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.

Definition of Wells: 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).

Base Purchase Price and Tax Allocations (Clause 2.02): 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.

Production Handling Agreements (6.02(j)): 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.

Various Operational Matters (6.02(k)-(o)): 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.

Records Relating to Operated Tangibles (6.02(r): 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.

Regulatory Production Penalties and Regulatory Production Allowable (6.02(s)&(t): 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

Area of Mutual Interest or Area of Exclusion (Paragraph 6.02(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.

No Notice of Offset Obligations (Paragraph 6.02(v)): 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)

Subclause 6.03A: 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.

Subclauses 6.03B and C: 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.

Subclause 6.03D: 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

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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.

Subclause 8.02A: 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!

2017 CAPL Property Transfer Procedure: Transition To Use
CAPL Negotiator, February, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

The January article was about the process of transferring well and tangibles licences under the Regulations and the endorsement of the PTP. This month's article is about the transition to use.

Lessons Learned From The 2000 PTP

I believed for many years that the 2000 PTP was infrequently used by industry based on a combination of my larger company experiences and the small number of calls I had ever received about it. I discovered in a discussion with representatives of the EPAC Land Committee on another topic in the fall of 2015, though, that my assumption was wrong. Not only was it used regularly by many small companies for their low to modest value transactions without major problems, but the personal experiences of the EPAC representatives were very positive. They also thought that the time was ideal for an update and that there would be a greater receptiveness to an updated PTP.

In considering how best to approach the 2017 update, we needed to understand why the 2000 PTP did not receive the level of acceptance that had been anticipated when the 2000 PTP was completed and to apply those learnings to the new project.

We determined that one of the major reasons for the narrower than expected usage was that the original vision for the 2000 PTP was overly ambitious. We believed in 2000 that it would become widely used for a broad spectrum of transactions by a diverse range of users. The reality proved to be quite different, however. The 2000 PTP was far from being a one size fits all model, and did not suitably address user needs or expectations for large or otherwise complex transactions, such as those with Investment Canada, Competition Act or employee issues. We had also assumed from the participation of larger companies in the commenting phase on the 2000 PTP that they would be much more willing to consider using the 2000 PTP than ultimately proved to be the case.

Based on that assessment, we made two strategic decisions for the 2017 PTP update project.

The first was to be much less ambitious in our objective. We designed the 2017 PTP for undeveloped lands transactions and other relatively straightforward transactions on the low to modest end of the value spectrum. Our belief was that we could have the greatest efficiency impact on industry by focusing on the 75%+ of deals at this end of the range, while being clear that we were not making any attempt to disrupt the more traditional approach to complex or higher value transactions. This decision had a significant impact on both the way that we communicated the case for change and the content we chose

not to include in the PTP, such as seismic, employees and Investment Canada and Competition Act approvals.

The second was to recognize that larger companies were likely to be sufficiently comfortable with the status quo that they would be unlikely ever to regard the PTP as their “document of choice”. The consequence of this was the more extensive and visible participation of EPAC representatives on the Committee and the associated emphasis over the course of the project on trying to engage the smaller and intermediate companies.

How Is The 2017 PTP Likely To Be Used?

We anticipate that the document will most likely be used for two types of transactions.

The first is for relatively straightforward producing property sales and swaps on the low to modest value end of the deal spectrum (i.e., the under $20-25MM range). That being said, we also expect that some users who are not already familiar with the 2000 PTP will proceed more cautiously by initially using a materially lower internal threshold, such as $5MM, with a vision of increasing their threshold as comfort, confidence and industry acceptability increase.

The application of a threshold test by users does not reflect a structural design that limits use of the PTP for relatively straightforward transactions with a greater value. Similarly, it does not reflect any belief on our part that we took shortcuts on the quality of coverage included in the document for the less complex transactions for which it was designed. Instead, it reflects the practical realization that management and legal advisors would typically be much less comfortable in using a CAPL form for transactions with a value at the higher end of the deal spectrum.

The second major contemplated transactional use of the 2017 PTP is to bring much greater efficiency to the increasing number of undeveloped land transactions, as addressed in greater detail in the November, 2016 article in The Negotiator and throughout the annotations.

Most companies have a short form conveyance agreement of 5-15 pages they use for these transactions, with certain associated tradeoffs in breadth and depth of coverage in favour of brevity. These forms are all different in coverage, balance and overall quality, such that there are likely to be several drafts of the agreement and delays while the drafts are reviewed and discussed.

As shown in Addendums V-VII of the 2017 PTP, parties using the PTP, on the other hand, can complete these types of transactions in one or two pages by using the PTP as the foundation for their transaction, while obtaining greater breadth and depth of coverage.

The use of the 2017 PTP for undeveloped land transactions has the added benefit of providing potential users with a low risk way to become familiar with the document and to assess its suitability for future use, an avenue that we did not explore sufficiently with the 2000 PTP.

To facilitate use of the 2017 document, we have made annotated and unannotated versions of the PTP election sheet and examples of producing property and undeveloped lands transactions available in a downloadable format from the CAPL and CAPLA websites.

There is one other impactful use. We anticipate that users of all experience levels in companies of all sizes will also soon begin to use the 2017 PTP as a reference document when reviewing the draft agreement of another party and when considering a potential issue under an existing agreement.

Turning The Document Standardization Engagement Process Upside Down

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 use the document and the associated annotations and case studies to enable users of all experience levels to enhance their expertise. And, last, but certainly not least, the fourth is to create a document that will be widely used in due course by creating a clear case for change and by ensuring that the document is balanced and of high quality.

My approach in other agreement standardization projects in which I have been involved has been to try to build momentum to use initially with the larger companies, so that they would cascade use of the document outward to the remainder of industry.

Having recognized that the updated PTP is unlikely ever to be the "document of choice" for larger companies, we chose to turn the traditional approach upside down for this project. We decided to try to build momentum to use initially with the smaller and intermediate companies, so that they would cascade use of the 2017 PTP outward to their peers and the larger companies.

Although the larger companies are unlikely to be early embracers of the 2017 PTP, there are five reasons for them to become familiar with the document in the near-term. The first is that the review will probably identify improvement opportunities to their existing precedent agreement forms. The second is that the PTP is likely to be used by commenting parties on an increasing basis to assess the reasonability of draft agreements presented to them for review, such that existing precedents will come under increasing scrutiny by the other party. The third is that users of the PTP will probably request its use for transactions at the lower end of the value spectrum, particularly if they are the vendor. Although larger companies are unlikely to agree today, the fourth is that larger companies are likely to experiment with the PTP in due course for lower value transactions when they have competing internal demands, particularly for transactions involving undeveloped lands. The fifth is that the annotations are an excellent reference and teaching tool that can be helpful in examining issues in new and older agreements, even if the PTP is not then being used by the applicable company.

Déjà Vu And The 1997 CAPL Farmout & Royalty Procedure

The transition to use following completion of a document standardization project can be extremely slow, as was the case for the 2007 CAPL Operating Procedure. It can also be surprisingly fast, as was the case for the 1997 CAPL Farmout & Royalty Procedure.

Between the two, the 2017 PTP feels much more like the 1997 CAPL Farmout & Royalty Procedure.

Current industry conditions create an appetite for efficiency, effectiveness and change, particularly for the smaller to intermediate companies that we believe are the likely early users of the document. Based on informal feedback we have been receiving, we believe that the combination of the compelling business case for a step change in approach and the quality of the document will see significant early stage interest by at least that subset of users.

As was the case with the 1997 CAPL Farmout & Royalty Procedure, we also believe that companies that use the document in one or two transactions will want to use it routinely for the transactions for which it was designed once they experience for themselves the quality of the document, how intuitive it is to users and the resultant uplift in efficiency when each of us is being challenged on a daily basis to do more with even less.

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

The Property Transfer Procedure: An Idea Whose Time Has Come
CAPL Negotiator, February, 2018
George V. Lepine and William M. Laurin, EnerNext

A famous quote by the French poet and novelist Victor Hugo, author of both *Les Misérables* and *The Hunchback of Notre-Dame*, is often translated as "Nothing is as powerful as an idea whose time has come." That sentiment is entirely appropriate for the arrival of the 2017 CAPL Property Transfer Procedure (PTP); its completion is a monumental achievement and the CAPL PTP Committee is to be applauded. This updated version of the PTP is extremely well suited for its intended purpose; namely small and medium sized asset transactions under $20 million (Targeted Transactions), and in our view, is destined to be quickly and widely adopted by industry.

Considering the longstanding and universal adoption by negotiators of the CAPL Operating Procedures, the CAPL Farmout & Royalty Procedures and of the PJVA's Construction, Ownership and Operating Model Form Agreements (Co-Ownership Agreements), it has always been troubling as to why purchase and sale agreement (Sale Agreements) did not follow a similar arc when the original version of the PTP was introduced in 2000. The most straightforward explanation for the difference in adoption rates and extents, is that the relationship among co-owners is much more "symmetrical" under Co-Ownership Agreements, than the relationship between the vendor and the purchaser under a Sale Agreement. It made sense for industry to standardize Co-Ownership Agreements because each co-owner retained a broad set of independent development rights, and most companies were both operators and non-operators, making it easier to reach a common understanding of what was "market" in terms of language, leaving an appropriate suite of elections to reflect commercial terms. On the other hand, during the late 1980s and the 1990s throughout Western Canada larger, established legacy companies such as Imperial, Shell, Chevron and Amoco were "net sellers" which preferred using existing precedent agreements, while the junior and immediate market such as Renaissance, CNRL and Penn West were "net acquirers". In 2000 there was not sufficient homogeneity among Sale Agreements in common use, nor was there the commonality of interest that evolves with regularly being both a vendor and a purchaser; the 2000 PTP was simply ahead of its time. An easy parallel is the residential housing market, where a standardized real estate purchase contract was broadly adopted as in general most participants in the market are concurrently a buyer and a seller.

Virtually all Sale Agreement forms currently in use for Targeted Transactions follow the same basic agreement structure and contain largely identical commercial terms, representations, indemnities and conditions; albeit worded in slightly different ways. By distilling the various parallel Sale Agreement forms into a single commonly accepted agreement form, the PTP will eliminate much of the time and effort that goes into negotiating specific wording. At the same time, by providing alternative elections for many key substantive issues, the PTP will allow buyers and sellers to quickly focus on negotiating those key issues without engaging in seemingly trivial semantic debates regarding definitions and largely standardized clauses. The PTP strikes a thoughtful and extremely well-reasoned balance between consistency of language and flexibility over key terms. Given the need for cost competitiveness facing the Western Canadian Sedimentary Basin from onshore U.S. oil production, the efficiencies and savings to be realized by industry through a swift and broad adoption of the updated PTP will be recognized by industry from the outset. Adoption of the PTP will also greatly enhance the predictability, consistency and stability of the deal making process. By focusing attention on key substantive issues, the PTP will generally foster a much more meaningful discourse in industry about those substantive issues. Imagine where we would be if, like in the 1960s, we still drafted and negotiated operating procedures; by standardizing Sale Agreements negotiators and administrators will have more time and energy to focus on functions that meaningfully add value.

Without ever being acknowledged as such, CAPL was an early entry in the disruptive trend of the "commoditization of legal services". In a global context many industries are, with the benefit of advances in technology, undertaking the adoption of standardized agreements, processes and procedures in a concerted effort to reduce legal costs, standardize terms and ease agreement administration. The Co-

Ownership Agreements that CAPL has been providing to industry for 45 years, are examples of transforming what used to be “bespoke legal services” (i.e. the drafting of complex joint ventures in a highly regulated industry), into essentially a “legal commodity” (i.e. a standardized, widely accepted, non-negotiated arrangement available for a low, fixed cost without any appreciable degradation in quality). Interestingly, the structure and form of the Co-Ownership Agreements and the PTP are also ideally suited for the next “big thing” in technology; namely the introduction of blockchain technology to the energy industry. Harvard Business Review defines blockchain as "an open, distributed ledger that can record transactions between two parties efficiently and in a verifiable and permanent way", and in Calgary on November 30, 2017 IBM hosted a “Blockchain for Energy Roundtable” which provided a window on its potential application to the management and administration of oil and gas assets. The most interesting aspect for negotiators and asset administrators will be introduction of so-called “smart contracts”, which are computer protocols intended to facilitate, verify, or enforce the negotiation or performance of a contract. Contractual clauses may be made partially or fully self-executing, self-enforcing, or both with a view to reducing the transaction and compliance costs associated agreement administration. Imagine, if you will, a version of the industry where all lands, leases and assets are recorded on a single, common, cloud-based “ledger” where ownership interests are permanently recorded and verified, where the terms governing co-ownership (i.e. Co-Ownership Agreements) are hard-wired into that ledger, and those ownership interests are readily traded with the push of a button on the basis of standardized terms agreed to in a front-end user agreement (i.e. the PTP).

But let’s not get ahead of ourselves - there is one thing the PTP does not do yet, it does not think for you. Asset deals, by their nature, have varying degrees of complexity. While a small purchase and sale of undeveloped Crown land is generally quite straight forward; other deals, even if their value is small, may be quite complex. Furthermore, the world is always changing. The ever-shifting landscape of AER license transfers is a good example of this change. The PTP Committee made a conscious decision to avoid addressing transitory current events and included in the PTP only standard and stable terms and conditions that will stand the test of time. This means that transitory issues will need to be addressed in the head agreement. Finally, in certain instances, the PTP Committee had to make judgement calls as to what would be in or out of the PTP. For example, the PTP is generally structured to exclude most seismic data from the definition of "Assets". For all of these reasons it is critical that anyone who uses the PTP do the following: (i) actually read, understand and become familiar with the PTP; and (ii) think critically about the interplay between the PTP and the specific assets that are the subject of the transaction. In sum, the PTP is a very robust document and well suited for its intended use but it doesn't do your thinking for you … at least not yet.

While several pages could be filled with commentary about the opportunities and possibilities afforded by our technological revolution, we have more pressing matters to attend to. We have recently connected our door locks to the black box with the blinking red light that sits in the corner of our office kitchen (which we named "HAL" - that may have been a mistake). We are presently locked inside the office and when we asked HAL to open the door he said: "I'm afraid I can't do that George". If you are not too busy when you read this article we would appreciate if you come over to Suite 760 in Calgary Place 1; and please bring a crowbar with you if it is not too much trouble.

2017 CAPL Property Transfer Procedure: Clauses 2.01-2.03
CAPL Negotiator, March, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

The February article was about the transition to use. This month's article is about Clauses 2.01-2.03.

Clauses 2.01 And 2.02: A Shift Of Content To The Property Transfer Procedure

The 2000 PTP had been structured so that the content in Clauses 2.01 and 2.02 would be included by the Parties in their Head Agreement and customized to their particular transaction. This was modified as of the 2017 PTP by including these Clauses in the PTP. This reflects the intention to increase consistency and the belief that these Clauses would be suitable for the majority of transactions. Shifting these Clauses into the PTP simplifies the creation of the typical Head Agreement, notwithstanding that adjustments would be required for an Asset Exchange or a transaction with different Asset types (e.g., the exclusion of Tangibles or the addition of seismic).

Clause 2.01 is a generic reference to the acquisition and disposition of the Assets.

Clause 2.02 identifies the Base Purchase Price and the associated tax allocation.

The definition of Base Purchase Price was introduced in the 2017 PTP to differentiate between the original negotiated price and the adjusted Purchase Price that reflects adjustments, any other modifications and the handling of any Interest Amount that accrues during the Interim Period.

Tax Allocations: The Parties must allocate the consideration for tax purposes among the Petroleum and Natural Gas Rights, the Tangibles and the Miscellaneous Interests, with an additional allocation to product inventory if Paragraph 4.01(g) applies to sulphur and any required allocation to seismic. This allocation is required because of the difference in tax treatment between land acquisition costs (basically a 10% declining balance writeoff) and Tangibles (generally a 25% declining balance writeoff for "Class 41" assets, with some different rates for certain special classes of assets).

A Vendor would prefer to maximize the allocation to Petroleum and Natural Gas Rights and to minimize the allocation to the Tangibles to maintain the maximum benefit associated with its tax pools. A Purchaser would generally wish to maximize the allocation to Tangibles.

Occasionally, a Purchaser will be a non-taxable or tax deferred entity that is not anticipated to be taxable in the foreseeable future. In such cases, there may be an initial temptation to structure the allocation to maximize the benefits to the Parties. This could involve a minimal allocation to the Tangibles for the benefit of the Vendor and a reduction of the Base Purchase Price for the benefit of the Purchaser.

However, the allocation must always be reasonable. An artificial allocation would be reviewable under the anti-avoidance provisions of the *Income Tax Act* (Canada).

Notwithstanding the requirement that the allocation be reasonable, industry experience has generally indicated that a reasonable allocation for a typical producing property is 80% to Petroleum and Natural Gas Rights and 20% to Tangibles, and the Clause reflects that handling.

The onus is on the Parties to assess the suitability of that outcome in their Agreement. The Parties can easily modify those allocations for any particular transaction, however, and the bolded Paragraph in the sample annotated Schedule of Elections and Modifications included as Addendum I reminds users of this. It would not be appropriate to use those allocations, for example, if the property comprised primarily capped wells with minimal associated Tangibles, passive interests (ORRs and NPIs) or primarily Tangibles, such as a major gas plant.

<u>Asset Exchange</u>: Significant modifications to Clause 2.02 would be required if the transaction were an Asset Exchange. Addendum IV at the end of the PTP provides a sample provision that might be considered for an Asset Exchange.

<u>Seismic Data</u>: The issues with geophysical data (e.g., data owned with third parties, the handling of derivative products, change in control) are complex. They would have required the inclusion of layers of content that would often have no application to the typical modest to low value transaction for which the PTP has been designed. As a consequence, we chose not to include that content, such that Parties that required that content would need to negotiate provisions applicable to their situation (e.g., a definition of “Seismic Data”, a modified definition of Assets, a Schedule outlining the location of the applicable program areas and probably the form of a licencing agreement).

A licenced copy of proprietary seismic data could be included in the transaction for nominal consideration or as a value item. If the latter, a separate allocation to seismic would be required, with a consequential modification to the reference to the allocation to Miscellaneous Interests, such as “Miscellaneous Interests Other Than Seismic”.

Clause 2.03 - Receipt And Handling Of Deposit

The 2000 PTP was structured so that any Deposit was created in the Head Agreement. This was modified as of the 2017 PTP by including an optional Deposit Clause. In practice, a Deposit will often not be required in minor value transactions, such that this optional Clause would not be selected to apply. This is particularly the case if the Vendor determines that the ongoing business relationship between the Parties is such that a Deposit is not required to secure performance.

The Deposit in this Clause is structured as 10% of the Base Purchase Price, to reflect the most typical Deposit threshold. The Parties can easily modify this threshold for any particular transaction, and the bolded Paragraph in the sample Schedule of Elections and Modifications included as Addendum I reminds users of this.

The Clause is consistent with the provision typically used in industry’s Purchase & Sale Agreements, in that it acknowledges receipt of any required Deposit. The Parties will need to determine the logistics for delivery of the Deposit under their particular Agreement. For the typical transaction for which the PTP is being used, the Vendor might often choose to have its representative exchange a copy of its execution page of the Agreement for the Deposit. A more elaborate process might be used if the Deposit is being made through a wire transfer.

The Clause also addresses some of the procedural obligations if there is a Deposit. The Vendor will hold it in trust on behalf of the Purchaser, to be applied against the Purchase Price if Closing occurs. A

Purchaser might require a modification so that a Deposit would be held in a special trust account if the Deposit were very large or there were material concern about a Vendor's financial situation.

If Closing does not occur, the handling of the Deposit is addressed by this Clause and the default provisions of Article 12.00 (i.e., the Deposit would be defaulted to the Vendor if Closing did not occur because of a default of the Purchaser). If the Deposit is to be returned to the Purchaser, interest accrues on the Deposit at the Prime Rate, plus one percent, even if the Vendor does not deposit the funds with a financial institution. Prime Rate, plus one percent, was chosen for consistency with the treatment in the definition of Interest Amount and under Clause 2.06, to recognize that the Deposit would only be returned if the Purchaser was not at fault. As the interest rate payable on short term deposits will typically be approximately 2% below the Prime Rate, Parties might sometimes prefer to modify the PTP to use revised rates.

Become Familiar With What Is An Election And What Isn't

One of our objectives when preparing the 2017 PTP was to minimize the number of elections and optional elements to make it more user friendly than the 2000 PTP. One of the things we did in this regard was to pick 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 it would not be uncommon for the Parties to choose a different value in any particular transaction (e.g., the 80-20 tax allocation in Clause 2.02 and the optional 10% Deposit in Clause 2.03).

It is very important for users to understand this approach as they begin to work with the document. To assist users with their transition to the 2017 PTP, an overarching annotation about this approach that identified the more typical provisions of this type that should be considered for each transaction was included at the beginning of the annotations. These items are also identified in the applicable text and in the bolded reference in the Schedules of Elections and Modifications included in the various Addendums at the end of the document.

One of the first things someone considering using the 2017 PTP should do, therefore, is to review the Schedule of Elections and Modifications in Addendum I to become familiar with what is and is not an election in the PTP.

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

2017 CAPL Property Transfer Procedure: Clauses 2.04-2.06
CAPL Negotiator, April, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

The March article was about Clauses 2.01-2.03. This month's article is about Clauses 2.04-2.06.

Clauses 2.04: Determination OF Purchase Price And Form Of Payment

The amount specified as the Base Purchase Price in Clause 2.02 is before any adjustments under Article 4.00 and any other modifications due to the exclusion of Assets as contemplated in Clause 1.05 (e.g., exercised ROFRs, Assets excluded due to Title Defects) or otherwise as agreed by the Parties (e.g., a negotiated reduction in price to accept certain discovered Title Defects or unexpected Environmental Liabilities).

Any Interest Amount that accrues is an increase to the Purchase Price. In a transaction with Petroleum and Natural Gas Rights, Clause 2.06 reflects the typical industry practice by allocating the Interest Amount to them, rather than to the Tangibles. This reflects the view that the foundation of the accrual of the Interest Amount is because of the benefit to the Purchaser of receiving net production income that accrues from the Effective Date.

Subclause 2.04B reflects the overall handling of Environmental Liabilities under Clause 13.04. This Subclause recognizes that each Party would have taken into account the contemplated Environmental Liabilities associated with the Assets when determining the Purchase Price, and reinforces the Purchaser's responsibility for those obligations. This is not intended to affect the environmental due diligence process or the rights of the Purchaser thereunder.

Subclause 2.04C provides that payment might be made by certified cheque, bank draft or wire transfer. However, a wire transfer to the Vendor's designated bank account will sometimes be required because of a $25MM cap on the use of cheques, bank drafts and other paper based payment items going through Canada's financial clearing system. This limitation is a requirement of the Canadian payments system to enhance the stability of that system.

This Subclause is structured to recognize the possibility that a wire transfer could potentially be required for a Deposit or payment of any other amount required to be paid by a Party at a time other than the Closing Time. That being said, it is unlikely that a wire transfer would be required under financial clearing procedures for the amount of a Deposit or adjustment associated with the typical low to modest value transaction for which the PTP would most likely be used.

Some Parties will also probably modify this Subclause so that all payments being made will be through a wire transfer.

Clause 2.05: GST/HST And Other Sales Taxes

The starting point when considering this Clause and Clause 4.03 respecting the handling of Interim Period income for tax purposes is that the Clauses in the 2000 PTP and the 2017 PTP were drafted in consultation with the Canada Revenue Agency.

Clause 2.05 requires the Parties to disclose their GST/HST Registration Numbers. The Purchaser's Registration Number is particularly relevant if, for example, real property is being conveyed (as the reverse collection mechanism likely will apply) or the Alternate 2.05A(2) section 167 election is made.

Subclause 2.05A includes two Alternates, with Alternate 1 being selected most frequently.

Under the general rules, the Vendor will be required to collect and remit GST/HST on the conveyance of all personal property (including what is generally described as Tangibles, Miscellaneous Interests, and, if applicable, seismic). As the Purchaser generally will be able to claim the GST/HST paid by it as an input tax credit, there will be no cost to the Purchaser, except for the cost associated with the time value of money incurred during the recovery period. The allocation of value among the relevant classes of property must also be reasonable for GST/HST purposes.

The annotations address some of the intricacies of GST/HST and provincial taxes in more detail than is appropriate for this article.

Clause 2.06: Interest Accrual

This Clause is premised on the Agreement not being executed prior to the Effective Date. If it is executed prior to the Effective Date, there may be circumstances in which the Parties will modify the interest and Clause 2.03 Deposit mechanisms.

Most Vendors believe that they should have been entitled to funds at the Effective Date. As the Vendor has arguably "loaned" the funds to the Purchaser for the Interim Period, it is a well-accepted practice that "interest" will accrue at a *per annum* rate between prime and prime plus 2%, so Alternate 1 has been included using the Prime Rate, plus 1% *per annum*. The justification for the interest charge on the adjusted Purchase Price is generally regarded as the accrual, to the Purchaser, of the incremental revenue applicable to the Interim Period.

Despite the broad use of this practice, there are others who object to the mechanism if Closing follows the Effective Date by 4 - 6 weeks and the Parties have been proceeding diligently since they "struck a deal." In essence, they believe that no interest should accrue during the period that the Parties are diligently preparing for Closing, since the Parties are working within logistical limitations that preclude them from Closing immediately. They note that the Purchaser is receiving no benefit during the Interim Period for non-productive Assets, arguably including the production that will be obtained following Closing (i.e., the $Y in value that does not include the cash flow for the Interim Period), while the Vendor has the benefit of limiting its potential exposure to future expenditures and legal liabilities from an Effective Date prior to Closing. They also note that the Purchaser will have paid for the incremental revenue for the Interim Period in its Purchase Price and that the incremental revenue would not actually be received until late in the month following the production month anyway.

This view is at the foundation of Alternate 2.06(2). The premise behind Alternate 2 is that Closing should occur shortly following the time reasonably allocated for the completion of the Purchaser's due diligence work and the Vendor's pre-Closing work to prepare documents, address partner consent/ROFR issues and respond to Title Defects. Closing could often occur between 3 and 6 weeks after the agreement on

price in a transaction using the PTP, assuming the prompt finalization of the Agreement and land interests of moderate complexity.

Alternate 2 is designed to compensate the Vendor with interest if Closing is delayed beyond the time reasonably anticipated for completion of the pre-Closing work because of such factors as the Purchaser's delay in providing ROFR values or in commencing and completing its title review. The interest rate was adjusted to Prime Rate plus 1% *per annum* in the 2017 PTP to be consistent with the other interest calculations in Article 2.00.

A problem relating to the interest mechanism in both Alternates 1 and 2 is the assumption that the Vendor has done nothing to delay Closing. Closing is often delayed by the Vendor's less than diligent efforts in processing the transaction, the Purchaser's difficulties in completing its due diligence review if the Vendor's files have not been well maintained or the Vendor's delay in addressing Title Defects. As it is not appropriate to have interest accrue in those cases, the Vendor is required to assume responsibility for delays that are solely attributable to it under both Alternates, including any such delay that results in a second Closing for Assets for which Title Defects were remedied by the Vendor after Closing (Subclause 8.02F). Similarly, interest does not accrue insofar as Closing is delayed because the Parties are involved in an arbitration under Article 9.00.

The Clause includes a third option - not to accrue any interest on the Purchase Price, by selecting that neither Alternate 1 nor 2 will apply. In practice, this option will often be selected in the PTP for Asset Exchanges, minor value transactions and transactions with a short anticipated Interim Period.

If the Parties select to apply Alternate 1 or 2, interest is calculated on the Purchase Price net of the Deposit and any adjustments made at Closing under Paragraph 4.02A(a). Those adjustments include any modifications resulting from the exclusion of certain Assets under Clause 1.02 and any net adjustments under Article 4.00.

To illustrate, assume that a transaction with a $10MM Base Purchase Price sees a reduction of $2MM because of ROFR exercises and an Article 4.00 adjustment of $500K in favour of the Purchaser in circumstances in which there is no Deposit. The interest would be based on the adjusted $7.5MM amount. This approach is administratively simpler than calculating interest separately on the Purchase Price from the Effective Date and on production proceeds from the time of receipt.

"Show Me The Money"

Article 2.00 of the 2017 addresses the specifics of the consideration for the transaction, and includes key content that would have been included in the head agreement for an Agreement that used the 2000 PTP. Including that content in the 2017 PTP reflects our objective of making it easier to use the 2017 PTP for the typical low to modest value transactions for which it was designed.

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

2017 CAPL Property Transfer Procedure: Article 3.00
CAPL Negotiator, May, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

The April article was about Clauses 2.04-2.06. This month's article is about Article 3.00 (Closing).

General Qualification Re Required Regulatory Approvals

The PTP does not address the situation in which the Licencee Rating for either Party is such that special provisions are required to transfer the licences for Wells or Tangibles. As noted in the general annotation at the beginning of the PTP and the annotations on Licencee Rating, Paragraphs 6.02(q), 6.04(d) and 10.01(e), the onus is on the Parties to add custom content in their Agreement to address their particular needs. Reviewing the Regulations for each 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 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 the PTP was not structured to include any specific provision to address an issue that is a moving target. The alternative of including a "one size fits all" solution for relevant jurisdictions based on a snapshot in time assessment of the Regulations would ultimately create risk for users because of potential reliance on a provision that might not suitably address the issue for their transaction.

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.

A customized response to a required review of a proposed transfer by regulatory authorities could see Parties choosing to create a Closing in escrow process, particularly if the approval of regulatory authorities might not be granted. 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.

This critical message is reinforced in the annotations throughout the PTP and in the Addendums.

Clause 3.01: Closing

The price/value and other material terms were agreed upon at the time of execution of the Agreement. However, under a Purchase and Sale or Asset Exchange structure, the transaction will not be complete (and possession will not pass) until completion of the Purchaser's "due diligence" review of the Assets, the payment of the Purchase Price, the satisfaction of the conditions in Article 10.00 and the execution of the General Conveyance. The completion of the transaction is referred to as Closing, and is further described in Article 3.00. As noted in Clause 3.01, Closing is premised on the conditions in Article 10.00 having been satisfied.

Clause 3.02: Effective Date Of Transfer

Although the Purchaser generally will acquire the benefits and obligations respecting the Assets retrospectively to an earlier Effective Date, it will not take possession of them until the Closing Time.

This Clause was structured to link obligations (e.g., financial and liability and indemnification) to the Effective Date because: (a) this matched the net production income or loss being adjusted under Article 4.00 with the associated obligations (e.g., potential accrued liabilities) in accordance with the "matching principle" at the foundation of the accrual system of accounting; (b) the Purchaser has a high degree of influence on operational decisions made during the interim period under Article 5.00; (c) the Purchaser is protected by the "No Substantial Damage" condition in Clause 10.02 for any significant damage to the Tangibles; (d) of the typical use of the Effective Date as the "transfer date" under any notice of assignment relating to a land agreement; (e) it encourages Parties to select the Effective Date on a current basis; and (f) as long as the net production income or loss during the Interim Period is handled in compliance with the requirements of the Canada Revenue Agency prescribed by Clause 4.03, it is unlikely that the CRA would otherwise concern itself with the terms negotiated by the Parties.

That being said, some companies prefer to follow the CRA's general historic practice of passing obligations at the Closing Time and regarding the Effective Date as simply an accounting reference date, particularly if the interim period between the Effective Date and the Closing Date is long. Those companies can address their concerns relatively easily by changing the Effective Date references in this Clause, Article 13.00 and the General Conveyance, and by choosing a corresponding "transfer date" in the NOAs.

Notwithstanding the construction of Clause 3.02, the Purchaser would not have an insurable interest until Closing, though, such that a Purchaser would want to understand the policies of insurance held by the Vendor under Clause 5.02.

The Effective Date and the Closing Time will seldom coincide. Article 5.00 addresses the Vendor's obligations to the Purchaser for the maintenance of the Assets until the date possession is transferred, and will be the subject of a separate article in due course. This is an area that the Parties should review carefully in the context of any particular transaction to ensure that there is a suitable breadth and depth of coverage, particularly if using a different document format than the PTP.

It is the better practice for the Vendor's field personnel to spend time with the Purchaser's personnel prior to Closing to familiarize them with any Assets that they will be operating. In some circumstances, it will not be feasible for the Purchaser to take over the operated Assets at Closing, so it may be necessary for the Vendor to continue to operate the Assets for a short time as a contract operator under a side agreement. It is in the mutual interest of the Parties to have an agreement outlining any such transitional services arrangement, including any applicable fees.

Clause 3.03: Deliveries At Closing

Preparation of Specific Conveyances: The Vendor is responsible for the preparation of documents respecting the conveyance of the Assets. There may be instances in which the Purchaser prefers to prepare those documents, though (i.e., a Vendor without significant A&D expertise disposing to a Purchaser with the expertise and the resources to prepare the documents), and that change could easily be made.

Subclauses 3.03A and B are structured so that the applicable Specific Conveyances are fully executed for Closing. Industry experience has been that those documents are often not prepared diligently by Vendors if the Specific Conveyances are not delivered until after Closing. Similarly, the historic industry experience has been that documents were not executed by the Purchaser and distributed to third parties promptly by it if documents executed only by the Vendor were delivered at Closing. The distribution of the Specific Conveyances after Closing is addressed in Clause 3.05.

The PTP does not prescribe a process in which drafts of the Specific Conveyances are provided to the Purchaser for review several days before Closing. That being said, it is the better practice for drafts of those documents to be provided to the Purchaser a reasonable period prior to Closing, so that any required corrections can be made to the documents being executed at Closing. Addressing required corrections prior to Closing is greatly preferable than redoing the documents if errors have been discovered after distribution to the applicable third parties.

Don't Assume a "4A" NOA Election: The increasing importance of Environmental Liabilities is such that the Parties need to be very careful when preparing a notice of assignment under the CAPL Assignment Procedure for a land agreement that originally included rights in addition to those being acquired by the Purchaser. Suppose, for example, that the original land agreement included Sections 1-4 and 9-12, that there were abandoned wells on sections 4, 9 and 10 and the only Lands still held under the Leases and that are all included in the transaction are Sections 1, 2 and 12.

The typical traditional approach would be to include a 4A (interest in entire agreement) election in the NOA prepared for distribution to the affected third parties, as the Purchaser is acquiring all of the Purchaser's live mineral rights subject to the land agreement. Is that the correct election, though, if any of those previously abandoned wells were still in the reclamation process or if regulatory authorities identified a problem with one of those previously abandoned wells 10 years after closing?

Both Vendors and Purchasers need to assess the evolution of a land agreement over time much more carefully than they have in the past when making the 4A or 4B (assignment of interest in less than entire agreement) election in the applicable notice of assignment.

Master Agreements for Surface Rights: As noted in the definition of Specific Conveyances and the related annotations, Surface Rights relating to road use agreements and crossing agreements are typically held under "master agreements" between the applicable grantor and grantee. As the Vendor cannot assign its interest thereunder, they fall outside the definition of Specific Conveyances. Although the existence of any such agreement would be identified to the Purchaser, the Purchaser will need to enter into new agreements for the applicable Surface Rights within 60 days after Closing.

Deliveries after Closing: Notwithstanding the general expectation that the Specific Conveyance will be fully executed for Closing, Specific Conveyances will sometimes be delivered after Closing. Parties sometimes agree to proceed with Closing without Specific Conveyances being completed for Closing (i.e., large, complex, transaction with an accelerated Closing). The document could easily be modified for such a transaction, but any such modification should address the Parties' expectations about the timing of the delivery of the applicable Specific Conveyances.

The nature of the conveyancing process is also such that Purchasers are reasonably flexible in this area in practice if certain Specific Conveyances are delivered after Closing. This is particularly the case if it is apparent that the Vendor has prepared most of the Specific Conveyances for Closing, that there is a good reason for the delay respecting the outstanding documents and that the Purchaser's experience over the course of the transaction is that the Purchaser believes that completion of the outstanding Specific Conveyances will be pursued diligently by the Vendor.

Transitional Administration: The complexity of the transaction may be such that the Purchaser would not be able to set the files up immediately. It is important that the Vendor and Purchaser discuss the degree to which the Purchaser wishes the Vendor to conduct some of the post-Closing administration in such cases. The two most obvious examples would be the payment of rentals accruing in the one or two month period following Closing and production accounting. These matters should be discussed in the context of the individual transaction. They should be documented on a custom basis, to minimize the likelihood of a misalignment of expectations, if Clauses 3.06 (timing of electronic transfers re rentals), 3.07 (handling of pipeline transfers), 5.05 (rentals after Closing) and 5.06 (production accounting after Closing) do not suitably address their needs for the transaction.

Clause 3.04: Delivery Of Files

As a general statement, original copies of the applicable files and records are to be provided to the Purchaser at the Vendor's expense within 10 Business Days after Closing. There are four potential qualifications to that handling. Firstly, the Parties may agree to a short delay for the provision of those materials if the Vendor is making scanned copies or photocopies. Secondly, the Purchaser may not require those materials if it is already an owner and the materials duplicate its own. Thirdly, the Vendor may provide photocopies if it is also retaining an interest. Fourthly, the Parties might modify the Clause to include special handling processes if seismic or microseismic data are included.

There will be many circumstances in which the period specified for file delivery will not be appropriate, particularly for large transactions. If it is too short or if a Party requires a longer period as a corporate standard, the period can easily be modified by the Parties. Similarly, there may be circumstances in which the relative simplicity of the transaction or the Purchaser's desire to obtain immediate access to the files will cause the Parties to modify the provision to shorten the period for file delivery.

In practice, file delivery can be somewhat complicated if the Vendor's practice is to retain copies of files. This is particularly the case if the transaction is large, a large number of properties are being sold at the same time or Closing will occur near the end of the year. As the Parties will be working with the files for the title review and ancillary document preparation, scanning or copying logistics should be considered carefully early in the transaction cycle. In some cases, it may be beneficial to scan or copy the files prior to conclusion of the initial negotiations.

Subclause B recognizes that not all Vendors make scanned copies or photocopies of the applicable files. If required by the Vendor for audits or third party claims, for example, it may, at its sole expense, obtain copies of the required materials within a prescribed period after the Closing Time, insofar as the Purchaser retains those materials. Insofar as the Purchaser subsequently disposes of its interest in any of the Assets to an assignee, the Purchaser has an obligation to take reasonable steps to have its assignee comply with this obligation for the remainder of the prescribed period.

The 2000 PTP had been structured so that this period was a blank to be negotiated. The 2017 PTP was updated to include a default election of 72 months that the Parties could easily override for their own Agreement (e.g., "for so long as the Purchaser or any of its Affiliates retains an interest in the applicable Assets"). The provision is less than ideal because the Vendor would not have any direct contractual relationship with any subsequent assignee of the Purchaser. However, the Purchaser can create a duty in that later Agreement to provide the access required under Subclause 3.04B that the Purchaser would be able to enforce on behalf of the Vendor.

Clause 3.05: Distribution Of Specific Conveyances

One of the biggest problem areas in processing A&D transactions during industry's initial experiences with A&D had been the delay in the recognition of the Purchaser by third parties. This Clause includes options to address this, with Clause 3.06 addressing the handling of electronic transfers for applicable Leases and Surface Rights and any applicable transfers of the licences for Wells and Tangibles. Clause 3.06 is particularly relevant for transfers of licences for Wells and Tangibles and the Alberta Crown's monthly statement process for Crown rentals.

To streamline this process, 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 generally is on getting the properties into its system. Both Parties benefit through earlier recognition by the operator and other third parties, 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. It may be particularly attractive for a particular transaction 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 the early 1990s, it is now used relatively selectively.

The Alternates each provide the flexibility for the Parties to agree on a different handling of some of the Specific Conveyances. The Parties may agree, for example, to use the selected Alternate for certain Specific Conveyances and a different process for others. It would be important for Parties to document any such segmented responsibility for the handling of Specific Conveyances.

The third party recognition process is also facilitated by selecting an Effective Date within 4-6 weeks of the contemplated Closing Time wherever feasible, as there will be fewer adjustment issues if that timing were selected. While this approach frequently will not be feasible for large transactions that were managed through a competitive bid process, it should be considered to simplify the associated administration for the typical low to modest value transactions for which the 2017 PTP was designed.

Clause 3.06: Electronic Transfers And Rentals

Under this Clause, the Parties coordinate the applicable electronic transfer process, if any, for transfer of the applicable interests in the Leases and, for operated properties for which the Purchaser will be the operator, the Surface Rights and licence transfers for Wells and Tangibles. This requires the Purchaser to accept the applicable transfer on a very short cycle following Closing. The expectation is that electronic transfers will be effected promptly, given the nature of any such electronic transfer process and the relative simplicity of a transaction for which the PTP is most likely to be used. However, this is subject to the overarching qualification about required regulatory approvals for transfers of operated properties identified at the beginning of this article.

Notwithstanding the mutual objective for an accelerated recognition of the Purchaser's interest, the nature of the monthly statement rentals process is that Parties will sometimes modify their approach to transfers of interests in documents that have a near term rental date in order to provide the Purchaser with the opportunity to set up its records for the acquired Assets. Insofar as requested by the Purchaser, the Vendor will pay rentals and other similar land maintenance payments due in the month in which Closing occurs and the two subsequent months. Notwithstanding that the Purchaser has the right to require the Vendor to manage upcoming land maintenance payments for that transition period, there will be many circumstances in which the Purchaser will be able to integrate the files into its records relatively quickly after Closing, such that the Purchaser will not require the Vendor to provide any such transitional support or to do so for only a shorter period. Insofar as the Vendor manages any such payments at the Purchaser's request, any related electronic transfers would be deferred until shortly

following the applicable payment date. The Parties would modify the Clause to manage any different handling. (The Vendor's obligation to pay rentals and other such land maintenance payments during this transitional period is addressed in Clause 5.05.)

Clause 3.07: Pipeline Records And Associated Licence Transfers

This Clause was addressed in greater detail as part of the January, 2018 article respecting transfers of regulatory licences.

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 in this Clause 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 has been included to add flexibility. It allows the Parties to choose to share financial responsibility for any engineering assessments required to rectify any 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.

"Houston, We Have A Landing"

The introductory half day "launch" training session for the 2017 PTP was held on March 21st. The session targeted an invited audience of about 50 larger or active companies and select law firms. There were 39 registrants for the session, representing a diverse audience of over 30 different small, intermediate and large companies and two law firms.

Other than for the larger companies, the vast majority of the attendees had some experience with the 2000 PTP, and confirmed that they had not experienced major issues with that document. For the smaller and intermediate companies in particular, their prior experience with the 2000 PTP will allow them to transition relatively easily to the 2017 PTP. Several of the attendees have already begun to use the 2017 PTP, and, based on their experiences to date, made positive comments about the quality of the new document and the resultant efficiency gains associated with its use.

It was apparent from the introductions at the session, the questions during the session and the opportunity offered for feedback at several points in the session that interest in the potential use of the 2017 PTP for the transactions for which it was designed is significant. This early stage momentum for the new PTP is reminiscent to me of the rollout of the 1997 CAPL Farmout & Royalty Procedure. As was the case with that document, our belief is that companies that use the 2017 PTP for a particular transaction within the PTP's design parameters are likely to prefer to use it for similar transactions in the future after their initial effort to familiarize themselves with the 2017 PTP.

My overall sense of the dynamic in the room at the session, then, is that the real question is not if your company will use the 2017 PTP for certain transactions, but when that use will occur.

The Committee expresses our appreciation to the CAPL Board for its ongoing support of the project, to the parties that commented on the document for helping make it better than it was going to be without your insights and to those who have already taken the initiative to turn the 2017 PTP into a new reality for the low to modest value, straightforward transactions for which it was designed.

We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.

2017 CAPL Property Transfer Procedure: Article 7.00
CAPL Negotiator, June, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

This month's article is about Article 7.00 (Third Party Rights And Consents). As a preliminary comment, Rights of First Refusal and consents are considered in detail in the miscellaneous annotations at the end of the PTP. Users might also review the annotations on Clauses 24.01 and 24.02 of the 2015 CAPL Operating Procedure.

<u>Subclause 7.01A</u>: The Vendor will promptly serve any required ROFR notices. The Purchaser may not waive the existence or operation of a ROFR (Clause 10.04). The Vendor is to provide the Purchaser with copies of the applicable ROFR waivers at Closing under Paragraph 3.03A(c).

Other than for the timing prescribed for delivery of the Purchaser's ROFR values, Clause 7.01 is not prescriptive about the timing for handling any required ROFR notices. In practice, the Parties are mutually motivated to discuss the draft form of ROFR notice and to issue them promptly, recognizing that it is unlikely that a Vendor would issue a ROFR notice before execution of the Agreement.

<u>Subclause 7.01B</u>: The ROFR values to be provided by the Purchaser are to be determined in good faith and on a reasonable basis. As the Vendor retains the contractual relationship with the third parties receiving a ROFR notice, it should not blindly accept the Purchaser's ROFR value. While the proposed value will frequently be used by the Vendor without further discussion, the Vendor should initiate a discussion if the proposed values are not within its expected range.

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 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 new optional sentence at the end of the Subclause.

Subject to any application of the optional sentence, any dispute about the value to be included in a ROFR notice is resolved under the dispute resolution Article (Article 9.00). In theory, this could see arbitration used to resolve the ROFR value. In practice, however, the potential reference to arbitration encourages the Parties to resolve their differences through negotiation, as neither Party would prefer to see a value imposed on it through arbitration. If either Party believes that the determination of an allocated ROFR value will be contentious, it might also request that execution of the Agreement be deferred until it is confirmed.

Subclause 7.01C: The Vendor is to notify the Purchaser promptly following notice from a third party challenging the validity of a ROFR notice, a ROFR value, the election period or the purported application of an exemption to the ROFR under the applicable Title and Operating Document.

Subclause 7.01D: Assets for which ROFRs are exercised are excluded under Clause 1.02, with a corresponding requirement to amend the Agreement prior to Closing. Unless otherwise provided in the Head Agreement, the Vendor would retain the funds associated with a ROFR exercise. There will be circumstances in which it will be preferable to structure the Head Agreement so that ROFR proceeds flow directly to the Purchaser from the ROFR party at completion of that deal. This is particularly the case in an Asset Exchange, as the Vendor will usually wish to retain the characterization of the entire Transaction as a trade for tax and accounting reasons.

Subclause 7.01E: Optional Subclause E may enable 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. This Subclause has been included as an option because Vendors will often resist providing a Purchaser with a potential election 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.

Although the Subclause has been populated by a default of a 50% threshold (rather than a blank), the bolded paragraph at the bottom of the sample Schedule of Elections and Modifications included as Addendum I reminds users of the need to confirm that this value is appropriate. What is material will vary between Transactions, and a strategically critical asset could have a ROFR value significantly below that threshold. To illustrate, it is quite possible that a key Facility ROFR value could represent less than 50% of the total value. Similarly, an allocation of a portion of the Base Purchase Price to seismic data would mean that there would be a smaller value base from which to satisfy the 50% test.

Subclause E and Paragraph (d) of Alternate 8.02B(2) were updated significantly in the 2017 PTP. The 2000 PTP included a negotiated threshold for the combination of Title Defects and ROFR exercises. As of the 2017 PTP, the two processes are independent.

Subclause 7.01F: This Subclause is new in the 2017 PTP. Although the Title and Operating Documents generally require prior consent to a disposition on a “consent not to be unreasonably withheld basis”, those requirements are usually only honoured on an exception basis in practice. The Parties should consider modifying this Subclause to provide for prompt issuance of a consent notice if the Purchaser has a reasonable basis to assume that a third party may attempt to withhold its consent to the disposition. There may be circumstances in which the Parties require a specific condition under Article 10.00 if they believe that any particular consent may be an issue in their Transaction.

That being said, a particular Title and Operating Document, such as a freehold lease granted by an industry player, could potentially include a consent requirement that allows a third party the subjective discretion to withhold a consent. The Parties would need to address any such consent in the manner contemplated in the applicable Title and Operating Document as a consent to be requested prior to Closing. This Subclause provides the Purchaser with the right to request the Vendor to address any such consent requirement promptly.

Potential Closing in Escrow: It is possible that an outstanding consent or ROFR could delay Closing in circumstances in which the Parties would prefer to proceed with Closing. The Parties might consider proceeding with Closing on the unaffected Assets and either a delayed Closing on the affected Assets or a Closing in escrow. The latter would see the applicable amount paid in trust to the Vendor's solicitor, who would hold the funds and the applicable Specific Conveyances until the matter is determined. This would then see the trust conditions lifted or the exclusion of the Assets from the Transaction under Clause 1.02, with the return of the Specific Conveyances to the Vendor and the applicable funds to the Purchaser. Other than a reference in the annotations, the PTP does not address this situation, such that the Parties would need to negotiate their preferred handling in the context of their situation.

"See You In September"

The 2017 PTP will be the subject of one of the education sessions at the upcoming CAPL Conference. We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.

2017 CAPL Property Transfer Procedure: Conditions To Closing
CAPL Negotiator, October, 2018
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 invested in the 2017 document over 20 months by our 15 member committee.

This month's article is about Article 10.00 (Conditions To Closing). The price/value and other material terms were agreed upon at the time of execution of the Agreement. However, the transaction will not be complete (and possession will not pass) until Closing, and Closing is premised on the conditions in Article 10.00 having been satisfied.

Two of the key conditions often applicable to large value transactions are approvals under the *Investment Canada Act* and the *Competition Act*. The annotations provide an overview of those approval requirements as a reference for users. However, they are not addressed in this article because those approvals will seldom be required for the typical low to modest value transactions for which the 2017 PTP was designed.

Clause 10.01-Conditions For Benefit Of Each Party

This Clause addresses conditions that are included for the mutual benefit of the Parties.

Paragraphs (a) & (b): Paragraph (a) addresses the unlikely possibility that approvals could be required under the *Investment Canada Act* and the *Competition Act*. Paragraph (b) ensures that any applicable ROFRs have been managed. Clause 10.04 is structured so that no Party may waive the existence of any ROFR or the need to obtain any approvals required under Paragraph 10.01(a).

Paragraph (c): This Paragraph requires compliance in all material respects with obligations that were to be performed prior to Closing. Purchasers sometimes object to the materiality qualification, and suggest its deletion. However, the exclusion of that qualification would literally enable a Purchaser to terminate the Agreement for any failure of the Vendor to comply precisely with every provision of the Agreement, no matter how minor.

Paragraph (d): This Paragraph requires a Party's reps and warranties to be true and correct in all material respects. However, a Representations and Warranties Certificate is only required if the Parties include a Schedule that includes the form of the certificate. The Parties will often choose not to require this certificate in lower value Transactions for which the PTP is used.

Paragraph (e): This Paragraph addresses the possibility that the transfer of a regulatory licence could be contingent on the submission of a deposit. As noted in the annotations throughout the PTP, 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 this Paragraph. Reviewing the Regulations for each 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. 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.

Each Party is required to address any deposit requirements applicable to it under the Regulations (e.g., due to its Licencee Rating). The Parties might also modify this Paragraph to reflect their needs.

Paragraph (g): As was the case with the construction of the reps and warranties of the Vendor in Clause 6.02 and the Purchaser in Clause 6.04, Paragraph (g) recognizes that the Parties may wish to include additional conditions for their mutual benefit in their Head Agreement. Any such additional condition is treated in a manner consistent with those made in Clause 10.01.

Clause 10.02-Conditions For Benefit Of Purchaser

Paragraph (a): The Purchaser's primary condition precedent is that there will not have been material adverse damage to the Assets after the date of the Agreement/the Effective Date. A Purchaser cannot be expected to complete the Transaction if the Tangibles have been materially damaged during the period that the Vendor is maintaining the Assets on its behalf.

That being said, the Purchaser might still choose to proceed with Closing if there are insurance proceeds accruing for its benefit under Subclause 5.02B. However, this would be at the option of the Purchaser because the potential operational delay in correcting the problem might not be acceptable to it. This would also require the Parties to address a number of insurance related issues at the time (e.g., handling of deductibles, amount of proceeds, settlement rights, litigation management).

The foundation of this Paragraph is that the Vendor has a duty under Clause 5.01 to notify the Purchaser promptly upon becoming aware of any damage of the type contemplated in this Paragraph.

Paragraph (b): The Purchaser will require the Specific Conveyances for Closing, and there is a mirror condition for the benefit of the Vendor in Paragraph 10.03(b).

Paragraph (c): Purchasers will require confirmation that any adverse security registrations will not affect them after Closing. The form of confirmation that is required will depend on the type of Security Interest, and a "No Interest" letter will often be sufficient.

Paragraph (d): Purchasers might attempt to negotiate the inclusion of additional conditions in the Head Agreement. Examples are: (i) approval of the Board of Directors or bank financing; (ii) specified approvals under the Regulations; (iii) an environmental review; (iv) a production audit to confirm that production and accounting data provided to it at the time of the offer were accurate and to confirm current production rates; (v) a physical inspection of the Assets to ensure that they are in good working condition; and (vi) a review of J.V. processing arrangements, etc.

There are two important points to keep in mind about additional conditions. The first is to ensure that any conditions like those in (iii) - (vi) are presented in the context of a discretion that must be exercised reasonably. The second is that it will often be desirable to use a date significantly earlier than the Closing Time as their trigger date, so that the additional conditions are addressed promptly.

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 _____________."*

Purchasers will sometimes structure a condition about the status of Environmental Liabilities that is 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 would more typically be used for larger value Transactions, though.

As noted in the general annotations on the introduction of optional Article 8.00, there is an increasing trend to require the due diligence process to be completed prior to execution of the Agreement. This approach is addressed expressly as of the 2017 PTP through modifications whereby Article 8.00 has become an optional Article. 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 approach will often be 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.

Clause 10.03-Conditions For Benefit Of Vendor

Paragraph (a): The Vendor's primary condition will be delivery of the required payment at Closing.

Paragraph (c): The Vendor may choose to add additional conditions precedent in the Head Agreement under this Paragraph. This will typically be a management approval condition or one respecting specified approvals under the Regulations. The latter would frequently mirror additional Purchaser conditions, so might be included as a mutual condition under Paragraph 10.01(g).

Clause 10.04-Waiver Of Conditions Precedent

Other than for the existence of a ROFR or required regulatory approvals, the conditions in Clauses 10.01, 10.02 and 10.03 may be waived by the Party for which the condition had been included.

Clause 10.05-Failure To Satisfy Conditions

The additional conditions included in the Head Agreement will often be conditions that should be cleared well before Closing. This Subclause places the onus on the Party requesting any such condition to address it in a timely manner, as it is deemed to have been waived if that Party does not notify the other Party by the prescribed time that the additional condition has not been satisfied.

Clause 10.06-Parties To Exercise Diligence With Respect To Conditions

This Clause reiterates the common law duty of the Parties to use reasonable efforts to satisfy any conditions precedent.

Conference Update

The 2017 PTP was reviewed at one of the education sessions at the September CAPL Conference. The opportunity to explain the potential efficiencies associated with use of the document and for attendees to gauge the reaction of their peers was a key step in the process of increasing awareness and use of the document in the land community.

We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.

2017 CAPL Property Transfer Procedure: Liability And Indemnification
CAPL Negotiator, January, 2019
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 on the final draft 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 it will demonstrate convincingly the thought and effort invested in the 2017 PTP over 20 months by our 15 member committee.

This month's article is about Article 13.00 (Liability And Indemnification). Notwithstanding that a transaction has closed, each of the Vendor and Purchaser has certain residual trailing liabilities to the other Party that extend beyond Closing. The liability and indemnification obligations set forth in this Article are one of the most important examples, and reflect generally accepted industry practices.

This article also reinforces something that is not always considered as fully as it should be-that a liability and indemnification obligation is ultimately only as good as the financial viability of the Party with the obligation at the time that a problem arises.

Clause 13.01-Responsibility Of Vendor

This Clause was simplified in the 2017 PTP. Provided that Closing has occurred, the Vendor will be responsible to the Purchaser for its Losses and Liabilities for the Vendor's breach, as of the Closing Date, of any of its representations and warranties made under Article 6.00. This requires the Clause to be read in conjunction with Article 6.00 and for the Vendor to ensure that it does not inadvertently create any inconsistencies between the two Articles with respect to such matters as survival periods.

This is subject to several significant qualifications. The Vendor may accrue responsibility for Losses and Liabilities: (i) under Clause 5.08 due to its Gross Negligence or Wilful Misconduct when managing the Assets on behalf of the Purchaser; and (ii) for fraud respecting representations and warranties or information provided to the Purchaser, as contemplated in Clause 6.05. The Vendor retains responsibility for certain adjustments under Subclause 4.02C. The Clause is also subject to limitations in Clause 13.03 and the allocation of responsibility for Environmental Liabilities under Clause 13.04. Notwithstanding those qualifications, there is an overarching exception insofar as Losses and Liabilities suffered by the Purchaser are due to its own Gross Negligence or Wilful Misconduct.

Subject to the adjustments contemplated in Subclause 4.02C and any allegation of fraud on the part of the Vendor, any notice of a claim by the Purchaser must be made within one year after the Closing Time. However, the Parties might choose to modify this period and the corresponding survival period for representations and warranties under Article 6.00 for certain transactions (e.g., six months for certain undeveloped lands deals), as noted throughout the 2017 PTP.

Clause 13.02-Responsibility Of Purchaser

Provided that Closing has occurred, the Purchaser will generally assume liability and indemnification

responsibilities to the Vendor as of the Effective Date. Note the use of the Effective Date as the trigger date in this Clause, rather than the Closing Date at which possession actually passes. This ultimately reflects a linkage between the financial benefits that accrue to the Purchaser as the result of the use of the Effective Date as the date for financial adjustments (such as net production proceeds) and the associated risks relating to the Assets during that period. In that regard, it is important to remember the obligations of the Vendor to the Purchaser during the Interim Period under Article 5.00 (Maintenance Of Business) and the right of the Purchaser to terminate the transaction under Paragraph 10.02(a) if there was substantial unrepaired damage to the Assets.

As in Clause 13.01, there is an exception insofar as Losses and Liabilities suffered by the Vendor are due to: (i) its Gross Negligence or Wilful Misconduct, including that under Clause 5.08 respecting the management of the Assets on behalf of the Purchaser; or (ii) fraud by the Vendor with respect to reps and warranties or information provided to the Purchaser, as contemplated in Clause 6.05.

There are two major differences between Clauses 13.01 and 13.02. The first is that the liability and indemnification obligation of the Purchaser under Clause 13.02 is not limited to breaches of its representations and warranties under Article 6.00. The second is that there is no survival period comparable to that in Clause 13.01. These differences reflect the fact that loss events could be occurring years after Closing.

Clause 13.03-Limit On Responsibility For Losses And Liabilities

The total of the Vendor's liabilities and indemnities, including the claims relating to its representations and warranties, cannot exceed the consideration for the Assets under Subclause A. This had been an optional Subclause in the 2000 PTP, and was changed in the 2017 PTP because it is generally accepted. As noted in the bolded paragraph in the sample Schedule of Elections and Modifications included as Addendum I, the Purchaser will sometimes want to modify this for smaller transactions.

There have sometimes been suggestions that the liability for a breach of representation should be limited to the amount paid for the applicable Asset. There are, however, two problems associated with that view. The first is that the breach of a representation respecting a Tangible, for example, could have an unrecognized domino effect on other Assets. The second is that such a provision would effectively eliminate damages for the breach of a representation respecting the Miscellaneous Interests (typically valued at not more than $10), even though their existence (e.g., a production sale contract) may have induced the Purchaser to purchase the Assets.

Purchasers sometimes request a similar cap on the Purchaser's legal responsibility because of the belief that the limitation should be reciprocal. This is not appropriate, though, assuming the *caveat emptor* principle in Clause 13.04 is maintained. Once the Vendor has disposed of the Assets, there are basically four ways in which it would have a claim against a Purchaser under Clauses 13.02 and 13.04 - (a) if the Vendor is responsible for losses of third parties because of delays in the formal recognition process under third party agreements; (b) if the Vendor retains an interest in a portion of the Leases and it holds the Purchaser's interest in trust; (c) if a third party commences a claim and includes the Vendor as a defendant because of its “deep pockets” or involvement in the property when the incident allegedly occurred; and (d) if Regulatory Authorities move along the chain to a previous owner for Abandonment and Reclamation Obligations or other Environmental Liabilities. Although unlikely, these events could happen at any time. The value at the time of the deal would have little relevance with respect to a major environmental problem 15 years later. The most obvious context for such an event would be with respect to a sour gas well, an old oil well or an old facility.

Subclause 13.03B was an optional provision in the 2000 PTP, for which the financial threshold was also to be negotiated. The optional elements were changed in the 2017 PTP because of prevailing industry practices. The Subclause sets a minimum $25,000 threshold/“deductible” for claims by either Party, to ensure that the Parties are not allocating resources to immaterial claims.

This amount may be too high for small transactions and too low for transactions at the higher end of the value spectrum for which the PTP is likely to be used in practice. The sample Schedule of Elections in Addendum I includes a reminder for users to consider if this threshold is appropriate for their transaction. While a blank could have been included (as in the 2000 PTP), this would have required an additional election when the $25,000 threshold will probably be quite reasonable for many transactions for which the PTP is most likely to be used.

Clause 13.04-Assets Acquired On "As Is" Basis

Provided that Closing occurs, the Purchaser is acquiring the Assets on an "as is" basis. The Purchaser is assuming full responsibility for all Abandonment and Reclamation Obligations, other Environmental Liabilities and obligations accrued or thereafter accruing with respect to the Assets, except for: (i) any claims it may have for fraud or the breach of the Vendor's representations with respect to the condition of the Assets under Clause 6.02; or (ii) any other negotiated outcome that deviates from this general handling. This principle has become generally accepted across industry.

That being said, the onus is on each Party to consider carefully environmental issues associated with the Assets in each transaction. In that regard, the annotations on Clause 13.04 offer additional insights of which users should be aware when preparing for a transaction.

Clause 13.05-Notice Of Claims

This Clause outlines the expectations for notification of any claim that arises that may trigger the indemnification and liability obligations in Article 13.00.

Clause 13.06-Substitution And Subrogation

This Clause is included to facilitate enforcement of rights with respect to representations and warranties that the Vendor may still enforce against a prior vendor under an earlier agreement relating to the applicable Assets.

Not All Purchasers Are Created Equal

The liability and indemnification obligations of each Party under Article 13.00 are only as good as financial viability of the Party with the liability and indemnification obligation at the relevant time.

Given the increasing vigilance of Regulatory Authorities and other working interest owners in assessing proposed transfers, a Vendor will often create greater shareholder value by selling Assets to a Purchaser that offers a less attractive price if that Purchaser were more financially viable and the outcome from the licence and partner approval processes were more predictable.

We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.

2017 CAPL Property Transfer Procedure: Adjustments
CAPL Negotiator, March, 2019
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 on the final draft 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 for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 it will demonstrate convincingly the thought and effort invested in the 2017 PTP over 20 months by our 15-member committee.

This month's article is about Article 4.00 (Adjustments). This Article apportions benefits and obligations respecting the Assets between the Parties as of the Effective Date in order to match revenues with the associated costs, risks and expenses.

We worked closely with PASC with respect to the 2017 version of this Article. As a consequence, it includes a number of significant enhancements relative to the 2000 PTP and the more traditional handling in industry A&D agreements. Companies not otherwise considering use of the PTP should review this Article, since it may identify improvement opportunities in existing internal precedents.

Clause 4.01-Benefits And Obligations To Be Apportioned

The benefits and obligations respecting the Assets are to be apportioned on an accrual basis between the Vendor and the Purchaser, as of the Effective Date, in accordance with established accounting practices in the oil and gas industry. J.V. billings will be a major source of this information, recognizing that there will be some issues about the accuracy of the billings and their linkages to particular time periods in many cases.

There will be many implementation type issues associated with a transaction that accounting personnel need to handle in the spirit of the principles in this Article, as it is not feasible to be prescriptive about all situations. It is recommended that Parties ensure that their respective accounting personnel are discussing these issues well before Closing to ensure a smoother transition. Two examples of these types of issues are the Alberta Crown Royalty recognition process (RMF2 form) and gas cost allowance ("cost allowance" under the current Alberta Regulations), and the latter can be particularly complex.

General Rule: As noted in Paragraph (a), one of the consequences of an accrual based approach to the adjustment process is that it is necessary to look at when the work was performed, rather than the invoicing cycle. If a well was rig released two weeks before the Effective Date, for example, the Vendor would retain full responsibility for those drilling costs in the absence of a different negotiated outcome, notwithstanding that the Purchaser would get all of the benefit from the expenditure and that at least some of the invoices for the pre-Effective Date expenditures would be delivered to the Vendor after the Effective Date.

Advances and Deposits: Paragraphs (b) and (c) recognize that advances, cash calls and deposits will often still be outstanding after Closing. While not an apportionment around a defined date like some

other items in the Clause, they need to be transferred to the Purchaser and addressed in the adjustment process.

Rentals and Land Maintenance Charges: Paragraph (d) addresses the handling of rentals and other land maintenance type charges for which the traditional approach has been to do a *per diem* rental allocation as of the Effective Date. Given the modest scale of the transactions for which the PTP is most likely to be used, this is an optional Paragraph as of the 2017 PTP. This recognizes that Parties will often choose to ignore a *per diem* rental adjustment for many small to modest sized transactions for which the PTP would 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 a very rough calculation indicates that the amount of this adjustment would be minor, it is probably attractive not to select this Paragraph for simplicity and devote the time to a more pressing matter.

If this Paragraph is selected, rentals are apportioned on a *per diem* basis under Paragraph (d). Even if this Paragraph is selected, some Vendors choose not to include rentals for non-operated surface rentals in this process in any event because of the effort required to confirm those amounts from J.V. billings and the fact that they are often relatively minor.

Taxes: Users must remember to include property tax adjustments in the Paragraph (e) adjustment. These can be material for some properties.

The applicable freehold mineral tax may be such that the Parties prefer to modify Paragraph (e) to eliminate any adjustment for that item.

Handling of Production Proceeds: Paragraph (f) was introduced in the 2017 PTP to provide greater certainty about the pricing to be used when determining the production proceeds accruing to the benefit of the Purchaser during the Interim Period and for that incremental period after Closing before it becomes recognized as the owner of the Assets.

Production proceeds are to be calculated using a Market Price unless otherwise provided in the Agreement or agreed by the Parties. The Market Price definition is based on the 2015 CAPL Operating Procedure definition, and is a sale price that is not unreasonable in the circumstances, having regard to current market conditions. This structure protects the Purchaser against a notional allocation of unfavourable hedges to production from the Lands. The corollary of this is that the Purchaser is not permitted to share in any attractive hedges that the Vendor had in place with respect to the property. The Parties are always free to negotiate a different outcome, however.

There may be circumstances, though, in which there are unique attributes to the Assets that cause the Parties to address marketing arrangements more specifically in the context of their particular transaction. This could result in the use of an index, such as AECO-C, less transportation differential, as the sales price for gas volumes being sold on the Purchaser's behalf from the Effective Date.

Production Inventory: As a general statement, production inventory is retained by the Vendor under Paragraph (g), subject to qualifications with respect to "tank bottoms" and a sulphur pad or storage block. While this handling of produced volumes reflects typical industry practice, Parties will sometimes prefer not to address produced volumes in tanks on site in this manner because of potential challenges in measuring volumes accurately, particularly if the volumes are modest. (See also the annotations on the Clause 1.01 definition of Excluded Assets.)

As a Vendor is unlikely to wish to retain its share of a low to negative value sulphur pad or storage block, the PTP provides that the Vendor's interest therein is included in the Assets, unless the Parties otherwise agree in the Head Agreement. This would require a determination of the value of the sulphur,

with a resultant tax allocation to product inventory. The Parties will wish to consider this in the context of their particular transaction in light of the associated assumption of potential liabilities and the value of the sulphur inventory. This handling of sulphur is also premised on the assumptions that the value of the sulphur inventory is very modest and that the Vendor's stored sulphur pertains only to production from the Assets. The Parties would need to address their expectations clearly in the Head Agreement if the sulphur pertained to other fields that were not included in the Assets.

Handling of Third Party Overhead: Paragraph (h) was introduced in the 2017 PTP, and is another provision that should be considered as part of a review of internal company precedents.

Insofar as the Vendor is operating any of the Assets under the Title and Operating Documents during the Interim Period and in a transitional period after Closing under Clause 5.04, any overhead recovery that accrues to the Vendor, as operator, under the applicable Title and Operating Documents is retained by it, and is not subject to the adjustment process. This would see the Vendor retaining overhead amounts paid by third parties. The Purchaser would not reimburse the Vendor for the Vendor's own share of the overhead charges through this mechanism, though, as the share of overhead paid by the Vendor would be handled as a cost under the adjustment process.

This handling reflects the principle that the Purchaser should not receive the benefit of overhead recoveries accruing under the Title and Operating Documents for activities conducted by the Vendor for which the Vendor is not receiving any compensation from the Purchaser under the Agreement.

Incentives: Incentives (Paragraph (i)) are generally of two types - those that accrue to operations without regard to the attributes of the participants (typically as represented by the operator) and those that accrue to a particular Party based on certain financial attributes or status personal to it. Incentives that accrue to a Party because of its unique attributes are excluded from the adjustment process. Those that accrue based on the activity without regard to the specific corporate attributes of the submitting party are included in the adjustment process.

Thirteenth Month Adjustments: Paragraph (j) addresses Thirteenth Month Adjustments.

The PTP goes beyond the typical industry handling by addressing the situation in which there is a significant variance in revenues, costs and throughput volumes during the respective periods of ownership in a Facility. This additional content is included because an operator's Thirteenth Month Adjustment typically uses annual averages that do not recognize variances during a year. In essence, the Parties will apportion on a *per diem* basis, but may conduct their own equalization to ensure that there is a more equitable allocation between the pre and post Effective Date periods. As this equalization can be a labour intensive process, it is only recommended if the perceived adjustments are sufficient to warrant the effort.

If the Vendor is the operator of such a Facility, it should consider completing any outstanding Thirteenth Month Adjustments at the earliest feasible date, as it can be difficult to allocate resources to this task for a Facility that has been sold. If the Vendor is a non-operator in such a Facility, the Thirteenth Month Adjustment could occur well after Closing, as contemplated in Subclause 4.02C.

No Interest on Adjustments: Except to the extent provided for the accrual of interest in Clause 2.06 and for the failure to pay revenues as due under Paragraph 5.04(c), no interest accrues on adjustments, as noted in Paragraph (k). Clause 2.06 is structured so that an interest accrual on the Purchase Price is based on the Purchase Price plus or minus any modifications resulting from the exclusion of certain Assets under Clause 1.02 and the net adjustment included in the interim statement of adjustments for Closing under Paragraph 4.02(a). Paragraph 5.03(c) creates an obligation to manage adjustments on a monthly cycle, failing which the applicable amount may accrue interest under Clause 12.02.

Dispute Resolution: Paragraph (l) provides that all disputes respecting adjustments are to be resolved under the dispute resolution provisions in Article 9.00.

Clause 4.02-Adjustments To Accounts

Subclause 4.02A: An interim statement of adjustments will often not be prepared for Closing if: (a) the amounts are minor; (b) Closing occurs shortly after the Effective Date; or (c) a transaction was completed on an accelerated basis. It was not included specifically in the deliveries at Closing under Subclause 3.03A as a result, although it is captured in the general reference in Paragraph 3.03A(e).

The interim statement of adjustments is processed on a cash basis because revenues are required to be forwarded on a monthly basis during the adjustment period under Paragraph 5.04(c). The Parties may wish to modify the PTP to use an accrual basis if their intention is to forward revenues with only the interim and final statements.

One of the Vendor's objectives is to minimize its G&A costs associated with a property. It naturally wishes its obligations to end as quickly as is possible, so a six-month adjustment period has been included in Paragraph A(b) for a final statement of adjustments, to reflect the most commonly negotiated period. The Parties remain free to override this period by selecting a different period. Purchasers will sometimes prefer a one-year period in Paragraph A(b), but that would usually exceed the period that is actually required for the vast majority of transactions for which the PTP is likely to be used. Similarly, the timing might be modified to a 90 or 120-day period for simple transactions.

Subclause 4.02B: Subclause B includes a mutual audit right because of the possibility that the Purchaser may receive information that is relevant to the adjustment process without the Vendor receiving that information. This could occur, for example, with respect to a Thirteenth Month Adjustment if the operator chose to provide information only to the Purchaser.

Although the timing is consistent with industry norms (i.e., PASC J.V. Audit Protocol and the relationship to Subclause 4.02C), the Parties may prefer to use different time periods in Subclause B because of the circumstances of their transaction or because of a corporate preference. The audit period, for example, will often be too long for small transactions or those in which the Purchaser is already the operator of the Assets.

Errors will occasionally be discovered after the audit period specified in Subclause B. In practice, Parties are typically able to resolve any such issues through discussion. However, it may be preferable to use a longer period in that Subclause for some complex transactions.

The $10,000 adjustment threshold included in this Subclause is one that Parties may prefer to modify for particular transactions or as a corporate preference change to the PTP.

Subclause 4.02C: Notwithstanding the timing used in the remainder of Clause 4.02 to settle accounts between the Vendor and the Purchaser, additional flexibility is required to address third party adjustment processes, such as Thirteenth Month Adjustments, operator error adjustments, J.V. audits and lessor royalty audits.

A 36-month cutoff period has been included in Paragraph C(a) because the typical 26-month audit provision under J.V. agreements is linked to a calendar year. If, for example, a sale closed in January, 2019, it is possible that the J.V. audit would not be completed until December, 2021, with outstanding audit exceptions potentially extending the process.

There is an exception in Paragraph C(b) for royalty audits or other reviews conducted by the grantor of the Leases, however. The Crown conducts its audits infrequently. As a result, the Vendor retains full responsibility for the period prior to the Effective Date, notwithstanding the timing limitations otherwise

imposed by this Clause and Clauses 6.05 and 13.01. The Crown (Alberta) can reassess royalties at any time in the event of negligence or fraud and within four years after the end of the month in which the Crown royalty was payable in all other cases.

The Vendor has a contractual obligation to satisfy the adjustment requirements under Subclauses 4.02C and D, even if those obligations are discovered or confirmed after expiry of the survival period for the Vendor's representations and warranties under Subclause 6.05A and Clause 13.01. Failure to fulfil these obligations leaves the Vendor open to a normal claim for breach of contract.

This Clause does not fully address pre-Effective Date audit issues. While the apportionment principles between the Parties are clear, this issue can be complicated significantly by third party operators. They may frustrate the principles herein by choosing not to match an audit adjustment to the pre and post Effective Date periods. They may also occasionally choose to deal only with the current owner, such that the Vendor largely relies on the good faith of the Purchaser for the distribution of positive audit adjustments that are unknown to the Vendor.

Subclause 4.02D: This Subclause was introduced in the 2017 PTP. It recognizes that nothing in the transaction will interfere with any rights or obligations of the Vendor with respect to audits for the period prior to the Effective Date.

Subclause 4.02E: This Subclause extends the limitation period in the *Limitations Act* (Alberta) for only claims that arise under Article 4.00 respecting adjustments and audits to two years after expiry of the time the applicable audit was permitted to be performed. This reflects the fact that the timing of adjustments will often be a function of adjustments and audits under the land and J.V. agreements that govern the Assets. Subject to the timing restrictions respecting representations and warranties and liability and indemnification in Articles 6.00 and 13.00, the normal limitation period applies to other claims under the Agreement.

Clause 4.03: This Clause was written in consultation with the Canada Revenue Agency ("CRA"). It has been modified significantly relative to the 2000 PTP Clause because the CRA was 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.

Most Agreements are subject to conditions precedent. As a consequence, beneficial ownership of the Assets is retained by the Vendor until Closing in the view of the CRA, 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 the Clause included in the 2017 PTP reflects the CRA's requirement that the income or loss 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, with a corresponding adjustment to the Purchase Price. This necessarily requires an equitable adjustment mechanism to the Base Purchase Price.

In determining the Purchase Price adjustment, care must be taken to ensure that all reasonable factors are taken into account, including the relevant income tax impact. This is important to avoid an overpayment or underpayment, as the case may be, by the Purchaser to the Vendor. Generally, in calculating the tax adjustment, the net production income should be calculated in accordance with the *Income Tax Act* (Canada).

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

The negotiation of this percentage can often be contentious. Vendors will often request the percentage to reflect the circumstance that they are currently fully taxable (even if in a long-term 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 does not consider the resultant impact on the Vendor's tax position in later years.

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

Clause 4.04: This Clause was introduced in the 2017 PTP. Insofar as the Purchaser erroneously received funds or an adjustment respecting the Assets and a period prior to the Effective Date, the Purchaser is to notify the Vendor of that error promptly and remit payment to it for the applicable amount. The Purchaser will hold any such amount in trust for the Vendor until that adjustment is effected. Any such amount is independent of the final statement of adjustments process, as the Purchaser has no right to any portion of such amount.

Please Review The Instructions Before Using

We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.

One piece of feedback that we received second hand was with respect to the use of the 2017 PTP for an operated property and major disappointment that there was a significant delay in the processing of the associated regulatory transfers by the Alberta Energy Regulator under its Bulletin 2017-13.

As noted in the January, 2018 article and consistently throughout the annotations and the Addendums to the PTP in the context of that Bulletin, the onus is always on the Parties to add custom content in their Head Agreement to address their particular needs if there is any question about the ability to effect any regulatory transfer associated with operated Assets. This might be done by including some 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 have potentially created unintended consequences for users.

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.

2017 CAPL Property Transfer Procedure: Maintenance Of Business
CAPL Negotiator, May, 2019
Jim MacLean

The 2017 CAPL Property Transfer Procedure ("PTP") was endorsed by the CAPL Board in December, 2017. 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 on the final draft 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 use of the PTP for anyone that wishes to use the document for a new transaction; (vii) a PDF of the text of the 2017 PTP without the annotations to facilitate use; (viii) a collection of the articles from The Negotiator to date on the PTP, as updated to reflect the final document; and (ix) 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 it will demonstrate convincingly the thought and effort invested in the 2017 PTP over 20 months by our 15-member committee.

This month's article is the last in this series, and is about Article 5.00 (Maintenance Of Business). This is an area in which many documents protect Purchasers insufficiently. Although the PTP has been structured to attempt to provide appropriate protections, each Agreement should be reviewed carefully to ensure that the expectations of the Parties are being met for their particular transaction.

The Article is premised on the Vendor's willingness to allocate resources to monitor the property sufficiently to comply with the obligations outlined in the Article. This has occasionally been a problem in the industry in the transitional period up to and following Closing, as some Vendors have not distributed new notices, AFEs, etc. to the Purchaser in a timely manner.

This is particularly important during the transitional period after Closing in which the Purchaser is in the process of being recognized by third parties. There is a particular risk that the Vendor's personnel may be operating under the mistaken belief that the Vendor's obligations to the Purchaser are complete after the Purchaser has "taken the keys to the car" at Closing.

Internal procedures must also be implemented to ensure that all of the Vendor's affected personnel are aware of the obligations of the Vendor under this Article, particularly with respect to material expenditures proposed after the Effective Date.

Clause 5.01-Assets To Be Maintained In Proper Manner

This Clause addresses the Vendor's obligations for maintenance of the Assets on behalf of the Purchaser during the Interim Period. It was modified as of the 2017 PTP to provide the Vendor with the authority to assume a new obligation for which the Vendor's share of the associated expenditure is reasonably expected not to exceed $50,000, even if the Vendor's share of the cost ultimately exceeds that amount. The latter qualification ensures that a Vendor's authority is not compromised if the estimate is too low, and is analogous to the handling of the Operator's discretionary financial authority in Subclause 3.01B of the 2015 CAPL Operating Procedure.

Clause 5.03 prescribes certain circumstances in which consultation with the Purchaser is required. There will be others in which consultation is reasonably expected, such as a continuation application or a land selection under the leases. A Vendor that allows a lease to expire without consultation with a Purchaser about the possibility of a continuation application could place itself at risk.

The Clause also includes a duty on the Vendor to notify the Purchaser promptly upon the Vendor becoming aware of any damage of the type contemplated by the "No Substantial Damage" condition in

Paragraph 10.02(a). This is relevant for both the purposes of that representation and any application of Clause 5.02 to the handling of insurance proceeds.

Clause 5.02-Obligations For Insurance

The Vendor is not required to obtain additional insurance for the Assets prior to Closing, except insofar as required to do so in the Head Agreement, under the Regulations or under applicable agreements with third parties, such as operating agreements. The premiums for existing policies attributable to the Interim Period would typically be minor with respect to the low to modest value transactions for which the PTP is most likely to be used, and would be unlikely to warrant the effort required to include that amount in the Article 4.00 adjustment.

The typical industry provision of this type does not refer to insurance. The express statement on insurance, however, simply alerts the Purchaser that it should be obtaining its own policies in due course. It is difficult for a Purchaser to argue that the usual provision that does not address additional insurance creates any obligation on the Vendor to obtain or maintain insurance.

Clause 5.03-Commitments During Interim Period

Subclause 5.03A: This Subclause addresses the Vendor's obligation to obtain the consent of the Purchaser before making expenditures or assuming any new commitments or obligations, except as provided within the authorities granted under this Subclause. This is subject to an exception for actions that are reasonably necessary for the protection of life or property.

Paragraph (a) includes a qualification to address the situation in which the Vendor is obligated to participate in certain expenditures that it has not approved. The most common examples of this situation would be with respect to expenditures within an operator's permissible authority limit and expenditures that have been approved through a vote of the applicable owners, such as a mail ballot under a CO&O Agreement or a unit agreement. The Vendor is required to notify the Purchaser of any such expenditure for which the Vendor's share of the cost is reasonably expected to exceed $50,000, together with appropriate supporting information about that expenditure. If it occurs prior to execution of the Agreement, it will often be helpful to include any such commitment in the Schedule that identifies outstanding AFEs. One important example of the latter would be the situation in which commitments have been made after the Effective Date, but prior to negotiations with the Purchaser.

The $50,000 expenditure threshold included in this Paragraph (as well as Clause 5.01 and Paragraph 6.02(h)) 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 in Addendum I.

Paragraph (b) enables the Vendor to sell production in the ordinary course of business under sales agreements permitted hereunder (i.e., in accordance with the requirements in Paragraph (c) of the Title and Operating Documents-sales contracts identified on a Schedule or sales contracts terminable on not more than 31 days' notice). In this regard, Paragraph 4.01(f) was introduced in the 2017 PTP to ensure that production proceeds were calculated using a "Market Price."

Paragraph (c) recognizes that portions of the Lands could expire in the normal course under the terms of the applicable leases. The general duty of the Vendor to maintain the Assets in good standing in a proper and prudent manner and to consult with the Purchaser would still apply in terms of coordination about any pending expiry and the possibility of retention of the applicable Lands, though.

Paragraph (d) includes a general obligation to consult with respect to mail ballots issued under the Title and Operating Documents. While the financial outcome respecting a mail ballot is also covered under Paragraph (a), mail ballots can address other situations. As under Paragraph 5.03(a), the Purchaser could be bound by a vote, even though the Vendor had voted against the mail ballot at the Purchaser's instruction.

Subclause 5.03B: This Subclause specifically addresses the chain of events that is to occur when a decision must be made with respect to an operation on the Lands or the exercise of some other right respecting the Assets. The most likely instances of those rights would be: (a) rights under an area of mutual interest provision; (b) elections with respect to an operation, such as an operation notice under Article 10.00 of the CAPL Operating Procedure; (c) elections under a surrender provision, such as Article 11.00 of the CAPL Operating Procedure; (d) elections under an abandonment provision, such as Article 12.00 of the CAPL Operating Procedure; and (e) elections under a Right of First Refusal provision, such as Alternate 24.01B of the CAPL Operating Procedure.

Notwithstanding the inclusion of this Subclause, the Parties would typically prefer to negotiate a provision that addresses their particular circumstances more directly if they believe that they will need to manage any such proposal.

Another way to manage this potential issue is to try to compress the period between the completion of negotiations and Closing to under 30 days if this is feasible under the Regulations. This issue may also require an acceleration of Closing in some circumstances for either all of the Assets or by segmenting the transaction to accelerate Closing for the Assets directly affected by the Proposal. This would be easier to achieve for smaller transactions, of course.

If a decision is required with respect to a particular operation notice, mail ballot, etc., the Vendor is to give notice of the matter promptly to the Purchaser, including supporting information in sufficient detail to enable it to have a reasonable understanding of the nature, schedule and cost (e.g., the information provided with the applicable AFE). This is subject to two qualifications that may require some discussion at the time. The first is that the disclosure is only permitted insofar as it is not prohibited under the applicable Title and Operating Documents (i.e., in breach of a JOA confidentiality obligation if the disclosure could damage the applicable third parties, such as information about a strategically important well while a ROFR is outstanding). The second is that the Vendor is not required to disclose any of its proprietary interpretations to facilitate the Purchaser's review of the matter.

The Purchaser must respond at least two Business Days before the Vendor is required to make its election, with the Vendor then making that election on behalf of the Purchaser. That period generally allows for internal handling of the matter by the Vendor. However, short notice AMI or casing point rights would often have to be dealt with by the Parties at the time on an exception basis, as the stated 12-hour response period for response periods under 48 hours would often be logistically difficult.

If the Purchaser elects not to participate in a particular operation, Paragraph (d) reminds users that the consequence of that non-participation is a Permitted Encumbrance, as noted in the introduction of Paragraph (a) of that definition. The net effect of that handling is that the Purchase Price will not be altered because of any resultant termination or alteration of the Vendor's interest in the Assets, and that consequence will not, of itself, constitute a Title Defect or breach of the Vendor's representations and warranties pertaining to the applicable Assets.

The Vendor will sometimes wish to obtain advance payment of the Purchaser's share of applicable costs prior to the Vendor's election to participate in an operation or land acquisition on behalf of the Purchaser under Paragraph 5.03B(e). The Parties may also consider other alternatives that may be appropriate based on the circumstances and their history.

This mechanism is unlikely to be contentious if Closing proceeds. However, it could problematic if Closing ultimately does not occur. While it is unlikely to pose problems in that situation if the Parties had a common view (positive or negative) of the matter, problems could arise if one Party favoured a proposed expenditure and the other did not.

Subclause 5.03C: The Purchaser may already have the right to propose operations under an existing operating agreement. However, it is generally precluded from requesting the Vendor to propose additional operations to third parties prior to Closing. In some cases, such as an expiry, it may be appropriate for the Vendor to propose an operation on behalf of the Purchaser, and this should be

addressed in the Head Agreement or by amending this Subclause. This would presumably be negotiated by the Parties early in their negotiations or as a particular need arises.

Subclause 5.03D: This Subclause allows the Vendor to refuse to follow certain instructions of the Purchaser. It was introduced in the 2017 PTP. It is based on the proviso in Paragraph 5.04(b) of the 2000 PTP, with the addition of a reference to the Regulations and a requirement to notify the Purchaser of the basis for its conclusion. This Subclause applies to both Clause 5.03 and 5.04 because of the *mutatis mutandis* reference in Paragraph 5.04(a) to the application of Clause 5.03.

Clause 5.04-Post Closing Transitional Maintenance Of Assets

The premise of this Clause is the same as in Clause 5.02. The Vendor is to continue to maintain the applicable Assets on behalf of the Purchaser until it can exercise its rights with third parties. The Vendor will try to provide notices of assignment at Closing. Assuming that the files are provided to the Purchaser at about that time, this should not impose a burden on the Vendor in practice.

Revenues received by the Vendor during the adjustment phase are to be processed in a manner consistent with its internal accounting process, and are to be forwarded to the Purchaser on a monthly cycle. This ensures that it receives its funds in a timely manner, while not placing an undue burden on the Vendor's personnel. If costs exceed revenues, the Vendor would invoice the Purchaser for the applicable amount. Amounts not paid when due may accrue interest under Clause 12.02.

The Parties may sometimes wish to address the transition in ownership through a separate contract operating agreement or transitional services agreement whereby the Vendor continues to operate applicable Assets on behalf of the Purchaser for a period after Closing. There may be other circumstances in which the Parties agree in the Head Agreement that the Vendor is to receive a negotiated monthly administrative fee for providing transitional support until the third party recognition process is complete or a date at which the Vendor's obligations under this Clause cease. This is unlikely to be considered for transactions for which the PTP is most likely to be used, though.

Clause 5.05-Payment Of Rentals By Vendor:

This Clause addresses the potential handling of rentals and other land maintenance payments during the transitional period when the Purchaser is setting up the files in its land information system. It should be read in conjunction with Clause 3.06 relating to the handling of electronic transfers. It is the better practice to address clearly the responsibility for rentals during this transitional period, as Purchasers will not be prepared to assume responsibility for those payments of rentals until several months after Closing (i.e., two months after Closing) in some cases.

Insofar as requested by the Purchaser, the Vendor will pay rentals and other similar land maintenance payments due in the month in which Closing occurs and the two subsequent months. Notwithstanding that the Purchaser has the right to require the Vendor to manage upcoming land maintenance payments for that transition period, there will be many circumstances in which the Purchaser will be able to integrate the files into its records relatively quickly after Closing, such that the Purchaser will not require the Vendor to provide any such transitional support or to do so for only a shorter period.

Clause 5.06-Production Accounting During Month In Which Closing Occurs

This Clause requires the Vendor to provide production accounting support for production obtained during the calendar month in which Closing occurs, in addition to its responsibility for production accounting for prior calendar months of the Interim Period. If, for example, the Effective Date were May 1st and Closing were July 16th, the Vendor would manage production accounting for the May-July production months. This would require the Purchaser to provide production data for July.

Clause 5.07-Transfer Of Incidental Obligations To Third Parties

This Clause was introduced in the 2017 PTP. It addresses the circumstance in which the Vendor holds interests on behalf of a third party in any of the Assets acquired by the Purchaser, such as a "silent partner." If the Vendor is disposing of all of its interest in the applicable Assets to the Purchaser, the Purchaser will step into the shoes of the Vendor with respect to any such third party.

While the Clause admittedly places a burden on the Purchaser that it would prefer not to have, the alternative of having the Vendor retain ongoing administrative obligations for a property in which it no longer holds any interest would be unacceptable to most Vendors. This Clause raises awareness of the issue, and a Purchaser that is concerned about it can try to negotiate a different handling.

Clause 5.08-Vendor Acting On Behalf Of Purchaser For Maintenance Of Assets

The Vendor is deemed to be acting on behalf of the Purchaser for all actions taken by the Vendor on behalf of the Purchaser under Article 5.00, assuming the Vendor's actions are in compliance with this Article and that its actions or omissions do not constitute Gross Negligence or Wilful Misconduct.

The Purchaser will indemnify the Vendor for Losses and Liabilities suffered by the Vendor as a result of acting on behalf of the Purchaser under Article 5.00. However, the Purchaser is not obligated to indemnify the Vendor, insofar as they result from the Vendor's Gross Negligence or Wilful Misconduct, unless the act or omission was done or omitted to be done on the Purchaser's instruction. Purchasers will sometimes request that the standard be simple negligence. The simple negligence standard was not included. The Vendor is not obtaining any benefit from this transitional "possession" of the Assets, and the inclusion of a simple negligence standard would require the Vendor to retain a higher level of responsibility than an operator has for operational matters under the Operating Procedure.

Thanks For Reading!

This article is the last of the current series on the 2017 PTP. The compilation of articles in the series can be accessed as a single document from the PTP section of the CAPL web page.

We greatly appreciate the opportunity to have been able to use The Negotiator to share this series of articles with you.

We look forward to hearing about your experiences in "making simple transactions simple again" as you begin to work with the 2017 PTP.