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Separating Surface Rights and Renewable Energy Rights: Thoughts on Legislative Amendments

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Despite considerable wind and solar development in Western Canada, certain elements of the character, scope, and exercise of renewable energy rights remains uncertain. This article contemplates a more efficient utilization of surface rights by severing the "renewable energy" estate from the "surface" estate and suggests some potential legislative amendments that would facilitate the consistent adoption of such severances.

1. Severing the Renewable Estate from the Surface Estate

Framing the issues to be discussed herein begins with the simple logic that, if a landowner owns section 1 in fee simple, which we will assume comprises from the center of the earth to the heavens, or "*cuius est solum eius est usque ad coleum et ad inferos neccesam*", it follows that they can obviously reserve out of a conveyance all mines and minerals, and the right to work the same" (the "**Mineral Estate**", eg. private transfers to homesteaders by the Canadian Pacific Railway Company and the Hudson's Bay Company, and the *Dominion Lands Act* (Canada) transfers to homesteaders by the Crown). Should it not also then follow that a present day owner of "section 1 excepting thereout all mines and minerals, and the right to work the same" should similarly be entitled to convey the "wind rights" or "solar rights" associated with their tract of land to a third party for renewable energy development (the "**Renewable Estate**", which must be distinguished from the "air rights" or "strata space", being the exclusive right to occupy, use and develop the space above land without interference from others).

Typically when a renewable energy developer (a "**Developer**") negotiates with a landowner to construct a wind turbine, or install solar panels, they enter into a "surface lease" with the owner of both the surface rights and the renewable energy rights, which grants to the Developer various rights including the right of access to the lands, the right to construct and operate the wind turbine or solar panels on the lands (together with any related associated equipment, facilities and transmission lines), as well as the right to utilize the wind or solar "resources" associated with the lands to generate electricity. As the name of the "leasehold" tenure suggests, the bundle of rights granted by the "surface lease" is limited in time, and this article intends to address potential legislative solutions to certain of the issues arising when the Renewable Estate is granted in perpetuity by way of a severing conveyance leaving "section 1 excepting thereout all wind rights and the right to develop the same, and all mines & minerals and the right to work the same" (the "**Surface Estate**").

2. Ability to Sever the Renewable Estate

With no judicial decisions or legislation in Canada to look to, a preliminary question arises as to whether a landowner is able to convey or retain the Renewable Estate separate from the Surface Estate. In the U.S. several states, including Nebraska, North Dakota, South Dakota and Colorado, have, largely on the basis of public policy concerns, passed statutes prohibiting the severance of "wind rights" or "wind interests" from the Surface Estate. By way of example, Title 38, Article 30.7 of the 2016 Colorado Revised Statutes (the "**Colorado Statute**") is entitled "Wind Energy" and provides that: "§(iii) 38-30.7-103. Wind energy agreements - recording - termination – transfer. (1) **A wind energy right is not severable from the surface estate** but, like other rights to use the surface estate, may be created, transferred, encumbered, or modified by agreement", the term "wind energy right" means the right of the owner of a surface estate, either directly or through a wind energy developer under a wind energy agreement, **to capture and employ the kinetic energy of the wind** , and the term "wind energy agreement" means a lease, license, easement, or other agreement between the owner of a surface estate and a wind energy developer to develop wind-powered energy generation.

a. Comparisons of the Renewable Estate to the Mineral Estate

Some commentators argue that comparisons of a Renewable Estate severance to a Mineral Estate severance are not necessarily legitimate and that, in the absence of statutory confirmation, the Renewable Estate may cease to be a "property right" once it is severed from the Surface Estate. The argument goes that the owner of the Surface Estate does not hold the Renewable Estate rights separate from the Surface Estate, but rather only possesses a right to use the wind that flows across the lands, or the sun that shines upon them. Is the appropriate analogy for the Renewable Estate to be found in *in situ* fluid hydrocarbons subject to the rule of capture, or are *ferae naturae* (i.e. wild animals) a better framework for analysis, as they move feely across property lines. Is a cause of action created when adjacent property owners block the wind, or create shade by building large structures? Or does the "ownership" of renewable energy only crystalize when the electricity is produced and reduced to "possession" (i.e. a profit a prendre) on the transmission line or in the storage battery?

b. Public Policy Concerns Regarding Renewable Estate Severances

Presumably severances of specific property rights within a tract of land, and in particular Mineral Estate severances, were historically justified under common law because the owner of the Surface Estate was not skilled enough, or perhaps not well capitalized enough, to exploit the Mineral Estate and thereby provide the "public benefit" to be derived from resource extraction. The traditional rationales behind encouraging Mineral Estate severances include that they result in relatively minimal damage to the Surface Estate, that they encourage development and that they are for a determinable period of time (i.e. until the non-renewable resource is eventually depleted, whereupon the use of the Surface Estate reverts to its original state). Unlike oil and gas drilling,

wind developments can tie up much of the Surface Estate with a spider web of roads, turbines, substations, and transmission lines and solar developments can literally blanket a tract of land rendering other uses, such as agriculture, impossible, and because both wind and solar are non-depletable resources, there could be perpetual sterilization of all or a portion of the Surface Estate. Additionally, severing the Renewable Estate from the Surface Estate could discourage renewable energy development as Developers and their capital providers may be hesitant to work on split-title tracts without a comprehensive agreement in place, or applicable legislation. Similarly, severing the Renewable Estate may contribute to the sterilization of significant tracts of prospective land either because the combined consideration demanded by the owner of the Surface Estate and the owner of the Renewable Estate renders the Developer's project uneconomic, or more significantly, activist NIMBY groups seeking to prevent renewable energy development altogether could acquire the Renewable Estate and refuse to permit its development. We note that in several U.S. jurisdictions "dormant estate" legislation has been put in place to address the potential sterilization of wind rights, including the Colorado Statute which provides: "§38-30.7-104. Expiration of wind rights under wind energy agreements. (1) Except as otherwise provided in a wind energy agreement or an amendment to the agreement, **all rights of a wind energy developer** to use real property for wind energy development or production under a wind energy agreement entered into on or after July 1, 2012, **expire if no wind-powered energy generation has occurred under the agreement for a continuous period of fifteen years**. The expiration of rights under this section does not modify any obligation to restore or reclaim the surface estate that is contained in the agreement or imposed by law."

c. Potential Legislative Approach

We posit firstly that the *Law of Property Act* (Alberta) (the "**Property Act**") could be amended to confirm that, similar to a Mineral Estate, the Renewable Estate can be successfully severed from the Surface Estate, and secondly that the *Land Titles Act* (Alberta) (the "**Titles Act**") could be amended to allow for a separate title to be issued in respect of the Renewable Estate similar to "all mines and minerals" titles.

3. The Renewable Estate as an Interest in Land

This section this article borrows heavily from the Ontario Court of Appeal decision in *Third Eye Capital Corporation* v. *Dianor Resources Inc*. ("**Dianor**").

The central issue in Dianor was whether a gross overriding royalty ("**GOR**") on certain mining claims constituted "interests in land" within the meaning of the law outlined by the Supreme Court of Canada in *Bank of Montreal* v. *Dynex Petroleum Ltd.* ("**Dynex**", which changed the common law in Canada to permit a GOR to achieve status as an "interest in land").

a. Interests in Land Pre-Dynex

At common law, rights in relation to land are divided into corporeal and incorporeal hereditaments, where a corporeal hereditament is an interest in land that is capable of being held in possession,

such as fee simple, and an incorporeal hereditament is an interest in land that is non-possessory such as easements, profits à prendre, and rent charges. Mineral extraction rights derived from the owner of the Mineral Estate are generally treated by the common law as profits à prendre, namely, "a real property interest entitling the holder to acquire some natural resource on land belonging to another", and to constitute a profit à prendre, a party must be granted the right to enter the lands of another and to exploit a natural resource. A working interest in the "Mineral Estate" is an interest in land granted by the fee owner to a mineral extractor to enter the owner's land and extract minerals or resources from the property. Prior to Dynex, at common law if a party did not have the right to enter and to extract a resource from the land, then it did not have a profit à prendre and did not have an interest in land, regardless of the parties' intentions. As such, an interest in land could not issue from an incorporeal hereditament, and accordingly the right to a payment or to profits was not itself a profit à prendre, and a royalty right contractually carved out of a working interest could not confer an interest in land.

Pre-Dynex an interest in land could not be granted out of an incorporeal hereditament, and accordingly the common law posed commercial challenges to holders of working interests who needed to secure financing sources to allow for the exploitation of the Mineral Estate. Resource extraction is a risky enterprise, requiring huge amounts of risk capital, and only a small fraction of which are successful. Various financing methods, including GORs, were used in the industry to provide incentives to key participants such as geological surveyors or drilling companies, or to vendors selling the mining claims or oil & gas leases. In granting a GOR, the working interest holder grants rights out of the lessee's working interest, without the calculation of the GOR being tied to the profitability of the mine. Third parties who obtain GOR rights do not own the working interest or profit à prendre and have no independent ownership interest in the land.

b. Interests in Land Post-Dynex

As the Court of Appeal of Alberta noted in Dynex, it became industry practice to draft contracts with the intention of granting GOR holders an interest in land because it was commercially and practically expedient to do so. Key participants often prefer an interest in land rather than a contractual right against the lessee because this allows "investments in a particular piece of property, not in a particular operator or company. ... The investment return on a royalty results from the success of the property regardless of who owns or is working the property". It follows then that interests in land can provide appropriate incentives to key participants, mitigate financial risks, and provide better financing terms; ultimately providing key participants with exposure to a potentially significant upside if the venture is successful.

Granting such an interest as a form of compensation reduces the amount of initial capital necessary to fund a new venture which allows the working interest holder to reduce its own exposure to loss and thereby spreads risk among key participants. Lenders to these key participants are able to secure real property interests and are better protected in the event of an insolvency, leading to better financing terms for borrowers. Consequently, for practical and commercial reasons, even before Dynex, parties often drafted GOR agreements with the intention of granting the holder an

interest in land rather than a contractual right against the lessee. In Dynex, the Supreme Court quite deliberately changed the common law in response to these commercial realities, in order to permit a GOR interest to become an interest in land, consistent with the industry practice.

As per the Supreme Court of Canada in Dynex, it is quite reasonable to assume that Canadian common law would in due course recognize that a "renewable energy interest" can be an interest in land if “the language used in describing the interest is sufficiently precise to show that the parties intended the [estate] to be a grant of an interest in land, rather than a contractual right to a portion of the [natural resources to be] recovered from the land”, and “the interest, out of which the [estate] is carved, is itself an interest in land.” In Dynex the Supreme Court knew that its ruling was changing the common law and cited the need “to keep the common law in step with the evolution of society, to clarify a legal principle, or to resolve an inconsistency.”

c. Potential Legislative Approach

The Property Act could be amended to confirm that a severed Renewable Estate, and consequently any royalties carved out of the Renewable Estate, is an “interest in land”. For context, Section 63(1) of the Property Act currently provides that: “The following are equitable interests in land: (a) a right of first refusal to acquire an interest in land; (b) an assignment of rents payable pursuant to a lease of land.” By way of example, the Colorado Statute provides that “§38-30.7-101. Legislative declaration. The general assembly finds and declares that **a wind energy right is an interest in real property appurtenant to the surface estate**”.

4. Crown Ownership of the Renewable Estate

If we are able to conclude that the Renewable Estate is a property right that at law can be severed and owned separately from the Surface Estate, in the context of the approach of the Alberta Crown with respect to gold and silver, ground water and pore spaces, and in the context of the approach of the British Columbia Crown with respect to geothermal resources, the question arises as to whether the public is best served by having the Renewable Estate overlying private Surface Estates owned by the respective Provincial Crowns.

a. Examples of Crown Assumption of Ownership of Strategic Resources

By way of reminder, we offer that (i) section 10 of the *Mines and Minerals Act* (Alberta) (the “**Minerals Act**”) provides that “It is hereby declared that **no grant from the Crown, whether relating to land, minerals in land or otherwise, has operated or will operate as a conveyance of gold and silver** unless gold and silver are expressly named and conveyed in the grant.”, (ii) section 3(2) of the *Water Act* (Alberta) provides that “The property in and the right to **the diversion and use of all water in the Province is vested in Her Majesty in right of Alberta** except as provided for in the regulations.”, (iii) section 15.1 of the Minerals Act provides that “It is hereby declared that (a) **no grant from the Crown** of any land in Alberta, or mines or minerals in any land in Alberta, has operated or **will operate as a conveyance of the title to the pore space** contained in, occupied by or formerly occupied by minerals or water below the surface of that land, (b) **the**

pore space below the surface of all land in Alberta is vested in and is the property of the Crown in right of Alberta …"; and (iv) section 2 of the *Geothermal Resources Act* (British Columbia) provides that "The right, title and interest in all geothermal resources in British Columbia are vested in and reserved to the government and the government may dispose of them only under this Act.".

In the context of facilitating development and having the necessary regulatory tools to incent industry to meet carbon emissions targets, strong arguments can be made for Provincial legislation vesting ownership of the Renewable Estate overlying private Surface Estates in the Crown. In short, renewable energy and the ability to generate electricity for the benefit of all, is arguably critical to our collective interests and therefore it may be determined to be in the Crown's best interests to encourage the maximum use of these natural resources rather than enable their control by a select few. The contrary position, obviously, is the blatant interference with private property rights, however, recent legislative activity confirms that Provincial governments in Western Canada are not particularly concerned with the sanctity of private ownership.

b. Potential Legislative Approach

The *Public Lands Act* (Alberta) (the "**Public Act**") could be amended to retroactively vest the Renewable Estate overlying private lands in the Provincial Crown.

5. Split Rights Issues

This section of this article borrows heavily from *The Severance of Wind Rights in Texas* by Lisa Chavarria and *Inheriting the Wind: A Brief Guide to Resolving Split Estate Issues When Developing Renewable Projects* by Will Russ.

Notwithstanding that the Renewable Estate severing conveyance would, at a minimum, include all of the elements of a typical negotiated "surface lease", as well as thoughtful modifications to reflect the fact that the transfer of the Renewable Estate is of a perpetual nature, a number of issues arise out of the "split estate" created by having the Surface Estate and the Renewable Estate owned by separate persons (in addition to the Mineral Estate).

a. Dominant and Servient Estates

Key to managing the relationship between the Surface Estate and the Renewable Estate is the determination of which estate is the dominant estate, and which is the servient estate. The Mineral Estate is, of course, dominant to the Surface Estate and as such at common law the owner of the Mineral Estate held certain implied rights to access the Mineral Estate and construct the infrastructure necessary to extract the minerals. If the Renewable Estate is severed from the Surface Estate a parallel priority needs to be established, which will ultimately govern in the case of a resource use or recovery conflict. As between the Mineral Estate and the combined Surface Estate and Renewable Estate, the Mineral Estate would presumably remain dominant and should proceed unhindered; however, the compensation awarded as a consequence of operations in

respect of the Mineral Estate must be fairly allocated if both the agricultural operations of the Surface Estate owner, and the energy generation operations of the Renewable Estate owner are negatively impacted.

b. Right of Entry Orders

Early Mineral Estate severances included mechanisms for landowner compensation, however they have since been superseded by the *Surface Rights Act* (Alberta) (the "**Surface Act**"), presumably because those negotiated compensation mechanisms were viewed as unfair. In this regard we note that Section 12(2) of the Surface act provides that "Notwithstanding anything contained in a grant, conveyance, lease, licence or other instrument, whether made before or after the commencement of this Act, and pertaining to the acquisition of an interest in a mineral, an operator does not obtain the right of entry in respect of the surface of any land unless the grant, conveyance, lease, licence or other instrument provides a specific separate sum in consideration for the right of entry of the surface required for the operator's operations, but this subsection does not apply in a case where the operator, prior to July 1, 1952, has for any of the purposes referred to in subsection (1) exercised the right of entry in respect of the surface of land in accordance with the provisions of a grant, conveyance, lease, licence or other instrument." A comprehensive compensation and dispute resolution mechanism as between the Surface Estate and the Renewable Estate should be included in any Renewable Estate severing conveyance, however ultimately only an amendment to the Surface Act would provide the necessary comfort and certainty.

c. Allocation of Compensation Paid by the Developer

Once the Surface Estate and the Renewable Estate are severed, a Developer will be required to enter into agreements with each of the holders thereof, or ideally enter into a single arrangement with both of the holders. Any compilation of all of the heads of compensation payable by a Developer to the Surface Estate owner and the Renewable Estate owner is necessarily incomplete; however, the following is an attempt to allocate such compensation to be paid by the Developer equitably between those two parties.

Amounts to which the holder of the Renewable Estate should be entitled include (i) any royalty payment based on the sale of the electricity generated by the wind turbines or solar panels located on the property and the associated renewable energy credits, (ii) any minimum payment made only to the extent it exceeds the royalty payments during the applicable period, (iii) any annual delay payments made if no turbines or panels are placed on the property, (iv) any option period payments made during an assessment, and (v) any payments for the installation of a measurement or meteorological tower or instruments (including potential ownership of the data if the project does not proceed).

Amounts to which the holder of the Surface Estate should be entitled include (i) surface disturbance fees, including compensation for the installation of wind turbines or solar panels on the property, payments for the installation of above ground transmission lines and roads, payments for the

placement of a substation or operations and maintenance building, and payments for the use of an area for the temporary storage of large equipment or for equipment assembly, (ii) compensation for replacement or repair of damaged fences, cattle guards or other improvements on the property caused by the Developer's activities, (iii) compensation for the loss of livestock directly attributable to the Developer's activities, (iv) reimbursement for losses sustained as a result of a disruption to hunting, grazing or farming during project construction, and (v) compensation for use of sand and gravel.

In addition, there are several items which, while not necessarily taking the form of monetary payments, are assurances and/or mechanisms burdening the Developer which should accrue solely to the benefit of the owner of the Surface Estate, including (i) subject to takeover rights by the holder of the Renewable Estate, upon termination of the project, all equipment installed by the Developer should be removed and the surface restored to its original condition, with a bond or other form of security is potentially posted to ensure the Developer's performance of its removal obligations, (ii) a Developer may review the proposed site layout for the project with a landowner and may re-locate certain equipment based on landowner input, and (iii) the Surface Estate holder and the Developer may provide mutual notices prior to engaging in certain types of activities.

d. Managing the Relationship with the Mineral Estate Holder

Assuming that the Mineral Estate is dominant over the Renewable Estate, or at least will be treated on an equal footing with the Renewable Estate, either negotiated or legislated multiple use and/or accommodation provisions that contemplate and mediate any conflicts between future uses of the Mineral Estate and the Renewable Estate are necessary. The principal purpose of such accommodation agreements is to prohibit the holder of the Mineral Estate from producing minerals in a manner that would interfere with the Renewable Estate, and the holder of the Renewable Estate from constructing renewable infrastructure that interferes with the extractive activities of the Mineral Estate holder.

Surface use agreements may be used to delineate the rights of each direct and derivative estate owner, whether Mineral Estate, Surface Estate or Renewable Estate, to use the surface of the land to extract value from their interest, while preserving the rights of the other interest owners to do the same. By way of example, an agreement by the Mineral Estate holder to abstain from mineral production on all or a portion of the surface, including the turbine or panel sites plus some reasonable buffer area around it, may be obtainable, as well as a surface rights "waiver" that includes language limiting any related activities, such as seismic testing, that might interfere with the Developer's activities. A related, but more targeted, form of contract is a drill site designation agreement, which, with the recent growth in new drilling techniques and technologies, many Mineral Estate holders may be willing entertain, whereby they designate one or more areas to which they will limit their mineral production activities. For obvious reasons, designation agreements are generally favored by Surface Estate owners and disfavored by Mineral Estate owners; however, they can be a very effective tool for giving all interested parties certainty that each will be able to use the lands in a manner that maximizes the value of its investment.

Although wind farms, in particular, are constructed over very large tracts of land, the actual amount of the surface required by the Developer is relatively small, since each wind turbine has a limited footprint relative to the overall project area. Once the wind farm has been constructed and put into operation, the remainder of the land can continue being used for other purposes; however, continuing non-interference covenants regarding the construction of large buildings the block the wind or the sun must be addressed.

e. Potential Legislative Approach

The Property Act and/or Land Act could be amended to confirm that the Renewable Estate is dominant over the Surface Estate, and the Surface Act could be amended to provide for right of entry orders, compensation mechanisms and concurrent development issues.