Maximizing Clean Tech Investments: Insights On CCUS Tax Credits For Canadian Businesses (Podcast)

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In this episode, hosts Brendan Sigalet and Derrick Osborne are joined by fellow Bennett Jones lawyers Shawn Munro, Luke Morrison and Sharon Singh, as they offer invaluable insights into the successful development and deployment of carbon capture, utilization and storage (CCUS) projects. Together, they unpack the complexities of the CCUS tax credit, revealing how this crucial incentive can significantly reduce industrial emissions while fueling sustainable growth across Canada.

An in-depth exploration of the CCUS tax credit is provided, highlighting its profound impact on businesses venturing into carbon capture. Industry leaders share practical advice on building and optimizing CCUS projects, equipping companies to stay competitive in this rapidly evolving sector. Additionally, the discussion covers strategies for overcoming regulatory hurdles and maximizing returns through effective use of tax incentives in CCUS ventures.

Tune in to stay informed and strategically positioned in the dynamic world of sustainable development.

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a tax perspective with the way the federal governments shape this tax credit. It contemplates a CCUS project being anything from capture only to transportation to storage only. But if you don't have anywhere to store your carbon there's not really any reason to capture it.

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Brendan Sigalet: [00:00:30] Welcome to Clean Incentives a podcast series within the Bennett Jones Business Law Talks podcast that discusses topics around taxation incentives for developing clean technology projects in Canada. I'm Brendan Sigalet and together with my colleague Derrick Osborne we are the host. For this podcast series.

Derrick Osborne: [00:00:47] Barnett and I are tax associates at Ben and Jones LLP and our practice includes advising on tax aspects of energy transition deals including renewable energy carbon capture and hydrogen projects.

In today's episode we're focusing on carbon capture utilization and storage investment tax credit otherwise known as the CCUS tax credit. The CCUS tax credit is designed to support the development and deployment of projects that capture transport store or use carbon emissions from industrial processes.

Brendan Sigalet: [00:01:22] Before we begin this podcast please note that anything set or discussed on this podcast does not constitute legal advice. Always seek proper advice from your legal advisor as every situation is different and outcomes can vary.

Today we are joined by Shawn Munro Luke Morrison and Sharon Singh. Shawn is a partner in the firm's regulatory and environmental practice group. He advises and represents clients in relation to the regulatory and environmental aspects of oil gas uh electricity developments including

regulatory proceedings for wells pipelines batteries upgraders plants power transmission lines carbon capture and storage.

Luke Morrison: [00:04:02] Sure. Thanks Brendan. And generally across the board you're going to have a CO2 emission source and that can be from. Oil and gas processing other generation operations pet cam industrial processes uh in a future podcast we will we'll talk about CCUS as being a key enabler for blue hydrogen and ammonia projects that's producing hydrogen from hitting methane with steam and then and then doing capture and storage from that.

But I think that's that's a good example of. of how CCUS as a tech is being deployed. So you you have your mission source. You'll apply different types of technology. Dealing with nitrogen is a really common element on the front end at the mission source. You'll have depending on the tech one way or the other typically have an amine or solvent solution at the capture source.

Shawn Munro: [00:06:19] Sure the normal use of CCUS is carbon capture and storage and. That involves as Luke mentioned capturing the carbon from the emitter and injecting it for be all and end all into the deep underground formation.

CCUS implies a utilization and that utilization uh can be for a couple of things. It can be for enhanced oil recovery and it also can be for uh CO2 use for feedstock for industrial purposes. So it's it's really a nomenclature thing but a number of the benefits that are available for CCUS aren't necessarily available for uh for CCUS.

Sharon Singh: [00:09:25] You know and generally speaking CCUS projects or CCUS projects being really the jurisdiction lies with the provinces um there will be some discrete situations where the feds may get engaged. So really what yoU.S.ee is by and large the provinces leading the charge here. I would say um Despite being in B.C. that Alberta it has obviously more

experience um with these projects predominantly because of the nature of the industry and the activities and the uh geological formations in that province. The B.C. Energy Regulator is the body here that regulates CCS or CCUS projects under the Energy Resources Act.

Brendan Sigalet: [00:15:17] Yeah and that kind of meshes in with the uh how this CCUS tax credit is intended to operate because in the dedicated geological storage. It's specifically restricted to jurisdictions with this kind of robust regulatory framework in order to ensure that the carbon isn't released at some later date. Um and and I think that that's partly why that they have put these restrictions in place as far as the different jurisdictions where this can operate.

And then additionally in uh the type of storage that will actually qualify you know it sounds like a lot of work in order to actually you know get all your ducks in a row as it were to actually get this storage qualified such that you could do this carbon capture.

Luke Morrison: [00:16:16] And I think you know an important point of where where Shawn just went through is technology and expertise particularly in Alberta on around management of gases generally including CO2. It's the technology itself is is pretty well trodden.

There's a lot of expertise in the province as well in the industry for running these these assets safely and long term. So the current kind of boom and surge of these larger CCUS hubs is in a lot of ways leveraging that expertise. Another important point the current surge it's not the first large project of this sort.

Shawn Munro: [00:18:55] And think of a think of a hub as like a wheel which is what it is. It's hubs and spokes. So you've got a sequestration facility in the center in the hub and the goal is is to allow for spokes being gathering lines to take

CO2 that’s captured from emitting sources from generation activities migrate them down the spokes to the central hub.

And the intent is to make this uh As much as possible not the vertical integration model that we’ve seen in past whereby you’ve got an emission source and you’ve got a you’ve got a single line to a sequestration facility but rather a service provider. So any party who’s not expert in any given industry can still capture and flow CO2 for injection to that central hub. So the goal is to have all of these wheels plop down across the province in strategic locations.

Derrick Osborne: [00:19:53] And I think that makes sense from a tax perspective with the way the federal governments shape this tax credit. It contemplates a CCUS project being anything from capture only to transportation to storage only. But if you don’t have anywhere to store your carbon there’s not really any reason to capture it.

So the CCUS hubs I think are really the precursor to getting this industry going. And what’s interesting from a tax perspective is you lose. Or have a clawback on your income tax credit to the extent that it’s not put to an eligible use. Have you guys dealt with any situations or contracts where somebody’s taking carbon from the capturer and is off to store it but it’s not clear what that carbon is going to be used for?

Luke Morrison: [00:20:53] Yeah I can start on that one Derrick. It’s a good question. I think using Shawn ‘s visual metaphor of the hub and spokes the projects we’re seeing so far they’re pretty linear. Can you use the Shell Atco Atlas example? Which was in the news yesterday a pretty major announcement. There’s an FID on uh the first phase of the Atlas Carbon storage hub. And on that project the first phase emissions being supported is is Shell’s Polaris Project.

That’s shell’s uh energy and chemicals park in Scotford. And

that one you know you have about 650000 tonnes of CO2 a year. Coming off operations there. So that one from that complex there's about a 22 km pipe that's going to be built out of out of the capture facilities to the injection site which takes currently two injection wells. So the commercial arrangement for that is a good example.

Shawn Munro: [00:22:32] Yeah the provincial vision is certainly and I don't know Sharon what it's like in B.C. and Alberta certainly it's intended to be open access to as much as possible. So the goal is to create a hub and it may well be supported by one or two or three emitting sources. Initially but the goal is is to allow parties to access these hubs as that trunk line starts to branch out and or other lines branch out to um to migrate that emitted CO2.

I don't know Sharon if that's a similar priority in British Columbia to make these things open access.

Brendan Sigalet: [00:23:08] Yeah and I was going to actually ask uh Sharon it sounds like we have this you know this contemplated idea of having these you know the hubs but you had mentioned previously that you know the basin as far as it's concerned in B.C. doesn't necessarily have the same capacity for storage. Um so is that kind of envisioned as a potential path forward for B.C.?

Sharon Singh: [00:23:28] Well I think there's a couple of things here in terms of when I think the previous discussion we've had around um proven suitable reservoirs. And of course the Western Canadian sedimentary basin has that proven suitability. Uh however it doesn't really extend out to um the rest of B.C. It's only a small chunk of it.

The other basins that we have you know the suitability of those basins isn't something that has yet been either confirmed or is very much in preliminary phases. And some you know the geological seals may not be there. There might be

limited information and the information to date has been shown to be mostly unfavorable. So I think we in B.C. and I'm not a technical expert here but we know that there's known sizes for certain depleted gas bowls. But in terms of where the opportunities lies I I think the open hub concept for B.C. makes sense.

Brendan Sigalet: [00:24:50] Interesting. And Sharon and I just wanted to ask about one other question. There's another class of specified percentage or the percentage that you actually get as far as the ITC is concerned and it's for direct capture. And so that's a 60 percent investment tax credit. Uh and understandably you know the policy reason behind it is because. You know how are you going to make money just capturing CO2 from other just directly out of the air rather than from your own project? And I understand that you potentially might know of some projects that are actually getting built to do this direct capture.

Sharon Singh: [00:25:25] So I mean I think B.C. is quite proud to host one of the leading providers of this technology which is carbon engineering. Um they provide a direct air capture technology. We've had a pilot plant in Squamish and it's been it's only a pilot since 2015. Unfortunately they decided to build up the commercial project plant in Texas but uh and there are relationships with um Occidental for instance where to your point around why would you just suck carbon out of the air um without you know You know some form of incentive to do so.

I think there are incentives and they are linked to uh industrial activities. So carbon engineering is probably the example that I can provide of. Just DAC in general hasn't to my knowledge in any event it's very exciting. But uh I haven't seen and maybe Luke or Shawn you have the take up of those yet at a scale like in the U.S. and those partnerships announced like in the U.S. uh as in um in Canada at the moment.

Shawn Munro: [00:26:25] I refer to it as an enabling technology in a lot of ways that is the drivers for this is not necessarily only the economics of the supply of CO2 to the service provider for sequestration but it also allows for and will be critical going forward for you know oil sands Uh for laser cement production um all sorts of different hydrogen all sorts of different projects.

Derrick Osborne: [00:26:54] I was also curious so you build a carbon capture project and the economics are really changed because of the CCUS tax credit. The idea is to make these things viable in Canada especially in competition with what's happening in the U.S. after the Inflation Reduction Act. But what makes Canada unique is that we also have the carbon tax.

Uh which means if we have an equally good tax credit as the U.S. you're still worse off building in Canada. So I'm curious if the economics of building a CCUS project in Canada also take into account any other benefits you get from capturing carbon such as emission offset credits.

Luke Morrison: [00:27:31] I think the short answer is absolutely. The economics of any of these projects is certainly underpinned by you know current legislation and what's going to occur at the federal level with the federal carbon plan and uh you know achieving net zero goals. I think the you know you don't have to look any further than a couple of months ago when Capital Powers Genesee CCUS project was shelved.

You know the economics generally were cited as the reason that that project wasn't going ahead. That that one was a. A natural gas fire generation plant there would have been capture facilities utilized there at site and then the type of sequestration we talked about earlier would have occurred after the point of capture there.

Luke Morrison: [00:27:31] … You contrast that with some of the

other projects we're seeing in petrochemicals and other industries. In those cases, you have the same kind of models running through in different ways, but it's different technology with capture, and I think that's where you're seeing still kind of early days.

There's a few transactions announced where the Canada Growth Fund is stepping in to be an offtaker, entering into a contract for difference. To provide some stability on what the price of credits off these projects is going to be, the mandate of that federal organization, large amount of capital allocated, that's precisely the goal of that program is to provide more certainty to proponents in the face of the market. And then, complimentary to what the CCUS ITCs are.

Brendan Sigalet: [00:29:52] And that brings up an interesting point in respect of government assistance. So a lot of these clean economy ITCs are reduced by any assistance received from the government. That means you have your capital cost of whatever equipment that you're buying, which is just the cost of the asset plus installation costs, legal costs to acquire, and that sort of thing.

Then, you get your specified percentage, which, as we've discussed, is your top line percentage times your eligible use percentage. But for other clean economy ITCs, that's actually reduced by the capital cost of their assets is reduced by any government assistance that's been received by the corporation claiming the ITC. But for the CCUS Tax credit, they actually made the conscious decision not to decrease the capital cost by that government assistance received by the project.

Brendan Sigalet: [00:31:02] So to your point, as far as the economics of it, they're trying to incentivize these projects to go ahead in multiple different ways. And it's kind of multifaceted in terms of the funding source for a lot of these projects. And that brings me to the next point I want to touch on, which is regarding the eligible use percentage. We've kind

of chatted a bit about it. And I'm getting the broad outline of how it works.

To determine your projected eligible use, you have to submit a project plan to the Minister of Natural Resources. That'll give you what your estimated eligible use will be, and then, you have to comply with many different compliance obligations going forward. One of which is to submit annual reports for a five-year period, calculate your average actual eligible use percentage, and if it's more than five percent less than what you projected, there's a clawback of the ITC. The clawback period extends up to 20 years, so there are significant compliance issues.

Luke Morrison: [00:32:19] So to address that question, Brendan, yeah, I think the answer is certainly the presence of a clawback itself. I don't think it's that dissimilar to other programs, whether it be royalties, other tax credits, or other government credits; the concept is that actuals have to align with what you filed, and if they don't, there's going to be an adjustment.

So commercially, you have monitoring provisions across the board influenced by that, even when it comes to a joint venture context. When you think of the end of the project, there's consideration for ensuring those things are cleared up before you completely wrap things up. The thing that comes to mind most, however, even more than all that, is what we're seeing in the insurance market. And in the last year, six months in particular, it's really starting to scale up.

Luke Morrison: [00:33:26] We're hearing activity in the U.S. a little bit ahead of Canada, but there are products on the market now to address exactly that risk. It's looking at products that can address how reassessments can impact economics, what the policies look like, premiums, and exclusions around that. With 45Q, we're not in the realm of theory anymore. We're hearing that there are projects further

along there with policies that are in existence.

And a lot of projects across Canada with similar concerns on the heels of the CCUS ITC coming into play are looking at those same products for the same drivers.

Brendan Sigalet: [00:34:01] Interesting. Yeah. So generally, as I understand the ITC insurance market, we've been involved in a couple of projects where we've got involved a little bit, but you have to get basically an opinion or maybe not an opinion, more of a memorandum of the issues.

And from my understanding, generally, if you know we can get the right opinion on it or a memorandum of the issues and grasp the risk, then it can be insured. So, have there actually been projects able to get insurance in Canada for the CCUS clawback risk, or is it too early given that C-58 and C-69 have just been passed?

Luke Morrison: [00:34:41] Yeah, I think as of the time of recording this podcast, there are discussions with brokers and underwriters happening in real-time. And I think the general view we're hearing is that the U.S. projects are a bit further along, in part due to the IRA funding down there. There are models, different legislation overarching, notwithstanding similar concepts. So like you said, Brendan, exactly, the sequence to get that insurance with getting an opinion on the nature of the project, the eligible use, and any risks around a reassessment occurring, that same model would happen here.

The projects we're seeing that are still in development are all taking that into account. It's starting to get built into models. It's more than just placeholders now, and it's a process that involves engaging with brokers and underwriters, understanding what the premiums are going to be, and the exclusions, and offhand, I think those are the kinds of things that will get implemented more fulsomely in the next year or two when projects get into critical FID stages and those

products are more than just paper slides. They can get placed and underwritten.

Brendan Sigalet: [00:35:59] Yeah, interesting. And interesting you bring up the United States as far as the different markets. I want to emphasize that there are similar ITCs in the U.S. under the Inflation Reduction Act, but there are key differences. And I think that the Canadian incentives are competitive. But one area in which the U.S. ITCs are a bit different is through this idea of production ITCs.

As compared to the Canadian context where we just have this investment tax credit for the actual capital cost of the equipment to build this, but not necessarily the same support on an ongoing basis. Has that come up at all in projects trying to decide which jurisdiction to operate in?

Shawn Munro: [00:36:46] I think there's a clear path. It's a complex path, and that path is in Canada. Perhaps our regulatory approval processes have been colored a little bit by some delays, but I think there's a lot of willingness to move these types of projects forward. I think you will see Canadian regulators work hard to evaluate projects fairly and quickly on an expedited basis so that companies can start to move forward, given it's so critical to so many industries.

So I think sometimes there's an unjust comparison with the suggestion that it's impossible to get major projects approved north of the border, which clearly isn't correct. So we do our best to encourage investment in the country by companies who can be confident that we have probably one of the best regulatory frameworks in B.C., Alberta, Saskatchewan, in the world for these types of things.

Brendan Sigalet: [00:37:47] Sharon, I know you mentioned earlier about getting up-front indigenous participation in a lot of these projects as being a requisite aspect of getting these projects built, not only from the regulatory perspective

but from a business development perspective as well.

So I just wanted to touch a bit on that and how these projects are being structured. Shawn and Luke, feel free to jump in since I know you both have a lot of structuring expertise.

Sharon Singh: [00:38:17] I think, in broad strokes, there's sort of two buckets. One is the traditional engagement consultation bucket, and within that stream, you can have partnerships as well. You can have partnerships around joint ventures, procurement, services, other forms of environmental management services, etc., but there is no ownership in, say, the infrastructure or the project itself.

And then you have the other stream, which is equity participation in either the actual CCUS project or adjacent infrastructure that enables the CCS project. Both are important, and both depend on the type of project, the risk tolerance of the nation or nations, funding opportunities available, and so on.

Sharon Singh: [00:39:10] I don't have a preference for saying one is better than the other because I think it really depends on the project's economics, the community's objectives, and the opportunity it presents for them. We are seeing a lot more equity participation occurring simply because it is now more mainstream in terms of the availability of funding and the willingness on both sides to entertain such opportunities.

There is also the scale of access to capital for equity participation that is occurring because it's not just equity for support in many instances. It's more than that, and some projects have that form of equity participation. There are nation-led projects also being contemplated, and there are other initiatives that rely more on the collaboration and consultation framework to address impacts or potential opportunities without needing equity participation.

Sharon Singh: [00:41:49] We often look at CCUS as a necessary

means to achieve our net-zero ambitions in this country and therefore believe it ought to be supported by all rights holders and stakeholders alike. But there are still many concerns that remain, and we can't take that support for granted.

There is a public education piece that is often missing in the discourse. We need to get out there and address it on a broad scale with the public, nations, NGOs, and dispel some of the myths out there. Also, emphasize the enormous amount of safety protocols in place and the rigor of our regulatory processes to ensure the risk is minimized to the greatest extent possible.

Brendan Sigalet: [00:42:10] That's an interesting concept. I always think about First Nations getting involved in the equity side, but getting First Nations' engagement on the other side is crucial for getting these projects built.

I often overlook that from just being a tax guy and think, "Okay, it's structuring, let's go."

Shawn Munro: [00:42:35] No, I'm just going to say the same thing. In any given project, there will be multiple First Nations who will be active in those areas, who may claim traditional lands in those areas, and there's an engagement obligation through regulatory processes. As well as through the provincial consultation office that all has to get done quite irrespective of any equity engagement.

It's really important to remember that this is, as I called it earlier, an enabling technology, so it's not fully embraced by parties who believe there ought not to be any of those.

Luke Morrison: [00:44:11] Brendan, for what you just said about what you and Derrick would do on the tax structuring side. I think as Sharon alluded to, you have models for different types of participation with First Nations that have been used on other projects that we're certainly seeing in

CCUS.

You add into the mix that the different proponents we talked about earlier, across industry from traditional E&P to midstreamers, industrial emitters in a wide variety of sectors, municipalities, and so forth, you get into some pretty complex equity ownership structures in a lot of these cases.

Luke Morrison: [00:45:31] And I think assumptions on how things like tax credits would normally work have been upended in CCUS. Some of the work you and our group have been doing on that front when it comes to structuring, there's been a lot of analysis done, and some different models have emerged as the ITC is taking shape.

Brendan Sigalet: [00:45:59] This whole conversation speaks to the idea that there isn't a one-size-fits-all solution for any of this. Every project, every participant, is a bespoke and convoluted bunch of parties and issues that need proper attention by the tax advisors, corporate counsel, and regulatory advisors on the file.

And that's critical to making sure these projects are successful.

Luke Morrison: [00:46:35] Absolutely, Brendan. Each CCUS project is unique and complex, and it's essential that we tailor the approach to each situation.

Brendan Sigalet: [00:46:47] Thanks for taking the time to listen to this episode. Don't forget to hit the follow button and like button on whatever podcast platforms you're using to listen. Take care, and we will catch you in the next episode.

Authors/Speakers: Brendan Sigalet, Derrick Osborne, Sharon G.K. Singh, Shawn Munro, Lucas (Luke) Morrison

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