Intelligence MEMOS

From: Charles DeLand

To: Energy and Natural Resources Minister Jonathan Wilkinson and Environment and Climate Change Minister Steven Guilbeault

Date: November 12, 2024

Re: **INHIBITING INVESTMENT: DON'T LET THE OIL AND GAS EMISSIONS CAP LIMIT CANADA'S PROSPERITY**

Ottawa's latest climate initiative – a cap on oil and gas emissions – is like bringing an excavator to plant flowers. It's unnecessary, expensive, and likely to do more harm than good.

With more than 70 federal climate policies already in place, adding yet another layer of regulation is unnecessary. Worse, it further risks Canada's economy at a time when it may already be facing tougher competition and incoming tariffs from the US, its biggest market.

Despite several policies now encompassing oil and gas, the government doggedly plans to implement yet another one: A sector-specific cap-and-trade system in which maximum emissions quantities are set and a limited market created in which to trade them. It aims to reduce 2030 emissions by 35 percent below 2019 levels and align with economy-wide net-zero emissions by 2050.

The cap on oil and gas emissions ought to be dropped. It is redundant, inefficient, expensive, and hurts productivity.

There's a better way forward. Instead of piling on "just one more plan," the federal government should 1) calculate the full cost of Canada's climate commitments, 2) evaluate which current policies work and which don't, and 3) focus on broad-based, cross-sector, solutions that work at lowest economic cost.

Let's be clear: Canadian energy producers aren't getting a free pass on emissions. Every province already has government-approved restrictions in place. These include tough rules on methane and emissions from major facilities, particularly in the oilsands. Large-emitter plans have been in place for several years and provide a strong incentive to reduce emissions where possible while maintaining export competitiveness by giving emitters a balance of "free" allowances.

Why are oil and gas emissions still rising? Simple physics and economics. Production has increased to meet global demand, and even though emissions per barrel have dropped significantly, producing oil and gas inherently requires energy. Companies need diesel fuel for remote operations and natural gas for heat and steam in the oilsands. Despite every incentive to cut emissions – from investor pressure to government mandates – scalable, cost-effective, non-emitting alternatives simply don't exist yet.

What to do about it? Economists mainly prefer broad-based, market-oriented emissions solutions because they provide incentives to cut emissions at the least economic cost. Treating some sectors differently than others undermines that principle. If it's cheaper to cut elsewhere, the environment and the economy both win. A national cap-and-trade system might accomplish this, but jurisdictional realities and regional economic differences, among other things, have made it hard to implement. Many provincial systems do allow emissions credit trading between economic sectors.

The lack of immediately implementable technologies to reduce emissions for oil and gas producers at the desired scale means that the emissions cap essentially acts as a production cap. If the federal government continues its fixation on short-term sector-specific reductions at these levels they must come from either producing less oil and gas or capturing and storing the emissions (carbon capture, utilization, and storage, or CCUS).

The industry's main solution – a $16.5-billion carbon capture project by the Pathways Alliance – could reduce emissions by 22 megatonnes annually by 2030 without allowing production to fall. But since no competing producers globally face similar requirements, Canadian taxpayers would need to shoulder much of this burden through tax credits and other incentives. If the government grits its teeth and narrowly bears down on oil and gas, it will have to come up with taxpayer dollars to help get it done.

Lower production would be bad for Canada. Canada desperately needs productivity-boosting investment. As my C.D. Howe Institute colleagues Bill Robson and Mawakina Bafale note, in 2024, Canadian workers will likely receive only 66 cents of new capital for every dollar received by the average OECD worker, and 55 cents per dollar received by their US counterparts. Greater investment means more Canadian jobs and higher incomes. Viewed from that perspective, oil and gas is a jewel – one of the most productive sectors and our greatest export by value.

We need to export more, not less, prudently recognized by the federal government's backing of the fully operational Trans Mountain Pipeline expansion. Canadian oil and gas exporters need more of that kind of defence, especially when confronted with possible US barriers.

Climate policy should not be a game of whack-a-mole, targeting individual sectors with overlapping regulations. If we're serious about both environmental protection and economic prosperity, we need to stop digging ourselves deeper into a regulatory hole.

A better approach looks across all economic sectors to see which are cheapest to mitigate. It's time for Ottawa to admit that when it comes to climate policy, fewer but better policies could do more.

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