

JOINT SELECT COMMITTEE ON AUSTRALIA'S CLEAN ENERGY FUTURE LEGISLATION

Transcript and additional notes from Professor Ross Garnaut

Tuesday, 27 September 2011

Members in attendance: Senators Birmingham, Cormann, Milne, Pratt and Urquhart and Mr Bandt, Ms Burke, Mr Cheeseman, Mr Christensen, Mrs Gash, Mr Husic, Mr Tony Smith and Mr Windsor.

Professor Ross Garnaut

CHAIR (Ms AE Burke): I declare open this public hearing of the Joint Select Committee on Australia's Clean Energy Future Legislation in its inquiry into the clean energy bills 2011. The bills implement the government's decision to introduce a cap-and-trade emissions trading scheme, which will commence on 1 July 2012. For the first three years the carbon price will be fixed at \$23 per tonne of carbon pollution and from 1 July 2015 the price will be determined by the market. The legislation provides that the carbon will be paid by liable entities, which includes those that have facilities that emit 25,000 tonnes or more of carbon pollution a year.

Before introducing the witnesses, I refer members of the media who may be monitoring this hearing to the need to fairly and accurately report the proceedings of the committee. I welcome Professor Ross Garnaut to today's hearing. Although the committee does not require you to give evidence on oath, I advise you that these hearings are legal proceedings of the parliament and therefore have the same standards as proceedings of the respective houses. Before we begin with questions, do you have an opening statement that you would like to make today?

Prof. Garnaut: Yes.

CHAIR: Can it be short? I am going to ask that of everybody. Please accept my apologies.

Prof. Garnaut: I see the current task of this committee as having historic importance. Climate change is one of the greatest challenges to human civilisation since its emergence. Developing policy to deal with it well while maintaining the global economic development upon which the advance of our civilisation depends is a diabolical policy problem. There is no chance of success unless all substantial countries—first of all the developed countries with high greenhouse gas emissions per person—do their fair share in a global effort. In my view the policy that underpins the draft legislation currently before the parliament allows Australia to do its fair share at reasonable economic cost and at far lower economic cost than the main alternative that has been put forward in public discussion. I draw attention to the sound arrangements for governance and for the land sector in particular.

It will be a historic achievement of Australian democracy and of this Australian parliament if the draft legislation becomes law and then moves from law into practice. It will be historic for more than the importance of the issue and the difficulty of the task. Australian public discussion of climate change policy over recent times has been the locus of more elaborate and extreme distortion reality and abuse of truth than I have seen in an adult lifetime of interest in public policy. The political culture of our generation of Australians risks condemnation in history for the corruption of our democracy embodied in this distortion of reality and abuse of truth. It will, however, be a vindication of our Australian democratic traditions if sound policy is now passed into law, despite the current obstacles. I myself played an early role in the policy process and the public discussion as the author of the 2008 Garnaut Climate Change Review and the 2011 update of the review, and as an independent expert in the parliamentary Multi-Party Climate Change Committee. That independent and official role ended at the end of June and I am before the committee today as an independent Australian.

Today in my introductory remarks I will focus especially on international dimensions of Australian climate change policy and I will seek to correct some of the most egregious distortions of reality and neglect of truth in this year's public policy discussion. I present for your records my *Update paper 2: Progress towards effective global action on climate change* and my *Update paper 3: Global emissions trends* because they are both relevant to my remarks this morning. I also draw your attention to chapters 3 and 4 in my final report—'What's a fair share?' and 'Pledging the future'—and I will place the original review before the committee.

CHAIR: We will accept those as exhibits. Thank you, Professor.

Prof. Garnaut: I draw the committee's attention to seven matters relating to international effects of climate change policy discussion, on which there has been distortion of reality and abuse of truth. First, I would like to draw the committee's attention to false statements, made prominently in the public discussion, that international purchase of permits will reduce government revenue. The truth is that Australian permit sales will not be reduced in volume by international purchases, so the revenue will not be affected in that way. Once we have international trade the price will be set internationally and so the price will not be affected by the volume of international trade in permits.

Secondly, I would like to draw the committee's attention to a rather specific distortion of things I said in *Update paper 3*. In this paper I present a very careful recalculation of what global emissions would look like in the absence of any mitigation policy. In particular, I comprehensively reworked the outlook for emissions growth in the three biggest developing countries—China, India and Indonesia—in circumstances in which there was no action or mitigation policy on climate change. I said very clearly, there and in the final report, that those projections were what would happen if there were no policy action. I also said that, fortunately, that will not happen, because there is policy action. Yet prominently in the public discussion there has been use of those projections of mine, attributed to me, in which I said very clearly, 'These are what will happen if there is no policy action, but they will not happen because there is policy action.' They were presented prominently in public discussion as my views on what would happen unconditionally. I would like to correct that for this committee. Thirdly, it has been said prominently in the public discussion that the policy that is embodied in the legislation requires all countries to have international trade in emissions permits from 2015 for us to get gains from trade. That is simply not true. I invite the committee to examine chapter 3 of my final Update report, drawing particular attention to a paragraph that specifically addresses this matter, on page 41, commencing:

Not all countries would benefit to the same extent from international trade in entitlements, and not all countries need to join in for large gains to accrue to participating countries.

I would like to correct the false statements in much of the public discussion that you would need to have participation of all countries in international trade to get the gains from trade that underpin the logic of the policy.

The fourth matter I would like to correct concerns the frequent assertion that is made without analysis in the public discussion that in following the course proposed in the legislation Australia will be doing more than its fair share and imposing unnecessary costs on itself in circumstances in which others are doing relatively little. I spend a considerable amount of space in *Update paper 3* and in the final report on discussing what is a fair share.

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Additional notes from Ross Garnaut inserted here at the Chair's request:

Update Paper 2 and the Update Final Report discussed at length the assessment of a "fair share". For good reasons, the international community has settled on assessing "fair shares" in terms of absolute reductions in emissions in developed countries and reduction in emissions intensity of production in major developing countries. The assessment of what is a

“fair share” of emissions reductions in Australia must be made within a framework for allocating responsibilities across the global community that has a reasonable chance of wide acceptance. Within the frameworks explained in the 2008 Review and 2011 Update, and within any of the alternatives that have been put forward in public discussion in Australia and elsewhere, there is no way that the unconditional targets for emissions reductions set out in the legislation can be seen as more than Australia’s fair share.

It has been common to assert in particular that Australia’s effort under the legislation would be excessive compared with that of the China or the United States, the world’s two biggest emitters of greenhouse gases in absolute terms. The absence of economy-wide carbon pricing in China and the United States is usually put forward in support of the assertion.

China’s ambitious targets for reduction in emissions intensity are being achieved through a wide range of policies: the forced replacement of small and environmentally damaging power generators and other emissions-intensive plants by larger and more environmentally and economically efficient capacity; the focus on emissions-reducing activities in the stimulus packages after the Great Crash of 2008; the embedding of emissions intensity reduction targets in the Twelfth Five Year Plan; fiscal discrimination against emissions-intensive activities; denial of power supply increases to and imposition of higher electricity prices on particularly emissions-intensive industries and plants; fiscal incentives for low emissions activities; and now the introduction of carbon pricing on a trial basis in some provinces and municipalities.

Some of these measures have achieved reductions in emissions intensity at low or even negative cost, while others have been extremely expensive. The combined effect of the measures has been to put China in a reasonable position from which to deliver the 40-45 percent reduction in emissions intensity of output from 2005 to 2008 to which it is committed.

The United States has placed before the international community an objective of reducing emissions by 17 percent from 2005 levels by 2020—corresponding to a 15 percent reduction on 2000 levels. It is making progress towards this objective through a combination of regulation of emissions and energy use at federal and state levels; fiscal support for deployment of emissions-reducing technologies; the introduction of carbon pricing in some states and regions; replacement of coal by gas power generation, supported by huge increases in reserves of shale gas; and a range of regulatory and political constraints that have made it impossible in practice to obtain permits for new coal-based power stations. A slower economic growth trajectory has also constrained emissions growth.

The United States seems to have passed the peak of its emissions, which is more than can be said about Australia. The 17 percent reduction of emissions by 2020 is not beyond America’s reach.

It is simply false to assert that Australia would be doing much more to reduce emissions below what they would otherwise be through the legislation before the Parliament, than China and the United States are doing through a range of mechanisms. Australia’s active

policy interventions would be achieving emissions reductions at lower costs than corresponding interventions in the United States and China.

Here I draw Senators' and Members' attention to Chapter 3 of the Update Final Report, and in particular to the paragraph commencing "Some Australians..." on p47.

A fifth distortion of reality that has entered public discussion is the assertion that the broad support across Australian business and major political parties for carbon pricing as late as November and early December 2009 was based on reasonable expectations of a binding international agreement on emissions reductions at the Copenhagen meeting in December 2009. The distortion says as well that these hopes were dashed by the failure to reach such an agreement at Copenhagen, and that the absence of such an agreement has removed the basis of support for carbon pricing.

The historical record shows that by the second half of 2009, long before the Copenhagen conference in December, there was no prospect of that kind of agreement. It now shows as well that since the Cancun conference of December 2010, there is an agreed international framework for mitigation that is stronger than anything that was in prospect in November 2009. The Australian legislation is calibrated well to what was agreed at Cancun.

A sixth distortion of reality that has been prominent in the Australian public discussion is that under the proposed legislation, the Australian carbon price will keep rising without limit, independently of what other countries are doing to constrain emissions. The truth is that international trade in permits from 2015 will link Australian prices to the mitigation effort in other countries.

Finally, I draw attention to an appalling distortion of reality and abuse of truth in relation to the policy of the United States of America and developments in the United States.

It has been common in the false Australian public discussion to assert that the absence of carbon pricing means that the United States is doing nothing to reduce emissions. I have already said something about the American reality. The analysis of United States policy and developments reported in Update paper 2 and the Update final report was based on close consultation with leaders of American Government, private analysis and business, including on far-reaching discussions with senior officials reporting directly to the President of the United States. The general story is that the United States government, having been blocked from economy-wide carbon pricing by Congressional politics, is seeking to do its fair share in emissions reduction in other ways. The most senior officials with policy responsibility in this area are clear that the cheaper and preferred option is carbon pricing, but that if this avenue is closed, others will be followed.

Australian proponents of the view that the United States is doing nothing, emphasise the positions of elements of the opposition to the United States Government that are seeking to block the President's policies in this as in many other areas. To assert that the policies of the opposition to the American President are the policies of the United States, is to abuse the truth.

End of additional notes from Ross Garnaut

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CHAIR: I think we would all probably agree that this whole debate has had a distortion—but that is my peculiar bent on it. I am going to hand over to Senator Milne, who has a question she would like to ask.

Senator MILNE: Since the release of the draft legislation, the exposure draft, there have been a number of comments from various places. Firstly, I would like your view on whether any of that criticism has changed the view that you held when we released the draft bills that an emissions trading scheme is the best way to address this problem and to allow for a scale-up in the level of ambition. Secondly, one of the specific criticisms has been from the coal fired generators, the supply association, complaining about the impairment of asset value across the electricity sector, in particular, in relation to the profitability of coal fired power stations. Could you comment on those two things please.

Prof. Garnaut: When the legislation came out I said that this was a good set of legislation that would allow Australia to do its fair share in the mitigation effort at reasonable cost. Nothing that I have seen in the debate since then has caused me to change my mind about that. On the views of the coal fired generators, I think they have been very generously looked after in this package. There may be some effect on asset value but it is not an established tradition of Australian policy, nor would it be a good tradition, for any change of policy that affects an asset value to lead to compensation for the affected asset.

Senator MILNE: In relation to that matter, as an economist in this sector over a period of time, would coal generators have known since the negotiation of the Kyoto protocol and the world moving under the UNFCCC that inevitably there will be carbon pricing and should that have been built into their projections over that period of time?

Prof. Garnaut: I do know that a number of major Australian businesses have been embodying a shadow carbon price into their calculations about business profitability for many years. At the time of release of my draft report for the 2008 review I was authorised by the chief executive of BHP to say publicly that that had been BHP's approach for a number of years. So certainly some Australian businesses have been working on the basis that the world will be moving towards costs of emissions and they have been embodying that in investment decisions. My own view is that it would have been imprudent for an emissions intensive business to take no account of the likelihood of the introduction of emissions pricing.

Mr CHRISTENSEN: Is it a distortion of reality to state that regional communities and industries are likely to become more vulnerable to the impacts of this legislation than urban centres due to their reliance on agriculture and other natural resource based industries and low levels of infrastructure stock?

Prof. Garnaut: I do not think that it is true in general that regional Australia will be affected more adversely. In fact, the exclusion of agriculture while other sectors are included in standard economic analysis suggests that there will be some boost to some kinds of agriculture. If it were true that carbon pricing affected the profitability at the margin of investment—in resources industries, for example—then that would increase the profitability of agriculture. So the exclusion of the agricultural sector may in fact introduce a relative benefit. In addition, the carbon pricing initiative and the opportunities for sale of land-based credits into the scheme, and therefore getting full value under the Carbon Farming Initiative, is potentially a source of very large revenue for rural Australia. So taking rural industry as a whole, I think it is unlikely that there will be relatively large effects. There may very well be some rural communities in which the effects are relatively large.

Mr CHRISTENSEN: That is an interesting response, because I was quoting chapter 16 of your report, 'Sharing the burden in Australia'. Those were your words. I will go on, and you are quite clear that agriculture is exempted. You say:

From the commencement of an emissions trading scheme, costs of agricultural inputs—electricity, liquid fuel and fertiliser—will rise. This will particularly affect parts of the sector where energy costs and energy-dependent costs are a large proportion of total costs. Do you stand by those statements?

Prof. Garnaut: Yes, that is quite true and not at all inconsistent with what I said before. They relate to some particular costs, but one has to look at the overall picture and some particular costs. That takes no account of what economists call the general equilibrium costs, through the exchange rate of putting the charges on other sectors but not on agriculture. And it takes no account of the carbon farming initiative. That is from the 2008 report, I think. At the time of the previous report, neither my report nor the subsequent legislation had the same arrangements for rewarding farmers who capture carbon in their soils, pastures and woodlands.

Mr CHRISTENSEN: Is it a distortion of reality to state that carbon dioxide and emissions in China will increase for the foreseeable future? I am not talking about intensity; I am talking about emissions.

Prof. Garnaut: I say very clearly in my report that there will be an increase in emissions in China for some years—a very much smaller increase than would have been the case under business as usual.

Mr CHRISTENSEN: Still a large increase, you would say?

Prof. Garnaut: Still a large increase, and I document that very clearly in paper No. 3 and in my final report.

Mr CHRISTENSEN: Is it a distortion of reality to state that in India carbon dioxide emissions will increase for the foreseeable future as well?

CHAIR: Why is it a distortion? I am a bit confused.

Mr CHRISTENSEN: I am just using the words that Professor Garnaut has used.

Prof. Garnaut: You use the words 'foreseeable future' as well there. In India, for quite a while, total emissions will increase. In China they will not continue to increase for the foreseeable future. I foresee a time when Chinese emissions will fall absolutely.

Mr CHRISTENSEN: Is it a distortion of reality to state that in the United States of America there will be no nationwide carbon price?

Prof. Garnaut: There will be no carbon price nationwide; I have said that very clearly. But there will be very strong policies of other kinds and it is the reality that in the United States they have probably now passed a peak in emissions, which is more than you can say about Australia.

Mr CHRISTENSEN: My final question goes again to comments that you have made in the past. Do you stand by this statement:

... imposing a carbon price in Australia ahead of similar carbon constraints in our trade competitors ... could result in some movement of emissions-intensive, trade-exposed industries from Australia to other countries that impose less of a carbon constraint. This could result in an increase in global emissions—in the event that the activity moves to a country that uses a more emissions-intensive production process than Australia.

Prof. Garnaut: Yes, I stand by that. The relevant points there are that I talk about carbon constraints in other countries. You can have carbon constraints without carbon prices. In fact, the carbon constraints through regulatory processes that have been applied in China and the United States in many cases impose more costs on businesses and households than carbon pricing to achieve equivalent reductions in emissions would.

Senator PRATT: What is the abuse of truth that you spoke of in your opening remarks?

Prof. Garnaut: There are quite a number of matters. I went through some of them. I was especially drawing attention to international matters. Strong assertions have been made in the Australian public discussion that bear no relation to the reality or the truth and, by repetition, some of these have come to be fairly widely accepted in the Australian community. It is really that process separating reality and truth from the Australian policy process that I referred to as a risk of corruption of the Australian democratic process.

Senator PRATT: One of the statements that I hear frequently in the Senate is that this legislation will not do anything to address climate change. Can you explain to the committee what the link is between Australia's action and global action?

Prof. Garnaut: It is very clear that this is a global problem. There will only be a solution if there is action by all substantial countries. Australia is one of those substantial countries. One could say that each country can free-ride on all of the others and get the benefits of others' actions, but we will not get a solution to the global problem if any substantial countries do that. Nor is it the way that Australians are used to looking at international affairs. What if we had said at the time of the Korean War, for example: 'Well, it will make no difference to the outcome of the war'—and that would have been a true statement—'whether or not we send young men to die in Korea'? Fortunately, we did not formulate the question in that way. We saw the reasonable policy of Australia as doing our proportionate part in a global effort, led by the United Nations, in Korea. That is the way we look at international cooperation.

This is a problem, like collective security, in which there will be no solution unless all countries play their part. So far, demonstrably, we have been doing less than our part. This legislation will allow us to do our part. Initially our contribution under this legislation will be modest. Regrettably, at the moment the contributions of many other countries will be comparably modest. But I think once we get started, once Australia and other countries develop confidence that what we are doing at home and what they are doing at home is not going to impose a huge economic cost, once confidence develops that each country is playing its part, then it is a reasonable prospect that we will see an increase in the global effort. So Australia's contribution has to be seen as a contribution to a growing global effort that, over time, can deal with the problem.

Senator PRATT: Are our relative wealth and our high per capita emissions an important part of being seen to play our part in that collective international action?

Prof. Garnaut: It is certainly seen by other people as relevant. We stand out as the developed country with the highest emissions per capita. We happen at the moment to have exceptionally high incomes. As a country that has been a rich country for a long time we have contributed much more than our share to the build-up of greenhouse gases in the atmosphere in the past, a matter to which developing countries draw attention. So, certainly as part of the international discussion, we stand out for the history and present reality of high emissions. That certainly does not reduce the onus on us to at least do our fair share.

Senator PRATT: So the idea that Australia taking action will not do anything to address climate change is one of those mistruths that you spoke of?

Prof. Garnaut: Definitely. It is as much of a mistruth as it would be to say that we should have made no contribution to the United Nations war effort in Korea.

Senator PRATT: To how many parliamentary committees have you now given evidence after which we have actually managed to pass legislation such as that before us?

Prof. Garnaut: I have spoken to lots of parliamentary committees about lots of subjects over many years. I think on climate change it is probably only a couple.

Senator PRATT: I have seen you at least at four or five.

Mr CHEESEMAN: I am interested to hear your thoughts on the dangers of corporate welfare in terms of the climate change debate and the proposed bills we have before us.

Prof. Garnaut: It is always a challenge in a democracy to allow businesses a full and free role in the democratic process, as is appropriate, and to make sure that their interest is contributing to the development of policies in the national interest. There is always some tension between corporate pressure for policies in the corporate interest and in the national interest. This was a matter of close interest to me in my studies of Australian protection where, for many decades, corporate interests defeated the national interest. It was only when an independent centre of the Australian polity asserted itself that we got rid of protection and got all the benefits that the Australian community has enjoyed from getting rid of protection. So it is quite legitimate for business to seek to obtain policies in its own interest, but it is also important for independent people in the policy process and the

Australian community to stand up for the public interest. We have to get that balance right. I think in this legislation getting the balance right over time will be assisted by the arrangements for the Productivity Commission to review assistance to industry over time. I think a process of professional analysis by the Productivity Commission and the transparent public release of the results as a basis for public discussion will help get the balance right between corporate pressure for policies in their own interest and in the public interest.

Mr TONY SMITH: Professor Garnaut, in your opening remarks, and I think Senator Pratt referred to this, you spoke a lot about democracy with respect to these bills. You are someone, I think you would say, who from your perspective looks at things as you see them. If you are talking about democracy, would you concede that these bills were not taken to the people at the last election and in fact that there is no mandate? I do not say that in a disrespectful way but, given the debate over the last few years, whilst you have made the statements you have made, in all consistency you would have to say that the government did not seek a democratic mandate.

Prof. Garnaut: It is a matter of record. The government did not commit itself to these bills before the last election. Within our democratic arrangements it is not unusual for governments to respond to new circumstances by adopting new policies and they take responsibility for that at the following election. Under our Constitution under our democratic traditions, there is no exclusion of new policies for a government. The important thing is that these matters will be the subject of democratic judgment at an election.

Mr TONY SMITH: Professor, you would concede that there have been reforms that have been effected with a mandate, big changes.

Prof. Garnaut: Big changes with a mandate and big changes without a mandate.

Mr TONY SMITH: And wouldn't you concede, if you are being consistent, that when a Prime Minister says six days before an election that she will—

CHAIR: No way!

Mr TONY SMITH: No way?

CHAIR: Off you go. No way! Thank you; my indulgence has been stretched beyond the limit.

Mr TONY SMITH: So that's all right. I mentioned the Prime Minister. That is a different story.

CHAIR: Thank you. There is absolutely no relevance to the bills before us.

Mr TONY SMITH: The Prime Minister has no relevance—so that is interesting.

CHAIR: No. Professor Garnaut is appearing in a private capacity, and I did not say the Prime Minister had no relevance. The question you were asking had no—

Mr TONY SMITH: That is a triumph of democracy, I would say.

CHAIR: relevance. And maybe some people should go and look up what mandated politics actually means.

Mr TONY SMITH: Yes, perhaps yourself, Madam Chair.

CHAIR: Professor, thank you for your attendance here today. If you have been asked to provide additional material would you please forward it to the secretary. I realise you have got it all written there. We are happy to accept that if your handwriting is fine. If you wish to change it please do and we will accept that as a submission. We really appreciate your time today. You will be sent a copy of the transcript of evidence to which you can make corrections of grammar and fact. Thank you very much for your involvement today. We really do appreciate it.