July 24, 2017

Mark Cauchi
Executive Director
Oil, Gas and Alternate Energy Division
Energy and Transportation Directorate
Environmental Stewardship Branch
Environment and Climate Change Canada
351 Saint-Joseph Boulevard
Gatineau, Quebec K1A 0H3

Sent by email to: ec.methane-methane.ec@canada.ca

Re: Regulations Respecting Reduction in the Release of Methane and Certain Volatile Organic Compounds (Upstream Oil and Gas Sector)

Dear Mr. Cauchi:

We are writing to provide comments on the proposed *Regulations Respecting Reduction in the Release of Methane and Certain Volatile Organic Compounds (Upstream Oil and Gas Sector)* ["the proposed Regulations"].[1] We strongly support the Government of Canada's focus on reducing fugitive and venting emissions of methane and other hydrocarbons from the upstream oil & gas sector. We agree that methane emission reductions from the sector will be a critical component in helping Canada meet its ambitious climate change goals and commend the Federal Government for showing leadership on this front.

With approximately C$6 billion in assets under management, NEI's approach to investing incorporates the thesis that companies can mitigate risk and take advantage of emerging business opportunities by integrating best Environmental, Social and Governance (ESG) practices into their strategies and operations. In practice, this means that our investment process involves the analysis of key ESG information to inform our actions as a fiduciary, from the decision to invest (or not invest) in corporate securities to our proxy voting and corporate engagement activities once we are invested. It is in this light that we provide the following comments.

We are committed, long-term investors in Canada's energy sector and have a material stake in several of the companies that will be impacted by the proposed Regulations. It is our belief that methane reductions represent the most cost-effective opportunity for the sector to reduce its greenhouse gas (GHG) emission footprint and have been actively engaging companies in our portfolio to pursue opportunities in this space. We also believe that companies that pursue best practices in managing their methane emissions are reducing key risks, making them a more attractive investment in the long run. At the same time, we believe that robust regulations will support the growth of companies focused on providing the technologies and services to reduce

[1] http://www.gazette.gc.ca/rp-pr/p1/2017/2017-05-27/html/reg1-eng.php#reg

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methane emissions, creating further investment opportunities.[2] Finally, in regard to the energy transition opportunities for natural gas, we agree with the International Energy Agency that the credibility of natural gas to play a role "fundamentally depends on minimizing [methane] emissions."[3]

In general, we believe the proposed Regulations are a welcome improvement to the status quo that will roughly align us with current practice in the U.S. and potentially allow Canada to meet its target of a 40-45% reduction in methane emissions. We do however have specific comments and recommendations that we feel would strengthen the proposed Regulations:

1. Provide incentives for affected companies to comply with the regulations ahead of schedule.
2. Provide incentives for companies currently exempt to comply with the regulations voluntarily.
3. Require public company-level reporting to allow investors to assess performance.
4. Ensure transparency on progress against national reduction targets.
5. Ensure transparency and consistency on provincial equivalency agreements.
6. Ensure the "potential to emit" standard captures all significant emitters.

Regulatory versus Market-Based Approach

In general, we agree with the decision to follow a regulatory approach to address methane emissions (versus a voluntary or market-based approach). A regulatory approach is simpler to enforce, provides certainty for companies, and can provide certainty for other stakeholders that is important for ensuring ongoing social license to operate. However, we do believe there is merit in assessing whether there are any opportunities to use market-based incentives to increase the uptake of best practices in emission reduction.

Specifically, we are struck by the government's assessment that the average cost incurred by the proposed Regulations (2018-2030) is \$16/tonne CO^2e. Once the economic benefit derived from the conserved gas is included the net cost is \$10/tonne. We contrast this with the federal government's proposed price on carbon in 2023 (when all of the proposed Regulations would come into effect) of at least \$50/tonne. The cost-effectiveness of the proposed methane reductions appears to offer a compelling opportunity.

We believe there are opportunities to drive further reductions through the use of incentives, while also allowing companies to achieve more cost-effective reductions. We note that the deadlines for implementing the proposed Regulations were adjusted to provide companies time to adjust to compliance (2020 and 2023,

[2] The Methane Emissions Leadership Alliance notes that there are more than 170 Canadian companies providing methane emissions management solutions and 80% expected job growth in the next 12-18 months as a result of methane regulations. http://nebula.wsimg.com/66a97d89a3e3a07982edd10c0783d812?AccessKeyId=11FAD840D32A2D9CF9F1&disposition=0&alloworigin=1
[3] Faith Birol, "World Energy Outlook Special Report: Energy and Climate Change." International Energy Agency. IEA, June 15, 2015, *available at* https://www.iea.org/publications/freepublications/publication/WEO2015SpecialReportonEnergyandClimateChange.pdf.

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depending on the specific regulation). While we understand the rationale for this approach, we are concerned the delay in implementation could lead to missed opportunities in methane reductions. Specifically, the sooner companies meet or exceed the proposed regulations, the greater the emission reductions. The greater the emission reductions, the more room for growth in the energy sector while still staying within Canada's climate targets. The federal government, in conjunction with the provinces, should consider how it could incent companies to meet or exceed the proposed Regulations before the compliance deadlines. In fact, consideration should also be given to how to incent companies to exceed the proposed Regulations once they are in effect.

This would entail some level of integration into the current provincial and federal carbon pricing systems (through some form of offsets or credits) for those companies whose facilities are covered by both systems (i.e. methane regulations and carbon pricing). If companies are able to create significant reductions before they are mandated to do so, it would be reasonable to allow them to use these reductions as a credit for the carbon pricing system they face (since methane emissions are not covered by any of the current or proposed carbon pricing mechanisms). Likewise, for the companies with facilities that would be exempt from the proposed methane regulations (e.g. emitting under 60,000 m^3 per year) but face an existing or proposed carbon pricing mechanism, there should be a way to incent voluntary participation in adopting the methane regulations.

While this would add a layer of complexity it would utilize the strengths of both the regulatory and market approach and would ultimately lead to greater reductions. From our perspective as an investor, experience tells us that companies are far more likely to take chances on implementing new technologies or systems if there is an incentive in place to offset the risks that come with change. Further, once companies find success in implementing innovative new approaches, there is a virtuous effect that leads to even greater opportunities for increasing efficiency or reducing impacts across the company – changes that often occur without any need for further external incentives.

<u>Disclosure and Transparency</u>

It is critical to responsible investment processes that investors should be able to access information on the corporate environmental, social and governance (ESG) policies and performance of the companies in which they seek to invest, as well as financial information. In regard to performance on methane emissions management, investors would be interested in high-level information regarding compliance and general performance on methane emissions.

Currently, the proposed Regulations note that operators will have to keep up-to-date records on all of their compliance obligations, but there does not seem to be a plan for a public reporting requirement as far as we can ascertain. We understand that the regulator is looking to ease the administrative burden of the proposed Regulations and we support that approach in principle. However, we believe that basic compliance performance information would not be onerous to collect and would give investors the ability to assess company performance on a key issue. For example, Alberta's annual reporting in regard to corporate performance against *Directive 060* is a useful resource by which investors can assess the relative efficiency of

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producers and assess long-term performance trends.[4] The federal government should consider ways to provide corporate compliance data (including emissions measurement data) in a transparent and open manner at the individual producer level.

At the national level, we note that the proposed Regulations are estimated to result in a 21 megatonne reduction in methane emissions in 2025, a reduction of 41% below 2012 levels. We believe that ongoing transparency regarding whether this estimate is accurate, and whether compliance rates are keeping us in line with this target, is very important. As such we recommend that the government commit to some form of annual reporting against the 40-45% reduction target. Currently it is not clear that the regular review and analysis of key performance indicators (as discussed in the proposed Regulations) would be available publicly.

On a related note, the proposed Regulations allow for equivalency agreements where a province has set up its own methane reduction framework. We agree that avoiding overlapping or contradictory regulations should be a priority, and support this approach. However, we believe that there should be a clear accounting of how provincial standards will meet the federal expectation of equivalency in order to ensure consistency with the federal methane targets and fairness across jurisdictions.

Regulatory coverage

The proposed Regulations have been crafted to recognize the unique attributes of the Canadian energy sector – namely, the prevalence of heavy oil operations. We agree that the Canadian heavy oil sector requires a regulatory approach that addresses the specific challenges and opportunities related to methane emissions in this sector. The proposed Regulations also attempt to isolate the largest emission sources in order to mitigate the impact on smaller facilities and operators, by utilizing a "potential to emit" standard of 60,000 m^3 per year in any of the past five years, with any facilities under that threshold exempt from regulation.

In engaging numerous companies on this issue over the past few years we have heard that the current measurement of methane emissions (from both oil and gas operations) is likely inaccurate – potentially by a significant margin. There is some research available that suggests this perception may be a reality.[5] Our concern is that certain facilities may actually be emitting far more than their “potential to emit” suggests, but because of inaccurate accounting of emissions will be exempt from the regulations. At the same time, companies that have implemented more robust measurement systems, and may in fact be emitting less methane, will be required to comply with the proposed regulations. We feel this is both unfair to the companies involved and a missed opportunity to reduce methane emissions.

We do not have a definitive recommendation to address this concern, other than to note the possibility that significant emissions may go undetected, and unmitigated, under the current proposal. Reducing the "potential to emit" ceiling is one option worth considering, but could potentially increase the regulatory burden on smaller operations. Another option is to build into the proposed Regulations a secondary, lower

[4] https://www.aer.ca/data-and-publications/statistical-reports/st60b
[5] http://www.atmos-chem-phys-discuss.net/acp-2017-109/; http://www.greenpathenergy.com/wp-content/uploads/2017/03/GreenPath-AER-Field-Survey-Results_March8_Final_JG.pdf.

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“potential to emit” threshold above which the regulator may perform random spot-checks on facilities. If it is apparent that based on the measured emissions the facility would likely exceed the 60,000 m^3 annual threshold, the facility should be required to begin regular measurement and reporting of its emissions. If that reporting shows a level of emissions above the mandated threshold, the facility would then be required to comply with the venting regulations. We believe this would be a fair and reasonable approach to ensure that the proposed Regulations reflect the growing evidence that methane emissions have been often overlooked and underreported.

Contact

In conclusion, we would like to commend the Government of Canada for setting ambitious targets for methane reduction and for allowing us the opportunity to comment on the proposed Regulations. We would be glad to engage further on any of the issues covered in this submission. For follow-up, please do not hesitate to contact me at jbonham@neiinvestments.com, 604 742 8328.

Sincerely,
NEI Investments

Jamie Bonham
Manager, Corporate Engagement

cc:
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