Nova Scotia Oil and Gas Corporate Taxation Summary

(Effective February 2008)

Framework

Corporate taxation of oil and gas activities both offshore and onshore Nova Scotia is comprised primarily of the following:

- Federal and Provincial income taxes on a corporation's taxable income (taxable income being determined in identical fashion federally and provincially);
- Provincial capital tax on a corporation's taxable capital employed;
- Federal / Provincial harmonized consumption tax (the Harmonized Sales Tax) on taxable goods and services.
- Commercial goods brought into Canada are subject to customs duty and the 5% Federal portion of the Harmonized Sales Tax, unless they are exempt or free of duty. Imports from countries such as the United States that have a free trade agreement with Canada would not be subject to customs duties. Of particular note for the oil and gas industry, there is a special holiday until May 2009 on customs duties for mobile offshore drilling units.

In addition to these forms of taxation, the Province of Nova Scotia collects a royalty on oil and gas production. Refer to the separate summaries of Nova Scotia's offshore and onshore petroleum royalty regimes.

Income Tax

Canadian Federal and Nova Scotia corporate income taxes are administered by a single agency: the Canada Revenue Agency (CRA).

Base

The base for Corporate Income Tax (CIT) is the federally defined and determined Corporate Taxable Income (CTI). Nova Scotia CIT is composed of CTI generated solely in the province by firms that do not conduct business in other jurisdictions and allocations of CTI to Nova Scotia by firms that operate in more than one jurisdiction (multi-jurisdictional firms). Nova Scotia rates are applied to the CTI allocated to Nova Scotia to determine gross provincial CIT. Provincial credits reduce gross CIT. Note that offshore and onshore Nova Scotia are separate jurisdictions for CIT purposes with the same rates applying in both.

Allocation

The allocation of multi-jurisdictional CTI is based on federally defined formulas. These formulas are proxy measures of the actual business activity generated and are intended to reflect the level of business conducted in a jurisdiction. The formulas are based on the existence of a Permanent Establishment (PE): - Fixed place of business - Authority to contract, or - Inventory order fulfillment - Use of substantial machinery - Rental income The hardest question to answer is whether there is a PE in a province. Essentially it comes down to whether there is a body or activity in place with an ability and authority to generate or contribute toward revenues or the business purpose. The most commonly applied allocation formula is the 1/2 of the ratio of allocated salaries and wages to total salaries and wages plus 1/2 of the ratio of allocated gross revenues to total gross revenues. The denominator in each might be the national or worldwide total depending upon whether or not the firm is Canadian resident.
Gross salaries & wages are allocated to where they report and usually involve less allocation issues because direct links are more readily identifiable. Gross revenues can be difficult to allocate. Federal rules typically use destination of the sale, the origin of negotiation or manufacture tests to resolve the allocation dilemma.

Rate

Federal CIT is calculated on a corporation's taxable income.

YEAR	CORPORATE INCOME TAX RATE
2008	19.5%
2009	19.0%
2010	18%
2011	16.5%
2012 & onward	15%

Nova Scotia provincial CIT is calculated at a rate of 16% on CTI allocable to either the onshore or offshore Nova Scotia tax jurisdictions.

Oil and Gas

In addition to the general summary above, highlighted below are further details on corporate income taxation of particular relevance to oil and gas producers:

- Federal income tax payable may be reduced by an investment tax credit of 10% earned on qualifying expenditures in Atlantic Canada. Qualifying expenditures include, among other things, the acquisition of buildings, machinery or equipment primarily for use in oil and gas exploration or production. A special concession is made to Canadian controlled private corporations to allow for 40% of the tax credit to be refunded regardless of the amount of federal tax payable.

- Depreciable property used in oil and gas activities is deductible for tax purposes by claiming capital cost allowance (CCA) on a declining balance basis. The CCA rates of relevance to oil and gas producers are as follows:

Class	Expenditures	Rate
41	• oil and gas well equipment	25%
8	• other tangible equipment	20%
10	• computer hardware and system software	30%
49	• pipelines not part of a gathering system	8%

- Special resource related deductions are available in respect of certain expenditures not qualifying for capital cost allowance. These discretionary deductions are computed on a declining balance basis as follows:

Category	Expenditures	Rate
Canadian Oil and Gas Property Expense (COGPE)	• oil and gas rights and royalty interests	10%
Canadian Exploration Expense (CEE)	• geological, geophysical, and geochemical	100%
	• drilling / completion of dry holes or discovery wells	
Canadian Development Expense (CDE)	• drilling / completion not otherwise included as CEE	30%

• Provincial royalties are deductible in determining taxable income.

• Special rules have been developed within Federal tax legislation to allow for the transfer of unclaimed resource related expenditure balances to another corporation (the "successor corporation" rules) or to a corporation's shareholders (using flow-through shares).

Capital Tax (Large Corporations Tax or "LCT")
Capital tax is a tax on corporate capital. Nova Scotia's general capital tax is deductible against federally determined Taxable Income.

Base
The base for LCT is basically all of the firm's debt and owner's equity less any current debt; essentially the long-term financial capital that makes up the firm:
- Capital Stock - Retained Earnings and contributed surpluses - Loans and advances to corporation - Debt with term greater than one year Less: - Investment allowance The capital base is reduced by the Investment Allowance for investments in other corporations to prevent double taxation of capital.
Allocation

Similar to CIT, Nova Scotia LCT is calculated separately for onshore and offshore Nova Scotia. Nova Scotia LCT is calculated on an allocation of national or worldwide Taxable Capital. The allocation of Taxable Capital to provinces is calculated using the federal Corporate Taxable Income (CTI) allocation factors. Where a firm is related to other corporations the Taxable Capital is determined for the total group. This total then becomes the base to determine the provincial rate and capital deduction eligibility.
Rate & Threshold

Typically LCT is only applied to firms with capital over a certain threshold. For Nova Scotia the rates are as follows:
-Under $10 million: $5 million deduction & 0.50% -$10 million and over: no deduction & 0.25% For firms with Taxable Capital of all related firms totaling less than $10 million the 0.50% rate is applied to the allocation of net Taxable Capital to Nova Scotia (either offshore or onshore). For firms with over $10 million in Taxable Capital of all related firms there is no deduction and the rate is 0.25% on the allocation of Taxable Capital to Nova Scotia. The 0.50% rate and the 0.25% rate are scheduled to decline by 0.05 and 0.025 percentage point increments respectively on July 1 for each of the next three years. The LCT is scheduled to expire entirely on July 1, 2009.

Harmonized Sales Tax (HST)

- A corporation is required to collect HST at the rate of 13% on all taxable goods and services provided within Nova Scotia. A corporation may offset the HST collected in a reporting period with HST paid on purchases of goods and services in the period. Any excess collected is remitted while any excess paid is refunded. HST paid by a corporation is fully recovered through this process.

- Joint venture partners may elect to have the venture operator administer HST in respect of the venture's activities.