

Western Leadership for a Canadian Energy Strategy

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Contents

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

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- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

THE CANADIAN ENERGY CHALLENGE

Every country in the world faces growing energy challenges, and Canada is no exception despite our wealth of resources. At the Canada West Foundation, we believe that coming to grips with how we produce and use energy is one of *the* critical policy imperatives of our age.

- ▶ The world has vast energy resources, of which Canada has a large share, but our ability to develop resources and move them to market in a way that is socially acceptable and environmentally sustainable is increasingly constrained. Countries that innovate with new approaches to regulation, new institutions for resolving social issues, and lower impact technologies will be among the economic leaders in the 21st century.
- ▶ Energy costs are likely to rise and possibly rise substantially in coming years because of increasing constraints on resource and infrastructure development, growing demand in a highly interconnected world, and the need to meet environmental imperatives. The energy cost challenge is also a productivity challenge, and countries that can increase their energy productivity will have lower cost structures with positive consequences for competitiveness and reduced strain on their social fabric.
- ▶ The physical environment is increasingly understood as a precious resource and no longer a costless dumping ground. Multiple environmental imperatives including the massive challenge of climate change will be prominent in the energy debate in coming years. The countries that succeed in the 21st century will be the ones that invent new approaches to energy that meet those environmental tests while ensuring that the core energy objectives of security, reliability and affordability are maintained.

In short, we would argue that many of the most important global policy choices in the decade to come will centre on the production and consumption of energy.

If Canada faces difficult energy challenges, we also have huge corresponding opportunities. We have an immense array of energy assets. We are the world's 5th largest energy producer of energy¹—the 3rd largest natural gas

1 <<http://www.capp.ca/library/statistics/basic/Pages/default.aspx#wH3E5XyDSXtq>>

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

producer, the 6th largest oil producer, and the 7th largest electricity producer.² We are the 3rd largest natural gas exporter, 4th largest oil exporter, and 3rd largest electrical power exporter.³ We are also the world's 3rd largest energy consumer on a per capita basis.⁴ Thus we not only produce but also export a diverse range of energy commodities and are home to many successful, world scale energy companies. Although we are far from meeting the claim that we are a clean energy superpower, we have many of the assets needed to make us a global leader in energy.

2 *The World Factbook*. 12 October 2010 <<https://www.cia.gov/library/publications/the-world-factbook/geos/ca.html> >

3 Ibid.

4 Ibid.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

A STRATEGIC RESPONSE

Many individuals and groups have come to the conclusion that this potential will only be realized if it is harnessed to a *Canadian energy strategy*, a platform of principles, goals and policies upon which we can build a sustainable energy future. We need much more than fortuitous energy endowments; we also need a clear sense of direction, a *vision* if you like, and an equally clear identification of the policy principles and tools that can be brought into play to realize that vision. In other words, a future shaped in some measure by design rather than by good fortune alone.

This conclusion has led the Canada West Foundation to be one of many voices calling for a Canadian energy strategy. We began this journey in 2008 with a series of regional roundtables testing and then demonstrating western Canadian receptivity to such a strategy.⁵ The 2009 Energy Framework Initiative (EFI), to which the Canada West Foundation contributed, stopped short of calling for a strategy *per se* but argued for an energy policy framework as the first step in this direction.⁶ A recent paper from the think tank community reflects the consensus of a diverse range of stakeholders, including the Canada West Foundation, on the need for a Canadian energy strategy.⁷ The newly created Energy Policy Institute of Canada (EPIC) is determined to advance this need, and the Senate's Energy, Environment and Natural Resources Committee has embarked on an ambitious effort to frame a Canadian energy strategy. The chorus is growing larger and stronger.

The case for a Canadian energy strategy that can be abstracted from this set of initiatives rests on a number of premises:

- ▶ the importance of energy to a widely dispersed, climatically challenged and export-driven Canadian economy;

⁵ Roger Gibbins and Kari Roberts, *Canada's Power Play: The Case for a Canadian Energy Strategy for a Carbon-Constrained World*. Canada West Foundation, September 2008.

⁶ The Energy Framework Initiative was supported by the Canadian Association of Petroleum Producers, the Canadian Energy Pipelines Association, the Canadian Gas Association and the Canadian Petroleum Products Institute. See energyframeworkinitiative.ca.

⁷ See *Towards a Canadian Clean Energy Strategy, A Summary of the Banff Clean Energy Dialogue*, April 8-10, 2010.

▶ The Canadian Energy Challenge

▶ A Strategic Response

▶ Strategic Objectives

1. *Security*

2. *Affordability*

3. *Environmental Performance*

4. *Culture of Innovation*

▶ Principles

1. *Economic Principles*

2. *Social Principles*

3. *Environmental Principles*

4. *Political Principles*

▶ Western Canadian Policy Leadership

▶ Next Steps

- ▶ the need to develop an energy strategy that complements but *is distinct from* Canadian climate change policy;
- ▶ the need to bring a greater degree of policy coherence to 14 different federal, provincial and territorial energy strategies, and thus to avoid further fragmentation of the economic union;
- ▶ growing pressures for policy coordination and harmonization with our largest trading partner and energy market, the United States; and
- ▶ growing concerns about energy security, and about the social license to build and operate large energy developments.

Underlying all of these points is the conviction that a robust, coherent and comprehensive Canadian energy strategy can help us realize our ambitions for a prosperous and sustainable future, for meeting climate obligations, and for remaining competitive within the global economy.

In the final analysis, of course, a fully developed Canadian energy strategy lies in the hands of governments with jurisdictional competence including, most emphatically, provincial and territorial governments. Those of us outside government need be cautious of overreach; a working “strategy” for all of Canada including its diverse regions and government actors is undoubtedly far too big a project for those in civil society. On the other hand, what civil society can do is to help organize the thinking from a variety of perspectives. It can help frame consensus where consensus can be found. It can raise the quality of debate where reasonable people simply disagree. And, it can serve as a constant prod to governments who may well view the inter-jurisdictional energy policy landscape with some apprehension.

The first step in such a contribution is to find some measure of agreement on the basic objectives of such a strategy—what are we trying to achieve?—and the principled scaffolding within which detailed policy development can take place. Here our thinking has been shaped by policy work from a variety of groups and initiatives, including those referred to above.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

STRATEGIC OBJECTIVES

What are the objectives—the outcomes—to which Canadians aspire between now and say, 2050? What do we want the Canadian energy system to look like in 2050? An energy powerhouse, a clean energy superpower or simply a very good steward and successful economic competitor in the realm of energy? Such visioning is never simple, but here we suggest four essential strategic objectives to frame our thinking.

1. Security

Security underpins everything because without it the energy debate—and society with it—stops cold. Pun intended. We propose that security needs to be understood as having four elements:

- ▶ The first and the one most associated with the term is energy security in the geopolitical sense, reflecting the fact that major oil supplies are found in troubled areas of the world.
- ▶ The second is infrastructure capacity to get resources to users.
- ▶ The third is operational reliability—the capacity to keep the system operating day to day and to prevent or expeditiously manage mishaps such as electricity blackouts.
- ▶ The last is security against deliberate attack—cyber or physical; politically or criminally motivated.

Security of the energy system is made up of all of these elements. It is an area where our society has been remarkably successful and where Canada's objective, broadly speaking, is a question of maintenance, enhancement and nimbleness in the face of constantly changing global circumstances.

A common refrain is that Canadians needn't worry about energy security. For several reasons this is a view to which we do not subscribe:

- ▶ Canada is one of the western world's most important energy assets due to our ability to contribute our physical resources, experience and ideas to global energy security.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

- ▶ Canada is tied into world and continental energy markets as an importer as well as an exporter, and disruptions elsewhere affect us directly.
- ▶ Canada's economic health is tied to that of our trading partners who might be affected by disruptions or price spikes.
- ▶ Finally, we are as vulnerable as any country to potential failures to ensure system adequacy, operational reliability or security against attack.

There is little room for complacency. If anything, Canadians should be thinking more about our world in 2050 and how secure we are against being stopped, and stopped cold.⁸

2. Affordability

We place affordability second in importance to security. More often than not Canadians equate affordability with the notion of “cheap” as in cheap hydro power. Many argue that gasoline prices should never rise, and that the energy delivered to their homes will always be “cheap” even as the costs of supplies and associated infrastructure rise. However, the simple reality for the future is that energy costs will probably rise for a variety of reasons outlined earlier.

In this context, affordability might best be approached along both economic and social dimensions. On the economic front, the issue is not cheap energy but energy costs that compare favourably to those of our economic competitors. In this sense, the issue is how productive we are in the use of our energy capabilities—not only resource production, but delivery capability and efficiency at point of use. In a word, it is not about energy (or resource) efficiency but efficiency in a whole system and total factor sense. Our objective for 2050 should be to be as efficient as possible in that large sense and thereby contribute to our economic competitiveness. To repeat, affordability is not all about cheap energy.

On the social front, the issue is one of equity for those least able to afford energy whether cheap or not. People in the lowest income ranges face disproportionately high energy bills as a share of household disposable income and if energy costs do rise, this burden is potentially unbearable

⁸ For example, Nexen Global Roundtable on Energy, Environment and Economy, Energy Security Conference, Calgary, Alberta October 13, 2010.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

for those most affected and unacceptable to society at large.⁹ There are several potential policy responses to this problem. One is to insulate some consumers from the real costs of energy, something that is counterproductive and unsustainable. Another is to directly assist vulnerable consumers to reduce their energy costs through greater efficiency, something that is constructive and feasible. Another is to address the income problem directly, something that needs doing but is beyond the realm of energy policy. Canada's objective in 2050 should be to minimize the hardship faced by low income and rural consumers in the face of potentially high energy costs but do so without masking the real costs of energy. Canada needs a realistic debate about energy affordability, what it is and is not, and what policy measures work and don't work.

3. Environmental Performance

Environmental performance is our proposed third objective and we put it third not in order of importance but because we believe that substantial failures on either of the first two—security or affordability—will inevitably trump environment concerns. Environmental performance can be and must be built on a foundation of security and affordability.

But environmental performance does not equate exclusively to low carbon. Whenever the climate debate leads the discussion rather than being embedded in a broader energy debate it draws us into at least three traps that have stalled action:

- ▶ If tackling carbon reduces diversity of options it reduces system resiliency and compromises security.
- ▶ If it adds costs without corresponding increases in efficiency it compromises affordability.
- ▶ If tackling carbon simply pushes the environmental pressures on to land, habitat, air quality or water, then those concerns—more local, more immediate—will trump the more abstract, long-term issue of carbon.

We take the view that the environmental debate should start with resource efficiency. Efficiency is where the environment and the economy converge in a positive and widely recognized synergy. Efficiency doesn't

⁹ Rural energy consumers also have distinctive challenges due to travel distance and limited alternatives.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

do everything, but it provides the platform that makes further steps more feasible for businesses, governments and consumers alike. Those further steps need to include strong and efficient environmental regulation across the board combined with the appropriate pricing of all energy to incorporate the full costs, including environmental costs. Canada's objective in 2050 should include realistic targets for reducing GHG, continuous improvement in air emissions and reduced impacts on land, habitat and water. The Canadian energy debate needs to focus on this.

4. Culture of Innovation

A culture of innovation is how we would characterize the fourth objective. Innovation underpins sustainable economic success, and it follows that for Canada to take full economic advantage of its energy capabilities, from its resource endowment through to its human skills, a central focus should be on innovation broadly defined. Here Canada has work to do. Despite strong corporate players in the resource and infrastructure sectors, we are thin in the technological end of the energy business. Our capacity for institutional innovation is in some question. It speaks badly of us that the many calls for an energy strategy for Canada often run up against the shibboleth of an energy policy mistake now 30 years in the grave. Taking another example, we have a world leading energy regulatory system that is vital to our future, but risks being overrun by political expediency if it proves unequal to the task of encompassing the realities of a 21st century energy delivery system.

Canada in 2050 should be able to count itself one of the premier innovators in energy. This should encompass strengths in energy technology niches, expertise in systems integration, advanced policy and regulatory approaches, and a human resource system that continuously promotes a culture of aggressive continuous improvement.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. Security
 2. Affordability
 3. Environmental Performance
 4. Culture of Innovation
- ▶ Principles
 1. Economic Principles
 2. Social Principles
 3. Environmental Principles
 4. Political Principles
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

PRINCIPLES

Effective public policy is built within the scaffolding provided by overarching principles. Principles in this case are not window-dressing shaping communication strategies; they are substantive, reflecting fundamental areas of agreement and providing an anchor for detailed policy development. Principles are the basic propositions that are broadly agreed to by policy makers and stakeholders in the energy system. Without them, policy coherence is impossible.

Much discussion with respect to principles (e.g., the EFI initiative) starts with the triple bottom line of economic, social and environmental sustainability. We accept these as a good starting point while also adding “political principles” to the mix.

1. Economic Principles

Canada is a society founded on the ideas of economic liberalism: free markets underpinned by the rule of law. With respect to energy, Canada in its most recent history has embraced these ideas in the move toward free trade (albeit with greater enthusiasm externally than internally) and deregulation of energy markets. This recent history has brought us much success and we would build our energy strategy on this principled foundation:

- ▶ Markets for energy commodities, services and investment should be as open as possible domestically and internationally, and Canada should be an international champion of such openness.¹⁰
- ▶ Markets must necessarily be fettered to varying degrees by government mandated rules and societal values. Nonetheless, to the greatest extent possible rules should be applied even-handedly and without prejudice with respect to the origin or ownership of any investor, buyer or seller.
- ▶ Energy prices should reflect the full economic costs of producing and delivering energy, including external environmental costs. This principle has two elements: costs imposed through taxes or regulation

¹⁰ Pierre Alvarez, Michael Cleland and Roger Gibbins, *National Energy Security An Exporter's Perspective: The Canadian Perspective*. Prepared for the North Pacific Energy Security Conference, Honolulu, Hawaii, December 2008.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

as appropriate to encompass externalities such as carbon, and deregulated prices that allow all costs to flow through to consumers.

2. Social Principles

Canada and its regions are more than a marketplace. Together they are made up of communities of people with a commitment to fairness and reasonable accommodation. This deep social contract provides the foundation for several social principles:

- ▶ While energy resource development and transport is in Canada's national interest, the benefits and costs are not evenly distributed. Many of the costs are arguably analogous to environmental externalities and Canada needs to develop better mechanisms for resolving differences and ensuring that the costs and benefits of energy are fairly distributed.
- ▶ Not all members of society are well able to bear the full costs of energy. Energy policy therefore needs mechanisms to assist consumers to improve their energy efficiency without masking price signals.
- ▶ Human health and safety must be paramount in all energy solutions. Canada's track record in ensuring health and safety in energy is exemplary but it needs to continue to be a focus of aggressive continuous improvement.

3. Environmental Principles

There is no question that Canadians have a strong, even passionate connection to their natural and built environments, and this connection is often the starting point in discussions of energy policy. Hence it is essential to reconcile energy strategies and goals with environmental responsibilities. Canadians are concerned about the environmental impacts of energy and believe, correctly, that these impacts can be mitigated if not eliminated. The largely successful history of dealing with acid rain, urban air quality and the land, water and habitat impacts of resource development are reflective not only of this belief but also of our ingenuity and capability to make positive progress. Climate change presents a uniquely challenging problem where the track record is discouraging in part because climate

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

policy in many countries including Canada has ignored many of the fundamental realities that underpin energy policy:

- ▶ All energy development and use has environmental consequences, direct or indirect, and therefore tradeoffs are inevitable. A sustainable approach to energy and environment must recognize this reality.
- ▶ Environmental sustainability is not an end point but a process of continuous improvement—sometimes with a sense of urgency but always with recognition that radical environmental improvement, however desirable as an ideal, will be constrained by established capital stock and human habits, and by the imperative of not compromising other energy objectives.
- ▶ Many energy related environmental issues need to be dealt with through regulation but the most fundamental requirement is that price signals for all energy—whether derived from carbon based fuels or not—reflect full costs including all environmental costs.

4. Political Principles

In the complex Canadian federal state, it is essential to supplement economic, social and environmental principles with political principles:

- ▶ The essential political principle is respect for the constitutional division of powers and responsibilities (Sections 91/92), and thus respect for provincial ownership of most of Canada’s resource endowment.
- ▶ A second principle, or at least reality, is that constitutionally subordinate or coordinate governments (municipalities, First Nations, northern territories) are all significant players when it comes to policies that affect the production and consumption of energy. Any *Canadian* energy strategy is necessarily an inter-governmental construct given that all governments have an important stake in effective policy outcomes.
- ▶ A third principle that guides our thinking is that energy policy should not be seen as a vehicle for the redistribution of wealth across regions or sectors. This is not to challenge the fact that many social and economic programs have redistributive elements, and that Canadians and their governments remain committed to the constitutional entrenchment of the equalization program. Rather, we would argue that adding wealth redistribution to the already complex and politically fraught

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

balancing act of energy and environment policy is to court failure when there is no very compelling reason for doing so. We have other, more suitable policy tools.

We make no claim that the objectives and policy principles sketched in above are exhaustive or comprehensive, nor are they beyond debate. However, they do provide a reasonable point of departure for the construction of a Canadian energy strategy. They provide the basic policy framework for individual governments—federal, provincial, territorial, First Nation and municipal—for intergovernmental cooperation and, ultimately, for a Canadian energy strategy. The challenge is to encourage movement along this trajectory, and it is here that western Canadians have a critically important role to play.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. Security
 2. Affordability
 3. Environmental Performance
 4. Culture of Innovation
- ▶ Principles
 1. Economic Principles
 2. Social Principles
 3. Environmental Principles
 4. Political Principles
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

WESTERN CANADIAN POLICY LEADERSHIP

The Canada West Foundation is firmly committed to the creation of a Canadian energy strategy. However, while there is considerable evidence that this initiative is finding some traction with provincial and territorial governments, there is a risk that the national initiative may still be a bridge too far, that we may be biting off too big a policy piece given existing political circumstances. At the same time, we are loath to lose traction on what we believe is one of *the* critical policy imperatives of our age: coming to grips with how we produce and consume energy. Thus in order to avoid any loss of traction, the Foundation has launched a comprehensive *regional* initiative.¹¹ This is not to be a substitute for a national strategy, but rather a means to drive the national conversation forward.

A regional approach also provides the opportunity for western Canadian leadership on a vitally important Canadian policy file. The argument here is not that national policy should be written in the West, but rather that western Canadians have a great deal of skin in the game, a great deal of expertise, and a large stake to bring to the table. If there is any policy discussion that western Canadians should lead, it is the national discussion of energy policy. Although getting this policy right is of potentially huge significance for Canada, it is of even greater significance for western Canada.

The case for western leadership *as a spur to national action* rests on a solid foundation:

- ▶ Energy circumstances in the West are a microcosm of national circumstances. The full range of Canadian energy assets are in play—natural gas, conventional and heavy oil, coal, hydro, wind, geothermal and other renewables—along with some found only in the West such as uranium.
- ▶ The policy challenges Canadians face with respect to the production and consumption of energy are all found in the West, with some exceptions such as the reengineering of the automobile industry for a carbon-constrained world.
- ▶ The West accounts for the majority of the oil and gas produced in Canada and all of its uranium production. Less well understood is

¹¹ For details on this regional initiative see *Powering Up for the Future* at www.cwf.ca.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

that the West also accounts for 29% of hydro production and 55% of electrical power from wind.¹²

- ▶ The West is a population magnet. Three of Canada's six primary cities—Calgary, Edmonton and Vancouver—and five of the six fastest growing Canadian cities are in the West.¹³ And communities are increasingly understood as one of the most critical variables in the energy equation—not only as big consumers of energy but as sources of energy through local supply and waste capture and as centres of the innovation that will underpin a sustainable energy future.
- ▶ Western Canadians are innovators and world leaders in key niches of the energy equation from production through to end use consumption. They are also innovators in policy and institution building from TILMA (see text box) to the BC carbon tax and engagement in state-provincial climate change initiatives.
- ▶ Western Canadians are successful creators of world scale companies from upstream oil and gas to pipelines to electricity generation and transmission companies, and many of them are increasingly taking leading positions in 21st energy solutions from renewable energy and waste management to end use energy efficiency. One of the West's

TRADE, INVESTMENT AND LABOUR MOBILITY AGREEMENT (TILMA)

Western Canadian leadership on an important national policy file is illustrated by the TILMA (Trade, Investment and Labour Mobility Agreement) signed by Alberta and British Columbia in 2007. Since the signing of the Free Trade Agreement in 1988, provincial governments had been working to reduce interprovincial barriers to trade, but with little success. Given the absence of movement on the national stage, BC and Alberta decided to do regionally with TILMA what could not be done nationally. Then, in the spring of 2010 TILMA was extended to Saskatchewan through the New West Partnership. The hope is that regional leadership will be a spur to national policy development, but if the national process remains frozen, the western provinces will still be better off than if left mired in an unproductive national process. The same line of thought can be applied to energy policy.

¹² Statistics Canada, *Electric Power Generation, Transmission and Distribution, 2007*, Catalogue 57-202-X.

¹³ Brett Gartner, *State of the West 2008*. Canada West Foundation, 2008.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

energy powerhouses, Manitoba Hydro, makes its headquarters in one of the most innovative high environmental performance buildings in Canada.

- ▶ Finally, and of perhaps greatest importance, if policy debates around the production and consumption of energy are among *the* most important policy debates for the next decade, as we argue they will be, these debates will play out with particular force in western Canada. The Canadian response to these debates will be largely shaped in the West.
- ▶ The potential for national leadership from the West is clearly here, and so too is the need. If the national push for an energy strategy is not to falter, a strong regional push is essential.

- ▶ The Canadian Energy Challenge
- ▶ A Strategic Response
- ▶ Strategic Objectives
 1. *Security*
 2. *Affordability*
 3. *Environmental Performance*
 4. *Culture of Innovation*
- ▶ Principles
 1. *Economic Principles*
 2. *Social Principles*
 3. *Environmental Principles*
 4. *Political Principles*
- ▶ Western Canadian Policy Leadership
- ▶ Next Steps

NEXT STEPS

Over the coming year the Canada West Foundation will advance the regional and national energy policy debates in a number of ways.

- ▶ First we will map out the starting point for the policy work that lies ahead, acknowledging that any discussion of where we want to go must begin with an understanding of where we are today. In this context, the Foundation notes and applauds the joint initiative of EFI and EPIC to commission work on “Canada’s Energy Circumstances.” For our part, we will develop a detailed and comprehensive description of the energy system in the four western provinces, and how that system connects south, east, north and to global markets.
- ▶ Second, in late 2010 we will conduct a national opinion study, with an expanded sample in each of the four western provinces, to explore a broad set of energy and environmental policy issues.
- ▶ Third, we will conduct roundtables across the region to encourage a vigorous discussion of policy challenges and regional opportunities.
- ▶ Fourth, we will conduct in-depth, in-person interviews with energy leaders from across the region, and across the full range of energy interests, aggressively articulate the need for policy innovation and change, building upon the arguments sketched in above.

In addition, we will engage in more specific policy research and commentary. Of course, not all energy issues are priorities and not all can be addressed simultaneously. Progress requires some concentration of effort organized around a manageable number of logically coherent subjects. Here, the Canada West Foundation proposes a research agenda built around the following questions:

- ▶ How do we get the full economic benefits from a diverse energy resource endowment?
- ▶ How do we offset the relative high cost of Canadian resources compared to competing sources?
- ▶ What do we need to do to address the “value added” conundrum while avoiding impediments to successfully developing our resources?

- ▶ The Canadian Energy Challenge
 - ▶ A Strategic Response
 - ▶ Strategic Objectives
 - 1. *Security*
 - 2. *Affordability*
 - 3. *Environmental Performance*
 - 4. *Culture of Innovation*
 - ▶ Principles
 - 1. *Economic Principles*
 - 2. *Social Principles*
 - 3. *Environmental Principles*
 - 4. *Political Principles*
 - ▶ Western Canadian Policy Leadership
 - ▶ Next Steps
- ▶ How do we continue to innovate and diversify so as to sustain economic benefits over the long run?
 - ▶ How do we continue to provide affordable energy to underpin the rest of the economy and protect consumers?
 - ▶ How do we ensure that energy supplies and energy systems are secure?
 - ▶ How do we place western Canada at the forefront of the rapidly emerging urban/community energy agenda?
 - ▶ How do we ensure a practical, comprehensive and cost-effective approach to environmental protection?
 - ▶ How do we protect social values in the face of energy developments?
 - ▶ How do we maximize cooperation among western governments in securing our energy future?

The intent throughout is to inform and animate a regional—but also national—discussion of Canada’s energy future. We are guided by the conviction that although policies around the production and consumption of energy are of huge importance for western Canada, they are no less important for the country as a whole. As is the case in so many policy areas, a strong West will contribute greatly to a strong Canada.

About Canada West Foundation

The Canada West Foundation is the only think tank dedicated to being the objective, nonpartisan voice for issues of vital concern to western Canadians. Through our research and commentary, we contribute to better government decisions and a stronger Canadian economy.

The West is in. And the Canada West Foundation helped put it there. Over the past 40 years, our research and commentary has improved government policy and decision making. Today, the West is on the national agenda and is at the forefront of the most important debates that will shape our country.

We give the people of British Columbia, Alberta, Saskatchewan and Manitoba a voice. A voice for their dreams, interests and concerns. As westerners, we understand the people and the places of the West. We know our history and how it influences our future. Whether it is the economy, energy, environment, education, healthcare, taxes, social services, urban issues, provincial-federal relations or any other policy area of importance to the West, we have researched it, commented on it, stimulated debate about it and recommended practical options for improving the policy response. Democracy lives.

Our credentials are impressive. We have the policy and economic experts you need. Our Board of Directors represent the who's who of the four western provinces. Our list of projects is long. We're just like the West. Absolutely essential. Absolutely part of Canada's success.

More information can be found at www.cwf.ca.



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