Intelligence MEMOS

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To: Alberta taxpayers

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Re: After Redwater, Environmental Cleanup Risks Remain

The Supreme Court of Canada last week overturned the Court of Appeal of Alberta's decision in the closely watched Redwater legal case. The court's ruling ensures environmental cleanup costs will get priority over creditors when companies go bankrupt.

The decision reinforces the polluter-pay principle, which is reassuring for Canadian regulators and taxpayers. However, it doesn't resolve the challenges posed by insolvent operators. While regulators are now first in line to access bankrupt companies' remaining assets, there is no guarantee those assets will be sufficient to cover cleanup costs. Taxpayers still risk being left on the hook.

These risks are especially relevant for Alberta – a province with a heavy load of industrial cleanup obligations.

As discussed in the C.D. Howe Institute Commentary, All's Well that Ends Well, Alberta accumulated a large and growing backlog of inactive oil and gas wells over the last several decades. Until these sites get cleaned up, they pose environmental and health risks to landowners. When a company cannot complete the cleanup, the job falls to the industry-funded Orphan Well Association. In recent years, the OWA had a harder time covering its costs. Thankfully, the Redwater decision does not make this problem worse. But the financial risk to Alberta taxpayers remains.

Perhaps even more worrying, however, is the potential cost to Albertans of dealing with the province's oilsands tailings. While the Alberta Energy Regulator officially estimates reclaiming the land disturbed by oilsands mines will cost $27 billion, internal AER documents have pegged the bill at $100 billion. Whatever the real costs, the province only holds $900 million in security from oilsands companies against these costs. If an oilsands company were to go bankrupt, a significant part of its cleanup costs would likely fall to taxpayers.

Of course, it's not a given any oilsands company will go bankrupt and pass its cleanup costs to the public in this way; rather, it's a risk. Given the scale of the potential liability, this should be a significant concern for Alberta taxpayers.

Fortunately, there are tools governments can use to address these kinds of risks. A key one is financial assurance. As the Ecofiscal Commission's report Responsible Risk outlines, financial assurance requires companies to commit funds against environmental cleanup costs or the risk of environmental damage. This can come in various forms, such as environmental bonds, insurance or an industry fund.

Financial assurance ensures funds are available for environmental cleanup regardless of whether a company goes bankrupt. Critically, it also helps reduce risk to the environment, since financial assurance puts it in a company's direct financial interest to limit environmental damage. And, by harnessing market forces, it helps reduce environmental risk at minimal cost to the economy. It's not new in Alberta. The government already uses it to cover some of the risks from oil and gas wells and oilsands tailings. But the current system has limited stringency: As noted above, the province holds less than $1 billion against a multibillion-dollar liability in the oilsands.

Alberta could strengthen its financial assurance system in several ways. First, the government could change the amount of assurance companies must provide, the timeline they provide it on or both. Second, the requirements could rise as risk rises; for example, firms with inactive sites that pose a greater risk of abandonment could provide more assurance. Third, a larger role could be established for lenders and insurers. Transferring risk to these actors would let the market put a price on companies' environmental risk, lessening the burden on regulators.

No matter what happens, good information will be critical. Financial assurance works best when risks are well-understood. However, the AER provides very little transparency on important elements of estimated liabilities, such as the liability held by individual projects and companies, assumptions about cleanup technologies and their costs, and key risk factors or uncertainties. Greater transparency will help Albertans have an informed discussion on how best to move forward.

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