Against income trusts, the federal Finance Minister said,

> "*The tax treatment of (income) trusts creates an economic distortion through the proliferation of income trusts that is threatening Canada's economic growth and competitiveness.*" (Finance News Release, Ottawa, October 31, 2006, 2006-061)

> "*Tax revenues are reduced as a result of the growth of the income trust sector and the overall tax burden is shifted onto the "shoulders of hardworking individuals and families"* (Statement, Minister of Finance October 31, 2006)

These claims are false. This brief is especially concerned to show that the claims are false relative to energy trusts and Alberta. Why especially Alberta? The Alberta Finance Minister, on March 22, 2006, fully six months before the federal Finance Minister made his false statements, said,

> *When corporations change themselves into income trusts, the way in which they are taxed also changes. When income is earned through a corporation, it is subject to corporate tax in the province where the business is located. With a shift to income trusts, no corporate tax is paid on the income. As a consequence, some businesses that operate in Alberta, using Alberta's infrastructure, do not contribute to the costs of that infrastructure.*

> *Rather than paying tax at the business level, investors pay personal income tax on the income in their province of residence. Alberta has 10 per cent of Canada's population, yet over 60 per cent of Canada's market capitalization for trusts… A recent estimate puts Alberta's net revenue loss at about $400 million per year.* (2006 Budget Fiscal Plan, page 139)

Here is what is true.

(1) Energy trusts pay more in conventional oil & gas royalties.

(2) Energy trusts reinvest more of their cash flow from conventional oil & gas.

(3) Energy trusts are increasing their conventional reserves at a time when conventional oil & gas reserves are declining in Alberta.

(4) Income trusts held by RSPs and RIFs enhance government tax revenues.

(5) The Canadian government lightly taxes U.S. citizens who invest in Canada, because Canada gets payback from Canadians who invest outside of Canada.

(6) Energy trust investors pay more income taxes than oil & gas corporations do.

(7) Alberta has more gains than losses from energy trusts.

The factual bases of these true statements come from,

- The Canadian Association of Petroleum Producers Statistical Handbook ("CAPP"), September 2007[1];
- SEDAR information for the year 2005 for thirty-one energy trusts[2];
- Canadian Energy Trusts (CET) report "An Integral Component of the Canadian Oil and Gas Industry", December 2006[3];
- Canada Revenue Agency (CRA) income statistics for the year 2004 (2005 is not yet available).[4]

(1) Energy trusts pay more in royalties

Table 1 has been compiled from CAPP and SEDAR information for conventional oil & gas operations in Canada for 2005. Royalties paid by energy trusts as a percentage of sales is highlighted in yellow.

| | Conventional oil & gas | |
|---|---|---|
| Operations (in '000s) | Energy trusts | Industry |
| Sales | 15,274,049 | 92,421,203 |
| Royalties | (3,099,150) | (15,822,400) |
| Operating | (3,501,369) | (11,929,000) |
| Cash flow | 8,673,530 | 64,669,803 |
| Royalty % | 20.3% | 17.1% |
| Cash flow % | 56.8% | 70.0% |
| | | |
| Capital costs | (4,046,461) | (25,597,000) |
| % of cash flow re-invested | 46.7% | 39.6% |
| | | |
| Net cash-flow | 4,627,069 | 39,072,803 |
| | 53.3% | 60.4% |

**Table 1**

Energy trusts have specialized in developing and maintaining the productivity of low volume and/or aging wells. **Energy trusts pay 3% more in royalties** compared to 17% for the industry as a whole. How much is the incremental 3% worth?—$**435 million**.

Notice in Table 1 that energy trusts reinvest 46.7% of their cash flow from conventional oil & gas, compared to 39.6% for the rest of the industry.

---

[1] For a copy of the CAPP *Statistical Handbook*, visit www.capp.ca/default.asp?V_DOC_ID=1071
[2] The SEDAR information is at www.sedar.com/issuers/issuers_en.htm. See Appendix for a list of the 31 Energy Trusts.
[3] Visit www.canadianenergytrusts.ca/documents/CompleteReportDec2006FINAL.pdf for a copy of this report.
[4] Visit www.cra-arc.gc.ca/agency/stats/gb04/pst/final/tables-e.html to access the tables mentioned here.

(2) Energy trusts reinvest more of their cash flow from conventional oil & gas

As we see in Table 1, energy trusts reinvest more of their cash flow from conventional operations. For all operations (conventional and oil sands), the results are as follows.

| | Conventional oil & gas and oil sands | |
|---|---|---|
| Operations (in '000s) | Energy trusts | Industry |
| Sales | 17,280,749 | 110,163,528 |
| Royalties | (3,118,750) | (16,641,400) |
| Operating | (4,467,569) | (18,233,900) |
| Cash flow | 9,694,430 | 75,288,228 |
| Royalty % | 18.0% | 15.1% |
| Cash flow % | 56.1% | 68.3% |
| | | |
| Capital costs | (4,846,061) | (39,934,000) |
| % of cash flow re-invested | 50.0% | 53.0% |
| | | |
| Net cash-flow | 4,848,369 | 35,354,228 |
| | 50.0% | 47.0% |

**Table 2**

For oil sands only, the results are as follows.

| | Oil Sands | |
|---|---|---|
| Operations (in '000s) | Energy trusts | Industry |
| Sales | 2,006,700 | 17,742,325 |
| Royalties | (19,600) | (819,000) |
| Operating | (966,200) | (6,304,900) |
| Cash flow | 1,020,900 | 10,618,425 |
| Royalty % | 1.0% | 4.6% |
| Cash flow % | 50.9% | 59.8% |
| | | |
| Capital costs | (799,600) | (14,337,000) |
| % of cash flow re-invested | 78.3% | 135.0% |
| | | |
| Net cash-flow | 221,300 | (3,718,575) |
| | 21.7% | -35.0% |

**Table3**

When the federal Finance Minister said energy trusts are "*threatening Canada's economic growth and competitiveness*", he spoke falsely. For conventional oil, energy trusts reinvest more than do oil & gas corporations. For the whole industry (conventional and oil sands combined), energy trusts reinvest 50% compared to 53%. So, energy trusts are not a threat to the Alberta economy.

(3) Energy trusts are increasing their reserves

In 2005, the industry as a whole increased Canada's energy reserves by about 6%. Energy trusts reserve additions in total were comparable to the industry additions in total.

| | Reserves | | | |
|---|---|---|---|---|
| | Conventional and oil sands | | | |
| Barrels of oil equivalent (boe) | Energy trusts | | Industry | |
| Open reserves | 4,329,173,374 | 100.0% | 17,097,335,163 | 100.0% |
| Additions | 564,896,191 | 12.7% | 2,579,791,229 | 15.1% |
| Production | (301,736,975) | -6.9% | (1,539,739,884) | -9.0% |
| Ending reserves | 4,470,787,407 | | 18,137,386,508 | |
| Ending as a % of opening | 106% | | 106% | |
| | Conventional oil & gas | | | |
| Barrels of oil equivalent (boe) | Energy trusts | | Industry | |
| Open reserves | 2,721,173,374 | 100.0% | 9,725,154,523 | 100.0% |
| Additions | 561,896,191 | 20.4% | 997,471,586 | 10.3% |
| Production | (269,736,975) | -9.9% | (1,180,547,482) | -12.1% |
| Ending reserves | 2,891,787,407 | | 9,542,078,627 | |
| Ending as a % of opening | 111% | | 98% | |
| | Oil sands | | | |
| Barrels of oil equivalent (boe) | Energy trusts | | Industry | |
| Open reserves | 1,608,000,000 | 100.0% | 7,372,180,640 | 100.0% |
| Additions | 3,000,000 | 0.2% | 1,582,319,643 | 21.5% |
| Production | (32,000,000) | -2.0% | (359,192,402) | -4.9% |
| Ending reserves | 1,579,000,000 | | 8,595,307,881 | |
| Ending as a % of opening | 98% | | 117% | |

**Table 4**

Reserve maintenance is important for future production. Additions to conventional new pool discoveries are diminishing. In the future, enhanced oil recovery will be important for extending the productive-life and royalties of the conventional oilfields.

(4) Income trusts held by RSPs and RIFs enhance government tax revenues

In his presentation to the Finance committee of the House of Commons (FINA) last winter, the federal Finance Minister said,

> *You will no doubt hear from some witnesses that there is no real tax loss and if there were, it would be more than made up in the future through personal income taxes or withholding taxes on foreign investors, or taxes on deferred pension plans or RRSP withdrawals.*

> *Think of what you are being told: give income trusts a definite tax break now but get it back sometime in the future. As Minister of Finance, I have a fiduciary obligation to the taxpayers of today, not tomorrow. I have an obligation to pay for needed social, environmental and economic programs today, not tomorrow. I cannot and will not fund today's programs from tomorrow's revenues.*

What the federal Finance Minister failed to say is that the Canadian governments gain tax revenue from retirement savings each day, every week and month of the year. The federal and most provincial governments are tax revenue positive from retirement savings; see Table 5.

Pension deductions vs. income

| | Alberta | Canada |
|---|---|---|
| Pension contribution deductions | $ 4,387,871,000 | $37,532,918,000 |
| Taxable pension income | 3,978,543,000 | 50,648,291,000 |
| Deduction or income (loss) or gain | $ (409,328,000) | $13,115,373,000 |

**Table 5, CRA 2004 Basic Tables 4A**
www.cra-arc.gc.ca/agency/stats/gb04/pst/final/tables-e.html

As Table 5 shows, the federal government gains $1.35 in taxable income for every $1 of pension deduction. Retirement savings "cost" Alberta about 10 cents on the dollar; that is because Albertans save more for retirement. On a per taxpayer basis, both Alberta and Canada gain more than double from pension savings; see Table 6.

Per taxpayer contribution deduction vs. pension income

| | Alberta | Canada |
|---|---|---|
| Pension contribution per taxpayer | 4,281 | 3,781 |
| Pension income per taxpayer | 10,687 | 13,339 |
| Taxable income per $1 of contribution | 2.50 | 3.53 |

**Table 6, CRA 2004 Basic Tables 4A**
www.cra-arc.gc.ca/agency/stats/gb04/pst/final/tables-e.html

Clearly, the federal Finance Minister spoke falsely when he said "*I cannot and will not fund today's programs from tomorrow's revenues.*" There is no "*tomorrow*". Retirement savings pay their way today.

(5) Canada willingly "under" taxes foreign investors

Foreign investors who earn income in Canada pay tax to the federal government at the rate of 0%, 10%, 15% or 25% depending on the type of income and their country's tax treaty with Canada.

Canadian residents pay tax at rates varying from 15% to 48%. A foreign investor with $100,000 of Canadian investment income will pay a maximum of $25,000 in tax. A Canadian earning the same income may pay as much as $48,000 in tax.

The tax rates applicable to foreign investors are neither acts of God nor forces of nature. The Canadian government has willingly chosen to tax foreigners less. Why? Obviously, if foreigners have to pay as much tax as Canadians, foreigners will not invest in Canada; but Canada wants foreign investment.

Just as Canada lightly taxes U.S. investors in Canada, so too the U.S. lightly taxes Canadians who invest in the U.S. Each puts a light touch on the other's citizens. When their citizens bring foreign income home, the citizens pay the full tax in their home country. In 2004, Alberta and Canada enjoyed tax revenue gains from foreign source income as follows.

Foreign source income / tax revenues

| | Alberta | Canada |
|---|---|---|
| Taxable income from foreign sources | $421 million | $4.5 billion |
| Tax revenues | $42 million | $450 million |

**Table 7, CRA 2004 Basic Tables 10**
www.cra-arc.gc.ca/agency/stats/gb04/pst/final/tables-e.html

Alberta gains a (flat) tax of 10% on taxable income. Canada gains, on average, 25% less a 15%, 10% or 0% withholding in the country of source. The federal Finance Minister did not say one word about his foreign source income gains. In the corporate world, such half-truth would constitute a failure to provide full disclosure. You would not want to be doing that in Chicago or New York.

(6) Energy trust investors pay more income tax than oil & gas corporations do
The Alberta Finance Minister said, "*With a shift to income trusts, no corporate tax is paid on the income.*" But how much corporate tax did energy trusts pay when they were corporations? CET mentions three examples of "before and after".

Before trust conversion, Paramount, Baytex and Bonavista paid (1) $20 million, (2) $0 and (3) $17 million in corporate income tax respectively.

After trust conversion, the Paramount, Baytex and Bonavista trust investors paid (1) $60 million, (2) $128 million and (3) $265 million in tax withholding or personal income tax respectively.

In sum, before $37 million; after $443 million–12 times increase.

The problem is not that energy trust investors do not pay income tax. The problem is that they pay tax to a province or state other than Alberta. The Alberta Finance Minister said, "*Alberta has 10 per cent of Canada's population, yet over 60 per cent of Canada's market capitalization for trusts.*"

The figure "*10 per cent of Canada's population*" is very suspect. Population percentage is irrelevant to taxable income and taxes payable. Provincial personal income as a percentage of national personal income is what we need to know. Here is what CRA says.

| | Alberta | Canada |
|---|---|---|
| Total personal income assessed | $94.3 billion | $751.1 billion |
| Alberta as a % of Canada | 12.6% | |
| Income in excess of national average | $19.2 billion | |
| Provincial tax thereon | $1.9 billion | |

**Table 8, CRA 2004 Basic Tables 5A**

www.cra-arc.gc.ca/agency/stats/gb04/pst/final/tables-e.html

Another reason to suspect the suggestion that Albertans own only 10% of energy trusts is that the directors and employees own 9% (6% and 3% respectively as per SEDAR filings for 2005 year-end) of the energy trust units. We may assume that Albertans own at least 20% of the energy trust units.

How much income tax should energy trusts pay Alberta? The large oil companies pay combined (federal + provincial) corporate income tax at the rate of about 4.4% of their sales (CCET, Canadian Energy Trusts, Dec 2006, page 63). Using a provincial percentage of 1.2% "standard" for energy trusts, we can answer how much income tax energy trusts should pay—$210 million.

Something does not compute. Alberta Finance Minister McClellan said, "Energy trusts cause Alberta a $400 million tax revenue loss"; and, in a letter to the federal Finance Minister, Alberta Finance Minister Oberg said "$450 million tax revenue loss." Why did McClellan, and why does Oberg, expect energy trusts to pay twice as much tax as oil & gas corporations pay?

In fact, the Alberta situation is even bleaker. A Freedom of Information request has disclosed a break-down by industry sector of provincial corporate income tax for 2005-06 (year ended March 31). In Alberta, all corporations paid $2.9 billion of income tax[5]. Is the oil industry at the top of the list of corporate income taxpayers? Actually, no; manufacturing was #1. If energy trusts paid income tax at the same rate as did oil & gas corporations did in 2005, their tax rate would be 0.8%; see Appendix 2, page 10, for more detail. Therefore, as comparable to corporations, energy trusts would only pay $137 million of provincial income tax. Why have two Ministers said $400 million or more?

| Corporate income tax comparison | Trusts | Corporations |
|---|---|---|
| Oil & gas sales (in '000s) | 17,280,749 | 65,076,128 |
| Provincial income tax as % of sales | 0.8% | 0.8% |
| Corporate income tax | 137,444 | 517,590 |

**Table 9**

[5] As per the Alberta Consolidated Financial Statements; see Appendix 2.

(7) The Alberta government gets payback for its energy trust tax losses

What is the full tax revenue accounting for Alberta? The Alberta Finance Ministers only look to Alberta's losses to other jurisdictions. They have not told us about what Alberta gains from other provinces, and foreign income earned by Albertans.

While it is true that Alberta has only 10% of Canada's population, Albertans receive 17.5% of taxable dividends in Canada. In 2004, the extra 7.5% was worth **$175 million** to the Alberta government (see CRA 2004 Basic Table 4 for Canada and Alberta.)

Albertans invest outside of Canada. In 2004, Albertans reported and paid tax on $421 million of foreign source income, which was worth **$42 million** to the Alberta government (see CRA 2004 Basic Table 10 for Canada and Alberta.)

As we have seen (on page 2), energy trusts pay more royalties. Alberta's tax revenues are as follows.

| Alberta's full revenue accounting | | millions |
|---|---|---|
| Albertans own 20% of energy trusts | $ | 78 |
| Albertans invested in other provinces | | 175 |
| Albertans invested in the U.S. | | 42 |
| Higher royalties paid by energy trusts | | 435 |
| Full revenues | $ | 730 |

**Table 10**

Below the line at the bottom

Under the line, we have a net tax or royalty revenue gain from income trusts of $597 million ($730 million less $137 million.) Energy trusts, in 2005, were about $600 million tax revenue positive for the Alberta Treasury.

So that's the bottom under the line. Now we need to get to the bottom of why one federal, and two Alberta, Finance Ministers failed to provide complete and accurate accounting of their respective income tax or royalty revenues from energy trusts. It is a curious thing, is it not? The federal Finance Minister and two Alberta Finance Ministers have not told the truth about energy trust taxation.

---

Prepared by Louis Mix
December 14, 2007
Last updated: January 12, 2008

## Appendix 1
## The Thirty-one Energy Trusts

| | |
|---|---|
| 1 | Advantage |
| 2 | Arc Energy |
| 3 | Baytex |
| 4 | Bonavista |
| 5 | Bonterra |
| 6 | COS |
| 7 | Canetic |
| 8 | Crescent Point |
| 9 | Daylight |
| 10 | Enerplus |
| 11 | Enterra |
| 12 | Fairborne |
| 13 | Focus |
| 14 | Freehold |
| 15 | Harvest |
| 16 | NAL Oil |
| 17 | Paramount |
| 18 | Pengrowth |
| 19 | Penn West |
| 20 | Peyto |
| 21 | PrimeWest |
| 22 | Progress |
| 23 | Provident |
| 24 | Shiningbank |
| 25 | Sound |
| 26 | Thunder |
| 27 | Trilogy |
| 28 | True |
| 29 | Vault |
| 30 | Vermilion |
| 31 | Zargon |

# Appendix 2
## Alberta provincial corporate income tax
## 2005-06

Alberta Government — Consolidated Financial Statements
2005-06 corporate income tax revenue

| Industry name | Tax revenue | % |
|---|---|---|
| Manufacturing | 607,402,800 | 20.83% |
| Oil and Gas Extraction | 517,590,000 | 17.75% |
| Finance and Insurance | 386,370,000 | 13.25% |
| Management of Companies and Enterprises | 222,490,800 | 7.63% |
| Accommodation and Food Services | 153,964,800 | 5.28% |
| Wholesale Trade | 137,052,000 | 4.70% |
| Professional, Scientific and Technical Services | 126,846,000 | 4.35% |
| Transportation, Warehousing and Storage | 104,392,800 | 3.58% |
| Construction | 96,519,600 | 3.31% |
| Real Estate and Rental and Leasing | 93,895,200 | 3.22% |
| Mining (Except Oil and Gas) | 93,312,000 | 3.20% |
| Retail Trade | 84,855,600 | 2.91% |
| Other Services | 68,817,600 | 2.36% |
| Waste Management and Remediation Services | 56,570,400 | 1.94% |
| UNKNOWN (Unclassified by taxpayer) | 55,404,000 | 1.90% |
| Utilities | 38,782,800 | 1.33% |
| Health Care and Social Assistance | 26,827,200 | 0.92% |
| Information and Cultural Industries | 20,703,600 | 0.71% |
| Agriculture, Forestry, Fishing and Hunting | 19,245,600 | 0.66% |
| Arts, Entertainment and Recreation | 3,499,200 | 0.12% |
| Educational Services | 874,800 | 0.03% |
| Administrative and Support | 291,600 | 0.01% |
| Public Administration | 291,600 | 0.01% |
| Total corporate tax revenue per Consol F/S | 2,916,000,000 | 100.00% |

| | | |
|---|---|---|
| Oil & gas sales in Alberta (CAPP *Stats Handbook*) | 82,356,877,000 | Table 4.19b |
| Less: energy trust sales (Table 2 above) | (17,280,748,613) | |
| Oil & gas sales by corporations (Table 2) | 65,076,128,387 | |
| Provincial corporate income taxes paid | 517,590,000 | |
| Prov corp tax as % of sales | 0.80% | |

| | |
|---|---|
| Energy trust sales | 17,280,748,613 |
| Comparable corporate tax rate | 0.80% |
| As corporations energy trusts would pay | 137,444,296 |

See **Schedule 1** of the Consolidated Financial Statements (page 40) at:
[www.finance.alberta.ca/publications/annual_repts/govt/ganrep06/confinst.pdf](www.finance.alberta.ca/publications/annual_repts/govt/ganrep06/confinst.pdf)