

Northern Oil and Gas *BULLETIN*



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Calculating Interest under the *Canada Petroleum Resources Act* and *Frontier Lands Petroleum Royalty Regulations*

The purpose of this bulletin is to clarify how provisions in the *Canada Petroleum Resources Act* (CPRA or the Act) and *Frontier Lands Petroleum Royalty Regulations* (FLPRR) relating to calculating interest are interpreted and applied, on a go-forward basis.

Rate

Under the CPRA and FLPRR, interest and penalties are charged to Interest Holders of production licences on overdue royalties, and interest is payable by the Minister for any overpayments made by Interest Holders on account of royalties, interest or penalties (sections 56 and 66 of the CPRA, respectively). The FLPRR adopts the prescribed rate of interest for any period contained in sections 4300-4301 in Part XLIII of the *Income Tax Regulations* (FLPRR 16(1) and 19(1)).

Rates are established every quarter and are based on the average rate paid on 90-day treasury bills during the first month of the preceding quarter ("Base rate"). The prescribed interest rate to be paid by an Interest Holder to the Minister is 4% plus Base rate. As of July 1, 2010 the prescribed rate to be paid by the Minister to an Interest Holder (who is by definition a corporation) is 0% plus Base rate (*Income Tax Regulations* section 4301). These prescribed rates are published before the beginning of each quarter by the Canada Revenue Agency and can be viewed at: http://www.cra-arc.gc.ca/tx/fq/ntrst_rts/menu-eng.html

When an Interest Holder makes a payment to the Crown, payments are applied first to penalties payable, second to interest payable and third to royalties payable (FLPRR section 20).

Date to which Interest is Applied

Amounts are overdue if not paid on or before the due dates specified by FLPRR. For royalties, the first installment for a production month is an estimate based on the previous month, and the second instalment or "true-up" (the balance of the actual royalties payable for a production month) is due on the last day of the second month following the production month (FLPRR section 5). For penalties, payment is due on the last day of the month after the month in which they are imposed (FLPRR subsection 17(3)).

Interest payable by an Interest Holder on arrears of royalties, interest or penalties is calculated from the day on which the royalties, interest or penalties were due to the day on which payment is received by the Minister, and are compounded monthly (FLPRR subsection 16(2)).

Where the Minister is paying interest on an amount owing to the Interest Holder, interest is calculated from the end of the second month after the month in which the overpayment was made and is compounded monthly. This means interest is charged from when the transaction took place, not from the date when the overpayment was discovered through the course of an assessment or audit (FLPRR 18(1) describes circumstances in which the Minister shall refund any overpayment made on account of royalties, interest or penalties, and FLPRR 19(2) describes how the calculation is made).

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Interest and Audit Assessments

Per section 61 of the CPRA, the Minister shall examine royalty returns, assess the royalty payable and send a notice of assessment to the person who filed the report or return. The assessment is valid and binding upon issuance. The requirement to pay royalties, interest and penalties for a period of twenty calendar days from the date of assessment, if the amounts due are paid in full within this period. This grace period provides the Interest Holder with time to produce and mail the cheque without incurring additional interest charges during this time.

In calculating the amount due in the assessment, two circumstances may occur: the Interest Holder may owe the Crown interest, or the Minister may owe interest to the Interest Holder.

1. When the Interest Holder owes the Crown, interest is calculated from the date royalty, interest or penalty was due. The Minister has discretion to waive interest if the underpayment occurred through "no fault" of the Interest Holder. The Minister will consider on a case-by-case basis the circumstances that gave rise to the underpayment. The onus is on the Interest Holder to file accurate royalty submissions, so it is incumbent upon the corporation to provide a detailed explanation for the underpayment and request that the Minister exercise his or her discretion to waive the interest.

2. When the Minister owes interest, the timing for applying interest described in FLPRR section 19(2) applies, as described above.

In the case where a company disagrees with audit findings, they may file a notice of objection to the assessment or appeal the assessment to the Federal Court (CPRA subsection 62(1) and subsection 63(1) respectively). CPRA subsection 64(2) states that during the period of a notice of objection or appeal, the Minister may suspend the requirement to pay any amount on account of royalty, interest or penalty payable. ***The Act does not suspend the accrual of royalty, interest or penalties, simply the requirement to pay them during the objection or appeal period.***

Once the objection or appeal is resolved, the requirement to pay ceases to be suspended. An updated assessment of royalties, interest and penalties will be issued by the Minister to the Interest Holder, which will include the findings of the objection or appeal. This assessment will include a calculation of royalty, interest or penalty from the period of time payment was originally due.

As with the assessment, the Department has decided to adopt a grace period of 20 days from the date of reassessment, so no additional interest is charged within this time if the amounts due are paid in full within this period.

Please note that to stop the accrual of interest and penalties during the period of objection or appeal, an Interest Holder may make an up-front payment of the amount due in the assessment. In the event that the objection or appeal is resolved in the Interest Holder's favour, the Minister will refund the up-front payment plus pay interest at the prescribed rate.

For clarification on royalties, penalties and interest, please contact:

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Note: This Bulletin is for information purposes only. In the event of an inconsistency between this bulletin and the *Canada Petroleum Resources Act* and *Frontier Lands Petroleum Royalty Regulations*, the original statute or regulation prevails to the extent of the inconsistency.