Protecting Australia's new climate change response from the Greenhouse Mafia

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A General Submission to the Garnaut Climate Change Review

by

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Author—High & Dry: John Howard, climate change and the selling of Australia's future

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An effective climate change response by Australia depends in no small part on seeing through the hitherto successful campaign of denial and delay run by Australia's worst polluting industries. At the heart of this campaign has been a self-dubbed greenhouse mafia—a group comprised of the core players at the Australian Industry Greenhouse Network (AIGN), and their acolytes in bureaucratic, political, and consulting circles.[1] If the lessons are not learned from how Australian greenhouse policy was captured by the carbon lobby over the past decade, I fear the Rudd administration will repeat some of the mistakes of the previous administration.

Since the election and Australia's ratification of the Kyoto Protocol, many wrongly assume that Australia's greenhouse mafia has been defeated. Such complacency is dangerous and misplaced. The campaign by our worst polluting sectors to undermine Australia's response to climate change is as strong and stealthy as ever. For many years members of the AIGN sponsored front groups denying the scientific basis for reducing greenhouse emissions. At the same time they funded a plethora of economic work which was used to create the erroneous impression that reducing Australia's emissions would wreck our economy. They used their partisan and bureaucratic connections to devastating effect.

These industries and corporations successfully argued generally against Australia adopting new greenhouse emission constraints, and specifically against an emissions trading scheme (ETS) in advance of an effective global response to climate change. This was the climate policy equivalent of the argument against trade liberalization we have grown accustomed to hearing from various sectors seeking a level playing field before trade barriers are wound back. Ultimately, the AIGN and its members had to concede that carbon pricing in Australia could not wait for a level playing field, so their campaign had to adapt.

Whereas previously the aim was to delay action to cut emissions in Australia, now it is more narrowly focused on delaying emission cuts by these sectors. This means shifting the burden of carbon pricing and any other new emission constraints onto other sectors and Australian society more broadly. Much of the new delay agenda of the carbon lobby is encapsulated in a list of 'carve out' and compensation provisions which has been very quietly and successfully incorporated into the two most important recent emissions trading policy development processes in Australia: the National Emissions Trading Taskforce (NETT), and the Prime Minister's Task Group on Emissions Trading (PMTG). In short, the new greenhouse mafia agenda is part of the greenhouse 'policy furniture' inherited by the Rudd government. Given how advanced this agenda was just prior to the 2007 federal election, unraveling it will be one of the most important and difficult tasks facing the Garnaut Review.

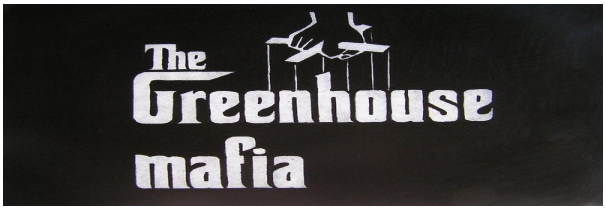
I view the Garnaut review as an extremely important opportunity for Australia to correct its response to the most important challenge of our time. In light of the appropriately broad terms of reference, and the views expressed in the Interim Report I am cautiously optimistic about the process. I am hopeful that it will help to set Australia on a course to

[1] For more on the origins of the greenhouse mafia see: Pearse, G.D. 'The Business Response to Climate Change in Australia: case studies of Australian interest groups, PhD Thesis, Crawford School of Government, ANU, 2005; and 'The Greenhouse Mafia', ABC Four Corners, Feb 13, 2006; and Pearse, G.D. High & Dry: John Howard, climate change and the selling of Australia's future, Penguin 2007.

deep emission cuts commensurate with what is required globally, and in an appropriate timeframe. I'm also hopeful that the Review will accelerate an effective response to the immense adaptation task facing this country. In *High & Dry* I expressed strongly held views on most aspects of Australia's response to climate change. In the months ahead, I hope to contribute broadly to broad public discussion around the Garnaut Review, and the government's response. However, at this stage due to the lack of attention it has received and due to its significance and urgency, I want to focus my remarks on the new delay agenda of the greenhouse mafia. Most of this agenda relates to the fine print of emissions trading scheme design.

I believe the public expects that an effective response to climate change by this country involves Australia making deep absolute cuts in its emissions by mid century consistent with what is required globally to prevent the worst impacts. I also think the public expects that our largest polluters will make commensurate cuts here in Australia, at their own expense. Instead, the carbon lobby is pursuing a series of policy outcomes that would have the practical effect of failing those public expectations and letting our worst polluters off the hook.

In the table below I have set out a list of the sort of arguments being mounted by the Australia's greenhouse mafia and their acolytes. It is not intended to be an exhaustive list, but most of these positions have been reiterated in the recent AIGN submission to the Garnaut Review.[2] Alongside are some brief comments on why it is in Australia's interests that each polluter argument be rejected.



Their new agenda to undermine Australia's response to climate change – and why it should be rejected

Polluter Outcome Sought	Polluter Spin	Why it should be rejected
1. A modest (ie. weak) emissions cap when an ETS begins	We mustn't shock the economy—industry needs time to adjust. It matters little when our emissions actually peak and start coming down. There's even a case for Australia having higher emissions than other countries, because our LNG, uranium and aluminium exports are contributing to lower emissions globally. Deeper cuts will be more affordable here later so it makes sense not to go too hard too soon.	The later Australian emissions peak, the greater the emission reduction task, and the greater our cumulative emissions are likely to be. A host of studies confirm that the longer Australia delays emission cuts the more it will cost. The argument that Australia's best contribution to reducing emissions globally is through its mining, metals and energy exports ignores the reality that production here is among the most emission intensive in the world. The same argument routinely overlooks the emissions generated by the use of exported Australian coal. It also ignores the affordability of deep emission cuts in Australia. McKinsey consulting recently found that Australia could cut its emissions 20% below 1990 levels by 2020 at no net cost to the economy; 35% below 1990 levels by 2030. [3] Strong long term and interim emissions reduction targets supported by a broad ETS with a strong emissions cap will maximize clean industrial development without shocking the economy.
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
2. Free permits to emission intensive industrial facilities for 40-50 years	Energy intensive facilities like power stations have long lead times and long operating lives—their operating lives should not be unfairly. Free permits for older facilities can be replaced by auctioned permits for new ones gradually.	Free permits to such facilities are a 'carbon subsidy' that could hardly run more counter to the aims of an ETS. It not only extinguishes the market incentive intended to encourage emission cuts; it amounts to a relative improvement in the competitiveness of dirty facilities relative to cleaner ones. It would lock in for decades the very facilities that an effective ETS should start to price out of operation
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
3. A low 'fine' for excess emissions	Polluters need a 'safety valve' in case emission cuts prove too expensive in any given year. A penalty for excess emissions puts a price ceiling on emission permits just in case.	The purpose of an ETS is to cap emissions and let the market decide the price required to achieve the emissions outcome sought. An emissions penalty effectively establishes a price ceiling. This destroys the business opportunities that would otherwise be available to higher priced emission reduction providers by allowing polluters to keep polluting instead. It means that so long as industry would prefer to 'pay the fine' emissions can increase indefinitely.
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
4. Compensation for loss of value of high polluting	A price on carbon reduces the value of the incomes that will be produced by emissions intensive industrial	Having been able to avoid paying for the damage associated with their greenhouse pollution for many yeas, these facilities now seek to cover the cost through a carbon subsidy. By 'internalizing' the costs of greenhouse pollution

[2] For the latest iteration of the AIGN position see: AIGN Submission to the Garnaut Climate Change Review, Australian Industry Greenhouse Network, March 2008.
[3] See: 'An Australian cost curve for greenhouse gas reduction,' McKinsey & Company, 2008, p.14.

industrial facilities	facilities. The more a facility pollutes, the more 'disproportionate the loss of value.' The owners of such facilities (eg coal fired power stations) should receive a 'once and for all time' allocation of free permits equivalent to the difference between their loss and the average nationally.	an ETS should establish a market that values industrial facilities more appropriately. Instead, the compensation being sought would artificially inflate the value of Australia's dirtiest industrial facilities. It would reward dirty investments knowingly made by public and private entities that have seen carbon pricing for some 2 decades. It would also be used to 'fatten for sale' publicly owned energy generation assets. It removes the market incentive the ETS was intended to create for these facilities, and shifts the burden onto cleaner sectors and the consumer.
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
5. All Trade Exposed Emission Intensive Industries (TEEIs) should receive free permits as 'Transitional' compensation to cover the impact of an ETS on their competitiveness	Energy intensive trade exposed industries are the backbone of Australia's economy and their competition would not be subject to a carbon cost equivalent to the one imposed through an Australian ETS. So TEEIs here should receive compensation (preferably free permits) until such time as their competition and prospective competition faces a commensurate carbon cost. But, don't worry, this compensation would only be 'transitional.' Unless we do this, Aussie carbon and Aussie jobs will move offshore for without any environmental gain—it might even increase emissions.	Energy intensive trade exposed industries are not the backbone of our economy—they generate less than $1 in 10 and less than 1 job in 20.[4] Giving them free permits largely exempts most of the worst polluting sectors from the ETS. According to ABARE, this doubles the eventual carbon price which would be paid by other sectors and households.[5] Perversely, it would also improve the relative competitiveness of dirtier industries against cleaner ones in domestic markets where they compete (eg aluminium, steel and cement vs timber in the building products sector). The compensation being sought would be anything but 'transitional' too. Just as progress towards global free trade has been glacial, the prospect of a level playing field worldwide in carbon trading is remote. The AIGN has acknowledged as much. So what is being billed as temporary compensation to TEEIs would in practice become a permanent subsidy. The 'carbon leakage' argument is grossly overstated. Multinationals might shift production at the margins to existing facilities in countries not subject to a carbon price, but to build new facilities they would need to be confident that such a carbon price would not be imposed for many decades and none can be confident of that. This partly explains why the carbon leakage argument was not supported by ABARE's work for the PMTG—it found that if TEEIs received no compensation, for every tonne cut by an ETS here only around 1/10th of a tonne would leak offshore. ABARE found that compensating TEEIs would reduce that carbon leakage to about 1/20th of a tonne but it would also suppress GDP. [6] This confirms other evidence that where production of energy intensive industry is moving there is a net environmental benefit because the movement is often to countries with cleaner sources of energy, not dirtier energy (eg aluminium to Iceland and Russia). The idea that competition need only be in prospect (ie. not even real) makes this transitional subsidy even harder to phase out. It would doubtless be rorted by multinationals gaming the system. Most TEEI companies (eg those in steel, aluminium, LNG, etc) have assets both here and abroad—enabling them to conjure 'carbon leakage' that would never have occurred but for the prospect of accessing compensation in Australia. Of course, carbon pricing will inevitably cause energy intensive production to move to the cleanest locations—compensation should be directed to the communities affected, not the footloose multinationals whose profits would hardly be affected.
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
6. New projects in trade exposed emission intensive sectors should be excluded from the ETS emissions cap	Emissions associated with new projects are largely unknowable, so it's unfair to add risk to major investment decisions. Including new projects in TEEI sectors makes carbon leakage even more likely—and these sectors are too important to take the risk.	Excluding new emission intensive developments from an ETS emissions cap is a potentially major threat to the environmental integrity of Australia's greenhouse response. A handful of major projects in aluminium, steel, LNG and other 'trade exposed emission intensive' sectors could generate large quantities of greenhouse emissions. A new aluminium smelter, for example, is roughly equivalent to adding 1 million new cars to Australia's roads. Excluding these developments from the emissions cap in an ETS risks an emissions blow-out—particularly if those same developments are issued with free permits as well. Presumably, the additional emissions could only be offset by a significant tightening in the cap or through additional abatement programs. Again, it would shift the burden of emission cuts away from Australia's worst polluting sectors onto the rest of the community.
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
7. Additional ETS permits to energy intensive sectors to offset the costs associated with Labor's increased Mandatory Renewable Energy Target	The increase in the MRET is another blow to the competitiveness of energy intensive sectors. As with the impact of the ETS on asset values and trade competitiveness energy intensive sectors should be compensated for the disproportionate impact of the MRET on energy intensive sectors.	The AIGN says its arguments for various carve-outs and compensation is based on the high moral principle of equity—that within each country, no industry or section of society should bear a disproportionate share of the emission reduction cost. This totally ignores the disproportionate responsibility that a few industries have for Australia's emissions. The MRET and the ETS are both measures that embrace the polluter pays principle. To compensate the worst polluting industries exclusively for the impact of these schemes is to turn the polluter pays principle on its head.

[4] Pearse, G.D. *High & Dry*, op-cit. p.299-300.
[5] Report of the Task Group on Emissions Trading, Australian Government—Prime Ministerial Task Group on Emissions Trading, PM&C, 2007 p.176
[6] Report of the Task Group on Emissions Trading, op-cit. p.176

	Equity demands that no section of society should bear a disproportionate share of the emission reduction cost.	
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
8. Unlimited international trading in carbon credits	What matters is reducing emissions globally at least cost, not where those emission cuts occur. So, Australian firms should have no restriction on the extent to which they use carbon credits generated offshore to meet their emissions trading obligations.	The public legitimately expects that Australia should cut <u>its</u> emissions—not that we outsource our obligations. Offsets generated offshore (such as those allowed for under the Kyoto Protocol through the Clean Development Mechanism) do enable developed countries to help fund a cleaner development path in poorer nations, but they should not be allowed to become a wholesale substitute for domestic emission cuts in countries like Australia. If there is no limit on the extent to which Australian emitters can use foreign offsets, there is no surety that emissions will ever fall in Australia. Indeed, they could spiral indefinitely as Australia becomes a mere donor to the global clean energy transition rather than being part of it. Limits on foreign offsets help ensure that emission cuts happen here—which is why it is being considered in the United States right now.[7]
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
9. Avoided deforestation credits should be eligible	Forests loss accounts for 20% of global greenhouse emissions, and avoided deforestation is the cheapest and quickest way to cut emissions with minimal disruption to industrial activity. Australian companies should be able to meet their emissions trading obligations by accessing low cost options wherever they are available on the planet. That includes carbon credits generated through the preservation of forest carbon sinks internationally.	Avoided deforestation—particularly in developing countries would be a highly dubious way for Australian polluters to keep avoiding emission cuts. It's difficult to be confident about the amount of carbon permanently stored by avoiding deforestation. It is also impossible to prevent 'carbon leakage'-- whereby as one forest is protected to generate carbon credits, wood production and agriculture shifts to another forest and/or another country with no environmental gain. If Australian polluters were allowed to meet their obligations under an ETS through forest protection it would also retard the deployment of clean energy in Australia. This is precisely why the EU recently ruled out the use of these credits in its ETS until 2020. In the US, the bi-partisan Lieberman-Warner Bill in the United States proposes that international forest carbon activities be limited to 3% of emission allowances.[8]
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
10. The MRET should be phased out	Even if emissions trading is not a 'silver bullet' and some other greenhouse programs are justified, the Mandatory Renewable Energy Target should be phased out. It duplicates the emissions trading scheme, unnecessarily adds administrative burdens for business, and unfairly excludes nuclear and 'clean coal'.	If the ETS has a strong cap, <u>and</u> the 'carve-out' and compensatory provisions being sought by energy intensive sectors are rejected, <u>and</u> there are appropriate limits on foreign carbon credits, and we could be confident that carbon credits generated through tree planting and avoided deforestation will not flood the market once an ETS begins, then the MRET might reasonably be phased out over time. Absent all of these conditions being met, the MRET is the only significant measure that guarantees that Australia is a participant in the clean energy transition, and not merely a donor and spectator. Indeed, given the modesty of the extended MRET which is only projected to reduce emissions in 2020 by a mere 3%-- more rather than less such measures are justified to encourage renewables in Australia (eg. feed-in tariffs for renewable electricity and renewables-based transport incentives)
Polluter Outcome Sought	**Polluter Spin**	**Why it should be rejected**
11. Big public subsidies for 'clean coal' R&D, part funded by ETS revenue	Australia cannot make deep cut its emissions and avoid economic devastation unless there is a large-scale deployment of new 'clean coal' technologies—especially carbon capture and storage. With emissions trading raising lots of revenue, there is an even stronger case for publicly subsidized R&D.	It is illogical to establish an ETS to direct investment to the most cost-effective clean energy options, and then use the revenue to subsidise the dirtiest low emission options. New 'clean coal' technology is not the panacea some would have us believe. Indeed, there is plenty of evidence confirming Australia can achieve deep cuts in its emissions without CCS. McKinsey found that Australia could achieve 30% reductions below 1990 levels by 2030 at no net cost to the economy without CCS or nuclear.[9] It makes no sense to compound the error of carving out emission intensive sectors from the ETS (through compensation), by using the funds raised from the ETS to provide R&D subsidies for the worst offenders. The argument that the future of Australia's coal industry depends on this subsidy is also disingenuous. 80% of our coal is not subject to an Australian ETS because it is used offshore, and the facilities in which it is being used (and will be used) do not involve carbon capture and storage on any scale that matters in any timeframe that matters—irrespective of R&D assistance. To the extent that any public assistance for CCS is warranted it should take these realities into account. ETS revenue would be almost certainly be better spent on, among other things: structural adjustment for communities and workers, energy efficiency incentives for consumers, public transport infrastructure, climate change adaptation works, and avoided deforestation.

[7] Lieberman-Warner Climate Security Bill 2007, US Senate, p.68; http://lieberman.senate.gov/documents/acsabill.pdf
[8] Lieberman-Warner Climate Security Bill, op-cit. 2007, p.108-9
[9] 'An Australian cost curve for greenhouse gas reduction,' op-cit, p.18

All of these arguments are designed to delay emission cuts by Australia's worst polluting industries as long as possible—to shift the mitigation burden onto other cleaner sectors of the economy, consumers, and other countries. Collectively they threaten to erode the environmental, economic and political integrity of an effective Australian response to climate change in general and an effective emissions trading scheme in particular. The practical effect of the outcomes sought would be to replace a market that externalizes the cost of greenhouse pollution with one that internalizes it, but subsidizes the worst polluters to cover those costs. In effect, what is sought is a carbon subsidy in a new form.

It should come as no surprise that these interests would dress up carbon protectionism and a flawed understanding of market failure as high principle and economic good sense. These interests are accustomed to advancing every imaginable self serving argument as long as politically feasible. Consider some of the other arguments that the greenhouse mafia have used previously (and perhaps shelved for now with the election of the Rudd government): the science is the Achilles heel of climate change[10]; Australia shouldn't ratify Kyoto, even if the US does[11]; increasing Australian emissions could be part of an effective global response[12]; A carbon price signal won't trigger investment in new clean energy technology[13]; if an ETS must happen it should be the Single Policy Instrument (ie replace all other greenhouse programs) [14]; and support for an ETS is conditional on the WTO agreeing not to treat ETS compensation as a carbon subsidy (even though it is one).[15]

All of these arguments, and many others used by Australia's greenhouse mafia, are deliberate attempts to confuse polluter interests with the national interest. They are designed to mislead governments and the public into believing that Australia cannot achieve deep cuts in its emissions without devastating its economy. Meanwhile, study after study finds that we can at least halve our emissions below 1990 levels and our economy would more than treble in size, with real wages roughly doubling, and with energy falling as a proportion of overall spending.

I am cautiously optimistic about the direction of the new government—Kyoto ratification, a 60% emissions reduction target for 2050, an ETS consistent with that long term target, and an extended MRET are among the important steps forward. However, they can all be undermined if the greenhouse mafia gets away with the agenda discussed here. I have been a strong supporter of emissions trading in Australia. However, the only thing worse than not having an ETS in Australia would be to have an ineffective one—particularly one that fails public expectations by allowing emissions <u>in</u> Australia to keep rising, while polluters are allowed off the hook through a mix of carve-outs, compensation, and outsourcing emission cuts offshore.

I appreciate what the Garnaut review is up against given how deeply embedded the greenhouse mafia's agenda is already. Without any serious critical analysis, many of their self-serving propositions have taken on the inertia of conventional wisdom. As such, the media has failed to grasp their significance while sections of the environmental movement have been pre-occupied with issues other than the crucial fine print of ETS design. While the headline issues (eg the strength of a national emissions target) do matter a great deal, I have no doubt that the real integrity test of Australia's post-Howard greenhouse response will be whether the greenhouse mafia's new agenda is accepted or rejected by the Garnaut Review and the Rudd government. The Interim Report of the Garnaut Review suggests a laudable lack of sentimental attachment to the NETT and PMTG, but it also leaves a worrying proportion of the greenhouse mafia agenda intact.

Ultimately, Australia has a choice—we can meet our greenhouse obligations by doing what the public expects, or we can use a combination of loopholes to say we've met our greenhouse obligations when we've betrayed public expectations in the process. The latter path may well be the one of least short-term political resistance, but if we choose it I fear we are setting ourselves up for a very difficult conversation with future generations. I hope very much that the Garnaut Review helps to prevent the need for that conversation.

[10] Daley, John (former Chief Executive of the AIGN), 'Implications of a carbon tax,' Address to the APEC Studies Centre Conference: Kyoto; The impact on Australia, ACIL Economics and Policy Pty Ltd, 12-3 February 1998, pp2-3
[11] Daley, John (former Chief Executive of the AIGN), 'Carbon price signals and emissions trading,' speech at Business Council for Sustainable Development conference, Brisbane, May 2006, p.8
[12] Response to States Emissions Trading Task Force Discussion Paper, Australian Industry Greenhouse Network, January 2007, p.11-2
[13] Submission to Prime Ministerial Task Group, Australian Industry Greenhouse Network, March 2007, p.3
[14] For example, see: Submission on A National Emissions Trading Scheme—Consultation Paper, A3P, 8 December 2005, op-cit. p.8
[15] Response to States Emissions Trading Task Force Discussion Paper, op-cit. p.9-10