



## Ontario's New Greenhouse Gas Strategy: Is it a Workable Solution?

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Because of the clear causal connection between the increase in emissions of greenhouse gases (GHGs, primarily carbon dioxide, methane, and nitrous oxide) and rising global temperatures, governments are seeking new strategies to encourage GHG emitters to reduce their emissions. For example, one method proposed is the use of market mechanisms to put a price on excessive GHG emissions.

The Ontario legislature passed the *Environmental Protection Amendment Act (Greenhouse Gas Emissions Trading), 2009*<sup>1</sup> (EPAA) in December 2009, and in doing so amended the *Environmental Protection Act*.<sup>2</sup> This allowed cabinet to make regulations establishing measures for the use of economic and financial instruments and market-based approaches to control and mitigate GHG emissions and for the establishment of an environmental emissions registry. Their purposes and approaches were aimed at facilitating the maintenance or improvement of environmental standards, protection of the environment, and to achieve environmental quality goals in a cost-effective manner. The EPAA specifies that such market-based approaches could include – but are not limited to – emissions trading. This caveat is significant as it keeps the government's options open to consider other ways to price carbon, such as a carbon tax or levy.<sup>3</sup>

As a direct response to this, and continuing its good record on environmental legislation, the Ontario government has issued a discussion paper on GHG mitigation, outlining its plan moving forward to address this issue.<sup>4</sup> The discussion paper has made sweeping recommendations on proposed changes to legislation dealing with carbon credits and how they are to be dealt with. This will greatly change the environmental landscape, and more importantly, dictate how companies carry out their day-to-day business. It must be noted that the system, as described in the discussion paper, appears to be focused primarily on the “larger emitters”; that is, large corporations and sources primarily associated with the fossil fuel sector. This approach may turn out to be less useful than a “ground-up” approach.

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<sup>1</sup> S.O. 2009, c. 27 (Bill 185). For background, see *Redefining Conservation – Annual Report 2009/10*, Environmental Commissioner of Ontario ([http://www.ecoissues.ca/index.php/Redefining\\_Conervation](http://www.ecoissues.ca/index.php/Redefining_Conervation)), part 2.5 (“ECO Report”).

<sup>2</sup> R.S.O. 1990, c. E.19.

<sup>3</sup> ECO Report, *supra* note 1.

<sup>4</sup> *Greenhouse Gas Emissions Reductions in Ontario – A Discussion Paper*, Ontario Ministry of the Environment (January 2013) ([http://www.downloads.ene.gov.on.ca/envision/env\\_reg/er/documents/2013/011-7940.pdf](http://www.downloads.ene.gov.on.ca/envision/env_reg/er/documents/2013/011-7940.pdf)) (“GHG Discussion Paper”).

Among the recommendations in the paper are:

- introduction of a reporting system in the form of a GHG registry
- phasing-out of coal plants by the end of 2014 and the implementation of the feed-in-tariff programme under the *Green Energy Act*<sup>5</sup>
- establishment of emissions limits aimed at stabilizing emissions over time, with proposed limits for each industrial sector set at the forecast of total emissions expected at the start of the programme, and thereafter declining by five percent over five years, which may be motivated by
  - production-based benchmarks
  - energy benchmarks
  - reductions from an historical baseline
- cost-saving investments geared at optimizing energy efficiency, maximizing competitiveness and productivity, and retaining and creating jobs (the paper cites research estimating the current worldwide investment in energy efficiency to be US\$700 billion, and projecting a tripling of this figure by 2020)
- a cap-and trade system with offsets, which would place progressively stricter limits on major GHG emitters and force them to purchase permits to discharge GHGs and establish a market in those permits, with a carbon registry providing a database from which the trading scheme would be constructed.

Of all of the proposals, the most important is the cap-and-trade regime, designed to help Ontario meet its 2020 target to reduce GHG emissions by 15 per cent below 1990 levels.<sup>6</sup> The system would be designed such that it would be compatible with other North American systems currently under development. To ensure the province is “on the same page” and working in tandem with cap-and-trade developments elsewhere in North America, in July 2008 Ontario joined the Western Climate Initiative (WCI), which is a collaboration of some U.S. states and Canadian provinces working towards a common framework for the design and implementation of a tradable carbon permit system.

### **Cap-and-Trade System versus a Carbon Tax**

Supporters of cap-and-trade argue that it has two main strengths. It sets a steadily declining ceiling on carbon emissions, and, by creating a market that rewards companies for slashing CO<sub>2</sub> (corporations that reduce emissions below their allotment can sell them on the open market), it uses the free enterprise system to wean the country off fossil fuels and onto renewable energy. Proponents of a carbon tax say their plan has one overriding benefit: its simplicity.<sup>7</sup> They contend that by imposing a predictable and steadily increasing levy on fossil fuels, the carbon tax will also encourage development of alternative sources of energy.

The cap and trade system will mainly rely on “offsets” – voluntary emission reductions that can then be traded with other market participants. A number of studies have shown that offsets can

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<sup>5</sup> *Green Energy Act*, S.O. 2009, c. 12, sched. A.

<sup>6</sup> GHG Discussion Paper, *supra* note 4.

<sup>7</sup> Matthew Bramley, *Key Questions for a Canadian Cap-and-Trade System* (2009) Pembina Institute (<http://www.pembina.org/pub/2015>).

be a critical and effective component for achieving low-cost reductions for covered industries.<sup>8</sup> They also may help to promote investment and innovation in uncovered sectors of the economy by providing financial rewards to emission reduction.<sup>9</sup>

A cap-and-trade system in isolation cannot reduce overall emissions unless the cap is periodically ratcheted down. However, cap-and-trade can establish an incentive for industry to reduce emissions well below the regulated cap – to over-comply – in exchange for the right to sell excess permits to others who may need them for compliance purposes. Proponents of tradable permit systems stress that greater emission reductions occur under a cap-and-trade system than under conventional command-and-control regulations because, under the latter, no one is overtly rewarded for over-compliance. However, tradable permit systems do not replace regulation: they work best when they are supported by strong regulatory frameworks.

Offsets, however, present two major risks. The first is that large volumes of offsets may flood the market and depress the carbon price to a point where it will become unpredictable. For example because of uncertainty in verifying some of the carbon offset claims (such as those emanating from agriculture or forestry sources) the Chicago Climate Exchange (CCX) since 2011 has switched from purely carbon trading to an offset registry programme that verifies and registers claimed reduction in emissions.<sup>10</sup> This is what appears to be happening in the European Union with their European Union Emissions Trading Scheme (“EUETS”). Currently, the share price for carbon credits in the EUETS has fallen some 75% over the last five years and is expected to continue to experience difficulties. Explanations ranging from an over-subscription to a recession in the EU economy have been blamed.<sup>11,12,13</sup> In addition, in Europe there is the European Climate Exchange (ECX), which was previously a subsidiary of the CCX but now is considered to be a sister company that privately trades on the European Futures Market.<sup>14</sup> However, with struggling carbon prices, an uncertain euro, and an unstable economy, what is in its immediate future?

The second risk regarding carbon offsets comes from the fact that it is very difficult to avoid awarding offset credits for emission reductions that would have occurred anyway, even in the absence of offsets. That is due partly to technical challenges, and partly to the fact that a lax offset system is in the interest of most buyers and sellers, who lobby accordingly. In the authors’ opinion, research seems to indicate that emissions under a cap and trade system would result in only a marginal decrease in emissions. Thus, this may not prove to be a practicable and sustainable solution to the GHG emissions issues.

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<sup>8</sup> *Ibid.*

<sup>9</sup> David Sawyer, Seton Stiebert, and Dale Beugin, “Regulating Carbon Emissions in Canada Offsets and Canada’s Greenhouse Gas Regulations: Reducing Costs, Improving Competitiveness and Lowering Emissions” (November 2011) Sustainable Prosperity & International Institute for Sustainable Development (<http://www.iisd.org/publications/pub.aspx?id=1528>).

<sup>10</sup> See <https://www.theice.com/ccx.jhtml> for background.

<sup>11</sup> “Copenhagen deal causes EU carbon price fall” *BBC News*, December, 21 2009 (<http://news.bbc.co.uk/2/hi/business/8425293.stm>).

<sup>12</sup> “Breathing difficulties – A market in need of a miracle” *The Economist*, March, 3 2012 (<http://www.economist.com/node/21548962>).

<sup>13</sup> Ewa Krukowska, “EU Risks 12 Years of Oversupply in CO2 Market: Report” *Bloomberg*, June, 11 2012 (<http://www.bloomberg.com/news/2012-06-11/eu-risks-12-years-of-oversupply-in-co2-market-report.html>).

<sup>14</sup> <https://www.theice.com/emissions.jhtml>.

## Impact for Environmental Consulting

Historically, the provinces have taken the lead with respect to environmental conservation and protection. Bill C-38 at the federal level reinforces this; however, the federal government maintains its role in this area, with some municipalities also becoming more active, as is evidenced by their use of bylaws to regulate such matters as the development of contaminated land, the discharge of liquid effluent into municipal sewage systems, and reporting on the emission of chemical substances in the course of business operations.<sup>15</sup>

But what does this all mean, and how is it rationalized within the context of the proposed changes in the Ontario discussion paper, and how will this affect environmental litigation? Quite simply, the state of affairs is presently uncertain. Consequently, many individuals and companies will likely be requiring the assistance of either in-house or independent counsel to assist them in navigating the mire that is now environmental regulation. Additionally, despite penalties and consequences laid out previously, there is no point in having such a complex system in place if one cannot expect the regulators to effectively monitor and marshal the whole exercise. The system therefore risks teetering on the edge leading to the same failure that has befallen other similar systems in other parts of the world.

Nonetheless, recently both the Quebec and California governments have announced a new cap-and-trade carbon credit system that will be shared (once all of the formalities have been decided). This system was to have come into effect in Quebec in January 2013, and has been in effect in California since 2012. Under this system, the two governments recognized that over-complicating the issue and ineffective monitoring would be counter-productive. They have instead started off small at the grassroots level, heavily restricting who can and cannot buy into the “carbon allowances”. They have implemented strict timelines for the application of allowances, and have reiterated their intention to regulate with an iron fist. Hopefully the Ontario government will pay close attention and learn from the experiences of these two governments.

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<sup>15</sup> *Report On Part 3 On Bill C-38 (Responsible Resource Development)*, House of Commons, Standing Committee on Finance, Subcommittee on Bill C-38 (Part 3) (2012, 41<sup>st</sup> Parliament, First Session) ([http://www.parl.gc.ca/Content/HOC/Committee/411/FINA/Reports/RP5645803/411\\_FINA\\_Rpt09\\_PDF/411\\_FIN\\_A\\_Rpt09-e.pdf](http://www.parl.gc.ca/Content/HOC/Committee/411/FINA/Reports/RP5645803/411_FINA_Rpt09_PDF/411_FIN_A_Rpt09-e.pdf)).