

**Energy and Mines**

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## Executive summary

In this chapter, we report on the Department of Energy and Mines and its special purpose fund, the Oil and Gas Environmental Fund. We also describe the key risks the Department must manage in order to be successful.

The Department's vision is to achieve prosperity and economic strength from responsible energy and mineral development. The Department must manage five key risks to realize this vision. We explain these key risks so that legislators and the public can better understand and assess the Department's performance. We have not assessed the adequacy of the Department's systems and practices to address its five key risks. To be successful the Department needs to:

- ◆ promote exploration to optimize the discovery and development of energy and mineral resources in Saskatchewan;
- ◆ ensure responsible energy and mineral development while optimizing government revenues to pay for programs and services;
- ◆ ensure responsible use and delivery of energy;
- ◆ ensure the completeness and accuracy of all royalties and taxes due to the Government; and
- ◆ ensure that industry activities are conducted in a safe and environmentally responsible manner.

In this chapter, we report that the Fund had reliable financial statements and that the Department had adequate rules and procedures to safeguard and control its assets and the assets of the Fund. We also report that the Department complied with authorities except for payments to NewGrade that continue to need proper authority. We provide an update on the status of our recommendations related to the Department's payments to NewGrade.

## Introduction

The Department of Energy and Mines is responsible for managing Saskatchewan's energy and mineral resources.

In 2000-2001, the Department had expenses of \$19 million and collected revenue of \$1,301 million. Information about the Department's revenue and expenses appears in its annual report and in the *Public Accounts 2000-01: Volume 2: Details of Revenue and Expenditure* (to view a copy of this report, see <http://www.gov.sk.ca/finance/paccts>).

## Special purpose fund

The Department is responsible for the Oil and Gas Environment Fund (Fund). The purpose of the Fund is to provide a mechanism to clean-up abandoned wells and to respond to environmental problems associated with the exploration, development, production, and transportation of oil and gas. The Fund had revenue of \$137,000 and held assets of \$2.5 million as at March 31, 2001. The Fund's financial statements are included in its annual report.

## Key risks the Department faces

Under *The Department of Energy and Mines Act* (Act), the Department is responsible for the exploration, development, management, and conservation of non-renewable resources and energy. To assess the Department's performance, it is important for legislators and the public to understand the Department's vision and mission and how it manages key risks.

The Department has documented its mandate, vision, guiding principles, goals, and strategic issues in its strategic plan. The Department's annual report sets out much of this information. Information about the Department and its services are also available at the Department's website ([www.gov.sk.ca/enermine](http://www.gov.sk.ca/enermine)). However, the Department does not make public its strategic plan and how it manages key risks. We encourage the Department to provide information on its strategic plan and how it manages key risks in its annual report and/or its website.

To carry out our work, we must understand the risks facing the Department. We think sharing our understanding with the legislators and the public will help them better understand and assess the Department's performance. To identify key risks, we reviewed various departmental documents and reports. We discussed our understanding of those risks with management and confirmed we have identified the correct risks.

To be successful, the Department needs to:

- ◆ promote exploration to optimize the discovery and development of energy and mineral resources in Saskatchewan;
- ◆ ensure responsible energy and mineral development while optimizing government revenues to pay for programs and services;
- ◆ ensure responsible use and delivery of energy;
- ◆ ensure the completeness and accuracy of all royalties and taxes due to the Government; and
- ◆ ensure that industry activities are conducted in a safe and environmentally responsible manner.

The following briefly explains each of the above risks and sets out systems and practices necessary to manage those risks. We have not assessed the adequacy of the Department's systems and practices to address its key risks.

## **Promote exploration**

Promoting exploration is essential for ensuring that the oil, gas, and mining sectors of the economy continue to grow. Exploring new areas and developing present resources allows optimization of Saskatchewan's mineral potential and encourages economic benefits in terms of jobs, income, and government revenues.

To promote exploration, the Department needs to update and improve accessibility to Saskatchewan's geoscience data. Better information makes it easier to explore and locate new deposits. The Department must

maintain an adequate mapping system that assists the industry in searching for new deposits. The Department must work with the industry to establish a competitive economic and regulatory system to promote exploration in Saskatchewan. The Department must promote its programs. If the industry does not know about Saskatchewan's geological potential, the industry will look elsewhere for new mineral discoveries.

The Department is currently undertaking a new exploration development strategy that addresses this risk. The new strategy consists of projects that include promotion, enhanced geoscience, and tax reduction programs.

## **Responsible energy and mineral development**

The Department must obtain, in a responsible manner, a fair share of the revenue from resource development for the people of Saskatchewan. At the same time, the Department must encourage continued investment and development of resources by ensuring the industry also receives a fair return on its investment. Energy and mineral resources are non-renewable. Therefore, the Department must optimize recovery of these resources given market conditions. The Department must also ensure that there is responsible use of non-renewable resources.

The Department must support research and development to enhance recovery and must ensure optimal development of energy and mineral resources. The Department must regulate and monitor the industry to ensure the industry's activities are conducted in a responsible manner. To protect the Government's interest, the Department must analyze the impact of policies, legislation, and regulations on market trends and the industry's performance.

The Department continues participation with the Saskatchewan Petroleum Research Incentive (SPRI) and the Petroleum Technology Research Centre (PTRC). SPRI and PTRC are involved in promoting expansion of enhanced oil recovery and other projects through research. The Department also plays a major role in a project to monitor the injection of carbon dioxide (CO<sub>2</sub>) into the Weyburn oilfield. The intent of the project is to understand more about CO<sub>2</sub> enhanced oil recovery and the capture of CO<sub>2</sub> because it is a greenhouse gas.

## **Responsible use and delivery of energy**

The Department needs policies and programs to encourage the responsible use of energy and the efficient and effective delivery of energy services in Saskatchewan. These policies and programs must ensure the efficient use of energy by Saskatchewan consumers. The Department must also ensure that there are no market restrictions for the delivery of electricity and natural gas services.

The Department must also develop energy conservation policies. The Department must participate in research and development to reduce the environmental impact of energy consumption. For example, the Department must investigate the impact of climate change on energy production and use.

The Department continues to monitor the changing circumstances in the North American electricity industry with respect to more open and competitive markets. The Department should receive public input and provide policy advice as the electrical industry undergoes changes. The Department also examines energy use regulation and assesses options for oil and natural gas pipeline regulation in Saskatchewan.

The Department is working with the University of Regina to establish the International Test Centre for Carbon Dioxide Capture. The Department is also on the National Air Issues Co-ordinating Committee. The Committee is responsible for implementing Canada's National Action Plan on Climate Change. The Department also represents Saskatchewan in the Greenhouse Gas Emissions Reduction Trading pilot project that encourages voluntary investment in emission reduction projects. This pilot project lays the groundwork for a possible future emissions reduction trading system.

## **Assessment and correction of royalties and taxes**

The Department must ensure that all of the non-renewable resource revenues, mineral rights taxes, and other fees due to the Government are accurate and complete. To do so, the Department must have rules and procedures so that all producers are aware of the deadlines for submitting required documents (returns) on time. The Department must then have competent staff check and review all returns for accuracy and

completeness. Delays in submission of returns by producers and undue delays in checking and reviewing those returns result in delays in proper assessment and collection of royalties and taxes due to the Government.

The Department must have rules and procedures to ensure that all producers complete and submit the necessary returns on a timely basis. The assessment of royalties and taxes is a very complex process, mostly based on self-assessment principles involving complex calculations. The Department must have a computerized system to process the returns submitted by producers without delays. The Department must also remind producers who do not submit their returns. Furthermore, the Department must promptly collect the assessed royalties and taxes from producers.

The Department has a royalty and production tax system. Also, the Department audits industry compliance with regulatory requirements. To encourage timely payments of royalties and taxes, the Department assesses penalties when amounts due are not paid.

## **Industry activities are safe and environmentally responsible**

The Department needs to ensure industry activities are conducted in a safe and environmentally responsible manner. Exploration, drilling, and extraction of resources must all be done in a safe and responsible manner.

The Department must ensure that it has the capacity for adequate field inspections so that the industry complies with departmental operating and environmental regulations. The Department must consult and educate companies on responsible and environmentally safe resource management techniques. The producers must be made aware of the consequences if they do not comply with departmental operating and environmental regulations. The Department must also address public concerns about environmental issues relating to exploration and extraction of resources.

The Department's officials meet and discuss environmental issues with officials of the oil and gas industry. It uses a fund called the Oil and Gas Environmental Fund to pay for expenses related to abandoned oil wells.

## Our audit conclusions and findings

In our opinion, for the year ended March 31, 2001:

- ◆ the financial statements of the Oil and Gas Environmental Fund are reliable;
- ◆ the Department had adequate rules and procedures to safeguard and control its assets and the assets of the Fund; and
- ◆ the Department complied with the authorities governing its activities and the activities of the Fund relating to financial reporting, safeguarding assets, revenue raising, spending, borrowing, and investing except for NewGrade payments that need authority as described below.

### NewGrade payments continue to need authority

Producers of gas on Crown land remit royalties to the Department under *The Crown Oil and Gas Royalty Regulations*. NewGrade Energy Inc. (NewGrade) buys some of this gas from producers to use in its heavy oil upgrader in Regina.

In 2000-2001, the Department paid \$2.4 million to NewGrade. The Department called this payment "NewGrade Royalty Rebate". The Department used Order in Council 7/89 as its authority for the payment.

The Order imposes the following conditions:

- ◆ Producers of the gas must pay the Department the full amount of royalties due under the law.
- ◆ Producers also must assign to NewGrade their right to the remission under this Order.
- ◆ The Department must pay the amount of the remissions to NewGrade for a minimum of fifteen years or until NewGrade's debt, guaranteed by the Government in December 1986, is paid.



The authority to issue this Order is section 24 of *The Financial Administration Act, 1993*.

Section 24 of the Act allows the Lieutenant Governor in Council (Cabinet) to remit (forgive) or exempt any person from liability to pay any tax, royalty, rental, or fee to the Crown.

We think the only persons who can be forgiven are the persons liable to pay the royalties. Because the Order imposes the condition that the producers must still pay, there is no forgiveness. The only change is that NewGrade receives the monies collected instead of the Crown. Therefore, the effect of the Order is not a remission to producers but a grant to NewGrade.

Section 24 of the Act gives Cabinet the power to remit royalties but not the power to make grants. Accordingly, the grant of \$2.4 million to NewGrade is not authorized under section 9 of *The Department of Energy and Mines Act*.

The Department records this grant as a reduction of revenue. The Legislative Assembly does not specifically approve reductions of revenue. We think the Department should record this grant as an expense. Recording the grant as an expense would provide the Legislative Assembly the opportunity to annually debate and provide the money to pay the grant. We think this is an important parliamentary principle.

We also reported this matter in our 1999 Fall Report – Volume 2 and previous reports to the Legislative Assembly. In these Reports, we recommended:

- ◆ The Estimates should present future payments to NewGrade under this agreement as expenditures.
- ◆ The Department should report these payments as an expense of the Department.

The Standing Committee on Public Accounts of the Twenty-Second Legislature considered this matter several times. This Committee made the following recommendation to the Legislative Assembly on May 25, 1992, March 17, 1993, and March 29, 1994:

If the remission of natural gas royalties is to continue to be paid to NewGrade Energy Inc. the amount to be provided should be included in the Estimates and presented to the Legislative Assembly for their consideration.

The Legislative Assembly agreed with the 1992, 1993, and 1994 recommendations of this Committee.

The Standing Committee on Public Accounts for the Twenty-Third Legislature considered this matter on December 13, 1996. This Committee reported as follows to the Legislative Assembly on April 24, 1997:

Your Committee reports that it disagrees with the Provincial Auditor's recommendations made at paragraphs 15.15 and 15.16, concerning the accounting of future payments to NewGrade Energy Inc. and the reporting of the payments of expenses. It is your Committee's view that the Department is in compliance with the accounting requirements provided for in section 24 of The Financial Administration Act as it pertains to Order in Council 7/89.

On November 24, 1998, the Standing Committee on Public Accounts considered this matter again and reaffirmed its decision reported to the Legislative Assembly on April 24, 1997.

On September 28, 2001, the Standing Committee on Public Accounts for the Twenty-Fourth Legislature considered this matter and did not concur with our recommendations.