

Quebec mining royalty agreements as seen through the lense of the Quebec Court of Appeal

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On August 6, 2013, the Quebec Court of Appeal rendered a very interesting decision in the case of *Anglo Pacific Group plc v. Ernst & Young Inc., 9261-0690 Québec Inc., Northern Star Mining Corp. and Jake Resources Inc.*

This decision is interesting in several respects, but particularly because of the court's analysis of the legal nature of a royalty agreement concluded in the context of Quebec mining law, and also as regards the court's ruling on the effects of its publication in the *Public Register of Real and Immovable Mining Rights*, a register maintained under the *Mining Act* (Quebec) ("**Mining Register**").

Facts

The debtors, Northern Star Mining Corp. and Jake Resources Inc., two gold exploration companies operating in Val d'Or, held mining claims and planned to begin extracting and exploiting ore for processing in their refinery. When the financing was extended by Anglo Pacific Group plc, the debtors signed a document entitled Senior Secured Convertible Debenture to which was attached a royalty agreement. At the time, the debtors did not yet hold a mining lease, in other words they did not yet have the right to extract the ore. Before entering into a mining lease, the debtors became insolvent and their assets had to be sold. At trial, the Superior Court found that, in the context of a vesting order under section 243 of the *Bankruptcy and Insolvency Act* (Canada), the purchaser acquired the property free of the royalty agreement. The Court of Appeal affirmed this judgment on this point. The court analyzed the royalty agreement under Quebec civil law, and it is this analysis in the judgment that we will be considering here.

Royalty agreement: real right or personal right

Firstly, the court had to decide whether the royalty agreement created real rights or personal rights, in order to determine whether these rights were extinguished by the bankruptcy and sale of the underlying assets, or if they benefited from a right to follow the property into the hands of the third-party purchaser.

At the outset, the court noted that the civil law is a complete system and that we must avoid adopting principles from foreign legal systems without questioning whether they are compatible with our law, a principle previously laid down by the Supreme Court of Canada in the case of *Farber v. Royal Trust Co.* This warning by the court turned out to be necessary because, in its arguments, the appellant was attempting to import common-law principles applicable to mining royalties.

Noting that a real right is a right in property, and not against a person, the court found that the terms of the royalty agreement under review did not have the effect of creating a real right in the minerals at the stage of the mining claim. It failed to do so because it did not confer a direct right in the minerals, as it did not give the claim holder the right to use them directly, or to enjoy or dispose of them. The payment of the royalties was subordinate to the sale by the debtors of the extracted or processed minerals. The court therefore found that the royalty agreement only created a personal right to collect the royalties.

From a strictly legal standpoint, this conclusion is not surprising considering the requirements in the *Civil Code of Quebec* (“**Civil Code**”) for the creation of real rights and dismemberments of the right of ownership.

The surprising element in this decision is that the court suggests, in an *obiter dictum*, that it would however be possible for a royalty agreement to create an innominate real right, that is to say a dismemberment of the right of ownership that is not expressly referred to in the Civil Code (such as usufruct, the right of use, servitude and emphyteusis). The court stated that it would be sufficient if the agreement granted a real right in the thing having one of the essential attributes of property – namely, the right of use (*usus*), the right of enjoyment (*fructus*), or the right to freely dispose of the property (*abusus*), as well as a right to follow the property in the event of a sale thereof.

Interestingly, the court justified its *obiter dictum* in the following terms:

[office translation] *At a time when mining law is promising to become a driving force of the Quebec economy, the civil law must adapt without undermining the foundations of the right of property and without obscuring the conditions for the creation of a real right behind the economic and legislative reality associated with mining law. The civil law is sufficiently flexible to permit the holder of a mining claim — a potential owner of extracted minerals — to confer a real right not only in the claim, but also in the extracted minerals in respect of which the owner will obtain a right of ownership once a mining lease is granted.*

The court’s position is particularly surprising because the debtors only held mining claims in this case. Indeed, a claim, while characterized as a real and immovable right in the *Mining Act*, is, in essence, temporary and only confers on the holder thereof an exclusive exploration right limited to certain minerals.

To reach this finding, the court drew a parallel between a hypothec on future rights, which is possible under Quebec law, and the potential right of the beneficiary of a mining claim to obtain a mining lease. This is only a potential right because the conditions for the issuance of the mining lease provided for in the *Mining Act* must first be met. It is the mining lease, once obtained, that confers on the holder the rights and obligations of an owner, including the right to extract and sell the minerals.

The court then concluded that it would theoretically be possible for a royalty agreement to grant an innominate real right directly in the minerals that are eventually extracted if the holder of the claim subsequently becomes the holder of a mining lease. This would be a kind of innominate real right granted under suspensive condition that a mining lease be obtained in the future. The court is therefore opening the door to a new type of royalty agreement. Drafting such an agreement is another matter!

Effects of the publication of a right in the Mining Register

Secondly, the appellant maintained that the publication of the royalty agreement in the Mining Register exempted it from registration in the land register to be enforceable against third parties. On

the other hand, the respondent and the impleaded party argued that the failure to register the agreement in the land register made it unenforceable against them.

After considering the applicable statutes, the court made two findings:

1. On the one hand, section 14 of the *Mining Act* (Quebec) provides that the transfer of a mining right or any instrument relating to such a right must be published in the Mining Register to be enforceable against the state;
2. On the other hand, since the *Mining Act* (Quebec) is silent with respect to enforceability against third parties, one must defer to the general regime in the Civil Code for the publication of rights, which requires registration in the land register of all immovable real rights.

Without commenting on the effect of the publication of a personal right on third parties, which would have been interesting, the court concluded that the sole effect of the publication of a right in the Mining Register is to render this right enforceable against the State, and that, to be enforceable against third parties, the royalty agreement should have been registered in the land register through registration in the Register of Real Rights of State Resource Development, since this register is an integral part of the land register.

Questions may be raised regarding the impact this judgment will have on the registration in the land register of such an innominate real right at the stage of the mining claim, and on the enforceability thereof against third parties and other creditors, given that exploration rights such as mining claims are in fact exempted by the *Mining Act* (Quebec) from registration in the land register, precisely in order to avoid the cluttering of the land register with registrations relating to mining exploration.