Chapter 5
Deferral of operation

5.1 On 4 May 2009, the Government announced 'a delay in the start date of the Carbon Pollution Reduction Scheme of one year to manage the impacts of the global recession.'[1] The delay will also be accompanied by a fixed permit price of $10 for the first compliance year of the scheme (July 2011–June 2012). This change to the timing and structure of the scheme is designed to provide greater business and investment certainty.

5.2 Table 5.1 shows the revised timetable for the introduction of the CPRS.

Table 5.1: Revised timetable for introduction of CPRS

Mar- June 2009	Consultation on exposure draft legislation; Senate committee inquiries
May 2009	Bills introduced into parliament
June 2009	Desired passage of bills
Sept qtr 2009	Regulator established
Dec qtr 2009	Legislative instruments tabled in parliament Copenhagen UN Climate Change Conference
First half 2010	Scheme caps to 2014–15 and gateways for 10 following years set
July 2011	Start of first compliance year (with fixed price permits)
First half 2012	First auction of permits
June 2012	End of first compliance year (with fixed price permits)
July 2012	Start of second compliance year
Oct 2012	Deadline for lodging of emissions reports for first year
Dec 2012	Deadline for surrender of permits for first year

Source: from *White Paper*, table 16.2; Minister for Climate Change, *Press Release*, 47/09, 27 February 2009; Prime Minister, Treasurer and Minister for Climate Change and Water, 'New measures for the carbon pollution reduction scheme', Media release, 4 May 2009.

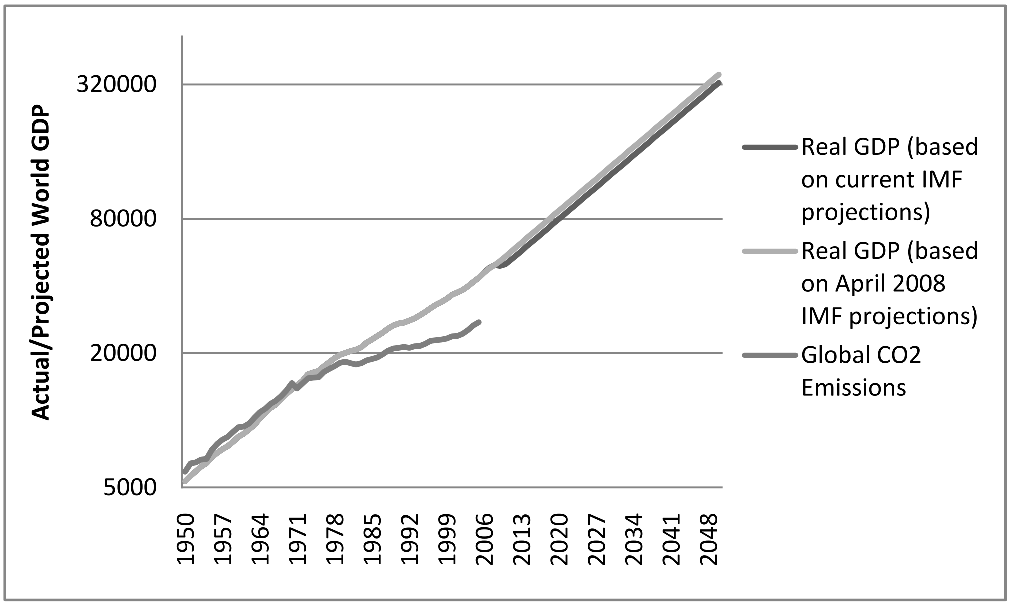
1 Prime Minister, Treasurer and Minister for Climate Change and Water, 'New measures for the carbon pollution reduction scheme', Media Release, 4 May 2009.

The global financial crisis and the delayed start

5.3 The economic outlook has deteriorated sharply over the past year. The size of the deterioration is illustrated by Chart 5.1. This shows the growth of global real GDP since 1950 (the upper line) and two forecasts—one based on the current International Monetary Fund projections and one based on those made a year ago.[2] The chart is on a logarithmic scale, so the slope of the lines represents growth rates.

5.4 The lower line in the chart shows the path of global CO_2 emissions. It is notable that the price signals arising from the mid-1970s oil crisis led to a marked slowing in emissions relative to economic activity.

Chart 5.1: Global real GDP and CO_2 emissions



Sources: Chart generated by Secretariat based data from IMF, *World Economic Outlook*; A Maddison, *The World Economy: Historical Statistics*, OECD, 2003; World Resources Institute, CAIT database.

5.5 The Department of Climate Change explained that the global financial crisis drove the delayed start date, (as well as the use of a fixed price for the first year of the scheme and the augmentation of the emissions-intensive trade-exposed assistance).[3]

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2 The IMF's April 2008 *World Economic Outlook* has projections to 2013 and the April 2009 issue out to 2014. In both cases the forecasts have settled down to around 4.8 per cent growth in the final projection years and this growth rate is assumed to continue to 2020 in the chart. The CO_2 emissions exclude those due to land use change and forestry. The units used in the chart are billions of 1990 (international Geary-Khamis) dollars for GDP and millions of tonnes for CO_2 emissions.

3 Mr Blair Comley, Deputy Secretary, Department of Climate Change, *Proof Committee Hansard*, 22 May 2009, p. 7.

5.6 Professor Garnaut does not believe that the global financial crisis is a good economic reason for delaying the start date but concedes it makes prompt action more politically difficult:

> It does affect the political difficulty of achieving an Australian and international policy outcome that reflects Australia's national interests. The depth of recession is a good time to invest in the new processes and industries that will make Australia's low emissions economy of the future [but]…as we know from long history that includes the depressions of the 1890s and 1930s, the recession makes the political process even more vulnerable than usual to pressures from vested interests.[4]

5.7 The World Wildlife Fund was concerned that the recession should not be seen as buying us time compared with the required path:

> Our view is very strongly that this scheme should be implemented as soon as possible. However, I think the main consequence of the fixed price, the postponement for a year, and indeed the global recession buffer and the additional money for energy efficiency is that it will quite significantly mute the near term signal to foster transformational low emissions technologies, not just garden variety low emissions technologies like wind but really significant low emission technologies like geothermal, marine or very large scale solar.[5]

5.8 The deferral of the starting date was welcomed by many business representatives:

> We welcome the delay in the CPRS commencement date…[6]

> A start date of 2011 will allow resolution of the complex EITE process, improving Australia's prospects of getting the right policy both designed and legislated.[7]

> Intergen (Australia) welcomes…a deferred start date till 1 July 2011…[8]

> …the CPRS should not start operation until economic conditions return to normal and there is a greater probability of this occurring by mid-2011.[9]

5.9 However, some business representatives were critical of the delay:

> A delay to the start date has the simple effect of delaying commitments to low emissions investments.[10]

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4 Professor Ross Garnaut, *Proof Select Committee on Climate Policy Hansard*, 16 April 2009, p. 45.

5 Mr Paul Toni, World Wildlife Fund, *Proof Committee Hansard*, 29 May 2009, p. 62.

6 Leighton Holdings, *Submission 18*, p 1.

7 BP Australia, *Submission 19*, p 3.

8 Intergen (Australia), *Submission 11*, p 1.

9 Caltex Australia, *Submission 27*, p 2.

10 Hydro Tasmania, *Submission 25*, p 3.

> ...delaying the commencement of the Scheme will have significant disadvantages for both the liable entities covered by the Scheme, as well as the carbon market services sector who are critical in providing liquidity.[11]

5.10 The Department of Climate Change also noted the impact of the crisis on some businesses' ability to prepare for the scheme, given the additional resources required to survive the recession:

> In terms of deferral, some businesses had raised a question of preparedness in advance of the scheme, but that was also partly in the context of the global financial crisis, because a number of firms were essentially saying that it was difficult for them to allocate additional time to those issues in the context of the current economic circumstances.[12]

5.11 Most witnesses and submitters who argued for a delay in the scheme were focussed on factors other than the global recession, including the importance of waiting for an international agreement to be reached, the damage that a premature start may have on Australian exporters' international competitiveness or the perceived deficiencies in the proposed scheme.

Committee View

5.12 The Committee acknowledges concerns that the global recession means that an early implementation of the CPRS may place undue pressure on some businesses. However the Committee feels that the crisis does not diminish the need for the implementation of the CPRS's comprehensive and ambitious mitigation strategy in the near future.

Business certainty and timing of the legislation

5.13 What is relevant for businesses making long-term investment decisions is not the timing of when the scheme starts but the rules that will govern the scheme over the medium- to long-term. For this reason, even if it is accepted that the global financial crisis is a valid reason for deferring the starting date, many business representatives called for the legislation to be passed in 2009:

> …certainty about the timing and the rest of the details of the CPRS were essential to enable business to plan for and respond to the impacts of the CPRS.[13]

> BP continues to support the case for policy action and certainty around climate change: until energy producers and consumers know and pay the cost of carbon, the uncertainty associated with planning and investing in the

11 Carbon Markets and Investors Association, *Submission 34*, p 3.

12 Mr Brian Comley, Deputy Secretary, Department of Climate Change, *Proof Committee Hansard*, 22 May 2009, p. 7.

13 Ms Maria Tarrant, Business Council, *Proof Committee Hansard*, 22 May 2009, p. 19.

> transition to a low carbon economy will remain high…we believe that the Government has largely 'got it right' with respect to many of the emissions trading design issues. [14]
>
> We support passage of the legislation this year...our members say that uncertainty is disruptive to business planning and is causing investment to be withheld.[15]
>
> We note that after significant debate over many years, both the current Government and its predecessor reached the conclusion that a cap and trade scheme was the best way forward...The longer we wait to address climate change, the more it will cost in the long term and the less flexibility Australia will have to transition to a lower-emissions economy when we do decide to start. We would like to see legislation passed to effect this cap and trade regime as soon as possible to address the continuing uncertainty for business, particularly in relation to capital intensive investment decisions.[16]
>
> …the Shergold report, which said that waiting until a truly global response emerges before imposing an emissions cap will place costs on Australia by increasing business uncertainty and delaying or losing investment.[17]
>
> We encourage the Government and opposition parties to move forward with the legislation by resolving the serious outstanding issues and complexities and passing the Bills.[18]
>
> Uncertainty in the regulatory framework is hindering investment decisions.[19]
>
> IGCC supports the introduction of the CPRS and supports its early passage through the parliament…Until a clear start date for emissions trading is set by the parliament, both debt-financing arrangements for these emissions-intensive assets and companies, and investment activities to support them will be delayed.[20]

5.14 One counterargument is that, to the extent the legislation is predicated on there being an international emissions trading scheme, it may be better to wait until after the Copenhagen Conference, or beyond, when more may be known about the design of other countries' schemes.

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14 BP Australia, *Submission 19*, pp 1-2.

15 Mr Peter Burn, Australian Industry Group, *Proof Committee Hansard*, 29 May 2009, p. 13.

16 Origin Energy, *Submission 32*, p 1.

17 Mr John Connor, *Proof Committee Hansard*, 29 May 2009, p. 57. The former government's Prime Ministerial Task Force on Emissions Trading (the 'Shergold report'), 2007, concluded 'However, waiting until a truly global response emerges before imposing an emissions cap will place costs on Australia by increasing business uncertainty and delaying or losing investment. Already there is evidence that investment in key emissions-intensive industries and energy infrastructure is being deferred' (p. 6).

18 CSR, *Submission 6*, p 1.

19 CO2 Group, *Submission 37*, p 2.

20 Investor Group on Climate Change, *Submission #*, p 1.

5.15 The Department of Climate Change disagreed with this view, arguing that the Copenhagen agreement will not be:

> … predicated on a particular view of a way mitigation is carried out at least uniformly in the rest of the world. It is predicated really on the view that, to the extent that Australia will take on emissions reductions commitments, it is desirable to use a mechanism that is the lowest possible cost way of achieving those emissions reductions.[21]

5.16 Other witnesses agreed that the discussions at Copenhagen will centre on targets, not the design of schemes. There is therefore no reason to delay legislation on aspects of the scheme other than the targets.

> We are not going to have any more insight about the optimal design of our domestic scheme as a result of the outcome at Copenhagen.[22]

> …we ought to, and we can, design a system that accommodates the range of possible outcomes from Copenhagen and subsequent international forums…[23]

5.17 Professor Ross Garnaut explained to the Committee his view that even before the Copenhagen Conference, it is clear that the direction in which the rest of the world is heading is towards a cap-and-trade emissions trading system (ETS):

> … it is very clear the way the Europeans are going. They are putting a lot of effort into cleaning up their ETS…There is no doubt where Europe is headed… The [United States] congress is now headed towards a cap and trade system and ETS… Japan and Korea will be heading that way. The main developed countries will be heading that way.[24]

5.18 The Committee notes that there had been claims that there was inadequate time to prepare if the legislation passed in 2009 envisaged a starting date in July 2010. On the same logic, delaying passing the legislation until 2010 would cause problems in meeting a July 2011 starting date.

Credibility at Copenhagen

5.19 The other main argument for passing the legislation soon is to bolster Australia's credibility at Copenhagen:

> …with respect to the international negotiations, Australia going to Copenhagen with a scheme capable of delivering large emissions reductions will have an impact on the international negotiations which,

21 Mr Blair Comley, Deputy Secretary, Department of Climate Change, *Proof Committee Hansard*, 22 May 2009, p. 4.

22 Dr Brian Fisher, *Proof Committee Hansard*, 29 May 2009, p 48.

23 Mr Peter Burn, Australian Industry Group, *Proof Committee Hansard*, 29 May 2009, p 15.

24 Professor Ross Garnaut, *Proof Committee Hansard*, 22 May 2009, p. 15.

> through that process, leads to an outcome in terms of potential global emissions.[25]
>
> …passing this legislation now will be of assistance. It will send important signals to the international negotiations that an advanced country can actually tackle these elements.[26]
>
> …the proposal to delay the vote on the emissions trading scheme until next year would weaken Australia's negotiating impact at the crucial UN talks in Copenhagen in December.[27]

5.20 It could be argued that it is particularly necessary for Australia to have legislation already passed, rather than just promised, as Australia could be viewed as having 'form' for not implementing agreed measures. After successfully negotiating a very favourable target at the Kyoto negotiations, Australia did not ratify the treaty (until a decade later).

5.21 The main counterargument is a claim that Australia is so unimportant that anything it says or does will be ignored:

> …we are a small player here. We are one per cent of emissions and we have about that same sort of level of influence worldwide... Not only are we relatively trivial… Certainly, when I have visited overseas and talked about Australia's climate policy nobody has known anything about it. We really do not count.[28]

5.22 The Committee found more convincing the evidence from other witnesses that what Australia says and does will matter. For example, Professor Ross Garnaut, who in addition to being a distinguished economist is a former ambassador to China, said:

> Australia in isolation will have a significant effect on the global discussion of climate policy which will affect global climate… it is a fact of political science and economic science that what Australia does is relevant to a global agreement.[29]

5.23 Daniel Price, an expert on electricity markets, gave an example of how Australia can be very influential in energy policy reforms:

> Australia was in fact a year ahead of the UK in spot electricity markets… I know from my own experience that there has been a conga line of advisers

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25 Mr Blair Comley, Deputy Secretary, Department of Climate Change, *Proof Committee Hansard*, 22 May 2009, p. 8.

26 Mr John Connor, Climate Institute, *Proof Committee Hansard*, 29 May 2009, p 54.

27 Mr Owen Pascoe, Australian Conservation Foundation, *Proof Committee Hansard*, 29 May 2009, p 68.

28 Dr Alan Moran, Institute of Public Affairs, *Proof Committee Hansard*, 22 May 2009, pp 30 and 34.

29 Professor Ross Garnaut, *Proof Committee Hansard*, 22 May 2009, p. 16.

> coming to Australia over the last decade to see how we have gone about doing that. So Australia can play an important policy leadership role.[30]

5.24 He also commented that the global press had reported Australia delaying the start of the CPRS scheme:

> Very interestingly, the delay was actually reported in newspapers in China, Japan, Korea and also in Europe. It was relevant to the international press…[31]

5.25 Among the advanced economies Australia ranks in the top five emitters, behind only the US, European Union, Canada and Japan. Furthermore, as the largest per capita emitter in the OECD, Australia's stance will be more closely watched than its share of global emissions might suggest.

The transitional fixed-price year

5.26 The final CPRS legislation introduced by the government includes a transitional price cap of $10 for the compliance year beginning July 2011 (see Table 5.1).

5.27 The *Garnaut Review* advocated stating with a fixed price, albeit twice as high:

> During the transition period, permits should be sold by the independent regulatory authority at $20 per tonne…[32]

5.28 The Australian Industry Group does not believe that the certainty created by the $10 price cap will influence investment decisions:

> The substantial incentive for investment in renewable energy is the long-run price curve for carbon. It is not really what the price will be in 2011-12 because no-one seriously makes an investment looking only at that term. We are talking about investments that live for 20-plus years. If anyone looks at that price curve, that is what the key driver of renewable energy will be and that is why even the renewable energy target scheme is proposed to be phased out, because it is recognised that that is the driver of investment in renewable energy… One-year price caps' impact on that is very much at the margin.[33]

5.29 The WWF was far from strong in their support of the fixed price aspect of the Government's changes:

> **Senator EGGLESTON—**Some people were a bit critical of the fact that there will be an unlimited number of permits issued at a fixed price of $10

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30 Mr Daniel Price, Chief Executive, Frontier Economics, *Proof Committee Hansard*, 22 May 2009, p. 35.

31 Mr Daniel Price, *Proof Committee Hansard*, 22 May 2009, p .35.

32 *Garnaut Review*, p 350.

33 Mr Peter Burn, *Proof Committee Hansard*, 29 May 2009, pp 23–24.

> per tonne for the first year… What do you say about that? Would you rather see auctions instituted immediately?
>
> **Mr Toni—**In an ideal world I would. As I said, the WWF is supportive generally of the proposals that the government has put…[34]

5.30 The Australian Conservation Foundation:

> …oppose a low fixed starting price of carbon at $10 per tonne. We think the market should be operating fully and we support a market operating from 2010. So, no, we do not think a fixed price for permits is the way to go. Certainly we should allow the strengthening mechanism to operate and to provide that carbon pricing. We need to encourage investment in clean energy and energy efficiency. A $10 carbon price really does not provide the incentive that you need to see off the mark.[35]

5.31 Treasury's modeller has said that:

> …the one-year delay is unlikely to significantly change the results [of the economic modelling] over the average to 2020.[36]

Impact on Revenue

5.32 Some witnesses expressed concern about the impact of the price cap on revenue. Environment Business Australia's view is that:

> Well, firstly, if all the permits in the CPRS were auctioned and that money hypothecated depending on whose analysis you use, that would create anywhere between $14 billion and $20 billion a year.[37]

5.33 The revenue raised in the first year could be as little as half what was originally anticipated because of the price cap (Table 1.1). This reduces the revenue available to the Government for household assistance. However, the lower assistance should be offset by similarly smaller increases in prices for household items such as electricity as a result of the lower carbon price.

Committee View

5.34 The Committee feels the $10 price cap is an appropriate transitional mechanism which will allow for the early introduction of a carbon price and then appropriate market based price flexibility once the results of the Copenhagen negotiations are known.

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34 Mr Paul Toni, *Proof Committee Hansard*, 29 May 2009, p. 64.

35 Mr Owen Pascoe, *Proof Committee Hansard*, 29 May 2009, pp 68 and 73.

36 Ms Meghan Quinn, Treasury, *Proof Committee Hansard*, 22 May 2009, p. 8.

37 Ms Fiona Wain, *Proof Select Committee on Climate Policy Hansard*, 15 April 2009, p. 47.