

COR-2022-1008-2

September 2, 2022

T. Christine Hogan
Deputy Minister
Environment and Climate Change Canada
Email: bsmdmo@ec.gc.ca

Dear Deputy Minister Hogan:

RE: Carbon Pricing System Assessment Against 2023-2030 Federal Benchmark

I wish to thank you for the ongoing and productive discussion on carbon pricing systems between our respective Departments, both on the output based performance system (OBPS) for large industry and carbon tax.

On April 8, 2022, the Department of Environment and Climate Change submitted a letter to you outlining the elements of Newfoundland and Labrador's proposed OBPS for large industry for 2023-2030, which aims to meet the stringency requirements of the new federal benchmark. This approach builds on the OBPS system for large industry that came into effect in 2019 and is attached as Annex A. In response to the letter of June 29, 2022 from Minister of Environment and Climate Change, the Hon. Steven Guilbeault, with regards to outstanding questions on this approach, we have provided additional information on the OPBS according to the federal [benchmark criteria](#) in Annex B.

As stated in Premier Hon. Andrew Furey's letter of September 2, 2022 to Minister Guilbeault, Newfoundland and Labrador proposes to retain the existing carbon tax approach, including exemptions for home heating fuels, that came into effect in 2019 (Annex A) for other sectors of the economy.

I look forward to our continued engagement on carbon pricing and other priority issues.

Sincerely,



VALERIE SNOW
Deputy Minister

cc: Judy Meltzer, Director General, Environment and Climate Change Canada
Michelle Jewer, Deputy Minister, Finance
John Cowan, Deputy Minister, Industry, Energy and Technology
Patricia A. Hearn, Deputy Minister, Intergovernmental Affairs

Annex A - Newfoundland and Labrador Carbon Pricing Plan, effective 2019

Made-in-Newfoundland and Labrador Carbon Pricing Plan

	Issue	Proposed Approach
1	Start date	January 1, 2019
2	Coverage	<p>Before exemptions, approximately 91 per cent of provincial GHG emissions in 2016 on a National Inventory Report (NIR) basis (9.8 MT of a total of 10.8 MT of GHG emissions). This share is the highest among provinces and reflects the fact that the province has a small share of GHG emissions from non-energy sectors such as agriculture, industrial processes and waste.</p> <p>Including exemptions as outlined below, the effective coverage is approximately 76 percent.</p>
3	Regulatory approach	<p>Hybrid system comprised of performance standards for large industrial facilities and large scale electricity generation, and a carbon tax on transportation, building fuels, electricity generation and other fuels combusted in the province.</p> <p>Within the overall 76 percent coverage of carbon pricing, coverage includes approximately 33 per cent for a carbon tax and 43 per cent for performance standards for large industry and large scale electricity generation.</p>
4	Greenhouse gasses covered	<p>CO₂, CH₄, N₂O, 19 HFCs, nine PFCs, and SF₆. NF₃ is not regulated at this time, however, the Province will amend its reporting regulations to include NF₃. (There are negligible NF₃ emissions in the province).</p> <p>CO₂, CH₄ and N₂O account for 99.9 percent of provincial GHGs subject to carbon pricing.</p>
5	Fuels covered	All fuels for which a federal carbon price is established in the federal <i>Greenhouse Gas Pollution Pricing Act</i> .
6	Legislative mechanisms	<p>Carbon tax – provincial <i>Revenue Administration Act</i> and regulations. Legislative amendments and new regulations to facilitate application of a carbon tax will be enacted in Fall 2018 following completion of stakeholder and Indigenous consultations. A copy of the existing <i>Act</i> and regulations are available at https://www.assembly.nl.ca/legislation/sr/statutes/r15-01.htm https://www.assembly.nl.ca/legislation/sr/Regulations/rc110073.htm</p> <p>Performance standards for large industry and large scale electricity generation – provincial <i>Management of Greenhouse Gas Act</i> and regulations. Legislative amendments will be finalized in Fall 2018 to facilitate GHG regulation in the offshore area, fully regulate large scale electricity generation and provide an opt-in for industrial and electricity generating facilities that emit between 15,000 and 25,000 tonnes per year. New regulations pursuant to the <i>Act</i> will be finalized in Fall 2018 to enable facility-level GHG targets to be set and fully establish alternative compliance mechanisms. Stakeholder and</p>

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		<p>Indigenous consultations have been completed. A copy of the existing <i>Act</i> and reporting regulations are available at https://www.assembly.nl.ca/legislation/sr/statutes/m01-001.htm https://www.assembly.nl.ca/Legislation/sr/Regulations/rc170014.htm</p> <p>Offshore area adjacent to Newfoundland and Labrador – federal <i>Canada-Newfoundland and Labrador Atlantic Accord Implementation Act</i> and provincial <i>Canada-Newfoundland and Labrador Atlantic Accord Implementation Newfoundland and Labrador Act</i> (the “<i>Accord Acts</i>”). The <i>Accord Acts</i> require amendments to establish enabling authorities to extend the <i>Management of Greenhouse Gas Act</i> to the offshore area adjacent to Newfoundland and Labrador and to enable the Canada-Newfoundland and Labrador Offshore Petroleum Board (C-NLOPB) to implement regulations pursuant to the <i>Management of Greenhouse Gas Act</i> in the offshore area. These amendments require the concurrence of the Federal Government. Provincial Minister Coady wrote to federal Minister Carr on April 18, 2018 to initiate this amendment process. A copy of the provincial <i>Accord Act</i> is available at https://www.assembly.nl.ca/legislation/sr/statutes/c02.htm</p> <p>The <i>Atlantic Accord Implementation Act</i> (the <i>Act</i>) allows for the imposition of provincial taxes as if the offshore area were in the Province. The current definition of “<i>Consumption Tax Acts</i>” included in the <i>Act</i> does not reference a provincial carbon tax. Provincial officials were advised by their federal counterparts in June that a change to the definition of “<i>Consumption Tax Acts</i>” to reference a provincial carbon tax is not necessary due to the fact that fuels used for offshore activities are likely purchased in our province. While this may be the case, the Government of Newfoundland and Labrador does have concerns as the overall tax rates that apply to fuel consumed by offshore operators shall increase significantly with the introduction of a carbon tax. It is the Province’s intention to impose the provincial carbon tax to the offshore area. The Province intends to monitor purchases of fuel used in offshore activities. Should tax leakage become an issue in the offshore area, we look forward to federal support in amending the <i>Act</i> to include carbon taxes.</p>
7	Sectors and sources covered	<p>All energy sectors and sources as contained in the NIR, pending amendments to the <i>Accord Acts</i> for the offshore area, will be subject to a carbon tax unless regulated by the <i>Management of Greenhouse Gas Act</i> or otherwise exempted.</p> <p>Before exemptions, a carbon tax is expected to cover approximately 47 percent of GHG emissions and sources in the province on a NIR basis, primarily but not limited to transportation, building fuels and non-large scale electricity generation. Proposed exemptions to a carbon tax are outlined below. These exemptions will reduce</p>

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		<p>coverage to about 33 percent.</p> <p>Before exemptions, performance standards are expected to cover approximately 44 percent of GHG emissions and sources in the province, including petroleum facilities in the offshore area (pending amendments to the <i>Accord Acts</i>), refining, primary mining, iron ore pelletizing, metal smelting, pulp and paper and large scale electricity generation (pending amendments to the <i>Management of Greenhouse Gas Act</i>) sectors that emit over 25,000 tonnes per year. The Province is exploring an opt-in provision to reduce this threshold to 15,000 tonnes of GHG emissions per year. Proposed exemptions to performance standards are outlined below. These exemptions would reduce the effective standards coverage to about 43 percent.</p>
8	Carbon price	<p>The provincial carbon tax rates shall commence at \$20 tonne. The provincial Gasoline Tax will be adjusted with a goal of Atlantic parity relating to provincial taxation (including carbon tax) of fuel products. The Carbon Tax rates will only increase based on changes to Atlantic parity that allows for rate increases.</p> <p>With respect to performance standards, the contribution rate to the Greenhouse Gas Reduction Fund, an alternative compliance mechanism established in the <i>Management of Greenhouse Gas Act</i> (section 6) (further detailed below), will mirror the carbon tax rates in the federal <i>Greenhouse Gas Pollution Pricing Act</i>.</p>
9	Exemptions to the carbon tax	<p>The Provincial carbon tax will provide the following exemptions:</p> <ul style="list-style-type: none"> i. The same exemptions as those contained in the federal <i>Greenhouse Gas Pollution Pricing Act</i> (with the exception as noted in (v) below). ii. Fuels sold to Registered Status Indians, Band Councils and Band empowered entities pursuant to the <i>Indian Act</i>. iii. Fuels combusted for regulated activities at regulated facilities under the <i>Management of Greenhouse Gas Act</i>. iv. All current provincial exemptions and/or rebates as specified under the <i>Revenue Administration Act</i> regulations, specifically sections 14, 16 and 19. v. Fuels sold in sealed, pre-packaged containers of ten litres or less. vi. Aviation fuel. vii. Fuels used for offshore petroleum exploration. viii. Silviculture. <p>Further to the exemptions listed above, the International Fuel Tax Agreement (IFTA) is a cooperative agreement among the Canadian provinces and most American states to make it easier for interjurisdictional carriers to report and pay taxes on fuel consumption. Member jurisdictions work together to track, collect and share the taxes payable on motor fuels. For administrative ease and</p>

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		<p>to mitigate compliance efforts, the Province is proposing to adopt British Columbia's approach to imposing the necessary price signals on IFTA commercial vehicles. In that province, fuel used in an IFTA commercial vehicle is exempt from carbon tax and an additional fuel tax is charged under the <i>BC Motor Fuel Tax Act</i> equivalent to the carbon tax.</p> <p>Among these exemptions, the largest categories include heating fuels (estimated at 9.5 percent coverage), aviation fuel (1.9 percent), marine transportation (1.0 percent), primary resource industries (1.0 percent), methane GHGs in the oil and gas sector (0.5 percent), and diesel electricity generation (0.4 percent).</p> <p>When combined with exemptions to performance standards, the combined carbon pricing coverage is approximately 76 percent of total provincial emissions.</p>
10	Performance standards – historical approach	<p>Performance standards will include the following parameters:</p> <ul style="list-style-type: none"> i. Each regulated onshore facility will be assigned an annual GHG reduction target equal to 6 percent below its 2016 to 2017 historical average emissions-to-output ratio for 2019 as calculated by the provincial government based on verified emissions reports submitted to the provincial government using the Western Climate Initiative methodology, rising to 8 percent below its 2016 to 2018 average emissions-to-output ratio in 2020, 10 percent below its 2016 to 2018 average emissions-to-output ratio in 2021 and 12 percent below its 2016 to 2018 average emissions-to-output ratio in 2022 and subsequent years. Fixed process emissions will be excluded from the calculation (details below). ii. Each regulated offshore petroleum facility will be assigned the same percentage reductions to its average emissions level, excluding federally regulated emissions for methane from venting and fugitives. iii. Mobile Offshore Drilling Units (MODUs) that are not undertaking exploration and meet the <i>Management of Greenhouse Gas Act</i> GHG threshold will be regulated under the <i>Management of Greenhouse Gas Act</i> with its annual target prorated based on the number of days it operates per year. MODUs not undertaking exploration and not meeting these thresholds will be subject to the carbon tax. iv. For the purposes of in-pit mining at a primary mining facility and at the request of the facility, output will be defined as total materials moved on the mining lease. v. An option will be provided for each industrial facility to use an industry-wide performance benchmark, where feasible, rather than an historical-based target (further details below). vi. Where a facility produces two or more distinct products, the

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		<p>facility's average greenhouse gas-to-output ratio for each product will be used where the facility demonstrates that the products are distinct and that the product-specific ratios are objectively and reasonably calculated.</p> <p>vii. For the Holyrood Thermal Generating Station, baseline production will be set at the level projected by Newfoundland and Labrador Hydro in its detailed 2012 study that informed the development of Muskrat Falls.</p> <p>viii. New entrants and significantly modified facilities will be phased in through establishing a three year grace period at the start of production, and progressively phasing-in greenhouse gas reduction targets in equal increments over a five year period until the full target is applied in year eight. MODUs are not to be considered as a new facility or significantly modified facility.</p> <p>Fixed process emissions identified in item (i) above include emissions from natural ore carbonates, limestone flux and dolomite flux at IOC's pelletizing operations, hydrogen production at North Atlantic Refining, and soda ash, lignosulfonate, hydrex 3443 and related sources at Vale's hydrometallurgy facility. These emissions will not reduce carbon pricing coverage for performance standards as, in the NIR, they are considered as industrial processes and are therefore not subject to carbon pricing.</p>
11	Performance standards – sector benchmark	<p>For a facility that opts to be regulated according to a performance benchmark, the benchmark will be set according to the following parameters:</p> <ul style="list-style-type: none"> i. It may include all comparable facilities that are located in Canada and the United States, as appropriate, that produced commercial output equal to at least 50 percent of its reported capacity in the year that the benchmark is set. ii. It will be set on the basis of capacity, production and greenhouse gas emissions as reported to Environment and Climate Change Canada and the United States Environmental Protection Agency and shall be adjusted at least annually or every third year, based on data availability. iii. All facility emissions will be included in calculation of the performance benchmark, including fixed process emissions. iv. Where that facility uses an energy source that differs from normal industry practices in North America, GHG emissions will be adjusted by converting the energy source used at the facility to the energy source generally used by industry on a British Thermal Unit basis using standard emissions factors published by Environment and Climate Change Canada and amended from time to time. The adjustment factor will be determined based on information provided by the facility where the facility demonstrates that the adjustment factor is objectively and reasonably calculated.

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		<p>v. The performance benchmark will be set at the top tercile of all facilities in the benchmark. However, performance credits (described below) can only be earned based on the facility exceeding the top quartile.</p>
12	Exemptions to performance standards	<p>The federal government is regulating methane GHG emissions from venting and fugitives in the oil and gas sector. These emissions will be exempted from performance standards. Offshore exploration activities will also be exempted. This will reduce the effective performance standards coverage by up to 1.0 percentage points.</p>
13	Alternative compliance options to meet performance standards	<p>The <i>Management of Greenhouse Gas Act</i> (section 5) provides for the use of greenhouse gas reduction credits as an alternative compliance mechanism. Three forms of credits are established in the Act, including:</p> <ul style="list-style-type: none"> i. Greenhouse Gas Reduction Fund credits. The Fund is established in Section 6 of the <i>Act</i> and the Fund purpose and structure is outlined in Sections 6 to 9 of the <i>Act</i>. These credits will be priced at the federal carbon tax rate. ii. Performance credits. Performance credits will be awarded to a facility for over-achieving its GHG reduction target in a year. However, for a facility opting for a performance benchmark, performance credits will only be awarded to a facility for over-achieving reductions up to the top quartile. Credits are bankable by a facility and are tradeable across facilities. The credit price will be determined by the market (i.e., the price may vary from the federal carbon price). iii. Offsets credits. The <i>Act</i> makes provision for offsets credits. The provincial system will not include carbon offsets in 2019. A provincial offsets system will be developed after 2019 and will be informed by the design of offsets system in other provinces and by the federal government, and by ongoing work by the Canadian Council of Ministers of the Environment. <p>Purchased greenhouse gas reduction credits by a facility, which excludes performance credits that it generates at its own facility, cannot be used to meet more than 90 percent of its GHG target obligation in 2020, 85 percent in 2021 and 80 percent in 2022 and subsequent years. If these thresholds are not met, a facility shall pay into the GHG Reduction Fund any required remaining obligation to be in compliance at a rate equal to 4 times the federal carbon price in that year. These limits on access to credits do not apply to offshore facilities.</p> <p>A greenhouse gas reduction credit cannot be used by a regulated operator to reduce carbon tax that may be levied under the <i>Revenue Administration Act</i> or any other provincial or federal legislation.</p>
14	Enforcement mechanisms	Carbon tax – Existing Department of Finance administrative processes will be used for monitoring and compliance. This will

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		<p>include fuel-specific sales volume and value data by fuel type and will be expanded to include fuels for which an existing gas tax is not applied. The <i>Revenue Administration Act</i> (Part II) contains inspection and compliance authorities that will apply to implementation of a carbon tax.</p> <p>Performance standards – Annual reporting process will include submission of an annual GHG report by June 1 of a given year following a reporting period, a verification report by September 1 of that year, and a compliance report by November 1 of that year. The <i>Management of Greenhouse Gas Act</i> (sections 13 to 25 and section 28) contains inspection and compliance authorities that will apply to implementation of performance standards. Pending amendments to the <i>Accord Acts</i>, the C-NLOPB will be delegated responsibility for receiving and approving reports from offshore petroleum facilities.</p>
15	Reporting	<p>Carbon tax – carbon tax revenues will be reported through annual provincial budget processes. Using these administrative records, the Province can estimate annual GHG emissions from fuels covered by a carbon tax on the basis of revenue received (estimates calculated using provincial administrative records may differ from NIR reported estimates using Statistics Canada data). Additional revenue detail can be provided to the Federal Government (pending a review of desired federal reporting requirements, once provided).</p> <p>Performance standards – the <i>Management of Greenhouse Gas Act</i> requires (section 6) public reporting on the activities of the Fund, including revenues collected, and requires (section 10) annual and public reporting of GHG emissions from regulated facilities. Regulations to this effect are in place (weblink provided above) and data collection started in 2016 (onshore facilities only). Operators of offshore petroleum facilities and the Holyrood Thermal Generating Station (HTGS) report their emissions on a voluntary basis (HTGS emissions estimates are published). Additional detail can be provided to the Federal Government (pending a review of desired federal reporting requirements, once provided).</p>
16	Anticipated environmental outcomes	Cumulative direct on-site GHG reductions below business-as-usual are projected to total up to 1.7 MT between 2019 and 2030.

Annex B – Response to Outstanding Issues on the OBPS, 2023-2030

Criteria 3.1.4 OBPS Stringency for Industry

- The Provincial Government established principles in its carbon pricing approach that were approved by the federal government in 2018, including the establishment of a carbon pricing system that recognizes, to the extent possible, the investment made in the Muskrat Falls hydroelectric generation project. This principle is manifested through OBPS performance credits awarded to Newfoundland and Labrador Hydro (NLH) for the Holyrood Generating Station in accordance with section 10(3) of the **Management of Greenhouse Gas Regulations**.
- The Provincial Government proposes to establish a floor price for the performance credits awarded to NLH for the Holyrood Generating Station through a legal mechanism external to the **Regulations**. A maximum 10 per cent discount rate for these credits below the regulated carbon price in 2023 will be applied. It will be reduced by one percentage point per year until it reaches five per cent in reporting year 2027, and it will be maintained at five per cent in future years.
- The provincial government reviewed floor prices established in greenhouse gas regulation elsewhere in Canada, including the cost containment program in the Alberta system, which includes a 15 per cent discount factor for both performance credits and offsets credits under its cost containment program.
- The province also commits that greenhouse gas emissions from a source category in sections 5(f) to (i) of the **Management of Greenhouse Gas Reporting Regulations** will be covered starting in 2023. The baseline for industrial process emissions would be set in the same manner as currently exists in sections 4 and 5 of the **Regulations**. ECCC Department officials have previously identified regulated facilities that would be impacted by this regulatory amendment.

Criteria 3.1.5/ 3.2.3 Application of OBPS and Performance-based Rebates

- The regulated facilities under the **Management of Greenhouse Gas Act** in the Province are in the petroleum, iron ore, nickel, and electric industries. These facilities (with the exception of electricity) fully or almost fully export their products to international markets. In these cases, provincial exporters compete with exporters from countries that may not be subject to a carbon constraint.
- Two reporting facilities to the federal Greenhouse Gas Reporting Program in each of 2017 to 2020 are not regulated by the provincial OBPS system as they fall outside the scope of eligible sectors defined by the Act, and are not at risk of carbon leakage.
- The **Act** and regulations do not make provision for any performance-based rebates. The **Act** (sections 6 to 9) establishes an arms-length fund that provides for project applications from regulated and non-regulated facilities in the electricity, oil and gas, mining, and manufacturing sectors, and requires that any project awarded to a regulated facility can only consider greenhouse gas emission reductions over and above required reductions. The approach does not establish any relationship between monies paid into the Fund and project monies awarded.

Process and Timelines for Finalizing System

- The province's intent is to finalize regulatory amendments by December 2022. In the event that an extension of this deadline is needed, section 30(2) of the **Management of Greenhouse Gas Act** provides for the retroactive application of regulations.