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COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
PLAINTIFF	ALBERTA ENERGY REGULATOR
DEFENDANT	LEXIN RESOURCES LTD.
DOCUMENT	**BRIEF OF THE APPLICANT MIDSTREAM CANADA LTD.**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	MacDONALD HANLEY Barristers and Solicitors Attention: James G. Hanley 2050, 736 - 6 Avenue SW Calgary, AB, T2P 3T7 Tel: 403-668-5432 Fax: 403-233-2033 File No.: 53397.001JGH jhanley@macdonaldhanley.com

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INTRODUCTION

1. This is the brief of the Applicant, Midstream Canada Ltd. ("Midstream") in support of its application for an order:

- lifting the stay of proceedings in the Receivership Order granted by this Court March 22, 2017 and the stay, if any, that may apply to the assets and estate of Lexin Resources Ltd. ("Lexin") as a result of the Bankruptcy Order dated October 25, 2017,
- authorizing Midstream to issue to Lexin, or its Receiver, the notice under Article 202 of the standard 1990 CAPL Operating Agreements in relation to assuming Operatorship of jointly operated Wells and under Article 303 of the Petroleum Joint Venture Association ("PJVA") 1999 Standard Operating Procedure incorporated into each of the Construction Ownership and Operation Agreements ("CO&O") governing the Gas Gathering facilities;
- directing the transfer of the Operatorship over the jointly operated wells and facilities in accordance with the Operating Procedures, and directing the Receiver to deliver all records, files and other materials pertaining to the wells and facilities to Midstream.

I. STATEMENT OF FACTS

2. On December 21, 2017, Midstream entered into a Purchase & Sale Agreement with ExxonMobil Energy Canada ("the Exxon PSA"), which agreement closed on February 1, 2018, to acquire certain wells and facilities in the area of High River, Alberta.

Affidavit of Neeky Noor-Ali, Sworn on April 30, 2018,
at paras. 3-4 **["Noor-Ali Affidavit"]**

3. As a result of that agreement, Midstream acquired Exxon's interest in 53 wells and a series of pipelines in the High River area.

Noor-Ali Affidavit at para. 4 and Exhibit A thereto

4. Lexin is the Operator, license-holder and working interest partner in 21 of the 53 wells acquired from Exxon by Midstream ("Lexin Wells").

Noor-Ali Affidavit at para. 5 and Exhibit B thereto

5. All operating agreements related to the Lexin Wells are governed by the 1990 CAPL Operating Procedure.

Noor-Ali Affidavit at paras. 6-7 and Exhibit D thereto

6. Midstream also acquired an interest in certain pipelines, gathering systems and related facilities under the Exxon PSA as follows:

- 25% interest in the Hooker Gas Gathering System;
- 25% to 50% interest based on Functional Unit in the Hooker East Compression and Gas Gathering System;
- 54.8822% interest in the South East Hooker Compression and Gas Gathering System; and
- 66.6667% interest in the Hooker North Gas Gathering System (the "Gathering Systems").

Noor-Ali Affidavit at para. 8

7. These Gathering Systems serve all of the 21 Lexin Wells, as well as the 32 other wells purchased from Exxon (the "non-Lexin Wells").

8. Midstream is the Operator of the Hooker North Gas Gathering System. Lexin is the Operator of the other three systems.

Noor-Ali Affidavit at paras. 10 and 12

9. Operation of each of the Gathering Systems is governed by a Construction Ownership and Operation Agreement ("CO&O"). The three agreements relevant to the Lexin-operated Gathering Systems are drafted in substantially similar terms.

Noor-Ali Affidavit at para. 9 and Exhibits E, F and G thereto

10. On March 22, 2017, a receivership order was issued by Jeffrey J over all the assets and undertakings of Lexin. Grant Thornton was appointed as the receiver. As part of that order, a stay of proceedings was issued.

Receivership Order dated March 22, 2017, paras. 10-12

11. On October 25, 2017, a Bankruptcy Order adjudging Lexin to be bankrupt was issued by Romaine J. Grant Thornton was appointed as the trustee in bankruptcy. This Order may have triggered the application of s. 69.3 of the *Bankruptcy and Insolvency Act*, which imposes a stay of proceedings:

> 69.3(1) [...], on the bankruptcy of any debtor, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.

Bankruptcy Order dated October 25, 2017
Bankruptcy and Insolvency Act, RSC 1985, c. B-3, s. 69.3

12. All of the 53 wells and the Gas Gathering Systems referenced above have been shut-in pursuant to or as a result of the AER Closure Order C2017-01 dated February 15, 2017 and pursuant to the Receivership Order granted by this Court on March 20, 2017. No production has been generated by any of the wells, nor has production flowed through any of the Gathering Systems.

Noor-Ali Affidavit at para. 13

13. Midstream purchased the assets from Exxon with the intention of re-starting the wells (both Lexin and non-Lexin), generating production and moving the production through the pipelines to sell to the market. In order to do that, the pipelines must be operational in advance of or concurrent with the wells coming on production. Additionally, the relevant facilities must be constructed and regulatory authority granted prior to production restarting.

Noor-Ali Affidavit at para. 14

14. Midstream wishes to become Operator of the three Lexin-operated Gathering Systems to allow it, as Operator, to reopen the pipelines and facilities after acquiring regulatory approvals.

Noor-Ali Affidavit at para. 14

15. Midstream also wishes to become the Operator of the Lexin Wells so as to re-start production from these wells.

Noor-Ali Affidavit at para. 15

16. In addition to the Lexin Wells, Midstream intends to re-start production from the 32 non-Lexin wells, which are also serviced by the Gathering Facilities and thus require that those Facilities be reopened.

Receivership Order of Romaine J, September 1, 2017

17. Article 202(a) of the 1990 CAPL Operating Procedure, which governs the relationship between Midstream and Lexin with respect to the Lexin Wells, provides for the immediate replacement of an Operating Partner upon the bankruptcy, insolvency, or similar financial distress of that Partner:

> 202 REPLACEMENT OF OPERATOR -
>
> (a) The Operator shall be replaced immediately and another Operator appointed forthwith pursuant to Clause 206 upon notice to such effect being served by any party to the other parties if:
>
> (i) the Operator becomes bankrupt or insolvent, commits or suffers any act of bankruptcy or insolvency, is placed in receivership, seeks debtor relief protection under applicable legislation (including, without restricting the generality of the foregoing, the *Bankruptcy Act* of Canada and the *Companies' Creditors Arrangement Act* of Canada) or permits any judgement to be registered against its working interest, and without restricting the generality of the foregoing, an Operator shall be deemed insolvent for the purposes of this Clause if it Is unable to pay its debts as they fall due in the usual course of business or if it does not have sufficient assets to satisfy its cumulative liabilities in full;

1990 CAPL Operating Procedure at Article 202(a), Exhibit D to the Noor-Ali Affidavit

18. Midstream wishes to exercise its right under Article 202(a) to give notice to Lexin, and subsequently to assume Operatorship of the Lexin Wells.

19. The CO&O's governing the Gathering Systems also provide for replacement of the Operator upon the bankruptcy, insolvency, or similar financial distress:

> 303. Replacement of Operator
>
> Operator shall immediately cease to be Operator in the circumstances described in Subclauses (a) and (b) below and in all circumstances described in this Clause a replacement Operator be appointed pursuant to Clause 304, if:
>
> (a) Operator becomes bankrupt or insolvent, commits or suffers any act of bankruptcy or insolvency, is placed in receivership or a receiver/manager or Person filling that role is appointed with respect to its property, seeks debtor relief protection under applicable legislation (including. without restricting the generality of the foregoing , the *Bankruptcy and Insolvency Act of Canada* and the *Companies' Creditor Arrangement Act of Canada)* or permits any judgment to be registered against its interest in the Facility or any portion thereof, and without restricting the generality of the foregoing, an Operator shall be deemed insolvent for the purposes of this Clause if its unable to pay its debts as they fall due in the usual course of business;

CO&O's, Exhibits E, F and G to the Noor-Ali Affidavit, at Article 303

20. Midstream wishes to exercise its right under Article 303 to give notice to Lexin, and subsequently to assume Operatorship of the three Lexin-operated Gathering Systems.

21. Under a 1990 CAPL Operating Procedure, notice must be delivered to the Operator when replacement is contemplated pursuant to Article 2.02. Notice is not required under the CO&O's, which state rather that the Operator of the Gas Gathering Systems shall immediately be replaced upon occurrence of an event indicated in Article 303.

CO&O's, Exhibits E, F and G to the Noor-Ali Affidavit, at Article 303

22. In February 2018, in-house counsel for Midstream notified counsel for the Receiver of their desire to assume Operatorship of the Hooker CO&O Gas Gathering System. Counsel for the Receiver on February 8, 2018 indicated its view that the stay of proceedings

imposed by the Receivership Order prohibited attempts to obtain Operatorship or issue notice of intention to do so.

Noor-Ali Affidavit, at para. 24

23. Under the Receivership, there are no funds and therefore the Receiver has no ability to respond to or deal with day-to-day operations, emergencies, contingencies, repairs or maintenance on the wells and facilities. The AER has therefore assigned care and custody of the Wells to the Orphan Well Association, or occasionally to working interest parties. The Orphan Well Fund does not operate wells and facilities, and consequently they are shut-in. The result is that these wells (both Lexin and non-Lexin), while capable of economic production, are not being produced due to the AER Closure Order, the pipelines being shut-in, the insolvency of the Operating partner, and the regulations pertaining to the Orphan Well Fund care and control of these assets.

Noor-Ali Affidavit, at para. 38

24. Midstream is prepared to open the Gathering Systems and operate the wells upon transfer of Operatorship.

Noor-Ali Affidavit, at para. 38

25. Midstream is a start-up oil and gas company focused on the acquisition and development of oil and gas assets. The management team has over 200 years of combined oil and gas industry experience and is fully capable of operating the wells and facilities. Midstream is eligible to hold licenses to the wells and facilities at issue. Midstream has received AER 067 approval relating to the Operatorship of these wells.

Noor-Ali Affidavit, at paras. 33-34

II. ISSUES

26. The issues before this Honourable Court are:

i. Is Midstream entitled to an order lifting the stay of proceedings?

ii. Should Midstream be authorized to assume Operatorship pursuant to Article 303 of the PJVA 1999 Operating Procedures attached to each of the Lexin-operated CO&O Agreements governing the Gathering Systems?

iii. Should Midstream be authorized to issue the notice required under Article 202(a) of the 1990 CAPL Operating Procedures, and to assume Operatorship of the jointly-operated wells and facilities?

III. ARGUMENT

(a) The Right to Operatorship is not Assignable by Lexin or the Receiver

27. Lexin's bankruptcy and its continued Operatorship of the 21 Lexin Wells and the Gathering Systems causes substantial prejudice to Midstream in that it prevents Midstream from re-starting operation of the 21 jointly-operated wells, as well as the 32 non-Lexin Wells, which require use of the Lexin-operated Gathering Systems. Midstream's intention in purchasing the working interests in these wells and facilities from Exxon was to re-start production, and to generate cash flow and profit. That purpose is entirely thwarted as long as Lexin retains Operatorship.

Noor-Ali Affidavit, at paras. 25-26

28. However, if Midstream could restart production of the wells, revenues and profits could be generated, which would accrue not only to Midstream, but also to Lexin as joint-operator. A transfer of Operatorship is therefore unlikely to cause prejudice to Lexin, but, on the contrary, may well result in a material benefit to Lexin.

Noor-Ali Affidavit, at paras. 28 and 35

29. Although the Receiver has attempted to market the Lexin Wells and other facilities to potential buyers, it does not appear that the assets offered included a transfer of Operatorship.

Noor-Ali Affidavit, at para. 29

30. In any event, it does not appear that such a transfer would be permitted without Midstream's consent, and in fact Midstream, upon request for such consent, would have the right to refuse and instead assume operatorship itself. This right is set out at Article 206 of the 1990 CAPL agreement:

> 206 APPOINTMENT OF NEW OPERATOR -
>
> (a) If an Operator resigns or is to be replaced, a successor Operator shall be appointed by the affirmative vote (by notice to the other parties) of two (2) or more parties representing a majority of the working interests In the joint lands, [...] **If there are only two (2) Joint-Operators and the Operator that resigned or is to be replaced is one of the Joint-Operators, the other Joint-Operator shall have the right to become the Operator.**

1990 CAPL Operating Procedure at Article 206(a), Exhibit D to the Noor-Ali Affidavit

31. Should Lexin or the Receiver attempt to offer transfer of operatorship over the wells and facilities to a potential buyer, Midstream intends to insist on its right to become Operator.

Noor-Ali Affidavit, at para. 29

32. As noted above, Article 206 of the 1990 CAPL Operating Procedure gives Midstream the right to assume Operatorship of the wells and facilities, should Lexin or the Receiver attempt to transfer that right to a potential buyer of Lexin's assets. The inability for Lexin or the Receiver to propose such a transfer or assignment to a third party was recently confirmed in ***National Bank of Canada v. Scollard Energy Ltd.***, where Dario J was dealing with a similarly worded provision of 2007 CAPL Operating Procedure:

> 19 I pause the analysis of lifting the stay pursuant to Clause 2.02A(a) of CAPL 2007 to address the more central issue in this case. Although not initially raised by counsel, I note that under CAPL 2007, at no time (even if solvent) is an

Operator able to transfer operatorship to an assignee (unless an affiliate) without the approval of the other working interest owners, which must be achieved by a vote of at least two parties with a working interest of more than 50% working interest: CAPL 2007 clauses 2.06C and 2.09. If there are only two Operators when the Operator resigns or is removed, the other party may become the Operator on the service of notice so long as it holds more than 40% of the working interest.

20 In the present case, Scollard and Firenze are 50-50% working interest owners for most of the 23 wells and associated Facilities in question. For all but four of the wells and associated Facilities, Firenze is a more than 40% working interest owner.

21 Firenze therefore appears to have the unconditional right to assume operatorship (in all but the four wells and associated Facilities in which it holds 40% or less of a working interest) under CAPL 2007. **Thus, Firenze argues, the transfer by the Receiver of Scollard's working interest cannot include a transfer of the right to operatorship. If this were permitted, the Receiver would be placed in a better position than Scollard, who could not have transferred the operatorship outside of the procedure set out in clause 2.06, and the Receiver would be conveying more than the debtor had the right to convey before the receivership.**

22 Courts have ruled on many occasions that the assignment of the contractual rights of a party in receivership is made subject to the contractual rights of the counter parties, such as the right to withhold consent or the right to first refusal: [...]. **Operatorship, a contractual right, may not be assigned outside of the terms of the contract.**

23 **I similarly find that the Receiver cannot transfer more than Scollard's interest in this case.** Firenze has the contractual right, under clauses 2.09 and 2.06C, to demand it become the Operator of all but four of the wells and associated Facilities at the time of Scollard's transfer of its working interest to a non-affiliate. [Emphasis added]

National Bank of Canada v. Scollard Energy Ltd., 2018 ABQB 126 at paras. 19-23, [2018] AJ No. 223 [Tab 1]

33. Consequently, the right which Midstream seeks to enforce - the contractual right to Operatorship over the wells and facilities - is not a right that any third party would be entitled to acquire under the receivership or the bankruptcy.

34. Midstream's application is therefore not an attempt to thwart or circumvent the receivership or bankruptcy process, nor to get a leg up on creditors of Lexin. Midstream

seeks simply to enforce a contractual right that cannot be acquired by or transferred to a creditor or purchaser, and the exercise of which will cause no or negligible prejudice to the estate of the debtor Lexin.

(b) Lifting the Stay of Proceedings

35. The criteria for lifting a stay of proceedings imposed by a receivership order were discussed in ***Alignvest Private Debt Ltd v Surefire Industries Ltd.*** The Court identified two criteria: (1) material prejudice to the party seeking the stay, or (2) other equitable grounds for lifting the stay:

> 40 The test for lifting a stay imposed pursuant to a receivership order **focuses on the totality of circumstances and the relative prejudice to the parties involved in the receivership**.
>
> 41 Guidance can be drawn from the provisions of section 69.4 of the BIA in determining whether a stay in a receivership should be lifted. The Court should be satisfied that **the party applying to lift the stay is likely to be materially prejudiced by the stay or that it would be equitable to lift the stay on other grounds.** The burden is on the applicant: *Re Ma*, [2001] OJ NO. 1189 (C.A.).
>
> ***Alignvest Private Debt Ltd v Surefire Industries Ltd***, 2015 ABQB 148 at paras. 40 -41, 608 AR 292 [Tab 2]
> affirmed 2015 ABCA 355, 31 CBR (6th) 98 [Tab 3]

36. In deciding whether to lift the stay, the court must consider whether there are "sound reasons" for doing so which are consistent with the bankruptcy or receivership regime:

> 75 [...] The court has discretion to lift the stay in circumstances where it is necessary. This is provided for in s. 69.4 and in s. 215 of the *BIA*. [...] Under s. 69.4 of the *BIA*, a person seeking leave need not prove a *prima facie* case, only that there are **sound reasons, consistent with the scheme of the *BIA* to relieve against the automatic stay**, [...].
>
> 76 With respect to receivers appointed by court order under the *BIA*, and monitors appointed under the *CCAA*, since the stay flows from the court's order, the court must be persuaded to lift the stay, and applies the same principles.
>
> ***Romspen Investment Corp. v. Courtice Auto Wreckers Ltd.***, 2017 ONCA 301 at paras. 75-76, 138 OR (3d) 373, 98 [Tab 4];

leave to appeal refused, ***Courtice Auto Wreckers Ltd. (Receiver of) v. International Union of Operation Engineers, Local 793***, [2017] S.C.C.A. No. 238, File No. 37636

37. "Sound reasons" exist where lifting the stay would alleviate prejudice to the applicant, but cause no real prejudice to other creditors. This was the case in ***Brookside Capital Partners Inc. v. RSM Richter Inc.***, where the applicant Brookside sought to lift the stay in order to perfect a security interest. Lovecchio J noted that lifting the stay to permit the applicant's request would have no impact on the reorganization of the debtor, and would not prejudice other creditors, but would permit the applicant to protect an interest it had negotiated with the debtor:

> 36 First, there is no question but that the Debenture is a secured instrument and that it was intended to be so. As a result, **this is not a case of a creditor trying to gain an advantage but rather simply a creditor trying to hold on to an advantage it had already negotiated**. [...]
>
> [...]
>
> 43 In this case, [...] **there is no reason to believe Brookside's amended registration would have any effect on the reorganization of Kodiak**. Indeed the evidence is to the contrary; when Brookside amended its registration on August 10, 2005, Kodiak had already filed materials a day earlier indicating that attempts to reorganize were at an end and that they were opting to liquidate the company. In fact, the amended registration did not affect Kodiak's reorganization efforts in any way.
>
> 44 I also find that **there is no prejudice to Kodiak or other creditors as a result of the amended registration** because if it were not for Kodiak obtaining the CCAA stay Brookside would have been entitled to amend its registration at any time to perfect the security interest it was granted. The same can be said about the receivership stay (also obtained by the debtor in this case). In these circumstances, **the greater prejudice would be to Brookside if leave were not given to amend its registration.** [Emphasis added]

Brookside Capital Partners Inc. v. RSM Richter Inc., 2006 ABQB 572 at paras. 36 and 43-44, 25 CBR (5th) 273 [Tab 5]

38. In ***National Bank of Canada v. Scollard Energy Ltd.,*** Dario J held that the contractual right to assume operatorship contained in the CAPL agreements is not, by itself, sufficient

reason to lift a stay of proceedings. However, she also indicated that the stay may be lifted where additional factors demonstrating prejudice are present:

> 12 The existence of the contractual right of transfer upon insolvency (or any of the other conditions set out in clause 2.02A(a)) is not in itself a sufficient basis to lift the stay. [...].
>
> 13 As such, **the court must look beyond the rights the parties intended to convey in clause 2.02A(a) to determine whether the stay should be lifted**. There must be sound reasons to relieve against the stay imposed pursuant to a receivership order; [...]

National Bank of Canada v. Scollard Energy Ltd., supra at paras. 12-13, [Tab 1]

39. Sound reasons were found to exist in ***Bank of Montreal v. Bumper Development Corp.*** wherein MacLeod J lifted a stay in order to permit the applicant, Eagle, to enforce its contractual right to assume operatorship of the jointly-operated wells and facilities. The application was opposed by Florent, who was the successful bidder that had purchased the assets of the insolvent operator, Bumper. Prior to sale of the assets, Eagle had agreed to delay enforcement of its right to replace the operator, in order to support the sale process. MacLeod J granted Eagle's application, affirming Eagle's right to immediate replacement of Bumper, and also noted that there was no prejudice to the the insolvent Joint-Operator's creditors, as the operatorship was not something otherwise secured and transferable:

> 17 It is quite clear from the contractual documents at issue that as between Eagle and Bumper, Eagle was entitled to be Operator of the wells and the Battery upon Bumper becoming insolvent or being placed in receivership (see *Tri-Star Resources Ltd v JC International Petroleum Ltd* (1986), [1987] 2 WWR 141 (ABQB), 48 Alta LR (2d) 355). The existence of such an arrangement reflects the understanding that Operators conduct operations on behalf of all parties and in so doing, frequently deal with money belonging to the non-operating parties.
>
> 18 Had Eagle pursued its right to be Operator at the time of the granting of the Receivership Order or soon thereafter, I can think of no reason why this Court would not have acceded to Eagle's request to lift the stay and grant a declaration with respect to both the wells and the Battery.

19 The stay was granted incidental to the appointment of the Receiver to permit for orderly realization and distribution. Eagle's right to operate, however, arises under a contract which pre-dates the receivership. Also, **there is no reason to interfere with the contractual rights of Eagle which are not subject to the security of Bumper's creditors**.

[...]

23 **In my view it would be unfair to deprive Eagle of its clear contractual right to be Operator of both the wells and battery. To do so would be tantamount to appropriating Eagle's right for the benefit of Bumper's creditors**. [Emphasis added]

Bank of Montreal v. Bumper Development Corp., 2016 ABQB 363 at paras. 17-19 and 23, 38 CBR (6th) 118 [Tab 6]

40. The decision in ***Canadian Sahara Energy Inc v Sonde Resources Corp***. also illustrates how benefit and prejudice to joint-operating parties may be weighed in evaluating whether to lift a stay. In that case, Sonde and Sahara were equal partners in an oil and gas venture. Sahara became insolvent while drilling was underway and filed a notice of intention to make a proposal under the BIA. Sonde served a Notice to Withdraw on Sahara arguing that restructuring proceedings were doomed to fail, and would simply deprive Sonde of valuable time to find a new partner to help cover the costs of drilling the well. The Court weighed the prejudice and benefit to each party and held that the uncertainty for Sonde of potential arrangements with a new partner proposed by the bankrupt, the need to proceed with drilling, and the substantial cost to Sonde if it had to finance operations on its own, all weighed in favour of lifting the stay:

12 All of these questions can be answered by looking at the benefits and prejudice suffered by each of the parties. I must balance the benefits to Sahara in allowing it time to finalize its agreement with Petroceltic with the benefits to Sonde in allowing it to terminate its relationship with Sahara so that it can pursue other partners. I begin with the obvious: **these parties agreed to the contractual provisions in the various agreements. While one party to a contract may, in certain circumstances, be entitled to relief from the harshness of contractual provisions, in most cases the need for contractual certainty must prevail and the contract must be enforced.** Both Sahara and Sonde knew what their respective rights and obligations were. Sahara now faces the prospect that it will forfeit its rights under the agreement because it has not been able to pay the

money it agreed to pay. Sonde now faces the prospect that it will need to find a new partner in very short order or take full responsibility for drilling the Zarat well.

13 **The factors that I find significant are the expenses which Sonde faces in drilling the North Zarat well**, the $ 64 million in guarantees given by Sonde, the uncertainty created by the Petroceltic agreement which is really only an option **which could leave Sonde without a partner as development of the project proceeds**, and the relatively small amount of costs paid by Sahara to date. **Sonde's risks and investment in this project are large**, Sahara's are small. The equities favour Sonde. [...] [Emphasis added]

Canadian Sahara Energy Inc v Sonde Resources Corp, 2010 ABQB 730 at paras. 12-13, 73 CBR (5th) 135 [Tab 7]

41. In the present case, it is submitted that the criteria for lifting a stay weigh in favour of granting the order sought by Midstream:

- The inability to re-open the wells and facilities, both Lexin and non-Lexin, represents a clear prejudice to Midstream;
- By contrast, lifting the stay would cause little to no prejudice to the estate of Lexin - in fact, it may well create a benefit to the estate, since revenues will be generated that will accrue to Lexin as joint-operator and enhance its financial position;
- Similarly, there is no prejudice to creditors of Lexin, since operatorship is not a transferrable asset, and in any event, has not been offered for sale as part of the receiver's marketing efforts;
- These factors constitute sound reasons for lifting the stay and are consistent with the bankruptcy or receivership of Lexin;
- To the extent that any prejudice may accrue to Lexin by lifting the stay, it is far outweighed by the prejudice to Midstream in refusing the stay, given its complete inability to re-open and operate the wells and facilities, both Lexin and non-Lexin.

(c) Transfer of Operatorship

42. Case law interpreting various versions of the CAPL operating agreement has recognized the right of a joint operator to immediately replace an operator who has become insolvent. In ***Tri-Star Resources Ltd. v. J.C. International Petroleum Ltd.***, Moore CJQB

dealt with an application filed by two joint operators seeking replacement of the operating partner, JCI, who had made a proposal in bankruptcy. Moore CJQB had no difficulty concluding that the applicants had a clear right to the relief they sought:

> It is interesting to observe the wording of para 202 of the operating agreement. It states "The operator shall be replaced immediately ... if the operator becomes bankrupt or insolvent ... " (the underlining is mine). **Clearly the mandatory nature of the words "shall be replaced immediately" dictates that J.C. International should be replaced by the party having the next greatest interest in accordance with the provisions of para 206 (b) and (d).** [Emphasis added]

Tri-Star Resources Ltd. v. J.C. International Petroleum Ltd., [1987] 2 WWR 141 at p. 4 (QL), 48 Alta LR (2d) 355 [Tab 8]

43. Similar reasoning was also applied in ***Eon Energy Ltd. v. Ferrybank Resources Ltd.*** In that case, Ferrybank was the operating partner for regulatory purposes, but Eon was appointed as Ferrybank's agent, with full discretion to manage the wells in any manner it saw fit. Ferrybank was also entitled to collect and hold revenues solution gas revenues from selected wells. Disputes arose between the parties on a number of points, and both applied to remove the other from its operator functions. Nixon J held that Ferrybank had committed acts of insolvency, which disentitled it from managing wells or collecting revenues:

> 311 The reason for removal of an operator in the case of insolvency is the risk to the co-owners if an insolvent operator co-mingles funds thereby putting at risk the co-owner's share of revenues: *Tri-Star Resources Ltd v JC International Petroleum Ltd* (1986), 48 Alta LR (2d) 355 (ABQB).
>
> 312 Eon has established that Ferrybank suffered an act of insolvency, disentitling it from managing the wells, and collecting revenues.
>
> [...]
>
> 321 Ferrybank, therefore, meets the definition of insolvency in Clause 202. It is not able to meet its obligations as they become due. **As such, it is disqualified from managing the wells, or receiving revenues for the joint account**. [...] [Emphasis added]

Eon Energy Ltd. v. Ferrybank Resources Ltd., 2016 ABQB 585 at paras. 311-312 and 321, [2016] AJ No. 109 [Tab 9]

44. ***Tri-Star*** was followed in ***Bank of Montreal v. Bumper Development Corp.***, cited earlier, where the working partner Eagle sought to enforce its right to take over operatorship. MacLeod J granted Eagle's application, noting Eagle's right to immediate replacement of the insolvent operator, Bumper:

> 17 It is quite clear from the contractual documents at issue that as between Eagle and Bumper, **Eagle was entitled to be Operator of the wells and the Battery upon Bumper becoming insolvent or being placed in receivership** (see *Tri-Star Resources Ltd v JC International Petroleum Ltd* (1986), [1987] 2 WWR 141 (ABQB), 48 Alta LR (2d) 355). [...].
>
> 18 Had Eagle pursued its right to be Operator at the time of the granting of the Receivership Order or soon thereafter, **I can think of no reason why this Court would not have acceded to Eagle's request to lift the stay and grant a declaration with respect to both the wells and the Battery**.
>
> ***Bank of Montreal v. Bumper Development Corp.***, supra at paras. 17-18 [Tab 6]

45. In the present case, it is respectfully submitted that:

- The receivership and bankruptcy of Lexin clearly fall within Article 202 of the 1990 CAPL Operating Procedure with respect to the wells and Article 303 of the PJVA 1999 Operating Procedure governing the gas Gathering Systems;
- The language of Article 202 and Article 303 are explicit and contains a mandatory requirement that Lexin (or the Receiver) shall be replaced as Operator;
- Midstream has a clear contractual right to replace Lexin as Operator over the Lexin Wells and Gathering Systems;
- Allowing Lexin, or the Receiver on its behalf, to continue as Operator causes serious prejudice to all parties, as it prevents the reopening and operation of the wells and facilities, both Lexin and non-Lexin, and deprives all parties, but most particularly Midstream, of substantial revenue.

IV. RELIEF SOUGHT

46. The Applicant Midstream Canada Ltd. therefore respectfully requests that this Honourable Court:

i) GRANT the present Application;

ii) ORDER that the stay of proceedings in the Receivership Order is lifted to allow Midstream to take any steps necessary to pursue the transfer and assumption of Operatorship for the Wells and Facilities described in the Affidavit of Noor-Ali ("the Wells and Facilities");

iii) DECLARE that Midstream shall be entitled to commence and continue any proceedings against the property and assets of Lexin to pursue the transfer and assumption of Operatorship and any steps necessary to give effect to the transfer of Operatorship for the Wells and Facilities;

iv) ORDER that Midstream shall be named Operator of those oil and gas Wells and Facilities for which Operatorship is sought in the Affidavit of Noor-Ali;

v) ORDER that the Receiver shall deliver to Midstream any and all records pertaining to the Wells and Facilities which are subject to this Order, including but not limited to all the well files, land files, processing, marketing, transportation and production agreements, all copies of contracts, names of contacts and field and contract operator information.

vi) GRANT costs of the application to Midstream; and

vii) ORDER such further and other relief as the Court may consider appropriate.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 24 DAY OF MAY, 2018.

MacDONALD HANLEY

Per: for

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