

A clean reboot for the economy of tomorrow

[Clean Prosperity](#)'s written 2021 pre-budget submission to the House of Commons' Standing Committee on Finance

Our recommendations

1. Improve the policy framework for carbon pricing in Canada by making changes to the federal carbon levy and dividend¹ program to grow support for this policy, and increase the future carbon price in line with Canada's climate commitments.
2. Establish and fund complementary policies to drive emissions reductions in sectors that do not respond directly to a carbon price.
3. Invest in seeding the carbon removal technology market with policy measures and direct support.

The greatest economic opportunity of our time

¹ The carbon levy and dividend is hereafter referred to as the carbon tax and rebate.

We are entering a decisive decade for climate action. Budget 2021 will reinforce Canada's policy response to the challenges that lay ahead.

Stakeholders across the spectrum are calling on governments to lead by example and build back better. As the federal government looks to restart the economy, it should capitalize on the greatest economic opportunity of our time - the transition to a low-carbon economy.

The global cleantech market is estimated to be worth at least [\\$26 trillion](#) in the coming decade. If Canada gets its [pro-rata share](#), our cleantech sector will outgrow our auto sector. There are many [reasons](#) why Canada can be a leader in this space. We have one of the greenest electrical grids in the world, are home to abundant resources, and have a thriving cleantech sector.

The right policy choices today will create the competitive playing-field of tomorrow, and unlock the green jobs and investment of the future. Carbon pricing is the most cost-effective policy tool for reducing emissions. It is a powerful market-based mechanism that provides Canadians with the flexibility to choose when and how to cut their emissions. The positive impacts of carbon pricing on the economy are well documented. It sends a clear signal to the private sector that businesses and investors will be rewarded for low-carbon innovation. Citizens are incentivized to change their behaviours and reduce their carbon footprint. And unlike other policy tools, carbon pricing sends money back to households, ensuring that the policy is affordable.

We support the federal carbon tax and rebate, and believe it can be strengthened. Our recommendations for change include providing regular direct payments to Canadians, gradually raising the carbon price over time after 2022, and incorporating the GST revenues from the tax into payments provided to non-urban households.

With carbon pricing at its core, the federal government should also implement complementary policies to firm up Canada's climate policy framework. This includes targeting sectors, like buildings, where carbon pricing has a more modest impact.

Lastly, Canada has an opportunity to lead the development of carbon capture utilisation and storage (CCUS) and direct air capture (DAC) technology. The UN's Intergovernmental Panel on Climate Change states that these technologies are critical to keeping global average temperature increases below 1.5°C. Experts agree they will help to avert the worst impacts of climate change. The federal government should move quickly to support the growth of these industries at home.

Recommendation 1. The government should improve the policy framework for carbon pricing in Canada by making changes to the federal carbon tax and rebate program to grow support for this policy, and increase the future carbon price in line with our climate commitments.

The federal government should **change the carbon tax rebate mechanism to a direct payment (direct deposit or cheque), ideally quarterly**. The climate action incentive (CAI) is currently paid out annually at tax time and is buried in recipients' notices of assessment. Our research shows that only one-third of recipients know about the rebate. This negatively affects support for the tax and, by extension, climate action. Providing quarterly direct payments to Canadians would not only increase awareness of the policy, but also save the government over \$30M annually by reducing the borrowing costs on a full-year of CAI payments.

Direct payments will also increase the impact of carbon pricing on reducing emissions. [Research conducted by the Martin Prosperity Institute](#) on the Canada child benefit, a direct-payment benefit, showed that recipients used the money in ways consistent with the program's goals. We believe that direct rebate payments will produce the same results, encouraging people to use their rebate to reduce their carbon footprint.

We also recommend that the government **use the GST that is gathered on the carbon tax to provide larger top-ups to non-urban residents**. The [PBO estimated in February 2020](#) that \$179 million in GST revenue would be collected from carbon pricing in 2020-21. This figure will grow to \$290 million by 2022-23. The carbon tax rebate currently provides a 10% top-up to rural residents in recognition that they have fewer options to reduce their carbon footprint. We recommend that GST funds be used to increase the top-up and expand the number of non-urban residents who receive it. Clean Prosperity will have research findings ready this fall that outline how to optimally allocate this additional revenue across these objectives.

The government should likewise **redirect the 7% of carbon tax proceeds that are rebated to small businesses via the Climate Action Incentive Fund (CAIF) into a tax credit for SMEs**. Our analysis suggests that SMEs could be given a credit equivalent to a 0.5% cut in the small business tax rate. This credit could be increased annually, reaching the equivalent of a 1% cut to the tax rate by 2022. A tax credit is a more direct way to compensate businesses for the increased costs they face from carbon pricing in comparison to CAIF's energy efficiency grants that are provided on a first-come, first-served basis.

Lastly, the federal government should begin planning to raise the carbon price after its last scheduled increase to \$50 per tonne/CO₂e in 2022. Canada's Paris commitments and our 2050 net-zero pledge mean the government will need to up its climate ambitions. Carbon pricing is the lowest-cost tool available to do this. Research shows that GDP per capita is estimated to be \$[1,200](#) higher under carbon pricing than the best alternatives. We recommend that the government **increase the carbon price by \$10/tonne annually from 2023 through 2030, with adjustments for inflation**. This would represent a credible increase and strengthen climate action while providing the private sector with the certainty needed to make low-carbon, job-creating investments.

Cost implications - The federal government should provide funding to the Canada Revenue Agency for the IT needed to move the CAI to quarterly direct payments. Based on past IT upgrades at the CRA, a conservative estimate of the cost of the upgrade is \$100 million. We estimate that the government can save at least \$35 million annually in moving to direct payments by reducing the interest costs of advancing a full-year of CAI payments to recipients. The IT upgrade will therefore pay for itself over a three year period, and the government will continue to save money after that.

Recommendation 2. The government should establish and fund complementary policies to drive emissions reductions in sectors that do not directly respond to a carbon price.

While carbon pricing is the most cost-effective policy to reduce emissions, not all sectors respond well to a market signal. These sectors require complementary policies. An example is the buildings sector, where incentives to reduce carbon footprints are different for landlords and tenants. To address this, the federal government should **fund a robust building retrofit program** that will get tradespeople back to work, make life more affordable for households by lowering energy bills, and reduce the carbon footprint of a sector that represents the third highest GHG emissions in Canada. Corporate and municipal buildings should also be eligible.

The program should feature a variety of new and previously committed policies, including interest free loans of up to \$40,000 for residential home retrofits, a scaling-up of funding and an extension of the Energy Manager Program for industrial, commercial and institutional facilities seeking energy efficiency savings and GHG reductions, and a scaling-up of the commitment to invest \$100 million in skills training for tradespeople working in the retrofit industry. Other stakeholders, notably the Task Force for a Resilient Recovery and those that contributed to the [*Building back better with a bold green recovery*](#) report, are calling on the government to invest over \$20 billion in the energy efficiency of buildings.

Cost implications - We believe the government should move aggressively in this area, expanding existing programs and creating new ones to accelerate a funding framework for retrofits on the national stage. The Canada Green Building Council has called on the government to increase its commitment to invest \$100 million in skills training to as much as \$500 million. Other groups have called for significant funding programs. The cost will ultimately depend on the level of ambition chosen by the government. We stress that building retrofits are a low-hanging fruit that will deliver significant emission reductions over time.

Recommendation 3. The government should invest in seeding the carbon removal technology market with policy measures and direct support.

Almost all scenarios for avoiding the worst impacts of climate change involve significant amounts of carbon removal from the atmosphere. Planting trees, soil sequestration and other natural solutions will all play a role, but will be insufficient. We will need wide-scale deployment of carbon removal technologies to get us there.

Canada has an opportunity to be a global leader in this sector. As of 2018, Canada was home to [15% of all global carbon utilization ventures](#), and to 20% of all commercial scale CCUS projects. We have world-leading companies and ample storage space to sequester billions of tonnes of carbon. We can also leverage the know-how and infrastructure of our energy sector, and provide new opportunities for displaced workers.

There are significant economic benefits to be had from the scaling-up of CCUS and DAC. [Recent analyses](#) of the latter's impact on the US market point to the creation of hundreds of thousands of jobs, and significant business opportunities across the supply chain.

Canada should draw on North American best practice on the use of fiscal incentives to support commercialization of carbon removal technologies. We recommend that the government **introduce a refundable and stackable tax credit, similar to the 45Q tax credit in the US**, that will better position CCUS and DAC facilities for financing opportunities from the private sector.

The federal government should also back its ambitious climate objectives and **establish an annual [reverse auction](#) to procure sequestered carbon**. This market-based mechanism would incentivize industry to sequester carbon and facilitate price discovery. A reverse auction would ensure efficiency through competition, enable the government to drive carbon removal at the lowest cost, and help it to achieve its [own emissions reduction targets](#). We recommend procuring at least 1-2 megatonnes/year from technological solutions between 2021 and 2025, after which the market may be self-sustaining.

Lastly, the **CIB should prioritize existing funding for large-scale carbon removal technology projects**. The Bank does not currently focus on these technologies. Prioritizing them would leverage Canadian cleantech expertise and attract P3 capital. It would also drive commercialization of projects and bolster low-carbon innovation with technologies developed at home.

Cost implications - The government should reallocate some of the CIB's \$35 billion funding envelope away from sectors where funds remain unspent and into carbon removal technologies. We recommend that the CIB make \$500 million available initially, and review this amount in future when reporting back to Parliament. The procurement cost of carbon removal via reverse auctions would be in the range of \$50-100 per tonne/CO₂e. This would depend on whether other incentives, like a stackable tax credit, are in place. The cost of the stackable tax credit will depend on the number of projects that capitalize on the credit. At \$50-100 per tonne, we estimate that the cost of the program over the next five years would be between \$50-200 million annually.