March 26, 2021

Hon. Jonathan Wilkinson
Minister of Environment and Climate Change Canada
351 Saint-Joseph Boulevard
Gatineau, Quebec
K1A 0H3
Via email: Jonathan.Wilkinson@parl.gc.ca

Dear Minister:

Reviews are underway by your department, as well as institutions like the Canadian Institute for Climate Choices (CCIC), to assess the effectiveness of the current Output-Based Pricing System (OBPS), as well as to summarize current provincial and territorial approaches to carbon pricing. These analyses, along with federal-provincial processes, will inform Government decisions on the operation of carbon pricing generally, including OBPS starting in January 2023. We expect federal announcements regarding any changes to the federal carbon-pricing system in spring-summer to allow provinces and territories time to respond. At the same time as these processes are underway, ECCC has posted two regulatory proposals for public comment (*Review of the federal Output-Based Pricing System Regulations* and *Canada Gazette, Part 1, Volume 155, Number 10: Greenhouse Gas Offset Credit System Regulations*).

The Conservation Council of New Brunswick (CCNB) collaborates nationally with non-government organizations to contribute to the effective implementation of Canada's climate action plans. CCNB fully supports submissions by these groups, including the Pembina Institute, David Suzuki Foundation, and Canadian Parks and Wilderness Society. CCNB and Environmental Defence are collaborating on this specific submission.

Principles guiding this submission include:

1. The need for Canada's efforts to align with the global carbon budget needed to limit global average temperature increase to no more than 1.5 degrees Celsius.
2. The need for Canada's efforts to align today with its fair contribution to global emissions reductions; a level suggesting 60 per cent reductions in domestic greenhouse gas emissions by 2030; and the need to reach near zero no later than 2050 and likely earlier.

The next few weeks and months will set the course for Canada for the next decade, with the April 22, 2021 U.S. Earth Day Summit and the United Nations Twenty-Sixth Conference of the Parties meeting (COP 26) in Glasgow in November. With this timeline and principles in mind, we have chosen to share our submission with you directly as we cover more than the narrow review of the OBPS and proposed offset regulation. This letter also represents our submission to these two consultations.

Principles underpinning an effective industrial carbon pricing regulation

Canada's largest polluters should, over time, incorporate the full cost of their carbon pollution into the cost of doing business as recommended by economists and in keeping with polluter pay principles. While we understand the need to manage the transition, Canada's current approach to the OBPS does not drive the transformative emissions reductions needed to position our economy for a decarbonisation reality. This broader, transformative perspective needs to drive the federal Government's approach to carbon pricing in the post-2022 period. With the need to do our fair share to stay within the global carbon budget in full view, we believe the following principles should guide near-term decisions about the OBPS:

1. Only truly emissions intensive, trade-exposed industries like cement, steel and chemicals should receive special consideration
2. 100% of other industrial emissions should be covered by carbon pricing regulations
3. Consistent implementation of the benchmark across all jurisdictions

Coverage and timeframe

We concede it is difficult to remove sectors once covered by the OBPS. We argue, however there is one sector too strategically important to Canada's decarbonisation efforts to include in the OBPS and that outside of chemicals, cement and steel, the OBPS should be temporary.

Temporary because competitiveness protection based on leakage concerns are not well supported and we believe is not needed once carbon pricing and/or regulatory equivalency with other jurisdictions is achieved. This industrial subsidy should be time limited.

Electricity is too important to be covered by the OBPS

The sector to remove now is electricity. It is not trade-exposed and is critical to the national process of decarbonisation because electrification will underpin much of the process. We strongly urge the federal government to remove electricity from the OBPS post 2022 and instead to intensify federal-provincial official and political processes to treat electricity as the strategic national asset that it is. One of the main impediments to electrification of the economy based on efficiency and a largely renewable system is the need for electricity legislative, regulatory and policy reform.

CCNB, collaborating with Ecology Action Centre and East Coast Environmental Law found in 2020 that the biggest barrier to electricity reform is government legislation, regulation and policy. A nationally coordinated process, including financial incentives, and federal commitments to a near-zero national electricity system is needed to drive this reform and electrification process. Leaving electricity in the OBPS under the guise of protecting industry and consumers from near-term rate impacts will not set Canada on course to significantly deeper emissions reductions and could undermine Canada's goal to achieve a 90 per cent emissions free electricity system by 2030.

The Benchmark

End inconsistent application of the benchmark

Inconsistent application of the federal carbon pricing benchmark has led to a race to the bottom, particularly in provinces like Ontario, New Brunswick, Prince Edward Island, and Newfoundland and Labrador. We now face a proposal from Saskatchewan to emulate New Brunswick's inadequate carbon pricing approach.

In New Brunswick, for example, the federal Government has approved carbon pricing programs where the facility-level (rather than sector-level) industry emissions cap declines by only one per cent a year leaving 90 per cent of emissions carbon levy free in 2030; electricity also emits carbon pricing free on 99 per cent of its emissions until 2022 and there is no schedule thereafter. Consumers also see dampened effects because the province, with federal approval, lowers excise taxes. The result is that in 2021-2022, consumers pay only 4.21 cents/litre in carbon levy compared to the federal rate of 8.8 cents/litre.

As noted in the Pembina Institute submission:

> "Ontario[1] and New Brunswick[2] both put forward their own regulations for pricing emissions for heavy emitters (also OBPSs) after the federally set submission deadline of September 2018 and the application of the federal OBPS in January 2019. The federal government accepted both provincial system in September 2020 and will stand down its own OBPS in those provinces ''as of a date in the future that will be determined in consultation with the provinces.[3]'' We regret this decision in light of the fact that Ontario and NB's OBPSs are significantly weaker than the federal OBPS. The lack of a detailed benchmark for the OBPS portion of hybrid provincial carbon pricing has led to a wide variability and to low average prices.
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> Sector-specific standards are expressed as a percentage of the average emissions intensity for a sector. Facility-based standards are expressed as a percentage of historical emission intensity of individual facilities. Hence, sector-specific standards are more effective at reducing emissions and incentivizing innovation than facility-based standards. New Brunswick's system uses facility-based standards. Ontario's system relies more heavily on facility-based standards than the federal system. Ontario has set sector specific standards

[1] Government of Ontario, Greenhouse Gas Emissions Performance Standards, O. Reg. 241/19. https://www.ontario.ca/laws/regulation/r19241

[2] Government of New Brunswick, Holding Large Emitters Accountable: New Brunswick's Output-Based Pricing System (2019). https://www2.gnb.ca/content/dam/gnb/Departments/env/pdf/ClimateClimatiques/HoldingLargeEmittersAccountable.pdf

[3] https://www.canada.ca/content/dam/eccc/documents/pdf/climate-change/climate-plan/annex_pricing_carbon_pollution.pdf

> for 13 industrial activities and facility-based standards for about 80 facilities. Under federal OPBS sector-specific standards were used for 193 of the regulated facilities and facility based standards were used for 24 facilities.[4]
>
> The emissions intensity standard is used to determine the portion of emissions subject to the price for a given facility. The federal system has set 80% standards for 42 sectors, 90% standards for 19 sectors, and 95% standards for 14 sectors. This means that the majority of sectors under the system will pay the price on pollution on 20% of their emissions. While Alberta's OBPS is stronger than NB's and Ontario's, it is worthy of mention that the Technology Innovation and Emissions Reduction (TIER), accepted by the federal government and effective as of effective as of January 1, 2020, is weaker than the system for heavy emitters established under the previous Alberta government. TIER was a step backwards for Alberta and is weaker than the federal system in so far as it relies more on facility specific benchmark, instead of product benchmarks, and sets a weaker starting standard of 90%."

We do not support federal approval of Ontario and New Brunswick's OBPS (and NB's and PEI's consumer levy) programs. The federal government should close the loopholes created through these decisions. At minimum, approval in Ontario should be delayed until sufficient detail to determine equivalency is provided. We also encourage federal delay of its OBPS stand down in NB as long as possible. Ideally, NB would opt to maintain the federal system. Now is the time to ensure provinces are well aware that benchmark loopholes will no longer be tolerated as they undermine effectiveness of pollution pricing.

With the Supreme Court decision in favour of the constitutionality of the *Greenhouse Gas Pollution Act* adding wind to its sails, the federal must strengthen and consistently implement the benchmark. If Canada fails to apply the benchmark consistently across all jurisdictions, it could leave the country vulnerable to carbon border adjustments now under consideration by the European Union and the United States.

Strengthen the benchmark

The challenge with including sectors in the OBPS regime is that it is difficult to remove sectors once covered. To account for this reality, we would like to see ramp down rates consistent with staying within the global carbon budget and Canada's fair share, and with each sector's ability to transition to non-emitting processes. Ramp down rates in the range of eight to ten per cent a year is more consistent with these considerations, than the two per cent ramp down rate used in the modeling informing the December 2020 climate-action plan update. The ramp down rate could vary by sector to represent technical potential assessments in line with decarbonisation.

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[4] Communications with Environment and Climate Change Canada (Note: numbers may change over time as new facilities join the OBPS)

We appreciate further modeling is needed to determine an effective ramp down rate but our suggestion is in line with global carbon budget estimates.

OPBS is a fossil-fuel subsidy

As noted, we believe competitiveness claims for industries included in the OBPS are overstated. We would further argue that inclusion in the OBPS unfairly subsidies industrial emissions given only 20 per cent or fewer emissions face the carbon levy.

Another potential subsidy vulnerability is the failure to ensure entities account for all greenhouse gases emitted from their operations. The national greenhouse gas inventory includes land-use change related emissions but regulation is not assigning these emissions to the entity generating these land-use change emissions. The review of the *Greenhouse Gas Pollution Pricing Act* provides an opportunity to include land-use change emissions resulting from industrial activities. This integrated approach is consistent with polluter pay principles. Please see the submission from the Canadian Parks and Wilderness Society for additional insights on this issue.

Offsets

Offsets offer no incremental greenhouse gas emissions reductions. The requirement for rapid and deep emissions reductions and atmospheric drawdown suggest the need to regulate sectors responsible for landscape-level emissions like forestry and agriculture to encourage nature-based climate solutions that generate biodiversity and ecological services benefits.

The fixation on project-based offsets creates stakeholder pressure to avoid regulating activities that should be like advanced refrigeration, landfill methane, forest management, and soil carbon. Proposals to include these activities in offsets programs need to prove why regulation is a less effective route to emissions reductions.

Flexible regulation is a reasonable objective, but our concern is that the current proposed approach sustains the failure to signal and to create appropriate incentives to industry the need for deeper transformation. In the spirit of responding to Government's current proposals, however, we offer these recommendations:

1. Allowing 75 per cent of an entity's emissions overdraft to be met through offsets seems excessive given the low level of emissions covered by the current OBPS and the suggestion that a two per cent ramp down rate to 2030 (as used in recent modeling). We suggest reversing the proportions so that offsets contribute no more than 25 per cent to resolve emissions overdraft obligations. Over time, we recommend that offsets options could increase as the ramp-down rate exposes more emissions to full carbon pricing, with consideration of an eight per cent cap as in California.
2. Start date for offset projects should be January 1, 2022 to ensure offsets generate credits that increase compliance flexibility in the post 2023 period when emissions coverage should increase.

3. Integrity considerations like applying risk factors applied to biological projects, buffer credits and leakage considerations should be set at compliance-quality, best-practice levels. Soft regulations lead to low quality, low-cost offsets that undermine progress. Climate Action Reserve and the Air Resources Board use five per cent for non-forestry projects; leakage rates of 20% apply to forestry projects.
4. Expert panels risk being dominated by stakeholders hoping to make money through offsets markets. Independent experts, including academics, must inform protocol development to ensure integrity. Representatives from provinces or the private sector who have an interest in maximizing offset creation should not dominate panel processes. Non-vested external peer review will be essential to finalizing protocols.

We appreciate your consideration of our submission.

Sincerely,

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