



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

Reference: Carbon Pollution Reduction Scheme Bill 2009 and other related bills

FRIDAY, 22 MAY 2009

CANBERRA

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**SENATE STANDING COMMITTEE ON
ECONOMICS**

Friday, 22 May 2009

Members: Senator Hurley (*Chair*), Senator Eggleston (*Deputy Chair*) and Senators Cameron, Joyce, Pratt, and Xenophon

Participating members: Senators Abetz, Adams, Back, Barnett, Bernardi, Bilyk, Birmingham, Bishop, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, Bushby, Cash, Colbeck, Collins, Coonan, Cormann, Crossin, Farrell, Feeney, Ferguson, Fielding, Fierravanti-Wells, Fifield, Fisher, Forshaw, Furner, Hanson-Young, Hefernan, Humphries, Hurley, Hutchins, Johnston, Kroger, Ludlam, Lundy, Ian Macdonald, Marshall, Mason, McEwen, McGauran, McLucas, Milne, Minchin, Moore, Nash, O'Brien, Parry, Payne, Polley, Ronaldson, Ryan, Scullion, Siewert, Sterle, Troeth, Trood, Williams and Wortley

Senators in attendance: Senators Bushby, Cameron, Eggleston, Hurley, Joyce, Pratt and Xenophon

Terms of reference for the inquiry:

To inquire into and report on:

Carbon Pollution Reduction Scheme (Charges—Customs) Bill 2009; Carbon Pollution Reduction Scheme (Charges—Excise) Bill 2009; Carbon Pollution Reduction Scheme (Charges—General) Bill 2009; Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009; Carbon Pollution Reduction Scheme (CPRS Fuel Credits) (Consequential Amendments) Bill 2009; Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009; Carbon Pollution Reduction Scheme (CPRS Fuel Credits) Bill 2009; Carbon Pollution Reduction Scheme Bill 2009

WITNESSES

BRADSHAW, Mr Michael, Senior Adviser, Department of the Treasury	42
COMLEY, Mr Blair Robert, Deputy Secretary, Department of Climate Change	2
DAVIS, Mr Graeme, Manager, Finance Strategy Unit, Business Tax Division, Department of the Treasury	42
GARNAUT, Professor Ross Gregory, Private Capacity	13
HARRIS, Mr Matt, Consultant, Frontier Economics	35
McCREA, Mr Glen James, Manager, Indirect Tax Unit, Department of the Treasury	42
MORAN, Dr Alan, Director, Deregulation Unit, Institute of Public Affairs	26
PARKER, Ms Cherie Rebecca, Analyst, Investor Protection Unit, Corporations and Financial Services Division, Markets Group, Department of the Treasury	42
PRICE, Mr Daniel, Managing Director, Frontier Economics	35
QUINN, Ms Meghan, Manager, Climate Change Modelling Unit, Department of the Treasury	2
SAKELLARIS, Mr Tas, Assistant Secretary, Legislation and Governance Branch, Department of Climate Change	2
STERLAND, Mr Barry Keith, First Assistant Secretary, Emissions Trading Division, Department of Climate Change	2
TARRANT, Ms Maria, Director, Policy, Business Council of Australia	19

Committee met at 9.46 am

CHAIR (Senator Hurley)—I declare open this hearing of the Senate Economics Legislation Committee inquiry into the Carbon Pollution Reduction Scheme Bill 2009 and related bills. On 14 May 2009, the Senate referred the provisions of 10 bills and any other bill that forms part of the government's Carbon Pollution Reduction Scheme to the committee for inquiry and report by 15 June 2009. In April this year, the Senate Standing Committee on Economics reported on the provisions of the exposure draft of the legislation to implement the Carbon Pollution Reduction Scheme. This inquiry will focus on the major changes to the exposure draft legislation, especially the amendments announced by the government on 4 May.

These are public proceedings, although the committee may agree to a request to have evidence heard in camera or may determine that certain evidence should be heard in camera. I remind all witnesses that in giving evidence to the committee they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to a committee, and such action may be treated by the Senate as a contempt. It is also a contempt to give false or misleading evidence to a committee.

I remind members of the committee that the Senate has resolved that departmental officers shall not be asked to give opinions on matters of policy and shall be given reasonable opportunity to refer questions to superior officers or to a minister. This resolution prohibits only questions asking for opinions on matters of policy and does not preclude questions asking for explanations of policies or factual questions about when and how policies were adopted.

If a witness objects to answering a question, the witness should state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer having regard to the ground which is claimed. If the committee determines to insist on an answer, a witness may request that the answer be given in camera. Such a request may of course also be made at any other time.

[9.48 am]

COMLEY, Mr Blair Robert, Deputy Secretary, Department of Climate Change

SAKELLARIS, Mr Tas, Assistant Secretary, Legislation and Governance Branch, Department of Climate Change

STERLAND, Mr Barry Keith, First Assistant Secretary, Emissions Trading Division, Department of Climate Change

QUINN, Ms Meghan, Manager, Climate Change Modelling Unit, Department of the Treasury

CHAIR—I welcome the witnesses. Do you wish to make an opening statement?

Mr Comley—To assist the committee, we had a discussion on Wednesday with a different committee about the 4 May major architecture changes, but I thought it might be helpful to briefly outline some of the other changes that were made between the exposure draft and the bill that is now before the parliament. I will ask Mr Sterland to run through those major changes very briefly.

Mr Sterland—I will begin by identifying which government agencies are responsible for the bills falling within this inquiry's terms of reference. The first six bills in the terms of reference are the core bills to establish the Carbon Pollution Reduction Scheme. The Department of Climate Change has lead responsibility for these bills. The next four bills seek to deliver the government's cent-for-cent fuel tax reductions and to establish the CPRS fuel credits scheme. The Treasury has lead responsibility for these bills, and I understand representatives from the Treasury are appearing this afternoon, so we can refer any questions on those bills to them.

The reference from the Senate also includes any other bills that form a part of the government's Carbon Pollution Reduction Scheme. There is one bill that falls into that category apart from those listed, the forthcoming bill to provide household assistance using revenue from the sale of emissions units. The Treasury has the lead responsibility for this bill, and the government intends to introduce that bill in the near future.

The six core bills for which the Department of Climate Change is responsible were published in draft form for public comment over a period from 10 March to 14 April. The public comment included around 160 non-campaign submissions on the draft legislation and over 11,000 campaign submissions. It also included feedback from workshops with industry, technical and legal experts and this Senate committee. The constructive engagement by stakeholders in this process has helped to make significant improvements to the exposure draft bills. Having taken into account the public comment, the Senate Economics Committee's report on the exposure draft bills and the impact of the global recession, the government has made a number of changes to the bills. The most significant changes flow from the announcement by the Prime Minister on 4 May 2009. Important changes for the waste sector were also announced by the Parliamentary Secretary for Climate Change on 14 May 2009.

The most significant changes from the exposure draft versions of the bill are as follows. First, the CPRS will have a phased start; industry will only be obliged to purchase and surrender emissions units in 2011-12 and there will be a \$10 fixed price for those units in that year. This is reflected in the definition of the eligible financial year and in the fixed price provisions in the bill. Second, the government has indicated it is prepared to adopt a national target to reduce greenhouse gas emissions by 25 per cent by 2020 compared to 2000 levels if an ambitious global agreement is achieved, and this is reflected in the objects clause of the bill. Third, amendments have been made to clauses 14 and 15 relating to scheme caps and gateways. There is a new requirement for a written statement to be tabled in parliament outlining the minister's reasons for regulations underlying scheme caps and gateways. The government has made a commitment to include an explanation in this statement of how voluntary action to reduce emissions has been taken into account.

It is worth noting that in its report on the exposure draft bills this committee noted community concern about the role of voluntary action under the CPRS and recommended that clause 14 be amended to provide that the minister must rather than may take into account voluntary action in setting scheme caps. Having given careful consideration to this recommendation and having taken legal advice, the government decided to address this issue in the way I have described through a statement in parliament and in a commitment to address voluntary action in that statement. The approach that has been adopted addresses the committee's concerns by ensuring that voluntary action will be taken into account in a transparent way.

A fourth significant amendment relates to landfill facilities. Stakeholders making submissions on the exposure draft argued that they should not be responsible for legacy waste emissions, that is, emissions attributable to waste deposited before the commencement of the scheme. The government has accepted this argument and this is reflected in the bill.

Finally, significantly more detail has been inserted in the bill regarding assistance to emissions-intensive trade-exposed industries, particularly in the context of the matters to be addressed in the five-yearly independent reviews. For example, the expert advisory committee must review whether the EITE assistance program supports the competitiveness of EITE activities in Australia. The more generous assistance for EITE industries for the first five years of the CPRS under the global recession buffer announced by the Prime Minister on 4 May has not required amendments to the bill and will be outlined by regulation. This is clearly outlined in the explanatory memorandum.

There are a number of other technical changes that have been made in response to stakeholder comments, and we have a document that outlines all of those changes. We are happy to provide that to the committee.

CHAIR—Thank you, that would be useful.

Senator EGGLESTON—I might just begin by making a short statement on behalf of the coalition senators. As Deputy Chair of the Senate Economics Committee and on behalf of the coalition senators, I wish to express my objection to the impossible timetable imposed by the government on this inquiry. More grievously, I wish to formally record a protest about the selection of witnesses called to appear at these hearings. As you know, these amended CPRS bills were referred to the legislation committee on 14 May 2009 and we are due to report to the Senate on 15 June. One month at this point in the parliamentary calendar, with two weeks of estimates looming, is an almost impossible deadline. We believe we cannot hope to conduct a rigorous assessment of these changed bills in that short time and regret that the government has not acceded to our requests for an extension of time. Delaying the inquiry report date it seems does not fit in with the government's climate change legislation agenda.

On the choice of witnesses to give evidence, we protest that the opposition was not consulted prior to witness selection and the coalition's effort to have our input into the witness list was not accepted. We urged the inclusion of representatives from industry and this was declined, with the exception of two additional witnesses. We view this as a very regrettable action on the part of the government. With our impossibly tight timeframe, is it necessary for both Professor Garnaut and his economist colleague Dr Ron Ben-David to be allocated a separate hearing time? Is it necessary that we hear from both ACOSS and the Brotherhood of St Laurence and shut out key affected industry and agricultural organisations from our inquiry? The coalition senators' objection is to the balance of the opinions and arguments which will be presented to this inquiry. It is very obvious that the government is getting the business of an inquiry over and done with and does not care whether the process is one which is consultative and deliberative. I say this because as we embark on this process this morning there are no submissions. In fact, we are in hearings before the date for the receipt of submissions has even closed.

The outcome of this inquiry, endorsement of the government's legislative changes, is already decided. The government has hijacked the inquiry processes to its own ends and we believe is engaging in an abuse of process. We feel that the Rudd government is in fact in total contempt for the Senate and also for the interests of the people of Australia.

In closing, I recognise the valiant efforts of the Economics Committee secretariat in seeking to meet the government's impossible timetable.

CHAIR—Thank you. Do you have any questions?

Senator EGGLESTON—Yes. First of all for the department, there are things we probably do not disagree with, like the waste disposal cut-off, but there are areas where we do have concerns. I wonder whether the delayed starting date makes such a significant difference. You will have the legislation in place and the issue, it seems to me, is not the starting date so much as the nature of the legislation and the nature of the scheme, which is an emissions trading scheme. I wonder whether it would not have been more appropriate not to introduce the legislation at this stage and for Australia to go to the Copenhagen conference with an open mind and see whether or not other countries are going to engage in emissions trading schemes and then amend our legislation or change the format of it in accordance with what we find. This legislation is very much predicated on there being an international emissions trading scheme, and as far as we understand there is very little evidence that countries like China, Japan and the United States, our major trading partners, are actually going

to set up an ETS. So wouldn't it be better to delay the legislation altogether rather than just delay the introduction of it?

Mr Comley—Senator, maybe I can pick up a couple of comments in your opening question. The question I think you are coming to is to what extent is the emissions trading scheme, the Carbon Pollution Reduction Scheme, predicated on a particular form of mitigation response in other countries.

Senator EGGLESTON—Yes.

Mr Comley—The view of the department would be that it is not predicated on a particular view of a way mitigation is carried out at least uniformly in the rest of the world. It is predicated really on the view that, to the extent that Australia will take on emissions reductions commitments, it is desirable to use a mechanism that is the lowest possible cost way of achieving those emissions reductions. That is the primary motivation. The intention of the government of moving legislation into parliament now is to try and provide certainty about the nature of that scheme as early as possible to business. Having said that, the government stated that the actual setting of the targets which build upon the architecture of the scheme will not occur until 2010, so after the Copenhagen conference. This approach is to bring in the architecture of the scheme so that businesses can plan for the type of compliance obligations, the type of business plan they will need to do, but the actual targets will not be set until after the Copenhagen conference.

Senator EGGLESTON—I am not so much talking about targets but taxes. Your scheme requires the carbon taxes to be offset by emissions trading with other countries. We do not believe that there will be an international emissions trading scheme but what will happen in fact is that taxes will be imposed on Australian industry which will impose huge extra costs, cost jobs and maybe lead to industries leaving this country because they will not be able to trade off those taxes with anybody else in the world in reality. While we do not disagree that some sort of carbon mitigation scheme would be a good idea, and is necessary perhaps, we do think that it is rather a flight of fancy to imagine that countries like China and Japan, our major trading partners, are going to have an ETS. You must have the same information as we do and surely you must have some reservations about this particular format. Why not have something simple like a carbon tax?

Mr Comley—Our view would be that there is nothing simpler about a carbon tax than what we actually have in terms of an emissions trading scheme. If you look at the details of the bills before us, the vast majority of the bills would have to cover issues which you would have to cover in a carbon tax. So fundamentally the issue of who would be a liable party, the way in which emissions would be monitored, reported and verified, the extent to which you would provide any exemptions or removal of liability, all those questions would arise under a carbon tax as would apply under an emissions trading scheme. The only additional complexity that may exist under an emissions trading scheme is the trading of the permits themselves which goes on.

Senator EGGLESTON—Exactly. And that is our issue.

Mr Comley—In terms of complexity, though, that is not particularly complex compared with the things that are required for a carbon tax and also has a range of benefits which would have to be considered against that, in particular the capacity of people to manage their risk in a forward-looking way as you have secondary financial markets for those carbon permits. The other issue with the carbon trading approach—and I acknowledge your point that not every country in the world will move to an emissions trading scheme immediately—is that there are significant international carbon markets at the moment which allow access to international abatement, which is difficult to access under a carbon tax regime.

Senator EGGLESTON—Nevertheless, a carbon tax would be simpler within Australia. It does not depend on the need to trade with other countries in carbon, and we do not see that an international emissions trading market is really going to be set up in the near future. This really is a matter which should cause the government and the department to reconsider its position.

Mr Comley—There is an international carbon market at the moment—

Senator EGGLESTON—On a small basis. The EU and New Zealand, but not the United States, not China, not Japan, not Korea, not Thailand, not Indonesia or India, who are our trading partners.

Mr Comley—There are actually two issues here. One is the size of the permit market in terms of accessing international abatement. Compared with the likely needs of Australia to import permits, that market is actually quite large. In fact, we would not anticipate that Australia's demand for international permits would substantially change the price of international permits.

I think the second part of your question or observation is really about: to what extent are other countries undertaking mitigation commitments? The question there is not really whether they have an emissions trading scheme; the question is whether they have taken on mitigation commitments and what the effective impact on their industries is. The government has recognised that, and that is why there is the emissions-intensive trade-exposed assistance program, which seeks to address the fact that not all countries will simultaneously be moving to impose the same mitigation commitments or carbon constraints in all countries.

Senator EGGLESTON—Dealing with the emissions intensive industries, the cost of assisting these industries is going to be very high. Surely there must be other ways of doing it. We do not accept that this is a real solution to the problems of those industries. We have been told and expect that industries like cement, oil refining, malt production and perhaps a whole lot of others will move offshore because what you are proposing is not adequate.

Mr Comley—The first point to make on specific industries is that, as you are aware, the process to determine emissions-intensive trade-exposed industries is continuing. There is a process where activities are being defined in consultation with industry, and that will lead to the establishment of eligibility and allocated baselines going forward. That process will continue to identify the particular industries. It is perhaps worth putting in context the nature of the emission-intensive trade-exposed assistance for those who are the most emissions intensive and therefore the most exposed to potential competitiveness effects. Following the 4 May announcement by the Prime Minister, the initial rate of assistance was around 94½ per cent of liability. It is important to put that in context. Even in the fixed price period of \$10 a tonne, that is equivalent to having a carbon price of around 50c a tonne imposed upon those activities. To put that in context, the New South Wales GGAS, which applied to some parts of industry, had a price of above \$10 a tonne at various points.

The other point to make is that the basis of that assistance is provided on 2007-2008 intensity baselines. To the extent that industries have been able to improve their emissions intensity efficiency over the period to the commencement of the scheme, that does not reduce the amount of assistance provided but does reduce their liability under the scheme. So the level of actual liability for the most emissions intensive firms is significantly reduced by the emissions-intensive trade-exposed assistance and moves it to a level that is relatively small compared with the overall costs.

Senator CAMERON—I am not sure who wants to answer this question. There were some reports in the *Australian* this morning headed ‘Carbon plan will cause jobs carnage’ and ‘Climate change warning: emissions trading scheme to “cost 24,000 jobs”’. This was on the basis of a report commissioned by the Minerals Council, acting on behalf of multinational mining companies. Can you give us your view on this analysis and why it differs so much from the Treasury’s analysis?

Mr Comley—Perhaps I will make an opening comment and then I will ask Ms Quinn to comment. The difficulty for me at the moment is that I have seen the press reports but I have not actually seen the report. For example, that report covers quite similar territory to the report released by the Coal Association—again, a commissioned report. The numbers in that around eight times as high for the direct job impacts. We have been following up on the Coal Association report and are still seeking further detail as to how it was actually conducted. It is very difficult for us to be in a position to comment without having the full details of the model it has actually done. Ms Quinn, would you like to add anything else to that?

Ms Quinn—As you say, the report is in the newspapers this morning and was released this morning, so I have not had a chance to look at it in great detail. There is not a significant amount of detail in the published report, which I have been able to have a quick look at this morning. But I would like to underline that the impacts across industries, as reported in the Concept Economics report, look roughly similar to the Treasury analysis in *Australia’s low pollution future*, except for some of the coal industry, where the numbers are significantly larger than found in the Treasury analysis and significantly larger than found in other analyses using the MMRF model. It is difficult to understand why other industry results would be broadly similar and yet the coal industry results would be significantly different.

There are a few other comments in the report that I just wanted to flag. They suggest that the Treasury modelling undertaken for the government’s report is inaccurate for various reasons. I just wanted to highlight that some of these stated reasons are inconsistent with the published information. For instance, they suggest that ‘the absence of assumptions concerning the scale and timing of binding emissions reductions by other leading economies’ in the public domain makes the Treasury modelling suspect, yet we have documented comprehensively the assumptions that we used. In fact, those assumptions have been used by the Concept

Economics report itself. It seems they have picked up some criticisms from previous light analysis and have reproduced those numbers in those criticisms.

The other criticism, for instance, is that reference case assumptions for metal prices and energy prices cannot be verified, which is a reference to an earlier report for the Minerals Council, which took Treasury index numbers, placed it on Concept Economics' own real-world data and came up a spurious result. That is completely inconsistent with what Treasury has used in its analysis. That was addressed also in the technical annex in our report, setting out the assumptions that were used in the Treasury modelling report.

Senator JOYCE—So theirs is spurious and yours is quite correct?

CHAIR—Senator Joyce, we are short on time.

Senator JOYCE—Well, that is not our fault.

CHAIR—I think Senator Xenophon is now on the line as well.

Ms Quinn—Can I just address that point quickly?

CHAIR—Yes, but I just want to establish if Senator Xenophon is on the line.

Senator XENOPHON—Yes, I have been on the line all along.

Ms Quinn—It is not that the modelling is spurious. Modelling can produce different results depending on different assumptions, and you need to look at the substance of it. All I am saying is that the commentary on the Treasury assumptions in the report is false.

Senator CAMERON—Can someone take us through the conditions for the more ambitious 25 per cent target? Could you also comment on the rationale for the conditions?

Mr Comley—As I am flicking towards the conditions, the overall rationale for the conditions is that Australia would only go to 25 per cent if there was a genuine agreement that would meet a 450 parts per million CO₂ equivalent concentration outcome in the atmosphere. What the conditions attempt to do is to put some flesh on that—to say what concretely you think you would need to have a world outcome that was consistent with a 450 parts per million agreement. So that is the top down approach. I think in the committee discussion we had on Wednesday, which I think you participated in by phone, there was a question about these various tight conditions—and at one level they are, but they are because reaching a 450 parts per million agreement is actually quite a difficult thing to do. So the condition for the 25 per cent level is that there has to be:

Comprehensive global action capable of stabilising CO₂-e concentrations at 450ppm CO₂-e or lower. This requires a clear pathway to achieving an early global peak in total emissions, with **major developing economies** slowing the growth and then reducing their emissions, **advanced economies** taking on reductions and commitments comparable to Australia ...

The first part of that is really fitting within the general framework of the international agreement, which has tended to take a common-but-differentiated responsibilities approach—that is, different countries, reflecting their historical situation and their capabilities, would have to take on different emission reduction commitments. It is generally acknowledged that advanced economies will have to lead that process with greater emission reductions; major developing economies would have to make a contribution by slowing their growth. Advanced economies in this context are the annex I countries in the Kyoto protocol UNFCCC, but it also includes some high middle-income economies which will be the subject of negotiation.

There would also have to be a 'full range of international abatement opportunities through a broad and functioning international market in carbon credits'. The idea essentially is that, for us to reach a 450 parts per million agreement, there is going to have to be very concerted global action, but also Australia is going to need to access some international abatement; otherwise, the domestic costs of seeking purely domestic abatement may be too high. This would involve:

... comprehensive coverage of gases, sources and sectors, with inclusion of forests ... and the land sector (including soil carbon initiatives ... if scientifically demonstrated) ...

The point about the inclusion of forests, particularly reducing and avoiding deforestation, is that they contribute around 20 per cent of global emissions at the moment. So, to really do something consistent with the 450 parts per million agreement, it would be necessary to have coverage of those sectors and some reduction activities.

There would have to be a:

... clear global trajectory, where the sum of *all economies*' commitments is consistent with 450ppm ... or lower, and with a nominated early deadline year for peak global emissions not later than 2020 ...

All the scientific evidence indicates that you have to peak your emissions relatively soon if you are credibly to be on a path for a 450 parts per million outcome.

The next point is:

... *major developing economy* commitments to slow growth and to then reduce their absolute level of emissions over time, with a collective reduction of at least 20% below business-as-usual by 2020 and a nomination of a peaking year for individual—

countries. Again, this is recognising that the major developing countries, from their starting point, will need to continue to grow their emissions for some time but will need to slow the rate of that growth of emissions to be on a credible path to 450 parts per million.

Then there is:

... global action which mobilises greater financial resources, including from *major developing economies*, and results in fully functional global carbon markets—

over time. That is really to give access to the lowest cost abatement across the world, because if that does not exist there are going to be significantly higher costs to meet that outcome. I will pause there. Mr Sterland, is anything that you want to add?

Mr Sterland—No.

Mr Comley—No. That is fine.

Senator CAMERON—Given the time, I would like you to take some questions on notice. The proposition has been put here this morning that other countries are not going to engage either one way or another in reducing their carbon emission footprint. I have some information that a significant amount of work has been done in China, India, South Korea and the US. Is there any way that you could give us an analysis of what is happening so that we can deal with this argument that we are unilaterally taking on this issue?

Mr Comley—Yes, we can certainly provide some of that on notice, but certainly in China there have been quite a lot of efforts, including improving energy efficiency and other measures, to try and reduce their carbon footprint, including substantial renewables. Mr Sterland, do you want to comment?

Mr Sterland—I think we addressed this at a previous hearing, but we could give you a document that lists that.

Senator CAMERON—Could you also take on notice the potential for employment increases in Australia by getting to the front end of this global change?

Mr Sterland—We will take that on notice too.

CHAIR—Thank you. I have Senator Bushby next, and then I will go to you, Senator Xenophon, for questions after that.

Senator XENOPHON—Thanks, Chair.

Senator BUSHBY—Thank you to the officers of the two departments who have come along. We heard earlier in answer to a question that the impact of the global recession was one of the factors that were taken into account when developing the changes between the exposure draft and the legislation we are looking at today. Which changes in particular were incidental to consideration of the impact of the global recession?

Mr Comley—I think the primary changes were the deferral of the start date, the use of a fixed price for the first year of the scheme and the augmentation of the emissions-intensive trade-exposed assistance.

Senator BUSHBY—So it would be fair to say that the impact of the global recession was the primary reason for those changes?

Mr Comley—I think that was the primary reason. Also, in terms of deferral, some businesses had raised a question of preparedness in advance of the scheme, but that was also partly in the context of the global financial crisis, because a number of firms were essentially saying that it was difficult for them to allocate additional time to those issues in the context of the current economic circumstances.

Senator BUSHBY—To what extent do these measures, particularly the changes that have introduced delay, delay the likely date at which global emissions can be reduced or limited to a sufficient extent to avoid climate change consequences?

Mr Comley—We would expect that they would have very modest, if any, consequences for the capacity to reduce emissions. The significant caveat to that is: provided that there is certainty in the business community that the scheme would actually commence—in other words, the most certainty is provided by legislative passage.

Senator BUSHBY—So are you answering my question in the context of Australian emissions or in terms of actually addressing the global issues?

Mr Comley—There are two parts to it. The first part is: in terms of domestic emissions, sending that signal drives the investment climate. The second part is: with respect to the international negotiations, Australia going to Copenhagen with a scheme capable of delivering large emissions reductions will have an impact on the international negotiations which, through that process, leads to an outcome in terms of potential global emissions.

Senator BUSHBY—The reason why I am asking—and it is not the main focus of my questions—is that I am a little confused, and I am sure many Australians are a little confused, because of the urgency that was required in getting all this up and running so that we could address the problem, which is imminent, when last night, on *Q&A*, the minister was on, as was Bob Ellis. He was saying that it is all too late—these delays. It needs to be done now; we cannot delay these things. And there are a lot of other commentators out there of a similar view. And the minister herself had, in the past—particularly in response to questions in the Senate—also made similar statements: that these things needed to be done urgently and they would not be delaying, for the reason that the world could not wait. Yet, here we are, delaying. I am just trying to understand what the consequences of this delay will be, and whether, if we are on a time line, it is going to cause problems in terms of actually meeting that time line.

Mr Comley—I understand the question. I am trying to draw a distinction between delay in the commencement of the scheme and delay in the decision and the certainty that the scheme will exist, and also the implications that has for the international negotiations, including the fact that the government has put on the table a 25 per cent reduction potential for negotiation which was not part of the package before 4 May.

Senator JOYCE—Do you think Australia will make it through the next year unscathed?

Mr Comley—Senator, can you clarify your question?

Senator JOYCE—With this delay, do you think we will survive?

Mr Comley—I think I need a little more precision in the question.

Senator JOYCE—Well, a little bit more precision is what we have been looking for all the way through.

Senator BUSHBY—Has the impact of the CPRS—as it now stands, the proposed model—on the economy been modelled, Ms Quinn?

Ms Quinn—The economic modelling that was reported in October has not been updated for the 4 May announcements.

Senator BUSHBY—My question is on the impact on government revenues from company and other taxes. As to industries that will be directly affected by the CPRS and be forced to make changes—which is part of the intention of it—has the impact on government revenues of the taxes that they pay, and their contributions to government revenues in general, been included in any modelling?

Ms Quinn—So the—

Senator BUSHBY—The impact of changes to the CPRS. Obviously, you have not got up to date with the 4 May changes. But, as to the impact on the industries that will be subject to changes as a result of the CPRS, has the impact on government revenues been taken into account as part of your modelling?

Ms Quinn—The question that I answered was about the economic modelling in terms of the CGE modelling of the impact of the changes of 4 May on the Australian economy—had that been updated? The answer was no, and that is partly because the one-year delay is unlikely to significantly change the results over the average to 2020. Has the impact of the CPRS on the budget analysis been updated in the budget estimates? The answer is yes.

Senator XENOPHON—I will put some questions on notice given the time. Firstly, Mr Hooke, on *AM* this morning and in his opinion piece in the *Australian* today, criticises Treasury modelling, saying that it does not capture all the transitional elements—namely, in terms of the job losses in the short and medium term. Could the government officials provide a response to the Concept Economics report, once they have had a chance to

look at it, particularly addressing the transitional elements, and also to the criticism Mr Hooke made in the media this morning that the problem with the Australian scheme is that it has auctioning of permits at a much greater level than what is proposed in the US legislation and that that is a problem in terms of its transitional economic impact?

Mr Comley—We will take the first one on notice. As you are aware, Senator, we have not had a chance to analyse the report.

Senator XENOPHON—No, I understand that.

Mr Comley—On the second one: things are moving very quickly in the US but the last information I have on where the Waxman-Markey bill is at—and I recognise that it is a long way from where the thing will end up—is that there will be an allocation to emissions-intensive trade-exposed industries of around 15 per cent of the permits and to petroleum refining of around two per cent. It is possible that that information is out of date, but it was provided to me within the last 24 hours.

Senator XENOPHON—That is what Mr Hooke has said I think in his opinion piece.

Mr Comley—I am not quoting the opinion piece; I am looking at the piece of paper that was released by Chairman Waxman and Chairman Markey. We can take on notice what the actual situation is there, but my understanding is that the allocation to emissions-intensive trade-exposed industries in the current version of the Waxman-Markey bill is 15 per cent plus two per cent to petroleum refining.

Ms Quinn—On the first question, we are happy to provide more details on notice. I want to address the transition costs. I have answered this question before but I will repeat for clarity. We had three economic models and two of them account for transition costs. The results reported for Australia from the MMRF model do account for transition costs in terms of changes in employment in the near term and short term. It is not true to say that we ignore those transition costs in the analysis in the report.

Senator PRATT—I have some questions that I want to place on notice on the Minerals Council report. I want to raise at this point specifically the use of the scenario in the minus five reductions. I want to ask you about the assumptions that that makes in relation to global action on climate change that that report might misconstrue in some way.

Ms Quinn—The CPRS minus five scenario in the modelling undertaken by Treasury assumes action in 2010 for annex 1 countries and the United States. It assumes that there is a delay of five years before high-income developing countries—and China is part of that group—take action in 2015; India and middle-income countries will take action in 2020 and lower income countries will take action in 2025. To be clear, this means that they start reducing their emissions relative to a reference case at those dates; it does not mean that they reduce in absolute terms their emissions. For instance, China's actual emissions do not start to fall in absolute terms until into the 2030s and India's until into the 2040s. It captures the concept that the developing countries slow their emissions growth from the starting dates.

That is what is in our modelling. It means that there are times in which Australian exports are exposed potentially to issues of carbon leakage. That is the reason why in our report we found that the emissions-intensive trade-exposed industries assistance as outlined at that time in the green paper did provide transitional support for the industries covered by that assistance. But by the time everybody is in in 2025 then there will be no need for assistance. It is not in the Concept Economics report for the Minerals Council. There is no information about how they have applied the CPRS minus five scenarios. It is not clear whether they have taken the international assumptions as well as the carbon prices and other elements of the CPRS.

One thing that is quite important in terms of the coal industry results in particular is it is action internationally that has a significant impact on the coal industry. Our modelling found that the major impact on the coal industry is the reduction in demand for coal in countries around the world as a response to having a price on emissions. For that reason if carbon capture and storage becomes a viable technology it will be very important for the Australian coal industry. That was outlined in a section in the report on the coal industry in particular.

Senator PRATT—Thank you. I want to move on from that and I will put those other questions in relation to the Minerals Council on notice. I want to ask about the impact of the recession and how that intersects with the prospect of carbon leakage. I will try to put it more specifically. Is the global recession a buffer for businesses, with transition to the scheme? Does it minimise carbon leakage? Does it exacerbate carbon leakage? What is the relationship between the recession and any prospect of carbon leakage? Is there one?

Mr Comley—I think Ms Quinn might want to comment but, broadly speaking, it comes back to this concept of a reference case. Essentially, if you have positive economic times or negative economic times, what you are looking at is the impact of the carbon price as a change compared with that level of activity. So, broadly speaking, it does not change the extent of carbon leakage you would expect. It may be that the economic prospects of a particular sector are weaker than they were previously, but the change associated with the carbon leakage would not be expected to be exacerbated by the position you are in within the cycle.

Ms Quinn—To add to that, the only reason why there would be a difference between countries or industries is if the global recession for some reason was affecting some countries or industries more or less than other countries or industries. My understanding—not being the Treasury expert on the global recession—is that this is a shock that has hit all industries in all countries and has affected industries in different countries roughly the same way, which would mean that it would not necessarily change the competitiveness between nations. Carbon leakage is related to the competitiveness between countries. So, to paraphrase, all the industries are in the same boat together and so they are all suffering a reduction in demand equally.

Senator PRATT—I wanted to lastly ask about the factors that will be taken into account in withdrawing assistance for emissions-intensive trade-exposed industries and how that is looking now as a result of the plans.

Mr Comley—There are three levels of the nature of the change in assistance. The first is the 1.3 per cent per year reduction in the rate of assistance which happens each year, and that is an automatic reduction in the rate of assistance. The second is the removal of the global recession buffer after a five-year period. The third is that, if there is a review conducted of the international environment, the review would essentially look at the extent of carbon constraints that have been imposed in the rest of the world.

An important part of that review is that it will need to look at both industries and sectors to look at carbon constraints in different areas, but it would also have to look at the total level of emissions reductions commitments across the globe. The broad intention is to look at the extent of carbon constraints in different countries, bearing in mind that they will not all be in the form of emissions trading schemes and they will not all be in the form of carbon taxes. So the review will have to do an analysis of the effective level of carbon price imposed in each country.

Returning to Senator Cameron's earlier observations, you might look at China, for example. If China has at some point in the future banned a coal fired power station, imposed a renewable energy target or done something else that drives a lower emissions outcome than otherwise would be the case, what you would be doing is trying to calculate the additional costs that that imposes upon Chinese business and compare that additional cost to the cost imposed by the Carbon Pollution Reduction Scheme in Australia. So that will be the process. It will probably be done through an independent review that will make a recommendation to the minister on the extent of those restrictions. Mr Sterland, do you want to add anything to that?

Mr Sterland—I would just add the point that some of the things mentioned there are happening now in China, so it is about how those evolve over time. They have some renewable measures that would already be imposing some degree of carbon constraint there, and obviously the conditions outlined in the government's statements would be looking for more over time in the context of a wider deal.

Senator PRATT—So what we can see from that is that the debates about industry assistance are clearly going to remain quite active in terms of industry putting its position and us having to be on top of the research internationally to demonstrate what is going on. Does that task start now?

Mr Comley—It has already effectively started. We have started a work program within the department to think about how we will do those calculations. It is a very complex task, as you can imagine. What you are effectively trying to do is look underneath a whole range of regulations in different countries and say what the effective impact on those industries is. It is quite a complex task and it will take some time to get those calculations right.

I would also note in this area that most people we talk to about these exercises think that the results of this exercise will confirm their own views, in quite different ways. Some groups look at it and say this will demonstrate there is no action elsewhere. Others will say this will actually demonstrate there is a lot of action going on elsewhere that should be fed into the process. I think that information is going to be very useful for the policy debate going forward.

Mr Sterland—I think, to underpin that, the need for an transparent review that really looks at these in an arms-length way and is convincing to all those sides of the debate is a critical part of the bill itself. It is outlined in some detail in the bill and the government's policy framework in general.

Senator JOYCE—For the purpose of brevity, I am going to ask some specific questions that move away from the hypothetical to the actual. What is the price of carbon permits currently in India?

Mr Sterland—Are you asking about, say, some of the Kyoto—

Senator JOYCE—I just want to know, if I want to buy a carbon permit in India, through the Indian domestic economy, how much does it cost me?

Mr Sterland—India would be participating in the Clean Development Mechanism under the Kyoto protocol. I would have to take on notice the exact price, but they are around the \$15 to \$20 mark, depending on the project.

Senator JOYCE—In India at the moment?

Mr Sterland—Internationally.

Senator JOYCE—And they are tradeable in India?

Mr Sterland—Yes. So, under the scheme proposal, those credits could be used by Australian companies to fulfil their compliance obligations.

Senator JOYCE—That is in place at the moment?

Mr Sterland—Yes, under the Kyoto protocol.

Senator JOYCE—So it is in place regardless of whether we go forward with this scheme or not.

Mr Comley—It is, in terms of producing project based credits. In terms of having economy-wide measures in India, they are not currently in place, but in terms of—

Senator JOYCE—In India, economy-wide measures are not in place, are they?

Mr Comley—There is not an economy-wide measure—

Senator JOYCE—Let us go to China. What about the price in China and the economy-wide measures in China? What are they like?

Mr Comley—I think we have already taken on notice to provide information—

Senator JOYCE—They are not there either.

Mr Sterland—Certainly I think it would be fair to say that there is a more extensive suite of policies in China, as our answer to the question on notice will reveal.

Senator JOYCE—What is the price of a domestic tradeable carbon unit in China at the moment?

Mr Comley—The answer to the previous question indicated that, in terms of determining at least the competitiveness impacts, that is not necessarily the relevant question. The question is—

Senator JOYCE—It is relevant because I asked it.

Mr Comley—The point of the answer to Senator Pratt's question is that the issue is not what is the price of a tradeable permit in a country; the question is what is the level of restriction that is imposed upon businesses, in the same way that if you had a mandatory—

Senator JOYCE—So they are comparable? If you have a restriction on businesses or tradeable permits, they are comparable, are they?

Mr Comley—In terms of the impact on carbon competitiveness there is an equivalence between the two. The question is—

Senator JOYCE—So there are definitely alternative schemes to the emissions trading scheme, aren't there?

Mr Comley—There certainly are alternatives. The question is which is the higher or lower cost of achieving a particular form of abatement—

Senator JOYCE—Which one has China decided is the best?

Mr Comley—At the moment, China is adopting a suite of measures across different sectors, but—

Senator JOYCE—Do they have an emissions trading scheme in China?

Mr Comley—They do not have a broad based emissions trading scheme.

Senator JOYCE—Does the United States have an emissions trading scheme?

Senator CAMERON—The export tax—

Senator JOYCE—Does the United States have an emissions trading scheme?

Mr Comley—Parts of the United States have emissions trading schemes.

Senator JOYCE—California.

Mr Comley—There are two regional emissions trading schemes currently operating in the United States. There is the Regional Greenhouse Gas Initiative and there is the Western Climate Initiative, which has a carbon trading scheme, in the United States.

Senator JOYCE—California.

Mr Comley—California is included in that.

CHAIR—We have a minute left before our break. If anyone wants—

Senator JOYCE—How is the Californian economy going at the moment, Mr Comley?

Mr Comley—I do not have the information in front of me.

Senator JOYCE—I can help you. It is broke.

Senator CAMERON—Not because of emissions trading.

Senator JOYCE—You talked about the Waxman-Markey bill. Has that even been out of committee in the United States yet?

Mr Comley—Senator, as I have said to previous committees in the past few weeks, it has not come out of committee yet.

Senator JOYCE—It has not come out of committee, has it? So is it going to get through Congress? Can you give me a guarantee using your modelling whether it is going to get through Congress?

Mr Comley—As I have answered previously on this, we are not in a position to make a guarantee or even a revised forecast about a particular piece of legislation in the US. For the purposes of modelling, there are assumptions made about the path of—

Senator JOYCE—You have made an assumption it will get through. You have said that when they go to Copenhagen, this will have gone through. I am amazed: you seem to know more about the American political system than the Americans do.

Mr Comley—Senator, we have not made an assumption about a particular piece of legislation going through the US Congress.

Senator JOYCE—Because it possibly won't.

CHAIR—Okay, the committee—

Senator JOYCE—Hang on! Your Labor Party speakers took from 8.26 to three minutes ago, and it is the Labor Party that has decided that it is not worth having an extension of the inquiry. Senator Cameron spoke for about 10 to 15 minutes, Madam Chair.

CHAIR—No. I am sorry, I have written—

Senator JOYCE—Madam Chair, are you fair dinkum about this?

CHAIR—I will show you in the break, I have written every time down and that is not the case.

Senator JOYCE—This is a joke!

CHAIR—The committee will have a short break in proceedings for a few minutes, and when we return we will have Professor Ross Garnaut.

[10.48 am]

GARNAUT, Professor Ross Gregory, Private Capacity

Evidence was taken via teleconference—

CHAIR—Welcome again, and thank you for attending. Do you have an opening statement you would like to make?

Prof. Garnaut—No. I spoke to the committee some weeks ago. I am appearing at the request of the committee and I am happy to answer questions.

Senator PRATT—Professor Garnaut, when you appeared before us last time, we had a discussion about targets. The position since then has changed. I want to talk to you about the importance of the Australian government making its conditional offer to encourage developing countries to also take action. Could you comment on that please?

Prof. Garnaut—Yes. I think it was an important step. I advised the committee some weeks ago when we last met that Australia put back on the table its preparedness to reduce emissions from 2000 levels by 25 per cent by 2020. The calculation reported in my review would be Australia's proportionate part in an ambitious global agreement to hold concentrations of emissions in the atmosphere at 250 parts per million. Of course we would have to keep going beyond that and as I mentioned in my report our proportionate part of that global agreement would require us to reduce emissions by 90 per cent by 2050. The focus of the Copenhagen meeting and of the international community at the moment is on 2020 targets. By showing that it was prepared to take this step if other countries took comparable steps or took steps that were consistent with an ambitious outcome Australia has put itself back in the game of working towards a strong outcome.

Senator PRATT—What is the importance of the conditionality of that offer? We are prepared if you are prepared. Is that the best way to get as many parties as possible to the table?

Prof. Garnaut—It is certainly a reasonable way. It is much more costly as well as much less beneficial to do things on your own. The most valuable steps we can take are steps which encourage an ambitious global agreement. It is only through a global agreement that we are going to get a strong outcome. I think the only practical way of getting a strong outcome is by countries saying what they are prepared to do if others support a strong outcome. You are seeing that sort of approach being adopted in some other countries, certainly in Europe. I think now there is a reasonable chance of building momentum towards that sort of approach.

Senator PRATT—That leads me to my next question. There has been some debate and indeed some doubt expressed on the committee whether the rest of the world is taking action on climate change. Can you flesh out your last statement for us in terms of what action our trading partners are taking and how that moving-together in the lead-up to Copenhagen and beyond is looking?

Prof. Garnaut—Anyone who says that other countries are not doing enough at the moment is quite right just as anyone looking at Australia who says that we are not doing enough is quite right. We are not doing anything much at all at the moment. Most developed countries are doing more than us at the moment but they are not doing enough to play their part in an ambitious global agreement to hold concentrations at 450 parts per million or lower. We all have to ratchet up our efforts and the global effort. Just comparing what Australia is doing now with what other countries and regions are doing now, obviously we are doing much less than Europe, which has been taking effective action for some time, nowhere near as strong as is eventually going to be needed but they have made a start. Quite a number of states in the United States and provinces in Canada are taking strong steps, not always in the form of an emissions trading scheme. In America, for example, so far the preferred approach has been a regulatory one. For example, California mandating steps to reduce energy use and emissions in vehicles, appliances and houses. They are quite radical steps which have had large effects, but they add up to significant reductions in emissions. There is something similar in some of the states and great cities of the north-east of the United States including New York, Massachusetts and Connecticut.

In the developing countries most Australians would be surprised to see how much is actually being done. In China there are various measures to make it more costly for the highly energy intensive and emissions intensive industries like aluminium, steel and cement to expand. They are costly measures which of course are very much unwelcomed by the industries concerned. In Japan mainly through regulatory and other measures has been taking a strong approach on reducing energy intensity for a long time. That is one of the reasons why

they used to be the world's biggest aluminium producers and now they are, I think, the world's biggest aluminium importer, drawing a lot of aluminium from, amongst other places, Australia.

South Africa has a carbon tax, and that is an important developing country that competes with Australia in many resource industries. In lower income developing countries there is a lot of discussion of the issues but not enough action yet. But I see in our near neighbours Papua New Guinea and Indonesia a preparedness to look at going a long way. What they need is the encouragement of an international regime in which, if they accept targets, they can sell permits if they do better than their targets.

Let's not pretend that this is an easy job. It is not. It is a diabolical problem, getting international agreement on a matter like this, where every individual country has an incentive to stand back and hope that others do the work. Our climate change problems would be fixed if every country did everything and we took a free ride on them. But we are not going to get international agreement like that. As I demonstrated in my report and as the Australian government accepted in its white paper, Australia will be the most damaged of developed countries through unmitigated climate change, so we have a very strong interest in getting a strong global agreement, and it is in Australia's national interest that there be a global agreement around 450 parts per million. In the discussion that is going on in lots of countries there is a basis for building a strong global agreement. We are not there yet, and the steps that Australia takes over the next little while have to be judged by how much they contribute to building a strong global agreement.

Senator EGGLESTON—You made some international comparisons there, and you referred to the European Union model. I believe that they only auction about four per cent of permits and that we will be auctioning about 70 per cent, so the European model does not seem to be a very substantial model.

Prof. Garnaut—I was not holding up the European model of the ETS as a model. I was saying that they are taking substantial action on reducing emissions, and they are doing that through a wide range of things: support for deployment of low-emissions technologies, huge incentives for deploying solar and wind technology in some European countries, big regulatory steps on reducing energy intensity of buildings and strong pressure for energy efficiency in cars—and their average car emits far less than the average Australian car. The emissions system in Europe gives them a basis for reducing emissions over time, but they have not got their act together yet. They began by giving out, as you say, most of their permits free. That led to large transfers of income from ordinary taxpayers and ordinary citizens of Europe towards the big energy companies—just transfers of wealth. That was one of the reasons the system became unpopular.

Senator EGGLESTON—You mean electricity prices went up?

Prof. Garnaut—That is why, when they issued their green paper on post-2012 arrangements, they favoured not giving any free permits to the domestic energy sector and phasing out free permits to the trade exposed industries. You have drawn attention to an important point—that is, as countries go towards general priced based mechanisms for reducing emissions, like an ETS or a carbon tax, there is strong pressure on all of them to give free permits to trade exposed industries, and each one uses the argument that others are not doing it. Barack Obama came to office with a promise to introduce a scheme that would auction all of its permits, but obviously there is a political process going on putting pressure on that.

In the end this is going to be a budgetary measure and a trade policy issue. If you give out the permits for free and you still have in mind giving compensation to low-income households and giving support to trade exposed industries as the world recovers from this crash budgetary burdens are going to be very heavy in circumstances, in which case countries will not be able to carry them. I think there is a very big shared interest with all countries in the world in quickly getting to a position where we have comparable carbon pricing in all countries so that no-one is under pressure to give out free permits because others are and one in which we can use movement towards carbon pricing as a plus and not a minus in the immense task of bringing all of our budgets back into reasonable balance within a reasonable time.

Senator EGGLESTON—Thank you. I would like to come back to a point you made earlier. You said that the European scheme was not an emissions trading scheme and what we are talking about in Australia is an emissions trading scheme. Carbon reduction is another matter but what we are actually dealing with is an emissions trading scheme here with the CPRS. As I understand it, you are correct, the European system is not an ETS. China is certainly looking at renewable energy programs and nuclear power and I understand Japan is too. Is it prudent for us to be jumping into an ETS before the Copenhagen conference or should we really be waiting and seeing what happens at Copenhagen and what other countries are willing to do before we jump into an ETS when we could use other methods of carbon reduction?

Prof. Garnaut—Europe has an ETS. What I was saying was that the main reduction in energy use and emissions in Europe that have actually taken place so far—

Senator EGGLESTON—I accept that but it is a minor issue.

Prof. Garnaut—Looking forward it is very clear the way the Europeans are going. They are putting a lot of effort into cleaning up their ETS. They know they made some big mistakes in its introduction and they are seeking to avoid them and introduce a much more effective system in the post-2012 arrangements. There is no doubt where Europe is headed.

Senator EGGLESTON—Shouldn't we just wait and see what happens? There are other options. We could end up with a very expensive ETS, which is going to cost jobs, imperil industry and see industries going offshore, and we may find that we are like a lonely little petunia in a garden patch with nobody else doing it.

Prof. Garnaut—I do not think there is much doubt now about where the world is headed especially now that Barack Obama is strongly committed to an ETS.

Senator EGGLESTON—Barack Obama may be but the US congress as such is not. A politician president may have an objective but congresses and parliaments do not always agree.

Prof. Garnaut—The congress is now headed towards a cap and trade system and ETS.

Senator EGGLESTON—Some people do not think that.

Prof. Garnaut—There is some debate in the US about the best way of going forward. My assessment is that that is in the process of being resolved in favour of an ETS. Japan and Korea will be heading that way. The main developed countries will be heading that way.

Senator EGGLESTON—With respect, Professor, other people disagree with you.

Prof. Garnaut—In which countries?

Senator EGGLESTON—In Japan and in China. The Institute of Public Affairs does not agree with the position you have just put.

Senator CAMERON—Very good!

Prof. Garnaut—I did not mention China in that list.

Senator EGGLESTON—You mentioned Korea.

Prof. Garnaut—There is discussion of an ETS in China and there is also discussion of a carbon tax and other measures, and I would be less certain of which way China will end up going. I am confident that China will accept constraints on emissions in the context of a global agreement but how that works itself out I wouldn't say for sure at this stage. It is clear to say which way the main developed countries are headed.

Senator EGGLESTON—I wonder if that is the case. Everybody might agree on carbon reduction but not necessarily on an ETS. One of the amendments to this legislation is in regard to free permits to emissions-intensive trade-exposed industries having been increased to at least five years under what the government refers to as 'the global recession buffer'.

Those firms were previously eligible to receive 90 per cent free permits. They will now receive 95 per cent. Those that were going to get 60 will now get 66 per cent. I wonder whether that is really sufficient to counter the impact of the proposed ETS on the balances of those sorts of industries or, again, is this a reason for us not to pass this legislation at this moment rather waiting to see what happens in Copenhagen and then deciding what we should do?

Prof. Garnaut—I am on the public record in my report and also in the evidence I gave to this committee and the other Senate committee earlier in saying that I do not think that Australia has adopted the ideal approach to assistance for trade-exposed industries. I now accept that we are not going to get a big reform of that except in the context of changes in the international environment—a comprehensive agreement that leads to comparable emissions constraints in the main countries or agreement perhaps within the WTO on comparable ways of achieving these things. Under the proposal of the government, comparing that with the assistance that industries would get under a principled approach that really dealt with the carbon leakage issue in an efficient way, my assessment, my estimate, would be that a number of industries are getting much more than would be necessary to avoid carbon leakage and some would be getting less. I have accepted that that is where our discussions are at the moment and we need progress in the international sphere to unwind the imperfections in the system.

Senator JOYCE—How much is the world going to warm by reason of Australia's delay for one year?

Prof. Garnaut—In the whole scheme of things that depends entirely on judgments that you make about the effects of Australia's action on a global agreement. I do not think that will necessarily have a negative effect on a global agreement whereas I think our commitment to go 25 per cent, if the rest of the world adopts comparably ambitious targets, will have quite a positive effect.

Senator JOYCE—I asked a specific question: how much will the world warm because of Australia not participating for one more year?

Prof. Garnaut—I will give you a specific answer. That will depend on the effect of Australia's action on an international agreement and I do not think that that will be insignificant.

Senator JOYCE—So it is what the international environment does and not what Australia does that really matters isn't it?

Prof. Garnaut—And what Australia does to affect the international agreement.

Senator JOYCE—I will talk about the international effect. Mr Blair Comley who was just in here said, 'Australia's demand for international permits will not change the price for international permits.' Would that be based on the fact that our effect is so small that it is infinitesimal?

Prof. Garnaut—That would be based on that judgment, yes. Not that it is infinitesimal but that it is small.

Senator JOYCE—It really is going to do nothing. Australia in isolation will do nothing to the global climate.

Prof. Garnaut—Australia in isolation will have a significant effect on the global discussion of climate policy which will affect global climate.

Senator JOYCE—That is an argument about debating, not an argument about science. If our debating skills are good enough, we may be able to affect the international environment. But the science, the actual hard-nosed fact, which everyone seems to be dancing around, is that what Australia emits has infinitesimally small effect, in fact no real consequential effect on global climate.

Prof. Garnaut—Not infinitesimally small but small and it is a fact of political science and economic science that what Australia does is relevant to a global agreement.

Senator JOYCE—Political science for me is oxymoronic. You are saying that really what this is about is to give us a good debating point at a certain conference in a certain European city.

Prof. Garnaut—Much more than that it is a part of what is going to be necessary, whatever the context, in getting global action.

Senator JOYCE—You said you were confident that China would be on board. What do you base that confidence on, Professor Garnaut?

Prof. Garnaut—Things they have already done and many discussions I have had with senior Chinese analysts, officials and policymakers.

Senator JOYCE—So they have given you a guarantee?

Prof. Garnaut—No. It is not for them to give me a guarantee or ask for one. I am giving you an assessment.

Senator JOYCE—Have they given anybody a guarantee?

Prof. Garnaut—I am giving you my assessment.

Senator JOYCE—Has India given anybody a guarantee?

Prof. Garnaut—No, and I have not given a similar assessment about India. India is not in exactly the same position as China.

Senator JOYCE—I want to go to one thing, specifically part 10 of this bill, 'Reforestation' where it speaks of the changes to encourage reforestation. Is the purpose of reforestation beneficial because of its capacity to store carbon? Is that correct?

Prof. Garnaut—Yes, and that is potentially quite an important part of a global mitigation system.

Senator JOYCE—So you would be aware of the studies of people such as Dr Christine Jones that say that more carbon is actually stored in summer grasses than in dry sclerophyll forest. So if we actually go down that path, wouldn't it make more sense to be pulling down dry sclerophyll forest and planting buffel grass and

mittell grass because, based on the science if your premise is to store carbon, that would be far more efficient and that is something that we should be concentrating on. If it is not why not?

Prof. Garnaut—I say very clearly in my report that it is highly desirable that we have comprehensive carbon accounting in the agricultural, pastoral and forestry sectors so we are giving comparable incentives for absorbing carbon in agricultural, forestry and pastoral activities to those we give elsewhere in the economy. What we need is a market based system that gives comparable incentives across the board. My assessment would be that within such a system agricultural, forestry and pastoral activities would make significant contributions in Australia.

Senator JOYCE—Professor Garnaut, my argument is: what is the point of replacing a more efficient carbon storage mechanism with a less efficient carbon storage mechanism and paying people to do it?

Prof. Garnaut—I am all in favour of environmental and economic efficiencies.

Senator JOYCE—But that is not in this bill, because if we believe in reforestation we believe in removing summer grass pastures which store more carbon than a dry sclerophyll forest. Why would we be paying people to reduce the carbon efficiency unless the motive is moving away from carbon sequestration and to another argument about forests and furry animals?

Prof. Garnaut—I am all in favour of efficient market based approaches to encouraging carbon sequestration wherever it occurs. That is what I say at great length in the report.

Senator JOYCE—Let us go to another issue that people keep on talking about: trying to second-guess America's position. There is 26 per cent of the world's global economy there so really what they do matters. Obviously, they are all looking at the Waxman bill. For the record, one senator said off the record that it has passed the house. It has not. It has only passed the committee stage at this point. I think 33-25 was the vote.

CHAIR—Senator Xenophon, do you have questions?

Senator XENOPHON—Yes, I do further to Senator Joyce's line of questioning. Professor Garnaut, do you see one of the problems at the moment with Australia going forward on this being that the accounting mechanisms, particularly for agriculture, are inadequate in that they have not been sorted out yet? Firstly, is that a fundamental problem in terms of the accounting mechanisms under Kyoto do not adequately credit the potential benefits of agriculture in relation to carbon sequestration?

Prof. Garnaut—There are a couple of issues, Senator Xenophon. One is that the Kyoto mechanisms do not create comprehensively sequestration through agricultural and pastoral activities and forests, and that is a weakness of the Kyoto arrangements. I myself attribute that weakness partly to the absence of Australia and the United States from very important discussions because Australia and the United States have a much bigger interest in these issues than the European countries that are left with excessive influence on design when we and our friends across the Pacific pull back. We should be working to correct that weakness in the international agreements. It is a tremendously important weakness not only for us but for our major developing country partners: Papua New Guinea and Indonesia and others in South-East Asia and the South Pacific. We should be doing all we can on that.

The second issue is that this is one reason that has been given for the emissions in the international regime. More work needs to be done on measuring carbon in soils, pastures and forests. Australia has made very good contributions to the supplied science in recent times. I would give very high priority to research in continuing that work. The fact that we are not there yet in measurement is the principal reason why in my report I spoke about bringing in agriculture and related activities 'as soon as possible' rather than immediately. I think if we give priority to development research 'as soon as possible', it can be soon but not right now. I think we should be working with other countries with a strong interest in these matters, including Indonesia, Papua New Guinea and the small countries it is working with in the rainbow coalition and also the United States, towards the international regime accepting comprehensive carbon accounting.

Senator XENOPHON—Finally, in questioning by Senator Macdonald at another parallel committee looking into emissions trading, I think your view, Professor Garnaut, was that it was a line ball decision—

Prof. Garnaut—Yes.

Senator XENOPHON—as to whether we should go ahead with the previous targets. Is your view the same? In other words, should we wait until Copenhagen, or has your view changed since the changes announced on the 4 May?

Prof. Garnaut—When I was asked by Senator Macdonald and answered that it was line ball, I said that there were three steps the government could take that would make it substantially beneficial. The first of those measures was to put back on the table the condition of 25 per cent reduction of emissions by 2020. The government has done that, so my assessment is that it now would be clearly a positive for this bill to be passed into law.

Senator XENOPHON—Even though there are concerns, such as from the Minerals Council in media reports today by Mitch Hooke, their CO, saying there are issues about the transitional elements of it and that jobs that could be lost because of concerns about the design features of the scheme?

Prof. Garnaut—I am not in a position to comment on every detail that Mitch Hooke has raised. As I have said, the treatment of the trade exposed industries does have some characteristics that I would consider to be less than ideal. I think the most important thing is that we make it clear we are going to get rid of the system of assistance for trade exposed industries when the rationale for it disappears. The rationale will have disappeared either when we have comparable emissions constraints in a large part of the rest of the world or when the major countries of the world have agreed on a comparable and principled approach to assisting trade exposed industries.

Senator CAMERON—Professor Garnaut, I would be happy for you to take these questions on notice. I want to come back to the reports in the *Australian* this morning—headlines like, ‘Carbon plans will cause jobs carnage’ and ‘Climate change warning: emissions trading scheme to “cost 24,000 jobs”’. In the body of the second report it says that 11,440 jobs will be lost in Queensland by 2020. Why didn’t your analysis pick this up, if this is correct? I would like you to give some thought to that. You can answer it now or in the future.

Secondly, Senator Joyce has raised another issue that I think is a bit of a furphy and I would like your analysis of that. He is linking the budget problems in California with the initiatives that Governor Schwarzenegger has taken on climate change. As I understand the situation from the Governor’s own website—

Senator JOYCE—Oh, that’s a reputable source!

Senator CAMERON—the problems in California are fluctuating tax revenues and autopilot spending, not anything to do with climate change. I am not sure if you can comment on those issues.

Prof. Garnaut—I am a busy person, and I am afraid I have not read the *Australian* this morning. Now that you have mentioned these things, I will in due course. But I did take seriously the question of employment; it was something that we discussed considerably in the review and in discussions with other parties. There is no reason to think that a regime of ambitious emissions reduction will lead to a net fall in jobs. There will be increased jobs in some industries and reduced jobs in others. It is likely that the reduction in jobs in some industries will mainly take the form of reduced expansion in future rather than sudden reduction, although it cannot be ruled out that in some businesses there will be early reductions. But overall there will be as many new jobs created as old ones lost. On the Californian situation, it would be drawing a very long bow to say that the fretful budgetary problems of California have anything to do with Governor Schwarzenegger’s approach to reduction of emissions.

Senator JOYCE—It would be drawing a very long bow to say they do not.

CHAIR—Thank you, Professor Garnaut, for giving us your time again this morning.

Prof. Garnaut—I am very happy to do that. Good luck with the rest of the work.

CHAIR—Thank you.

Senator CAMERON—Governor Schwarzenegger used to be your hero, Senator Joyce. Things change.

[11.23 am]

TARRANT, Ms Maria, Director, Policy, Business Council of Australia

Evidence was taken via teleconference—

CHAIR—Thank you for giving evidence on behalf of the Business Council of Australia this morning, Ms Tarrant. Do you have an opening statement you would like to make?

Ms Tarrant—Yes, I will do that. First of all, many thanks. I appreciate you arranging the teleconference. I will just make a quick statement, and then we can go to questions. By way of background, the BCA membership consists of the CEOs of 100 of Australia's largest businesses. The work of the BCA revolves around national public policy, and our, if you like, underpinning interest is that of sustaining growth and social prosperity. The CEOs within the BCA come from all sectors of the economy, including manufacturing, the industrials, chemicals, mining, business services, ICT, consumer services, financial services and health amongst others. The way we come to our policy positions is through research and discussions led by task forces within the BCA; the membership of those task forces consists of the actual CEOs.

The BCA membership came to the policy debate about global warming not as scientists and not from the point of view of international relations. In November 2006, it was agreed within the membership to relook at the issue with regard to global warming from, if you like, a risk management perspective and how to manage the risk at least cost, and it is those factors that have driven the work of the BCA in the subsequent three years. Over that time we have released three reports—the first in April 2007, with another in May 2007 and, most recently, one in August 2008. During that time we have also made submissions to both the previous government's Prime Ministerial Task Group on Emissions Trading, the Garnaut review, this government's green and white paper processes and, more recently, the Pearce review and the Senate committee's reviews.

At the core of the BCA's position are five critical elements in responding to global warming. The first is that the BCA believes that global warming is a global problem which can only be solved by a global solution. The BCA's policy position in relation to the risks of global warming is that you need to take a multifaceted approach and that that needs to include emissions trading, research and development, adaptation and energy efficiency. A well-designed emissions trading scheme capable of international linking has the potential to be the least costly way for Australia to move to a low-emissions future and to contribute to a global solution. The introduction of a national emissions trading scheme, though, must, in the absence of a global approach, be done in a way that maintains competitiveness. The setting of Australia's targets and caps must be done recognising what is physically possible within the electricity generation sector and in a way that facilitates a plan to transition to low-emissions technologies.

If I come specifically to the CPRS legislation, I think it is fair to say that the BCA was extremely concerned when the green paper was released. In our work 'Modelling Success in Designing an ETS that Works', we highlighted a number of design issues and their likely adverse impacts on business. The government then made a number of subsequent changes between the green paper and the white paper. At the time of the release of the white paper, we noted that some individual companies still had very specific concerns unique to their business or sector and that both the BCA and those companies would continue to address these issues with government and the opposition.

With the release of the exposure draft we, along with others, continued to highlight the need for further changes, especially in light of the global recession. The government announced a number of further changes on 4 May which have been supported by the BCA, including the deferment of the start date, the GFC buffer and the fixed permit price for the first year. Greg Gailey, who is the President of the BCA, noted in his statement following those announcements that the changes should be included in any legislation and that certainty about the timing and the rest of the details of the CPRS were essential to enable business to plan for and respond to the impacts of the CPRS. At the same time, he noted that the BCA would continue to work with government to ensure that the assistance delivered in the CPRS achieved the objectives of both preserving jobs and avoiding carbon leakage. He also sought a bipartisan approach to working through the details.

Coming to the bill that was released on 14 May, I have to be perfectly honest and say we are still working through the large number of pages. What I have to say today reflects, if you like, a work in progress. Even with the introduction of that legislation, there remain many details that are still to be resolved, and it remains unclear to us that the proposed treatment of the coal based electricity generators will ensure a smooth shift to low-emissions electricity generation. There is a risk of disruptions in the sector if the CPRS is not improved.

There are also outstanding issues related to the treatment of the coal industry in the absence of a global carbon price, and there remain significant matters of detail to be resolved in relation to the emissions-intensive trade-exposed industries. This goes to matters of definition of the activity, the formula for value-adding, the level of permits to be allocated et cetera.

So getting the detail of the scheme right means, from our perspective, that we need to know that the scheme does not include the risk of reducing competitiveness or that it brings with it a disruptive transition of the electricity sector or a deferral of investment, business closures and job losses. Business will need to consider both the act and the regulation to be sure that the details are right. Once the detail is right, we would like to see the legislation passed this year so that businesses are clear about what is expected of them and so that they can plan for the impacts of the CPRS. But what remains critical is to see all those details. I think that sort of sets the scene from the BCA's perspective, and it might be best to move to your questions.

Senator JOYCE—I am going to go through a few things. With respect to part 3, division 6, of the amending legislation, the transfer of liability in joint ventures and the prevention of liability being transferred to a foreign entity because of the difficulty in enforcements on foreign entities and maintaining consistency, as per clause 73(b), do you envisage any problems with sovereign wealth funds and the capacity of their involvement in the mining sector and possible discrepancies between an Australian based mining company and a venture with access to a foreign sovereign wealth fund?

Ms Tarrant—As I said, we are still going through the detail and, to be honest, the whole issue of ownership and transferring of liabilities is one of the areas on which we are still seeking some advice. Can I take that on notice and get back to you?

Senator JOYCE—It is pretty complicated, isn't it? We need a lot more time to go through things such as that, don't we?

Ms Tarrant—It is certainly taking up a lot of time to go through it.

Senator JOYCE—That could have a vital impact on Australian miners and their capacity to compete against external miners in our own country?

Ms Tarrant—Because we are still trying to be clear about what is intended and how the drafting can be interpreted, we actually do not know whether it will but we are concerned it could. As I said, I will get back to you as quickly as we can, but we are still taking advice.

Senator JOYCE—The part 3, division 6, amendment amazes me a little bit, because I wonder who will be lobbying to exempt foreign entities in our nation?

Ms Tarrant—I do not know the background to it. As I say, from our point of view, we are looking at the legislation as it is drafted, not how it got there.

Senator JOYCE—Because there is no exemption for domestic entities, so I suppose it must be someone from overseas who is lobbying our government for that exemption.

Ms Tarrant—I do not know.

Senator JOYCE—I also want to go through part 4, division 3: the deeming of assets to be personal property. What is your view that this would have a capacity to get to a tipping point into deeming an asset to be a non-real-property asset; therefore a foreign entity would be capital gains tax exempt on sale and purchase?

Ms Tarrant—You are probably going down through all the same levels of drafting here that all of us are currently trying to unbundle and clearly trying to understand the implications. We think it could have an unintended consequence and we have a series of questions out to member companies trying to get to the bottom of this.

Senator JOYCE—That is another thing. You would then have a domestic company that would be up for capital gains tax on the purchase and sale, but another company, because it is an overseas entity, would be exempt from capital gains tax on non-real-property assets and, because the credits are deemed to be personal assets, that could have the capacity to take them to a tipping point to make them a non-real-property asset. This is another complication that has not been properly fleshed out because this inquiry is not going for long enough.

Ms Tarrant—I guess we all working to whatever the time constraints are. We are working as fast as we can to get to the bottom of it and to understand the implications of this legislation. That is why my comments today are a work in progress.

Senator JOYCE—The other matter is the hoary chestnut that is belted around. We have gone through the technicalities and showed the deficiency in the assessment of them, but let us now go to a big picture item: the issue of green jobs. Where on earth are these green jobs going to be and who will we be competing against and where is the modelling that says they have the capacity to pick up the slack from the mining industry?

Ms Tarrant—We have not done work trying to separate out what you might call green job versus a non-green job. In terms of talking with the BCA membership we can identify there will be jobs emerging around the CPRS or as a result of the CPRS. We have not done any work on what the quantum of those will be and whether they are substitutable.

Senator JOYCE—These are questions I would like to have asked the department, but I did not have time. You have said you had a lot of difficulty working through the 1,300 pages.

Ms Tarrant—Yes.

Senator JOYCE—How are you going? Where are you up to?

Ms Tarrant—What we have done is focus on the areas that we have had a particular interest in, which is around the EITEs, the electricity sector and what is happening in terms of the objectives and the principles in the legislation. That has been our first order. We have got a number of people looking at some of the tax issues and, dare I say, the liability issues and the treatments of the assets. I guess we are working under the same time constraints everybody else is.

Senator JOYCE—And you have had the capacity on these 11 pieces of legislation to do the modelling for your members and to get back to them to tell them what the repercussions are so you can make a value judgment in your representations to political members on how they vote?

Ms Tarrant—We have not done modelling, I do not think, in the terms that you mean it. We are going through and alerting members to the issues and implications and seeking their feedback.

Senator JOYCE—With the advent of free permits, do you see that there is any capacity there for that to exclude entry of new participants in a market, especially the mining market, because one person has free permits and another person does not?

Ms Tarrant—Our understanding—and we are still going through the legislation—is that it will not preclude new entrants. In fact, the new entrants will come in under the same arrangements. We are just checking that.

Senator CAMERON—Does the BCA accept the science that has become the consensus on climate change and the view that we have to have a global response to reduce the carbon footprint?

Ms Tarrant—As I said in the opening statement, BCA membership really have come to the policy issue not as scientists and not from the point of view of international relations. We have really said that, in light of what is happening in terms of other research and commentary, we needed to think through what was the best risk-management approach and then, if you think about markets as a way to get a least-cost response, how you would use market mechanisms to provide the levers for the risk management.

Senator CAMERON—You say the ‘least-cost response’, but there is obviously a cost to dealing with this global challenge. Is that accepted by BCA?

Ms Tarrant—It is, yes. The reason we say ‘least cost’ and not ‘no cost’ is that we recognise there will be a cost. From our perspective, to try and minimise that cost you do want a global response. Certainly, in the absence of that global response, whatever you put in place in Australia as the interim arrangement has to have some sort of compensatory mechanisms that make sure our competitiveness is not put at risk.

Senator CAMERON—The mining industry are extremely vocal in terms of the current situation, especially the Minerals Council. The BCA have had a long time to look at the Treasury modelling and the modelling done by Professor Garnaut. I have not seen any critique of that modelling that says that there will not continue to be growth in the Australian economy over time and that that growth will be robust. Does a BCA have a different view to that?

Ms Tarrant—If you look at the Treasury modelling, what you are doing is comparing a current point and a point in the long term. You would expect, with general equilibrium modelling, to balance out a number of the

issues over time. I think what concerns the BCA and a number of other organisations is the transition process. If you think that you might see jobs coming out of a sector but being replaced by jobs in another sector, at a macro level that might all balance out but at a micro level what would be of concern is how the substitution happens and what sort of disruption or dislocation there is. That is why, from our point of view, managing the EITEs properly and thinking about how you skill up for the transition and how you manage it become critical elements.

Senator CAMERON—The transition process is part of the short-term response. The BCA have been critical about short-termism in Australia and have actually published papers on short-termism. Do you agree with some of the arguments that the BCA put forward in that paper—that we really need to look at the long term? If you agree with that, isn't the real long-term issue reducing the carbon footprint globally?

Ms Tarrant—The long-term issue from BCA's perspective is how Australia contributes to a global response. But part of addressing that long-term issue is how you manage the various steps along the way. We do not actually know as a country what that transition period is because it is very much dependent on how different countries internationally respond and what comes out of Copenhagen and subsequent international agreement. To think that the transition is short term, that is one or two years, I think would be a bit naive. We may well be in gradual transition over a much longer period of time. If you go to the electricity sector, there is no way you can suddenly switch off the current way we get our electricity in Australia and switch on a different way in a matter of a few years. That is going to take a decade of investment.

Senator CAMERON—Has the BCA studied the national climate change program announced in China in June 2007, or the act on climate change 2009 in South Korea, or India's national action plan on climate change? Have you had a look at any of the initiatives that are taking place globally?

Ms Tarrant—We do keep, if you like, a high-level review of what is happening internationally, whether people are looking at using energy efficiency policies or other sorts of mechanisms to respond. One of the reasons why we were supportive of what the government has proposed as conditions and the method of checking the conditions in terms of shifting from lower to deeper targets is that that actually provides a mechanism by which you can actually evaluate what those other countries are doing in practice and what that does to Australia's competitiveness.

Senator CAMERON—Does BCA support the argument that Australia is acting unilaterally?

Ms Tarrant—I do not know what that means, sorry.

Senator CAMERON—This has been a big part of the debate. I am surprised you have not had look at it. Mitch Hooke, the chief executive of the Minerals Council, was very strong in his argument to previous committees that Australia was acting unilaterally. I think it is quite simple: we are either acting unilaterally or we are not.

Ms Tarrant—The terminology has been used by journalists to mean different things in different spaces. If you look at what the previous government was doing towards the end of its time and what this government is doing now, my view is that they are gearing up to be part of some sort of global response. So I do not necessarily think setting targets and going into international discussions of itself is acting unilaterally. What would be acting unilaterally is for us to do something that ignores what is happening internationally. This comes back, from my perspective, to how we manage the trade exposed emissions intensive industries. If we do not have a mechanism that calibrates the treatment of those sectors in line with what is happening in other competitive countries, in effect we would be acting unilaterally.

Senator CAMERON—But you are not arguing that the government is about to set off on unilateral action which would create devastation in the employment sector of Australia, are you?

Ms Tarrant—No, what we are saying at the moment is that the devil is in the detail. Until we know how the trade exposed emissions intensive industries are going to be treated and how that competitiveness risk is going to be managed sector by sector in the intervening time until there is a global carbon price, we need to know that to know that we would not actually be putting jobs and things at risk.

Senator CAMERON—Coming back to the initial question I put to you, you say you monitor developments overseas. Professor Garnaut has just given evidence to say that we are probably doing less than even some of the developing countries overseas. I have quoted some of the acts that are in place in China, India and other countries. What is your view? Do you think we are doing too much at the moment?

Ms Tarrant—You can announce a whole range of policies and programs and acts of legislation—and it does not matter whether you are a developed or developing country—but the challenge is whether they translate to actions on the ground. The challenge, particularly if you look at, say, China, is that I do not know that anyone knows what is actually happening at the moment. If you look at some of the announcements in terms of India, they are prospective, not current. So I can see where Professor Garnaut is coming from, because there have been all these announcements. But, from a business perspective—and when you are worrying about competitiveness—you want to know how that translates on the ground and what that actually means to keeping a level playing field. We at the BCA are not confident we know at the moment.

Senator CAMERON—Sorry, you are not confident you know what?

Ms Tarrant—We are not confident that we know what it is translating to on the ground. The timing for when those policies will take an effect on the competitiveness of, say, steel and coal out of China versus from Australia. That is why, if you look at what the government has proposed around conditions for shifting the targets, the independent review is so critical.

Senator CAMERON—So you do not know whether China has imposed an export tax on energy efficient industries, including a 10 per cent tax on primary steel products? You do not know that?

Ms Tarrant—We do not know how that is actually translating.

Senator CAMERON—But do you agree that they have imposed the tax?

Ms Tarrant—We agree that it has been announced. We have not seen how it is working in practice. This has been a discussion not just for China but for a number of countries in the last six months. It is a bit like looking at what is being proposed at the moment in the US. How will that translate? We do not know yet.

Senator CAMERON—Okay. I may have some questions on notice.

Ms Tarrant—That would be fine.

Senator CAMERON—Thank you.

Senator XENOPHON—In relation to the whole transition, is what the BCA is concerned about in going from a high carbon to a low carbon economy the transitional costs? What do you say would be an alternative method of still getting to the same target in terms of reducing greenhouse emissions without the same level of transitional costs?

Ms Tarrant—What we are concerned about is the process of transition and managing it in a way that does bring unnecessary shocks. The BCA's position has been, after much consideration, that a linked world emissions trading scheme is the best way forward. We have had discussions within the membership and, assuming it is a well designed ETS, at the end of the day it will give companies the discretion to work out how best to manage this. It is quite a different proposition to say a tax. So when we start from that principle then the next thing for us is to ask: 'What is the mechanism that facilitates management of the electricity sector and what is the mechanism for facilitating management for trade-exposed emissions-intensive industries?'

What we are concerned with at the moment with the electricity sector is that what is in the bill itself may not be sufficient to actually deal with asset impairment. It may not be sufficient to deal with working capital and hedging issues. You have got a conflict because you have got states capping electricity prices, so how do you actually reconcile putting the price up to manage the impact of the scheme et cetera? They are the things that we are still wanting to talk about with anybody who will listen to us over the coming weeks to get them right around electricity.

With the emissions intensive trade exposed, until we know what are going to be the final activities covered in each of the sectors and then to what degree there are administrative allocations of permits, and until there is a global price, we do not know whether those transition policies are going to do the job or not. That is why I come back to: the devil is in the detail and seeing the regs is going to be really important.

Senator EGGLESTON—On that very line, a major independent analysis conducted by the Centre for International Economics concluded that the government and community could have little or no knowledge of the cost and effectiveness of the government's proposed emissions trading scheme over the next 20- to 30-year transition period because 'there is no analysis of the different scenarios concerning the start date for other countries during that 20- to 30-year transition period, there is no analysis of the impact of the global financial crisis and there is no empirical analysis of alternative approaches to achieving a reduction in CO2 emissions'. That troubles me and I am sure it would trouble the Business Council of Australia as well.

Ms Tarrant—There is a plethora of different bits of modelling which will deal with some of this, mainly in the long term, and some of it will be for a particular sector with particular assumptions. The concern that we have had within the BCA is: how do you design a scheme that can actually be robust enough to deal with what might come out of any of that modelling? If you get the mechanisms around the emissions intensive trade exposed right, if you get the mechanisms around electricity right, if you manage the international linkage and make sure you get access to the cheapest permit structures, then in a way you have built the building blocks to deal with what the modelling might throw up. So I guess we have taken a slightly different approach.

Senator EGGLESTON—I understand that. Nevertheless, it is still a matter of great concern.

Ms Tarrant—The challenge will be that modelling of itself can give you important parameters and ranges but it is not the solution. We do not have that many resources within the BCA so our energy has gone into finding ways that are robust enough to manage whatever comes out of the modelling, not to do the modelling itself.

Senator EGGLESTON—The coalition's greatest concern is that the Rudd government has, deliberately, largely ignored the impact of its proposed ETS scheme on our competitiveness and jobs in the first 20 years of transition if major competitors do not reciprocate by establishing an ETS. The design of the Rudd government's scheme assumes that our major competitors will move to put in place a major new tax on carbon in the early years. Our concern is: what if China, India, Indonesia, the Middle East, South American countries and many of the other competing developing countries do not apply a tax for carbon for 15 or 20 years?

Ms Tarrant—We would share exactly the same concern, that Australia would be at risk if there is not a carbon price internationally that all our competitors are putting on their products. That is why we have put so much energy into how you deal with the trade exposed emissions intensive industries and how you deal with the electricity sector, because if you get the right interim policy instruments in place—

Senator CAMERON—But, on this point, you gave evidence that you did not see that Australia—

Senator EGGLESTON—Senator, with respect I am asking questions now.

Senator CAMERON—This is on this point, that Australia—

CHAIR—Senator, it is very confusing with people talking in a teleconference. Senator Eggleston has the call.

Ms Tarrant—I must admit I could not understand the interplay. I will finish my answer. We are concerned that we ought to maintain Australia's competitiveness in the absence of a global price, and that is why we have focused on whether what was in the previous government's model or what is in this government's approach has robust levers or specific policies that maintain the competitiveness, because we will have to do that internally here, unlike countries that are not part of an international program that can somehow or other discount and make the equivalence.

Senator CAMERON—Ms Tarrant, the basis of that question—

Senator EGGLESTON—I have the floor.

Senator CAMERON—I am entitled to come in on that issue.

CHAIR—No, excuse me.

Senator EGGLESTON—Chair, I do object in a formal sense, that this is an outrageous interruption. I have to finish my question.

CHAIR—Senator Eggleston, you do not have to object in a formal sense. Continue with your question, please.

Senator CAMERON—You are such a sook.

Senator EGGLESTON—Senator Cameron, I think you should learn the rules of conduct of the Senate.

Senator CAMERON—You should behave yourself, then, and stop being such a sook.

Senator EGGLESTON—We are not in a union brawl at the moment. I know you know a lot about that.

Ms Tarrant, the problem is that Treasury has never modelled those scenarios and yet the government is proceeding to introduce this legislation and wants it passed by the end of June. We feel that that imperils industry in Australia. I put this question to you: would you not think it was more prudent to defer this legislation until that Treasury modelling has been done so that we do know where we are going before this legislation is put in place and so we do know what the outcome of the Copenhagen conference will be?

Ms Tarrant—If I go back to what I said in the opening statement around that—the issue, if you like, of timing—the discussion amongst the BCA members has been to focus on knowing what the scheme details are and getting them right. To do that we will want to see both the draft act and the regulations to be sure that the detail is right. Once we know that is right, we would like to see the legislation passed this year so that businesses are clear about what is expected of them so they can plan for the impacts of the CPRS. The integral concern for the BCA is to see and know the detail is right. Having the detail right is about having mechanisms that make sure our trade-exposed emissions-intensive industries are not at risk in terms of competitiveness and that there is a mechanism that makes sure we do not have disruptions in the electricity sector.

Senator EGGLESTON—But isn't that an argument for deferring passing the legislation until there is proper modelling done and analysis produced on those very issues?

Ms Tarrant—Not necessarily, because—

Senator EGGLESTON—Well, you cannot do it in two weeks, and that is all you have got.

Ms Tarrant—I think there is for us a concern around the sequencing of the act versus the regs. A lot of the detail to do with the emissions-intensive trade-exposed is in the regs, and that is what we will want to see. I still can imagine that you can get both the regs and the act reviewed by business before the end of the year.

Senator EGGLESTON—You have to get it done in the next two weeks, with respect.

Senator PRATT—I will put my questions on notice and will defer my couple of minutes to Doug. Thank you.

Senator CAMERON—Ms Tarrant, you were questioned by Senator Eggleston on the basis of a hypothetical about Australia moving ahead of its competition and acting unilaterally. I will put the question to you again: do you have any evidence that Australia is about to act unilaterally and deliberately put jobs in jeopardy in Australia?

Ms Tarrant—This is where I feel like we are playing with words a bit. The government has announced a unilateral minus five target. That is irrespective of what happens internationally. Business has said that that is a hard ask. The issue about whether we are about to put an emissions trading scheme in place in a way in which it is unilateral is a different question. There are emissions trading schemes elsewhere. From our point of view, what we are looking at in the emissions trading scheme is regulations and legislation that make sure we do not put our emissions-intensive trade-exposed industries at risk because our competitors do not have an equivalent scheme in place.

Senator CAMERON—But do you accept that the government has put in place appropriate checks and balances before we move to a higher target, and that requires an ambitious global deal?

Ms Tarrant—Yes, that is what I indicated. The BCA has supported the conditions that are there for the transition to the minus 25 and the independent review to check that those conditions are met. From our point of view, making sure all those commitments are met and using that independent review to do that remains important—is essential.

Senator CAMERON—If the government meets its commitments on those issues then this argument from Senator Eggleston that we will put our business in some severe disadvantage does not stand up, does it?

Ms Tarrant—If the commitments that are in the shift from the minus five to the minus 25 are evidenced—and that requires action not by Australia but by our international competitors—then we would not be disadvantaged relatively.

CHAIR—Thank you for taking the time to give evidence to the committee.

Ms Tarrant—It was a pleasure. I think Dr Grant has an email address for any questions on notice.

CHAIR—Thank you very much—that is good of you.

Proceedings suspended from 12.00 pm to 12.49 pm

MORAN, Dr Alan, Director, Deregulation Unit, Institute of Public Affairs

CHAIR—The committee has reconvened. We welcome Dr Alan Moran from the Institute of Public Affairs. Would you like to make an opening statement?

Dr Moran—Sure. I will keep it brief. I want to traverse some of the stuff we heard before as background. I am not going to go through the whole of the prehistory, but, basically, what we have seen in terms of climate oscillations. Since about 1,400 BC there has been a warmer climate, and we have seen all civilisations flourishing. It has been going up and down since then. In early Roman times, the Tiber used to freeze and a lot of civilisations declined. The sorts of things regarding temperature that are most familiar to us have happened since warming. During the Roman times we had the Roman warming, with vines in northern England and vast population increases in central Asia. Roughly at that stage, 200 B.C. to 500 AD, temperatures were about two degrees Centigrade warmer than today. We saw temperatures falling in the Dark Ages, the medieval warming, with the Viking colonisation of Greenland et cetera, and then a cooling again. So we have seen a lot of oscillations.

In the past 100 years we have seen temperatures increase until about 1940. Then there was a slight fall, and then an increase again until the mid-nineties. Since then it seems to have fallen again. Theoretically, all things being equal, the warming accompanying a doubling of preindustrial CO₂, which is 280 parts per million, would be about 0.3 degrees Centigrade to one degree Centigrade—just that on its own. That temperature is logarithmically associated; therefore, with each doubling it diminishes and it peters out as an effect at about 900 parts per million. To arrive at the more alarming temperature increases projected as a result of increased human induced CO₂, the model used by the IPCC and others bring in the feedback, and that feedback on seven models raises the temperature effect of CO₂ to two degrees to five degrees Centigrade. This is quite disputed. Bill Kininmonth, who is the former head of the Australian National Climate Centre, has mounted a very strong case that major positive feedback of that nature is impossible. NASA's Roy Spencer has produced evidence that the feedback is actually negative.

One feature, though, of the association of warming and CO₂ in the past is that invariably the CO₂ increase followed the warming, not vice versa. That does not actually mean that it is impossible for the effect of increased CO₂ to trigger an increase in temperatures but it does undermine somewhat the carbon association. In this respect I think it is worth mentioning that the earth's warming over the past century is pretty similar to the warming that has taken place on Mars, Jupiter, Neptune and Pluto, where the temperature changes, like those on earth, at least in the past, are almost entirely governed by changes in solar radiation. I do not make these points as an expert as such in climate science but as a background to the various oscillations and the risks that are prevalent in Australian government policy on climate change.

In terms of the economic effects and what leads to them, it is barely conceivable that the world can stabilise CO₂ emissions. To do so, we are talking about emissions at a level of about three tonnes per capita. At present, Australia does 16 tonnes, the United States does 20 tonnes and the EU does nine tonnes. China, which is only one-third developed, is already at 4.5 tonnes. In other words, it is 50 per cent above the level at which the world has got to be—even in China's case. India is somewhat below that. If Australia closes down its entire coal industry, including the 85 per cent of electricity that is coal generated, we will still not get close to the target. If we replace coal with gas and add 50 per cent to the price, it would still leave very high emissions. Replacement by wind would not be feasible, and wind is, in any event, three or four times the cost of coal. The only two feasible means of getting there are nuclear, which is a cost similar to the entire national economy, or poverty, if we go backwards in terms of living standards.

Australia's goal is to reduce, as you know, the emissions by five to 25 per cent by introducing the cap and trade carbon tax, which is designed to change behaviour of businesses and consumers. These measures are accompanied by a funding which seeks to drive technical solutions in terms of green buildings, green coal, renewable energy et cetera, and these fundings, which are already in the budget papers and have been for some time, are threefold. We have the MRET system, which with state schemes and other measures will require by this year 10 per cent of electricity to be supplied by subeconomic renewable resources, and that is at a cost of \$843 billion. We have got various subsidies in this year's budget which are about \$500 million specifically for greenhouse matters; more than that because there are some issues which are not classified as greenhouse but are related. And then there are the state matters too. The third one is that we have got various regulations the

most important of which is five star on building and housing in particular, which has a tax equivalent of about \$1 billion.

If you were to combine all that together and make it into a tax, it would be a tax on static forms of energy, electricity et cetera, of about 10 per cent. Not very long ago 10 per cent, which is what we presently theoretically impose, would have been the level people were saying was necessary to do the trick to eliminate carbon or to severely erode its presence. Cap and trade will go on top of those sorts of things and will add additional costs. I think many of you would have seen submissions from industry. For example, Caltex has said that just to survive would cost it \$23 million to \$40 million a year to purchase the carbon credits and that that would not be borne by its competitors overseas and in the end, of course, Caltex would relocate, which would mean the end of a valuable production facility. OneSteel has made some similar suggestions. Alcoa has warned that it would need to shed its two Victorian aluminium smelters, two of the state's most important facilities. Again, that output would be simply replaced by other output from countries which are not intending to apply a carbon tax at the present time. There are other effects on the electricity producers. TRUenergy has said that as a firm it would need to cease operating by 2015. It is saying that I think not as a threat, it is saying that because it is looking at its memorandum of association and its loan book et cetera. And it suggests that Loy Yang and International Power would be in the same boat. That is 90 per cent of Victoria's electricity.

If an ETS is to be implemented globally, as of course it must be, it would require the elimination of coal as a source of energy unless there is some cheap form of carbon capture and storage. There is no prospect of that on the horizon. Australia has got about 76 billion of coal reserves. If we wipe out coal as a possible use, for Australia, even if coal is worth as little as \$10 a tonne, it is a sacrifice of \$760 billion wealth, if you like, just from coal and compounding that we would have wealth shedding from shale oil and gas and various other things.

An ETS would not only stifle current business operations but would virtually eliminate new investment in power generation as well as other energy intensive processing. Leakage would be inevitable despite of the energy intensive allowances which are in place. All they would do is retard—

Senator JOYCE—You say 76 billion. What time frame are you talking about?

Dr Moran—Basically in order to achieve the stabilisation of carbon, it means you have to wipe out coal.

Senator JOYCE—Are you saying that the whole resource in the ground is only worth \$76 billion?

Dr Moran—No, it is \$760 billion. It is probably worth more; that is just valuing it at \$10 in the ground a tonne. It is probably worth more than that. If anyone has got a better guess that is great.

CHAIR—I think that sound shows we have lost Senator Xenophon's teleconference link for the moment.

Dr Moran—I will just finish very briefly. It would require an awful lot to do this. It is not only the developed countries that would need to reduce their emissions levels to one-third, or whatever, of their present levels but also the developing countries that would need to do that, and it would nip in the bud any chances of them developing. These issues are compounded if Australia is to take a very high, proactive position on this. We are 1.2 per cent of global CO₂ emissions. If we move in advance of other countries we will lose an awful lot of industry as well as the value of the coal and all the other natural wealth we have. One of the key outcomes of the Treasury modelling which offers a promising policy approach is that Treasury estimate that the cost of doing nothing to 2020 and then catching up with the 2050 target thereafter, should the need of such action prove necessary and achievable, would be 0.3 per cent of GDP by 2050. It seems to me that, even if this is not overstated, 0.3 per cent of GDP is a reasonable insurance policy price to pay, rather than imminently embarking on the measures that will be, in the white paper's words, 'the most significant structural reform of the economy since the 1980s'. By 2020 the need for emissions reduction policies will be clearer and presumably we will have access to all the technological advances that Treasury claim will be forthcoming by that time. It seems to me that preparing for the action but deferring doing anything concrete would be an ideal solution for Australia.

CHAIR—Thank you.

Senator CAMERON—Do you agree with the proposition that is up on your website sourced to David Bellamy, who talks about scepticism? He says:

The first question most people ask me these days are how could all those global warmers have got it so wrong? My answer is to remind them of the millennium bug, the dot com bubble and the credit crunch, together these have caused tens of thousands of the worlds' most highly paid and computer literate people to succumb to a mass hysteria.

Is climate change a mass hysteria?

Dr Moran—I do not know. It is not my area of expertise. I note that there are a lot of doubts put forward by people like Bellamy. There are very prestigious scientists, like Lindzen and others, who have their doubts. From my perspective, all I am looking at is: what would it cost Australia to start doing the sorts of actions that are being proposed?

Senator CAMERON—That is fine. I am just saying you pick this up almost immediately when you go to the IPA website, so it is given quite a big focus on the website. I think it sets a tone for the IPA.

Dr Moran—You may say so, but I do not agree that it sets the tone for the IPA. It is not really our core business. I do not think that is the major front page of the IPA at the present time. It may have been when you looked because it was a contemporary piece.

Senator CAMERON—You say it is not your core business, yet you went to China to have a look at climate change.

Dr Moran—I did indeed.

Senator CAMERON—And your report runs to about two pages.

Dr Moran—When I say it is not our core business, I mean science is not my core business. My core business is the economics.

Senator CAMERON—Did you have a look at the economics on this in China?

Dr Moran—Yes.

Senator CAMERON—And you produced a two-page paper. Is that it? Is there something I am missing? Is there more?

Dr Moran—No, you are not missing anything.

Senator CAMERON—That is your analysis of China?

Dr Moran—I would be very pleased to do a longer one if you wish.

Senator CAMERON—Can you explain the key issues that China have adopted in the National Climate Change Program?

Dr Moran—They have major subsidies for wind. I am not sure what proportion of Chinese electricity is wind. It is probably under one per cent, but they do have major subsidies. They are actually protectionist subsidies. The subsidies are not to wind but to Chinese manufactured wind turbines.

Senator CAMERON—That is not what I have. Have you read the policy?

Dr Moran—Yes.

Senator CAMERON—Can you explain to me the key issues? Aside from wind, what other policies are they adopting?

Dr Moran—The Chinese policy is essentially that they see their carbon dioxide emissions rising to about double their current levels of nine—

Senator CAMERON—You say you know the policy, you say you have been to China; could you please give me your understanding of the National Climate Change Program in China? You have written papers—two pages—about it. Can you explain it to me, please?

Dr Moran—The Chinese have got a lot of different policies on things, but I can tell you what their outcome is.

Senator CAMERON—No, I am interested—you went to China. The landmark position they have adopted is their national climate change policy. You come back and say, ‘This is what’s happening in China.’ I would like you to explain to me how you understand their national climate change policy. What are the key aspects in it?

Dr Moran—The key aspects are that the Chinese are intending to reduce their emissions over time. An aspect of that is that they are not intending—and this is coming from their current statements—to take any immediate action other than to subsidise wind, which they are doing in quite a big way. They are opening new power stations, coal powered stations, at quite a lick at the present time.

Senator CAMERON—I am sorry, but that is not the policy. I would like you to come back to the policy. You went to China and you looked at climate change. The key aspect of China's climate change policy is their Climate Change Program; I would really like you to take me to the key aspects of that program.

Dr Moran—I will tell you what the key aspects are. The Chinese are not going to do anything—you have read my paper, haven't you?

Senator CAMERON—I have read your paper.

Dr Moran—Do you disagree—

Senator CAMERON—Can I say to you that it did not give me any understanding of what was happening in China other than a philosophical dissertation from you about what you think is the right thing. I am interested in the factual basis of what is happening. Let me put some points to you individually.

Senator JOYCE—Give him a chance to answer.

Senator CAMERON—He can't answer; he doesn't know.

Senator JOYCE—All we are hearing is you.

Senator CAMERON—And he comes here as an expert!

Senator JOYCE—We are hearing you, Senator Cameron; we are not hearing from Dr Moran.

Senator CAMERON—If he comes here as an expert, he should know.

CHAIR—Can you just finish the question, Senator Cameron.

Dr Moran—The answer is that the Chinese are expanding their fossil-fuel power levels at a very strong pace. They have a very strong nuclear policy, which they are intending to increase.

Senator CAMERON—That is not—

Dr Moran—If that is not their policy, what is their policy?

Senator CAMERON—No—

Senator JOYCE—Let Dr Moran answer.

CHAIR—Senator Joyce, I will deal with this.

Dr Moran—They have a very strong nuclear policy. Realistically, they do not expect their levels of carbon dioxide emissions to start declining until after 2030, at which time they are expecting their levels to be around nine tonnes per capita compared to 4½ tonnes at the present time. They have strong aspirations about doing things about wind and they are doing things there. They have a very strong nuclear program, but essentially they are rapidly expanding.

Senator CAMERON—What is the top 1,000 enterprise program?

Dr Moran—I don't know.

Senator CAMERON—You don't know?

Dr Moran—No.

Senator CAMERON—What is their program to eliminate inefficient power plants? What is the percentage they want to reduce inefficient power plants by?

Dr Moran—They have a number of 30 per cent in various places, to eliminate 30 per cent of emissions.

Senator CAMERON—What is their plan for inefficient industrial plants?

Dr Moran—They have a plan also to reduce inefficient industrial plants.

Senator CAMERON—What export tax have they put on energy intensive industries?

Dr Moran—I don't think they have any.

Senator CAMERON—See, you don't really know this stuff, do you? You come here as an expert—

Dr Moran—You tell me what the—

Senator CAMERON—Wait a minute. You come here saying you are an expert in this area: 'I have been to China.' You gave this big dissertation. You really don't know what is happening. Is that correct?

Senator BUSHBY—That's badgering the witness.

Dr Moran—Do you believe the Chinese have got an export tax—tell me this, Senator; you sound like you are an intelligent man—

Senator CAMERON—You don't question me.

CHAIR—Senator Cameron and Dr Moran, can I have order please. Senator Bushby has a point of order.

Senator BUSHBY—Senator Cameron is impugning the witness. The witness came in here and said that he was an expert on the economics of how this would apply in Australia. Senator Cameron has gone off and found something—he happened to go to China and had a look at what was going on there and made some comments.

CHAIR—I think this is debate more than it is a point of order.

Senator BUSHBY—But he is impugning the witness's character.

Senator CAMERON—He doesn't know what he's talking about!

Senator BUSHBY—The witness stated initially what he was here to talk about and Senator Cameron has taken him off on a furphy and is impugning him on that.

Senator CAMERON—You come here as an expert and you don't know!

Senator JOYCE—It is like Gollum asking, 'What's in my pocket?'

CHAIR—Let us just continue. If I think that it is getting any more than the vigorous questioning I have seen here before in this committee, I will pull him up.

Senator CAMERON—Let us go back to the National Climate Change Program. You have been in China; you have studied what is happening in China; but you do not know what is in the Chinese National Climate Change Program.

Dr Moran—I have been to China. I went to visit China to talk to people in China about what they are doing. I went to Japan as well, and I went to the United States. I discussed with people, experts in the area, what they are doing. I wrote a report. It was not a PhD thesis; it was a report.

Senator CAMERON—It certainly was not, no.

Dr Moran—But it was doubtlessly better than you could have done.

Senator EGGLESTON—What we are here to do today is discuss the changes to the CPRS submission trading scheme proposal put up by the Rudd government. This whole scheme is predicated on the concept of there being emissions trading markets out there and I am concerned, as is the coalition, that we may introduce the scheme based on a world emissions trading market in the next two weeks and find that our major trading partners do not actually go down that road. We wonder whether it might be better in fact if we deferred the whole thing. Having passed legislation this month, might it be better if we deferred the whole thing and waited to see what was happening in the rest of the world at the Copenhagen conference and then considered what an appropriate scheme for Australia would be? Would you comment on that, Dr Moran?

Dr Moran—My own view is that we are a small player here. We are one per cent of emissions and we have about that same sort of level of influence worldwide. If we actually take a pre-emptive step by moving forward, we do put our industry in some sort of jeopardy especially in the context that other countries may not follow. There are a lot of lofty statements being made by administrations across the world about what they are going to do, including the Chinese, as Senator Cameron has made clear, but there is very little action. If we go ahead and undertake action before other countries do, we will be in great jeopardy. The minimum we ought to do is to ensure that other people are going to be in lock-step with us. Even then there will be a cost to Australia because we are an energy-intensive economy—we do have a lot of coal. But at the minimum we ought to ensure that other countries are in lock-step, otherwise industries here will disappear into other countries which are not imposing that cost.

Senator EGGLESTON—That is true for energy-intensive industries, and that is a serious matter. The government in this paper has increased free credits to these industries. Do you think that what these amendments propose is enough to protect our emissions-intensive industries from going offshore?

Dr Moran—They certainly do not—and it does not seem to me that they are either. If the major users of energy have to incur a cost or a doubling of the price of the energy—even if energy is 20 per cent, and it is rather more than that in the case of aluminium—then they would not be competitive and they would move offshore. Even quite small changes in price do cause firms to move offshore, as we are seeing in terms of all

the globalisation debates over industries, Adidas, Puma and organisations like that moving where they manufacture their shoes from one country, Indonesia, to Vietnam et cetera on the basis of quite small changes in costs. That is the sort of reality of the world economy as it is now.

Senator EGGLESTON—The coalition feels very concerned that here we are going down the road of an ETS when some sort of different scheme might be more appropriate for a small country, as you said, which is only equivalent to one per cent of the world's GNP and 1.4 per cent of the world's emissions. It seems to me that we may find ourselves in a situation where we set up an ETS with high carbon costs and nowhere to trade those costs off. What would you consider to be an alternative to that which might be effective?

Dr Moran—I think that the best alternative would be to prepare along the lines that the government, and before that, the opposition, was being prepared to undertake measures should these be the measures which are adopted in the world forums. I think that behind your question is the inference, which I agree with, that Australia doing it alone is pointless. Not only are we relatively trivial in terms of the size of Australia's economy, but certainly if we did it alone there would not be any reason why others would not simply take up the slack. In other words, if the aluminium industry was closed down in Australia, it would reopen in the Persian Gulf or the ex-Soviet Union where there is at the present time not likely to be any carbon tax.

Senator XENOPHON—Dr Moran, if you assume that there is a public policy imperative to reduce greenhouse gases, what do you say is a better alternative to get the same public policy objective in terms of reducing carbon pollution?

Dr Moran—The best way of doing it, if there is a public policy imperative, is either a cap and trade, or a tax. It does not matter which way you go—they are both market instruments. The way you would not go is by having a detailed industry-by-industry or emission-by-emission procedure because that would not allow market mechanisms to give you any more efficiency. Whether you go a cap or a tax—and there has been a bit of a debate about that—really depends on how you see your preference for existing emissions compared to new emissions. With a cap and trade, in the European style anyway, you allocate your emissions to the existing producers of those emissions and allow them to trade. That leaves them virtually whole in terms of the costs to their shareholders et cetera, but it does incur costs the newcomers. If you have a tax then, arguably, you are expropriating the shareholders of the existing industries but you are protecting your newcomers. Either a cap and trade, or a tax will give you the best policy outcome if there is that policy imperative.

Senator XENOPHON—What would you do to improve the design features of the current scheme in terms of minimising the impacts that you are concerned about but still trying to achieve the same public policy outcome?

Dr Moran—I do not think that it is possible to do that. I do not think that you could minimise those costs—or you could minimise the costs insofar as, if there is a policy imperative, you are going to have to have a tradeable system, either a tax or tradeable rights. But certainly there is no escaping the costs whichever route you go by.

Senator PRATT—I want to begin by asking you whether the Institute of Public Affairs receives any donations or funding from resources companies—petroleum companies—or any other entities that will be liable under the CPRS.

Dr Moran—The answer is that I am not fully aware of what our funding is. But I can tell you in broad terms that we receive about \$1½ million, which is pretty small. We receive funding from a wide group of people—I think about 4,000 people—who give us some money. Probably the majority of that is from industry firms. I do not know what the percentage would be of energy firms. One aspect which I am closely associated with is something called the Energy Forum, where we bring together firms in the electricity and gas industries basically to hear from dignitaries and officials and politicians et cetera.

Senator PRATT—Would you be able to answer that in more detail on notice? We have clearly had other witnesses who have written reports and commissioned evidence on behalf of other organisations so I would like some further information.

Dr Moran—No, we do not write reports on behalf of other organisations—

Senator PRATT—No, I understand that, but the point still stands.

Dr Moran—I think that our policy is not to say who our donors are in detail, for a number of reasons. One is because some nefarious people go after the donors and say, 'You are working with the Greens or the ALP or

whatever and you are giving money to IPA as well. Stop doing it, otherwise we will give you a bad press.' That has happened in the past. That is one reason we do not disclose.

Senator PRATT—But you have indicated there would perhaps be some gas and energy companies making donations.

Dr Moran—Well, yes, they are part of something called an energy forum. The energy forum is to do with the national market for gas and electricity. There are obviously implications for greenhouse, but it is basically about the national market for gas and electricity.

Senator PRATT—I want to ask you about your recent article for the *Australian*, where you have stated that formally announcing a total abandonment of the carbon trading scheme must be the next step and that Australia can never afford to carry such baggage. I note that Treasury modelling has found that the cost to the GDP of tackling climate change is about 0.1 per cent slower a year. Is that 0.1 per cent too high a price to pay to address climate change, especially when Australia is one of the countries most at risk from this phenomenon?

Dr Moran—The Treasury modelling, when you go out beyond a year, is very difficult; it is not very reliable. It does depend an awful lot on assumptions about new technologies that come in.

Senator PRATT—Say their assumption was correct. Would it be something that you supported? You say, 'Okay, that's an okay price to pay based on mitigating the risk of whether climate change is real or not'.

Dr Moran—Well 0.1 per cent per year over 50 years or something like that is five per cent of GDP. Is it worth taking the risk of that to avoid what you think—

Senator PRATT—Catastrophic climate change?

Dr Moran—It could be. It would depend on what your—

Senator PRATT—It could be?

Dr Moran—Of course it could be. It would be depend on what you estimate is of catastrophic. There are a lot of insurance policies that we take for remote risks, but we do not take every insurance policy, otherwise it would take up all of our income. Certainly, if in fact you believed the 0.1 per cent per year, then that would be more persuasive. However, you would have to say, 'Are you confident that we would not see the elimination of some of these industries'. Are you confident we could do that? The 0.1 per cent a year also depends upon people accepting a lower level of standard of living. Senator Cameron's workers would have to accept wage cuts, and willingly do so, or otherwise there would be—

Senator PRATT—Many are calling for much deeper cuts when you are talking about what is reasonable insurance. You said something along the lines of 'we do not insure against every risk'. But, frankly, that is not what this global agreement seeks to do; it is seeking to stabilise the global climate. Many climate scientists are saying that we might need to do more. Clearly we are not at the stage of absolute insurance against climate change, even with these policies in place.

Dr Moran—My point on this is that in order to achieve this, we have to do things which are barely conceivable. We have to find different forms of energy that are not carbon forms of energy. We will probably have to go nuclear, which is not very popular in this country, or accept a much lower standard of living. You might want to believe the 0.1 per cent a year over 50 years, and doubtless you have it if you have asked Treasury for the progression of that.

Senator PRATT—But in essence you support a market-based mechanism to achieve that. I cannot see how you can say we are just going to invest in a couple of super solutions and abandon a market approach to dealing with an issue like this.

Dr Moran—A market approach would throw up, presumably, a nuclear solution, unless there is something we do not know yet in terms of all of the gee whiz things that have not been discovered yet. A market approach without the government's intercession would result in that, which is a conceivable way forward.

Senator PRATT—And what kind of emissions target do you think we are looking at to achieve something like that?

Dr Moran—To achieve stabilisation?

Senator PRATT—Yes.

Dr Moran—The answer is basically we go from 16 tonnes per capita to three tonnes per capita—in other words: one-fifth of what we presently use.

Senator PRATT—And what is a reasonable target for Australia, for its contribution?

Dr Moran—If nobody else does anything, the reasonable target is nothing.

Senator BUSHBY—In an answer to questions by Senator Pratt, the issue of modelling came up. Earlier we talked about the potential for serious job losses in various industries. We have heard a lot about that. Just today we had the Minerals Council saying that there is potential for 23,500 jobs to go, mostly in Queensland, and we have had BlueScope and OneSteel saying that 12,000 jobs at the Port Kembla steelworks would be under threat. I could read you a list of multiple thousands of jobs, where industries have actually said, on the basis of their knowledge of where they operate, that jobs are at risk. But that is not reflected in the modelling. I tried to ask questions of the Treasury this morning. I did not get too far because we ran out of time, but the questions I did ask highlighted the fact that they were not predicting massive job losses in the hundreds of thousands, if you add them all up. How do you reconcile the industries that operate in their own areas saying what they say with Treasury modelling saying this?

Dr Moran—One of the aspects of general equilibrium modelling is that you ‘close’ it. The ‘closure’ assumes that you do not have any change in employment, so the Treasury model is based on no change in employment.

Senator BUSHBY—It actually has that as an assumption?

Dr Moran—Yes, virtually all models do. It is based on the idea that you do not have any change in employment. If you are reducing the wherewithal of the economies to produce, the slack is taken by lower wages. The normal way in which those econometric models work is essentially to assume that employment stabilises but real wages decline, so it still becomes remunerative to employ people.

Senator BUSHBY—That is not realistic, is it?

Dr Moran—I do not know. The sorts of industry submissions that you are getting have people saying, ‘This is my firm. This is what I would have to do. I would have to close this firm.’ It may be that all those people and those resources move to some other industry. Certainly that is the assumption of the modelling—that they do, at a given price.

Senator BUSHBY—But that is built in as an assumption rather than as an outcome of the model?

Dr Moran—Yes. That is the closure of the model, and then the model tells you where it thinks people will be employed in the different segments of the various industries.

Senator BUSHBY—We were also talking about firms moving offshore and, essentially, the carbon leakage issue. From what we have heard in evidence in this and other inquiries, firms choosing to go elsewhere to set up their operations is certainly a potential outcome. But aren’t there also other ways that carbon leakage can occur? There is a far more simple thing—that is, import substitution—whereby if you have those additional costs imposed on an Australian firm they become uncompetitive compared with imports that can come in from countries where they do not have the same costs imposed on them, and as a result the carbon leakage occurs not by an Australian firm actually pulling up stumps and going elsewhere but by them just becoming uncompetitive and moving out of that particular area.

Dr Moran—They are both carbon leakage. One is physically moving the factory; the other is where it erodes because another factory is more efficient or lower cost because it has not got the impost. They are both carbon leakage, but there are different ways in which that occurs.

Senator BUSHBY—The EITE assistance is supposed to address some of that. Do you think it does cover it or is there still potential for that to occur?

Dr Moran—Yes, I think there is. I do not think that anybody would doubt that. With the EITE, basically there is a 1.3 per cent annual reduction in the benefit that they get over time, so it does slow it down. There is no question about that. But the bottom line is that, unless everybody else has the same costs imposed, there is a cost differential and that will cause those facilities to migrate elsewhere or simply to close down.

Senator JOYCE—I see that Senator Doug Cameron is very interested to ask you questions, but they seem very hesitant to invite people such as Kate Carnell, from the Food and Grocery Council, along here so that they can give their evidence.

Senator CAMERON—Is this is a question or what? Is it a dissertation from Barnaby?

Senator JOYCE—He always interrupts when he knows he is wrong, so he interrupts quite a bit. He is a very rude man, Doctor. You just have to put up with him.

You do understand politics, Dr Moran, so I am interested in your views on the transition of the current Waxman-Markey bill. It is now out of committee. Now that it is going to go in, do you think that it is just going to wander through the rest of the political process in America without any changes by the time Copenhagen comes around and that President Obama will wander in like a knight in shining armour and all of a sudden global alchemy as we know it will change? I am asking about the political process, about whether you think the United States will fall into line with the Waxman-Markey bill. Or do you believe that the Republicans will probably want to change it a little bit?

Dr Moran—I think all members will probably change it. The only time we have had a vote on that in the US Senate—I think it was 48 to nil—was when they were not going to accept the Kyoto discipline.

Senator EGGLESTON—Forty-eight to nil.

Senator CAMERON—That was under George W.

Dr Moran—It was basically the Senate voting. There were no supporters for it then, possibly because it was under George W—in fact, it was not; it was before Bush. Essentially, your knowledge of the American political system is probably greater than mine. But the senators there have to confront the issue much more personally than perhaps is the case elsewhere. If you are a senator, whether a Democrat or a Republican, in Kentucky and a bill is going to close down a whole industry in your state you will be very concerned, whereas the party political lines here tend to be more national. We are finding—and I am sure you are seeing it as well—that not only are the Republicans, who are divided on this issue, as are the Democrats, but both of them, as they are coming closer, are now looking at this and seeing what the implications are for their constituents. I do not think anybody thinks that that bill will stay as it is at present. That is not to say that Mr Obama won't do—

Senator JOYCE—Finally, in this form of global climate alchemy, which has been proposed by Mr Rudd where he will change the climate of the globe by the domestic policy of Australia, have you ever known of any other economic views that Australia has purportedly expressed to the world that has changed the way the globe has worked? Have we ever had the capacity or global political weight to fly solo and infer a change in the way the globe works economically on any issue? We might have done so on minor issues, but have we ever done it on any major economic issue—that is, ipso facto, do you think the world gives a flying whatever about Australia's domestic climate policy?

Dr Moran—No, I really do not think so. Certainly, when I have visited overseas and talked about Australia's climate policy nobody has known anything about it. We really do not count—nobody has been discourteous—but why should we? We are not a very big country. It is most unlikely that people will say, 'Ah, ah, Australia has a great policy, we are all going to follow it. We are all going to go down that path.' I have never known that happen before. It is unlikely that we would have the ingenuity to formulate the hidden secret, which nobody else has yet found. But certainly it is not the case, as far as I can see, that major countries are looking at Australia and saying, 'That is the way to go, and we will follow.'

CHAIR—Is it not possible that other people in the world do not know much about Australia's climate change policy because we have only recently signed up to the Kyoto agreement and been a part of that world discussion about climate change?

Dr Moran—I think we were a part of that world discussion even when we were not signed up. We have had a Department of Climate Change, they wander around the world and go to all the conferences and we have the CSIRO doing the same sort of thing. So I think people are as aware now of Australia's climate change policies as they were then.

CHAIR—I think it could be argued that, as such, we really did not have a policy or a plan of action?

Dr Moran—Possibly, but I do not think that, simply because we have signed up, it markedly affects other people's knowledge of Australia's policy as it is—and we had a policy then of course

CHAIR—Thank you, Dr Moran, for coming in today. We thank you for your assistance.

Dr Moran—You are welcome.

[1.35 pm]

HARRIS, Mr Matt, Consultant, Frontier Economics

PRICE, Mr Daniel, Managing Director, Frontier Economics

CHAIR—Good afternoon. Nice to see you again, Mr Price. Mr Price or Mr Harris, do you have an opening statement you would like to make?

Mr Price—Yes. I was asked to come along and initially at least talk about the implications of the recent announced changes to the CPRS, which really are threefold, I guess: there is the delayed start by a year, a cap on the emissions price for a year and increased compensation for emissions-intensive trade-exposed industries. This could be very short. I do not think it fundamentally changes anything; it is just a way of managing the transition from where we are to where we need to be. I have no problem with managing transition at all—I think it is a wise move—but I do not think it fundamentally changes the scheme. The concerns I have spoken to you about before still remain. I still think that Australia deserves a modification of the existing CPRS. I do not think the CPRS needs to be changed completely. I really believe that the design can be refined to be far more effective and to far better manage the transition to a lower emission economy.

Just reflecting on the last question from Senator Joyce about Australia's prominence on the world stage, I was overseas at the time—actually, in China, although I do not profess to be—

Senator Cameron interjecting—

Mr Price—I am looking forward to it. I do not profess to be an expert on China, but I will tell you what I do know. Very interestingly, the delay was actually reported in newspapers in China, Japan, Korea and also in Europe. It was relevant to the international press—probably because of the fact that Australia had been so resistant to signing Kyoto. When the new government came in and were very committed to doing something it was quite prominent that there had been a delay. They did not read anything into it, but they were very interested in it. There was very little commentary on that other than just noting it.

It is probably fair to say that I do not have the same view as Dr Moran about Australia's irrelevance in the world. One area which I have had a lot to do with over the years has been electricity market reform. Australia was in fact a year ahead of the UK in spot electricity markets. The UK was a year ahead of us adopting the first one, but we thought about it earlier. There was a very strong interaction between the UK and us. That has provided very good early examples of how these markets work around the world. I know from my own experience that there has been a conga line of advisers coming to Australia over the last decade to see how we have gone about doing that. So Australia can play an important policy leadership role. That has always, in fact, been my concern about the effectiveness of the CPRS: if we do this badly, being an energy-intensive economy, there will be a lot of attention on how badly that has gone. As I have said to you before, I seriously believe that the CPRS in its current form potentially threatens the reputation for carbon emissions reduction schemes globally. It has always been my interest to make sure that that does not happen.

Senator JOYCE—Thank you very much, Mr Price. I noted you talked about the interaction between the UK and us in on the electricity market. It was precisely that: it was the bilateral interaction between two countries rather than the solo position of one saying, 'We are the Messiah. Follow us.'

Mr Price—I agree. There is no doubt in my mind that there are benefits to be had from coming to a good understanding of how these schemes could function and how they could be implemented to the benefit of the environment and to the economy. I am a big fan of making sure we get this right first time around. I think we would benefit by more interaction internationally.

Senator JOYCE—Do you think that, if this legislation gets rammed through before Copenhagen, the attendees at Copenhagen will take it as some sort of Messianic epiphany from Australia as to how the world should work?

Mr Price—Obviously I doubt that but, as I said before, I think Australia can make a valuable contribution, as any country can. It is more than just an intellectual exercise; it is an important thing for the globe to understand what the best policy response is. I cannot see why we cannot have an effective role in that. Australia generally thinks pretty clearly about these things. We think a pretty broadly about different policies. I guess my disappointment throughout the course of this debate is that there has not been enough consideration of the options—although, as has been claimed, there are very few places where there has been a good debate

about the alternative schemes and the effects and the ways in which we can mitigate the effects of introducing these schemes.

Senator JOYCE—The first thing I want to touch on is that I remember watching an episode of *The Simpsons* once and they had this modelling of Lisa's teeth and what would happen if she did not see an orthodontist. They had her teeth growing through the roof of the house and out into the garden. What occurred to me is how horribly wrong modelling can go for the uninitiated and where it all ends up. Do you still see those issues present now, where people have a model and they plug-in their figures and prove from that, for example, that England will sink under the weight of people by the year 2010—as it was supposed to according to the Club of Rome—or whatever it was? Fortunately, it did not. In fact, the population started going down.

Mr Price—I think I have said in this forum before that I am very sceptical of modelling generally. We do that all the time and I have a healthy scepticism of how to use the results. We are very careful about how we use models and particularly models performed by other people where there is greater uncertainty. Models are clearly just a very crude guide at best—economic models particularly but I think the climate change models and other scientific models where there is a lot of uncertainty have the same sort of characteristics.

Senator JOYCE—How do you feel that Treasury has gone in assessing the short- to medium-run adjustment costs in where we are going with this ETS?

Mr Price—I do not really know what you mean by, 'How do you think they have gone?'

Senator JOYCE—In your experience of Treasury, do you think they have proven themselves to be a capable assessor of the modelling critique that is required to show the effects on the economy? It was in only February that they were telling us that the \$200 billion facility would be drawn down from our own budgets in 2013 and 2014. You would think that they would understand that hopefully far better than they understand climate. So what reliance do you think you can put on Treasury modelling and on the modelling that has been put around domestically about where this is all going to end up?

Mr Price—The modelling exercise that Treasury has undertaken they reported as one of the most ambitious, detailed and comprehensive that has been done. That is probably true. I do not doubt that. But it depends on how you use these models. If you use them as a way of trying to establish a precise estimate of how things are going to look in the future in very uncertain systems, that is a bad use of those types of models. If you use those models to explore the relative effects of different policies, I think that is a sensible use of those models. I would not criticise Treasury for the quality of the model they have used. I guess I would take them to task over the way in which the results have been applied.

Senator JOYCE—The big thing I would question is: has the Treasury, to your knowledge, modelled a go-it-alone scheme where Australia wanders off into environmental 'nirvanaville' by itself with its own ETS while everybody else sits back and watches?

Mr Price—I do not believe so. I have been asked this question before and I do not believe they have undertaken that modelling exercise. You might be interested to know that, with the type of model that they used, if they did conduct that type of modelling exercise it would not have actually come up with a very different conclusion. That may sound surprising, but the reason it will not come up with a very different conclusion is that these types of general equilibrium models which Dr Moran referred to before assumed that the economy is almost infinitely flexible and responsive to changes in prices and resource costs. Particularly in light of the assumption that the model has to do what it does to an economy to achieve full employment, it just moves people and resources from one sector to another and you end up with almost the same result. That sounds counterintuitive.

Senator JOYCE—I just want to talk about the regional issue there. The model still assumes full employment; therefore it assumes the transferability of the employment workforce from Mackay to building wind chimers in Nimbin.

Mr Price—That is not to suggest, though, that these models do not actually indicate regional effects. Some studies that we did before were widely reported in terms of the regional effects of these types of schemes. Even if you have the modelling that I think was reported by the Minerals Council in the paper today, which talks about there being an aggregate effect and which talks about a loss of jobs, you have to understand that that does not necessarily imply that employment and absolute value are going down; it is just that the growth of employment is lower than it would have otherwise been. So, on the one hand, you have the government saying, 'Our modelling shows that employment will grow,' and, on the other hand, you have the Minerals Council saying that employment will shrink. They are actually saying the same thing but reporting different

numbers, so you have to understand that. But, even if our aggregate employment stays the same under an emissions trading scheme, there will be regions which involve very carbon intensive activity which will be in significant decline.

Senator JOYCE—Where are those regions?

Mr Price—It is not hard to imagine: wherever there is major industrial activity.

Senator JOYCE—Such as?

Mr Price—Central Queensland, the Latrobe Valley, the Hunter Valley, the Kimberleys—anywhere that you have major energy using, particularly industry. Coalmining is an example. Of course—and I have said this before in this forum—if you did not have an adverse effect on those regions, the scheme would not work. You have to actually cause a reduction in those industries to achieve a reduction in emissions. It depends on what the government's policy objective is. That may make sense if they can manage the structural adjustment from one industry through to another and manage the flow of resources from, say, Central Queensland to South-East Queensland, where new jobs are found for the green industry.

Senator JOYCE—Can the model specifically predict that, if we shut down coal jobs in the Illawarra, Mackay, industrial cities such as Gladstone, the Latrobe and the Hunter Valley, those jobs might be recreated in new, green jobs but they might be created in new, green jobs overseas?

Mr Price—If you let the model do that—and I think a significant part of the additional work that Treasury did was linking Australia with the rest of the world, which is critically important for an emissions trading scheme. A lot of that is just not reported because not many people find it interesting, except for other economists. Once you have that linkage between the domestic economy and the international economy, a model can explore the movement of production jobs to other parts of the world. But, even then, that is a very crude estimation, because the rest of the world is generally characterised by a handful of economy types rather than individual economies.

Senator JOYCE—We could end up, Mr Price, with the ridiculous situation where we cannot move the coalmines, so the coalmines close down, and then a country without an ETS, such as China, starts producing the photovoltaic cells to send back to Australia, so it is an all-sum net loss across the board for Australia. You export your jobs; you import the product and close down your mines.

Mr Price—I have heard a few people say it will all be okay when the rest of the world gets on board with a scheme, but that is not necessarily the case for Australia because, if the rest of the world gets onto an emissions trading scheme, the first thing that they are going to do is stop buying things like coal. When you conduct these modelling exercises you in fact see a sharper economic downturn when you do a simulation where Australia goes it alone then the rest of the world comes on. In fact, you see a very sharp decline, because they stop buying things that we sell, like coal, for example. That has much bigger effects.

When you conduct a modelling exercise over a period—let us say from 2010 to 2020—where there is a lot of shielding going on of the effects, with or without the rest of the world, there are very muted effects on the economy, because they are basically charging on the one hand and taking it, and giving it back on the other. So a lot of the effects are muted. That is the whole idea of a transition from one point to another. As I have said before, I have no problem in doing that to get a policy accepted. But when you take that shielding off and simultaneously assume that the rest of the world gets on board with the scheme, Australia's fortunes degenerate very quickly. And that would be the case unless we had prepared ourselves in those 10 years to be able to exploit any opportunities that might come from the rest of the world adopting the scheme. It seems to me that the most sensible thing the federal government could be doing is putting money into preparing industry to be able to take advantage of those opportunities. Certainly that is what the government is claiming at least part of the policy is about.

Senator JOYCE—I just want to go to one technical part which is of interest to me, and that is part 3 division 6 of this legislation, which talks about the transfer of liability within joint ventures. Are you aware of this section?

Mr Price—No.

Senator JOYCE—Have you had a chance to have a look through the 1,300 pages of these 11 pieces of legislation?

Mr Price—Not in detail, no.

Senator JOYCE—You are a very astute person, Mr Price. How much time do you think you would need to go through this in a forensic way so as to show the Australian people the respect that you understand it enough to comment on it and that therefore the Senate has the capacity to find out from you the information that we can put into a report? How much time would you need?

Mr Price—Well, I have been asked to do that and I think it will take a couple of months. ‘Astute’ I am maybe not, but I am familiar with emissions trading and particularly the sectors that it mostly affects—I am very familiar with those sectors—and it will take me probably a couple of months to do that.

Senator CAMERON—Thanks, Mr Price. I want to deal with some of the issues Senator Joyce has raised and some of the fundamentals that he has laid as the basis of his questioning. I think he is morphing into Tim Fisher the more I hear him!

Senator JOYCE—Who are you referring to, Senator Cameron?

Senator CAMERON—I think you are morphing into Tim Fisher.

CHAIR—Can we get on with questions for Mr Price.

Senator JOYCE—*Extraordinary Popular Delusions and the Madness of Crowds*, a la Senator Doug Cameron.

Senator CAMERON—All of the questioning that Senator Joyce has raised talks about coal mines closing down and the industry closing down. None of the analysis of Treasury goes to the issue of the coal industry closing down. It actually says there will continue to be substantial growth in the coal industry, but it may not grow as fast as if we did not have a scheme in place. Do you challenge that fundamentally?

Senator JOYCE—No, you challenge that, Senator Cameron, because they are your workers who are about to lose their jobs.

CHAIR—Senator Joyce!

Mr Price—I know that Treasury say that, but there is not sufficient detail to be able to confirm that. In our own modelling we find that, in certain sectors, including mining, there are three categories. I will talk generally first and then answer your question about coal. There is the category of both regions and sectors that would be in decline in any case, and an emissions trading scheme just makes that worse. There are sectors that would not grow but now are in decline. And there are sectors that would be growing rapidly but not as fast. Coal mining could fall into any one of those categories, depending upon the nature of the resource, where they are located and who they sell to. So I do not think you can generally say whether a coal mine will close or not. Certainly there will be some coalmines that continue to grow but not at the same rate, and there will be some coalmines that become marginal and, given that they face an international price, will just become uneconomic. I think there would be a few categories of those types of mines.

Senator JOYCE—It sounds like the answer is yes.

Mr Price—It is yes and no because it depends very much on the resource and who they sell to—which is related to the first point.

Senator CAMERON—Is it appropriate that a price signal be sent to the coal industry?

Mr Price—I think it is appropriate. If your policy is designed to reduce emissions and the world community wants that I am very strongly in favour of using price signals to do that. It is my natural tendency as an economist to want that. If coal is part of that—and I think it is important to have as much coverage of emissions-intensive activity as possible to reduce the cost of achieving that outcome—a price should be part of that. I have never taken exception to that as a principle; my main concern has really been about the form of the scheme and making sure that you do not crater the Australian economy and give emissions trading a bad reputation so that it gives reason for people around the world not to put it in place.

Senator CAMERON—You say that the government’s scheme has not fundamentally changed, but there are a number of changes, including broadening our target to 25 per cent based on certain conditions. Are you aware of those conditions?

Mr Price—Yes—broadly, in relation to what happens with the rest of the world and what other trading nations do.

Senator CAMERON—If we meet those commitments—if the government says, ‘That’s our commitment; that’s where we stand’—that takes a lot of the doom-and-gloom argument away from Senator Joyce. We would not be acting unilaterally and there would be conditions placed on our actions. Isn’t that the case?

Mr Price—Yes. As I said before, it is not clear that having the rest of the world do this sooner rather than later is necessarily a good thing for Australia. It actually makes it harder for Australia to transition from where we are to a much lower emissions environment, because we are an energy-intensive economy. The first thing that people will do is reduce their demand for the things that we sell overseas. I know it sounds perverse, but earlier action by the rest of the world community actually places us at a disadvantage in one sense.

Senator CAMERON—But there is no analysis I have seen where, no matter what happens, coal's international use will reduce significantly.

Mr Price—I think that is probably a reflection on the fact that most people do not think that a lot of our major buyers will introduce schemes and think, therefore, that the demand for our energy-intensive goods-and-services exports will not change. I think that is a reflection of that.

Senator CAMERON—Do you still support the baseline-and-credit type approach as more effective?

Mr Price—I have always been characterised as a baseline-and-credit freak.

Senator CAMERON—I did not say that!

Mr Price—I am putting words in your mouth so you can throw them back at me later! What we have been supporting is, in fact, an emissions-intensity arrangement, which is sort of a halfway house between the cap-and-trade and a baseline-and-credit, and the reason why is that it does a few things. It provides a far more stable carbon price, and that is really critical to these schemes because you will only reduce emissions by investment. This is a policy that can only be achieved by massive and ongoing investment.

Senator CAMERON—But why does no-one else agree with you? Why are you isolated in that view in Australia and internationally?

Senator JOYCE—How can you say that?

CHAIR—Senator Joyce, you have had a long turn. Senator Eggleston, if we make good progress you will also have a long turn, so can we stick to answering the question?

Mr Price—It is interesting; when you look at the CPRS, it is in fact a mutant version of an intensity scheme. The way the scheme works is it charges every tonne of emission and then hands back credits on the basis of intensity by sector. That is exactly what an intensity scheme does, but the key difference between what the CPRS is recommending and what we are is that ours does not involve the massive churn of revenue between industry and government.

Senator PRATT—That has been contradicted by other witnesses.

Senator XENOPHON—I will disclose again that I travelled to the US and Canada with Mr Price earlier this year. I do not think he has forgiven me for all the Greyhound bus trips I dragged him on! Mr Price, one of the criticisms of an emissions intensity approach is that you cannot get an absolute cap and you do not get the certainty of reduction in emissions compared to what has been proposed by the government. What do you say about that?

Mr Price—Let us presume that I accept that the CPRS has a hard cap in it—but I will come back to that. Between these two schemes it is a choice between a hard cap and a volatile price, which is the CPRS, or a more stable price and a floating cap but the target is achieved over time. If you start with the principle that this scheme will only be effective if you get the investment, the only way you are going to get investment on an efficient and timely basis is if people can have a good sense of what the longer term price will be and the certainty of that price. So the intensity based scheme gives a far more stable, predictable price and therefore it is much easier to make the decisions about investment in that context. For that reason alone, I think you would choose an intensity based scheme, because it will deliver the same greenhouse gas outcomes over time—not necessarily year on year but certainly over time—and you will do that at much lower cost than you would under the CPRS.

Senator XENOPHON—When you say 'over time', is this over a five-year period or a 10-year period or what? And you alluded to the fact that you do not necessarily accept there is an absolute cap with the current CPRS.

Mr Price—That is right. You may not achieve the cap in a particular year, but you will achieve it over whatever timescale the intensity target is established. But let me go to the other point, about the supposed hard cap in the CPRS. The changes that you have announced basically are a response to the politics of the harsh outcomes of the CPRS. The moment that you start to cap the carbon price below cost, that is an effective

reduction in target. The moment that you delay the commencement of the scheme because of the harshness of the transition, that is an effective reduction in target. The moment that you take into account the effects of voluntary reductions in the target, that is a change in the target. The CPRS already is racked with uncertainty about the target. The moment that you put in a gateway, there is uncertainty about the target. So there is no sense in which the CPRS actually delivers a hard target. It is the most soft target of any scheme in the world, almost.

Mr Harris—There is also the aspect of international trading. You do not have that certainty of domestic emissions in any case.

Senator XENOPHON—Why does this mute the price of electricity compared to a classic cap and trade? Are you saying that ultimately, whether it is over a five- or a 10-year period, you will still get the same outcomes in terms of reducing greenhouse?

Mr Price—Yes. In the supposed move to the hard cap, you are actually creating all of these carve-outs, which gives effect to a very volatile cap, to try and manage the price volatility. Why not do that far more directly with an intensity based scheme and still achieve the same outcome? Better still, because of the more stable price qualities of an intensity based scheme, you actually make it easier for investors to respond to that type of environment. The government will not achieve its outcome if it does not get the investment. It will raise the costs and prices for the Australian economy and make it uncompetitive if you put a lot more price volatility into it. It is a particularly important thing for investors where that price is actually dictated by a set of regulations—it is not dictated by economic fundamentals; it is dictated by regulatory settings. There is enough uncertainty of that price in any case. Why make it even more difficult for investors?

Senator XENOPHON—In terms of the Canadian scheme, it seems the Canadians will not go down that path because the US is going to go down another path. What is your understanding of that? To what extent is what you are proposing in terms of a hybrid emissions intensity with a cap and trade scheme compatible internationally with other schemes in terms of permits and credits and international trade?

Mr Price—There are two parts to that. One is in relation to the Canadian scheme and Canada's response to the US, and I will answer that first. As you well know, the Canadians have a very well developed, ready to go scheme which is an intensity based scheme. What was communicated to us by the Canadian government is that they are holding off on that because they are very concerned about the way in which the Americans will respond to the introduction of that scheme. It has been given a bad rap because of the way in which it was developed in the context of trying to preserve the Canadian oil sands projects.

Senator XENOPHON—The tar sands?

Mr Price—Yes, the tar sands projects in Alberta. That is really just the environment in which that policy was discussed, and I think you need to separate that from the actual underlying mechanics of that scheme. The Canadians are waiting to see what the US will do in order to be able to blend in with them because they are very worried about the threats they have received about a potential trade retaliation on Canada, particularly in relation to the tar sands projects. So you need to separate those two issues. Could you remind me of your second question, Nick.

Senator XENOPHON—The second question is: what is the international compatibility if you have a hybrid scheme in terms of being able to trade and in relation to permits and credits from overseas?

Mr Price—They are perfectly compatible. As I said before, there is a misguided belief that you have to have the same scheme to be able to be internationally compatible. That is not at all true. A tonne of emissions reduction under one scheme is worth the same as a tonne of emissions reduction under another scheme—the price will be equalised. In fact, you can have a look at the European arrangements, where you have both a cap-and-trade scheme and a baseline and credit scheme operating in the one market. They are two completely different schemes and now, through time, those prices are equalising. They are perfectly compatible; and an intensity scheme sits in between those two. There is no in principle reason why those schemes cannot work. We already see working examples around the world right now.

Senator EGGLESTON—Coming back to the changes in this legislation that we are talking about, I notice that the first review of the CPRS is in 2014, if this scheme is introduced. Do you think that is too far away to be reviewing it?

Mr Price—That is a good question. I had not really thought about that very much, so my response will be off the cuff and I might come back and revise it. This is in the realm of highly organised energy markets, in that there are very strict rules of engagement and price-setting rules. I was always in favour, going back 15

years, of having a review soon after that market started in case we got something fundamentally wrong. In fact, the Western Australian Labor government put in place an electricity market there which was very different from any other market in Australia and they required an annual review. In the first review, the regulator there took the view that there were signs the market may not be working quite as they intended but that the market should be allowed to continue on, and so they kept a watching brief over that. But let us say that there was a timed review in 2014. Governments do not just walk away and let a market fall apart. Almost certainly, any responsible government, if they saw something going fundamentally wrong, would probably step in and make a change. So I think it is probably a moot point as to whether it is a timed review or one that is ongoing, because governments generally are pretty responsible about these things.

Senator EGGLESTON—I guess if we put 2014 we would know what other, if any, countries were going to have an emissions trading scheme from which a carbon market was derived that we could trade into, wouldn't we?

Mr Price—Yes.

Senator EGGLESTON—So it would give us an indication of whether or not, as Senator Joyce would suggest, we were running off along a little fairytale pathway or whether we needed to revise the scheme that was put in place.

Mr Price—There are a few points to make about that. Firstly, as I have said recently, it is not necessary to have a common set of arrangements for us to be compatible with the rest of the world. We can think about a scheme that suits our own conditions. I have said before that I do not think it is even desirable to have the same scheme all around the world. It is probably more desirable to have schemes which are internationally compatible but bespoke for the circumstances in a particular country—and that is what I have been consistently arguing for. That includes transitional arrangements. For example, an energy intensive economy like ours does not want to go around destroying industry in a very cavalier fashion, because all that is going to do is shock international investors all around the world. They would be very reluctant to invest in an economy like Australia.

So we can have different scheme designs and different transitional arrangements, but it does not necessarily mean that we should have to wait for everybody to do something before we do something. And we can always modify a scheme through time as well.

Senator EGGLESTON—Basically this scheme is predicated on an international carbon market, isn't it? Some people have a lot of reservations that that will actually be established and we will end up carrying huge cost burdens from the carbon taxes imposed under this proposal.

Mr Price—That comes back to the idea that it is not mutually exclusive to have a scheme and be the only one in the world. That is the purpose of things like the shielding and transitional arrangements. The government has actually said in the CPRS that those arrangements will be in place as long as it is thought necessary or until others put another scheme in place. As a principle, I am supportive of that, but it actually creates a lot of uncertainty as well because, unless you are very clear about the criteria around when you remove those protections, you basically will not have people stumping up the billions of dollars of investment in infrastructure to meet that scheme if they think that, at a moment's notice, politics could conspire to take that compensation away. On the one hand you want to be flexible in your transitional arrangements; on the other hand you need to give enough certainty in price and criteria around transitional measures to encourage investors.

That is a very tricky line to walk and I do not think the CPRS has that right. In fact, the scheme that we have been promoting actually takes that issue off the table in that an intensity scheme gives a lot more certainty of price and, because it is not reliant on the federal government handing back money, that uncertainty is removed. So we could have a scheme which is more economically responsible and provides a lot more certainty around the form of compensation and a much more stable price. That seems a more appropriate model for a small, open, energy intensive economy like Australia—not the CPRS.

CHAIR—Thank you for appearing.

[2.13 pm]

BRADSHAW, Mr Michael, Senior Adviser, Department of the Treasury

DAVIS, Mr Graeme, Manager, Finance Strategy Unit, Business Tax Division, Department of the Treasury

McCREA, Mr Glen James, Manager, Indirect Tax Unit, Department of the Treasury

PARKER, Ms Cherie Rebecca, Analyst, Investor Protection Unit, Corporations and Financial Services Division, Markets Group, Department of the Treasury

CHAIR—Welcome. Would you like to make an opening statement?

Mr Davis—Yes. It might help the committee if I outline and clarify the areas of responsibility of the officers here today.

CHAIR—I am sure that would be useful. Thank you.

Mr Davis—I know that this morning Barry Sterland from the Department of Climate Change talked about what they were responsible for and what Treasury were responsible for in this legislation. I will not read that out again, but I will briefly summarise it. With respect to the people we have here today, I will just clarify this, the notice of this inquiry was pretty short. We put together the people we had available so that, even with the areas which we are responsible for, we may still need to take some things on notice because not everyone was able to be here today.

CHAIR—Certainly.

Mr Davis—The real essence is that we can cover the issues that relate to legislation and in particular the changes in legislation since the CPRS exposure draft bills went out as they relate to the areas where Treasury has primary responsibility for the legislation. Those areas are around the taxation of emissions units and the main changes there were around the income tax treatment to create greater flexibility in valuing emissions units held at the end of the income year. The second area is around eligible emissions units being treated as financial products for the purposes of the Corporations Act and the Australian Securities and Investment Commission Act. Essentially, there were no changes, as I understand it, between the exposure draft and what is in the legislation now. The third area is around the technical details or the technical aspects of the fuel tax adjustments. Correct me if I am wrong, Glen, but I understand there was not an exposure draft of that, is that correct?

Mr McCrea—A draft was placed on the Treasury website for consultation purposes. That did occur.

Mr Davis—The committee may not have looked at that previously

CHAIR—Thank you.

Senator JOYCE—I want to go to part 4, division 3 of personal property and capital gains tax events. Will the decision of units being deemed to be personal property have an effect on the capacity to have assets deemed that were real property to be non-real property assets and therefore given exemption from the capital gains tax act if they are owned by a foreign entity?

Mr Davis—There are a lot of steps in that. I think the best way for me to answer that is that I will take it on notice. There are a number of bits in it and I would just like to make sure.

Senator JOYCE—We know that the non-real property assets are a huge hole in the income tax capacity because if an overseas entity has a non-real property asset in Australia, they do not pay tax. This has the capacity to influence that and possibly take things from a tipping point over to where they are a non-real property asset if it is deemed to be that the permit is now personal property and non-real property. Therefore, there are definitely ramifications there for Treasury and I want to know about them. I am sorry that we have not got enough time, but that is not my problem.

Mr Bradshaw—I might be able to assist in the meantime, Senator. Australian emissions units, as you say, are personal property, but under the income tax law they are generally treated on revenue account by which we mean that a direct deduction is available and they are specifically carved out of the capital gains tax regime.

Senator JOYCE—Of course, so therefore we have the capacity to influence that. I want to know what effect is on Treasury and whether we have done any modelling on what the capacity is of influence on this on the revenue taken in Australia by people who could have been deemed to be greater than 50 per cent real

property then saying, 'We can now morph this into being less than 50 per cent real property so we are now exempt.'

Mr Davis—As I said, Senator, we will take that on notice.

Senator JOYCE—Okay. With respect to part 25, clause 353 can you just quickly take me through the measures that were considered there? It is to do with independent reviews on a five-yearly basis.

Mr Davis—Are you referring to the main bill or the consequential amendments bill, Senator?

Senator JOYCE—I imagine this would be in the consequential amendments. It is in the 11 schedules that we have before us here at the moment.

CHAIR—The secretariat advises that it is at page 403 of the main bill.

Mr Davis—I think that is a matter for the DCC.

Senator JOYCE—It is about assistance and you are Treasury. I want to know what the cost is to the Australian people of the change in the decisions on assistance.

Mr Davis—Senator, I tried hard to explain when we started what I could and could not talk about.

CHAIR—Senator Joyce, we will put that on notice for the Department of Climate Change.

Senator JOYCE—Then I will go to part 3, division 6, on the transfer of liabilities. I want to know: what is the effect of the lack of capacity in joint venture agreements with our not being able to apply a charge on foreign entities, what is the extent that we can charge on foreign entities, and what are the ramifications to Treasury of that?

Mr Davis—Once again, they are not provisions we are responsible for, but we can take that on notice and either the DCC or ourselves will get back to you.

Senator JOYCE—These are the problems when they rush this stuff through. Have modelled this on a go-it-alone alternative?

Mr Davis—I cannot discuss it. I am not responsible for the modelling. I am not quite sure which bit of the modelling you are talking about.

Senator JOYCE—If Australia goes it alone, has Treasury modelled this on a go-it-alone premise?

Mr Davis—As I discussed at the start, that is not our area. I can take that on notice.

Senator JOYCE—Okay. What are the differentiations for these new 11 schedules? What are the differentiations to regional Australia from this?

Mr Davis—I think that is a question for the DCC.

Senator JOYCE—With the emission reduction comparisons, the percentage change from 1990 to 2020, I noticed that the USA's was based on—

CHAIR—Senator Joyce, is this about the tax treatment?

Senator JOYCE—Yes, it is. It is about the bill we are about to vote for.

CHAIR—Senator Joyce, we had the Department of Climate Change appear earlier today.

Senator JOYCE—Who I had four minutes to speak to.

CHAIR—Yes, and your colleagues had the remainder of the time. As has been explained this morning and just now today, Treasury are not here today to discuss general issues. They are here to deal with the tax treatment.

Senator JOYCE—And there are people out there in Australia who are very interested in what actually happens here. That is what we are paid to do.

CHAIR—If you want to put these questions on notice for the Department of Climate Change, we will put them through the secretariat to the Department of Climate Change, but it is using up time to ask questions that—

Senator JOYCE—Oh no, it is not using up time. It is asking questions that are unable to answered, and not by fault of the Treasury but by fault of the truncating of this process. There are people doing their homework in order to ask the questions. It is just that there are no people capable of answering them. It is not because they are not capable; it is because they have not had the time.

Mr Davis—Senator, the fact that I cannot answer the questions you are putting to me does not mean that there is not someone who is capable of answering them.

Senator JOYCE—Some of them were specifically in the areas that you said at the start that you had covered. What—in your view, from the areas that you do cover—is going to be changed because we have delayed this for one year?

Mr Davis—I do not think that our legislation needs to change at all on that basis.

Senator JOYCE—Is there any cost to it in any form whatsoever that you are aware of because of the delay of one year?

Mr Davis—If you want me to talk about what needs to change in the legislation, I can do that. I am not here to do costings; I am not here to do modelling.

Senator JOYCE—I might come back later on. It just goes to show the Australian people how ridiculous this whole process is.

Senator EGGLESTON—The coalition is concerned that this ETS scheme of the Rudd government has largely ignored the impact of the scheme on our competitiveness and jobs in the first 20 years of transition if our major competitors and trading partners do not reciprocate in establishing an ETS in a carbon market. The design of the Rudd government scheme assumes that our major competitors will move to put in place a major new tax on carbon in the early years. But suppose our major trading competitors do not do this? There appears, from what we can gather, that there has not been any analysis at all of the impact of a scheme such as the Australian scheme not having the ability to trade into a carbon market and reciprocal ETSs in other countries. I wonder why you have not tested that proposition as far as we know. It has been seven months since the Treasury modelling was released, but there is still no information that I know of about this scenario that would apply if other countries do not adopt an ETS.

CHAIR—Senators, we had the person from Treasury responsible for modelling this morning and a number of questions were asked of her. I repeat that this is about the taxation aspects, not general Treasury—

Senator EGGLESTON—I stand corrected them; my apologies. You obviously do not have the capacity to answer that question, so I will not proceed with it.

CHAIR—Are there any other questions?

Senator JOYCE—Maybe you would like to suggest some that we could ask.

CHAIR—Senator Joyce, as I said before, the Department of Climate Change will take questions on notice. If you provide them to the secretariat, they will forward them on.

Senator JOYCE—I am sure the Australian people are going to be fascinated.

Senator CAMERON—They would like to see you get your act together with their colleagues so that we can—

Senator JOYCE—It is your problem. It is you that has fallen over on this.

CHAIR—Senators! As there are no further questions, I thank Treasury for coming in this afternoon. If senators have other questions, I take it that they will put them on notice.

Committee adjourned at 2.27 pm