

**Submission to the Senate Select Committee on Climate Policy
Concerning the choice of emissions trading to reduce Australia's carbon emissions**

Summary of the main points

- Any program to be effective in reducing Australia's consumption of fossil fuels and greenhouse gas emissions *must* increase the price of fossil fuels paid by Australian businesses and householders. This is an "Inconvenient Truth" that the government must understand, accept, and confront openly and honestly. The "good news" is that higher fuel prices can be offset by reduced taxes in other areas, or provision of additional social services, with no reduction in overall standard of living.
- An emissions reduction program must have a uniform, coherent basis that applies to all individuals and businesses, without exception, exemptions or special conditions.
- The emissions reduction program should be administered through clear, consistent rules. Any attempt by Government to "play God" or "pick winners" (through arbitrary decisions, exemptions, exceptions and compensation) will undermine the integrity of the program and the government.
- A carbon tax will be the most, direct, transparent and effective incentive for businesses and householders to reduce their emissions.
- The emissions reduction scheme must provide parity for Australian products competing against overseas imports and exports. The only workable and equitable option to achieve this is by:
 - ❖ Exempting exports from emission reduction taxes.
 - ❖ Applying import tariffs equivalent to emission reduction taxes that would be payable by an Australian company.

Currently, the costs of electricity and fuel do not include any allowance for environmental impacts and, in effect, are being subsidized by our children and future generations. For decades, the price of energy has been kept artificially low - often by deliberate government policy. The low price of energy distorts decisions that Australians make every day about where we live, which car and appliances we buy, which materials we use, which foods we buy and in which season, and whether we can be bothered to turn off a light. If the government continues to insulate Australians from the real cost of energy, Australians will continue to make decisions based on a distorted view of benefits and costs.

Any program to be effective in reducing Australia's consumption of fossil fuels and greenhouse gas emissions *must* increase the price of fossil fuels paid by Australian consumers (household and business), and increase the price of goods according to the amount of energy used in production and transport. A carbon tax will be the most direct, transparent and effective incentive for householders and businesses to modify their behaviour and lifestyles to reduce their consumption of fossil fuels and emission of greenhouse gases.

A tax on consumption of fossil fuels (and thus, on greenhouse emissions) would be analogous to well-accepted taxes on socially destructive products such as cigarettes and alcohol. Such an approach accepts that it is unreasonable and unrealistic for such products to be banned, but requires users to bear some of the costs that these products impose on society. Such taxes encourage users to moderate their consumption.

I have no doubt that governments have promoted carbon trading schemes, rather than carbon/energy taxes, because the term “emissions trading” is commonly misconstrued to conceal the fact that consumers will have to pay more for their energy. “Emissions trading” is widely promoted as an opportunity for business to make money, and I expect that many companies would profit through complex and non-productive administration and certification schemes, exaggerating or misrepresenting energy savings, exploiting exceptions and compensation schemes, or creating loopholes and exceptions through lobbying.

The reality is that measures intended to make an emissions reduction scheme more politically acceptable - by protecting producers and consumers from higher energy costs, by hiding the higher price of energy and energy-intensive products, or by creating exceptions and loopholes - will ensure its ultimate failure.

An effective emissions reduction program must be applied on a consistent, objective basis. Exemptions, compensation and arbitrary ad hoc rules will undermine the effectiveness of the program; open the system to lobbying, political expediency and corruption; and create a corrosive atmosphere for various industries to compete for more favourable treatment than other industries. Furthermore, the program must be relatively simple to administer, impartial and forward-looking. It should not reward inefficient and wasteful companies with permits for simply reducing unnecessary energy consumption. For each of these requirements, a carbon tax would appear to be superior to an emissions trading scheme.

There is no doubt that energy-intensive export-oriented industry sectors will be vulnerable to higher prices that will result from an effective emissions reduction scheme. This should not be addressed through ad hoc exemptions or compensation for “trade exposed industries” (*all* industries are exposed to overseas competition to some extent). This can only be equitably addressed if the emissions reduction scheme provides a “level playing field” for Australian companies in all industries to compete with overseas competitors in a global trading environment.

The emissions reduction scheme must provide parity for Australian products competing against overseas imports and exports. This parity can only be equitably achieved by:

1. Exempting exports from emission reduction taxes (in the same way that exports are currently exempted from GST). This need not impose high administrative costs, as exporters could claim credits for emissions reduction taxes (at an appropriate rate determined for that product category for an Australian company using industry best practice).

2. Applying import tariffs equivalent to emission reduction taxes (at an appropriate rate determined for that product category for an Australian company using industry best practice).

Requirement (1) implies a fundamental philosophical position that the *user* (rather than the producer) must ultimately bear the cost for emissions resulting from the burning of fuel or consumed in the manufacture of products. It requires that Australians pay for emissions caused by their use of fossil fuels or embodied in the products they consume - but not be responsible for emissions associated with overseas exports of Australian coal, aluminium or other products. That must be the responsibility for the countries to which Australia exports. While the reader may debate the moral virtue of this position, it is the only basis for a workable and consistent system. Any attempt by the Australian government to impose carbon taxes on overseas customers will cause them to seek alternative suppliers. Hopefully, other countries will eventually impose equivalent carbon emissions reduction schemes, allowing Australia to meld its carbon reduction scheme seamlessly with these countries.

For many high-tech and high-value products, embodied energy would likely account for an insignificant fraction of its value, and the equivalent tariff rate or export emission credit might simply be set as zero. For low-value products, the content of energy-intensive materials like steel, aluminium or plastic might comprise a major share of its value, and the equivalent tariff rate or export emission credit could impact significantly on the price.

To allow producers and consumers to adapt, the emissions reduction scheme must be phased in gradually. It is not necessary that high emissions reduction taxes be imposed initially to provide a strong incentive: what is important in influencing the planning decisions of individuals and businesses is *certainty* that emission reduction taxes will increase.

The increase in price of energy and energy-intensive products is only “one side of the equation” for a carbon tax or an effective emissions trading scheme. The “good news” side is that a carbon tax can be applied in a revenue-neutral manner, so that a person or business using an average amount of fuel or electricity (relative to other users at that time) would bear the same overall tax load as they do currently. In this way, increasing the price of energy paid by Australians will not necessarily reduce their living standards. However, people and businesses that are profligate in their energy use will pay more, and such businesses would face strong competitive pressure to become more energy-efficient.

Revenue raised by a carbon tax can be offset by a reduction in company tax, personal income tax or other taxes (in particular, state payroll taxes are a direct tax on employment). Alternately, the revenue can be committed towards improved community services (education, health, public transport, etc). Perhaps the best approach would be a combination of business and personal tax reductions, improved government services, and an enhanced allowance for the disabled and pensioners (who are unable to benefit from a tax reduction).

As the carbon tax is gradually scaled up in the years ahead, the government would have the option to allocate some of the revenue towards repayment of government debt accrued in stimulating the economy during the current global financial crisis. This would avoid the introduction of major new taxes or the need to reduce community services in the decade ahead. For example, an increase in the carbon tax of \$30 per tonne CO₂ (adding about 3 cents/kWh to the cost of electricity, or 7 cents/litre to motor fuel) would generate sufficient revenue to retire about \$10 billion/year of future debt.