

# Carbon Pricing Plan Summary

Office of the Third Party, 20 September 2018

Climate change is the single greatest challenge facing humanity, and Prince Edward Island in particular, in the 21st century. Our province is one of the most vulnerable places in the world to the effects of climate change but also one of the smallest contributors to it. Many might therefore ask: what can we do to change the behaviour of larger greenhouse gas (GHG) emitters in other parts of the world? The answer is that by providing visionary leadership and proof of how a society can successfully transition to carbon neutrality, we can give others the tools to make the transition that we need them to make. PEI can and should be a world leader in fighting climate change. After all, we have the most to lose: our Island.

Our province has already shown leadership in this regard, including development of wind power; innovative use of energy storage and other technologies by the City of Summerside; and the recent Climate Change Action Plan and 10-year Provincial Energy Strategy. While these actions will not achieve the goal of carbon neutrality, they will, if fully implemented, set a solid foundation from which to build toward that goal.

Broadly speaking, there are two main ways in which the provincial government can have an impact on reducing GHG emissions: public programs or regulations, and modifying private behaviour through the market.

## Public program and regulatory approaches:

We are already quite familiar with these programs on PEI. They include actions like building government-owned wind farms, mandated renewable energy targets for utilities (repealed 2015), converting heating for public buildings to wood chip boilers, subsidies for cleaner technologies (e.g. electric vehicles [repealed 2013] or heat pumps), and stricter regulations for buildings (e.g. adoption of National Energy Code [currently being implemented]). The Climate Change Action Plan and Provincial Energy Strategy contain a plethora of recommendations to create more of these types of programs. While these types of programs can generally provide fairly reliable and predictable emission reductions, they can also come at significant cost to the public purse.

## Market-based approaches:

These types of actions generally aim to modify behaviour by making desired behaviours less expensive, thus 'nudging' people into making better choices. They also help to correct the market where the true cost of a product is not reflective of what people are paying for it. In public programs as described above, governments decide how people should reduce emissions, while the market allows individual consumers and businesses to choose the best option for themselves. A very successful example of a market-based strategy is the Montreal Protocol of 1987 which established a cap-and-trade system for ozone-depleting substances, successfully reducing them at minimal cost. Economists widely agree that market-based approaches to reducing GHGs (cap-and-trade or carbon taxes) are the most cost-effective way to reduce emissions.

Canadian economists widely agree that carbon pricing should be the core of any plan to reduce GHG emissions because it would reduce the most emissions at the lowest cost. The current strategies in place on PEI provide a decent range of public programs but are missing the market-based approach, a price on carbon, which would be the main driver of emission reductions. The federal and provincial governments recognized this when they created the Pan-Canadian Framework on Clean Growth and Climate Change in 2016, in which all provinces and territories (except Saskatchewan) committed to implementing a carbon price, along with other measures. The agreement provides that the federal government will implement a carbon price (called the federal backstop) in provinces that choose not to do it themselves. This federal backstop will come into effect January 1, 2019.

## **A made-for-PEI carbon price**

While the federal backstop carbon price would provide the missing piece of PEI's climate change plan, it is designed to be a Canada-wide solution, and is not the best option for PEI. We are proposing a made-for-PEI carbon price that better fits our province's needs and meets our commitments. Following the benchmark set by the Pan-Canadian Framework and the federal backstop, a price on carbon would be set at \$20/tonne for 2019 and increase by \$10 per year.

### **Revenue neutral approach**

Establishing a price on carbon will generate revenues for the province, which can be used in various ways. For example, Alberta has chosen to divide these resources between investments in renewable energy, tax rebates to residents, and other measures. British Columbia adopted a 'revenue neutral' approach in which all revenues are returned to taxpayers through tax rebates and cuts to other taxes, rather than using revenues to pay for other programs. We propose that PEI adopt a revenue neutral approach, as described below.

### **Carbon Pollution Dividend**

We propose that government create a Carbon Pollution Dividend which would provide every Islander, with the exception of top earners, with a quarterly check (similar to the HST rebate), regardless of their actual carbon cost. The higher cost of carbon would encourage people to spend less on fuels, while the Dividend would offset the impact of these higher costs. It would also create an extra incentive: as people make changes to conserve energy (e.g. by installing a heat pump or driving less) they will reduce their costs while still receiving the same Dividend. The Dividend would also be scaled to income so that lower-income Islanders are not negatively impacted, and that they actually come out ahead and can better afford to make the changes that will reduce their emissions. Higher-income Islanders who can most afford to pay would bear more of the cost.

Other programs already exist within Efficiency PEI to help Islanders pay for things like heat pumps and energy efficiency upgrades. The Carbon Pollution Dividend would provide extra help on top of these programs, making it easier for Islanders to reduce their energy use.

### **Support for Island business**

We expect businesses to pass the increased cost of goods and services on to consumers, and the Carbon Pollution Dividend compensates for this, but we would further support Island businesses in reducing their carbon cost. Efficiency PEI has recently opened its programs to businesses, but we feel that the importance of small businesses in creating jobs warrants additional support. Both British Columbia and Alberta use part of the revenues from carbon pricing to reduce their small business tax rates. A portion of PEI's carbon pricing revenues will similarly be used to reduce the small business tax rate.

### **Agriculture and fisheries**

While a carbon price is meant to apply to all or most emissions, it is recognized that some exemptions may need to be made. For example, the federal backstop recommends exempting fuels used in agriculture. Our plan would exempt marked fuels used in both the agriculture and fisheries sectors from the carbon price.

We further propose that the Government of PEI work with the federal government to implement this carbon pricing plan with the aim of reducing duplication and administrative burden. Much technical work has already been completed for the federal backstop and this plan would follow that model, with the changes noted above.

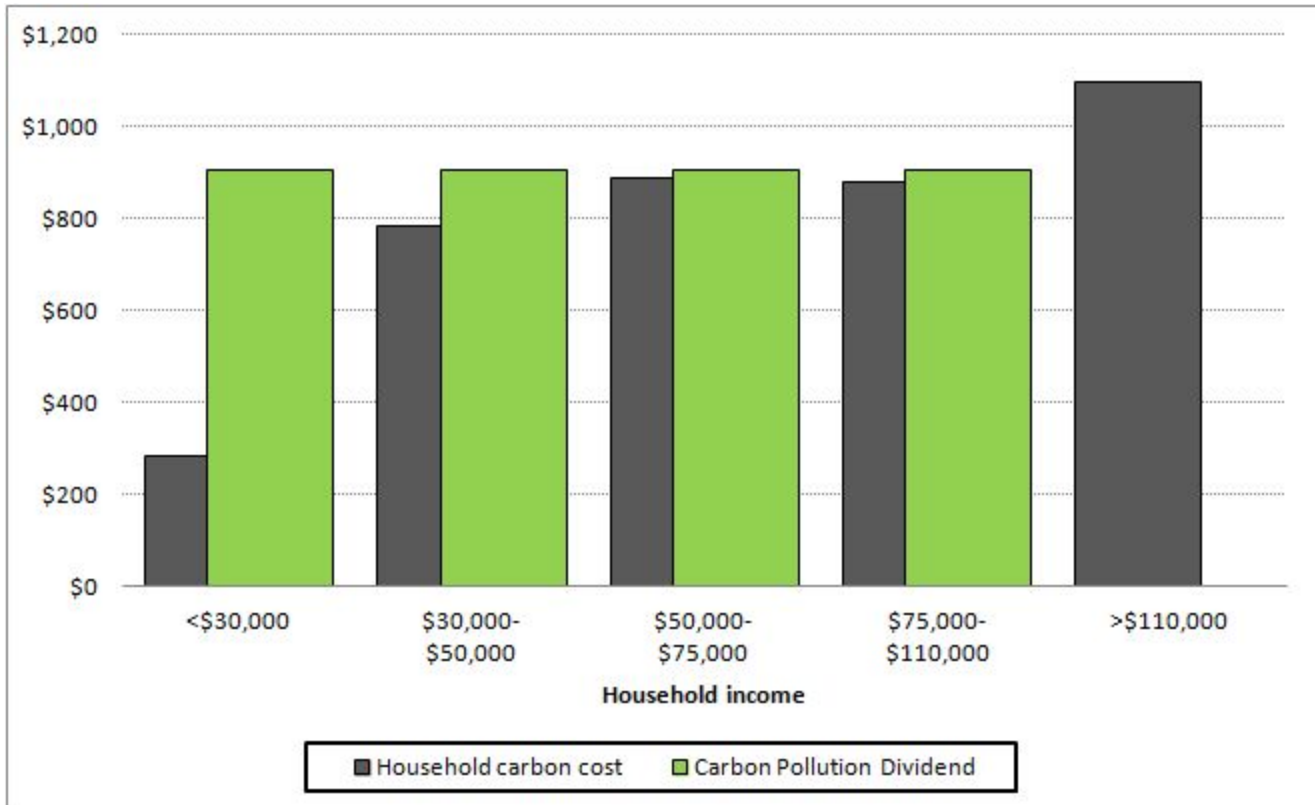


Figure 1: Estimated household cost of carbon pricing by income quintile in PEI (\$50/tCO<sub>2</sub>e). Calculations based on Dobson & Winter (2015) and Winter (2017), using data from Natural Resources Canada [Comprehensive Energy Use Database](#) and Statistics Canada [Table 11-10-0223-01](#).