



4 June 2009

The Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
CANBERRA ACT 2600

By email: economics.sen@aph.gov.au

Dear Secretary

Re: Submission to the Senate Standing Committee on Economics Inquiry into the Carbon Pollution Reduction Scheme Bill 2009 and related bills

BlueScope Steel Limited and OneSteel Limited welcome the opportunity to make a submission to the Senate Committee on Economics.

Under the banner of BOSMA (The Bureau of Steel Manufacturers of Australia Ltd) both companies have engaged with government throughout the development of its proposed Carbon Pollution Reduction Scheme (CPRS).

The global financial crisis and economic recession aside, the introduction of a domestic emissions trading scheme is the single most important public policy issue facing the Australian iron and steel industry.

We believe that the CPRS, as currently proposed, will disadvantage the competitiveness of the Australian iron and steel industry for a potentially worse environmental outcome. The changes announced by the Government on 4 May 2009 were welcome improvements, which go some way towards addressing our concerns about the scheme's impact on the iron and steel industry's trade competitiveness. However, there are still a number of significant outstanding issues that we believe must be addressed before the scheme is passed into law. In summary these are:

- **Effective rate of assistance:** The effective rate of assistance (i.e. the proportion of the industry's total emissions covered by free permits) is likely to be significantly less than the headline rate of 94.5% because significant portions of the businesses will not receive any assistance. The current draft EITE Activity definitions, which determine the activities to qualify for assistance, are inadequate, because they exclude significant parts of our businesses, particularly our hot rolling operations. Exclusion of hot rolling in this manner is inconsistent with international practice (e.g. EU ETS; NZ ETS) and with the point at which the bulk of competition occurs, especially in the domestic market (which is from hot rolled products onwards). The precise steelmaking activities that will be eligible for assistance are the subject of ongoing discussion with government, but we believe hot rolling – at both integrated and satellite mills – must be included in the EITE activity definitions for integrated iron and steelmaking and electric arc furnace steelmaking.

We also remain concerned that EITE activities will be defined in regulations rather than legislation, despite the fact that these definitions will be crucial in determining whether the Government delivers on its commitment to ensure no competitive disadvantage for EITEs. Similarly, the eligibility criteria for EITE assistance and the timing and rate of decay in EITE assistance – both critical issues for the iron and steel industry - are also not dealt with in the Bill but will be dealt with in regulations.

- **Scope 3 costs:** We are very concerned about the potential pass through of emissions costs from suppliers (Scope 3 costs) especially in relation to emissions associated with the extraction of metallurgical coal, the iron and steel industry's most significant source of Scope 3 emissions. Scope 3 costs could exceed Scope 1 and 2 costs for the iron and steel industry, given that both companies source the majority of their coking coal from the Illawarra region, which has gassy mines.
- **Decay in EITE assistance:** The annual decay in assistance (1.3% annual "productivity dividend") is likely to rapidly exceed the industry's capability to abate its emissions, given current technology. This results in a significant risk that the CPRS will simply act as a tax rather than as an incentive to reduce emissions. We believe the decay in assistance should be moderated and more closely tied to demonstrable international action on carbon pricing, including amongst our major competitors.

It is the iron and steel industry's view that these three issues must be addressed before the CPRS legislation is passed by the Parliament this year. In the case of matters that will be dealt with in regulations, this could be achieved by ensuring these regulations are introduced to the Parliament in a timely manner this year, coincidental with the legislation. We believe these changes to the design of the scheme are necessary if the Government is to meet its own environmental and economic objectives.

The iron and steel industry further believes that it is important to get a clear understanding of the design of emission trading schemes that our major trading partners may be considering. The initiation of draft legislation for a US emissions trading scheme is one such key example. This US legislation is a major milestone in progress towards a global approach to climate change policy. This breakthrough is not something that Australia can or should ignore, but it has not been taken into account in the design of Australia's CPRS.

Given the global significance of the US, we believe that it is important to obtain a clear understanding of the design of United States' emissions trading scheme, including its provisions for assistance to EITEs, and to fully consider the implications of the US approach for the design of Australia's CPRS. The current draft US legislation appears to differ markedly from the Australian scheme in a number of important respects, including the later commencement date, broader activity coverage for affected sectors including steel, and a more prescriptive and quantitative test for international action.

The precedent set by the US is particularly important for the iron and steel industry. Approximately 30% of BlueScope Steel's exports from its Australian operations go to the United States. The Australian steel industry also competes with US steel producers in third party export markets. It is essential that material differences between Australian and US climate change legislation do not distort our trade competitiveness.

At a minimum, the Government should ensure that the important precedent set by the US is acknowledged, and that it has sufficient flexibility to adjust the CPRS as US policy becomes clearer. This will assist in ensuring that Australian industry is not put at a disadvantage with respect to its international trade competitors.

Although opportunities are constrained by technological limits, Australian steelmakers are prepared to reduce their emissions but can only fund major abatement expenditure if they remain economically competitive.

We believe it is important to take the time required to get this complex policy reform right. This is particularly important in the present global economic downturn when the Australian iron and steel manufacturing industry is facing extraordinarily severe conditions.

Yours sincerely



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1. The Australian Steel Industry's Position on the CPRS

Steel is a fundamental building block of the nation's infrastructure and demand for this product is driven by the needs of a modern economy and community.

OneSteel and BlueScope Steel are the leading firms in the Australian iron and steel industry. Together, the two companies employ approximately 20,000 people in Australia and exported over \$1.6 billion in steel products in the last (2007/ 2008) financial year.

The global economic crisis and the possibility of domestic recession aside, the Government's approach to climate change is the single most important public policy issue currently facing the Australian iron and steel industry.

We support the Australian Government's stated public policy objectives for the Carbon Pollution Reduction Scheme (CPRS); that is, to reduce greenhouse gas emissions while maintaining the competitiveness of Australian emissions-intensive trade-exposed (EITE) industries.

However, there is a clear danger that the CPRS as currently designed will fail to meet the Government's environmental and economic objectives, and instead severely disadvantage the Australian iron and steel industry for potentially a worse environmental outcome.

It is highly unlikely that the world's largest steel manufacturing countries, such as China, will impose comparable carbon costs in the short to medium term. Even in the European Union, under the current second phase of the EU emissions trading scheme, iron and steel manufacturers receive 100% free permits for their direct emissions until at least 2012.

The approaches taken with respect to emissions reduction by our major trading parties are of great significance to Australia's international competitiveness. For example, recent legislative developments in the United States clearly will be very important to what emerges on climate change policy at a global level. The draft bill for the *American Clean Energy & Security Act of 2009*, or Waxman-Markey Bill, was released in May 2009. There is obviously a great deal of political debate ahead to determine the precise terms of the US legislation. However, there is no doubt that the Waxman-Markey Bill is among the most important pieces of environmental legislation ever contemplated in the world's largest economy which is also a major source of the globe's greenhouse gas emissions.

The initiation of draft legislation for a US emissions trading scheme is clearly a major milestone in progress towards a global approach to climate change policy. This breakthrough is not something that Australia can or should ignore. However, it has not yet been taken into account in the design of Australia's emissions trading scheme.

Given the significance of the policy reform under consideration in Australia, it is important to obtain a clear perspective on the design of trading systems such as that proposed in the United States. The current draft US legislation appears to differ markedly from the Australian scheme in terms of the commencement date, broader activity coverage for affected sectors including steel, and reductions in EITE assistance subject to more prescriptive and quantitative criteria for measuring international action.

The precedent set by the US is particularly important for the iron and steel industry. Approximately 30% of BlueScope Steel's exports from its Australian operations go to the United States. The Australian steel industry also competes with US steel producers in third party export markets. It is essential that material differences between Australian and US climate change legislation do not distort our trade competitiveness.

In summary, the Government needs to fully consider the implications of the approach of major trading parties, such as the United States, with respect to the design of the Australian CPRS. These considerations should also include the commitment to amend the CPRS, should international trading systems such as that proposed by the US negatively impact on the competitiveness of Australian EITEs such as the steel industry.

2. Why the EITE assistance proposed in the CPRS is inadequate

The CPRS as currently designed would impose a highly significant cost burden on the domestic iron and steel industry that will not be borne by our larger global competitors. These costs would be very difficult to bear in good economic times. In the context of the deep economic downturn – globally and in Australia – the cumulative costs of the CPRS are intolerable and are very likely to cause a fall in profitability, investment and jobs.

The changes announced by the Government on 4 May 2009 were welcome improvements, which go some way towards addressing our concerns about the scheme's impact on the iron and steel industry's trade competitiveness. However, there are still a number of significant outstanding issues that we believe must be addressed before the scheme is passed into law. In summary these are:

- **Effective rate of assistance:** The effective rate of assistance (i.e. the proportion of the industry's total emissions covered by free permits) is likely to be significantly less than the headline rate of 94.5% because significant portions of the businesses will not receive any assistance. The current draft EITE Activity definitions, which determine the activities to qualify for assistance, are inadequate, because they exclude significant parts of our businesses, particularly our hot rolling operations. Exclusion of hot rolling in this manner is inconsistent with international practice (e.g. EU ETS; NZ ETS) and with the point at which the bulk of competition occurs, especially in the domestic market (which is from hot rolled products onwards). The precise steelmaking activities that will be eligible for assistance are the subject of ongoing discussion with government, but we believe hot rolling – at both integrated and satellite mills – must be included in the EITE activity definitions for integrated iron and steelmaking and electric arc furnace steelmaking.
- **Scope 3 costs:** We are very concerned about the potential for the pass through of emissions costs from suppliers (Scope 3 costs) especially in relation to emissions associated with the extraction of metallurgical coal, the iron and steel industry's most significant source of Scope 3 emissions. Metallurgical coal is mostly sourced from the Illawarra collieries, which are gassy mines. BlueScope Steel is a captive customer of the collieries, with dedicated rail infrastructure established to bring coal from the collieries to the nearby Port Kembla Steelworks. There is currently no infrastructure for shipping and storing alternative supplies of coal. OneSteel also purchases the bulk of its metallurgical coal from these mines. The government has yet to finalise its approach to dealing with the coal industry under the CPRS. For the iron and steel industry, Scope 3 costs could exceed Scope 1 and 2 costs and the government's approach to emissions from the coal industry will be important to determining the costs of the CPRS to the Australian steel industry.
- **Decay in EITE assistance:** The annual decay in assistance (1.3% annual "productivity dividend") is likely to rapidly exceed the industry's capability to abate its emissions, given current technology. This results in a significant risk that the CPRS will simply act as a tax rather than as an incentive to reduce emissions. We believe the decay in assistance should be moderated and decay in assistance more closely tied to demonstrable international action on carbon pricing, including amongst our major competitors.

In addition, the Renewable Energy Target scheme will impose further costs on the industry, although we acknowledge that the partial exemption from RET proposed by the Council of Australian Governments (COAG) will ameliorate these costs. It is important to note, however, that until EITE activity definitions are settled for iron and steelmaking the extent of any residual RET costs remains unclear.

The CPRS, even as modified in the current CPRS bills, will impose unsustainable costs on the steel industry and significantly damage its competitiveness, with investment and jobs put at risk. Our key competitors are not likely to face these carbon costs in the short to medium-term, which will compound the negative impact on the Australian iron and steel industry.

We believe that the CPRS should be amended to address the above three core issues, thereby reducing this cost burden on the domestic iron and steel industry, protecting the industry's international competitiveness and providing genuine incentives to reduce emissions.

As well as taking issue with the CPRS as designed, the companies have concerns with the Government's approach of placing details of the EITE program in regulations rather than in the Bill itself and the speed with which the Government is seeking to implement these significant changes. These concerns relate to:

- a) The Bill inappropriately delegating legislative power for, in effect, the whole of the EITE assistance program;
- b) The Government not adhering to the policy of providing transparency and business certainty by not including details of the EITE assistance program in the draft legislation;
- c) The Government acting inconsistently and inequitably in its treatment of EITE industries compared with other industry sectors receiving assistance under the scheme; and
- d) Insufficient government consultation on draft legislation for the EITE assistance program as a result of this detail being left for the regulations.

We have attached more detailed comments on these issues for the Committee's consideration.

3. Conclusion

We believe that an affordable and sustainable emissions trading scheme that does not alter the Australian iron and steel industry's competitive position would:

- Move in tandem with, and not ahead of, our competitors and other major emitting economies including the United States;
- Recognise the technological constraints on abatement in steel making;
- Provide incentives for investment in abatement;
- Reflect the current economic crisis;
- Minimise the risks to jobs, competitive manufacturing industry and the economy; and
- Include appropriate transitional mechanisms.

If the CPRS is to proceed, the Government must ensure that the design of the CPRS offsets the competitive disadvantage of emissions-intensive, trade-exposed industries. If it does not, the danger is that job losses and a decline in investment will be inevitable – for possibly a worse environmental outcome.

The threat to the competitiveness of Australian EITE's in the revised CPRS bills is still apparent. The CPRS should act in concert with the rest of the world, not ahead of it, and ensure no material competitive impact on the Australian iron and steel industry ahead of major international competitors.

We believe that the introduction of an emissions trading scheme warrants the close attention of the Committee and we thank the Committee for its consideration of our submission on this major environmental and economic reform.

Attachment: Submissions regarding the legislative process for introduction of the Carbon Pollution Reduction Scheme (CPRS)

We have previously made submissions to the Senate Committee on Economics regarding the Exposure Draft of the Carbon Pollution Reduction Scheme Bill 2009 (“**CPRS Bill**”). We continue to have concerns regarding the Government’s decision to place details of the EITE assistance program in the regulations (a draft of which is yet to be released) rather than in the Bill itself.

Our concerns are that by not including details of the EITE assistance program in the CPRS Bill:

- The CPRS Bill inappropriately delegates legislative power;
- The Government is not adhering to its fundamental policy of providing transparency and business certainty;
- The Government is acting inequitably in its treatment of industry sectors; and
- The Government is not undertaking sufficient consultation on the regulations.

In our view, the regulation-making power contained in Section 167 of the CPRS Bill inappropriately delegates legislative power. It provides that, matters which should be regulated by Parliament are to be dealt with by subordinate legislation. Details of the EITE assistance program should be created and maintained in the CPRS Bill.

EITE assistance program

An assistance program for emissions-intensive trade-exposed industries (“**EITE assistance program**”) has formed a fundamental element of the Government’s Carbon Pollution Reduction Scheme through all stages of scheme design and parliamentary process. The Government’s Green Paper, White Paper and Explanatory Memorandum for the CPRS Bill all contained details of how the EITE assistance program was intended to operate, including:

- Eligibility criteria for EITE assistance;
- The level of assistance to be provided to EITE activities; and
- The timing and rate of decay in EITE assistance.

None of these fundamental elements of the EITE assistance program have been included in the CPRS Bill. Nor has the Government published a draft of the regulations for the EITE assistance program. Instead, Section 167 of the CPRS Bill only provides that the regulations *may* formulate an EITE assistance program.

The exclusion of details of the EITE assistance program from the CPRS Bill is inappropriate for the following reasons:

- The EITE assistance program forms a fundamental element of the Carbon Pollution Reduction Scheme. It is appropriate that this fundamental element be subject to the transparency and scrutiny provided by the parliamentary process.
- While details of the EITE assistance program have been provided in Government papers, and policy changes have been announced as they have occurred, no draft legislation or regulations have been published to date which contain the details of the EITE assistance program. This means that, in considering and voting on the CPRS Bill, the Senate does not have before it draft legislation covering all key aspects of the scheme.
- The CPRS Bill does not require that an EITE assistance program be established, it simply provides that one “may” be. The inclusion of the EITE assistance program in the regulations rather than the CPRS Bill does not provide the Senate or affected industries with sufficient clarity or certainty regarding whether and to what extent the Government will in fact establish and maintain EITE assistance. This uncertainty is heightened because regulations may be disallowed by either House of

Parliament, meaning a key element of the scheme could be cancelled at any time by the government or combined opposition parties of the day.

- The treatment of EITE industries under the CPRS Bill is inequitable compared with the treatment of other industries. The CPRS Bill describes the circumstances in which coal-fired generators will receive assistance whereas it does not for EITE industries.

Previous submissions and changes to the draft legislation

The Bureau of Steel Manufacturers of Australia has previously made submissions to both the Department of Climate Change and to the Senate Standing Committee on Economics in response to the Exposure Draft of the CPRS Bill regarding this issue.

The Government appears to have responded to these submissions by including additional detail in the CPRS Bill regarding the basis on which the five-yearly independent reviews of assistance will be conducted (refer to section 353(1)(h) of the CPRS Bill), but has not provided any additional certainty to EITE industries in the CPRS Bill regarding the fundamental elements of the EITE assistance program that will be established from scheme commencement.

Conclusion

In light of the importance of the EITE assistance program for Australian industry and the Carbon Pollution Reduction Scheme, it is crucial that the transparency and scrutiny afforded to a Bill are applied to the details of the program. The EITE assistance program should be created and maintained in an Act.

- Ends -