

Canadians for Clean Prosperity Presentation to the Standing Committee on General Government Hearings on Bill 4, Cap and Trade Cancellation Act, 2018

Canadians for Clean Prosperity is a not for profit public policy advocacy organization dedicated to advancing market-based approaches to address environmental challenges in ways that will simultaneously protect and improve our natural environment, including reducing greenhouse gas emissions, while strengthening our economy.

Canadians for Clean Prosperity had deep reservations about Ontario's previous cap and trade system as set out under the Climate Change Mitigation and Low-carbon Economy Act, 2016. Specifically, we objected to the previous government's decision to dedicate the entire \$3 billion in revenues raised from auctions for cap and trade allowances towards the Greenhouse Gas Reduction Fund to be used for emissions reduction programs (many of which we felt were not cost effective), rather than returning all of – or even some of - the money to the consumers and businesses who in fact paid the increased carbon costs. Furthermore, we objected to the government's plan to allow firms to purchase allowances from California and Quebec as a way of meeting their obligations under cap and trade, as in our view California had in effect created an artificial surplus of allowances which kept the carbon price artificially low. This meant that there would be a large net flow of capital from Ontario to California for at least the first 5-10 years of the program and that Ontario would achieve less domestic emissions mitigation than it would have under the federal carbon price backstop.

However, we did recognize that the previous cap and trade plan at least represented a meaningful first step in putting a price on carbon in Ontario. In our view, and in the view of most economists working in this field, putting a price on carbon, whether through a carbon tax or a cap and trade system, is the single most important, effective, and lowest cost means of reducing carbon emissions.

Thus we are disappointed that in the new government's decision to eliminate cap and trade, it missed the opportunity to replace cap and trade with a better system – such as a revenue neutral carbon tax which would return all carbon revenues back to citizens and businesses as tax reductions. Instead, the government chose to eliminate carbon pricing altogether, promising a new climate plan with unspecified targets at some unspecified future date.

We want to address three major concerns with Bill 4 and the current government's climate policies generally: 1) the treatment of large industrial emitters in the transition away from cap and trade; 2) the use of revenues from carbon pricing; and, 3) the lack of defined targets to replace Ontario's current 2030 emissions reduction target.

Treatment of Large Industrial Emitters

The new Ontario government was explicit in its election commitments that it would eliminate carbon pricing on gasoline and home heating, the areas of most direct concern to Ontario consumers. But the government has also made clear that it intends to hold large polluters accountable for their emissions. For example, in a press conference on June 2, 2018, Progressive Conservative Leader Doug Ford said that "the polluters, any companies that decide to pollute, we're going to come down heavy on them, we're going to come down really heavy on them."¹ Similarly, on September 25, Environment Minister Rod Phillips said that "We are focusing on the polluters, in terms of people producing the most emissions, not on individual families and people."²

Ontario's cap and trade system had elements of both a direct price on individual families and consumers and a system for holding large industrial emitters accountable. The direct price element was the requirement for transportation fuel and natural gas distributors to buy allowances for all of the carbon emissions associated with the gasoline and natural gas they supply – effectively passing on a carbon price of roughly \$19 per tonne to consumers. It is understandable that the government, given its electoral promises, decided to remove this element of the cap and trade plan. But the other part of cap and trade, the requirement for large industrial emitters – large industrial facilities such as steel, cement, or chemical plants – to buy allowances to cover their emissions was precisely the kind of mechanism required to hold large polluters to account. There was no need to remove the system for industrial emitters in order to reduce the carbon price burden on consumers. Even such notable carbon tax opponents as Saskatchewan Premier Scott Moe and Alberta opposition leader Jason Kenney have acknowledged the need for a system which imposes a price on large industrial emitters in their provinces.

Canadians for Clean Prosperity was critical of the previous system for being too generous to large emitters by giving them free allowances initially equal to the level of their emissions cap (although declining in future years). In our view, the Output Based Pricing System proposed under the federal backstop carbon pricing legislation, or as implemented in Alberta, represented a superior means of holding large emitters accountable that effectively rebates most (but not all) of their carbon costs. As things stand, the large emitters who were participants in the previous cap and trade system up until July, 2018 will now be required to transition to the federal Output Based Pricing System for January, 2019. A more sensible approach

would have been to leave the existing rules for large emitters in place and replace the requirement to buy allowances at auction with a requirement to buy allowances at a fixed price – say \$20 per tonne – while leaving in place a (perhaps slightly less generous) allocation of free allowances.

The abrupt ending of cap and trade has created significant transition issues. Bill 4 would restrict compensation to firms that purchased more allowances than necessary to cover their emissions for the period from January 1, 2017 to July 3, 2018. But as the Environmental Commissioner of Ontario Greenhouse Gas Progress Report for 2018 points out, that means that the large polluters who **did not** purchase sufficient allowances to cover their emissions for that time period are effectively being subsidized by the provincial government compared to their competitors who did buy sufficient allowances. “This punishes organizations that prepared for compliance with the law in good faith, and rewards those who did not.”³ Rather than “come down heavy” on large polluters, in Bill 4 the government has decided to let them off the hook.

Use of Carbon Revenues

The government’s decision not to implement any form of carbon pricing has left Ontario subject to the federal carbon pricing backstop, which will impose a carbon tax on the province at \$20 per tonne starting on January 1, 2018. Fortunately, the federal Greenhouse Gas and Pollution Pricing act specifies that the federal government must return all revenues raised to Ontario – either via transfer to the provincial government, or direct payments to individual Ontario residents. It is our hope that the federal government will choose to return carbon revenues directly to households through an equal per capita dividend. But in choosing not to bring in any form of carbon pricing, the Ontario government has foregone the opportunity to decide how carbon revenues raised in the province will be spent and has put that decision in the hands of the federal government.

A far superior strategy, in our view, would be for Ontario to announce that it is ending cap and trade and voluntarily requesting that the federal government implement its carbon price backstop, but that Ontario itself could then decide how to spend those revenues. Three mechanisms that the Ontario government could choose to redistribute revenues raised by the federal carbon price would be:

- a) Direct dividends to households, as proposed in the recent paper from Canadians for Clean Prosperity, sending every individual in Ontario a direct dividend or rebate cheque starting at \$135 per person in 2019 and rising to \$322 per person in 2022.⁴
- b) The tax reductions proposed in the People’s Guarantee platform published by the Progressive Conservative Party in November, 2017. This would have included a 22.5% cut to the middle income tax rate and a 10% cut to the lowest income tax rate, an increase in the Sales Tax Credit by \$100 per person, and a 28.5% reduction in Ontario’s small business income tax rate.⁵

- c) The tax reduction proposal from University of Calgary economist Trevor Tombe, prepared for the Ontario 360 project of the University of Toronto's School of Public Policy and Governance, which recommended increasing the Ontario Sales tax Credit by 80% (about \$240) and eliminating the Ontario Health Premium.⁶

All three of these approaches would return 100% of carbon tax revenues to Ontarians, albeit with different outcomes in terms of progressivity under each system. All of them, however, would be superior to doing nothing, and would leave the decision of how to spend Ontario carbon revenues with the government of Ontario, rather than ceding that responsibility to Ottawa.

Ontario's Greenhouse Gas Reduction Targets

Finally, I want to turn my attention to Ontario's greenhouse gas reduction targets. The previous government established a target of a 37% reduction in emissions from 1990 levels by 2030. This would imply reducing emissions from 1990's level of 182 megatonnes (MT) to 115 megatonnes in 2030. While significant reductions of roughly 20 MT per year were achieved by Ontario's phaseout of coal-fired electricity generation, it would be extremely challenging for Ontario to achieve a 37% reduction target from its remaining industrial, transportation, and building emissions. That is why the cap and trade system essentially relied on the availability of low cost allowances from California to achieve most of its reductions. Clean Prosperity was critical of this approach, and advocated that rather than having an unrealistic target dependent on importing foreign credits, Ontario should have set a more realistic target compatible with Canada's national climate goals, but achievable primarily through domestic emissions reductions.

The federal "Guidance on the pan-Canadian carbon pollution pricing benchmark" states that provinces that do not implement a direct carbon price but opt for a cap and trade system should have a target that includes "(i) a 2030 emissions-reduction target equal to or greater than Canada's 30 percent reduction target and (ii) declining (more stringent) annual caps to at least 2022 that correspond, at a minimum, to the projected emissions reductions resulting from the carbon price that year in price-based systems."⁷

If Ontario wishes to introduce its own climate plan that does not include either cap and trade or a carbon tax, for any such plan to be credible, Ontario must be able to demonstrate that it will achieve a target at least equivalent to the targets proposed by the federal government.

For Ontario, setting a 2030 target of 30% below Ontario's 2005 levels of 204 MT would mean a 2030 target of 143 MT – a further 20 MT per year reduction from Ontario's current emissions level of roughly 163 MT. For the years between now and 2022, Ontario would need to set annual targets that would achieve reductions at least equivalent to the reductions that could be expected from the implementation of the federal carbon tax. Based on research by EnviroEconomics,

who have done modelling for many provincial governments, including the Ontario government's own cap and trade plan, the federal benchmark would be expected to result in emissions of 161 MT from 2018 to 2020, falling to 159 MT in 2021 and 157 MT in 2022 – roughly a 6 MT reduction from current levels.⁸ So a credible emissions reductions target for Ontario under this new act should be set at roughly a 6 MT reduction to 157 MT by 2022 and a 20 MT reduction to 143 MT by 2030.

Conclusion

In our view, Bill 4 and the government's climate plan to date is flawed for these three reasons:

- Bill 4 unnecessarily eliminates carbon pricing for large industrial emitters alongside the elimination of consumer carbon pricing for gasoline and natural gas, creating significant transition issues and rewarding emitters who did not purchase sufficient allowances for the 2017-2018 period at the expense of those who did.
- Bill 4 forfeits the opportunity for Ontario to decide on its own how to distribute carbon revenues to households and businesses, instead leaving that decision in the hands of the federal government.
- Bill 4 eliminates the previous Ontario emissions reduction target for 2030 (which was admittedly unrealistic and depended on the import of allowances from California to achieve), but does not put forward a replacement target which would be compatible with Canada's overall 2030 emissions reduction goals.

We hope that the government will correct these flaws and bring in a new or amended bill which will return Ontario to a leadership position in dealing with the challenge of climate change.

Sources

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- ² CBC News, “Ford government ‘*gutted*’ climate change programs that were working: report”, September 25, 2018 <https://www.cbc.ca/news/canada/toronto/ontario-environment-minister-climate-change-plan-1.4837410>
- ³ Environmental Commissioner of Ontario, “*Climate Action in Ontario: What’s Next? 2018 Greenhouse Gas Progress Report*” <https://docs.assets.eco.on.ca/reports/climate-change/2018/Climate-Action-in-Ontario.pdf> at pp. 70-71
- ⁴ Canadians for Clean Prosperity, “*Carbon Dividends Would Benefit Canadian Families*” <https://www.carbon-dividends.ca/>
- ⁵ Progressive Conservative Party of Ontario, “*People’s Guarantee*” downloaded at https://d3n8a8pro7vhmx.cloudfront.net/themes/58386dc76ad5754297000000/attachments/original/1513353728/People’s_Guarantee.pdf?1513353728
- ⁶ Trevor Tombe, “*Climate Policy Transition Briefing: An evidence-based climate policy for Ontario*,” Ontario 360, University of Toronto School of Public Policy and Governance <http://on360.ca/policy-papers/evidence-based-climate-policy-for-ontario/>
- ⁷ Environment Canada, “*Guidance on the pan-Canadian carbon pollution pricing benchmark*” <https://www.canada.ca/en/services/environment/weather/climatechange/pan-canadian-framework/guidance-carbon-pollution-pricing-benchmark.html>
- ⁸ Dave Sawyer, EnviroEconomics “*A Better Trade-Off Analysis of Ontario Carbon Pricing Choices*,” December 4, 2017, downloaded at <https://drive.google.com/file/d/1QGURUYvsIPlsxanrvVkt50OGIHZ0q3iT/view>