

# GETTING IT RIGHT

## Design Recommendations for Ontario's Cap-and-Trade System

Executive Summary

October 2015



CLEAN  
ECONOMY  
ALLIANCE

Ontario has committed to developing a cap-and-trade program as part of a larger strategy to fight climate change. This report outlines a series of recommendations on the design of Ontario's cap-and-trade program, developed by the Clean Economy Alliance, a multi-stakeholder alliance with more than 80 members. These recommendations build upon the Alliance's founding principles on cap-and-trade program design.

The recommendations have been informed by the perspectives of experts on cap-and-trade programs and by the experiences of other jurisdictions, with particular attention paid to Quebec and California, which Ontario is expected to link with under the Western Climate Initiative.

Cap-and-trade can be an effective tool to help reduce emissions, but it's important that the system be designed well if it is to live up to its promise. With that in mind, the Alliance offers the following recommendations for consideration by the Province of Ontario, as the provincial government develops its cap-and-trade program.

## RECOMMENDATIONS

### COVERAGE

Following from the principle that the cap-and-trade program should apply to as large a share of Ontario's emissions as is practicably possible, coverage in Ontario should be aligned with Quebec and California at a minimum of 85 per cent coverage of the economy, including electricity, buildings, transportation and industry. Fuels should be included in the system from the outset. No exemptions should be given.

## **STRINGENCY**

Ontario's cap-and-trade program should be implemented by 2017 and the emissions cap should decline by approximately five megatonnes (MT) per year, on a clear and transparent schedule to provide businesses certainty. The cap needs to decline commensurate with Ontario's 2020 and 2030 targets. Consistent with the recommendations on coverage above, fuels should not be subject to delayed implementation.

## **PRICE STABILITY**

Ontario's program should include a price floor, a market stability reserve, and an allowance purchase limit. Ontario should establish an auction reserve price (acting as a price floor) that increases by five per cent per year plus inflation to align with Quebec's and California's systems. It should establish a market stability reserve (acting as a price ceiling) that holds allowances and contains clear guidelines for adding and removing allowances from the system. Lastly, it should establish an allowance purchase limit to prevent covered industries from purchasing unnecessary allowances and artificially raising the price.

## **OFFSETS**

Ontario should limit the use of offsets to a maximum of eight per cent of an entity's total compliance obligation, consistent with California and Quebec. Offsets should be subject to high standards in terms of verification to show that they are additive and permanent.

## **COMPETITIVENESS IMPACTS**

Any process for assessing and addressing competitiveness impacts must be rigorous, transparent and based on sound economic analysis. If any permits are allocated without cost, they should only be granted to a very small set of industries where there is compelling evidence that there will be competitiveness challenges and leakage. Furthermore, any free allocation of permits must be transitional, decreasing consistently over time and in keeping with emissions intensity targets that also decrease consistently over time.

## PROGRAM OVERSIGHT AND REVENUE ALLOCATION

The proceeds from carbon pricing should be dedicated to the Greenhouse Gas Reduction Account, per the Environmental Protection Act (2009), and disbursed according to the provisions of that legislation, including but not limited to:

- Mitigation of climate impacts on low-income and otherwise marginalized communities
- Monitoring, reporting, verification, oversight and governance, similar to the allocation of \$45 million for “coordination, monitoring and accountability” in Quebec’s Climate Change Action Plan
- Development and deployment of low-carbon technologies, such as renewable energy, clean technology, energy efficiency and conservation, public transit, and infrastructure for active transit, such as walking and cycling, that will support economic transformation and innovation and position Ontario to build a 21st century clean economy.

The fund should be administered by a third party in a transparent manner in order to avoid the perception of political interference and to facilitate widespread popular support. The determination of which projects receive funding should include a per dollar assessment of the GHG reduction potential of the initiative, economic analysis to ensure the proceeds deliver the greatest impact possible, and consideration of when an initiative will begin delivering emissions reductions. Ontario should also consider allocating a portion of proceeds to municipal planning authorities to develop climate change action plans to help municipalities mitigate and adapt to climate change.

## LINKAGE WITH QUEBEC AND CALIFORNIA

Through the WCI, Ontario should focus on similar design details as those in California and Quebec to facilitate linkage, while making minor improvements that ensure its system is just as, or more stringent, equitable and effective than the others while accommodating Ontario’s unique economy and environment.