

Standing Committee on The Alberta Heritage Savings Trust Fund Act

Thursday, September 4, 1980

Chairman: Mr. Payne

2:40 p.m.

MR CHAIRMAN: Mr. Minister, on behalf of the members of the heritage fund committee who are here today, I would like to thank you for participating in our deliberations this afternoon. Before I invite the minister to make any preliminary comments he might feel are appropriate, I would like to indicate that there are perhaps four or five pages in the annual report that will be germane to our deliberations the balance of the afternoon. On page 6, there is an interesting graphic portrayal of Alberta's conventional crude oil profile; on page 15 is explanatory information on the Alberta Energy Company and the Syncrude equity; on pages 32 and 33, Schedule 2 of the Alberta Investment Division Investments, there is additional information tabulated. With that reminder, then -- Mr. Minister, did you care to make any opening comments?

MR LEITCH: Thank you, Mr. Chairman. I don't have any opening comments. I will be happy to deal with, as best as I can, any questions the committee may have.

MR R CLARK: Mr. Chairman, I wouldn't want the minister to feel we didn't have any questions for him. Mr. Minister, might I start by saying that in the annual report, page 15 reports a \$2.3 million dividend from the Alberta Energy Company to the heritage fund. Mr. Minister, being very direct and not beating around the bush at all, what will the effect be on the Alberta Energy Company if the federal government put in a natural gas export tax?

MR LEITCH: In my judgment, it would be serious. I say that without having any analysis done of that particular question, and I don't know how one could without making some assumptions as to size, timing, and things of that nature. As committee members will be aware, there is significant income to the Alberta Energy Company that flows from the sale of natural gas. Any export tax that may be imposed on natural gas has to be paid by the producer of natural gas and the provincial government, in the sense of reduced revenues to the producer and a reduced royalty revenue to the provincial government. In my view it's clear that an export tax cannot be added on to the sale price of the natural gas now being sold in the United States. In fact at current price levels, which are \$4.47 per MCF, there is considerable sales resistance in the United States as a result. It varies from area to area because of the competing energy sources. In some areas where Canadian natural gas is competing with heavy fuel oil, of which there is an abundance in the west coast, northwestern United States, or with cheaper electrical power from hydro, sales have dropped off dramatically. That has been particularly true of export sales from British Columbia, but it has also been true of export sales from Alberta.

MR R CLARK: A supplementary question to the minister. If the export tax were to come on, then in the future we would see a sizable reduction in the dividend that comes back from the Energy Company to the Heritage Savings Trust

Fund, going back to the \$2.3 million that came in this year? That's really what has to concern the committee at this immediate time.

MR LEITCH: I don't know that I would accept the sizable reduction in the dividend. As members of the committee would know, the size of a dividend is determined by the board of directors, and they take a number of factors into consideration. I think it more accurate to say that, in my judgment, there would be a reduction in the Energy Company revenues as a result of an export tax. I suppose in the ordinary business course one could make the next assumption that that would have an impact on dividend size. I say that with the caution that the size of a dividend is determined by many factors, only one of which would be the revenue from a particular economic activity of the company.

MR R CLARK: Mr. Chairman, one last question, somewhat beyond the scope of the committee and merely a matter of interest. Mr. Minister, the report is going around that the Energy Company would be the largest gas producer in the province that would be affected by a natural gas export tax. Are you, sir, in a position to verify that or make any comment on it?

MR LEITCH: Not without looking at the numbers. I'm aware that it's a large element in their revenue, but in comparison with other natural gas producers in the province -- I wouldn't want to rely on my memory. I'd like to go back and look up the numbers.

MR NOTLEY: Mr. Chairman, just on the question of a natural gas export tax, I notice on page 6 our composition of non-renewable resource revenue: 32% of it would be from natural gas royalties. No doubt with a natural gas export tax, that would also affect our bonuses and sales. Has there been any estimate -- it's very difficult not knowing what a natural gas export tax would be -- on the impact on our revenue, which of course will affect our heritage trust fund, of an export tax of, say, \$1 per MCF? I agree with the minister that it's going to come from two places, the producing companies and the government of Alberta -- possibly even a bigger share from the government of Alberta because of the impact on the bonus sales.

MR LEITCH: I have not had any studies done on that. You could only usefully do it by making a number of assumptions as to the timing, the size of the tax, and things of that nature. I have not felt such studies would be of any appreciable benefit to us. As members of the committee will know, we have been very vigorously opposed to an export tax on natural gas, on the principle that it is the equivalent of a federal royalty, if you like, on a provincially owned resource.

MR NOTLEY: Mr. Chairman, just to follow that up. I have been advised by IPAC people that we might be looking at about \$250 million or \$300 million lost to the province and about \$0.5 billion to the companies. Would that be ballpark figures of the potential?

MR LEITCH: I can't respond to that, because we'd have to know the size.

MR NOTLEY: At \$1 per MCF?

MR LEITCH: Well, again, one would have to just multiply that by the MCFs we export. I wouldn't comment on those figures. I don't carry in my head those numbers.

MR PAHL: Mr. Chairman, after considering the prospect of a man-made disaster as a natural gas export, I wonder if the minister could direct his attention to the sort of natural disasters that we suffered over the last summer with wild fires in our forests. I phrase the question with respect to the Pine Ridge Forest Nursery and its provision of something like 10 million seedlings a year. This is perhaps unfairly looking into the future, but could the minister indicate how that facility has met the need or met the projected need, in view of the rather disastrous forest fire year and the need, I assume, for more reforestation?

MR LEITCH: Mr. Chairman, first of all, the 10 million per year for seedlings is accurate, but I wouldn't want the committee to overlook that there is a further 10 million other than as seedlings. I am currently reviewing with members of the department the advisability of an expansion of that facility. We haven't completed the review yet. It may be that we will reach the conclusion that our capacity to provide additional stock for reforestation needs to be increased. I can't really speculate on what our conclusion will be, but we are certainly looking at it at the moment.

MR PAHL: A supplementary. I wonder whether there has been any thought given by the minister or his department toward recommending expenditures of heritage savings trust funds toward preventing such dramatic fire losses in the future. I realize it is in part an operating budget, but if we apply the principle that the Heritage Savings Trust Fund should provide for the future, perhaps there is an argument that could be made for heritage savings trust funds into a more comprehensive or more reactive fire prevention scheme for the province.

MR LEITCH: Mr. Chairman, I haven't been giving any thought to doing that with funds from the Alberta Heritage Savings Trust Fund. But we have been carrying out an extensive review of our fire-fighting capability which, in my judgment, serves us well in nine out of the 10 years. Going over our history, we find that about once every 10 years we get the kind of very serious fire circumstance that arose this year. Particularly we're looking at the question of whether we should increase what we call our initial attack crews. Our basic method of controlling fires is to discover them early and get a crew on site within half an hour, that kind of time frame. We have found that whenever we're able to do that, the success ratio is 90-some per cent in controlling them. But if a fire has been able to get under way or burn for any appreciable length of time, it is very, very difficult to bring under control. In some cases you're doing more of a guiding operation, controlling the flanks of the fire, as opposed to actually trying to put it out.

So we're examining whether it would be appropriate to increase essentially our initial attack capacity. If we reach the conclusion that we should recommend that, I would recommend that it be done with the normal fire fighting operating budget. I think we would be in difficulty in an accounting sense, if not for other reasons, trying to divide essentially the same operation between general revenue funding and heritage savings trust funding.

So I guess the short answer to the question is that we are taking a very close look at our fire-fighting capacity and may recommend increasing it, but if we do I had always contemplated doing it out of the General Revenue Fund, in the normal budgetary process.

MR R CLARK: Mr. Chairman, Mr. Leitch, last year when you appeared before the committee, you indicated that you had not yet had a chance to address your mind to whether or not to exercise the option to convert the Gulf Canada and Cities Service debentures held by the fund. As I recall, it is March '83 or '84 that a decision has to be made on that. I notice that the report appears

to maintain the status quo. Has the government reached a decision as to whether those debentures will be converted?

MR LEITCH: Mr. Chairman, that's really a question -- I remember dealing with it in an earlier appearance before the committee, but I think I dealt with it in my capacity as Treasurer. It is really a question for the Treasurer. I may have commented on it while Minister of Energy and Natural Resources, but it's really a question primarily, I think, for the Provincial Treasurer.

MR R CLARK: Perhaps I might try a second area, Mr. Chairman, and this question may get the same fate. It deals with the recommendation the committee made of a major investment into the Alaska pipeline. Recognizing that the prebuild is just now going ahead, what stage is the government at in its thinking as to this question of making a major investment in the pipeline?

MR LEITCH: Again, Mr. Chairman, I think that would be one that is even more directly within the Provincial Treasurer's ambit than the preceding question.

MR BORSTAD: Through you, Mr. Chairman, to the minister. I believe there was a statement made by the Minister of Energy for Canada that with the discovery of the Hibernia field, there would possibly be no need for any further expansion of the oil sands projects at this time. Will this have any effect on the allotments to AOSTRA?

MR LEITCH: It wouldn't have any effect on my recommendations with respect to the activities of the Alberta Oil Sands Technology and Research Authority. I hope that Hibernia fulfils the most optimistic expectations that we've heard to date. I think it would be a great thing for Canada and for the provinces immediately affected if that turned out to be the size of crude oil resource that some reports have indicated. But even if it did, in my judgment that doesn't affect the need for us to continue the kind of research work that is being done by AOSTRA in respect of the two areas in which it's now working: new technology in the deep sand primarily and technology designed to get additional volumes of oil out of our known conventional reserves. It wouldn't seem to me that major discoveries off the Atlantic coast or major discoveries in the north should alter the planned level of activity at all for AOSTRA. That is just something that is in our interest to get on with as expeditiously as we can.

MR NOTLEY: Mr. Chairman, just on the question of the impact of energy negotiations, one of the proposals that I recall the Alberta government made at the meeting with the Prime Minister a few weeks ago was with respect to a natural gas pipeline into Atlantic Canada. What priority does the government place upon that? Do we have any cost estimates? Would it be the type of investment for the heritage trust fund that would be a likely recommendation?

MR LEITCH: Mr. Chairman, I have a little difficulty responding to that when we get into the question of: is it a good investment, or is it a new investment that the Heritage Savings Trust Fund should take up. As I said a few moments ago to Mr. Clark, it seems to me that those questions are much more in the Provincial Treasurer's area than in mine. Looking at it from the responsibilities of my portfolio, I would be looking more at the question of the impact on the overall energy requirements of Canada, on the impact of that line on the industry within Alberta. That would be my prime responsibility. When we get to questions of whether such a line would be a sound investment for the fund, it seems to me I should pass those to Mr. Hyndman.

MR NOTLEY: Mr. Chairman, I could perhaps rephrase the question a bit to see if we can fit it into the minister's area of responsibility, because we are looking at the revenue to the fund; that's the other side. And the revenue to the fund involves markets. In that sense it is the minister's responsibility, to what extent there is an available market opportunity and would it be in the interests of the province, quite apart from the rights and wrongs of an investment in a pipeline *per se*, to proceed.

MR LEITCH: Mr. Chairman, in my view the proposal, which is really called the incentive natural gas pricing proposal, is one that is good for Alberta, and that of course was the reason we made it. It does open up significant new markets within Canada for Alberta natural gas, particularly the Q portion of the line, which would carry natural gas eastward from Montreal into Quebec City. We do have an incentive pricing plan which would be applicable for a period of nine years, with each annual volume of natural gas attracting a lower price, 65 per cent of the oil price on a BTU basis, calculated at Toronto, rather than the 85 per cent for flowing volumes. Each new volume of natural gas, calculated on an annual basis, would attract that lower price for five years. At the end of the five years, the price then goes up to the price for currently flowing volumes of natural gas.

I think there are other advantages to Canada, and in the sense that there are advantages to Canada they are also advantages to Alberta. That additional natural gas would push out oil and reduce our dependence on imported oil. Our estimates are that the Q portion of the line could push out as much as 100,000 barrels a day of imported oil. The quantities of oil that would be pushed out by the M portion of the line would be appreciably smaller.

So I think those are the principal advantages to Alberta. I think it's good for Canada that the more of Canada that is tied into a long-term, secure energy supply for domestic purposes, such as heating, the better it is for the whole of the nation, and that of course includes Alberta. From those perspectives I am very supportive of the incentive natural gas pricing plan.

MR NOTLEY: Mr. Chairman, unaccustomed as I am to supporting the government, I think that's a wise direction to follow too. The minister has indicated that the Q portion would reduce the import of about 100,000 barrels a day. I am interested in whether we have any figures on what both projects, the Maritimes and Quebec, would mean in terms of a market for natural gas itself in terms of our present production. It has been brought to my attention by some people in the industry that it would be relatively small, but it strikes me that at 65 per cent, there should be a pretty substantial market opportunity for natural gas conversion.

MR LEITCH: I can't give you the percentages because, again, I don't carry those figures in my head. Certainly we have them available. It's unquestionably a significant increase in the market, but I can't recall the percentages.

MR STEWART: Mr. Chairman, Mr. Minister, you mentioned earlier that heating fuel was a cheaper product or a more readily available product in the northwest states that our natural gas being exported there had to compete with. Is it more sophisticated refining processes that would utilize this heating fuel if natural gas replaced it in the eastern provinces and in the American states?

MR LEITCH: Essentially that is true. The refinery configuration determines the output of the barrel that goes through the refinery. Currently the refineries in North America are turning out more heavy fuel than the market

requires. That's certainly true of Canada. Incidentally a good deal of the heavy ends of the barrel come out of Petrosar. I think something like 84,000 barrels of oil per day goes into the inlet side of Petrosar and something like 65,000 barrels per day of the heavy ends come out the outlet side, of which we have to export about 35,000 a day to the United States simply because there isn't a demand for it in Canada. The same is true of the refinery configuration. In fact some of the oil that is now going to the United States, primarily from Saskatchewan, is going there because there isn't a refinery capability in Canada at the moment to handle it.

Changes are occurring in the refineries in North America -- there have been some recent announcements -- and those changes lead to less heavy fuel oil coming out the outlet side of the refinery. I regard the surplus of heavy oils in North America to be a relatively short-term phenomenon. I think that within a few years, refineries will change and we will find more of the barrel coming out in the form of gasoline and fuels of that nature where there isn't a surplus.

MR STEWART: One other question. Is this additional refining process an expensive process from the refining point of view, once the capital investment is in? Or is it mostly the capital investment that's holding back the refineries from changing over or upgrading, if you would call it that?

MR LEITCH: Mr. Chairman, I think it would be treading on fairly treacherous ground for me to get into the economics of refineries. I know the capital expenditures are large in order to change the nature of a refinery, but I'm not familiar with the operating cost differences that occur once you put the structural changes in place. It's an area in which I think wisdom requires me not to comment on any further.

MR NOTLEY: Mr. Chairman, just one other additional question, with respect to research into solar and wind energy. Where does that matter stand this year, Mr. Minister? How much are we allocating? Has there been any contact with the government of Saskatchewan? I believe they've got a Saskatchewan conservation house. What co-ordination is there, if any, or exchange of information between the two provinces on that matter?

MR LEITCH: Mr. Chairman, I can't recall the particulars of our support for solar research. We aren't doing any by funding from the Alberta Heritage Savings Trust Fund. We are supporting solar research in other ways, primarily through a fund that is administered jointly by the federal and provincial governments, research funding. I believe the report which would give the details on that was filed with the Legislative Assembly during the spring session. If my memory is wrong about that, the reports are filed periodically in any event with the Legislative Assembly.

With respect to the Saskatchewan project -- and I assume Mr. Notley is referring to the construction of some houses making use of solar energy. No doubt we are keeping abreast of that project and its results. Of course there are some differences between the Saskatchewan and Alberta situations, in the sense that Saskatchewan imports natural gas from Alberta to supply its heating requirements. As members of the committee will be aware, a very, very high percentage of the homes in Alberta are now using natural gas. So I think there is a difference in the factual situation between the two provinces.

MR R CLARK: Mr. Chairman, to the minister. Mr. Minister, what kind of research is AOSTRA involved in in helping develop viable technology for smaller scale oil sands plants?

MR LEITCH: I'm not sure that they're involved in smaller scale plants in the sense of smaller scale Syncrudes, which I assume is what your question referred to. Their prime thrust is in the experimental or research work which they hope will lead to economic recovery of the deep sand, which will be quite a different operation from the Syncrude or Suncor plants which, as members of the committee would know, deal only with the shallower sands. There may be some project which I can't call to mind that would fit the description of your question, but I'm not aware of it at the moment.

MR R CLARK: Perhaps I could broaden the question a bit. What I'm primarily thinking of is the kind of situation we have in the Cold Lake-Grand Centre-Bonnyville area. Either through AOSTRA or some other agency, are we involved in looking at the possibilities of not really having to have megabuck projects, but smaller projects which may be more economical?

MR LEITCH: The answer to that, Mr. Chairman, is that AOSTRA is giving consideration to that. But they use a little different phraseology in that it is a heavy oil upgrading facility, is really what they're talking about, which is somewhat different from an oil sands plant. There is no specific project that is going ahead, but a good deal of work is being done by AOSTRA on the question of whether they shouldn't proceed with some research project in that area. But it hasn't yet reached the point where they have selected a project and said, let's ask for approval of this. They're still exploring the area.

MR R CLARK: I take it from the answer, Mr. Minister, that AOSTRA is positively inclined if the economics and the proper project comes forward. Is that . . . ?

MR LEITCH: Yes. I think it would be accurate to describe the situation as being one that they feel something may need to be done and they are looking for the something that should be done. If a proposal or project comes forward that they feel would be one that ought to be proceeded with, I'm sure they'll be asking for approval to proceed.

MR R CLARK: Mr. Chairman, just following along from there, I had the opportunity to visit the project AOSTRA is involved in helping fund at Peace River and was very impressed. What is the state of the art as far as the oil sands or heavy oil, depending on the terminology, in the Wabasca-Desmarais area? I ask the question because from the standpoint of northern Alberta development, if at some time in the foreseeable future Peace River comes along and Cold Lake area goes ahead, then the Wabasca-Desmarais may be the next logical area. If it's in the report, I apologize if I missed it.

MR LEITCH: Mr. Chairman, I was just checking the report to see whether there is anything dealing with that particular area.

MR CHAIRMAN: I checked a few moments ago and couldn't find it.

MR LEITCH: No, I don't think there is, and I can't call to memory any particular bit of information about that. I would be happy to check on it if you would like and perhaps respond by memorandum to the Chairman of the committee.

MR STEWART: I've heard it said that plants that upgrade heavy oil have to have a capacity in the neighborhood of 100,000 barrels for them to be economically feasible to operate. Is this a factor that determines the size of a lot of these heavy oil projects that we're discussing?

MR LEITCH: There are knowledgeable people in the industry and in the research area who are considering whether the large plant is necessary to make it economic. I know there have been discussions within the department, discussions with AOSTRA, as to whether a pilot project of much smaller size, say 10,000 or 25,000 barrels per day, oughtn't to be proceeded with just to determine whether it is economic to have smaller sized upgrading plants.

MR STEWART: To supplement that question: the pilot plant at Cold Lake, Esso's project, is there a sharing of information between AOSTRA and Esso on the technology of the development of heavy oil in the Cold Lake area? Or are those two separate projects that are each going their own way?

MR LEITCH: I don't know that I can respond with respect to that specific project. The general situation in Alberta is that there is no requirement to make technology public. AOSTRA operates on the basis that the successful technology that may come out of any of the particular projects they are involved in will be shared with their industry partners, in the sense that the industry partner has the right to use, free of charge, that technology in their projects. AOSTRA has the right to market the technology to anyone else who may want to use it. So there is not a sharing, even by AOSTRA, in the sense that people are free to use the technology. If they're not part of the project, they acquire the right to use that technology by making some financial arrangement with AOSTRA.

MR R CLARK: Mr. Chairman, might I ask Mr. Leitch: what is the stage of negotiations between, well, Alberta and the companies in the Lloydminster area? For a number of years there has been talk of the possibility of some refinery or some project going ahead, be it in Saskatchewan or Alberta, negotiations with the federal government, PetroCan, and so on. What's the state of that whole heavy oil development in the area?

MR LEITCH: Mr. Chairman, so far as I am aware the most accurate way to describe that would be that the projects are in the discussion stage, the contemplation stage. There would be a number of things that I think would have to occur before they proceeded further, one of which would be pricing. What's the price that is going to be paid for the oil that comes out of the other end of the project? So I'm not aware of it having advanced beyond the discussion stage.

MR R CLARK: Mr. Chairman, I ask then for an update from Mr. Leitch on the Cold Lake project and the project north of Fort McMurray, the Alsands project. I suspect they're in very much the same kind of limbo.

MR LEITCH: Yes, I think it's accurate to say that, Mr. Chairman. Ever since I assumed the portfolio -- and these discussions were going on before I assumed the portfolio -- there have been continuing discussions with the Alsands group, and Esso Resources with respect to Cold Lake, on the commercial terms agreement, which is really the royalty agreement. That we worked at very hard, simply to ensure that we would be in the position that if the projects did receive approval to go ahead, there would be no delay caused by our then having to negotiate those agreements. So we've been working on that for the past year or so.

The state of those negotiations is such that, in my view, if an approval were granted for the projects to go ahead, I think they could be very quickly concluded. That agreement really determines, so far as the Alsands and Esso Resources group are concerned, the cost of the feedstock that goes into the one end of the plant.

The other key element that Alsands and Esso Resources need to know before they can make a decision whether to proceed is what the price is going to be of the oil that comes out of the other end of the plant. As members of the committee would be aware, the only offer that has been put out by the federal government with respect to that price is \$32 per barrel, escalating by the CPI increases. While I don't purport to speak for either Alsands or Esso Resources, I'm sure that that price would not be acceptable to them and would not be acceptable to Alberta. That is the next thing that has to occur before those projects can move forward: there has to be an acceptable price. That has not yet occurred, and discussions on that are not now going on between our government and the federal government. Until that did occur, until there were an acceptable price for the product that comes out of the plant, I think nothing else can occur.

MR R CLARK: Mr. Chairman, to the minister. What is the attitude or the position of the government of Alberta about the possibility of, say, a separate agreement for synthetic crude coming out of those two plants, to get those two projects going prior to an agreement being worked out between the federal government and Alberta on the larger pricing question?

MR LEITCH: Mr. Chairman, I guess what we're into now is sort of a hypothetical question as to what the government's position might be if a certain set of circumstances came about. I really have not put my mind to that because the need to do so has not yet arrived. I think first of all we have to have the pricing that's acceptable, and there is little point in deciding these other questions until there is some indication an acceptable pricing arrangement might be worked out. So I really don't hold an opinion or a view on it now. It's just something I haven't thought about.

MR R CLARK: Mr. Chairman, to the minister. Mr. Minister, can I put it this way: as a result of the failure of the federal government to move with much substance on this question of pricing, I take it the Alberta government is not prepared to attempt to work out a separate agreement for synthetic crude to enable those plants to go ahead. I take it, Mr. Minister, when you indicated to the committee that it's something you hadn't addressed your mind to, that it's not something Alberta is prepared to consider.

MR LEITCH: I don't know that I can expand on my earlier answer. We're not there; it's not a question that has arisen. I'm sure members of the committee would all be aware that you probably can't deal with that question in isolation. It will be an entirely new scene or new scenario, depending on what the federal government may do with respect to energy matters. And that we're not going to know, obviously, for a while.

MR CHAIRMAN: Any further questions of the minister? Mr. Minister, on behalf of the committee I would like to thank you for participating with us today. This committee will now stand adjourned until 10 a.m., Wednesday, September 10.

The meeting adjourned at 3:25 p.m.