



2010 ALBERTA CHAMBERS OF COMMERCE RESOLUTION Improving the Competitiveness of Alberta's Oil & Gas Industry

In 2009, the Government of Alberta commenced an Alberta Natural Gas and Conventional Oil Investment Competitiveness Study to ensure the province has the appropriate regulatory and fiscal environment to remain attractive for investment.

Energizing Investment – A Framework to Improve Alberta's Natural Gas and Conventional Oil Competitiveness was released in March 2010. Based on the findings of the study, it will modify conventional oil and natural gas royalty rates; promote innovation; and improve regulatory efficiency. The framework recognizes that new drilling techniques have unlocked large new reserves in other areas of North America, with Alberta under competitive pressure to attract investment.

I. Industry's Contribution to Alberta's Prosperity

Alberta's energy industry creates jobs and prosperity for the whole business community, from the driller to the dry cleaner. It influences the success of every industry and every Albertan. The oil and gas industry and associated economic activity account for 50 per cent of the provincial economy.¹ Its health and growth are of utmost importance to Alberta's future.

Maximizing Alberta's energy resource potential requires a strong partnership between government, industry and Albertans. At the heart of the Competitiveness Review is the opportunity to articulate a long-term vision of energy development in the province and create a forward-focused, stable, fiscal and regulatory regime that is globally competitive and responsive to technological change. The key outcome is to attract investment, create jobs and ensure economic prosperity for all Albertans.

The Alberta Chambers of Commerce was looking for action in five key areas:

- Communicate the Vision and Benefits of Energy Development
- Predictability and Stability
- Fiscal and Regulatory Competitiveness
- Fostering Technological Innovation
- Constructive Ongoing Dialogue

Release of *Energizing Investment* took positive steps in a number of these areas, and with further revisions to the royalty curves expected by May 31, the initiative will help restore investor confidence and attract new investment.

¹ Canadian Association of Petroleum Producers. (2010). News release – Alberta Competitiveness Review Released. March 11, 2010.



II. Communicate the Vision and Benefits

The Competitiveness Review is an opportunity to analyze and discuss with Albertans the positive contributions the energy industry makes to local communities, standard of living and overall prosperity. Important facts include:

- One in six Albertans are directly or indirectly employed in the industry.
- Each dollar invested in the provincial oil and gas industry produces three dollars of value.
- Over the next 25 years, energy development in Alberta could produce \$2.5 trillion in new economic activity.
- Between 1999 and 2008, non-renewable resource revenues have, on average, contributed 32 per cent of total government revenues.

Many of these contributions were noted in the *Energizing Investment* document. The Alberta Chambers of Commerce was pleased with the government's vision to position Alberta as one of the most competitive North American destinations for energy investment, along with its commitment to communicate this vision to Albertans. It is critical that government communicate this vision to Albertans, Canadians and international audiences to raise awareness of Alberta's competitive position globally.

III. Predictability and Stability

The Alberta Chambers of Commerce submits that there are three important considerations in an investment decision:

- Certainty - assumption that the underlying terms of investment will not be arbitrarily changed.
- Rate of return for the risk taken - must be reasonable with sufficient upside potential, and attractive relative to competition.
- Constructive dialogue - willingness to dialogue with industry on key policy decisions reduces uncertainty and allows companies to provide valuable information on impacts and unintended consequences. Dialogue also enables stakeholders to work together and develop solutions to unanticipated changes affecting certainty and rate of return.

A number of positive steps were taken in the *Energizing Investment* Framework to address these issues. The Chamber was heartened by the provincial government's clear intent to create greater stability and predictability in the fiscal and regulatory framework. The government is encouraged to provide sufficient time and collaborate with industry before another major review to provide stability for companies in making long-term investment decisions. Reduction of short-term, temporary measures will simplify the royalty regime and provide additional stability.

Regarding the rate of return for risk taken, changes to front-end and maximum royalty rates will have an immediate impact, allowing investors to recoup upfront investment, reinvest quicker, and provide a more competitive risk-reward balance. This is likely to increase activity, leading to greater economic benefits for all Albertans.



The Competitiveness Review process has improved discussion and understanding between the industry and government. Consultation with industry to finalize the new royalty curves by May 31 2010 and improve regulatory efficiency will be another opportunity for constructive dialogue and to improve competitiveness. Commitment to involve industry in any further revisions will go a long way to restoring investor confidence.

IV. Fiscal and Regulatory Competitiveness

Alberta's natural gas industry faces stiff competition from new supplies (e.g. shale gas) in the United States with the strong possibility of declining market share. The U.S. Energy Information Agency predicts that U.S net imports of natural gas will decline from 16 percent of supply in 2007 to 3 percent in 2030.²

Reduced market demand, distance to markets and higher production costs create a challenging environment in which to operate. In addition, maturing conventional oil and gas resources have become more difficult and expensive to tap. Therefore competitive fiscal and regulatory policies are critical to attract investment in the industry, realizing Alberta's energy development potential.

The Competitiveness Review compared Alberta's investment competitiveness to major competing jurisdictions of British Columbia, Saskatchewan and ten U.S. states. The report acknowledges that while total natural gas and conventional oil expenditures in Alberta have stagnated, B.C. and Saskatchewan have seen significant increases. Alberta's reinvestment has also dropped, from an average of 60 per cent over the last decade, to about 40 per cent in 2008. Natural gas completions have decreased by 33 – 53 per cent across Western Canada in response to investor interest in U.S. shale gas plays.

As noted by the Alberta Chambers of Commerce and other industry stakeholders, the risk-reward balance needed to be readjusted to improve investment competitiveness. Actions in the Competitiveness Review included:

- Making permanent the maximum five per cent front-end rate on new natural gas and conventional oil wells (with current time and volume limits of 12 months, 50,000 barrels of oil equivalent, or 500 million cubic feet equivalent of natural gas)
- Reducing the maximum royalty rate for conventional oil from 50 per cent to 40 per cent.
- Reducing the maximum royalty rate for natural gas from 50 per cent to 36 per cent.

These are important first steps toward recognizing that different extraction methods (e.g. shale gas production and enhanced oil recovery) are fundamentally different operations with different economic drivers, requiring extraction-specific fiscal and regulatory frameworks.

² U.S. Energy Information Agency. *Annual Energy Outlook 2009 with Projections to 2030*. . Release Date: March 2009. Available online: <http://www.eia.doe.gov/oiaf/aeo/gas.html>



Achieving Sustainable Development While Improving the Regulatory Environment

Regulatory efficiency is important to Alberta's competitive position. A number of government Ministries and agencies are involved in industry regulation including the Departments of Energy, Sustainable Resource Development, and Environment; and the Energy Resources Conservation Board (ERCB). Improvement in coordination and collaboration among the bodies could improve regulatory processes and reduce energy producers' costs.

The Alberta Chambers of Commerce agrees with the Competitive Review conclusion that "Alberta's regulatory system needs to be more integrated, more practical and more efficient."³ The Government of Alberta's intent to shift to an outcome-based approach is commended. A consolidated approach to environmental assessment, public and Aboriginal consultation for regions that are intensely developed could be an effective mechanism to improve efficiency.

The Task Force announced to provide recommendations on creating a more efficient and effective regulatory system is strongly supported by Calgary's business community.

Use of 'Real-Time' Data

The Competitiveness Review used up-to-date data that led to better dialogue and decision-making. This led to more effective dialogue between industry and government. It is important that the Department of Energy continue to work closely with industry to access 'real-time' data and financial modeling.

V. Fostering Technological Innovation

Currently, only about 27 per cent of light oil and 15 per cent of heavy oil is recovered in Alberta.⁴ The Energy Resources and Conservation Board estimates that improvements in technology could increase the current average recovery efficiency by 26 per cent.⁵

CO₂ Enhanced Oil Recovery Opportunity

Western Canada is well positioned to be a leader in carbon capture and storage (CCS). The unique storage potential of the Western Canada Sedimentary Basin, along with the Government of Alberta and industry partnership (\$2 billion from the government to be at least matched by industry) to fund research and development of CCS facilities, is a strong step towards developing new industrial capacity.

³ U.S. Energy Information Agency. *Annual Energy Outlook 2009 with Projections to 2030*. . Release Date: March 2009. Available online: <http://www.eia.doe.gov/oiaf/aeo/gas.html>

⁴ Government of Alberta. 2009. Energyeconomics - Understanding royalties. Available online: http://www.energy.gov.ab.ca/Org/pdfs/Energy_Economic.pdf

⁵ ERCB. *Alberta's Energy Reserves 2008 and Supply/Demand Outlook 2009-2018*. Available online: http://www.ercb.ca/docs/products/STs/st98_current.pdf



The Alberta Carbon Capture and Development Council sees big potential for CO₂ enhanced oil recovery. With a price of \$75 per barrel of oil, the Council estimates that sufficient capacity exists to store 450 megatonnes (Mt) of CO₂ and produce an additional 1.4 billion barrels of oil from conventional reservoirs. This represents a doubling of the province's conventional oil recovery. It would result in \$105 billion in additional revenue during development and generate \$11 - \$25 billion in additional provincial royalties and taxes.⁶ If half of the CO₂ storage capacity was used in Alberta (225 Mt), Alberta would more than meet its climate change reduction target of a 14 per cent absolute reduction (200 Mt) in greenhouse gas emissions by 2050.

Maximizing the Potential of Alberta's Shale and Tight Gas Resources

The Alberta Chambers of Commerce believes that the end goal, based predominantly on the potential for new economic growth and reduced environmental impacts associated with gas (i.e. combustion of natural gas results in 50 per cent less greenhouse gas emissions), is fully developing the potential of this resource. Due to the technological risk and costs associated with this resource, a unique fiscal structure is necessary. The announcement to make permanent the maximum five per cent front-end rate on new natural gas and conventional oil wells is a positive step. It will help to encourage innovation by recognizing the higher costs of new technology and allowing faster recovery of capital.

The Government of British Columbia has recognized the commercial risk and cost of new technologies and has created the *Net Profit Royalty Program* to maximize development of economically marginal resources. The B.C. program is directed at development of expensive resources that are not commercially viable under existing royalty programs and either technically complex or remote from existing infrastructure. Eligibility for this program is determined through a Request for Applications (RFA) process.⁷ The Alberta Chambers of Commerce suggests that a simpler approach may be to extend the timeframe and volume limits of the maximum five per cent front-end royalty for new oil and gas wells to account for the costs and risks of new technology.

In general, the Alberta Chambers of Commerce supports the Competitiveness Review's focus on driving innovation and the acknowledgement of the substantial technical and financial risk associated with pioneering new technologies. The Chamber agrees that these costs must be factored into the overall economics of an oil or gas well. The government's intent to better support pilot projects is also positive movement in this area.

Industry / Government Partnership

In the 1970s, the Government of Alberta and industry joined forces to collaborate and invest in a new vision of energy development for the province by investing \$2 billion in

⁶ Alberta Carbon Capture and Storage Development Council. 2009. *Accelerating Carbon Capture and Storage Implementation in Alberta*. March 2009 -Final Report. Available online: http://www.energy.gov.ab.ca/Org/pdfs/CCS_Implementation.pdf

⁷ Government of British Columbia. 2009. *British Columbia Royalty Programs*. Presentation at the Unconventional Gas Technical Forum. April 2009.



oilsands research through the Alberta Oil Sands Technology Research Authority (AOSTRA). This led to important technical innovations such as steam-assisted gravity drainage (SAGD) and the creation of the Alberta Energy Company (AEC) to invest in the necessary pipeline and electricity infrastructure to support long-term oilsands development. It is estimated that this investment will yield total government revenues of \$123 billion (income tax, royalties, corporate tax, provincial sales tax, GST, property tax, etc.) and a total increase in GDP (gross domestic product) of some \$885 billion from investment and development in oilsands during the period 2000 to 2020; a significant return on the government's investment.⁸

Similar partnerships between industry and provincial and federal governments (including the United States) will be necessary to immediately capitalize on emerging technologies that are deemed promising but too expensive to implement in their current state. Evidence from AOSTRA indicates great benefits for Albertans.

The business community looks forward to discussing additional ways to recognize and account for higher costs of new technologies required to develop mature conventional oil and gas plays and unconventional natural gas.

VI. Constructive Ongoing Dialogue

The Competitiveness Review has gone a long way to increase dialogue and understanding between industry and government. It was a positive process that enabled the industry to discuss industry realities and investment decision-making frameworks in a way that will lead to more effective fiscal and regulatory systems, ultimately benefiting all Albertans through job creation and a higher standard of living.

This momentum must be continued. The Alberta Chambers of Commerce has suggested the creation of a permanent and ongoing forum for industry/government dialogue to address emerging issues, ensure understanding of industry investment decision metrics, and explore opportunities to capitalize on emerging resource development.

The Chamber acknowledges the Government of Alberta's commitment to sit down with industry prior to any changes to the fiscal and regulatory system to better understand potential impacts. This pledge begins the process to restore investor confidence and trust. It is important that constructive and open dialogue be maintained on an ongoing basis.

Recommendations

The Alberta Chambers of Commerce makes recommendations to the Government of Alberta in several key areas.

⁸ Canadian Energy Research Institute (CERI). 2005. *Economic Impacts of Alberta's Oil Sands. Volume 1.*



Communicate the Vision and Benefits of Energy Development

1. Develop a campaign, both within the province, nationally and across North America, to outline the vision of energy development in the province, and highlight the benefits of jobs and prosperity for Albertans, Canadians and North Americans.

Predictability and Stability

2. Provide sufficient time intervals before another major review takes place, ensure that future reviews are inclusive of industry at the outset, and focus on ensuring that the fiscal and regulatory system continues to be current and responsive to technological change and long-term resource plays.

Fiscal and Regulatory Competitiveness

3. Continue to maintain the goal of positioning Alberta as one of the most competitive North American destinations for investment.
4. Compare the competitiveness of Alberta's regime internationally to understand capital deployment alternatives, and mitigate against the loss of capital.
5. Work with the energy industry to make further adjustments to the royalty curves to improve competitiveness with comparable jurisdictions.
6. Ensure data is 'real time' and, as appropriate, consider external sources of data and financial modeling from world-class energy financial companies.
7. Consider a consolidated approach to environmental assessment, public and Aboriginal consultation for regions that are intensely developed.

Fostering Technological Innovation

8. Work with the energy industry to extend the timeframe and volume limits of the maximum five per cent front-end royalty for new oil and gas wells to account for the costs and risks of new technology.
9. Maintain industry and government collaboration in energy research and development to share technological and cost risks (e.g. carbon capture and storage investment partnership).

Constructive Ongoing Dialogue

10. Create a permanent and ongoing forum for industry/government dialogue to address emerging issues, ensure understanding of industry investment decision metrics, and explore opportunities to capitalize on emerging resource development.