



Offshore Petroleum Royalty Regime

Overview

Nova Scotia has an Offshore Petroleum Royalty Regime that is based upon revenues and profits. The regime is designed to recognize the inherent risks involved in offshore oil and gas exploration and production. The regime provides arrangements for the current Sable Offshore Energy Project and the Cohasset-Panuke Project, as well as a generic formula for future projects. The generic royalty regime is explicitly designed to encourage risk-taking by offering lower royalties for the first project in a new area - a so called **High risk project**.

Authority

The authority for the Government to put in place regulations that set royalty levels for oil and gas projects in the offshore Nova Scotia area comes from the Offshore Petroleum Royalty Act. The Act also provides for royalty agreements to be put in place between offshore production license holders and the government of Nova Scotia.

In July of 1999, the government of Nova Scotia signed formal royalty agreements with each interest owner of the Sable Offshore Energy Project. At the same time, generic royalty regulations were put in place that would apply to future offshore oil and gas projects. The SOEP royalty regime and the generic royalty regime each stipulate that royalty will be a function of both the value of petroleum leaving a project boundary as well as profits associated with the operation of a project.

Royalty is initially set as an increasing percentage of gross revenues before it switches to increasing percentages of net revenues. Royalty rates increase with project profitability. Once net revenue royalty levels are reached, royalty cannot be less than a specified level of gross revenues.

Royalty Terminology

Gross Revenues (GR): The value of petroleum leaving the boundary of an offshore project.

LTBR: Long Term Government of Canada Bond Rate (10 year).

Net Revenue (NR): The gross revenue of a project less the costs associated with getting the petroleum to the project boundary.

Return Allowance (RA): A percentage of unrecovered project costs. Once simple payout is achieved, the return allowance ceases to be calculated.

Simple Payout: The point at which project revenues first reach or exceed the sum of allowed exploration costs, capital costs, operating costs and royalties paid. Corporate income tax is not an allowed cost for royalty purposes.

Sable Offshore Energy Project Royalty Regime

	GROSS REVENUE ROYALTY
Tier 1	1% GR, 36 month period
Tier 2	2% GR, until simple payout + RA based on 5% + LTBR
Tier 3	5% GR, until simple payout + RA based on 12.5% + LTBR
	NET REVENUE ROYALTY
Tier 4	30% NR, until simple payout + RA based on 45% + LTBR *
Tier 5	35% NR *

* minimum of 1% or 5% of GR payable depending on average gas price.

Generic Royalty Regime

ABASE REGIME[®]

	GROSS REVENUE ROYALTY
Tier 1	2% GR, until simple payout + RA based on 5% + LTBR
Tier 2	5% GR until simple payout + RA based on 20% + LTBR
	NET REVENUE ROYALTY
Tier 3	20% NR until simple payout + RA based on 45% + LTBR *
Tier 4	35% NR *

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	GROSS REVENUE ROYALTY
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Tier 1	2% GR until later of 2 years or simple payout + RA based on 5% + LTBR
Tier 2	5% GR until later of 3 years or simple payout + RA based on 20% + LTBR
	NET REVENUE ROYALTY
Tier 3	Same as Tier 3 of BASE REGIME *
Tier 4	Same as Tier 4 of BASE REGIME *

AHIGH RISK^e

	GROSS REVENUE ROYALTY
Tier 1	Same as Tier 1 of BASE REGIME
Tier 2	Same as Tier 2 of BASE REGIME
	NET REVENUE ROYALTY
Tier 3	20% NR *

* Minimum of 5% GR payable

For projects that fall under the Base Regime, only successful finding costs are allowed costs for royalty purposes. For projects that fall under the Small Oil or High Risk regimes, in addition to successful exploration costs, unsuccessful exploration costs associated with the project may be allowed costs for royalty purposes.

For more information on royalties onshore and offshore Nova Scotia including areas designated as High Risk for royalty purposes, please contact:

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