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Mr John Hawkins
Committee Secretary
Senate Select Committee on Climate Policy
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Parliament House
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Dear Mr Hawkins

Senate Select Committee on Climate Policy

The Australian Industry Group (Ai Group) welcomes this opportunity to make a submission to the Senate Select Committee on Climate Policy with specific reference to the proposed Carbon Pollution Reduction Scheme (CPRS).

The CPRS is one of the most far-reaching government initiatives of recent times. If enacted the CPRS will play a central role in a transformation of the domestic economy that is rightly compared with the transformations flowing from the suite of liberalising reforms embarked upon from the early 1980s.

Background

Ai Group supports Australia putting in place a cap and trade emissions trading scheme capable of delivering the Australian contribution to a global effort to reduce the accumulation of greenhouse gases and reduce the risks of dramatic climate change.

An emissions trading scheme provides powerful incentives for business to search for least-cost emissions reductions; it reduces the scope for bureaucratic and political meddling in investment decisions; and, in contrast to a carbon tax, is able to align directly with a national reduction target through the quantity of permits issued.

Ai Group's policy positions on climate change policy are guided by the following principles:

- The reduction of emissions at the lowest possible cost to the domestic economy;
- Provision of investment certainty;

- The requirement for a sensibly-paced start that gives business time to adjust;
- Effective protection of Australia's trade exposed businesses from the additional costs imposed relative to competitors abroad;
- Securing the supply of electricity; and,
- Keeping compliance costs to a minimum.

In the light of these principles, Ai Group's National Executive has recently resolved the following points.

The start date for the CPRS should be delayed until 2012

There are considerable administrative difficulties imposed by the proposed 1 July 2010 start date that are becoming increasingly apparent. Not the least of these is the narrow window of opportunity for comments on the draft exposure legislation. Further, the detrimental impacts of the global financial crisis on the business environment - including in relation to the ability to undertake expenditure to reduce emissions – has set back businesses readiness. Both elements point to desirability of deferring the start date to 2012. We note that Australia is on track to meet our Kyoto targets and that the global slowdown will reduce the current emissions trajectory without the need for the CPRS to begin in 2010.

Additional Measures for Trade Exposed Industries

Ai Group believes there are further changes that can be made to the detail of the CPRS to reduce the potential impacts on trade exposed businesses. Areas that should be considered include:

- Broadening eligibility for emissions intensive trade exposed permits (for example by extending "Scope 3" emissions to incorporate such emissions related to feedstock on a more consistent basis than presently proposed, and lowering the emissions intensity threshold at which eligibility for permit allocation applies);
- Raising the quantity of permits allocated;
- Ensuring the Climate Change Action Fund has a particular focus on trade-exposed businesses; and
- Reducing Australia's unilateral commitment as insurance against a break-down of international negotiations.

Ai Group supports the passage in 2009 of legislation giving effect to the fundamental architecture of the CPRS

Legislation this year is needed to provide a greater degree of certainty to business and assist in informing business decisions in key areas of investment.

Ai Group maintains its opposition to the current Renewable Energy Target

Ai Group is opposed to the current Renewable Energy Target because it is a comparatively expensive approach to emissions reduction; because it adds an additional layer of costs to business and because there is no current proposal to protect Australia's trade exposed businesses from these additional costs.

Ai Group supports exploration and exploitation of the full range of abatement opportunities

We recognise the importance of giving full recognition to genuine abatement and urge the Government to accelerate consideration of such abatement opportunities both within the Kyoto framework and in the domestic offset market. For example, the considerable opportunities in approaches to sequestration such as soil carbon should be explored.

Comments Specific to the Terms of Reference

The following comments relate specifically to the Select Committee's terms of reference.

Emissions Trading Scheme (ETS)

The Committee has been asked to assess the choice of emissions trading as the central policy to reduce Australia's carbon pollution, taking into account the need to:

- reduce carbon pollution at the lowest economic cost,
- put in place long-term incentives for investment in clean energy and low-emission technology, and
- contribute to a global solution to climate change.

Ai Group supports Australia's use of an ETS as the central policy to reduce Australia's net contribution to global greenhouse gas emissions.

We see this market-based instrument as significantly superior to an alternative approach under which government's and/or government agencies mandate (for or against) particular technologies, processes or products.

The ETS is designed to let market forces select which opportunities for emissions reduction are exploited and in what order. If there are opportunities to reduce emissions at a cost less than the market price of permits, the sensible course of action is to bear the lower cost and reduce emissions. For sources of emissions that can only be reduced at a cost that is above the permit price, the sensible course of action is to surrender permits rather than reduce the emissions. In this way the ETS is expected to "select" for elimination the sources of emissions that are most affordable for the economy as a whole.

In this context one of the main attractions of the CPRS is that it removes the rationale for many alternative regulatory measures that have been advocated and it also opens up the opportunity for Governments at all levels to remove existing regulatory measures related to greenhouse gas emissions.

Ai Group maintains that an ETS will put in place appropriate incentives to invest in “clean energy” and low emissions technology among other abatement measures.

Under the proposed CPRS the combination of a long-term target (currently to reduce greenhouse gas emissions by 60% of 2000 levels by 2050); medium term gateways (currently a range emission levels of between 5% and 15% below 2000 levels by 2020); and annual targets will provide investors with a solid basis for estimating forward permit prices. This will inform, and indeed to some extent is already informing business decisions over the relative value of alternative investments – inclusive of the cost of greenhouse gas emissions.

We note that this mechanism is not particularly targeted to incentives in relation to investment in “clean energy” and low emissions technology. We regard this as a virtue of the ETS in that it does not select specific areas but provides similar incentives across the full range of abatement possibilities.

Ai Group also maintains that the ETS is the most appropriate way for Australia to link to international efforts to reduce the threat of climate change.

Complementary Measures

The Committee has been asked to assess the relative contributions to overall emission reduction targets from complementary measures such as renewable energy feed-in laws, energy efficiency and the protection or development of terrestrial carbon stores such as native forests and soils.

Ai Group maintains there is a limited though important role for complementary measures to address greenhouse gas emissions. The principle that guides our support or non-support of complementary measures is whether measures can reduce greenhouse gas emissions at a cost lower than the current (or projected) permit price.

- If emissions reduction under a complementary measure can be achieved at a price lower than the permit price, these additional emissions reductions will tend to lower the overall burden on the economy of greenhouse gas reduction.
- If, on the other hand, the per unit emissions reductions that would be achieved under a complementary measure would cost more than the permit price, adopting the measure would increase the overall burden on the economy of greenhouse gas emissions.

For example Ai Group does not support the currently-proposed Renewable Energy Target (RET). We expect the RET will add costs to business both through an expected increase in wholesale electricity prices and the obligation to purchase Renewable Energy Certificates. It will also add to consumer prices where higher business input costs can be passed on. It will not reduce Australia's net contribution to global greenhouse gas emissions beyond what would be achieved in the absence of the RET. We expect the same level of net emissions reductions to be achieved at a higher cost to the economy than would occur in the absence of the RET.

On the other hand, Ai Group does support complementary measures such as appropriately-designed public sector support for research into low emissions energy generation and programs to improve the dissemination to households and businesses of information about existing low-cost energy efficiency and emissions reducing processes, practices and technologies.

Ai Group strongly supports the exploration of the abatement potential offered by sequestration of carbon in soils and forests. We would welcome steps aimed at testing the suitability for recognition under international agreements of all forms of sequestration.

Effectiveness of CPRS

The Committee has been asked to assess whether the Government's Carbon Pollution Reduction Scheme will be environmentally effective, in particular with regard to the adequacy or otherwise of the Government's 2020 and 2050 greenhouse gas emission reduction targets in avoiding dangerous climate change.

Ai Group recognises that avoiding dangerous climate change will require a coordinated global effort. Assessment of the effectiveness of Australian action cannot be considered in isolation.

Australian action taken alone will not have a material impact on the threat of climate change. This is particularly the case if, by taking action domestically, economic activity or potential economic activity and the associated emissions migrate from Australia to countries that do not take action. This would not reduce - and may even increase - global greenhouse gas emissions and the threat of climate change.

Ai Group does nevertheless maintain that Australia can play a role in developing a coordinated global response to climate change. In particular if Australia can demonstrate the ability to take action to reduce emissions by providing appropriate incentives for abatement without harming its economy or losing investment and jobs abroad, other countries may be more encouraged to take action themselves.

Specifically in relation to the medium-term target to reduce Australia's net greenhouse gas emissions by between 5% and 15% below 2000 levels, we

note that this range is a substantial task. Relative to business-as-usual projections, this target will require a reduction in emissions of between 1/5th and 1/3rd of 2020 levels.

The proposed unilateral commitment to reduce Australia's greenhouse gas emissions to 5% below 2000 levels in 2020 will represent a very imposing challenge if international negotiations fail to build on the measures that have been agreed upon to date. Ai Group believes that consideration should be given to adopting a lower unilateral commitment than the level currently proposed.

Appropriate Mechanism for determining a Fair and Equitable Contribution

The Committee has been asked to assess an appropriate mechanism for determining what a fair and equitable contribution to the global emission reduction effort would be.

While Ai Group does not profess any particular expertise in this area, the formulation advanced by Professor Garnaut that national targets based on per capita emissions would be preferable to national targets that did not take into account differential rates of population growth has considerable appeal.

Signalling Powers of the CPRS

The Committee has been asked to assess whether the design of the proposed scheme will send appropriate investment signals for green collar jobs, research and development, and the manufacturing and service industries, taking into account permit allocation, leakage, compensation mechanisms and additionality issues.

Broadly Ai Group regards the design of the CPRS as able to deliver the appropriate signals to markets in relation to jobs, investment and research and development.

We note however the general failure of markets to adequately reward investment in research and development and to overcome information barriers in the development of the labour market. In these areas we regard there to be scope for additional measures sponsored by governments to ensure the economy is best positioned to meet the challenges and take advantage of the opportunities presented by climate change.

Ai Group has also advocated, as part of measures to assist the transition of the economy, incentives for investment in energy efficiency and emissions reduction. As indicated above, Ai Group also recommends establishing programs to better inform business and households about opportunities for low-cost greenhouse gas abatement and energy efficiency.

Ai Group is concerned that the measures currently proposed to address carbon leakage from trade exposed industries leave many businesses at risk of a material loss of competitiveness. This includes businesses in the iron and steel sector; in non-ferrous metals; in plastics and chemicals – including petrochemicals; in segments of industries processing agricultural goods and in the paper and paper products sector for example.

Once again, Ai Group appreciates this opportunity to comment on this important area of policy. Please do not hesitate to contact me if you would like any further information or elaboration of our views.

Yours sincerely,

Heather Ridout
Chief Executive