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Submission to Environment and Climate Change Canada

Response to Canada Gazette, Part I, Volume 158, Number 45: Oil and Gas Sector Greenhouse Gas Emissions Cap Regulations

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Introduction:

The release of the oil and gas sector greenhouse gas emissions cap draft regulation was a much needed step in the right direction for Canada. It brings Canada one step closer to limiting and reducing oil and gas pollution, which is fueling climate change.

Greenhouse gas (GHG) emissions from the oil and gas sector in Canada have continued to increase over the years and now account for nearly a third of Canada's domestic emissions.¹ In fact, the increase in oil and gas emissions have wiped out emissions reduction made by other sectors leading Canada to be once again off track for meeting its climate targets.²

The oil and gas sector greenhouse gas emissions cap was first promised in 2021 by Prime Minister Trudeau.³ Over the last three years, this regulation has faced numerous delays, while GHG emissions from the oil and gas sector have continued to increase. **The Government of Canada must move quickly to release the final regulations of the oil and gas sector greenhouse gas emissions cap as soon as possible, before the end of the current federal mandate.**

Although the release of the draft regulation is a significant step in Canada's effort to limit and reduce pollution from the oil and gas sector, there are some concerning elements proposed. Environmental Defence makes the following recommendations to strengthen the oil and gas sector greenhouse gas emissions cap.

- **Target and Level of Ambition:** As it stands, the proposed emissions reduction target is much lower than Canada's 2030 target, which is 40 - 45 per cent emissions reduction by 2055 levels.⁴ Worse still, it is even lower than the target set out by the federal government in the Emissions Reduction Plan.⁵ The current proposed target will enforce a GHG emissions reduction target of only 21 per cent, without compliance flexibilities, from 2026 levels by 2032. This will only lead to a meager emissions reduction of 13.4 MT under the emissions cap regulation, a far cry from the level of emissions reductions that are needed. The current design of regulation will ensure that the oil and gas sector will not be required to achieve its fair share of emissions reductions, and other sectors, households and businesses in Canada will continue to bear the unfair burden of

¹ Government of Canada (2024). National Inventory Report 1990 –2022: Greenhouse Gas Sources And Sinks in Canada. Available: https://publications.gc.ca/collections/collection_2024/ecccc/En81-4-2022-1-eng.pdf

² Office of the Auditor General in Canada (2024). Canadian Net-Zero Emissions Accountability Act—2024 Report. Available: https://www.oag-bvg.gc.ca/internet/English/parl_cesd_202411_07_e_44576.html

³ Office of the Prime Minister (2021). Prime Minister Trudeau announces enhanced and ambitious climate action to cut pollution at the COP26 summit. Available:

<https://www.pm.gc.ca/en/news/news-releases/2021/11/01/prime-minister-trudeau-announces-enhanced-and-ambitious-climate>

⁴ United Nations Framework Convention on Climate Change (2021). Canada's 2021 Nationally Determined Contribution Under the Paris Agreement. Available:

https://unfccc.int/sites/default/files/NDC/2022-06/Canada%27s%20Enhanced%20NDC%20Submission1_FINAL%20EN.pdf

⁵ Government of Canada (2022). Canada's 2030 Emissions Reduction Plan. Available:

<https://www.canada.ca/en/services/environment/weather/climatechange/climate-plan/climate-plan-overview/emissions-reduction-2030/plan.html>



achieving additional emissions reductions. This is also far lower than the recommendation made by the International Energy Agency (IEA). The IEA has made it clear that oil and gas companies must reduce their GHG emissions by 60 per cent from current levels, by 2030, to keep the rise in global average temperatures to below 1.5°C.⁶ Furthermore, the oil and gas sector greenhouse gas emissions cap draft regulation proposes that the baseline year for the GHG emissions from the oil and gas sector should be 2026, and makes the assumption that oil and gas emissions will be lower in 2026 as compared to emissions in 2019. This assumption relies on the oil and gas sector reducing their emissions over the next two years because of additional regulations, such as the methane regulations as well as the industrial carbon pricing mechanism. However, the Canadian Climate Institute published an analysis⁷ on Canada's 2023 GHG emission levels, which shows that emissions from the oil and gas sector continue to increase.

Recommendations:

- Environmental Defence recommends that the emissions reduction target be strengthened so that it is in line with Canada's Nationally Determined Contribution (NDC) targets. This would mean that the target must match Canada's 2030 emissions reduction target and ensure that oil and gas emissions are reduced by 40 - 45 per cent from 2005 levels.
 - Environmental Defence recommends that the federal government return to using 2019 levels as the baseline year for setting targets, rather than 2026. This is because it is not a given that oil and gas emissions will decline from current levels to 2026, given that the sector's emissions have continued to increase. Moving to 2019 as the baseline year would ensure that the cap is not weakened if oil and gas emissions are not 8 per cent lower in 2026, as is being assumed in the draft regulation.
 - The inclusion of interim annual targets for each compliance period is an important metric to ensure that each operator is on track to comply with their allocations. Environmental Defence recommends that the federal government continue to include interim targets in the final version of the oil and gas sector greenhouse gas emissions cap regulations.
 - We recommend that the Government expand covered activities to include on-site electricity generation where electricity is used by the producing facility. This is important to cover a compliance exemption left in s.12(1) of the Clean Electricity Regulations.
- **Trajectory:** The proposed draft regulation lacks future targets beyond the first compliance period, which goes from 2030-2032. The lack of long-term targets creates

⁶ International Energy Agency (2023). Emissions from Oil and Gas Operations in Net Zero Transitions. Available: <https://www.iea.org/reports/emissions-from-oil-and-gas-operations-in-net-zero-transitions>

⁷ Canadian Climate Institute (2024). Early Estimate of National Emissions. Available: <https://440megatonnes.ca/early-estimate-of-national-emissions/>



uncertainty around Canada's trajectory to meeting its net-zero by 2050 climate goals. A clear, ambitious trajectory will provide guidance for the oil and gas sector, enabling operators to align their investments with Canada's climate goals and facilitating a predictable transition pathway. In contrast, The Government of Canada has indicated that they will not set any future targets until after 2032, which is much too late to ensure the urgency in achieving Canada's climate goals.

Recommendation:

- Environmental Defence recommends establishing a clear trajectory to achieve zero emissions from the oil and gas sector by 2050. This should be developed a year after the regulations are introduced, by 2026. In addition, the legal upper bound should also decline progressively along the same trajectory as the emissions cap for each subsequent compliance period. A prescribed emissions reduction trajectory would not only enhance policy certainty but also encourage innovation and investment in decarbonization efforts.
 - The final regulation must include an explicit regulatory requirement for achieving net-zero by 2050. Canada's goal to achieve net-zero by 2050 is legislated by the Canadian Net-Zero Emissions Accountability Act (NZEAA), which means that all activities covered under the emissions cap regulation are obligated to achieve net zero emissions by 2050 under the NZEAA.
- **Timeline:** The proposed regulatory timeline is much slower than what is needed to mitigate the worst impacts of climate change. Canadians across the country are forced to deal with the devastating impacts of climate disasters along with the rising costs of basic needs because of climate change. As proposed in the draft regulation, oil and gas operators will not have to reduce their GHG emissions under the oil and gas sector greenhouse gas emissions cap until the first compliance period, between the years of 2030 - 2032. This effectively means that the proposed regulation will not play a meaningful role in achieving Canada's 2030 targets. Canada is already dangerously off track from meeting its 2030 emissions targets, and without addressing the largest source⁸ of GHG emissions, Canada risks falling behind even further.

Recommendations:

- Recognizing that there is a reporting gap within the sector for small emitters, Environmental Defence recommends implementing a staggered approach for the sector to comply with the oil and gas sector greenhouse gas emissions cap. Large emitters, facilities that emit more than 10 000 CO₂e, should be required to comply much earlier as the emissions data is already available under the National Pollutant Release Inventory. Using a staggered approach will ensure

⁸ Government of Canada (2024). National Inventory Report 1990 –2022: Greenhouse Gas Sources And Sinks in Canada. Available: https://publications.gc.ca/collections/collection_2024/eccc/En81-4-2022-1-eng.pdf



that large facilities can contribute towards Canada's 2030 target, increasing the chances of Canada meeting its climate targets for the first time. Environmental Defence recommends that large operators should be required to comply with the cap starting January 1st, 2026.

- For small operators, the reporting obligations should begin January 1st, 2026 to address the knowledge gap that currently exists on their GHG emissions. This would mean that for the initial compliance period for large operators, which based on Environmental Defence's recommendation would begin from 2026 - 2029, small operators would report on their GHG emissions so that they can begin complying with the oil and gas sector greenhouse gas emissions cap starting with the second compliance period starting in 2029.
- **Compliance flexibility mechanisms:** The current design of the draft regulations includes a variety of compliance flexibilities, which allow the oil and gas sector to escape their responsibility of achieving direct emissions reductions from their own operations. As it stands, oil and gas operators can excuse up to 20 per cent of their GHG emissions through the use of compliance flexibilities. The purpose of the oil and gas sector greenhouse gas emissions cap should be to enforce reductions in emissions directly from oil and gas operations. The two most concerning loopholes that are being proposed in the draft regulation are the use of carbon offsets and the decarbonization fund. Carbon offsets weaken the emissions cap regulation because they allow oil and gas operators to avoid making direct emissions reductions from their own operations in favor of funding emissions reduction projects elsewhere. Many offset projects have failed to produce permanent and additional emissions reductions⁹ and in some cases, even lead to an increase in total emissions.¹⁰ Indigenous Peoples have also raised valid concerns of how land-based offsets perpetuate colonization through land grabs, and transfer responsibility of emissions reductions from wealthy polluters to low-income jurisdictions.¹¹ The decarbonization fund unfairly creates a pay-to-pollute system and will award oil and gas operators by offering them a way out without achieving direct emissions reductions from their operations, shifting the onus onto the government instead. As proposed, oil and gas operators can excuse up to 10 per cent of their annual GHG emissions by paying into a fund, which is ultimately returned back to the sector to support their decarbonization. Currently, there are no set rules around the decarbonization fund, which means that the fund could potentially be used for technologies like carbon capture and storage (CCS), which after decades has failed to reduce any meaningful emissions despite costing public taxpayers billions of dollars.¹²

⁹ Climate Analytics (2023). Why offsets are not a viable alternative to cutting emissions. Available:

https://ca1-clm.edcdn.com/assets/why_offsets_are_not_a_viable_alternative_to_cutting_emissions.pdf?v=1697123932

¹⁰ Carbon Brief (2023). Mapped: The impacts of carbon-offset projects around the world. Available:

<https://interactive.carbonbrief.org/carbon-offsets-2023/mapped.html>

¹¹ Indigenous Climate Action (2021). Decolonizing Climate Policy in Canada Report from Phase One. Available:

https://static1.squarespace.com/static/5e8e4b5ae8628564ab4bc44c/t/6061cb5926611066ba64a953/1617021791071/pcf_critique_FINAL.pdf

¹² Environmental Defence (2022). BUYER BEWARE: Fossil Fuels Subsidies and Carbon Capture Fairy Tales in Canada. Available: <https://environmentaldefence.ca/wp-content/uploads/2022/03/Buyer-Beware-FFS-in-2021-March-2022.pdf>



Similarly, hydrogen - especially fossil fuel produced hydrogen, is a problematic alternative as it can be just as polluting as fossil fuels.¹³ Another major problem with the decarbonization fund is the risk of double counting emissions reductions, which occurs when double the credit is given for one unit of emissions reductions. If emissions reductions in the oil and gas sector, funded by the decarbonization fund, are also counted by operators for achieving their allowances, the result would be double counting of the same reductions – which would undermine the regulation's credibility.

Recommendations:

- Environmental Defence recommends that the total percentage of compliance flexibilities available to oil and gas operators be reduced to 10 per cent of an oil and gas operator's absolute annual GHG emissions. Furthermore, the total percentage of permitted compliance flexibility should decline progressively over time to concretely hold the oil and gas sector to a steady decline in direct emissions from oil and gas operations.
- Environmental Defence strongly recommends that the federal government includes no offsets in the oil and gas sector greenhouse gas emissions cap regulation. The inclusion of offsets undermine the credibility and effectiveness of this regulation as it will allow oil and gas operators to fund offset projects elsewhere instead of reducing GHG emissions from their own operations. If the Government of Canada chooses to include offsets as a compliance flexibility, then Environmental Defence recommends that the total percentage of offsets available to oil and gas operators be reduced to 10 per cent of an oil and gas operator's absolute annual GHG emissions.
- If the Government of Canada chooses to include offsets, then it must also ensure that the available offsets for the oil and gas sector meet the strictest standard that guarantee permanent and additional emissions reductions. The monitoring of the available offsets must be made through a third party, with publicly available reports each year. If at a future date, it is determined that the offsets used by an operator have not led to the promised emissions reductions, then the operator must face the same penalties as an operator that failed to comply with the emissions cap.
- Environmental Defence recommends that an offset fund, which has been excluded in the draft regulation, should not be re-considered as another compliance flexibility for the oil and gas sector.
- Environmental Defence strongly opposes the inclusion of a decarbonization fund. However, if the federal government decides to move forward with the decarbonization fund, it must not exceed the total 10 per cent limit of compliance flexibilities as recommended in the draft regulations, and it should include the following components:

¹³ Ilissa B. Ocko and Steven P. Hamburg (2022). Climate consequences of hydrogen emissions. Available: <https://acp.copernicus.org/articles/22/9349/2022/>



- Prioritizing the phase out of the decarbonization fund as a compliance flexibility after the 2nd compliance period under the oil and gas sector greenhouse gas emissions cap regulation.
 - Only fund proven emissions reduction technologies in the operations of the oil and gas sector, which can be accomplished in a short period of time. Examples of such measures include electrification of oil and gas operations and fuel switching to renewable energy.
 - The cost per tonne to pay into the decarbonization fund must be increased to match the projected social cost of carbon on Canadians in 2030.¹⁴ This will ensure that the oil and gas operators pay their fair share into the decarbonization fund with payments that accurately reflect the cost paid by Canadians for GHG emissions.
 - The rules for the decarbonization fund must ensure that there will be absolutely no risk of double counting emissions reductions under the fund and the oil and gas sector greenhouse gas emissions cap regulation.
 - Where possible, the fund should support a just transition for the re-training of workers and communities from the fossil fuel sector to the renewable energy sector.
- **Internationally Transferred Mitigation Outcomes (ITMOs):** The exclusion of ITMOs in the draft regulations was a positive step. ITMOs are especially concerning as there are no rigorous set of rules that can verify that the use of ITMOs will be credible and additional.

Recommendation:

- Environmental Defence urges the Government of Canada to continue excluding the use of ITMOs from the final version of the regulation. Although ITMOs have been excluded from the draft regulation, the federal government is still considering its inclusion in the final version of the oil and gas sector greenhouse gas emissions cap. Recently, there has been a concerning narrative that suggests that Canada can use ITMOs to meet its 2030 target by exporting LNG to other nations. This is a flawed idea as producing and transporting LNG, an emissions-intensive process which leads to methane leakage, can not be counted on to achieve actual emissions reductions globally as Canadian LNG can just as easily be used to displace renewable energy as coal.¹⁵

¹⁴ Government of Canada (2023). Social cost of greenhouse gas emissions. Available:

<https://www.canada.ca/en/environment-climate-change/services/climate-change/science-research-data/social-cost-ghg.html>

¹⁵ Clean Energy Canada (2024). An uncertain future. Available: <https://cleanenergycanada.org/report/an-uncertain-future/>



- **Allocations and incentivizing early reductions:** The current design of the oil and gas sector greenhouse gas emissions cap proposes free allocation of emissions allowances to oil and gas operators. Free allocations provide oil and gas operators a free right to pollute and go against the Polluter-pays principle, a key guiding principle for Canada Environmental Protection Act.¹⁶ Furthermore, auctioning allowances can provide the federal government much needed revenue to support climate-affected communities along with communities impacted by the energy transition. Auctioning allowances also incentivizes companies to implement quicker and cheaper reductions. The current design for distributing allocations also incentivizes oil and gas operators to delay reducing their GHG emissions to receive more allocations, as the federal government has proposed to use a three-year rolling average of production to determine how many allowances each operator will receive - the higher the average, the more allowances an operator receives.

Recommendations:

- Environmental Defence recommends that instead of free allocations, the Government of Canada should auction off the emissions allowances. However, if emissions allowances are allocated freely during the first compliance period, then the current allocation formula must be changed so that allocations are prioritized for operators that have low-emissions intensity and operators that are early adopters of decarbonization measures, in order to reward pre-2026 reductions. Making this a fundamental requirement of distributing allocations will encourage early decarbonization investments from the oil and gas sector and reduce the risk of oil and gas operators delaying decarbonization to increase the number of allocations they receive for the first compliance period. Currently, there are no safe guards in place in the draft regulations to prevent oil and gas operators from delaying decarbonization until after 2026, which jeopardizes Canada from achieving its 2030 climate targets.
- Similar cap and trade programs in other jurisdictions, such as in Quebec,¹⁷ California¹⁸ and the European Union¹⁹ all have transitioned to auctioning allowances. For the auctioning of allocations, Environmental Defence recommends the following design features:
 - i. The auction needs a price floor.
 - ii. Use proceeds to support climate-affected communities and communities impacted by the energy transition.

¹⁶ Government of Canada (2005). Canadian Environmental Protection Act at a glance. Available: <https://www.canada.ca/en/environment-climate-change/services/canadian-environmental-protection-act-registry/general-information/fact-sheets/at-a-glance.html>

¹⁷ Ministère de l'Environnement, de la Lutte contre les changements climatiques, de la Faune et des Parcs (2024). The Carbon Market. Available: <https://www.environnement.gouv.qc.ca/changements/carbone/Ventes-encheres-en.htm>

¹⁸ California Air Resources Board (2024). Cap-and-Trade Program. Available: <https://ww2.arb.ca.gov/our-work/programs/cap-and-trade-program>

¹⁹ European Union (2024). Auctioning of Allowances. Available: https://climate.ec.europa.eu/eu-action/eu-emissions-trading-system-eu-ets/auctioning-allowances_en#:~:text=From%202021%20onwards%2C%2057%25%20of,cap%2C%20published%20in%20November%202020%20.



- iii. The allowances can also be auctioned by subsector to ensure there is equity between smaller and larger oil and gas companies.
 - iv. New entrants should have to purchase allowances from pre-existing producers who have excess credits. There should be no reserve of allowances, as this would incentivize growth of the sector and weaken the oil and gas sector greenhouse gas emissions cap. It could also lead to potential breaching of the allowance levels.
- **New Facility Compliance:** In the draft regulation, the federal government proposes a delay in compliance for new facilities emitting over 10,000 CO_{2e} annually, allowing them to avoid complying with the oil and gas sector greenhouse gas emissions cap until their fifth year of operation, although these facilities must report their GHG emissions during their first four years. However, the risk is that by not including these new emissions under the cap, that the level of emissions exceeds the target during the years that the new facility is not bound by the regulation. As it currently stands in the draft regulation, a new facility's GHG emissions are deemed to be zero until its first year of compliance under the oil and gas sector greenhouse gas emissions cap.

Recommendations:

- Environmental Defence recommends against excusing a new facility's total GHG emissions as zero during its reporting years. Instead, the federal government should lower the total number of allocations available to the entire sector by the same amount of GHG emissions that a new facility emits. This means that after each annual reporting cycle for a new facility, the federal government must readjust the total available allocations to ensure that the cap level is not exceeded each time a new facility comes online.
- Environmental Defence recommends modifying the proposed rules to require new facilities exceeding the 10,000 CO_{2e} threshold to comply with the oil and gas sector greenhouse gas emissions cap starting in their fourth year, following three years of emissions reporting. This adjustment would balance operational lead times with the urgent need for tangible reductions.
- Environmental Defence commends the inclusion of a pro-rated system for total allowable emissions, ensuring the oil and gas sector greenhouse gas emissions cap is maintained even as new facilities come online.

Enforce strong compliance mechanisms that result in real and tangible emissions reductions from the oil and gas sector. Penalties or fines for not complying with emission allowances should be significant enough to serve as a strong deterrent rather than allow oil and gas companies to internalize the penalties as a cost of doing business. Compliance mechanisms that are not financial should also be considered, for example in the event that an oil and gas



operator fails to comply with an emissions allowance, that operator must be required to pause their operations until appropriate measures are undertaken that can reduce their emissions in line with their allocations. Additionally, a regulatory review process should be conducted by validated third-party operators to ensure that the oil and gas sector greenhouse gas emissions cap is in fact working as intended and that all oil and gas operators are following the entire process, from reporting emissions to complying with the allocations. This information should be transparent and made available to the public. In addition, the regulations should require auditing of verification reports from different verification bodies to ensure reporting is accurate across both verification bodies and operators.

Uphold Indigenous Rights and Authority by ensuring that the oil and gas sector greenhouse gas emissions cap is aligned with a full and sincere implementation of the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP). This includes ensuring securing free, prior and informed consent from each impacted Indigenous nation.