

INSIGHT: HOOKED ON SIN • FAILING TO SAVE FOR THE FUTURE • HISTORY OF EXPLOITATION

ANALYSIS: FLAT TAX THREAT TO SERVICES • MISPLACED GENEROSITY • CORPORATE PROFITS SOAR

JANUARY 2011

# U·n·i·o·n

INSIGHT & ANALYSIS  
AN ALBERTA FEDERATION OF LABOUR PUBLICATION



## FUNDING OUR FUTURE

Why fixing our broken revenue system is the key to building a better, more prosperous Alberta

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## JANUARY 2011

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*Union* is a seasonal publication of the Alberta Federation of Labour (AFL). It is a magazine intended to provide insight and analysis into ongoing social, economic and political issues of concern to union activists, officers and staff. The AFL is Alberta's largest central labour body representing more than 137,000 Alberta workers and their families.

*Union* is published in electronic and paper versions. It is distributed free of charge to subscribers. Subscription requests can be made online at [www.afl.org](http://www.afl.org) or by contacting the AFL office. *Union* is edited collectively by the senior staff at the Alberta Federation of Labour.

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# First Thoughts

It hasn't been very fashionable to say this over the past 20 or 30 years ... but the reality is that neither our province nor our nation could function without government and the vital services it provides.

Broadly speaking, governments are the vehicles through which we pool our resources to meet public needs. They also play a central role in building the foundations of a strong economy and a healthy society.

Critics of the public sector like to suggest that tax dollars are wasted dollars. But the reality is that, for most individuals, families and even businesses, tax-funded services are the best deal going.

Without public Medicare, how many Canadians could afford high-quality care for themselves and their loved ones?

Without public schools, colleges and universities, how many people could afford to fulfill their potential and achieve their dreams?

And without well-trained workers, top quality infrastructure and low-cost health care (all provided courtesy of the public sector) how many small and medium-sized businesses could thrive?

The good news is that generations of Canadian voters and political leaders have understood the value of using the public sector to deliver services that benefit society but which individuals could not afford on their own.

The bad news is that 20 years of bad decisions on tax and royalty policy by successive Conservative governments has left our province's vital public services extremely vulnerable to under-funding.

As our provincial government begins to contemplate yet another austerity budget, Albertans need to change the direction of public debate.

Instead of buying the Conservative line that we have a spending problem (which we don't), we need to point out that what we really have is a revenue problem.

And instead of saying "the cupboard is bare, so we need to cut," what Albertans should really be asking is "why is the cupboard bare in the first place?"

The bottom line is that if we want our province to be all it can be, we need to protect our vital public services. But we can't do that without fixing our broken revenue system.

**Gil McGowan**  
President



## THIS ISSUE'S THEME:

### ***Our future depends on reforming revenue***

Alberta's broken revenue system has important implications for us all.

Without secure and predictable revenue, the province lurches from crisis to crisis as it tries and fails to provide those vital public services that Albertans want and which are the cornerstone of our economy and the bedrock of our communities. Without stable funding, there's no way to plan for our future, so we can ensure that our children and grandchildren have good jobs and good lives.

In this issue of *Union* magazine, Terry Inigo-Jones looks at how Alberta gets its money - and reveals how the province has become dependent on revenue from gambling and boozing.

Tony Clark explores Alberta's flat tax on personal income and finds that only one other jurisdiction follows the same tax model - Albania! The introduction of the flat tax was a boon to wealthy individuals, but bad news for our bottom line.

In *Misplaced Generosity*, Regan Boychuk reveals how Tory energy policy has cost Albertans tens of billions of dollars in lost revenue. The government has failed to meet its own targets in the amount of rent it collects from industry almost every year in the last decade.

In *Up, up - and Away!*, Inigo-Jones paints a picture of Alberta as a promised land for corporations, where profits soar and taxes fall. In *Failing to Save for Our Future*, Shannon Phillips looks at Alberta's Heritage Fund, weakened by years of backwards financial planning.

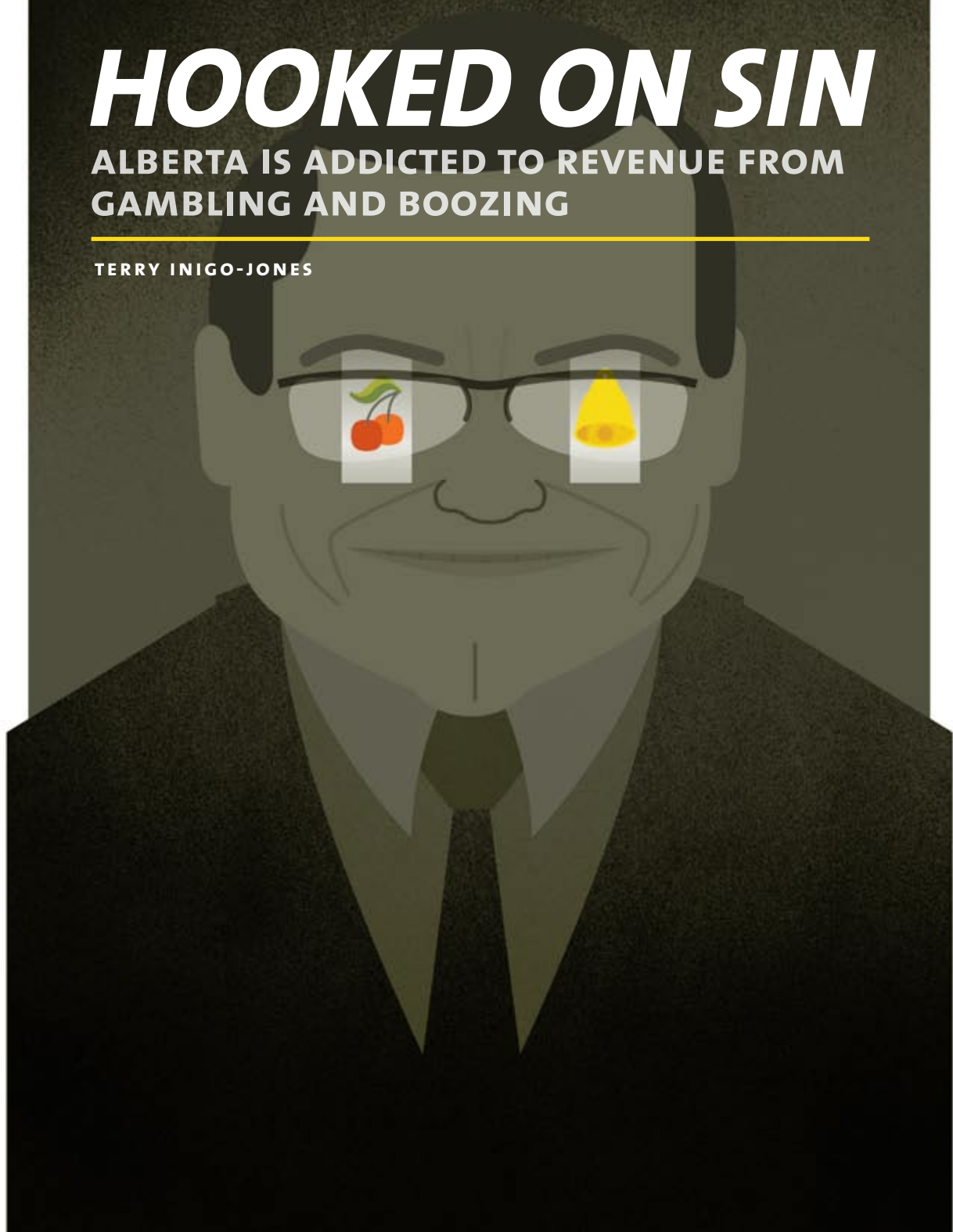
Finally, Winston Gereluk of the Alberta Labour History Institute shows that the fight over resource revenue, and the Alberta government's failure to collect a fair share, is a story that goes back decades.

# ***HOOKED ON SIN***

**ALBERTA IS ADDICTED TO REVENUE FROM  
GAMBLING AND BOOZING**

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**TERRY INIGO-JONES**





**I**n Alberta, we sit amid the oil and gas wells of the Western Sedimentary Basin and play in a (oil)sand box that contains the second largest oil reserves in the world. If our roads are not paved with gold, surely they must at least be paid for with oil.

But, when it comes to paying for our public services and infrastructure – including our roads, schools and hospitals – it’s not just oil to which the government of Alberta is addicted. We are also increasingly hooked on revenue from gambling and boozing. With natural gas prices predicted to stay low and Premier’s Stelmach’s recent rollback on oilpatch royalties, the government’s dependence on so-called sin taxes is growing.

Taxes on gaming and lottery are expected to earn the government \$1.3 billion in 2010-2011, according to a recent report in the Calgary Herald. Another \$700 million is expected from liquor taxes.

Together, the province will earn more from drinking and gaming than from natural-gas royalties, which are expected to be \$1.9 billion. Four years ago, the province earned \$6 billion from natural gas royalties.

Royalties from conventional crude oil, meanwhile, are also expected to come in lower than the figure for gaming and liquor at \$1.9 billion.

So, how did we end up addicted to gaming revenue and hooked on liquor money? Why is the government relying more and more on those sources of income, instead of revenue from natural resources, personal income taxes and corporate income taxes?

Two of the major factors responsible for the shifting balance of government revenue are changes to the province’s personal and corporate income taxes that led to reduced revenue and the government’s dependence on volatile natural-resource revenues.

### **The Attack on Taxes**

In 2000, Alberta became the first and only jurisdiction in Canada to abandon its progressive personal income-tax system and replace it with a flat-tax scheme. The immediate effect was a drop of \$1.5 billion in revenue the first year. The main beneficiaries of the change were the very wealthy, who have enjoyed a 25 per cent tax cut under the new regime. While low-income earners benefitted from an increase in personal and spousal exemptions, the main outcome of the change was to shift the burden of taxation from the rich to the middle-income earners.

“That flat tax was an extremely foolish thing to do,” says Greg Flanagan, a public finance economist who has taught in various colleges and universities for 30 years, most recently as Assistant Dean, Faculty of Management, University of Lethbridge (retired). He is also a research associate at the Parkland Institute. There was no political need for the government to introduce the flat tax, it cost a huge amount in lost government revenue, and there is no evidence to support the notion that it stimulated work effort or boosted the economy, he says.

Not satisfied with reducing only one revenue stream, the Progressive Conservative government also attacked corporate income taxes. Since 2001, Alberta has cut its corporate rate to 10 per cent from 15.5 per cent, making it the lowest rate in Canada. Restoring the rate to 15.5 per cent would boost revenue by \$1.1 billion.

The government’s overall tax structure depends heavily on volatile natural-resource revenues. When oil and gas prices slump, its income from those sources also slumps, and so a greater fraction of its total income will come from other revenue streams – including gaming and liquor.

However, adding to the problem of volatility in commodity prices and its effect on government revenue has been the government’s own fluctuating policies on royalty rates. The recent decision to bow to industry pressure to cut royalty rates will mean reduced government income.

These attacks on taxes – which benefitted wealthy individuals and wealthy corporations – came at a time when the economic wealth of the province was surging, says Liberal MLA Kevin Taft in his report *Follow the Money, Where is Alberta’s wealth actually going?*, which was compiled with the assistance of Mel McMillan, professor of economics at the University of Alberta, and Junaid Jahangir (PhD candidate).

Describing the province’s “super-sized” economy, Taft says:

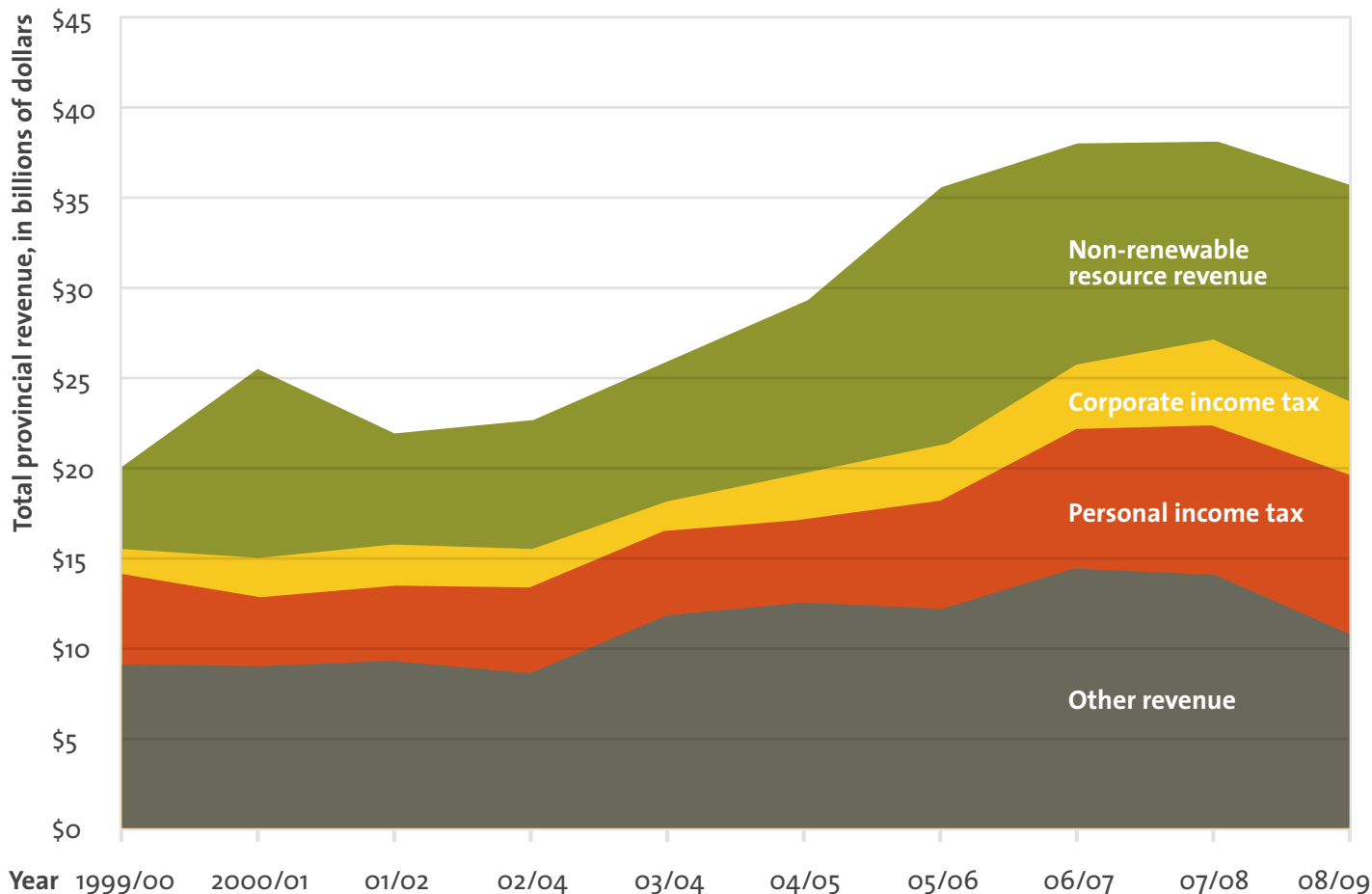
- Alberta’s economy grew in real terms per capita by 76 per cent from 1989 to 2008, reaching a level 73 per cent higher per person than the average of the other provinces. Compared with the rest of Canada, Alberta is a very wealthy place.



- Personal income in Alberta, after adjusting for inflation, rose from \$28,440 per person in 1989, to \$39,524 in 2008. The 2008 average for the other nine province was just over \$31,000.
- Corporate profits have soared in Alberta during the past two decades, from \$3,635 per capita in 1989 to \$15,050 in 2008 (adjusted for inflation) – a rise of 414 per cent.
- In 2008, corporate profits per capita in Alberta were well over three times the average in the other nine provinces.

In the report, Taft asks: “Above all, if Alberta is Canada’s wealthiest province – as it clearly is – why is our current provincial political debate one of cuts and crises, instead of investment and prosperity? Even with the downturn in the global economy, shouldn’t Alberta be in better financial shape? In short, where has all the money gone?”

## Alberta's Dependency on Oil and Gas Revenue, 1999–2000



The problem is that while government revenue has risen – by 23 per cent per capita between 1989 and 2008 according to Taft – the economy has grown faster than government revenue and when measured against Gross Domestic Product (GDP), revenues actually fell 25 per cent.

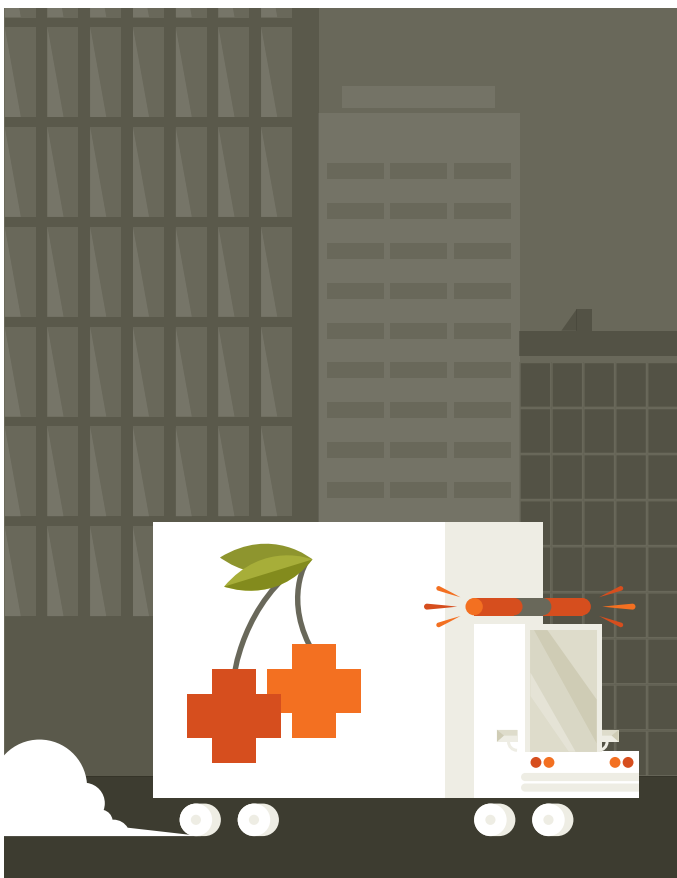
As a portion of the economy, Alberta collects significantly less than other provinces, says Taft, and it collects a significantly smaller proportion of personal and corporate incomes. “Alberta government revenues are a smaller portion of the provincial economy than those of any other provincial government. With the exception of a spike in 2001, Alberta’s revenues were below 20 per cent of GDP every year since 1993,” says Taft’s report. “From 2002 to 2008 they averaged just under 16 per cent.”

This compares with Ontario and Saskatchewan collecting 19 per cent of GDP, while B.C. collected 21 per cent and Manitoba 24 per cent.

The evidence says Alberta is a wealthy place and will continue to be so for some time. As Taft points out, almost half the world’s oil reserves that are available for free-market development are in this province. “As a result, in 2010 CAPP (the Canadian Association of Petroleum Producers) forecast that \$1.07 trillion will be invested in Canada’s oil and gas industry of the next 25 years, most of it in Alberta. (A trillion is a thousand billion.) CAPP estimates the economic impact of this on Alberta will be \$2.55 trillion.”

By not collecting enough revenue, Alberta has been missing out on an opportunity to invest in the future, for a time when our non-renewable resources have run out.

“By any financial measure, Alberta is a very wealthy place. But that wealth is based on a commodity, and history repeatedly shows that economies based on a commodity are prone to dramatic failures, whether the commodity is renewable (e.g.,



rubber, wheat, tulips) or non-renewable (e.g., copper silver, coal),” says the report.

“Alberta’s super-sized economy will not last – unless Albertans manage it well and seize the opportunities it presents. Albertans have the chance to do something extraordinary: to build a permanent foundation for prosperity.”

### **A Plan, A Plan, My Province for a Plan ...**

What’s needed is a real plan covering government spending and revenue, one that will get us off the revenue rollercoaster, which leads to essential services being threatened every time revenue dips.

The first stage of that plan, according to Flanagan, is to establish what Albertans need in the way of public services. How much health care, education, transportation, infrastructure and other services are required to make the kind of communities in which we want to live.

The next step, he says, is to determine which services should be provided by the public sector, rather than by the private sector, because it is more efficient or because we don’t want those services affected by short-term fluctuations.

In good economic times or bad, these demands should be stable and the province should be able to meet them. For example, if your mother needs life-saving heart surgery, it’s no good telling her she has to wait until the economy improves.

Also, it is more efficient, and cheaper, to keep some services in the public sector. The single-payer public health-care system in Canada is enormously efficient compared to the system in the U.S., Flanagan says. Similarly, education is expensive, but the public has shown that it wants the public sector to be involved in providing it.

Once we have established the spending needed to provide these services, the province should devise a revenue system to meet those needs. Currently, says Flanagan, “we are hugely short in a normal revenue stream and very dependent on our resource revenue, which in many cases will be gone at some point.”

In order to prepare for the time when resource revenues disappear, he suggests creating a natural resource revenue fund, not unlike the Heritage Fund, that puts income from natural resources aside, converts it into financial capital that generates income. The fund could be used to pay for physical, tangible investments, such as roads, dams and educational facilities. Income from the fund, but only income, could be used to help pay the public sector’s annual operating budget.

Clearly, setting aside natural-resource revenues means there will be a shortfall, at least until the fund has grown big enough to generate significant income, and that lost revenue must be replaced by other means.

“If I could play around as finance minister for a moment, I would introduce a sales tax in a minute, I would change the income tax back to an extremely progressive tax – I would get the revenues up that way,” says Flanagan.

McMillan, however, says there are issues with introducing a sales tax, which tends to be a regressive tax. The major argument in favour of a sales tax is that it would add a relatively stable source of revenue, but if the underlying volatility of relying on fluctuating natural-resource revenue is not fixed first, the sales tax becomes just an additional tax, with the volatility remaining.

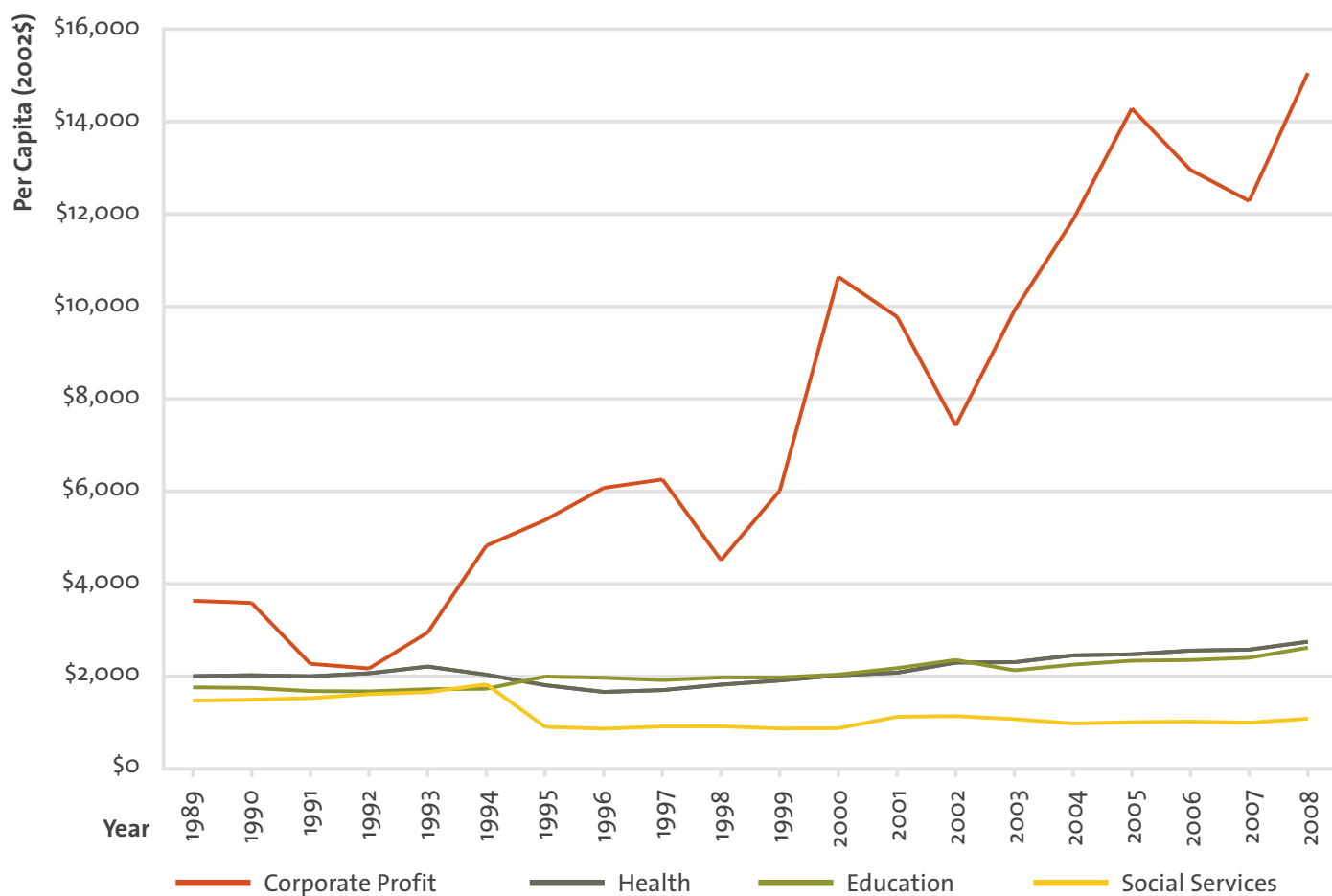
“It may just continue the volatility, but with higher taxes and higher spending. I don’t think the Alberta taxpayer will be very interested in that option,” he says.

For most provinces, the major sources of revenue are personal and corporate income taxes and it is in these areas that Alberta could look to generate more income.

McMillan favours abandoning the flat tax on personal incomes and moving to a structure with two or three different rates, with higher rates for people with higher incomes.

“These are people that benefit greatly from the Alberta economy and the public sector. I have no qualms in paying what I would consider my fair share, as long as everybody else is paying theirs.” **U**

### Alberta Health, Education & Social Services Expenditure compared to Alberta Corporate Profit



Source: CANSIM · Social Services\*: AB v632444 · Post Secondary Education\*: AB v632453 · K-12 Education\*: v632452 · \* Provincial and Local government consolidated data  
 Health Expenditures: AB v645792 · Corporate Income: v687290 · CPI (2002=100): AB v41694625 · Population: ABv469503

# ALBERTA'S FLAT TAX PUTS VITAL PUBLIC SERVICES AT RISK

ONLY ALBANIA HAS FOUND OUR INCOME-TAX  
REGIME WORTH EMULATING

TONY CLARK



**A**s the Alberta government posts a record \$5-billion budget deficit for 2010-2011, the largest in the province's history, Albertans are right to ask: "Where did the money go?"

The government blames "global volatility" for the province's sagging bottom line, but the downturn in the global economy is only part of the story surrounding Alberta's recent money troubles.

A better explanation can be found in our overall revenue mix. For the highest income Albertans, personal income taxes are too low. The same goes for taxes on large corporations. Ten years ago, Alberta gutted its most stable sources of revenue – income taxes from individuals and corporations. Instead, we rely on a mix of unreliable natural-resource revenues and revenues from liquor, gambling and cigarettes.

When Alberta moved from progressive income taxes to a flat income-tax system, it erased billions of dollars in revenue. This undermined the financial stability the tax system gave us, putting our vital public services at the mercy of the global

economy and leading to pressure for layoffs, budget cuts and privatization.

While the poor and middle class saw no benefit from the flat tax – and were faced with the spectre of public-sector layoffs and deteriorating public services – there was one segment of the population that gained - the very wealthy.

## The Complicated Birth of the Flat Tax

In 1998, the Alberta government began the process of moving from a progressive income-tax system, where tax rates increase as income increases, to a flat-tax system where all income levels are taxed at the same rate.

Under Stockwell Day, the Alberta Treasurer in 1999, the government announced a move to a single tax rate: 11 per cent for all income levels, with increased personal and spousal exemptions.

Prior to the flat tax, Alberta levied 44-per-cent provincial taxes on the federal personal income taxes. In other words, whatever amount in income tax you paid to the federal government, you made another payment of 44 per cent of that total to the Alberta government.

Because the federal income tax was progressive (meaning those who could afford to pay more were charged more and those who could afford to pay less were charged less), low-income Albertans paid about 7.5 per cent of their income in provincial taxes. However, with Stockwell Day's proposed flat tax, low-income Albertans would have seen their taxes increase from 7.5 per cent to 11 per cent. Conversely, high-income Albertans would have seen their income tax decrease from 12.75 per cent to 11 per cent. Middle-income Albertans would see a slight decrease in taxes.

To complicate matters, the federal government announced it would reduce the federal income taxes for the \$29,590 to \$59,180 income bracket from 26 per cent to 24 per cent. This would have meant that under the flat-tax scheme, every income group except for the wealthiest Albertans would see their personal income taxes actually increase.

In response to the federal income-tax cut, the Alberta government hastily reduced the flat-tax rate from 11 to 10.5 per cent and increased personal and spousal exceptions.

The final round of tinkering with the flat tax came in

early 2001, when the new Provincial Treasurer Steve West announced plans to lower the flat-tax rate from 10.5 per cent to 10 per cent. The final cost of these tax reductions to the Alberta Treasury was estimated to be \$1.5 billion a year in 2001.<sup>1</sup>

Under the 10 per cent flat tax, low-income Albertans only saw a tax cut because of the dramatic increase in personal and spousal exemptions. It was the increases in personal and spousal exemptions that benefitted poor and middle-class Albertans, not the flat tax. When changes to personal and spousal exemptions were announced, an estimated 132,000 low-income taxpayers were removed from the province's tax rolls.

Leaving aside exemptions, Alberta's middle- and low-income earners paid higher taxes with the 10-per-cent flat tax than if the Alberta government had maintained the old 44 per cent tax-on-tax system. People earning between \$30,755 and \$61,509 would have paid only 9.68 per cent under the old system instead of the 10 per cent flat tax.

<sup>1</sup> Alberta government, "Alberta's single income tax rate lowered to 10 percent," January 3, 2001, <http://www.alberta.ca/acn/200101/10160.html> accessed October 6, 2010



The wealthy, meanwhile, were left with more cash in their pockets. Those earning between \$60,510 and \$100,000 saw their Alberta income-tax rate from to 10 per cent from 11.44 per cent; those earning more than \$100,000 had rates drop to 10 per cent from 12.76 per cent.

The wealthy in Alberta used to pay higher personal income taxes. Other wealthy Canadians pay higher taxes. All of this suggests Alberta's wealthy can afford to pay more – to pay their fair share – now.

The simplest, most straightforward way to capture more revenue from Alberta's ultra-wealthy would be for the government to implement a surtax. This is an add-on tax that applies when personal income exceeds a certain level and targets only wealthy Albertans who have inordinately benefitted from the flat-tax system.

Surtaxes are simple to understand, easy to apply and many Canadians are familiar with them. In fact, Alberta had an eight-per-cent surtax before the 2001 shift to the flat-tax system. Other provinces have surtaxes aimed at their wealthy populations. Ontario has a two-tiered surtax, which climbs as taxable income increases: 20 per cent on provincial taxes higher than \$4,006 and 36 per cent on provincial taxes in excess of \$5,127.

The government of P.E.I. levies a 10-per-cent surtax on provincial taxes higher than \$12,500. P.E.I. estimates that the surtax applies to about 3,700 people with the top 3.5 per cent of taxable income.

### **Personal Tax Simulations: Two Options to Consider for Alberta**

Simply re-applying Alberta's previous surtax, eight per cent on \$3,500 of taxable income, would allow the Treasury to reap more than a quarter of a billion dollars in personal income-tax revenue, the bulk coming from high-income earners. However, this system still sees slight tax increases for working people (individuals earning \$60,000 to \$100,000), even if only marginally.

### **The P.E.I. Surtax Model**

If the Alberta government were to impose the same surtax P.E.I. applies to its wealthy citizens, an additional \$157 million of addition revenue could be gained. Under this surtax, only individuals earning more than \$100,000 would see an increase. This tax increase would not be onerous by anyone's standards. People earning between \$100,000 and \$250,000, for example, would see an average tax increase of about \$414 on their tax bill.

Some might claim that if we increase their taxes, the wealthy will pack up and leave. Aside from Alberta's non-existent provincial sales tax and low-low gas taxes, the province's generous personal and spousal tax credits leave ample room for surtaxes aimed at the wealthy.

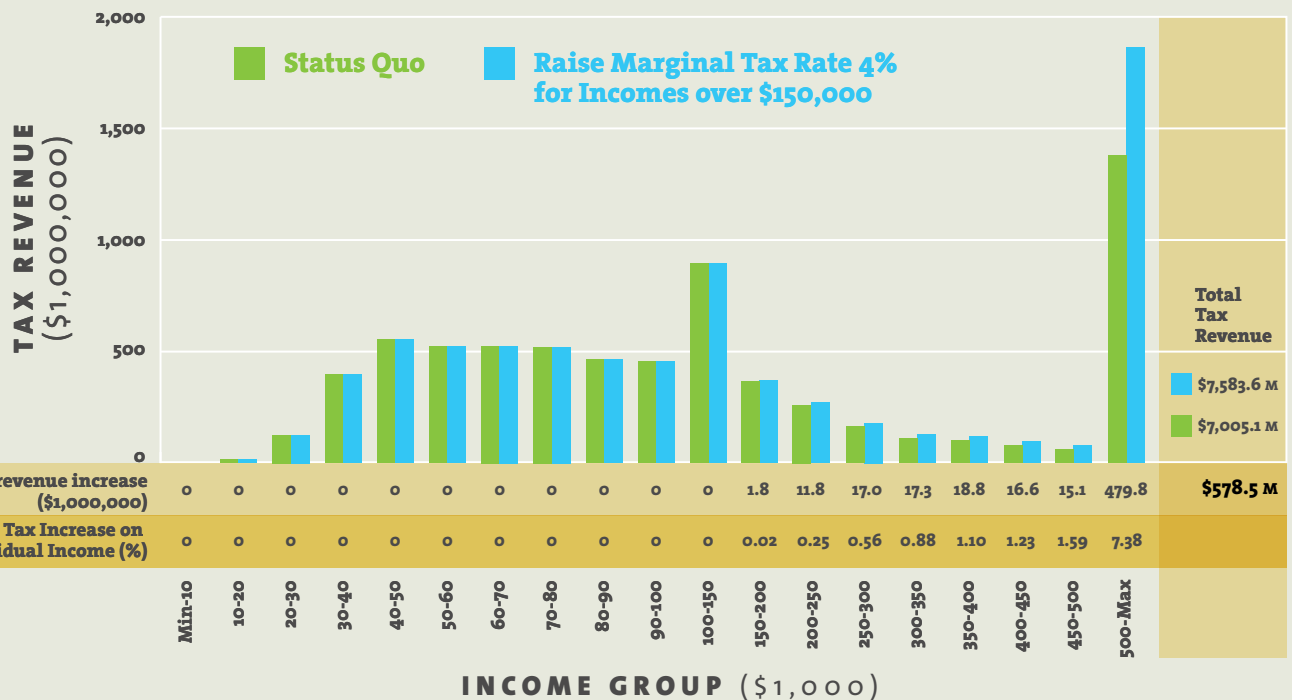
With P.E.I.-style surtaxes, every income group would still pay lower taxes in Alberta than elsewhere. This is because everyone claims basic personal amounts, despite their income. Leaving aside other tax issues such as sales taxes and gas taxes, Alberta's tax regime is low compared to other provinces.

### **Flat Taxes A Rarity Around the World**

Only seven American states use the flat-tax system, but American states deliver far fewer programs than Canadian provinces. Even after the George W. Bush era, the U.S. federal government still has a progressive tax system.

Around the world, only nine Eastern European countries have embraced the flat tax with any enthusiasm. All flat-tax rates in Eastern Europe, except one, are higher than Alberta's 10 per cent flat rate – for example, Estonia levies a 24 per cent flat tax. Albania's flat tax is the lowest national flat tax rate in the world: Alberta and Albania share a 10 per cent flat tax rate.

## Raising the Tax Rate Only For the Wealthiest Albertans – 2006 Tax Year Modelling



### Increase Alberta's tax rate for those earning more than \$150,000/year

A better way to change the system would be to increase tax rates for those earning more than \$150,000/year by up to four per cent. This small increase would leave taxes the same for low- and middle-income people. It would mean someone earning \$150,000/year would pay slightly more – but not much more.

Alberta's marginal rates for the very wealthy are by far the lowest in Canada. A simple upward adjustment in taxes for those earning over \$150,000 would net us more than \$500 million in extra revenue every year, and would still see us charge the lowest marginal rates in Canada for the super-rich.

As the above simulations show, there is plenty of room to get much-needed government revenue through targeted taxation of the super-wealthy, who saw a 25 per cent tax cut in 2001 and have enjoyed far lower rates than the rest of the country for a decade. **U**

*Tony Clark is the former director of communications for the Alberta NDP Opposition. He now calls Vancouver home where he works as a writer and researcher and remains involved in local, provincial and federal politics.*

Analysis for this article was based on Statistics Canada's Social Policy Simulation Database and Model and the article "Alberta's Single-Rate Tax: Some Implications and Alternatives," by Mel McMillan published in 2000 in the Canadian Tax Journal (Vol. 48, No. 4). The assumptions and calculations underlying the simulation results were prepared by Tony Clark and the responsibility for the use and interpretation of these data is entirely that of the author.



# *Misplaced Generosity*

How Tory energy policy has  
cost Albertans tens of billions  
in lost revenue

**REGAN BOYCHUK**



**F**or a brief moment in 2007, Alberta's dominant industry was subjected to a degree of democratic influence. The public, as owners of the oilpatch resources, actually had a say in how they would be developed by being included in consultations during the Alberta Royalty Review.

This public participation was to be short-lived.

As DeltaOne Strategic Energy president Peter Linder later told the CBC, for decades, royalties had been set by the government in consultation with the oil and gas industry. "The public has – and should have – really no say in this matter because they don't understand the intricacies of the royalty system," he explained. "Stelmach was the first premier ever to make it a public situation – it should have never been public in the first place."

Capping a series of concessions to the oilpatch, the provincial government's so-called "Competitiveness Review" of 2010 took the last few steps in reversing that historical anomaly of public engagement. Unlike in 2007, the Competitiveness Review excluded the public. Instead, it revived the former practice of holding consultations with executives from oil and natural gas companies and the financial sector, including briefing sessions, surveys, interviews, a workshop, focus groups and meetings with industry lobby groups. These groups' main concerns led to the royalty cuts adopted by the government on March 11, 2010.

*Left: An oil and gas drilling rig near Airdrie. A Calgary Herald/Edmonton Journal poll in 2007 said 88 per cent of Albertans didn't think we were getting our fair share of revenue from industry.*

*Photo: Larry MacDougal*

Three years after the Alberta Royalty Review, the province's most important file had been returned to its undemocratic status quo. This effectively reversed the compromises of the Stelmach government's 2007 New Royalty Framework, itself a compromise of the Royalty Review Panel's recommendations.

All this in spite of public opinion. The 2007 Royalty Review Panel's recommendations were overwhelmingly supported by Albertans, according to a Calgary Herald/Edmonton Journal poll, which said 88 per cent didn't think we were getting our fair share from industry and 67 per cent wanting Stelmach to adopt the panel's report in its entirety. The Calgary Herald later reported that the March 2010 royalty cuts were opposed by 58 per cent – including two-thirds of the ruling Progressive Conservative Party's supporters.

Without the sort of royalty reform that the Tories have demonstrated they are incapable of accomplishing, Alberta will continue to lose an immense amount of revenue from the oilpatch. The true scale of the excess, unearned profits pocketed by industry reveals just how misplaced the generosity of Tory energy policy has been.

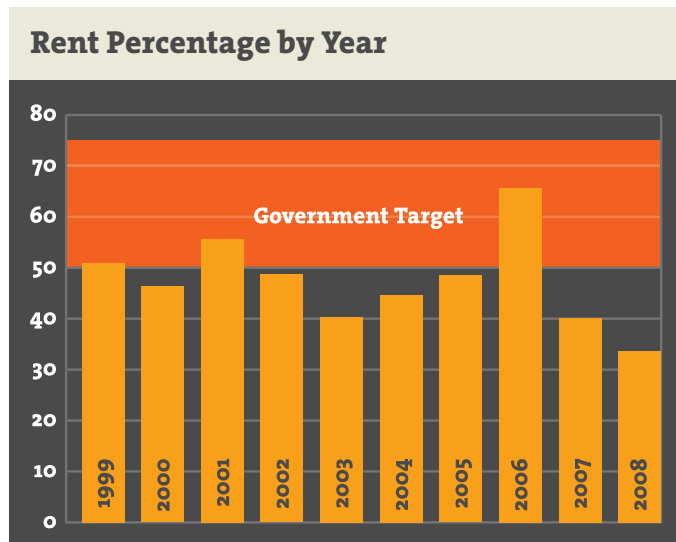
To get a sense of how much wealth is generated by Alberta's natural resources and how that wealth is distributed, the Parkland Institute used statistics on the Alberta oilpatch compiled by the Canadian Association of Petroleum Producers (CAPP). The industry's own statistics help us gauge the health of the industry to see whether it was necessary for the provincial government to administer further royalty medicine to relieve the aches and pains about which the industry was complaining.

The scale of wealth produced from Alberta's oil and natural gas is truly stunning. Over the last decade (1999-2008), the value of our province's conventional oil and natural gas production

(excluding the oil sands) exceeded \$525 billion. In addition to paying almost \$93 billion in royalties and nearly \$11 billion in land sales to the province for exploration rights, industry spent \$273 billion on exploration, development and operating. This left oil and natural gas companies operating in Alberta with more than \$148 billion in pre-tax profit.

Alberta Energy simultaneously maintains two targets for how much of the value of our oil and natural gas it wants to capture with royalties and land sales; one is based on a share of total industry revenue, the other on a share of resource “rent.” Their share-of-revenue target has been lowered over the years from 35 per cent under the Lougheed government down to 20 to 25 per cent today, a share it has managed to capture in only one year since 2001.

But share of revenue is a crude measure. Another approach is to look at these profits in terms of economic or resource “rent.” Resource rent is the financial surplus left after recovering costs and a reasonable profit from selling a resource. As we use it here, rent is the annual value of oil and natural gas



produced minus annual costs for exploration, development and operations minus a “normal” 10 per cent margin on industry costs. What remains is the “rent.” Royalties and land sales aim to capture that rent for the owners – in our case, Albertans. Whatever resource rent is not captured by royalties and land sales remains in corporate coffers as excess, unearned profits – excess because it is over and above a normal rate of profit.

To illustrate, assume industry spends \$45 to produce \$100 worth of oil or natural gas. A 10-per-cent margin on its costs would be \$4.50. The remaining financial surplus or “rent” would be \$50.50 (\$100 in oil or gas minus \$45 in costs minus the \$4.50 profit margin). After paying \$17 in royalties and land sales, \$33.50 in “excess” profit over and above a normal 10-per-cent profit is left in corporate coffers. That gives \$38 in pre-tax profit on costs of \$45. While this may seem too good to be true, it mirrors actual 2008 statistics from Alberta’s oil and gas industry. The \$17 in royalties and land sales captures only about 34 per cent of a potential \$50.50 in total rent—precisely the proportion of rent the Alberta government captured for its citizens in 2008.

The share of rent the province aims to capture is 50 to 75 per cent. Between 1999 and 2008, the share of rent captured by royalties and land sales in Alberta averaged only 47.4 per cent, ranging from a low of 33.7 per cent in 2008 to a high of 65.6 per cent in 2006. Alberta failed to capture its target range of rent almost every year last decade:

### Taxpayers pick up \$1.7 billion gas bill

More than half the cost of natural gas used by oil sands extractors is paid for by taxpayers, according to a report in The Tyee – <http://thetyee.ca>.

Taxpayers will be on the hook for about \$1.7 billion in 2010. That figure will rise as the use of natural gas grows, says the story published in November 2010.

“Oil sands operations currently consume about one billion cubic feet of gas per day, heating thick bitumen so it can be extracted from surrounding rock and gravel. This ... eats up about 20 per cent of Canada’s natural gas demand and may balloon to 40 per cent by 2035.”

Much of the cost of the natural gas is written off against corporate taxes. The story says: “Companies operating in Alberta’s oil sands are allowed to deduct fuel costs from their provincial and federal taxes. They are also allowed to double dip and deduct these same fuel expenses from the royalties payable the Alberta taxpayer.”



Pumpjacks at work pumping crude oil near Halkirk, Alta. In 2008, while industry complained about a coming \$1.4 billion increase in royalty rates, its excess profits soared to nearly \$23 billion

*Photo: Larry MacDougal*

The Tories' failure to set royalties to capture even the bottom of their target range for resource rent has cost Albertans dearly.

If the government had managed the middle of their 50 to 75 per cent range, it would have collected an additional \$37 billion over the last decade – almost \$5 billion more in 2007 and almost another \$10 billion in 2008. If royalties had been set to capture the upper end of the target range, Albertans would have enjoyed another \$65 billion in revenue – almost \$8 billion more in 2007 and another \$14 billion in 2008.

Imagine what another \$37 to \$65 billion in revenue could have done in Alberta in terms of funding education and health care, addressing environmental issues, diversifying our economy, building much-needed infrastructure or simply saving for future generations.

Tens of billions more in excess, unearned profits aren't even targeted for collection. Remember, Alberta Energy doesn't even try to capture 100 per cent of the resource rent, only 50 to 75 per cent. That's why, even if Alberta Energy did manage the upper

range of its targets, oil and natural gas companies would still have been left with \$56 billion in excess pre-tax profits over the last decade. One assumes the private sector's legendary efficiency would allow it to somehow survive on mere 11-figure excess profits.

While the battle surrounding the Alberta Royalty Review was raging in 2007, the industry's excess profits more than doubled from 2006 to more than \$13 billion. In 2008, when the industry was moaning about the new royalty regime's increased take of \$1.4 billion sometime in the future, its excess profits almost doubled again to nearly \$23 billion.

In all, between 1999 and 2008, Alberta's traditional oil and natural gas industry enjoyed more than \$121 billion in excess, unearned pre-tax profits – more than a quarter of which accrued in 2007 and 2008. Yet throughout the recession in 2009 and 2010, the Stelmach government's numerous drilling incentives and royalty reductions forfeited another \$3 billion in badly needed revenue.

On the one hand, Alberta Energy recognizes “a decision to not capture the full [economic rent] amounts to a decision to sell the province’s resources at less than their full value.” But on the other, Alberta’s low royalty targets are considered too greedy for some. One former energy minister told the Auditor General in 2007 that 50 per cent of rent was the appropriate target.

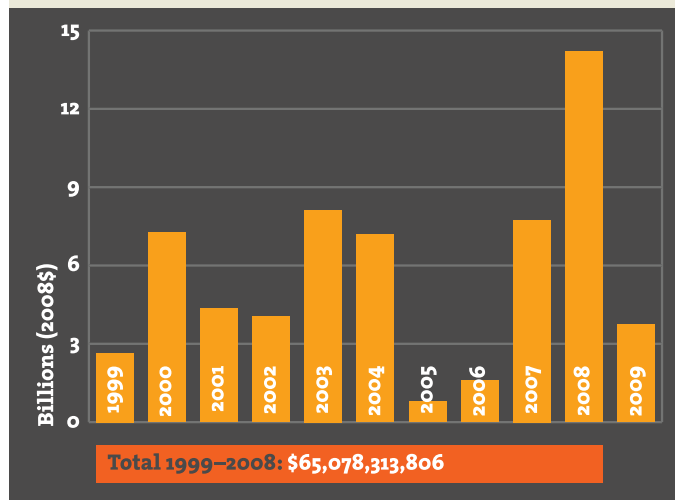
In spite of claims that higher royalties would cripple oilfield investment, the stats tell a different story. Actual industry investment in exploration and development remained virtually unchanged the year following the royalty changes were announced in 2007 – a rather surprising fact considering the looming royalty increases and the severity of the recession that took hold in the final quarter of 2008. After the decision had been made to raise royalties, land sales (an indicator of future investment) actually increased by more than 20 per cent in 2008. In 2009, when higher royalties were already in effect, land sales declined only marginally, despite the recession, and remained above 2007 levels. It seems oil and natural gas companies planned to continue investing in Alberta despite the increased royalties.

This simple accounting of industry profits produces admittedly crude estimates. These calculations are not intended as a forensic accounting of every dollar lost over the last decade. Rather, this is a simple attempt to sketch the enormous scale of oilpatch profits in an effort to put the campaign against higher royalties into perspective. The figures are rough – overestimating costs and leaving some factors out—but they still paint a reasonable picture of the industry’s pre-tax profits.

Since Premier Stelmach took office and kept his promise to review Alberta’s royalty regime, excess pre-tax profits quadrupled – from less than \$6 billion in 2006 to almost \$23 billion in 2008. Yet this is the context for the campaign waged by oil and natural gas companies against higher royalties and for the government’s repeated capitulation to industry pressure.

A review of the scale of industry profit raises serious questions about whose interests the Tory government is serving. “The interests of the owners are not foremost in the minds of the

## Revenue Lost by Not Maximizing Share of Rent Targets

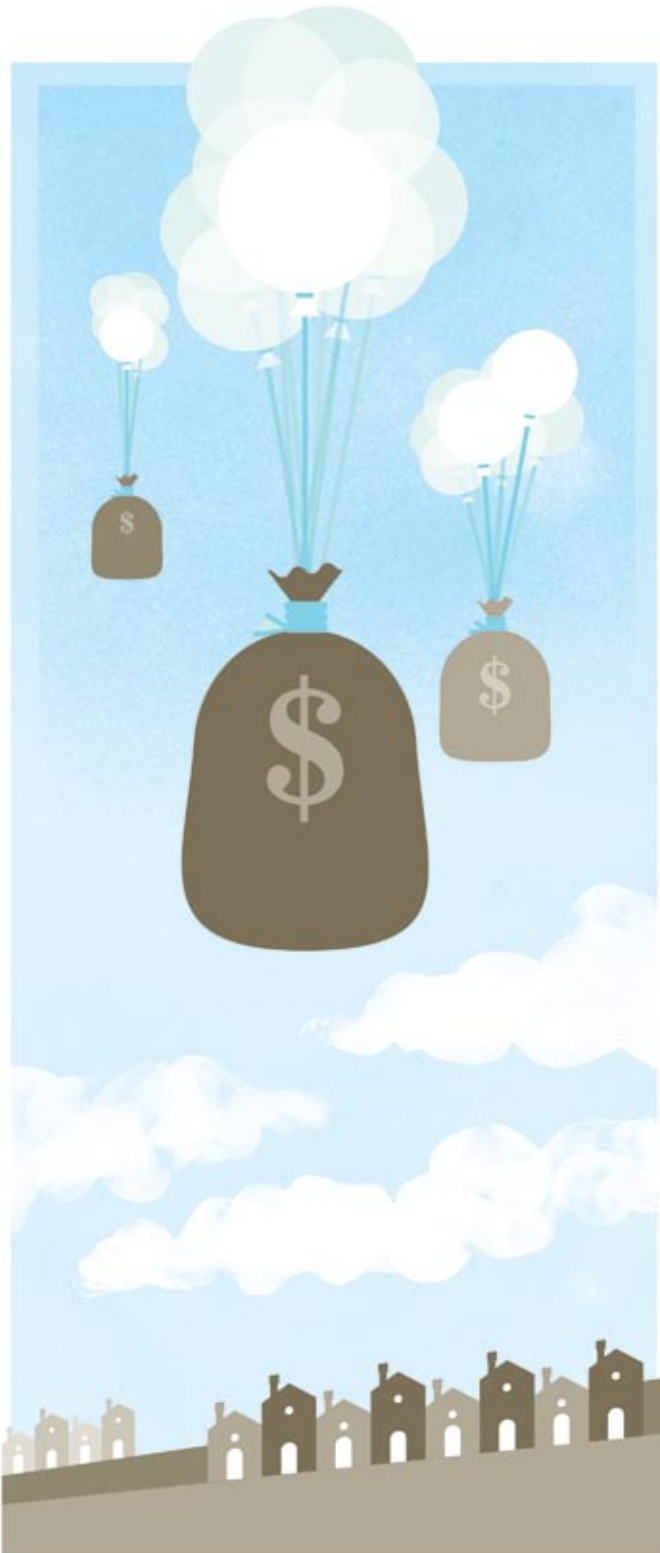


people who make the decisions,” said University of Alberta energy economist and 2007 Alberta Royalty Review Panel member André Plourde. “What concerns me in all of this is who’s speaking for the owners? It’s clear the government isn’t and hasn’t been for some time.”

This episode serves as another stark illustration of Alberta’s substantial democratic deficit. The distance between public opinion and public policy in this province is often considerable – and the ease with which industry was able to reverse even the modest proposals of the 2007 Royalty Review Panel should give pause.

In this case, as in many others, the industry’s gain was Albertans’ loss. It is reasonable to expect this state of affairs to continue unless an aroused public once again intervenes. Ignoring the self-serving lectures from the oilpatch that Albertans are not capable of understanding the intricacies of this issue, an informed and engaged public is the only hope Alberta’s natural wealth might one day be managed in the public interest. **U**

*Regan Boychuk is a Public Policy Research Manager with the University of Alberta’s Parkland Institute, which has just published an in-depth study of oilpatch profits (including the oil sands) that can be viewed online at <http://parklandinstitute.ca>.*



# Up, Up – and Away!

CORPORATE PROFITS SOAR, BUT ALBERTA

LETS ITS SHARE OF THE MONEY GO

## TERRY INIGO-JONES

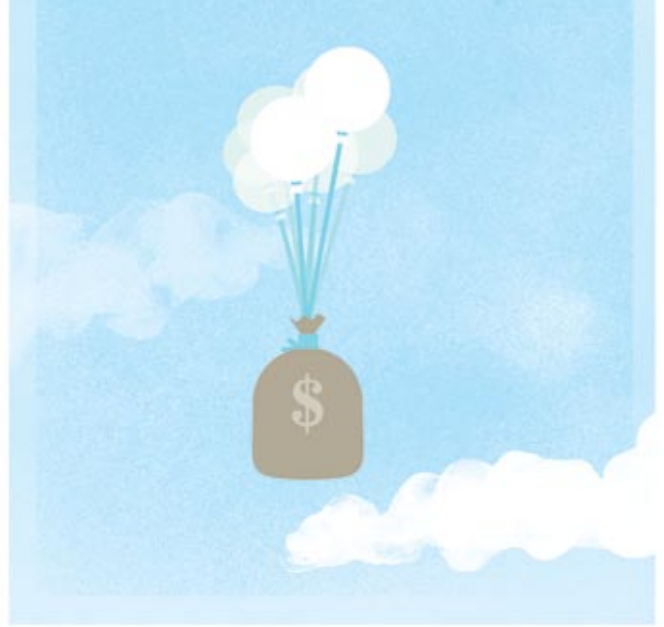
Welcome to Alberta, the Promised Land – at least if you're a wealthy corporation - where profits go up, up and up while taxes go down.

Corporate profits in the province have soared in the last two decades, from \$3,635 per capita in 1989 to \$15,050 in 2008 (adjusted for inflation), a rise of 414 per cent, according to Liberal MLA Kevin Taft in his report *Follow the Money, Where is Alberta's wealth actually going?*

In 2008, corporate profits per capita in Alberta were more than three times the average in the other nine provinces, he says.

While the corporations make lots of money on one hand, the Alberta government gives them more in the other hand. Since 2001, Alberta has cut its corporate income tax rate to 10 per cent from 15.5 per cent, making it the lowest in Canada and depriving the Alberta treasury of \$1.1 billion annually.

In 2008 corporate profits in Alberta were \$66 billion, compared to Ontario at \$58 billion, according to Erin Weir, a senior



economist with the International Trade Union Confederation and a former economist with the United Steelworkers union in Canada. However, corporate income tax revenue in Alberta came in at \$4 billion, compared to the \$7 billion raised in Ontario.

But the corporate tax madness doesn't stop there. The Alberta government is also giving away billions in tax dollars to the U.S. government.

"Many Alberta corporations are affiliates of American-based corporations," says Weir. "When they repatriate profits to the U.S., they pay the American federal corporate income tax minus a credit for corporate income tax paid in Canada. As Ottawa and Edmonton cut their combined rate below the American rate, these corporations must pay the difference to Washington."

The U.S. government tax rate is 35 per cent, while the combined rate in Canada is 25 per cent (15 per cent charged by federal government and 10 per cent by Alberta). Last year, the 10-per-cent difference flowing to the U.S. from American companies operating – and earning their profit – in Alberta was \$2 billion. Alberta could double its rate, keep that \$2 billion here and the bottom lines of those U.S. companies would remain the same.

"The Alberta government has tremendous potential to collect more revenue through resource royalties and corporate taxes," says Weir. The usual objection to raising corporate taxes is that it would destroy Alberta's competitiveness, but that objection is flawed, he says.

"First, Alberta's oil and gas reserves are immobile. They are not like a factory that can relocate anywhere in pursuit of lower costs." While some marginal development might shift to other jurisdictions for a while, it will return to Alberta when commodity prices rise or when reserves are depleted elsewhere.

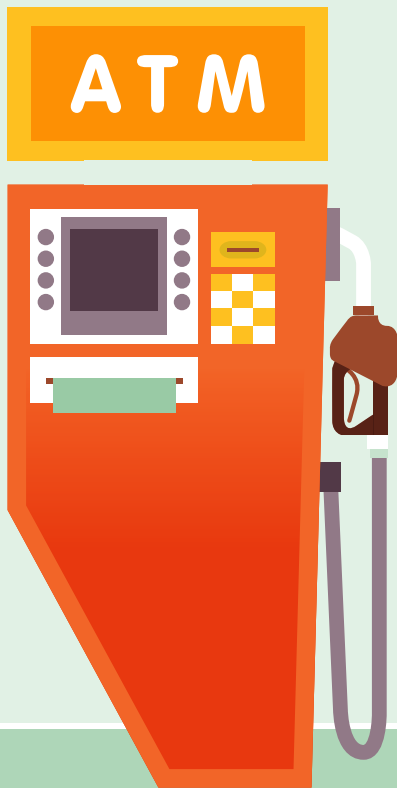
"Delaying some marginal development seems like a small price to pay for a better return on existing production and on more lucrative development."

The oil sands, meanwhile, has few viable competitors vying for the interest of business owners.

"The only comparable geology is the Orinoco oil sands in Venezuela. But Alberta has plenty of room to charge higher royalties and taxes while remaining more business friendly than Hugo Chavez."

Meanwhile, there is little evidence to suggest that low corporate taxation spurs investment. Alberta has been cutting its corporate income tax rate since 2001 and, while business investment has grown, it can largely be attributed to soaring commodity prices. Federally, the government cut its corporate income tax rate by a third, from 29 per cent in 2000 to 18 per cent, but business investment actually decreased as a share of the nation's economy.

"The 'Alberta Advantage' was a self-defeating strategy," says Weir. "It did not create a durable competitive advantage, but left Alberta and other provinces with less public revenue. Because Alberta has the most fossil fuels and corporate profits, it is well-positioned to show leadership in reversing this race to the bottom." **U**



# FAILING TO SAVE FOR OUR FUTURE

## Heritage Fund hampered by backwards financial planning

**SHANNON PHILLIPS**

It's the kind of savings scheme that would get a failing grade in any financial planning 101 course: Put aside a little for your retirement when you're young, stop saving for 25 years and spend most of the money you earn in interest.

That's the story of Alberta's Heritage Fund. While the province has also put some money into a rainy-day fund, it's barely enough for emergencies and not something that can be counted on for securing the province's long-term future.

In the real world, nobody in their right mind would spend the investment returns earned on their RRSPs on an annual basis,

and no one would call their tiny emergency fund a plan for future retirement security. However, this kind of backwards financial planning is exactly how the government of Alberta treats the Heritage Savings Trust Fund.

The Heritage Fund could be so much more – but how we use it is linked to how we collect revenues – corporate taxes, personal income-tax and oil and gas royalties. In the absence of reforms to our revenue system, the Heritage Fund will continue to wither. However, if we take a hard look at our finances and make some adult decisions about how we collect revenues, we're in a position to lead the country in a number of ways – financial stability and economic diversification. The choice is ours.

## The Story of the Heritage Savings Trust Fund

The Heritage Savings Trust Fund was established in 1976, with an initial \$1.5-billion deposit from royalties and another \$620 million from general revenue. Between 1976 and 1982, we saved 30 per cent of our resource royalty revenue and the Heritage Fund grew to \$12 billion. This was the high-water mark for the fund. By 1982, Alberta had already ratcheted down the percentage of royalty revenue saved to 15 per cent and, by 1987, we stopped making deposits entirely.

### Stop the Roller-Coaster, say Alberta Professors

There's a way for Alberta to get off the revenue roller-coaster, according to two professors of economics at the University of Alberta.

Rather than rely on volatile resource revenues, which go up and down with global oil and gas prices, professors Stuart Landon and Constance Smith propose the province creates a stabilization fund and commit to depositing a fixed percentage of resource revenues into it each year, while withdrawing a fixed percentage of the assets each year to support current spending.

This would be an improvement on the existing Sustainability Fund, where deposits and withdrawals have changed frequently at the discretion of government. By 2013, this fund is set to fall to \$3 billion, the professors wrote in a column in the *Edmonton Journal* in November 2010.

To avoid putting pressure on current revenue and spending, the proportion of resource revenues committed to the new fund would be increased gradually over the years to a set target level.

The professors' C.D. Howe Institute Commentary, *Energy Prices and Alberta Government Revenue Volatility*, can be found at [www.cdhowe.org](http://www.cdhowe.org).

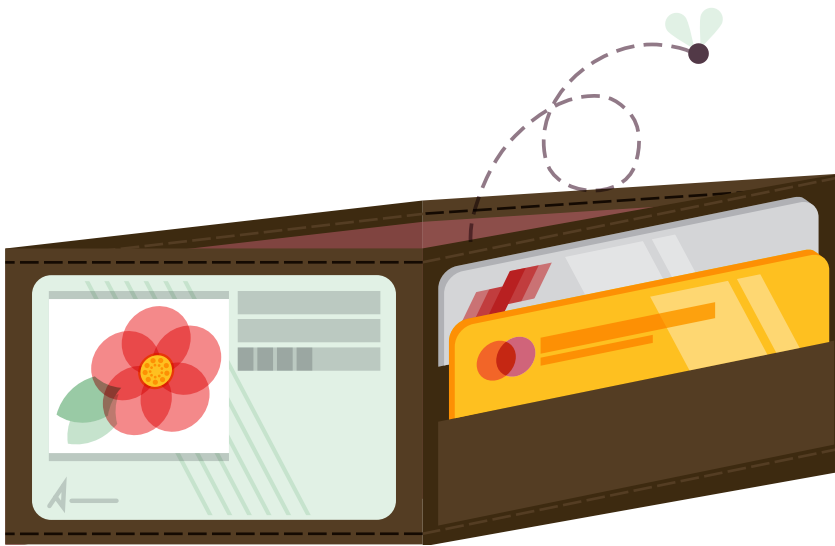
The Heritage Savings Fund was an important part of then-Premier Peter Lougheed's plan to diversify the Alberta economy and make us less dependent on oil and gas. It was designed as a province-building tool and gave government a way to exercise leadership in the economy. In addition to acting as a savings vehicle, the Fund issued loans to other provinces, invested in Alberta companies, funded research and development and built capital projects.

The Heritage Fund was designed to invest directly in commercial enterprises in Alberta and there were some notable successes, such as jump-starting the petrochemical industry via Nova Corporation and maintaining a government window on the oil industry via the Alberta Energy Corporation (later sold to become EnCana). Other crown corporations included the Alberta Agricultural Development Corporation, the Municipal Financing Corporation, and Alberta Government Telephones. The fund also had tangible assets – for example, in 1988 it held \$3.2 billion in mortgages through the Alberta Mortgage and Housing Corporation.

Don Getty's government stopped adding royalty revenue to the Heritage Fund in the late 1980s, when conventional crude oil prices went into a global nosedive. But a simultaneous global trend was also afoot – a tectonic shift in how we understand government's ability to exercise economic leadership.

Using the Heritage Savings Trust Fund as a way to encourage government-led economic diversification, some level of public ownership and public participation in the economy were ideas that would not withstand the ideological assault of 1980s Reaganomics. By that time, it was fashionable to claim that government had “no business being in business.”

Government stopped the private investment functions of the Heritage Fund in the late 1980s, and in 1996 outlawed the practice. In the 1990s, the Heritage Fund sold its investments in AGT to Telus and sold off the mortgages it held to private institutions. Those sales deprived the fund of continuing revenues and provided only a one-time injection of \$1.6 billion,<sup>1</sup> and show the extent to which privatization robs governments of ongoing cash: investments in AGT and Alberta Mortgage Corporation were worth a total of \$4.37 billion in 1988.<sup>2</sup>



Alberta did not make a single deposit to the Heritage Fund between 1987 and 2005. Through the 1990s, all yearly income from our initial investments was spent. Over that time, Alberta lost \$7 billion to inflation alone.

The Calgary Chamber of Commerce calculates that had Alberta continued to save 30 per cent of resource revenues in the Heritage Fund, it would now be worth \$128 billion.

### A Political Consensus on Saving

It's rare that the Parkland Institute, the Calgary Chamber of Commerce, the Alberta NDP and Preston Manning all share the view that Alberta should be saving more of its natural-resource revenues.

Conservatives began championing a more robust approach to saving in the early 2000s. Business elites who fund organizations like the Canada West Foundation and the Canadian Taxpayers' Federation have a range of motivations for supporting increased savings.

First, when Alberta was posting massive surpluses, there was a palpable fear that Ottawa and other provinces would increase Alberta's equalization payments – raising the federal government and the “Rest of Canada” as a bogeyman preying on Albertans' wealth. Regardless of the validity of these fears, they remain a powerful motivator in Albertan public policy.

Furthermore, there are valid arguments to be made that Alberta's responsibility to fund a transition from a fossil-fuel-based energy economy to one more compatible with international legal obligations to address climate change

should, in fact, involve fiscal transfers to the rest of Canada in some form, whether those transfers occur as part of an overall lending strategy, incubation funds for the private sector or publicly funded commercial ventures aimed at reducing greenhouse gas emissions, or outright transfers to the federal government.

Second, a savings strategy is seen by business elites and their think tanks as a way to keep a lid on Albertans' expectation of high-quality public services. Couched in terms of “curbing spending,” establishing “firm fiscal rules” and “discipline,” the Heritage Fund is positioned by commentators like Preston Manning or the Canadian Taxpayers Federation as a way to further a political agenda – preventing democratic demands for adequate funding for health care, social services, child care, or other government programs that Albertans can legitimately afford.

A Heritage Fund savings strategy like the one proposed by the Chamber of Commerce – that we put away 30 per cent of our non-renewable resource revenues - would mean throwing health care, education, and social services into total disarray. If, as they argue, we kept all other taxes and revenues the same, we would deprive our public-sector programs of \$2.19 billion in 2010 – about eight per cent of our provincial program spending.

1 Brett Gardner, “Alberta's Money Jars: Current Provincial Savings and Endowment Funds,” *Alberta's Energy Legacy* (Canada West Foundation, 2007), 9-25.

2 Glen Mumej and Joseph Osterman, “Alberta Heritage Fund: Measuring Value and Achievement,” *Canadian Public Policy* XVI (1), p. 29-50, 1990.

Even more radically, the Canadian Taxpayers' Federation recommends Alberta ramp up its savings program to encompass all non-renewable resources, forecast at \$7 billion in 2010, or a quarter of provincial program spending – that's all of our spending on education, children's services, and seniors. Imagine the impact of 25-per-cent cuts across the provincial government – each and every year. For context, the worst of the Klein cuts in 1993-94 was a one-time across-the-board cut of 20 per cent, followed by almost immediate reinvestment.

Progressive think tanks like the Parkland Institute, however, favour saving resource-royalty revenue because of its very nature – resource revenues are finite and must be used to build a different kind of economy. Given that royalties are a rent we charge companies for the use of our declining fossil fuel resources, most economists argue that governments should capture as much of that rent as possible.

Royalties are the rent paid for use of our natural assets, and once the oil, gas and coal are gone, the rents are gone. It makes sense, then, that resource-royalty rent for our declining assets should be converted into some other kind of asset – converting natural capital into financial investments, such as green infrastructure and renewable energy industries. This is the wisest, most prudent and most practical use of our oil and gas wealth.

### **Revenue Reform: There has to be something to save**

Household analogies only take us so far in understanding government finances. The parallels fall down when we consider that no ordinary person dictates their salary, benefits or pension. Ordinary people can't decide what we get paid, who pays us or the interest rates on our loans. Our investments are not large enough to influence the direction of the economy. If we don't like our jobs, we don't have the capacity to build a new industry from scratch in order to hire ourselves for a job we might like better. But governments have varying degrees of control over all of these aspects of their finances.

This is where a savings strategy is deeply intertwined with the broader question of taxes, royalties and other revenues in Alberta. Business elites are right to point out that we should be saving more of our royalty revenue – this is the wisest and most prudent way to make sure our current wealth benefits future generations. We can use public policy to ensure we



have a different kind of economy in place when the world has moved on from fossil fuels.

But Alberta has had to use the vast majority of our royalty revenues for program spending, rather than saving or planning for a greener future, because we are not capturing enough revenue from taxes. Furthermore, because we leave so much royalty revenue on the table, we are allowing our natural assets to vaporize into the thin air of profits for large oil and gas companies - and a great deal of those profits is repatriated beyond Alberta's borders.

### **What the Heritage Fund Could Do**

With royalty and tax reform, we would not need to raid the Heritage Fund of its annual growth for general program spending. If oil and gas royalties were to increase to fair and reasonable levels, we could legitimately save 30 per cent – or more – of our royalty revenues without starving public programs. As we've seen, we could make up some of that revenue today with tax reform, let alone the billions left on the table in non-renewable resource revenues.

Within a reformed revenue strategy, Alberta could take a hard look at what the Heritage Fund was originally intended to do and update those expectations to reflect 21st-century values and priorities.

For example, the Heritage Fund should be the primary vehicle for building a sustainable, green economy. Because its revenues are directly derived from our oil and gas wealth, we should be using the fund for the eventual and inevitable time when fossil fuels are no longer the energy source of choice for the majority of the world's population. The resource bounty we all enjoy now is a privilege, but also implies great responsibilities to the environment and future generations in the context of climate change.

The Heritage Fund could be used to finance the growth of a green energy sector in Alberta and across the country. The Fund could be used as a revolving, no-interest source of cash for municipalities and other non-profit entities to invest in green infrastructure in ways they cannot afford to do right now.

The Heritage Fund could be used to start an Albertan-owned public Crown Corporation focused on green energy, or could also be used to invest in projects that are only marginally economical now but show great promise in the future, such as rail links between major cities or between cities and suburbs.

It could be used on a low-interest basis by the private sector and even by other provinces to build green energy infrastructure, including research and development, grid upgrades and even venture capital. None of this is wild, radical or impossible – it could begin to happen tomorrow, as long as we are also prepared to have a grown-up conversation about taxes, royalties, and what kind of legacy we want to leave to future generations of Albertans. **U**

## WHAT ALBERTA SAVES

### HERITAGE FUND

**2010 Equity Forecast: \$13.8 billion**

*Policy and Purpose:* There is no legal requirement for the government of Alberta to make regular deposits into the Heritage Fund, or any requirement that a certain percentage of non-renewable resource revenues be saved. In fact, the law governing the fund requires that all investment income from the Heritage Fund be transferred to general revenue except the amount required to guard against inflation.

### SUSTAINABILITY FUND

**2010 Estimate: \$14.9 billion**

*Policy and Purpose:* When commodity prices are high, a portion of resource revenues are required, by law, to go to the Sustainability Fund. For example, in 2006-07, any resource revenues over \$5.3 billion – that were not deposited into the Capital Account or other endowment funds – were required to go to the Sustainability Fund.

The Sustainability Fund is not a savings fund. It is an account within the government's General Revenue. Its purpose is to smooth out the effects of short-term dips in commodity prices, fund emergency or disaster response, or natural gas rebates.

### ENDOWMENT FUNDS: 2010 FORECAST

Alberta Heritage Foundation for Medical Research - \$1.257 billion

Alberta Heritage Science and Engineering Research - \$714 million

Alberta Heritage Scholarship - \$695 million

Alberta Cancer Prevention Legacy Fund - \$101 million

Alberta Energy Innovation Fund - \$200 million

Alberta's net assets forecast for 2010: \$47.99 billion

*Source: Government of Alberta Budget 2010: Striking the Right Balance, Fiscal Plan Tables, p. 80*

### NORWAY'S GOVERNMENT PENSION FUND – GLOBAL

All of Norway's oil and gas royalty revenue and all net profits from Norway's state-owned oil and gas firm, Statoil, are invested in the Government Pension Fund – Global.

Norway did not begin saving resource revenues until 1996. Just 14 years later, the value of the Government Pension Fund - Global is valued at US\$512 billion. It is the largest stock holder in Europe and the second largest sovereign wealth fund in the world, after the Abu Dhabi Investment Authority.



# Low WCB Premiums Put Squeeze on Injured Workers

**TERRY INIGO-JONES**

There is a concept at the core of insurance programs – the higher the risk, the higher the premiums. It is a concept that appears to be lost on Alberta's Workers' Compensation Board (WCB).

Alberta is one of the most dangerous places in Canada to be a worker, with more people working in dangerous industries than other provinces (22 per cent of Albertans work in the four most dangerous occupations versus about 15 per cent in other provinces) and a workplace fatality rate higher than the national average (5.9 per 100,000 workers compared with 4.2 per 100,000 workers in the rest of Canada).

You don't have to be a mathlete to figure out that this should lead to more and higher insurance payouts and, therefore, higher premiums to cover those payouts.

Alberta's WCB, however, collects the lowest premiums in Canada from employers in dangerous industries. Simply put, WCB is not collecting enough revenue from premiums and it balances its books on the backs of workers and their families by putting a squeeze on payouts.

In Alberta, oil and natural gas exploration companies pay just \$0.55/\$100 payroll, while companies in the rest of Canada pay four times as much, at \$2/\$100 payroll. Industrial construction companies in Alberta pay just \$2.04/\$100 payroll. In the rest of Canada companies pay more than double that, at \$4.30/\$100 payroll.

At its 2010 annual general meeting (AGM), the WCB reported that its average collected rate had been cut every year since 2004, from \$1.96/\$100 payroll to \$1.24/\$100 payroll.

How has the WCB been able to cut its premiums by so much while the province remains such a dangerous place to work?

Alberta is one of the most dangerous places in Canada to be a worker, with more people working in dangerous industries than other provinces.



The answer, according to Edmonton WCB advocate Gail Cumming, is in the way WCB approaches its operations.

“Their focus is return to work. Anything you see from WCB, even their logos, is return to work. Their mandate is not to compensate you if you can’t return to work,” says Cumming, CEO and senior consultant with Cumming Consulting, who has worked in the WCB field for 30 years.

By declaring claimants fit to work, the WCB cuts the amount it has to spend in compensation for injured workers. Indeed, the drop in premiums is mirrored in the drop in the number of lost-time claims (LTCs – claims involving employees unable to work because of workplace injuries) filed, from 36,000 in 2004 to 27,100 in 2009.

Total claim costs for Alberta’s WCB were \$704.7 million in 2009, 34.7 per cent below budget and 27.5 per cent lower than 2008, partly due to “effective claim management” according to WCB chief financial officer Ron Helmhold in his report to the AGM.

This “effective claim management” can be seen in the increasing number of claims rejected by WCB.

Dr. Bob Barnetson, assistant professor of labour relations at Athabasca University, says the annual rejection rate for lost-time claims between 1996 and 2001 was 3.98 per cent. After 2001, there was a distinct upwards trend in the rate of LTC rejections and in 2009 it was at 6.6 per cent. Medical-aid-only claim rejection rates also increase after 2001, rising from five per cent to 9.7 per cent in 2009. Disabling injury claim rates grew from 3.4 per cent in 2002 to 6.4 per cent in 2009, he says.

WCB chief executive officer Guy Kerr told the AGM: “Together, we managed to help 93 per cent of injured workers get back to the job, amongst the highest return-to-work rates we have ever seen.”

Part of this high return-to-work rate was due to WCB’s approach to modified work for injured employees, which meant that 43 per cent of disabling injury claims resulted in no time away from work because employers provided modified work duties.

An early return to work can be good for workers, both financially and psychologically. However, the WCB’s focus on declaring employees fit to return to work, or returning to work on light or modified duties - in order to keep claims down and premiums low - leads to pressure to push people back to work too soon.



The WCB drive to reduce employer premiums means that workers may not be receiving adequate compensation for work injuries, says Dr. Bob Barnetson of Athabasca University.

This pressure is hurting workers, says Cumming. For example, there was a 104-per-cent increase in the number of reoccurrence claims in 2009 – those are claims that were closed off by the WCB, but where applicants attempted to reopen them later. There were 16,696 of these in 2008 and 34,758 in 2009.

“So, why are we having more claims trying to reopen? Because they are cut off too soon,” says Cumming.

To support her claim that files are being closed and workers cut off too soon, Cumming says she has a success rate of about 96 per cent at the appeals commission, which is an independent, arm’s-length body free from the pressure felt by WCB staff.

That pressure on staff to close files and cut payments is intensified by its controversial bonus system, which has seen bonuses averaging \$6,500 a year paid to staff members who help the board meet its goal of premium reduction. No other Canadian WCBs give bonuses to case managers for closing files or meeting quotas.

Barnetson says: “It’s pretty clear there have been significant decreases in the lost-time claim rate that are mostly an artefact of administration and not an actual reduction in injuries.”

Alberta’s WCB is enamoured with schemes to reduce employer premiums in the expectation that this will influence employer safety behaviour, says Barnetson, who used to work for the WCB. “The evidence for that is very unclear and one of the outcomes may well be that workers do not receive adequate compensation for work injuries.” **U**



# Parties Fight for Share of Resource Wealth

## ALBERTA'S OIL & GAS: AN HISTORICAL PERSPECTIVE

WINSTON GERELUK

**“Albertans do not receive their fair share from energy development and they have not, in fact, been receiving their fair share for some time.”**

*Bill Hunter, chair of panel that wrote a surprisingly blunt report on whether Alberta was receiving adequate oil and natural gas revenues. Calgary Herald, September 18, 2007.*

Ever since the oil boom triggered by the blowout at Leduc #1 in 1947, Alberta's politics and financial fortunes have been closely aligned with those of the oil industry.

The move by Premier Ed Stelmach in 2007-2008 to raise oil royalties - and his later undignified retreat - was simply another in a line of attempts to change the balance of power held by the petroleum industry in order to gain a more equitable share of the wealth produced by our oil and gas fields for the people who own them.

The discovery of Leduc #1 in 1947 was front-page news in The Western Examiner. Ever since oil and gas began flowing in Alberta, varying parties have fought for a share of the wealth

Glebow Archives NA-789-90



Ever since oil and natural gas began flowing in Alberta, many parties have scrimmaged over a share of the wealth, including the petroleum industry, its workers, and the governments of Alberta and Canada! In the process, governments have been threatened and replaced and workers have led bitter fights over trade union rights. Among all these, a few key moments explain why the industry is today able to exploit our energy resources for a fraction of the rates it pays in such jurisdictions as Norway, and even Alaska.

Canada's oil industry may have been born in the east, but really only came of age with discoveries in Alberta. The first occurred in 1883 when a well near Langevin to get water for the CPR's steam-driven locomotives produced natural gas instead. The second in 1890 near Medicine Hat, led to the discovery of a huge gas field that prompted Rudyard Kipling's famous remark during a 1907 visit that the town had "all Hell for a basement."

In 1914, oil fever swept Alberta after discovery of wet gas (containing naphtha and other gas liquids) and oil at Turner Valley; in one 24-hour period, investors formed more than 500 companies. Turner Valley became Canada's first major oil and gas play and the largest in the Commonwealth, establishing Calgary as Canada's oil and gas capital.

That changed on February 13, 1947, when Imperial's Leduc #1 blew out marking a field that produced previously undreamed of quantities of oil and natural gas. Rapidly expanding production led to an Interprovincial Pipeline in 1950 to transport oil from Edmonton to Superior, Wis., and later to Sarnia, Ont. A Mountain Pipeline (oil) was completed to Burnaby, B.C., in 1953 and gas was exported to Eastern Canada by Trans-Canada Pipelines in 1957. Oil-sands production began in 1967 with Great Canadian Oil Sands Ltd. (later Suncor) at Fort McMurray, followed by the Syncrude plant in 1978.

### Our share of the proceeds

Our oil and natural gas have now flowed freely for more than 60 years, creating huge returns to some of the world's largest corporations. At the same time, the billions in revenue contributed to the Alberta Treasury have created a dependency that we live with today.

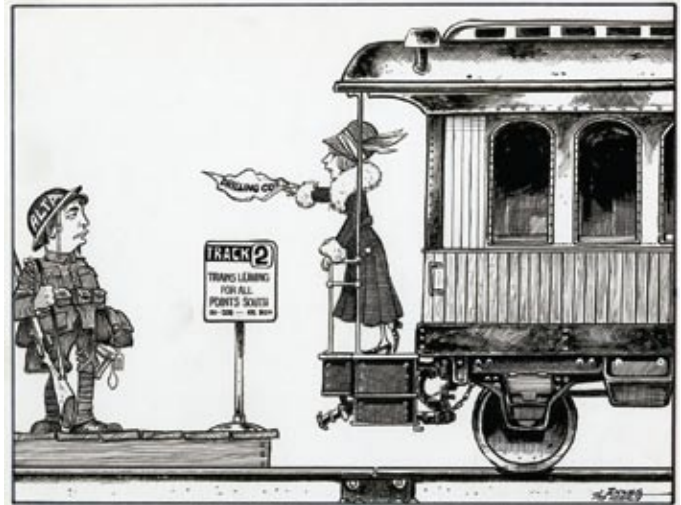
According to the Canadian Association of Petroleum Producers (CAPP), in 1949, only one full year after Leduc #1, the value of all production in the province was \$61.6 million (\$573.6 million in 2008 dollars). By 2008, the year of Stelmach's weakened royalty revision, the value of production in Alberta had ballooned to \$108 billion.

In 2008, as Stelmach introduced royalty revisions weaker than recommended by his advisory panel (revisions that were to be scaled back even further in 2010) the province received some \$12.5 billion in royalties (before subtracting tax expenditures and other incentives offered to the oil and gas industry), as well as several hundreds of millions of dollars more in land sales and leases.

From the beginning, there were broad suspicions, such as those voiced by Co-operative Commonwealth Federation (CCF) stalwart and radio commentator I.V. Macklin in Grande Prairie, that the people who owned these non-renewable resources were being fleeced (see I.V. Macklin, *The Canadian Sell-Out to the United States*, Radio Broadcast, 1953, Glenbow Institute). Farm organizations, trade unions and political opponents regularly called on government to stand up to the industry to get a greater share for the people.

As early as 1941, the province “aroused the indignation of the oil opera” by its attempts to “grab” a greater share of revenues from Turner Valley Oil. This marked the beginning of strategies to pacify the industry through accelerated tax write-offs and concessions (Financial Post, July 26, 1941).

Royalties make up the major portion of the public’s share of oil revenues: the others are taxes, land leases and workers’ wages. When constitutional amendments finally guaranteed provincial ownership of natural resources in 1930-1931, the province’s United Farmers of Alberta (UFA) government set



When Premier Peter Lougheed hiked royalties in 1974, and the federal government cancelled the ability of corporations to deduct royalties from taxes, oil companies took their drilling rigs south to the U.S.

*Glenbow Archives M-8787-138*

royalties at a flat rate of five per cent. This was doubled to 10 per cent in 1935 to offset lost government revenues during the Depression.

From 1941-1943, the Social Credit administration of “Bible Bill Aberhart” introduced a flexible oil royalty rate of between five and 15 per cent based on production. The gas royalty was increased to 15 per cent, and later to 16.67 per cent under E.C. Manning, where it remained until the price spikes of the 1970s.

Today, royalty rates may appear to be much the same, except that the government now forfeits billions in tax expenditures and incentives. As one example, companies exploiting our oil sands pay only one per cent of gross revenues until all project construction costs are recouped, at which time the rate climbs to 25 per cent of revenues, once costs are subtracted.

"Farm organizations, trade unions and political opponents regularly called on government to stand up to the industry to get a greater share for the people."

- Winston Gereluk, *Alberta Labour History Institute*

### The Rise of OPEC

Social Credit Premier E.C. Manning's successor, Harry Strom, learned first-hand the political power of a disgruntled oil industry. In the late 1960s, the industry began to pull out of Alberta, claiming that most of our conventional oil had already been discovered. As well, they were not happy about a 1961 agreement reserved profitable markets east of the Ottawa Valley for imported oil, shutting out Alberta production ("Alberta worried about the future of her oil," *Montreal Gazette*, March 29, 1969).

Many credit this timely slowdown in the oil industry for Strom's defeat by the Lougheed Conservatives in 1971. By that time, the province had collected about \$3 billion in petroleum and natural gas leases, drilling reservations and royalties, with \$300 million collected in 1969-1970 alone, almost a third of total government revenues (*Montreal Gazette*, March 29, 1969). This was slightly less than the 38 per cent of revenues contributed by the industry in the 1950s, which had been steadily reduced by tax write-offs and concessions. The oil industry wanted more.

To be fair, Lougheed began as a champion for a greater public share, raising royalty rates to a maximum 25 per cent one year after his election, with a vow that Albertans would collect healthy "economic rents" for their provincial resources. However, this bold stance would succumb to developments half way around the world. When Egyptian and Syrian troops moved into Israeli-occupied territory on October 6, 1973, the United States and most western nations backed Israel. Arab oil producers began to use their oil resources as leverage and cut production, initially by 25 per cent, with plans for further cuts of five per cent a month until a settlement could be reached. Almost overnight, oil jumped from \$3 US per barrel to \$15, reaching almost \$40 by the end of the decade as the Organization of Petroleum Exporting Countries (OPEC) maintained its quotas and Iran was locked in civil war.

While consumers paid the price at the gas pumps and poor nations were driven deeper into debt, multi-millionaires sprang up in Alberta. Everyone wanted to get into the action, and

thousands of people flooded into the province every month. At the height of the boom, Calgary issued more than \$1 billion worth of construction permits annually, and apartment vacancy rates in major cities approached zero. A new entrepreneurial political culture was created as professors, lawyers and carpenters began speculating in real estate and oil ventures.

Lougheed hiked royalties again in 1974 – but this time it was to ensure that OPEC windfalls stayed in Alberta rather than going to Ottawa. When the federal Liberal-NDP coalition responded by cancelling industry’s rights to deduct royalties from corporate taxes, oil companies responded with an exodus of drilling rigs to the U.S, stemmed only when Alberta agreed to refund them the difference. Grant Notley, Alberta’s lone New Democrat MLA, was the only one to speak out against this concession.

Lougheed went a step further in 1976, creating the Alberta Heritage Savings Trust Fund “to save for the future, to strengthen or diversify the economy, and to improve the quality of life of Albertans”. The Fund would receive 33 per cent of non-renewable resource revenue received by the government of Alberta, and with an initial allotment of \$620 million, as well as a special contribution of \$1.5 billion transferred from Alberta’s General Revenue Fund, began life with a nest egg of just over \$2 billion. Today, 44 years later, it stands at just over \$14 billion (AHSTF 2010-11 Qtr. 1 Update, August 25, 2010).

## Demonizing the National Energy Program

Public ownership and intervention are easily dismissed in a province where bumper stickers proclaim that “oil feeds my family and pays my taxes.” It has been unnaturally easy for the industry to whip up public sentiment against any policies designed to return a fair share revenues to the citizens of Canada, or to increase public ownership.

This was the purpose of the National Energy Program (NEP), introduced by the federal government of Pierre Trudeau upon its return to power in 1980. Along with plans to repatriate the Constitution, it became the scapegoat for much of the slow-down that subsequently occurred in Alberta’s oil patch.

The “crime” of the NEP was that it proposed oil self-sufficiency for Canada, a secure oil supply particularly for the industrial base in eastern Canada, domestic ownership of the energy industry, lower prices, development of alternative energy sources, and increased government revenues through a variety of taxes and agreements. It also included a greatly expanded Petro-Canada to help “Canadianize” the entire oil industry.

It was hard to tell who was more enraged; the oil industry or the Alberta government. Whatever the case, Albertans were barraged with messages that the NEP was a federal attempt to seize Alberta’s resources. The Petro-Canada building in Calgary was dubbed “Red Square” and stickers on pickup trucks echoed remarks by Calgary’s mayor – one Ralph Klein: Let the Eastern bastards freeze in the dark! Said political scientist Larry

Pratt: “The idea of an independent West, hitherto confined to a cranky right-wing fringe, suddenly became appealing to large numbers of western Canadians.”<sup>1</sup>

It did not help that, by the early 1980s, rapid expansion and a worldwide economic recession had already begun to hit the industry hard. In 1982, for example, Dome Petroleum, Canada’s largest oil company, barely avoided collapse with a last-minute bailout package from Ottawa.

The oil industry, for its part, acted en masse to withdraw investments from Alberta, bringing the oil patch to a virtual standstill. Worse yet, a glut of oil appeared (as if on cue) to drive oil and gas prices down, and in 1982-1983, the Alberta government ran a deficit of \$2 billion, the first most Albertans could remember.

Fears were already aroused, and when Alsands, our third major oil-sands plant, was abandoned in 1982, the Lougheed government could count on public acceptance for a series of huge royalty holidays, tax cuts and other incentives. Economist Sten Drugge found that provincial deficits after 1986 could be attributed much more directly to corporate giveaways than to runaway spending on programs and services. Lougheed’s 1982 Economic Resurgence Plan alone amounted to a total tax expenditure estimated at \$1.6 billion over three years, and was supplemented by even more “stimulants” estimated to total \$5.6 billion between 1982 and 1986.<sup>2</sup> In fact, during the fiscal year ended March 31, 1982, Alberta’s corporate sector as a whole received \$162 million more from Alberta taxpayers than it paid out in taxes, royalties and fees.<sup>3</sup> The Alberta Advantage indeed!



Bumper stickers echoed the sentiments of Calgary mayor Ralph Klein: *Let the Eastern bastards freeze in the dark!*

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- <sup>1</sup> Pratt, Larry and Garth Stevenson (1981) *Western Separatism: The Myths, Realities and Dangers*. Edmonton: Hurtig Publishers. P.1
- <sup>2</sup> Drugge, Sten. “The Alberta Tax Advantage: Myth and Reality”, in Trevor Harrison and Gordon Laxer (ed.) 1995. *The Trojan Horse: Alberta and the Future of Canada*. Montreal: Black Rose Books. See also Pratt, Larry, “Energy, Regionalism and Canadian Nationalism, 1982-86”, *Newfoundland Studies* 1, No. 2, Fall 1985, p.188.
- <sup>3</sup> Shaffer, p.122.

When the Alsands plant was abandoned in 1982, the Lougheed government knew the public would accept a series of royalty holidays, tax cuts and other incentives.

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## Oil and Labour

As labour lawyer Brent Gawne observed: “The vast wholesale migration of drilling companies out of the province, and the alarm that it caused in the streets of Calgary was seen as necessitating a fundamental change.”<sup>4</sup>

The NEP would not survive. When the federal Conservatives led by Brian Mulroney came to power in 1984, one of their first acts was to dismantle the NEP - but not before it had fuelled widespread separatist sentiment in Alberta. The federal Liberals became the enemy in the minds of many, rendering Alberta a secure base for provincial and federal Conservatives to the present day, and calls for a “firewall” to separate the province from the rest of Canada. Canada’s government would not challenge the oil industry again.

In 1986, world oil prices declined again. However, the crusade against public spending, debt and deficit was well entrenched even before this produced a drop in government revenues. As economists Melville McMillan and Allan Warrack pointed out in *The Trojan Horse*<sup>5</sup> (a publication that caused considerable consternation in Tory circles), statistics show that, despite the de facto capital strike by the industry in 1981-’82, government real per-capita revenues grew at a healthy rate until 1986, outstripping other provinces.<sup>6</sup>

4 G. Brent Gawne, *Labour History Day Address, Alberta Labour History Institute, August 2, 2004*

5 McMillan, Melville L. and Allan A. Warrack, “One Track (Thinking) Toward Deficit Reduction”, in Trevor Harrison and Gordon Laxer (ed.) 1995. *The Trojan Horse: Alberta and the Future of Canada*. Montreal: Black Rose Books.

6 McMillan and Warrack, p.136-7.

7 See Roberts, Wayne. (1990) *Cracking the Canadian Formula: The Making of the Energy and Chemical Workers Union*. Toronto: *Between the Lines*. p.22.

8 Interview with Brad Bulloch, November 16, 2005.

Even at the best of times, the energy industry has been patently anti-union. Employer-sponsored “company unions” that persisted in Alberta’s oil industry well into the 1980s were a legacy of the late John D. Rockefeller, who invented “donkey councils” on the advice of William Lyon Mackenzie King as part a union-avoidance strategy, following the Massacre of 1914 in his Colorado fields.<sup>7</sup>

Alberta’s construction trade unions experienced another side of this. Alberta’s oil booms are really construction booms; once completed, they leave little permanent employment. When construction projects fell precipitously in the early 1980s, contractors took advantage of a huge reserve of unemployed workers to strike a blow at their unions. They employed a strategy that combined 24-hour lockouts with “spin-off” companies to unilaterally terminate collective agreements with the building trades unions – and the Alberta government allowed it.

Brad Bulloch with Carpenters Local 2103 described the effect. “It was devastating to anybody that had a mortgage, a car payment, or a family - such as me. We lost members, and some lost their lives through suicide. There were many marriage break-ups, people lost their homes, lost their vehicles. In 1984, people were selling their homes for \$1 to get out of liabilities.”<sup>8</sup>

Tradespeople were not the only ones to be devastated. Communities across Alberta suffered the consequences as overnight, thousands of well-paid construction workers found themselves reduced to poverty, taking money out of their local economies.

## Free Trade and control of the oil industry

Just after he was elected in 1984, Mulroney announced that Canada was “Open for Business” - adding that with 10 years in power, he would render the Canada we know unrecognizable. He began by corporatizing Canada Post, then proceeded to slash the budgets of VIA Rail and the CBC.

Mulroney’s major gift to the oil industry, however, was free trade, a project launched at a 1985 meeting at Montebello, Que. (the Shamrock Summit), where he joined U.S. President Ronald Reagan in singing *When Irish Eyes Are Smiling*. The duet culminated in an agreement to eliminate barriers to trade between Canada and the United States, facilitating conditions of competition and liberalizing significantly conditions for investment. The Free Trade Agreement (FTA) was followed in 1991 by the North American Free Trade Agreement (NAFTA), which would enshrine rules that would make it almost impossible for any Canadian government to protect the public’s interest in a national oil policy.

Since then, the room for Canadian governments to act on behalf of citizens is shrinking even more with rapid developments contained in the Security and Prosperity Partnership (SPP), an agreement that calls for complete integration of North American energy markets. While governments all over the world are developing strategies and policies to ensure energy security, maximize revenues and limit the impacts on the environment, the government of one of the coldest countries on earth continues to rely on the whims of the markets and the big oil companies to dictate energy developments and policy direction (Energy Revenues: Are Canadians Getting Fleeced? A report by Jean-Yves LeFort, Energy Campaigner, the Council of Canadians, October 23, 2007).

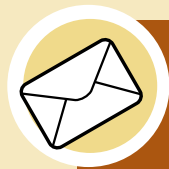
This was the historical background against which Premier Stelmach appointed a panel of businessmen and experts in 2007 to review Alberta’s oil royalty structure.<sup>9</sup> He had which little choice but to back down, in spite of the Alberta Royalty Review Panel’s clear conclusion that Albertans have not been receiving their fair share of revenues.<sup>10</sup> He chose to enact a scaled-down version of report recommendations and, under relentless pressure from industry and the Wildrose Alliance Party, retreated from even that position.<sup>11</sup> **U**

*Winston Gereluk is vice-president of the Alberta Labour History Institute. ALHI brings together trade unionists, academics, labour archivists, political activists and writers to preserve and tell the story of Alberta’s working people and their organizations. Since its founding in 1998, it has interviewed more than 300 leading trade unionists and community activists; preserved and archived records, photos and publications; produced Alberta Labour History Calendars; hosted Labour History Days; provided material for city and provincial centennial celebrations; and made presentations to trade unions, schools and other organizations. In 2007, ALHI partnered with the Alberta Federation of Labour (AFL) in Project 2012: 100 Years of Alberta Labour to provide an historical and educational foundation to the centennial the AFL will celebrate in 2012. Visit ALHI at [www.labourhistory.ca](http://www.labourhistory.ca)*

<sup>9</sup> Much of this summary is taken from a report in the *Calgary Herald*, March 11, 2010

<sup>10</sup> *Our Fair Share: Report of the Alberta Royalty Review Panel*, September 18, 2007

<sup>11</sup> Retrieved October 18, 2010 from <http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/alberta-royalty-cuts-set-a-dangerous-precedent/article1526628/>



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