

Additional Comments by Senator Nick Xenophon

As previously stated, I support action on climate change, however it is crucial that the scheme is credibly internationally and sustainable domestically.

I have long advocated for an intensity-based scheme, as proposed by leading economic consultancy, Frontier Economics, whereby emitters are penalised for emissions above a set baseline and rewarded if their emissions intensity is below that baseline.

This approach preserves the same intention the Government has to reduce Australia's emissions but would not unnecessarily raise tax revenue (or prices to consumers) in the same way the proposed carbon tax will or the proposed emissions trading scheme that will follow it.

It will also enable a higher emissions reduction target – it is cheaper and greener than the Government's Clean Energy plan.

In addition to the concerns raised to the Interim Report, I am also concerned that, under the current legislative proposal and based on existing modelling that has been provided by Treasury, taxpayers may face a multi-billion dollar shortfall.

Treasury assumes a price per carbon unit of AU\$29 in 2015, however Bloomberg analysts assumes a price per carbon unit of AU\$16.

As compensation to households under the Government's proposal is in the form of lump sum compensation, which will not change in line with the carbon price, the concern is that carbon revenue will fall to about half of what is predicted if Bloomberg's forecast is correct.

This means that households would, in effect, be over-compensated and the Govt will see a significant deficit in revenue.

For example, revenue from sale of permits in 2014/15 is expected to be \$8.6 billion.

If the price in 2015/16 is \$16, as predicted by Bloomberg, not \$29 per carbon unit, then this revenue will fall to approximately \$4.7 billion.

Under the intensity-based model proposed by Frontier Economics, this would not be an issue as compensation to households would fall with the carbon price.

This proposition was put to Treasury during the recent 2011 Supplementary Estimates.

Senator XENOPHON: Bloomberg New Energy Finance, with 200 analysts around the world, say that the price of carbon is going to be \$16 a tonne in 2015. The Treasury modelling says \$29 a tonne in 2015. If the price in 2015 is \$16, not \$29, the revenue will go from \$8.6 billion to \$4.7 billion. There will be a revenue shortfall of almost \$4 billion. If Bloomberg is right, there will be a significant revenue shortfall, won't there?

Dr Parkinson: If the carbon price is dramatically different from what is assumed, and people purchase the permits from overseas, there will be an impact on the revenue collection.

Senator XENOPHON: Are you concerned that Bloomberg New Energy Finance—which is, I think, a reputable financial analyst with 200 analysts around the world that look at this specific issue—is making an assumption—

Dr Parkinson: But are they talking about the European permit price or CDM prices?

Senator XENOPHON: In terms of Bloomberg's analysis they are talking, I think, not just about Europe but about the global carbon prices.

Dr Parkinson: But it depends on what can actually be brought into the Australian market.

Senator XENOPHON: Sure, but if the global price is reduced—

Dr Parkinson: But there is not a single global price. So if what they are saying is that the European price is lower and we do not accept European permits then it does not matter, in a sense. The international price that is relevant is the price of the permits that are allowed into the Australian system. Senator, when you calculate your number, are you talking about just the household compensation or about the value of the free permits as well? The value of the free permits moves automatically with whatever the price is.

Senator XENOPHON: My understanding—and I will be corrected if I am wrong—is that there was anticipated revenue of \$8.6 billion in 2015-16.

Dr Parkinson: That is net of free permits?

Senator XENOPHON: That is my understanding.

Senator Wong: That is in the bill. You will see the fiscal tables.

Dr Parkinson: Yes, that is right. So that is the revenue from the sale of the permits themselves. So obviously if there is less revenue from the sale of the permits and all of the outlays remain unchanged then there will be a fiscal impact.

Ms McCulloch: There are elements of the package that will move with the price, so you cannot just do a straight calculation of what the impact would be from a change in price just by looking at the simple table. For example, some of the free permit or EITEIs assistance would move depending on what the price was. So the amount of compensation that you provide to industry would be linked to those changes. The other point that you need to bear in mind is that, if the prices are different, you may have different

emissions trajectories, which would also affect the volume of revenue or the value of the revenue.

Senator XENOPHON: I guess, Dr Parkinson, that the concern in my question is that Bloomberg undertook this relatively recent analysis, saying that they think that the carbon price will be much less than what has been forecast in Treasury assumptions.

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Senator XENOPHON: But is there not an issue there that there is a potential downside that, given that compensation for households is relatively fixed—the compensation for households is relatively fixed, is it not—

Dr Parkinson: That is correct.

Senator XENOPHON: So that is one part of the package that is relatively inflexible.

Dr Parkinson: Yes.

Senator XENOPHON: I understand the policy rationale, but that could cause a fiscal hole if the carbon price is less.

Dr Parkinson: And that is why I said that if everything else is constant you are correct. The bits that are constant are around the household assistance. But, as Ms McCulloch said, it is not then just a case where if the permit price is 10 per cent lower then it flows through automatically, because the value of the—

Senator Wong: Because other bits move.

Dr Parkinson: Because other bits will move.

Senator XENOPHON: Yes.

Dr Parkinson: But you are right: the household compensation component is—

Senator XENOPHON: That is relatively fixed; that is less flexible.

Dr Parkinson: That is right. Hence, if the cost of permits is lower, the extent to which households are compensated or overcompensated becomes larger.

Senator XENOPHON: That is right.

Dr Parkinson: It is akin to a tax cut or a payment to households.

Senator XENOPHON: If Bloomberg is right on that assumption, there is a significant potential fiscal downside.

Dr Parkinson: There has always been that in the same way that, if permit prices were higher, there was always a sense that you might find there would be more revenue, but you would need to think about returning that to households or what you were going to do in terms of compensation.

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Senator XENOPHON: Yes, I appreciate that. Minister, let us suppose that in 2015 the carbon price is much lower than has been forecast and the biggest fiscal risk is that the amount of compensation for households is fixed. But, if the carbon price is lower, the price impacts will be lower. Does that mean that the compensation package could also be lower in order to reduce the fiscal risk? In other words, if the carbon—

Senator Wong: That has been quite clearly ruled out by the Prime Minister.

Senator XENOPHON: So, even if the carbon price collapses, people will still get the same—

Senator Wong: The assistance is permanent.

Dr Parkinson: The compensation that comes into effect starting in May next year is permanent.

Senator Wong: It should be recalled too—and I think this was referenced earlier—that the assistance package has a range of public policy objectives. You recall that one of the significant benefits in the package is the increase in the tax-free threshold. There are obviously participation benefits associated with that as well. We have combined the carbon price assistance package with a package in terms of the tax and transfer system which is designed to encourage participation and is consistent with the direction of the Henry review.¹

This exchange strengthens the arguments for the Frontier Economics approach, which involves less revenue churn and significantly less price effects on the electricity sector, while achieving greater environmental benefits.

Finally, I reiterate my position that any proposal for a price on carbon should not be implemented until a Federal Election has been called and a mandate obtained for the introduction of such a policy.

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¹ Supplementary Estimates – Economics Committee, Thursday 20 October 2011, Page 41