

From: Ian Parry  
To: Governments Signatory to the Paris Accord on Climate Change  
Date: July 26, 2018  
Re: CANADA'S CARBON PRICE FLOOR: A MODEL FOR THE WORLD?

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In October 2016, Prime Minister Justin Trudeau announced a pan-Canadian approach to carbon pricing ensuring that carbon pricing applies across provinces and territories in Canada with increasing stringency over time. Jurisdictions are free to use an explicit price-based system like a carbon tax (as in British Columbia) with a price rising to \$50 per tonne of carbon dioxide (CO<sub>2</sub>) by 2022, or an equivalent emissions trading system (as in Quebec), in either case with revenues remaining in the jurisdiction of origin. The federal 'carbon pricing backstop system' will impose emissions pricing in any province or territory that requests it or that does not have a pricing system aligned with federal requirements. This could apply to Ontario, which has just cancelled its trading program.

There is much to like about Canada's approach, as I [wrote](#) recently. Carbon pricing meets environmental objectives at lowest economic cost while raising valuable new revenues and these virtues are increasingly recognized by policymakers. In fact, there are more than 50 examples of carbon pricing schemes around the world either in place, or slated for introduction, at the regional, national and sub-national level. Canada's scheme will comprehensively cover fossil fuel emissions and the emissions price for 2022 is a reasonable intermediate target on the road to considerably higher prices that will ultimately be needed to meet Canada's pledge for the 2015 Paris Accord (cutting emissions by 30 percent below 2005 levels by 2030). And there are provisions in the federal backstop, or jurisdictional schemes, lowering burdens on firms without weakening mitigation incentives, to address concerns about Canada's international competitiveness.

In fact, Canada's approach could provide a valuable prototype for a carbon price floor arrangement among large emitters at the international level, to complement and reinforce the Paris process. 190 countries made mitigation commitments for the Paris Accord, but these commitments differ considerably in their stringency and reducing emissions in some countries (e.g., those currently using a lot of coal) is less costly than in others. This means that, as countries progress on their commitments, there is likely to be considerable cross-country divergence in emissions prices, creating pressure for some degree of international price coordination.

A carbon price floor arrangement, based on the Canadian model, is a natural way to provide this coordination, and the approach would also be analogous to tax floor agreements for indirect taxes in trading blocs like the European Union designed to limit competition by countries over mobile tax bases. A carbon price floor would provide some degree of reassurance against losses in competitiveness while allowing individual countries the flexibility to exceed the floor price which may be necessary to meet their mitigation commitments.

The main distinction with the Canadian approach is that there is no mechanism to enforce a carbon price floor at the international level (analogous to Canada's federal backstop). However, provisions for trading mitigation credits in the Paris Agreement, could encourage participation: countries for whom the price floor exceeds the price required to meet their mitigation pledge would benefit from selling their excess mitigation credits to other countries that would otherwise need prices well above the floor price.

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