PATHWAYS ALLIANCE SUBMISSION TO THE 2023 FEDERAL BUDGET CONSULTATION PROCESS

October 2022

BY EMAIL

Alexandre Roger, Clerk of the Standing Committee on Finance
Tel: (613) 992-9753
E-mail: FINA@parl.gc.ca

The Pathways Alliance is pleased to offer the following submission to the House of Commons Standing Committee of Finance as part of its pre-budget consultations in advance of the 2023 federal budget.

About Pathways Alliance

The Pathways Alliance is an initiative of Canada's six largest oil sands producers: Canadian Natural, Cenovus Energy, ConocoPhillips Canada, Imperial, MEG Energy and Suncor Energy, which together operate approximately 95 per cent of Canada's oil sands production. The Pathways Alliance is working on an ambitious and actionable plan to help Canada meet both its 2030 Paris commitments and our collective 2050 net zero goal. Pathways Alliance members have already embarked on this collaborative effort and are in the process of assessing the major investments needed to achieve them. Achieving these plans will necessitate a suite of technologies that will require both private investment and public support.

Policy and Economic Issues for Consideration

Canada faces the triple challenge of reducing greenhouse gas (GHG) emissions in support of national climate goals, ensuring a reliable, affordable and secure energy supply and maintaining a strong economy. We believe Canada's oil sands sector is well positioned to support all three priorities.

The Oil Sands Pathways to Net Zero Alliance (Pathways Alliance) supports the government's goals of achieving a large absolute reduction in GHG emissions by 2030, and the goal of achieving net zero emissions by 2050.

Energy security means ensuring that Canadians and the world have access to affordable, reliable, responsibly produced energy. This in turn requires a healthy, competitive oil and gas sector that is investing in both maintaining production levels and reducing GHG emissions. As our sector decarbonizes, we believe that the oil sands can play an even bigger role in producing energy for Canada and the world. If Canadian oil sands can reduce its carbon intensity below other global sources of oil, we believe Canada should seek to increase its market share for responsibly produced, lower emissions energy, even if global market demand, as a whole, begins to decline.

The cost of decarbonization corresponding to Canada's ambition is expected to be high and will take time. Balancing climate ambition with what is feasible will be key to a successful energy transition. Importantly, Canada needs an enabling policy framework and a prerequisite competitive investment structure that will attract global capital and incentivize investment in decarbonization technologies within Canada.

Canada's Future Competitiveness

Budget 2023 must take into consideration Canada's ability to attract global capital to enable investment in decarbonization activities. Investors will prioritize jurisdictions where policy clearly defines how investments will recover costs in a predictable and sustainable manner and deliver competitive project returns.

To that end, we note that other jurisdictions – the United States in particular - are taking meaningful steps to attract global capital to deploy clean technology. The US recently passed amendments to the 45Q tax credit for carbon capture activities as defined through the *Inflation Reduction Act, 2022*. Independent analysts, such as BMO Capital Markets, estimate that the enhanced 45Q tax credits provide more than double the net value of Canada's proposed Investment Tax Credit for carbon capture, utilization, and storage and that "the Canadian Investment tax Credit (ITC) announced this spring falls far short and there remains the need for additional funding support from provinces and / or better assurances around the value of future credits to improve project returns and promote wide scale deployment."[1]

It will be important for Canada to remain in step with competing jurisdictions and key trading partners such as the United States to ensure Canadian decarbonization projects remain competitive. If we are successful in executing major decarbonization infrastructure in Canada (carbon capture and storage, hydrogen, renewables, small modular reactors, etc.) and establishing Canada as a global leader in these areas, there will be significant opportunities to export the associated technical, commercial and manufacturing expertise to a massive global market that will be hungry for such services.

Strong fiscal policy will be a prerequisite to enabling investment in Canada and to provide long term certainty. Canada needs a competitive investment structure including fiscal measures that promote investment in transformative decarbonization technologies that are needed to support Canada in meeting its climate goals, while recognizing the financial or technological risk, and provides predictable revenue sources over long payback periods to support project economics.

The following fiscal measures either support the significant upfront capital expenditures or help to offset the annual operating expenses of key enabling decarbonization technologies that have long payback periods. Importantly, these fiscal measures also help to circumvent investment challenges resulting from an uncertain policy landscape and help to establish a level playing field with competing jurisdictions that could otherwise risk competitiveness driven carbon leakage and flight of capital from Canada.

[1] BMO Capital Markets, "Canada Falling Behind in CCUS Policy, Following US Upgrade", August 22, 2022

Budget 2023 Request

1. Enhance the federal Investment Tax Credit (ITC)

Extend carbon capture, utilization and storage (CCUS) ITC eligibility to include: a) project operating expenditures, b) intangible subsurface costs including exploration and development costs in class 59 and 60, as well as c) intangible costs of securing rights to dedicated underground geological storage.

Grandfather the 2022-2030 CCUS ITC rates for post-2030 expenditures for projects that commence construction by 2032; the reduced ITC rates would remain applicable for projects that commence construction after 2032. If undue regulatory delays hamper the ability for projects to commence construction, then this grandfathering provision should be revisited to accommodate projects that have made best efforts to meet the 2032 deadline.

Increase capital cost allowance ("CCA") amortization rates for Class 57 and 58 property to align with rates applicable to specified clean energy generation and energy conservation equipment and include intangible costs of securing rights to dedicated underground geological storage in proposed class 60 which is subject to a 30% CCA rate.

2. Support operating costs, which could be met through some combination of the following:

Enhance the ITC to include project operating expenditures for a sufficient period, as noted above.

Establish a production tax credit (PTC). A PTC is another form of a tax credit that would be based on a $/T for captured CO_2 that is sequestered over time. Similar to the enhanced ITC, a PTC would also provide a predictable revenue source to support to the project through the operational phase. A PTC could be developed through the ITC legislation or separately.

Establish carbon contracts for difference (CCfD) offtake agreements. CCfDs can provide guarantees on credit value over a period of time. We note that a guarantee on credit volume and duration is equally important to a guarantee on credit price. A carefully designed CCfD offtake agreement can also mitigate the potential distortions to the carbon pricing markets.

Conclusion

The Pathways Alliance was created to be part of Canada's net zero by 2050 solution. As our sector does its part to reduce GHG emissions and help Canada achieve its climate goals, it will be important that Budget 2023 help industry through the transition by removing barriers to investment in decarbonization 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.