



ENVIRONOTES - BC CLIENT ALERT

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CLIMATE CHANGE: CARBON TAX V. CAP AND TRADE

Putting a price on carbon is probably the single most important thing a government can do right now.¹

Recently, University of Ottawa think tank, Sustainable Prosperity, ranked British Columbia's carbon tax as the most effective climate change policy in Canada. However, the BC carbon tax is not without its controversy, becoming a political issue in the recent BC election. With the release of the National Roundtable on the Environment and Economy policy paper on Carbon Pricing for Canada, the debate continues as to whether greenhouse gas reductions will be achieved through a cap and trade system or a carbon tax.

British Columbia introduced a carbon tax on July 1, 2008 as part of its Climate Action Plan in order to shift consumer behaviour and reduce greenhouse gas emissions. As Harvard professor, N. Gregory Mankiw, former advisor to President George W. Bush, said:

Basic economics tells us that when you tax something, you normally get less of it. So if we want to reduce global emissions of carbon, we need a global carbon tax.

The BC carbon tax is to be phased in over 5 years, with an initial price of \$10 per tonne of carbon, increasing to \$30 per tonne by 2012. In practical terms, gasoline increased by 2.41 cents per litre and will increase by 7.24 cents per litre by 2012 at the pumps. In addition, the tax is collected on residential heating and electricity bills based on the customers' consumption of fossil fuels and electricity.

The tax is estimated to apply to about 76% of BC's GHG emissions as the carbon tax is a tax on the combustion of fossil fuels and consequently doesn't cover emissions from the processing of natural gas, cement manufacturing or aluminium manufacturing; leakages from pipelines, or venting; or flaring from natural gas or oil operations. Nor does the tax apply to landfill gas, though the BC government has tackled the landfill gas issue through a regulation under the *Environmental Management Act*.

The carbon tax in BC is said to be "revenue neutral", which means that the tax revenue generated is to be returned to tax payers via reductions in personal and business taxes, together with an annual climate action credit for low income residents of BC. In addition, recently the BC budget allocated \$200 million to rural and remote communities to provide further relief. Increasingly, though, municipalities are requesting a share of the carbon tax revenue to assist with climate related projects such as regional transportation and transit, which could strain the legislated mandate for the tax to be "revenue neutral".

The other mechanism introduced in BC and in many other jurisdictions is that of a cap and trade system, which is designed to work with the carbon tax.

Recently, the National Roundtable and the Environment and Economy (NRTEE) released a policy paper "Achieving 2050: A Carbon Pricing Policy for Canada", which looked at the issue of which carbon pricing policy instrument would be best to reach the federal 2050 greenhouse gas reduction targets. The NRTEE specifically stated that it was not a question of a tax versus of a cap and trade

¹ Jeff Rubin, chief economist, CIBC World Markets, February 28, 2008.

system, but it was a matter of blending price-setting and quantity-setting approaches. However, foremost in its considerations were that most provincial, federal and international carbon pricing regimes are considering, implementing, or have already implemented, a form of cap and trade system. It may be simpler to transition multiple provincial cap and trade systems into one national or international system. The NRTEE recommended a national cap and trade system to cover large emitters (51% of the economy) and remaining emissions (36% in buildings, households, transportation and light manufacturing). Large emitters would be covered with a portion of the national cap and the rest of the economy under the remaining portions. There would be full trading of permits between both groups under a single national system, which would be designed to commence before 2015.

At the federal level, it appears that although Ottawa has the wheels in motion on a federal climate change regime, it is also closely looking south of the border at the new federal US administration and the legislative options being considered there and has indicated an intention that Canada's cap and trade system should be similar to that adopted by the US.

The year ahead holds many challenges and opportunities as it becomes clearer where the federal and provincial regimes are headed. Stay tuned.

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