

# Ontario Court of Appeal upholds constitutionality of federal carbon pricing regime

JULY 15, 2019 10 MIN READ

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Authors: [Richard J. King](#), [Jennifer Fairfax](#), [Tommy Gelbman](#)

## In this Update

- On June 28, 2019, the Ontario Court of Appeal issued a [majority decision](#) that the *Greenhouse Gas Pollution Pricing Act* (GGPPA) is constitutional.
- The Ontario government has indicated it will appeal the decision to the Supreme Court of Canada (SCC). The Saskatchewan government has already appealed its unsuccessful challenge to the GGPPA and is expecting it to be heard in December.
- In the interim, the Ontario government is pressing ahead with its “Made in Ontario” greenhouse gas (GHG) reduction regime. On July 4, it released two regulations to implement Ontario’s new Emissions Performance Standard.

## Introduction

On June 28, 2019, the Ontario Court of Appeal [rendered its advisory opinion](#) regarding the constitutional validity of the *Greenhouse Gas Pollution Pricing Act* (the GGPPA) — colloquially known as the federal “carbon tax.” In a 4-1 decision, the majority held that the GGPPA is constitutional. The Ontario government has said that it will appeal the decision to the SCC.

The decision marked the second time that a Court of Appeal has upheld the constitutionality of the federal carbon pricing regime. The Saskatchewan government has already appealed the decision of the Saskatchewan Court of Appeal to the SCC and expects to have the matter heard in December.<sup>[1]</sup>

Despite the significant weight of concurring Court of Appeal decisions in Saskatchewan and Ontario, the debate regarding the constitutionality of the GGPPA appears far from settled. Alberta is pursuing a reference to its Court of Appeal, and Manitoba has applied to the Federal Court for a judicial review of the decision to impose the Federal Backstop (defined below). The New Brunswick government recently announced that it will abandon previous plans to challenge the GGPPA in court.

In the shadow of a fall federal election, these legal proceedings matter to Canadian businesses because they will likely (i) determine the fate of carbon pricing in Canada and each of the provinces, (ii) influence the scope of federal and provincial powers to regulate environmental matters and (iii) develop the jurisprudence on taxation in Canada. The recent decision of the Ontario Court of Appeal provides an opportunity to review the constitutional arguments that are likely to be considered in future legal proceedings.

In this Osler Update, we summarize the most significant aspects of the Ontario Court of Appeal decision and discuss the practical implications should the GGPPA continue to be upheld, particularly when, in the interim, the Ontario government is pressing ahead with its “Made in Ontario” GHG reduction regime. On July 4, Ontario released two regulations — [O. Reg. 241/19](#) and [O. Reg. 242/19](#) — to implement Ontario’s new Emissions Performance Standard.

## Background

The GGPPA, which entered into force on June 21, 2018, established a federal GHG emissions pricing scheme that ensures the existence of carbon pricing throughout Canada in the form of (i) a fuel charge and (ii) an output-based pricing system (OBPS) for large industrial emitters. A critical element of the legislation, and the source of some provincial discontent, is the so-called backstop, whereby provinces are entitled to enact their own carbon pricing schemes that meet designated federal benchmarks — but those that do not are subject to the federal pricing regime (the Federal Backstop).

The fuel charge generally applies to fuel producers and distributors operating in backstop jurisdictions. The fuel charge backstop is currently applied in Ontario, New Brunswick, Manitoba, Saskatchewan, Yukon and Nunavut. It is scheduled to be applicable in Alberta on January 1, 2020.

The OBPS applies to facilities that (i) have reported 50 kilotonnes or more of carbon dioxide equivalent emissions in any year since 2014, (ii) carry out a covered activity<sup>[2]</sup> and (iii) operate in a backstop jurisdiction. It also applies to facilities that have reported 10 kilotonnes or more of carbon dioxide equivalent emissions in a year since 2014 and volunteer to opt-in to the OBPS. Like the fuel charge, the OBPS backstop is currently applied in Ontario, New Brunswick, Manitoba, Prince Edward Island, Yukon, Nunavut and partially in Saskatchewan. It is also scheduled to be applied in Alberta on January 1, 2020.

The current benchmark price for the fuel charge and the OBPS is \$20 per kilotonne of carbon dioxide equivalent emissions and it is set to increase by \$10 annually until 2022. However, the GGPPA is not designed to raise revenue. It requires all revenue collected from the fuel charge and the OBPS to be returned to the jurisdiction where it was collected, via the jurisdiction’s government or prescribed entities to be defined by regulations. The Ontario government challenged the GGPPA in court on the grounds that Part 1 (the fuel charge) and Part 2 (the OBPS) — which Ontario labels a “carbon tax” — are unconstitutional. Ontario argued that Parliament is not entitled to regulate all activities that produce GHG emissions and that the jurisdiction Canada asserts under the GGPPA “would radically alter the constitutional balance between federal and provincial powers.” Specifically, Ontario took the position that (i) the fuel charge and the OBPS are unconstitutional because they cannot be supported under any federal head of power under the *Constitution Act, 1867*, and (ii) the charges are not legislatively authorized as taxes and do not have a sufficient nexus to the purposes of the GGPPA to be considered valid regulatory charges.

## The majority opinion

Rejecting Ontario’s submissions, Chief Justice Strathy, writing for the majority, found that the GGPPA is constitutionally valid. Three key findings underpin the majority’s conclusion.

First, the majority established the purpose of the GGPPA by focusing on its preamble, Canada’s international commitments and its domestic initiatives. This led the majority to reject both Ontario’s characterization of the legislation as “a comprehensive regulatory

scheme for the reduction of greenhouse gas emissions from all sources in Canada” and the federal government’s characterization of the legislation as the “cumulative dimensions of GHG emissions.” Instead, the majority characterized the “pith and substance” of the GGPPA as “establishing minimum national standards to reduce greenhouse gas emissions.” In a concurring opinion, Associate Chief Justice Hoy found that the majority’s characterization of the GGPPA was too broad and that its true substance was captured by “establishing minimum national greenhouse gas emissions pricing standards to reduce greenhouse gas emissions.”

Second, influenced in part by prior SCC jurisprudence recognizing that the environment “is not a ‘matter’ of exclusive jurisdiction, resting with one or other level of government,” but rather an “area of shared jurisdiction,” the majority classified the position of the GGPPA within the constitutional division of powers as falling under the national concern branch of the “Peace, Order and Good Government” power.<sup>[3]</sup> Applying the principles expressed in *R v Crown Zellerbach*<sup>[4]</sup> in its analysis, the majority found that establishing minimum national standards to reduce GHG emissions is a single, distinct and indivisible matter. The majority asserted the characterization was narrowly constrained to address the risk of provincial inaction regarding a problem that requires cooperative, national action: “[n]o one province acting alone or group of provinces acting together can establish minimum national standards to reduce GHG emissions. Their efforts can be undermined by the action *or by the inaction* of other provinces. Thus, the reduction of GHG emissions cannot be dealt with in a piecemeal manner. It must be addressed as a single matter to ensure its efficacy. The establishment of minimum national standards does precisely that.” Third, the majority confirmed that the charges imposed by the GGPPA were regulatory and not taxes. In doing so, the majority rejected Ontario’s submission that the regulatory charges imposed by the GGPPA are unconstitutional because the charges have no nexus to the purpose of the GGPPA. The majority held that (i) when regulatory charges are used to change behaviour, they need not reflect the cost of administering the scheme or be a cost-recovery mechanism and (ii) the revenue raised need not be used to further the purpose of the regulatory scheme. The majority went on to opine that, even if it was necessary to show that the revenues raised are used for the purposes of the GGPPA, “this has been established. The funds are returned to provinces, taxpayers and institutions to reward them for their participation in a program that benefits the provinces and the entire country. This promotes and rewards behaviour modification, encourages shifts to cleaner fuels, and fosters innovation, all of which are purposes identified in the Preamble of the” GGPPA.

## The dissenting opinion

In the sole dissenting opinion, Justice Huscroft found the majority’s characterization left the minimum standards “free-floating” for the purposes of classification. In his opinion, this made the matter of national concern identified by the majority too vague to appropriately limit the reach of Parliament’s authority into provincial heads of power. Questioning the majority’s foundational premise that a national standard is required to regulate GHG emissions, Justice Huscroft also noted the inaction of one province speaks to political disagreement and not provincial inability to address the GHG problem.

## Ontario marches forward

On July 4 — a few days after the Ontario Court of Appeal’s decision — the Ontario government released its regulation (O. Reg 241/19) regarding the Ontario Greenhouse Gas Emissions Environmental Performance Standard (the EPS Regulation), as well as complementary amendments, through O. Reg. 242/19, to the Greenhouse Gas, Quantification, Reporting and Verification regulation (O. Reg 390/18 or the Reporting

Regulation). Ontario stated that it developed the EPS Regulation “as an alternative to” the OBPS component of the GGPPA “that is now in effect in Ontario.”

The EPS Regulation establishes limits on GHG emissions for covered facilities (e.g., facilities within certain sectors that emit 50,000 tonnes CO<sub>2</sub>e or more per year, with an opt-in provision for those facilities emitting between 10,000 tonnes and 50,000 tonnes). If the limits are not met, the covered facility will be required to acquire compliance units.

While Ontario’s new EPS Regulation will apply to GHG emissions from covered facilities “as early as January 1, 2019,” the compliance obligation would only apply in the year that the federal government removes Ontario from Part 2 of Schedule 1 of the GGPPA, the OBPS component of the federal regime. Other amended provisions of the Reporting Regulation would also only apply if Ontario is removed from the OBPS.

As a result, for now, only the registration provisions of the EPS Regulation currently apply. At this time, it is not clear whether the passage of the EPS Regulation and further clarity regarding Ontario’s climate change plans will spur the federal government to remove Ontario from the OBPS component of the GGPPA. For now, the federal OBPS remains in place in Ontario. If Ontario is removed from the OBPS, the Ministry of the Environment, Conservation and Parks “expects further amendments” to the EPS Regulation and the Reporting Regulation to “address transition” from the federal regime and to expand the program to include additional sectors.

## Conclusion

The Ontario Court of Appeal decision provides an insightful assessment of the constitutional validity of the federal carbon pricing regime. The Ontario Court of Appeal’s reasoning was slightly different from that of Saskatchewan’s, although the key conclusions and outcomes were the same. For now, Canadian businesses must be prepared to comply with the GGPPA, as well as understand the developments occurring in the backstop provinces, such as Ontario, Saskatchewan and Alberta. Osler will be closely following jurisprudential, legislative and political developments in the months ahead to assist clients in understanding both the federal and provincial regimes.

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[1] For a discussion of the GGPPA advisory opinion rendered by the Saskatchewan Court of Appeal on May 3, 2019, refer to this [Osler Update](#).

[2] Covered activities include oil and gas production, minerals processing, chemicals, pharmaceuticals, iron, steel and metal tubes, mining and ore processing, nitrogen fertilizers, food processing, pulp and paper, automotive and electricity generation.

[3] The majority noted that GHGs “combine in the atmosphere to become persistent and indivisible in their contribution to anthropogenic climate change. They have no concern for provincial or national boundaries. Emitted anywhere, they cause climate change everywhere, with potentially catastrophic effects on the natural environment and on all forms of life. They are exactly the type of pollutant that [was] contemplated would fall within the national concern branch of the POGG power.”

[4] [1988] 1 SCR 401.