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# Trust Agreements and Trust Declarations

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# Overview

- trust agreements and trust declarations are some of the most common business tools being used in the Canadian oil and gas industry
- many people drafting, executing, and administering these tools are not aware of their importance or the best practices for their use in land administration and A&D



## Background Fun

- trust law developed in England during the Crusades
- when knights went charging off to the Middle East they had to leave a friend in charge of their lands in order to pay and collect feudal dues



## Background Fun (cont'd)

- before the development of trust law, the only way this could be done was for the crusading knight to convey land ownership to a friend on the understanding that it would be conveyed back when the knight returned
- often the friend was rather surprised that the knight didn't die on the journey or the battlefield and actually came home



## Background Fun (cont'd)

- many trusted friends were not pleased by this turn of events and refused to give the land back
- the knight had no recourse except to appeal to the king
- the king would set things right if he felt like it, but sometimes he was just as happy to let the knight rust in the rain alone and landless



## Background Fun (cont'd)

- this kind of case was became so frequent that the king didn't have time for it anymore
- delegated the job to the Lord Chancellor by empowering him to do what was just and equitable on a case-by-case basis
- it became common for the Lord Chancellor to recognize the claims of all returning crusaders



## Background Fun (cont'd)

- the concept developed that the legal owner – the friend – would hold the land for the benefit of the original owner – the crusading knight – and would be compelled to convey it back when requested
- the crusading knight was the *beneficiary* and the friend was the *trustee*
- the term *use of land* was coined and in time developed into what we now know as a *trust*



# Trust Components

- from this history we can see that land interests are made up of two separate components:
  1. the *legal* interest (often a registered interest); and
  2. the *beneficial*, or equitable, interest

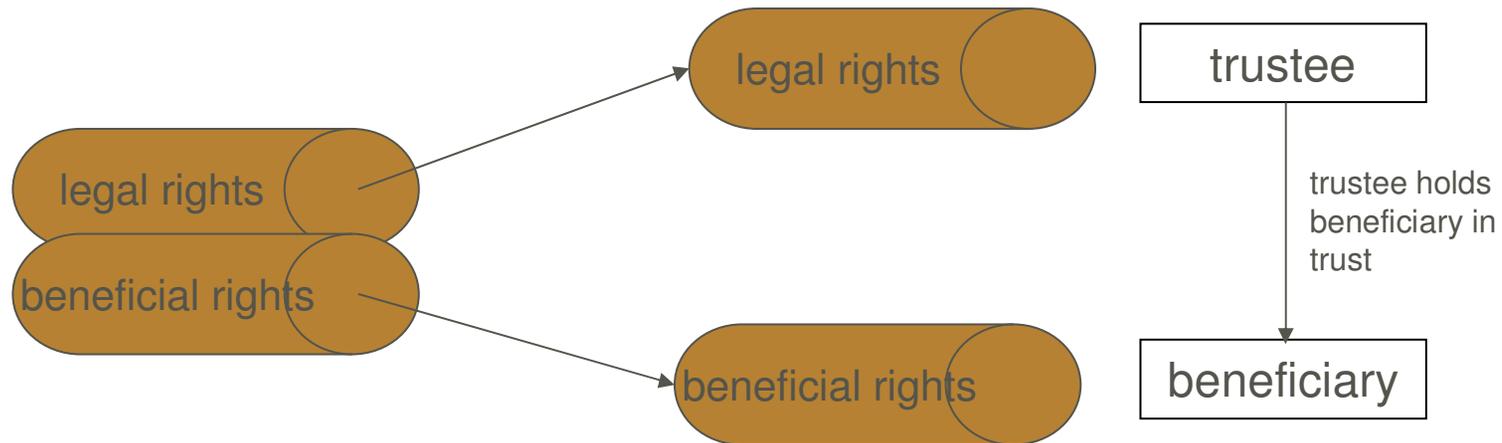


## Trust Components (cont'd)

- when the legal owner is using and occupying the land, or benefiting from it, these two interests are bundled together
  - but, they can be taken apart and held separately
- when separation of interest occurs, a trust exists
  - eg. when a land agent holds the legal, or registered, interest in a mineral lease and the land agent's principal holds the beneficial interest



# Trust Components (cont'd)





# Trust Law

- general legal principles:
  - the trustee owes a fiduciary duty to the beneficiaries of the very highest order
  - a court will view a breach of trust as a grievous contractual breach and the trustee usually faces significant liability



## Implied Trusts

- the existence of an underlying trust might not be documented separately
  - it can come into existence through the conduct of the parties
  - eg. pre-earning farmouts when one company (farmor) is holding the beneficial right to access and drill on lands in trust for another company (farmee)
- these are known as *implied trusts*



## Express Trusts

- express documentation of a trust relationship
  - expressly confirms the nature of a trust in its own separate agreement
- sets out how the holder of the legal interest – the trustee(s) – will manage the legal interest on behalf of the holder(s) of the beneficial interest – the beneficiary(ies)
  - these are known as *express trusts*
  - most common form is a *trust agreement*



## Trust Declaration

- a.k.a. Declaration of Trust or “Trust Dec”
- signed unilaterally by the trustee
- acknowledges that land interests are being held on behalf of a beneficiary(ies), but is not signed by the beneficiary(ies)
  - quick rule-of-thumb, no matter what the title on the document – whether it’s called a trust agreement, trust declaration, or declaration of trust – if it’s only signed by one party, then it’s a trust declaration



## Trust Declaration (cont'd)

- often executed just to have it on related mineral files as a physical flag warning administrators that a trust exists
- big difference between a trust declaration and a trust agreement is that the trust declaration is *not assignable*
- when conveying land that is subject to a trust declaration, the assignee who will become the new trustee needs to
  - execute its own declaration, or
  - consider entering into a trust agreement with the beneficiary
- A&D assisted if these documents are identified in the land system
- if trust declarations are overlooked, a divesting trustee may either
  - fail to transfer its trust obligation, or
  - inadvertently sell the beneficial interest it doesn't own to a 3<sup>rd</sup> party and later need to amend and adjust the deal



## Legal Risks

- trustees must ensure that land records accurately document any beneficial interests to minimize and mitigate potential legal liability
- especially important where a governing contract includes a ROFR with implied trust for silent partner
- legal consequences of not documenting the beneficial interest
  - eg. a beneficiary having to defend itself before the ERCB and/or the courts to prove its ownership or entitlement to the underlying beneficial interests
  - beneficiary would have a cause of action in damages against the trustee



## Legal Risks (cont'd)

- eg. a company acquires a trust interest in lands that are subject to royalty payments
- not aware of its royalty obligations to the trust beneficiaries and overlooks paying the royalty
- *James H. Meek, Jr. Trust v. San Juan Resources Inc.*, 2005 ABCA 448



# Best Practice Tip #1

- **use trust agreements**
- avoid implied trusts
- document all trust agreements/declarations with separate:
  - physical file
  - file number
  - linked record in the land system
- makes the trust agreement/declaration trackable and reportable
- ensures that beneficial interests are properly reflected in the various equity splits/subs in a land system
- ensures that trust interests are scheduled, administered, and conveyed properly during A&D processes
  - trust agreements that are buried on mineral files are often overlooked



## Best Practice Tip #2

- **ensure trust agreements are assignable**
- application of the 1993 CAPL Assignment Procedure to trust agreements follows the same rules as for any other kind of contract
  - unfortunately, the terms of many trust agreements don't include the 1993 CAPL Assignment Procedure
  - possibly because precedents haven't been updated
- companies that want to minimize administrative costs are careful to draft trust agreements so they do include the 1993 CAPL Assignment Procedure
  - if all parties agree, amend existing trust agreements to include the 1993 CAPL Assignment Procedure



## Best Practice Tip #3

- **set-up active trusts**
  - whenever a trust agreement is found on a mineral file an administrator can add value by analyzing it to decide whether or not the trust is active
  - active trust agreements should be pulled from the mineral file and set it up in the land system as a separate contract that is related to the mineral interests
    - this really speeds up the A&D conveyancing process because the trust is no longer a hidden agreement and the trust interest more likely to be reflected correctly on the P&S land schedule
- inactive trusts
  - don't have the same set-up urgency
  - may still be helpful for them to be trackable in the land system when some land/legal research or accounting query needs to find it



Thank you.

