Coalition Senators' Dissenting Report

1) Introduction

Coalition Senators subscribe to the position articulated by Rupert Murdoch that when it comes to carbon dioxide emissions, no matter what your personal views, "the planet deserves the benefit of the doubt."[1]

It is in the planet's and Australia's interests to reduce the world's, and Australia's, carbon dioxide emissions.

However, it is in no-one's interests for Australia to implement a flawed and bureaucratic emissions trading scheme which fails to make a measurable impact on reducing global atmospheric concentrations of carbon dioxide, while at the same time costing Australian jobs and industrial output to other parts of the world.

The so-called Carbon Pollution Reduction Scheme manifestly fails to achieve the joint aims of reducing emissions while protecting jobs.

The Government has rushed this flawed, bureaucratic and poorly detailed legislation before the Committee and is set to try and rush it through the Parliament, asking the Parliament to take them on trust, the bulk of the detail of the scheme, including shielding for emissions intensive, trade exposed industries, which will be delivered through regulation.

Labor want us to move ahead of the world, yet provide only six pages of legislation to try and cushion our emissions intensive, trade exposed industries; they have failed to model the legislation before this Committee.

Also the Government has failed to take account of the effects of the global recession, both in regard to the added risk on jobs imposing the CPRS places at this time, and the effect it has had on global emissions, which have slowed as a result and bought the world "breathing space."

Finally, due to the unnecessary rush, there has been a lack of proper consideration of alternative carbon pollution reduction schemes, such as carbon taxes, baseline and credit schemes, hybrid schemes such as the McKibbin-Wilcoxen Hybrid Model, or indeed alternative carbon pollution reduction measures such as bio-char.

2) Rushed inquiry

The Government's timetable for the introduction of the Carbon Pollution Reduction Scheme is extraordinarily rushed, especially for a piece of legislation which represents the largest structural reform to the Australian economy in decades.

[1] Rupert Murdoch, ABC "AM", 7th November 2006

The development of this legislation has been rushed by the Government and is set to be rushed into the Parliament without proper consideration.

The exposure draft of the Carbon Pollution Reduction Scheme legislation was released on the 10th March 2009, and referred to the Economics Committee for Inquiry on the 11th March 2009. Public hearings commenced just a week later, on the 18th March 2009, giving interested persons just one week – five working days – to consider the legislation.

Coalition Senators consider that this is a grossly insufficient period of time to allow interested and affected persons to properly consider the legislation and to provide considered evidence and views to the Committee.

It was therefore no surprise to Coalition Senators that a number of witnesses expressed grave concerns about the very tight timetable that the Government has allowed for this inquiry, a timetable which saw the absurd situation of witnesses giving evidence before they had had time to prepare written submissions.

For example, Ms Belinda Robinson from the Australian Petroleum Production and Exploration Association told the Committee:

> *…APPEA is concerned about the very tight timetable allowed for submissions – nine working days – and hearings, most, including this one, held before submissions are due on a package of legislation and commentary that runs for over 700 pages.* [2]

And Mrs Aileen Murrell from the Chamber of Minerals and Energy of Western Australia, noted:

> *This period of consultation, whilst greatly appreciated, is inadequate given the complexity of the proposed scheme and its potential ramifications on the Australian economy. The CME comments to the Senate committee inquiry will therefore be limited to general comments on the Carbon Pollution Reduction Scheme draft bill.* [3]

Even Professor Ross Garnaut, the author of the *Garnaut Report* commissioned by the Government, told the inquiry that he had not had sufficient time to consider the legislation:

> *…I have not, because of my many day jobs, had the opportunity to carefully go through the legislation, so I am not present myself as an expert on the legislation. I was told to come nevertheless.*[4]

When even someone with as close an interest in the Carbon Pollution Reduction Scheme has not had the opportunity to examine the legislation, it is clear that the allowed timeframe is insufficient.

As a result, this inquiry at times descended into farce, often with hours of hearings going by with no direct examination of the contents of the legislation itself.

On top of this extraordinary rush, it quickly emerged during hearings that the exposure draft legislation for the Carbon Pollution Reduction Scheme is extraordinarily light on for genuine detail.

For example, perhaps the most controversial and significant element of the Bill, that relating to the Emissions Intensive Trade Exposed industries, comprises just six pages of legislation. Six!

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[2] Committee Proof Hansard, 24th March 2009, p. E2

[3] Committee Proof Hansard, 23rd March 2009, p. E2

[4] Professor Ross Garnaut, Senate Proof Hansard, 23th March 2009, E53

Instead, the majority and substantive nature of the legislation will be enacted through regulation, should the Bill pass.

Indeed, the word "regulations" appears no less than 222 times in the substantive bill – that is, an average of over once for every two pages of legislation.

As Mrs Murrell told the Committee:

> *It should also be noted that key sections of the draft legislation, such as part 8 relating to the Emissions-Intensive Trade-Exposed Assistance Program, contained little detail, leaving a substantial amount to be set out in the regulations not planned for release until June 2009.*[5]

Further, we are told in the Commentary to the exposure draft that

> *Other elements of the White Paper package which need to be implemented through legislation are expected to be introduced with the bills referred to above, although they are not being publicly exposed at the same time. This includes legislation to implement the household assistance package and a maritime levy on emissions from shipping services provided by vessels engaged in international voyages carrying domestic cargo and domestic passengers.*[6]

Furthermore, Coalition Senators have been denied a clearer understanding of the aforementioned regulations as questions on notice put to the Department of Climate Change during the enquiry were not answered before the report was due.

Given that the household assistance package, along with the EITE provisions, is a key element of the CPRS, Coalition Senators are concerned that the Senate is being asked to deliberate on legislation which takes some $11.5 billion out of the economy in its first year of operation, and which will dramatically increase electricity and gas prices for all Australians, and yet take on trust, the Government's statement that it will subsequently introduce legislation which offsets some of these costs to the community.

Coalition Senators are extremely concerned that the Senate is being asked to essentially vote through a "blank cheque" for the Government which will enable them to detail the operation of the CPRS without the opportunity for fine-tuning and adjustment in the Parliament as is appropriate.

It is of concern to Coalition Senators that both rushed timeframes, and putting the detail in the regulations rather than the legislation, is becoming a pattern under this Government, with Coalition Senators on this committee having expressed similar concerns about another piece of legislation also considered recently by this Committee in November 2008, the Corporations Amendment (Short Selling) Bill 2008.

As the saying goes 'the devil is in the detail' and Coalition Senators believe that model regulations should be provided to the Committee for assessment.

3) The CPRS Scheme

[5] Committee Proof Hansard, 23rd March 2009, p. E2
[6] Carbon Pollution Reduction Scheme Bill 2009, Commentary, p. 13

The CPRS model of the emissions trading scheme is the Government's response to the Garnaut Report's prediction that unless carbon emissions are significantly reduced there will be a 4% increase in global temperatures.

According to the supporting documentation of the exposure draft, the objectives of the scheme are:

1. To meet Australia's obligations under the Kyoto protocol by reducing carbon emissions;
2. To support the development of an effective global response to climate change; and
3. To reduce Australia's carbon emissions to 60% below 2000 levels by 2050 and between 5% and 15% below 2000 levels by 2020.

The question Coalition Senators have sought to answer is whether these are reasonable objectives for a small country like Australia which produces only 1.4% of global carbon emissions or whether a more modest scheme, which concentrates on local reduction of carbon emissions, would be more appropriate and less costly to the Australian economy.

According to the Institute of Public Affairs (IPA):

> *"Over the past decade, Australia's economy has been buoyed up by being the quarry to the world's fastest growing economies. But notwithstanding our natural wealth, and economic reforms, we have struggled to grow at one third of the rate of less well placed countries like India and China. Moreover, the accumulation of regulatory imposts and threats, of which those on energy have increased most, is now contributing to recessionary warnings.*
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> *Australia has more to lose than almost any other country from the costs imposed by CO2 emission restraints. Cheap coal based electricity has been the bedrock on which much of our industrial development rests. Smelting industries in particular gravitated to Australia in the wake of the 1970s oil price hikes but low cost electricity has assisted the competitiveness of all our tradable goods industries. While we might speculate on the long term costs of global warming on Australia, the short term costs of increasing the price of electricity supplies are self evident.*
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> *With only one per cent of world GDP, we are neither prominent among world nations nor particularly influential within world councils. And while Australia has many well qualified scientists few of these are considered to be world authorities on climate change. Accordingly, it is pure hubris for Australia to attempt to take the lead in abatement activity."*[7]

4) Assessment of the CPRS Model

The proposed Emissions Trading Scheme (ETS) is a so called 'Cap and Trade' model under which industry will be required to obtain permits, know as Australian Emissions Units (AEUs), from the Australian Climate Change Regulatory Authority.

While the ETS will apply to a variety of greenhouse gases listed in the Kyoto Protocol, including methane, nitrous oxide, sulphur hexafluoride, hydrofluorocarbons and perfluorocarbons, these gases account for roughly 24% of greenhouse emissions and CO2 the remaining 75%.

Notably, the Rudd / Wong CPRS proposal will not apply to all Australian Industry. In fact, only about 1000 firms, considered to be the largest emitters in the country, will be required to initially comply

[7] Alan Moran, 2008, *Submission to the Green Paper on Australia's Carbon Pollution Reduction Scheme,* Institute of Public Affairs, September 9, p3.

with the scheme. It has been noted that the exclusion of petrol, for up to 3 years, reduces the coverage of the ETS by another 14%. In addition, agriculture will be excluded for 10 years and de-forestation will not be included to avoid 'practical difficulties'.

According to the background paper, the Government has not decided whether the Joint Petroleum Development Area and the Greater Sunrise Oil and Gas Field will be included in the Scheme. It is clear that the Scheme will have only restricted application in the Australian Economy and there is certainly little provision for individual Australians to have any recognition of contributions they may make to the reduction of emissions, for example, by installing solar powered hot water systems on their roofs or by having their homes designed according to principles of energy conservation.

Emissions credits (AEUs) will be treated as financial products and consequently will be regulated by ASIC. In due course, the ASX will introduce a futures market for emissions credits prior to the issue of permits, so it is said, to assist industry in managing risk.

The Government envisages linkages with similar trading schemes when established and in fact envisages Australia becoming a regional hub for carbon trading. With countries such as China, Japan, South Korea, and Indonesia, considered unlikely to establish ETSs in the near future, the concept of Australia becoming a carbon trading hub appears to be optimistic.

One of the features of the CPRS is that emitters will be able to purchase credits from other countries based on overseas mitigation programs such as forest plantations in Indonesia. Such credits will mean that Australian companies purchasing such credits will be able to produce a commensurate amount of carbon emissions above Australia's cap. Coalition Senators find it hard to understand how such arrangements can be seen as consistent with the reduction of world carbon emissions which is one of the 3 objectives of the CPRS.

5) Alternative approaches

Australia is a small country accounting for around 1% of global GDP and producing only 1.4% of world emissions. Coalition Senators believe that it is important to not lose sight of the fact that we live in a competitive world and while Australia does have some competitive advantages in attracting investment, such as political stability, a sound banking sector, reliable law and low sovereignty risk, these are only relative benefits. It would be unwise for Australia to significantly increase unilaterally the operating costs of industry in comparison to our competitors.

As stated in the Age, Mr Don Voelte, CEO of Woodside Petroleum, warned that:

> "*the proposed emissions trading scheme would cost LNG projects between 15% and 30% of after-tax profit.*"[8]

The Institute of Public Affairs has also expressed the view that it is unwise for Australia to overlook what a small player it is in the commercial affairs of the world and to imagine that adopting an ETS which imposes higher costs on industry will not put Australia at a competitive disadvantage.

Coalition Senators are of the view that any Australian ETS should be primarily concerned about encouraging reductions in carbon emissions in Australia without imposing undue increases in costs to

[8] Mathew Murphy, 'Emissions scheme threatens LNG', *Age*, 25 September 2008, p2.

Australian industry and consumers which would respectively cause economic disadvantage and loss of jobs to industry and increase the cost of consumer goods and living costs for Australian citizens. Accordingly, Coalition Senators believe that alternatives to the proposed CPRS should be considered.

Coalition Senators believe that three alternative schemes should be evaluated with those being:

A. A Carbon Tax;

B. McKibbin-Wilcoxen Hybrid Model; and

C. Emissions trading developed using the baseline and credit method, otherwise known as the Canadian Scheme.

5a) Carbon Tax

A Carbon Tax is a tax based on carbon emissions where emitters are charged / taxed a fixed amount per unit of carbon emitted. The price certainty which a Carbon Tax would provide is regarded as a significant advantage compared to the uncertainty which would prevail under the proposed auction of credits as outlined in the CPRS.

An argument used against the use of a Carbon Tax is that it would need to be periodically re-set, however Coalition Senators believe that this is an overstated problem and that the Carbon Tax for any forthcoming year could be included as an item in the May Budget along with most other taxes and any adjustments made to those taxes.

> ***Senator EGGLESTON—*** *Nobody disagrees that a global system is a great ideal, but many people think it will be a long time before it is implemented because the kind of countries we are dealing with, like Indonesia, India and Malaysia, are not going to have emissions trading schemes in the foreseeable future. So, whilst it is an ideal, it is not necessarily a very practical basis upon which to work. Some people have suggested that, in fact, a carbon tax would be a better approach and say that a carbon tax is preferable to a carbon trading system because it is more efficient, effective, simple, flexible, transparent and, more importantly, has the added benefit of providing revenue which could be used to cut other taxes, including domestic taxes. A revenue neutral carbon tax may have little or no economic cost to us in Australia. Economic cost is a big issue because it may translate into loss of jobs and have an adverse effect on our economy.*[9]

Coalition Senators concur with the view expressed in the Garnuat Report that "*a carbon tax would be better than a heavily compromised emissions trading scheme*".[10]

Most importantly however, Coalition Senators believe a Carbon Tax should be considered because it would specifically focus on addressing the need for reduction of emissions in Australia rather than overseas.

Whilst the CPRS holds grandiose overtones which promote the scheme as an example for the world to follow, Coalitions Senators cannot ignore that the CPRS represents a complicated emissions trading scheme which risks higher costs to our economy and disadvantages to our people.

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[9] Senator Alan Eggleston, *Proof Committee Hansard*, 24 March 2009, p26.
[10] Ross Garnuat, 2008, *The Garnuat Climate Change Review: Final Report,* p299. Melbourne: Cambridge University Press.

Coalition Senators repeat the view expressed in the Garnuat Report that a Carbon Tax would be preferable to a heavily compromised emissions trading scheme which the CPRS, with all its uncertainties and presumptions, will almost undoubtedly prove to be.

5b) McKibbin-Wilcoxen Hybrid Model

Professor McKibbin gave compelling evidence to the CPRS Inquiry in Canberra. It was noted that he is an advisor to the US Government on climate change and co-director of the energy and climate economics project at the Brookings Institute in Washington. Under the McKibbin-Wilcoxen hybrid model, as explained by Professor McKibbin, large emitters would be allocated long term permits which would be tradeable, within Australia (and not internationally), for carbon credits as under the current CPRS model. As well the government would issue short term annual permits at a fixed price. McKibbin believes that this model would reduce the volatility and unpredictability of carbon prices associated with emissions trading and the CPRS in particular.

Professor McKibbin provided the Committee with a copy of an address he gave entitled *"Lessons for climate policy from monetary history"* and Coalition Senators include in this report the summary given in that address as the points made are extremely relevant to consideration of this issue:

> *"To sum up: climate change policy is a serious issue. Dealing with climate change uncertainty is what matters. Any effective policy will be a major change to the Australian economy. A new market has to be created. It is not a short-term carbon market. It is not a new tax. It is a long-term market in trading climate uncertainty, which is needed at the national and global level.*
>
> *The second point is that there is still a great deal of uncertainty about where the world is heading, so if a Garnaut-type approach is taken, where you commit to a precise target or a range of targets on the off-chance that you would be able to trade your way out of it by buying cheap permits offshore, and the permit market does not develop offshore, what do you do? You may have locked yourself into an international agreement with no safety valve. Relying on the development of a global trading system without a safety valve domestically is a very risky policy.*
>
> *The final point I want to make is that we need to get away from the idea that we know exactly where we want to go and that there are no trade-offs in getting there. That's called religion. We have to deal with the trade-off between the environmental benefit of taking action, and the economic costs of getting there. If this is not acknowledged, international agreement will not occur, because it is over cost issues where the international negotiations are failing. Developing countries have bigger problems to deal with, from their own viewpoint, than climate change, but they are willing to be part of the international process if it is designed the right way.*
>
> *Monetary history has a lot to teach policymakers about how to design effective climate policy at the national level within a cooperative global agreement. It is time to move in the direction of building a transparent, credible, national or regionally focussed policy framework, with flexibility to adjust in a clear way over time towards a global concentrations goal. The almost religious focus on targets and timetables regardless of costs is the biggest hurdle to overcome in the climate change policy debate. There are better ways to generate carbon prices than what is currently proposed. One such better approach has been the focus of this presentation."*[11]

[11] Professor Warwick McKibbin, 2008, Dinner address: Lessons for climate policy from monetary history. In *Promoting Better Environmental Outcomes: Roundtable Proceedings,* Canberra, 2008, p226. Melbourne: Productivity Commission.

Coalition Senators are of the view that the stabilization of prices that the McKibbin-Wilcoxen Hybrid Model promises means that further evaluation of the McKibbin-Wilcoxen Hybrid Model is certainly justified. In addition, the McKibbin-Wilcoxen Hybrid Model, by not permitting international trading of credits, would have the desired effect of an Australian scheme focusing on the domestic price of carbon rather than Australia being drawn into the issues of unpredictability and uncertainties which will inevitably surround international carbon trading models.

5c) The Canadian Model – Baseline and Credit

The presentation by Frontier Economics in Melbourne made the point that since Australia is a small, open economy it is necessary to ensure that any scheme introduced to reduce carbon emissions needs to be economically efficient.

Frontier Economics pointed out that this is particularly the case if Australia is drawn into setting up any scheme ahead of competing nations.

Mr Price, Managing Director of Frontier Economics, made a strong case for consideration to be given to a "carrot and stick" approach, which he stated as having "*the key benefit [] that the absolute price effect through the economy is much smaller for exactly the same emissions reduction and exactly the same resource cost. So it has the same economic efficiency characteristics but the price effect is much smaller.*"[12]

The point was also made that the baseline and credit approach which he proposed would avoid what he described as the "*need to churn billions and billions of dollars of revenue*"[13] as would be the inevitable outcome, as he stated, of the CPRS system proposed under the Rudd / Wong plan.

Another point of concern which the Canadian model addresses is the negative impact the proposed CPRS will have on complementary programs and voluntary actions. As explained by Mr Price:

> *"the way the CPRS works is that if complementary measures are put in place by other state governments, or if voluntary actions are undertaken by consumers, all that does is leave additional emissions that are allowed to be produced by industry. It undermines the incentive for voluntary action and undermines the effectiveness of complementary measures that governments put in place at the federal, state and local levels because the way these schemes work is that it is a target that is consistent through time, irrespective of the economic conditions. It provides investors with a great deal of certainty. It maintains the task for producers and consumers to continue to reduce emissions through time. It does not give them a let-up if the economy goes back a little bit. It still keeps the pressure on reducing emissions through time and it does not undermine the incentive for voluntary action or complementary schemes."*[14]

Coalition Senators are of the view that voluntary action and complementary schemes should not be rendered ineffectual in the overall plan to reduce carbon emissions. Many people, whose votes were influenced by the Labor Government's promised action on carbon emissions, would be greatly discouraged if the proposed CPRS disempowered them, allowing for emitters to benefit from their voluntary actions rather than the environment.

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[12] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p70.
[13] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p72.
[14] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p72.

Frontier Economics also made the point that the CPRS scheme inadvertently benefits higher emitters and removes the incentive for those higher emitters to reduce their emissions:

> *"the CPRS creates some perverse impacts in that it tends to reward higher emitters in the compensation arrangement than lower emitters and in fact discourages high emitters from reducing their emissions."*[15]

Coalition Senators are concerned about this possibility and took note of Mr Price's comments regarding the need for a stable price for carbon:

> *"Because the emissions task is constant through time under the scheme we are promoting, carbon prices will be far more stable through time. We spend a lot of time with investors in the energy sector in particular and the one thing they like is stable commodity prices or prices against which they can decide their investments. The last speaker I heard talked about the European emissions price rising and collapsing rapidly according to what happened in the regulatory arrangements. You will see the same thing with the CPRS through the course of re-establishing the so-called gateways. Prices will rise and collapse as you come close to those gateways. It will create lot of price instability. Price instability makes it very difficult for investors to make long-lived infrastructure investments. This type of arrangement provides much more stable prices."*[16]

Mr Price concluded by making the point that a Canadian style cap and credit scheme would probably produce a relatively lower cost of electricity and thus a lessened impact through the general macro-economy. Mr Price stated that he believed the cost savings if this approach was applied just to electricity would be *"…in the order of $300 billion to $400 billion cheaper than the CPRS."*[17]

The baseline and credit or intensity scheme model, which Frontier Economics promoted at the hearings, was said to be "*…a scheme design which is more dominant around the world and more prominent in Australia in terms of operations*." It was further claimed by Frontier Economics that "*it received virtually no attention in the course of any analysis that Professor Garnaut undertook.*"[18]

Coalition Senators are of the view that intensity schemes should be given further consideration as a possible model for an Australian ETS in view of the clear economic benefits such a scheme is said to offer.

6) Underlying assumptions

The Rudd / Wong CPRS scheme depends for its success on three underlying assumptions. These are firstly, that there will be an international market established for carbon trading and that most countries in the world, including Australia's major trading partners, will introduce ETSs. The second assumption is that the process of accounting for the volume of permits traded internationally will be valid and can be relied upon as financial documents in good standing and thirdly, that the MRET target of 20% of Australia's power being provided by renewable energy is achievable.

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[15] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p72.
[16] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p72-3.
[17] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p73.
[18] Daniel Price, *Proof Committee Hansard*, 24 March 2009, p81.

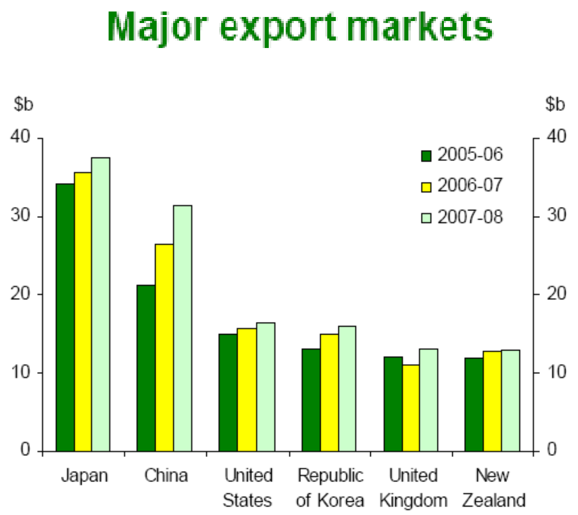
Regrettably there is doubt about all of these assumptions being realized.

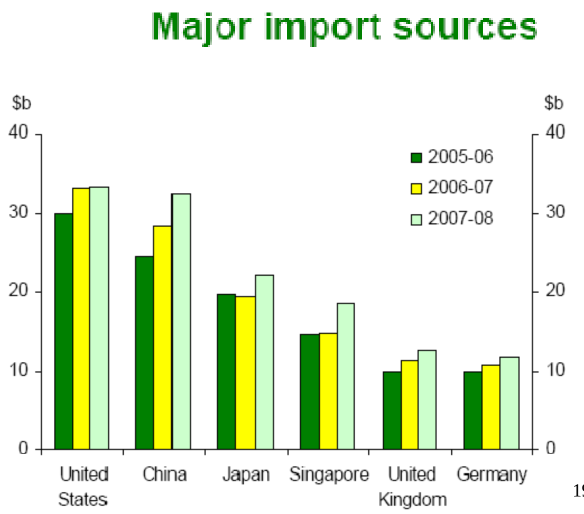
The establishment of an international carbon market

The Rudd / Wong CPRS depends heavily on the establishment of an international carbon market enabling countries with ETSs to trade in carbon in which Australia would participate. In fact, the existence of an international market for carbon credits is integral to reducing the cost burden of an ETS on Australia as trading in international credits is expected to put downward pressure on the price of permits by enabling the purchasers of permits to buy them where they are cheapest.

For a carbon market to have any meaning Australia's major trading partners would have to be involved, otherwise Australia would find that the added cost of an ETS would put Australia at a competitive disadvantage.

Australia's major trading partners are now in East Asia, including China, Japan, Korea and Singapore, while the USA, the UK, and Germany remain significant trading partners as shown in the graphs below.





[19]

Of the above countries, the UK and Germany, as members of the European Union, are participants in their ETS and New Zealand has established its own ETS.

The patterns of world economic power and trade are changing as is demonstrated by the growth of the Chinese economy and in considering future patterns, India must also be recognised as being a growing economic power with which Australia will become increasingly engaged in future years.

Alan Moran, in an article entitled "Climate Change: China's approach" referring to the 2008 White Paper issued by the Chinese Government, said:

> *"In a notable turn, the White Paper shifted the policy priority to adaptation. This is a recognition that China (and therefore others in the developing world that embark on a rapid growth path) will*

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[19] Department of Foreign Affairs & Trade, 2008, *Composition of Trade 2007-08.* Canberra: Commonwealth of Australia.

not initiate serious abatement measures at least until Western levels of emissions are reached. And in this respect the White Paper discusses cumulative levels of emissions which would justify China out-emitting Western countries on the basis of the past levels of emissions. A corollary is that the sort of CO2-e levels of emissions said to be required to stabilise the warming effect will not be reached."

In a similar review article on Japan, entitled "Japan and Global Warming Policies", written in November 2008, Alan Moran wrote:

"Other sources confirmed that Japan is taking a de facto approach that involves no action of a substantive nature. Japanese industry is very concerned to combat measures that would add to its costs and retard growth. It also takes the view that it is highly efficient already and points out that the Japanese use less energy than others domestically due to the smallness of their houses, a matter which called forth deprecating comment from the western media not long ago. Even so, the policy approach followed is not consistent with the 3-4 tonnes per capita average global emission levels that would be required if CO2 levels are to be stabilised at the 550 ppm level."

On the likelihood of Japan introducing an ETS, Alan Moran wrote:

"Japan will participate in all international matters and contribute to carbon savings but is not considered at all likely to introduce a tax or ETS that involves any disciplines on industry."[20]

With respect to the USA establishing an ETS, Tim Wilson claimed in his March 2009 paper already referred to above, that:

"the US has made it clear that it will not participate in a post-Kyoto agreement without the involvement of developing countries. And despite postulations by President Obama, the US will not be in a position to make significant cuts to its emissions. Obama's recently appointed Special Envoy on Climate Change, Todd Stern, said that the 25 to 40 per cent emissions reductions committed to in the Bali Road Map were "not possible" for the United States. And his comments have been echoed by the head of the Intergovernmental Panel on Climate Change, Rajendra Pachauri, who said recently that President Obama would face a "revolution" if he committed to deep cuts in emissions.[21]

From this it would seem that there are reasonable grounds for doubt that an international ETS market involving many of Australia's major trading partners will be established in the foreseeable future.

Reliability of Carbon Permits as Financial Instruments

In his previously mentioned article, Tim Wilson also raised questions about whether the volume of permits traded internationally will be valued appropriately and could be relied upon as financial documents in good standing:

"Carbon markets operate essentially the same as a normal financial market. The value of a financial product is diminished the more are issued, or the credibility of the equity to underwrite the financial product is uncertain. If a carbon permit is traded at a certain price it is essential that

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[20] Alan Moran, 2008, 'Japan and Global Warming Policies', Institute of Public Affairs Occasional Paper, November 2008.

[21] Tim Wilson, 2009, 'Australia's delinked and non-compliant Emissions Trading Scheme', Institute of Public Affairs Occasional Paper, March 2009, p15.

"the value of the credit will be maintained". If the government issues too many permits, or cannot substantiate the equivalent carbon emissions for the permit, it loses value. And with the loss of value goes the credibility and certainty provided in the market, the incentive to invest and the credibility for linking markets. Bowen lays out the conditions for, an efficient and effective global emissions trading market as:

• Having efficient rules and administrative arrangements (including monitoring, enforcement and penalties).

• Including all major suppliers of, and demand for, permits.

• Ensuring that supply and demand for permits delivers a price on carbon that is enough to encourage abatement, yet not so high as to dramatically reduce growth.

• Delivering certainty.

Similar conclusions followed from an EU simulated exercise on emissions trading, and the Government's White paper."[22]

Wilson adds:

"Yet currently most of the infrastructure necessary to provide certainty doesn't exist in countries, including developed countries. In Australia the Federal Government is still collecting initial data of Australia's emissions from the private sector. And Australia is significantly more advanced than most other countries.

That would mean establishing government infrastructure in all participating countries to be able to monitor, account and enforce their emissions; and have credible permits equivalent to their emissions sufficient that investors want to buy those permits. As Peterson argues "permit trading can only be an efficient instrument if emission and permit trade are monitored and accounted appropriately and if compliance is enforced".

But without such regimes the certainty of each country's emissions are questionable. The Kyoto Protocol requires Annex 1 countries to have a "national system for the estimation of anthropogenic emissions by sources and removals by sinks of all greenhouse gases". Considering the serious economic transactions taken on the basis of national reporting of their emissions and the subsequent volume and value of permits, estimations provide limited certainty to investors."[23]

This conclusion, in turn, raises the question of whether Australia's carbon reduction program should be designed to be linked into an international emissions trading scheme or whether it would be more practical and prudent for an economically small nation like Australia, contributing just 1.4% of world emissions, to develop a more simple program concentrating on reducing domestic emissions, such as a Carbon Tax.

Renewable Energy

A key underlying presumption of the CPRS is that renewable energy will provide an increasing contribution to base load power needs and an MRET of 20% has been set for 2020 which will require around 12 gigawatts of power to be generated from renewable sources.

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[22] Tim Wilson, 2009, 'Australia's delinked and non-compliant Emissions Trading Scheme', Institute of Public Affairs Occasional Paper, March 2009, p10.

[23] Tim Wilson, 2009, 'Australia's delinked and non-compliant Emissions Trading Scheme', Institute of Public Affairs Occasional Paper, March 2009, p11.

The view has been expressed that the Renewable Energy Industry will be the principle beneficiary of the CPRS were it to be introduced, in the sense that the Renewable Energy Industry will be the recipient of large amounts of funding in the hope of breakthroughs in the output and efficiency of renewable energy mechanisms. However the reality is that Australia is not well endowed with cheap renewable energy sources such as hydro-power. Unlike Norway and Switzerland, Australia does not have large snow covered mountain ranges capable of delivering large amounts of hydro-power.

Instead, with our principle hydro-power sites in the Snowy Mountains and Tasmania plus small units in locations such as Kununurra in the Ord Dam, hydro-power accounts for only 5% of Australia's power supply. The next most important source of renewable energy is wind power with wind farms located chiefly in Southern Victoria, Tasmania and the South and Mid-west coasts of Western Australia.

Wind power is regrettably inconsistent in power deliver due to fluctuations in the flow of wind and is never expected to provide much more than 10% of Australia's renewable energy and even then at a high cost.

Solar power is obviously the most abundant source of renewable energy available in Australia but although much research over many years has gone into developing the technology so far, there is currently no possibility of solar cells providing base load power for Australian power grids.

Other possibilities are harnessing tide and wave movements to produce power, but so far the technology for these forms of power have not progressed sufficiently to be considered a viable source of base load energy. Similarly while research into energy production from geothermal sources is being carried out, there is a long way to go before geothermal energy can become a source of cheap base load power.

Given this the inclusion of a target of 20% of Australia's power to be generated from renewable sources seems unlikely to be achievable, at least within the time frames under consideration and probably not for many years.

Again, the Coalition Senators are disturbed that yet another of the key underlying presumptions of the CPRS appears to be optimistic to say the least, if not unrealistic in fact.

7) Treasury Modelling

Coalition Senators continue to be frustrated by the fact that the Government has been unable to produce any economic modelling to justify its claims about the likely effect of the CPRS upon jobs and upon the environment.

While the Government continues to claim that it has done modelling, the reality of the matter is that the Treasury modelling referred to does not specifically model the CPRS legislation.

While Treasury did model a number of scenarios, including a five% cut (the minimum under this legislation) that modelling was based on a number of premises; those being, a global agreement to reduce carbon dioxide emissions being in place by 2010, China signing up in 2015, and India in 2020.

However, the CPRS legislates a minimum five percent cut irrespective of what happens in the rest of the world – irrespective of whether global agreement is reached in Copenhagen later this year, irrespective of whether China comes on board, irrespective of whether India comes on board, irrespective even of whether the US comes on board.

On top of this, the Government concedes that the Treasury modelling cited in explanation of the CPRS does not take into account the global economic crisis.

The model used by the Treasury in doing their modelling – the general equilibrium model – assumes that there will be a seamless adjustment in the labour market between one area and fails to take account of the inevitable massive short and medium term dislocation as a result of the employment changes the CPRS will inevitably bring about.

As the Acting Secretary of the Department of Climate Change, Mr Blair Comley, told the Committee:

> ***Mr Comley*** *- "If you have a full employment closure of a CGE model then essentially you have assumed that the labour released in one area, if there is a change in the relative growth rates of a sector, will be absorbed elsewhere."* [24]

Coalition Senators understand the real world to be different to the CGE model used by Treasury, and that while short to medium term job losses and social dislocation can be explained and "absorbed" elsewhere in Treasury's modelling, this will not be the case in real world.

Concerns about the accuracy of the Treasury modelling are not only held by Coalition Senators and affected industry, but even by the social services sector.

As Tony Westmore, of the Australian Council of Social Services, told the Committee:

> *"We are very concerned that the Treasury modelling may be wrong, that provisions that are in place may be inadequate…"*[25]

Coalition Senators are therefore of the view that until the Government produces modelling of its proposed legislation, which, amongst other things, takes into account the current global recession, it is virtually impossible to make a considered judgement of the effect of the CPRS upon the economy and upon jobs. Coalition Senators note that despite an absence of Government modelling, various industry groups have presented evidence illustrating the potential of the CPRS to have significant impacts.

8) Effects of a recession

There has been much debate in the public arena, and indeed evidence to this inquiry, regarding whether a recession is the right or wrong time to be moving ahead with such a significant structural change to the economy.

Both sides of these arguments were encapsulated by Professor Ross Garnaut, who stated:

> *Is it a good or a bad time in a recession to introduce mitigation measures? It is a very good time to introduce support for new low-emissions technologies because the opportunity cost of labour*

[24] Committee Proof Hansard, 30 March 2009, E27
[25] Committee Proof Hansard, 23 March 2009, E26

and capital is low…. So I think now is a very good time for a big emphasis on public support for research, development and commercialisation of the new technologies. [26]

However, Professor Garnaut also noted:

On carbon pricing, there is a reason to be somewhat cautious about putting an extra cost on some firms while the recession continues because of financial fragility during recession.[27]

Coalition Senators agree with both of these statements. Now is a very good time to be investing in new, low emissions technologies and research. But it is a very risky time to be putting an extra cost impost on firms already under significant financial pressure.

Further, while distressed about the current state of the world and Australian economy, which is being made worse by the Rudd Government's actions, Coalition Senators note that the recession does provide some breathing space in terms of time to address carbon dioxide levels.

Indeed, it is axiomatic that as industrial output falls, so too will emissions.

This point is conceded by the Government themselves; noting that Australia's level of emissions fell in 1990 in conjunction with Paul Keating's "recession we had to have" and did not return to 1990 levels until 1997.

While it is impossible to quantify exactly how much of this fall was due to the fall in industrial output in the recession, as opposed to contributors such as changes to land-clearing regimes, there is no doubt that the recession did slow emissions output.

Senator Abetz: Are you saying that the recession had any impact on the reduction?

Dr Gruen: Undoubtedly the recession would have had some impact.[28]

This view was supported by Professor Ross Garnaut, who while not advocating for a delay in passing the legislation, did state:

Clearly, the deep global recession is pulling emissions well below what they otherwise would have been. Emissions may have actually fallen in the September quarter and since…my best guess is that if the world was not doing anything about mitigation this would put back the level of emissions of the world by two or three years. ***That is equivalent to a pause in emissions for two or three years.***[29] *[emphasis added]*

Unfortunately, more elaborate consideration of this issue has been limited by the Department of Climate Change's failure to provide Coalition Senators with answers to their questions in time to be included in this report.

Coalition Senators are therefore strongly of the view that this evidence supports our argument that it is better to take a bit of extra time, and to get the emissions reduction mechanisms right, rather than rush a scheme into place which is ill-considered, flawed, bureaucratic and which won't achieve the stated outcomes.

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[26] Committee Proof Hansard, 23 March 2009, E65
[27] Committee Proof Hansard, 23 March 2009, E 65

[28] Committee Proof Hansard, 25 March 2009, E8
[29] Committee Proof Hansard, 23 March 2009, E60

We should use the “breathing space” provided by the current global circumstances wisely.

9) CPRS and the WA Electricity Market

Griffin Energy, in their submission to the inquiry into the exposure draft of the CPRS, made the point that the Western Australian Electricity Market, in which gas power generation is dominant, suffers discrimination because the Treasury modelling uses the same competitive spot market assumptions made for the Eastern States Electricity Market in its assessment of the need for ESAS assistance.

In fact however the WA Electricity Market is very different to that of the Eastern States Electricity Market in that WA has a high dependency for electricity generation on gas from the North West Shelf being carried to the South West in the Dampier to Bunbury pipeline, and this will continue to be the case even if renewable replace coal.

Griffin Energy point out that there is a historic price competition between gas and black coal in the Western Electricity Market and state that WA’s long term security of supply will likely be compromised by the current CPRS settings.

Griffin points out that the so call National (i.e. Eastern States) Electricity Market is based on a competitive spot market into which all generators supply electricity whereas the Western Electricity Market is based on bilateral contracts.

In the selling model the price of electricity is locked in for the length of contracts and there is no capacity in the Western Electricity Market to pass through to consumers the increasing price of carbon which the generators will bear over 15 years. By contrast in the National Electricity Market Model, based on competitive spot prices, the additional cost of carbon over 15 years will be passed through via the market clearing price.

Griffin states that the Western Electricity Market requires a separate ESAS formula with an emissions intensity cut off limit of 0.75tCO2e.

Griffin suggests that this can be achieved by amendments to part 9, division 2 with a separate section 176A in the legislation which allocates WEM assistance to eligible assets and that there should be a separate section 182A to deal with the annual assistance factor applicable to the Western Electricity Market which will apply a consistence design methodology to both the WEM and NEM based on the relative proportions and intensities of each market.

Given the fact that the Wester Electricity Market will be based increasingly on gas and renewable energy while the Eastern Market will remain coal based, the Coalition Senators request Treasury to recognise that different circumstances apply in WA and implement Griffin’s suggestions.

10) CPRS and its impact on agriculture

The Government’s decision to avoid addressing Australian agriculture within the context of a Carbon Pollution Reduction Scheme (CPRS) until 2015 is alarming. Agriculture contributes 16% of Australia’s emissions and the Senate Committee’s report on the proposed introduction of the scheme acknowledges that after stationary energy, agriculture is a leading CO2e emitter. Yet the report and proposed legislation has deferred any policy decisions for the agricultural sector until at least 2013.

Subsequently, there is insufficient policy debate on the impact the CPRS will have upon agriculture and the regional economy.

This section of the dissenting report aims to readdress the considerable short-coming of the majority report by highlighting significant problems and issues raised in a series of independent reports which conclude that a CPRS will have a dire impact on the agricultural sector. This section of the dissenting report also expresses its concern that, particularly within a rural and regional context, the CPRS is a policy which is more akin to international "grandstanding" than sound policy for the economic or social well-being of all Australians. This report commends the work of the Australian Farm Institute, the Centre for International Economics and the Australian Bureau of Agricultural and Resource Economics, each having made a contribution to better understanding the impact of a CPRS on agriculture.

This report shares the concerns of the Australian Farm Institute that a CPRS and associated carbon trading will cause a decline in agricultural output but fail to produce any benefits in terms of global greenhouse emissions.[30] This report agrees with the Australian Farm Institutes' hypothesis that if a CPRS and associated emission trading scheme were introduced, agricultural production in Australia would be cut by $2.4 billion a year by 2020 and $10.9 billion a year by 2030.

The CPRS will negatively impact farm enterprises in two ways; firstly, the indirect rises in costs associated with farm inputs, secondly, after 2015 farms are financially liable for emissions attributed to their farming enterprise.

There is no doubt that the CPRS will increase the price of fuel and electricity. In the agriculture sector this will be a rise in a range of production costs. Contracts for cropping, pasture chemicals and fertilisers will increase by 5%.[31] ABARE also acknowledges an increase in production costs of 2.4 per cent across industries. It argues those costs are relatively small because of the range of assistance being offered by Government. ABARE highlight that there will be fuel credits for the first three years of the scheme and assistance in the price paid for fertilisers and chemicals.[32] This report, however, views the government assistance as an artificial subsidy funded by the taxpayer to support an overambitious greenhouse policy. Speculatively, there is also a concern about how our major trading partners and WTO may interpret this kind of assistance given a climate of greater trade liberalisation and a reduction in agricultural subsidies. Another perspective of the rise in costs and international trade is the impact it will have on Australia's competitiveness. Agricultural exporters in South America, Asia and Eastern Europe will not be subject to the same rises in input costs.

This report shares the view of the Australian Farm Institute that if farmers are made to pay for emissions it has attributed after 2015 farm cash margins will suffer. Modelling suggests that a broadacre farm can expect severely reduced incomes in 2016.[33] Even if farms are declared Emissions Intensive and Trade Exposed farmers can expect a reduction of up to 25%. [34]

When viewing the impact of the CPRS in terms of a cost/benefit analysis for the agricultural industry it becomes clearly apparent that for the billions of dollars lost in production and export we gain little

[30] Keogh, M & Thompson, A, Preliminary modelling of the farm-level impacts of the Australian greenhouse emissions trading scheme, Australian Farm Institute, September 2008.
[31] *ibid*, 8
[32] Ford, M, *et al*, Issues Insight, Agriculture and the carbon pollution Reduction Scheme: Economic Issues and implications, ABARE, March 2009.
[33] Keogh, M & Thompson *op.cit*, 2008.
[34] *ibid*

in the global reduction of carbon pollution. The Coalition is of the opinion that the introduction of the CPRS is detrimental to competitiveness in agricultural trade, the sustainability of farming and food security. From an agricultural perspective and the perspective of those rural and regional areas based on the agricultural economies the risk is too great for the small reward.

From an agricultural perspective there are a number of other policy incentives which could be incorporated to reduce carbon emissions in the sector. The funds spent on compensating the agricultural industry could be best directed toward increases in research and development which will improve farm productivity and develop sound emissions mitigation technologies.

The absence of any clear plan for the agriculture sector in developing the CPRS and its legislation is of a great concern to the Coalition considering the impact it will have upon producers. It demonstrates a city-centric perspective that ignores the important role agriculture plays in Australia's national economy. Subsequently, from a rural and regional perspective, which bases itself upon a robust agricultural economy, this legislation cannot be presented to Parliament.

11) Emissions Intensive, Trade Exposed (EITE) industries

Unless there is meaningful global action, Coalition Senators are in absolutely no doubt that should the CPRS be implemented as proposed, not only will Australian jobs be exported to nations without emissions trading or a carbon tax, so to will emissions.

Indeed, this view has been acknowledged by the Minister herself.[35]

We have already expressed our serious concerns about the lack of detail in the legislation setting out support for emissions intensive trade exposed industries (just six pages), and that the Senate is being asked to take on trust what the Government will regulate in this space.

While initially eligible EITE industries will get either 90% or 60% free permits, Coalition Senators are also concerned that because of the 1.3% so-called "carbon dividend" that over time the value of these permits will be eroded and that Australian industry will suffer a death of a thousand cuts.

As the President of the ACTU, Ms Sharan Burrow told the Committee:

> The 1.3 per cent reduction, which of course came down from four per cent in the original paper, is something that as a blanket piece probably needs further consideration. There will be some industries that will struggle to make that 1.3 per cent, but others, including some of the largest companies, will do it much more easily.[36]

Coalition Senators are also doubtful of claims put to the Committee that the likelihood of so-called "carbon leakage" is overstated. While the Department of Climate Change claims that there is "very little" evidence of carbon leakage in Europe as a result of their emissions trading scheme, this is hardly surprising given that virtually all emissions intensive, trade exposed industry is exempted from the European scheme.

[35] Penny Wong, *Sydney Morning Herald,* 23rd February 2009
[36] Proof Committee Hansard, 24th March 2009, p. E84

As to the Treasury's modelling which claims there is "little evidence of carbon leakage"[37], this claim means nothing given that the Treasury did not actually model the CPRS as it stands – that is, Australian action irrespective of global action.

In defending the charge that the CPRS in isolation will lead to businesses going offshore, witnesses resorted to school-boy style debating tactics:

> ***Mr Cameron*** *– "… I am unimpressed by the idea that businesses move from one jurisdiction to another because a modest price of carbon is imposed by a government in the public interest. I would very much like to see the farewell speech of the business leader to his or her staff saying, 'We're leaving the country to set up offshore because we cannot carry the obligations to reduce our emissions within this jurisdiction. We are going to carry on polluting and thereby creating risk to your fellow citizens. By the way, you're losing your jobs too.' I just do not regard that as a plausible argument and I would very much like to see the CEOs make that speech and then wave them goodbye at the airport."*[38]

While one may agree or disagree with Mr Cameron's comments, as Senator Bushby pointed out[39], this simplistic answer does not address the fact that Australian-made goods will be disadvantaged against those produced without the impost of a carbon price.

It also fails to take account of the very real likelihood of business – rather than closing an existing operation – simply deciding against further investment in Australia and instead investing in countries without a carbon price.

It is for these reasons that Coalition Senators again express their serious concern about Australia imposing a carbon price on our industry, through the CRPS, before the rest of the world has signed up to a similar scheme.

12) A tax or not a tax?

Coalition Senators are extremely concerned that, even at this stage, with the Exposure Draft legislation being considered by this committee, the Government is unclear as to whether the CPRS is a tax or not.

Reflecting this uncertainty, the Government has even introduced three additional "technical" bills "in case" at some time in the future the emissions units under the CPRS are considered a tax.

> *Three of the draft bills are technical bills, in case the charge for Australian emissions units issued as the result of an auction or fixed charge is, at some time in the future, considered to be taxation.*[40]

When asked directly, the head of Treasury's macroeconomic group, Dr David Gruen, simply said he did not know.

> *Senator Abetz: "My question is this: is the CPRS a tax or is it not a tax"?*
>
> *Dr Gruen: "I simply do not know what the legal status of it is.*

Even proclaiming:

[37] *Australia's Low Pollution Future,* p xiv
[38] Mr James Cameron, Climate Change Capital, Committee Proof Hansard, 19th March 2009, p. E 25
[39] Senator David Bushby, Climate Change Capital, Committee Proof Hansard, 19th March 2009, p. E 25
[40] Commentary, p. 12

Dr Gruen: “I am not sure we are the right people to ask”. [41]

It is astounding that a senior Treasury official would not only not know the answer to this question, but suggest that Treasury should not be expected to know. Whether or not the CPRS is a tax has serious, complex and potentially costly financial implications for affected parties, which one would expect Treasury to have considered.

In regard to whether or not the CPRS is a tax, Coalition Senators make note that once again, their capacity to scrutinise the CPRS has been limited by the Department of Climate Change not providing responses to written questions on notice in time for inclusion in this report. These are basic questions and the failure to answer them proves that the entire CPRS process is rushed and flawed.

Notwithstanding the Government’s confusion, Coalition Senators consider that given that the CPRS looks like a tax, smells like a tax and talks like a tax, it is a tax.

13) Conclusion: The need for global action

Everybody, even Minister Wong, agrees that without meaningful global action to reduce carbon emissions, any action taken by Australia in isolation (or relative isolation) to reduce carbon emissions would have no impact on total global emissions while costing Australian jobs.

> ***Minister Wong****: “There is no point in putting a cost on carbon pollution in Australia if it simply results in jobs and emissions being exported to countries that do not yet face a carbon price.*
>
> *To overlook the perverse environmental outcome that would result from emissions simply being exported to other nations is environmentally irresponsible, and disingenuous in the extreme.”*[42]

Therefore, central to the debate about whether Australia should introduce the CPRS at this time is the issue of whether Australia is leading the world; and whether, if so, Australia should be leading the world, irrespective of actions the rest of the world may or may not take.

On the one hand, the Government claims that Australia, in implementing the CPRS, is acting in concert with the rest of the world:

> **Dr Parkinson**: *“…I think it is seriously misleading to pretend that Australia is somehow ahead of the rest of the developed countries.”*[43]

However, on the other hand, the Government admits that very few countries have actually committed to real action. As noted by Dr Parkinson, Secretary for the Department of Climate Change:

> *“Setting a cap on most of your national emissions means that you have a guaranteed way of meeting your national objectives. Without a cap, targets are only ever aspirational.”*[44]

He then went on to note:

> ***“Few countries have announced specific quantitative commitments to medium-term targets.”*** [emphasis added] [45]

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[41] Committee Proof Hansard, 25th March 2009, E6
[42] Penny Wong, *Sydney Morning Herald,* 23rd February 2009
[43] Committee Proof Hansard, 18th March 2009, p. E5
[44] Committee Proof Hansard, 18th March 2009, p. E5

Coalition Senators have noted that the reality is that only very few countries actually have emissions trading schemes in place, namely, the European Union (where the scheme has been roundly criticised for failing to deliver CO_2 reduction outcomes) and New Zealand.

It is the view of Coalition Senators that it is foolhardy in the extreme to actually legislate to commence an emissions trading scheme without knowing what may be decided at this year's critical Copenhagen Conference.

While it may be the view of the Government that to do so would provide "leadership", there was no evidence presented to this inquiry that if Australia were to legislate the CPRS as proposed it will somehow force key developing nations to come on board.

It compromises Australia's negotiating position and puts at risks thousands of Australian jobs by locking us into a scheme when it is possible that the rest of the world may say, at this time of economic uncertainty, that action should be delayed.

Accordingly, Coalition Senators recommend that the exposure draft Carbon Pollution Reduction Scheme not be presented to Parliament, and that the Government go back to the drawing board before presenting a properly modelled and considered plan to the Parliament which reflects the outcomes of this year's Copenhagen climate change meeting and the best interests of Australia.

Senator Alan Eggleston
Deputy Chair

Senator David Bushby

Senator Barnaby Joyce

Senator the Hon. Eric Abetz

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[45] Committee Proof Hansard, 18th March 2009, p. E9