



REGIONAL MUNICIPALITY
OF **WOOD BUFFALO**

**SUBMISSION TO THE
ALBERTA ROYALTY REVIEW PANEL**

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Fort McMurray, AB

Presented by:

Regional Municipality of Wood Buffalo

MEMBERS OF THE ALBERTA ROYALTY REVIEW PANEL

The Regional Municipality of Wood Buffalo respectfully submits the following report, expressing our views on the Alberta Royalty System for oil and gas. We appreciate the opportunity to appear before you and submit the full text of our report for your review.

OVERVIEW

The Panel is tasked with the responsibility to determine whether Albertans are receiving a fair share from the resources this province has been blessed with. We believe there is wide agreement that, as owners of Alberta's energy resources, Albertans are entitled to benefit from the development of those resources. We in the Regional Municipality of Wood Buffalo respect the right of the oil sands industry to make a healthy profit. Our concern is that the individuals living in the communities that support such development are experiencing an increasingly unacceptable deterioration in their quality of life.

The Regional Municipality of Wood Buffalo ("RMWB") is significantly impacted by development in the Athabasca Oil Sands right now. In recent years, oil sands development has increased dramatically, creating profits in the billions of dollars for oil sands developers, while at the same time, placing unprecedented pressure on the infrastructure and services in the Region. If the level of monetary support from the Province and Industry remains unchanged, the residents of the Region will continue to experience now, and be left with a legacy of insurmountable environmental, fiscal and social impacts long after the oil sands developers are gone.

Despite Alberta's booming economy, infrastructure deficits are becoming more and more pronounced, indicating an imbalance in the system – both in the *quantity* of revenues generated from royalties, taxes and other costs, and in the *manner* that those revenues are distributed. The RMWB believes the Province must act now to implement changes that will lay the foundation for a genuine "fair share" for Albertans for the future. A fair royalty regime is one that provides sufficient revenue to address all of the costs of energy resource development (environmental and social) and provides a fair return to Albertans for the development of their resources. Further, the provincial government must ensure that these revenues are re-invested in the communities that support such energy resource development and where the biggest impacts are felt.

BACKGROUND

The RMWB comprises 68,454 square kilometers in northeastern Alberta. It was formed in April 1995 by consolidation of the City of Fort McMurray and Improvement District #18. In addition to Fort McMurray, the RMWB includes the Hamlets of Anzac, Janvier, Conklin, Draper, Saprae Creek, Gregoire Lake Estates, Fort MacKay, Fort Chipewyan, Fort Fitzgerald and Mariana Lake.

The RMWB is home to the Athabasca Oil Sands, which have brought about unprecedented growth in development and population over the past several years. It is widely recognized that Alberta's oil sands deposits are the second largest commercial oil deposits in the world – next only to Saudi Arabia. Demand for oil and gas worldwide is increasing each year.

In 1964, the Great Canadian Oilsands Company (now Suncor) received approval for the region's first oil sands project, which began production in 1967. The Syncrude project began construction in 1973, with production commencing in 1978. Since approximately 1996, the development of the oil sands has expanded dramatically. There are currently no less than 50 major oil sands projects in the Wood Buffalo Region in various stages of application, approval and production. This is only a small fraction of the development yet to come.

In the mid 1990's, the National Oil Sands Task Force projected that investment in the oil sands would total \$5.7 billion over 25 years. That prediction proved to be grossly underestimated. Between 1996 and 2005, \$37.4 billion had already been invested, with another \$56.6 billion projected to be spent in construction capital for the oil sands industry by 2011 alone.¹ Most of this investment relates to projects in the Fort McMurray area. With the commercially recoverable oil reserves in Alberta estimated to be 175.6 billion barrels², the vast majority of which is in oil sands, the development boom in the region can only be expected to continue.

The RMWB is the only municipality in the province, and perhaps in the country, experiencing this level of large-scale industrial development. Oil sands industry expansion is a major driver of economic activity in Alberta, accounting for 62% of all major projects.³ Production is expected to triple to 3 million barrels per day by 2020.⁴

IMPACTS OF OIL SANDS DEVELOPMENT ON THE RMWB

The 2006 Municipal Census indicates a population of 79,810 citizens, of which 64,642 reside in Fort McMurray. As a result of oil sands industry expansion, the region has experienced an unprecedented annual growth rate approaching 9% over the past six years, nearly doubling in size since 1999.

¹ Athabasca Regional Infrastructure Working Group ("RIWG"), "Realizing the Vision" – Presentation to the Standing Policy Committee on Energy & Sustainable Development (June 12, 2006), p. 6, <http://www.oilsands.ca/pdfs/RIWG%20SPC%20on%20Energy-June%2012-06.pdf>.

² Alberta Energy and Utilities Board, News Release, "Forty Years of Oilsands Production Leaves Bitumen Reserves Largely Untapped", June 15, 2006, <http://www.eub.ca/docs/new/newsrel/2006/nr2006-24.pdf>.

³ Alberta Employment, Immigration and Industry, "Oil Sands Industry Update", December 2006, p. 1.

⁴ Alberta Energy Research Institute, "Energy Development and Future Outlook" for Standing Senate Committee on Energy, the Environment and Natural Resources, http://www.aeri.ab.ca/sec/new_res/docs/Isaacs_du_Plessis_Submission_to_Senate_Committee_050307.pdf.

The RMWB recognizes the economic benefits that oil sands development brings to the region. However, at the same time, this explosive influx of people has placed tremendous strain on the ability of the RMWB to provide and maintain the municipal services and infrastructure required to support a healthy, vibrant, and sustainable community. The facilities and services in the region are taxed to their maximum limits. This includes: housing, transportation, health, social, leisure, policing and emergency services, traffic, and education.

Municipal Infrastructure

The unprecedented rate of investment and growth in the RMWB has created tremendous pressure on existing municipal infrastructure. The existing deficit in public infrastructure and services in the region has been quantified and presented to the Alberta government in the various forms over the past five years. In 2002, the Region identified the need for \$563 million in public sector capital infrastructure requirements between 2003 and 2007.⁵ By March 2005, the capital required for infrastructure projects had increased to \$1.2 billion between 2005 and 2009, including \$353 million in municipal projects, such as water, waste water, road, and recreation facilities.⁶ By December, 2005, just 9 months later, the \$1.2 billion figure had grown to \$1.9 billion, and the \$353 million figure for municipal projects had escalated dramatically to \$814 million.⁷ Part of the reason for the increase in municipal projects was that anticipated funding from senior government was not forthcoming – no grants, other than those offered to all municipalities in Alberta, were received.⁸

The RMWB's current capital plan projects the need to fund approximately \$800 million in necessary municipal infrastructure by 2010. Some of the urgently needed municipal capital projects include expansions to the water and wastewater treatment facilities and the solid waste facility, all of which are operating over or near capacity. Other necessary projects included in the capital budget are: water and wastewater treatment facilities in outlying communities, road upgrades, bridge rehabilitations, new RCMP facilities, fire hall upgrades and expansions, storm water management facilities, heavy equipment replacements, transit improvements, recreation facilities and overwhelmed municipal facilities. The list goes on.

The completion of these projects is critical to support the existing needs of the community and to help facilitate additional growth expected for the region. The municipality is simply unable to fund all of these necessary projects on its own. This problem is aggravated by the significant inflation in construction costs experienced in the RMWB. Due to the tremendous pressures from energy development in the area, cost escalations have significantly impacted the municipality's capital program. These

⁵ RIWG, Wood Buffalo Business Case 2005, March, 2005, p. 26,
<http://www.oilsands.ca/pdfs/Wood%20Buffalo%20Business%20Case%202005.pdf>.

⁶ *Ibid*, p. 5.

⁷ RIWG Wood Buffalo Business Case 2005 – Update & Progress Report, December 2005,
<http://www.fortmurraychamber.ca/start.htm>, p. 4.

⁸ *Ibid*, p. 10.

problems are compounded in that the RMWB must compete with the industrial projects for labour, contractors and equipment.

These figures represent the cost for physical infrastructure only, and do not reflect other costs which cannot be calculated, such as the high cost of living, difficulty in attracting and retaining staff, and the resulting deterioration of the quality of life for residents of the region.

Municipal Services

The magnitude and rate of residential and non-residential growth in the region has also placed significant strain on municipal services. In an increasingly tight labour market, it has been difficult to attract and retain the workers necessary to meet the demand for municipal services. Adding to the difficulty of recruiting staff is the rising cost of housing in the area, particularly in recent years.

The RMWB, Health Region, public and separate school boards, Keyano College and non-government and volunteer-based agencies, are all having difficulty recruiting and retaining the staff and volunteers they require to meet the needs of the residents in the region. Employees and volunteers are overwhelmed due to staff shortages and heavy workloads.

The RMWB is at a disadvantage as compared to industry employers. While oil sands companies can provide living-out allowances, signing bonuses, stay bonuses, and even profit sharing in lieu of overtime, the municipality has that fiduciary responsibility to their ratepayers that restricts those types of practices out of the public purse.

The current staff turnover rate for the RMWB is substantially higher than other similar-sized municipalities – more than 1.5 times higher than St. Albert and Strathcona and more than 2.5 times higher than Medicine Hat and Lethbridge. In 2006, the RMWB was operating with approximately 12.5% vacancy in its total staff complement. In order to keep up with the expected demand for services, the RMWB is projecting to add a total of 225 new positions between 2006 and 2008. Given its current difficulty in recruiting and retaining staff, the RMWB expects difficulty in achieving the capacity we need to offer an acceptable quality of service to our citizens.

Housing

As the oil sands industry has expanded, and the population increased faster than anticipated, the demand for and price of housing has increased dramatically. Single family dwelling prices in Fort McMurray quadrupled between 1995 and 2005. As of April, 2007, the average price for a single-family dwelling in Fort McMurray had reached \$557,899⁹, as compared to \$413,488 in Edmonton.¹⁰ Currently, rental rates in Fort

⁹ Fort McMurray Real Estate Board: <http://www.woodbuffalo.net/www.woodbuffalo.net/housing.html>.

¹⁰ Edmonton Real Estate Board: <http://www.ereb.com/marketactivity/April2007.html>.

McMurray are approximately double the rates in Edmonton and the vacancy rate is effectively zero.

The RMWB estimates that there is currently a shortfall of 4,000 housing units in Fort McMurray. At the current growth rate approaching 9% per year, approximately 12,500 new dwelling units will be required in the RMWB between 2007 and 2011 (plus the 4,000 shortfall). This demand for housing far outstrips the rate of new housing development over the past several years. Even at record production levels, it will be virtually impossible for the RMWB to close the existing shortfall and construct the housing units required to meet the future demand. Preliminary work conducted by Nichols Applied Management on behalf of the Athabasca Regional Issues Working Group anticipate a minimum of 9% population growth to continue in Fort McMurray for at least the next 5 years.

Projected Dwelling Units Required In Ft. McMurray

YEAR	6% Population Growth	9% Population Growth	12% Population Growth
2007	1387	2081	2775
2008	1471	2268	3108
2009	1559	2473	3481
2010	1652	2695	3898
2011	1752	2937	4366
5 Year Total	7,821	12,454	17,628
2006 shortfall	3,918	3,918	3,918
Units Needed	11,739	16,372	21,546

The local housing market has become so tight and expensive that many households are being forced into alternate accommodation, such as doubling up, renting illegal suites, staying at the homeless shelter, living in campgrounds, couch surfing, etc.

The housing gap is growing, and will continue to widen if these key barriers to increasing housing supply are not addressed. Continuing to expand the oil sands industry within the RMWB without first increasing the housing supply will further inflate housing costs. Both time and resources are needed in order to address the RMWB's severe housing shortfall and to properly plan and develop complete and integrated communities that will enhance the quality of life for residents.

Quality of Life

The cumulative impacts of oil sands industry expansion have negatively affected the quality of life for long-term residents of the region. The Federation of Canadian Municipalities has been studying quality of life over the past 10 years in 20 Canadian Cities, based on 11 sectors, including: demographics, affordable housing, civic engagement, community and social infrastructure, education, employment, local economy, natural environment, personal and community health, personal financial security, and personal safety. In reviewing the indicators developed by FCM, the quality of life in Fort McMurray is deteriorating in all sectors but two – local economy and employment.

This is important, because people working in the RMWB have a choice. Many of those working in the oil sands now drive in to work and have their primary residence in some other community, driving home on weekends. More and more, we receive indications that future expansion in the oil sands will feature fly-in/fly-out proposals. The RMWB has serious concerns about the impacts of such camp-based operations – little economic benefit flows to local workers and businesses, and neither the plant workers nor their families become invested in the region, adding to the existing sense of transience and weak sense of community within the RMWB. This is a competitive time in the Province and the declining quality of life in the RMWB detracts from our ability to encourage our current and future citizens to live here.

The social indicators in Fort McMurray also point to a gradual degradation of the quality of life. The negative social impacts described by local residents include: inflation, extreme housing shortages, labour shortages, family stress, drug and alcohol abuse, increased crime, destruction of the traditional social fabric, and time lag between growth and upgrading of services.

Oil sands industry expansion in the region is further emphasizing the northern resource town nature of Fort McMurray, which creates community stresses that impact the quality of life for some residents, including the following:

- The rapid population growth in Fort McMurray is producing a sense of transience and a weak sense of community. Most of the construction workers in this region have permanent homes elsewhere, and many people who move to Fort McMurray to take advantage of employment opportunities do not intend to stay for the long-term.
- Rapid growth also creates a prosperity gap between high-paid oil sands industry workers and everyone else in the community, including public and private service sectors and those on social assistance or otherwise on the margins of the wage economy. Generally speaking, people employed directly or indirectly in the oil sands industry can afford the high cost of living, while everyone else cannot.
- The shift work characteristic of the oil sands developments means that many residents of Fort McMurray are working long and irregular hours, which places

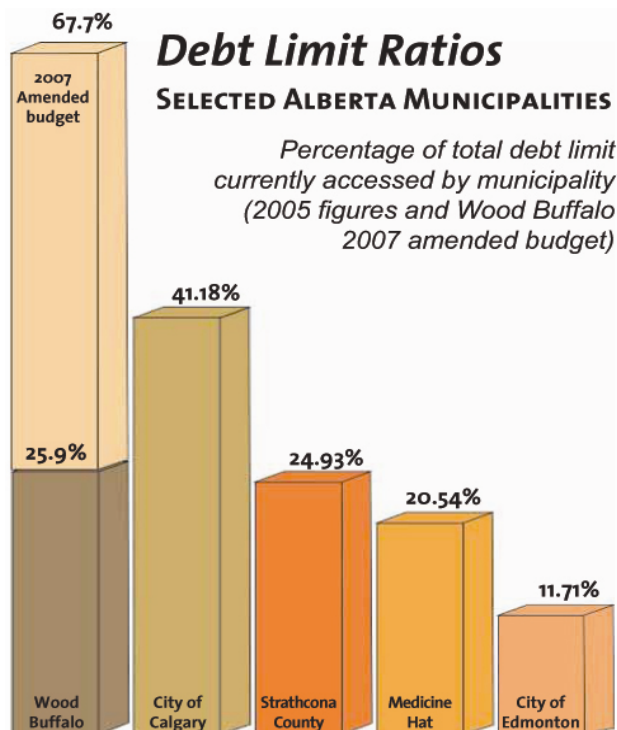
stress on families and reduces the amount of time that people have available to contribute to their community.

These broad community effects, in turn, impact the individual residents of the community. For instance, the weak sense of community increases the isolation felt by residents and increases the demand for all social services “from childcare to counseling.” Because of the long and irregular hours worked by those in the oil sands industry, children spend more time without parental supervision. The residents of the RMWB are becoming increasingly concerned about the perceived overall deterioration of quality of life in their communities.

The Municipal Debt

The RMWB debt is the highest in the province. In Alberta, the provincial government has mandated municipalities to remain within a debt limit of 1.5 X annual revenue. Because of its unique circumstances, the Regional Municipality of Wood Buffalo last year was granted provincial approval for a debt limit that equals two times annual revenue, joining Calgary, Edmonton and Medicine Hat as the only other municipalities in the province with that distinction.

In 2007, the municipal debt is projected to be \$335 million, giving the municipality a debt limit ratio of 67.7%. By 2008, and for the foreseeable future, the municipal debt will exceed 85% of the legislated debt limit, but RMWB has set a threshold to maintain a financial cushion, giving the municipality the flexibility to deal with its changing environment and emerging issues and service demands.



Unfortunately, the unique pressures Wood Buffalo faced with the pace of oilsands development is creating a situation whereby the municipality soon will not be able to borrow the funds necessary to provide for new capital projects and infrastructure.

RECOGNITION THAT CURRENT FUNDING IS INSUFFICIENT

Currently, there are insufficient funding mechanisms available to provide for the municipality's extraordinary infrastructure and service needs in a timely fashion. Current provincial funding mechanisms are not adequate and have not been modified to reflect the unique nature and magnitude of the challenges faced by this municipality and the region's strategic importance to the Alberta economy. This has cumulatively had a negative impact upon the RMWB and the quality of life for its citizens.

The sole source of revenue for a local government currently is the property tax. In 2005 the RMWB received support for two resolutions from both the Alberta Urban Municipalities Association (AUMA) and the Alberta Association of Municipal Districts & Counties (AAMDC) to petition the Province to amend the legislation concerning Machinery and Equipment assessments.

The first resolution called for the abolishment of the discount on Machinery and Equipment assessments to 77% of market assessment. Non-residential and residential property classes are assessed at 100% market value, thereby creating an inequitable and unfair distribution in taxes amongst the various property classes.

The second resolution asked for the repeal of MGA Section 354 (3.1) which restricts the municipality to taxing the Machinery and Equipment assessment class at the same rate as the non-residential assessment class. The Machinery and Equipment assessment class is granted an exemption from paying Provincial Education taxes. All other property classes are not. Also, under the Machinery and Equipment Assessment Minister's Guidelines, the assessed value of Machinery and Equipment is subject to an immediate 25% depreciation factor which further diminishes the assessed value at which Machinery and Equipment is taxed in comparison to the other property assessment classes. This results in the municipality being unable to fairly distribute the total tax burden amongst the assessment property classes. The resolutions were forwarded to the Minister of Municipal Affairs by both Associations and, to date, both have been rejected.

It would be reasonable for the provincial government, who placed the restrictive legislation and regulations concerning Machinery and Equipment assessments on the municipality's ability to levy fair and equitable property taxes, to return to the municipality a portion of royalties collected equal to the shortfall in taxes the municipality is unable to collect.

For example:

Machinery and Equipment Capital Cost = \$1,000,000

Less immediate 25% depreciation	=	-250,000
Less 77% assessment level	=	<u>-172,500</u>
Total Assessment	=	\$ 577,500

If the Provincial Government, by legislation, refuses to allow the municipality to collect full property taxes on an oil sands industry, and if the Province is not collecting enough in Royalties to transfer the funds necessary to support a high-growth community, then the Royalty on oil and gas should be increased to allow them to do so.

The financial return to the provincial and federal governments from Alberta's energy resources is significant. While it is the RMWB that provides the roads, water and other services that facilitate resource development in the region, our economic return is marginal compared to the senior levels of government. The RMWB receives property taxes from oil sands developers and their workers, but that is miniscule in terms of the share of the resource wealth that is extracted from this region. In 2005 to 2006, the provincial government received \$950 million in oil sands royalties.¹¹ During that period, the RMWB received no special funding to address the extraordinary infrastructure requirements created by oil sands development in the region, other than interest costs for four years on a \$136 million loan for upgrades to the wastewater treatment facility. Over the next 5 years, Fort McMurray will receive only \$64 million out of the \$3 billion Alberta Municipal Infrastructure Program.

The RMWB has been falling behind in its struggle to keep pace with the nature and rate of the current development, not to mention the impact of new and future projects. This has created serious deficits in infrastructure and gaps in municipal services. Development in the region has reached a critical stage. The RMWB Council has taken the position that before any additional oil sands approvals are issued, the region requires immediate funding to address these serious issues together with a commitment by senior government and industry to long-term planning for growth in the region.

Recently, there has been increased recognition that there is a need for increased funding for municipalities experiencing high population growth, and that perhaps the Province and Industry should have an expanded role in this. The RWMB fully supports these suggestions, and believes that the companies who extract resources and wealth from the region should contribute in a meaningful, planned manner to the communities which they depend on and which they impact the most. This includes providing funding to pay for the infrastructure and services that are required to support the development. Adjusting the royalty regime to achieve this is an option that makes sense.

¹¹ Alberta Ministry of Energy, 2005-2006 Annual Report, p. 18,
<http://www.energy.gov.ab.ca/docs/aboutus/pdfs/AR2006.pdf>.

The Final Report of the Oil Sands Ministerial Strategy Committee, dated December 29, 2006, "Investing in our Future: Responding to the Rapid Growth of Oil Sands Development" (the "Radke Report") recognized that:¹²

- A substantial level of investment in the oil sands is expected to continue for the next five years and beyond. Estimates are that production will reach close to 4 million barrels of oil per day by 2020. The pace of development in the oil sands has been accelerating, and forecasts indicate that the current level of investment will continue for at least the next 5 years.
- The pace of growth has caused pressures on essential services and infrastructure, particularly in Fort McMurray. The community is hard-pressed to keep up with growing demands for housing, transportation, health care and education. There are significant gaps in housing, health care and basic infrastructure in Fort McMurray.
- The housing shortage is particularly acute in Fort McMurray, and the shortage of affordable housing compounds the challenge of attracting and retaining the necessary workforce. Provincial funding is not sufficient to meet the needs in the Fort McMurray area. The RMWB does not have the capacity to complete the necessary planning processes in a timely fashion so that land can be sold, developed and housing constructed.
- As a result of the rapid population growth over the past 7 years, all major infrastructure systems in Fort McMurray need significant expansions. The water treatment plant, waste water treatment plant and solid waste facility are currently all at or over their designed capacity and need major expansions immediately.
- The ability of the RMWB to fund the critical infrastructure projects needed for water treatment, waste water treatment, and solid waste is in doubt. Existing funding approaches are not adequately addressing infrastructure needs in an appropriate and timely manner. It may be unreasonable to expect the municipality to fund the full cost of basic municipal infrastructure required to support the massive oil sands projects which benefit the entire province.
- Health services in the Northern Lights Health Region are inadequate to meet the needs of a rapidly growing population.
- Transportation issues are a growing concern in the RMWB. While the provincial government has committed to address a substantial portion of the transportation requirements, much of this is still in the design and planning stage and a significant portion remains unfunded.
- There are a number of social issues affecting residents of the RMWB, including homelessness, addictions, and lack of affordable child care.
- Fort McMurray will continue to be a high growth area. The population of Fort McMurray is forecast to grow at about 8% per year for the next 5 years, which is

¹² Final Report of the Oil Sands Ministerial Strategy Committee, dated December 29, 2006, "Investing in our Future: Responding to the Rapid Growth of Oil Sands Development", pp. 4-8.

well above the growth rate of other communities in the province. In percentage terms, the population growth rate of Fort McMurray exceeds the growth rate of any other community in Alberta by a wide margin.

- The planning and decision-making process within Alberta government is deficient in the areas of housing, health care, basic municipal infrastructure, transportation and social services. The Province has failed to forecast potential problems and has not, as a result, been able to provide solutions in advance of the problems becoming serious deficiencies.

One of the issues raised in the Radke Report was the suggestion that industry, especially new oil sands developers, needs to make larger contributions to the communities in which they operate. The Report suggested that this could occur “either through a surcharge applied to the sale of leases, by an increase in royalty rates, or by government dedication of a certain portion of royalty returns and lease sales to infrastructure development in the affected communities.”¹³ The RMWB supports this suggestion. The Radke Report states that comparing the population of the RMWB to the population of Alberta indicates that for every dollar per capita “taken off the top” of the Alberta budget and dedicated to meeting the needs in the RMWB, it would reduce the per capita allotment to other Albertans by only 2.43 cents – “a small price to pay for future prosperity”.¹⁴ One of the options outlined for supplementing revenues to the municipalities in the oil sands was to dedicate a certain portion of lease and royalty payments received from oil sands projects to the municipality where development occurs to finance the infrastructure required by new growth. The Radke Report notes that there is some support for this idea from some of the operators in certain areas.¹⁵

While the Radke Report recognized the need to fund some \$800 million in critical municipal infrastructure projects in the RMWB¹⁶, the province has to date announced only \$103 million in funding to complete the water treatment and wastewater facilities in Fort McMurray¹⁷, leaving a funding gap of approximately \$700 million for necessary municipal projects.

Similarly, the Report to the Minister of Municipal Affairs, dated March 5, 2007, presented by the Minister’s Council on Municipal Sustainability, recognized that:

- The difficulty faced by municipalities in funding the local infrastructure required to support Alberta’s growing population and thriving economy now represents one of the major hurdles to overcome in ensuring Alberta’s continued prosperity.¹⁸

¹³ *Ibid*, p. 132.

¹⁴ *Ibid*, p. 131.

¹⁵ *Ibid*, p. 148.

¹⁶ *Ibid*, p. 75.

¹⁷ Alberta Government News Release, “Funding for Fort McMurray helps meet urgent needs brought on by oil sands growth”, February 26, 2007, <http://www.gov.ab.ca/acn/200702/21083FEE10ED0-02C5-4D66-36A829A8522FEDCE.html>.

¹⁸ The Minister’s Council on Municipal Sustainability, Report to the Minister of Municipal Affairs, March 5, 2007, p. 4, <http://www.aamdc.com:8081/library/Advocacy/Publications/Reports/2007%20->

- Municipalities in Alberta simply do not have access to sufficient revenues to respond to the demands of rapid economic and population growth. Much of this funding shortfall is due to the current pace of growth, which is severely taxing existing municipal infrastructure and creating significant demand for new infrastructure and services.¹⁹
- The provincial government should provide the funds necessary to significantly assist municipalities in addressing existing municipal infrastructure deficits.²⁰
- “Economic rent” (what is due to Albertans for the use of their resources after the costs of doing business and the generation of reasonable profit are taken into account) should be redefined to include those costs which directly affected municipalities must bear to support resource development.²¹
- Sharing of provincial revenues is necessary to assist municipalities in addressing their large and growing infrastructure deficit, and to ensure that municipalities have access to revenues that respond to economic growth.²²

One of the recommendations coming out of that Report was that the Government of Alberta should reconsider the concept of “economic rent” to include the direct costs imposed upon municipalities as a result of resource development and provide municipalities access to revenues from industry to offset these costs. One of the options for achieving this was increased provincial resource royalty rates, with the increase earmarked for allocation to directly affected municipalities.²³ The RMWB fully supports this recommendation.

COMMENTS ON THE EXISTING ROYALTY REGIME

The current royalty system for oil sands was established in 1997, and was specifically designed to encourage investment, recognizing the significant risk to oil sands developers. At that time, the technology was new, there were a limited number of companies involved, and there was no certainty that the extraction of oil from the oil sands would be economically viable. Compounding the risk was the low price of oil (about \$27 per barrel) and the high cost of producing oil (about \$15 per barrel).²⁴ This strategy proved to be successful. Between 1998 and 2005, investment in the oil sands increased by 300%.²⁵

[%20Minister%27s%20Council%20on%20Municipal%20Sustainability%20Report%20to%20the%20Minister%20of%20Municipal%20Affairs.pdf](#).

¹⁹ *Ibid*, p. 9.

²⁰ *Ibid*, p. 10.

²¹ *Ibid*, p. 11.

²² *Ibid*, p. 12.

²³ *Ibid*.

²⁴ Government of Alberta, “Royalties in Alberta, Background Information”, http://www.albertaroyaltyreview.ca/more_info/background.pdf, p. 6.

²⁵ *Ibid*, p. 8.

In its application to the AEUB for the expansion of its existing oil sands mine, Albian Sands Energy Inc. stated:

Since 1996, a number of different factors have coincided to create a climate that is favorable for oil sands project development. These factors include the following:

- the introduction of generic royalty and corporate taxation regimes that created certainty regarding the royalty / tax schedules and decreased front-end risk for developers;
- technological changes, including the adoption of truck and shovel mining, hydro-transportation of bitumen sand and advances in in-situ recovery methods; and
- favourable product prices and price forecasts.²⁶

The circumstances that were in place when the generic royalty regime was implemented have all changed, contributing to an environment where there is now certainty that oil sands development will be not only economically viable, but highly profitable. For instance, applications submitted to the AEUB by oil sands developers indicate that while the estimated capital costs are high, return on investment is positive at oil prices of \$24 to \$28 US per barrel.²⁷ In actuality, the price per barrel in recent years has been more than double that estimate, ranging between about \$50 and \$70 US per barrel. The RMWB believes that the existing royalty system is not sufficiently sensitive to market conditions. When the price of oil increases, making oil sands development highly profitable for industry, royalty rates should increase accordingly, so that Albertans receive their fair share of that benefit.

Energy company profits have soared due to an increased world demand for oil and gas, high prices, and technological advances. It is evident that there is no longer the need for incentives to develop the oil sands – the resource is there, demand is increasing, oil sands operations have proven to be highly profitable, and developers are now clamoring to construct new, and expand existing, oil sands projects.

There are several indications that the existing royalty regime is not achieving an optimal balance:

- There are currently insufficient revenues available to the Alberta Government to address the infrastructure and service deficits that have been created by energy resource development across the Province and to also provide a fair return to Albertans as the owners of the resources. As a result, the resource owners are receiving less benefit than they are entitled to.

²⁶ Albian Sands Energy Inc., Socio-Economic Impact Assessment, April, 2005, Volume 4, Section 7.7.3.2, p. 7-222.

²⁷ Albian Sands Energy Inc., Application for Approval, April, 2005, Volume 1, Overview, Section 1.1, p. 1-4; See also Suncor Energy Inc., Application for Approval, March, 2005, Volume 1, Section 1.4, p. 1-17

- Even if there were sufficient revenues, there is not sufficient and accessible funding available to the municipalities that support such development to ensure that the quality of life of the residents of those communities is maintained and provided for in the future.
- The existing royalty regime, in conjunction with all of the other factors favourable to oil sands development, has resulted in a number of oil sands projects being constructed and operated simultaneously. This has led to an overheated economy, including severe shortages in labour, materials and equipment, dramatic increases in costs, and project cost overruns. This, in turn, means less revenue for Albertans who own the resource.
- There is some concern that the existing royalty regime lends itself to manipulation by energy companies. The 1% royalty rate until project payout is an incentive for oil sands companies to reinvest profits into *expansions* of existing oil sands projects, so that the timeline for project payout is delayed. As a result of this practice, increased royalties can be delayed for significant periods of time, thereby reducing the amount of return to Albertans for the use of their resource.
- There is an ever-increasing imbalance between economic development in the province and the lasting cumulative social and economic impacts of that development. Albertans are becoming increasingly concerned that the royalties are insufficient to cover the environmental and social costs of resource development going into the future.

WORKING WITH INDUSTRY

The Regional Municipality submits this paper for the purpose of ensuring that we have the resources necessary to develop and maintain a community that will provide our citizens, and oil patch employees, with a reasonable quality of life. Our residents expect no less than that of other Albertans. We believe Industry would agree with this statement and, in this competitive economy, believe a viable community to be critical to their success in attracting the thousands of workers necessary to develop their projects and to keep them here as the projects mature.

We believe any disagreement would come from interpretation. In our discussion with Industry, they believe governments have a clearly defined mandate to provide services and already collect the revenue necessary. From a municipal perspective, we submit to the Panel that we're not the experts in establishing an economic principle like a royalty regime. We know that we can't provide a quality of life for our community with the current funding formula provided to us. We say that, if the province is not raising the money necessary to support us, they need to raise more. If it's a matter of reallocating the funds necessary for that support and they don't need to amend the royalty formula, then they should do that. In the end, for us it comes down to providing the funds in a reliable, planned manner that allows the RMWB to proceed with surety into the future.

We believe the Industry submissions to the panel will oppose any changes to the existing royalty regime; however, should the Province make changes, we know there is industry support to see **predictable, annual royalty revenues** returned to producing regions for infrastructure support, rather than industry stepping forward with dedicated infrastructure contributions paid directly to municipalities.

SUMMARY AND RECOMMENDATIONS

The RMWB recognizes that the royalty regime must strike a balance between providing a fair return for Albertans and providing sufficient incentive for development of Alberta's energy resources that allows Alberta's economy to prosper. However, if Alberta is not receiving the funds from Industry to provide the infrastructure necessary to maintain the development of the resource, the balance must be weighted too heavily in favour of industry to the detriment of Albertans. In this booming economy, oil sands developers are recovering record profits from our resources while Albertans are experiencing a deteriorating quality of life, as municipalities struggle to keep pace and the infrastructure and service deficits grow. If the status quo remains, this imbalance will become even more pronounced in the future, as the environmental and social impacts grow. Now is the time to plan for the future, so that the Alberta Government can ensure that Albertans receive the *benefits* that we are entitled to.

The RMWB makes the following recommendations to the Alberta Royalty Review Panel:

1. We believe it prudent to re-visit the generic royalty regime for oil sands in light of the vastly different circumstances that exist today, including increased oil prices, improved technology, and better return on investment. In particular:
 - a. Revise the definition of "economic rent" to include the direct costs imposed upon the RMWB as a result of the development of the Athabasca Oil Sands.
 - b. If necessary to provide funds to support high-growth municipalities, increase the percentage payable before "payout", which was common in the individual arrangements prior to the implementation of the generic royalty regime and after "payout" to an *ad valorem* rate higher than the current 25%. Although if more plants mature and actually pay at the 25% level, this may provide the level of income necessary to allow the province to adequately transfer the funds necessary for high-growth municipalities to maintain their infrastructure.
 - c. Implement a new system for calculating royalties that reflects the price of oil so that higher royalties are payable when profits are higher. This way, higher royalties are paid when profits are high, but can remain relatively low during cost recovery and when profits are lower.
2. Dedicate a predictable, annual portion of royalty revenues received from oil sands projects to the RMWB and other municipalities where the development

occurs and which are most directly affected by development to help finance infrastructure and services required by the new growth.

3. Monitor the existing royalty regime to ensure that companies are in fact paying the royalties that the regime is designed to capture. For instance, re-define “project payout” so that the capital costs of expansions of *existing* projects are not included in the *original* project costs. Oil sands companies should not be entitled to avoid paying higher royalty rates by expanding existing projects. Rather, expansions should be treated as new projects in order to achieve the intent of the oil sands royalty regime – that the higher royalty rate is payable once the capital costs of a project plus an acceptable rate of return is reached.

The RMWB would like to thank the Alberta Royalty Review Panel for the opportunity to make these submissions.

On behalf of the Regional Municipality of Wood Buffalo,

Melissa Blake
Mayor

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