

KYOTO PROTOCOL RATIFICATION BILL 2003

*ACCI SUBMISSION
TO THE
SENATE ENVIRONMENT, COMMUNICATIONS, INFORMATION
TECHNOLOGY AND THE ARTS COMMITTEE*

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Background

The Australian Chamber of Commerce and Industry (ACCI) is the peak council of Australian business associations. ACCI's members are employer organisations in all States and Territories and all major sectors of Australian industry.

Through our membership, ACCI represents over 350,000 businesses nation-wide, including the top 100 companies, over 55,000 enterprises employing between 20-100 people, and over 280,000 enterprises employing less than 20 people. This makes ACCI the largest and most representative business organisation in Australia.

Membership of ACCI comprises State and Territory Chambers of Commerce and national employer and industry associations. Each ACCI member is a representative body for small employers or sole traders, as well as medium and large businesses.

Introduction

On 26 November 2003, the Senate referred the *Kyoto Protocol ratification Bill 2003* to the Environment, Communications, Information Technology and the Arts Legislation Committee for inquiry and report by 4 March 2004.

The purpose of the Bill is to require the Government to ratify the Kyoto Protocol to the United Nations Framework Convention on Climate Change within 60 days of the Act's commencement and to require compliance with a number of related measures.

ACCI Policy on Climate Change

ACCI accords a high priority to climate change policy. We have taken a lead role within the business community to develop a considered response to the Government on climate change issues.

It is critical that any policy responses to achieve greenhouse gas abatement and adaptation to climate change are part of a national strategy and not some fractured state-by-state policy hodge-podge, the Government should release its national forward climate change strategy soon. Only a truly national approach on policy responses will deliver certainty for business and optimum public policy outcomes.

Although the economics and the science guiding policymakers on this issue is developing, and sometimes called into question, ACCI believes there is enough evidence to suggest that industry,

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governments and the community must continue to understand and systematically address this issue.

Given the current Australian and international economic, environmental, social and political operating context, the question today is what policy approaches should be adopted to achieve substantial, least-cost abatement.

The ACCI General Council agreed ACCI's current policy position on climate change in March 2003:

- noted the status of the Kyoto Protocol of the UN Climate Change Convention and reconfirmed ACCI's position of not supporting ratification until it is considered to be in the national interest;
- agreed to support, in principle, emissions trading as an option to abate greenhouse gases, noting however that more work needs to be done to develop an appropriate and comprehensive model, taking into account the effect on trade-impacted industries and sectors;
- in the absence of an agreed model for an emissions trading scheme, agreed to support broad-based mechanisms such as fiscal measures (for example, research and development incentives, accelerated depreciation and investment allowances) and negotiated agreements (for example, extending the Greenhouse Challenge Program);
- agreed to oppose the introduction of a carbon tax;
- noted that emissions reduction steps need to give recognition to economic growth encouraging the best use of the most efficient technologies and practices;
- opposed fragmented state-based policies. And further noted that, if Australia develops an integrated national strategy on climate change, it should be consistent with an international system;
- noted that governments should also be conscious of solving multiple sustainable development challenges, and should look for synergies with related issues, for example 'carbon sinks' and dry-land salinity
- agrees to promote the policy position that greenhouse gas abatement is a community issue demanding a community-based solution; and
- agreed that ACCI should continue to take a leadership role with government to develop a national strategy on climate change.

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It is important to re-iterate is that while ACCI is opposed to the ratification of the Kyoto Protocol, that does not mean we are opposed to reducing greenhouse gases or learning to adapt to climate change.

Government-Business Climate Change Dialogue Process

As a means of putting industry preferred greenhouse gas abatement and adaptation policies on the table, industry in August 2002 met with Government and formed five working groups. By April 2003, these five working groups had examined closely what policies are preferable given the unique characteristics and needs of Australian industry. One group, the Cross-Sectoral Working Group discussed the greenhouse issue from a broad perspective, giving consideration to how industry, regardless of orientation or size, can address the issue of climate change. The remaining four Working Groups addressed climate change as it relates to the energy and resources; energy intensive manufacturing, the transport and transport infrastructure; and the agriculture and land management industries.

ACCI played a significant role in contributing to the work and recommendations of these working groups. ACCI's Chief Executive, Peter Hendy, was the Chairman of the Cross-Sectoral Working Group as well as the Chairman of the Steering Group that guided the work of all five working groups.

As the Government Business Climate Change dialogue concluded some time ago, business is waiting for a response from Government to that dialogue in the form of the Government's forward strategy on climate change.

The overarching requirement of the national strategy should be that in achieving reductions in greenhouse gases, Australian industry's profitability and productivity must be maintained and promoted.

The strategy must also be integrated with the Government's Energy Policy and its response to the Report of the Review of the Mandatory Renewable Energy Target – both of which are expected within the next few months.

Environmental Parameters

There is no denying that carbon concentrations have risen since the industrial revolution, and as the world's leading scientific body on climate change, the United Nations Intergovernmental Panel on Climate Change (IPCC) concludes, this increase can be attributed to human activities. There is also no denying that global warming is taking place. The uncertainty lies in what is the exact sensitivity

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between the increase in greenhouse gas concentrations and the effect on global warming. Furthermore, it is difficult to separate what may be variability due to increasing concentrations of greenhouse gases in the atmosphere from underlying climate variations due to other causes. Essentially, although climate change science continues to improve, it does not give us definitive explanations to these questions.

The IPCC believes that the extent of the increase in temperatures would be in the band 1.4 degrees celsius to 5.8 degrees by the year 2100 relative to 1990. However, many commentators have put the view that it is much more likely that the extent of global warming would be between 2 degrees and 3 degrees. In an historical context, stretching over many thousands of years, there have been periods where global temperatures have fluctuated significantly over relatively short periods of time. Some of these fluctuations have exceeded the magnitude of the temperature change predicted to be the result of greenhouse gases. However, never before has such temperature variation occurred in the context of a large human population of in excess of 6 billion people.

The science of climate change suggests there are large leads and lags between when actions occur and the consequent changes in climate – possibly as much as 30-50 years. It is likely that impacts of climate change will occur over the next 30-50 years that cannot be avoided.

Further, it is not unimportant that in the year, Ian Castles, former Australian Statistician, and David Henderson, former chief economist at the OECD, have thrown doubt on the magnitude of the IPCC's projections. There is concern that an unrealistic assumption about economic growth in developing countries was used, skewing the accuracy of emissions and climate change projections. The IPCC is reviewing its calculations in light of these criticisms.

Economic Parameters

ACCI firmly believes that a strong economy is a prerequisite for a strong society. The business sector is a significant force in creating economic growth, opportunity and wealth.

Australia is rich in natural endowment and this provides us with a number of comparative advantages in the global market. As a result of this endowment, and the competitive advantages that we have accrued, Australia is in the unique position of being a world leader in the production of energy and energy intensive products.

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Although Australia's comparative advantages are not constrained to just these types of industries, it is important to note that the emergence of a price signal created in a carbon-constrained operating environment will have a proportionately greater effect on these industries.

A fundamental concern for Australian industry is that a number of our competitors do not have binding abatement targets under the current Kyoto Protocol rules. Consequently, these nations will not see a price signal within their domestic industries and will be able to enter global markets with lower cost structures. The scenario that Australian Governments must mitigate against is the situation where domestic greenhouse abatement policies introduce a price signal here that impedes our ability to remain internationally competitive.

The marginal cost of abatement will cascade through supply chains – being passed on from supplier to supplier. Ultimately, there will be a point in the chain where certain trade-exposed domestic industries will be unable to pass on the marginal cost as imported products will be less costly.

'Carbon leakage' is also a major concern. There is a possibility that new investment in industries like aluminium or LNG production could move offshore in response to cheaper energy costs in developing countries that do not have emission reduction targets.

The effect of these issues on our traded-goods sector, in terms of lost competitiveness, could potentially be significant. A disparity in price in the global market between Australian manufactured goods and competing goods may create major investment and trade distortions. This is critical and should be a major determinant when considering what suite of abatement measures should be implemented in Australia.

Although Australia because of its reform agenda is showing an increasing resilience to external shocks, we are still exposed as a player in the global economy. Combined with our reliance on trade in energy and energy related goods and services, there must be an emphasis on maintaining our cost competitiveness in the global market with whatever abatement approach we take.

Political Parameters

Australia is a federation of six states and two territories that have primary responsibility for land management and energy supply and demand. As a result, national cohesion and national consistency with policy delivery is not always possible.

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A case in point is the NSW Government's assertion 'that it will go it alone on' on greenhouse. The re-vamped NSW Electricity Retailers Scheme is an example of this policy approach. This scheme sets an overall benchmark target of 5% below 1989/90 levels by 2007 and a penalty of \$10.50 per tonne of CO₂ on excess emissions.

To deliver substantial, least cost greenhouse gas abatement it is essential that a national approach be applied. The effect of piecemeal measures is that certain industries, dependent upon location and output, will bear a disproportionate cost burden placing pressure on their domestic and international competitiveness.

Social Parameters

The issue of who pays for abatement is a critical issue. ACCI's position is that the cost of abatement should be viewed from a 'beneficiary-pays' perspective and as such, industry and the community should share the cost of abatement. This has large implications for how financial incentives and other measures that would support Australia's transition to a lower emissions signature are funded.

Costs of abatement should not be borne alone by industry, but should instead be supplemented by financial incentives and fiscal measures funded from consolidated revenue.

Policy Approaches

Given the uncertainty in relation to the extent human behaviour is impacting upon human behaviour, and the evidence that global temperatures will increase with or without a drastic decrease in greenhouse gases in the foreseeable future, the issue that warrants an obvious response is whether abatement or adaptation should be pursued as a policy priority.

The correct response is that both must be addressed, but in a way that is precautionary and flexible enough so as to allow an appropriate response to the issue as the science improves. ACCI's position is that while it is incorrect to assume that climate change does not exist (and nothing should be done) it is equally incorrect to assume that climate change is so important that there is no cost too high to tackle the problem. The correct policy approach must lie somewhere in-between and must recognise the risks as well as the costs to society of any abatement response.

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Industry needs to take a risk management approach to ‘climate-change’. Science tells us that there is a problem, but it cannot tell us definitively how it will manifest itself. A carbon-constrained operating environment is inevitable, and as a result, industry should continue to build its capacity to meet any imposed obligations commensurate with its contribution to the global problem.

In terms of measures that will achieve substantial, least cost abatement, the application of an economy-wide, or broad-based measure is meritorious. Broad-based measures are policy instruments that have the potential to capture, in theory, as many emitters, gases and sinks as possible. Theoretically, this approach has the potential to generate widespread, transparent, equitable and consistent abatement incentives. In practice, there is a growing stream of evidence to support this view.

The 2003 OECD Report – *Voluntary Approaches in Environmental Policy* - compared the relative success of broad-based, command and control, and voluntary environmental measures in a number of different countries. It found that in terms of environmental effectiveness and economic efficiency, broad-based measures should be considered by policy makers as a ‘first best’ approach.

Emissions trading and carbon-taxes are examples of ‘broad-based’ measures.

Emissions Trading

Under a “Cap and Trade” scheme, a government determines a greenhouse gas emissions cap and issues tradable emissions permits up to this limit. A tradable emissions permit is a legal right to emit a specified quantity of greenhouse gas emissions (for example, one tonne of CO₂ equivalent). This right can be bought or sold on the permit market, with the price determined by the demand and supply of permits. A government can choose how it wishes to allocate permits (including auctioning, “grandfathering” the application to various emitters and mixed systems) and where the point of acquittal will occur.

Under a “Baseline and Credit” scheme, an emissions baseline is established for greenhouse gas emitters. Liable parties whose emissions are below their baseline will be able to sell credits and those parties with emissions above their baseline can purchase these credits. That is, trading occurs for permits around the baseline.

A price signal in Australia caused by the implementation of a national emissions trading scheme, but not operating in countries that we compete against and import from, would, depending on a

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number of market conditions, impede the competitiveness of many Australian industries. Calculating the true economic costs of this is difficult as at the end of the day, it will be dependent upon whether our competitors assume any form of targets and whether these targets impose higher costs on them. Further, the ability of nations to absorb and pay for abatement will also determine the eventual economic cost to Australia.

If there were to be an international emissions trading scheme and a national scheme operating concurrently here in Australia, it is likely that Australia would be a net buyer of abatement to meet targets. To ensure that we can access the least cost credits, it is important that the international trading and sequestration environment is operating as efficiently as possible to push the international price down. If it doesn't, Australia may face higher than anticipated prices for its credits. At present, there is concern that, one model, the Kyoto Protocol is distortionary, in that, it will most likely not allow carbon credits to be accessed at a price that is least cost.

To be truly comprehensive, the trading scheme must cover as many sectors, gases, sources and sinks as possible. A major constraint preventing this would be the high transaction and administration costs that could be incurred.

Emissions Taxes

Unlike an emissions trading scheme where the cost of greenhouse gas abatement is determined by the market, a regulator would set the marginal cost of abatement (ie the emissions tax amount).

Price regulators of regulated entities have by nature a very difficult task, for they must determine a price that mimics a competitive market outcome (thereby ensuring that the 'supply' side remains profitable and is allowed to re-invest, and the 'demand' side does not pay an overly high price) but with very little information about industry efficiency and performance.

ACCI does not support an emissions tax on the grounds that the setting of a tax 'price' that is equitable and efficient is extremely difficult and is likely to understate or overstate the original objective which is to achieve a certain pre-determined abatement target.

Other Abatement Measures

When considering policy approaches, it is important for the Federal Government to couple abatement objectives with operational efficiency and competitiveness objectives.

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Australian industry must keep pace with international developments in energy use technology. In response, ACCI calls on the Federal Government to pursue policies that promote bi-lateral and multilateral relationships with nations as a means to promote investment and technology co-operation. Governments must also encourage businesses to undertake the R&D required to create innovative technology. This can be achieved through measures such as tax rebates, R&D concessions and changes to depreciation regimes.

While there are a number of technologies which offer the prospect of low or zero emissions, these at this stage are not commercially viable and do not compare with current coal-based energy sources. Although Australia should pursue renewable technologies, there is evidence to suggest that our emphasis should be on improving the efficiency of our power generation, for example by promoting coal gasification. Further, studies are beginning to show that sequestration of CO₂ in geological structures can provide large-scale greenhouse gas mitigation.

By identifying what are the least cost abatement options considering the unique characteristics of Australia, coupled with government and market incentives to adopt new technologies that promote production and abatement efficiencies, it is possible to remain competitive and adapt to developments in energy use.

Adaptation Measures

The CSIRO has concluded that climate change for Australia is inevitable and is expected to result in the following outcomes: more evaporation; more hot days and fewer cold days; rainfall decreasing in the south and east (mainly winter/spring); some inland and eastern coastal areas experiencing wetter summers; and extreme rainfall and tropical cyclones becoming more intense.

ACCI believes that Australia industry must prepare for the unavoidable climate change impacts. Industries that will be directly impacted upon include agriculture, tourism, insurance, and infrastructure. Governments are encouraged to work more closely with industry to obtain greater clarity about the potential impacts of climate change. Key considerations should include: the nature of the potential impact; the magnitude of the potential impact; the timing of the potential impact; the frequency and duration of the potential impact; and the location of the potential impact.

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Conclusion

Dealing with the climate change consequences may require some of the smartest R&D that has ever been pursued before. Australia, with its vast intellectual base will be an important player in these issues.

In working towards abating greenhouse gases and adapting to climate change, the pursuit of sustained high GDP growth must not be forgotten. Our nation deserves a balanced approach that delivers for industry and the broader community. Ratification of the Kyoto Protocol will not deliver global abatement and adaptation to climate change. It is not the solution.