitment to deliver. (See also Paragraph 6.02(i).)

This rep includes an exception for Clause 1401 of the 1990 CAPL Operating Procedure. This is because of the limited commitment to deliver obligation with respect to "production facilities" operated thereunder. That being said, it is important for users to recall that the 1990 CAPL Operating Procedure and the subsequent updates cover minor production facilities originally designed solely for use in the exploitation of the lands subject to the applicable land agreement. (That commitment to deliver obligation was eliminated as of the 2007 CAPL Operating Procedure.)

Not a Disposition of Substantially all Vendor's Assets (Paragraph 6.02(x)): This rep is included because special shareholder approvals would be required if a Vendor were selling all or substantially all of its assets in the transaction. The advice of legal advisors would be required if it were apparent that this were an issue.

Leased Vehicles, Equipment and Premises (Paragraph 6.02(y)): This rep was introduced in the 2017 PTP. It will be important for a Purchaser becoming the operator of a property to understand the Tangibles, personal property and buildings that are owned and those that are only leased.

No Removal of Assets (Paragraph 6.02(z)): This representation was introduced in the 2017 PTP. Other than for any excess inventory belonging solely to it, the Vendor should not remove from the location of an operated property equipment that is serving the Assets, such as inventory owned for the joint account. (See also the removal obligation under Clause 11.03 if there is any excess inventory.)

It is the better practice to remove any such excess inventory on site before the Purchaser's site visit or to identify it clearly as inventory that will be removed prior to the Closing Date or shortly thereafter.

Quiet Enjoyment (Paragraph 6.02(aa)): Purchasers will often request a "quiet enjoyment" representation from the Vendor. The rep suggested by Purchasers is often too broad, as it may not recognize the interrelationship between the quiet enjoyment rep and the limitations applicable to the Vendor's delivery of the Assets - the other reps and warranties provided by the Vendor and the Permitted Encumbrances (includes the Title and Operating Documents and Title Defects that have been waived by the Purchaser). Failure to recognize that connection in the quiet enjoyment rep arguably eliminates much of the protection a Vendor intends with those limitations.

Additional Representations (Paragraph 6.02(bb)): Both Clause 6.02 and Clause 6.04 (Paragraph 6.04(f)) anticipate that the Parties may choose to include additional representations in the Head Agreement. Any such additional custom representation is treated in a consistent manner with those in the PTP, as if it had been made under Clause 6.02 or Clause 6.04.

One rep that will probably often be included in a Head Agreement pertains to long term inactive wells and facilities and the measures being taken by Regulatory Authorities at the relevant time to manage the abandonment and reclamation issues associated with orphan wells and facilities. Parties will increasingly choose to address this issue specifically in a rep because of the potential negative impact associated with the acquisition of an inactive well or an inactive multi-well facility under, for example, the Alberta AER requirements. Both Vendors and Purchasers should be aware of the requirements of the applicable Regulatory Authorities on this issue and the consequences of non-compliance. Although a very important issue, this was not included in the list of optional reps in Clause 6.02

because of the need to review the matter on a case-by-case with business and legal advisors if it is an issue and the degree to which the regulatory regime will continue to evolve. (See also the definition of Licencee Rating, Paragraphs 6.02(q) and 6.04(d), together with the associated annotations.)

Purchasers often request additional representations. Examples are reps that: (a) the Vendor has made reasonable inquiries and searches for material documents and information relating to the Assets and for all information reasonably required to ensure that its reps and warranties would not be misleading; (b) the Tangibles are suitable for the production of Petroleum Substances; (c) no Wells need to be abandoned; (d) there are no Environmental Liabilities of which a Purchaser should be aware; (e) to the knowledge of the Vendor, the production and financial data provided to the Purchaser were not materially inaccurate; and (f) the Vendor knows of nothing that would reasonably cause the Purchaser to wish to terminate the transaction. Some of these are far too broad, and attempt to pass business risk to the Vendor. The Vendor is not privy to the Purchaser's evaluations of the property, for example, and cannot be expected to know how it proposes to operate a property.

A Purchaser might also consider addressing some of the items noted above as part of its due diligence process or as a condition to Closing. Similarly, a Purchaser could also have a remedy for fraud in circumstances in which, for example, the financial information presented by a Vendor to the Purchaser/potential bidders was deliberately misleading.

**Clause 6.03 – No Additional Representations Or Warranties By Vendor (2000 PTP Clause 6.05)**

<u>Subclause 6.03A</u>: This Subclause was added in the 2017 PTP to reinforce that the Purchaser could not claim a breach of a rep insofar as the applicable matter were disclosed in the Agreement.

Agreements sometimes include language stating that the qualification extends to any matter, event or circumstance that was disclosed in the Agreement, in a data room or of which the Purchaser was otherwise aware. Subclause 6.05C offers a more balanced outcome. It allows either Party to raise as a potential defence with respect to a breach of a rep that the other Party did not rely on it.

<u>Subclauses 6.03B and C</u>: Subclause 6.05A of the 2000 PTP was substantially rewritten as Subclauses 6.03B and C of the 2017 document. Subclause 6.03B reinforces the “as is, where is” nature of the transaction by building on the first portion of the former Subclause 6.05A. Subclause 6.03C greatly expands the content that had been included in the last sentence of the former Subclause 6.05A with respect to the Purchaser’s due diligence inspection of the Assets and its analysis of the value of the Assets. Notwithstanding the expanded wording in these Subclauses relative to the 2000 document, the principles remain unchanged.

A prudent Purchaser will ask for copies of the Vendor’s environmental records respecting the Assets as part of its normal due diligence process (whether conducted under optional Article 8.00 or prior to execution of the Agreement, as contemplated in the introduction to Article 8.00). A Vendor that withholds records that the Purchaser had requested the opportunity to review potentially finds itself in breach of the rep about the provision of documents (Paragraph 6.02(p)) if it has been selected to apply. Even if that rep were not selected to apply, there could be extreme circumstances in which a conscious decision by the Vendor to withhold records or to disclose selective records that create a misleading presentation of the circumstances could leave it open to a claim for fraud. In this regard, it is important to remember that that a claim for fraud is not limited to the normal period prescribed for the survival of representations and warranties under Subclause 6.05A and Subclause 13.01C.

<u>Subclause 6.03D</u>: This Subclause is similar to Subclause 6.05B of the 2000 document. A similar provision is typically used in A&D Agreements.

The Vendor makes no reps respecting the Assets in addition to those provided in Clauses 6.01 and 6.02, including those made in the Head Agreement under Paragraph 6.02(bb). The Vendor has generally provided information in its possession to the Purchaser to assist the Purchaser to conduct its own evaluation of the Assets. The Vendor did so without any intention of guaranteeing that the information was accurate. Excepting fraud on the part of the Vendor and the Vendor's responsibility for its reps on the basis provided in the Agreement, the acquisition of the Assets is ultimately a business decision of the Purchaser, based on its assessment of the accuracy of all available data.

The Vendor has three reasons for the inclusion of this type of Subclause.

Firstly, the Vendor wishes to reinforce that the Purchaser relies on information outside the contract at its own risk. Except as provided in the Agreement, it is responsible for conducting its own evaluation of the Assets. Any information provided by the Vendor, such as a contract summary from a land information system, is intended to assist the Purchaser in its due diligence review, not to replace it.

Secondly, the inclusion of representations/information outside of the Agreement poses difficult proof problems, even assuming that the "parol evidence rule" (a general prohibition on consideration by a court of negotiations/collateral representations outside the contract) could be overcome by the Purchaser. It would be difficult to prove if and how the alleged information was provided and the degree of the Purchaser's reliance thereon.

The most practical reason, though, is that a Vendor wishes to minimize the possibility that unauthorized personnel and authorized, but uninformed, personnel could make statements that would impact the Parties' contractual arrangement. It is common for the Purchaser's representatives to be in contact with a number of the Vendor's representatives at any time, requesting various pieces of information. In their desire to assist, the Vendor's personnel occasionally provide honest, but incorrect advice, largely because the Purchaser's representatives often request an immediate response.

The probable result of the exclusion of the general release would be the creation of a very formalized process. Each Party would designate a representative through which all questions and answers would be directed in writing. In practice, the cost of such a mechanism seems to exceed the perceived benefit of the change when dealing with credible parties.

**Clause 6.04 – Purchaser's Representations And Warranties (2000 PTP Clause 6.03)**

<u>Investment Canada Act (Paragraph 6.04(a))</u>: Notwithstanding the brief references to the *Investment Canada Act* (Canada) and the *Competition Act* (Canada) in the PTP, it is unlikely that the PTP would be used in practice for any disposition that would be subject to review under either of those Acts. In the unlikely event that the PTP were used for any Transaction that was reviewable under one or both of those Acts, legal assistance would be required to address the process to be used by the Parties.

The references included in the annotations about those Acts are primarily included to offer a general context for users because of the likely use of this document as a reference document. This offers a context about the requirements that could apply to larger transactions. The *Investment Canada Act* (Canada) is considered briefly in the annotations on Paragraph 10.01(a), for example. If the transaction is "reviewable" under that Act, Paragraph 10.01(a) will apply.

<u>No Lawsuits or Claims (Paragraph 6.04(b))</u>: This rep was introduced in the 2017 PTP to offer similar protection as that offered to the Purchaser under Paragraph 6.02(b). While unlikely, the Purchaser could be subject to legal proceedings that could threaten its ability to complete the transaction. The Vendor would need to assess the risk of Closing occurring if this were a potential issue.

<u>Acquiring as Principal (Paragraphs 6.04(c))</u>: The Vendor wants to be able to enforce the Purchaser's ongoing obligations under the Agreement against it. Recognition of potential risks in this area also reinforces to the Vendor's personnel that ongoing obligations, such as liability and indemnification obligations, are ultimately only as good as the financial viability of the Party that has those obligations.

Wells and Tangibles Transfers (Paragraph 6.04(d)): Given potential restrictions on the transfer of licences under the Regulations, the Purchaser represents that it is eligible to accept a transfer of the licence for Wells and Tangibles anticipated to be operated by it. A Vendor must carefully screen potential buyers and only attempt to dispose of properties to a financially viable Purchaser.

The Purchaser sometimes will not be able to make this rep as of the Effective Date. It will need to be modified for those cases, so that the required steps to become eligible have been completed by Closing. This would typically require identification of the eligibility gaps to the Vendor. The rep could have been structured more broadly to apply the eligibility test only as of Closing. This was not done because of the Vendor's need to understand any eligibility issues in this area early in the transaction.

As noted in the annotations on the definition of Licencee Rating, Clause 3.04, Clause 3.06, Paragraph 6.02(q) and Paragraph 10.01(e), the onus is on the Parties to work with their business and legal advisors to add custom content in their Head Agreement to address their particular circumstances and needs if there are any contemplated issues about the transfer of Well licences in addition to the condition to Closing in Paragraph 10.01(e). Reviewing the Regulations for a Transaction is particularly important if they include a requirement for a review of a proposed transfer of a regulatory licence, permit or approval through a process in which that approval might not be granted, since this could require the inclusion of a Closing in escrow process in the Agreement. The fluidity of the Regulations on this area over time and across jurisdictions was also such that any more specific handling of the issue in this document would potentially create unintended consequences for the Parties over time.

Simplifying the review of the other procedural aspects of the overall transaction through use of the PTP facilitates a more focused examination of this important business issue by the Parties' representatives relative to what would be the case without the PTP.

Financial Capacity (Paragraph 6.04(e)): Subject to any condition to Closing respecting financing, the Purchaser represents that it has the available funds to make the payments required by it at Closing and to perform any other financial commitments required under the Head Agreement.

**Clause 6.05 – Survival Of Representations And Warranties (2000 PTP Clause 6.04)**

Subclause 6.05A: The representations and warranties are to be true on the Effective Date, at execution of the Agreement and at the Closing Time. A rep that was true at the Effective Date would be of little comfort to a Purchaser if it was not also true at Closing.

The representations and warranties will not survive Closing unless the provision states that they are to survive beyond Closing. Although the inclusion of a limited survival period is generally accepted, the duration of the period has sometimes been a matter of negotiation. The norm has become 12 months for material transactions, with six months sometimes used for minor transactions involving non-operated properties or only undeveloped lands.

The survival period was modified from a negotiated number of months to one year in the 2017 PTP to reflect the most typical outcome. Parties that prefer a different survival period in this Subclause and Subclause 13.01C remain free to negotiate a different time period.

This Subclause does not go so far as to state that the representations and warranties cease to have any effect at the end of the prescribed period because of the exception for fraud noted in Subclause 6.05B and the related annotations.

The survival period for representations and warranties in this Subclause does not enable the Vendor to avoid its contractual obligations for J.V. and royalty audits under Subclause 4.02C, however.

Subclause 6.05B: If a representation or warranty was made fraudulently, the limited survival period probably would not prevent a Party from subsequently pursuing its full legal rights within the normal legal limitation period prescribed under the *Limitations Act*. However, the inclusion of the exception for fraud provides Purchasers with additional comfort, and should be of no concern to a Vendor that is processing its divestitures properly.

A Party claiming a breach of a representation or warranty after Closing must do so by providing notice with reasonable particulars about the alleged breach within the prescribed period, subject to the qualification for fraud noted above. It has no basis to make any further claim for that breach if it misses the prescribed period within which to make a claim.

Subclause 6.05C: Vendors occasionally include a provision whereby a Purchaser would be prohibited from commencing an action for any rep if the Purchaser had any knowledge that would cause it to question the truth of that rep. A Purchaser pursuing a claim for damages for the breach of a rep would be required to convince a court that there had been a breach of the rep to its detriment and, if so, to prove that the damages suffered by it resulted from its reliance on the rep.

It would seem difficult for a Purchaser to make this argument if it had knowledge at the time that indicated that it was not relying on the rep. Although the defence might also be available at common law in the absence of this Subclause, the document states that a Party may offer as a possible defence that the other Party was aware, prior to Closing, of the matter that forms the basis of its claim for breach of a rep and that it chose to proceed with Closing anyway. However, the success of the defence would ultimately depend on the facts.

Purchasers sometimes request amendments to provisions like Clauses 6.03 and 6.05 whereby there is a recognition that the Parties have, in fact, relied on the representations and warranties made by the other Party under this Article. This is inappropriate. The other Party would not have relied on the representation if it knew that it was untrue, but Closed anyway.

Subclause 6.05D: This Subclause was introduced in the 2017 document to try to mitigate the risk that the survival periods for representations and warranties under this Clause and Clause 13.01 might not be effective because of the potential application of Subsection 7(2) of the *Limitations Act* (Alberta).

There has been some uncertainty as to whether that Subsection might impact the typical practice to include survival periods on reps and warranties in commercial agreements. This topic was considered in the 2015 Alberta case of NOV Enerflow v. Enerflow Industries Inc. The Court found that sophisticated contracting parties are free to agree to expiration dates for reps and warranties in a contract. It also found that a party making a claim for breach of one or more reps and warranties could not make a very broad claim initially and then modify its claim to add additional breaches of unrelated reps and warranties after expiry of the survival period for the reps and warranties.

**Takin' Care Of Business**

The representations and warranties provision has historically been one of the most heavily negotiated provisions of A&D Agreements with respect to both the types of representations that are to be included and their wording. As noted in last month's article, the PTP mitigates the potential for this to occur for the transactions for which the PTP is designed by providing a common framework that allows the Parties to focus on the more substantive business issues associated with their transaction.

We will be issuing what is expected to be the final industry draft of the PTP in June.

**2017 CAPL Property Transfer Procedure: "Taking It Out For A Test Drive"**
**CAPL Negotiator, October, 2017**
**Jim MacLean**

The third draft of the 2017 CAPL Property Transfer Procedure ("PTP") was made available to industry in July through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed 36 page matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 20 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the third draft relative to the January, 2017 draft; (vi) Word versions of the election sheets and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the draft in a new transaction; and (vii) a redline of the third draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that redline will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last 18 months by our 15 member committee.

The June article was the second article about Article 6.00 of the PTP, which relates to the Parties' representations and warranties.

This month's article is completely different from the other articles in this series. As a number of individuals have been using earlier drafts of the PTP in their recent low to modest value transactions, this article provides them a platform to comment on their experiences in using the new document.

**Moving From "Lab Tests" To "Road Tests"**

The Committee members used our collective experience with transactions to try to design the PTP in a way that would optimize the outcomes for users. As shown by the redline to the 2000 PTP and the 36 page matrix outlining changes relative to the 2000 PTP, this was a very labour intensive process that saw the Committee evaluate the document very critically. We also prepared five sample case studies to test the potential application of the PTP to a broad range of transactions, and have included those materials in Addendums at the end of the document for context and as potential reference documents.

Some companies that had been using the 2000 PTP for selective transactions recognized the major uplifts offered in the pending 2017 PTP. As a consequence, they took this one step further than the "lab tests" presented in the Addendums. They have already taken the document out for a "road test" by using prior drafts of the 2017 PTP in certain low to modest value transactions.

As shown in the verbatim comments below, their experiences in using the PTP for their real world transactions were very positive.

Larry Buzan, CAPL President and Land Manager at Prairie Storm Energy Corp.:

> *Prairie Storm Energy Corp. has found the early draft 2017 PTP form very useful, both as a training tool for our land department, and as an aid to closing five transactions under $1MM these past 3 months. The introduction of the preferred use of the 2017 doc to our Vendors has been positive, especially when the previous history for each had been lawyers, a myriad of draft reviews and of course, the inevitable last minute changes and stress that comes with it. The 2017 doc afforded all the parties time to review it, confirm the elections and the simplicity of the final doc itself. We were able to easily accommodate changes to the Head Agreement in each case, and particularly when we had related closings under the same agreements, the process was made that much easier.*

*I would say that this 2017 PTP form even in its earlier draft forms created a new conversation for us here in our land department and raised the bar for those who worked with us to transact.*

Lynn Gregory, Manager of Contracts and Land Administration at Velvet Energy Ltd. and member of the 2017 CAPL Property Transfer Procedure Committee:

*Velvet Energy Ltd. has used the 2000 and the current circulating 2017 version of the Property Transfer Procedure ("PTP") for 15 transactions since 2013. We have been both Vendor/Transferor and Purchaser/Transferee and used the procedure in simple Purchase and Sale Agreements and also with a number of Asset Exchange Agreements. The transactions varied from undeveloped lands only through to producing assets with wells and related tangibles covering values between $10,000.00 and $15,000,000.00. Using the PTP has allowed Velvet to close the transactions quicker and has not found any party unwilling to endorse and use the PTP when we've proposed it. There have been times that amendments are required due to unusual terms or additional undertakings between the parties, however, modifications in the Head Agreements have allowed those negotiations to be easily captured. The content of the document is sound, resulting in little, if any, discussion between the parties which results in reduced cycle time providing the ability to close quickly depending on the asset, due diligence, ROFRs, etc.*

*A portion of the enhancements in the 2017 includes the reduction in the number of elections that required negotiation between the parties under the 2000 version. The election sheet provided in the package guides users to those removed elections, offering the parties the opportunity to either accept the elections as drafted or negotiate an alternate outcome with a simple amendment in the Head Agreement. The addition of the choices to conduct due diligence prior to execution of the P&S and to remove the calculation of per diem rentals, together with all of other enhancements made to the 2000 version, warrant review and consideration for your future transactions. We intend to continue using the PTP whenever we can and encourage others to consider a similar decision.*

James O'Connor, Vice President Land, Westbrick Energy Ltd. and member of the 2017 CAPL Property Transfer Procedure Committee:

*The PTP has been an integral part of a very active acquisition program over the last 5 years at Westbrick. We have built our asset base in the trenches through numerous small acquisitions as opposed to one large transaction. Westbrick is still a small shop without an A&D or legal department and part of the advantage is our ability to move very quickly from negotiation to closing once deal terms are agreed. The PTP allows the parties to proceed very quickly without getting bogged down in a protracted negotiation of a PSA. I can think of at least four or five smaller transactions in the last few years involving a section or two and a producing vertical well that we were able to close within a week of agreeing on terms using the PTP.*

*We have used the draft PTP for several transactions, once with another member of the Committee and other times with new users who were familiar with the 2000 PTP. For example, we recently used the 2017 draft PTP to close a fairly complex transaction which was an asset exchange of a significant producing property for cash and some undeveloped land. Both parties were open to using the document and it was easily adaptable to suit the particular circumstances of the transaction. We were able finalize the agreement and move to close quickly and efficiently.*

Brock Young, Senior Vice President, Land, Sinopec Daylight Energy Ltd. and member of the 2017 CAPL Property Transfer Procedure Committee:

*I have found that the majority of the transactions we have been working on over the past few years have been land consolidation type swaps, acquisitions and dispositions. The Property*

*Transfer Procedure ("PTP") has proved to be an excellent option for these types of deals. We have recently entered into an agreement with a third party and have agreed to use the June 25, 2017 draft of the PTP. It is a simple deal to acquire a partner's working interest in joint lands along with a few joint wells so the Head Agreement was very easy to put together. Our partner had used the 2000 PTP in the past and was very receptive to using the modernized 2017 draft for this transaction. We required minimal modifications and therefore we were able to finalize the agreement quickly with very little administrative effort.*

*The 2017 PTP is intended for smaller deals but is set up such that it could be used for larger transactions as well. Sinopec Canada will continue to use our precedent PSA for larger deals but will use the 2017 PTP for the more modest straight forward transactions. With the number of undeveloped land swaps and working interest consolidation deals going on in the current environment I believe this agreement will catch on quickly given its ability to ease the administrative burden and greatly reduce the cycle time in finalizing A&D transactions. I believe many of the smaller players will utilize this document given its ease of use but will also have many applications for the larger companies as well.*

**Who Wants To Take The "2017 Property Transfer Procedure Challenge"?**

The experiences to date with the 2017 PTP validate our belief that the 2017 document will, in fact, enable CAPL to enhance industry's transactional efficiency significantly by "making simple transactions simple again."

Although some users have already begun to use the draft document in their current transactions, the reality is that most of us will not be sufficiently comfortable with the 2017 Property Transfer Procedure to use a draft of that document in a current transaction.

So, perhaps take the "2017 PTP Challenge" instead.

Why not take a recent low to modest value, straightforward transaction for a developed or undeveloped property and see how you would have managed that transaction with the PTP and compare the outcomes? This would offer you context about the degree to which the PTP can enhance the efficiency with which you negotiate your agreement and are able to move future transactions to closing in a timely manner. You can get a pretty good sense of this by working from the election sheet in Addendum I of the draft PTP and the applicable case study template from the sample alternatives presented in Addendums III-VII.

Give it a try and let us know what you think. More importantly, tell your peers and encourage them to take the "2017 PTP Challenge" too.

The July draft was the third draft issued for industry comment. In the absence of surprises, we will work collaboratively with commenting parties to complete the document late this year.

**2017 CAPL Property Transfer Procedure: The Due Diligence Process**
**CAPL Negotiator, November, 2017 (Updated December, 2017)**
**Jim MacLean**

The third draft of the 2017 CAPL Property Transfer Procedure (“PTP”) was made available to industry in July through a web enabled distribution. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed 36 page matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a 20 page coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the third draft relative to the January, 2017 draft; (vi) Word versions of the election sheets and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the draft in a new transaction; and (vii) a redline of the third draft relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that redline will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last 18 months by our 15 member committee.

The October article was about the experiences of some of the users who have used drafts of the 2017 PTP for new transactions. It ended with a suggestion that readers take the “2017 PTP Challenge” by comparing how one of their recent low to modest value, relatively straightforward transactions could be documented using the 2017 PTP as a foundation.

This month’s article is about the due diligence process, and relates primarily to Article 8.00 of the PTP.

**Vendors, Please, Please, Pretty Please Understand Your Assets!**

A Vendor should consider conducting a due diligence review of a property to be divested prior to the sale process whenever feasible. This review would include a review of all material aspects of the property, including land records, J.V. records, Surface records, HSE records, marketing arrangements, production accounting and a review with the applicable field personnel of the operational aspects of the applicable assets.

There are several reasons why the Vendor should conduct this type of review for the typical low to modest value property for which the PTP is most likely to be used.

A Vendor that prepares well for a sale has a very good basis on which to determine the value of its property and to present the property optimally to a potential Purchaser in order to help the Purchaser see that value when preparing its offer.

This type of review also enables the Vendor to describe the property in the manner contemplated in the PTP with respect to such matters as land agreements, applicable ROFRs, J.V. type agreements, marketing arrangements, a list of Wells, the exclusion of certain surface rights, the identification of Facilities and Tangibles, any potential issues in the transfer of regulatory licences and other approvals, any outstanding production accounting issues and any required qualifications to the representations and warranties in Article 6.00. This information would, in turn, also be used to simplify preparation of the Specific Conveyances for Closing.

This review also has the major benefit of mitigating the potential for either Party to be surprised during the Purchaser’s due diligence process. Not doing this work in advance leaves the Vendor vulnerable to price erosion or possibly even loss of the deal in an extreme case if the Purchaser’s due diligence process were to identify material problems with the property.

A prior review, for example, would allow the Vendor to attempt to address title deficiencies it believes are material early in the transaction cycle, and would mitigate the potential for issues prior to Closing.

Put simply, a Vendor is trying to sell a product in a competitive marketplace. Its ability to optimize sale outcomes and its “brand” as a Vendor more generally will be influenced by the quality and integrity of the information it uses to present its properties to potential Purchasers.

**Due Diligence Without A Due Diligence Provision?**

The starting point in a review of the 2017 PTP due diligence provisions is to note the major change whereby the Article 8.00 Purchaser’s review process is structured as an optional Article.

This does not reflect a perspective that a Purchaser should not conduct its normal due diligence review or that it is precluded from conducting such a review. Instead, it reflects the view of an increasing number of Parties that they are unwilling to sign an Agreement until the Purchaser’s due diligence review is complete and the Vendor understands the concerns, if any, being raised by the Purchaser about the Assets.

Proponents of this approach believe that it provides each Party with greater control over any negotiations required to resolve any negative matters encountered in the due diligence review, and ultimately increases deal certainty if the Parties are able to resolve those matters. This approach allows each Party to know if there are material problems before execution, rather than finding themselves in a potential lingering dispute after the Agreement is executed. This binary close/don’t close approach may be particularly attractive for the more straightforward Assets for which the PTP would typically be used, and it also offers a significant potential simplification if the Assets comprise only undeveloped lands.

Even if Article 8.00 is not selected to apply, the introduction of Article 8.00 creates protections for each Party with respect to whatever due diligence process was conducted before execution of the Agreement. The duties in Clause 8.01 apply to the Vendor with respect to the access it provided for the Purchaser’s due diligence review prior to execution of the Agreement (something that should be reinforced in a letter of intent), and the indemnification obligations in the last paragraph of that Clause apply to the Purchaser for its due diligence review. (See also the Vendor’s representation about the provision of documents in Paragraph 6.02(p).) Similarly, Subclause 8.02D applies to any such due diligence review to ensure that the Purchaser is in the same position after Closing as it would have been if it had acquired the Assets in an Agreement in which Article 8.00 was selected to apply.

**Due Diligence Other Than Title Review**

Clause 8.01 of the PTP imposes a duty on the Vendor to provide the Purchaser's nominees with reasonable access to records and a reasonable opportunity for a field inspection of the Assets, and this is reinforced in optional rep 6.02(p).

However, the PTP is otherwise silent about due diligence concerns that do not pertain to the Vendor’s title (e.g., environmental condition, confirmation of production data, confirmation or condition of Tangibles). Because of the wide variance in expectations on those issues and the likelihood that transaction specific provisions would need to be negotiated, we chose not to address those issues in the PTP. Instead, we noted in the annotations that Parties should address their expectations about any issues of this type in their Head Agreement, and noted that they would probably often choose to do so through the inclusion of additional conditions to Closing under Clause 10.02.

Examples of conditions to Closing that Purchasers might attempt to negotiate relate to such matters as: (a) specified approvals under the Regulations; (b) an environmental review; (c) a production audit to confirm that production and accounting data provided to it were accurate and to confirm current production rates; (d) a physical inspection of the Assets to ensure that they are in good working condition; and (e) a review of J.V. processing arrangements, marketing arrangements, etc.

There are two important considerations for a Vendor to keep in mind when reviewing the potential inclusion of these types of additional conditions.

The first is to ensure that any conditions like items (b)-(e) above are presented in the context of a discretion that must be exercised reasonably. The inclusion of a condition to Closing linked to the subjective discretion of the Vendor or its business or legal advisors, for example, potentially turns the transaction into "an option to purchase." This should be of particular concern during a period of volatile commodity prices.

The second is that it will often be desirable to use a date significantly earlier than the Closing Time as the trigger date for any such conditions. Otherwise, the Vendor could discover that the Purchaser will be exercising its right to terminate the transaction two days before Closing. Addressing those types of conditions early in the process also allows the Vendor to consider an alternate Purchaser much earlier than would otherwise be the case. This is particularly important if a property is being sold through a competitive bidding mechanism or close to year end. (See also Subclause 10.05C, which operates to waive any such condition in the absence of notification by the applicable Party by the specified date that the condition has not been satisfied.)

A sample of this type of condition follows: *"_____ Review: The Purchaser will have completed a review of ________________ prior to ____________, through which the Purchaser is satisfied, acting reasonably, with _____________."*

As noted in the annotations on the definition of Environmental Liabilities and on Paragraph 8.01(b), Purchasers will sometimes structure a condition about the status of Environmental Liabilities that is also linked to an environmental defects provision analogous to the Title Defects procedure in Alternate 8.02B(2). This would allow modifications to the Purchase Price and a potential termination right at certain value thresholds. This structure would more typically be used for larger value transactions, though, so has not been included in the PTP.

**Title Defects**

The foundation of the Article 8.00 title review process is the definition of "Title Defects". In essence, it is an attempt to link the title review process to deficiencies in title that would be regarded as material to purchasers assessing the Assets in an objective manner. This definition reflects the practical consideration that many of the deficiencies that are presented as title defects by Purchasers are immaterial, and only operate to frustrate the ability of both Parties to complete the transaction by the contemplated Closing Date.

The definition has been included to: (a) introduce an element of objectivity into the process; (b) focus the attention of the Parties on items that matter; and (c) ensure that the title review process does not turn the transaction into an "option to purchase", under which a Purchaser can, in effect, terminate the transaction at will if, for example, it "does not receive a title opinion satisfactory to it from its solicitors."

The 2017 definition has been updated to include two Alternates.

Alternate 1 is similar to the 2000 definition. It is a much less prescriptive definition than Alternate 2. Alternate 1 should be used if Alternate 1 of Subclause 8.02B is selected, although it could still be used if Alternate 2 of Subclause 8.02B were selected.

Alternate 2 is a more elaborate definition, and is designed primarily for use with Alternate 2 of Subclause 8.02B. It identifies items that are Title Defects. However, it also specifies a number of items that are not to be regarded as Title Defects, and this type of definition sometimes includes items that are very “Vendor friendly.”

Some Vendors require this type of definition for at least their larger value Transactions because of negative experiences in which Purchasers have attempted to use the title review process to attempt to negotiate a reduction of the Purchase Price for purported “defects” that are, in practice, remote risks that the Vendor would often be unable to address. Should a Vendor be expected to prove payment of an Alberta Crown rental in 1974, for example, when it is clear that the Lease has not reverted to the Crown? Similarly, is it feasible to be able to provide proof of payment of a freehold rental from 1962 if there is no proof of payment on file, nothing on file to indicate any concern by the lessor at the time and ongoing communications with the lessor that are fully consistent with a mutual belief that the freehold lease remains in good standing?

As noted in more detail in the annotations, this Alternate was designed to offer a reasonably balanced handling of the concept between Vendors and Purchasers, recognizing that some Vendors will attempt to broaden this Alternate if it is selected and that some Purchasers will attempt to narrow it.

**Clause 8.02 Title Review Process**

The title review process can be one of the most frustrating aspects of a transaction, notwithstanding that the bells and whistles of industry agreements are ultimately used relatively infrequently to exclude Assets from Closing.  No matter which form of agreement the Parties choose to use for a transaction, the annotations on Clause 8.02 offer insights about the title review process that can be helpful to both Vendors and Purchasers for their transaction.

<u>Subclause 8.02A</u>:  The Purchaser is to notify the Vendor of Title Defects at least seven business days prior to the Scheduled Closing Date or another agreed upon date (as compared to a negotiated period in the 2000 PTP), although it is often advantageous if items are disclosed to the Vendor as discovered.  The Vendor is to respond not later than three business days prior to that date.

These are arbitrary periods, premised on the assumption that the title review will be a relatively straightforward process, and they can be modified easily for any particular transaction.  If the Land Schedule is complex, this may not be feasible.  The notice period will sometimes have to be modified (or Closing delayed) to provide the Purchaser with an additional opportunity to complete its review. If Closing is to be delayed while the Title Defects are being remedied, the Parties should address their expectations at the time about the handling of any interest that would otherwise accrue during that period under Clause 2.06.

It is critical for Purchasers to retain the responsibility for management of the title review process, so that the transaction is conducted efficiently. If the property is complex, it may be beneficial for the applicable Land personnel responsible for Closing to meet early to discuss the process to move towards Closing and the respective expectations for managing the title review process.

The title opinion of the Purchaser's solicitors will often list many title deficiencies.  Many, though, will not fall within the definition of Title Defects.  A Vendor generally wishes to cooperate with both the Purchaser and its solicitors in the due diligence review, but cannot be expected to devote significant effort to the review of immaterial title deficiencies. To minimize this possibility, the Purchaser is to provide notice of the Title Defects, the Affected Assets, a list of missing documents and the Purchaser's requirements for rectification.

This encourages a Purchaser to screen its solicitors’ title opinion, by focusing the Vendor’s efforts on those Title Defects that matter to the Purchaser. It must determine which deficiencies are Title Defects and the actions that will be required to rectify them.  Subject to the exceptions in Subclause 8.02D, the provision is also structured to prevent the Purchaser from surprising the Vendor with additional Title Defects after the prescribed notification deadline.

Subclause 8.02B: This Subclause addresses the impact of Title Defects on Closing, and can only apply if the Purchaser has served a notice under Subclause 8.02A. (There are only rights under this Subclause if a notice of Title Defects was served by the required time.) It includes two Alternates.

Alternate 8.02B(1) provides the Purchaser with three options. It can: (a) provide the Vendor with additional time to remedy the Title Defects by delaying the Closing Time to such date as the Parties may agree; (b) waive the uncured Title Defects and proceed with Closing; or (c) terminate the transaction. Alternate 1 of the definition of Title Defects should be used if Alternate 8.02B(1) is selected.

That being said, the construction of this Alternate is ultimately binary. Unless otherwise agreed by the Parties, the ultimate choice of the Purchaser is to proceed to Closing or to terminate the transaction. The major advantages of this approach are its relative simplicity and the prohibition of "cherry picking", such that it can be particularly attractive for minor value transactions. In addition to avoiding the potential for cherry picking, this mechanism also avoids the valuation problems inherent with the potential exclusion of portions of the Assets. It also assumes, though, that the Vendor would be able to find an alternative Purchaser easily, something which may not be true.

There is a risk that a Purchaser might terminate a Transaction under this Alternate if there are Title Defects for which the value of the Affected Assets is not material to the entire Transaction. This could place a Vendor at significant risk during a period of volatile prices. Parties will sometimes modify this Alternate to include a requirement of a minimum value threshold before the Purchaser can exercise this termination right.

Alternate 8.02B(2) includes greater flexibility in the handling of the Title Defects, and it would typically be used in conjunction with Alternate 2 of the definition of Title Defects. Closing will proceed if the value of the outstanding Title Defects is below a threshold of 10% of the Base Purchase Price. The sample election sheet included as Addendum I reminds users that the typical 10% threshold might not provide a suitable result for a minor value transaction if they choose to select Alternate 8.02B(2).

If the value of uncured Title Defects is above the 10% threshold, the Purchaser has four options: (a) to provide the Vendor with additional time to remedy the Title Defects by delaying Closing to an agreed date; (b) to waive the uncured Title Defects and to proceed with Closing; (c) to proceed with Closing for the Assets not affected by the Title Defects, with the consideration being reduced accordingly, insofar as that value is greater than the 10% threshold; or (d) to terminate the Agreement if at least 25% of the consideration is applicable to the Assets affected by the uncured Title Defects. However, the Vendor may also terminate the Agreement if the Purchaser is proposing to exclude Assets with a value of at least 25% of the Purchase Price under Paragraph B(c). (The Parties also always have a fifth option in practice, to substitute other mutually agreed upon assets of the Vendor.)

Some Vendors prefer a variation to Paragraph (c), so that the Purchaser acquires the Affected Assets with a reduction in the Base Purchase Price. This is designed so that a Vendor is not required to retain Assets that would be difficult to dispose separately. There is an associated risk, though, that this could potentially encourage a Purchaser to identify Title Defects in order to attempt to acquire all of the Assets at a lower Base Purchase Price.

The 10% threshold in Paragraph (c) of this Alternate is, in effect, a deductible. In the absence of the deductible aspect, Purchasers would be encouraged to raise additional concerns to try to satisfy the 10% threshold and obtain a full recovery, an approach that the PTP does not reinforce.

The thresholds in Paragraphs (c) and (d) of this Alternate were modified from a blank to be negotiated for each Transaction in the 2000 PTP to 25% as of the 2017 PTP. This was done to reflect the most typical negotiated outcome and to reduce the number of elections associated with use of the PTP. The Parties always remain free to negotiate a different handling in any particular transaction, and the bolded paragraph in the sample annotated Schedule of Elections and Modifications in Addendum I reminds users to review the default values included in the 2017 PTP.

Paragraph (d) of this Alternate and Subclause 7.01E were updated significantly in the 2017 PTP. The 2000 PTP had been structured so that the threshold in Paragraph (d) was a negotiated threshold for the combination of Title Defects and ROFR exercises. As of the 2017 PTP, the two processes are independent.

Subclause 8.02D: If a Purchaser Closes with respect to Assets, the Purchaser generally should not be able to assert after Closing that there are Title Defects. Subclause D addresses this. However, it is possible that Title Defects may subsequently be discovered after Closing in circumstances in which it would not be appropriate to preclude the Purchaser from a potential remedy. The primary examples of the latter would be Title Defects that were: (a) not apparent because of the Vendor's failure to provide access to the required files in violation of Paragraphs 6.02(p) and 8.01(a); (b) created as a result of the Vendor's breach of its maintenance of business obligations under Clause 5.03; and (c) subject to Clauses 6.05 and 13.01, in violation of the Vendor's representations and warranties under Article 6.00. The qualifications to Clause 6.05 address both the time limitation and the ability of the Vendor to raise a "no reliance" defence if appropriate in the circumstances.

Subclause 8.02E: There may not have been any prior agreement with respect to the portion of the Purchase Price that is attributable to the Assets affected by the Title Defects. This Subclause addresses the determination of the value if the Parties proceed with Closing for the Assets not affected by the Title Defects. In essence, the Purchaser would make a good faith estimate of that value, pending the resolution of the value of the Affected Assets by agreement of the Parties or under Article 9.00 (negotiation/arbitration). They would accelerate any such arbitration.

Subclause 8.02F: The Vendor will often rectify uncured Title Defects for excluded Assets shortly following Closing. The Vendor may, at its option, require the Purchaser to complete the acquisition of those Assets on the same basis as in the Agreement, subject to any obligation to issue ROFR notices again. Including this as an option of the Vendor is a disincentive for Purchasers to exclude Assets, as there is no right to re-acquire the excluded Assets. Similarly, the Purchaser is under no obligation to acquire excluded Assets if the Vendor is unable to remedy the applicable Title Defects within 30 days after the initial Closing. That being said, there may be circumstances in which the Purchaser would still be interested in acquiring the applicable Assets if the applicable Title Defects were remedied at a later date. The Parties will enter into a separate Agreement for the acquisition of the applicable Assets in the form of the Agreement, except that Clause 2.06 interest would not accrue for the period prior to the Vendor's notice under this Subclause. As this is a separate Agreement, it would use the original Effective Date, but would have its own Closing Date.

Subclause 8.02G: This Subclause protects the Vendor against the possibility that the Purchaser may attempt to terminate the Transaction under Paragraph (d) of Alternate 2 of Subclause 8.02B in circumstances in which the Vendor believes that the values attributed to the Title Defects have been inflated. This Subclause enables a Vendor to delay the Closing Time until two business days following a determination of the applicable value under Article 9.00. At that point, the Purchaser may again make the election under Subclause 8.02B, subject to any obligation to issue ROFR notices again. The Vendor would also presumably be attempting to remedy outstanding Title Defects during that period as well.

**Would You Rather Have A Title Review Or A Root Canal?**

Let’s be honest, the title review process can, well, be painful.

It can be much less painful, though, if each Party prepares suitably for the process.

The Vendor can make the process much less frustrating for its own personnel and the Purchaser by doing a reasonably detailed due diligence review early in the divestiture process, by identifying and beginning to address material title deficiencies and by presenting a high quality Land Schedule and list of wells, by presenting its file materials in a reasonably organized manner and by making its personnel available to answer questions of the Purchaser’s representatives.

The Purchaser can make the process much less frustrating for its own project personnel and the Vendor if the Purchaser’s business representatives engage in the process sufficiently to ensure that the concerns being identified to the Vendor are truly material to it, rather than just the shopping list of material and immaterial deficiencies identified during its title review. The Purchaser should also ensure that its representatives commence the title review in a timely manner, conduct it diligently and identify major concerns to the Vendor at the earliest opportunity.

The annotations on Article 8.00 offer a helpful reference for personnel involved in A&D transactions, even if the PTP is not being used for a particular transaction.

**Tick, Tock**

The July draft was the third draft issued for industry comment. In the absence of surprises, we will work collaboratively with commenting parties to complete the document late this year.

**2017 CAPL Property Transfer Procedure: Transfers Of Regulatory Licences**
**CAPL Negotiator, January, 2018**
**Jim MacLean**

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December. The package on the CAPL web page includes: (i) an overview of the project scope and the major changes relative to the 2000 PTP; (ii) a detailed 39 page matrix that outlines all material changes relative to the 2000 PTP and their rationale; (iii) a clean copy of the text and annotations; (iv) a coded comment matrix that presents the detailed verbatim comments we received from a modest number of commenting parties, together with our responses to each individual comment; (v) a redline of the final document relative to the July, 2017 draft; (vi) Word versions of the election sheets and the case studies included as Addendums to the PTP to facilitate early use of the PTP for anyone that wishes to use the document in a new transaction; (vii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (viii) a redline of the final document relative to the 2000 PTP. While we do not expect that the redline to the 2000 PTP will be reviewed in any detail, we believe that even a cursory glance at that redline will demonstrate convincingly the thought and effort that has been invested in the 2017 document over the last 20 months by our 15 member committee.

The November article was about the due diligence process. This month's article is about the process of transferring well and tangibles licences under the Regulations and the endorsement of the PTP.

**AER Bulletin 2017-13 Has Changed The Goal Posts**

The Alberta Energy Regulator issued Bulletin 2017-13 in late July. It introduces major changes to the process of transferring licences in a way that will have a significant impact on the manner in which industry's A&D transactions are conducted.

Some of the major elements of the AER's modified process for handling licence transfers are:

-a requirement to bundle all transfers from one holder to another associated with a transfer;

-a standard review period of 30 days before a decision is issued by the AER;

-publication of transfer applications to allow for the filing of a "statement of concern";

-further potential delays in effecting transfers if there are any "statements of concern", as the AER will typically request, as a minimum, that the transferor respond to the filer of the statement of concern in writing.

This Bulletin will see major changes in the manner in which industry will often negotiate A&D transactions in which there are any required transfers of regulatory licences.

In the absence of any change to the AER's process, cautious parties will often choose to close in escrow because the Vendor and Purchaser will not have sufficient certainty to know if the transfers of regulatory transfers associated with their transaction will be approved. Including a customized closing in escrow step would see the parties structuring their transactions so that some or all of the transaction would be undone if the required AER approvals are not obtained, with any associated return of funds.

**So, How Has AER Bulletin 2017-13 Impacted The PTP?**

While the implementation of the revised process outlined in the Bulletin will have a significant impact on the manner in which transactions are effected, we have chosen not to modify the provisions of the PTP to address the Bulletin.

The definition of Licencee Rating, the Vendor's representation about its ability to transfer regulatory licences (Paragraph 6.02(q)), the corresponding Purchaser representation in Paragraph 6.04(d) and the mutual condition about regulatory transfers in Paragraph 10.01(e) are structured so that they can apply across multiple jurisdictions.

If the ability to effect a transfer of any licence for any of the Assets is in question (as under Bulletin 2017-13), the onus is on the parties to add custom content in their Head Agreement to address their particular needs. As noted several times in the annotations, this might be done, for example, by including additional definitions, a Clause that relates to the specific handling required for their circumstances, the possible inclusion of a Closing in escrow mechanism and the inclusion of additional conditions to Closing.

There were two reasons for this approach. The first was the belief that the PTP should not attempt to predict or prescribe the handling of an important emerging issue that should be assessed and handled by the parties and their applicable business and legal advisors on a case by case basis. The second was that the fluidity of the Regulations on this area over time and across jurisdictions was such that any more specific handling of the issue in the PTP based on a snapshot in time would potentially create unintended consequences for the parties over time.

Simplifying the review of the other procedural aspects of the overall Transaction through use of the PTP facilitates a more focused examination of this important issue by the parties' representatives relative to what would be the case without the PTP.

**Pipeline Records**

The PTP also includes a generic definition of Pipeline Records and other provisions in response to AER Bulletin 2015-34. That Bulletin contemplates that the AER could conduct compliance monitoring (for existence and transfer of required records) on a random basis or during routine field inspections, typically after the transfers have been processed.

The new licencee (transferee) is responsible for producing the applicable records on request of the AER, which places an onus on the Purchaser to protect itself through its due diligence process. A licencee that fails to do so will be in a non-compliance position. Non-compliance could, among other things, force it to conduct an engineering assessment to demonstrate that the applicable pipeline is fit for its intended use. Pending such an assessment, the AER could order the pipeline out of service, which may require wells to be shut-in. Compounding the challenge of compliance is that the parties might not agree about whether the Pipeline Records are complete for the purposes of the review by the regulatory authority and that the regulatory authority's expectation for completeness might not be known until any site inspection.

The references to Pipeline Records in Clause 3.07 require the selected party (Vendor or Purchaser) to bear accountability to address any deficiencies associated with Pipeline Records. The optional representation included in Paragraph 6.02(r) is fairly onerous, and Vendors will typically be extremely reluctant to assume a trailing liability. One would typically expect Vendors would have a strong preference not to accept that representation and to select Alternate 1 of Clause 3.07 as a consequence. Conversely, one would expect that Alternate 2 would be selected only (but not necessarily) if a Vendor has agreed to provide that representation.

Alternate 3 of Clause 3.07 has been included to add flexibility. It allows the parties to choose to share financial responsibility for any engineering assessments required to rectify identified deficiencies on a different negotiated basis under the Head Agreement. A negotiated cost sharing creates reinforcement for each party to address any deficiencies in a timely and cost effective manner.

**Check Out The Case Studies**

As noted in my earlier November, 2016 article in The Negotiator, the Addendum to the draft includes five case studies that were prepared to provide a compelling case for use of the 2017 PTP for the low to modest value transactions for which it has been designed. To a large degree, those case studies will determine the pace at which the PTP will ultimately be accepted by industry. They show the potential use of the PTP for: (i) a simple sale of a producing property; (ii) a simple swap involving producing properties; (iii) a simple sale of an undeveloped property; (iv) a more complex sale of an undeveloped property involving reserved rights and the reservation of an ORR; and (v) a simple swap of undeveloped properties. The common theme is that use of the schedule of elections from the PTP allows the head agreement for each of those case studies to be not greater than two pages, as shown for item (iii) in that article.

To facilitate a transition to use, the CAPL website includes Word versions of the annotated and unannotated election sheets to the PTP and those case studies.

As noted in the October, 2017 article in The Negotiator, consider using the case studies to take the "2017 PTP Challenge". Take a "road test" of the PTP and see how you would have managed one or two of your recent low to modest value, straightforward transactions using the PTP and compare the outcomes to the agreement you used for your transaction.

**"Making Simple Transactions Simple Again"**

Our committee is a diverse one, with representation from smaller companies, intermediate sized companies and larger companies. Our members represent not only CAPL, but also our partners in CAPLA, EPAC, PADA, PASC and the Legal Community. Despite our differences in background and functional expertise, we were united by a common belief-that our industry does not efficiently process our low to modest value, straightforward A&D transactions.

One of the major contributing factors to this is the lack of standardization in our agreements. We currently have hundreds of different companies saying basically the same thing in many different ways. This lack of consistency is apparent when we see the deficiencies in agreements presented to us and when we recall the bias in the documents we often see proposed. It is most apparent, though, when we consider the additional effort and associated delays respecting many of our low to modest value, straightforward transactions because of labour intensive reviews of different presentations of similar concepts and a tendency to debate how best to say basically the same thing as what had been originally proposed.

Put simply, our industry has done a remarkable job of making simple transactions much more complex than they should be, than they must be in a business environment that requires us to do more with even less.

We believe that our work demonstrates that there is, in fact, a better path available to us for low to modest value, straightforward transactions. We believe that current industry conditions create an appetite for efficiency, effectiveness and change. Most importantly, however, we believe that a critical mass of the smaller and intermediate sized companies will quickly embrace the 2017 CAPL Property Transfer Procedure as "first followers" for the transactions for which it is designed.

This strong existing undercurrent of support for "making simple transactions simple again" is why we have dedicated so much of our effort on this project to target the smaller and intermediate sized companies and why we believe that use of the 2017 PTP will cascade quickly within at least that segment of potential users.

We look forward to hearing about your experiences as you begin to work with the 2017 PTP!