CAPP CANADA'S OIL & NATURAL GAS PRODUCERS

2023 Federal Pre-Budget Consultation Submission

February 9, 2023
Canadian Association of Petroleum Producers

Introduction

CAPP supports the Government of Canada's desire to create a path for meeting its international climate change objectives which will require innovation, major investment, a healthy industry, and good public policy. With the right incentive-focused policies, we can continue to build on Canada's world class innovation investment and GHG reduction leadership.

Emissions Cap

On July 18, 2022, the Government of Canada published a discussion paper to launch formal engagement on two potential regulatory options to cap and reduce oil and gas sector GHG emissions. CAPP and the Government of Canada share both principles and goals on the emission cap policy, namely accountability of our emissions and performance, supporting ambitious, effective, and achievable climate and economic policy, and attracting global capital while promoting low emissions energy growth in Canada. We are appreciative of government committing to working throughout 2023 to ensure that this policy is properly designed. Although we share the stated goals, it is the industry's opinion that the two proposed emission cap options on Canadian oil and natural gas emissions are unlikely to reduce global emissions.

Since responding to the discussion paper, CAPP has been extensively reviewing the two options and potential emission reduction trajectories.

It is recommended that the Government of Canada in relation to an emissions cap:

- Reconsider adding another layer of regulation as the current regulatory framework has already driven substantial emission reductions.
- If an emissions cap is considered, implement realistic trajectories to increase certainty for large-scale investments in energy and decarbonization projects.
- Enable markets to ensure that cost effective opportunities are available for all, as emissions reduction projects compete with other investments and are global in nature.
- Leverage efficiencies across the economy avoiding a sector-by-sector approach and consider policy alternatives focused on enabling key objectives.

In addition to the policy considerations, it will be key for government to understand and account for the variances between different production types within the oil and gas sector in Canada while designing the emission cap. The different types of production can range from large scale oil sands operations to smaller scale conventional oil and gas production. These different types of production have vastly different emission profiles and the solutions for emissions reduction will often be very different. Upstream conventional oil and natural gas operations are often small in scale with shorter durations. It is expected that existing production will be replaced with new wells and facilities that will come online with leading technology and will have lower absolute emissions, reducing Canada's overall intensity. The upstream conventional oil and gas sector represents approximately half of the total production and emissions in Canada [1] and the conventional subsector has great potential for further production and emissions abatement in the short-term.

Further, conventional assets are spread out geographically across Canada and, as such, much of the conventional oil and natural gas produced in Canada is used in Canada, 77 percent and 60 percent respectively. In addition to methane abatement and CCUS, electrification is a meaningful opportunity for emissions reduction

[1] National Inventory Report 1990 –2020: Greenhouse Gas Sources and Sinks in Canada

for the conventional oil and natural gas sector. However, our industry will not be able to do this alone and will need to work closely with all governments to ensure affordable and sufficient supply and grid connectivity to enable industry to pursue greater electrification.

CAPP supports government working closely with industry throughout 2023 to develop policy mechanisms that recognize industry's contribution to Canada's emissions reductions, energy security, and consider the differences of operations within the sector and policy tools necessary to drive reductions. As such, CAPP recommends that the government of Canada:

- Recognize the unique nature of the upstream sector and the key differences between conventional oil and natural gas with that of the oilsands as well as the unique technologies that will support emissions reductions.
- Ensure that resources can flow quickly and directly to projects that reduce emissions and support innovation, eliminating red tape from government grant programs.
- Ensure existing carbon pricing effectiveness is not compromised (i.e. credit market maintained, emission intensive trade exposed protection, carbon price level consistent, economy wide).
- Continue to work collaboratively with industry throughout 2023 to get the right policies in place for the upstream sector to drive emissions reductions.

CCUS Investment Tax Credit (ITC) vs. Updated U.S. 45Q

CAPP believes Ottawa's planned CCUS ITC, in addition to the measures and competitiveness urgency announced in the recent Fall Economic Statement, are significant steps forward in federal support for emissions-reducing technology and our climate goals. Key under the Canada Growth Fund was the announcement of Carbon Contracts for Differences (CCFD). CCFD's must be designed in a way to help provide certainty for industry investing in long term emission reduction solutions and, as such, must account for duration, volume, and price of carbon abated.

Industry modelling shows the Canadian ITC required to equal the same economics as the updated 45Q would need to be doubled to an ITC effective rate of 85 percent (the current Government of Canada 50 percent and 37.5 percent ITC equates to an effective 42 percent ITC given the capital spend mix). A project built in Canada under the proposed federal ITC would not even meet its cost of capital whereas the same project constructed under the current U.S. 45Q under the same assumptions here in Canada would not only meet its cost of capital but would return positive cash flow over the project's life.

It is recommended that the Government of Canada in relation to CCUS:

- Consider a flexible policy approach that achieves fiscal parity with the U.S. 45Q such as a production tax credit, inclusion of operating costs, or other financial policy levers, and CCFDs.

Methane

We recognize methane emissions are one of the highest potential GHG abatement opportunities for our industry and we support taking actions that lead to further reductions of methane emissions. Based on the National Inventory Report, the Canadian upstream oil and gas industry has succeeded in reducing its total methane emissions significantly since 2012, with a 43 percent reduction (equating to 27.5Mt of CO2e per year),

as of 2020.[2] We are very interested in working with the Government of Canada to identify opportunities to further reduce industry's methane emissions. Government's approach to methane reductions must be guided by the fundamental principle that regulatory requirements should be technically achievable, appropriately targeted at emissions sources, and support the continued safe operation of facilities. As a first step working with provinces, Canada can repurpose any unallocated amount in the Emissions Reduction Fund (ERF) – Onshore Program to support the large-scale infrastructure necessary to conserve low gas volumes from multiple operators in an effort to reduce methane emissions and support local economies.

It is recommended that the Government of Canada in relation to methane emissions:

- Working with provinces, repurpose unallocated ERF dollars to support large-scale infrastructure to conserve low gas volumes.

Budget 2023 Requests

Emissions cap

- *Reconsider adding another layer of regulation as the current regulatory framework has already driven substantial emission reductions.*
- *If an emissions cap is considered, implement realistic trajectories to pragmatically map pathways to increase certainty for large-scale investments in energy and decarbonization projects.*
- *Enable markets to ensure that cost effective opportunities are available for all, as emissions reduction projects compete with other investments and are global in nature.*
- *Leverage efficiencies across the economy avoiding a sector-by-sector approach and consider policy alternatives focused on enabling key objectives.*
- *Recognize the unique nature of the upstream sector and the key differences between conventional oil and natural gas with that of the oil sands as well as the unique technologies that will support emissions reductions.*
- *Ensure that resources can flow quickly and directly to projects that reduce emissions and support innovation, eliminating red tape from government grant programs.*
- *Ensure existing carbon pricing effectiveness is not compromised (i.e. credit market maintained, emission intensive trade exposed protection, carbon price level consistent, economy wide).*
- *Continue to work collaboratively with industry throughout 2023 to get the right policies in place for the upstream sector to drive emissions reductions.*

CCUS

- *Consider a flexible policy approach that achieves fiscal parity with the U.S. 45Q such as a production tax credit, inclusion of operating costs, or other financial policy levers, and CCFDs.*

Methane

- *Working with provinces, repurpose unallocated ERF dollars to support large-scale infrastructure to conserve low gas volumes.*

Conclusion

In conclusion, CAPP and its membership are committed to meaningful emissions reductions by 2050 to reduce GHG emissions and help Canada achieve its climate goals. It will be important that Budget 2023 help industry

[2] Based Canada's 2022 National Inventory Report to the Intergovernmental Panel on Climate Change and a global warming potential of 28. Analysis combines methane emissions associated with "oil and gas extraction as a stationary combustion source" and "oil and natural gas fugitive sources". Available at https://data.ec.gc.ca/data/substances/monitor/canada-s-official-greenhouse-gas-inventory/A-IPCC-Sector/EN_GHG_IPCC_Canada.xlsx

through the transition by removing barriers to investment in emissions reduction activities. The country should strive to maintain a level playing field with competing jurisdictions and accelerate emission reductions through an incentive-based policy approach, as opposed to a policy approach that adds costs and regulatory burden. If Canada is able to attract global capital for investment that advances decarbonization projects at scale, there are many benefits and opportunities to be realized broadly by Canadians.

Equally important for CAPP and its membership is government recognition that Canada's upstream energy sector is large and diverse. A one size fits all policy approach to emission reduction policy does not account for the differences in product, production, extraction modality, economics, and geography. We encourage government to work collaboratively with industry through 2023 to minimize the risk of unintended consequences as government seeks to implement emission reduction policies for all parts of the upstream industry.

Sincerely,

Lisa Baiton MBA, ICD.D
President and Chief Executive Officer