Government of Newfoundland and Labrador
Department of Natural Resources
Office of the Deputy Minister

Stephen Lucas
Deputy Minister
Environment and Climate Change
Government of Canada
200, boul. Sacre-Coeur
2nd Floor, Office 249
Gatineau, QC K1A OH3
stephen.lucas@canada.ca

Dear Mr. Lucas:

Re: Clean Fuel Standard

I am writing to discuss the federal government's proposed Clean Fuel Standard (CFS). The Government of Newfoundland and Labrador continues to have significant concerns that the proposed CFS does not sufficiently address the unique economic and geographic situation of our province and could cause significant economic harm to the people of Newfoundland and Labrador.

Since the federal government announced its intentions on the CFS in a December 2017 regulatory framework, officials with the Government of Newfoundland and Labrador have monitored its progress through the CFS Multi-Stakeholder Consultative Committee and the CFS federal-provincial-territorial working group. It was at one of the first CFS meetings on December 18, 2017 that provinces and territories, including Newfoundland and Labrador, provided the CFS team with questions on the proposed CFS. It is my understanding that the CFS team was to publish the answers to these questions; however, this did not occur.

On February 9, 2018, the Government of Newfoundland and Labrador provided the CFS team with a document outlining the Government's position on the proposed CFS, noting the outstanding provincial-territorial questions from December 18, 2017 and the importance of receiving answers (see position document at Annex A). We are not aware of any response discussing specifically the issues outlined in our position document.

On March 15, 2018, the Government of Newfoundland and Labrador Department of Municipal Affairs and Environment also participated in an in-person meeting on the CFS with officials from Environment and Climate Change Canada along with Government of Newfoundland and Labrador Department of Natural Resource officials via phone. Government of Newfoundland and Labrador officials reiterated concerns about the CFS but did not receive any clear response from federal officials on how they would address specifically these concerns in the development of the CFS.

Newfoundland Labrador

I would also highlight that the Government of Newfoundland and Labrador's concerns with the CFS are consistent with those raised by industry in this province. Industry stakeholders have advocated to both the Provincial and Federal governments that they are very concerned about CFS impacts on their operations and their ability to compete nationally and globally.

Given this Province's unique geography, demographics, and economy and the potential impact of the CFS on Newfoundland and Labrador, it is important that the CFS address and accommodate our Government's concerns as detailed in our submissions to date. We look forward to hearing from you. Thank you.

Sincerely,

GORDON McINTOSH
Deputy Minister

Encl.

c. Jamie Chippett, Deputy Minister
Municipal Affairs and Environment

Newfoundland Labrador

Annex A:
Written Submission to Environment and Climate Change Canada
Regarding its December 13, 2017, Clean Fuel Standard Regulatory Framework

Submitted by: Department of Natural Resources and
Department of Municipal Affairs and Environment
Government of Newfoundland and Labrador

The Department of Natural Resources and the Department of Municipal Affairs and Environment provide the following provincial context and comments on Environment and Climate Change Canada's December 13, 2017, Clean Fuel Standard Regulatory Framework as outlined in the subsections below.

Current Federal Policy Framework – Provincial Exemption to the Renewable Fuels Regulations

The Government of Canada currently has Renewable Fuels Regulations with an objective to reduce greenhouse gas (GHG) emissions by mandating an average 5% renewable fuel content based on the gasoline volume and 2% for diesel fuel and heating distillates. Fuels in Newfoundland and Labrador are excluded from these regulations, due to various factors including: generally poor extreme cold-weather performance of fuels containing renewable fuels; limited infrastructure for the mixing and distribution of renewable fuels; limited supply options given existing distribution networks and geographic and demographic constraints (i.e., lack of biofuel feedstock due to challenging agricultural conditions and short growing season, absence of natural gas pipelines, lowest population density of any province makes natural gas infrastructure uneconomic); and energy security constraints that will arise if distribution channels are compromised. All of these factors remain unchanged today, thus making them directly relevant to any new Clean Fuel Standard. Newfoundland and Labrador notes that this exemption was established for Newfoundland and Labrador even though the Renewable Fuels Regulation establishes a national credit trading market for suppliers unable to meet their obligations.

During ECCC's December 18, 2017 webinar, federal staff indicated that while the Renewable Fuels Regulations renewable content requirement will be maintained in the short term, exemptions may not be maintained. Newfoundland and Labrador also understands from federal staff that once the Renewable Fuels Regulation is succeeded by the Clean Fuels Standard Regulatory Framework, coverage will be extended to include all fuels, including fuels extracted by industrial producers and consumed on-site, and any existing exemptions at that time may not be maintained. Newfoundland and Labrador notes that during the December webinar, more than 60 questions were asked which ECCC committed to answering and posting on its website. As of this date, however, no answers have been posted, hampering Newfoundland and Labrador in providing its comments. Furthermore, there is no comprehensive cost/benefit analysis including regional impacts. This is a gap that further hinders response. As such,

Newfoundland and Labrador may make additional comments once such analysis and answers to questions become available.

Emerging Federal Policy Framework – Renewable Fuels and Clean Fuels Standards Regulation

Newfoundland and Labrador has serious concerns regarding the proposed framework as outlined on December 18, 2017, and advocates that its current exemption under the federal Renewable Fuels Regulations be maintained and extended under the Clean Fuel Standards Regulatory Framework. There are three broad reasons for this.

First, the policy rationale for the current exemption as described above has not changed.

Second, the emerging policy framework will result, for the foreseeable future, in a situation where provincial consumers and businesses, excluding large industrial facilities, will be separately subject to both a carbon tax on transportation, buildings and electricity generation fuels and clean fuels standards related costs. This is because, given the current situation, the proposed credit market will be the primary and likely sole mechanism for regulatory compliance, placing Newfoundland and Labrador at a disadvantage to other provinces. This will mean that consumers and businesses will have to pay for pass-through credit market costs incurred by producers and importers including Newfoundland and Labrador Hydro, as well as a carbon tax on higher carbon content fuels (i.e., fuels that don't meet Clean Fuels Standard requirements). This contrasts to other provinces where consumers and business will be able, in many circumstances, to purchase lower carbon content fuels that meet the Clean Fuels Standard, thereby reducing their exposure to carbon pricing. Purchasing lower carbon content fuel will likely cost consumers however any cost imbalance between the two compliance options – low carbon fuel versus credit offsets – is an area of concern for Newfoundland and Labrador.

Third, the extended coverage of the regulation to include all fuels in all sectors will have incremental impacts on large industrial facilities in the province. The North Atlantic Refining Limited and the Holyrood Thermal Generating Station (until 2021) rely on residual bunker fuels that are shipped by marine transportation from the United States. Separately, the Iron Ore Company of Canada (IOC), Vale's Voisey's Bay facility and Tata Steel's facility are all located in remote areas in Labrador and rely on bunker and diesel fuels being shipped by rail (over 400 km) or boat. IOC also utilizes coke breeze at its mine site in Labrador which would be expected to be subjected to cost increases as a result of the CFS. Last, offshore petroleum facilities that are located over 350 km from land produce and consume own-source natural gas. In each of these cases, infrastructure, geographic and distribution constraints will mean, similar to the previous point, that the credit market will be the primary and likely sole mechanism for regulatory compliance as it is not clear whether blended or low-carbon fuels can be brought into Newfoundland and Labrador from other Canadian jurisdictions. Moreover, credit market costs will be separate from pending carbon pricing costs and will adversely impact on industrial competitiveness. Industrial facility-specific issues are further described below.

Newfoundland and Labrador acknowledges that the Clean Fuels Standard Regulatory Framework, similar to the Renewable Fuels Regulation, is intended to include a credit trading market for suppliers unable to meet their obligations. However, as noted above, if the Clean Fuels Standard is applied in Newfoundland and Labrador, participation in this credit market will be the primary compliance mechanism rather than the compliance mechanism of last resort. In this context, the credit market will effectively result in higher costs to consumers, businesses and industrial facilities in the province, depending on the credit prices and wealth leakage to fuels suppliers in other jurisdictions. Newfoundland and Labrador further notes that the experience with a similar credit market program in the United States, RINS, has been reported to be particularly costly for independent refiners and importers.

The Newfoundland and Labrador annex in the Pan-Canadian Framework on Clean Growth and Climate Change indicates that a made-in-NL climate change plan, that includes carbon pricing as a mechanism to reduce GHG emissions, will address the province's particular social, economic and fiscal realities. Any federal action that is in support of this framework needs to consider, among various factors outlined, impacts on remote communities, vulnerable groups, indigenous communities, consumers and trade-exposed industries as well as the absence of lower carbon alternatives. Newfoundland and Labrador also notes that some trade-exposed facilities import fuels directly from the United States and almost entirely export products to other countries rather than other provinces, thereby negating any potential competitiveness distortions that may otherwise be created within Canada. Thus, it is imperative that the current exemption under the federal Renewable Fuels Regulations be maintained and extended under the Clean Fuel Standards Regulatory Framework until such time that technological development and deployment allows for the use of a broad range of low carbon fuels, energy sources and technologies.

Further, the federally proposed implementation timelines of releasing draft and final Clean Fuel Standards regulations in 2018 and mid-2019 appears rushed and unrealistic. This is further underscored by the lack of cost/benefit analysis or answers to questions about the CFS, as described previously. Furthermore, while federal officials indicated on the December webinar that the coming-into-force date would be after 2019, no firm timeline was provided.

NARL Competitiveness and Energy Security

Newfoundland and Labrador's only oil refinery, North Atlantic Refining Limited (NARL) would be competitively exposed if the current exemption under the federal Renewable Fuels Regulations is not maintained and extended under the Clean Fuel Standards Regulatory Framework, even if it had access to a credit trading market. The majority of NARL's output is exported to international markets with about 10% to 15%, on average annually, sold in Newfoundland and Labrador. Even though only 10% to 15% of production is sold locally, this accounts for approximately 45% of the province's total fuel consumption, and almost all of certain sub-fuel groups (e.g. propane). NARL does not export fuels to other provinces and, as such, must recoup all costs incurred, including direct compliance costs and trading market costs, from the Newfoundland and Labrador market. NARL has indicated to provincial officials that its anticipated carbon pricing costs, combined with renewable and clean fuels costs if the current

exemption was not extended, would risk closure of the refinery. This would seriously jeopardize Newfoundland and Labrador's energy security and would be a significant economic loss.

NARL faces significant structural barriers in sourcing less carbon intensive fuels for distribution. NARL's energy requirements are met by electricity purchased from the province's crown utility, Newfoundland and Labrador Hydro, fuel oil (with higher carbon emissions compared to natural gas) and gaseous fuels. As such, NARL is geographically disadvantaged in terms of energy costs compared to other North American refineries that have access to natural gas. Further, as NARL is only located in Newfoundland and Labrador, it does not have the ability of larger companies to implement initiatives in one province, allowing them to meet clean fuel standards for their company as a whole, even though various locations across Canada do not have these initiatives. Therefore, not extending NL's current exemption under the federal Renewable Fuels Regulations to CFS would result in not recognizing the regional disparity smaller regional suppliers, such as NARL are facing. Further, as NARL will be challenged to meet the federal Clean Fuel Standard, it will instead result in a large economic burden that will further impede their competitiveness and negatively impact the economy and energy security of Newfoundland and Labrador.

The analysis below provides more information on the importance and serious economic ramifications of this issue for critical industries and electricity generation in Newfoundland and Labrador.

Offshore Petroleum

Newfoundland and Labrador petroleum explorers face challenging economics and harsh environmental conditions to explore and develop in our offshore. Implementing the CFS has the potential of burdening exploration in Newfoundland and Labrador.

Newfoundland and Labrador has significant offshore natural gas resources. Despite this potential, operators have not attempted to develop these, partly due to economic burdens and lack of infrastructure. Currently, Newfoundland and Labrador offshore operators don't have an economical means of producing natural gas for market (e.g. via a pipeline or floating liquid natural gas (FLNG) facility). Offshore petroleum facilities produce and consume own-source non-marketable natural gas for electricity and power generation. They re-inject produced gas to enhance reservoir production and for pressure management (i.e. falling under CFS's "self-produced and used" category). This self-sufficiency should be encouraged as a CFS could also lead to increased flaring operations.

Diesel fuels are only used at offshore fields: when compression is lost, to power freight cranes, for emergency situations, and to power separate mobile drilling units which are contracted for use from time to time. GHG estimates suggest that diesel comprises less than 5% of GHG emissions in the sector. Situated 350 kilometers offshore in the Atlantic Ocean, these platforms are constrained from: an infrastructure basis (i.e. retrofits are challenging to implement in a harsh environment, equipment is challenging to procure and transport, on-board turbines are simple-cycle given weight constraints, and the platforms are space constrained); regulatory basis (i.e. there are limits to how many crew can be on-board at any given time, and operational staff largely fill regulatory limits); and cost basis (i.e. three of the four fields are past peak

production and face declining reserves, and the fourth field is new and the platform uses best available capital stock at this time). In addition, operators of the platforms have only a limited ability to switch fuels from produced natural gas and/or purchased diesel needed to produce crude oil. Given this, like carbon pricing, provincial officials expect that offshore petroleum companies will rely almost exclusively on credit trading markets for compliance. Provincial officials note that these costs, when combined with carbon pricing costs for the companies, will result in lower resource royalties and corporate tax revenues to the Province, thereby exacerbating fiscal constraints, and may impact on the competitiveness of the sector for further exploration and development. The CFS regulation likely will become an added cost to the sector both directly, through an obligated compliance pathway (i.e. purchasing credits) as well as indirectly from costs passed down through purchased fuels. As an energy-intensive trade-exposed industrial sector, any such additional costs for offshore oil and gas production could impact the sector's ability to compete in terms of exploration and development against jurisdictions that do not incur these costs.

The CFS would not apply to petroleum operators that export their oil and natural gas yet would apply to crude oil produced, imported, and consumed in Canada. Incentives should exist to encourage Canadians' use of their own natural resources and, as it stands, CFS could encourage operators to export our resources then tax the oil and gas imports that Canadians will still need to meet national demands.

The CFS will affect gaseous fuel distributors such as pipelines. Pipeline development and distribution should be incented over other transportation methods that have been shown to be more harmful to the environment or aren't as safe, such as rail.

It has yet to be determined if the carbon intensity values will differ for sweet vs. sour gas. There is a greater level of work involved for operators when they plan to drill and develop sour gas wells (e.g. developing emergency response plans). Applying a great carbon intensity value to these wells could burden their economics.

Newfoundland and Labrador suggests exempting offshore operators from the CFS and incenting natural gas pipelines or FLNG development.

Electricity Generation

Currently, over 80 per cent of the province's electricity is generated from renewable resources, and this number will further rise to 98 per cent once the Muskrat Falls hydroelectric project comes into service mid-2020. The completion of this project will enable closure of the 490 megawatt oil-fired Holyrood Thermal Generating Station (Holyrood), displacing approximately one million tonnes of greenhouse gas emissions annually. As a result of the province's investment in this project, Holyrood is scheduled to discontinue operating as a generation facility in 2021. If the Clean Fuel Standard was applied before this date, the province's crown utility, Newfoundland and Labrador Hydro would be expected to incur higher fuel costs; however, there is no business case to invest in Holyrood to reduce fuel consumption given its pending closure prior to the end of its useful life. these CFS costs would then be passed on to ratepayers who are already paying the cost of the Muskrat Falls project, which without mitigation efforts, is currently projected to approximately double domestic electricity rates.

Newfoundland and Labrador Hydro also maintains 21 regulated electricity-isolated diesel systems along the coasts of our province (one is currently in the process of being decommissioned). These diesel systems serve approximately 3,400 customers and have a total installed capability of approximately 36 megawatts. On average, ratepayers on these systems only pay 8 percent of their cost of service, which actually ranges from 86 to 138 cents per kilowatt hour. The cost difference is covered through a ratepayer subsidy and a government subsidy. While diesel is commonly used throughout the world to ensure reliable and low cost electricity in isolated communities, the Government of Newfoundland and Labrador recognizes the environmental concerns it produces, as it emits greenhouse gases and must be trucked in or shipped to the remote communities. Since 2008, government has provided $3.5 million for studies to determine if alternative energy sources, including wind and hydro, can be used to reduce generation costs in isolated Labrador communities. Further, the Premier's 2017 mandate letter to the Minister of Natural Resources directed the Minister to encourage "more diverse distributed energy generation by seeking opportunities to develop wind farms and small scale hydro, and prioritizing communities isolated from the primary power grid, such as coastal regions of Labrador." If electricity generation in isolated communities was subject to the Clean Fuels Standard, this would result in higher subsidies being provided by ratepayers (who are consuming renewable electricity) and taxpayers for diesel electricity generation. At the same time, ratepayers and taxpayers will be subsidizing carbon pricing costs for electricity generation in these communities and electricity rates for hydroelectricity on the island interconnected grid are expected to increase substantively. This will have the effect of increasing consumer costs and exacerbating the provincial fiscal situation without achieving environmental outcomes.