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Mr. Chairman I am here on behalf of Pengrowth Energy Trust and as one of the founders of the Energy Royalty Trust Industry.
Energy Trusts are Different

Mr. Chairman, we are here to explain why the energy royalty trusts are different from income trusts.

Mr. Chairman, the energy royalty trust industry is fundamentally different from REITs and from existing businesses that have restructured themselves as income trusts. The differences include a long history, substantial ongoing capital requirements and an active business model of strategic importance to all Canadians including significant new capital fundraising that has encouraged growth, efficiency, innovation, productivity and minimal environmental impact. The royalty trust industry has become a pivotal part of the Canadian oil and gas industry in the last 20 years.

Our business model was only undertaken after careful consultations with the Department of Finance supported by a series of tax rulings that have provided the discipline and framework for our industry for over 20 years.

Mr. Chairman, energy royalty trusts are highly efficient facilitators of the movement of capital within the oil and gas industry, enhancing the productivity and ultimate recovery of our mature fields, rewarding exploration success of junior oil and gas companies, spawning new exploration companies, acquiring mature assets from the majors and supermajors that has freed up capital for other large infrastructure projects such as the oil sands and the MacKenzie Valley Pipeline. Energy royalty trusts are at the forefront of CO₂ injection and other technologies that will not only increase recovery and productivity but also minimize the environmental impact of the energy industry.

There are substantial capital requirements for Canada's mature oil and gas industry in the future, including our oil sands and pipeline infrastructure. The vast amounts of capital required for the development of our oil and gas industry is generally not available in the Canadian marketplace and we must compete for that capital from the US and elsewhere.

The Playing Field will not be leveled by the Government's Proposals

The information that has been presented to this Committee is clear, conclusive and compelling. There is no tax leakage associated with energy royalty trusts compared with traditional Canadian oil and gas companies. Energy royalty trust unitholders will pay approximately \$1.8 billion in current income and withholding taxes on \$8 billion of cash distributions in 2006, generating over 30% of the tax revenue collected from public Canadian oil and gas entities while representing only 16% of revenue. Indeed, it has been estimated that the Government tax revenues would be reduced by approximately \$1 billion a year if energy royalty trusts convert to a corporate structure.

Why is this? The application of a 31.5% tax at the trust level in 2011 with no deductions available is inconsistent with the taxation of oil and gas corporations that are taxed upon net earnings, have significant deductions and pay only modest cash taxes. Combined Provincial and

Federal taxes on corporations were 32.1% in 2006/07, but the net effective marginal tax rate in the oil and gas industry is only 6.7%. The after tax earnings of corporations can be distributed as dividends, but oil and gas companies do not normally make significant dividend payments. Taxes imposed upon energy royalty trust distributions are however are based on cash flow, and cash flow is approximately twice the level of net earnings. Distributions for the energy royalty trusts are 80% of cash flow vs. a relatively low payout of earnings as dividends from corporations. Cash taxes for the major oil and gas independents in Canada average only about 5% of EBITDA compared to 18% for the trust industry. Substantially more taxes are paid presently on a proportionate basis by investors in the energy royalty trust industry.

The U.S. Example

We suggest that a careful study be made of the U.S. experience with flow through entities, and that the Government exempt energy royalty trusts in existence as at October 31, 2006.

In 1986 and 1987 the U.S. Government, after lengthy hearings in the House and Senate, introduced provisions to restrict corporations from converting into MLP's for tax reasons. Energy related vehicles were exempted and continue to permit the pre-tax pass through of cash flow due to their importance in raising capital, and to encourage domestic security of supply.

We submit that the same rationales apply in Canada, and believe there is a clear and compelling case for grandfathering Canadian energy royalty trusts, and we encourage you to make that recommendation to the Government.

I hope my presentation today opens a door to work together on this very important issue. Thank you very much for your attention and kind reception. I look forward to answering the Committee's questions.