
Submission to the Senate Select Committee on Climate Policy



Federal Chamber of Automotive Industries

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OVERVIEW

The Federal Chamber of Automotive Industries (FCAI) provides the following submission to the Senate Select Committee on Climate Policy.

The FCAI is the peak industry organisation representing vehicle manufacturers and importers of passenger vehicles, light commercial vehicles and motor cycles in Australia.

The FCAI supports the inclusion of transport fuels within a CPRS as the most efficient and effective method to reducing emissions from passenger motor vehicles.

The FCAI submits that the introduction of additional regulation of vehicle CO₂ emissions is unnecessary and inconsistent with the market based incentives of a CPRS.

BACKGROUND

Road transport and passenger road transport, is integral to economic development and has “dramatically enhanced mobility, economic prosperity and quality of life for billions of people”.¹

The growth in demand for passenger vehicles in Australia and globally, and increased use will deliver greater benefits. The challenge for the industry and governments is to enable future road transport demands to be met in a sustainable and environmentally responsible way.

The FCAI acknowledges that the growth in road transport contributes to global greenhouse gas emissions and that the automotive industry, internationally and in Australia, has a responsibility to contribute to efforts to mitigate the impact of climate change.

Australian passenger motor vehicles accounted for 7.8 per cent of Australia’s total greenhouse gas (GHG) emissions in 2005.² Australia has one of the oldest average fleets among developed economies with an average vehicle age of 9.7 years³. Consequently, as new vehicle technologies are developed and become available to the market, benefits take a long time to diffuse through the vehicle stock.

Globally, automotive manufacturers are investing heavily in a range of technologies and advances in vehicle design that have the potential to make further significant contributions to reducing motor vehicle CO₂ emissions. Some of the key approaches being pursued include:

- Development of advances in electric vehicle capability and design, including advanced battery technologies;
- Improvements in vehicle design, including increased thermal efficiency in engines; reduced friction loss; enhanced aerodynamics; reduced rolling resistance; and reductions in vehicle weight;
- Advances in hybrid vehicle technology;

1 Julia King, The King Review of Low Carbon Cars (UK), March 2008, Page 3

2 Australian Greenhouse Office, April 2007, State and Territory Greenhouse Gas Inventories 2005

3 Australian Bureau of Statistics, 2007, Motor Vehicle Census, catalogue no. 9309.0

- Development of enhanced alternative fuels capability, including new generation renewable biofuels.
- Hydrogen fuel cell vehicles.

Significant opportunities exist for the uptake and the further development of a range of these technologies by the Australian automotive industry.

AUSTRALIAN INDUSTRY PERFORMANCE

The three Australian vehicle manufacturers are members of the Australian Government’s Greenhouse Challenge Plus program which enables companies to form working partnerships with the Government to improve energy efficiency and reduce greenhouse gas emissions.

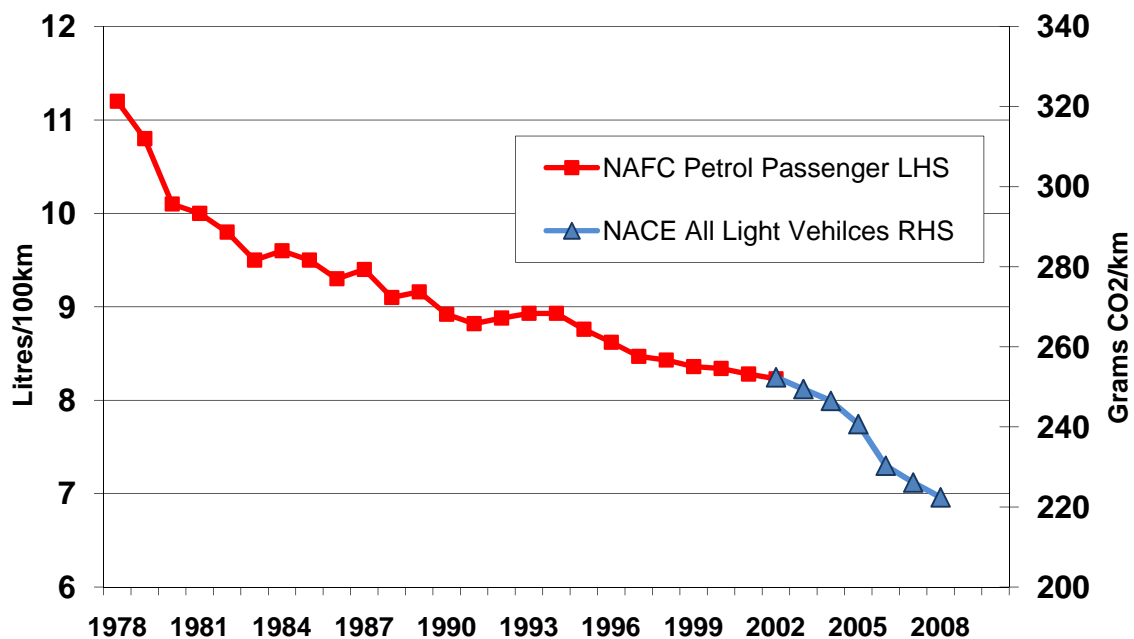
The Australian industry also has a long history of pursuing voluntary targets to reduce fuel consumption, dating back to the 1970s.

In 2005, the FCAI developed a voluntary code aimed at progressively reducing average carbon emissions from new light vehicles. The target was “to achieve a reduction in CO₂ emissions for all new light (under 3.5t GVM) vehicles to 222 g CO₂/km by 2010.” The FCAI developed this Code to demonstrate the continuing commitment by the Australian automotive industry to improving environmental performance.

The National Average Carbon Emissions (NACE) for all new light vehicles sold in Australia for 2008 was 222.4 grams of CO₂/km.

This is a 12 per cent reduction in CO₂ emissions from new light vehicles since 2002. New light vehicles are therefore making a significant contribution to the government’s target of a 5 to 15 per cent reduction in carbon emissions by 2020.

Chart 1: Fuel Economy and Emissions in Australia



The Prime Minister, in his 2008 World Environment Day speech (5 June 2008) suggested that the current NACE is due for revision. The industry agrees and it is the FCAI's intention to develop a new target to challenge manufacturers and consumers to achieve further reductions in carbon emissions from new vehicles.

The FCAI and the Australian Government have a long history of developing voluntary agreements to reduce fuel consumption or carbon emissions, dating back to 1979.

In light of the rapid progress toward the 2010 target, the FCAI has commenced the development of a new NACE target.

CARBON POLLUTION REDUCTION

Reducing CO₂ emissions is a complex challenge and improving vehicle technology and the efficiency on new passenger vehicles is only part of the solution to reducing emissions from passenger transport. The automotive industry continues to invest in research and development of new technologies to improve the fuel economy and lower the emissions from new passenger cars and introduce them into the Australian market. .

The FCAI supports the inclusion of transport fuels within a CPRS as the most efficient and effective method to reducing emissions from passenger motor vehicles.

Any additional policies aimed at reducing emissions from passenger transport must be complementary to the CPRS.

A comprehensive strategy to reducing emissions from transport is required. This strategy must recognise that a CPRS is the main tool for reducing transport emissions and that any additional measures must complement the CPRS without distorting the carbon price or placing a disproportionate burden on the transport sector. Complementary initiatives could include policies to minimise travel time, facilitate technology uptake and reduce fleet age will ensure the greatest environmental outcomes.

COMPLEMENTARY MEASURES

Since one tonne of CO₂ emitted has the same impact whatever its source, this implies that the cheapest abatement opportunities should be accepted first, wherever these opportunities may occur. An unconstrained CPRS will allow the market to provide efficient emissions reductions by exploiting the least cost opportunities available.

The effect of an CPRS on the transport sector would be to influence driver behaviour through an increase in the petrol price. If there were a permit price of \$30 per tonne of CO₂, the expected increase in the price of petrol would be around 7-8 cents per litre.⁴ Some parties suggest that because a CPRS has a relatively small impact on the price of petrol, and that demand for petrol is relatively inelastic to price movements, that a CPRS would have little impact on emissions from

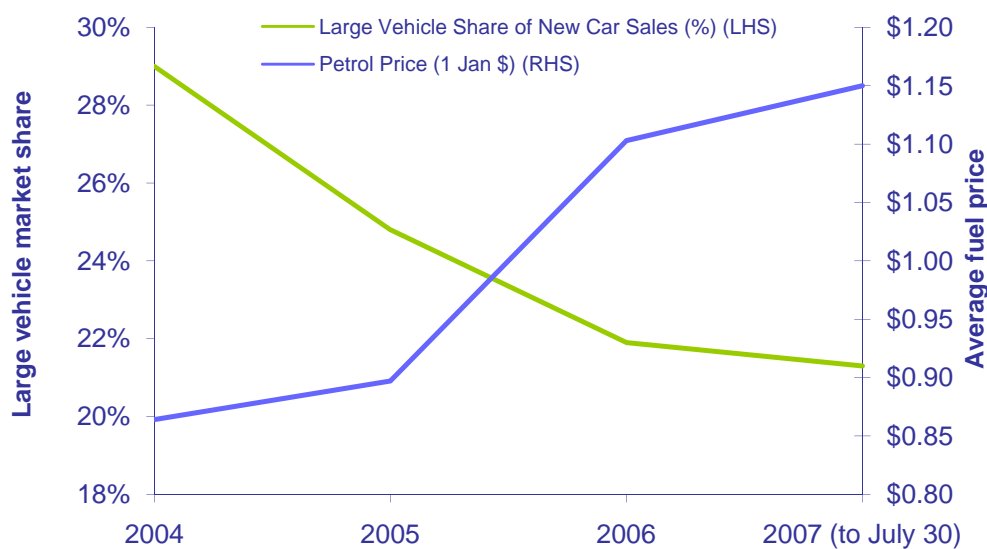
⁴ The RIS for 'Vehicle emissions and fuel quality standards for the post 2006 period', prepared by the Australian Department of Transport and Regional Services concluded that "applying the sulphur limit to regular unleaded or lead replacement petrol is not warranted on cost benefit grounds."

the transport sector. Proponents of this train of thought argue that this is a rationale for additional measures in the transport sector, such as mandating standards for emissions or for fuel consumption.

There are several points to be made to refute this proposition. First, as discussed below, such an approach would offend against the major objective of the CPRS, that is, to drive emissions reductions from the cheapest available source. By imposing additional measures on the transport sector, it would suggest that it is worth paying more to abate one tonne of CO₂ from the transport sector than from elsewhere. The rationale for this is not clear.

Based on recent evidence, an increase in the price of fuel as a result of the establishment of a CPRS, will drive emissions reductions both by reducing vehicle use and by inducing consumers to buy smaller cars. As illustrated in Chart 2 below, increases in petrol prices over the last few years have resulted in a significant shift in market segmentation, suggesting a link between petrol prices and new vehicle purchasing decisions.

Chart 2: Petrol Price versus Large Vehicle Sales



Source: FCAI VFACTS and Department of Innovation, Industry, Science and Research: Australian Petroleum Statistics.

Inclusion of Transport Fuels

An economy-wide CPRS will allow the market to identify/encourage efficient emissions reductions by exploiting the least cost opportunities available.

The FCAI therefore supports the Government's preferred position that transport emissions be covered from the Scheme's commencement, with scheme obligations applied to upstream fuel suppliers.

In introducing the CPRS on passenger fuels, consideration should be given to the relative price impact of the CPRS on different fuels to ensure that consumers receive the appropriate incentives to maximise emissions abatement.

The impact of the CPRS on relative prices of fuels is complicated by:

- existing fuel taxation arrangements which have evolved over decades of public policy decisions which have not, until recently, considered the impact of these fuels on climate change, and
- the proposal that fuel excise will be cut on a cent for cent basis to offset the initial price impact on passenger fuel.

The FCAI has concerns that the combination of these factors could distort relative prices of fuels in a way that does not result in maximising incentives for motorists to reduce emissions.

Synthetic Greenhouse Gases

Synthetic greenhouse gases are commonly used, in small volumes, in the air-conditioning systems of passenger cars.

Given that the draft legislation proposes that entities importing more than 25,000 tonnes of CO₂-e a year of synthetic greenhouse gases will be covered by the CPRS, it is likely that vehicle brands importing more than 25,000-30,000 vehicles will be required to acquit the relevant number of permits or emissions units under the new Scheme.

While it is understood that it is the Government's intention that an equivalent carbon price be applied to all synthetic greenhouse gases sold in Australia, details of the mechanism proposed to be applied to those entities which import or supply less than 25,000 tonnes CO₂-e are not yet available.

To this end, the FCAI urges the Australian Government to undertake further consultation with industry to clarify the most effective design of any complementary measures that would apply below the CPRS threshold. Indeed, there may be benefit in providing vehicle brands with the opportunity to opt for coverage under one or the other, regardless of whether or not they exceed the CPRS threshold.

As a further and final point, I also note that the importation of synthetic gases used in motor vehicle air conditioning systems are currently covered by licensing and product stewardship arrangements under the provisions of the Ozone Protection and Synthetic Greenhouse Gas Management Act 1989. Further clarification on how these arrangements will operate in conjunction with the CPRS or any complementary measures is warranted.

ASSISTANCE TO EMISSIONS-INTENSIVE TRADE-EXPOSED INDUSTRIES

The Australian automotive industry is highly trade exposed. In 2008 over 1 million vehicles were sold in Australia of which around 18 per cent of sales were manufactured in Australia.

Of the countries from which Australia imports vehicles, three of the top five countries (by volume) are Annex II countries under the Kyoto Protocol (Thailand which is ranked second, Korea which is third and South Africa which is fifth) which are not bound to reduce greenhouse gas emissions. Together, these countries represent 28.2 per cent of vehicle sales in Australia.

In addition, the local industry exports 40 per cent of vehicle production to countries including in the Middle East, the United States, New Zealand, Korea and South Africa. These markets are also highly competitive and any increase in costs in the Australian industry can compromise its future prospects.

Vehicle and component manufacturing are heavily reliant on a number of other industries, which are also significant energy users, including aluminium, steel, glass and plastics. Increases in the cost of production of these commodities will flow through to the cost of vehicle manufacturing in Australia.

Many Australian manufactured vehicles are also manufactured in other markets throughout the world. Australian vehicle manufacturers therefore have products which are perfect substitutes to Australian made components which are manufactured to the same specifications and all-ready supplied to their corporations but do not induce a carbon price.

The Australian vehicle manufacturers and component suppliers will therefore have strong commercial incentives to purchase raw materials and/or manufactured components from markets which do not include a carbon price.

Measuring Emissions-Intensive Trade-Exposed Industries

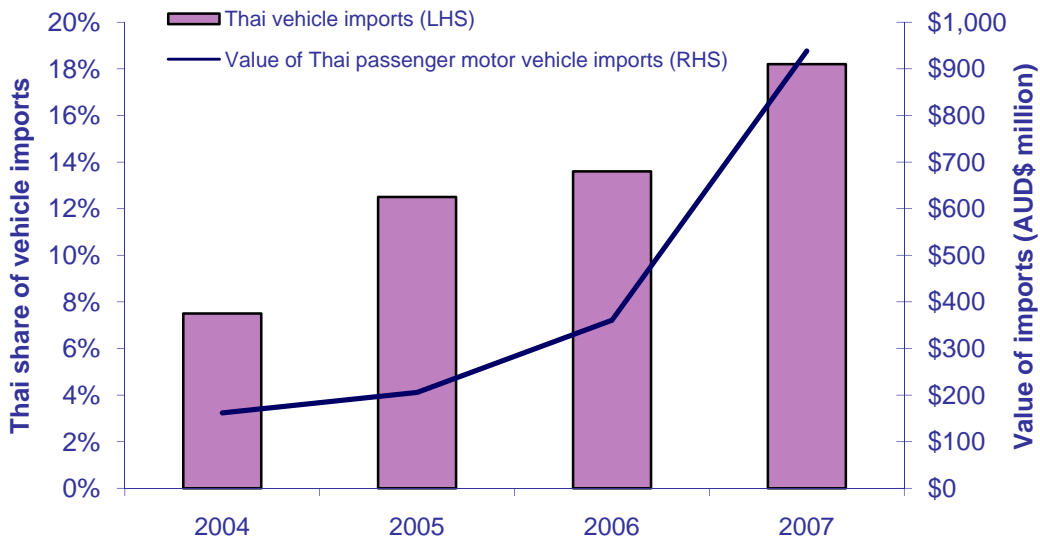
The measurement of emissions intensity as 'emissions per unit of revenue' is inheritably biased against companies and industries which undertake high value adding activities. Each time a product is transformed or modified it incurs an additional cost. With the introduction of a CPRS these additional costs are increased as each stage will inevitably include some form of energy. Therefore, highly manufactured products will incur the costs of a CPRS at numerous stages through the manufacturing process and therefore their cost (or 'revenue') will also increase.

A system which defines emissions intensity based upon emissions per unit of revenue would seek to promote low value adding activities against those which sought to produce highly advanced products, such as motor vehicles.

The Australian automotive industry faces significant international competition from countries which do not have international obligations to cut emissions (Annex II countries under the Kyoto Protocol) and should be included among EITEs.

Passenger motor vehicle imports from Thailand illustrate the level of competition that the Australian automotive industry faces. Thai imports pay no import duties when entering the Australian market, a result of the free trade agreement which commenced on 1 January 2005. Since this time there has been significant growth in Thai imports, as shown in Chart 3: Passenger motor vehicle imports from Thailand.

Chart 3: Passenger Motor Vehicle Imports from Thailand



Source: FCAI, Vehicle Sales, available at www.fcai.com.au and DFAT, 2007, *Composition of trade Australia 2006-07*, p283

Note: Vehicle sales based upon calendar years and value based upon financial year.

In addition, the local industry has now become a major exporter, mainly selling large cars to countries in the Middle East. These markets are also highly competitive and any increase in costs in the Australian industry can compromise its future prospects.

It should further be noted that the automotive components industry also faces significant international competition, particularly with the rise of China as a low cost manufacturer of increasingly sophisticated products.

In terms of energy intensiveness, both the vehicle assemblers and the component manufacturers are significant users of electricity. As a consequence of the industry's location, much of the base load power it uses is sourced from brown coal generators in Victoria's Latrobe Valley. Under any CPRS, electricity generated from brown coal will be subject to the highest increase in costs.

The FCAI maintains that the classification of trade exposed emissions intensive industries should be undertaken on a case by case basis. This would avoid establishing arbitrary criteria which may not adequately reflect the competitive impact on individual industries or sectors. The case by case approach can also take into consideration the existence of a CPRS, or equivalent, in competing nations.

CONCLUSION

The FCAI acknowledges that the growth in road transport contributes to global greenhouse gas emissions and that the automotive industry, internationally and in Australia, has a responsibility to contribute to efforts to mitigate the impact of climate change.

The FCAI supports the inclusion of transport fuels within an economy wide CPRS. Imposing a carbon cost within the price of transport fuels will drive emissions reductions both by reducing vehicle use and by inducing consumers to buy more efficient cars.

The FCAI submits that the introduction of additional regulation of vehicle CO₂ emissions is unnecessary and inconsistent with the market based incentives of a CPRS.

An economy-wide CPRS will allow the market to provide efficient emissions reductions by exploiting the least cost opportunities available. Australia is leading the world by introducing a CPRS which includes passenger transport. Countries including Japan, the United States and European economies have implemented a range of second best measures to reduce vehicle emission, due to the absence of a more efficient, market based measure such as a CPRS.

Whilst the automotive industry concentrates on undertaking research and development of new technologies to improve the fuel economy and lower the emissions from new passenger cars a strategy to reduce vehicle emissions cannot focus excessively on vehicle technology. A comprehensive and economy-wide approach will result in larger, cost-effective CO₂ emission reductions. A comprehensive approach will not only affect new cars, but also the existing vehicle fleet, fuel quality, traffic infrastructure growing, congestion, and a rise in annual vehicle travel time.

Whilst the FCAI is supportive of the implementation of the CPRS it is noted that this will affect the competitive position of locally manufactured vehicles. Other major vehicle producing nations are not bound to reduce greenhouse gas emissions.

In addition, the local industry exports 40 per cent of vehicle production to countries including in the Middle East, the United States, New Zealand, Korea and South Africa. These markets are also highly competitive and any increase in costs in the Australian industry can compromise its future prospects.

The measurement of emissions intensity as 'emissions per unit of revenue' is inheritably biased against companies and industries which undertake high value adding activities. The FCAI maintains that the classification of trade exposed emissions intensive industries should be undertaken on a case by case basis.