



NO.: **IT-476R**

DATE: September 18, 2008

SUBJECT: INCOME TAX ACT

Capital Cost Allowance – Equipment Used in Petroleum and Natural Gas Activities

REFERENCE: The definitions of “Canadian exploration expense” and “Canadian development expense” in subsections 66.1(6) and 66.2(5), respectively, and the definition of “Canadian field processing” in subsection 248(1) of the *Income Tax Act* (the “*Act*”); subsections 1100(2.21), 1101(4c), (4d), (5u) and (5v), 1102(14), 1102(14.2), 1103(2d) and 1104(5) to (7), paragraphs 1100(1)(y) and (ya), the definitions of “designated underground storage cost”, “gas or oil well equipment” and “specified temporary access road” in subsection 1104(2) and paragraph 1102(1)(a) of the *Income Tax Regulations* (the “*Regulations*”); and Classes 1, 6, 7, 8, 17, 41, 43 and 49 in Schedule II of the *Regulations*

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This bulletin cancels and replaces Interpretation Bulletin IT-476 dated April 30, 1981, formerly entitled *Capital Cost Allowance – Gas and Oil Exploration and Production Equipment* and the Correction Sheet C.S. 3 related to it dated June 6, 1983. The effective date of a particular legislative provision discussed in the bulletin may be indicated in the *Discussion and Interpretation* section of the bulletin. However, where the bulletin is silent with respect to the effective date of a particular provision, such date can be obtained from the legislation itself. Also, unless otherwise noted, all statutory references throughout the bulletin are to the *Act*.

Summary

This bulletin discusses the capital cost allowance (“CCA”) provisions that apply to equipment used in petroleum and natural gas (“P and NG”) activities. Generally, exploration or development equipment, gas or oil well equipment, Canadian field processing equipment and equipment used in bituminous sands projects are included in Class 41. This bulletin discusses the requirements to be met in order for equipment to be included in that class as well as the CCA classes for pipelines, pipeline appendages, and other assets. In addition, it identifies property that is excluded from depreciable property. Some of the rules affecting the calculation of CCA are also provided. Schedules outlining the income tax treatment of certain assets used in P and NG activities are appended to the bulletin.

Discussion and Interpretation

Assets Used in Petroleum and Natural Gas Activities

Class 41

Introduction

¶ 1. Equipment used in P and NG activities that qualifies for Class 41 includes:

- (a) most property used in bituminous sands projects, by virtue of paragraphs (a), (a.1), (a.2), (a.3) or subparagraph (b)(i) of Class 41 (see ¶s 10-14)
- (b) property described in Class 10 under paragraphs
 - (f.1) — a designated underground storage cost,
 - (j) — gas or oil well equipment (see ¶s 3-4),
 - (t) — exploration or drilling equipment, and
 - (u) — heavy crude oil processing equipment by virtue of subparagraph (b)(i) of Class 41, and
- (c) property used in Canadian field processing, pursuant to paragraphs (c) and (d) of Class 41 (see ¶s 5-9).

¶ 2. “Designated underground storage cost” and “gas or oil well equipment” are defined in subsection 1104(2) of the Regulations. Exploration or drilling equipment (e.g., a drilling rig) refers to property designed principally for the purpose of determining the existence, location, extent or quality of accumulations of oil or gas, or for the drilling of oil or gas wells.

Gas or oil well equipment

¶ 3. Gas or oil well equipment includes

- (a) equipment, structures and well tubing, other than well casing and cementing, acquired by a taxpayer to be used in a gas or oil field in the production therefrom of natural gas or crude oil. This includes equipment, structures and connecting lines, including pipelines to water disposal wells, compressors, pumps and well head equipment (hereinafter referred to as “other production equipment”) used for the purpose of

- disposing of waste substances produced from an oil or gas well,
 - injecting gas or liquids into a gas or oil formation to facilitate production, or
 - enhancing the recovery from a gas or oil well; and
- (b) pipelines acquired by a taxpayer to be used
- to carry gas or oil well substances from the wellheads to the primary separator, or
 - **solely** for transmitting gas to a natural gas processing plant (see ¶ 4).

Based on the case *Texaco Exploration Company*, 75 DTC 5288, [1975] CTC 404 (FC-TD), the production of natural gas or crude oil from a gas or oil field ceases at the wellhead (i.e., the upstream side of any separator).

¶ 4. A pipeline that only transmits natural gas to a natural gas processing plant for further processing (in order to extract natural gas liquids, condensate, water vapour, hydrogen sulphide, carbon dioxide, nitrogen, or a combination of any of these substances) is considered to be a pipeline used solely for transmitting natural gas to a natural gas processing plant.

Canadian field processing

¶ 5. The definition of “Canadian field processing” in subsection 248(1) includes the following activities, if carried out in Canada:

- processing of raw natural gas at a field separation and dehydration facility;
- processing of raw natural gas at a natural gas processing plant to any stage that is not beyond the stage of natural gas that is acceptable to a common carrier of natural gas;
- processing of hydrogen sulphide derived from raw natural gas to any stage that is not beyond the marketable sulphur stage;
- processing of natural gas liquids at a natural gas processing plant where the input is raw natural gas derived from a natural accumulation of natural gas to any stage that is not beyond the marketable liquefied petroleum stage or its equivalent; and
- processing of crude oil, other than heavy crude oil recovered from an oil and gas well or a tar sands deposit, recovered from a natural accumulation of petroleum to any stage that is not beyond the crude oil stage or its equivalent.

These activities are excluded from manufacturing and processing (“M and P”) activities that qualify for the M and P tax credit and the CCA class for M and P assets (by virtue of paragraph (k) of the definition of “manufacturing or processing” in subsection 125.1(3) and paragraph 1104(9)(k) of the Regulations, respectively).

¶ 6. Property (such as primary separators, dehydrators and other field plant facilities and pipes within the plant) acquired by a taxpayer

- to be used directly or indirectly by the taxpayer in Canada primarily in Canadian field processing, or
- to be leased, in the ordinary course of carrying on a business in Canada of the taxpayer, to a lessee who can reasonably be expected to use, directly or indirectly, the property in Canada primarily in Canadian field processing carried on by the lessee,

that would otherwise be included in Class 29 if it were read with certain changes, is included in Class 41 by virtue of paragraphs (c) or (d), respectively, and is hereinafter referred to as “Canadian field processing equipment”. Short lines of pipes running between pieces of equipment or within a field plant facility that may reasonably be considered to be an integral and component part of the equipment or facility, as the case may be, may be included in the same CCA class as that equipment or facility.

¶ 7. A temporary storage tank (also known as a stock tank or battery tank) that is used in the field as a necessary and integral part of Canadian field processing activities is considered to be Canadian field processing equipment. However, a storage tank located away from the field (such as those at a tank farm) used to hold crude oil after the completion of Canadian field processing activities will not be considered as Canadian field processing equipment and will be included in Class 6.

¶ 8. By virtue of paragraph (h) of the definition of Canadian field processing, a natural gas processing plant (or part thereof) that is devoted primarily to the recovery of ethane is not considered to be a natural gas processing plant for the purposes of the activities described in ¶ 5. In addition, the processing of natural gas at a “straddle plant” in Canada would not generally qualify as Canadian field processing for the following reasons:

- due to its location and size, a straddle plant would generally not be considered as being a field separation and dehydration facility described above;
- the processing of natural gas at a straddle plant is generally considered to be processing to a stage that is beyond the stage that is acceptable to a common carrier of natural gas;
- the input at a straddle plant is not **raw** natural gas, as natural gas that has been received by a common carrier ceases to be **raw** natural gas for the purposes of the definition of Canadian field processing.

Therefore, both of these processing activities qualify as M and P activities and qualifying property used in these activities is included in Class 43.

[See Note at the end of ¶ 9]

¶ 9. In a fractionation plant, natural gas liquids are processed and fractionated into various products, such as ethane, propane, butane, pentane, etc. Since the input to such a plant is not **raw** natural gas, the plant equipment will not qualify as Canadian field processing equipment. Instead, qualifying property of such a plant is included in Class 43.

Note: The 2007 Federal Budget proposes that qualifying M and P assets acquired after March 18, 2007 and before 2009 be included in Class 29 which provides for a CCA rate of 50 per cent on a straight line basis, while the 2008 Federal Budget proposes to extend Class 29 treatment to eligible M and P assets acquired before 2010. The 2008 Federal Budget also proposes that eligible M&P assets acquired in 2010 be included in a separate Class 43 that will be entitled to an additional allowance in the year that the property first becomes available for use and in the subsequent taxation year. Eligible M&P assets acquired in 2011 will also be included in a separate Class 43 that will be entitled to an additional allowance only in the year that the property first becomes available for use. Eligible M and P assets acquired after 2011 will be included in Class 43, with no additional allowance.

Bituminous sands projects

¶ 10. Bituminous sands projects, using either surface open pit mining or “in-situ” operations, are treated as mines for CCA purposes. In-situ extraction generally involves introducing sufficient steam or heat into bituminous sands to reduce the viscosity of the bitumen, thus allowing it to flow and be recovered via a well; however, it may also include other extraction methods, such as cold heavy oil production with sand. Property acquired by a taxpayer for the purpose of gaining or producing income from a bituminous sands project in Canada will generally be included in Class 41. “Bituminous sands” is defined in subsection 248(1).

The determination of whether an “in-situ” operation constitutes one project and, therefore, a single mine for the purpose of subsection 1104(7) of the Regulations, is to be made on the basis of the “extractive unit” concept since a mine has been defined as an “integrated system for the extraction of ore”. The mine site consists of the physical surface area on which the mine operations take place. The boundaries of the site are determined on the basis of the facts of a particular situation based upon the degree of integration of the operations within the boundaries, and do not necessarily correspond to the boundaries of the production lease or leases.

Property that qualifies for inclusion in paragraphs (a), (a.1) or (a.2) of Class 41 is eligible for accelerated CCA (see ¶s 12 and 13), while property included in paragraph (b) of Class 41 (see ¶ 11) and paragraph (a.3) of Class 41 (see ¶ 14) is not.

Note: the 2007 Federal Budget proposed to phase out the additional CCA for the new phases of bituminous sands projects for which major construction did not commence before March 19, 2007; however, the regular 25-per-cent CCA rate for Class 41 property will not be affected. Under this proposal, accelerated CCA will continue to be available in full for:

- assets acquired before March 19, 2007, and
- assets acquired before 2012 that are part of a project phase on which major construction began before March 19, 2007.

For other assets, accelerated CCA will gradually be phased out over the period from 2011 to 2015.

¶ 11. Property that is acquired to be used in a bituminous sands project that is not described in ¶ 12 or ¶ 14 is included in subparagraph (b)(i) of Class 41, if the property is described in Class 10 under paragraphs

- (g) — buildings or other structures that would otherwise be included in Class 1, 3 or 6 (other than property described in paragraphs (l) or (m) of Class 10),
- (k) — a structure (that would otherwise be included in Class 8) or machinery and equipment (other than property included in paragraphs (l) or (m) of Class 10),
- (l) — certain property used to provide services to the project or to the community where its workers reside, and
- (m) — railway tracks and related machinery and equipment used in the project.

To be described in one of these paragraphs in Class 10, the property must be acquired for the purpose of gaining or producing income from a mine. Subsections 1104(5) and (6) of the Regulations define income from a mine for the purposes of Class 10 to include income reasonably attributable to the processing of

- ore from a bituminous sands deposit, whether or not owned by the taxpayer, to any stage that is not beyond the crude oil stage or its equivalent (i.e., it includes custom processing), and
- materials extracted by a well from a bituminous sands deposit, whether or not owned by the taxpayer, to any stage that is not beyond the crude oil stage or its equivalent.

Pursuant to paragraph 13(7.5)(a) of the Act and subsection 1102(14.2) of the Regulations, where a taxpayer is required to make payments to a government body for costs incurred by that body relating to property that, if acquired by the taxpayer would be included in paragraph (l) of Class 10 (and hence eligible for inclusion in Class 41), the taxpayer will be considered to have acquired depreciable property of that class having a capital cost equal to the amount of those payments.

¶ 12. The capital cost of property

- described in paragraphs (g), (k) and (l) of Class 10,
- included in Class 41 because of subsection 1102(8) or (9) of the Regulations (i.e., plant and equipment used to provide electricity to a mine – see ¶ 14), or
- in the case of paragraph (a) of Class 41, described in paragraph (m) of Class 10

that is acquired principally (i.e. more than 50%) for the purpose of gaining or producing income from a bituminous sands project in Canada that is operated by the taxpayer will generally be included in either paragraph (a), (a.1) or (a.2) of Class 41, as the case may be,

- (a) if it is used in a new mine that uses either surface or in-situ mining techniques or in a major

expansion to an existing surface mine (paragraph (a) of Class 41);

- (b) to the extent of the portion of the taxpayer's cost of such property used in either an existing surface or in-situ mine, that becomes available for use in the year (see ¶ 13) in excess of 5% of the gross revenue (as defined in subsections 1104(5.1) and (5.2) of the Regulations) from the mine for the year (assuming a 365 day taxation year) (paragraph (a.1) of Class 41); or
- (c) if it is used in a major expansion to an existing in-situ mine (paragraph (a.2) of Class 41).

For purposes of accelerated CCA, the expression “income from a mine” is defined in subsection 1104(5) of the Regulations as including income that is reasonably attributable to

- processing by the taxpayer of ore, all or substantially all of which is from a bituminous sands deposit owned by the taxpayer, to any stage that is not beyond the crude oil stage or its equivalent
- processing by the taxpayer of materials extracted by a well, all or substantially all of which is from a bituminous sands deposit owned by the taxpayer, to any stage that is not beyond the crude oil stage or its equivalent,
- production by the taxpayer of material from a deposit of bituminous sands, and
- rail transportation of the output from a bituminous sands deposit owned by the taxpayer, that has been processed by the taxpayer to any stage that is not beyond the crude oil stage or its equivalent.

With respect to the “all or substantially all” test referred to above, the CRA considers that this test is met where 90% or more of the ore or material that is processed by the taxpayer is from a bituminous sands deposit owned by the taxpayer. Therefore, if the “all or substantially all” test is not met [i.e. generally where more than 10% of the ore or material processed by the taxpayer is not from a bituminous sands deposit owned by the taxpayer (i.e. custom processing)], none of the income attributable to the custom processing would be included as income from a mine.

¶ 13. Additional CCA may be claimed under paragraphs 1100(1)(y) and 1100(1)(ya) of the Regulations for the mining properties described in ¶ 12. Such additional CCA is limited to the lesser of the undepreciated capital cost of the separate prescribed class for Class 41 property of a mine, or mines, as the case may be, at the end of the taxation year and the taxpayer's income from such mine or mines, as the case may be, with certain adjustments thereto, as determined under the relevant paragraph of the Regulations. The “50% rule” referred to in ¶ 33 does not apply when making this calculation. Since subsection 1101(4c) of the Regulations requires that separate classes be maintained for each mine, a separate CCA calculation must be performed for each mine. However, where a property is used in two or more mines, that property must be included in a separate Class 41

pursuant to subsection 1101(4d) of the Regulations. Since paragraph 1100(1)(y) of the Regulations requires that income under that paragraph be determined before any deduction under paragraph 1100(1)(ya), the calculation and claim for additional CCA must be made for the properties assigned to a separate class under subsection 1101(4c) of the Regulations (used in only one mine) before the calculation and claim for additional CCA on properties assigned a separate class under subsection 1101(4d) of the Regulations (used in more than one mine).

Where the 5% of gross revenue test referred to in ¶ 12(b) is not met, the portion of the cost of the property that becomes available for use in the year will be included in paragraph (b) of Class 41 and will not be eligible for the additional CCA.

[See Note at the end of ¶ 10 concerning the phase out of accelerated CCA for most bituminous sands property acquired after March 18, 2007.]

¶ 14. Pursuant to subsections 1102(8) and (9) of the Regulations, electrical generating or distribution equipment and plant that is acquired by a producer or distributor of electrical energy, or by the mine operator, to provide electrical power to a bituminous sands project and at least 80% of the electrical output produced by such equipment during the first two years of operation was used in the bituminous sands mining operation is included in paragraph (a.3) of Class 41, unless it otherwise qualifies for inclusion in any of paragraphs (a), (a.1) or (a.2) thereof (see ¶ 12).

Pipelines

¶ 15. Depending on its use, a pipeline may be included in Class 1, 8, 41 or 49, as the case may be. A pipeline acquired by a taxpayer that is **not**

- (a) gas or oil well equipment – Class 41 (see ¶s 3-4),
- (b) Canadian field processing equipment – Class 41 (see ¶ 6),
- (c) a new pipeline acquired after February 22, 2005 used for the transmission of petroleum, natural gas or related hydrocarbons – Class 49 (see ¶ 17), or
- (d) a pipeline for which the CRA, in consultation with the Minister of Natural Resources, is satisfied that the main source of supply is likely to be exhausted within 15 years of it becoming operational – Class 8 by virtue of paragraph (i) thereof

will be included in Class 1 by virtue of paragraph (l) thereof.

Note: The 2007 Federal Budget proposes that a new pipeline, including control and monitoring devices, valves and other equipment ancillary to the pipeline, used for the distribution (but not the transmission) of natural gas that is acquired after March 18, 2007 be included in new Class 51 which will have a CCA rate of 6 per cent on a declining balance basis. The 2008 Federal Budget proposes that a new pipeline used for the transmission of carbon dioxide that is acquired after February 25, 2008 be included in Class 49.

¶ 16. Examples of pipelines included in paragraph (l) of Class 1 are as follows:

- pipelines (other than new pipelines eligible for Class 49 – see ¶ 17) used for the transmission of petroleum, natural gas or related hydrocarbons;
- pipelines used to transmit oil from the primary separator to the transmission line or to an oil processing plant (i.e., refinery);
- in the case of heavy crude oil, a pipeline used to transport condensate to the field blending facilities;
- pipelines from the primary separator in a gas field to the transmission line (other than a pipeline used **solely** to transmit natural gas to a natural gas processing plant – see ¶s 3 and 4);
- pipelines from a gas processing plant to the transmission line;
- a water supply pipeline from a river or any other source to a gas processing plant;
- pipelines (other than new pipelines eligible for Class 49 – see ¶ 17) used to transmit natural gas to a straddle plant. Such pipelines are considered to be used primarily for transmitting the gas to market;
- product sales lines from a gas processing plant to loading facilities or a transmission line;
- liquefied petroleum gas and ethane pipelines from a gas processing plant to storage facilities; and
- pipelines used for the distribution of petroleum, natural gas or related hydrocarbons. *[See note at the end of paragraph 15].*

Attachments to a pipeline that are considered to be an integral and component part of a pipeline (e.g., valves, control devices, branches, extensions, racks) will be included in the same CCA class as the pipeline of which they are a part.

For comments concerning linefill in a pipeline and the capital cost of a pipeline, see the current version of IT-482, *Pipelines*.

¶ 17. Class 49 includes property acquired after February 22, 2005 that is a pipeline, including control and monitoring devices, valves and other equipment ancillary to the pipeline, used for the transmission (but not the distribution) of petroleum, natural gas or related hydrocarbons. This is a functional determination as to whether a pipeline is used for the transmission of a product. Therefore, for example, a pipeline used in the transmission phase of a company's business that consists primarily of the distribution of gas, may qualify for inclusion in Class 49. Similarly, a pipeline used to transmit natural gas to a straddle plant may be included in this class.

However, only property that has not been used or acquired for use for any purpose by any taxpayer before February 23, 2005 is eligible to be included in Class 49. Eligible property does not include

- pipelines described in ¶ 15(d) above,

- a building or structure, or
- pipeline appendages (see ¶s 18 to 24).

A separate class election, which must be made for the taxation year in which the property is acquired, is available under subsection 1101(5v) of the Regulations for Class 49 property. Although this separate class election does not change the CCA rate for such property, it does provide that any terminal loss or recapture will be realized at the time of disposition.

As indicated in the Note at the end of ¶ 15, it is proposed that a new pipeline used for the transmission of carbon dioxide that is acquired after February 25, 2008 be included in Class 49.

Pipeline Appendages

¶ 18. Where an attachment to a pipeline is not an integral and component part of the pipeline, it is considered to be separate equipment from that of the pipeline (a “pipeline appendage”). For further information and examples, see the current version of IT-482.

¶ 19. Except as noted in ¶ 24(a), where a pipeline is included in Class 41 (see ¶ 15(a) and (b)), any appendage to it will also be included in that class.

¶ 20. A pipeline appendage acquired by a taxpayer that is not included in Class 41 as described in ¶ 19 will be included in

- Class 7 by virtue of paragraph (j) thereof, if it is pumping, compression or any ancillary equipment acquired after February 22, 2005 related to a transmission pipeline for petroleum, natural gas or related hydrocarbons (see ¶ 21);
- Class 8 by virtue of paragraph (i) thereof, if it is a compressor station acquired before February 23, 2005 that is used
 - (a) for the transmission of natural gas from a gas field or gas plant to a transmission pipeline, or
 - (b) in conjunction with a transmission pipeline, but is not used in conjunction with the distribution of natural gas (see ¶ 22);
- Class 8 by virtue of paragraph (i) thereof, if it is used for the transmission or distribution of crude oil and it is not included in paragraph (j) of Class 7; or
- Class 1 by virtue of paragraph (n) thereof, if it is acquired primarily for the distribution of natural gas and it is not included in paragraph (j) of Class 7 (see ¶s 21 to 24).

Note: The 2008 Federal Budget proposes that any pumping, compression or ancillary equipment acquired after February 25, 2008 that is on a carbon dioxide transmission pipeline be included in Class 7.

¶ 21. Paragraph (j) of Class 7 includes pumping and compressing equipment that pumps or compresses petroleum, natural gas or related hydrocarbons for the purpose of moving it

- through a transmission pipeline,
- from a transmission pipeline to a storage facility, or
- to a transmission line from a storage facility.

This class will include certain property acquired after February 22, 2005 that would have previously been included in Class 1 by virtue of paragraph (n) thereof (see ¶ 24) since property described in Class 1 is included in that class only if it is not included in any other class (such as Class 7).

A separate class election, which must be made for the taxation year in which the property is acquired, is available under subsection 1101(5u) of the Regulations for property included in Class 7 by virtue of paragraph (j) thereof. Although this separate class election does not change the CCA rate for such property, it does provide that any remaining balance of undepreciated capital cost in the class after the disposition of the property, can in the year of disposition, be fully deducted as a terminal loss.

¶ 22. Paragraph 8 of archived Interpretation Bulletin IT-482, *Capital Cost Allowance – Pipelines*, dated November 1, 1981, indicated that:

“A compressor station that is used in the transmission of natural gas from a gas field or a gas plant to a transmission pipeline, or that is used in conjunction with a main transmission pipeline, is included in Class 8. A compressor station that is used in conjunction with the distribution of gas is included in class 2 by virtue of paragraph (d) thereof [now paragraph (n) of Class 1].”

This bulletin was issued before the Federal Court of Appeal (FCA) decisions in *Northern and Central Gas Corporation v. The Queen*, 87 DTC 5439, [1987] 2 CTC 241 and *Pacific Northern Gas Limited v. The Queen*, 91 DTC 5287, [1991] 1 CTC 469 (see ¶ 23). Prior to the FCA’s decision in *Northern and Central Gas Corporation*, a Special Release to IT-482 dated February 28, 1986 was issued which indicated that the position in ¶ 8 of the bulletin would continue to be followed pending the outcome of the appeal of the case. However, for a number of reasons, the bulletin was not revised once that decision was released. Therefore, notwithstanding the view expressed in ¶ 23, the CRA will maintain the position in ¶ 8 of IT-482 that compressor stations used in the transmission of natural gas or in conjunction with a transmission pipeline acquired before February 23, 2005 will be included in Class 8. Such compressor stations acquired after February 22, 2005 will be included in Class 7 by virtue of paragraph (j) thereof (see ¶s 20 and 21).

In interpreting the words in the second sentence in ¶ 8 of IT-482, “A compressor station that is used in conjunction with the distribution of gas...”, the CRA has generally adopted a “main purpose approach” rather than a functional approach to the classification of natural gas pipeline compressors. For example, compressors that form part of a taxpayer’s transmission system that is used primarily in the taxpayer’s business of distributing natural gas would be included in paragraph (n) of Class 1 and not in Class 8.

Distribution of natural gas includes deliveries to the ultimate consumers, regardless of whether they are residential, commercial or industrial and whether or not the taxpayer is the owner of the natural gas being distributed.

¶ 23. Paragraph (n) of Class 1 generally includes property that is manufacturing and distributing equipment and plant (including structures) acquired primarily for the production or distribution of gas. Based on the decisions of the courts in *Northern and Central Gas* and *Pacific Northern Gas Limited*, it is the CRA's view that the words "distributing equipment and plant" and "distribution of gas" as used in paragraph (n) of Class 1 should be interpreted in a broad and general sense and should not be given the more restrictive meaning used by the natural gas industry to distinguish between a natural gas transmission system and a natural gas distribution system.

¶ 24. Examples of pipeline appendages that would generally be included in Class 1 by virtue of paragraph (n) thereof are as follows:

- (a) pipeline appendages attached to a pipeline used **solely** for transmitting gas to a natural gas processing plant (Note: they do not qualify as gas or oil well equipment);
- (b) compressors acquired before February 23, 2005 that are used primarily in the taxpayer's business of distributing natural gas (see ¶s 22 and 23); and
- (c) liquefied natural gas (LNG) facilities and related storage facilities (other than designated underground storage costs). (See the decision in *Northern and Central Gas Corporation*.) LNG facilities include facilities which liquefy the natural gas prior to shipment, those which regasify it after transport and those that liquefy natural gas for storage during periods of low demand and regasify it for use during periods of high demand.

However, where the pipeline appendages referred to in paragraphs a) and b) above are pumping, compression and any ancillary equipment related to a transmission pipeline for natural gas acquired after February 22, 2005, they will be included in Class 7 by virtue of paragraph (j) thereof (see ¶ 21).

Note: The 2007 Federal Budget proposes that eligible equipment acquired after March 18, 2007 that is part of an LNG facility that liquefies or regasifies natural gas be included in Class 47, which has a CCA rate of 8 per cent. Eligible equipment will include controls, cooling equipment, compressors, pumps, storage tanks, vaporizers and ancillary equipment, loading and unloading pipelines on the facility site used to transport the LNG between a ship and the facility and related structures; but will not include a building, breakwater, dock, jetty, wharf or similar structure, or property acquired for the purpose of producing oxygen or nitrogen.

Other CCA Classes

¶ 25. Generally, buildings or other structures are included in Class 1. However, certain buildings that have no footings or any other base support below ground level are included in Class 6. In addition, as noted in ¶ 11, buildings or other

structures may qualify for inclusion in subparagraph (b)(i) of Class 41 because they are described in paragraph (g) of Class 10. For further information, see the current version of IT-79, *Capital Cost Allowance – Buildings or Other Structures*.

¶ 26. Depreciable property (such as a service rig) used in the completion, re-completion or work-over of an oil or gas well will generally be included in either paragraph (a) of Class 10 or paragraph (i) of Class 8. Generally, automotive service rigs are included in Class 10 by virtue of paragraph (a) thereof and non-automotive service rigs are in Class 8 by virtue of paragraph (i) thereof. For a discussion of CCA in respect of offshore drilling rigs, see the current version of IT-267, *Capital Cost Allowance – Vessels*.

¶ 27. Pursuant to paragraph 13(7.5)(b) of the Act and subsection 1102(14.3) of the Regulations, where a taxpayer has incurred costs on account of capital for the building of or right to use roads, parking areas, storage areas or similar surface construction and the amount of these costs would not otherwise be included in the capital cost to the taxpayer of depreciable property, the taxpayer is considered to have acquired a depreciable property having a capital cost equal to the amount of such costs. The capital cost of such property would be included in the undepreciated capital cost of property of Class 17 by virtue of paragraph (c) thereof.

Schedules

¶ 28. The schedules appended to this bulletin indicate the appropriate CCA classification of certain equipment used in P and NG activities, as well as certain expenditures that qualify as either Canadian exploration expense ("CEE") (as defined in subsection 66.1(6)) or Canadian development expense ("CDE") (as defined in subsection 66.2(5)). In addition to Class 41 assets, the schedules also describe some of the assets that are included in Classes 1, 6, 7, 8, 17, 43 and 49. Since the classification of certain assets used in bituminous sands projects is described in ¶s 10-14, they are not included in the schedules.

Exclusions from Depreciable Property

¶ 29. A "specified temporary access road" (as defined in subsection 1104(2) of the Regulations) is generally a road built for temporary access to an oil or gas well in Canada in the course of drilling or completing such well. It is excluded from Class 17 by virtue of paragraph (c) thereof and excluded from Class 8 by virtue of subparagraph (i)(vi) thereof. Since it is not depreciable property of a prescribed class, the cost of a specified temporary access road may qualify as CEE or CDE provided that other requirements of those provisions are met.

¶ 30. An "oil or gas well" (as defined in subsection 248(1)), including well casing and cementing, is not considered to be "gas or oil well equipment" and it is also excluded from Class 8 by virtue of subparagraph (i)(iv) thereof. An oil or gas well in Canada is a "Canadian resource property" (as defined in subsection 66(15)), the cost of which

qualifies as “Canadian oil and gas property expense” (as defined in subsection 66.4(5)).

Depreciable Property Excluded from CEE and CDE

¶ 31. Pursuant to paragraph (k.1) of the definition of CEE in subsection 66.1(6) and paragraph (i.1) of the definition of CDE in subsection 66.2(5), the CEE and CDE of a taxpayer do not include an expense that is a cost, or any part of the cost, to the taxpayer of any depreciable property of a prescribed class that was acquired after 1987. Other provisions dealing with the treatment of depreciable property vs. resource expenses (e.g., CEE and CDE) are

- for taxation years that end after 1987 and before December 6, 1996 — subsection 13(34), and
- for taxation years that end after December 5, 1996 — paragraph 1102(1)(a) of the Regulations and paragraph (l) of the definition of CEE in subsection 66.1(6) and paragraph (j) of the definition of CDE in subsection 66.2(5) of the Act.

Calculation of CCA

¶ 32. CCA for equipment used in P and NG activities may be claimed under paragraph 20(1)(a). The maximum annual rate of CCA for Class 41 property is 25% applied to the undepreciated capital cost of the class. The CCA rates for the other classes are indicated in brackets beside the name of the class in the appended schedules. As indicated in ¶s 12-13, property acquired to be used in a new bituminous sands project or in a major or a minor expansion to an existing bituminous sands project may qualify for additional CCA.

¶ 33. The maximum annual CCA claim (other than the additional CCA described in ¶ 13) is subject to the “50% rule” for property acquired in a year, or that became available for use in a year. No amount in respect of the cost of depreciable property may be included in calculating a taxpayer’s undepreciated capital cost of property of a prescribed class before the property is considered to have become available for use by the taxpayer. For more information concerning the available for use rules and the “50% rule”, refer to subsections 13(26) to (31) and the current version of IT- 285, *Capital Cost Allowance – General Comments*.

Paragraph 1100(2.21)(a) of the Regulations provides that where a taxpayer is deemed to have disposed of and acquired or reacquired a property, for purposes of certain CCA provisions including subsection 1102(14) of the Regulations (see below), the acquisition or reacquisition will be deemed to have been from a person with whom the taxpayer does not deal at arm’s length. Therefore, the “50% rule” will not apply upon the deemed acquisition or reacquisition of the property.

¶ 34. When a taxpayer disposes of a property of a prescribed class in a taxation year and before the end of that year acquires another property of another prescribed class, the taxpayer may be able to elect to transfer the former property from the former class to the present class of the new property if the requirements of subsection 1103(2d) of the Regulations are met. For further information, refer to the current version of IT-472, *Capital Cost Allowance—Class 8 Property*.

¶ 35. When a taxpayer acquires a property in the course of a qualifying butterfly reorganization described in paragraph 55(3)(b) or from a non-arm’s length party, subsection 1102(14) of the Regulations generally requires the taxpayer to place the property in the same prescribed class or separate prescribed class as that of the person from whom it was acquired. See the current version of IT-147, *Capital Cost Allowance—Accelerated Write-off of Manufacturing and Processing Machinery and Equipment* for a discussion of this provision.

Schedules – Certain Assets Used in Petroleum and Natural Gas Activities

NATURAL GAS PRODUCTION, GATHERING AND FIELD PROCESSING SYSTEMS

<p>Class 1 (4%)</p> <ul style="list-style-type: none"> • pipelines not included in Class 8, 41 or 49 (see ¶s 15-17) • pipeline appendages not included in Class 41 (e.g., a compressor on a pipeline used solely for transmitting gas to a natural gas processing plant) (see ¶s 18-24) 	<p>Class 6 (10%)</p> <ul style="list-style-type: none"> • fencing • condensate storage tanks not included in Class 41 (see ¶ 7) • qualifying buildings having no footings or base support below ground level (see ¶ 25) 	<p>Class 8 (20%)</p> <ul style="list-style-type: none"> • a pipeline for which the main source of supply is to be exhausted within 15 years (see ¶ 15) 	<p>Class 17 (8%)</p> <ul style="list-style-type: none"> • roads (other than specified temporary access roads) and parking areas 	<p>Class 41 (25%)</p> <p><u>Exploration or drilling equipment</u> (see ¶ 2)</p> <p><u>Gas or oil well equipment</u> (see ¶s 3-4)</p> <ul style="list-style-type: none"> • equipment and structures, including wellhead equipment and well tubing, (but excluding well casings and cementing) acquired to be used in a gas field in the production of natural gas • pipelines used solely for transmitting gas beyond the primary separator to a natural gas processing plant (other than a straddle plant) for processing • pipelines and related pipeline appendages used to carry gas well substances from the wellhead to the primary separator <p><u>Canadian field processing</u> (see ¶s 5 to 9)</p> <ul style="list-style-type: none"> • Canadian field processing equipment which may include pipelines, pipeline appendages and temporary storage tanks 	<p>Class 49 (8%)</p> <ul style="list-style-type: none"> • a new pipeline acquired after February 22, 2005 used for the transmission of natural gas or related hydrocarbons (see ¶s 15-17) <p>Proposed</p> <ul style="list-style-type: none"> • a new pipeline acquired after February 25, 2008 used for the transmission of carbon dioxide [See Note at the end of ¶ 15]
<p>Proposed: Class 7 (15%)</p> <ul style="list-style-type: none"> • any pumping, compression or ancillary equipment acquired after February 25, 2008 that is related to a pipeline used for the transmission of carbon dioxide 					

GAS PROCESSING PLANTS

<p>Class 1 (4%)</p> <ul style="list-style-type: none"> • pipelines not included in Class 8, 41 or 49 (see ¶s 15-17) • pipeline appendages used in conjunction with the distribution of natural gas (see ¶s 22 - 24) 	<p>Class 6 (10%)</p> <ul style="list-style-type: none"> • condensate storage tanks not included in Class 41 (see ¶ 7) • fencing • qualifying buildings having no footings or base support below ground level (see ¶ 25) 	<p>Class 7 (15%)</p> <ul style="list-style-type: none"> • pumping, compression and any ancillary equipment related to the transmission pipeline for natural gas or related hydrocarbons acquired after February 22, 2005 (see ¶s 20-21) <p>Proposed</p> <ul style="list-style-type: none"> • any pumping, compression or ancillary equipment acquired after February 25, 2008 that is related to a pipeline used for the transmission of carbon dioxide 	<p>Class 8 (20%)</p> <ul style="list-style-type: none"> • assets (that are not included in another class) used in the storing and selling of finished goods, including by-product loading facilities and sulphur storage and handling equipment • compressor stations used for the transmission of natural gas not included in Class 7(j) or Class 1(n) (see ¶s 20 - 24) 	<p>Class 17 (8%)</p> <ul style="list-style-type: none"> • roads (other than specified temporary access roads) and parking areas 	<p>Class 41 (25%)</p> <ul style="list-style-type: none"> • Canadian field processing equipment pipelines, pipeline appendages and temporary storage tanks (see ¶s 5 to 7) 	<p>Class 43 (30%)</p> <ul style="list-style-type: none"> • straddle plants (see ¶ 8) • all or part of a natural gas processing plant used primarily for the recovery of ethane (see ¶ 8) • fractionation plants where natural gas liquids are processed and fractionated into various products (see ¶ 9) <p>Proposed: These assets will be included in Class 29 (50% straight-line) if acquired after March 18, 2007 and before 2010.</p>	<p>Class 49 (8%)</p> <ul style="list-style-type: none"> • a new pipeline acquired after February 22, 2005 used for the transmission of natural gas or related hydrocarbons (see ¶s 15 - 17) <p>Proposed</p> <ul style="list-style-type: none"> • a new pipeline acquired after February 25, 2008 used for the transmission of carbon dioxide
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Crude Oil Production, Gathering Systems and Field Processing

<p>Class 1 (4%)</p> <ul style="list-style-type: none"> a pipeline not included in Class 8, 41 or 49 (see ¶s 15-17) 	<p>Class 6 (10%)</p> <ul style="list-style-type: none"> oil and condensate storage tanks not included in Class 41 (see ¶ 7) qualifying buildings having no footings or base support below ground level (see ¶ 25) 	<p>Class 7 (15%)</p> <ul style="list-style-type: none"> pumping, compression and any ancillary equipment related to the transmission pipeline for petroleum acquired after February 22, 2005 (see ¶s 20-21) <p>Proposed</p> <ul style="list-style-type: none"> any pumping, compression or ancillary equipment acquired after February 25, 2008 that is related to a pipeline used for the transmission of carbon dioxide 	<p>Class 8 (20%)</p> <ul style="list-style-type: none"> a pipeline for which the main source of supply is to be exhausted within 15 years (see ¶ 15) pipeline appendages not included in Class 7 or 41 (see ¶s 19-21) 	<p>Class 17 (8%)</p> <ul style="list-style-type: none"> roads (other than specified temporary access roads) and parking areas 	<p>Class 41 (25%)</p> <p><u>Exploration or drilling equipment</u> (see ¶ 2)</p> <p>Gas or oil well equipment (see ¶s 3-4)</p> <ul style="list-style-type: none"> equipment, structures and well tubing, other than well casing and cementing, acquired to be used in an oil field in the production of crude oil – this includes the wellhead, pump jack, production tubing, sucker rods, downhole pump, etc. battery or storage tanks in the field storing the product before it is metered for sale pipelines and related pipeline appendages used to carry oil well substances from the wellheads to the primary separator <p><u>Canadian field processing</u> (see ¶s 5-7)</p> <ul style="list-style-type: none"> Canadian field processing equipment which may include pipelines, pipeline appendages and temporary storage tanks <p><u>Processing of heavy crude oil</u></p> <ul style="list-style-type: none"> Condensate storage tanks used to hold condensate that is blended with heavy crude oil in a processing activity 	<p>Class 49 (8%)</p> <ul style="list-style-type: none"> a new pipeline acquired after February 22, 2005 used for the transmission of petroleum (see ¶s 15-17) <p>Proposed</p> <ul style="list-style-type: none"> a new pipeline acquired after February 25, 2008 used for the transmission of carbon dioxide
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EASEMENTS & RIGHTS OF WAY RELATING TO PIPELINES AND GATHERING SYSTEMS

- eligible capital expenditure (as defined in subsection 14(5))

UNDERGROUND STORAGE FACILITIES

<p>Class 1 (4%)</p> <ul style="list-style-type: none"> • pipelines leading to and from the underground storage facilities (other than a pipeline included in Class 49) • liquefying and storage facilities (other than designated underground storage) located on a natural gas transmission line that are used to store natural gas during periods of low demand (see ¶ 24) • compressors (not included in Class 7(j)) used to pump natural gas under pressure into or out of an underground gas storage facility (see ¶s 20-23) 	<p>Class 7 (15%)</p> <ul style="list-style-type: none"> • pumping and compression equipment acquired after February 22, 2005 and used for the purpose of moving petroleum, natural gas or related hydrocarbons from a transmission line to a storage facility or to a transmission line from a storage facility (see ¶ 21) 	<p>Class 41 (25%)</p> <ul style="list-style-type: none"> • designated underground storage cost—the cost incurred by a taxpayer of developing a well, mine or other similar underground property (such as salt caverns and non-producing gas wells) for the storage of petroleum, natural gas or other related hydrocarbons 	<p>CDE</p> <ul style="list-style-type: none"> • payments for any right, licence or privilege to store underground petroleum, natural gas or related hydrocarbons in Canada
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ROADS

<p>CEE or CDE</p> <ul style="list-style-type: none"> • expenses incurred in building a temporary access road to an oil or gas well in Canada may be eligible for treatment as either CEE or CDE if the requirements of paragraph (a) of the definition of CEE in subsection 66.1(6) or subparagraph (a)(ii) of the definition of CDE in subsection 66.2(5), respectively, are met (see ¶ 29) 	<p>Class 17 (8%)</p> <ul style="list-style-type: none"> • roads (other than specified temporary access roads) and parking areas • costs associated with the building of roads and similar projects as provided under subsection 13(7.5) (see ¶ 27)
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Explanation of Changes

Introduction

The purpose of the *Explanation of Changes* is to give the reasons for the revisions to an interpretation bulletin. It outlines revisions we have made as a result of changes to the law as of the date of this publication, as well as changes reflecting new or revised interpretations.

Reasons for the Revision

This bulletin is being revised to reflect various amendments that have been enacted since the date of the last bulletin and before the date of this bulletin, including

- the introduction of paragraph (j) of Class 7, Classes 41, 43 and 49;
- the new definitions of Canadian field processing and bituminous sands;
- the treatment of a bituminous sands project as a mine; and
- amendments to the definition of CEE and CDE to exclude depreciable property.

Legislative and Other Changes

Since the scope of the bulletin has been expanded to include assets used in natural gas processing plants, bituminous sands projects, as well as a discussion of various types of pipelines and pipeline appendages used in P and NG activities, the title of the bulletin has been revised accordingly.

New ¶s 1 and 2 indicate the types of equipment used in P and NG activities that are included in Class 41.

¶s 3-4 (portions of former ¶s 4-7) list some of the assets that are included in gas or oil well equipment.

New ¶s 5-9 explain the types of activities that qualify as “Canadian field processing”, as well as the CCA classification of property used in those activities.

New ¶s 10-14 describe the CCA classification of assets used in bituminous sands projects and the additional CCA that is available for certain property used in such projects .

¶s 15-17 (portions of former ¶s 5 to 7) discuss the CCA classification of various types of pipelines, including those included in new Class 49.

¶s 18-24 (portions of former ¶ 7) contain the CCA classification of various types of pipeline appendages, including those described in new paragraph (j) to Class 7.

New ¶s 25-27 indicate certain assets that are included in other CCA classes.

New ¶ 28 provides a discussion about assets included in the new schedules appended to the bulletin.

¶s 29-30 (a portion of former ¶ 4) describe certain property that is excluded from depreciable property.

¶ 31 (former ¶ 2) has been revised to include the legislative amendments to the definitions of CEE and CDE that specifically exclude depreciable property from being CEE or CDE.

New ¶s 32-35 explain certain rules affecting the calculation of CCA.

The new schedules appended to this bulletin indicate the classification for CCA purposes of certain assets used in P and NG activities, as well as certain expenditures that qualify as CEE or CDE.