

Update on Canadian Cap and Trade Programs Under the Western Climate Initiative

By Fred Cass

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On July 6, 2011, the government of Québec announced the publication of a draft regulation that will enable the Province to be ready to set up a carbon market as soon as January 1, 2012. Québec is a member of the Western Climate Initiative (WCI), which developed a program design for a cap and trade greenhouse gas emissions trading system, with an intended start date of January 1, 2012 (although it was not expected that all WCI partner jurisdictions would implement the program at that time).¹ The announcement by the Québec government indicates that the draft regulation is based on the guidelines of the WCI.

The WCI was formed in February of 2007, when the Governors of Arizona, California, New Mexico, Oregon and Washington signed an agreement to collaborate on a number of actions aimed at the reduction of greenhouse gas emissions. According to the agreement, the scope of the collaboration includes setting an overall regional goal for reduction of emissions, developing a regional market-based mechanism (such as a load-based cap and trade program) to achieve the reduction goal and participating in a multi-state registry for entities that reduce emissions.²

In August of 2007, the WCI issued a statement setting out its regional goal for reduction of greenhouse gas emissions. The goal is an aggregate reduction of emissions to 15 per cent below 2005 levels by 2020. In order to achieve the 2020 goal, the WCI partners have recommended a comprehensive regional effort that combines a broad cap-and-trade program with complementary policies. The recommendations of the WCI partners for the design of a regional cap-and-trade program were released in September 2008. This was followed by a white paper on complementary policies³ in May of 2010 and then by the cap and trade program design in July of 2010.

The WCI cap and trade system applies to facilities emitting more than 25,000 tonnes of carbon dioxide equivalent⁴ per year. It calls for each partner jurisdiction to issue emission allowances that make up a total “allowance budget” for the jurisdiction. Credit will be given for early action (i.e., emission reductions from 2008 through 2011) in the form of Early Reduction Allowances and there will be recognition of offset certificates and instruments from other programs. Emitters must report their emissions annually and, at least once

every three years, they must submit enough emission allowances and offset certificates to cover their reported emissions.⁵

The five states named in the WCI's 2007 agreement have since been joined by Montana and Utah and by four Canadian provinces. British Columbia and Manitoba joined in 2007 and Québec moved from observer status to partner status in April of 2008. At the first-ever joint meeting of the Cabinets of Québec and Ontario held in June of 2008, the Premiers of the two provinces signed a Memorandum of Understanding on a Provincial-Territorial Cap and Trade Initiative. This Memorandum envisaged that the two provinces would work cooperatively with other jurisdictions on a “joint regional market-based greenhouse gas cap and trade system” for implementation as early as January 1, 2010. In July of 2008, Ontario also changed its status within the WCI from observer to partner.

Obviously, the idea of implementing a cap and trade system as early as January 1, 2010 was overly optimistic. Nevertheless, Québec and Ontario, and the other two Canadian provinces that are partners in the WCI, British Columbia and Manitoba, have taken steps to lay the legislative groundwork for development of cap and trade regimes. In British Columbia, the *Greenhouse Gas Reduction (Cap and Trade) Act*⁶ was enacted to establish the foundation for a cap and trade system consistent with the design developed by the WCI. In Manitoba, the *Climate Change and Emissions Reduction Act*⁷ authorizes passage of regulations “respecting the use of economic and financial instruments and market-based approaches to reduce emissions or achieve and emissions reduction target”. The statutory basis for a cap and trade system in Québec was put in place through amendments to the *Environment Quality Act*⁸ and other legislative provisions. Ontario proceeded by way of amendments to the *Environmental Protection Act*.⁹

Ontario's legislative framework for a cap and trade system leaves much to be determined by regulations. The statute authorizes regulations to determine many basic features of the program, such as its scope and the emitters to which it will apply; monitoring and reporting requirements; and the creation, distribution, trading, use and retirement of economic and financial instruments. Such regulations may provide for instruments to be distributed free of charge,

1 Design for the WCI Regional Program, Western Climate Initiative, July 2010, Introductory letter from The WCI Partners, July 27, 2010.

2 Agreement on Western Regional Climate Action Initiative, February 26, 2007.

3 The complementary policies are intended to address barriers to greenhouse gas reduction initiatives and to bring about a reduction in emissions from sources that are not affected by the cap and trade program.

4 The Global Warming Potential of a greenhouse gas is its position on a scale in which carbon dioxide is 1 and other gases are assigned a rating that measures their relative impact on global warming compared to carbon dioxide. The carbon dioxide equivalent of a greenhouse gas is the product of multiplying the number of tonnes of a gas by the Global Warming Potential for that gas.

5 WCI partner jurisdictions recommend that the use of offset certificates and other instruments be limited to no more than 49 per cent of the required emissions reductions across all programs of the partner jurisdictions because emitters within the scope of the program should make the majority of the reductions needed to achieve the 2020 goal.

6 S.B.C. 2008, c. 32.

7 C.C.S.M. c C135.

8 R.S.Q. c. Q-2.

9 *An Act to amend the Environmental Protection Act with respect to greenhouse gas emissions trading and other economic and financial instruments and market-based approaches*, S.O. 2009, c. 27.

or by auction, sale or other means that are not free of charge, but, in the event that monies are paid for the distribution of instruments, the statute requires that the funds be deposited into a Greenhouse Gas Reduction Account.¹⁰

The Québec legislation provides for a cap and trade system that operates on the basis of “emission units” granted by the government.¹¹ It requires the government to establish a greenhouse gas reduction target for the province and provides for the target to be broken down into specific targets for particular sectors of activity. In light of these targets, the government sets a cap on the emission units that may be granted and these are allocated either without charge or by sale. Greenhouse gas emitters subject to the cap and trade system must cover their emissions with an equivalent amount of allowances, which can take the form of emission units, offset credits, early reduction credits, or such other type of emission allowance as may be determined by regulation.

The Québec legislative scheme provides that all greenhouse gas emission charges collected in accordance with a regulation under the statute are to be paid into the Province’s Green Fund¹² and are to be used for specified activities to tackle climate change. Among the specified activities are greenhouse gas reduction measures, public awareness campaigns and Québec’s participation in regional and international partnerships.

According to the draft regulation published in July of 2011, the Québec cap and trade system will apply to industrial sites with annual emissions of 25,000 tonnes or more of carbon dioxide equivalent. Every emitter to which the regulation applies is required to register and every person other than an emitter who is interested in purchasing emissions allowances must apply for registration as a participant. Emission allowances may be traded only between emitters or participants registered for the system and only registered emitters or participants may hold emission allowances.

The draft regulation also addresses “coverage” of greenhouse gas emissions by emitters. Every emitter to which the regulation applies must report on the coverage of emissions by providing information that includes the total quantity of verified emissions and the num-

ber and type of emission allowances to be deducted from the emitter’s compliance account in order to cover the emissions. The draft regulation states that the total number of offset credits that an emitter may use to cover greenhouse gas emissions cannot exceed 8 per cent of emissions for the compliance period.

While the draft regulation will enable the Province to be ready to set up the carbon market as early as January 1, 2012, the first year of the program will be transitional. During this transitional period, emitters subject to the regulation will be able to register as system users, take part in pilot project auctions and trade emission allowances. It is expected that the cap and trade system will actually take force on January 1, 2013.

It did not come as a complete surprise that the Province of Québec brought forward a draft regulation providing for a cap and trade program that will operate only on a transitional basis during 2012. On June 29, 2011, the California Air Resources Board (CARB) announced that the start of California’s cap and trade program would be delayed until 2013. At the time of this announcement, it already seemed unlikely that the provinces of Manitoba and Ontario would be in a position to implement cap and trade programs in 2012. The CARB announcement caused observers to think that the other two Canadian provinces that are members of the WCI, British Columbia and Québec, would follow a path similar to that of the state of California.

The CARB announcement touched on some of the context of California’s efforts to implement a cap and trade program. In March of 2011, a trial court in San Francisco made a ruling that CARB had not met the requirements for consideration of alternatives to a cap and trade system. On appeal to the First District Court of Appeal, it was determined that CARB could continue working on the development of a cap and trade regulation pending the outcome of the appeal. CARB proceeded to release for public comment a revised analysis of alternatives. Not long thereafter, the CARB announcement indicated that, in light of the importance of the regulation and “the need for all necessary elements to be in place and fully functional,” the state’s cap and trade program would be initiated in 2012, but requirements for compliance would not start until 2013.¹³

10 Money may be paid out of this account for purposes that include reimbursement of the government’s expenses in administering the program and carrying out or supporting greenhouse gas reduction initiatives, particularly those that relate to the sectors of the Ontario economy that are subject to the program.

11 *Environment Quality Act*, R.S.Q. c. Q-2, sections 46.5 to 46.18.

12 The Green Fund is discussed under heading 12(6) in this chapter, Carbon Tax.

13 Statement to the Senate Select Committee on Environment, Economy & Climate Change by Mary D. Nichols, Chairman, California Air Resources Board, June 29, 2011.

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