ERRATA

The article, "International Royalties on the Extended Continental Shelf: Implications for Canada, Newfoundland, and Equinor" by Alexandra Terrell, which appeared in volume 57 issue 3 of the *Alberta Law Review*, should be corrected as follows:

- On page 790, the paragraph beginning "Pursuant to Article 5…" and the subsequent three paragraphs should be struck and replaced with the following paragraph:

> Residence is defined at common law as the place in which a corporation's "central management and control is exercised."[117] Additionally, a corporation is deemed resident in Canada if it was incorporated in Canada after 26 April 1965.[118] Equinor Canada Ltd. is likely resident in Canada because it was incorporated in Alberta and is therefore subject to the deeming provision in the *Income Tax Act*. As a result, 100 percent of the royalties it pays to the province would be allowable deductions. In effect, this settles some of the burden of the royalty on the rest of the taxpaying Canadian public.

- Footnote 117 should read: Government of Canada, "Residency of a Corporation" (15 March 2018), online: <canada.ca/en/revenue-agency/services/tax/international-non-residents/businesses-international-non-resident-taxes/residency-a-corporation.html>.

- Footnote 118 should read: *Income Tax Act*, *supra* note 115, s 250(4).

- On page 791, the first sentence of the paragraph beginning "The question remains…" should be struck and replaced with the following: Even with this beneficial tax treatment, the question remains whether, normatively speaking, a project proponent *should* pay this international royalty.

INTERNATIONAL ROYALTIES ON THE EXTENDED CONTINENTAL SHELF: IMPLICATIONS FOR CANADA, NEWFOUNDLAND, AND EQUINOR

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Canada's international obligations under Article 82 of the United Nations Convention on the Law of the Sea *impose domestic responsibilities to determine which party is to absorb the royalty payments owed to the International Seabed Authority. Currently, uncertainty exists in the royalty regime for projects within Canada's 200 nautical mile limit waters, with multiple disputes arising between parties to sophisticated contracts. Given the comparatively ambiguous Article 82 language, it is important for Canada, Newfoundland and Labrador, and project proponents to come to a clear conclusion as to who will pay the international royalties. This raises the normative questions of which party should ultimately be paying these royalties, and whether Canada should be shifting its obligations to another party.*

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I. INTRODUCTION

Article 82 of the *United Nations Convention on the Law of the Sea* imposes on coastal States an obligation to make payments or contributions in kind with respect to the exploitation of non-living resources on the continental shelf beyond 200 nautical miles.[1] Article 82 is a somewhat ambiguous provision, providing room for interpretation.

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[1] *United Nations Convention on the Law of the Sea*, 10 December 1982, 1833 UNTS 397 (16 November 1994) [*LOSC*].

Determining which interpretation is to be applied has substantial implications on Canada's financial obligations. With Equinor, a Norwegian offshore operator, soon to commence exploitation on Canada's extended continental shelf off the coast of Newfoundland, Canada must formulate a fiscally sustainable plan to fulfill its Article 82 obligation. This article examines the potential options, which include placing the burden wholly on Canada, Newfoundland, or Equinor, or reaching a compromise between stakeholders. This problem requires consideration of the royalty agreement between Canada and Newfoundland as well as Canada's federal equalization program. In weighing the advantages and disadvantages of each option, this article assesses its administrability, its economic viability, its impact on Canadian taxpayers, and its implications for future exploitation. The best solution is one that is sustainable in both the short and long term, aligns with the purposes expressed in the *Atlantic Accord*[2] and the *LOSC*, and does not deter future developments.

II. THE HISTORY OF SOVEREIGN RIGHTS ON THE CONTINENTAL SHELF

Over the past 75 years, the rights of a coastal State over the continental shelf contiguous to its coast have substantially evolved. An appropriate starting point for the history of this evolution is 28 September 1945. On that day, President Harry S. Truman signed United States Presidential Proclamation 2667, known today as the Truman Proclamation.[3] Within it, President Truman proclaimed that "the United States regards the natural resources of the … continental shelf … contiguous to the coasts of the United States, subject to its jurisdiction and control."[4] This stance is justified in the preamble, which addresses the concern that, given technological progress, expert opinions indicating rich resources in the continental shelf, and the "world-wide need for new sources of petroleum and other minerals,"[5] efforts to discover new supplies ought to be encouraged. It further states that because the exploitation of such resources requires cooperation and protection from shore to ensure "conservation and prudent utilization," this exercise of jurisdiction by the contiguous nation is "reasonable and just."[6] Before the Truman Proclamation, state practices across the globe with regard to continental shelf rights were inconsistent or nonexistent. The Truman Proclamation acted as a catalyst, stimulating states to make similar claims over the seabed and subsoil of their continental shelves.[7] The continental shelf has clear geomorphological markers and is scientifically defined as "the gently sloping submerged marginal zone of the continents extending from shore to an abrupt increase in bottom inclination."[8] The continental shelf rights declared in the Truman Proclamation align with this scientific definition. The Truman Proclamation states that "the continental shelf may be regarded as an extension of the land-mass of the coastal nation and thus naturally appurtenant

[2] *The Atlantic Accord: Memorandum of Agreement Between the Government of Canada and the Government of Newfoundland on Offshore Oil and Gas Resource Management and Revenue Sharing*, 11 February 1985, online: <gov.nl.ca/snl/files/printer-publications-aa-mou.pdf> [*Atlantic Accord*].

[3] *1945 US Presidential Proclamation No. 2667, Policy of the United States with Respect to the Natural Resources of the Subsoil and Sea Bed of the Continental Shelf*, 10 Fed Reg 12305 (1945) [Truman Proclamation].

[4] *Ibid.*

[5] *Ibid.*

[6] *Ibid.*

[7] Donald R Rothwell & Tim Stephens, *The International Law of the Sea*, 2nd ed (Portland: Hart Publishing, 2016) at 105.

[8] Jacob Verhoef, David Mosher & Steve Forbes, "Defining Canada's Extended Continental Shelves" (2011) 38:2 Geoscience Can 85 at 87.

to it."[9] However, state claims to continental shelf resources were not limited to the scientifically defined continental shelf region. Several state claims, including those of Chile, Costa Rica, El Salvador, and Honduras, extended to a fixed distance of 200 nautical miles regardless of the geomorphological markers that would normally delimit it.[10]

At the 1958 Geneva Conference on the Law of the Sea (UNCLOS I), the United States' stance on coastal State sovereignty over the resources of seabed and subsoil of the continental shelf was officially codified in international law. The Convention on the Continental Shelf defined the continental shelf as:

> (*a*) the seabed and subsoil of the submarine areas adjacent to the coast but outside the area of the territorial sea, to a depth of 200 metres or, beyond that limit, to where the depth of the superjacent waters admits of the exploitation of the natural resources of the said areas; (*b*) to the seabed and subsoil of similar submarine areas adjacent to the coasts of islands.[11]

Article 2 granted the coastal State exclusive sovereign rights over the continental shelf for the purposes of exploring it and exploiting its natural resources. Paragraph 3 provided that such rights "do not depend on occupation, effective or notional, or on any express proclamation."[12] A coastal State thus possesses sovereign rights over its continental shelf resources *ipso facto*, *ipso jure*, and *ab initio*.[13]

The definition of the continental shelf was revised at UNCLOS III 1973–1982 to address the risk that, due to advancing technologies, the 1958 definition could result in an ever-expanding continental shelf at the expense of the common heritage of mankind. Article 76 of the Convention on the Law of the Sea produced at UNCLOS III narrowed this risk. The 1958 definition did not specify a particular distance at which the coastal State's sovereign rights would end. The Article 76 definition specifies such limits in one of two ways, "the natural prolongation of its land territory to the outer edge of the continental margin, or to a distance of 200 nautical miles from the baselines from which the breadth of the territorial sea is measured where the outer edge of the continental margin does not extend up to that distance."[14] Paragraphs 4 to 7 of Article 76 define the continental shelf to include not only the shelf proper, but the continental margin and potentially parts of the deep sea bed. Further, these paragraphs provide guidance on geological markers and ocean depth delineating the extended continental shelf limit. The coastal State must submit measurements to the Commission on the Limits of the Continental Shelf (CLCS), and the CLCS will correspondingly make recommendations related to establishing the outer limits of the continental shelf.[15]

The process of establishing the outer limits of the continental shelf is technically difficult and requires the coastal State to dispense a great deal of resources — monetary, technological, and otherwise. Canada has conducted several expeditions in an effort to

[9] *Supra* note 3.

[10] Rothwell & Stephens, *supra* note 7 at 105.

[11] *Convention on the Continental Shelf*, 29 April 1958, 499 UNTS 311, art 1 (10 June 1964) [*CCS*].

[12] *Ibid*, art 2 at para 3.

[13] Rothwell & Stephens, *supra* note 7 at 109.

[14] *LOSC*, *supra* note 1, art 76(1).

[15] *Ibid*, art 76(8).

establish its extended continental shelf limits — in 2013, Canada made a partial submission to the Commission regarding its continental shelf in the Atlantic Ocean;[16] in 2015, Canada launched a scientific survey aimed at gathering data for a submission on its extended Arctic continental shelf;[17] and in 2016, the Canadian icebreaker CCGS Louis S. St-Laurent departed from Dartmouth, NS, headed towards Norway on another Arctic exploration project.[18] In each of the 2015 and 2016 expeditions, Canada collaborated with several other nations and collected data in support of the Atlantic Ocean Research Alliance, which was created pursuant to the Galway Statement on Atlantic Ocean Cooperation, signed by Canada, the United States, and the European Union in 2013.[19] On 23 May 2019, Canada filed submissions regarding its claim to the continental shelf in the Arctic Ocean.[20]

An estimated 85 countries, including Canada, enjoy an extended continental shelf.[21] As of 12 December 2019, the CLCS reported a total of 85 submissions pursuant to Article 76, paragraph 8 of the *LOSC*.[22] With nearly 200 countries worldwide, several of which are entirely land-locked with no coastal access, the riches of the continental shelf are by no means evenly distributed. The *LOSC* addresses the windfall-like gain that coastal States possessing an extended continental shelf receive by imposing an international royalty on resources extracted on it. Article 82 of the *LOSC* entitled "Payments and contributions with respect to the exploitation of the continental shelf beyond 200 nautical miles" provides that: (1) the coastal State must make payments or contributions in kind in respect of any non-living resources exploited on the extended continental shelf;[23] (2) such payments or contributions shall be made annually, starting in the sixth year of production at 1 percent and incrementally increasing by 1 percent to a maximum of 7 percent in the twelfth year. The 7 percent rate remains in place until production desists.[24] It further provides that a "developing State which is a net importer of a mineral resource produced from its continental shelf is exempt from making such payments or contributions in respect of that mineral resource."[25] Finally, it establishes that the payments or contributions should be made through the International Seabed Authority (ISA), "which shall distribute them to States Parties to this Convention, on the basis of equitable sharing criteria, taking into account the interests and needs of developing States, particularly the least developed and the land-locked among them."[26]

[16] Global Affairs Canada, "Canada Marks Major Milestone in Defining Its Continental Shelf" (9 December 2013), online: <international.gc.ca/media/aff/news-communiques/2013/12/09a.aspx?lang=eng>.

[17] Foreign Affairs, Trade and Development Canada, News Release, "Canada Launches Scientific Survey Toward Submission for Extended Arctic Continental Shelf" (24 July 2015), online: <canada.ca/en/news/archive/2015/07/canada-launches-scientific-survey-toward-submission-extended-arctic-continental-shelf.html>.

[18] Global Affairs Canada, News Release, "Canada Launches 2016 Arctic Survey in Support of Continental Shelf Submission" (21 July 2016), online: <canada.ca/en/global-affairs> ["Arctic Survey"].

[19] Fisheries and Oceans Canada, "Canada's Participation in the Atlantic Ocean Research Alliance" (8 October 2019), online: <dfo-mpo.gc.ca/science/collaboration/aora-eng.html>.

[20] United Nations Division for Ocean Affairs and the Law of the Seas, "Submissions, through the Secretary-General of the United Nations, to the Commission on the Limits of the Continental Shelf" (12 December 2019), online: <un.org/depts/los/clcs_new/commission_submissions.htm> ["Submissions"].

[21] "Arctic Survey," *supra* note 18.

[22] "Submissions," *supra* note 20.

[23] *LOSC*, *supra* note 1, art 82(1).

[24] *Ibid*, art 82(2).

[25] *Ibid*, art 82(3).

[26] *Ibid*, art 82(4).

In the negotiations at UNCLOS III, Canada's Secretary of State for External Affairs announced that Canada was "prepared to explore" the possibility of revenue sharing, but any agreement would be conditional upon establishing that the revenue-sharing "would in no way derogate from our established sovereign rights" and that any "financial contributions would go primarily to the developing countries, particularly the least-developed among them."[27] The popular view is that Article 82 was accepted by beneficiaries of the broad Article 76 definition as a quid pro quo for granting them sovereign rights over the continental shelf beyond 200 nautical miles. This rationale for adopting Article 82 will become important when discussing who should bear the burden of the international royalty obligation the article imposes.

III. RECENT DISPUTES ON CANADA'S CONTINENTAL SHELF

Canada's Article 82 obligation is predicted to be initially realized within the next decade. With Equinor soon to start exploitation in the Flemish Cap area approximately 300 nautical miles off the coast of Newfoundland, Canada must work in conjunction with Newfoundland and Labrador to establish a sustainable system for meeting its Article 82 obligation. Clear and sound policies are especially imperative given two recent complaints oil- and gas-producing proponents operating *within* the 200 nautical mile limit mounted against Newfoundland and Labrador. Both disputes arose in relation to individually negotiated royalty agreements between the project proponent and the province of Newfoundland and Labrador.[28]

The first of these disputes, *Newfoundland and Labrador v. ExxonMobil Canada Properties*, arose in relation to the province's treatment of operating insurance costs that the oil companies extracting under the Hibernia licence incurred and deducted from the revenue. These deductions reduced the net revenue on which royalty payments to the province would be calculated.[29] The companies operating under the Hibernia licence include ExxonMobil, Chevron, Suncor, Murphy Oil, Equinor, and Canada Hibernia Holding Corporation.[30] The province took the position that the operating insurance costs did not qualify as Resource Project Eligible Costs (RPECs) that could be deducted for the calculation of the royalty payable to the province in accordance with clause 29.7 of the royalty agreement.[31] An arbitral tribunal determined that the insurance premiums did qualify.[32] The province appealed, claiming that: "(1) 'the award has been improperly procured' in accordance with section 14 of the *Arbitration Act*; and (2) 'the award deals with a dispute not contemplated by or falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration.'"[33] The province and the oil companies operating under the Hibernia licence are parties to the Hibernia Project Royalty Agreement (HRA), a

[27] Rowland J Harrison, "Article 82 of UNCLOS: The Day of Reckoning Approaches" (2017) 10:6 J World Energy L & Bus 488 at 494.

[28] See Rob Antle, "Terra Nova Project Partners Sue over Royalty Calculations," *CBC News* (17 February 2016), online: <cbc.ca/news/canada/newfoundland-labrador/terra-nova-royalty-calculations-supreme-court-1.3450450> [Antle, "Project Partners Sue"]; *Newfoundland and Labrador v ExxonMobil Canada Properties*, 2017 NLTD(G) 147 at para 5 [*ExxonMobil*].

[29] *ExxonMobil*, *ibid*.

[30] Hibernia, "About Hibernia," online: <hibernia.ca/about.html>.

[31] *ExxonMobil*, *supra* note 28 at para 5.

[32] *Ibid* at para 1.

[33] *Ibid*.

private, commercial agreement specifying the terms of royalty calculations.[34] The HRA establishes a three-tier royalty scale on which royalty is paid by each project owner to the province. These include a tier one "Gross Royalty," a tier two "Net Royalty," and a tier three "supplementary royalty."[35]

This particular dispute arose out of the calculation of the net revenues on which the Net Royalty was to be paid.[36] Both the arbitral tribunal and the Newfoundland and Labrador Supreme Court (Trial Division) found, on the basis of principles of contract interpretation, that the insurance premiums qualified as RPECs that were properly deductible in calculating the net revenue.[37]

The second recent dispute involves the Terra Nova offshore oil project. The Terra Nova Project is subject to a three-tiered royalty regime consisting of a "Basic Royalty" and a two-tier "Net Royalty." The project owners, which include Suncor Energy, ExxonMobil, Equinor, Husky Energy, Murphy Oil, Mosbacher Operating, and Chevron Canada,[38] claimed that, when the royalty payments transition from one tier to the next, they are sometimes being forced to pay both Basic and Tier 1 Net Royalties. The project owners claim that the agreement stipulates that they pay "the greater of" the Basic and Net Royalty, but not both.[39] This is the second dispute launched by Terra Nova on exactly this issue.[40] The previous dispute was settled out of court in 2010, but the amendments to the royalty regulations following the settlement failed to completely correct the problem. This second dispute was settled in December 2017, with the province and Project Owners splitting Terra Nova's claim 50/50, resulting in the province paying out $19.3 million to the project owners.[41]

These disputes illustrate the immediate need for clear regulatory language in any future royalty agreements, including those that pertain to the international royalty obligations under Article 82. Newfoundland's economy is highly reliant on royalty payments from these offshore oil and gas companies. Future entanglements related to royalty payments will only become more complex with the additional international royalty obligation.

The disputes described above arose in relation to sophisticated commercial contracts with clearly defined terms. In comparison, Article 82 consists of only four relatively vague paragraphs. The signatories to the *LOSC* have expressed concern that Article 82 contains several ambiguities that might result in inconsistency from one coastal State to another, and more seriously, disputes between coastal States and the ISA regarding royalty calculation and collection. In order to mitigate the risk of future legal action related to royalty payments, both domestically and in the international context between Canada and the ISA, standardized definitions of key Article 82 terms must be established.

[34] *Ibid* at para 2.

[35] *Ibid* at para 11.

[36] *Ibid* at para 13.

[37] *Ibid* at paras 176–79.

[38] Suncor, "Terra Nova" (2020), online: <suncor.com/about-us/exploration-and-production/east-coast-canada/terra-nova>.

[39] Antle, "Project Partners Sue," *supra* note 28.

[40] *Ibid.*

[41] Rob Antle, "$38.7M in Disputed Royalties Split 50-50 in Terra Nova Settlement," *CBC News* (12 February 2018), online: <cbc.ca/news/canada/newfoundland-labrador/nl-government-terra-nova-dispute-settlement-details-1.4531365>.

IV. AMBIGUITY IN ARTICLE 82

The International Seabed Authority responded to the above concerns by releasing several technical studies in relation to Article 82,[42] the most recent of which is ISA *Technical Study No. 15*. This study attempts to promote uniformity by clarifying any textual ambiguities within the Article and establish uniformity in state practice to avoid unnecessary conflict.[43] An earlier study, ISA *Technical Study No. 12*, identifies ambiguous key terms, acknowledges issues that might arise in respect of such ambiguity, and seeks to come to a singular definition having considered those issues.[44]

Technical Study No. 12 resolves several of these ambiguities as a result of workshops with academic commentators and other participants held by the ISA in efforts to interpret these terms. The ambiguous terms include: "resource," "all production/volume," "value," "contributions in kind," "site," "payments," and "annually." In relation to "resource" the study identifies that issues might arise in relation to whether such resources are processed or raw and whether "derived commodities" qualify as resources.[45] It further recognizes that *when* royalty calculations occur depends on *how* "resource" is defined, and this could be the difference between calculating the royalty at extraction or upon sale.[46] In relation to "all production/volume," the study questions whether this means net or gross production and whether any volume deductions are permitted. It further raises the question of what "resources used in connection with exploitation" means, as such resources are not to be included in volume calculations. In relation to "value," the study questions how "all production" or "volume" is to be valued. It further raises the issue of the financial deductions that are allowable in relation to such valuations, including the expenses and accompanying risks of deep water drilling, the cost of transportation, and the cost of processing.[47] Several questions arise in relation to "contributions in kind," especially regarding how such contributions are to be collected and administered. Questions that are considered include the point at which legal title to the product passes from one party to another, who is liable should an accident occur or product is otherwise lost, and who bears the costs of transportation and storage.[48] The term "site" raises questions as to whether the royalty is payable based on production from discrete well sites, the licence area, or the project as a whole.[49] The study further adverts to the issues of transboundary resources and unitization. In relation to payments themselves, questions arise as to the preferable currency and how currency

[42] See International Seabed Authority, *Issues Associated with the Implementation of Article 82 of the United Nations Convention on the Law of the Sea, ISA Technical Study No. 4* (Kingston, Jamaica: ISA, 2009); International Seabed Authority, *Non-living Resources of the Continental Shelf Beyond 200 Nautical Miles: Speculations on the Implementation of Article 82 of the United Nations Convention on the Law of the Sea, ISA Technical Study No. 5* (Kingston, Jamaica: ISA, 2010); and International Seabed Authority, *Implementation of Article 82 of the United Nations Convention on the Law of the Sea, ISA Technical Study No. 12* (Kingston, Jamaica: ISA, 2013) [*Technical Study No. 12*].

[43] Wylie Spicer & Elizabeth McIssac, International Seabed Authority, *A Study of Key Terms in Article 82 of the United Nations Convention on the Law of the Sea, ISA Technical Study No. 15* (Kingston: ISA, 2016) at 6 [*Technical Study No. 15*].

[44] "Annex 1: Report of Working Group A on Implementation Guidelines and Model Article 82 Agreement" in *Technical Study No. 12*, *supra* note 42 at 19.

[45] *Ibid* at 20.

[46] *Ibid* at 21.

[47] *Ibid* at 20.

[48] *Ibid*.

[49] *Ibid* at 21.

conversions ought to be performed. Finally, "annually" raises questions of the periodicity of such payments.[50]

Technical Study No. 15 further consolidates a uniform glossary of terms and their definitions by drawing from the domestic legislation of several countries, including the United States, Brazil, Canada (both Alberta and Newfoundland and Labrador), Australia, Nigeria, the Russian Federation, the United Kingdom, and Norway. It concludes that "resource" generally refers to the raw resource rather than any derived commodity. However, it notes specific exceptions where hydrocarbons are subject to minimal initial treatment, such as oil that has been "dewatered, desalted, and stabilized."[51] It also concludes that initial treatment does *not* include refining or deballasting.[52]

In most domestic legislation, production volume is subject to various allowable deductions, including reasonable losses, unavoidable losses, or losses up to a prescribed limit. Most jurisdictions further allow deductions for flared or reinjected gas. Hydrocarbons used for production purposes are, in most jurisdictions, allowable deductions. Such production purposes include drilling for resources, gathering resources on a lease, pumping resources onshore, subjecting the resource to initial treatment, or the operation of gas processing plants. Newfoundland and Labrador has statutory provisions that require royalty payments on flow testing. On this issue, there is significant cross-jurisdictional variation. The study provides that all value/production means the following:

1. Gross, not net, of commercial production.

2. Determined at the wellhead.

3. Commercial production *excludes* test production, contrary to both Brazil and Newfoundland and Labrador's legislation.

4. Reinjected and flared gas is similarly excluded from gross production.

5. There is *no* deduction of financial resources, contrary to the provisions in most jurisdictions.[53]

With regards to valuation, there is considerable variation across jurisdictions as well. As such, the technical study clarifies that the following conditions apply regardless of jurisdiction:

1. Value is directly linked to "all production."

2. It is based on gross production and the fair market value of the resource at the wellhead.

[50] *Ibid* at 22.
[51] *Technical Study No. 15*, *supra* note 43 at 13.
[52] *Ibid*.
[53] *Ibid* at 84.

3. There are no allowable deductions of any costs before value/volume is calculated.

4. Value and volume calculations should produce the same result.

5. The method of calculating value should be disclosed.[54]

The study notes that most jurisdictions' legislation does not provide specific guidance on contributions in kind.[55] An exception to this general trend is the legislation of Newfoundland and Labrador, which provides detailed guidance as to the chain of legal status of such contributions, who pays for what services and in what circumstances, as well as allocates the risk of transport with the interest holder until the oil is delivered in the manner requested by the government.[56] More clarification will need to take place in relation to contributions in kind, as this study does not adequately settle the issues that might arise.

The study notes that the surveyed jurisdictions lacked consistency in relation to the terms "site," "payment," and "annually." As such, it leaves the definition of "site" to the coastal State and indicates that "payment" should be made in a convertible currency, preferably at regular intervals. There was no consensus in relation to the term annually, but, based on the intervals defined in domestic legislation, the study suggests that a defined schedule of transfers throughout the year might be most desirable.[57]

The study does clarify several of these terms; however, it seems that "resource" may require further clarification, with clear delineation of which exceptions are acceptable and which are not, relying on established industry standards. Basing production volume on gross rather than net production reduces the risk for several interpretive debates that might arise in relation to allowable deductions. The recent outcome in the *ExxonMobil* case discussed above is exemplary of the fact that even in detailed commercial contracts between sophisticated entities, disputes in relation to allowable deductions are anticipated to arise.[58] By basing production volume on gross rather than net production, such complexities and opportunities for disagreement are substantially avoided.

However, while resolving textual ambiguity is one significant step towards effective implementation of Article 82, the actual administrative mechanisms of collection, compliance, and enforcement are the responsibility of the coastal State. Given the current cooperative federalist regime between Newfoundland and Labrador and Canada in relation to Newfoundland and Labrador's offshore oil and gas resources, Canada's method of implementation is somewhat complicated and its concrete form ought to be discussed now, before Article 82 obligations commence.

[54] *Ibid.*

[55] *Ibid* at 14.

[56] *Ibid.*

[57] *Ibid* at 11.

[58] See generally *ExxonMobil*, *supra* note 28.

V. THE HISTORY OF THE NEWFOUNDLAND OFFSHORE

In order to determine the optimal administrative mechanism for fulfilling Canada's Article 82 obligation, establishing a basic understanding of the current legislative regime governing the Newfoundland offshore is a necessary starting point. An overview of the history of that legislative regime will also inform an assessment of who should ultimately bear the burden of the international royalty.

That history begins with extensive negotiations between the governments of Canada and Newfoundland and Labrador regarding jurisdiction over continental shelf resources. Brian Peckford, Newfoundland's Minister of Mines and Energy from 1976–1979 and then Premier from 1979–1989, worked to establish Newfoundland's right to offshore oil and gas revenues. His efforts were initially thwarted by the Supreme Court of Canada's 1984 opinion in the *Reference re Newfoundland Continental Shelf*, more commonly referred to as the *Hibernia Reference*.[59] The issues to be decided were whether Canada or Newfoundland: (1) had the right to explore or exploit the mineral and other natural resources, and (2) had the legislative jurisdiction to make laws in relation to the exploration and exploitation of the mineral and other natural resources.[60] The Supreme Court described that, in order for Newfoundland to succeed in establishing that it, rather than Canada, held sovereign rights over the continental shelf off its coast, it would have to succeed on each of the following points: (1) international law must have recognized the right to explore and exploit in the continental shelf prior to Newfoundland's entry into Confederation on 31 March 1949; (2) the Crown in right of Newfoundland must have been in a position to acquire these rights; and (3) the Crown in right of Newfoundland must not have lost those rights under the Terms of Union with Canada. On these issues, the Supreme Court concluded the following:

> (1) Continental shelf rights are, in pith and substance, an extraterritorial manifestation of external sovereignty.
>
> (2) Canada has the right to explore and exploit in the shelf off Newfoundland because:
>
> (a) any continental shelf rights available in international law in 1949 would have been acquired by the Crown in right of the United Kingdom, not the Crown in right of Newfoundland;
>
> (b) even if Newfoundland could have held continental shelf rights prior to Union, they would have passed to Canada by virtue of the Terms of Union.
>
> (c) in any event, international law did *not* recognize continental shelf rights by 1949; such rights were not indisputably recognized before the Geneva Convention of 1958.
>
> (3) Canada has legislative jurisdiction in relation to the right to explore and exploit in the continental shelf off Newfoundland by virtue of the peace, order, and good government power in its residual capacity.[61]

While Canada would maintain jurisdiction over continental shelf resources, this did not preclude Newfoundland from negotiating an agreement in which it received some of the monetary benefits of such resources. Soon after the *Hibernia Reference* was released, Progressive Conservative leader, Brian Mulroney, made a written promise that, if elected,

[59] [1984] 1 SCR 86 [*Hibernia Reference*].
[60] *Ibid* at 86–87.
[61] *Ibid* at 128–29 [emphasis added].

"he would give the province equal say over offshore management and make it the 'principal beneficiary' of the oil and gas industry."[62] In February 1985, shortly after Prime Minister Mulroney entered office, Canada and Newfoundland and Labrador signed the *Atlantic Accord*.[63] The *Atlantic Accord* is a political agreement that lays the groundwork for a legislative regime. The federally enacted *Canada-Newfoundland and Labrador Accord Implementation Act*[64] and provincially enacted mirror legislation entitled the *Canada-Newfoundland and Labrador Atlantic Accord Implementation Newfoundland and Labrador Act*[65] were soon to follow.[66] Because of the finding in the *Hibernia Reference* that Newfoundland and Labrador had no legislative jurisdiction over the offshore, this federal-provincial mirror legislation was necessary.[67] The provisions of the *Implementation Act* are often interpreted in conjunction with provisions of the *Atlantic Accord*, which provides, in section 2, its primary purposes as follows:

> (a) to provide for the development of oil and gas resources offshore Newfoundland for the benefit of Canada as a whole and Newfoundland and Labrador in particular;
>
> …
>
> (c) to recognize the right of Newfoundland and Labrador to be the principal beneficiary of the oil and gas resources off its shores, consistent with the requirement for a strong and united Canada;
>
> …
>
> (e) to provide that the Government of Newfoundland and Labrador can establish and collect resource revenues as if these resources were on land, within the Province.[68]

In establishing the proper stakeholder on which to settle the burden of the international royalty payments, the political history and these purposes so central to the cooperative federalist arrangement between Canada and Newfoundland and Labrador must be given adequate consideration.

VI. THE CURRENT ROYALTY COLLECTION MECHANISM ON NEWFOUNDLAND'S OFFSHORE

There are currently four production facilities in the Newfoundland Offshore: Hebron, Hibernia, Terra Nova, and White Rose. Discovered in 1980, the Hebron Field is operated by ExxonMobil Canada Properties and is estimated to produce more than 700 million barrels of recoverable resources throughout its production span.[69] The Hibernia Field was discovered

[62] Jenny Higgins, "The 1985 Canada-Newfoundland Atlantic Accord" (2012), online: *Newfoundland and Labrador Heritage Website* <heritage.nf.ca/articles/politics/atlantic-accord.php>.

[63] *Supra* note 2.

[64] SC 1987, c 3 [*Implementation Act*].

[65] RSNL 1990, c C-2.

[66] Matthew Clarke, "Primary Beneficiaries: Newfoundland and Nova Scotia's Struggle to Achieve the Promise of Petroleum Wealth" (2004) 13 Dal J Leg Stud 1 at 4.

[67] *Ibid*.

[68] *Supra* note 2.

[69] Hebron, "The Project" (2015), online: <hebronproject.com/project/index.aspx>.

in 1979 and consists of two principal reservoirs in the Jeanne d'Arc Basin.[70] It is estimated to produce 1.2 billion barrels, and as of 2009, 667 million barrels had been extracted.[71] Its ownership is as follows: ExxonMobil Canada (33.125 percent), Chevron Canada Resources (26.875 percent), Suncor (20 percent), Canada Hibernia Holding Corporation (8.5 percent), Murphy Oil (6.5 percent), and Equinor Canada Ltd. (5 percent).[72] Canada Hibernia Holding Corporation's 8.5 percent shareholding of the Hibernia project becomes important in the *Hibernia Dividend Backed Annuity Agreement*, a revenue-sharing agreement between Canada and Newfoundland and Labrador. This is discussed in more detail in the Equalization Payments section below (Part VII). The Terra Nova Project was discovered in 1984 and is operated by Suncor Energy. It is estimated to contain 400 million barrels of recoverable resources.[73] Finally, the White Rose Project is operated by Husky Energy, with Petro-Canada holding 26.125 percent and the Government of Newfoundland and Labrador holding an equity stake of 5 percent.[74] The White Rose oilfield is estimated to contain 230 million barrels of oil, which is expected to be extracted within 12–15 years of achieving first oil, which occurred in 2005.[75]

Development of the offshore petroleum industry off the coast of Newfoundland shows no sign of slowing. On 6 November 2019, the C-NLOPB announced the results of the Call for Bids NL19-CFB01 for the South Eastern Newfoundland Region, which consisted of nine parcels totalling 2,270,472 hectares either fully or partially beyond the 200 nautical mile limit.[76]

Equinor has made several discoveries in the Flemish Pass Basin off the coast of Newfoundland outside the 200 nautical mile limit of the continental shelf. The first of these was Mizzen in 2009, followed by Harpoon and Bay du Nord in 2013. Bay du Nord is expected to hold over 300 million barrels of crude oil. Finally, in 2016, two additional discoveries were made requiring further appraisal: Bay de Verde and Baccalieu.[77] In a presentation in February 2017, Equinor indicated that planned start-up for drilling in the Bay du Nord oil field in the Flemish Cap was scheduled for 2022.[78]

Article 82 of UNCLOS requires that royalties be paid starting in the 6th year of production. This means that, based on Equinor's forecast start-up in 2022, the international royalty obligation will initiate by approximately 2028. While this is still nearly a decade away, because of the costs related to developing such projects, should the burden fall upon project proponents, they ought to be alerted sooner rather than later in order to accommodate the royalties in their development strategy. Further, if the burden is to fall to Canada or the

[70] C-NLOPB, "Producing Projects," online: <cnlopb.ca/offshore/>.

[71] "Hibernia Oil and Gas Field Project" (2020), online: <offshore-technology.com/projects/hibernia/>.

[72] Hibernia, *supra* note 30.

[73] Newfoundland and Labrador Canada, "Terra Nova Offshore Petroleum Field," online: <gov.nl.ca/nr/energy/petroleum/offshore/projects/terranova/>.

[74] "White Rose Oil and Gas Field" (2020), online: <offshore-technology.com/projects/white_rose/>.

[75] *Ibid.*

[76] C-NLOPB, News Release, "C-NLOPB Releases Results for 2019 Calls for Bids" (6 November 2019), online: <cnlopb.ca/news/nr20191106>. See also "Call for Bids No. NL19-CFB01 South Eastern Newfoundland Region" (8 February 2019), online: <cnlopb.ca/wp-content/uploads/landissuance/nl1901map.pdf>.

[77] Equinor, "Canada" (2018), online: <equinor.com/en/where-we-are/canada.html>.

[78] Garrett Barry, "Statoil Sees Bay du Nord Development in its Future," *CBC News* (8 February 2017), online: <cbc.ca/news/canada/newfoundland-labrador/statoil-bay-du-nord-exploratory-drilling-future-1.3971039>.

province or be divided between them, negotiation between the two governments will be necessary and additional legislation and regulations or amendments to current legislation and regulations may be required. Given Newfoundland and Labrador's reliance on offshore oil royalties, any negotiations will be politically sensitive and will likely require a great deal of time and resources.

As noted above, the Government of Newfoundland and Labrador relies heavily upon royalties collected from these projects. In the province's 2016–2017 annual report on the economy, it was noted that the oil and gas industry is the largest contributor to GDP and, in 2015, accounted for 16.7 percent of the province's nominal GDP. In 2016, the industry provided 3.0 percent of the province's total employment.[79] The success of the industry has immediate and direct effects on the vitality of the province's economy. The province's Department of Finance annual report from 2017 notes, "[o]ne of the biggest challenges is the fluctuation in oil royalties, which is impacted by commodity prices; the exchange rate; production/sales volumes; and capital and operating costs."[80] This impact is so significant that, in order to stabilize future revenues despite fluctuating oil prices, the province made a commitment in the 2016 Budget to establish a Diversified Wealth Fund.

In order to best assess the most effective means of collecting the international royalty, it is necessary to lay out the statutory instruments, the administrative mechanisms currently in place pursuant to such statutory instruments, and how those mechanisms function in relation to the royalties Newfoundland levies from the private proponents currently producing on the continental shelf off its coast. The statutory instruments and their pursuant regulations include:

(a) The *Atlantic Accord*

(b) The *Canada-Newfoundland and Labrador Accord Implementation Act*

  i. The *Newfoundland Offshore Petroleum Resource Revenue Fund Regulations*[81]

(c) The *Canada-Newfoundland and Labrador Atlantic Accord Implementation Newfoundland and Labrador Act*

(d) The *Petroleum and Natural Gas Act*[82]

  i. The *Offshore Oil Royalty Regulations*[83]

[79] Government of Newfoundland and Labrador, *The Economy 2017* (St John's, NL: Department of Finance, 2017) at 22, online: <gov.nl.ca/fin/files/e2017-theeconomy2017.pdf>.

[80] Newfoundland and Labrador, Department of Finance, *Annual Report 2016-17* by the Honourable Tom Osborne at 10, online: <gov.nl.ca/fin/files/publications-pdf-finannualreport2016-17.pdf>.

[81] Canada SOR/95-257 [*Resource Revenue Fund Regulations*].

[82] RSNL 1990, c P-10.

[83] NLR Reg 37/17.

As mentioned above, the *Atlantic Accord* was the founding document establishing an agreement between Canada and Newfoundland and Labrador that Newfoundland and Labrador was to be the primary beneficiary of the petroleum resources produced off its coast. Clause 36 of the *Atlantic Accord* stipulates:

> The principles of revenue sharing between Canada and Newfoundland with respect to revenues from petroleum-related activities in the offshore area shall be the same as those which exist between the Government of Canada and other hydrocarbon producing provinces with respect to revenues from petroleum-related activities on land. The federal legislation implementing the Accord, therefore, will permit the Government of Newfoundland and Labrador to establish and collect resource revenues and provincial taxes of general application as if these petroleum-related activities were on land within the province, through incorporation by reference of Newfoundland laws (as amended from time to time), or through appropriate legislative mechanisms.[84]

The *Atlantic Accord* outlines a jointly managed regulatory body called the Canada-Newfoundland and Labrador Offshore Petroleum Board. The *Atlantic Accord* directs that the Board will consist of seven members: three of whom are to be appointed by the Government of Canada, three of whom are to be appointed by the Government of Newfoundland and Labrador, and a Chairman who is to be jointly appointed by both governments. Clauses 22–24 of the of the *Atlantic Accord* assign decision-making duties to the Federal Government, Provincial Government, and Board respectively. Clause 22 provides that Parliament, the Government of Canada, or Federal Ministers alone are to make decisions under legislation of general application not specifically related to oil and gas exploration and production as well as decisions related to the application of federal taxes. Most importantly for the purposes of this article, Clause 23 provides that the royalty regime, "other provincial-type revenues," and "decisions related to provincial laws of general application having effect in the offshore" are to be made by the Newfoundland Legislature, the Newfoundland Government, or the Provincial Ministers alone. This clause essentially grants jurisdiction over the negotiation and administration of royalty agreements to the provincial government. Clause 24 provides that all other decisions related to regulating and managing the offshore area fall to the Board. Clause 25 enumerates several fundamental decisions of which the Board must notify both governments before finalizing. Clause 37 enumerates the revenues that will flow to Newfoundland. These include:

> (a) royalties;
>
> (b) a corporate income tax which is the same as the generally prevailing provincial corporate income tax in the province;
>
> (c) a sales tax that is the same as the generally prevailing provincial sales tax in the province;
>
> (d) any bonus payments;
>
> (e) rentals and licence fees; and

[84] *Supra* note 2.

(f) other forms of resource revenue and provincial taxes of general application, consistent with the spirit of this Accord, as may be established from time to time.

Clause 38 indicates that the Board is responsible for collecting royalties, bonus payments, rentals and licence fees, which it is to remit to the Government of Newfoundland and Labrador along with any other revenues enumerated in Clause 37. It seems that despite the fact that Clause 38 indicates that the Board shall collect royalties, this duty, as indicated by Clause 23, is in fact administered by the province. The private agreement between the province and the Hibernia Project contains several provisions that indicate that payments are to be made directly to the province in accordance with the terms stipulated in the agreement.[85]

The *Implementation Act*[86] officially establishes the Canada-Newfoundland and Labrador Offshore Petroleum Board and describes its administration and jurisdiction. Section 214(1) of the *Implementation Act* provides that an account known as the Newfoundland Offshore Petroleum Resources Revenue Fund is to be established in the accounts of Canada. The *Newfoundland Offshore Petroleum Resource Revenue Fund Regulations*[87] provide further details, indicating that the Federal Minister shall credit the Revenue Fund with an amount equal to the aggregate of any amounts referred to in sections 214(2)(a)(ii) and 214(2)(a)(iv) of the *Implementation Act*. Section 214(2)(a)(ii) refers to "an amount equal to the aggregate of the amounts assessed or reassessed in respect of any fiscal year on account of taxes imposed pursuant to section 211, after taking into account any credits, reductions, deductions, rebates, surtaxes and remissions that are applicable in respect of such taxes." Section 211 refers to "the taxes, interest and penalties that would be imposed, levied and collected under the Newfoundland and Labrador Income Tax Act in respect of that taxable income if the offshore area were in the Province." These provincial taxes, pursuant to section 212 are to be remitted to the Receiver General of Canada, and then it appears that section 214(2)(a)(ii) essentially ensures that the equivalent of such funds are returned to the province through the Revenue Fund. Section 214(2)(a)(iv) refers to "an amount equal to the aggregate of any amounts … received and not required to be returned during any fiscal year under Part II or any regulations made thereunder." The amounts that might be received under Part II include royalties, excluding those royalties paid to the province according to the *Offshore Oil Royalty Regulations* made pursuant to the *Petroleum and Natural Gas Act*, as well as interests and penalties "that would be payable in respect of petroleum under the Petroleum and Natural Gas Act if the petroleum were produced from areas within the Province."[88] This arrangement seems to essentially ensure that the equivalent of any payments made to Canada in respect of Newfoundland's offshore oil, aside from federal corporate income tax, should be returned to the province through this Revenue Fund.

The *Petroleum and Natural Gas Act*[89] applies to petroleum production both within the province and in the offshore. Section 30(1)(c) indicates that the term "lease" includes offshore licences. Section 30(2)(a) defines the "Crown" as "Her Majesty in Right of the

[85] Hibernia Development Project, EL1093/PL1005 Royalty Agreement (16 February 2010), art XXIV: Calculation and Payment.

[86] *Supra* note 64.

[87] *Supra* note 81.

[88] *Implementation Act*, *supra* note 64, s 97(2).

[89] *Supra* note 82.

province." Section 32 provides that "[p]etroleum produced under a lease is subject to and an interest holder is liable for and shall pay royalty share to the Crown in an amount and in a manner prescribed by regulation." Pursuant to subsection (1) of section 33 of the *Petroleum and Natural Gas Act*, the province is authorized to enter into private contractual agreements with proponents regarding royalty payments that override the regulations. Section 39 authorizes the Lieutenant-Governor in Council to make royalty regulations, including establishing the applicable rates, allowable deductions, and the proper protocol for retention of documents. Sections 41(1) and 41(2) provide that reports and documentation must be submitted as required by the minister and regulation and, further, that such reports and documentation are subject to audits as established by the regulation.

Enacted pursuant to section 39 of the *Petroleum and Natural Gas Act* are the *Offshore Oil Royalty Regulations*, most recently amended in November 2017. The *Offshore Oil Royalty Regulations* provide in section 4(1) that "[a]n interest holder is liable to the Crown for royalty share calculated in accordance with these regulations." The "Crown" is defined in section 3(4)(a) of the *Offshore Oil Royalty Regulations* as "Her Majesty in Right of Newfoundland and Labrador."[90] Section 9 provides the Basic Royalty calculation, section 12 provides the net revenue calculation, and section 13 provides the net royalty calculation. Section 5(1) indicates that basic and net royalties are due on the "last day of the month following the month to which the royalty relates." The *Offshore Oil Royalty Regulations* include detailed reporting requirements in sections 31–39. Section 42(1) authorizes the minister to "at reasonable times enter upon the property and premises … of an interest holder [or] project operator … in order to inspect or audit records, inventories and assets or verify information that may affect the calculation of royalty share." Further, section 43 details the requirements for issuance of a warrant to enter premises or property of an interest holder when the minister suspects that such interest holder is withholding information or access in accordance with the *Petroleum and Natural Gas Act* and the *Offshore Oil Royalty Regulations*.

VII. EQUALIZATION PAYMENTS

Another major component of the arrangement between Canada and Newfoundland is the issue of equalization payments. The arrangement could have been made such that any dollar of royalty revenue that Newfoundland procured pursuant the *Atlantic Accord* and *Implementation Acts* resulted in a dollar reduction in the equalization transfer Canada was to pay to Newfoundland. Newfoundland recognized that such a dollar-for-dollar offset would place them in substantially the same financial position they had been before the *Atlantic Accord*. Although they might be less reliant on federal equalization payments, they would likely not benefit enough from the royalties to justify receiving no federal equalization payments whatsoever. The *Atlantic Accord* was drafted with this in mind. During the negotiation of the *Atlantic Accord*, the agreement established "equalization offset provisions" that ensured that Newfoundland and Labrador "would not experience dollar for dollar decreases in transfer payments as provincial revenues rose."[91] In 1993, the federal government revised its Equalization formula to ensure that "the equalization payment

[90] *Supra* note 83.

[91] Clarke, *supra* note 66 at 12.

flowing to … Newfoundland can be reduced by no more than seventy percent of the amount of their offshore oil and gas revenues."[92] The federal Equalization formula was later dramatically revised in 2007 and 2009.

The federal Equalization program is administered under the *Federal-Provincial Fiscal Arrangements Act*.[93] Its purpose is to address fiscal disparity among provinces by transferring federal funds to provinces with weaker economies. Entitlements under Canada's Equalization program are based upon a province's "fiscal capacity," or its ability to raise revenues. Equalization payments are calculated by determining the amount by which a province's fiscal capacity is below the average fiscal capacity of all provinces. Natural resource revenues like oil and gas royalties go into the formula to calculate Equalization payments, but only at a 50 percent rate to prevent disincentivizing development of natural resources.[94] There is also a "best of" feature whereby a province's fiscal capacity is calculated with 50 percent of resource revenues and a second time with 0 percent of resource revenues. The province is entitled to the higher of the two Equalization payments.[95] However, an additional feature of the formula involves a "'clawing-back' principle," or "fiscal capacity cap," which was introduced in 2007. Because provinces with resource revenues only include half of those revenues in any measure of their fiscal capacity, it is possible that a province could be entitled to an Equalization payment but, after receiving the payment, have a higher fiscal capacity than a province that is not entitled to an Equalization payment. The purpose of the fiscal capacity cap is to eliminate this possibility. Under the cap, the combination of a province's fiscal capacity, including revenues from all sources, and the equalization payment "cannot exceed the fiscal capacity of the poorest non-Equalization-receiving province."[96] To stabilize annual fluctuations, a province's Equalization payment in a given year is based on a "weighted three year moving average" starting with the year two years previous to the calculation of the payment.

On 14 February 2005, the Governments of Canada and Newfoundland and Labrador signed the *Arrangement between the Government of Canada and the Government of Newfoundland and Labrador on Offshore Revenues*.[97] The Arrangement requires the Government of Canada to "seek legislative authority from Parliament…to provide 100 per cent offset against reductions in Equalization payments resulting from offshore resource revenues."[98] It provides that, "[c]ommencing in 2006–2007, and continuing through 2011–2012, the annual offset payments shall be equal to 100 per cent of any reductions of Equalization payments resulting from offshore resource revenues."[99] However, it indicates that a successor arrangement will only be put in place for the period of 2012 to 2020 *if* the province qualifies for an Equalization payment in 2010–2011 or 2011–2012.[100] The province

[92] *Ibid* at 13.

[93] RSC 1985, c F-8.

[94] Trevor Tombe, "Unpacking Canada's Equalization Payments for 2018-19" (17 January 2018), online (blog): *University of Calgary School of Public Policy* <policyschool.ca/unpacking-canadas-equalization-payments-2018-19/>.

[95] *Ibid.*

[96] Parliamentary Information and Research Service, *Canada's Equalization Formula*, by Édison Roy-César (Ottawa: Library of Parliament, 2013), online: <lop.parl.ca/Content/LOP/ResearchPublications/2008-20-e.htm#a8>.

[97] (14 February 2005) at para 1, online: <www.fin.gc.ca/fedprov/nl-tnl2005-eng.asp> [Arrangement].

[98] *Ibid.*

[99] *Ibid.*

[100] *Ibid.*

did not qualify in 2010–2011 or 2011–2012.[101] As a result, it received no annual offset payments from the federal government in the period between 2012 and 2019.

The Arrangement specified that the parties would review it no later than 31 March 2019. It detailed that this review should assess Newfoundland and Labrador's fiscal position in relation to its offshore petroleum resource revenues and the effects of the *Atlantic Accord*.[102] As stipulated, a new agreement entitled the *Hibernia Dividend Backed Annuity Agreement* (Dividend Agreement) was executed on 1 April 2019.[103] The Dividend Agreement introduces sweeping changes to the previous Arrangement. Pursuant to the Dividend Agreement, Canada will pay Newfoundland a total of about $3.3 billion over the course of the next 38 years, beginning this year. In consideration for these payments from Canada, Newfoundland has promised to pay $100 million to Canada for eight years starting in 2045. The foundation of this Dividend Agreement is a federal Crown corporation with an 8.5 percent interest in the Hibernia project — Canada Hibernia Holding Corporation (CHHC). CHHC, because of its 8.5 percent interest in the Hibernia project, will be the primary source of funds to be transferred to Newfoundland. Each year, Canada will transfer to Newfoundland what it calls a "Hibernia Dividend" in the requisite amount.[104] However, the amount Canada is to pay Newfoundland each year is *not* dependent on the profits experienced by CHHC. As a result, if CHHC's profits are less than the amount Canada is required to pay to Newfoundland, the federal government must make up the difference. Where the profits exceed the amount to be paid to Newfoundland, the federal government retains the difference.[105]

One primary purpose of making these consistent payments to Newfoundland — payments that do not rely on CHHC's profitability — is to provide Newfoundland with a secure, long-term, and predictable revenue stream.[106] This underlying purpose will play an important role in determining where the burden of the Article 82 payments should fall.

VIII. COMPARING THE ADVANTAGES AND DISADVANTAGES OF PLACING THE ARTICLE 82 OBLIGATION ON PROJECT PROPONENTS, CANADA, OR NEWFOUNDLAND

The general content of the Article 82 obligation is not at issue; however, to whom it applies is. Who is to pay this incrementally increasing international royalty and what justifies their fulfilling the obligation over any other potential stakeholder? The relative equity, neutrality, and administrability of the provision changes based on who pays. The equity of any arrangement must be considered in the context of Newfoundland and Labrador's arrangement with Canada as established by the *Atlantic Accord* and supporting legislation.

[101] Department of Finance Canada, "Federal Support to Provinces and Territories" (2 February 2017), online: <canada.ca/en/department-finance/programs/federal-transfers/major-federal-transfers.html>.

[102] Arrangement, *supra* note 97.

[103] Intergovernmental Affairs, News Release, "New Agreement to Secure Newfoundland and Labrador's Share of Offshore Revenues" (1 April 2019), online: <canada.ca/en/intergovernmental-affairs/news/2019/04/new-agreement-reached-to-secure-newfoundland-and-labradors-share-of-offshore-revenues.html>.

[104] *Ibid*.

[105] Simon C Baines & Aqeel Virk, "A New Day for the Atlantic Accord" (5 April 2019), online: <osler.com/en/resources/regulations/2019/a-new-day-for-the-atlantic-accord>.

[106] Intergovernmental Affairs, "Hibernia Dividend Backed Annuity Agreement" (1 April 2019), online: <canada.ca/en/intergovernmental-affairs/news/2019/04/hibernia-dividend-backed-annuity-agreement.html>.

Neutrality refers to the goal that the arrangement minimally interfere with project proponents' economic decision-making. The arrangement should not act to deter project proponents from developing the ECS off the coast of Newfoundland. Finally, administrability refers to the practical administrative aspects of the arrangement — it should be easy to comply with, difficult to evade, and easy to enforce.[107] Administrability thus requires that the terms of Article 82 be sufficiently well-defined for the project proponents to know their scope. It also requires that enforcement does not call for inordinate investigative resources. These and some other collateral considerations must be put in balance to reach a reasoned determination of who ought to pay.

A. PROJECT PROPONENT PAYS

The Board seems to contemplate the idea that the private proponent may be at least partially responsible for the Article 82 obligation in future projects on the extended continental shelf. In the most recent calls for bids released by the Board on 3 April 2019, section 3.1 states:

> The Board informs prospective bidders that, for any parcel entirely or partially beyond Canada's 200 nautical mile zone, it has been advised by the Government of Canada that, in order to meet obligations arising pursuant to article 82 of the *United Nations Convention on the Law of the Sea*, additional terms and conditions may be applied through legislation, regulations, amendments to licences or otherwise.[108]

A few issues arise in relation to the notion of neutrality should the international royalty obligation be imposed on project proponents. The first is that the added royalty, if imposed on project proponents, may deter investment on the extended continental shelf. The extent to which this might occur would require an economic analysis that is beyond the scope of this article. However, more qualitatively, it is helpful to compare the international royalty obligation to Newfoundland's generic royalty regime to determine whether the financial burden of the international royalty on project proponents would be significant. Newfoundland and Labrador's Generic Offshore Oil Royalty Regime is two-tiered. The first tier is the Basic Royalty, which is calculated by multiplying the Basic Royalty Rate (BRR) by the remainder of transportation costs subtracted from gross sales revenue (Basic Royalty = (gross sales revenue – transportation costs) x BRR). The BRR depends on the R factor, which is calculated by dividing the cumulative gross sales revenue and incidental revenue less cumulative transportation costs less cumulative basic and net royalty paid to the prior month by the sum of the cumulative pre-development, capital, and operating costs. The BRR ranges from 1 percent when the R factor is less than 0.25 to 7.5 percent when the R factor is greater than or equal to 1.25. The Basic Royalty is initiated at first production and increases with project cost recovery. Once the project cost has been recovered, the Net Royalty applies in lieu of the basic royalty. The Net Royalty is calculated as follows: (gross sales revenue + incidental revenue – transportation costs – project capital and operating costs) x Net Royalty Rate ("NRR"). The NRR ranges from 0 percent when R is less than 1 to 50 percent when R is greater than 3. Where R is greater than or equal to 1 and less than

[107] Anthony C Infanti, "Tax Equity" (2008) 55:4 Buff L Rev 1191 at 1192.

[108] C-NLOPB, "Call for Bids, No. NL19-CFB01 (South Eastern Newfoundland): Exploration Licences in the Canada-Newfoundland and Labrador Offshore Area" at 5, online: <cnlopb.ca/wp-content/uploads/landissuance/nl1901calldoc.pdf>.

or equal to 3, the NRR ranges from 10 percent to 50 percent, again depending on the R factor. The Basic Royalty acts as a credit against the Net Royalty.[109]

The international royalty is comparatively simple. As explained briefly above, essentially, after five years of production the international royalty is triggered, starting at 1 percent in year 6 and increasing in 1 percent increments to a maximum of 7 percent in year 12. The rate remains at 7 percent until the production site is decommissioned. As mentioned above, ISA *Technical Study No. 15* indicates that these calculations are made on the value of all production, meaning gross, not net, commercial production as determined at the wellhead. No deduction of financial resources such as operating costs, capital costs, or transportation costs is allowed. The major differences between the basic royalty and the international royalty are as follows:

1. Basic royalty begins at production while international royalty begins in year six.

2. Basic royalty rate is dependent on the R factor, while international royalty rate is dependent on the year of production.

3. Basic royalty is calculated on gross sales revenue after transportation costs are deducted while international royalty is calculated on gross value of all production based on the fair market value at the wellhead with no deductions allowed.

4. The basic royalty rate ranges from 1 to 7.5 percent while the international royalty ranges from 1 to 7 percent, which is actually quite similar.

These are relatively difficult to compare given the allowable deductions under Newfoundland's basic royalty, but overall the rates are not wildly different, and while they change based on different variables, the range is fairly narrow. Because of the allowable deduction of transportation costs and the fact that the R factor takes costs into account, it is likely that once the international royalty is triggered, it will exceed the Basic Royalty.

Unless the R factor is less than 1, the Net Royalty, once it is triggered, will always be 10 percent or more. As its title indicates, the Net Royalty is based on net sales revenues rather than gross production value. However, because the rate ranges from 10 percent to 50 percent depending on the R factor, it is difficult to say how the international royalty rate will compare at any given time. It is likely that it will generally be substantially lower than the Net Royalty simply because of the Net Royalty's higher starting rate and significantly higher rate cap.

As a somewhat cursory conclusion, it seems that the international royalty is insubstantial in comparison to the royalties Newfoundland will impose, even though it is based on the value of gross volume rather than gross sales revenue or net sales revenue. It is unlikely to be a substantial deterrent in itself given the more significant royalties the province already imposes. Additionally, the fact that these petroleum resources are very location-dependent renders it more unlikely that the international royalty obligation will deter project proponents.

[109] *Offshore Oil Royalty Regulations*, *supra* note 83, ss 9, 13.

It is not as if a project proponent can forum shop in the same way it might for a flag state. However, much is dependent upon the policies of other coastal States with extended continental shelves. Norway has already indicated that it plans to place the burden of the royalty payments on the project proponent.[110] However, its tax system works to completely reimburse the project proponents, passing the obligation on to Norwegian taxpayers.[111] Atlantic Canada would thus be comparatively less competitive. If it becomes common practice for all coastal States with an extended continental shelf to place the burden of international royalty payments on the project proponent, Atlantic Canada will remain competitive.

Another issue of neutrality that one might consider is that project proponents may choose to bid on parcels within the 200 nautical mile limit rather than those beyond it in order to avoid the royalty obligation. However, it seems that wherever this burden is placed, the responsible party may hold this same preference to develop within the 200 nautical mile limit. As a result, this particular neutrality argument does not weigh in favour or against placing the burden on project proponents.

Another possible neutrality issue is that a project proponent may wish to extract at a faster rate than it otherwise might in order to avoid paying the higher 7 percent rate for a long period of time. As mentioned above, the White Rose oilfield contains an estimated 230 million barrels of oil and has an expected production span of only 12 to 15 years. The Bay du Nord site contains around 300 million barrels of oil, and while production in deeper waters may proceed more slowly, with advancing technologies, there is certainly the possibility that it would not even reach the 12-year mark. However, the project proponent cannot simply choose to produce at a higher rate without any oversight. The Board regulates fundamental decisions such as the "pace of production" with the approval of both the provincial and federal governments.[112] Absent Board approval, a project proponent is not free to produce at a faster pace than stipulated in the production licence. As well, oil prices fluctuate based on supply and demand. Where faster production significantly increases supply, oil prices can potentially fall. However, the biggest influence on oil prices is the Organization of Petroleum Exporting Countries (OPEC),[113] and oil produced on the Atlantic offshore comprises only about 0.4 percent[114] of the world's oil production, so any increase in production rate is unlikely to have a real impact on oil prices. It is thus unlikely to act as a deterrent for project proponents to produce faster.

Given Canada's taxation of petroleum resources, in the end, project proponents resident in Canada would likely not pay the full amount of the royalty. Corporations in Canada are taxed at flat corporate rates. Newfoundland's provincial corporate tax rate is 15 percent and the federal corporate rate on active business income is 15 percent, resulting in a total

[110] Alister Doyle & Nerijus Adomaitis, "Exclusive: Norway Plans Tax Breaks for Remotest Arctic Oilfields – Letters," *Reuters* (5 September 2017), online: <reuters.com/article/us-energy-norway-exclusive/exclusive-norway-plans-tax-breaks-for-remotest-arctic-oilfields-letters-idUSKCN1BG2CE>.

[111] *Ibid.*

[112] *Atlantic Accord*, *supra* note 2, s 25.

[113] Nick Lioudis, "What Causes Oil Prices to Fluctuate?" (updated 3 October 2019), online (blog): <investopedia.com/ask/answers/012715/what-causes-oil-prices-fluctuate.asp>.

[114] Wade Locke, "Economics of Newfoundland and Labrador's Offshore Oil Industry: Separating Fact from Myth" (Lecture delivered at the NOIA Annual Conference, Memorial University of Newfoundland, 22 June 2006), online: <em.gov.bc.ca/DL/offshore/Reports/noia_presentation_2006_final.pdf>.

corporate tax of 30 percent. The *Income Tax Act*[115] allows a 100 percent deduction for provincial royalties and production taxes.[116] However, this deduction does *not* apply to non-resident corporations.

Pursuant to Article 5 of the tax treaty between Canada and Norway (Canada-Norway Tax Treaty), Equinor Canada Ltd. would be likely considered a Permanent Establishment in Canada. A Permanent Establishment is defined in Article 5, paragraphs 1 and 2 as follows:

> 1 For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.
>
> 2 The term "permanent establishment" includes especially:
> a) a place of management;
> b) a branch;
> c) an office;
> d) a factory;
> e) a workshop; and
> f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.[117]

Clause 48 of the *Atlantic Accord* requires that a corporation operating on the offshore establish headquarters in Newfoundland. Equinor Canada Ltd. operates as a subsidiary of Equinor and is registered in Newfoundland as an extra-provincial foreign corporation. Its office in Newfoundland is located in St. John's. Equinor Canada Ltd.'s operations clearly fall into paragraph (f): "a mine, an oil or gas well, a quarry or any other place of extraction of natural resources."

The Canada-Norway Tax Treaty stipulates in Article 11, paragraph 4 that royalties derived from a Permanent Establishment are to be treated as business income, which is addressed in Article 7. Article 7 provides that business income derived from a Permanent Establishment may be taxed in the Contracting State in which that Permanent Establishment is situated. In the case of Equinor Canada Ltd., the aforesaid Contracting State in which the Permanent Establishment is situated is Canada. Article 7, paragraph 1 indicates that only the profits attributable to the Permanent Establishment in Canada may be taxed by Canada.[118]

Because Equinor Canada Ltd. is a Permanent Establishment in Canada and not resident in Canada, it does not benefit from this deduction. As such, where the project proponent is a non-resident corporation, any potential reduction in the tax burden due to this deduction of provincial royalties is not settled on the rest of the taxpaying Canadian public. Although a non-resident project proponent such as Equinor Canada Ltd. does not benefit from the deduction of provincial royalties, that is not to say that an additional deduction might

[115] RSC 1985, c 1 (5th Supp).

[116] KPMG LLP, "Guide to Oil and Gas Taxation in Canada" (May 2018), online: <assets.kpmg/content/dam/kpmg/ca/pdf/2018/05/oil-gas-guide.pdf > at 9. See *Income Tax Act*, *ibid*, s 65(1)(a).

[117] *Convention Between the Government of Canada and the Government of the Kingdom of Norway 2002: For the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital* (12 July 2002), online: <canada.ca/en/department-finance/programs/tax-policy/tax-treaties/country/norway-convention-2002.html> [*Canada-Norway Tax Treaty*].

[118] *Ibid*, art 7(1).

someday be legislated that relates specifically to deducting the Article 82 royalty from a project proponent's income.

The question remains whether, normatively speaking, a project proponent *should* pay this international royalty rather than the province or Canadian taxpayers. What rationale exists other than the relatively unconvincing argument that they may have the deepest pockets? Unless the provincial royalties and corporate taxes exceed 50 percent of the corporation's profits, the project proponent is the primary beneficiary of the profits they make on petroleum products extracted from the continental shelf. However, the project proponent is investing the labour and resources required to produce the petroleum, so the fact that they are the primary beneficiaries should hardly be reason to impose the international royalty obligation upon them. The question comes down to what they might be paying elsewhere. Within 200 nautical miles, they would be paying only royalties to Newfoundland and Labrador. If they were outside of the 200 nautical mile limit off the coast of the United States, it seems likely they would be paying royalties to the United States but no international royalty — at least not yet. If they were operating in the international seabed area (the Area), royalties have yet to be established, but discussions project the royalty obligation will be 3–5 percent. Where private contractors have licences to mine in the Area, this royalty will be levied directly from them and not the States in which they are resident.[119] Without the quid pro quo between Articles 76 and 82 of the *LOSC*, the extended continental shelf beyond 200 nautical miles may well in fact have become part of the Area. As well, if all coastal States levy the international royalty from project proponents, this practice could eventually become customary international law and the United States, even if it never becomes a signatory of the *LOSC*, may be compelled to adopt a similar practice. In light of this, imposing the extended continental shelf royalty on private project proponents does not seem unreasonable.

Under the previous royalty regulations in Newfoundland and Labrador, the province negotiated separate royalty regimes with each project. These negotiations consumed considerable time and resources. Adding the international royalty obligation to the discussion would likely introduce additional time and expense in future negotiations. Recognizing that such negotiations are unsustainable and introduce substantial uncertainty for future developments, in 2015, the province released a generic royalty regime as described above. This generic royalty regime reduces the administrative resources required for extended royalty negotiations and provides fiscal certainty to project proponents — they will know the royalty rates even before they submit bids to the Board. However, contractual provisions can still replace the generic royalty regime and negotiations will still likely take place. As discussed above, the *Petroleum and Natural Gas Act* contains an override provision — section 33 authorizes the province to negotiate royalty agreements that prevail over the existing regulatory framework.[120] This new framework applies to the Bay du Nord project. In the summer of 2015, Premier Paul Davis said he was "weeks away" from signing a term sheet with Equinor, implying that the generic royalty is being somewhat altered.[121] Where

[119] International Seabed Authority, *Making the Most of Deep Seabed Resources* (Kingston, Jamaica: ISA, 2014) at 59, online: <ran-s3.s3.amazonaws.com/isa.org.jm/s3fs-public/documents/EN/Regs/FinTerms 2014.pdf>.

[120] *Supra* note 82.

[121] Terry Roberts, "Statoil Term Sheet on Bay du Nord 'Weeks Away,' Premier Says," *CBC News* (16 June 2015), online: <cbc.ca/news/canada/newfoundland-labrador/statoil-term-sheet-on-bay-du-nord-weeks-away-premier-says-1.3115241>.

the province seeks to vary the terms of this generic royalty regime, its bargaining position may be detrimentally affected by imposing the international royalty on the project proponent. Even if it is not directly part of the negotiation process, it may loom in the background to lower the proponent's bottom line. This means that in a certain respect, the province might itself be subsidizing Canada's international royalty obligation by virtue of its compromised bargaining position.

Imposing the royalty on project proponents introduces an extra administrative step in royalty collection. If project proponents are to pay, the most likely administrative mechanism to ensure timely collection and overall compliance already exists. As outlined in the *Offshore Oil Royalty Regulations*, project proponents are required to submit documentation to the province at regular intervals and are subject to audits by the Minister of Natural Resources. Despite these mechanisms outlined on paper, the province struggles to ensure compliance due to a lack of a sufficient labour force and financial resources. In 2014, Newfoundland and Labrador's Auditor General Terry Paddon noted that the Ministry of Natural Resources' royalties division need to improve auditing timelines to ensure potential audits are not missed altogether, resulting in lost revenues.[122] While an additional royalty payment from existing project proponents is unlikely to greatly increase the workload, the fact that the royalties division already struggles to keep up with its own royalty collection introduces the potential that, because of the division's insufficiencies, the international royalty obligation will circumstantially fall to the province. The resources required to ensure compliance should come from Canada rather than Newfoundland. As well, if payments are to be made directly from Canada to the ISA, Canada will have to ensure the province's collections are accurate. If anything, should the obligation fall to project proponents, provisions should be in place to ensure that Newfoundland is not ultimately held responsible for discrepancies that result from a project proponent's noncompliance.

Canada, not the project proponent, is the signatory of UNCLOS. Several academic commentators have characterized the Article 82 obligation as a quid pro quo for the expansive Article 76 definition[123] and a quid pro quo simply for the other benefits of being an UNCLOS signatory.[124] The expansive Article 76 definition directly benefits Newfoundland, and by extension, Canada. Newfoundland can thus collect royalties on petroleum produced in the area beyond 200 nautical miles, which it otherwise would not be able to do if the Article 76 definition included the continental shelf only up to 200 nautical miles. The definition does not in itself benefit the project proponents. Their operations would be substantially the same regardless of whether they were extracting on the inner continental shelf or the area as opposed to the extended continental shelf. This may be reason enough not to impose the royalty on project proponents. However, before one can decide whether this is the case, one must first analyze the remaining options — imposing the royalty on Newfoundland or resting it on Canada, and ultimately, the Canadian taxpayer.

[122] "N.L. Could Be Missing out on Royalties: Auditor General," *CBC News* (24 January 2014), online: <cbc.ca/news/canada/newfoundland-labrador/n-l-could-be-missing-out-on-oil-royalties-auditor-general-1.2508866>.

[123] Wylie Spicer, "Canada, the Law of the Sea Treaty and International Payments: Where Will the Money Come From?" (2015) 8:31 University of Calgary School of Public Policy: SPP Research Papers 1 at 9.

[124] Harrison, *supra* note 27 at 494.

B. NEWFOUNDLAND PAYS

As described above, Newfoundland's economy heavily relies upon revenues from oil royalties, so much so that forcing the international obligation on Newfoundland is not a viable option. Given the purposes enumerated in section 2 of the *Atlantic Accord*, this obligation should not fall to Newfoundland. Such an action would be antithetical to those stated purposes, which include "to recognize the right of Newfoundland and Labrador to be the principal beneficiary of the oil and gas resources off its shores, consistent with the requirement for a strong and united Canada." Should Newfoundland pay, whether it remains the "principal beneficiary" of those resources is debatable. There is a chance that in certain months, it would in fact pay more on the international royalty obligation than it receives from the project proponents operating on the extended continental shelf under its own royalty regime. Newfoundland would put in the administrative work — and accompanying expense — to collect the international royalty and ensure compliance but receive significantly less of the benefit than anticipated by negotiated royalty agreements already in place. As well, production from current projects within 200 nautical miles is likely to begin to wane, so extended continental projects will start becoming necessary to replace royalty revenues from decommissioned inner continental shelf projects. Subtracting a substantial portion of the royalty revenues solely from Newfoundland's overall revenues to fulfill an obligation Canada as a whole committed to is simply not justifiable given the premise of the *Atlantic Accord*.

Burdening Newfoundland with the international royalty does not comport with the new *Dividend Agreement* discussed above. If Newfoundland is forced to pay the international royalty, this will disrupt the underlying purpose of the federal government's consistent payments to Newfoundland. Whatever consistency the Hibernia Dividend might bring to Newfoundland's economy would be subject to the fluctuations of the international royalty.

Further, there is a risk that imposing this royalty would alter Newfoundland's priorities in the offshore. If Newfoundland is to pay the international royalty, it will prefer restricting development to the area within 200 nautical miles. However, as mentioned above, the Board has jurisdiction over resource management, which includes regulating calls for bids and issuing exploration licences, significant discovery licences, and production licences. The Board is jointly controlled by the Governments of Canada and Newfoundland. Unless the Chair and CEO, who is jointly appointed by the two governments, consistently decides in favour of Newfoundland's interests, there is no guarantee that, even though Newfoundland will suffer the financial consequences of the international royalty, Newfoundland will have the capacity to prioritize calls for bids and issuance of licences within the 200 nautical mile limit.

Administratively, imposing the royalty obligation on the province would be fairly straightforward. Because the province already collects and audits existing royalty payments, it would simply have to calculate the respective international royalty amount and remit that amount to Canada at specified intervals. Canada would then transmit the funds to the ISA. Canada would again be responsible for ensuring calculations were accurate, which introduces an extra step of accountability. In the grand scheme of things, however, this is administratively easy.

C. CANADA PAYS

A plain reading of Article 82 suggests that the international royalty obligation was intended to fall upon the coastal State. Paragraph 1 provides that "[t]he coastal State shall make payments or contributions in kind in respect of the exploitation of the non-living resources of the continental shelf beyond 200 nautical miles from the baselines from which the breadth of the territorial sea is measured."[125] At the very least, it suggests that the international royalty payment must be made *from* the coastal State *to* the ISA. It is unclear whether, if Newfoundland took on the burden, it would have the capacity to make payments directly to the ISA. More likely, it would have to transfer amounts to Canada, which would then transmit them to the ISA.

Administratively, the arrangement is simplest if Canada pays. Canada would have to conduct calculations of the international royalty based on information Newfoundland and Labrador collects from project proponents. While audits of project proponents will still be necessary, Canada would make payments directly to the ISA, and a provincial intermediary would not be interposed in the process.

Ultimately, Canada is the signatory to the *LOSC* and benefits not just from the expansive Article 76 definition, but also from the various other agreements that arise out of the *LOSC*.[126] Neither the project proponents nor Newfoundland had any control over whether or not Canada agreed to Article 82. Neither the project proponents nor Newfoundland played any role in the negotiation process at UNCLOS III at which Article 82 was settled upon. Canada agreed to fulfill an equitable obligation for the benefit of less developed and land locked countries. Out of principle, it should not downstream this commitment.

If Canada does bear this expense, it ultimately falls to the Canadian taxpayer, including the project proponents operating on the extended continental shelf. The royalty obligation would thus be widely distributed amongst the Canadian population and have the fewest negative effects on Newfoundland and Labrador and on future investment in the continental shelf beyond 200 nautical miles.

IX. CONCLUSION

Who pays the international royalty comes down to political, economic, and administrative feasibility. Between the three options, imposing the royalty obligation on Newfoundland is the least feasible both economically and politically. Canada is in a difficult position because it is to set a precedent for other coastal States developing their continental shelves. It has no basis for knowing whether, if it imposes the royalty on project proponents, it will remain competitive in the offshore oil industry. Imposing the royalty on the project proponents is possible, but it has the potential to compromise Newfoundland's bargaining position in coming to its own royalty agreements. This risk is somewhat offset by the fact that the generic royalty regime is already in place and does not require negotiation. If Canada fulfills the obligation it agreed to, the cost ultimately falls to the Canadian taxpayer. Distributing the

[125] *LOSC*, *supra* note 1, art 82 at para 1.
[126] *Ibid*.

obligation over a large tax base ultimately results in greater neutrality than imposing the royalty on solely Newfoundland’s population or on the project proponents. Based on the above analysis, Canada is the most favourable option in most respects. If Canada pays, the royalty regime is the simplest to administer and introduces no reason to deter investment. However, because of the impact on the Canadian taxpayer, it remains to be seen whether it is politically feasible. Throughout future discussions, it may become apparent that a compromise must be reached between Canada and project proponents to share the international royalty obligation.

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