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BACKGROUNDER

LNG INCOME TAX BALANCES COMPETITIVENESS, FAIR RETURN

VICTORIA — The Province continues to develop and implement all the elements of a competitive tax and policy environment to assist with LNG development in B.C. To this end, government intends to introduce legislation later this year to introduce an income tax applicable to the LNG industry.

The LNG Income Tax will be a two-tier tax with a tier-one tax rate of 1.5 per cent and a tier-two rate of up to seven per cent, with the final rates to be determined and confirmed in legislation. The LNG Income Tax will apply to income from liquefaction of natural gas at LNG facilities in British Columbia.

A description of how the two tiers operate is as follows:

- The tier one tax rate of 1.5 per cent applies to an operator's net proceeds (revenue less expenses) after commercial production begins. The amount of the tier one tax that has been paid can be deducted from the tier-two tax.
- Net income for purposes of the tier two tax will be net proceeds less up to 100 per cent of the capital investment account (as described below). As such, the tier-two tax rate is not effective until the capital investment account is depleted.

The costs associated with constructing an LNG facility will form the basis of the capital investment account. An LNG facility is a plant that is built to liquefy natural gas. It typically includes gas purification and liquefaction systems, together with storage tanks and marine loading systems. An LNG facility may also include support functions for the liquefaction process, such as control rooms, material and equipment warehousing, maintenance shops and infrastructure facilities.

A review of the tier two tax rate and specific tax features will continue until the legislation is introduced in the fall of 2014. Global and local economic conditions will be considered as government finalizes the key components of the LNG Income Tax to ensure B.C. remains competitive.

To illustrate how the proposed LNG Income Tax works, assume a new LNG plant in B.C. produces 12 million tonnes per year (MTPA) of LNG and earns constant profits over 10 years. Assuming that commercial production of LNG starts in year one, for the first three years only the tier-one tax rate applies. Starting in year four, once the proponent has deducted its capital account, the tier-two rate applies.

However, during the first three years, the amount of the tier-one tax paid is eligible to be used as a credit against the tier-two tax in years four and five. In year six and thereafter, the tax credits for taxes paid in earlier years will have been used and the full tier-two tax will be in effect.

The following types of income generated from the liquefaction of natural gas will be subject to the LNG Income Tax:

- sale of liquefied natural gas;
- rents and fees payable for the use of a LNG facility; and
- fees for processing natural gas at a LNG facility.

The LNG Income Tax will apply to all LNG facilities in the province regardless of whether the LNG is exported or for domestic use.

It is anticipated the key components of the legislation will be ready for introduction by fall 2014 (e.g. tax rates and specific features). Remaining legislative components, such as administration and enforcement, are planned to be ready for introduction in 2015.

The Province has consulted with industry in the development of the LNG Income Tax and believes that this will now help to provide added certainty for proponents as they work towards making final investment decisions.

Competitiveness

The B.C. government has reviewed the tax and royalty regimes of key competitor jurisdictions, namely Australia and the US. It has also consulted with proponents and received their perspectives. In this process, the government retained independent consultants to examine and assess the competitiveness of the B.C. framework, which includes the proposed B.C. LNG Income Tax, with comparable frameworks in those other jurisdictions.

The consultants concluded that the proposed framework, which includes the proposed B.C. LNG Income Tax, appears competitive relative to the existing frameworks in Australia and the five US states examined—Alaska, Georgia, Louisiana, Oregon and Texas.

B.C.'s LNG Income Tax regime is just one element that makes the province internationally competitive for new LNG investment. In addition to a low overall tax burden and a competitive royalty regime, B.C. has large reserves of natural gas located fairly close to proposed facilities; a skilled workforce; robust infrastructure; relatively short transport times to key Asia markets; and a cooler coastal temperature that saves energy and costs during the liquefaction process.

Learn More:

- LNG 101: A Guide to British Columbia's Liquefied Natural Gas Sector:
  http://www.gov.bc.ca/mngd/doc/LNG101.pdf
- For an update on B.C.'s LNG strategy, visit:
  http://www.gov.bc.ca/com/attachments/LNGreport_update2013_web130207.pdf
- 2013 Employment Impact Review:
  http://www.empr.gov.bc.ca/OG/Documents/Grant_Thornton_LNG_Employment_Impacts.pdf
- VIDEO: B.C.'s Liquefied Natural Gas Opportunity:
  http://engage.gov.bc.ca/lnginbc/