



Auditor's Report

To the Minister of Energy

I have audited the statements of financial position of the Department of Energy as at March 31, 2010 and 2009 and the statements of operations and cash flows for the years then ended. These financial statements are the responsibility of the Department's management. My responsibility is to express an opinion on these financial statements based on my audits.

I conducted my audits in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Department as at March 31, 2010 and 2009 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Original signed by Merwan N. Saher

CA
Auditor General

Edmonton, Alberta
June 8, 2010

MINISTRY OF ENERGY
CONSOLIDATED STATEMENTS OF OPERATIONS
Year ended March 31

| | (in thousands) | | |
|--|---------------------------|---------------------|----------------------|
| | 2010 | | 2009 |
| | Estimates (Schedule 3) | Actual | Actual |
| Revenues (Schedule 1) | | | |
| Non-Renewable Resource Revenue | \$ 5,903,000 | \$ 6,767,941 | \$ 11,915,296 |
| Freehold Mineral Rights Tax | 200,000 | 124,466 | 260,913 |
| Industry Levies and Licences | 145,743 | 142,226 | 140,567 |
| Other Revenue | 12,959 | 45,833 | 42,636 |
| | <u>6,261,702</u> | <u>7,080,466</u> | <u>12,359,412</u> |
| Expenses - Directly Incurred (Note 2 and Schedules 2 and 3) | | | |
| Ministry Support Services | 2,195 | 2,010 | 2,053 |
| Resource Development and Management | 279,146 | 176,214 | 174,228 |
| Energy and Utilities Regulation | 219,995 | 209,737 | 218,519 |
| | <u>501,336</u> | <u>387,961</u> | <u>394,800</u> |
| Net Operating Results | <u>\$ 5,760,366</u> | <u>\$ 6,692,505</u> | <u>\$ 11,964,612</u> |

The accompanying notes and schedules are part of these consolidated financial statements.

MINISTRY OF ENERGY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
As at March 31

| | (in thousands) | |
|---|---------------------|---------------------|
| | <u>2010</u> | <u>2009</u> |
| Assets | | |
| Cash (Notes 3 and 7) | \$ 532,113 | \$ 528,966 |
| Accounts Receivable (Note 4) | 1,292,459 | 582,991 |
| Inventory Held for Resale | 16,595 | - |
| Prepaid Expenses | 6,474 | 3,031 |
| Accrued Pension Asset (Note 8) | 8,298 | 8,272 |
| Tangible Capital Assets (Note 5) | 87,860 | 83,427 |
| | <u>\$ 1,943,799</u> | <u>\$ 1,206,687</u> |
| Liabilities | | |
| Accounts Payable and Accrued Liabilities | \$ 643,719 | \$ 231,667 |
| Gas Royalty Deposits (Note 6) | 1,040,553 | 1,040,214 |
| Unearned Revenue | 71,414 | 71,652 |
| Security Deposits (Note 7) | 38,557 | 35,941 |
| Tenant Incentives | 428 | 1,070 |
| | <u>1,794,671</u> | <u>1,380,544</u> |
| Net Assets (Liabilities): | | |
| Net (Liabilities) Assets at Beginning of Year | (173,857) | 1,536,650 |
| Net Operating Results | 6,692,505 | 11,964,612 |
| Net Financing Provided for General Revenues | <u>(6,369,520)</u> | <u>(13,675,119)</u> |
| Net Assets (Liabilities) at End of Year | <u>149,128</u> | <u>(173,857)</u> |
| | <u>\$ 1,943,799</u> | <u>\$ 1,206,687</u> |

The accompanying notes and schedules are part of these consolidated financial statements.

MINISTRY OF ENERGY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Year ended March 31

| | (in thousands) | |
|---|--------------------|---------------------|
| | <u>2010</u> | <u>2009</u> |
| Operating Transactions | | |
| Net Operating Results | \$ 6,692,505 | \$ 11,964,612 |
| Non-cash items included in Net Operating Results | | |
| Amortization | 21,520 | 20,692 |
| Loss on Disposal of Tangible Capital Assets | 500 | 7 |
| Valuation Adjustments | 784 | 785 |
| | <u>6,715,309</u> | <u>11,986,096</u> |
| | | |
| (Increase) Decrease in Accounts Receivable | (709,468) | 1,517,931 |
| (Increase) Decrease in Inventory | (16,595) | 14,081 |
| Increase in Prepaid Expenses and Accrued Pension Asset | (3,469) | (1,024) |
| Increase (Decrease) in Accounts Payable and Accrued Liabilities | 411,268 | (142,246) |
| (Decrease) Increase in Unearned Revenue | (238) | 262 |
| Decrease in Tenant Incentives | (642) | (725) |
| Cash Provided by Operating Transactions | <u>6,396,165</u> | <u>13,374,375</u> |
| | | |
| Capital Transactions | | |
| Acquisition of Tangible Capital Assets | (26,491) | (28,214) |
| Proceeds on Disposal/Sale of Tangible Capital Assets | 38 | - |
| Cash Applied to Capital Transactions | <u>(26,453)</u> | <u>(28,214)</u> |
| | | |
| Financing Transactions | | |
| Net Financing Provided for General Revenues | (6,369,520) | (13,675,119) |
| Increase in Gas Royalty Deposits | 339 | 54,090 |
| Increase in Security Deposits | 2,616 | 4,717 |
| Cash Applied to Financing Transactions | <u>(6,366,565)</u> | <u>(13,616,312)</u> |
| | | |
| Increase (Decrease) in Cash | 3,147 | (270,151) |
| Cash at Beginning of Year | 528,966 | 799,117 |
| Cash at End of Year | <u>\$ 532,113</u> | <u>\$ 528,966</u> |

The accompanying notes and schedules are part of these consolidated financial statements.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 1 Authority

The Minister of Energy has been designated as responsible for various Acts by the *Government Organization Act* and its regulations. To fulfill these responsibilities, the Minister administers the organizations listed below. The authority under which each organization operates is also listed. Together, these organizations form the Ministry of Energy.

| Organization | Authority |
|---|--|
| Department of Energy (The Department) | <i>Government Organization Act</i> |
| Energy Resources Conservation Board (The ERCB) | <i>Energy Resources Conservation Act</i> |
| Alberta Utilities Commission (The AUC) | <i>Alberta Utilities Commission Act</i> |
| Alberta Petroleum Marketing Commission (The Commission) | <i>Petroleum Marketing Act and the Natural Gas Marketing Act</i> |

Note 2 Summary of Significant Accounting Policies and Reporting Practices

These financial statements are prepared primarily in accordance with Canadian generally accepted accounting principles for the public sector as recommended by the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants. The PSAB financial statements presentation standard for government summary financial statements has been modified to more appropriately reflect the nature of the Ministry.

Basis of Financial Reporting

Basis of Consolidation

The accounts of the Department, the ERCB, the AUC, and the Commission are consolidated. Revenue and expense transactions, capital and financing transactions, and related asset and liability accounts between entities within the Ministry have been eliminated.

The reporting period of the Commission is December 31. Transactions that have occurred during the period January 1 to March 31 and that significantly affect the consolidation have been recorded.

Revenues

All revenues are reported on the accrual basis of accounting. Cash received for which goods or services which have not been provided by year end is recorded as unearned revenue. The provincial royalty system is predicated on self-reporting where the petroleum and natural gas industry is expected to understand the relevant energy legislation (statutes and regulations) and comply with them. This has an impact on the completeness of revenue when the petroleum and natural gas industry do not fully meet the legislative requirements and, for example, report inaccurate or incomplete production data. The Ministry has implemented systems and controls to detect and correct situations where the petroleum and natural gas industry has not complied with the various Acts and Regulations the Ministry administers. These systems and controls, based on areas of highest risk, include performing audits of the petroleum and natural gas industry records where determined necessary by the Ministry. The Ministry does not estimate the effect of misreported revenue.

Crude oil and natural gas royalties are determined based on monthly production. Revenue is recognized when the resource is produced by the mineral rights holders.

Synthetic crude oil and bitumen royalties are determined based on revenues from production sold by projects less the costs of that production and the costs of selling the Crown's royalty share. Royalty revenue is recognized when the resource is produced by the mineral rights holders.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 2 Summary of Significant Accounting Policies and Reporting Practices (continued)

Basis of Financial Reporting (continued)

Revenues (continued)

Freehold mineral taxes are determined at the end of a calendar year based on production and costs of production incurred in the calendar year. Revenue is recognized on a prorated basis, by month, of the estimated calendar year taxes and royalty that will be due to the Crown.

Revenue from bonuses and sales of Crown leases is recognized when the Crown leases are sold. Rentals and fees revenue is recognized over the term of the leases.

Industry levies and assessments are recognized as revenue in the year receivable.

Expenses

Directly Incurred

Directly incurred expenses are those costs the Ministry has primary responsibility and accountability for, as reflected in the Government's budget documents.

In addition to program operating expenses such as salaries, supplies, etc., directly incurred expenses also include:

- amortization of tangible capital assets.
- pension costs which comprise the cost of employer contributions during the year.
- current service costs for the defined benefit pension plans. The ERCB and the AUC have their own defined benefit pension plans. The ERCB's and the AUC's pension expense is actuarially determined using the projected benefit method prorated on length of service and management's best estimate of expected plan investment performance, projected employees' compensation levels, and length of service to the time of retirement. Net accumulated actuarial gain or loss is deferred and amortized over the average remaining service period of the active employees, which is 8 years. For the purpose of calculating the expected return, plan assets are valued at fair value. Past service costs arising from plan amendments are deferred and amortized on a straight line basis over the average remaining service period of active employees at the date of amendment.
- valuation adjustments which include changes in the valuation allowances used to reflect financial assets at their net recoverable or other appropriate value. Valuation adjustments also represent the change in management's estimate of future payments arising from obligations relating to vacation pay.

Grants are recognized as expenses when authorized and eligibility criteria, if any, are met.

Incurred by Others

Services contributed by other entities in support of the Ministry operations are disclosed in Schedule 3 and are not reflected in the consolidated statements of operations.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 2 Summary of Significant Accounting Policies and Reporting Practices (continued)

Basis of Financial Reporting (continued)

Assets

Financial assets are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations. Financial assets of the Ministry are limited to financial claims, such as advances to and receivables from other organizations, employees and other individuals.

Assets acquired by right are not included. Tangible capital assets of the Ministry are recorded at historical cost and amortized on a straight-line basis over the estimated useful lives of the assets. The threshold for capitalizing new systems development is \$250 and the threshold for major systems enhancements is \$100. The threshold for all other tangible capital assets is \$5.

Inventory consists of conventional and synthetic oil in feeder and trunk pipelines. Inventories are stated at lower of cost or net realizable value.

When physical assets are gifted or sold for a nominal sum to parties external to the government reporting entity, the fair values of these physical assets less any nominal proceeds are recorded as grants in kind.

Liabilities

Liabilities are recorded to the extent that they represent present obligations as a result of events and transactions occurring prior to the end of fiscal year. The settlement of liabilities will result in sacrifice of economic benefits in the future.

Liabilities include all financial claims payable by the Ministry at fiscal year end.

Valuation of Financial Assets and Liabilities

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

The fair values of cash, accounts receivable, advances, accounts payable and accrued liabilities, security deposits, and gas royalty deposits are estimated to approximate their carrying values because of the short term nature of these instruments.

Net Assets (Liabilities)

Net assets (liabilities) represent the difference between the carrying value of assets held by the Ministry and its liabilities.

Note 3 Cash

Cash consists of deposits in the Consolidated Cash Investment Trust Fund which is managed by the Province of Alberta with the objective of providing competitive interest income to depositors while maintaining appropriate security and liquidity of depositors' capital. The Fund is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of three years. As at March 31, 2010, securities held by the Fund have a time-weighted rate of return of 1.0% per annum (2009: 3.0% per annum). Deposits received by the Ministry as security against leases are included in cash.

Note 4 Accounts Receivable

Accounts receivable are secured by a claim against the mineral leases.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 5 Tangible Capital Assets

| | Land | Equipment | Computer hardware and software | 2010 Total | 2009 Total |
|----------------------------------|---------------|------------------|--------------------------------|-------------------|-------------------|
| Estimated Useful Life | Indefinite | 3 to 10 years | 3 to 20 years | | |
| Historical Cost | | | | | |
| Beginning of Year | \$ 320 | \$ 46,877 | \$ 171,575 | \$ 218,772 | \$ 193,488 |
| Additions | - | 2,628 | 23,863 | 26,491 | 28,214 |
| Disposals, Including Write-Downs | (38) | (386) | (3,151) | (3,575) | (2,930) |
| | <u>\$ 282</u> | <u>\$ 49,119</u> | <u>\$ 192,287</u> | <u>\$ 241,688</u> | <u>\$ 218,772</u> |
| Accumulated Amortization | | | | | |
| Beginning of Year | \$ - | \$ 28,149 | \$ 107,196 | \$ 135,345 | \$ 117,576 |
| Amortization Expense | - | 4,267 | 17,253 | 21,520 | 20,692 |
| Effect of Disposals | - | (383) | (2,654) | (3,037) | (2,923) |
| | <u>\$ -</u> | <u>\$ 32,033</u> | <u>\$ 121,795</u> | <u>\$ 153,828</u> | <u>\$ 135,345</u> |
| Net Book Value, March 31, 2010 | <u>\$ 282</u> | <u>\$ 17,086</u> | <u>\$ 70,492</u> | <u>\$ 87,860</u> | |
| Net Book Value, March 31, 2009 | <u>\$ 320</u> | <u>\$ 18,728</u> | <u>\$ 64,379</u> | | <u>\$ 83,427</u> |

Equipment includes leasehold improvements, office equipment and furniture, and other equipment.

Historical cost includes work-in-progress at March 31, 2010 totaling \$13,871 (2009 - \$9,739) comprised of software.

Note 6 Gas Royalty Deposits

The Ministry requires that natural gas producers maintain a deposit which in most cases is equal to one-sixth of the prior calendar year's royalties multiplied by the ratio of the long term gas reference price on the date which the recalculation of the gas deposits is determined to the prior calendar year average gas reference price. The Ministry does not pay interest on the deposits.

Note 7 Security Deposits

The Ministry encourages the timely and proper abandonment and reclamation of upstream wells, facilities, pipelines, and oilfield waste management facilities by holding various forms of security. At March 31, 2010, the Ministry held \$38,557 (2009: \$35,941) in cash and an additional \$77,717 (2009: \$138,130) in letters of credit. The security, along with any interest earned, will be returned to the depositor upon meeting specified refund criteria.

Note 8 Employee Future Benefits

The Ministry participates in multi-employer pension plans, Management Employees Pension Plan and Public Service Pension Plan. The Ministry also participates in the multi-employer Supplementary Retirement Plan for Public Service Managers. The expense for these pension plans is equivalent to the annual contributions of \$14,051 for the year ended March 31, 2010 (2009 - \$11,502).

At December 31, 2009, the Management Employees Pension Plan reported a deficiency of \$483,199 (2008 - \$568,574) and the Public Service Pension Plan reported a deficiency of \$1,729,196 (2008 - \$1,187,538). At December 31, 2009, the Supplementary Retirement Plan for Public Service Managers had a deficiency of \$39,516 (2008 - \$7,111).

MINISTRY OF ENERGY
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 (in thousands)

Note 8 Employee Future Benefits (continued)

The Ministry also participates in two multi-employer Long Term Disability Income Continuance Plans. At March 31, 2010, the Bargaining Unit Plan reported an actuarial deficiency of \$8,335 (2009 – deficiency \$33,540) and the Management, Opted Out and Excluded Plan an actuarial surplus of \$7,431 (2009 – deficiency \$1,051). The expense for these two plans is limited to the employer's annual contributions for the year.

In addition, the ERCB and the AUC maintain their own defined benefit Senior Employees Pension Plan (SEPP) and two supplementary pension plans to compensate senior staff who do not participate in the government management pension plans. Retirement benefits are based on each employee's years of service and remuneration. The date used to measure all pension plan assets and accrued benefit obligations was March 31, 2010. The effective date of the most recent actuarial funding valuation for SEPP was December 31, 2008. The effective date of the next required funding valuation for SEPP is December 31, 2011. Significant actuarial and economic assumptions used to value accrued benefit obligations and pension costs are as follows:

a) ERCB

| | <u>2010</u> | <u>2009</u> |
|--|-------------|-------------|
| Accrued benefits obligations | | |
| Discount rate | 6.2% | 8.6% |
| Rate of compensation increase (weighted average) | 3.5% | 3.5% |
| Benefit costs for the year | | |
| Discount rate | 8.6% | 6.1% |
| Expected long-term rate of return on plan assets | 6.5% | 6.3% |
| Rate of compensation increase | 3.5% | 3.5% |

The funded status and amounts recognized in the Consolidated Statements of Financial Position are as follows:

| | <u>2010</u> | <u>2009</u> |
|--------------------------------|-----------------|-----------------|
| Plan assets at fair value | \$ 28,497 | \$ 24,440 |
| Accrued benefit obligation | 28,544 | 17,690 |
| Plan (deficit) surplus | (47) | 6,750 |
| Unamortized net actuarial loss | 7,474 | 673 |
| Accrued pension asset | <u>\$ 7,427</u> | <u>\$ 7,423</u> |

The asset allocation of the defined benefit pension plans investments is as follows:

| | <u>2010</u> | <u>2009</u> |
|-------------------|---------------|---------------|
| Equity securities | 46.5 % | 40.4 % |
| Debt securities | 41.7 % | 39.7 % |
| Other | 11.8 % | 19.9 % |
| | <u>100.0%</u> | <u>100.0%</u> |

Additional information about the defined benefit pension plans are as follows:

| | <u>2010</u> | <u>2009</u> |
|-------------------------|-------------|-------------|
| ERCB contribution | \$ 812 | \$1,519 |
| Employees' contribution | 386 | 319 |
| Benefit paid | 851 | 919 |
| Pension benefit costs | 808 | 1,391 |

MINISTRY OF ENERGY
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 (in thousands)

Note 8 Employee Future Benefits (continued)

b) AUC

| | <u>2010</u> | <u>2009</u> |
|--|-------------|-------------|
| Accrued benefits obligations | | |
| Discount rate | 6.2% | 8.6% |
| Rate of compensation increase (weighted average) | 3.5% | 3.5% |
| Benefit costs for the year | | |
| Discount rate | 8.6% | 6.1% |
| Expected long-term rate of return on plan assets | 6.2% | 6.3% |
| Rate of compensation increase | 3.5% | 3.5% |

The funded status and amounts recognized in the Consolidated Statements of Financial Position are as follows:

| | <u>2010</u> | <u>2009</u> |
|---------------------------------------|---------------|---------------|
| Plan assets at fair value | \$ 3,450 | \$ 2,950 |
| Accrued benefit obligation | <u>3,607</u> | <u>2,000</u> |
| Plan (deficit) surplus | (157) | 950 |
| Unamortized net actuarial (gain) loss | <u>1,028</u> | <u>(101)</u> |
| Accrued pension asset | <u>\$ 871</u> | <u>\$ 849</u> |

Additional information about the defined benefit plans are as follows:

| | <u>2010</u> | <u>2009</u> |
|-------------------------|-------------|-------------|
| AUC contribution | \$200 | \$328 |
| Employees' contribution | 100 | 84 |
| Benefit paid | 231 | - |
| Pension expense | 178 | 274 |

The asset allocation of the defined benefit pension plans investments is as follows:

| | <u>2010</u> | <u>2009</u> |
|-------------------|---------------|---------------|
| Equity securities | 44.5 % | 39.0 % |
| Debt securities | 39.5 % | 38.4 % |
| Other | 16.0 % | 22.6 % |
| | <u>100.0%</u> | <u>100.0%</u> |

Note 9 Trust Funds under Administration

The Ministry administers trust funds which are regulated funds consisting of public money over which the Legislature has no power of appropriation. Because the Province has no equity in the funds, and administers them for the purpose of various trusts, they are not included in the Ministry's financial statements.

As at March 31 trust funds under administration were as follows:

| | <u>2010</u> | <u>2009</u> |
|--------------------------------|-----------------|-----------------|
| Oil and Gas Conservation Trust | <u>\$ 3,806</u> | <u>\$ 3,718</u> |

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 10 Commitments

Commitments to outside organizations in respect of contracts entered into before March 31, 2010 amount to \$247,645 (2009 - \$63,582). These commitments will become expenses of the Ministry when terms of the contracts are met. Payments in respect of these contracts and agreements are subject to the voting of supply by the Legislature.

These amounts include obligations under long-term leases with lease payment requirements in future years of:

| | Grant Agreements | Service Contracts | Long-term Leases | Total |
|------------|---------------------|----------------------|---------------------|-------------------|
| 2011 | \$ 28,999 | \$ 14,095 | \$ 8,821 | \$ 51,915 |
| 2012 | - | 2,202 | 9,763 | 11,965 |
| 2013 | - | 2,202 | 9,665 | 11,867 |
| 2014 | - | 2,202 | 9,737 | 11,939 |
| 2015 | - | 2,202 | 9,533 | 11,735 |
| Thereafter | - | 2,202 | 146,022 | 148,224 |
| | <u>\$ 28,999</u> | <u>\$ 25,105</u> | <u>\$ 193,541</u> | <u>\$ 247,645</u> |

Alberta Petroleum Marketing Commission

The Alberta Petroleum Marketing Commission has allocated a portion of its anticipated pipeline requirements to transportation agreements expiring in March 2012. These agreements obligate the Commission to pay tariff charges for contracted volumes in accordance with contracted rates. The aggregate estimated commitment at December 31, 2009 is \$17,986 (2008 - \$30,044). This commitment will be paid from future oil royalty revenue. Costs for these pipeline services are expected to be within the range of normal transportation costs.

| | Total |
|------|------------------|
| 2010 | \$ 7,994 |
| 2011 | 7,994 |
| 2012 | 1,998 |
| | <u>\$ 17,986</u> |

Note 11 Contingencies and Other Liabilities

Set out below are details of contingencies resulting from administrative actions and litigation, other than those reported as liabilities.

(a) Land Claims

The government identifies and set aside specific tracts of land to satisfy land claims made by Indian Bands. The claims related to these lands are under negotiation but are not yet resolved. In one instance, the Ministry may have to revoke 23 petroleum and natural gas dispositions for which the government accepted bonuses, rental payments and royalties. When these land claims will be resolved is unknown. In the opinion of management, any losses that may result from the eventual settlement of these land claims cannot be determined at this time.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 11 Contingencies and Other Liabilities (continued)

(b) Legal Claims

At March 31, 2010, the Ministry is a defendant in six legal claims (2009 – seven legal claims). Four of these claims have specified amounts totaling \$1,373,265 and the remaining two claims have no specified amount (2009 – five with specified amounts totaling \$1,375,596 and the remaining two claims with no specified amount). The Ministry has been jointly named with other entities in four claims (2009 – all claims specified amounts totaling \$1,375,596). One claim totaling \$572,500 (2009 – zero) is covered by the Alberta Risk Management Fund.

The resulting loss, if any, from these claims cannot be determined.

(c) Bitumen Royalties

On January 1, 2009, the Province implemented the New Royalty Framework. As part of the New Royalty Framework, the Bitumen Valuation Methodology (Ministerial) Regulation (the "BVM Regulation") was enacted. The BVM Regulation establishes a method to determine a deemed price for bitumen for producers who dispose of bitumen mostly through non-arm's length transactions. This price so determined factors into the calculation of royalties due to the Province from oil sands projects.

The Province has "Royalty Amending Agreements" with two oil sands royalty projects, governing royalties through 2015. In each case the Royalty Amending Agreement (RAA) undertakes that the bitumen valuation methodology ("BVM") applicable to the project will include "reasonable adjustments" to reflect quality differences between the project's bitumen and the bitumen reflected in the deemed price used in the BVM Regulation and also to reflect transportation costs to the reference price location.

Non-renewable resource revenue reported in 2010 on the consolidated statements of operations includes an estimate of the royalties that the Ministry expects to recover from the two projects.

During 2009, Suncor and Syncrude filed non-compliance notices with the Province, alleging that the BVM Regulation does not establish the reasonable quality and transportation adjustments required by their respective RAAs.

The Province amended the Oil Sands Royalty Regulation in 2009 to include a methodology to determine royalty amounts due to the Province on pre-2009 inventory and pre-2009 transitional inventory. This royalty was due April 30, 2010. Both companies have indicated that no amounts are owing for this inventory because of their RAAs.

The Royalty Amending Agreements include a dispute resolution process that, if unsuccessful, will culminate in the one instance in arbitration and in the other instance in Court proceedings. Bitumen royalties reported may be adjusted following resolution of these issues, potentially significantly.

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 12 Measurement Uncertainty

Measurement uncertainty exists when there is a significant variance between the amount recognized in the financial statements and another reasonably possible amount. Natural gas and by-products revenue recorded as \$1,525,397 and synthetic crude oil and bitumen royalties recorded as \$3,160,349 in these financial statements are subject to measurement uncertainty.

Natural gas and by-products revenue is calculated based on allowable costs incurred by the royalty payers and production volumes that are reported to the Ministry by royalty payers. These costs and volumes could vary significantly from that initially reported. The Ministry estimates what the costs, volumes and royalty rates for the fiscal year should be based on statistical analysis of industry data. Based on historical data, natural gas and by-products revenue could change by \$175,000.

For projects from which synthetic crude oil and bitumen royalties are paid and the project has reached payout, the royalty rate used to determine the royalties is based on the average price of West Texas Intermediate crude oil in Canadian dollars for the calendar year. Royalty rates will start at 25% of net profits when oil is priced at fifty five dollars per barrel or less, and increase to a maximum of 40% of net profits when oil is priced at one hundred and twenty dollars or more. Payout is defined at the first date at which the cumulative revenue of a project first equals the cumulative cost of the project.

Drilling royalty credits recorded under the Energy Industry Drilling Stimulus Program include an estimate of \$283,000 for credits expected to be claimed in the future for royalties paid between April 1, 2009 and March 31, 2010. The actual amounts claimed and paid could be materially different than the amount estimated.

Note 13 Related Party Transactions

The Ministry paid \$5,466 (2009 - \$7,670) to various other Government of Alberta departments, agencies or funds for supplies and/or services during the fiscal year and received \$293 (2009 - \$2,388) as revenue. Included in these services was a payment of \$48 (2009 - \$412) for the lease of a research facility from Alberta Infrastructure. The remaining term of this lease is 76 years and the future annual payments are \$48.

Accommodations, legal, telecommunications, personnel, internal audit services, and certain financial costs were provided to the Ministry by other government organizations at no cost. However, services contributed by other entities in support of the Ministry operations are disclosed in Schedule 3.

Note 14 Royalty Reduction Programs

The Ministry provides the Energy Industry Drilling Stimulus Program along with seven other oil and gas royalty reduction programs. The intent of these programs is to encourage industry to produce from wells which otherwise would not be economically productive. For the year ended March 31, 2010, the royalties received under these programs were reduced by \$1,465,144 (2009 - \$671,066).

Note 15 Bitumen Conservation

In 2004-05 the Alberta Energy and Utilities (EUB) Board released its Bitumen Conservation Requirements decisions regarding the status of natural gas wells in the Wabiskaw-McMurray region of the Athabasca Oil Sands area. The decisions recommended the shut-in of Wabiskaw-McMurray natural gas totaling about 53.6 billions of cubic feet annually to protect about 25.5 billion barrels of potentially recoverable bitumen. The Natural Gas Royalty Regulations, 2002 was amended to provide a royalty mechanism that would allow the Minister of Energy to calculate a royalty adjustment each month for gas producers affected by the EUB decisions. The Natural Gas Royalty Regulations, 2002 was also amended to provide for the royalty adjustment to be recovered through additional royalty on the shut-in wells when they return to production through amendments to the provisions that deal with the calculation of the royalty share of gas. The amendments provide for an increase over and above the usual royalty rate, and extend to new wells that produce from the shut-in zone. The effect of these adjustments was to reduce natural gas and by-products revenue by \$61,919 (2009 - \$132,018).

MINISTRY OF ENERGY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands)

Note 16 Energy Industry Drilling Stimulus Program

Starting April 1, 2009, the Ministry implemented a drilling stimulus program that impacted the royalties for the year ended March 31, 2010. The first feature was a maximum royalty rate of 5% for the first 50,000 barrels of oil or 500,000 Mcf of gas produced from a well drilled on or after April 1, 2009.

The second feature was a drilling credit of \$200 per metre for wells drilled between April 1, 2009 and March 31, 2010. A sliding scale of 10% to 50%, (based on the oil and gas production level of a company) of 2009/10 natural gas and conventional oil royalties, caps the amount of the credit a company can receive. The Province announced an extension of the program by one year on June 25, 2009.

In the fiscal year ended March 31, 2010, natural gas and by-product royalties and conventional oil royalties were reduced by \$197,226 and \$135,625 respectively due to the New Well Royalty Rate feature, while \$786,203 was reduced due to the drilling credit feature.

Note 17 Approval of Financial Statements

The financial statements were approved by the Deputy Minister and the Senior Financial Officer of the Ministry.

MINISTRY OF ENERGY

Schedule 1

CONSOLIDATED SCHEDULES TO FINANCIAL STATEMENTS

Revenues

Year ended March 31

| | (in thousands) | | |
|---|---------------------|---------------------|----------------------|
| | 2010 | | 2009 |
| | Budget | Actual | Actual |
| Non-Renewable Resource Revenue (Note 14) | | | |
| Synthetic Crude Oil and Bitumen Royalty (Note 11c) | \$ 1,008,000 | \$ 3,160,349 | \$ 2,973,132 |
| Crude Oil Royalty | 1,249,000 | 1,848,269 | 1,800,120 |
| Natural Gas and By-Products Royalty (Note 15) | 3,687,000 | 1,525,397 | 5,834,006 |
| Bonuses and Sales of Crown Leases | 631,000 | 1,164,407 | 1,112,403 |
| Rentals and Fees | 143,000 | 157,707 | 159,865 |
| Coal Royalty | 27,000 | 30,866 | 35,770 |
| Energy Industry Drilling Stimulus Program (Note 16) | (842,000) | (1,119,054) | - |
| | <u>5,903,000</u> | <u>6,767,941</u> | <u>11,915,296</u> |
| Freehold Mineral Rights Tax | 200,000 | 124,466 | 260,913 |
| Industry Levies and Licenses | 145,743 | 142,226 | 140,567 |
| Other Revenue | | | |
| Other | 9,859 | 45,074 | 39,975 |
| Interest | 3,100 | 759 | 2,661 |
| | <u>12,959</u> | <u>45,833</u> | <u>42,636</u> |
| Total Revenue | <u>\$ 6,261,702</u> | <u>\$ 7,080,466</u> | <u>\$ 12,359,412</u> |

MINISTRY OF ENERGY

Schedule 2

CONSOLIDATED SCHEDULES TO FINANCIAL STATEMENTS

Expenses - Directly Incurred Detailed by Object

Year ended March 31

| | (in thousands) | | |
|---|-------------------|-------------------|-------------------|
| | 2010 | | 2009 |
| | Budget | Actual | Actual |
| Voted | | | |
| Salaries, Wages and Employee Benefits | \$ 198,282 | \$ 190,579 | \$ 181,536 |
| Supplies and Services | 80,446 | 93,314 | 85,597 |
| Grants | 190,000 | 68,709 | 93,904 |
| Amortization Of Tangible Capital Assets | 20,088 | 22,020 | 20,699 |
| Well Abandonment | 13,000 | 13,000 | 12,727 |
| Valuation Adjustments | - | 784 | 785 |
| Financial Transactions and Other | 120 | 120 | 122 |
| Total Voted Expenses before Recoveries | <u>501,936</u> | <u>388,526</u> | <u>395,370</u> |
| Less Recovery from Support Service Arrangements with Related Parties | (600) | (565) | (570) |
| Total Voted Expenses | <u>\$ 501,336</u> | <u>\$ 387,961</u> | <u>\$ 394,800</u> |

MINISTRY OF ENERGY

Schedule 3

CONSOLIDATED SCHEDULES TO FINANCIAL STATEMENTS

Allocated Costs

Year ended March 31

(in thousands)

| Program | 2010 | | | | | | | 2009 | | Total Expenses | Total Expenses |
|-------------------------------------|-------------------------|-----------------------------|----------------------|-----------------|---------------------|-----------------|-----------------------|-------------------|-------------------|-------------------|----------------|
| | Expenses ⁽¹⁾ | Expenses Incurred by Others | | | | | Valuation Adjustments | | | | |
| | | Accommodation Costs | Transportation Costs | Service Alberta | GOA Learning Centre | Legal Services | Vacation Pay | Doubtful Accounts | | | |
| Ministry Support Services | \$ 2,010 | \$ 307 | \$ - | \$ - | \$ - | \$ 142 | \$ 8 | \$ - | \$ 2,467 | \$ 2,345 | |
| Resource Development and Management | 176,214 | 5,844 | 475 | 3,358 | 130 | 3,414 | 774 | 2 | 190,211 | 182,088 | |
| Energy and Utilities Regulation | 209,737 | - | - | - | - | - | - | - | 209,737 | 218,683 | |
| | <u>\$ 387,961</u> | <u>\$ 6,151</u> | <u>\$ 475</u> | <u>\$ 3,358</u> | <u>\$ 130</u> | <u>\$ 3,556</u> | <u>\$ 782</u> | <u>\$ 2</u> | <u>\$ 402,415</u> | <u>\$ 403,116</u> | |

(1) Expenses - Directly Incurred as per Statement of Operations, excluding valuation adjustments.