

# CARBON MARKET BUSINESS BRIEF

## CANADA FEDERAL OUTPUT-BASED PRICING SYSTEM (OBPS)

### CANADA'S OBPS AT A GLANCE

Years in operation	Began in 2019, with annual compliance periods.
Overall cap & trajectory	<p>The OBPS applies to facilities that emit over 50,000 tonnes CO<sub>2</sub>e/year.</p> <p>Emissions reductions obligations are determined using an output-based standard (OBS), which becomes more stringent over time. The OBS varies based on the industrial activity and competitiveness analysis on the sector.</p>
Target(s)	30% below 2005 by 2030, to reach 511 million tonnes CO <sub>2</sub> e. Canada also intends to reach net-zero emissions by 2050 and set legally binding five-year emissions reductions targets.
Emissions Reduced to date	No data available yet
Sectors covered	<p>Sectors covered under the OBPS include:</p> <ul style="list-style-type: none"> <li>• Oil and gas production</li> <li>• Mineral processing</li> <li>• Chemicals</li> <li>• Pharmaceuticals</li> <li>• Iron and steel</li> <li>• Mining and ore processing</li> <li>• Lime and nitrogen fertilisers</li> <li>• Food processing</li> <li>• Pulp and paper</li> <li>• Automotive</li> <li>• Electricity generation</li> <li>• Cement</li> </ul> <p>Cement, iron and steel manufacturing, and lime and nitrogen fertilisers have been deemed to have high competitiveness risk, and their output-based standard (OBS) is set accordingly.</p>
GHGs covered	<ul style="list-style-type: none"> <li>• CO<sub>2</sub></li> <li>• Methane</li> <li>• N<sub>2</sub>O</li> <li>• SF<sub>6</sub></li> <li>• PFCs</li> <li>• HFCs</li> </ul> <p>The OBPS covers 27% of GHG emissions where the backstop applies.</p>
# of covered entities	217 registered in 2019

Allocation method	Output standards are set per industrial activity based on the sectors' average emissions intensity. The starting point for industry is 70%. Sectors that have been identified as having high competitiveness risk have an OBS of 90% of their average emissions intensity.
Trading rules	<ul style="list-style-type: none"> <li>• A facility may comply through any combination of payment of the emissions charge, use of surplus credits, and use of offset credits</li> <li>• Surplus credits have a five-year expiry limit</li> <li>• Surrendered compliance units will be retired by ECCC</li> <li>• A facility may choose to voluntarily retire their compliance units</li> </ul>
Use of offsets and linking	Entities can use offsets from a recognised protocol and programme from a list published by ECCC. The federal government is also developing a federal offsets programme; draft regulations are expected in Spring 2020. There is a 75% cap on the use of offsets.
Other features	<p>Programme reviews:</p> <ul style="list-style-type: none"> <li>• 2020: Interim review of the Pan-Canadian Pollution Pricing benchmark, focused on competitiveness and energy-intensive trade-exposed industries</li> <li>• 2022: Total review of the benchmark</li> </ul>
Penalties for non-compliance	Penalties for intentional non-compliance are ensure the benefits of non-compliance are less than the costs of non-compliance.
Use of revenues	<p>All direct proceeds from the federal fuel levy are returned to the province or territory where they were collected.</p> <p>The Government is seeking input to inform the approach for returning OBPS proceeds.</p>

## MAJOR DEVELOPMENTS

Canada's federal carbon pricing system includes a carbon levy on fossil fuels and an output-based pricing system (OBPS). The OBPS launched on 1 January 2019 and the federal fuel levy launched on 1 April 2019. The federal fuel levy started at C\$20/tCO<sub>2e</sub> in 2019 and increases by C\$10/t per year, reaching C\$50/t in 2022.

The OBPS applies to industrial facilities that emit more than 50,000 tCO<sub>2e</sub>/year, and allows for tradable compliance credits, including offsets eligible under current provincial systems, surplus credits, and trading. It also features an Excess Emissions Charge among its compliance options, which increases in 2021 and 2022 to \$40/tCO<sub>2e</sub> and \$50/tCO<sub>2e</sub> respectively.

## MARKET COMMENTARY

As the OBPS programme is still in its nascency, several key mechanisms are still being developed, including the Federal GHG Offset System and Recognized Units.

Despite the compliance flexibility built in to the OBPS, it is anticipated that the market will have a significant shortage of compliance units; it is expected that the few facilities that will emit below their emissions limit will bank surplus credits for future compliance periods when the Excess Emissions Charge price is significantly higher.

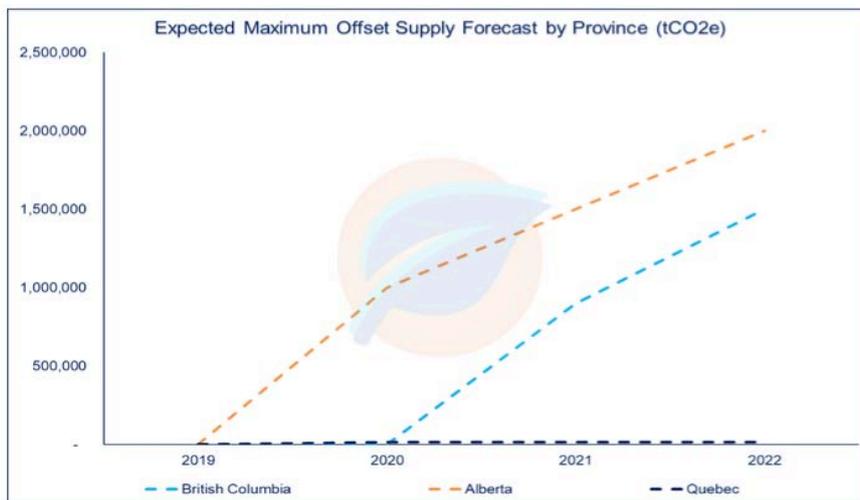
The recent announcement from Environment and Climate Change Canada (ECCC) delaying the OBPS reporting and verification deadline to 1 October 2020 will impact the timing of the issuance of Surplus Credits to eligible covered facilities. However, since the compensation deadline for the 2019 period was delayed to 15 April 2020, this will not have an impact on the volume of Surplus Credits available in the OBPS to use for compliance.

Within the expected low volume of surplus credits issued, ClearBlue projects the vast majority will be generated from

a specific industrial circumstance involving thermal heat generation; therefore, surplus credits in the early years of the programme will not be representative of facilities emitting below their caps. Also, these surplus credits will likely be tied to contractual obligations between facilities and therefore not available on the open market for surplus credits.

As for offsets, since the government is still developing the Federal GHG Offset System, it is highly unlikely that a relevant volume Offset Credits will be supplied to the OBPS market and available by the first compliance deadline of 15 April 2021. The ECCC’s initial goal to publish OBPS Draft Offset Regulations by June 2020 has been pushed back to autumn due to the impacts of the COVID-19 pandemic. Once the regulations have been finalised and project development can commence, there will be further delays bringing offset credits to market as offset projects typically take over a year to register and issue credits after beginning development.

Additionally, credits from approved projects in active provincial offset registries, including Alberta, British Columbia, and Quebec, will be eligible under the OBPS, known as Recognized Units. It is expected that credits from agriculture, waste, land use and forestry project types will be prioritised and that only projects with a start date of 1 January 2017 or later will be eligible. In regards to Recognized Units, ClearBlue expects the majority of the supply will come from established protocols in British Columbia and Alberta, with Quebec supplying a minimal amount of Recognized Units for the duration of the programme (Figure 1).



**FIGURE 1**  
Expected Maximum Offset Supply Forecast by Province (tCO2e)

Currently, these registries carry a very limited number of offset credits that would be eligible under the current priority protocols; it is estimated that there is only a maximum of 1 million offsets at the moment that could be supplied from these active registries to the OBPS.

In Canada, carbon pricing programmes remain a political issue and there continues to be a risk of the OBPS being quickly scrapped by a future government, rendering unsold Compliance Units worthless. This risk may also drive compliance entities and offset developers to consider bringing compliance units to market earlier instead of waiting until 2021 or 2022 when the Excess Emissions Charge increases to C\$40/t and C\$50/t respectively.

## USEFUL LINKS

[Environment and Climate Change Canada, Pan-Canadian Framework on Clean Growth and Climate Change](#)

[Environment and Climate Change Canada, Pricing pollution: how it will work](#)

[Environment and Climate Change Canada, Output-Based Pricing System](#)

[Environment and Climate Change Canada, Technical paper: federal carbon pricing backstop](#)

## REFERENCES

[Environment and Climate Change Canada, Canadian Environmental Sustainability Indicators: Progress towards Canada's greenhouse gas emissions reduction target](#)

[Minister of Environment and Climate Change Canada Mandate Letter](#)

[Environment and Climate Change Canada, Output-Based Pricing System Regulations](#)

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