Title: Wednesday, April 13, 2005 Public Accounts Committee
Date: 05/04/13
Time: 8:30 a.m.
[Mr. MacDonald in the chair]

The Chair: Good morning, everyone. I would like to call this meeting of the Standing Committee on Public Accounts to order. I would like on behalf of all members of the committee to welcome those in attendance this morning, and I would like to note for information purposes that agenda packages were mailed out on Monday, April 11, to each member.

Now, before we seek approval of the agenda, I would like to quickly go around so we can introduce ourselves for the benefit of the minister and his staff.

[The following members introduced themselves: Mr. Bonko, Mr. Chase, Mr. Griffiths, Mr. Johnston, Mr. Lindsay, Mr. MacDonald, Mr. Oberle, Mr. Prins, Mr. VanderBurg, and Mr. Webber]

Mr. Elsalhy: Mo Elsalhy, Edmonton-McClung. I'm not on the committee; I'm just here to observe.

Ms Pastoor: Bridget Pastoor, Lethbridge-East. I'm also an observer.

Mrs. Dacyshyn: Corinne Dacyshyn. I'm the committee clerk.

[The following staff of the Auditor General's office introduced themselves: Mr. Drotar, Mr. Dunn, and Mr. Wylie]

[The following departmental support staff introduced themselves: Mr. Giesbrecht, Mr. Keech, and Mr. Smith]

Mr. Melchin: Greg Melchin, Calgary-North West and Minister of Energy. Do I have the option of being an observer at this committee? [interjection] Okay. We'll be happy to participate.

The Chair: Could I please have approval of the agenda that was circulated?

Mr. Bonko: Yes.

The Chair: Thank you. Moved by Mr. Bonko that the agenda for the April 13, 2005, meeting be approved as distributed. Everyone in favour? Opposed? Seeing none, thank you very much.

Now, we will move to item 3 on our agenda, and that is our meeting this morning with the hon. Minister of Energy, Mr. Greg Melchin, and his staff. It is a tradition in this committee that there be up to 15 minutes for the minister to provide an overview to the committee members, of the fiscal year 2003-04. Everyone, hopefully, has a copy of the annual report for the ministry, and if they do not, the chair will share his. Okay?

If there are no questions at this time, I would ask the minister to please proceed. Thank you.

Mr. Melchin: Thank you, Mr. Chairman. One question maybe before I start. Not all of the members of the department have yet been introduced, and they may wish to respond. I suspect we could bring them up to a microphone. Is that going to be the requirement or the need, to come to a microphone? Or can they respond from back there? Or do you need it for recording purposes? [interjection] Oh, there's a mike? Okay. Excellent.

We've had everybody around this table introduced. Before I get going, I'm going to have a few more members of our department that are at the back introduce themselves, if we could.

[The following departmental support staff introduced themselves: Mr. Borland, Mr. Boyd, Mr. Breakwell, Mr. Ekelund, Mr. Fluckiger, Ms Housdorff, and Mr. Shepherd]

Mr. Melchin: I could have potentially easily introduced them myself, but it was a lot more enjoyable to watch them all parade up to the microphone and make sure that everybody's breathing and anxious to be able to respond to the questions that the committee may have.

Unlike many, having come from a financial background, I actually view this as a very important and good exercise in making sure that we do understand and account to the public as to in this case the Department of Energy and its accounts for the year 2003-2004.

In my introductory remarks I'll go through just a few items in particular with the summary, with the report. The ministry includes the Department of Energy, the Alberta Petroleum Marketing Commission, and the Alberta Energy and Utilities Board. So those are the three areas in particular that we might address. The department is primarily responsible for matters related to resource development and the assessment and collection of nonrenewable resource revenues.

The Alberta Petroleum Marketing Commission accepts delivery of the Crown's royalty share of crude oil and sells it at current market value. The department's and the Alberta Petroleum Marketing Commission's operations are integrated and fully funded by the Crown.

The Energy and Utilities Board, on the other hand, is an independent, quasi-judicial agency of the government of Alberta, and its responsibility is to regulate Alberta's energy resource and utility sectors. While the Energy and Utilities Board reports to the ministry itself, it does make its formal decisions independently, that being in accordance with various statutes and regulations. The Energy and Utilities Board's operations are jointly funded by the Crown and industry.

The year 2003-04 for the oil and gas industry was another very substantial and, I guess, exciting year, a very profitable year for the industry and for the province in particular. Producers delivered $7.68 billion in resource revenues to the Crown, and at that stage that was the second highest total in the history of Alberta. We've just completed another year which surpassed that one, so it now becomes the third highest. But at that time it was the second highest in light of the high stage of commodity prices in the current climate. Industry investment totalled over $20 billion, and that's supported by more than 300,000 direct and indirect energy-sector jobs, a very significant aspect of this province. Many of us are fully aware of that portion of it.

In 2003-04, the first fiscal year in which Alberta's proven oil sands reserves of 174 billion barrels were acknowledged and reported by the United States Energy department – it's a reserve of about 1.6 billion barrels, a very substantial resource, the proven being 174 billion at this stage and quite likely will be a number substantially higher than that in the not-too-distant future.

In July of 2003 the McBride Lake Wind Farm was completed. This solidified Alberta as the number one in Canada when it comes to total wind power capacity. This played a role in Alberta's total installed electric capacity exceeding 11,500 megawatts, a 45 per cent increase over the previous decade.

In 2003 we also saw the launch of the natural gas rebate program. This was initiated to help Albertans offset high natural gas prices during the winter months, November through March.

The Alberta hub attracts attention as a first-class pipeline network for northern gas producers, providing highly competitive access to markets for natural gas in Alberta and across North America, and we want to continue to build on the Alberta hub as being truly the economic and market advantage for all of the northern gas pipelines that yet could be developed in the future, a very significant and important aspect of positioning the Alberta hub.

Industry satisfaction has been important to this ministry for many years, and having said that, we're always looking for opportunities for improvement. In November 2003 independent survey results showed overall satisfaction with the department at 84 per cent. Department staff do consistently provide excellent customer service, and this proves invaluable to our day-to-day business activities.

It certainly has been my experience in the previous ministry and in this one also, the Department of Energy, that we do have very excellent, professional, qualified personnel in our department. We are very fortunate to have the dedicated staff that we have in the leadership of Ken Smith and the deputies and those that are here. We could, clearly, introduce you to hundreds of others, actually, that come with substantial qualifications and professionalism. So we're very fortunate to have that support in our department. The department continued to place a strong emphasis on public communication and awareness, dealing effectively with public inquiries relating to electricity, gas billing, and prices and government rebate programs.

8:40

Alberta is a major player in the global energy industry, and we continue to make significant progress in elevating the international profile and recognition of Alberta's energy resources. I'd like to also emphasize that this is going to become an even more and more important aspect of our awareness, that Albertans become more understanding of the vastness of the resource that is here and the opportunity that it can be for Albertans by appreciating that it's not a sunset industry but that it's really a sunrise industry. It's only in its infancy of opportunity, and that's not just because of the oil sands, as we quoted, but clearly in natural gas from coal and the conventional sources. With improved technology we have truly centuries of perpetual opportunity in this province, and communication of that is going to be a very vital aspect of the ministry going forward.

Alberta also will continue to maintain the competitive royalty and regulatory framework necessary to attract capital investment from world markets. The Alberta government owns 81 per cent of the province's mineral rights. The remaining 19 per cent is owned by individuals and companies or by the federal government on behalf of First Nations and national parks.

Our natural gas business unit ensures that the Crown receives full value for our natural gas resource and promotes and encourages natural gas activities and operations. With the price of natural gas fluctuating wildly through 2003, you can certainly appreciate the challenge in trying to provide forecasts in commodity prices. We've seen that historically – and even at a time right now when they're high – when the expectations are that they're only going one way, there's a substantial risk that they could actually retreat. So forecasting is really a challenging aspect. It will continue to be part of the ministry, and I think it prudent that we should forecast on a conservative basis, that we not put at risk financing the programs of the government based upon a high price forecast.

In the end we still collected about $5.5 billion in natural gas royalties. We are reviewing and have been reviewing royalty structures to ensure competitiveness, and our oil and gas royalty regime is ranked one of the most rigorous regimes in Canada and in the world, successfully striking the balance between encouraging continued development while collecting a fair share of resource development profits.

Last year conventional oil royalties totalled about $981 million. Our oil sands royalty regime is unique. It allows for lower royalty rates in the early years of a project's development. Those rates then return to more normal levels once development costs are recovered. They are unique very much in the sense that there is nowhere else, really, in the world that has the high intensive capital costs up front, substantial risk up front, to explore and develop these resources. Our production grew, and our oil sands revenues were $197 million for the last fiscal year.

The department also concluded work on the new Electric Utilities Act, and Albertans are seeing the results of a more competitive electricity market with new supply, products, service options, and competitive prices. Eight hundred and thirty megawatts of new power came on stream during the 2003 calendar year with plans for additional generation continuing, showing investors' confidence in Alberta's market.

For the 2003 calendar year Albertans paid on average 30 per cent less for residential natural gas compared to other Canadian households. An amendment to the Natural Gas Price Protection Act makes the program more responsive to gas prices on utility bills.

Our tenure business unit through its bimonthly land sales made available 3 million hectares for industry development, receiving $967 million from the sale of oil sands, petroleum, and natural gas rights.

Alberta Energy is the leader in implementing e-business, and 2003-04 saw the Petroleum Registry of Alberta complete its full year of operations. It continues to be recognized as a forward-thinking, money-saving, web-based resource that has already won a technology in manufacturing award. Other provinces are also looking to potentially work in conjunction with that very successful initiative.

Coal royalties for 2003-04 were $8.6 million. In this province there is enough coal to meet current consumption levels for the next 1,000 years. Coal has recently undergone a resurgence of importance in world markets with prices improving.

Alberta collected just under $1 million in royalty revenue from limestone, salt, gold, and shale operations. Minerals of interest for exploration purposes were mainly diamonds and precious metals, while minerals of interest for production purposes were industrial minerals, particularly lime and limestone, and base metals, particularly iron and magnetite.

The department was also actively involved in the implementation of Alberta's Water for Life strategy and will continue to be involved in such.

Royalties collected through the department continued to provide about 30 per cent of the government of Alberta's total revenue for that particular year and will continue probably in the foreseeable future to play a very significant part of the overall government's revenue.

With those brief comments, Mr. Chairman, I'd be more than happy to entertain any questions that the members of the committee have.

The Chair: Thank you very much, hon. minister.

Mr. Dunn, do you have any . . .

Mr. Dunn: Yes. Thank you very much, Mr. Chairman. Our 2004 annual report section on the Ministry of Energy contains three numbered recommendations, of which recommendation 10 has been highlighted as a key recommendation. This recommendation comes from a systems audit which our staff carried out on the administration of the oil sands royalty regime. Our work involved reviewing 10 projects out of the then 48 active oil sands projects. The deficiencies noted in the department's processes have been reported in our recommendation 10 and the audit findings which follow this recommendation.

Our recommendation 11 is directed at the department's own audit assessment group, whose mandate is to "ensure Crown resource revenues, allowed costs [by the producers] and various supporting submissions are complete, accurate and fairly valued." Our audit findings result from the examination of five of the department's audit files out of the 48 active projects. Those audit findings are detailed on page 128 of our annual report.

The government's response to our recommendations 10 and 11 addressed to this committee indicates that certain corrective actions or improvements have already taken place.

Recommendation 12 is a repeat recommendation concerning a very old royalty tax credit program. We are looking to the Department of Energy to "document and communicate the objectives" for this royalty tax credit program and to "use measures to assess whether the program is meeting its objectives." The government's response indicates that the recommendation has been accepted with the commitment that the Department of Energy will work with Alberta Finance to obtain a formal approval of the objective, which was only a draft objective last year.

We've also provided a status report on the progress that the department has made on two prior year recommendations concerning well and production data and other royalty reduction programs. We believe that the department has made satisfactory progress in addressing both of those prior year's recommendations. However, we will continue to follow up those recommendations until they have been fully implemented by the department.

Those are my opening comments, Mr. Chairman. I and my staff will be pleased to answer any questions the committee will direct to us.

The Chair: Yes. Thank you.

Mr. VanderBurg would like to ask for a clarification, please, Mr. Dunn.

Mr. VanderBurg: Mr. Dunn, you talked about the expected ranges for analyzing costs and forecasted resource prices.

Mr. Dunn: Right.

Mr. VanderBurg: I've been following this for a long time. I see the experts on the financial side, and I see the experts on the oil and gas industry, and I see our own experts. There's quite a range within that. Who in your department is the expert on this?

Mr. Dunn: Okay. I'm not going to say that we are the expert. What we're looking for is the department having the expertise in order to establish what they believe to be the expected ranges. We'd expect that they would have that information within the department. As the minister has mentioned, they have very, very sophisticated and professional members within their department. We would expect that they will have that information.

8:50

Mr. VanderBurg: I understand that, but everybody has that big range. You know, it doesn't matter whether it's the financial industry, our own industry. But are you saying that we need to peg that figure closer in our budgets? Or what are you saying by that?

Mr. Dunn: Remember, in this recommendation – what the member is referring to is recommendation 10 and the details behind 10 – we're looking at the fact that when they do a discounted assessment of a future project out there, that has to take into account current information and use relevant risk-rated discount rates. So we're saying that you should have an expected range in there. That's not the range that may come into the government's budget forecast, but it should be the range that they will look at that that project should be able to yield over its life, which may be a 25- to 40-year life.

Mr. VanderBurg: Okay.

The Chair: Before we start with the formal question and answer session, I would like to advise the minister and his departmental officials that if there are any questions that are in detail, the details can be provided in writing through the clerk to all members, please.

There's no need to touch your microphones. Sometimes we have problems here, but there's no need to touch your microphones.

For those who are visiting the committee today, you are welcome to participate in the proceedings, but you just cannot vote. That is, members of the Assembly who are not members of this committee, you are welcome to participate, but you just cannot vote on any of the proceedings here.

I see that we have been joined this morning also by Mr. Hinman. Mr. Rodney is present, for the record, and would like to ask a question, and also Mr. Eggen.

Perhaps we will start with Mr. Chase, representing Calgary-Varsity.

Mr. Chase: Thank you very much, Mr. Chair. Mr. Melchin in his foreword talked about risk, and that is what my question is about: risky business, basically. We had a situation this past year where Peter Elzinga was basically playing both sides of the fence. He was lobbying on behalf of an oil sands company that was claiming their project was an extension of a previous project and not a new project, and at the same time he was advising the Premier. My question is to the Auditor General. What is the financial risk associated with what I see as a lack of definition of what is a new project and what is an extension project?

Mr. Dunn: I'll answer the economic part of that question. The financial risk within the royalty regime, as the minister has indicated in his opening comments, is that until the project reaches payout, 1 per cent of gross revenue is the royalty. Once a project gets to payout, then it becomes 25 per cent of net revenue. Clearly, if a project is about to reach maturity and go into the 25 per cent royalty regime and then you expand it, you will delay that if that's seen as an expansion versus a new project. If it's all part of the original project, you will therefore then delay the introduction of a 25 per cent royalty rate. So that's the risk, that it may result in a delay to the other royalty rate.

The department may also want to answer that.

Mr. Melchin: I would like to first state that I don't know all of it, but a lot of the preamble I don't think is correct as to what was lobbied by a certain member or the person that you're talking about. Those decisions were made without that interjection or otherwise, so that wasn't even part of the discussion.

In particular, the company that was referenced, in this case it would be Suncor, is actually a little different than even the generic royalty regime in the sense that there were a few companies in transition to the generic royalty regime: Suncor, Syncrude, those that had been in operation before the transition period to a generic oil sands regime. Those agreements continue through most of this decade in their transition. So it's really some of those very particular aspects of their agreements which are unique because prior to that every company had their own structure and royalty agreement. Therefore, in helping to let them exit their old royalty regime and onto the new generic, there had to be a transition period and an agreement to get there.

Even with all of the best efforts it's hard to anticipate all of the future events that could happen. In this case, events have happened substantially faster than everybody thought. Prices have been higher, more activity, more investment. Therefore, all of those new expansion projects or new projects by process are required to come to the department to ensure that they do meet the specific requirements, and the department has made their judgment and ruling on that in particular.

The Chair: Thank you.

Your second question, Mr. Chase, please.

Mr. Chase: My supplemental, and Mr. Melchin may have partially answered it: is the definition of what is an extension or an expansion versus a brand new project clear in the Auditor General's mind so that we can apply a set of principles and say that this should be a 25 per cent rate versus a 1 per cent rate? Are you satisfied that there is a clear distinction, and we can start billing oil sands companies appropriately?

Mr. Dunn: I'll pick up on the main part there: are we clear in our mind? What we look to is for the department to have very, very clear rules that can be applied on a consistent and uniform basis. That's what we look to. So when we go in to look at the systems by which they make those determinations, if it appears from our perspective that there may be some uncertainty around what is an expansion, what is not an amalgamation, that's when we will raise it. So I'd like to see that the department will be able to confirm to you that they have very clear rules, that there's no uncertainty in their mind.

Mr. Melchin: I think I'll let the deputy minister actually respond, unless he wishes someone else on staff to.

Mr. Smith: Just a couple of comments. The generic royalty regime, when it was established back in the '90s, came with a regulation, the oil sands royalty regulation. That regulation includes specific criteria for the evaluation of projects under the regime. Those criteria include distance criteria, economic management of the facilities, and other criteria. Those are considered. In the end it's the ultimate responsibility of the minister to determine whether it's in the public interest to approve the project or not, having regard for those types of criteria. There are guidelines that supplement those criteria that have been issued and have been in place for quite some time. That is what we use to evaluate whether projects are, in fact, an expansion or a new project when they're presented to us for review.

The Chair: Thank you.

Mr. Prins, followed by Mr. Bonko.

Mr. Prins: Thank you, Mr. Chairman. I'm looking at page 87 in the annual report of the Department of Energy. Looking down the column here, it shows that there was an overexpenditure of $3.7 million on program support. I'm just wondering: what was the reason for this overexpenditure? This is not a huge budget, but it's still $3.7 million over.

Mr. Keech: Perhaps I can address your question. First, just let me clarify that the overexpenditure is in a particular area, program support. It is not the overall budget. In fact, the department's overall budget was underspent in the year 2003-2004.

In this particular instance, there are a couple of things that account for it. We had put an increased emphasis on both energy awareness and also energy research. We redirected some of our funding from our base budget into those two areas in particular. You'll see in one of our performance measures with respect to the awareness component that we haven't made as much progress as we had hoped, but with 3.2 million people in the province it's very difficult to get the message out. So we had placed an increased emphasis on that to try and increase the awareness of the significance of the oil and gas industry to Alberta. Most Albertans understand that it's important, but they don't understand the significant contribution that the revenues make to our province, both in keeping our taxes low and increasing our ability to be able to spend money on infrastructure and health and education, and so forth.

9:00

Another component of that, related to amortization of The Petroleum Registry, that the minister referenced earlier, The Petroleum Registry of Alberta, was a $25 million expenditure by government to produce a system, a database, of all of the information with respect to the oil and gas information in Alberta. The amortization component of it is not a cash expenditure; however, it does get recorded as an expense, and that accounts for about $700,000 of that total. The expenditures on the increased awareness and the increased research components comprise about $2 million of that.

The rest was directed specifically to increasing our security on our IT systems to ensure, basically, that after some of the problems associated with 9/11, we were in a position to recover from any disaster that may occur and not suffer the slings and arrows of not being able to collect our royalties and, therefore, creating increased pressure on our province. So we had, again, redirected about a million dollars toward increasing our security with respect to our IT systems.

Mr. Prins: Thanks. Another question: on the information part of this overexpenditure, what you had mentioned earlier, do you expect to see a payback, or is this even measurable?

Mr. Keech: Well, certainly on the research side. We have invested some money on a project with the University of Calgary, with the Canadian Energy Research Institute, I think grants totalling about 19 different organizations specifically addressed to research. So certainly we see that in the future. The minister just mentioned briefly when he talked about conventional sources that most of our resource still remains in the ground even though we've been producing since 1948 because the technology has not got to the point where you can extract the resource on a commercially acceptable basis. So much of the research that's going on today is how to be able to enhance the recovery of our resource, how to reduce the cost of producing some of the resources that we do have. As the minister suggests, this is something that will carry on for many generations. Certainly, we're very fortunate to do that, but in order for that to happen, there has to be additional research, and you know government has in our case stepped up a little bit with trying to direct some of this research specifically toward enhancing our recoveries.

Mr. Prins: Thank you very much. No further questions.

The Chair: Thank you.

Mr. Bonko, followed by Mr. Johnston.

Mr. Bonko: Thank you, Mr. Chairman. Of all the companies that operate within the province of Alberta that are extracting the resources, that are essentially the resources of the people of Alberta, how many companies are actually paying that 25 per cent royalty?

The Chair: That's the oil sands royalty, correct?

Mr. Ekelund: Correct.

Mr. Melchin: I don't have the specific numbers. I would say that we were looking at a number of projects at payout. I don't know if someone's got the stats on them, but there are already a number of smaller projects that have reached payout on that, especially with the high price. Is there someone that's – Mike?

Mr. Boyd: Perhaps I can help with that. For the fiscal year that we're looking at, 25 of the 62 projects in the oil sands areas had reached payout. I don't have company statistics. We work on a project-by-project basis.

Mr. Bonko: Okay. Then, do we have any idea as to how much potential to the province of Alberta, with regard to when we do expansions, we are losing out on? It was mentioned earlier that we continue to expand or amalgamate in the word of efficiencies, but we continue to put off that royalty payment, continuing to make new expansions. So, again, we further delay that magic number. At what point do we cut the tie there and just ask for specifics? At what point is this going to come?

Mr. Melchin: As mentioned earlier – and I might have various members of our department respond or supplement – there are a number of criteria that were established as to determining: is this a new or an expanded project? So there are criteria established in regulation for that and guidelines as well. It isn't really a matter of preference; it is a matter of: does it truly make sense that what they're intending to do is an expansion of their existing operation? So there are criteria that are around that. It's hard to anticipate everything that will happen in the future. Therefore, when they're looking at their existing operation, is it just an expansion and added to it, or is it truly a new project?

I would say that it is in our interest to encourage the development of these resources. That's why we've tried to set – rather than an absolute structure that says your costs incurred today are part of the existing and anything else, even though it might be related to that project, you could say: should those costs incurred in the future relate to a new project? We've tried not to be that way because each of the projects are continually investing. It's not just a one-time, upfront cost. Their existing operations have substantial improvements to their operation continually.

So because of the large upfront risk capital – and I've got to emphasize that; I mean, we're talking billions of dollars, really, for many of these projects – to help ensure that we can attract the investment to actually develop these resources, that's why the generic royalty regime was established in the first instance, that it was a 1 per cent until payout.

Mike, supplement if you wish. I don't know if there's anything more to add to that.

Mr. Ekelund: Yes. Okay. I can help. Supplemental information on this: under section 17 of the oil sands royalty regulation, if I've got the section correct, one of the tests specifically for expansion is that there must be no reduction in the net present value of royalties received by the people of Alberta. Under that basis, I would say that the answer in terms of loss potential is that there is none.

To be approved as an expansion, you have to show that the people of Alberta are at least equal if not better off on a net present value basis.

The Chair: Mr. Johnston, followed by Mr. Eggen.

Mr. Johnston: Thank you. My question will take us to page 55 of the annual report: performance measures, second goal; information sharing to stakeholders and stakeholder satisfaction. If you look at 2003-2004, there's a drop of 1 per cent. So it's been identified to improve this. What progress has been made to date?

Mr. Smith: The department has been trying to track this on an ongoing basis. We believe that a change of this size is probably not significant. In terms of the overall, you're within a percentage point. More importantly, perhaps, is that our statistics are indicating that our work with the industry and with the clients that we have is really at a very high level, and if you look at standards in other organizations, nongovernment organizations, many would like to see their performance being rated in the 70 per cent range. When you think of all of the interaction that we have with industry and the complexity of their requests and the kinds of information that we provide, I think we're finding that we have a very high level of satisfaction being reflected in the work that we do.

Mr. Johnston: Okay. My supplementary: what additional steps is EUB considering to improve access to data and customer satisfaction levels?

Mr. Giesbrecht: We continue to look at that. We've been investing in our IT systems to get us to that point.

Mr. Johnston: Thank you.

The Chair: Thank you.

Mr. Eggen, followed by Mr. Griffiths.

Mr. Eggen: Good morning. Thank you. My question is to do with the Auditor General's report, specifically to do with the royalty reduction program on page 128 of the Auditor General's report. I think that this is an ongoing difficulty in being able to evaluate quantitatively the benefits that have been given as a result of royalty reduction, things under the OSR97 specifically. As an example of that, the Auditor General identified five files that either failed to document the cost that was paid during the time period or the nature of the work, et cetera. I would just like some clarification as to what specifically is going to be done to shine some clarity and transparency on this whole area of the royalty tax credit program here in this coming up year, generally and specifically, you know.

9:10

Mr. Breakwell: I can talk about the deep gas royalty holiday program. It's one of the five that the Auditor General had identified, and it's been in place since 1985. The purpose of the program when it was first set up was to increase the drilling activity and to improve the information that we have from that foothills area to understand where that gas is actually located. Over that period of time we've provided a royalty investment. We see it as an investment as opposed to a reduction, as it's been penned, of about $700 million. But we've returned about 2 and a half billion dollars over and above that amount in royalties that we believe we would not have seen had we not had that program. The program has actually increased the drilling in that area about twice over any other area within the province over that period of time.

Now, that was the initial performance objectives for that program. We're now looking at establishing what those objectives should be on a go-forward basis given the new environment of prices and costs within that. And that's what we're looking at doing right now, working with the Auditor General's group.

The Chair: Thank you.

The Auditor General would like to add some comments to that. But, sir, could you please clarify for us, for the committee: this deep gas royalty holiday that was implemented in 1985, is that for the foothills front area only or is that for the entire province?

Mr. Breakwell: It's for the province. It's for drilling deeper than 2,500 metres, so anywhere in the province where that occurs, but primarily within that foothills area is where it has been over this period of time.

The Chair: Mr. Dunn, please proceed.

Mr. Dunn: There's a bit of miscommunication here. What has been answered wasn't the question that was asked. Indeed, he's talking about a royalty tax. What we were looking at here was evidence which is gathered by the audit staff of the department regarding qualifying expenses, whether it be for the capital or the ongoing operations. Maybe through my staff you can help clarify what it is that we reported here.

Mr. Drotar: On page 128 this still relates to our review of the oil sands royalty regime, and I believe that's where the question was being asked.

Mr. Eggen: Yes. Although it was quite illuminating in regard to the gas as well.

Mr. Keech: Perhaps I can just answer that. First of all, just while they're sitting here, I mean, I'd like to acknowledge the work that the Auditor General's department does. Certainly, we like to work with them to determine if there are better ways of doing things.

In this particular instance we have a group of auditors in Calgary that are responsible for basically doing our internal audit as it relates to the companies and the production and the royalties that they've paid and so forth. In what has been reported in the Auditor General's report with respect to increasing some of the documentation, there have been several things that have already taken place, and I believe Mr. Dunn would attest to that as well.

We've reviewed and updated the file documentation standards, and we're sure that all of our auditors are aware of what those standards are and what's required in each and every file. We've prepared a sample audit working paper that's used for references for the oil sands audit so any new auditor that may come on board will have an opportunity to review the sample file in advance of doing the audit to ensure that they understand what's required. We've created permanent files for each oil sands project. What had happened in the instances reported here is that there were temporary files kept after the audit was complete. Those were not turned into permanent files. We've ensured that they're now permanent files, so if you want to go back 20 years from now, you'll be able to find the audit that was done on that particular file.

Mr. Eggen: Just a supplemental to that. Obviously, it's a changing market that we have here. What's becoming more apparent to our caucus and to the public in general is that perhaps the overall royalty regime is out of step with the profits that are being brought in not only from the oil sands projects but through the whole energy industry. I would like to ask the minister if he would be willing, you know, to increase the royalty regime in general in keeping with the changing market conditions in Alberta today.

Mr. Melchin: I'd like to first mention that it's true that there are some higher prices in oil today, but it hasn't yet been said that the risk has changed. We're looking at long-term projects. When you're investing $5 billion to $10 billion on a project up front, the oil companies are looking for payout. A lot of those companies have not reached payout. Even in today's market, the risk capital for them is still all sunk. Albertans are still receiving some royalty in that respect throughout this period.

I guess you could always look at different regimes, but the reason the regime was chosen was to ensure – we have such a large resource. With the complexity of going in there with such risk capital up front, you had to approach it differently. So once payout occurs, the good thing that is happening is that the present value of that is also going to be realized by Albertans. That means that payout is going to occur rapidly on less production so that the future production and more of the future production will occur at the higher rates of royalty. We do benefit substantially. Although the cash isn't in higher royalty today, it will be sooner. It'll occur in a faster time.

The other challenge to this, though, is that it's based on bitumen. We continue to hear about the present price of oil, you know, the $55 range, but this is paid at the bitumen level. That's before upgrading, which is another very significant capital cost to upgrade that oil to get it to the light grades that would be comparable to that $55 range. In December, for example, they were actually on the netbacks losing money despite the perception that it's a high price. So there is a different price. A question is: can the marketplace handle all of the bitumen that's coming onto the marketplace? There's the integrated question of having to make sure that we get the upgraders and the refining capacity to realize that full potential.

I guess what I'm here to say is that when the royalty regime is measured by various other analyses – you know, there was a Van Meurs study that ranked it about a hundredth in the world out of all of the areas that are compared. So it might sound generous, but it still is not in the sense of trying to maximize the share of the profits. Albertans are still going to realize a very significant share of those profits. Albertans have to be patient, just like the companies have to be patient. There's a substantial amount of risk capital up front, and it will take some time before we all realize that benefit.

Mr. Eggen: So you're not willing to bring up the overall . . .

The Chair: Excuse me, please. There's a long list of members who've indicated that they have an interest in asking questions as well.

Mr. Eggen: Sure.

Mr. Griffiths: My question comes from the annual report, page 95. It's actually a question regarding the EUB, the Energy and Utilities Board financials. Looking through this, under the category of revenues there are industry levies and assessments. I've noticed that year after year it's very consistent. The actual is pretty close to the budgeted amount. It's always realized. But in this particular year, 2004, there was a $9 million difference between the actual realized and the budget projected. I'm wondering if you can explain why.

9:20

Mr. Giesbrecht: That basically comes from the orphan well levy that we collect. We use the EUB facilities to collect the orphan well levy on industry. We essentially had two levies in the fiscal year '03-04. The reason for that was that the Orphan Well Association wanted to collect the money earlier in the year, and two of those happened to fall in the fiscal year. So in the fiscal year you get two levies for two calendar years, one for '03 and one for '04.

Mr. Griffiths: Can you explain to me why they wanted to collect that in two years? What were the circumstances that . . .

Mr. Giesbrecht: Well, it really wasn't collecting in two years. It was accelerating it more to the beginning of the calendar year so that the money was available for the year.

Mr. Griffiths: I understand. Thank you.

Mr. Hinman: Mine is more just a general question, I guess, on our royalty reduction and our capital expense initiatives. Is the ministry looking at extending capital expense initiatives to perhaps other industries that need to switch over because of the increase in natural gas prices? Industries such as Rogers Sugar down in Taber are no longer competitive. They could switch over to coal, but the capital expense makes it prohibitive. Is the ministry looking at extending this initiative to spawn industry in ways to help us be competitive on an energy basis? We're losing that competitive edge here in Alberta, yet we seem to have lots of energy.

Mr. Smith: I'm not sure what you're referring to on the capital expenditure side.

Mr. Hinman: Well, you do it so that industry can expand energy, and we can get more out of the ground.

Mr. Smith: Like in the oil sands? You're referring to that type of an example?

Mr. Hinman: Yes. The royalty reduction. Would you look at doing that? We have many industries that have been on natural gas and even in the production of electricity, yet we have an abundance of coal. The technology is much cleaner, and it's good today, but the prohibitive cost of switching to that doesn't allow such industries like Rogers Sugar to switch over. They're going to have to shut down because the cost of natural gas is putting them out of – they can't compete with other world markets.

Mr. Melchin: I'm not really certain. We've done no work that I'm aware of specifically on that topic. I'm guessing because I'm not certain that I fully understand the question. You're talking about Rogers Sugar in this case, particularly those that are using various energy – natural gas or coal – and looking for replacement and some incentive for them to switch from one form of energy to another?

Mr. Hinman: Or just a capital expense initiative in the province. I mean, we've done it in the past with the packing plants when they've come in. The Alberta advantage is to be able to use our energy here, yet it just seems like it's on an export basis. What are you looking at in order to give initiatives so that industry can put value-added products here in the province?

The Chair: Mr. Hinman, excuse me, please.

This is through the chair to all hon. members. Questions in this committee are reflective of the fiscal year 2003-04. This is not a policy meeting. This is Public Accounts. So to all members of the Assembly who are gathered here this morning, please consider that in your questions to the minister and his department.

I think we're going to move on to Mr. Lindsay now, please.

Thank you.

Mr. Lindsay: Thank you, Mr. Chairman. To the minister. Early this year we had a gas blowout by Acclaim Energy, and I guess my question is regarding the gas that escapes into the atmosphere. Is that company required to pay royalties on that gas, or is that just lost revenue for Albertans?

Mr. Melchin: I don't know the answer to that. We'll see if someone does.

Mr. Breakwell: Yeah. The royalties we receive are when the gas actually hits the pipeline side. So in this case, if it was burned or lost, we would not have collected royalties on that side.

The Chair: Thank you. Could you please, for the convenience of the chair and *Hansard*, identify yourself, if you don't mind? I apologize.

Mr. Breakwell: Sure. I'm Dave Breakwell.

The Chair: Okay.

Mr. Lindsay: Just a supplemental. If the company, whoever the company may be that was involved with the blowout, were at fault due to negligence, I would assume that there would be fines that would be in place, then, to help recover the loss of that revenue.

Mr. Melchin: You're assuming something that I don't know the answer to, so let's see if we have answers. I suspect, as he said in the response – I'm going to get a supplement to this – that in this case there wasn't a recovery, hence it didn't get to the pipeline stage, and therefore royalties weren't calculated.

Mr. Smith: Perhaps before we go much further, we'd ask the board to clarify where they're at in their process in terms of the response from the regulatory side. There is no provision that I'm aware of for us on the royalty collection side to impose a penalty as a result of a blowout, but there are consequences from a regulatory perspective with respect to the Energy and Utilities Board. I think they have that under review at this point in time.

John.

Mr. Giesbrecht: That's correct, and our report will be coming out in a few months.

The Chair: Thank you.

Mr. Chase, followed by Mr. Oberle, please.

Mr. Chase: Thank you. Minister Melchin mentioned in his introduction the thousand years of coal potential. In terms of resource availability I would suggest that coal by far is number one in terms of availability. I would assume number two would be oil, and number three would be gas.

My question has to do with the efficient usage of gas. The tar sands are using a tremendous amount of gas-fired energy to extract what I would consider to be a less expensive oil product. We can't keep using this gas as an extraction. Also, at the same time they've required a number of the gas producers to cease exploration in that area because, I gather, it interferes with the extraction of the oil from the tar sands.

The other concern I have with regard to the gas is the amount of gas we have left. A tremendous amount of it is sour gas. We're talking about coal-bed methane extraction, which is rather inefficient, and the amount of gas that we can get from that extraction process is limited. Has the department looked at coal for firing the generators involved in the oil extraction from the tar sands? In other words, we've talked about the availability of coal. Instead of having gas-energy plants, including up in the tar sands . . .

The Chair: Question, please, Mr. Chase.

Mr. Chase: . . . can we use coal to a greater extent to maximize our profits, save our gas, and extract the oil more efficiently? Sorry; it's round about, but that's what I'm trying to get at.

Mr. Melchin: I might have some others supplement as well. Coal gasification is clearly a technology that can be employed. In the oil sands they have coking operations. It's a very heavy oil, so they have to take out carbon or add hydrogen to get it to the lighter crude. In taking out the carbon, you're actually producing coal. It's really a coal substance, and they are already actually employing that coke in some of the gasification to replace the natural gas. Some of that already does occur in their operations. There are a variety of other inventive projects going on at this stage to actually use processes other than natural gas.

The signals about price – these are the great things about market signals – are that they really create the inventiveness to look: are there not alternative ways? In this case, if gas becomes a very high-priced and valuable and, therefore, short-of-supply kind of commodity, it really will encourage more alternatives other than just the gas, and that's what you're starting to see.

I do want to clarify just a couple of things, and I may have some others supplement. It is true that there's some work being done on the gas over bitumen because there's some gas that's shut in. The resource of the oil is so large, its magnitude substantially more than the gas in that place, that you can't afford to lose the oil in relation to developing the gas. There are some projects being done at this stage to see: can we not do both? And I think technology will help us answer that question.

9:30

I also thought I'd like to clarify one thing about coal-bed methane. You look at the gas, the undiscovered or potential of our conventional sources of natural gas – and I'm trying to remember – something in the magnitude of about 80 TCF they thought was still available in this province in conventional sources. This was just from a meeting I had yesterday with CAPP. If you look at the coal-bed methane, it's about 500 TCF, the potential of a resource there. And it's already in some of the zones, the Horseshoe Canyon zone, being commercially developed. Very significant. So it's not a limited play. This is going to be a very substantial play for, you know, a century plus to come yet.

But in respect to the gasification or any other projects, anybody else want to supplement?

Mr. Ekelund: There are no coal uses in the oil sands at present. I'm not aware of any companies looking specifically at that, but I know that there's some general interest in it. Where they're going: it appears at this time that the OPTI/Nexen project is looking at using the bitumen itself through their processes as fuel. As well, I believe that under our regulations – I would have to check this – the coke that's produced is required to be maintained as potential fuel. Finally, the projects that do have upgrading on-site, the upgrading, if they're using a coking process, generates natural gas as well so that they are small net users. So there are a number of things which are going on, and they're mostly, as the minister said, led by the price signal to look at these options.

The Chair: Thank you.

A brief one, Mr. Chase.

Mr. Chase: A very, very brief supplemental: what current practices is Alberta using in the extraction of coal-bed methane that would avoid, say, a Wyoming?

Mr. Melchin: Actually, you know, very different in this sense: Wyoming didn't have rules and regulations. They put out saline water, put it upon the surface. This is still natural gas. We have very stringent regulations in the developing of natural gas, of which this still is. It just happens to be in the coal seams, but it's natural gas. So there are very precise rules about managing water here that we handle every day in all of the conventional plays as well as in some of the natural gas in coal. The regulations do fit both, so we don't have that environment of what's happening in Wyoming. That hasn't been allowed in the past, and it's not being allowed in the future.

But the Horseshoe Canyon, one of the interesting things about this resource that's mostly at play right now: very, very nominal, in many cases little, if any, water at all in that zone. It actually comes out in a purer form than much of the natural gas that goes into your home. It comes out under lower pressure in many of the areas than what goes into your home. Actually, you couldn't find a better natural gas play than that Horseshoe Canyon. Some of the deeper zones in the Mannville area do have water; therefore, we have regulations in place about how you manage water. Water is not allowed to be just left and thrown on the surface and disposed and those kinds of things. It's unfortunate; that Wyoming story is really a very misleading misrepresentation of natural gas in coal. That is not the case of what's happening here in Alberta.

The Chair: Thank you.

Mr. Oberle, followed by the hon. Member for Edmonton-McClung.

Mr. Oberle: Thank you, Chair. The department's first goal is to secure benefits for Albertans. You mentioned in your introduction the word "fair" several times and in response to another question over here that the department collects a fair share of revenues generated from resource development. And, indeed, page 22 again speaks of "a fair share." Those of us with children know just how subjective the word "fair" can be. How do we know that we're collecting a fair share? How do you determine that?

Mr. Melchin: The real balance in that question is just trying to see how you maximize the economic opportunity and value for Albertans too. So there is an economic rent kind of formula. I'll have the department supplement more on the specifics.

Mr. Ekelund: Yeah. That's essentially the way that it's looked at. When determining whether or not we're collecting the appropriate share, we take a look at a number of representative plays. With natural gas, in one of our early reviews we took several hundred different plays; same thing with oil; same thing on the oil sands. We take a look at the various types of plays, large and small, and whether our royalty structures provide and are capturing a significant portion of the economic rent that's available. It's a recognized economics term that's used generally around the world in terms of setting appropriate structures. We capture the value through both the bonus bidding system and through a royalty that captures a large portion of that rent over the life of the play.

If we want to get into a more technical discussion of that, I'd be more than happy to do that with whoever is interested, or we could provide a written response.

The Chair: A written response to the clerk would be appreciated. Thank you.

Mr. Oberle: In your introduction and in response to other questions you talk about the changing market and, obviously, changing prices. Do you see at this time any need for a change in the royalty structure to respond to that?

Mr. Melchin: We have, certainly, and continue to monitor our royalty structures. I would say that in measuring the fair share, we still do participate in all the higher prices because it's a percentage. So even as price escalates, so do we get an escalation in our royalties, on the upside. They were fixed accordingly. In fact, one of the sliding scales of calculation is that our rate percentage that we recover is determined both by production – i.e., higher producing wells or lower producing wells – and also by price. So the higher producing wells plus price gets you to the maximum rate. In that sense you could have some lower producing wells with higher price that could start getting us there as well. So we are realizing that.

We have to remember that in most of our conventional sources we have very small producing fields in comparison to the world. Sometimes comparisons are made to Norway or Alaska. I don't have the numbers in front of me, but we are magnitudes, multiples smaller in production volumes on a well basis than those areas. What we're trying to encourage is that we get as much of that resource extracted as possible. So when you're having low producing wells, you have to have a royalty regime that also allows for economic rent that is a smaller amount for both the producer and for Albertans. In that sense I'd say that that's why I think we have struck a very fair balance on it.

Mr. Oberle: Thank you.

The Chair: Thank you.

Mo, followed by Mr. Ray Danyluk.

Mr. Elsalhy: Thank you, Mr. Chairman. The hon. minister in his initial presentation and also as appears on page 5 of the ministry annual report indicated that they "continue to monitor industry satisfaction" and that an independent survey in 2003 indicated that "overall [industry] satisfaction with the department was 84 per cent." Again, I am just a guest here and maybe as a new MLA almost naïve to some extent. Has the ministry conducted similar surveys of the public? I recognize the industry as maybe one customer of the ministry, but the public is probably a more important customer. So has a poll or a survey been conducted, or are you looking at maybe conducting one soon?

Mr. Smith: The department business plan does have a performance indicator that pertains specifically to Albertans' attitudes with respect to the energy industry, and – I think it was mentioned earlier – we've seen good results in terms of awareness amongst Albertans. But we are concerned that there isn't enough detailed understanding of the industry amongst the general public. So that is a concern for us, and it was identified earlier in our business planning processes.

Since Minister Melchin has joined us in the ministry, we've had extensive discussions about the need to communicate further with Albertans with respect to awareness about the energy industry and what it does for Alberta. We believe that that indication of overall awareness – and when I say "awareness," I mean awareness in the sense that the energy industry makes a large contribution to Albertans' quality of life. That's clearly understood by Albertans, but how that actually happens is an area we need to work on.

9:40

Mr. Melchin: One thing I'd like to just supplement on that question. One of the concerns I do have: what is it that Albertans would like to do with some of these resources? Take sour gas as an example. It's not a matter of which company is applying for an application; there are various applications before the Energy and Utilities Board at the present time. Clearly, sour gas is a lethal substance. This is not something you take lightly, and it's not something you would do without very stringent regulation. To answer the question: can you preserve the safety of the public? That's paramount. You wouldn't do something if you thought even one life was at peril.

Can you appropriately manage that substance? The only reason that I could say to you why you would ever choose to deal with a toxic substance such as sour gas is that it must, then, have some substantial benefits. Therefore, you've got to be able to balance: are the risks appropriately managed to realize the benefits?

One benefit in particular I would say to you is that – well, first off, there are about 6,000 sour gas wells around the province. They're all around communities, large cities. There are about a hundred wells I know, in particular, right around Calgary. Some of them are right inside the city boundaries of Calgary. They're all around our cities and neighbourhoods, and we've had decades of history of being able to manage this safely. You don't find people going in and drilling sour gas well after sour gas well without knowing how to appropriately manage this. The engineering is substantially improved as to the technology of managing this.

Some of the benefits in particular. For example, about a third of our gas is sour. Over $6 billion last year came in royalties on natural gas; a couple of billion dollars of that is royalties from sour gas. The dollar amount and the benefit is so large to Albertans, as to offsetting a variety of factors, that there are huge upside benefits. It also supplies good gas into your home. You take a toxic substance; you actually take and manage it and turn it into a benign and usable and very good fuel. So you manage also that aspect and turn it into a very safe commodity, that's used by all of us to heat our homes in very cold temperatures in this country. So there's a huge upside for Albertans being able to manage these things.

That's a challenge for our department, to be able to be out in front. Is this what Albertans would like to do? Is there satisfaction in managing those appropriate risks and benefits that are associated?

The Chair: Thank you.

Please proceed.

Mr. Elsalhy: My supplemental to the hon. minister: what I'm understanding from yourself and your deputy is basically an issue of communication. You want to, quote, maybe inform or educate the public as to what benefits they're reaping from the marketplace.

But another angle, maybe, to this is the rebates with natural gas.

In the report it says that the program with rebates "was launched in 2003" and "will continue over the next two years." Are there any assurances that it might actually continue after 2005-2006? Are we stopping at that point? Are we abandoning the rebate program, or are there other mechanisms that are being investigated now to offset some of those high prices?

Mr. Melchin: Well, that would get into some policy discussions which are outside of the scope of the public accounts for 2003-04. I would say that that policy was a three-year program which was by requirement to be reviewed, so that will be a future policy discussion.

The Chair: Thank you.
Mr. Danyluk, followed by Mr. Bonko, please.

Mr. Danyluk: Thank you very much. Mr. Minister, you spent a lot of time, you know, touching on some royalty issues from one aspect to another, from oil sands to gas. My question is maybe more of a holistic question, but let me ask it in such a way to say that we have different areas in the province, whether it be coal methane gas to regular gas deposits, the oil sands, the light oil, the heavy oil as we have in our area. Could you please tell me, maybe in generalities, the process of how you set some of these royalties and how they're accomplished?

Mr. Melchin: Not having been here in the past when the rates were actually established, I can't quite identify the process as to how to get there. I do know the principle, though, upon which those structures were based. They were based upon an economic rent, that you look at the profitability, of sorts, that's available in total and, therefore, what share of that should Albertans have versus the industry, recognizing that there are all risks in this question.

Therefore, that took in factors such as production, higher producing wells. Obviously, on a per-barrel basis of oil, if you have a higher producing well, more production, some of the costs are fixed. You know, your annual lease might be fixed. The drilling cost would be the same. Regardless of the production rate the drilling for that well would be the same. So if you have more production, you have more revenues coming off for the same amount of costs and, therefore, could pay a higher rent.

On the converse, with a low-producing well, you've still got a lot of those upfront costs, and there may be very little profitability to share with the industry and with Albertans. That's why there was a structure chosen to say that production was very instrumental because you would trap resources in the ground if you kept the same rates, the high rates of royalties. It would mean that there would be a loss for the companies. There would be no profits for the companies. Albertans would maybe take a higher percentage rate, but you'd shut it in, and therefore no one would realize anything. So that's why the volume of production became a very important factor, trying to maximize the amount of natural gas and oil that we could extract from it.

Similarly with price. That was the other way to offset. If you had low production, yet you had high prices, then obviously there's more profit that could be shared. So when determining volumes of production and price, those factors significantly increased the economic rent that was available to share among the industry for their risk capital and return on their investment and with Albertans for the ownership of those resources.

The other side of it is to attract capital. You've got to look at how you attract investment. You have to still be competitive in attracting investment from around the world. You know, this is in competition. There's oil and gas throughout the world. We still have to have a regime that's attractive to all of the countries in the world. In many measures we're actually viewed, some of the studies say, as being one of the most stringent regimes in the world, not the least.

So it's a matter of trying to find that right balance. There is no magic number that you could particularly choose. That's a general type of response.

Mr. Danyluk: I appreciate your comments, and I suppose my supplemental, if I may, Mr. Chairman, is in regard to: when we talk about initiatives for exploratory projects, how do we initiate incentives? Let me speak about heavy oil, as in my area. How do we initiate those incentives for the oil companies to have higher recovery, and with that initiative how does the royalty rate affect, you know, the future in that same field?

Mr. Melchin: I think that in this department, very different than most other departments, we have to remember that we are the owners of a resource and are trying to maximize the value of that resource and, therefore, investment in various policies.

We have, for example, a program that was put out as a royalty credit for $200 million for technology improvement. It was really to offset royalties that would be paid, to put dollars back into technology since technology is really the answer to us being able to maximize the potential of that resource. It's a technological problem in the conventional oils that we leave 73 per cent of the oil in the ground. It's a technology kind of question that we need to solve as to how to extract a higher amount of that under current economic conditions.

9:50

In the oil sands it's a similar kind of a question. It's what led to the generic royalty regime, actually, as a response to the attraction of capital to develop a resource that had substantially higher cost structures than normal conventional plays.

If there are any other specifics of programs, I'm not certain, Mike, if you'd want to . . .

Mr. Ekelund: I think I can probably help on that. In terms of the general question of how we look at each of the different characteristics of resources in different areas, when we look at the royalty structures, we look at what those characteristics are. For example, that's why the oil sands has a more classic resource rent tax kind of basis, because it takes a long time for the payout of the major capital.

We at one time did have an exploratory regime in the oil sands area, but that was a 1 per cent regime. When the generic regime was put in place, we did the analysis and determined that a 1 per cent regime with a 25 per cent after payout was still appropriate for exploratory because you still had that lower upfront royalty rate, but if it did turn out to be an economic and paying project, then it went to the 25 per cent automatically. So in the heavy oil sands area that still does account appropriately for that.

In other areas we break down the province into a number of different types of production characteristics. We have put in different regimes when we found that the production characteristics are such that they cannot handle the same type of regime. In fact, a number of the royalty reduction programs that have been identified are precisely for that. For example, if you put in a horizontal reentry well, what we found out was that in the economics of doing that, the royalty structure itself was enough to be a disincentive to do that. It no longer paid.

That's precisely why a number of these programs have been put in place. When there's simply not enough economic rent generated by the project for it to go ahead with the full royalty rate, it's been reduced so that we are better off in terms of getting those projects going ahead paying a lower amount of royalty.

The Chair: Thank you.
Mr. Bonko, followed by Mr. Rodney, please.

Mr. Bonko: Thank you, Mr. Chairman. Just to quote a little bit of history. Back in the early '90s there was a reduction to promote the industry during the low prices. Well, I think that given that the industry has seen record prices, would there be a reason not to bring that back up to the full price that was once there instead of remaining where it is now?

Mr. Melchin: I'd like to clarify. Which area are you speaking of? Is this gas or oil or oil sands or . . .

Mr. Bonko: Oil. It was a two-thirds reduction.

The Chair: Mr. Bonko, we have to restrict our questions from policy to issues that are in the annual report, please. I'm afraid, again, that's a policy question. If you could keep your question directed – these are the limited rules that we operate under – for the fiscal year 2003-04, please.

Mr. Bonko: Thank you, Mr. Chairman.

Mr. VanderBurg: Those questions would be appropriate, though, for question period.

Mr. Bonko: I appreciate that then.
On page 130 the Auditor General had a piece in there that the recommendation was not implemented. How was management making "effective decisions when program objectives are not clearly defined and performance measures are not . . ."

Mr. Melchin: Could I have you state what page number you're on again?

Mr. Bonko: That was page 130.
Again, if the recommendation is not implemented, how does management "make effective decisions when program objectives are not clearly defined and performance measures are not used to assess the results of the program?"

Mr. Melchin: I'm sorry. I'm just barely catching up to speed, so I'm going to defer to the department to see if they've got the answer to that.

The Chair: Well, if you would like to respond to that question in writing, you're quite welcome to.

Mr. Melchin: They may have the answer. I'm just barely getting to the page number.

Mr. Ekelund: I'm trying to find the specific page number.

Mr. Bonko: Page 130 of the Auditor General's report.

Mr. Ekelund: Oh, sorry. The ARTC.

Mr. Smith: We'll respond later on that one, I think.

The Chair: Thank you.
Your second question, please, Mr. Bonko, followed by Mr. Rodney.

Mr. Bonko: Well, it would be under recommendation 12 again. It was, "We again recommend that the Department of Energy document and communicate the objectives of the Alberta Royalty Tax Credit program and use measures to assess whether the program is meeting its objectives." Why didn't the department implement this recommendation from last year?

Mr. Melchin: I'll defer to the department, too, unless the Auditor General . . .

Mr. Dunn: Just for clarification. You're referring to recommendation 12 . . .

Mr. Bonko: Correct.

Mr. Dunn: . . . on what's known as the ARTC, the Alberta royalty tax credit, which relates back to 1974, when royalties were not allowed for income tax deduction. This program arose because of the federal/provincial conflict at that time, and this has been sitting there for many years. Maybe in answer to that, it is described in the financial statements of the department at $81 million. They've now disclosed that the impact of the ARTC is $81 million last year.
Maybe through the minister to the department.

Mr. Ekelund: Sorry; I was just trying to find out whether that was the ARTC versus the reduction programs. On the ARTC side we actually are working on criteria at this point so that we can put those forward and meet the requirements of the Auditor General.

The Chair: Thank you.
Mr. Rodney.

Mr. Rodney: Thank you, sir. I'm glad we're able to fit this in just before our witching hour.
So many of us are here for at least a couple of reasons, that being energy and environment. I know that people in my area are continually concerned with the balance. I keep hearing that word "balance." When I look outside the window, I think a lot of these buildings wouldn't be here if it wasn't for energy, and if it wasn't for the environment, there wouldn't be people in them. So we do have that fine balance that I think is demonstrated well in the annual report on page 49.
Amongst other statistics, we see that in 2003 the reduction in solution gas flared was 70 per cent from 1996, and the reduction in solution gas vented from 2000 was 38 per cent. Both of those numbers are parts of growing trends in very positive directions. I know it's a big concern that we do this safely, and, Minister, I must commend you and your department for making sure that the stakeholders do that. I'm just wondering what is being done or what was done in 2003 to make those numbers continue to improve and to address these concerns?

Mr. Melchin: I'll have the department respond on the specifics, but I would like to make one general comment, and that is, you know, there's a high level of support from industry to develop these resources I would say in a very sustainable way and with great recognition to all of the environmental impacts associated with the industry, to deploy the best technology, to deploy the best practices and available technology for extraction of those resources. All of us want to see that our environment is preserved for future generations. How do we, then, allow for the extraction of the resources while also preserving that environment?

But on the specifics I'll have the department . . .

Mr. Smith: I'll make a few comments, and then perhaps John can help me with the EUB's part. The Clean Air Strategic Alliance worked with industry to develop a program for addressing specifically the issue of venting. It was done on the basis that we set some very aggressive targets that industry would try and meet. We gave a period of time that would allow them to get their house in order to do that and then offered that if they didn't comply, we would see regulations come into play that would actually get their attention.

What has happened is that with that target being set, they have aggressively pursued it in the absence of regulation. In fact, the results are amazing to see, the extent of reduction up to 70 per cent in flaring and venting on a voluntary compliance program, which indicates to me the kind of activity that you can generate in the right direction without having necessarily the heavy hand of regulation in play.

John, I don't know if you want to supplement that or not.

Mr. Giesbrecht: I just concur. It's been driven by co-operation with industry, and technology is another piece.

Mr. Rodney: Okay. Just as a follow-up to that then. Am I hearing you correctly in thinking that there are no additional actions that are required to continue this positive trend of reducing flaring and venting? Are we on the right track, or is there more that can or should be done?

Mr. Smith: I think this is a continuing work-in-progress. The work that's been done to date shows that we clearly can see reductions. I believe that the CASA process would allow for a review of the results and a further recommendation, if warranted, to see additional reductions coming forward through that process.

What's key to all of this is that it was done jointly with the communities and with the industry to establish what were realistic targets. I'm sure that with the success that's been seen, if there's room for further improvement, it will be done.

Mr. Rodney: Excellent. Thank you very much.

10:00

The Chair: Thank you very much.

That concludes this portion of the meeting. I would like to thank the hon. minister and his staff for their time and attention this morning and also on behalf of all members the Auditor General and his staff as well. You're free to go if you would like. We have a few more items to discuss briefly on the agenda.

Mr. VanderBurg: I just have one comment that I wanted to make to the minister. In your opening statements you made some comments about the diversity of this Energy department. You know, I would hope that you remember one thing: oil and gas wells come and go, but diamonds are forever.

The Chair: And on that note, I would like on behalf of all members of this Public Accounts Committee to wish the hon. Member for Battle River-Wainwright the very best this weekend. I hope that he and his family have many years of happiness and prosperity and good health.

Hon. Members: Hear, hear.

Mr. Griffiths: Thank you.

The Chair: Now, we have a couple of housekeeping items at this time. Last week the clerk distributed this GOPAC memo. That is the Global Organization of Parliamentarians Against Corruption: Leading the Fight for Accountability, Transparency and Good Governance. One of the movers and shakers in this is the hon. MP for Edmonton-St. Albert, John Williams, the chairperson of the federal Public Accounts Committee. That's for your information.

I would like to briefly remind hon. members that I have received, and Mr. VanderBurg as well has been copied, a letter from the Minister of Agriculture, Food and Rural Development indicating a willingness to appear in the fall at our convenience when this committee meets. So that's just to note.

I would like to remind you that any time you would like to discuss the operations and the schedule of this committee, just see either myself or Mr. VanderBurg. The date of the next meeting is April 20, next Wednesday, and we're meeting with the Hon. Heather Forsyth, Minister of Children's Services.

If there are no other questions or other new . . .

Mr. Webber: Mr. Chair, I have a question, and that's with respect to the list you had made for these questions to the hon. Mr. Melchin. Were there names left over? I had thought I had indicated that I was on that list.

The Chair: Yes, there were. There was the hon. Member for Edmonton-Calder, yourself, and George VanderBurg, and Mr. Prins had indicated. If you would like to discuss at some point, the chair can certainly meet.

Mr. Webber: It seems to me that we pretty much have to get our names in almost immediately, before the meeting even starts, before we can have an opportunity to ask a question. That seems to be the case. I guess, first-come, first-served.

The Chair: No. The chair is at the will of the committee. If you would like shorter questions to the minister, if you would like the ministerial overview reduced from, say, 15 minutes to 10 or even five, that's at the discretion of the entire committee. If you want no preambles, that's entirely up to you, the members. I'm certain we could speed this up and have many more questions.

Mr. Johnston: We have members of this committee, and we have guests come in. You know, you folks are running this show, but it seems to me that we run out of time to ask our questions, and we have people that are visiting that are asking questions. Should it not be that the committee members get the time to ask their questions first?

The Chair: Well, in our Standing Orders all Members of the Legislative Assembly are welcome to participate in the process. It is the opposition's rotation that is being reduced, not the government members' when people appear and indicate a willingness to participate; for instance, today the Member for Cardston-Taber-Warner or Mo from Edmonton-McClung. It is the opposition's rotation that they are filling, not government members. The question rotation is set up opposition, government, opposition, government, so government members would not be losing their turn. If you indicate that you would like the process faster, then we could certainly do that.

Mr. Johnston: Is it just me, or does anyone else feel the same way?

An Hon. Member: I agree.

The Chair: Mr. Eggen was next.

Mr. Eggen: Yeah. I would like to suggest to each of us that we might consider shaving down the first part because we're reading, presumably, the department's report before anyhow. I mean, it's certainly appropriate to have an introduction, but I think we could take that down a bit. Then, again, using a timing system, you know, within reason to perhaps shave off some of the responses or even, I would say, the preambles of the questions would be appropriate. Volume is better, and I appreciate some of the different opinions in regard to your question.

The Chair: Thank you.

Mr. Danyluk: Mr. Chairman, my point is on a previous point. You specifically talked about it being this committee's option and directive to organize this meeting, and you answered the question by saying: well, when other members come in, it is still going to form in its rotation. But I think the way that I gathered the point, it was that regular members may not have that opportunity in that situation. Right? Let us just say that another person comes in, and they put their name ahead; you are going to acknowledge it.

The Chair: Well, if they're a member of the opposition. If it was a government member that came in . . .

Mr. Danyluk: No, no. But members of the opposition or not.

The Chair: Yeah, they're going to go on the list. They certainly will. The Standing Orders indicate that. The precedent was set last year. Reverend Abbott was participating in this committee.

Mr. VanderBurg: I think the point is, though, Mr. Chair, that the members are saying that Mr. Eggen is a member of our committee. We think that he should be higher priority than the Member for Cardston-Taber-Warner because he is a member of this committee and he is a member of the opposition, and we feel that he should rank higher on the list. So if he gets left out and the Member for Cardston-Taber-Warner doesn't, we'd rather have the Member for Cardston-Taber-Warner have his question in writing than Mr. Eggen.

The Chair: Okay.

Mr. VanderBurg: It's just a priority thing for members.

The Chair: We could do that, but I'd have to remind you that in Standing Orders – and we don't write the Standing Orders, but we're under their direction – clearly every hon. member of the Assembly is entitled to attend these meetings and participate. They just cannot vote. Those are the rules. We can go to any other committee, and we can participate if we wish.

Mr. VanderBurg: Well, I think Mr. Eggen made a good point. Why don't we just cut the preamble down and have the ministers to 10 minutes instead of 15 minutes?

The Chair: Ten minutes.

Mr. VanderBurg: Let's just try that. We'll perfect it.

The Chair: Okay.

An Hon. Member: Yeah. We'll try that, and then we'll see about that.

The Chair: And I will be much more diligent not only if there are lengthy preambles from certain members of this committee but also certain ministers, and we'll see if we can speed this up so everyone can participate to their interest.

Mr. VanderBurg: Yeah. And the '03-04.

The Chair: And the '03-04.

Mr. VanderBurg: That would help out.

The Chair: That would really help out.

Mr. VanderBurg: I think the issue is that most of us get more out of this than we do question period. There's some real good information being asked, and I think that we just want to make the best out of it.

The Chair: Yes.
Okay. So next week if you have any . . .

Mr. VanderBurg: The problem is Fred Dunn. I think that his report is way too long.

The Chair: Could I be excused for a second and ask for a motion for adjournment, please? Thank you, Ray. Moved by Ray Danyluk that the meeting be adjourned. All in favour?

Hon. Members: Aye.

The Chair: Thank you. Seeing none opposed, carried.
Thank you very much.

[The committee adjourned at 10:10 a.m.]