



CANADIAN ASSOCIATION
OF PETROLEUM PRODUCERS

December 17, 2007

The Honourable Richard Hurlburt, Minister
Energy Strategy/Climate Change Action Plan
Department of Energy, Government of Nova Scotia
400-5151 George Street
P.O. Box 2664
Halifax, NS B3J 3P7

Dear Minister Hurlburt:

RE: Nova Scotia Energy Strategy and Climate Change Action Plan

The Canadian Association of Petroleum Producers (CAPP) welcomes the initiative of the Government of Nova Scotia to update its Energy Strategy and develop a Climate Change Action Plan for the province.

Attached is a submission outlining some suggestions and ideas for your consideration. Our submission focuses on the immediate need to attract offshore exploration activity to the region to help build a sustainable petroleum industry in Nova Scotia. We recognize that Government is working hard to implement policies and programs to try and attract more investment in the Nova Scotia offshore. CAPP applauds these efforts and offers some additional ideas related to incentives and regulatory improvements which may help make Nova Scotia more competitive for investment.

The submission also provides some views related to implementing climate change policies. The offshore natural gas industry holds a relatively low share of the greenhouse Gas (GHG) emissions in Nova Scotia. In fact, it is widely accepted that natural gas production can play a key role in the solution to reducing GHG emissions. Nonetheless, we are pleased to offer some perspectives on climate change policy in the context of the competitiveness of the global petroleum industry based on lessons learned in other jurisdictions. CAPP members share concerns related to climate change and the need to reduce GHG emissions and integrate these concerns into their business decisions.

We hope you find the attached submission helpful. CAPP members with interests in the Nova Scotia offshore fully endorse the content of this submission and its transmittal to the Government of Nova Scotia. Should you wish to discuss or clarify any of the issues raised in this submission, please contact me at (709) 724-4202.

Sincerely,

R. Paul Barnes
Manager, Atlantic Canada

Attachment

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CANADIAN ASSOCIATION
OF PETROLEUM PRODUCERS

SUBMISSION

**Response to the “Consultation
Paper: Nova Scotia’s Renewed
Energy Strategy” and “A Background
Paper to Guide Nova Scotia’s Climate
Change Action Plan”**

December 2007

The Canadian Association of Petroleum Producers (CAPP) represents 150 companies that explore for, develop and produce crude oil, natural gas, gas liquids, oil sands and elemental sulphur throughout Canada. CAPP members produce approximately 95% of Canada's natural gas and crude oil. CAPP also has 130 associate member companies providing a wide range of services that support the upstream oil and gas industry. CAPP's mission is to enhance the economic well being and sustainability of the Canadian upstream petroleum industry in a socially, environmentally and technically responsible and safe manner. This mission is reflected in the operating practices of our members.

For more information: Please contact Paul Barnes, Manager, Atlantic Canada at (709) 724-4200. This document is also available on our website at www.capp.ca.

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INTRODUCTION

The Canadian Association of Petroleum Producers (CAPP) is pleased to participate in the consultation process for Nova Scotia's Renewed Energy Strategy and Climate Change Action Plan. The timing for this consultation process is appropriate given the critical issues around climate change which have been at the forefront of public attention recently and the need for a revised Energy Strategy which more accurately reflects the current state of the energy sector in Nova Scotia.

Nova Scotia's offshore oil and gas industry is an important part of the provincial energy sector and an important contributor to the local economy. Nova Scotia currently has one offshore natural gas project in production - the Sable Offshore Energy Project operated by ExxonMobil Canada Corporation. Another natural gas development, Deep Panuke, recently received project sanction by EnCana Corporation's Board of Directors. The regulatory approval and project sanction for the Deep Panuke project is a critical milestone for Nova Scotia's offshore industry. In 2001 when the Nova Scotia Energy Strategy was first developed Nova Scotia's offshore was viewed to be a highly prospective area which would see tremendous growth. Today, as the Consultation Paper states, the realization has set in that "the geology of our offshore energy resources has not been as well understood and predictable as expected." Downgrading of reserves at Sable and a lack of exploration success in the offshore in recent years has led investors to question the prospectivity of the area which is a key issue for the future of Nova Scotia's offshore petroleum industry.

The petroleum industry, while small compared to other jurisdictions, is still a key driver of the provincial economy in Nova Scotia. Besides personal income taxes and the Harmonized Sales Tax, petroleum royalties are the largest provincial source of revenue for the Provincial Government. Given the positive economic impact that the industry is having on the province, working to build a sustainable petroleum industry in Nova Scotia is a worthy undertaking.

Creating a sustainable economy is a theme that is apparent throughout the Consultation Paper. Several years ago when Nova Scotia's offshore industry was experiencing multiple exploration programs and associated activities, the link between creating a sustainable economy and creating a sustainable oil and gas industry was clear. Oil and gas was seen as the industry which would provide opportunities and benefits for Nova Scotians for generations to come. Today, Nova Scotia is experiencing low levels of exploration activity and production at Sable will begin to decline in 2008. There has been some good news with the sanction of the Deep Panuke natural gas project but beyond that there are no major developments on the horizon. This does not mean the link between creating a sustainable economy and creating a sustainable oil and gas industry is no longer apparent. It does however mean that in order to keep the benefits associated with natural gas flowing into the economy, and develop a sustainable industry for future generations, more has to be done to attract exploration and build the industry.

The region is high-cost and high-risk and exists in a competitive market for industry investment. Future offshore gas development in the province depends heavily on encouraging industry to continue investing to identify and develop new resources. The challenges facing industry in today's competitive environment means it will take government action to stimulate

exploration activity and to encourage investment. The Province must respond to this challenge and, in particular, consider measures such as incentives to enhance the competitiveness of the Nova Scotia offshore to stimulate exploration activity and continued development. Meeting this challenge will help create wealth for the Province, secure employment opportunities for Nova Scotians, and sustain the oil and gas expertise accumulated in the last decade. If this challenge is not met, the industry will be less inclined to invest in the Nova Scotia offshore. In our view, sustainability can best be accomplished by:

- encouraging more exploration to enable more discoveries;
- achieving regulatory efficiency;
- tackling key issues associated with skills, education and training;
- conducting operations in an environmentally responsible and safe manner; and
- advancing shared research and development priorities, which benefit the Province and industry.

CAPP's submission will provide ideas and input into each of these areas. While we recognize that Government's plan is to renew its energy policy and develop a separate Climate Change Action Plan, this submission will provide our input into both documents. CAPP represents the upstream petroleum industry (exploring, developing and producing) therefore our submission will focus only on the areas of the Consultation Paper which may affect the upstream petroleum industry, and the Nova Scotia offshore in particular, and provide suggestions on ways the Nova Scotia Government can help build this industry.

Our comments are made in the context of the global oil and gas industry. It is important to understand the global environment the petroleum industry operates within, in order to ensure that any policies or actions stemming from this process are made in the interests of ensuring that Nova Scotia is competitive for investment internationally. To put this in perspective, Nova Scotia is competing with other jurisdictions around the world – many with more attractive international investment prospects, growing political and regulatory reform and lower exploration risk. In Canada alone we are seeing provincial governments reducing corporate income tax in some cases and eliminating capital tax to attract further industry investment. Finally, Canada's offshore operating areas, including Nova Scotia, are some of the most high-cost operating environments in the world.

The best way Nova Scotia can compete for investment from the oil and gas industry is to focus on making the area as attractive to national and international investors as possible. In addition to the five key areas identified above that our submission will focus on, there are other principles which come into play when attracting investment. Creating an attractive investment climate means defining and maintaining a positive, predictable and stable regulatory environment, avoiding policies that impede free market principles and avoiding policies which add time and complexity to energy developments. It also means maintaining fair and predictable fiscal regimes and stability and certainty with regard to energy policy. CAPP believes that these principles should be central to the Energy Strategy update and creation of the Climate Change Action Plan.

Finally, in addition to the comments found in this submission, CAPP would encourage the Government of Nova Scotia to continue working to promote the province as a good place to do

business. Changing policy to make the area more attractive for investment is only the first step in building the industry. Demonstrating Government's commitment and desire to attract investment by meeting with key players in Calgary, Houston and other centers where corporate offices of oil and gas companies are located and investment decisions are made should be included in any new Energy Policy implementation plans.

CLIMATE CHANGE

Industry recognizes the increasing public and government concerns around global climate change. CAPP members share these concerns and integrate them into their business decisions. As stated in the Consultation Paper, natural gas is a relatively clean fuel and therefore offshore natural gas projects, including the associated onshore processing, hold a relatively low share of the greenhouse Gas (GHG) emissions in Nova Scotia. In fact, it is widely accepted that natural gas production can play a key role in the solution to reducing GHG emissions.

The path to reduced GHG emissions will likely involve a transition over many decades to low and zero emission coal, oil and natural gas use through deployment of CO₂ capture and storage in fossil fuel power generation, some large industrial operations and eventually in the production of alternatives to gasoline and diesel for transportation fuels.

Given this broader context, the Province should aim to adopt policies in its area of jurisdiction that complement the federal climate change program. It is important for all levels of government to collaborate on issues related to climate change planning and policies in order to avoid a patchwork of conflicting federal and provincial policies.

As Nova Scotia begins working to develop and implement its Climate Change Action Plan, CAPP would advise Government to consider the following suggestions. Some of the suggestions below are already identified as possible actions in the Consultation Paper and Climate Change Action Plan backgrounder.

- **Begin with a manageable first step:** Start with lower cost actions for industry with a clear signal of intent to move to increasingly higher cost actions over time.
- **Put a cost on emissions:** There is a general agreement that putting a cost on emissions – *emission pricing* – should be a core element of policy.
- **Increase investment in advancing technology:** Investing in technology will help reduce cost and increase capacity to deploy currently high cost actions that can make a difference (e.g. CO₂ capture & storage) and help in the discovery and development of breakthrough technologies.
- **Focus on actions:** The focus of the policy should be on actions rather than solely on monitoring and adhering to annual emission volumes. Fluctuating annual emission volumes in any given year and related uncertainty is unimportant relative to being on the right track to major reductions over the coming decades. Government policy must allow for uncertainty for various factors that lead to a specific level of emissions in any given year.

The Consultation Paper indicates three specific actions being considered related to climate change policy: establishing a technology fund paid into by emitters, imposing a financial penalty to those unable to meet regulatory requirements, and using carbon credits in a “cap and trade” regime. CAPP agrees with putting a price on emissions and strongly supports using the funds generated to advance technology through the establishment of a technology fund. With regard to imposing a financial penalty on those unable to meet regulatory requirements, we would caution that this must be considered in the context of the international trade environment. As we increase the effort and costs of actions to reduce GHG emissions, we must simultaneously address trade issues which may be created when a region implements such policies. To date, there has been a very uneven GHG effort across regions which may impact a region’s ability to be competitive nationally and internationally for investment. Policies must create a level playing field in Canadian and international markets. Again, any funds generated through these types of initiatives should be invested into the area of technology. We see technology as key in reducing GHG emissions. With regard to emission trading, CAPP would caution that such types of policies must be sensitive to details – the levels and allocations involved are critical to the outcome of such policies. We would also caution that emission trading is difficult to implement and extend across the whole economy.

Overall, we are pleased with the level of focus the Government of Nova Scotia is placing on climate change policies. The targets outlined in the Consultation Paper are ambitious. Meeting these targets will require strong policies and a strong commitment to implement these policies in the coming years.

FISCAL INCENTIVES

Nova Scotia’s offshore is a high-cost, high-risk area for the petroleum industry and is experiencing increased competition for industry’s investment. CAPP has been advocating for several years for fiscal measures to encourage investment in Nova Scotia’s offshore petroleum industry. We continue to recommend several fiscal measures to the Federal and Nova Scotia Governments that could enhance the competitiveness of the region, including: restoring the Atlantic Investment Tax Credit to 15 per cent, providing Class 41 accelerated Capital Cost Allowance, and increasing the Canadian Development Expense rate. Most importantly, exploration incentives should be considered given the immediate need to stimulate exploration offshore Nova Scotia.

As part of the Atlantic Energy Roundtable process, CAPP and the Government of Nova Scotia examined fiscal incentives in depth in 2005. The Roundtable was tasked with researching current and historical fiscal incentives used in Canada and elsewhere to encourage oil and gas exploration and development and to identify the most successful fiscal measures in terms of how they stimulated renewed exploration and development and allowed economic development of smaller fields in other regions. The chart below illustrates fiscal incentive models used in other jurisdictions. As a result of this work, CAPP recommended the Government look at a 25-50% assignable federal or provincial tax credit exploration incentive.

	CANADA		ALASKA	NORWAY	UNITED KINGDOM	GULF OF MEXICO	ATLANTIC CANADA
	Federal	Provincial					FOR CONSIDERATION
EXPLORATION INCENTIVES							
	PIP and other cash grants (up to 80% for Canada Lands)	Cash grants modeled after Federal	50% Tax Credit Assignable	78% Cash Tax Refunds (applies to both successful and unsuccessful drilling)	10% Exploration cost uplift		25%-50% Tax Credit Assignable Federal or Provincial
	Exploration Tax Credits (25%)	Refundable Tax Credits					
DEVELOPMENT INCENTIVES							
Tax Based	Investment Tax Credits (10%-15%) Deductions in excess of costs incurred Oil Sands Class 41a (acceleration of tangibles)	Tax credits deductible against income tax or royalties payable	10% Tax Credit Lower Production tax for marginal fields	Uplifts on Capital Expenditures Tax relief for marginal projects	25% Write-off rate increased to 100% First Year Allowance	No State Tax Accelerated Write-offs for intangible drilling and completion cost	10% Provincial AITC or 15% Federal AITC rate increase Accelerated Tangible Write-offs (Class 41a) 100% CDE
Royalty Based		Royalty Holiday Royalty Reduction for marginal fields Horizontal Reentry Experimental EOR Relief	Royalty Reduction for marginal fields	No Royalty	No Royalty or Petroleum Revenue Tax on new fields	Deepwater Royalty Relief / Volume-based Royalty Holiday	

Another area where the Government of Nova Scotia can help make the area more attractive for investment is by working to reduce some of the costs of operating in the region. In 2003, through discussions at the Atlantic Energy Roundtable, the federal government decided to change the Customs Tariff Act to exempt duty on mobile offshore drilling units involved in offshore exploration and development. The current moratorium on the important duty is set to expire in 2009. CAPP wishes to extend the moratorium given that high drilling costs in the region are a deterrent to exploration activity. Other offshore areas around the world are showing more favorable conditions and lower drilling costs and the Canadian offshore needs to be more competitive in order to attract further investment. We believe that the moratorium has succeeded thus far in showing the petroleum industry that the region is open for business, is serious about reducing regulatory costs, and that government is working to promote increased activity for the benefit of Nova Scotians.

REGULATORY EFFICIENCY

The petroleum industry is global. Nova Scotia is competing for investment internationally which means that any efficiency which can be achieved in the regulatory environment would help better position Nova Scotia in the context of attracting investment. The revision of the energy strategy provides a perfect opportunity to look at other ways that Government can make itself more

attractive to investors through regulatory efficiency. CAPP suggests that the Government of Nova Scotia consider the following initiatives as areas where regulatory efficiency can be achieved:

- **Regulatory Renewal Initiative:** The Government of Nova Scotia has been an instrumental player in the Frontier and Offshore Regulatory Renewal Initiative (FORRI). This initiative was established in 2005 to renew and modernize the regulatory framework governing Canada's frontier and offshore oil and gas sector. The FORRI is made up of federal, provincial and territorial government departments, the National Energy Board and the two offshore petroleum boards in Atlantic Canada. The work completed by this group such as the flow testing amendment to drilling regulations, drafting drilling and production regulations and organizing the safety case workshop have all been significant accomplishments with industry to further enhance the regulatory environment in Nova Scotia and Atlantic Canada. In the spirit of continuous improvement of the regulations governing the offshore, we would strongly encourage the Government of Nova Scotia to continue its work and involvement in FORRI and dedicate appropriate resources to it.
- **Offshore Strategic Energy Agreements:** The recent sanction of the Deep Panuke offshore natural gas project saw the first implementation of the Offshore Strategic Energy Agreement (OSEA) process. Overall the process was effective and succeeded in reaching an agreement to help ensure benefits for Nova Scotians from the project's development. As this was the first offshore project to undergo the OSEA process, it also serves as an opportunity to examine any lessons learned to make the process even smoother for the next development. In particular, we would suggest looking at ways to make the OSEA process more inclusive of other levels of government. Although the OSEA is an agreement between industry and the province, involving the Federal Government in the process to develop the OSEA would help ensure that all interested parties understand the details which lead up to the final agreement. By extension, this involvement by all interested parties may make the regulatory process more efficient for offshore developments thanks to a greater level of understanding by all participants.
- **Local Benefits Reporting:** Reporting guidelines for offshore oil and gas activities continue to require expenditure content to be calculated in accordance with the Canadian General Standards Board (CGSB) definitions. Based on over twenty years of reporting local content for exploration programs (geophysical or exploratory drilling), there is no material change from program to program. In the producing operations phase of development projects much of the needed labour, materials and services are logically, sourced locally since the local supply community is best situated to meet the need. In the case of development projects, the application of the guidelines to determine local content, require additional resources and processes for local suppliers. This generally places the local supplier at a competitive disadvantage to foreign firms, and leads to unnecessarily higher overall project costs in an industry that is trying to compete internationally for investment. In summary, the guidelines result in limited representative data and present a potential impediment to the success of the local supply community. We would urge the Government of Nova Scotia to work with the Canada-Nova Scotia Offshore Petroleum Board (CNSOPB), industry and the supply community to eliminate the use of the CGSB Definition of Canadian Content in reporting requirements for oil and gas activities.

RIGHTS MANAGEMENT

The Consultation Paper states that Government is considering “licencing flexibility” as a potential initiative aimed at increasing offshore investment. In particular Government is considering the consolidation of exploration acreage and through the CNSOPB offering new terms and conditions for exploration licences. CAPP recently met with the CNSOPB to discuss proposed changes to its Rights Management Policy. We indicated at that time that we are encouraged by several of the proposed changes, most notably the extension of Period I of the term for deepwater exploration licences, the gross-up of allowable expenditures in the first three years of the licence term and the movement to actual costs (verifiable by audit) for purposes of allowable expenditures. We also indicated that concern remains with respect to the global competitiveness of exploration in Nova Scotia. A balance between proposed changes and technical risks needs to be considered such that the overall policy changes being proposed will enable increased exploration activity, which should be the primary goal of any changes to the rights management system.

Promote licences, fallow field initiatives and infrastructure codes of practice are all identified in the Consultation Paper as initiatives that have worked in other jurisdictions. The experiences of other jurisdictions are not easily transferable to the Nova Scotia offshore because of the large number of operators and infrastructure in place in some other jurisdictions. The Fallow Program which was implemented by the U.K. Department of Trade and Industry in 2002 is one such example. It was designed to increase drilling activity. If licenses are held without meaningful activity the licensees will have to drop them. The first phase of the Program focused on the release of the exploration acreage in a license where the program had been fulfilled but there was no activity. The second phase focused on the release of sub-economic discoveries where there were no plans for development. Under the Fallow Program, license holders faced escalating acreage fees during the period of inactivity. There was a financial burden associated with keeping these licenses. The Program was introduced with consultation with the industry. What resulted was that many companies decided to release acreage in order to save the escalating fees but the Program did not cause much in the way of additional activity. It should be noted that this Program was introduced after more than 30 years of production history with an extensive infrastructure base in place. The UK Fallow Program did drive a small amount of diversification in a basin that has many operators and is quite advanced in its maturity. In addition, the extensive infrastructure already in place is enabling discoveries that were once marginal to now become economic.

Given the complexity of the programs currently underway in other jurisdictions, working with industry is the best way to ensure that any initiatives being considered as part of the Nova Scotia Energy Strategy are the right initiatives for the Province. CAPP also cautions against any policy changes related to rights management, which compromise the new data disclosure policy CAPP has been working on with the CNSOPB. In recent discussion with the CNSOPB we have learned that the Board may call on the release of all geoscience data at the end of the term of a licence. This contradicts the approach to data disclosure policy that industry has been working on with the CNSOPB on for several years, which industry understood had been agreed upon, and further reduces the minimum protections for such data as outlined in the Accord Act. This is a major concern for industry and we would urge the Government of Nova Scotia in its Energy Strategy update to avoid any new policies that contradict the data disclosure policy of the CNSOPB.

It is industry's view that changes to rights management policies can either encourage or strongly discourage future investment and therefore will require extensive consultation with industry. We would commit to working with the Provincial Government to explore these options and any potential negative impacts.

SKILLS, EDUCATION AND TRAINING

The focus of this submission has largely been about the need to attract investment in Nova Scotia. Regulatory efficiency and fiscal incentives are some of the ways we have suggested that Government can help make the Nova Scotia offshore more competitive for investment. Another key factor affecting a region's competitiveness is the availability of human resources. Nova Scotia's ability to position itself as a good place for offshore investment will depend partially on the availability of skilled workers in the area. The availability of skilled workers is a major issue for the oil and gas industry nationally. We are facing limits from labour shortages in a number of skills/professions that are expected to worsen over time and extend across a greater number of career areas. Many of the same skilled trades and professionals required for oil and gas development will be sought by other development and investment initiatives throughout the country.

CAPP recognizes that the Nova Scotia Government has made some major investments in skills, education and training through the Department of Education. The recent "Parents as Career Coaches" workshop is one example of a great initiative underway to better equip parents to help their children make informed career decisions. We applaud these efforts and would be interested in working with the Government of Nova Scotia in future initiatives. The petroleum industry also engages in similar types of initiatives. For example, our members participated and supported an "Energy Day" career fair type of event for students in Guysborough in May 2007. We also work with an elementary school every year in Nova Scotia through a program called Energy in Action. The program is designed to teach students about being responsible stewards of the environment and teach them more about the petroleum industry at an early age.

In the neighboring Province of Newfoundland and Labrador the petroleum industry and government work together on human resources issues facing the industry through a working group called the Petroleum Industry Human Resources Committee. The Committee recently developed a curriculum resource for teachers of a new mandatory high school course centered on career development. The Committee also actively engages with teachers through forums held across the province to better equip teachers, career counselors and principals with the tools needed to inform students about career opportunities in the oil and gas industry. The Committee has worked well in Newfoundland and Labrador and we think this model can work well in other regions, including Nova Scotia. While attracting skilled labour for the petroleum industry in Nova Scotia may not be a critical issue right now, it will be a challenge moving forward if other petroleum projects proceed and other resource industries in the province grow.

RESEARCH AND DEVELOPMENT

The Government of Nova Scotia has made major investments in research and development over the past year. CAPP commends Government on recognizing the role of research and development in building a sustainable oil and gas industry. The establishment of the Offshore Energy Environmental Research (OEER) and Offshore Energy Technology Research (OETR) organizations was an important step in the right direction. Investing in new research and development initiatives is critical to the future of Nova Scotia's offshore. There is also an added opportunity in Nova Scotia to capitalize on the work of other organizations and other government initiatives around research and development.

Petroleum Research Atlantic Canada is an organization that is widely supported by CAPP and its members along with educational partners and governments, including the Government of Nova Scotia. PRAC's expertise in research and development planning, management and administration is an asset and a useful vehicle through which to coordinate research and development spending. We are pleased that the Government of Nova Scotia has involved PRAC in its new research initiatives and believe that there may be more opportunities for this kind of collaboration in the future. It is critical that the respective research organizations in the region work together to ensure that there are no overlapping management efforts and to maximize the value of research and development funding.

Industry and federally funded research and development programs such as the Environmental Studies Research Fund and the Program of Energy Research and Development (PERD) can also play a role in the future of Nova Scotia. PERD in particular is currently undergoing a major reorganization which provides an ample opportunity for Nova Scotia to get involved and play a bigger role in how PERD funds are distributed and what kinds of research projects are funded. Having a voice at the decision making table of such R&D organizations can ensure that Nova Scotia's environmental, technical and socio-economic petroleum-related issues and related research projects are accurately represented and promoted.