

RIWG Royalty Review Presentation Notes

June 5, 2007 Fort McMurray, Alberta

RIWG Royalty Review Presentation Panel Presentation – Slide 1

Good morning and thank you for the opportunity to present today. 14 meetings in 5 different communities stretching over 3 months - this panel has undertaken an ambitious effort to hear diverse voices on royalty returns to Albertans. My organization, the Athabasca Regional Issues Working Group, or RIWG as we're more commonly known, is pleased to lend our regional perspective here in Fort McMurray today. Given the focus of my organization, I will specifically address the generic oil sands royalty regime and provide some examples of what it means to the local economy. An appropriate and successful oil sands royalty regime is important to the Wood Buffalo region, the province of Alberta and the country of Canada.

RIWG Membership: Slide 2

RIWG is a non-profit, professional association made up of 24 member companies who are active in the Wood Buffalo Region and to some extent, Lakeland County. 17 of our members are oil sands producers and under our umbrella, they meet to analyze, discuss and solve regional issues that affect

their stakeholders, employees and overall development plans. The Regional Municipality is included as a member in special standing and the government of Alberta often participates in our various committees. Every year, we survey our membership to help create an updated, overall picture of the direction that oil sands development is taking. We predict local trends such as employment growth and population growth. Working with our colleagues at the Canadian Association of Petroleum Producers, we also generate forecasts on some more province wide indicators such as future royalties to the government of Alberta which we will discuss with you today.

Oil Sands – Many Different Returns to Albertans: Slide 3

Certainly Albertans see returns through their provincial and municipal governments in the form of taxes or royalties but they also see a multitude of positive returns in the form of direct and indirect contracts and employment. This brings manufacturing and asset building to the entire province. It also brings research and development spin offs, helping to create new businesses. While the dollars that flow to government in the form of royalties and taxes are significant, I submit to you that the total economic benefit to Albertans is generated primarily by the billions invested by oil sands developers in new and sustaining capital projects combined with ongoing operating expenses

which also amount in the billions annually. This truly is what's driving the economic engine of our province and most of our country and I encourage everyone not to lose sight of this fact.

Working Together – Aboriginal Involvement in Oil Sands Development

– Wood Buffalo Region: Slide 4

Let's take some time at the beginning of this presentation to review some of the more specific, regional benefits that oil sands development brings, beginning with Aboriginal involvement in the Wood Buffalo Region. From an economic perspective, this year's 06/07 survey of RIWG member companies demonstrates a continued commitment from oil sands producers and aboriginal people to realizing value:

- 1500 + Aboriginal employees in permanent operations jobs
- \$412 million in contracts with Aboriginal companies
- Average annual salaries of \$81,000 for aboriginal employees
- \$3.7 million in contributions to Aboriginal communities

Some describe a situation of near full employment for aboriginal people living near oil sands development. While our member companies view this as a positive indicator, nothing is taken for granted as we continue working

on strengthening relationships with aboriginal people in many different ways.

Regional Corporate Donations: Slide 5

Well before oil sands companies produced their first barrel of oil, they began working on the sustainability of Fort McMurray and surrounding communities. Community investment plays a key role through charitable donations and support for local non-profit groups. While clearly this support has a significant monetary value – most recently eleven and a half million in 2006 – in addition to the cash, donations of gifts in kind, support and services are also provided.

This includes ensuring oil sands leadership and employees actively volunteer within the region. While oil sands executives regularly serve on local charitable boards, our member companies also encourage support for the United Way and employee volunteerism through a variety of programs. In 2006, this was so successful that Fort McMurray became the highest per capita contributor to the United Way in all of Canada, generating over \$3 million dollars this year alone.

RMWB Municipal Tax Base Growth: Slide 6

Return from oil sands investment will be of direct, growing benefit to Albertans living in the Wood Buffalo Region through the stewardship of their municipal government. As oil sands producers build more infrastructure in the Regional Municipality of Wood Buffalo, the local government will have a greater assessment base upon which to collect greater revenue, if they so chose. This chart shows a 12% compounding annual growth in assessment capacity for the municipality growing from roughly \$10 billion in 2007 to over \$35 billion in 2017. This is of course, predicated on growing, uninterrupted capital investment. One thing this slide does not capture is the municipality's ability to increase taxes. Just two weeks ago, the Municipality raised its rural non-residential mill rate which primarily targets assessable facilities belonging to oil sands producers. In a matter of a few weeks, the current 3 oil sands miners saw their anticipated 2007 property tax bill rise from approximately \$71 million in 2006 to an estimated \$123 million in 2007, a 72% increase. This increase occurred partly because of an expansion of an existing facility but was mostly due to a major increase in the general Municipal tax rate. The municipality cited less than expected revenue from the provincial government as a reason for their need to increase taxes on oil sands

producers. This is an important regional and provincial taxation development to highlight because it is indicative of some of the increasing fiscal uncertainty oil sands producers are seeing that is increasing costs and affecting net returns.

Oil Sands Royalties: Historical & 2007 Forecast (all Alberta): Slide 7

Now is a good time to move to the larger provincial royalty regime. The slide you see here represents RIWG's most up to date, 2007 forecast of future royalty returns to the government of Alberta. This recent forecast is within 5% of the government of Alberta's projections for the next two years based on their most recent budget. This graph is based on an average \$60 US WTI per barrel price case. We have also produced a \$50 and \$40 version which we would be happy to share with you at your request.

Click first text box

Firstly, it is important to mention that 06/07 was a record year for the government of Alberta. Based on last year's average oil price of \$65 per barrel, the government of Alberta received \$2.4 billion in oil sands royalties. While the royalties drop in 2008 and then plateau with some ups and downs stretching out to 2014, it is important to keep our focus on the long term

benefits to Alberta. Here you see the province receiving nearly \$4.5 billion in royalty revenue by 2016. So, why the plateau?

Click second text box

Firstly, this is indicative of a period of extremely high capital investment where royalties are comparatively low which makes the investment possible. Secondly, it is important to note this forecast is based on a \$60 US WTI average oil price compared to last year's \$65 average price. It also presumes that Suncor and Syncrude will both elect to pay royalties on bitumen production although it remains to be seen whether both companies will take this election. Finally, it is important to note that additional capital investment will take some projects back down to the 1% of gross pre-payout royalty designed to stimulate greater oil production and government royalty revenue in the future. A plateau may be coming but take time to notice the elevation of this plateau compared to previous years.

Click third text box

In 2014 we see the beginning of a dramatic increase in royalties to the government of Alberta. Simply put, many of the projects that enjoy royalty relief during the preceding "plateau" years are predicted to reach pay out

status at this point. Here they begin paying 25% of their net profit, bringing oil production, royalties and taxes to a new level. Let's not forget either that the plateau leading up to this increase can be elongated or compressed, depending on oil prices.

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By the time we reach the end of this graph, we see a projected royalty return to the Government of Alberta of \$4.5 billion a year and climbing. If you add RIWG's extrapolation of future corporate taxes to this amount, the Alberta government receives an estimated \$7 billion a year. Here is where, after 10 years of realizing economic returns in the form of capital investment in the province, Albertans see a move into higher royalties while still realizing the benefits of the other taxes applied to our operations.

Oil Sands Royalties and Capital Expenditure: Historical and Forecast:

Slide 8

Let's now examine the significant returns to Albertans from oil sands development that comes in the form of private capital spending, economic development and job growth. On this graph we have taken the royalty projection you've already seen and overlaid it against RIWG's capital

expenditure forecast. The left axis refers to construction capital spending while the right refers to royalty payments. In RIWG's opinion, this slide illustrates the current royalty regime working as it was meant to. It shows strong return to Albertans both in terms of economic development and government revenue. It shows that during periods of relatively lower government return, higher amounts of private construction capital are spent. During times of declining private construction capital, increased amounts are paid to the Alberta government via royalties. Over the last three years, we've seen a period of significant increases in both government revenue and private construction capital. The overarching point is that government agrees to take reduced revenues during times of construction in an effort to attract private capital. It then ups its revenue again once projects are built and new oil is actually being produced. Again, RIWG believes this graph is a picture of the royalty regime at work. It is doing precisely what it was meant to do and is producing record results that many thought were impossible to achieve.

Continuing Benefits: Oil Sands Operations Spending and Jobs – Wood Buffalo Region – Slide 9

Let's not forget that the benefits do not start or stop at construction capital and royalties. This slide demonstrates yet another way that Albertans see increasing returns under the current royalty regime. Here we see the operating capital that oil sands projects are planning to spend in addition to the construction capital we saw on the previous graph. While construction capital ebbs and flows with the creation of new projects, operating capital, used to maintain what has already been built, shows steady growth. Here we see growth from a little over \$5 billion this year to approximately \$25 billion in 2017. This means additional direct and indirect job creation and business development for Albertans. It means more return for all of us. This is reinforced by the operations hire bar graph underneath. Here we see a lock step increase in employment following increased operation capital expenditure. We move from under 5000 permanent operations jobs in 06/07 to approximately 18,000 jobs by 2017. This does not take into account the attendant job growth that will occur. It is believed that for every full time oil sands job created, two indirect jobs and two induced jobs are also created. It is safe to assume this is a big part of what people mean when you hear them say, "What's good for Fort McMurray is good for Alberta" or "What's good for Fort McMurray is good for Canada". Both the province and the federal government will see greater income tax from new jobs and greater corporate

taxes as long as construction and operation capital continue to be spent in Alberta.

Royalty Regime Recommendations – Slide 10

So, allow me to sum up RIWG and industry's position regarding the treatment of the oil sands royalty regime within the province of Alberta.

Firstly, we concur with the recommendations and submissions made by the Canadian Association of Petroleum Producers on this matter.

In our view, oil sands members worked tirelessly with the provincial and federal government to establish the National Oil Sands Task Force and the generic oil sands royalty regime. Fundamentally, this royalty regime is working very well and is generating the total economic return envisioned in 1996 when it was adopted.

We believe this regime is fair, providing a reasonable return for both the investors who risk billions in capital on these projects and the people of Alberta who own the resource. Moreover, it is simple in its application and has proven resilient to wide variations in oil prices and other economic conditions since its inception.

Today, the billions generated annually to the province through royalties, taxes and lease purchases, coupled with the indirect taxes paid by business and employment generated from our operations, allows Albertans to experience opportunities nearly unimaginable through the nearly 20 years when no expansion in the oil sands industry occurred.

I would submit to you that it is in the province's best interest to retain the generic royalty structure as it exists to ensure we continue realizing these economic benefits and not risk the unintended consequences of lost capital investment likely if the regime was modified.

Distinguished panel members, thank you for your time today, I sincerely hope RIWG's contribution assists you in future conversations and deliberations.