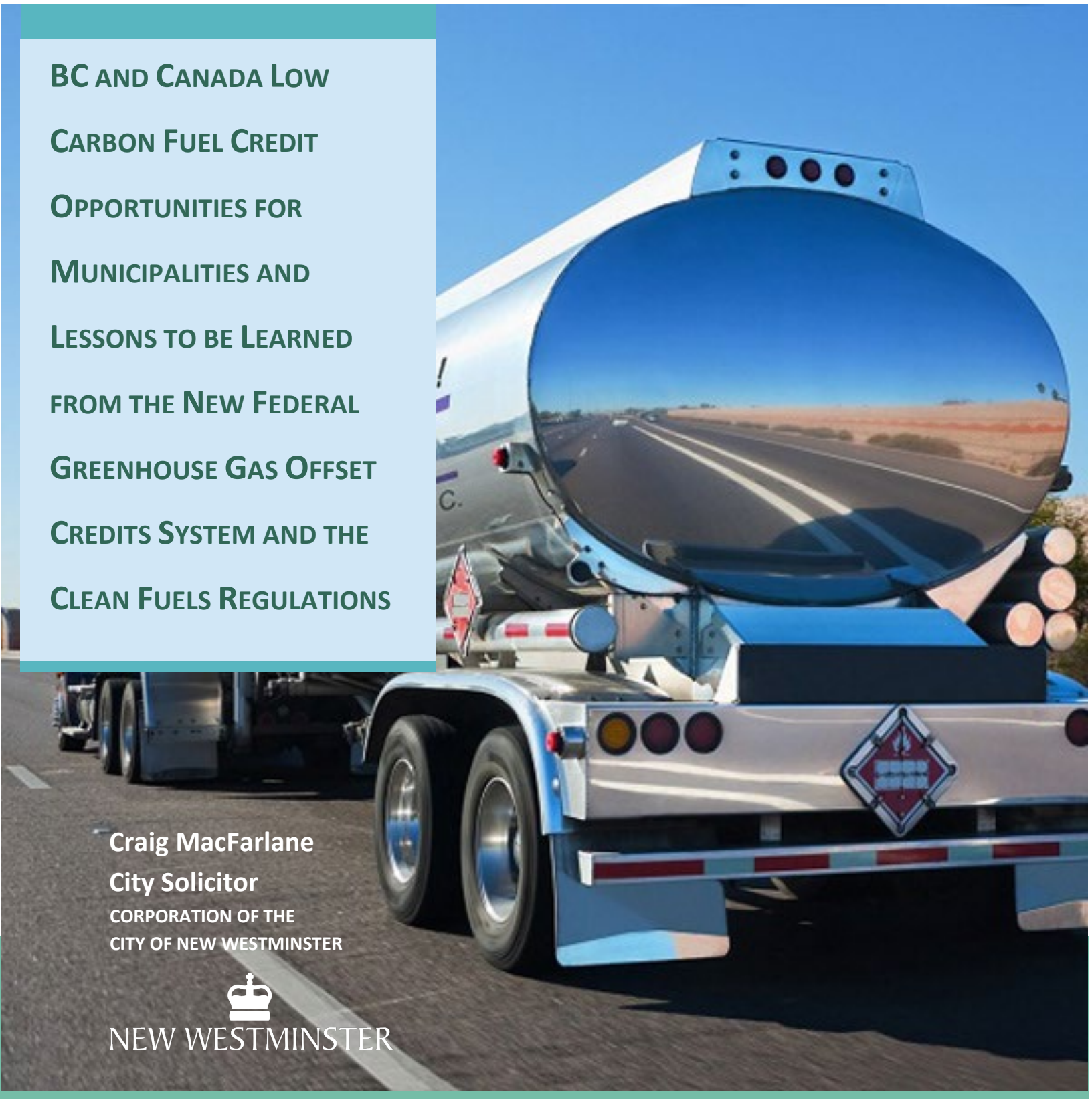
BC and Canada Low Carbon Fuel Credit Opportunities for Municipalities and Lessons to be Learned from the New Federal Greenhouse Gas Offset Credits System and the Clean Fuels Regulations



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NEW WESTMINSTER

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INTRODUCTION

The City of New Westminster has recently sold British Columbia Low Carbon Fuel Standard (BC LCFS) credits it earned during the 2013-2020 period to Elbow River Marketing Ltd. of Calgary, Alberta for $26,395,700. Elbow River Marketing is a wholly owned subsidiary of Calgary's Parkland Corporation an independent supplier of fuel and petroleum products in Canada, the USA and the Caribbean. It also owns and operates the Burnaby BC Refinery. These funds have been used to establish a new Climate Action Reserve Fund in the City's budget to support New Westminster's commitment to a zero carbon future.

In B.C., suppliers of transportation fuels with a high carbon intensity (such as gasoline or diesel) are required to reduce the carbon intensity of their fuels by several means, including through the purchase of low carbon fuel credits, which are generated by suppliers of transportation fuels with a low carbon intensity (such as electricity or biodiesel). This is a market-based mechanism which incentivizes suppliers of carbon-intensive fuels to reduce their fuel's intensity and provides a financial investment to support the growth of low carbon fuels. New Westminster earns BC LCFS credits as a Part 3 classified fuel supplier due to having its own Electrical Utility, and it offered its credits for sale to qualified registered proponents in a competitive RFP process. Elbow River Marketing is a registered participant in the BC LCFS program and a Part 3 fuel supplier.

The $26 million earned in the sale will fund a new reserve, established through the passing of the Climate Action Reserve Fund Bylaw No. 8321, 2022. The reserve will provide funding for one-time investments to accelerate projects, actions, or initiatives that support climate mitigation and adaptation by targeting energy and greenhouse gas reductions. The move is directly aligned with the City's Seven Bold Steps for Climate Action.

The City, through its operation of a wholly-owned Electric Utility servicing TransLink's SkyTrain, is regulated and registered as a supplier of low carbon fuel under the Greenhouse Gas Reduction (Renewable and Low Carbon Fuel Requirements) Act, SBC 2008, c.16, (GGRA). As part of the regulation under the GGRA, the City accumulated annually a large quantity of low carbon fuel credits. When the City began collection of fees for public EV charging, it began generating additional low carbon fuel credits from its public EV infrastructure. Both the EV charging infrastructure and electricity supplied to the SkyTrain qualify as low carbon intensity fuels under the GGRA.

BC LCFS credits can be validated by the Ministry of Energy Mines and Low Carbon Innovation (the "Ministry") back to and including 2013 when the 2008 GGRA program was actually implemented. The BC LCFS credits do not expire and any surplus of BC LCFS credits can be banked for future compliance and ultimate sale in the market.

BRITISH COLUMBIA'S LOW CARBON FUEL STANDARD AND OPPORTUNITIES FOR LOCAL GOVERNMENTS

British Columbia's Low Carbon Fuel Standard is a "market-based mechanism" to reduce greenhouse gas (GHG) emissions in the transportation sector. The "market" in this context is compliance, not a specific market for a specific fuel. Fuel suppliers receive debits for fuels with a carbon intensity higher than the current limit and accrue credits for fuels with a carbon intensity lower than the current limit. Credits can then be traded between fuel suppliers.

Other municipalities in B.C., such as Victoria, are regulated suppliers of fuel under the GGRA through the operation of compressed natural gas (CNG) fueling stations at their works yards to fuel City vehicles. Victoria's sales of recently generated credits from supplying CNG is generating an ongoing income stream to the City in addition to credits sold from its EV charging stations.

Renewable Natural Gas (RNG) has now been approved by the Ministry for inclusion within the province's BC LCFS. RNG can be produced by municipalities in plants dedicated to the conversion of organic waste streams into RNG. Credits from production of RNG can now be validated by the Ministry and sold to other registered fuel suppliers with higher carbon intensity than current limits.

Another promising opportunity for municipalities are low carbon fueled district energy plants. New Westminster and Surrey, B.C. are planning to tap into sustainable energy sources from heat generated in sewers. In New Westminster heat pumps will extract heat from a Metro Vancouver sewer line and supply energy to a nearby hospital and new residential development. This will generate a new source of low carbon fuel credits for the City.

As noted later in this paper (at page 10) under Canada's Greenhouse Gas Offset Credit System new federal legislation will allow landfill operators to receive offset credits if they recover landfill gas and subsequently destroy or utilize it. Introduced on June 8, 2022 this credit system creates market based opportunities for municipalities, indigenous communities, industry and individuals to implement GHG emissions and removal solutions. Canada's new Clean Fuel Regulations and Opportunities for Low Carbon Energy Producers also discussed in this paper (at page 13) will allow municipalities, in provinces without B.C. GGRA low-carbon fuel standards type programs, to create compliance credits and generate revenue by being an electric vehicle charging-network operator under the federal legislation.

Another source of revenue for local governments is the sale of display advertising on their EV charging stations. Chargepoint Holdings Inc., the largest operator of U.S. EV charging stations is rolling out a nationwide advertising network in partnership with digital and video advertising companies.

BRITISH COLUMBIA'S LOW CARBON FUEL CREDITS/CARBON OFFSETS

Low carbon fuel credits are different than carbon offsets.

Low carbon fuel credits are a mechanism for fuel suppliers in B.C. to meet the compliance requirements of B.C.'s Low Carbon Fuel Standard.

Carbon offsets are a mechanism for companies, and others, to balance out the carbon they are emitting by investing in projects that either remove carbon from the atmosphere or avoid emitting it in the first place. A recent hybrid example of both the sale of offset credits for project construction and ongoing credit sales from facility operation is Tidewater Renewables Ltd. construction of a renewable diesel and renewable hydrogen complex at Prince George, B.C. The company entered into a multi-year agreement with an investment company to realize total proceeds of more than $53 million over the term of the agreement extending to 2024, which reduces the value realization risk on a portion of the BC LCFS credits that Tidewater will receive. The applicable B.C. legislation to these transactions is discussed below under the Greenhouse Gas Industrial Reporting and Control Act, SBC 2014, c 29.

As the City is not a supplier of carbon-intensive fuels, the City doesn't need to use the low carbon fuel credits for compliance purposes. The City can choose to sell its low carbon fuel credits and invest into climate action initiatives by selling its credits to carbon-intensive fuel suppliers who are required to purchase credits for compliance. This incentivizes suppliers of carbon-intensive fuels to reduce their fuel's intensity and provides a financial investment to support the growth of low carbon intensity fuels.

Under the Climate Change Accountability Act, SBC 2007, c 42, British Columbia sets certain greenhouse gas (GHG) emissions reduction targets. One initiative for meeting these climate change goals is the carbon credit system governed by the Greenhouse Gas Industrial Reporting and Control Act, SBC 2014, c 29 (GGIRCA). It establishes GHG emissions reporting requirements, allows for the creation of emission standards applicable to industrial facilities, and allows for the adherence to emissions standards through earning or purchasing emissions offsets and/or credits or purchasing government-generated credits.

So long as GGIRCA meets or exceeds federal carbon pricing standards as outlined in the Canadian Greenhouse Gas Offset Credit System Regulations, SOR/2022-111 and the Greenhouse Gas Pollution Pricing Act, SC 2018, c 12, BC's system will likely remain independent from the federally legislated Greenhouse Gas Offset Credit System.

Three regulations have been created under British Columbia's GGIRCA:

- Greenhouse Gas Emission Reporting Regulation, BC Reg. 249/2015 (GGERR);
- Greenhouse Gas Emission Control Regulation, BC Reg. 250/2015 (GGECR); and
- Greenhouse Gas Emission Administrative Penalties and Appeals Regulation, BC Reg. 248/2015 (GGEAPAR).

The GGERR, GGECR, and GGEAPAR together govern the use and issuance of carbon credits in the province. Collectively, they are functionally equivalent to Alberta's Technology Innovation and Emissions Reduction Regulation, AB Reg. 133/2019 (TIER). Under the GGERR, facilities that emit over 10,000 tonnes or more of GHG per year, measured in Carbon Dioxide Equivalent (CO2e), fall within the scope of the legislation and must report its emissions.

GGIRCA defines three types of emissions reduction credits. Offset Units (Offsets) are issued based on verified reductions of emissions from a facility or verified removal of emissions from the atmosphere by a project such as a carbon capture facility. Offset generating projects must meet certain requirements outlined in GGIRCA's regulations. Earned Credits (Credits) are issued to regulated facilities if they fall under their emission limit for a given compliance period. Finally, Funded Units (Units) can be purchased directly from the government.

Each Offset, Credit, or Unit represents one (1) tonne of CO2e and together, are collectively referred to as Compliance Units (CU). CUs are tradeable certificates that can be purchased or sold on the market. The GGECR also establishes the BC Carbon Registry, which monitors CU transactions, and enables the issuance, transfer, and retirement of CUs.

The Government of B.C. issues GGIRCA Bulletins regularly, which provide further legal information, clarifications, and guidance regarding the carbon credit system and its associated regulations. Interested parties should regularly review the Bulletins for any which may affect their project regulated under the legislation.

The emissions reduction targets British Columbia has legislated over the next several decades mean industry participants will face many challenges in meeting their emissions targets. The province's carbon credit system will be a key mechanism by which those challenges can be met. Interested parties should stay up to date on any changes to it and fluctuations in the price of credits.

LEGAL ANALYSIS AND CONTRACT TERMS

Under the *Greenhouse Gas Reduction (Renewable and Low Carbon Fuel Requirements) Act* SBC 2008, c.16 (the "GGRA"), a Part 3 fuel supplier's compliance with the low carbon fuel requirements of the *Renewable and Low Carbon Fuel Requirements Regulation B.C. Reg. 394/2008 (*the "RLCF Regulation") is calculated in terms of credits for low carbon fuels and debits for high carbon fuels as specified by section 6 of the Act. Fuel suppliers may transfer debits and validated credits in order to achieve compliance with the low carbon fuel requirements.

Before credits can be transferred they must be validated by a Ministerial Director at the Province. Credits are most commonly validated through the submission of an annual Compliance Report that includes a net credit balance. As noted earlier in this paper. LCFS credits can be validated back to 2013 when the program was first implemented. LCFS credits do not expire and any surplus LCFS credits can be banked for future compliance.

All credit and debit transfer proposals must include a "fair market value" of any consideration, under section *11.11 (2) (c) (iv)* of the *RLCF Regulation.* Transfers that the Ministerial Director considers are underestimating "fair market value" or those using a "zero dollar" value must include a written explanation justifying the use of the identified credit or debit value.

All credit and debit transfers must be approved by the Ministerial Director. Part 3 fuel suppliers may apply for the approval of transfers through the Transportation Fuels Reporting System ("TFRS"). The transfer of credits or debits will take effect on either the date on which the transfer is approved by the Ministerial Director, or a date specified in the Credit Transfer Proposal, whichever is later.

All Part 3 fuel suppliers must be recognized by the Ministry of Energy Mines and Low Carbon Innovation (the "Ministry"). A list of recognized suppliers, including municipalities, is published by the Ministry, with the permission of the organization, and is provided for convenience only. It is recommended that each organization interested in credit transfers confirm with their trading partner their current status as a Part 3 Fuel Supplier since credit transfers can only be made between recognized Part 3 fuel suppliers. Transfer of validated credits must apply for approval by submitting a Credit Transfer Proposal online in the TFRS which in my experience has been a user friendly exercise. To use TFRS, you will need to register with BCeID and have a Business BCeID account set up for each member of your organization requiring access to TFRS.

(see-https://www2.gov.bc.ca/gov/content/industry/electricity-alternative-energy/transportation-energies/renewable-low-carbon-fuels/transportation-fuels-reporting-system).

Effective November 2019, credit transfers processed through the TFRS are automatically reported with submission of the annual Compliance Report.

Summary of Typical Contract Terms

- Clause allowing the purchaser of credits to re-sell the carbon credits at their discretion and at a price that is not less than 75% of the original contract price received from the City;
- Term of the contract typically ongoing with auto-renewals, with the option to terminate the contract by either party providing 10 days' written notice;
- The City's contract requires proponents to add the City as an additional insured and has an indemnity clause for actions that may be brought against the City for damages that arise from the breach of the agreement or for the purchase/use of the credits. An indemnity is essentially a promise by one party to compensate the other party for the losses suffered from the actions of the party at fault; and
- Confidentiality clause requiring both parties to keep the terms of the contract confidential, except where required to disclose such terms pursuant to the Freedom of Information and Protection of Privacy Act or other applicable legislation. Buyers of credits typically like to keep the unit price paid for each credit confidential.

GHG Reduction Schedule for BC

The Province has credited the Low Carbon Fuel Standard with being one of its most successful approaches to reducing GHG emissions in the transportation sector. Between 2010 and 2020 the program resulted in the avoidance of over 10 million tonnes of GHG emissions. As seen in the table below, the Provincial Government is requiring suppliers of transportation fuels to further decrease the carbon intensity of their fuels by an additional 1.09% annually. The benefits of this will be felt in the way of additional emissions avoided and improved air quality.

Reduction schedule

Compliance Period	Percentage reduction	Carbon Intensity Limit for Diesel Class Fuel (g CO2e/MJ)	Carbon Intensity Limit for Gasoline Class Fuel (g CO2e/MJ)
2020	-9.1%	86.15	80.13
2021	-10.2%	85.11	79.17
2022	-11.3%	84.08	78.20
2023	-12.4%	83.04	77.24
2024	-13.5%	82.01	76.28
2025	-14.5%	80.98	75.32
2026	-15.6%	79.94	74.36
2027	-16.7%	78.91	73.40
2028	-17.8%	77.88	72.44
2029	-18.9%	76.84	71.47
2030 and subsequent compliance periods	-20%	75.81	70.51

It should be noted that reducing the carbon intensity of fuels does not directly translate to emissions reductions. This is because emissions intensity refers to the amount of emissions produced on a per unit basis. If the total quantity of fuel consumed increases then it is still possible for total emissions to increase as well. However, this increase to total emissions would be less than it would be without reductions to emission intensity. On the other, if the quantity of fuel consumed decreases, then emissions reductions can be accelerated. This highlights the importance of decreasing overall fuel consumption through the increased use of active transportation, transit, and electric vehicles.

SUMMARY OF B.C. LOW CARBON FUEL CREDIT MARKET

The following tables from the Ministry provide a summary of the low carbon fuel credit market, excluding credit transfers reported with zero or near-zero price. These tables indicate a significant increase in credit prices during the 2021-2022 months reported.

Category Type	Definition
Category A	The agreement to transfer credits was reached within the last 6 months.
Category B	The agreement to transfer credits was reached between 6 months to 1 year ago.
Category C	The agreement to transfer credits was reached more than 1 year ago.
Category D	Transfers reported with zero or near-zero price.

Time Period	Transfers (number)	Category	Volume (credits)	Average Price ($ per credit)
Jul 2022	26	A	233,833	$444.85
	0	B	0	N/A
	0	C	0	N/A
	0	D	0	N/A
	26	All categories	233,833	$444.85

Current Month Summary

Time Period	Transfers (number)	Total Volume (credits)	Average Price ($ per credit)	Minimum Price ($ per credit)	Maximum Price ($ per credit)
Jul 2022	26	233,833	$444.85	$400.00	$490.00

Previous Three Months Summary

Time Period	Transfers (number)	Total Volume (credits)	Average Price ($ per credit)	Minimum Price ($ per credit)	Maximum Price ($ per credit)	A	B	C
Jun 2022	6	24,934	$406.31	$340.00	$485.00	2	2	2
May 2022	0	0	N/A	N/A	N/A	N/A	N/A	N/A
Apr 2022	2	3,126	$372.93	$340.00	$485.00	N/A	N/A	N/A

Historical Credit Transfers

Time Period [2]	Transfers (number)	Total Volume (credits)	Average Price ($ per credit)	Minimum Price ($ per credit)	Maximum Price ($ per credit)
Q4 2021	21	150,404	$483.25	$345.00	$519.19
Q3 2021	15	142,529	$472.32	$425.00	$495.00
Q2 2021	19	44,710	$421.09	$345.00	$493.50
Q1 2021	30	214,263	$410.73	$85.00	$457.00
CY 2021	85	551,906	$447.24	$85.00	$519.19
CY 2020	32	102,890	$250.44	$32.50	$385.20
CY 2019	35	263,512	$269.33	$32.93	$324.08
CY 2018	48	435,221	$193.44	$55.00	$210.50
CY 2017	31	240,164	$164.30	$60.00	$185.00
CY 2016	15	198,705	$170.93	$100.00	$190.00
CY 2015	2	14,354	$169.95	$20.00	$170.00

[2] Q: quarter; CY: compliance year

CANADA'S GREENHOUSE GAS OFFSET CREDIT SYSTEM

On June 8, 2022, the federal government launched Canada's Greenhouse Gas Offset Credit System (**Credit System**) in an effort to meet Canada's emissions reduction goals. The Credit System creates market-based incentives for municipalities, Indigenous communities, industry players, and individuals to implement innovative solutions to reduce Greenhouse Gas (**GHG**) emissions and remove GHG from the atmosphere.

The Credit System is governed by the *Canadian Greenhouse Gas Offset Credit System Regulations*, SOR/2022-111 (**Regulations**), created under the **Greenhouse Gas Pollution Pricing Act**, SC 2018, c 12 (**GGPPA**).2 The Credit System was designed and created in alignment with the *Pan-Canadian Greenhouse Gas Offsets Framework*, which incorporates experience and expertise from Alberta, British Columbia, and Québec, who have already launched their own offset credit systems. Currently, only provinces which do not already have a carbon pricing system that meets or exceeds federal requirements are subject to the GGPPA and the Credit System. For example in Alberta, the TIER Act and regulations govern instead. Under the Regulations, participants to the Credit System must be registered and follow a federal protocol setting out how GHG emissions reductions or GHG removal from the atmosphere are measured. Such reductions and removals must also come from activities which are not otherwise obligated by law or falling under an existing carbon pricing system. Generated offset credits are tradeable and sellable on the market.

The first federal protocol which allows for generation of offset credits is the new Landfill Methane Recovery and Destruction protocol. Under it, landfill operators who recover landfill gas and subsequently destroy or utilize it are eligible to receive offset credits. Additional protocols applicable to the refrigeration, agricultural, and forest management sectors are currently under development. A protocol for Direct Air Carbon Capture and Sequestration technologies will also come in the near future.

CANADA'S CLEAN FUEL REGULATIONS FOR LIQUID FUEL SUPPLIERS AND OPPORTUNITIES FOR LOW-CARBON ENERGY PRODUCERS

On June 20, 2022, the final *Clean Fuel Regulations*[SOR/2022-140(CF5)] under the *Canadian Environmental Protection Act, 1999*[SC 1999, c.33] were registered, bringing a Canadian Clean Fuel Standard (CFS) into law. The final version of the CFS was published in the *Canada Gazette* on July 6, 2022; however, it came into force upon registration, with the exception of two sections repealing the pre-existing *Renewable Fuels Regulations* (RFRs), which will come into force on September 30, 2024.[CFS. s.176]

The CFS targets carbon emission reductions from carbon content in liquid fossil fuels, primarily those used in transportation, and hopes to allow for innovation and economic growth in the low-carbon fuels sector. The federal government hopes that the CFS will drive consumer choice towards low-carbon energy sources for transportation fuel (such as biofuel and electricity) by decreasing their price while increasing the price of liquid fossil fuels.

The CFS imposes on "primary suppliers" that domestically produce or import at least 400 cubic metres (m3) of gasoline or diesel during a "compliance period" (6-month periods in 2023, when the obligations take effect, and calendar years thereafter),[CFS, ss1(1) and 4(1)] and highlights opportunities for low-carbon energy producers to generate compliance credits under this new regime.

The CFS will replace the RFRs, established in August 2010. The RFRs require primary suppliers to have an average renewable content of at least 5% for gasoline that they produce in Canada and/or import, and 2% for diesel fuel (and heating distillate oil). Primary suppliers under the CFS must continue to achieve a renewable fuel content of at least 5% in gasoline and 2% in diesel that they produce in Canada and/or import during a compliance period.[CFS, ss.6(1) and 7(1)]

The CFS requires greenhouse gas (GHG) reductions on a lifecycle basis, accounting for emissions from the production to the end use of the fuel. The CFS establishes lifecycle carbon intensity (CI) limits for each fuel type (gasoline and diesel), expressed in grams of carbon dioxide equivalent per megajoule (gCO2e/MJ). Primary suppliers must lower the CI of the gasoline and diesel that they produce in Canada and/or import in accordance with these limits. Rather than requiring each primary supplier to calculate the current CI of their unique gasoline and diesel pools, the CFS establishes a baseline CI for each fuel. [CFS s.5 (3)] Primary suppliers must lower the CI of their unique gasoline and diesel pools by an amount equal to the difference between the baseline CI for that fuel and the CI limit for the corresponding compliance period.[CFS s.5(2)]. Note that the Proposed CFS would have applied to kerosene, light fuel oil, heavy fuel oil and jet fuel in addition to gasoline and diesel, but these fuels

were removed in the final CFS. Fuel produced in Canada that is ultimately exported for use in another country is also exempt from the CFS. [CFS s. 4(2)]

The first annual CI limits are 91.5 gCO2e/MJ for gasoline and 89.5 gCO2e/MJ for diesel, which are for the 2023 calendar year. [CFS s.5 (1)] Based on the baseline CIs of 95 gCO2e/MJ for gasoline and 93 gCO2e/MJ for diesel, [CFS s. 5(3)] primary suppliers will have to reduce the CI of the gasoline and diesel that they produce in Canada and/or import by 3.5 gCO2e/MJ in 2023. Reduction requirements will increase by 1.5 gCO2e/MJ per year until 2030, which is a higher rate of increase than was initially outlined in the Proposed CFS.

Primary suppliers will be required to meet their reduction requirement on a company-wide basis, based on the total volume of gasoline and/or diesel that they produce in Canada and/or import during a given compliance period. [CFS s. 8(1)] In other words, the CFS imposes a burden on primary suppliers to oversee the total volume (m3) of their pools of gasoline and/or diesel to calculate their reduction requirement. These pools include fuel that was (i) dispatched from their fuel production facilities; (ii) used to fuel equipment at their fuel production facilities; and (iii) imported. Primary suppliers can subtract fuel sold or delivered for certain uses from this pool (e.g., space heating and generating electricity in underserviced areas); [CFS s.8 (2)] therefore, primary suppliers should keep track of the intended end use of the fuel they sell.

The CFS allows primary suppliers to defer satisfaction of a small portion of their reduction requirements for a compliance period for up to five years, subject to certain conditions. [CFS s.16]

Compliance Credits and Credit Market

Primary suppliers must lower the CI of their fuel using “compliance credits.”[CFS s .5(2)] Each compliance credit is equivalent to a one-tonne reduction of life cycle CO2e emissions for the applicable compliance period. During each compliance period, primary suppliers must use the number of credits necessary to meet their reduction requirement. Compliance credits can either be created by primary suppliers or transferred to them by other “registered creators.”[CFS ss. 11(1) and 11(2)] It should be noted that compliance credits are the only mechanism for primary suppliers to achieve compliance with their reduction requirement. Lowering the actual CI of the fuel that a primary supplier produces has no effect on their reduction requirement, which is based on a set baseline CI.

Creating Compliance Credits

Any registered creator — including primary suppliers — can generate compliance credits through activities in the following three main categories: [CFS ss. 19(1) and 25(1)]

1. Compliance Category 1: CO2 emissions reduction projects, including carbon capture and storage projects[CFS s 30-40]
2. Compliance Category 2: producing or importing low-CI fuel (i.e., fuel with a CI below the applicable CI limit)[CFS ss94-97]
3. Compliance Category 3: end-use fuel switching in transportation (i.e., an end user of fuel changes or retrofits their vehicle to be powered by a low-carbon fuel or energy source)[CFS ss. 98-]

For Category 3, an electric vehicle (EV) charging-network operator [CFS s. 1(1)] is one of the entities that can create compliance credits through end-use fuel switching in transportation. However, it can only do so during a compliance period if all of the revenue it receives from the transfer of previously created compliance credits is reinvested in expanding EV charging infrastructure or reducing the cost of EV ownership (through financial incentives to purchase or operate an EV). Revenue from credit transfers must also be reinvested within two years of the end of the compliance period in which the credits are transferred. [CFS ss.102-103]

Registered creators can also generate compliance credits by reducing the CI of gaseous fuels (as opposed to liquid fuels), through the same kinds of activities listed in Categories 1 and 2 above. This includes projects that reduce the lifecycle emissions of gaseous fuels and promote low-CI gaseous fuels (e.g., renewable natural gas, biogas, hydrogen, renewable propane).[CFS s.20] However, a primary supplier cannot satisfy more than 10% of their reduction requirement with compliance credits derived from gaseous fuel CI reduction.[CFS ss. 15(2) and 28(b)]

Only compliance credits created before the end of a compliance period can satisfy a primary supplier's reduction requirement for that compliance period, meaning registered creators cannot bank credits for longer than one compliance period.[CFS s.11(3)]

Compliance-credit Market

The CFS contains provisions that establish a market for compliance credits, in which both primary suppliers and other registered creators can participate. As well as providing primary suppliers with alternative compliance options, this credit market will enable low-carbon energy producers to generate revenue by voluntarily generating credits and selling them into this new carbon market.

Primary suppliers can enter into credit-creation agreements with other registered creators — including biofuel producers, EV charging site hosts, fuel station owners/operators and upstream and downstream operations — whereby primary suppliers compensate registered creators for the compliance credits they produce during a compliance period.[CFS ss.21 and 22] Primary suppliers and other registered creators can also transfer compliance credits that they have already created to other participants for "fair market value."[CFS ss. 105-109]

Another option for registered creators with excess compliance credits is to pledge to transfer these credits through the "clearance mechanism", whereby primary suppliers who cannot otherwise satisfy their CI reduction requirements must acquire compliance credits through the clearance mechanism at a price that cannot exceed the maximum amount set out in the CFS ($300 per credit, adjusted for inflation), up to the amount necessary to satisfy their reduction requirement. [CFS ss. 110-112]

Unlike other carbon credit markets, such as the Technology Innovation and Emissions Reduction (TIER) regime in Alberta and the B.C. programs, the CFS regime allows emission reduction activities in one jurisdiction to be used to create compliance credits for primary suppliers in another jurisdiction. In fact, upon application by a credit creator, the Minister may recognize CO2e-emission-reduction projects in other countries for CFS compliance credits if there is an agreement in place with that country. [CFS ss.38 and 39] This feature of the CFS will remove one of the key obstacles to a liquid market that we have seen in other carbon credit regimes, where the supply of carbon credits is limited to emissions-reduction activities in a single jurisdiction (i.e., province). The CFS regime may therefore provide more optionality for parties relative to other compliance carbon credit markets currently operating in Canada.

On the other hand, the CFS regime may attract potential generators of carbon credits to create credits for the CFS regime as opposed to others (e.g., TIER) and thereby reduce availability of carbon credits under other regimes. The CFS may also increase the administrative burden on generators of carbon credits because these parties will now have another carbon credit market to understand and comply with, potentially increasing the fragmentation of carbon markets in Canada today.

Compliance Funds

As an additional interim compliance option, primary suppliers may meet up to 10% of their annual CI reduction obligation through payments into a registered "compliance fund" at a set price per tCO2 (equivalent to one compliance credit).[CFS ss.15(1), 19(2) and 118] This price will start at $350/tCO2.[CFS ss. 118(3) and 118(4)] Credits secured by making a payment into a compliance fund cannot be traded and must be used for compliance in the same compliance period.[CFS ss. 19(2), 118, 119(1) and 119(2)]

Canada will maintain a list of approved compliance funds. Eligible funds must use the contributions to finance projects and activities in Canada "that support the deployment or commercialization of technologies or processes that will reduce CO2e emissions" in the short term. Other eligibility criteria are designed to ensure the funds' transparency, sound management and independence. [CFS ss.115 (1) and 115(2)]

Though just one of several compliance options available to primary suppliers under the CFS, the compliance fund mechanism may increase financing for emissions-reducing technologies in Canada.

Conclusions

The details set out in the long-anticipated CFS will assist fuel suppliers across Canada understand their obligations under this new regime, and parties will now have six months to do so before the compliance obligations become effective in 2023. The federal CFS have been criticized as an indirect subsidy for the fossil fuel sector. It does not provide the same clean fuel standards as B.C.'s Low Carbon Fuel Standard collectively regulated under the GGRA and the RLCF Regulation. The B.C. regime sets CI targets that decline each year and at the end of each compliance period, suppliers must have a zero balance or more credits to avoid non-compliance. New amendments to the regulations of the GGRA will take effect January 1, 2023 and will have a new schedule of carbon intensity reductions to achieve a 30 % reduction of existing fuel pools by 2030.