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About Freehold Mineral Rights

In most modern industrialized democracies, petroleum and natural gas were recognized as strategic commodities and nationalized before any significant deposits which might have presented political barriers to nationalization had been discovered within the jurisdiction. As a result, there is no private ownership of subsurface oil and gas in most countries.

Rock oil was first discovered in the United States in 1859 in a well drilled to a depth of 69 feet near Titusville, Pennsylvania. What followed has been likened to a gold rush. Farms, which had been virtually worthless before the discovery, sold for \$1.3 million in 1865 and \$2.0 million several months

later¹. In the 1860's, rock oil was used primarily as a substitute for whale oil and coal oil in lamps. During the latter half of the 19th century, the refining and marketing of this illuminating oil provided the foundation for most of today's major oil companies, but the strategic value of oil only became apparent in the 20th century as war loomed in Europe and it became obvious that the internal combustion engine could propel battle ships more efficiently than coal-fired steam engines.

Perhaps because the Pennsylvania oil boom or similar oil booms in Texas and Oklahoma in the early 1900's had established subsurface hydrocarbons as a landowner's potential 'nirvana' before the strategic value of subsurface hydrocarbons was recognized, or perhaps because of the protection for property rights afforded to the citizens of the United States by their constitution, the United States federal government has never attempted to nationalize subsurface petroleum or natural gas. As a result, title to the vast majority of subsurface hydrocarbons within the original 48 states of the American Union is held by the owner of the surface rights.

In Canada, a more complex ownership regime developed.

In 1670, the King of England granted approximately 1 billion acres of land in the drainage basin of Hudson's Bay to the Governor and Company of Adventurers of England Trading into Hudson's Bay. This land grant, which comprised roughly half of what is now Canada, included everything from the surface to the centre of the earth except for "gold, silver, gems and precious stones to be found or discovered"². The Gentlemen Adventurers principal trading rival was the Northwest Company whose sphere of influence included southern British Columbia, Washington and Oregon. In 1821, the Gentlemen Adventurers combined with Northwest Company to become the Hudson's Bay Company (the "HBC"). Following Canadian confederation in 1867, a major priority of the Dominion Government was to thwart potential United States expansion across the 49th parallel. Sir John A. MacDonald, Canada's first prime minister, was particularly concerned with the possibility that British Columbia, which was then a British Crown colony, would fall into American hands. British Columbia was prepared to join the Canadian confederation, but only if a railway was built linking the Pacific coast to the existing rail system in Ontario and Quebec.

MacDonald recognized that such a railway could only be economically viable if the vast expanse of prairie lands controlled by the HBC was colonized. Although the 1670 land grant required the Gentlemen Adventurers to colonize the land, very little colonization had occurred because colonization conflicted with the groups' primary objective which was to profit from trading furs with natives. In 1869, the Dominion Government entered into an agreement with the HBC whereby the 1670 land grant was surrendered in return for 300,000 pounds sterling and 1/20th of the arable land in western Canada (approximately 4.5 million acres of land). In 1870, the North-West Territories, which then included Alberta and Saskatchewan, were admitted to the Canadian confederacy, and the Dominion Government negotiated the terms of British Columbia's entry. Under the agreement with British Columbia, the Dominion Government committed to starting the construction of a transcontinental railway within 2 years, and completing it within 10 years³.

To encourage settlement of the North-West Territories, the Dominion Government granted, or sold for token consideration, farm-sized parcels of land (generally 160 acres) to individuals prepared to establish prairie homesteads. Concurrently, the Dominion Government attempted to follow the American example of having transcontinental rail lines built by providing land grants to private corporations. Prime Minister MacDonald's initial attempt to involve private capital ended in disgrace in 1873 when he was forced to resign after it was discovered that he and his government had taken substantial bribes from Sir Hugh Allen, the first president of the Canadian Pacific Railway Company⁴. Succeeding governments spent more than \$31 million of taxpayers' money and built some of the more difficult portions of the rail line⁵, but when Sir John A. MacDonald was returned to power in 1878, much of the line remained uncompleted. Macdonald encouraged the formation of a new group of financiers and, in 1880, his government entered into a contract (the "Canadian Pacific

Railway Company Charter”) with a syndicate organized by George Stephen, then reputedly the richest man in Montreal⁶. In addition to giving the Canadian Pacific Railway Company (the “CPR”) those portions of the rail line which had already been built by the Canadian taxpayer, Section 9 of the CPR Charter provided:

“... the Government agree to grant to the Company a subsidy in money of \$25,000,000 and in land of 25,000,000 acres, for which subsidies the construction of the Canadian Pacific Railway shall be completed and the same shall be equipped, maintained and operated, ...”.⁷

The Dominion Government was presumably aware of the potential value of subsurface hydrocarbons because the first successful oil well in North America had been completed near Oil Springs, Ontario in 1858, and, by 1863, nearly 100 oil wells and about 30 primitive refineries were operating in the area⁸. Nevertheless, it was not until 1887 that the Dominion Government began to reserve petroleum and natural gas for its own account in land sales and grants. As a result, settlers who acquired homestead land from the Dominion Government prior to 1887 acquired title to both the surface and to subsurface hydrocarbons, including coal, petroleum and natural gas. So too, the lands acquired by the HBC from the Dominion Government in 1869 and the 25,000,000 acre land grant provided to the CPR included title to subsurface hydrocarbons.

Fortunately for western Canadian settlers, the CPR and the HBC were even more myopic than the Dominion Government. Almost a quarter of a century passed before the railway company began, in approximately 1902, to reserve coal for its own account in land sales to settlers. Another four years passed before, in approximately 1906, it began to reserve coal and petroleum. It was not until approximately 1912 that the CPR began to reserve all mines and minerals for its own account in land sales to settlers. The HBC began to reserve all mines and minerals for its own account in approximately 1908⁹.

As a result of the foregoing, Canadian settlers who purchased homestead lands from the Dominion Government prior to 1887, from the HBC prior to 1908, or from the CPR prior to 1902, acquired title to all mines and minerals within, upon or under their lands. The term ‘all mines and minerals’ is somewhat misleading as gold, silver and other precious minerals were reserved to the Crown and did not form part of the settlers’ title. However ‘all mines and minerals’ does include all subsurface hydrocarbons - coal, the natural gas in coal or coal bed methane (“CBM”), petroleum, the natural gas in petroleum, and natural gas itself.

As a further result of the CPR’s myopia, the titles to subsurface hydrocarbons became split beneath homestead lands purchased from the railway company by settlers during the 1902 - 1912 period. In the period from 1902 - 1905, settlers purchasing CPR lands acquired the surface and all subsurface mines and minerals except coal. Those settlers purchasing during the 1906 - 1912 period acquired title to the surface and all mines and minerals except coal and petroleum (in some instances the railway company also reserved valuable stone). On these ‘split title’ lands, the railway company retained either the right to any coal or to any coal and petroleum found to exist within, upon or under the settlers’ lands. The last step in the creation of the peculiar hydrocarbon ownership regime which exists in western Canada occurred in 1930, when the Dominion Government transferred its residual rights in petroleum and natural gas to the prairie provinces¹⁰.

Settlement of the prairie provinces generally progressed from east to west. The timing of this settlement controls both the degree of private ownership of subsurface petroleum and natural gas within the province and whether this private ownership now lies in the hands of the freeholders who purchased or inherited farm land from the original settlers, or the corporate successors to the HBC and the CPR.

The fertile southwest corner of Manitoba was one of the first areas settled in the prairies. Considerable settlement had occurred before the Dominion Government decided to retain petroleum

and natural gas for its own account in 1887, and settlement was largely completed before the HBC and the CPR began to retain petroleum and natural gas for their own accounts¹¹. Consequently, an estimated 80% of the subsurface hydrocarbons in southwest Manitoba (the only area of the Province with known subsurface hydrocarbon reserves) are privately-owned, the vast majority by individual freehold owners¹².

There had been no substantial settlement in the portion of the North-West Territories now known as Alberta prior to 1887. As a result, the vast majority of settlers who acquired homestead lands from the Dominion Government in what was to become Alberta acquired only the surface rights, and the majority of the individually-owned freehold mineral rights in Alberta were acquired from the CPR prior to 1912 or from the HBC prior to 1908.

The CPR Charter provided for the railway company to select lands “in alternate sections of 640 acres each, extending back 24 miles deep, on each side of the railway”¹³. But the Charter also permitted the CPR to select lands in other areas south of the 57th parallel if lands “fairly fit for settlement” could not be located along the main line right of way¹⁴, and for the lands selected to be free from taxation for 20 years¹⁵. To maximize this tax advantage and enhance the value of its land grant, the CPR delayed selection of portions of its grant¹⁶. Although the transcontinental railway was completed in 1885, it was not until 1903 that the CPR made its final selection of lands - an approximately 3,000,000 acre block of land east of Calgary to be developed as an irrigation project¹⁷. Due to this delayed selection, a disproportionate amount of the CPR’s land grant was selected in Alberta.

Overall, the CPR retained 9.6 million acres of petroleum and natural gas rights from its 25 million acre land grant (8.3 million acres in Alberta, 1 million acres in Saskatchewan and 0.3 million acres in Manitoba)¹⁸. In 1971, the CPR transferred its petroleum and natural gas rights to PanCanadian Petroleum Limited (“PanCanadian”), an 87%-owned subsidiary. In a 1996 publication PanCanadian stated “the key to Canadian Pacific’s fortunes” does not lie in what was obvious in 1880 because: “To a very large extent, the railway’s payback is flowing from rich resources below the land’s surface.”¹⁹

In 2002, PanCanadian merged with the Alberta Energy Company Ltd. to become EnCana Corporation (“EnCana”).

Within Alberta, the petroleum and natural gas beneath approximately 81% of the Province’s surface area (133 million of the total 163 million acres) is now owned by the ‘Crown in right of Alberta’, and the petroleum and natural gas beneath approximately 16 million acres is privately-owned²⁰. EnCana owns the majority of this, but individuals who are the assigns or descendants of Alberta's original homesteaders are the registered owners of the petroleum and/or natural gas beneath approximately 6.0 million acres (4% of the Province’s surface area).

The petroleum and natural gas ownership regime which exists in Alberta is unique in three important respects.

In no other major oil and gas producing jurisdiction does a single corporate entity control such a significant portion of the petroleum and natural gas rights - EnCana owns the oil and gas beneath approximately 12% of southern Alberta (south of Township 60). Due to the wide aerial distribution of EnCana's rights and due to the nature of oil and gas industry operations, it is virtually impossible for an energy company of any significant size to operate in southern Alberta without dealing with EnCana.

In no other major producing jurisdiction do individually-owned petroleum and natural gas rights comprise such a small proportion of the total rights within that jurisdiction. In other major oil and gas producing jurisdictions, either the government owns all petroleum and natural gas and there is no

freehold, or, as in the lower 48 states of the United States, the vast majority of petroleum and natural gas interests are owned by individual freehold owners. In these other jurisdictions there is either no freehold ownership 'problem' as there is no freehold, or freehold ownership is so widespread that legislators, regulators, and the courts have been forced to address the concerns of freehold owners.

In no other jurisdiction do 'split title' mineral rights exist as a separate class. The CPR's belated recognition of the value of the subsurface hydrocarbons included in its railway land grant, gave rise to two types of split title land. The first comprises approximately 1.0 million acres of land in southern Alberta in which EnCana holds title to coal and petroleum and title to all mines and all other minerals (including natural gas) is held individual freeholders who are the descendants or assigns of settlers who purchased CPR lands in the 1906 - 1912 period. There are currently an estimated 10,000 individual owners of Alberta split title natural gas. The second comprises an additional approximately 1.5 million acres of land in which the successor corporations to the CPR hold title to coal and title to all mines and all other minerals (including petroleum and natural gas) is held individual freeholders who are the descendants or assigns of settlers who purchased CPR lands in the 1902 - 1906 period.

The unique hydrocarbon ownership regime which exists in Alberta results in certain oil company-lessee/freehold owner-lessor conflict of interest situations which are not found in other jurisdictions (see "[The Split Title Issues](#)").

End Notes:

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4. *Ibid*, p. 20, 30, 34 -35
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11. *History of the Canadian Pacific Railway*, W. Kaye Lamb, 1977, MacMillan Publishing Co., Inc., New York, N.Y., p. 252
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14. *Ibid*
15. *Ibid*, S. 16, p. 306
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17. *Land Settlement Policies in the Prairie West*, in *The CPR West: The Iron Road and the Making of a Nation*, Hugh A. Dempsey, Douglas & McIntyre, Vancouver/Toronto, 1984, p. 184
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20. Province of Alberta Natural Gas Commission Report, R. J. Dinning Commissioner, March, 1949



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