BRITISH COLUMBIA'S OIL AND NATURAL GAS ROYALTIES

CANADA'S OIL & NATURAL GAS PRODUCERS

OVERVIEW

Natural gas and oil development has been an economic cornerstone of British Columbia since the 1950s. Development of these resources is a partnership among industry, Indigenous peoples, and government, which creates more than 10,000 jobs in the province and provides government with hundreds of millions of dollars annually to help provide the services British Columbians rely on every day.

Technology and expertise to develop the province's resources have advanced over the decades and increased the volume of economically recoverable natural gas in British Columbia. This has resulted in increased private investment, well-paying, high-quality jobs, growing provincial revenues and investment in research and development.

Global energy demand is expected to reach pre-pandemic levels in early 2023, while natural gas is expected to see a dramatic increase of 30 per cent by 2040. With over 575 trillion cubic feet (Tcf) of remaining marketable potential of natural gas in B.C., the province has an opportunity to meet rising global energy needs. The success of B.C.'s industry is strongly shown through its environmental performance. From 2011 to 2019, emissions intensity decreased by 33 per cent. During the same period, natural gas production in B.C. doubled. Improved emissions management, particularly actions aimed at achieving methane emissions reduction targets and multi-well drilling pads, are key drivers in emissions intensity reduction in this sector.

In B.C., the upstream oil and gas industry is a partnership among industry,Indigenous peoples,and government, which creates more than 10,000 jobs in the province and provides government with hundreds of millions of dollars annually.

BRITISH COLUMBIA'S RESOURCE: DEEP AND TECHNICAL

Since 2002, the British Columbia royalty regime has been structured and implemented to maximize the public share ("economic rent") collected from produced natural gas and oil, while ensuring producers can earn a fair return on investment. The regime consists of several targeted programs to address specific characteristics of the resource. Programs are designed to encourage additional investments, including building the extensive water and natural gas treatment facilities required for production, as well as investments in clean technologies to further improve environmental performance.

The Deep Well Royalty Credit Program is targeted to attract investment and promote the development of B.C.'s extensive and deep unconventional resource. Today, most of B.C.'s natural gas and oil resources, such as those in the Montney Basin and Horn River Basin shale formations, are found at very deep locations, approximately 1.4 to 3.8 kilometers underground. Accessing resources at these depths requires extra effort and cost, and it's for this reason a well-established royalty credit program was developed to stimulate private investment in the development of the province's publicly owned resources. In exchange for a defined amount of royalty deductions to cover the extra development cost of B.C.'s deep resources, industry invests heavily into the province, an average of more than $5 billion annually. The upstream natural gas and oil sector is the third largest investor in B.C. after transportation and infrastructure and utilities. Royalty programs do not require any upfront investment of public money, and these industry investments have generated significant government revenues. As a result of B.C.'s competitive royalty system, billions of dollars of new private investment flow into the province annually and industry pays hundreds of millions of dollars in royalties each year. These royalties are paid in addition to corporate taxes, property taxes, and sales taxes.

Companies must commit significant new capital into developing B.C.'s deep natural gas and oil resource to be eligible to earn royalty credits to offset the higher drilling and completion costs associated with deep wells. If the well failed to produce any natural gas, the credits can never be used and have no value. Since the Deep Well Royalty Program's inception in 2003, government reports indicate that industry has accumulated approximately $2.9 billion of unused deep well royalty credits. Any newly drilled producing well in B.C. always pays a minimum royalty. Once the earned deep well credits are deducted to zero over time, standard royalties continue to be paid. The accumulation of this type of royalty credit is an indicator of low commodity prices, which have negatively impacted both producers and government revenues. Even at low prices, however, millions of dollars of royalties are paid monthly and represent an important and ongoing source of revenue needed to help fund government services. For the resource owner and investor, the risk and reward represent a fair exchange.

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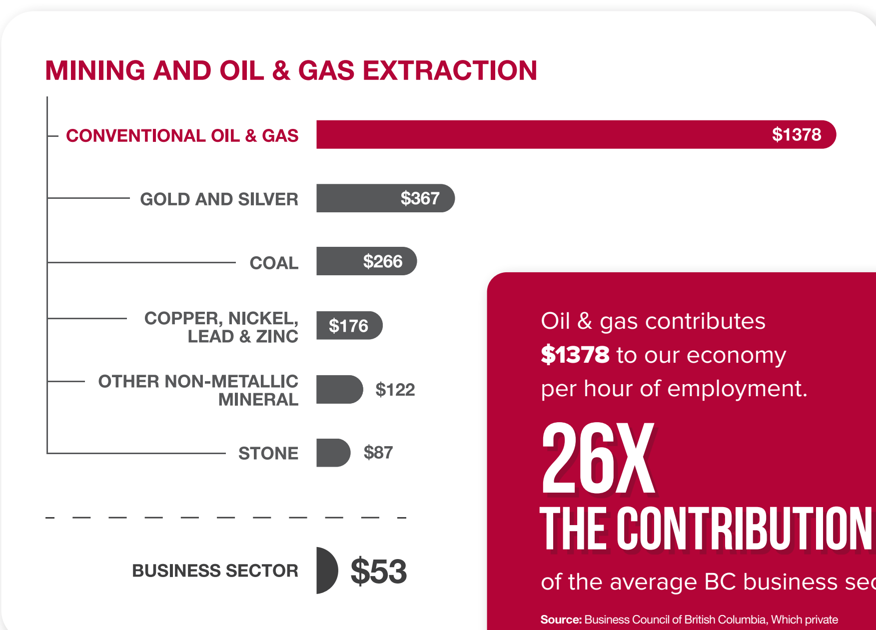

Oil & gas contributes **$1378** to our economy per hour of employment.

26X THE CONTRIBUTION

of the average BC business sector.

Source: Business Council of British Columbia, Which private sector industries "pay the bills" for British Columbia?, July 2020

According to a Business Council of British Columbia study titled "Which private sector industries pay the bills for British Columbia?" oil and natural gas jobs are the most productive jobs in B.C.'s economy by the measure of real GDP per hour work.

GOVERNMENT ROYALTIES REFLECT MARKET CONDITIONS

The value of royalty payments the B.C. government receives from natural gas producers is determined by the volume and price of natural gas as set out in the Petroleum and Natural Gas Royalty Regulation. When prices are high, government benefits by collecting more royalties and when prices are low the converse is true. This demonstrates a well-balanced, competitive risk-sharing mechanism between resource owner and industry. Even with increased industry activity, more jobs and greater volumes being produced, falling natural gas prices can result in lower total royalties. As the price of drilling a well generally does not fluctuate with the price of the commodity, this arrangement results in risk sharing between the resource owner and the producers. As global natural gas prices continue to rise due to pressures inflicted by Covid-related supply bottlenecks, B.C. has an opportunity to alleviate these pressures and rising inflation, while paying for innovation, infrastructure, and services if changes to the royalty regime remain competitive.

Changes made to British Columbia's Royalty Regime must maintain a competitive fiscal environment, or risk losing investment at a time when the economy has an opportunity to recover stronger and reduce growing government debt. Capital investment shifting to other jurisdictions (referred to as carbon leakage), would result in worse environmental outcomes globally, fewer jobs for British Columbian workers and reduced government revenues.

The Government of British Columbia must consider four key elements when revising the current Royalty Regime:

1. Maintain B.C.'s competitiveness to create jobs
2. Support the B.C. low-carbon advantage
3. Identify feasible ways to share economic opportunities with Indigenous peoples, while continuing to grow relationships based on trust and respect
4. Keep producing affordable energy and economic growth for British Columbia.

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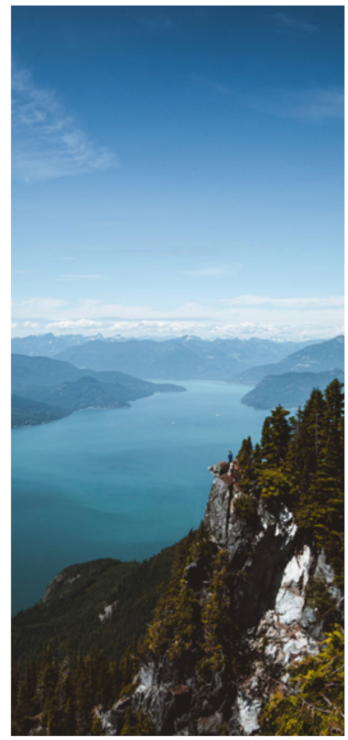

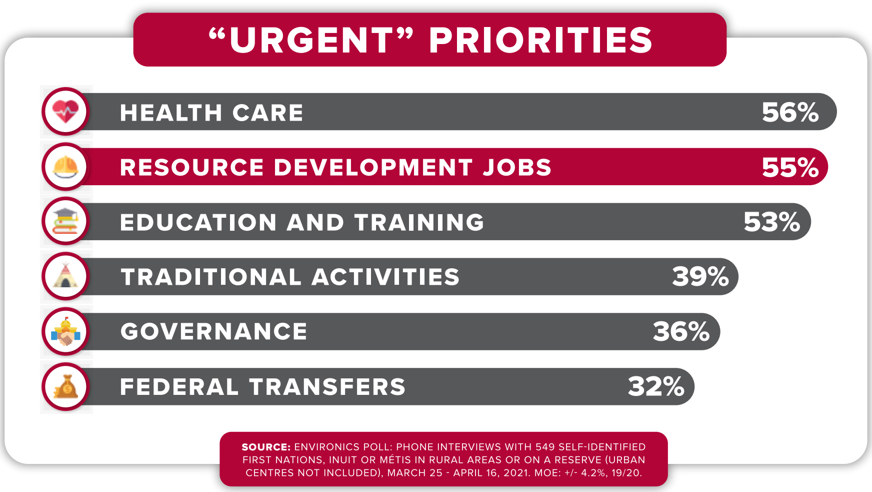

Did you know?
Resource Development is one of the highest priorities for Indigenous communities.

[1] IEA's World Energy Outlook 2020 for Natural Gas
[2] https://www.nrcan.gc.ca/our-natural-resources/energy-sources-distribution/clean-fossil-fuels/naturalgas/shale-and-tight-resources-canada/british-columbias-shale-and-tight-resources/17692
[3] Source: CERI 2019