Conservation Council *of* New Brunswick
Conseil de conservation *du* Nouveau-Brunswick

Briefing Note — Carbon Pricing

January 2018

Background

The Government of Canada introduced on January 15, 2018 its Legislative Proposals Relating to the *Greenhouse Gas Pollution Pricing Act*, as well as its proposed approach to regulating trade-exposed industries through its Output Based Pricing System. These proposals follow several other documents released by the federal Government detailing its plans to establish a nation-wide carbon pricing backstop.

The carbon pricing backstop requires all provinces and territories to have in place in 2018 carbon pricing policies equivalent to or exceeding the federal backstop. Provinces and territories have three options. They can choose a carbon charge set at a level and schedule matching or exceeding those set by the Government of Canada ($10/tonne 2018 rising by $10/year until 2022). Or, provinces and territories can opt for a cap and trade system that achieves incremental year over year reductions leading to a reduction of at least 30% below 2005 levels by 2030. The third option is a hybrid, which includes both a carbon charge and intensity based output system for trade exposed large industrial emitters (over 50,000 tonnes).

Provinces and territories can opt for any one of the three approaches or have the federal government apply its hybrid backstop. In the Atlantic, Nova Scotia has opted for cap and trade, PEI appears set to adopt the federal hybrid and Newfoundland/Labrador has indicated it will also pursue a hybrid based on the Alberta model.

New Brunswick recently announced it will allow the federal Government to apply the output-based pricing system for industry, but that it would not apply a new carbon levy. Instead, the province is proposing, through Bill 39, to re-profile existing excise gas taxes into a Climate Fund. The accounting measure means that government expenditures with a climate change link will be accounted for by the excise tax. It also means that citizens, industry and business cannot apply to the Climate Fund as it will be used to account for government expenditures. As a result, New Brunswick is not in compliance with federal rules because it fails to meet one of the key design principles required that a province's carbon pricing program must deliver incremental GHG emissions reductions that can be attributed to the effects of carbon pricing.

Federal Environment and Climate Change Minister Catherine McKenna has already publicly indicated that Nova Scotia and New Brunswick appear not to comply with federal carbon pricing requirements (as is also the case for Saskatchewan and Manitoba). Each province and territory now have until March 1, 2018 to indicate if it would like the federal system to apply (i.e., New Brunswick for the output-based pricing system), or until September 1, 2018 to submit their proposed provincial/territorial approach to the federal Government (i.e., New Brunswick for its excise tax/Climate Fund proposal created through Bill 39).

The federal Government will evaluate provincial and territory approaches in the last quarter of 2018 and announce the results of its evaluation by year-end. Provinces and territories not complying will have their systems topped up or have the federal backstop apply by Jan. 1, 2019 starting at $20/tonne for the carbon levy. Industry intensity/best practice standards will also apply in 2019.

Federal carbon pricing backstop details

1. Provinces/territories that "choose" the federal backstop will have any revenues raised federally returned to the province to be used at their discretion. The NB proposal to have the federal Government regulate NB trade-exposed industry means that any revenue raised from taxing industry would be returned to the province.

2. Provinces/territories the where federal backstop is imposed, in whole or in part, could see revenue returned to the province directly, through persons or a combination. The mechanism has not yet been determined. This could mean that because NB has not applied a carbon charge on transportation and heating fuel distributors that money raised by the federal Government could be returned to the province, but it could also come back via cheques or credits to NB citizens. The Prime Minister has indicated he is concerned about ensuring that the vulnerable (i.e. Those unable to afford energy price increases) are protected. The comment suggests cheques could be sent to low-income households.

3. The output-based pricing system industrial system will apply to base metal smelting and refining, bitumen and heavy oil upgrading, cement, chemicals (ethanol), iron ore pelletizing, iron and steel, lime, mining, natural gas pipelines, nitrogen fertilizers, oil sands and heavy oil, other manufacturing, potash, refining, steam/heat and upstream oil and gas companies if they emit more than 50,000 tonnes of greenhouse gas emissions per year. Companies emitting between 10,000 and 50,000 tonnes/GHG can voluntarily participate if approved by the regulator.

4. The proposed output-based pricing system would come into effect Jan. 1, 2019 and will start by requiring industries to meet an emissions intensity standard is 30% better than sector's intensity average. If an entity's performance is 30% better, it receives credits; if performance is worse, the entity must pay a carbon charge equal to the carbon charge schedule price for that year (i.e., $20/tonne in 2019; $30/tonne in 2020; $40/tonne in 2021 and $50/tonne in 2022). This standard apparently is achieved for the Saint John refinery, but pulp and paper mills and the Glencore smelter may not be compliant.

5. Companies above their emissions intensity limit can pay the charge to the Government of Canada; they can submit surplus credits issued by the federal Government or they can submit eligible offsets.

6. The electricity sector is not trade-exposed, so it is not covered by the output-based pricing system. Electricity will be covered by the coal-fired power plant regulation, the proposed emissions intensity regulations for natural gas fired electricity, as well as package already in place and the upcoming clean fuel standard that will lower the allowed GHG emissions intensity of fossil fuels in transportation, buildings and industry. Additional plans for the electricity sector are not yet defined but could include indirect approaches like crediting downstream users for their investments in energy efficiency and renewable energy technologies. Comments on how electricity should be handled on a regional basis is of interest to the federal Government and groups will need to work together to think through options.

7. The carbon pricing backstop and output-based pricing system will be reviewed in 2020 (soft review) and again in 2022 at the level of ministers and First Ministers.

Federal carbon pricing backstop next steps

Stakeholders have until Feb. 12, 2018 to comment on the draft federal legislative proposal. The Government of Canada will then introduce the legislation for debate and likely passage in 2018 either as a standalone bill or as part of the federal budget bill. Stakeholders have until April 9th to comment on the federal proposal for the output-based pricing system. Environment and Climate Change Canada officials will meet with provincial industry stakeholders and governments to discuss the proposal in January and February. Minister McKenna is also considering a meeting of Atlantic environment ministers to talk about the option of moving toward an Atlantic carbon pricing system that is consistent and coordinated in the region.

Outstanding issues; longer-term opportunities

New Brunswick is in non-compliance with the federal backstop. Stakeholders, including business and non-government organizations have said that a regional approach is their preferred approach. The Government of Canada has also said that is its preferred approach. The output-based pricing system is an intensity approach that should be considered acceptable only as a transition measure. Comments on federal proposals and public messaging should focus on highlighting the need to comply with federal requirements to ensure New Brunswick meets its 2030 greenhouse gas reduction targets and to protect carbon pricing revenue. Messaging should also socialize the idea that the output-based pricing system can help industry get ready for a carbon constrained world, but that after 2022 absolute caps on industry must lead to deeper and sustained reductions. It is not yet clear, for example, what the federal Government is proposal as the emissions intensity decline rate after 2019 (so ratcheting up from 30% better than the industry after).