

BHP Billiton

Submission on the Garnaut Climate Change Review Interim Report



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## Key Points of the Submission

1. BHP Billiton supports the Government's aim of facilitating international agreement on climate change response and the development of an Australian emission trading scheme (ETS) in line with our emerging international obligations.
2. BHP Billiton supports the Garnaut review of economic impacts and anticipates that it will provide useful input to Government decisions on future Australian greenhouse gas emissions targets and timeframes as well as design aspects of the ETS.
3. Industry has a strong legitimate interest in the Garnaut review, including its modelling methodology and assumptions. We ask that the review be transparent in all respects and provide for genuine stakeholder consultation at every stage prior to the release of final findings.
4. BHP Billiton welcomes the opportunity, provided by Australia's ratification of the Kyoto Protocol, to link an ETS with other emissions trading schemes. However, this may be incompatible with the concept of a domestic permit price cap to safeguard our economy against unanticipated impacts. We support having such a safety valve in the initial phase of the ETS, and therefore believe the timing and process of our linking with other trading schemes needs to be carefully managed.
5. BHP Billiton supports the approach of providing relief to Australia's trade exposed emissions intensive (TEEI) industries. Otherwise, the ETS scheme would impose potentially significant competitive disadvantages on our Australian operations and could bias businesses' investment decisions towards countries with no caps or restrictions on carbon emissions.
6. We believe it is important that previous Government commitments to avoid policies that disadvantage early (pre-June 07) movers on emissions abatement be upheld and reflected in the ETS. BHP Billiton has invested in abatement projects on this basis since 1995.

BHP Billiton is pleased to provide this submission regarding the Interim Report of Professor Ross Garnaut's Climate Change Review. Developing an appropriate and effective response to the threat posed by climate change is an important policy task, and an area in which harnessing the support and capabilities of the private sector is vital. BHPB continues to invest significantly in reducing the environmental footprint of its operations, and strives to achieve high levels of environmental performance consistent with growth and income objectives. We are a global company with a strong Australian asset base. It is in our interests and those of the wider Australian community to ensure that the policies developed to address climate change do not place an undue burden on our competitiveness, and are designed to ensure the strength and resilience of the Australian economy into the future.

In the Interim Report, Professor Garnaut reviews climate science developments and the pace of growth in international carbon emissions, presents concepts to encourage developing country participation in global mitigation efforts, and previews his design recommendations for the Australian Emissions Trading Scheme (ETS). Areas of primary interest to BHP Billiton in the Garnaut Review Interim Report include the discussion of global cooperation, international linkages of emissions trading schemes, and the design of the ETS.

BHP Billiton has previously provided comments in these areas through submissions on the report of the Prime Ministerial Task Group on Emissions Trading and the Discussion Paper on Abatement Incentives Prior to Commencement of the Australian Emissions Trading Scheme and we build upon those previous comments in this submission.

Also, as the Government has signalled its intent to accelerate the implementation of the ETS by at least one year from the timetable of the previous Government, we are concerned that in the rush to finalize this scheme, the Government may be unable to adequately consider the full range of impacts on the economy and business competitiveness. If this results in poorly informed decisions and less than optimum system architecture and rules, it could severely strain industry and the Australian economy. We believe the Government should be prepared to defer the 2010 commencement target, if necessary, in the interests of developing a more effective system that will provide a stable framework for investment in greenhouse gas reductions over the long term.

## Global Cooperation

BHP Billiton recognizes that addressing climate change through mitigation of greenhouse gas emissions is a global challenge that cannot be met by countries acting individually. Until a comprehensive international arrangement is in place, the risk of emissions intensive industry relocating from countries with strong mitigation policies to countries with few or no emissions restrictions remains high. This can only be avoided by taking measures to ensure the participation of all major emitting countries in an effective global mitigation scheme. We support Professor Garnaut's conclusion that Australia stands to benefit from an effective international mitigation effort, but we raise the concern that premature linkages with international trading schemes could have adverse impacts on the economy and in particular on the costs borne by participants in the ETS. We also support Professor Garnaut's concept of Australia making an initial commitment to contribute carbon reductions at a lower level whilst keeping open the possibility of stronger targets in the context of effective global action. However, clarity must be given around what types of projects could be admitted into the trading scheme and the total quantity allowed to be imported in the interim period.

## Linkages with International Trading Schemes

Kyoto Protocol ratification opens the door for Australia to link with the EU emissions trading scheme. When linkages occur, the private sector should have access to the same mechanisms as players in other markets (CER's and ERU's). Early linkage with the EU scheme would quickly bring carbon trading prices in the Australian trading scheme to the same levels as those in the EU (current EU futures are about US\$37 per tonne carbon). However, Australia could lose the opportunity to provide a safety valve price cap or to fully realize the benefits of less expensive emissions reduction opportunities at the start of its program.

We recommend:

1. Keep open the possibility of a safety valve price cap in the start up phase.
2. Ensure linkages with international trading schemes are managed in a way that ensures the less costly abatement options are available to Australian participants during the early stages of the ETS.

## Emissions Trading Scheme Design

The further development of the ETS presents a number of important and pressing issues for BHP Billiton, many of which Professor Garnaut raises in his Interim Report. These include emissions reduction targets in the medium and long term backed up by economic modelling, treatment of disproportionately affected (trade exposed-emissions intensive) industries, and whether emissions caps will be coupled with a safety valve limit on the carbon price to ease the shock of the start up phase. We support Professor Garnaut's notion of rights to emit being

allocated to owners of permits for a specified period and allowing the owners of permits to use them at a time of their choosing within that period.

## Emissions Reduction Targets

Ratification of the Kyoto Protocol has an immediate impact on Australia's near term targets and, when an international agreement is reached, the longer term national targets for greenhouse gas reductions. For the 2008 - 2012 Kyoto commitment, Australia's target is an 8% increase above 1990 levels. Analysts believe Australia is positioned to meet this initial target. The parties to the Kyoto Protocol have agreed to work towards a consensus on targets for the second commitment phase by year end 2009. Suggestions of 25 to 40% reduction targets by year 2020 have been put forward but not yet agreed by the parties.

Professor Garnaut was commissioned to conduct economic modelling to determine how emissions trading and interim targets will affect the Australian economy and it is anticipated that he will use his findings to guide his recommendations on national targets.

Decisions made on emissions trading and targets will have an immediate and lasting impact on the profitability and competitiveness of Australian industry. The accuracy of the study results is highly dependent on the study design and particularly on the assumptions used in the modelling. Therefore industry has a strong interest in the Garnaut study, including the underlying economic and scientific assumptions and how they will be used in the modelling to form the basis for decisions and recommendations on the ETS design, targets and timeframes. The assumptions and scenarios being used by Professor Garnaut and Treasury must be made available for review by industry with sufficient time to assess how they are applied and to offer comments and suggestions.

We recommend:

1. Maintain openness and transparency regarding the modelling process and the assumptions used.
2. Enable stakeholder consultation during the process, with sufficient time for consideration and discussion of the modelling assumptions before the results are publicised, to ensure the Government has the best information available for decision making.

## Relief for Trade Exposed Emissions Intensive Industries (TEEI's)

The Government has assured stakeholders that relief will be provided for disproportionately affected industry, including TEEI's, through free allocation of emissions credits during the first years of the program. Professor Garnaut recognizes the importance of this relief to avoid carbon leakage. We are concerned that in the rush to accelerate the ETS, provision for relief may be set aside or limited to a small set of TEEI's if perceived as too controversial or complex. The TEEI's are most vulnerable to competition from industries in developing countries without Kyoto-based CO<sub>2</sub> emissions reduction obligations. Dislocation of an industry to a developing country, although reducing CO<sub>2</sub> emissions for Australia, could increase global CO<sub>2</sub> emissions if the new manufacturing facilities in the developing country are built with older, less efficient production technology with no CO<sub>2</sub> removal capabilities.

It is important to consider extension of relief for TEEI's to new entrants in sectors that fall into this category. This relief could be based around a baseline of using best practice for commercially viable technology. The ETS scheme design should also provide consideration for the increased cost of power incurred by TEEI power users due to the cost of carbon applied to the power generator's emissions and passed on in the power price.

We recommend:

1. Ensure that relief criteria for TEEI's and criteria for credit for early abatement actions will be completed in time for inclusion in the ETS
2. Provide a clear definition and criteria for TEEI early in the stakeholder consultation process.
3. Ensure relief for TEEI's continues until such time as competing countries adopt emissions mitigation policies that alleviate this concern.

### Credit for Early Action

Although not specifically addressed by Professor Garnaut in his interim report, during the recent consultation process on Abatement Incentives Prior to the Commencement of the Australian Emissions Trading Scheme one of our major concerns was that the Government was not planning to allow credit in the scheme for actions occurring before June, 2007. BHP Billiton has invested in successful voluntary greenhouse emissions reduction projects, primarily related to capture and destruction of coal bed methane, before the June 2007 cut-off date and credits from these leadership efforts should be eligible for trading. Now that Australia is planning full ratification of the Kyoto Protocol, we note that the Kyoto baseline is 1990 and therefore allowing credits only for actions taken after the former Prime Minister's announcement of the ETS in June 2007 would be inconsistent with the Kyoto framework.

The eligibility criteria for credit for early action are likely to be perceived as complex and controversial and the Government may be inclined to tightly restrict or eliminate provisions for credit for early action altogether. Government decisions on early action and trading system design should not undermine the economics of past greenhouse investment, or harm the credit earning and permit allocation potential of operations that reduced their emissions profile prior to 3 June 2007, relative to those that cut emissions after that date.

We recommend:

1. Ensure projects initiated prior to June 2007 are eligible for early action credits.
2. Ensure provisions for early action credits are maintained in the final design of the ETS and not sacrificed to expedite the system completion.

### Other Policy Interventions

An effective market-based ETS needs to take into account other policy interventions, such as renewable energy targets. In particular, the interaction between the Renewable Energy Target (RET) and the ETS needs to be closely examined. The RET has the potential to direct investment away from least cost abatement options – in contradiction to the intent of a market-based ETS.