

CANADA RELEASES DRAFT OIL AND GAS SECTOR GREENHOUSE GAS EMISSIONS CAP REGULATIONS

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The Government of Canada recently released Proposed Oil and Gas Sector Greenhouse Gas Emissions Cap Regulations (“Proposed Regulations”)^[1] under the *Canadian Environmental Protection Act, 1999* (“CEPA”).^[2]

The Proposed Regulations set a cap on greenhouse gas (“GHG”) emissions from the oil and gas sector, equivalent to 35 percent below 2019 levels. They also aim to provide for some compliance flexibility through a cap-and-trade system based on Canadian offset credits and through decarbonization units, for a total of 20% of remittance obligations.

Consultation on the Proposed Regulations is open until January 8, 2025.^[3] The Government has indicated that it proposes to publish the final regulations in 2025 and for them to be in force in 2026.

Background

In 2022, the Government of Canada put out a discussion document called *Options to Cap and Cut Oil and Gas Sector Greenhouse Gas Emissions to Achieve 2030 Goals and Net-Zero by 2050*.^[4] The paper sought input on two potential regulatory approaches:

- the development of a new cap-and-trade system under the CEPA, and
- changes to existing carbon pollution pricing systems under the *Greenhouse Gas Pollution Pricing Act* (“GPPAA”).^[5]

Based on the feedback received, the Government designed a proposed regulatory approach for a national emissions cap-and-trade system. The *Regulatory Framework for an Oil and Gas Sector Greenhouse Gas Emissions Cap* was published in late 2023 and again engendered significant feedback.^[6]

Unsurprisingly feedback differed as between interested parties. Oil and gas-producing provinces and industry questioned the rationale for the cap and raised concerns around the need for, stringency of the cap and its potential impact on the economy and energy security. Environmental organizations meanwhile provided feedback primarily designed to support a strict regulatory system including concerns about compliance flexibility. Indigenous groups provided views about potential impacts on their rights and economic interests.

Outline of the regulations

The Proposed Regulations would set up a national cap-and-trade system in the oil and gas sector, covering upstream oil and gas activities. The cap would be on emissions.

The Proposed Regulations would:

- Apply to operators rather than facilities. Operators would be responsible for all facilities under their control and all operators would have to register and meet reporting deadlines starting in 2027 for 2026 emissions.
- Prohibit an operator emitting GHGs from any of the relevant activities at its facilities unless the operator is registered.
- Establish a threshold for determining which operators are covered under the emissions cap and therefore are subject to remittance obligations and eligible to receive emissions allowances. A covered operator would be any operator whose cumulative production in a calendar year is 365,000 barrels of oil equivalent or more. The operator would remain a covered operator until its total production was less than half the annual threshold for four consecutive years.

The Proposed Regulations would require Operators to remit one allowance for each tonne of carbon emissions that the operator has emitted. There would be a total number of emissions allowances equal to the emissions cap, and these would be distributed free of charge to remitting operators. Operators with remittance obligations would be able to buy allowances from other operators.

The sector would be permitted some emissions above the cap using compliance flexibility units which are eligible Canadian offset credits and decarbonization units. Decarbonization units come from contributing to a decarbonization program which would fund projects that support the reduction of emissions from the sector.

Operators would be permitted to use eligible offset credits to meet obligations under carbon pricing regimes as well as remittance obligations related to the cap.

The Proposed Regulations do not permit the use of carbon offset credits from other countries as a compliance option. However, the Government has indicated that it continues to consult on this issue and that the final Regulations could include what are called Internationally Transferred Mitigation Outcomes as a compliance mechanism.

Key issues

The cap for emissions from the sector set out in the Proposed Regulations is 27% below reported emissions for 2026. The Government projects that this will be 35% below 2019 emissions levels and maintains that the regime

is designed to be technically achievable based on current technology.

The Government aims to provide compliance flexibility options in the Proposed Regulations. One outstanding issue is that the Proposed Regulations only enable domestic carbon offset credits to be used. This is an area where the Government has stated it will continue to consult. In addition, the allowances cannot be used with other regulatory systems that are not in Canada.

Legally the cap is a cap on emissions. The Government's position is that production can continue to grow while emissions are reduced under the cap. Some stakeholders assert that the cap will reduce production and be a disincentive for investment.

An important question is how the cap interacts with a complex suite of other regulatory measures taken to reduce greenhouse gas emissions including the industrial price on carbon under the *GGPPA* and provincial regimes, the *Clean Fuel Regulations*,^[7] the proposed *Clean Electricity Regulations*^[8] and the *Regulations Respecting Reduction in the Release of Methane and Certain Volatile Organic Compounds (Upstream Oil and Gas Sector)*^[9] along with their proposed amendments.^[10]

Finally, Alberta has indicated that it is exploring bringing a constitutional challenge to the Proposed Regulations on the basis that exclusive jurisdiction over natural resources lies with the provinces.

For any questions regarding the Proposed Regulations or other environmental matters, please contact one of the authors or your McMillan relationship partner.

[1] News Release: [Canada releases draft regulations to cap pollution, drive innovation, and create jobs in the oil and gas industry](#) (November 4, 2024).

[2] S.C. 1999, c. 33.

[3] [Canada Gazette, Part I, Volume 158, Number 45: Oil and Gas Sector Greenhouse Gas Emissions Cap Regulations](#).

[4] [Options to cap and cut oil and gas sector greenhouse gas emissions to achieve 2030 goals and net-zero by 2050 - discussion document](#).

[5] S.C. 2018, c. 12, s. 186.

[6] [Regulatory Framework for an Oil and Gas Sector Greenhouse Gas Emissions Cap](#).

[7] SOR/2022-140.

[8] Canada Gazette, Part I, Volume 157, Number 33.

[9] SOR/2018-66.

[10] Canada Gazette, Part I, Volume 157, Number 50.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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