

Business  
Council of  
Australia



# **Business Council of Australia**

**Carbon Pollution Reduction Scheme Green Paper  
Submission**

**September 2008**

## **Declaration of interest**

The Business Council of Australia (BCA) represents the Chief Executives of 100 of Australia's leading companies. The BCA's objective is to develop and advocate, on behalf of its Members, public policy reform that positions Australia as a strong, vibrant and globally engaged economy and society. The companies that our Members lead are responsible for a significant share of Australia's domestic and overseas business activity. They therefore have a significant interest in government policy, especially those areas of policy related to Australia's economic, environmental and social well being that is the key drivers of Australia's future prosperity.

## Introduction

Australia should take a long term and risk management approach to climate change policy which incorporates both mitigation and adaptation elements, is calibrated to international responses and builds on our skills, resources and regional location.

The economic, social and environmental risks are substantial both if we take no action on climate change and if we take the wrong action.

Whilst some might argue that Australia should sit back and wait and see – this does not provide the basis for a proactive management of the risks nor does it locate Australia with its international peers in seeking to resolve the inherent challenges associated with climate change.

The Business Council of Australia therefore fully supports the introduction of an emissions trading scheme in Australia capable of international linkages and is pleased to respond to the Australian government's recently released Carbon Pollution Reduction Scheme Green Paper (CPRS).

The implementation of Australia's CPRS has the potential to provide many opportunities. A market driven price on carbon brings with it the potential for:

- the deployment of existing low carbon technologies at greater rates across the economy;
- the development and scaling up of technology which is nearly at the commercialisation stage;
- incentives to find new breakthrough technological solutions;
- reengineering many of the processes that underpin our current businesses;
- new employment opportunities and the reskilling of the workforce in response to new technologies; and

- the development of a new financial market and financial instruments to underpin the trading in permits.

The implementation of the CPRS in Australia ahead of our competitors does however require careful management, as we will be doing this in the absence of a global carbon price in the early years. Care must be taken to ensure there are transitional policies in place during this interim period.

There is little to be gained if in the early years of implementation there are unintended consequences such as 'carbon leakage', deferral of investment or business closures and employment losses.

The BCA submission is designed to provide the Government with new research which for the first time considers how best to introduce the CPRS and minimise the risk of unintended consequences during the early years, whilst putting Australia on the path to contributing to global emissions reduction.

The BCA submission is in two parts:

- Attached is *Modelling Success: Designing an ETS that Works*. This report includes an evaluation of the mechanisms proposed in the Green Paper to assist emissions intensive trade exposed (EITEs) and whether they will fulfil their stated outcome.

It also provides a comprehensive analysis of the electricity sector investment required to ensure a shift to low emissions technology and the impact of the introduction of the CPRS on electricity generation asset values.

- Below is discussion of a number of other key elements of the CPRS which may require further consideration in the coming months as the Government's White Paper is finalised.

## Discussion

The Business Council of Australia welcomes the Australian Government Carbon Pollution Reduction Scheme Green Paper (CPRS) which is designed to meet the following three objectives:

- to meet Australia's emissions reduction targets in the most flexible and cost-effective way;
- support an effective global response to climate change; and
- provide for transitional assistance for the most affected households and firms.

The Green Paper has recognised the principles identified in the BCA report of 2007 *Strategic Framework for Emissions Reduction* namely establishing a trading scheme that is long term in nature, covers as many industry sectors and gases as feasible, has caps on emissions, maximises offsets, recognises the impact on the competitiveness of trade exposed emission intensive industries in the absence of a global response and the possible impact of disproportionate loss for some sectors.

In considering the Government's proposed approach to implementing the CPRS there are a number of areas where the BCA proposes there is further consultation to ensure the scheme objectives and principles are met.

### ***Governance arrangements***

The Green Paper explores a number of critical issues in relation to governance and importantly notes the need to separate the policy setting role from the regulation enforcement role. The Green Paper also outlines the role of the Parliament in the governance framework.

The BCA has identified the importance of bipartisanship in the development and implementation of the CPRS. Such an approach if in place for the long term would assist in the governance framework.

However such an arrangement is not assured.

The BCA is therefore concerned that there may be an unintended consequence in what is proposed - namely a substantial reduction in policy predictability and certainty.

This is particularly the case if Parliament is in the position of being able to disallow regulations which annually extend the 5 year fixed caps and every 5 years extend the gateways.

Consideration should be given to including in the enabling legislation the role of the Minister on these and other policy issues related to the operation of the CPRS; matters the Minister must consider in making determinations; and the nature of the directions the Minister can give the regulator. In determining the role and responsibilities of the regulator, consideration should be given to how best to use the regulator to assist in providing business certainty.

### ***Setting emissions trajectories and gateways***

A key concern for business, in making long term investments, will be the degree of forward knowledge on likely emissions caps and trajectories. The Green Paper is proposing a combination of mechanisms which will provide 5 years of fixed caps and ten year gateways. Such a duration may not be sufficient for major new investments. Consideration should be given to either extending the forward knowledge to 20 years or for major capital investments - the use of a contract with government or other mechanism.

Similarly as discussed in detail in the attached report a mechanism needs to be identified to address growth in the EITE sectors during the transition phase.

### ***Coverage***

The Green Paper has outlined a process for the consideration of the inclusion of the agricultural sectors over time. It will be important to ensure there is clarity about the processes of review and date of inclusion of agriculture as any ambiguity will have an impact on permits in the market and also whether other policy mechanisms will be required to drive emissions reduction in agriculture.

## **Banking and borrowing**

The Green Paper approach to these important mechanisms in a fully functioning CPRS limits borrowing but allows unlimited banking. Consideration should be given to removing the limits on borrowing, otherwise there is a risk of distortions to the permit price path.

However should there be an initial fixing of the permit price banking and borrowing would need to be deferred.

## ***Price signals***

As identified in *Modelling Success*, the removal of a price signal to consumers of fuel for private transportation until 2013, appears contrary to the policy intention of using a price signal to drive changes in behaviour.

## ***Household assistance measures***

The introduction of the CPRS will lead to increased costs for electricity and many goods and services. These increased costs will affect the living standards of those in low income households. Measures should be introduced to offset these impacts but at the same time still ensure there is an awareness of the price signal.

## ***Emissions intensive trade exposed industries***

The Government has recognised that during the interim period between the introduction of the CPRS and the establishment of a global carbon price there will need to be arrangements in place to reduce the potential for carbon leakage.

An administrative allocation of permits will be required. The mechanism to do this will be critical to ensuring there are not unintended consequences. The attached report, using data that has not previously been available to either government or organisations like the BCA, assesses the mechanism outlined in the Green Paper and makes a number of recommendations to address particular issues in what has been proposed.

### ***Taxation and accounting matters***

Appropriate taxation and accounting policy settings will be essential to the efficient operation of the CPRS.

From the BCA's perspective, there are a number of concerns in relation to the proposed taxation and accounting treatments that must be resolved, well in advance of the CPRS start date, in order to allow companies adequate time to prepare for the changes.

#### Income Tax

The BCA supports the proposal to include specific provisions governing the CPRS in the taxation legislation, for the purpose of increasing certainty and reducing complexity.

However, the BCA is aware of a range of income tax-related issues still requiring clarification to ensure the efficient and effective operation of the CPRS. These include, but are not limited to:

- The effect of various start and cut-off dates in relation to the scheme on companies with substituted accounting periods;
- Potential adverse consequences for taxpayers with pre-existing long term supply contracts;
- Interaction with other legislation, for example the financial service regulatory rules under the Corporations Law, and the Taxation of Financial Arrangements legislation;
- The deductibility of any make good provisions contained in penalties (the BCA considers that make good components should be deductible);
- Interactions with the general tax treatment of joint venture operations;
- The taxation treatment of free permits and cash payments (the BCA is particularly concerned at the potential cash flow impacts of the effective up-front taxation currently proposed under the Green Paper);

- The election of a valuation method under the 'Rolling Balance' system (the BCA believes taxpayers should be entitled to elect which valuation method they wish to adopt); and
- The broader impacts on taxpayer's overall tax profiles (for example, rapid changes in thin capitalisation position or the interaction with the controlled foreign corporation provisions) that may require transitional arrangements.

### State Taxes

The BCA considers it imperative that the effective operation of the CPRS market not be impeded by the imposition of additional state taxes, in particular stamp duty on traded permits (or associated derivative products). This position must be clarified before the scheme commences.

### Good and Services Tax (GST)

The BCA is concerned that the GST status of permits should be clarified as soon as possible. For the avoidance of doubt, the BCA believes the GST status of permits should be specifically clarified in the GST legislation (as is proposed for income tax).

### Accounting

The BCA understands the International Accounting Standards Board intends to have an appropriate standard for the treatment of emissions trading in place by 2010. The BCA welcomes this move. However, should the development of an international standard be delayed, the Government must support the Australian Accounting Standards Board in the development of an interim standard to which Australian businesses can adhere, until such time as an international standard is finalised. This will minimise the potential confusion and disruption of reporting that would occur in the absence of an agreed standard.

## **Complementary programs and policies**

Whilst the CPRS should be seen as the key tool to support emissions reduction, there will remain a need to better understand and map Australia's adaptation agenda. This will require ongoing government support and community engagement.

Similarly there remains a need to undertake ongoing research and development investment following the introduction of the CPRS by government and business.

The BCA in its submission to the Wilkins review identified the need to review and wind up State based policies and programs which would impact on the efficiency and effectiveness of an emissions trading scheme or duplicate the policy intent of an ETS. It remains essential that this action be taken over the coming months. A copy of the full submission is attached.

## **Conclusion**

The design, passage and implementation of the CPRS is the single most important decision the Rudd Government will make. The government can lead the way in the implementation of a credible and successful national emissions trading scheme that provides an example of what can be achieved for other countries to follow.

The BCA is committed to working with the government to devise an effective CPRS both in the short and longer term.

Australia has a real opportunity to achieve better social, economic and environmental outcomes based on higher productivity – and carbon productivity in particular.

Business has a critical role to play in this process and it is committed to playing that role. The BCA looks forward to continued discussions with the government as it develops its White Paper.

## **Further information**

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