December 17, 2014

The Honourable Jim Prentice
Premier of Alberta, President of Executive Council, Chair of Planning and Priorities, Minister of Aboriginal Relations, Minister of International and Intergovernmental Relations
Government of Alberta
307 Legislature Building
10800 - 97 Avenue
Edmonton, Alberta T5K 2B6

Sent by email to: premier@gov.ab.ca

Re: Renewing Alberta's Climate Change Framework

Dear Premier:

With approximately C$6 billion in assets under management, NEI Investments' approach to investing incorporates the thesis that companies integrating best environmental, social and governance (ESG) practices into their strategy and operations will build long-term sustainable value for all stakeholders and provide higher risk-adjusted returns to shareholders. Alberta-based companies represented over 13% of our total worldwide equity holdings at the time of writing. Our holdings include companies that operate in the conventional and unconventional energy sectors in Alberta, as we believe these resources can be developed responsibly in a way that provides returns to all stakeholders.

We are writing today to support the government in its stated intention to update its climate policy and strongly agree that this should be a priority area for Alberta policy development.[1] We see a time-sensitive opportunity to enhance Alberta's reputation as a world class jurisdiction for energy development.

We have led investors previously in submitting comments to the 2011 public consultation held by the Alberta Environmental Monitoring Panel (AEMP)[2], and later in writing to the Federal and Alberta governments to call for timely implementation of the recommendations of both the AEMP and the Environment Canada Integrated Oil Sands Monitoring Plan.[3] In those letters we discussed investor-perspective concerns about environmental and social impacts from oil sands development, and the need to understand, acknowledge and mitigate the impacts in a timely fashion if companies were to avoid serious risks to their long-term value. We have been pleased to see ongoing implementation of an expanded and scientifically-credible monitoring system and commend both levels of government on this progress.[4]

[1] We wrote to the Government of Alberta in 2013 to express support for action on updating the Specified Gas Emitters Regulation (SGER). The present letter reiterates some points made on that occasion.
http://www.neiinvestments.com/documents/PublicPolicyAndStandards/2013/NEI%20Comments%20on%20Specified%20Gas%20Emitters%20Regulation.pdf
[2] NEI Investments (2011). Re: Alberta Environmental Monitoring Panel: World-Class Environmental Monitoring for the Oil Sands Region
http://www.neiinvestments.com/documents/PublicPolicyAndStandards/2011/Investors%20Oil%20Sands%20Monitoring.pdf
[3] NEI Investments (2011). Re: Implementation of a World-Class Monitoring System for the Oil Sands Region
http://www.neiinvestments.com/documents/PublicPolicyAndStandards/2011/Oil%20Sands%20Monitoring%20Implementation_Investor%20Letter.pdf
[4] http://www.jointoilsandsmonitoring.ca/

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It is our understanding that the determination of a new climate change framework for Alberta is imminent.[5] It is with this in mind that we provide our investor perspective on the issue, and note that getting the framework right is of utmost performance. The current economic situation will undoubtedly complicate the process, but a robust policy must be focused on the long-term benefits at stake.

As an investor in companies operating in Alberta, carbon policy is a material topic for our portfolio. We believe that the implementation of a fair, robust and credible carbon policy will be critical to the performance of the energy sector and key to the diversification of Alberta-based investment opportunities writ large. We strongly agreed with the 2011 findings of the Premier's Council on Economic Strategy that the optimization of Alberta's natural resources means using the profits from today's development to fuel the diversification of opportunities tomorrow.[6]

Our argument rests largely on two key points: market access and the pace and scale of innovation.

In our opinion it is likely that at some point in the near future, all fossil fuels will be judged by the market based on their climate change impact. This impact will be defined not only by the actual greenhouse gas emissions associated with the production and use of the fossil fuel, but also by whether the producers of the fossil fuel are paying for the externalities of its production (i.e. paying a price on carbon). In the case of Alberta's oil sands, this scenario is not hypothetical. Rather, oil sands producers already face market access issues based, at least in part, on carbon footprint. We see these pressures only increasing. While recognizing the immediate economic challenges, we believe that over the longer term the additional costs incurred by oil sands producers from an increased carbon price would likely be more than offset by a reduction in the bitumen discount through increased market access.[7] This math is compelling to us.

The case for increased innovation is as compelling. The Climate Change Emissions Management Corporation (CCEMC) is a good step towards the transformation that will be achieved through investing in climate change solutions. Such investments not only help Alberta move towards its goal of economic diversification, but they also make the energy industry itself more competitive. However, we believe both the scale of investment and the ambition of the fund should be enhanced. The landscape is changing dramatically, and the pace and scale of innovation needs to increase significantly. A meaningful price on carbon, assuming the same compliance mechanisms are in place as under the current SGER, will greatly increase the funds available for investing in the technologies and companies of tomorrow. We would prefer to see this innovation occur in Canada, rather than elsewhere.

On the topic of innovation, we would like to highlight an opportunity that we believe has not received enough attention. In our dialogues with the energy companies we hold, in particular companies operating in the oil sands, we are pushing for development of robust strategies for diversification. Many oil and gas companies are ideally positioned to take a leading role in the future low-carbon energy system, given their access to capital and sizable cash flows, experience with high-risk technology development, complex project management skills and an overall appetite for risk. To be clear, we are not advocating for oil sands companies to become renewable energy companies overnight. However, we do see commitment to investment in this area as a relatively low-cost hedge with tremendous upside potential.

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[5] http://calgaryherald.com/news/politics/prentice-says-oil-and-gas-climate-change-rules-cant-be-allowed-to-impact-economy
[6] Premier's Council for Economic Strategy (2011). Shaping Alberta's Future. http://alberta.ca/AlbertaCode/images/ShapingABFuture_Report.pdf
[7] The argument that increased pipeline capacity and market access will lead to substantial price increases for Canadian crude is well illustrated in the following paper from the University of Calgary's School of Public Policy: http://policyschool.ucalgary.ca/sites/default/files/research/mmoore-oilmarket.pdf

We would urge Alberta to consider how its new framework could actively encourage this kind of investment. Given a choice between paying into a compliance fund and providing direct investment capital to a potentially lucrative opportunity, we feel that most companies would choose the latter. From Alberta's perspective, this would help to build the narrative of today's resource exploitation fueling tomorrow's low-carbon energy system.

NEI does not advocate for a specific price on carbon, though we do have a perspective on carbon pricing levels in general. For several years we have been requesting that energy companies in our portfolio perform shadow carbon pricing for their projects to ensure that these investments would be safe in a future with a significant price on carbon. This practice has spread to become an industry norm among major oil and gas companies, evidenced in a recent study by Sustainable Prosperity that found energy companies operating in Canada were utilizing an average shadow carbon price range of C$15/tonne to C$68/tonne.[8] While this was a study of just 10 companies, the findings are in line with our own research.

The message from both conventional and unconventional oil and gas companies that have undertaken shadow pricing analysis has been consistent: not one has pointed to a material impact on profitability that would endanger the viability of projects. We would suggest that the Government of Alberta keep this in mind as it negotiates a new cost of carbon with industry. Unless companies have been deliberately misleading investors – and we do not believe they have – there is room for the government to increase the cost of carbon while still allowing for responsible energy development. In fact, it is our opinion that future prosperity depends in part on the implementation of an increased cost of carbon that can withstand international scrutiny. This means that not only must the price be substantial; it must be seen as substantial by key stakeholders.

Lastly, we agree with the International Monetary Fund's assessment that carbon pricing policies should be credible, flexible, broad-based and equitable.[9] We would stress that being equitable does not necessarily mean having the same rules or objectives regardless of the sector. Equitable treatment would allow for recognition that the unique characteristics of the utility, natural gas and oil sands sectors warrant unique approaches. It would also mean recognizing that Alberta's key emissions reduction opportunities lay in electricity generation.

In conclusion, we commend the Government of Alberta again for its efforts to raise the bar for environmental performance in the energy sector. We reiterate our support for the development of a robust and credible carbon policy framework that supports market access and innovation, and that will benefit the industry in the long term. If you have any questions regarding this letter, please contact **Jamie Bonham, Manager Extractives Research & Engagement, NEI Investments (**jbonham@neiinvestments.com **604-742-8328).**

Sincerely,
NEI Investments

John Kearns
Chief Executive Officer

Robert Walker
Vice President, ESG Services & Ethical Funds

8 http://www.sustainableprosperity.ca/dl976&display
9 http://www.imf.org/external/np/exr/facts/enviro.htm

CC:
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