8th April 2009

Committee Secretary
Senate Standing Committee on Economics
P O Box 6100
Parliament House
Canberra ACT 2600
Email: economics.sen@aph.gov.au

Dear Sir/Madam,

Re: **Inquiry into the exposure drafts of the legislation to implement the Carbon Pollution Reduction Scheme**

This Submission is not confidential

The particular form of ETS proposed in the draft legislation is unnecessarily onerous for any target or cap. That is because the proposed requirement for non-exempt and uncompensated firms to acquire at auction Australian Emissions Units (AEU), i.e. permits, has horrendous cash flow implications. These result from the necessity to acquire and acquit permits for 100% of the *allowed* emissions *every* year. This aspect seems not to have been much appreciated.

A wholly valid analogy is that this feature of the proposed ETS is tantamount to having **to pay fines** for very kilometre per hour we drive at **below** the allowed speed limit, and then to pay **additional** fines for each km/hour we **exceed** the limit, as we do now, except that we do not have to pay fines for driving below the speed limit. This is clearly absurd, but it is exactly what the ETS involves, by requiring firms to purchase AEU permits **both** for what they are allowed to emit, **and** also for extra permits (from other firms) for any tonne of CO_2 they may wish to emit above the applicable cap. This concept is wholly unnecessary at least to any economist or businessman who has heard of the concept of Marginal Cost.

An intelligent ETS requires only auctioning of permits for emissions **ABOVE** the allowed CAP. Broadly this has been the EU's system until now. In other words, the cost of such permits is like a fine for exceeding the speed limit. For firms staying within the Cap, there would be no need to buy permits - and therefore no impact on their cash flows and balance sheets, as the huge outlays to acquire permits for **ALL** their emissions are unnecessary. Those firms wishing to emit more than their permitted ceiling or cap would have to buy at auction or in the market only as many AEUs as they needed to achieve their planned increased level of output. The price signal to encourage adoption of less CO2-intensive inputs would be exactly the same.

The reason the economists in DCC and Treasury who must know that the marginal cost approach is correct have of course been overruled by politicians whose eyes are dazzled – both President Obama's and Mr Rudd's – by the enormous revenues created by auctioning of permits for the full amount of all emissions whether allowed or not. The resulting slush fund will be available to be spent on political rather than climate change issues, and the proposed Act does indeed establish that the proceeds will mainly be used to transfer income from the richer to poorer members of society, by enabling the latter to improve their standard of living despite rising prices of carbon-intensive energy.

The Cap & Trade of the ETS proposed by the Rudd Government is the worst possible scheme, involving both reporting of emissions, monitoring, inspection, and punishment, and special deals for favoured industries and other parties. In the USA the ETS favoured by the Obama Administration with its auctioning of permits for **total** emissions is already coming to be known as the "Lobbyists' Full Employment Act of 2009." The same is already true in Australia.

Sincerely

Timothy Curtin