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The Carbon Price

Understanding the key details

The carbon price policy package has been released.

The package is a solid first step toward a clean economy and a safe climate. It has more support for renewable energy, energy efficiency and biodiversity than the Rudd Government's Carbon Pollution Reduction Scheme (**CPRS**). Several features of the industry assistance package and the carbon price mechanism itself have also been improved.

This Briefing Paper sets out the key elements of the scheme (see outline below) and on pages 5–6 identifies the areas to watch in the coming weeks.

In this Briefing Paper

What has been announced?

An emissions trading scheme

Despite what you might have heard, it's an emissions trading scheme, not a carbon tax. Polluting companies have to buy permits for each tonne of greenhouse gases (GHG) they emit. Permits will be issued by the Federal Government (**the Government**) and can then be traded between companies via the carbon market. What may be confusing is that the scheme has two phases: a fixed price phase and a floating price phase. The first phase runs from 1 July 2012 to 1 July 2015, where permits can be bought for a fixed price — a scheme which, economically, functions like a tax. The second phase runs from 1 July 2015 onwards, where a limited number of permits can be bought for a price set by the market. This will be an emissions trading scheme (ETS).

HOW DO EMISSIONS TRADING SCHEMES WORK?

- The purpose of an ETS is to make activities that produce carbon pollution more expensive, to reflect the cost that their pollution has on the environment, and make low pollution alternatives comparatively cheap and attractive.
- Only the biggest polluters will need to buy permits to pollute, but they will pass their increased costs to their buyers which will encourage their buyers to also choose low polluting options.
- Polluters can choose whether it is cheaper to reduce their emissions by investing in new practices, or to buy permits and keep polluting.
- A trading cap will limit the number of permits available, thus ensuring that overall emissions will reduce

The price

The starting price is $23 per tonne of GHG. That price will increase by 2.5% in real terms for three years until 1 July 2015. On 1 July 2015, the permit price will be set by the market. However, the scheme includes a price floor and a price ceiling for the first time. The price floor will be $15, meaning no permits can be bought for less than $15 after 1 July 2015. The price ceiling (that is, maximum permit price) will be set by 31 May 2014 at $20 above the expected international permit price in 2015–16.

The transition

The transition from a fixed price to a floating price will happen on 1 July 2015. This removes any doubt about the transition to full emissions trading, thereby giving business the certainty that they need to shift their investments from polluting industries to clean industries. The Australian Network of Environment Defenders Offices (**ANEDO**) asked for this change in its submission to Government on the carbon price.[1]

The cap

The permit price after 1 July 2015 will depend on the 'cap' — the maximum amount of permits to pollute that the Government makes available. The cap is different from the Government's emissions reduction target (because it does not cover the entire economy) but is an important tool to reach those targets. The cap will be set by the Government on the advice of the Climate Change Authority (**CCA**) — a new independent statutory body similar to the Climate Change Commission in the United Kingdom. ANEDO asked for this kind of body during consultation with the Government.[2] Caps will be set five years in advance, with the first five caps set no later than 31 May 2014. The caps will be set by regulations (which either house of Parliament can disallow). Voluntary action will be taken into account in setting the caps.

1 ANEDO submission to the Department of Climate Change and Energy Efficiency, 10 May 2011, pp.7–8.

2 ANEDO submission to the Department of Climate Change and Energy Efficiency, 10 May 2011, pp.6–7.

The targets

The Government has increased its long-term emissions reduction target. In addition to maintaining its commitment to cut emissions by 5% from 2000 levels by 2020, it has now committed to an 80% reduction by 2050 (up from 60%).

Coverage

This scheme covers fewer polluters than the CPRS would have. Whereas the CPRS was expected to apply to about 1000 companies, this scheme is expected to apply to about 500. The key criterion of coverage remains the same: any facility emitting more than 25,000 tonnes of CO2e (carbon dioxide equivalent) will be a 'liable entity'. However, some sectors are excluded from this criterion. Agriculture, land and forestry are all excluded, and dealt with exclusively by the Carbon Farming Initiative (**CFI**).

Fuel is not covered by the carbon price mechanism at all. The Government will in effect apply a carbon price on fuel through changes to the fuel tax credits and aviation fuel excise. This will not apply to light commercial vehicles (4.5 tonnes or less), to the agriculture, forestry or fisheries industry, or to households. The Government also wants to impose a carbon price on heavy on-road transport by 1 July 2014, which is a 'Government-only' measure (that is, one that the Multi-Party Climate Change Committee (**MPCCC**) did not support). The Productivity Commission will review the fuel excise regime to see whether it can be amended to reflect the emissions intensity of each fuel (i.e. impose higher excise on those fuels that emit more carbon per unit of energy).[3]

Gases

The scheme will only apply to four GHGs (carbon dioxide, methane, nitrous oxide and perfluorocarbons). The other two major GHGs (hydrofluorocarbons and sulphur hexafluoride) will face an equivalent carbon price under existing synthetic greenhouse gas legislation.[4]

Permits

Permits will be personal property. This means that the permit itself is the legal property of the emitter like any other form of property. ANEDO opposed this on the grounds that it could limit the Government's ability to amend and administer the scheme.[5] It would be better if permits were legally classified as a limited licence to emit GHG. This would allow permits to be traded as normal, but would give the Government more power to amend the scheme if it needed to. This is the approach taken in emissions trading schemes in most other countries, including all the major schemes in the United States.

International linking

International permits cannot be used in Australia during the fixed price phase. But from 1 July 2015, polluters will be able to meet up to 50% of their obligations by buying permits from international carbon markets.[6] Export of permits is prohibited in the fixed price phase, but will be allowed during the flexible price phase (however, until 2020 they may only be exported to countries with which Australia has a bilateral agreement).

Carbon Farming Initiative linking

Polluters will be able to meet their obligations by purchasing offset credits (Australian Carbon Credit Units, or **ACCUs**) generated under the CFI. The CFI is an offset credits scheme which rewards activities in the agriculture, land and forestry sectors that reduce emissions, with tradeable credits. The CFI will produce two types of credits: 'Kyoto compliant' credits (if the offset project meets the Kyoto rules) and non–Kyoto compliant credits (if they don't). Only Kyoto-compliant credits will be eligible under the emissions trading scheme. In the fixed price phase polluters may only meet 5% of their obligations this way, but from 1 July 2015 there is no limit. This poses a risk to the budget if the CFI is too successful, because the more CFI credits are used, the fewer permits the Government sells and the less scheme revenue it obtains.

3 *Clean Energy Future* Appendix A Table 5.

4 *Ozone Protection and Synthetic Greenhouse Gas Management Act 1989* (Cth).

5 Because it may activate the Constitutional requirement to provide compensation for acquisition of property if the scheme needs to be changed and permits acquired by the Government. ANEDO Submission to the Department of Climate Change and Energy Efficiency, 10 May 2011, pp.9–11.

6 This restriction will be reviewed by the CCA in 2016.

Household assistance

As mentioned above, emissions trading schemes impose costs on big polluters, which are then passed down to consumers through increased prices. Accordingly, the price of carbon-intensive goods and services (that is, goods and services that require the emission of lots of greenhouse gases during their production and/or transport) will rise, and households will face increased costs. Treasury modelling estimates that as a result the average family will pay $9.90 more per week in the first year.

The scheme contains two measures to protect households from that impact. First, households will receive generous tax relief to assist them in meeting the expected rise in costs. The tax-free threshold will be tripled from $6,000 to $18,200, exempting 1 million people from the need to pay income tax or file a tax return. People earning less than 80,000 per annum will also receive a tax cut, which for most people will be around $300 per annum. Second, households will also receive generous assistance through welfare payments. Pensioners and self-funded retirees, family payment recipients and allowance recipients will all see their payments increase.

Contrary to what you may have heard, this will not undermine the 'carbon price signal' (that is, the incentive to reduce consumption of carbon-intensive goods and services). So long as household compensation measures are separate from the carbon price (which they are in this case) households still have an incentive to reduce their consumption of carbon-intensive goods and services. This will allow them to reduce their carbon costs, while retaining their household compensation. In other words, they can actually make money by reducing their carbon footprint.

Industry assistance

There are six streams of industry assistance in the carbon price package.

The **Jobs and Competitiveness Program** provides $9.2 billion worth of free permits to 'emissions-intensive trade-exposed' (**EITE**) industries. EITE industries are those which emit a lot of GHG, but have limited ability to pass the carbon price through to consumers due to competition from international markets that are not subject to a carbon price. They include steel manufacturing, aluminium production and cement production. As in the EITE assistance program under the CPRS, they will receive either 94.5% or 66% of their permits free, depending on exactly how emissions-intensive they are. But unlike under the CPRS, liquefied natural gas producers will receive 50% of their permits for free. The rate of assistance will reduce by 1.3% per annum, and the entire program will be reviewed by the Productivity Commission in 2014–15.

The **Clean Technology Program** is new. It provides $1.2 billion worth of grants to manufacturing industries to allow them to improve their energy efficiency and adopt low-pollution technology. It also includes funding for clean energy and energy efficiency research and development. Industry must match Government spending dollar-for-dollar.

The **Coal Sector Jobs Package** provides $1.3 billion of transitional assistance over six years to implement carbon abatement technologies in the most polluting coal mines, rewarding them for reducing their emissions. This is a Government-only measure, not supported by the MPCCC. It will be implemented through spending programs and does not require legislation or parliamentary approval. This package will also be reviewed by the Productivity Commission in 2014–15.

The **Steel Transformation Plan** is also new, and is also a Government-only initiative (though it will require Parliamentary support). It provides $300 million worth of transitional assistance over five years to encourage investment and innovation in more efficient and environmentally friendly practices in the steel industry.

Small business (with less than $2 million annual turnover) will see their instant asset write-off increased to $6,500, and be able to access a $40 million **Energy Efficiency Information Grants** program.

The **Energy Security Fund**, valued at $5.5 billion, is aimed at coal-fired electricity generators. This is more targeted than the compensation program offered under the CPRS. Cash assistance and free permits will be given in return for generators adopting clean energy investment plans showing how they will reduce their pollution. Generators will also receive short-term loans to help them buy permits. Importantly, the fund will be used to support the negotiated closure of 2000 MW of highly polluting generating capacity by 2020 (roughly equivalent to the capacity of the Hazelwood Power Station: 1,600 MW).

Clean energy

In a major improvement on the CPRS, a Clean Energy Finance Corporation (**CEFC**) will be established, and given $10 billion to leverage private investment in clean energy through loans, loan guarantees and equity investments. ANEDO and a range of other bodies have advocated for such a body to be included in the scheme.[7] The CEFC will be commercially oriented, and staffed by experts in clean energy and finance.

About $3.2 billion worth of existing renewable energy grants will be brought within the aegis of the Australian Renewable Energy Agency (**ARENA**) — a new independent statutory body tasked with coordinating research, development and demonstration programs for renewable energy.

Biodiversity fund

In a major break from the CPRS, the scheme will establish a Biodiversity Fund providing $946 million over six years to fund projects that protect and improve biodiversity and store carbon. This fund will provide a valuable complement to the CFI, and is crucial to ameliorating many of the deficiencies of that scheme. ANEDO supported the development of such a fund in consultation on the development of the CFI.[8]

This fund will be complemented by several other funds designed to encourage abatement in the land sector (the Carbon Farming Futures Program, Carbon Farming Skills Program, Indigenous Carbon Farming Fund and Regional Natural Resource Management Planning for Climate Change Fund). A Land Sector and Biodiversity Board will be established to advise on the implementation of these measures.

Governance

The Climate Change Authority (**CCA**) will be established to advise the Government on setting pollution caps, and on its progress to achieving its emissions reduction targets. It will be chaired by former Reserve Bank Governor Bernie Fraser. It will also be responsible for periodic reviews of the carbon price, the Renewable Energy Target, the CFI and the National Greenhouse and Energy Reporting System. All CCA reviews will be public and involve public consultation.

The advisory functions of the CCA will be complemented by the Clean Energy Regulator which will actually administer the scheme. The Productivity Commission will have an ongoing role in reviewing industry assistance provided under the scheme.

What’s next?

By September, the Government plans to introduce legislation implementing the carbon price, and hopes to pass it by the end of the year. The legislation will resolve several crucial details, which there may still be scope to influence. The EDO will release a briefing paper explaining the legislation when it is released, and will continue to make comment to Government on how the scheme should be improved.

How flexible will the caps be?

On the one hand, it is important that pollution caps can be set far in advance, to provide maximum business certainty. On the other hand, it is important that the caps can be adjusted in response to rapid market developments or changes in the science of climate change. The Government has committed to setting the caps five years in advance. But exactly how set in stone these caps will be, and whether the Government will be obliged to set scheme ‘gateways’, which limit the range of caps that may be set for a further five years in advance, remains to be seen in the legislation.

7 ANEDO submission to the Department of Climate Change and Energy Efficiency, 10 May 2011 pp 8–9. The idea has been advocated by the Australian Conservation Foundation and the Clean Energy Council for several years.

8 ANEDO submission to the House of Representatives Climate Change Environment and Arts Committee; ANEDO submission to the Senate Environment and Communications Legislation Committee.

How watertight will the caps be?

The most valuable feature of an emissions trading scheme is the overall cap on emissions. By allowing only a finite number of permits to circulate, it provides a guarantee that no more than that amount of GHG will be emitted from covered sectors. However, that guarantee only works if the legislation ensures that the cap is watertight — that is, that the scheme does not allow any permits to enter the scheme over and above the 'cap'. The CPRS allowed several types of permits to be acquitted over and above the cap, opening the door to an oversupply of permits and a plummeting permit price. It is important that the legislation for this carbon price does not make the same mistake.

Will review of decisions be even-handed?

The legislation is likely to include provisions for seeking merits review of decisions made by the bodies administering the scheme. The CPRS legislation made such provision, but it only allowed liable entities to apply for merits review — no provision was made for groups or individuals to review decisions to defend the public interest. It is important that the carbon price legislation avoids this one-sidedness.

Will the Government be able to implement its Government-only measures?

There are three Government-only measures in the carbon price package:

- imposing a carbon price on heavy on-road vehicles by 1 July 2014;
- the Steel Transformation Plan, valued at $300 million; and
- the Coal Sector Jobs Package, valued at $1.3 billion.

The Coal Sector Jobs Package can be achieved through expenditure only, and the Government believes it can price heavy on-road vehicles through regulations only. But the Steel Transformation Plan requires the support of Parliament. Whether the Government is able to get these measures passed remains to be seen.

How will State Governments respond?

Several State Governments — including the Victorian Government — have explicitly declared their intention to wait and see the carbon price package before making climate change policy of their own. To an extent this makes sense, because it allows Governments to avoid overlapping and inefficient policy. However, it should not be used as an excuse to avoid action at a State level. There are a range of climate change policy measures that are required regardless of a carbon price, such as amending the planning regime to encourage sustainable and climate-friendly planning. For more information, see our analysis 'States Can Reduce Emissions, Too' in *New Matilda*, 29 June 2011. [9]

For more information

If you want to know more, visit the comprehensive Australian Government website www.cleanenergyfuture.gov.au.

You can also contact the Environment Defenders Office (EDO) on 03 8341 3100 (metro) or 1300 336842 (regional), or send us an email at edovic@edo.org.au, for more information or to find out how you can get involved in the rest of the process. See also the following page for more about the EDO.

9 http://newmatilda.com/2011/06/29/states-can-reduce-emissions-too, accessed on 12 July 2011

About the Environment Defenders Office (Victoria) Ltd

The Environment Defenders Office (Victoria) Ltd ('EDO') is a Community Legal Centre specialising in public interest environment law. We support, empower and advocate for individuals and groups in Victoria who want to use the law and legal system to protect the environment. We are dedicated to a community that values and protects a healthy environment and support this vision through the provision of information, advocacy and advice.

In addition to Victorian-based activities, the EDO is a member of a national network of EDOs working collectively to protect Australia's environment through public interest planning and environmental law.

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