
# ENVIRONMENTAL OBLIGATIONS TRUMP LENDERS: THE TREND CONTINUES

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The Court of King's Bench of Alberta decision in *Re Mantle Materials Group, Ltd* ("***Mantle***")[1] continues a recent trend in Alberta in which environmental remediation obligations are found to have priority over the interests of secured creditors. This bulletin provides an overview of the *Mantle* decision and updates our previous bulletin (found here), which addressed the intersection of environmental protection and secured creditor rights in Canada.

**An Overview of *Mantle***

Mantle Materials Group, Ltd. ("**Mantle**") operated fourteen gravel pits on public land and ten gravel pits on private land in Alberta pursuant to surface material leases issued by Alberta Environment and Protected Areas ("**AEPA**"). Such surface material leases require its holder to complete certain environmental reclamation obligations at the end-of-life of the gravel pits. These obligations were secured by a $1 million dollar financial assurance held by AEPA. In 2021, Mantle acquired business related assets from JMB Crushing Systems Inc. ("**JMB**") through JMB's *Companies' Creditors Arrangement Act* ("**CCAA**") proceedings. As part of those proceedings, JMB's undesirable assets were transferred to a residual company pursuant to a Reverse Vesting Order while JMB and a subsidiary retained their desirable assets. Mantle then amalgamated with JMB and its subsidiary.[2]

Subsequent to the commencement of JMB's CCAA proceedings, AEPA issued Environmental Protection Orders (the "**Environmental Orders**") against JMB requiring it to comply with its environmental reclamation obligations with respect to its gravel pit operations. When Mantle amalgamated with JMB and its subsidiary, it became liable for JMB's outstanding Environmental Orders.[3]

In order to fund the acquisition of equipment for use in its operations, Mantle obtained a loan in the amount of $1.7 million dollars from Travelers Capital Corp. ("**Travelers**"), which was secured by a purchase money security interest in the equipment.[4]

Soon after Travelers' loan was issued, Mantle began experiencing financial difficulties, which were compounded by the excessive debt inherited from the JMB CCAA proceedings and Mantle's obligation to

comply with the Environmental Orders. Mantle ultimately filed a notice of intention to make a proposal under section 50.4 of the *Bankruptcy and Insolvency Act*. In this proposal, Mantle sought priority charges in favour of the involved restructuring professionals and its interim (debtor in possession) lender. Mantle took the position that Travelers should not be entitled to realize on its security interest until the reclamation work was completed, as completion of the work would result in the release of $1 million dollars in financial assurance posted by Mantle with the AEPA. Travelers argued against this proposal submitting that the restructuring charges could not rank senior to its security interest and that it should be permitted to realize on its security right away.[5]

**The *Mantle* Decision**

In the Court of King's Bench of Alberta decision, Justice Feasby relied on three leading cases regarding priority of environmental obligations in insolvency proceedings, being *Orphan Well Association v. Grant Thornton Ltd.* ("***Redwater***"),[6] *Manitok Energy Inc (Re)* ("***Manitok***"),[7] and *Orphan Well Association v. Trident Exploration Corp* ("***Trident***");[8] all of which have upheld the principle that end-of-life environmental obligations must have priority over the interests of secured creditors (i.e., a super priority). In the *Mantle* case, all parties therefore proceeded on the basis that the Environmental Orders issued by AEPA had the same legal effect as an abandonment and reclamation order issued by the Alberta Energy Regulator and should be subject to like treatment in insolvency proceedings.

Travelers disputed the application of these cases on the basis that there is an exception to the super priority for assets unrelated to the environmental condition or damage.[9] However, Justice Feasby held that he was bound to follow the decision in *Redwater* and that the court in *Trident* found that unlicensed personal property assets were determined to be related to the environmental obligations because the company had only one business, being oil and gas production. Practically, it did not make sense to differentiate between assets, as it would undermine the policy purposes behind the super priority principle.[10]

The Court in *Mantle* found Mantle's equipment to be analogous to the equipment and real estate in *Trident*; the equipment over which Travelers had a security interest was as much a part of Mantle's gravel business as the equipment in *Trident* was a party of Trident's oil and gas production business.[11] Accordingly, Travelers' security interest was held to be subordinate to the restructuring charges that were necessary for completion of environmental remediation work to the satisfaction of the AEPA and could not be enforced until the environmental reclamation was complete.[12]

**Looking Ahead**

*Mantle* demonstrates the requirement for thorough due diligence on the part of a lender, paired with the expansion of a super priority claim into a non-oil and gas context. Interestingly, the Court in *Mantle* noted that


Travelers had conducted its own due diligence, and among the materials available, were documents highlighting the live nature of Mantle's environmental reclamation obligations. However, it is possible Travelers did not appreciate the risks of the Environmental Orders having priority over its security in these circumstances because the case law in this area is still developing. Going forward, lenders who take security based on the value of equipment used in resource extractive industries in Alberta, and likely other Canadian jurisdictions, will need to be aware of the risk that their security may be found to rank behind public duties to protect the environment.

[1] *Re Mantle Materials Group, Ltd*, 2023 ABKB 488 [*Mantle*].
[2] *Ibid* at paras 4 - 11.
[3] *Ibid* at paras 6, 11.
[4] *Ibid* at para 12.
[5] *Ibid* at paras 13 - 15.
[6] *Orphan Well Association v Grant Thornton Ltd*, 2019 SCC 5.
[7] *Manitok Energy Inc (Re)*, 2022 ABCA 117.
[8] *Orphan Well Association v Trident Exploration Corp*, 2022 ABKB 839.
[9] *Mantle, supra* note 1 at para 30.
[10] *Ibid* at para 36.
[11] *Ibid* at paras 38, 40.
[12] *Ibid* at para 43.

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**A Cautionary Note**