

Written Submission for the Pre-Budget Consultations in Advance of the 2019 Budget

By: *STEP Energy Services*

- **Recommendation 1:** That the government allow immediate deductibility of capital costs, including the capital invested in the oil and gas services (OGS) sector, for tax purposes in the year in which they occur, to be applied broadly across the economy in a manner that aligns with similar tax reforms in the U.S. while providing the collateral benefit of enhancing the ease of tax compliance and administration;
- **Recommendation 2:** That the government increase the level of protection to approximately 80% coverage of the aggregate compliance cost for Energy Intensive Trade Exposed industries, including the OGS sector, to address the competitiveness gap with the U.S. and to avoid carbon leakage;
- **Recommendation 3:** That the federal government review the Scientific Research and Experimental Development (SR&ED) program, with a view to: ensuring it is a meaningful incentive for large and small companies; for research whether environmental or not; and that its qualification parameters include emissions-reduction technology and other field-based innovation;
- **Recommendation 4:** That the government continue to take a leadership role in framing the opportunity for international recognition of Canada's progress in reducing global GHG emissions via its natural gas exports, and in seeking international credits through trade agreements under Article 6 of the Paris Agreement;
- **Recommendation 5:** That the federal government continue to pursue a permanent exemption from U.S. tariffs currently imposed on steel and aluminum exports;
- **Recommendation 6:** That the federal government provide relief for companies impacted by any potential safeguard measures introduced by the Government of Canada for steel and aluminum based on volumes traditionally sourced from the U.S. that must now be sourced globally due to lack of availability or timely availability in Canada.

As one of Canada's largest industries, the energy sector, including oil and gas services (OGS), plays a key role in the Canadian economy while also providing environmentally and socially responsible energy to global markets. Given growing global demand for oil and gas, the Canadian industry has the potential to continue to do so for several decades. To realize this opportunity, the oil and gas industry is of the view that there is a near term imperative for actions by industry and governments to address significant and systemic competitiveness gaps relative to competing jurisdictions, particularly the United States.

Industry strongly believes that focused and coordinated action is required in the very near term, in order to restore investor confidence and renew growth in the sector for the benefit of all Canadians while supporting the transition to a lower carbon economy. This urgency arises from a confluence of several factors, most notably the increasing momentum toward migration of investment capital to other jurisdictions, challenges in attracting new capital to Canada and the timing of the next window of opportunity to participate in global natural gas markets. Once established, this negative momentum is difficult and time-consuming to reverse. Canada has large and high-quality crude oil and natural gas resources, but the value of these resources (responsible development, jobs, economic benefits) can only be realized if industry invests the capital necessary to monetize these resources. The oil and gas industry in Canada is at a critical juncture in terms of near term decisions on several large investment projects.

Canada and the world are currently facing a significant challenge in meeting growing demand for safe, reliable and affordable energy, while also responding to the impacts of climate change and the need to transition to a lower carbon energy system/economy over the next several decades. These two imperatives are not incompatible if addressed in a balanced and responsible manner over time. In fact, for Canada they should go hand-in-hand.

The recent International Energy Agency's (IEA) World Energy Outlook New Policies Scenario projects that global energy demand by 2040 will have increased by about 30% from today's level. This demand growth is driven by population increases and by greater urbanization and industrialization, largely in Asia. The IEA also projects that by 2040 oil and natural gas will continue to supply over half of the global energy demand. As such, the timing is opportune for Canadian supply to capture new markets, with the next cycle of LNG demand emerging over the 2022-2030 period. As the fifth largest producer of natural gas Canada should be responsive to this market opportunity and continue to play a very important role in meeting global energy demand and reducing global energy poverty. Canada can do so in a manner that contributes to reducing global carbon emissions and positions Canada among the global leaders in environmental and social performance standards. If Canadian supply does not meet this demand, then supply will be provided by other jurisdictions that are likely to have lower environmental and social standards.

Canada's energy industry is among the largest economic engines driving our economy, both directly and through its linkages to other industries such as petrochemicals, power generation and the manufacturing sector. For Canadians, our oil and gas resources can continue to provide secure, reliable and affordable energy supply, while sustaining employment and economic prosperity throughout the value chain. The oil and gas services (OGS) sector represents over 450,000 of the jobs in the oil and gas

industry, most of which are middle class and include manufacturing, high tech and clean tech jobs. As well, a greater percentage of Indigenous peoples are included in the jobs in our sector versus other industries. This sector also provides Indigenous peoples with numerous entrepreneurial opportunities.

At the same time as this economic opportunity presents itself, there is also an international consensus on the need to address global climate change and to reduce carbon emissions from the global energy system. Canada has committed to work toward significant reductions in greenhouse gas emissions, through its commitment to the 2015 Paris Climate agreement and through the Pan-Canadian Framework on Clean Growth and Climate Change. The Canadian oil and gas industry recognizes the need to address global climate change and is broadly supportive of the climate policy goals and policy frameworks being implemented by Canadian governments, provided that such policies are implemented in a manner so as to provide incentive for industry to reduce greenhouse gas emissions, while addressing the competitiveness impacts for sectors that are competing in the open market with companies operating in jurisdictions with less stringent climate policies.

Canada therefore has the opportunity to play a leadership role in the global transition to a lower carbon energy system/economy, with the vision being: ***Canada is a preferred supplier of cost and carbon competitive oil and gas to domestic and global markets, produced with leading environmental and social performance standards.***

The Canadian OGS sector is world-renowned for its technology, innovation and expertise and we will continue to work to reduce carbon emissions and other environmental impacts to supply the world with responsibly-developed energy.

Canada continues to have a number of positive attributes in terms of investment attraction, among them the size and quality of the resource, world-class environmental standards, and competitive royalty regimes. However, both industry and the investment community are of the view that the competitiveness of Canada's oil and gas sector is increasingly challenged. Investment is leaving Canada's oil and gas sector and the sector is having difficulty attracting new investment capital.

These competitiveness challenges arise from several factors, including cost structure, changes in the business investment climate such as tax policy changes in the U.S., constraints on market access and resultant negative impacts on prices, regulatory timelines and complexity, and public perception issues. In particular, Canada faces significant market access problems, preventing growth of production and the associated benefits. For natural gas, Canada is losing market share to the U.S. in areas of Canada and the U.S. traditionally supplied by Canadian gas and to date has not participated in the rapid growth of liquefied natural gas (LNG) export markets. This lack of market access options is being manifested in significant price discounts for both Canadian oil and natural gas.

Some of these competitiveness issues reflect broader market conditions (e.g., growth of shale oil and gas disrupting North American market dynamics) and some are reflective of policy and regulatory decisions by federal and provincial governments in Canada. At the same time other competing

jurisdictions are acting to make their fiscal regimes and regulatory systems more competitive and efficient, exacerbating the situation in Canada. While these changes in competing jurisdictions may or may not be durable, they are currently having a material impact on investment attraction and capital flows.

U.S. tariffs on steel and aluminum are also affecting the oil and gas industry as pipe, manufactured parts, machinery and other products cross the border several times during production and servicing. As well, while industry is supportive of Canada's retaliatory tariffs, they too are increasing costs, contributing to a lack of competitiveness for the industry.

Ensuring that Canada remains competitive would re-establish the investor confidence required to attract the capital to sustainably grow the Canadian industry and economy. Potential actions to address this issue are within the purview of both industry and governments, working collaboratively with Indigenous peoples and stakeholders.

For its part industry has reduced, and continues to reduce, cost structure and address GHG emissions intensity across all areas of the business by seeking efficiencies, and by applying new technology and innovative systems and processes.

Therefore, actions by governments, including the following, are urgently required to address competitiveness challenges:

- The allowance of immediate deductibility of capital costs for tax purposes, to be applied broadly across the economy in a manner that aligns with similar tax reforms in the U.S.;
- Increasing the level of protection to approximately 80% coverage of the aggregate compliance cost for EITE industries, across the energy industry including the OGS sector;
- Proceeding with the commitment to review the SR&ED program, with the inclusion of qualification parameters surrounding emissions reduction technology and other field based innovation;
- Taking a leadership role in gaining international recognition of Canada's progress in reducing global GHG emissions via its natural gas exports, and in seeking international credits under Paris Agreement Article 6;
- Pursue a permanent exemption from U.S. tariffs currently imposed on steel and aluminum exports;

- Provide relief for companies impacted by any potential safeguard measures introduced by the Government of Canada for steel and aluminum based on volumes traditionally sourced from the U.S. that must now be sourced globally due to lack of availability or timely availability in Canada.

In summary, we believe that Canada's oil and gas industry – specifically liquid rich natural gas (LRNG) and light tight oil (LTO) – presents a significant opportunity for inclusive growth that provides broad benefits to Canadians and is aligned with Canada's economic, environmental and social objectives. The recommended actions would help to ensure Canada remains globally competitive and in turn restore investor confidence, attract investment and provide the platform for a broader consensus on the future of the Canadian oil and gas industry, all of which could lead to significant growth of the sector – protecting Canadian jobs and working people, providing opportunities for Indigenous Canadians and contributing to the economic prosperity necessary to support our standard of living and quality of life and to enable transition to a lower carbon energy system/economy.