CLIMATE INSTITUTE POLICY BRIEF

AUSTRALIAN CLIMATE POLICY AND ITS ROLE IN A GLOBAL CLIMATE AGREEMENT

Briefing > AUSTRALIAN CLIMATE POLICY AND ITS ROLE IN A GLOBAL CLIMATE AGREEMENT > MAY 2008

INTRODUCTION

On the 4th of May the Prime Minister announced stronger potential emission reduction targets and amendments to its emissions trading scheme - the Carbon Pollution Reduction Scheme (CPRS). The amended package differs from the package announced by the Government in the December 2008 White Paper in the following key ways:

1. **Stronger target:** The Government has committed to adopting a 25 percent reduction target on 2000 levels by 2020 as part of an international agreement involving global action to stabilise greenhouse gas concentrations at 450 ppm-e or lower. They also indicated their willingness to reduce emissions by 25 percent by 2024 if a less ambitious global agreement is reached in Copenhagen. This is based on the strongest previously set reduction target of 15 percent by 2020.
2. **Extra assistance but greater transparency:** Changes have been made to the amount of assistance for trade exposed industries, and to the processes for reviewing this assistance. This includes issuing more free permits; reviewing assistance as soon as an ambitious international agreement is reached; and publishing independent regular assessments of real and proxy carbon prices in competitor countries to increase transparency around the need for assistance.
3. **Changed timetable:** The Government still aims to pass the legislation this year, but the scheme's start date has been delayed by one year to 2011. In 2011 permits will be issued at a fixed price of $10/tonne, with full trading starting in 2012.

The CPRS should be seen in the context of other critical policy moves in recent weeks including:

1. the Council of Australian Government's (COAG) support for implementing the 20 percent by 2020 Renewable Energy Target
2. key commitments in the Federal Budget[1], and
3. announced and pending elements of a National Energy Efficiency Strategy to be agreed by COAG mid year[2].

This brief outlines what has changed since the CPRS White Paper was released and how the Climate Institute views these changes.

Overall, while the proposed CPRS is far from ideal, the amended package provides an important foundation for Australia to help achieve an effective global climate agreement that is in the national interest. Along with the Renewable Energy Target, and announced Budget and energy efficiency improvements, the Government is strengthening investment signals for clean energy and other low carbon jobs and industries.

On balance, the Climate Institute believes the amended CPRS should be passed so the Government can focus on achieving an effective global climate agreement and further strengthening investment signals in clean energy and low carbon jobs and industries.

[1] The Government has committed around AUD 15 billion over eight years to climate change investments such as research, development and demonstration into solar and carbon capture and storage, and energy efficiency programs. In addition it has committed around AUD 4.6 billion to public transport infrastructure.

[2] The key remaining gap in the Government's or COAGs energy efficiency packages are financial incentives to unlock major energy savings on the commercial building retrofits.

KEY CHANGES TO CPRS WHITE PAPER

TARGETS:

The December White Paper included a firm commitment to reduce overall greenhouse gas emissions by 5-15 per cent below 2000 levels by 2020.[3] The Government also acknowledged that these proposed national targets "*are complemented by an unambiguous statement that Australia's national interest will be best served by a comprehensive global agreement to stabilise atmospheric concentrations of greenhouse gases at around 450 parts per million of carbon dioxide equivalent (ppm CO2-e) or lower…*".

Treasury's modelling linked the 15 per cent figure to a 510 ppm CO_2-e outcome, while the Government commissioned Garnaut Review concluded a 25 per cent reduction by 2020 would be Australia's "fair share" to 450 ppm-e. This created a "credibility deficit" for the Government and attracted criticism both at home and abroad.

Changes:

1. The target range was broadened to include up to a 25% reduction on 2000 levels by 2020. "*The Government will adopt a 25 per cent target only as part of an ambitious international agreement involving comprehensive global action capable of stabilising greenhouse gases in the atmosphere at 450 ppm CO2-e or lower.*" They have defined such an agreement as including, among other things:
    a. a clear global trajectory, where the sum of all economies' commitments is consistent with 450 ppm CO2-e or lower,
    b. a peak of global emissions no later than 2020,
    c. aggregate advanced economy reductions of at least 25 per cent below 1990 levels by 2020, and
    d. major developing economy commitments to slow growth and then reduce their absolute level of emissions over time, with a collective reduction of at least 20 per cent below business-as-usual by 2020.
2. If a less ambitious agreement is reached and Australia adopts a 15 percent target for 2020, the Government has indicated that Australia would reduce emissions by 25 percent below 2000 levels by 2024.
3. The Government will also undertake an independent review as part of the ratification process to ensure the numbers add up to a 450 ppm-e or lower agreement. This is similar to what will be done in the EU for shifting to a 30% target.[4] The Government has also noted that "*If an ambitious international agreement is reached, the case for* [emission intensive trade exposed industry] *EITE assistance is significantly reduced and an EITE assistance review would be triggered immediately.*"

[3] Note 2000 levels and 1990 levels are nearly identical for Australia. On 1990 levels, these reductions would equate to around a minus 4-14 per cent reduction.

[4] See http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P6-TA-2008-0610+0+DOC+XML+V0//EN&language=EN#BKMD-12

CLIMATE INSTITUTE POLICY BRIEF

Climate Institute comments:

For the Climate Institute, the main issue is whether the proposed targets allow Australia to actively participate in international talks to get an effective global climate agreement in Copenhagen and beyond. Putting 25% on the table potentially unchains our negotiators from the previously inadequate targets and opens the door for Australia to be a strong positive force in the global talks.

How effective or important this is will depend on Australia backing this up with credible proposals on other key elements of the international negotiations – in particular finance mechanisms, technology mechanisms, the length of the next commitment period and the overall “shared vision”. In this context, the Climate Institute is also pleased the Government has opened the door for the first time on using auction revenue to help drive emission reductions outside of Australia (see below).

There has been a lot of focus on Australia’s 5 percent unconditional target but this is misplaced. Even at this relatively early stage of negotiations, countries have begun to put targets on the table, many of which are broadly comparable to Australia’s 15% scenario. This is a strong indication that the dynamics of the global negotiations inevitably mean that Australia’s target will be higher than 5 percent in the final deal.

The conditions set for shifting to a 25 per cent reduction are challenging to meet but represent a realistic scenario of what is needed for an effective global agreement.[5] Unless global emissions are turned around before 2020 we virtually lose any chance of stabilising greenhouse concentrations at 450 ppm-e or lower. Australia must focus on achieving an effective global climate agreement.

Based on preliminary analysis by the Climate Institute, using various models to determine a fair distribution of emission rights, a 25% cut for Australia would imply developed countries as a group should be cutting overall emissions towards the higher end of the 25 to 40 percent by 2020 range indicated by the Intergovernmental Panel on Climate Change (IPCC) and being discussed internationally.

For example, it is still not widely understood that the 25-40 per cent reductions by 2020 discussed in the reports of the IPCC refer to possible targets for industrialised countries (Annex 1) *as a group*. Based on preliminary analysis of a range of approaches for allocating emission obligations across countries to achieve a 20% cut in Annex I emissions by 2020, Australia’s target would need to be around 10-15% by 2020.[6] For 30% and 40% Annex 1 reductions, Australia’s targets would be around 20-25 percent and 25-30 percent respectively.

---

[5] For example, last year in its submission to the Garnaut Review the Climate Institute suggested that global greenhouse concentrations need to peak at well below 500 ppm-e and after the peak global concentrations need to continue to decrease to below 400 ppm-e. In this context the Climate Institute highlighted that industrialised countries’ overall emissions should be around 30 per cent below 1990 levels by 2020, developing country emissions should peak and begin to decline rapidly over the same time period; and that global action to rapidly reduce emissions from land use change and deforestation is also required.

[6] Based on M.G.J. den Elzen, N. Höhne, J. van Vliet, C. Ellermann (2008), Exploring comparable post-2012 reduction efforts for Annex I countries, PBL Report 500102019/2008, Netherlands Environmental Assessment Agency, and rescaled to include projected LULUCF emissions. Comparable effort scenarios include equal reduction below baseline, countries reducing emissions up to a level at which an equal marginal abatement costs (MAC) for the reduction of a unit of emissions is reached, countries taking on equal costs as a percentage of the GDP, converging per capita emissions and the Triptych approach (future reductions among countries are based on converging technological standards or targets at the sectoral level, e.g. electricty sector emission intensity converges to a common point).

CLIMATE INSTITUTE POLICY BRIEF

INDUSTRY ASSISTANCE/TRANSPARENCY:

In the White Paper, the majority of emission permits were to be auctioned. Initial estimates suggested 60 per cent of revenue will be returned to households through 'cash handouts' (around AUD 6 billion/year) with around 25 percent being given as free permits to emission intensive trade exposed industries (EITEIs) at the start of full trading in the scheme.

Without reductions in assistance to industry over time as the result of a global agreement that reduces trade exposure, handouts to EITEIs is expected to grow through time to around 45 percent by 2020. This is despite the White Paper proposal that the rate of assistance be reduced by 1.3 percent a year to drive carbon productivity.[7] Electricity generators receive a "once off", once and for all allocation of free permits worth AUD 3.9 billion over five years.

The Government's position on CPRS permit revenue in the White Paper was that "*every cent will be spent on Australian homes and businesses*", which restricted Australian negotiators on questions of how to finance clean technology in developing countries, which are central to the post-2012 deal.

Changes:

1. Additional free permits are granted for trade exposed industries in the first five years. Based on preliminary calculations this will increase the share of free permits to trade exposed industries from 25 percent to around 27-28 percent of permits in year two of the scheme.
2. A review of all EITEI assistance is now guaranteed as soon as an ambitious international agreement is reached (as opposed to in 2014) and an independent assessment of real and proxy carbon prices in competitor countries will be published in that and subsequent reviews of EITEI assistance.
3. After 2015 permit revenue is able to be used to invest in international measures such as avoided deforestation.
4. No change in the 1.3 percent rate of decline in assistance set out in the White Paper.
5. No additional permits for coal fired electricity generators or extra assistance for coal mines.

Climate Institute comments:

For the Climate Institute, the main issues with EITEI assistance have been its ability to constrain the ability of the Government to accept a stronger emission reduction target, its ability to erode public support for the scheme, the increased costs the assistance implies for other parts of the economy and the dampening of price signals to drive investment towards a low emission economy. We have always accepted the need for some limited assistance to those activities that are genuinely at risk from carbon leakage and that this assistance to be tied to driving world's best practice emission reduction practices.

In isolation we still do not believe the proposed allocation of free permits is being undertaken in a fair or economically responsible way. In the Climate Institute's view many industry claims of carbon leakage are not supported by independent analysis and have been wildly exaggerated[8].

---

[7] The White Paper proposes to reduce the rate of assistance available for EITE activities in line with improvements in 'carbon productivity'. While the carbon productivity improvement will reduce the level of free permits available per unit of output, this does not actually reduce the total number of permits available to EITEIs. In fact, as the Government clearly points out in the White Paper, if a company increases production, resulting in higher emissions, it will be eligible to claim more free permits.

[8] See the Climate Institute's submissions to the Garnaut Review, the CPRS Green Paper and subsequent Senate inquiries at www.climateinstitute.org.au.

However, the Government's commitments to instigate an independent review of assistance to trade exposed industries as soon as an ambitious international agreement is reached and that independent reviews (initially by the Productivity Commission) of real and proxy carbon prices in competitor countries will be implemented are welcome improvements. This, the Climate Institute believes, provides a greater level of transparency around future assistance. It will give both the community and business the confidence they need to ensure that on one hand we are not handing over billions of dollars in assistance unnecessarily and on the other hand that the government will not remove assistance arbitrarily. We also note bi-partisan recognition that under a strong international agreement the case for assistance is largely removed.

We also recognise that the Prime Minister, for the first time has signaled that Australia auction revenue can be used to drive emission reductions outside Australia. Financing for emission reductions and adaptation in developing countries will be critical to sealing the final deal in Copenhagen. Extra financing for developing countries mitigation plans and support for an effective financing mechanism are important as imminent tests of the Government's genuine ambition.

TIMING:

The White Paper proposed that the legislation to be introduced and through parliament by July 2009 and the trading of permits start in 2010.

Changes:

Legislation through this year but scheme starts in 2011 (one year delay), in 2011 permits are issues at fixed price of AUD $10/tonne, and full trading starts in 2012.

Climate Institute comments:

The delay in the CPRS by one year is not helpful but probably the least significant issue. The spot price of emission permits in the trading system is not as important as the long-term signals the scheme sends. Australia is on track to meet its 2012 commitments under the Kyoto Protocol and given the dampening impact this would have had on emission prices, most of the abatement in the early years of the CPRS was never going to be delivered by the CPRS (it would have come from complementary measures like the Renewable Energy Target).

The biggest initial impact of the CPRS will be driven by the medium and longer-term investment signals it sends and this underscores the need to get effective legislation through this year. With the prospect of a 25% reduction on 2000 levels by 2020 on the table, business will now, without delay, have to factor this into medium and long-term investment decisions. In light of this low-carbon investment horizon, high-emitting assets, such as coal-fired powered power stations, become much less attractive.

Passage of the legislation this year will also send an important signal to the international community that Australia is getting on with climate action and will end significant business uncertainty.