

Sharpening Canada's Competitive Edge

Competition Policy Review Panel
Consultation Process –
Written Submission

Petro-Canada
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On October 30, 2007 the Competition Policy Review Panel released its consultation paper, “Sharpening Canada’s Competitive Edge”. Petro-Canada makes this written submission to the Panel as part of the consultation process.

Introduction

Petro-Canada is following with interest the work of the Panel. A review of Canada’s policies regarding foreign investment and its impact upon the economy and Canada’s competitiveness is welcome.

As a publicly traded Canadian oil and gas company operating within and outside Canada, Petro-Canada benefits from foreign investment and also invests offshore. The role of foreign direct investment (FDI) and Canadian direct investment abroad (CDIA) is important to us. The report scheduled for delivery to the Minister on June 30, 2008 should address these interests from both perspectives.

The panel has set out to make recommendations that “... encourage Canadian firms to be active and aggressive investors at home and abroad, and maximize Canada’s attractiveness as a destination for new investment and talent.”¹. The recommendations made in the report should reflect the FDI and CDIA interests of Petro-Canada. The foreign investment aspect of the consultation paper dealing with the Investment Canada Act (ICA) provides the focus for our submission. The foreign investment element highlights other important issues for Canadian industry. The need for people to build and operate the economy goes hand in hand with investment. Although not dealt with in this submission, things like the use of technology, immigration, labour mobility, trades qualifications, streamlining of regulatory processes and infrastructure are key to increased competitiveness.

The consultation paper limits itself to a review of restrictions currently in place on foreign and domestic company ownership in specific industry sectors excluding the oil and gas sector. Nonetheless the Panel’s recommendations will be influential within Canada and throughout the government on matters that touch upon the oil and gas industry. For that reason we wish to provide our comments which will include instances of our industry’s own experiences. As the issue of State Owned enterprise investment is the subject of separate proposed legislation we will not address that topic.

Petro-Canada advocates the use of ICA as the sole vehicle for ensuring foreign investment decisions are in the best interests of Canada and Canadians. The strength and resiliency of Canada’s economy has proven itself able to manage foreign investment to the benefit of the country. Historically, ownership restrictions affecting Canadian business have relaxed and Canada’s objective should be to phase them out over time. A balance of inward foreign investment and outward foreign investment has become a feature of the Canadian economy with positive impacts on competitiveness, productivity and other measures.

Background in Oil and Gas Sector

The summary below, of previous reviews of foreign investment reveals an evolution in Canada's public policy regarding foreign investment. The evolution has seen continued expansion and acceptance of foreign investment within the Canadian economy. The evolution continues.

Review of foreign investment policy dates to 1914 and an ordinance addressing issues of ownership, levels of foreign control, place of business, and membership of the board of directors including matters pertaining to oil and gas. Many of the issues addressed in the 1914 review are still relevant regarding the current review.

Among other things, the 1914 review and ordinance, required companies in the oil and gas sector to be at all times and remain British companies registered in Great Britain or Canada, have their place of business within the dominions, and have a Chair and a majority of the Board of Directors that at all times would be British subjects. There was to be at no time, whether directly or indirectly, control by foreigners or by a foreign corporation².

The 1914 ordinance was revoked at the behest of the American and provincial governments in 1920. It was in the 1960s that foreign ownership issues were raised again with intensity. In 1961 foreign ownership in the energy sector was again included in the ongoing review. As a result, exploration permits were not subject to controls but only Canadian-owned companies or foreign controlled companies in which Canadians could invest were granted Crown production leases³.

Foreign investment and interest in Canada grew as limitations on investment in Canadian companies were relaxed. In 1966, letters setting out guidelines of good corporate citizenship were sent to all multinationals operating in the Canadian oil and gas sector which, at the time were regarded as failing to meet an appropriate standard. The guidelines, which have a familiarity with the issues in the current review, included for purposes of procurement the searching out and development of economic sources of supply within Canada; the development in Canada of technical research and design capabilities to enable Canadian affiliates to take advantage of product development programs which in turn took advantage of both foreign and domestic sales opportunities⁴. These guidelines continue to promote positive behaviour without being overly restrictive and should serve as a guide for the current policy review.

In the 1970's Canadian foreign investment policy was discriminatory with takeovers in the resource sector, for example, being blocked. Required Canadian-equity positions at a minimum of 25% pursuant to the Canada Oil and Gas Land Regulations, were put in place regarding production from federal lands. This policy approach culminated in the 1980's with the National Energy Program (NEP) with goals of 50% Canadian ownership of oil and gas production; Canadian control of significant oil and gas firms; and Government ownership in the oil and gas industry⁵. Shifts away from this policy began in 1984 with a change in government.

While the NEP had a negative impact on investment in Canada's energy sector, it was revealed to be bad policy as it adversely impacted other sectors such as manufacturing. There was a net reduction in capital inflow in Canada's FDI in manufacturing during the NEP's existence⁶.

It was in the 1990's that foreign investment regulations in the oil and gas sector were revised to permit increased foreign ownership. The new policy direction included a review to ensure that acquisitions were in the public interest, a similar theme to today's review. The oil and gas sector was put on equal footing as any other sector under the Investment Canada review process⁷.

I. Oil and Gas – A Case in Point: The Western Canada Sedimentary Basin

Foreign interest and investment has played a critical part in the development of the oil and gas industry in Canada. The development of the Western Canadian Sedimentary Basin was the start of an industry which has extended across the country, to Canada's offshore regions, and into the arctic. In addition the knowledge and expertise historically developed in the Western Canadian Sedimentary Basin is now being successfully exported through the operations of Canadian companies and by Canadian individuals internationally.

The history of the development of the Western Canadian Sedimentary Basin started with domestic endeavours that were small and isolated. These initial steps were enhanced and augmented through the contribution of technology, expertise and investment provided by foreign companies and investors. Foreign and domestic enterprises have co-existed and expanded in the Western Canadian Sedimentary Basin resulting in a strong and diversified industry. The industry continues to grow beyond Western Canada into new geographic areas as well as into new unconventional oil and gas opportunities such as coal bed methane, shale gas and oil sands.

The success of the Western Sedimentary Basin development shows that involvement by foreign companies was essential to the growth of the industry. The names of international companies are inseparably linked to many of the major oil and gas discoveries made in Western Canada. The oil and gas industry in Canada was largely defined by the 1947 Leduc well drilled near Edmonton, Alberta. After drilling 133 dry holes in Western Canada, U.S. controlled Imperial Oil Limited drilled the successful Leduc Number 1 Well which triggered an oil boom leading to the discovery of the bulk of Canada's oil reserves. The Leduc well is listed by the Government of Canada as one of the key economic events in Canada's history

(www.canadianeconomy.gc.ca/english/economy/1947Leduc_oil_discovery.html). In discussing the effect of the Leduc discovery, the Federal Government states:

“The oil find at Leduc ushered in the beginning of a massive economic revolution for Leduc and Alberta. Alberta changed from a predominately rural and agricultural province to an urban economy dominated by the oil and gas industry...The discovery of oil created opportunities for companies related to the oil industry.”

“...After the Leduc discovery, numerous American and British oil companies came to Alberta. Further exploration in the 1940’s and 1950’s uncovered large oil fields.”

Imperial’s knowledge, technology and investment were therefore key factors in the creation of this industry. The fact is, however, that Imperial’s entry into oil and gas exploration in Alberta had been delayed as a result of limitations placed on foreign companies. In 1914 Imperial Oil was first attracted to Alberta at the invitation of the Canadian Pacific Railroad in a joint effort to develop the petroleum potential of the railway’s lands hinted at by the discovery of gas near Medicine Hat. The activities of the oil company were, however, limited by government restrictions. At that time, Section 40 of Canada’s Petroleum and Natural Gas Regulations denied the granting of Crown leasehold interests to any company “directly or indirectly controlled by foreigners or by a foreign corporation”⁸. As a result Imperial was limited to searching for oil and gas found on freehold lands rather than the much more extensive Crown lands. Such a distinction nowadays seems artificial and short-sighted.

The involvement of foreign controlled companies such as Imperial Oil confirmed the existence of economic oil and gas resources which in turn led to the creation of the Canadian oil and gas industry. The Leduc discovery encouraged unprecedented investment and involvement by foreign oil and gas companies. Importantly, however, involvement by these foreign companies did not lead to their singular domination of the oil and gas industry. Leduc encouraged and attracted foreign companies, who in turn brought the technology, investment and skills that were necessary for the creation of a world leading industry. However, local individuals, companies and interests were not excluded from oil and gas development. Local involvement flourished as a part of the rapidly developing industry. The development of the Western Canadian Sedimentary Basin created opportunities for thousands of large and small oil and gas producers and service companies. Large and small independent producers continue to develop, grow and expand notwithstanding the initial and enduring involvement by many of the world’s oil majors. Today, many of the home grown Canadian oil and gas companies that have evolved to become domestic and international leaders in the industry owe some or a substantial amount of their success to the direct and indirect involvement of foreign corporations or foreign investment in their business.

This example shows the synergy that arises from reasonable foreign investment. Domestic activities, augmented by foreign investment and technology, leads to the creation of viable industry which in turn provides for the spin-off and growth of resource development and knowledge based industries.

II. Oil and Gas – A Case in Point: Canada’s Oil Sands

Development of the oil sands provides also a pertinent example for the Panel’s consideration. Although the existence of the oil sands has been known since 1719, its commercial history is relatively recent. The commercial development of the oil sands includes involvement and investment by government, domestic interests and foreign

companies. All three of these participants have added a critical component to the development of this resource.

The first true measured commercial exploration was started by the Alberta Research Council in the 1930's coincident with the activities with two American promoters, Max Ball and B.O. Jones, who had started Abasan Oils Limited at the same time. Coincident with the Research Councils' activities, mining at the Abasan plant began in 1941 and ended in 1945 as a result of a fire. Similar activities were undertaken between 1930 and 1955 by the International Bitumen Company Limited at Bitumont.

The first large scale commercial enterprise arose in 1962 when Great Canadian Oil Sands Limited (GCOS) received approval from the Alberta Government to build a plant near Fort McMurray. That plant was delayed until a subsidiary of U.S. based Sun Oil Company joined the GCOS consortium and provided the necessary significant financial backing. Suncor Energy Inc. is the successor in title to the original Sun Oil Company subsidiary. In addition to the Sun Oil Company the GCOS consortium included Abasan Oils, Canadian Oils Limited, Champions Oil Sands Limited and Oil Sands Limited (which was the new name for the International Bitumen Company). National and international interests combined to create an enduring commercial undertaking.

At about the same time, Syncrude, another oil sands pioneer, commenced its oil sands operations. In 1962 Cities Service Athabasca Inc., a Canadian subsidiary of the American Cities Service Company, proposed a 16,000 cubic meter per day plant at Mildred Lake. A revamped and much larger plant proposal received approval in 1969 and the Syncrude plant went into production in 1978. Syncrude now includes Canadian Oil Sands Limited, ConocoPhillips Oilsands Partnership II, Imperial Oil Resources, Mocal Energy Limited, Murphy Oil Company Ltd., Nexen Oil Sands Partnership and Petro-Canada.

The success of the oil sands operations of Suncor and Syncrude were both due in large part to foreign know-how and investment. Their success has led to significant growth and involvement in the oil sands by numerous foreign and domestic companies alike. The continued development of these resources will depend not only upon domestic financing, labour, and technology but also upon similar international investment and involvement. The development of the oil sands provides substantial promise for durable domestic energy resources. However, the challenges are significant and, like the development of the Western Canadian Sedimentary Basin, foreign involvement to meet these challenges will be equally crucial. That involvement should increase opportunities for financing, provide access to new technology and innovation, bring new skills and capabilities and, as in the case of the Western Canadian Sedimentary Basin, should not over-power domestic enterprise.

The Current Context

In a global economy where successful business is commenced and concluded across numerous international borders, a fair and reciprocal approach to foreign investment is necessary. This is especially true in the oil and gas industry where financing, technological capability and the consumption of energy products crosses national boundaries.

Foreign investment, in concert with domestic activity, has proven to be a winning formula with respect to the development of the Canadian oil and gas industry. Continuing international investment and interest in the oil and gas business in Canada will be crucial for the continued growth of our industry both domestically and internationally. This is particularly important at a time when reduced oil and gas resources globally means that increased knowledge and investment will be necessary to find and develop remaining reserves. In addition, the knowledge, skill and capabilities that have been developed as a part of Canada's domestic oil and gas industry are now being successfully deployed globally. As a result, the opportunity to operate in foreign countries is a key factor in expanding the Canadian industry. Those opportunities are often linked directly or indirectly to reciprocal business opportunities within Canada.

Canadian legislation regarding foreign investment contains powers to restrict investment. This historical debate often centres upon conclusions that a brain drain results from foreign investment; that Canada's cities are hollowed out with flight of offices and personnel out of Canada; and that issues of sovereignty and profits are put at risk with such investment. Past reviews have shown these effects are minor at best when compared to the advantages that result from FDI in capital, technology and innovation.

Federal government authority to review of foreign investments already exists. The ICA catches two types of investments; first, the acquisition of control, directly or indirectly, of existing Canadian businesses and; second, investments to create new Canadian businesses triggered by "non-Canadians". The key test is the net benefit test and is initiated based upon the value of the transaction and WTO status. The real test is whether Canadians are better off or at least neutral if an acquisition takes place and what restrictions should be placed upon the transaction for that to be the case.

Conclusion

The present policy review should include as an objective to do away with specific ownership restrictions and rely upon the ICA to safeguard Canada's interests. The movement in public policy should continue and be uniform for all corporate interests.

The presence of foreign investment levels that have been increasing for the last 30 years have had positive impacts upon the ability of Canadian corporations to compete domestically and globally.

Foreign investment and involvement in the oil and gas sector has historically been positive and should be maintained. This is especially important as oil and gas reserves become harder to exploit. Greater investment, improved technology and increased efficiencies, all of which are enhanced by foreign involvement, will be necessary to efficiently locate and develop future reserves. In the future a sustainable energy portfolio involving domestic and international resources will be necessary. A key component to building a mixed energy portfolio will be the existence of a fair and reciprocal program of foreign investment. This will help domestic efforts to continue to grow and will also be an important step to facilitate access to foreign resources by Canadian companies and to allow the sale of Canadian oil and gas knowledge and technology overseas.

We believe the ICA with its current power of review for large scale foreign investment can be retained without expanding those powers. Canada's FDI and CDIA levels reveal a balance that does not require adjustment to the ICA and its review provisions.

Where investment review provisions exist within legislation and regulation they should be brought together within the provisions of the ICA. Current levels of inward and outward foreign investment indicate that the strength of Canada's economy has been positively impacted from such investment and the ICA is more than adequate for purposes of acting as a monitor for foreign investment.

¹ "Sharpening Canada's Competitive Edge" Competition Policy Review Panel Consultation Paper, October 30, 2007, p. 2.

² "Canadian Government Policies Toward Inward Foreign Direct Investment", Steven Globerman and Daniel Shapiro, Industry Canada Research Publications, Working Paper 24 – September 1998, p. 29

³ Ibid., p. 29

⁴ Ibid., p.29

⁵ Ibid., p.29

⁶ Ibid., p.63

⁷ Ibid., p. 31

⁸ Canada Order in Council PC number 154, 19 January 1914, "Petroleum and Natural Gas Regulations". For a discussion of the origin of section 40 see D.H. Breen, "Anglo-American Rivalry and the Evolution of Canada Petroleum Policy to 1930". *Canadian Historical Review*, LXII, 3 (September, 1981) pages 283-304.