STORY 2

Removing Subsidies for Fossil Fuel Exploration and Development in Canada

Remove subsidies for fossil fuel production

FEATURED COUNTRY

CANADA

- A high-income OECD country
- A net exporter of oil, gas and coal
- The world's second largest reserves of unconventional oil

Key numbers

USD 70 billion in the G20 countries

This is the annual average value of fiscal support to the production of oil, gas and coal in 2013–14 (Bast et al., 2015). These subsidies mostly take the form of direct transfers to projects and tax breaks or deductions for specific expenses.

Canada has reformed seven policies since 2011

Since 2011, the Government of Canada has either completely phased out or reformed seven policies that subsidized the production of oil, gas and coal across the country. These reforms have primarily affected tax expenditures that benefitted exploration and development activities.

FEATURED REFORMS AND THEIR PERIOD

- Rationalization of certain tax expenditures for fossil fuel exploration and development between 2011 and 2018

STAGES OF FOSSIL FUEL LIFE CYCLE

- Exploration – Development

SECTORS AFFECTED BY REFORM

- Oil, gas and coal extraction industry

Context

In 2009, as a member of the G7, the G20 and the Asia-Pacific Economic Cooperation, Canada committed to reforming its inefficient fossil fuel subsidies. Historically, the federal government in Canada has primarily provided subsidies to the production of fossil fuels, while provinces have provided subsidies for production and consumption of fossil fuels (Organisation for Economic Development and Co-operation, 2018). The federal government has played a central role in developing the oil and gas industry in Canada, providing incentives for industry to explore and develop proven reserves as much as possible. However, between 1990 and 2007, the federal government reformed four tax deductions provided to oil and gas production in a first round of streamlining (Whitley & van der Burg, 2015). A second round took place from 2011 onwards (Office of the Auditor General, 2017).

Change in the mechanisms of government support to fossil fuels

Since 2011, the following reforms have been announced or completed:

- Oil sands property expenses that were treated as Canadian development expenses (CDEs) were reformed to be treated the same as all other Canadian oil and gas property expenses (COGPEs), bringing the deduction rate down from 30 to 10 per cent (2011).
- Pre-production expenses of new oil sands and oil shale mines that were treated as Canadian exploration expenses (CEEs) were reformed to be treated the same as all other CDEs, gradually bringing the deduction rate down from 100 to 30 per cent (2011–2016).
- The oil and gas and mining components of the 10 per cent Atlantic Investment Tax Credit were phased out completely (2012–2017).
- Pre-production mine development expenses (including coal mining) that were treated as CEEs were reformed to be treated the same as all other CDEs, bringing the deduction rate down from 100 to 30 per cent (2013–2018).
- Accelerated capital cost allowance (ACCA) for certain mining assets (other than for oil sands and oil shale mines and thus including coal mines) is being gradually phased out (2013–2021)
- Successful CEEs (e.g., oil and gas discovery wells) will be treated as CDEs for tax purposes, bringing the deduction rate down from 100 to 30 per cent (2019–2022).
- The reclassification of a portion of CDEs into CEEs for small oil and gas corporations when renounced to flow-through share investors was reformed, also bringing the deduction rate down from 100 to 30 per cent (2019–2022).

Drivers of reform

The reforms between 1990 and 2007 were principally undertaken because the subsidies were no longer regarded as necessary given that their goal had been reached: the oil and gas and sector had become “robust and growing” (Dobson & Asadollahi, 2014). The reforms announced since 2011 (Government of Canada, 2011, p. 88; 2012, p.118; 2013, p.353; 2017a, p.208) all explicitly referenced Canada’s G20 commitment as one of the drivers of reform.

Complementary policies

At the federal level, Canada committed to phasing out coal power generation by 2030 and to implementing just transition programs to help affected communities and workers. Though coal mined in Canada can be exported, the commitment to phase out coal power most likely means the sunsetting of coal mining in such land-locked provinces as Alberta (Vriens, 2018).

Did the reform generate fiscal or financial space? How was it used?

The four policies that were reformed between 1990 and 2007 had a combined value in the past of over USD 900 million (Whitley & van der Burg, 2015). Ultimately, the reforms implemented between 2011 and 2022 should result in additional savings of approximately USD 260 million annually (Government of Canada, 2017b; Office of the Auditor General, 2017). The fiscal space that was created was not directly earmarked for specific programs.

Watching brief

Missed opportunity: Canada introduced a new subsidy in 2015, the Accelerated Capital Cost Allowance for Liquefied Natural Gas (Office of the Auditor General, 2017), which is scheduled to be phased out only in 2025. Canada also did not review or reform its benchmark rate for the deduction of fossil fuel exploration and expenses for income tax purposes (Touchette & Gass, 2018).

Risk of backsliding: The federal government purchased the Trans Mountain pipeline that crosses the provinces of Alberta and British Columbia from Kinder Morgan Canada Limited (CBC, 2018). It is actively seeking to expand the pipeline and announced its intention to indemnify a potential future private owner from any delays in construction of the expansion.

Canada's peer review under the G20: In 2018 Canada announced it would proceed with a voluntary G20 peer review process of its fossil fuel subsidies alongside Argentina (Government of Canada, 2018).

Other countries in and outside of the G20 that implemented similar reforms:

Removal of subsidies to fossil fuel exploration and development counts several examples, including:

- Argentina – phase-out of several subsidies to oil production (see Story 3)
- European Union – phase-out of subsidies to hard coal mining by the end of 2018, which also encompassed the end of coal exploration in the European Union (see Story 4)
- Norway – in 2013, Norway established new rules for uplift calculation used to determine the accelerated depreciation schedule. As a result, the taxation burden on new projects has increased and several of them were shelved (Government of Norway, 2013).

Meanwhile, a number of countries announced decisions to phase out not just subsidies to oil and gas exploration, but to phase out oil and gas exploration itself (Gerasimchuk, 2018). They are:

- Costa Rica (indefinite moratorium on oil and gas production)
- France (ban on new exploration licences from 2017 and phase-out of oil extraction by 2040)
- New Zealand (end of oil exploration offshore from 2018)
- Belize (end of oil exploration offshore from 2018)

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