CANADIAN GLOBAL AFFAIRS INSTITUTE
INSTITUT CANADIEN DES AFFAIRES MONDIALES

The Inescapability of Carbon Taxes for Canada

by Dennis McConaghy

April, 2017

ENERGY SERIES

THE INESCAPABILITY OF CARBON TAXES FOR CANADA

by Dennis McConaghy

April, 2017

CANADIAN GLOBAL AFFAIRS INSTITUTE
INSTITUT CANADIEN DES AFFAIRES MONDIALES

Prepared for the Canadian Global Affairs Institute
1600, 530 – 8th Avenue S.W., Calgary, AB T2P 3S8
www.cgai.ca

ISBN: 978-1-988493-26-8

What had been called Canada's "market access" crisis for its hydrocarbons has been substantially redressed via the Trudeau government's explicit approval of the Kinder Morgan Trans Mountain and Enbridge Line 3 expansion projects, and its public support for a revived Keystone XL project, albeit catalyzed by Donald Trump's election to the U.S. presidency.[1]

If built, these pipeline projects would not only provide more efficient access to incremental markets for Canadian oilsands production but also potential for additional capacity for future incremental production.[2]

Another consequence is that carbon emissions from the oilsands are likely to be sustained at least at current levels, if not likely grow, over the economic life of these projects. All of this would unfold in the context of the developed world still trying to realize absolute carbon emission reductions, as codified in the Paris Climate Accord.[3]

Incredibly, Canadian governments have consistently committed Canada to carbon emission reduction targets in successive United Nations' processes, without any tangible plan on how such reductions could be physically achieved or at what cost to Canada relative to what its trading partners were prepared to impose on themselves. This has continued from Kyoto to Copenhagen to Paris.

Moreover, the world has yet to demonstrate it is capable of materially reducing its demand for crude oil and natural gas, at least out to the middle of this century, if not longer.[4]

Canada has as much right as any country to exploit its hydrocarbon resources, regardless of the relative carbon intensity of its oilsands production and attributed carbon emission per unit of production. Yet that relative carbon intensity has been the principal reason for the unique animus which the ENGO community directs at the Canadian oilsands, and which former U.S. president Barack Obama ultimately bought into in his fatuous and cynical rejection of Keystone XL in November 2015.[5] (Ironically, this was the same month that Alberta Premier Rachel Notley would introduce her carbon tax regime in Alberta).

Unless Canada chooses to eschew any opportunity to grow its oilsands and natural production, or even more extreme, to constrain existing production, Canada is unlikely to meet its Paris commitment, which is essentially a 25 per cent reduction in existing emissions by 2030.[6]

With that reality, how does Canada ever find credibility vis-a-vis other countries in terms of its contribution towards dealing with the global climate change risk? Obviously, carbon pricing is the only viable answer — by reasonably internalizing economically the otherwise unaccounted-for cost of its carbon emissions via a carbon price. However, this is a price essentially set by what Canada's trading partners are imposing on themselves via comparable explicit carbon pricing regimes or implicitly via their other policy instruments. If Canada's oilsands industry can afford that price, then it can continue to produce its hydrocarbons and therefore be deemed to have contributed adequately to dealing with the climate risk. Such a formulation should have been all that Obama could have reasonably asked of Canada given the significance of hydrocarbon production to its economy, and it should have been enough for him to have rationalized a Keystone XL approval. The same is true for Canada's other major trading partners.

Of course, the Harper government was never prepared to accept this logic. Instead, it offered disingenuous emission-reduction targets, regulated reductions in specific economic sectors and issued dubious invocations of technology breakthroughs. However, it had no intention of truly intervening to achieve targets. The cynicism was apparently not lost on the Obama administration.

Can it now be said that Prime Minister Justin Trudeau "gets" what former prime minister Stephen Harper didn't — that carbon pricing is the only viable carbon policy option for Canada?

Who can reasonably argue that the Notley government's initiative to impose a carbon tax with significant stringency — $30 a tonne — was not a necessary condition for Trudeau to justify the pipeline approvals of late 2016?[7] Trudeau's subsequent national carbon-pricing standard was intended largely to have carbon policy in other provinces conform to it. Clearly, carbon pricing is a cornerstone of carbon policy for the Trudeau government.[8]

For those conservative elements in Alberta who ask what their province got for having to endure a carbon tax, the answer should be obvious — regulatory approval of pipelines by liberal governments. Yet many are unwilling to concede the point, including, sadly, the current leaders of the province's two right-wing options. Conservatives across Canada, and certainly in Alberta, should focus on ensuring that appropriate conditions apply to carbon-pricing regimes in the country, rather than deconstructing them. Conservative should not expect that outright climate denialism is somehow a viable policy position.

Specifically, the following should be codified as fundamental conditions of Canadian carbon-pricing policy:

- Carbon pricing is to be implemented uniformly across the country via a consistent and transparent carbon tax on actual emissions that occur. No exceptions. No cap and trade. Ideally, it should be as a federally imposed national tax;
- Moreover, such a carbon tax is the pre-eminent, if not sole, policy instrument to deal with the risk of climate change in Canada. No mandates or cross-subsidies for clean technologies. No early phase-out of certain fuel types in certain sectors beyond what the incremental price signal from the carbon tax may or may not induce. And certainly there is no place for arbitrary emission reductions in

specific economic sectors. All emissions are priced the same, given that their impact is physically the same;

- The stringency of such a national tax over time will be a function of what Canada's major trading partners are doing in terms of carbon pricing explicitly, or implicitly via other carbon policy instruments;
- The tax will be applied as close as is practically possible to where the emission occurs;
- Adjustments for trade-exposed sectors must be provided;
- Such a tax will be revenue-neutral in terms of overall tax collection to Canadian governments. Off-setting its most regressive impacts is a priority, as is advancing tax reform to reduce those taxes that most negatively affect re-investment and productivity improvements within the country;
- Existing and future Canadian emission reduction targets, such as the INDC from the Paris Climate Accord, are acknowledged to be only aspirational, not binding legal commitments;
- Acknowledge existing contractual commitments that previous governments made to third parties to advance low-carbon technologies. These should persist as a matter of law.

The Trudeau government has yet to embrace such conditions explicitly. This is all the more reason for Canadians to insist that the federal government clarify itself on carbon policy and resolve contradictions and ambiguities. It ratified the Paris accord, but has yet to acknowledge how much it will cost the country to comply with it or what its actual legal constraints on Canada are. Pipeline approvals have been achieved although Paris emission-reduction commitments are at odds with them. There is no assurance that all Canadians will face the same price. Does the federal government expect that obstruction to specific infrastructure projects that have regulatory approval and related hydrocarbon production in Canada must cease? As long as the carbon tax is being paid on emissions attributed to specific projects and related production, then there is no constraint on them from a carbon perspective. Either a carbon tax implies a right to emit or it does not.

Canadian political leadership's great challenge is whether it can bring such appropriate rationality to carbon policy via carbon pricing, appropriately conditioned. Much remains for them to do.

[1] http://www.cbc.ca/news/politics/federal-cabinet-trudeau-pipeline-decisions-1.3872828, https://www.whitehouse.gov/the-press-office/2017/01/24/presidential-memorandum-regarding-construction-keystone-xl-pipeline

[2] https://mobile.twitter.com/trevortombe/status/803741757431107584

[3] http://environmentaldefence.ca/2016/12/01/how-will-canada-achieve-2030-carbon-reduction-target-despite-pipeline-approvals/

[4] http://corporate.exxonmobil.com/en/energy/energy-outlook

[5] https://obamawhitehouse.archives.gov/the-press-office/2015/11/06/statement-president-keystone-xl-pipeline

[6] http://www4.unfccc.int/submissions/INDC/Published%20Documents/Canada/1/INDC%20-%20Canada%20-%20English.pdf

[7] https://www.alberta.ca/climate-carbon-pricing.aspxb

[8] http://news.gc.ca/web/article-en.do?nid=1132149

About the Author

Dennis McConaghy is the former Executive Vice-President of Corporate Development at TransCanada Corporation. Previously, he was Executive Vice-President, Pipeline Strategy and Development. Dennis joined TransCanada in 1998, and has held senior positions in Corporate Strategy & Development, Midstream/Divestments, and Business Development. He has more than 25 years experience in oil and gas, including responsibility for Keystone XL.

Canadian Global Affairs Institute

The Canadian Global Affairs Institute focuses on the entire range of Canada's international relations in all its forms including (in partnership with the University of Calgary's School of Public Policy), trade investment and international capacity building. Successor to the Canadian Defence and Foreign Affairs Institute (CDFAI, which was established in 2001), the Institute works to inform Canadians about the importance of having a respected and influential voice in those parts of the globe where Canada has significant interests due to trade and investment, origins of Canada's population, geographic security (and especially security of North America in conjunction with the United States), social development, or the peace and freedom of allied nations. The Institute aims to demonstrate to Canadians the importance of comprehensive foreign, defence and trade policies which both express our values and represent our interests.

The Institute was created to bridge the gap between what Canadians need to know about Canadian international activities and what they do know. Historically, Canadians have tended to look abroad out of a search for markets because Canada depends heavily on foreign trade. In the modern post-Cold War world, however, global security and stability have become the bedrocks of global commerce and the free movement of people, goods and ideas across international boundaries. Canada has striven to open the world since the 1930s and was a driving factor behind the adoption of the main structures which underpin globalization such as the International Monetary Fund, the World Bank, the World Trade Organization and emerging free trade networks connecting dozens of international economies. The Canadian Global Affairs Institute recognizes Canada's contribution to a globalized world and aims to inform Canadians about Canada's role in that process and the connection between globalization and security.

In all its activities the Institute is a charitable, non-partisan, non-advocacy organization that provides a platform for a variety of viewpoints. It is supported financially by the contributions of individuals, foundations and corporations. Conclusions or opinions expressed in Institute publications and programs are those of the author(s) and do not necessarily reflect the views of Institute staff, fellows, directors, advisors or any individuals or organizations that provide financial support to the Institute.