**28/06/2023**

Cheryl Blundon
Executive Director and Board Secretary
Board of Commissioners of Public Utilities
P.O. Box 21040, St. John's, NL  A1A 5B2
120 Torbay Road, Prince Charles Building, Suite E-210
T: 709-726-8600 | F: (709) 726-9604 | E: cblundon@pub.nl.ca

**Letter of Comment – ECCC analysis of Grant Thornton's June 2023 report**

On May 31, 2023, ECCC provided feedback on the assumptions and methodologies used in two analyses: *Assessment of petroleum product benchmark options to support price regulation in the Atlantic Provinces* by Gardner Pinfold Consultants Inc. and *Review of the Cost of Carbon Adjustor Mechanism* by Grant Thornton Inc.

ECCC determined in the feedback of May 31, 2023, that the approach used in the two analyses significantly overestimated CFR compliance costs in 2023 compared to ECCC analysis, as published in the Regulatory Impact Analysis Statement (RIAS) accompanying the final regulations (https://www.canadagazette.gc.ca/rp-pr/p2/2022/2022-07-06/html/sor-dors140-eng.html).

- Enough credits are expected to be available in 2023 (13.4Mt in Canada) to allow for compliance with the reduction requirements (4.7Mt in Canada). Annual reduction requirements in NL in 2023 represent 0.6% of the credits expected to be created and banked in 2022 and 2023. The likelihood that primary suppliers of gasoline and diesel to NL cannot purchase credits on the market is low. Compared to an approach that relies solely on renewable diesel purchase, credit purchase is expected to be lower cost.
- It is estimated that credit creation from actions that are expected to occur in the baseline, plus banked credits from previous years, will be sufficient to fulfill the regulatory requirements in 2023 and 2024. These credits may also be created at relatively lower costs.
- Renewable diesel is supplied to BC and the credit costs under BC LCFS has never reached \$622/tonne[1]. Renewable diesel is also supplied in other provinces. This indicates that the assumptions and calculations used in the analyses *Review of the Cost of Carbon Adjustor Mechanism* and *Review of Clean Fuel Regulations* tend to overestimate the cost per liter that is necessary to pay in order to purchase renewable diesel in Canada and compete with California.

On June 21, 2023, Newfoundland and Labrador's Board of Commissioners of Public Utilities provided ECCC with Grant Thornton's June 2023 report on the potential costs for suppliers in Newfoundland and Labrador associated with the federal Clean Fuel Regulations which become effective for motor fuels on July 1, 2023.

The approach used in Grant Thornton's June 2023 analysis continues to significantly overestimate CFR compliance costs in 2023 compared to ECCC's analysis.

This approach continues to assume compliance mostly based on renewable diesel, one of the most costly of all compliance options under the Regulations.

[1] See variable R in Appendix C of the analysis *Review of the Cost of Carbon Adjustor Mechanism*

We recognize that the updated formula proposed in Appendix D of the June 2023 report takes into account the compliance fund, a compliance flexibility that may be used by primary suppliers, before purchasing credits at a higher price. As such, this updated formula better reflects the compliance options under the CFR than the original formula (Appendix C, renewable diesel only).

However, it does not fully reflect the compliance options available. Should you choose to use it, the updated formula may be further modified to take into account the flexibility within the CFR for primary suppliers to defer 10% of their 2023 obligation to 2024, until such time they can create credits or more credits are available on the credit market and the credit market has become more established. Taking into account the 10% deferral would mean changing the variable AH in the updated formula from 90% to 80% for compliance via renewable diesel.

In rows 30 to 32, the June 21 report notes:

*However, regulatory practice typically matches cost recovery to the period in which the cost was incurred. As such, the proposed mechanism does not incorporate an adjustment for a short-term compliance deferral.*

Please note that if 10% of the 2023 obligation is deferred to 2024, the compliance report including the retirement of credits for this deferral, will be submitted in 2025, in respect of the 2024 compliance period.

The approach used in Grant Thornton's June 2023 analysis is based on stakeholder concerns that supplying E10 (and even B2) will not create sufficient credits in the near term to meet compliance obligations and that it will not be possible to purchase credits on the market in 2023 as a liquid credit market in Canada will not exist. There is no evidence that there will be a lack of credits in the market in 2023. Credits created by primary suppliers or credits available on the market may be purchased in 2024 to comply with this 10% deferred to 2024. The cost of credits on the market in the early years of the CFR is expected to reflect the following conditions:

- The regulatory obligation is small at the outset andit increases gradually over time;
- In early years it is expected that there will be 3 times as many "business as usual" credits on the market than are required by regulated parties to come into compliance.

Sincerely,

**Judy Meltzer**
Director General
Carbon Markets Bureau
Environment and Climate Change Canada